



The new Insurance Distribution Directive – an overview and some initial reflections¹

Article published in Italian on dirittobancario.it on March 31, 2016

5 APR 2016

By: David Maria Marino | Andrea Pantaleo

More than 13 years after Directive 2008/92/EC, Europe's legislators have finally amended the rules governing insurance intermediation, by approving Directive 2016/97/EU of 20 January 2016 (the "Insurance Distribution Directive" or "IDD").

In general, it immediately appears that the IDD is entirely based on the notion of insurance "distribution", rather than that of insurance "intermediation" used by the previous directive.

This is no mere question of choice of words, but the means by which to broaden the list of persons or institutions addressed by the provisions of the IDD, which includes all persons or institutions (not only insurance intermediaries in the strict sense of the term) that, in various capacities, participate in the sale of insurance products.

The purpose of this broadening of the scope of the Directive in terms of the persons or institutions it addresses, lies on the one hand in the declared need to guarantee the uniformity of consumer protection, regardless of the person proposing the acquisition of insurance products, and on the other hand in the need to harmonize treatment among operators and to curb any distortive effects of competition (see, in particular, Recitals 5 and 6).

In general, it is also clear that the IDD is not designed to ensure the maximum harmonization of national legislation, but on the contrary attempts to provide a minimum basic legislative framework, while individual Member States remain free to maintain or adopt more stringent provisions safeguarding consumers, should the specific national context justify such.

The IDD – which is introduced by a total of 79 Recitals – is set out in 8 Chapters, namely:

1. Extension of scope and definitions
2. Registration requirements
3. Freedom to provide services and freedom of establishment
4. Product oversight and governance requirements
5. Information requirements and conduct of business rules
6. Additional requirements in relation to insurance-based investment products
7. Penalties and other measures
8. Final provisions

This work aims to outline and summarize the main changes concerning the following areas only: (1) the subjective extension of scope, with specific reference to comparison websites; (2) pre-contractual disclosure obligations, with specific reference to fees; (3) requirements regarding product management and control; and (4) insurance-based

investment products.

1. The IDD's subjective extension of scope, with specific reference to comparison websites

As mentioned above, the IDD extends its scope to a series of persons not included (at least not explicitly) among the addressees of the previous Directive. The IDD thus applies to all persons who, in various capacities, are involved in the sale of insurance products. It thus concerns not only insurance undertakings and insurance intermediaries, but also the other actors in the insurance market, such as, for example, travels agents and car rental companies, persons that distribute insurance products as a secondary activity in addition to their principal business (such have been given the ad hoc name of "*ancillary insurance intermediaries*"), and also those persons managing websites offering a ranking of insurance products, when these websites permit customers to "*directly or indirectly conclude an insurance contract*" (Article 2).

In regard to those persons who operate as ancillary insurance intermediaries, the IDD reintroduces the exemptions based on the type of risk covered (breakdown, loss, damage and non-use, or damage to, or loss of, luggage, or risks linked to travel), or on the amount of the premium paid (premiums of less than 600 Euro calculated proportionately on an annual basis).

In regard to those persons excluded from the scope of the Directive, in any case the IDD establishes that each Member State shall oblige the insurance undertaking or insurance intermediary to: (i) inform customers of its identity, address and the manner in which claims are to be submitted; (ii) establish adequate mechanisms to ensure compliance with the conduct obligations set out in Articles 17 and 24 of the IDD; (iii) provide customers with the information document relating to the insurance product in accordance with Article 20, paragraph 5, of the IDD.

The Recitals of the IDD contain other important specifications concerning the scope of the corresponding provisions.

In particular, Recitals 12 and 13 specify that the IDD:

1. should apply to persons whose activity consists of the provision of information on one or more contracts of insurance in response to criteria selected by the customer, whether via a website or other media, or the provision of a ranking of insurance products or a discount on the price of an insurance contract when the customer is able to directly or indirectly conclude an insurance contract, while
2. it should not apply: (a) to mere introducing activities consisting of the provision of data and information on potential policyholders to insurance or reinsurance intermediaries or undertakings or of information about insurance or reinsurance products or an insurance or reinsurance intermediary or undertaking to potential policyholders; (b) as in the existing system, to the management of claims (including loss adjusting and expert appraisal of claims).

