FINANSINSPEKTIONEN

Consumer protection on the financial market

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CONTENT

Foreword

Strong consumer protection on the financial market is crucial to both individuals and the economy at large. Finansinspektionen (FI) is now intensifying its efforts and taking a holistic approach to consumer protection matters.

By following developments on the market, FI can, at an early stage, intervene to alleviate the effects of the risks and problems arising, and to empower consumers. When the playing field between firms and consumers is more even, the conditions for, and confidence in, the financial system improve. This ultimately benefits the entire economy.

In order to bring consumer protection into greater focus, in April this year FI established a new area of operation, hence improving the possibilities of pursuing and communicating consumer matters while, at the same time, strengthening the conditions for developing both supervision and issuing regulations in the area.

As part of this work, FI presents this report on consumer protection on the financial market, which also describes risks and problems for consumers. FI's work on strengthening consumer protection is also described.

Stockholm, 15 May 2014

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Director General

Summary

Consumers on the financial market face a series of challenges and problems. For example, many savings products are complex, advice is often poor and information is, in many cases, deficient or difficult to understand. Finansinspektionen (FI) has previously called attention to several such problems, and has also taken measures. On some fronts, the situation has improved. On the whole, consumer protection is considered to be sound, even though it needs to be strengthened in several areas.

The financial market offers a number of important functions for consumers – savings, borrowings, payments and insurance. Everybody has to use these services to some extent. However, the functions can be associated with various risks and problems. Some only affect a certain group of consumers, but can have substantial financial consequences. Others affect a large number of consumers, but have limited financial consequences for the individual.

There are also risks associated with market abuse, money laundering and investment fraud, which also indirectly affect consumers. Although not a law enforcement agency, FI works actively on such matters. This report, however, focuses on the risks and problems that arise in the direct contacts between consumers and financial institutions. The risks and problems described are a result of FI's experience from supervision activities.

SAVING AND INVESTING

Financial products are becoming increasingly complex in structure with unclear fees, unclear and often very high risks, and return prospects that are hard to understand. The complexity makes it hard for consumers to assess risks, compare terms and understand return prospects.

In order for advice on financial products to be appropriate, it must be tailored to the needs of consumers. On several occasions, FI has called attention to financial advisors suggesting investments that are not suitable for the consumers. Commissions give rise to problematic conflicts of interest, and advisors lack incentives to gain insight into consumers' interests.

In order to create a sounder financial products advice market:

- FI has proposed a ban on commissions paid out directly in connection with signing up for products or entering insurance agreements, known as up-front commissions. Since FI is of the opinion that commissions are at the root of many of the deficiencies and problems in advice on financial products, FI is also investigating the possibility of a broader ban, comprising other types of commissions. A commission ban should apply to all advice on financial products, irrespective of the type of firm providing the advice.
- FI has strengthened supervision of the suitability assessment of advisors in connection with financial advice.

Deposit institutions are not covered by the state deposit guarantee. Hence, consumers can lose their deposits if the firm goes bankrupt. Deposit institutions must register with FI, but are not under supervision, and intervention possibilities are limited.

In order to improve consumer protection on the deposit market:

- FI has proposed that only firms authorised as a bank or credit market company should be able to accept deposits from consumers.

BORROWING

Instant loans only make up a small part of total indebtedness, but can nevertheless create major problems for individual consumers. Such loans are often granted to households with comparatively weak finances and, at worst, can lead to consumers falling into a debt trap. The business model of some instant loan firms is to lend money to consumers who do not have sufficient repayment ability.

In order to tighten the instant loan market:

- As of 1 July 2014, FI will supervise all firms that issue or mediate credits to consumers. In connection therewith, FI will have the ability to place demands on instant loan firms, and is currently in the process of preparing new regulations.

Mortgages make up the majority of household debt. FI's annual mortgage survey shows that most who are granted a new mortgage have sound repayment ability and are resilient to both changes in interest rates and loss of income. There are, however, households with slim margins, which are more poorly equipped to cope with altered financial conditions.

In order to strengthen the resilience of mortgage holders:

- FI has introduced a mortgage cap that limits the loan-to-value ratio to 85 per cent of the value of the home, and prepared a proposal for individually tailored amortisation plans.

The mortgage market features deficient information about mortgage rates, and high costs for transferring a mortgage from one bank to another. Consumers have no possibilities of comparing the actual lending rates of banks today. This lack of insight also applies to the factors that affect a bank's mortgage rate decision. The net margin on a three-month mortgage remains high, and increased in the first quarter of 2014. It shows that the need for greater insight into the mortgage rate is still important.

In order to improve openness about the mortgage rate:

- FI has proposed that banks should provide consumers with information about the actual average mortgage rate at the bank and the individual factors taken into consideration by the bank in its assessment of consumers, and that the bank should distinguish the cost of products and services offered besides the mortgage from the discount provided by the latter in the form of a lower mortgage rate. The Government has appointed a commission of inquiry to review how this proposal is to be implemented in Swedish legislation. In addition, FI is working on preparing new regulations that are to improve information about the mortgage rates paid on average by customers and the factors that are of importance to the mortgage rate.

In order to increase mobility on the banking market:

- FI has prepared a new calculation method that makes the interest rate differential charge more reasonable and better correspond to the creditor's loss. In addition, mobility and competition conditions on the banking market are expected to be improved. This method is to form the basis of a new model for calculating the interest rate differential charge. The law with the new model is expected to come into effect on 1 July 2014.

PENSION SAVING

Pension insurance policies are complicated and can be difficult to understand and evaluate. This potentially makes it difficult for consumers to make an appropriate, conscious choice. This is the case when, for instance, life insurance undertakings offer consumers the possibility of transferring or changing the terms and conditions of their pension insurance policy, because there is a risk of the undertaking presenting information based on its own interests.

In order to improve information in offers about transfers and amended terms and conditions:

- FI has amended its regulations and extended the information requirement in connection with offers for transfers or material amendments to the terms and conditions of insurance undertakings that offer life or occupational pension insurance.

There is also a risk that surpluses and deficits arising in life insurance undertakings are not distributed between pension savers in a manner that is fair based on how they have contributed premium and return on the one hand, and have incurred expenses on the other. The information provided to savers about entitlement to surplus is often unclear, and rarely describes the surplus that consumers may expect.

In order to make the distribution of surplus clearer:

- FI proposes that the authority be authorised to regulate policies for managing surpluses and bonuses. In FI's opinion, undertakings should be clear in their information about how surpluses arise and are distributed between the different savers throughout the entire duration of the insurance policy.

FI and consumer protection

The financial market fulfils an important function in society and all consumers need to use it to some extent. At the same time, the financial market has special characteristics that involve consumers often ending up at a disadvantage, and requiring protection. In particular, consumers often have poorer access to information than the firms. In addition, there are behavioural factors that can account for financial decisions not always being appropriate for consumers in the longer term.

CONSUMERS NEED PROTECTING

Consumer protection is one of the primary objectives of financial supervision. A fundamental factor in protecting consumers is that financial firms are stable, and can hence meet their obligations. In addition, the firms must act decently towards consumers, for instance by providing clear, relevant information.

Finansinspektionen (FI) monitors the market to ensure that financial firms are operationally and financially stable. FI also monitors the firms' conduct towards each other. It is important from the point of view of consumer protection, because it can affect consumers indirectly. However, this report is limited to the conduct and information matters that directly affect consumers.