In regard to those persons referred to in point (i) above (the "comparison websites") - who, moreover, were the subject of a recent investigation by the IVASS – in 2013 the EIOPA had already acknowledged the significant space occupied by such operators in the market, the absence of any consistent regulations governing their activities, and the requests submitted (including those of the BIPAR – the *European Federation of Insurance Intermediaries*) aimed at having them included among those subjects addressed by the provisions governing insurance distribution.

After all, even in the absence of the IDD, the provisions governing insurance intermediation set out in ISVAP Regulation 5/2006 meant that it was reasonable to believe that while the activity of mere comparison did not constitute intermediation, if, on the other hand, certain conditions arose, such as the case where by use of the comparison website, it was possible not only to compare products but also to purchase those products, then in this case such activity would come within the broader definition of intermediation.

2. Information requirements - Remuneration

Recital no. 40 underlines the importance of providing customers with information, prior to the conclusion of the contract, with regard to the status of those parties selling insurance products, and in particular with regard to the type of remuneration they receive.

In keeping with said Recital, Article 19 of the IDD establishes – without making any distinction between life and non-life

insurance products, and in regard to the latter, without making any distinction based on the nature of the risk – the intermediary's obligation to provide information about the nature of the remuneration: whether this is calculated on an hourly basis, or on a lump-sum basis, or otherwise.

With regard, once again, to pre-contractual information obligations, Article 20 of the IDD introduces two different documents, namely: (i) the "*personalised recommendation*", designed to specify the reasons why a particular product would best meet the customer's demands and needs (compared to other comparable products), whereby the intermediary provides advice to the customer; and (ii) (for non-life products) a standard information document, easy to read, containing similar basic information to the information currently contained in the information note referred to in IVASS Regulation 35/2010. In this regard, it should be pointed out that discussions are still ongoing between IVASS, consumer associations, insurance undertakings and intermediaries, with regard to the contents of a possible new "simplified" information note applicable to the non-life insurance sector.

Similarly to what is set out in the joint letter drafted by the Bank of Italy and IVASS in August 2015 (even though this still contains specific reference to policies linked to loans and finance agreements), Article 17 of the IDD underlines, in general terms, the importance of the fact that the insurance distributor does not make any arrangement by way of remuneration, sales targets or otherwise that could provide an incentive to recommend insurance products which do not meet the customer's needs

3. Additional requirements in relation to insurance-based investment products

The IDD establishes certain specific obligations regarding the distribution of insurance-based insurance products, that is, those insurance products offering a maturity or surrender value and where that maturity or surrender value is wholly or partially exposed, directly or indirectly, to market fluctuations.

In this regard, it should be pointed out that in the Italian legal system, insurance-based investment products have for some time been subject to the provisions of Italian Legislative Decree no. 58/1998 (the Consolidated Law on Finance), which establishes much more detailed rules than those introduced by the IDD. Thus the IDD is not going to have any significant impact on this category of products.

On the basis of the IDD, insurance-based financial products do not include: (i) non-life insurance products as listed in Annex I to Directive 2009/138/EC (Solvency II); (ii) life insurance contracts where the benefits under the contract are payable only on death or in respect of incapacity due to injury, sickness or disability; (iii) pension products which are recognised as having the primary purpose of providing the investor with an income in retirement; (iv) Company or professional occupational pension schemes; (v) individual pension products for which a financial contribution from the employer is required and where the employer or the employee has no choice as to the pension product or provider.

A precondition for application of the additional requirements provided for by Chapter VI of the IDD, is that insurance-based investment products are distributed by (a) an insurance undertaking or by (b) an insurance intermediary.

The section regarding insurance-based investment products establishes obligations relating to conflicts of interest, information about products and the associated costs and charges, the evaluation of the suitability of the product in the case of provision of advisory services.

With regard to conflicts of interest, an insurance intermediary or an insurance undertaking shall maintain and operate effective organisational and administrative arrangements with a view to taking all reasonable steps designed to prevent conflicts of interest from adversely affecting the interests of its customers. Where organisational or administrative arrangements made by the insurance intermediary or insurance undertaking are not sufficient to ensure that risks of damage to customer interests will be prevented, the insurance intermediary or insurance undertaking shall inform the customer of this fact in good time before the conclusion of the insurance contract.

As regards its obligation to provide information to its customers, an insurance intermediary or an insurance undertaking shall provide its customers with: (i) a periodic assessment of the suitability of the insurance-based investment products recommended to that customer; (ii) appropriate guidance on, and warnings of, the risks associated with the insurance-based investment products or in respect of particular investment strategies proposed; (iii) information on costs and charges, including the cost of advice (where provided) and the cost of the insurance-based investment product, and on the means of payment.