Since consumers are often more poorly informed, it is more difficult for them than the firms to assert their rights. While this is the case in many areas, in the financial area, there are circumstances that aggravate the problem. For instance, the time lapse between the purchase of delivery of certain financial services – for instance pension insurance– can be long. Also, it can be difficult, due to the complex structure of a product, to judge its quality. The extensive term of many contracts therefore carries uncertainty, because the purchaser cannot be sure that the firm is capable of fulfilling its commitments – or even if it will still exist on the market – when the time comes for the firm to deliver on the contract. All of these factors make it hard for consumers to compare the offerings and products of different firms, even retrospectively. Hence, consumer protection interests in the financial area are partially different to those in other areas.

Consumers have a lot to gain on making appropriate choices based on their circumstances, and a lot to lose if inappropriate choices are made. Relevant and understandable information about various financial products is fundamental to making appropriate choices.

However, information is not the only influencing factor in financial decisions. They are also affected by emotions and experience, which can lead to a simplification of reality.[1] It can be a matter of taking out an instant loan or refraining from saving in order to be able to consume today – despite this leading to lower consumption tomorrow. It can also be expressed in consumers drawing overly hasty conclusions from an enticing offer. One example is when consumers opt to become a full-service customer with a bank due to an enticing mortgage rate for a limited

1 See also Financial Conduct Authority Occasional Paper No 1 Applying behavioural economics at the Financial Conduct Authority

period of time, without taking account of the costs of the other products included in the package.

The fact that financial decisions are affected by simplifications of reality can lead to actions that conflict with the long-term interests of consumers. The consequences can be major for both individual consumers and society at large. Hence, in certain situations, it might be motivated to take broader measures that, to a certain extent, affect the freedom of choice of individual households. Examples that can be mentioned are that an age limit is in place for when consumers can start to draw their private pension investments and their occupational pensions.

Measures and rules for protecting consumers can, at the same time, create thresholds into the market. An analysis of the effects on competition must therefore always be performed.[2] All types of interventions require clear argumentation and assessment of the benefit outweighing the costs. Functioning competition is important for a smoothly functioning, dynamic market. However, in order for its effects to be positive for individuals, it needs to be effective by means of lower prices and higher quality.

The link between consumer protection and stability

Consumer protection is, in many ways, closely interlinked with financial stability. An example that can be mentioned is that consumers, in their capacity of depositors, lose confidence in their bank, withdraw their money and put the bank in a liquidity crisis. Because the banks rely on the ability to borrow money from each other, the problems can spread to the entire financial system.

At the same time, financial stability is, in many respects, fundamental to sound consumer protection. Financial stability and profitability enable banks and insurance companies to honour their commitments and not risk the money of consumers. However, there are conflicting objectives, because financial stability is closely linked to healthy profitability. Profitability can be achieved at the expense of consumers, such as through high fees and wide interest margins. Conversely, generous lending with low margins might be popular among consumers, but pose risks to financial stability at the same time.

Although the objectives of stability and consumer protection largely coincide, in certain situations and in certain areas, conflicting objectives and problems in striking a balance might thus arise, and need to be addressed.

FI's mandate for intervention on the financial market also poses several questions and problems in striking a balance. What is the responsibility of the Government, what is the responsibility of the firms, and what is the responsibility of the consumers themselves? [3]

How should the level of protection be determined, and how is this weighed against the risk of inefficiency and of participants acting in a way that enables them to avoid taking the full consequences themselves?

2 In its consequence analyses, FI takes competitive aspects into consideration. However, because competition is not FI's primary objective, the matter will not be discussed further in this report.

3 This is known as a moral hazard, which is a term used to describe the situations that arise when e.g. a firm or consumer is not fully affected by the effects of their own actions. The firm or the consumer thus has an incentive to act less cautiously than otherwise if it is believed that the risk is borne by another party.

In addition, the need for consumer protection changes over time, in line with product development, the advent of new participants and types of distribution, and as a result of the altered demands and needs of consumers.

CLEAR CONSUMER PROTECTION.

In order to achieve sound consumer protection, information about various financial products must be improved, and consumers need to be empowered through educational initiatives. Another important condition is a smoothly functioning set of regulations, and supervision to ensure compliance with them. FI works actively with this.

By imposing requirements on information from the firms, the possibilities of consumers to understand and assess financial products and services improve. The information must be accurate, relevant and comprehensible to make it easier for consumers to make conscious decisions and evaluate them. Product design and information must be adapted and suited to the consumers targeted by the firm.

In order to protect consumers, FI also imposes other requirements on financial firms. For instance, the firms must have sufficient capital and liquidity. They must also manage risks and conflicts of interest in their operations. FI presupposes that the firms that conduct financial operations are serious and have the relevant expertise for the products offered.

Enhancing financial knowledge

Besides imposing requirements on firms' information, risk management and stability, FI works with empowering consumers through education. Most of this work is conducted in close cooperation with other Swedish authorities, firms and organisations. The purpose is to increase the awareness and knowledge of consumers in the area of personal finances. The educational initiatives are to reach a broad target group and focus on training trade union representatives, instructors at adult education associations and representatives from pensioner organisations to be Certified Personal Finance Instructors. Several school projects are also under way. For example, films about personal finances and consumer rights have been produced. In the framework of the Swedish for Immigrants programme, FI has prepared material on personal finances in straightforward Swedish. In the Money Smart project, training courses are offered in municipalities throughout Sweden, and young unemployed people are invited to attend a two-day course in daily finances and consumer rights.

FINANSINSPEKTIONEN'S ROLE IN THE AREA OF CONSUMER PROTECTION

FI and the Swedish Consumer Agency have joint responsibility for consumer protection on the financial market and cooperate in many areas. FI supervises the firms that conduct financial operations that require authorisation. FI's supervision mainly pertains to the regulations of business law; that is, the rules that specifically apply to the firms conducting operations that require authorisation. The Swedish Consumer Agency supervises all firms that conduct financial operations, irrespective of whether or not their operations require authorisation – but from the point of view of market law. The Swedish Consumer Agency thus conducts supervision to ensure that firms follow the general regulations that apply to all types of operations that focus on consumers.

FI's work with consumer protection is preventive and aims to identify and, using general measures, counteract problems before they cause harm for the consumer. On the other hand FI does not intervene in the dealings of individual consumers and firms.

The Swedish Consumer Agency has been given the assignment of establishing and coordinating a new consumer information service, in which FI will also participate. Its purpose is to enable consumers, in a straightforward manner, to obtain answers to questions about rights and obligations in many areas, such as financial services, telecommunications, health, travel, accommodation, energy and automotive.

In addition to FI and the Swedish Consumer Agency, there are a number of other public authorities and organisations involved in consumer protection work on the financial market. The Swedish Pensions Agency has a consumer information assignment in the area of pensions, and the National Debt Office is responsible for information about and the management of the deposit guarantee. Finally, the Data Inspection Board supervises credit information and debt recovery firms. The Consumer Ombudsman and the Swedish National Board for Consumer Complaints also bear consumer protection responsibility.

The Swedish Consumers' Banking and Finance Bureau and the Swedish Consumers Insurance Bureau inform and guide consumers. The information and guidance of the bureaux are independent of firms on the market. The impartial position enables the consumer bureaux to supplement and broaden the information. This includes, for instance, comparative information in which both the terms and pricing of competing products can be described and analysed. Municipal budget and debt advisors, and consumer counsellors also have the task of assisting and guiding consumers.

Saving and investing

The range and complexity of products and services on the financial market are on the rise. At the same time, low interest rates play a part in consumers seeking savings alternatives that enable a higher return, which involves greater risk-taking about which consumers are not always aware. Financial advice can help consumers, but Finansinspektionen (FI) finds that much of the advice is deficient. Inappropriate advice, complex products and deficient or misleading information involve a risk of consumers making decisions about investing their money in a way that is inappropriate for them.

INAPPROPRIATE ADVICE

Financial advice aims to aid consumers on the financial market. The firms that provide financial advice include banks, management companies, insurance companies, insurance intermediaries and investment firms. FI has, on a number of occasions, called attention to deficiencies in advice and has issued sanctions against several firms in recent years. As a result, there has been some improvement to the situation. For example, information about commissions has become partially clearer. At the same time, the fundamental problem remains.

Commission-driven advice

Commissions from the producers of financial products are currently the main source of income for many firms that provide financial advice. This gives rise to conflicts of interest, because advisors have an incentive to provide advice based on the size of commissions rather than the interests of consumers. FI has, in its supervision, noted that many firms do not sufficiently manage and inform of such conflicts of interest. Neither do they provide sufficient information about the remuneration they receive from other firms and when they receive it, which they are obliged to do.[4]

Another example of the problems relating to commissions is when advisors neglect the interests of consumers when transferring structured products. In a transfer, a product that has not yet matured is sold in order to buy a new product for the same amount. The new product might be hard to assess and compare with the existing product, and is not necessarily better either. However, the advisor has the opportunity of receiving a commission on more than one occasion.

Sanction: Skandinavisk Kapitalförvaltning

In April 2014, insurance intermediary Skandinavisk Kapitalförvaltning had its authorisation withdrawn with immediate effect because the firm did not follow the rules in place to create sound consumer protection. For example, employees without sufficient knowledge and competence had been allowed to mediate insurance policies. Neither had the firm procured sufficient information about the consumers, and had hence not tailored its advice to the needs of the individual, which it has an obligation to do. Furthermore, the firm had not informed its customers of the remuneration it had received from other firms. Finally, the firm also had deficiencies in its documentation of advice.

4 This applies to both insurance intermediaries and investment firms. See Finansinspektionen's regulations and general guidelines (FFFS 2005:11) regarding insurance mediation and Finansinspektionen's regulations (FFFS 2007:16) regarding investment services and activities.

Measure for a sounder advice market

FI has previously proposed a ban on commissions paid out directly in connection with signing up for products or entering insurance agreements, known as up-front commissions. Since FI is of the opinion that commissions are at the root of many of the deficiencies and problems in advice on financial products, FI is also investigating the possibility of a broader ban, comprising other types of commissions. A commission ban should apply to all advice on financial products, irrespective of the type of firm providing the advice.[5]

A ban on commissions is, in the opinion of FI, the most efficient way of addressing the conflicts of interest linked to providing advice on financial products. Furthermore, the supply of cheaper financial products would probably increase when advisors lose incentives to recommend expensive products, and demand for cheaper alternatives would thus increase. A commission ban should be devised to strengthen clear advice in the interest of consumers. The advice should focus on the products and services that the consumers need and request. In addition, the cost of the advice should be clear.

A commission ban could, however, also have negative consequences. For instance, the number of firms offering advice on financial products might decrease, and consumers who are unable to pay through fees might not have access to advice.

In order for the effect of the reduced supply of advisors on the market to weigh against the advantages of independent advice, the advice that would potentially disappear from the market would have to generate benefits for consumers in the form of low prices and high quality.

Investment fraud

There are players that conduct operations based on outright investment fraud. The fraudsters often act in a professional manner in order to build up confidence. Consumers are lulled into a false sense of security by false product sheets and agreement proposals that refer to fictitious authorities to strengthen the credibility of the firms. The firms might have impressive websites, which in certain cases show the positive performance of the investment on false trading venues.

These players conduct criminal operations and are not authorised. FI is not empowered to investigate financial crimes, but can, however, issue warnings about such firms. On FI's website there is a warning list of firms that lack authorisation but nevertheless conduct financial operations. The list currently contains just over 4,700 warnings. FI issues its own warnings and also publishes warnings issued by other financial supervisory authorities.

FI also collaborates with other authorities. For instance, in 2014 cooperation was initiated with the national fraud centre of the police. Because fraudsters often work cross-border, FI also cooperates with other supervisory authorities, Iosco (International Organization of Securities Commissions) and ESMA (European Securities and Markets Authority).

5 The updating of the Directive on Markets in Financial Instruments 2, Mifid 2 introduces minimum rules, whereby a party purporting to be an independent advisor may not accept remuneration from a third party. The Directive enables Member States to go beyond that.

Inappropriate advice

In order for advice on financial products to serve its purpose, it must be adapted to the circumstances of consumers. Ahead of each advisory session, the advisor shall gather sufficiently comprehensive and relevant information about consumers. Insufficient information retrieval and deficient analysis of the information increase the risk of the firms recommending inappropriate investments.

FI has, in its supervision, noted that the link between retrieved information and advice is missing. There are shortcomings in the assessment of consumers' risk appetite, which makes it hard to judge a suitable risk level. In addition, many firms are deficient in their documentation, which is to enable retrospective evaluation of the advice. FI has issued sanctions against several firms in the past year for this reason.

Furthermore, there are examples of firms that do not accurately present the risk of the product, or how the fees of the product affect the return prospects of consumers.

Measure for improved advice

FI has strengthened its supervision of the suitability assessment of advisors, and in April 2014 informed the industry of the deficiencies noted and the applicable rules for suitability assessment in financial advice.[6] In order for advisory firms to provide appropriate advice about investments, FI expects them to retrieve information and assess suitability carefully and comprehensively. The information must be analysed and used in the advice. FI will continue to focus on such matters in its supervision.

Sanction: FFR, Försäkria Finansrådgivning AB

After having neglected material customer protection rules, insurance intermediary FFR, Försäkria Finansrådgivning AB was issued a remark and an administrative fine of SEK 750,000 in December 2013. The reason was that the firm had not gathered sufficient information on its customers to be able to adapt advice to their wishes and needs. They hence risked providing recommendations that were not appropriate for the individual.

Neither had the firm sufficiently documented what had occurred at the time of mediation, or the reasons for the recommendations provided to customers. Due to these deficiencies, it was not possible, based on the documentation materials, to follow up whether the firm's customers were recommended products suitable for them.

In addition to this, the firm did not document, or inform customers of, the remuneration received by the firm from a third party when mediating insurance policies. Consequently, customers have not had the ability to make their decisions on the foundation of an accurate decision-making basis.

6 FI conducts regular external knowledge seminars for the financial industry, known as FI Forums. The purpose is to spread knowledge about existing rules and to engage the industry in a dialogue at an early stage of the process on forthcoming regulations. Click on the link to watch the Suitability assessment in financial advice seminar (Swedish only): http://www.fi.se/Tillsyn/Presentationer/FI-forum/Listan/Webb-tv-FI-forum--Lamplighetsbedomning-vid-finansiell-radgivning/

COMPLEX PRODUCTS

The savings product market is in constant development. Products tend to become increasingly complex in structure with unclear fees, unclear and often very high risks, and return prospects that are hard to understand. The complexity makes it hard for consumers to assess risks, compare terms and understand return prospects.

At the same time, the risk of loss in common structured products, such as autocalls and equity-linked bonds, is probably higher than what an average investor reasonably expects. In the most risky products, the probability of loss can be substantial – in certain cases 50–75 per cent. In many cases, the risk can also be much higher than in the underlying asset. Furthermore, the costs of the products have a substantial impact on the risk level and prospect of return.[7]

FI has noted that certain types of structured products, with an early maturity option, manifestly often mature early. However, the advisor mediating the product receives remuneration when the investment is made based on the contractual duration of the product. Hence, the advisor receives commissions for the entire duration. This enables the advisor to sell a new product to receive further remuneration. Hence, there is a risk that the products were construed to have a high probability of maturing early and benefit the advisor at the expense of consumers.