Article 29 of the IDD also establishes that insurance intermediaries and insurance undertakings shall in any case be considered to have complied with their obligations under the Directive, should they receive fees, commission or non-monetary benefits from parties other than customers, provided that such payments or benefits do not have a detrimental impact on the quality of the service provided or on due compliance with the obligation to act in the customer's best interests. In any case, without prejudice to the Member States' right to prohibit or further restrict the offer or acceptance of fees, commissions or non-monetary benefits from third parties in relation to the provision of insurance advice, or to their right to require that, where an insurance intermediary informs the client that advice is given independently, the intermediary shall assess a sufficiently large number of insurance products available on the market which are sufficiently diversified with regard to their type and product providers.

Article 30 of the IDD also deals with the obligations in relation to the assessment of the suitability and appropriateness of insurance-based investment products in the event of the provision or otherwise of advice, defined by Article 1 as "*the provision of a personal recommendation to a customer, either upon their request or at the initiative of the insurance distributor, in respect of one or more insurance contracts*".

Without prejudice to the general obligations to provide information, set out in Article 20, insurance intermediaries and insurance undertakings that provide advisory services, must: (i) obtain the necessary information regarding customers' knowledge and experience in the investment field relevant to the specific type of product or service, their financial situation and their investment objectives, and (ii) recommend to customers the insurance-based investment products that are suitable for those customers and that, in particular, are in accordance with their risk tolerance and ability to bear losses.

Where no advice is offered, the intermediaries and undertakings shall limit their request for information to the customer's knowledge and experience.

As provided for in the previous directive, where the insurance intermediary or insurance undertaking considers, on the basis of the information received, that the product is not appropriate for the customer, the insurance intermediary or insurance undertaking shall warn the customer to that effect. Where customers do not provide such information, the insurance intermediary or insurance undertaking shall warn them that it is not in a position to determine whether the product envisaged is appropriate for them. That warning may be provided in a standardised format.

The IDD also establishes that Member States may introduce a simplified system of distribution for insurance intermediaries or insurance undertakings that do not provide customers with advice, a system that resembles the *execution only* service provided in the field of financial intermediation. In particular, insurance intermediaries and undertakings may be exempted from the obligation to request information about the customer's knowledge and experience, in the following cases:

- where the underlying of a product is a non-complex financial instrument;
- where the insurance distribution activity is carried out at the initiative of the customer;
- if the customer has been clearly informed that the insurance intermediary or the insurance undertaking is not required to assess the appropriateness of the product, and that the customer does not benefit from the corresponding level of protection;
- if the insurance intermediary or insurance undertaking complies with its obligations in regard to conflicts of interest.

The obligations of insurance intermediaries and undertakings also specifically include: (i) the establishment of records containing the documents specifying the parties' rights and obligations, and the terms on which the service is provided; (ii) the provision, on a durable medium, of regular reports including those pertaining to costs; (iii) in the event that advice is provided, the provision to the customer of a suitability statement specifying how such advice meets the customer's requirements.

4. Product oversight and governance requirements

Finally, the provisions set out in Article 25 of the IDD, regarding product oversight and governance requirements, are of interest here. They make provision for the introduction into the Italian legal system, in general and regardless of the nature of the insurance contract, of rules that once again refer to certain principles indicated in the joint letter of the Bank of Italy and IVASS concerning insurance policies combined with financings.

In fact, Article 25 establishes that insurance undertakings - as well as intermediaries which manufacture any insurance

product for sale to customers - shall maintain and operate specific procedures for the approval of each insurance product, the definition of its contents, and any significant adaptations to such, before it is marketed or distributed to customers.

Said procedure presupposes (on the basis of Article 25 once again) the analysis of an identified target market, that the intended distribution strategy is consistent with the identified target market, that reasonable steps are taken to ensure that the insurance product is distributed to the identified target market; and that principles are adopted for the regular review of both the products and the procedure itself, in order to ensure that the product constantly meets market requirements.

AUTHORS



David Maria Marino

Partner

Milan | T: +39 02 806181

davidmaria.marino@dlapiper.com



Andrea Pantaleo

Lead Lawyer

Milan | T: +39 02 806181

Andrea.Pantaleo@dlapiper.com