An increasing number of firms offer consumers the possibility of investing in riskier products, such as unlisted shares, bonds and subordinated loans issued by small, in many cases newly established, firms. Such investments can carry a high risk and are hard to evaluate. At the same time, many firms that mediate this type of product receive high remuneration, which gives rise to a conflict of interest whereby the interests of consumers risk being neglected.

Finally, FI has seen examples of firms that recommend that consumers of retirement age mortgage their home to invest in a financial product along the lines of endowment or depository insurance. Consumers are offered a return that will cover both interest expenses on the loan, and provide money over for e.g. consumption. In practice, this involves many times a much higher risk than consumers are aware of. The fee charged is often high, as is remuneration for the advisor. FI has previously warned of this type of product.

Measure for clearer information

FI has strengthened supervision of the area in the past year and will continue to monitor developments. In order to make information for consumers clearer for many types of investment products, work is also in progress at EU level. It will result in a regulation known as Priips.[8] The purpose is to provide consumers with information in set key investor information documents that make it easier to understand the individual product and compare between different products and product types. FI is actively participating in the work at EU level to prepare templates for the key investor information documents.

7 Result of the structured products survey, April 2014 A more in-depth presentation of the results of the survey will be presented in specific forms.

8 Package Retail and Insurance-based Investment Products.

Crowdfunding

A rapidly growing phenomenon on the investment market is so-called crowdfunding. In crowdfunding, a firm, organisation or person solicits financing from the general public for a project or business concept. The ideas and business plans are presented on a website, known as a platform. There are many different types of crowdfunding. Some of them are in a donations-only form, while in crowdfunding based on co-ownership, shares in the firm are offered.

Crowdfunding based on co-ownership is a relatively fast-growing phenomenon that does not come under existing regulations. For example, there is rarely an obligation to provide a prospectus. Because the transaction is not conducted on the platform, but through investment firms or directly between owners and investors, there is no authorisation requirement for the platform either, and it is therefore not under supervision.

A third version is when private individuals lend money to other private individuals in exchange for a relatively high interest rate. This is known as loan-based crowdfunding or peer-to-peer lending. Because the new Certain Loans to Consumers Act comes into effect in July, platforms that operate loan-based crowdfunding will require authorisation. This is because the mediation of loans to consumers will require authorisation from FI. Other types of crowdfunding are not covered by the new rules.

SAVING WITHOUT DEPOSIT GUARANTEE

There are deposits firms that offer alternatives to the savings accounts of banks, often with high deposit rates. However, the rules for deposits firms involve deficient protection for consumers' money, because deposits firms are not covered by the state deposit guarantee. Hence, consumers can lose the money they deposited if the firm goes bankrupt.

Deposits firms must register with FI, but are not under supervision, which represents an important difference. Registration can be incorrectly interpreted by consumers as a mark of quality. If a registered firm does not comply with laws, FI can order the firm to terminate its operations. Otherwise, however, the ability to intervene is limited and there is no ongoing, proactive monitoring of the operations.

Proposal for more secure saving

For products that resemble traditional banking products such as savings accounts, consumers ought to be able to expect the same protection from all providers. FI therefore finds that only firms authorised as a bank or credit market company should be able to accept deposits from consumers. This would entail tightened requirements for capital, reporting and supervision for firms that accept deposits. The deposits of consumers would hence be protected by the state deposit guarantee. [9]

DEFICIENT INFORMATION ABOUT FUNDS

Appropriate information is fundamental to creating an effective, open fund market on which consumers make well-founded decisions. Management companies are hence obliged to provide key investor information documents for the funds they manage. The key investor information document must be readily available and offered to consumers before they subscribe, and must contain information about the investment policy,

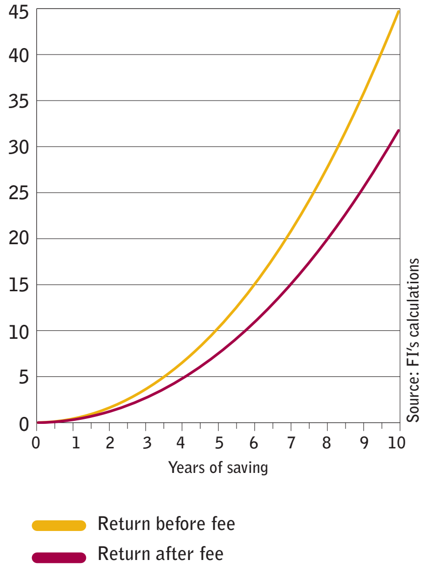
9 See the report Supervision and registration, April 2011

risk level and fees of the fund. The content must be relevant and logically presented and worded. Key investor information documents are devised according to an EU Regulation[10] to make it easy to compare funds throughout the EU.

FI has seen deficiencies in the information that risk leading to consumers making investment decisions based on incomplete or inaccurate information. The deficient areas include how the investment policy for certain funds is described, and how the management-related risks are explained.

In terms of the objective and investment policy of the fund, certain funds tend to describe them in a far too positive light. An example is funds which have a stated objective of outperforming the index, but which, in the actual management process, invest their assets so close to the index that it is rather a hope than an objective, accurate presentation of the characteristics of the fund. If the firm does not describe the fund's activity or ability to outperform the index accurately, it will be difficult for consumers to compare management costs between two funds that seem to have the same objective and investment policy. The fee is of great significance to how much consumers get back out of fund return (Diagram 1).

1. FUND RETURN
(thousands SEK)



Note: Assuming saving of SEK 1,000 per month, with a return of 6 per cent and a fund fee of 1.5 per cent.

The explanation of the fund's risks are standardised in certain cases and do not take the individual specificities of the fund into consideration. Information about the funds' risk levels is thus too general for consumers to be able to relate it to the fund in question and evaluate the risk compared to other investment alternatives.

In addition, FI has noted that the firms are deficient in the management of their transaction and analysis costs, and consumers hence do not know what they are paying for.

Measures for increased openness and a more efficient market

In FI's opinion, management companies should review their key investor information documents in order to ensure that they meet the requirements imposed, and has hence strengthened supervision thereof. The key investor information documents are to provide an accurate description of the fund's characteristics, and not be a way of marketing the fund.

In order to change industry practice regarding addressing transaction and analysis costs of funds, FI has, in a letter addressed to all management companies, clarified the regulations. During the year, FI will also commence regulatory work to further clarify this. The purpose is to improve openness and, in time, increase competition. Ultimately, this should lead to lower costs for people who invest in funds. Furthermore, it is a matter of ensuring that costs, besides those known to fund investors, are only charged to the fund if they increase the quality of management and are in line with the interests of fund investors.

FUNDS THAT ARE DIFFICULT TO VALUE

A key principle in fund operations is the equal treatment of all unit holders. A prerequisite is that the fund's assets are accurately valued, i.e. at the prevailing market value. The consequence of an overvalued fund is

10 The Commission Regulation (583/2010/EU)) implementing Directive 2009/65/EC of the European Parliament and of the Council as regards key investor information and conditions to be met when providing key investor information or the prospectus in a durable medium other than paper or by means of a website.

that subscribers pay too high a price for units. If the fund is undervalued, investors redeeming units will receive too low a price.

Funds that invest in certain types of financial instrument that are not traded on the regulated market may have problems in terms of reliable valuation, because it makes it harder to establish the market value. This pertains to shares in unlisted companies, OTC derivatives and certain corporate bonds and structured products. Valuation is established instead through contacts with brokers or by means of internal calculation models.

Measure for a smoothly functioning fund market

Accurate valuation of fund assets is fundamental to a smoothly functioning fund market. FI has therefore strengthened its supervision and is conducting surveys on the theme of valuation. The nature of the assets in which fund managers invest ought to be adapted to the conditions prevailing in an investment fund traded on a daily basis. An investment fund traded on a daily basis may not allow the market value to be unchanged from one day to the next without justifying why. The market value may be the same as on the previous valuation occasion, but in this case a new valuation confirming the value must be made.

Virtual currencies

On the financial market, there are several different virtual currencies. One that has attracted more attention recently is bitcoin – a digitally traded means of payment in the form of encrypted files which users can send to each other without a central intermediary.

Bitcoin has no central issuer, such as the Riksbank for Swedish kronor. Instead, the currency is created at a predetermined rate in a network which consumers can join and in which transactions are recorded in a journal. The volume of available bitcoin rose quickly when the currency was relatively new, but the rate of increase is now slowing down and the total volume finally amounts to around 21 million. Usage is relatively limited in Sweden and there are around 20 Swedish companies and websites that accept it as a means of payment.

In December 2013, FI endorsed the EBA's warning about virtual currencies. It is primarily a case of both the means of payment and the exchange venues largely being unregulated. Also, the value of bitcoin has varied sharply, posing a risk of losing vast quantities of money in a short space of time. Neither is there any legal protection in the event of a digital wallet or exchange venue being hacked into. The warning is published on FI's website.

Borrowing

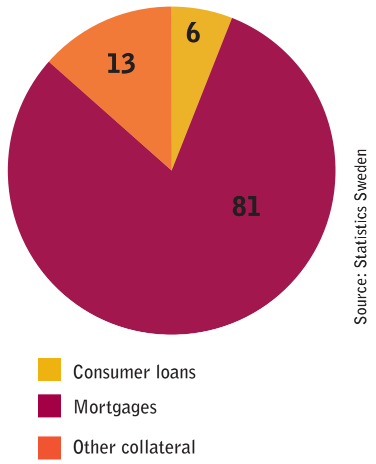
Borrowing provides consumers with the ability to even out their consumption level over time. At the same time, indebtedness – if it is not balanced – can cause problems and risks for consumers. Credit assessment is a key part of all lending. Many instant loan firms have shown deficiencies in their credit assessments and have dubious business models, which can lead to consumers falling into a debt trap. Instant loan firms will come under the supervision of Finansinspektionen (FI). Hence, FI will gain the ability to impose stricter demands on the firms, and the possibility of carefully monitoring developments.

HOUSEHOLD INDEBTEDNESS

The high indebtedness of households poses a risk for the individual and can pose a risk to financial stability. Indebtedness is therefore a crucial matter which FI closely follows. The consequences for individual households can be major if there are insufficient margins to cope with changed financial circumstances. [11]

The majority of household debts consists of mortgages (diagram 2). Consumer loans, i.e. unsecured loans, constitute around 6 per cent of the debts. Instant loans, which are a type of consumer loan with a short maturity and high interest rate, constitute a very small part of the total debts of households.[12] The risks and problems of indebtedness for individual consumers often vary depending on the type of loan. Instant loans are often taken out by households with comparatively weak finances, while mortgage holders generally have better payment ability.

2. HOUSEHOLD DEBTS
(per cent)



Note: The diagram is based on lending from Swedish monetary financial institutions (MFI) in February 2014. Note that the lending of instant loan firms is not included.

Credit assessment

Irrespective of the purpose of a loan, the creditor shall, according to the Consumer Credit Act, perform a credit assessment of the loan applicant. The purpose of the credit assessment is to prevent individuals with a low payment ability from taking on a loan, although it is impossible to predict unemployment, divorce or illness that could bring about an unexpected deterioration in the borrower's payment ability. A loan may only be granted if the consumer has the financial conditions to pay interest and amortisation instalments.

INSTANT LOANS CREATE THE RISK OF A DEBT TRAP

The number of firms offering instant loans has increased in recent years, and FI sees a number of risks and problems associated with such loans, which affect individual consumers. The business model of some instant loan firms is to lend money to consumers who do not have sufficient repayment ability. There are firms that pay a commission to their admi-

11 This report only focuses on the risks for the individual household and the measures to strengthen consumer protection in the area. In June, FI will publish a report focusing on financial stability which will highlight the risk from the point of view of stability.

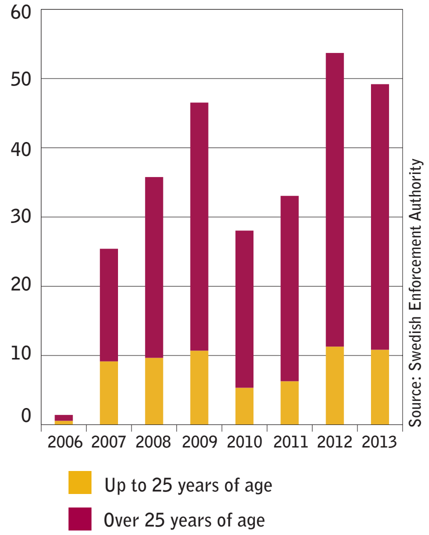
12 No statistics are currently available on the lending of instant loan firms. As of 1 July, which is when they will come under FI's supervision, FI will require the firms to report data to FI.

nistrators based on the loaned volume or the number of loans granted. The risks of the firms not getting their money back are low because they can appoint the Swedish Enforcement Authority to recover the debt.

Some instant loan firms offer an extension of the loan, i.e. the maturity is postponed. Such extension often carries a fee which, in certain cases, can exceed the total interest of the entire loan term. If this is done without a new credit assessment, there is a risk of the loan being extended despite a lack of repayment ability, so it not probable that the borrower will be in a position to repay the loan at a later stage either. Hence, the borrower incurs more costs without having paid off the existing debt first.

The consumers that end up at the Swedish Enforcement Authority due to unpaid instant loans are often young, have lower-than-average income and have other debts such as rent arrears, post order debts and telephony debts.[13] They also run a high risk of ending up in a vicious circle that makes it difficult for them to rid themselves of their debt problems. In recent years, the number of unpaid instant loans has increased, although there were slightly fewer in 2013 than in 2012 (diagram 3).[14]

3. UNPAID INSTANT LOANS
(number of loans in thousends)



Credit assessment is key to ensuring that loans are only granted to consumers with the ability to repay them. The Swedish Consumer Agency has, in its supervision, seen deficiencies in many of the instant loan firms' credit assessments.[15]

Measure for an improved instant loan market

As of 1 July 2014, firms that issue or mediate loans to consumers will need to apply for authorisation from FI and will come under supervision. FI can hence impose demands on the operations of the firms. FI is in the process of preparing regulations for such firms, with the purpose of reducing the risks associated with consumer credits.[16]

The rules are based on the firms conducting sound operations. A prerequisite for this is that the firms only lend money to consumers who are expected to be able to pay it back within the agreed term. Because the firms will require authorisation, they will have an obligation to report information about the operations to FI. FI will also conduct owner and management assessments and have the possibility of deciding on sanctions against the firms that do not comply with the regulations.

In addition to this, the Swedish Consumer Agency retains its supervision of credit assessment and marketing. Also, since 1 April 2014, the Swedish Consumer Agency has had the possibility of imposing a sanction fee on firms that do not conduct credit assessments properly.

Because FI will be given supervision of firms that issue consumer credits, the possibilities improve for monitoring developments in this type of loan and intervening against neglectful firms. Consumer protection is hence strengthened. However, supervision does not have any direct impact on consumer demand for credit. FI will closely monitor and evaluate the effects of the regulations.

13 Certain Loans to Consumers bill, Prop. 2013/14:107 (Appendix 5).

14 In 2013, the Swedish Enforcement Authority received 50,000 applications for payment injunctions regarding instant loans. 22 per cent of cases pertained to young people in the 18–25 age bracket (www.kronofogden.se).

15 http://www.konsumentverket.se/Nyheter/Pressmeddelanden/Pressmeddelanden-2012/Snabblaneforetag-varnas-for-otillracklig-kreditprovning/

16 http://www.fi.se/Regler/FIs-forfattningar/Forslag-nya-FFFS/Listan/Forslag-till-nya-regler-om-viss-verksamhet-med-konsumentkrediter/

Debt restructuring – a last resort

In order to empower consumers on the financial market, different types of advice and support are needed. Fundamental consumer protection includes, for example, budgeting and debt advice through municipal advisors and possibilities of so-called debt restructuring. In debt restructuring, a heavily indebted person may, in certain circumstances, be wholly or partially discharged from liability to pay their debts. Debt restructuring is usually conducted over a five-year period with the support of a determined payment plan. In practice, it involves all earned money above the subsistence threshold going directly to paying off the debts. In Sweden, the Swedish Enforcement Authority decides on debt restructuring. In order for an application to be accepted, it must for instance be considered that the borrower lacks the ability to repay the debts within the foreseeable future.

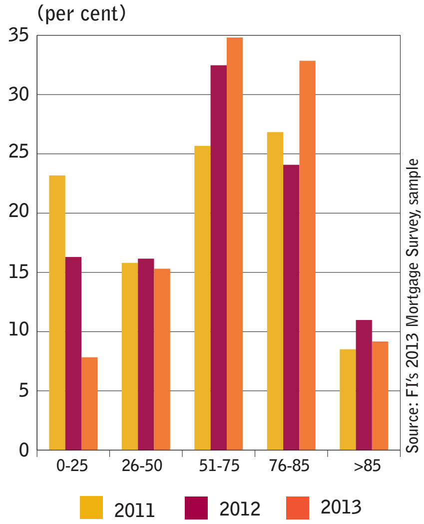
MORTGAGE HOLDERS WITH SLIM MARGINS

A mortgage is the biggest financial commitment for many households. Mortgages often carry a lower rate of interest than consumer loans, because they are collateralised by the home. At the same time, mortgages are often much higher than consumer loans, so interest expenses are affected quickly when interest rates rise. In addition, a changed situation in life, such as unemployment or illness, can lead to a deterioration in the ability of households to pay interest. Households must therefore have a safety buffer between the scope of the loan and the value of the home.

FI's annual mortgage report[17], which was published in April, shows that the majority of the households granted a new mortgage have sufficient margins, even in the event of a loss of income or a rise in interest rates.[18] There are however households with slim margins and which, in altered financial circumstances, would have difficulty in meeting their interest payments.[19]

At the same time as fewer households with new mortgages have a loan-to-value ratio above 85 per cent, an increasing number have a loan-to-value ratio of between 75 and 85 per cent (diagram 4). In addition, fewer households in this interval amortise than before, despite the recommendation of the Swedish Bankers' Association regarding amortisation.[20]

4. SHARE OF HOUSEHOLDS BROKEN DOWN BY LOAN-TO-VALUE RATIO INTERVAL, NEW MORTGAGES
(per cent)



Note: Shows the number of households in different loan-to-value ratio intervals as a share of the total number of the households in the new loan sample.

17 http://www.fi.se/Tillsyn/Rapporter/Rapporter/Listan/Den-svenska-bolanemarknaden-2014/

18 The survey includes Danske Bank, Handelsbanken, Länsförsäkringar Bank, Nordea, SBAB Bank, SEB, Skandiabanken and Swedbank. The materials gathered comprise several parts, such as an extensive sample covering all new mortgage agreements entered during the periods 27 August – 3 September 2013, and 26 September – 3 October 2013. A total of 26,010 loans are included. This is the fourth time FI has compiled such a sample.

19 FI has performed stress tests to measure the resilience of households. This involves testing various changes in the financial situation of households, such as hiked interest rates or a drop in income. For a more detailed description of how the tests were performed, see the report The Swedish Mortgage Market, April 2014.

20 According to the recommendation from 2010, borrowers should amortise the part of their mortgage that is above 75 per cent of the market value. The recommendation was revised in 2014 and pertains to all loans with a loan-to-value ratio above 70 per cent.

Measures for increased resilience

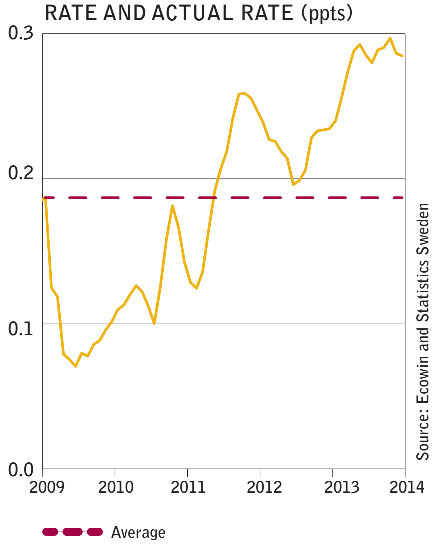
In order to strengthen the resilience of mortgage holders, in October 2010 FI introduced the mortgage cap, according to which loans collateralised by the home should not exceed 85 per cent of the market value of the home. The purpose of the mortgage cap is to prevent borrowers who take out mortgages from becoming excessively indebted, hence creating a safety buffer. All banks included in FI's mortgage survey comply with the mortgage cap. Even after the introduction of the mortgage cap, it is possible to borrow to over 85 per cent of the value of the home by taking out a non-collateralised loan (known as an unsecured loan). The fact that there are banks that offer unsecured loans in connection with mortgages does not mean that they fail to meet FI's general mortgage cap guidelines. Unsecured loans often carry a higher interest rate and must be amortised faster.

In order to strengthen the resilience of households in the longer term, in the autumn of 2013 FI prepared a proposal to the Government on the banks providing households with individually tailored amortisation plans. At the same time, the Swedish Bankers' Associated updated its recommendation for its members to introduce amortisation plans. In March 2014, it also tightened its recommendation on the amortisation of mortgages down to 70 per cent of the market value of the home within 10 to 15 years. By increasing the awareness of borrowers on how amortisation affects indebtedness in the long term, individual amortisation plans can lead to more households amortising.

INSUFFICIENT INFORMATION AND A SLUGGISH BANKING MARKET

Characteristics of a smoothly functioning market include consumers having access to quality information and the ability to easily switch supplier of a product or service. The mortgage market features problems in both areas – information about mortgage rates is deficient and transferring a mortgage from one bank to another can be expensive.

5. DIFFERENCE BETWEEN LIST RATE AND ACTUAL RATE (ppts)



Note: Difference between list rate and actual rate
Average since October 2005

Insufficient information about the mortgage rate

Unless consumers apply for a mortgage from several banks at the same time, they currently have very limited possibilities of comparing the actual lending rates of banks. The list rates published by the banks on their websites differ from the actual rate paid on average by borrowers. Because it is unclear what the list rate actually reflects, the value of the information can be questioned.

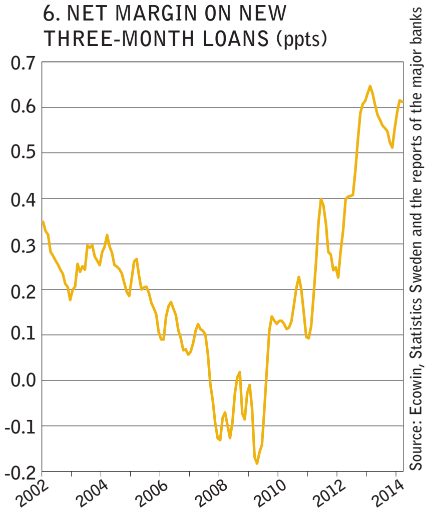
This lack of insight also applies to what affects the bank's mortgage rate decision. The banks do not currently need to explain the rate they offer.

Several banks give discounts on the mortgage rate in exchange for consumers undertaking to buy other products and services of the bank. There are also examples of banks giving discounts for an increased mortgage volume. It can be difficult for consumers to distinguish the interest rate discount from the cost of the other products and services offered by the bank. It can thus be difficult to determine whether it is ultimately worth committing to more products in return for a lower mortgage rate. Insight and clarity are necessary for the ability of consumers to make a conscious choice.

Measures for increased openness

FI has worked actively for several years on increasing openness about

6. NET MARGIN ON NEW THREE-MONTH LOANS (ppts)



Note: 90-day rolling mean

mortgage rates, and is now working preparing new regulations on the area. As part of this, in 2012 FI developed a calculation model for the average margin on new mortgages with a three-month fixed interest term. FI published an average margin on a quarterly basis for a couple of years, and worked with a view to making the banks more open about how they determine the mortgage rate. In the first quarter of 2014 the net margin increased and was 0.61 percentage points, compared to 0.55 percentage points in the fourth quarter of 2013 (diagram 5).[21] The increase was due to the fact that the funding cost dropped more than the mortgage rate. With a view to further increasing consumer insight into how actual lending rates for mortgages are determined, FI submitted a proposal to the Government in the autumn of 2013.[22]

FI proposed that the banks should provide information to consumers about the actual average mortgage rate at the bank, and the individual factors that the bank takes into consideration when assessing consumers. In addition, it was proposed that the bank should explain how various factors affect the mortgage rate offered. Furthermore, it was proposed that the banks be obliged to distinguish between the cost of products and services offered in addition to the mortgage, and the discount that these offer in the form of a cheaper mortgage rate. FI is now working on preparing new regulations that are to improve information about the mortgage rates paid on average by customers and the factors that are of importance to the mortgage rate.

At the beginning of the year, an agreement was also reached regarding a new mortgage directive in the EU. The directive includes a general ban on packaging loans together with other financial products and services without offering the loan separately. Hence, the bank may not make it a condition for a potential mortgage customer to purchase its other products and services. However, the bank may still offer other products in exchange for a lower mortgage rate.

The Government has appointed a commission of inquiry to investigate how the mortgage directive is to be implemented in Swedish legislation. The commission of inquiry will also investigate how the banks can become more open about how they set their interest rates on mortgages, in accordance with FI's proposal from the autumn of 2013.

A sluggish banking market

Consumers who have fixed their mortgage rate must pay compensation to the bank if they terminate the agreement prematurely. This interest rate differential charge is to cover the bank's loss that arises when the agreement is terminated. The method for calculating the interest rate differential charge has over-compensated the banks' losses, and it has been expensive for consumers to switch banks. This has limited the mobility of consumers on the banking market.

Measure for increased mobility on the banking market

The Swedish Parliament has adopted a bill with a new model for calculating the interest rate differential charge.[23] FI has prepared a new calcula-

21 The net margin shows difference between the actual three-month mortgage rate and all costs associated with conducting mortgage operations, i.e. the gross margins minus costs besides the funding cost. For a detailed description of how the calculations are performed, see the report Banks' interest rates and lending, Q3 2013, December 2013.

22 Increased openness about the mortgage rate, September 2013

23 Prop. 2013/14:44 Fairer rules for the early redemption of mortgages

tion method for computing the general interest rate, based on mortgage bonds instead of government bonds previously. This method is to form the basis of the new model. The effect is expected to be a more reasonable interest rate differential charge for newly granted mortgages that better matches the lender's cost. When consumers can switch banks less expensively, the conditions for mobility and competition on the banking market improve. The new law enters into force on 1 July 2014.

Pension saving

Pension insurance policies are complicated and can be difficult to understand and evaluate. At the same time, choices about pensions matter a great deal to the finances of consumers, and needs-based, comprehensible information is important for conscious choices. Also, it is important that life insurance undertakings distribute surpluses predictably and fairly between pension savers.

PENSION INSURANCE INFORMATION THAT IS DIFFICULT TO INTERPRET

For some time, the financial market has featured low interest rates. This has affected some life insurance undertakings that have issued high-return guarantees for their traditional types of saving. [24] Consequently, several life insurance undertakings offer consumers the possibility of transferring the value of their policies to a different policy or type of management.

Such offers are usually a case of transferring from one policy with guarantees to another with lower guarantees, or to one that entirely lacks guarantees, usually unit-linked insurance. The policyholder is offered the possibility of accepting material amendments to the policy terms and conditions, such as lower guarantees combined with more risky investments.

There is a risk of the insurance undertakings presenting information based on their interests in reducing guaranteed commitments, which are risky and costly for them. Consumers are at a disadvantage in terms of information in relation to the insurance undertaking, and there is a lack of insight. Because of these factors, it might be difficult to make well-founded and conscious choices on transfers or amended terms and conditions.

Occupational pension

Around 90 per cent of all people who work in Sweden are covered by a collectively agreed occupational pension. The size of the occupational pension varies, but on average it is about half of total retirement pension. The employer owns the occupational pension and pays the occupational pension premium for its employees. Then, in many cases, the employee can choose how all or parts of it are to be invested.

In most cases, consumers can choose between traditional insurance and unit-linked insurance. Traditional insurance most often contains a guarantee expressed as a certain amount or return, and on top of that there is a possibility to receive surpluses arising in the management process. Unit-linked insurance, on the other hand, can involve a higher risk because the financial risk is assumed entirely by consumers, but also a greater possibility of influencing the risk level and return. If unit-linked insurance is selected, consumers may also select the funds in which to invest the occupational pension. If no active choice of funds is made, the pension is commonly automatically invested in a standard solution, comprising funds selected by the insurance undertaking. The employee can also refrain from selecting a type of insurance, and then ends up with a default option.

24 Low interest rates have put severe pressure on the solvency of life insurance undertakings. Also, total return is probably low, particularly in relation to the return prevailing when the high-return guarantees were issued.

In collectively agreed occupational pension insurance, parties to the labour market decide which information is to be given to consumers. Finansinspektionen (FI) has in its supervision seen that the content of the information currently provided does not meet in all respects the requirements imposed on information regarding insurance and other occupational pensions.[25] It is a case of e.g. information on tax on returns, surpluses in traditional insurance that can be used to cover losses, general information about long-term investment targets, and the fund transfer process and the fees thereby incurred.

Measure for clearer information
FI finds that information about occupational pensions should be of a high standard on all important areas pertaining to consumers. The information should be needs-based and describe the prevailing situation to consumers, without the point of fact being concealed by the details. This should also apply to collectively agreed occupational pensions. It is also important that the undertakings are clear about the benefits and drawbacks entailed by a transfer or amended terms and conditions.

In mid-2013, FI amended its regulations and extended the information requirement in connection with offers for transfers or material amendments to the terms and conditions of insurance undertakings that offer life or occupational pension insurance.[26] FI intends to continue with its work to ensure that consumers are given clear, appropriate and relevant information.

DEFICIENCIES IN INFORMATION ABOUT PENSION SIZE

The size of a pension depends on a number of factors besides the premiums paid in over a working life. In traditional insurance, a surplus is created when the actual return on assets exceeds the guaranteed interest, or when costs turn out to be lower than expected. In addition, insurance undertakings make assumptions about e.g. life span, which affect the size of pension payouts.

Surplus in transfers and amended terms and conditions

There is a risk that surpluses and deficits in life insurance undertakings are not distributed between pension savers in a manner that is fair based on how they have contributed premiums and return on the one hand, and have incurred expenses on the other. This is particularly manifest when transferring the value of a policy or when terms and conditions are amended. There is then a risk that pension savers who opt to transfer their pension, and those who opt to remain, are not treated equally.

For consumers, it is important to obtain a comprehensible presentation of when surpluses arise, and about entitlement to receive surpluses. This is particularly relevant in transfers, when information is required about how pension savers who opt for transfers, and pension savers remaining with the undertaking, are treated. The information provided to savers about entitlement to surplus is often unclear, and rarely describes the surplus that consumers may expect.

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25 In 2013 FI conducted a survey covering pre-sale information for consumers ahead of, and partially during, the personal options process under two of the largest collective agreements (ITP1 and SAF-LO).

26 Finansinspektionen's regulations and general guidelines (FFFS 2011:39) regarding information about insurance and occupational pensions.

Measure for clearer surplus distribution

Surpluses shall be distributed based on how the various sub-holdings of policies have contributed to a surplus arising.[27] The insurance undertakings have the possibility of making exemptions from this by specifying how the distribution is to be carried out in their insurance terms and conditions or articles of association.

FI proposes that the authority be authorised to regulate policies for managing surpluses and bonuses. It is important that insurance undertakings distribute surpluses predictably and fairly to consumers with pension insurance. In FI's opinion, undertakings should also be clear in their information about how surpluses arise and are distributed between the different savers throughout the entire duration of the insurance policy. Such information shall describe how arisen deficits are to be funded, and the situations in which adjustments to the value of the policy may be needed.

Assumptions that affect pension payouts

In order to determine the size of actual pension payouts, insurance undertakings need to use specific methods and principles. It can be a case of assumptions about life span and future return, and various selectable payout models.

Undertakings may need to adjust such assumptions over time, which affects the size of pension payouts. Otherwise, the money would not suffice in future for those who save today. One example is when return is expected to be lower ahead, when the disbursed amount can also be lower or increase at a slower rate for the group of pensioners to which the assumptions apply. The same applies if life span increases in society. In this case, insurance undertakings might need to allow for payouts over more years than the amount assumed when the saving commenced. Then, the pension capital has to last for more years on average. This is particularly noticeable in cases where consumers have opted for life-long payouts

Measure for increased clarity

FI will continue to monitor how insurance undertakings apply the methods and principles used to determine the size of pension payouts, and how they devise the information received by consumers. FI finds it important that the undertakings work in an active manner, both in devising such methods and principles, and informing consumers about how pension payouts can change over time. This includes the calculation methods applied and the use thereof, and requires clarity, predictability and forward planning by the undertakings. The undertakings should be prepared to provide needs-based information to consumers regarding the motives for selected methods and assumptions, particularly regarding the effects on payouts in different future scenarios. This is particularly important when changes are made that reduce pension amounts.

FI works continuously with empowering consumers and will, on an annual basis, report its view of consumer protection on the financial market and how the authority works to alleviate risks and problems.

27 The contribution principle is described in the rules set forth by the corporate law of the Insurance Business Act, Chapters 11–13.

Glossary

Amortisation schedule The time frame within which the customer must have repaid a loan. The amortisation schedule for a bottom loan is often longer than for a top loan or unsecured loan. A borrower also often has the option of not amortising a bottom loan. In the survey, the amortisation schedule at the aggregate level shows how many years it takes to pay back the loan (bottom and top loans and, where applicable, unsecured loans) given that it is not an unamortised loan.

Autocall Financial product consisting of a bond component combined with one or more call options and an issued put option. Their structure, characteristics and risks can vary.

Bond Interest-bearing security which can be issued by governments, municipalities, credit market firms, mortgage institutions and large corporations. Bonds have a maturity of at least one year and the nominal amount is repaid upon maturity. Until then, holders receive payments mainly in the form of interest. Bonds issued by corporations are called corporate bonds and are an alternative to funding through e.g. bank loans.

Corporate bond Security issued by a corporation with a view to borrowing money. The maturity is one year minimum.

Derivative instruments Financial contracts that are linked to events or conditions at a specific future point in time or period of time. The value of a derivative instrument is linked to the value of the underlying asset. Derivatives redistribute risk and can thus be used both to increase and reduce investors' risk exposure. Examples of derivative instruments are options, futures and swaps.

Equity-linked bond One of the most common forms of structured products. The product consists of a zero coupon bond and a derivative component. The derivative component is one or several options whose value is linked to one or more underlying assets, such as equities. The duration is often 3–5 years, after which time the investor receives the nominal amount of the bond and any return generated by the options.

Financial markets An umbrella term for markets on which financial instruments are traded. The four most important markets are the foreign exchange market, the fixed income market, the equity market and the derivative market.

Finansinspektionen's general guidelines and regulations (FFFS) Regulations which supplement the laws and regulations that fundamentally govern financial operations. Regulations are binding while general guidelines serve as guidance.

Fixed interest term The period during which the interest rate on a loan is fixed. For treasury bills and most government bonds, the fixed interest term is equal to the remaining time to maturity of the loan.

Interest rate differential charge The compensation that a mortgage holder, in certain circumstances, must pay to the bank when a fixed-term mortgage is redeemed early.

List rate The lending rate marketed by credit institutions.

Loan-to-value ratio A percentage that describes the portion of the market value of a home that is mortgaged. If the market value of the home decreases, the loan-to-value ratio increases, given that the loan is held constant.

Maturity The amount of time remaining until the payment of a liability or until a bond falls due.

Mifid (Markets in Financial Instruments Directive) EU Directive regarding markets in financial instruments. Contains regulations about the operations of trading venues and transparency requirements for securities transactions.

Mortgage cap The mortgage cap came into effect on 1 October 2010 through FI's general guidelines FFFS 2010:2. These guidelines state that a loan collateralised by a home may not exceed 85 per cent of the market value of the home.

OTC (Over the Counter) Trade that occurs directly between a buyer and seller, but outside a market place. OTC derivatives are derivatives that are traded between two parties without using a market place and with fully or partially concealed order information.

Priips (Package Retail and Insurance-based Investment Products) EU regulation regarding key investor information documents for investment products.

Solvency Measure of the financial position and strength of an undertaking. Insurance undertakings must always have sufficient own funds amounting to a level calculated based on the nature and scope of the operations.

Subordinated loans A long-term loan without specific collateral raised by corporations, building societies and banks in exchange for interest-bearing debt instruments, known as subordinated debentures. An investment in a subordinated loan carries a higher risk than bonds but a lower risk than equities.

Trading venue Market for trading in financial instruments, for example investment firms which organise trading, stock exchanges or MTFs. Also called market place.

Unsecured loan A loan that is granted without any collateral or security. The banks often charge a higher interest rate for unsecured loans than collateralised loans such as top and bottom loans.

Structured product Financial instrument whose return is completely or partly dependent on the performance of several other financial instruments or assets. Often consists of a bond combined with a derivative, for example an option. Examples of structured products include equity-linked bonds or commodity bonds.

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