Implementation of IDD: impact on insurance and reinsurance distributors and better protection for policyholders

On 22nd August 2018, the law of 10th August 2018 (implementing the EU Directive 2016/97 of the European Parliament and of the Council of 20 January 2016 on insurance distribution ("**IDD**") and amending the law of 7 December 2015 on the insurance sector, as amended (the "**2015 Law**")) (the "**2018 Law**" or the "**Law**") was published in the Luxembourg Official Gazette n°710. The Law will enter into force on 1st October 2018.

Although the main purpose of this Law consists essentially in implementing IDD into the 2015 Law by introducing a similar protection when buying insurance products as the protection offered by the revised market in financial instruments directive[1] (MiFID II) in relation to financial products, the Luxembourg legislator took the opportunity in the 2018 Law to also reshape the preferential right granted to insurance creditors.

1. New provisions relating to insurance and reinsurance distribution

The main changes brought by the 2018 Law on insurance and reinsurance distribution may be summarised as follows:

- Extension of the scope of insurance and reinsurance distribution authorisation requirements;
- Clarification of the rules relating to insurance and reinsurance distribution on a cross-border basis;
- New rules of conduct applicable to insurance distribution.

[1] Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU

1.1. Changes to the scope of insurance and reinsurance distribution authorisation requirements

The objective of IDD was that customers, when buying insurance products, should benefit from the same level of protection notwithstanding the type of distribution channel being used. In this respect, any person or entity distributing insurance or reinsurance products (even on an ancillary basis) should be caught by the rules on distribution to ensure a level playing field between these different actors.

In this context, the scope of application of the rules governing insurance and reinsurance distribution activities of the 2015 Law, and thus the scope of authorisation as insurance or reinsurance distributor, has been extended to insurance and reinsurance undertakings directly marketing insurance products as well as to any natural or legal person who sells insurance products on an ancillary basis (e.g. travel agents and car rental companies), to the extent that they do not fall within the exclusions provided for in the Law (notably where the premium falls below a certain threshold).

It should also be noted that one of the innovations of the 2015 Law is the possibility to obtain an authorisation as insurance intermediary for only one branch of insurance.

Finally, precisions have been provided as to which activities are not considered as insurance distribution, which thus do not fall within the scope of authorisation (and would more be considered as so-called "business introducer" (*apporteur d'affaires*) activities).

1.2. Clarifications in relation to the distribution of insurance and reinsurance products on a cross border basis.

The Law simplifies the applicable regimes relating to business carried out under the freedom to provide services or the freedom of establishment. The registration of insurance, reinsurance and ancillary insurance intermediaries with their home Member State shall indeed facilitate the free provision of services in another Member State, provided that appropriate notification has been made to the *Commissariat aux Assurances*.

The Law further specifies the split of responsibilities between the home Member State and the host Member State supervisory authorities as well as their respective cooperation duties in relation to insurance intermediaries.

1.3. New rules of conduct and information requirements applicable to insurance distributors

Insurance distributors are now subject to new conduct of business standards. As a general principle, when distributing insurance products, insurance distributors must (i) always act in accordance with the best interest of their customers and (ii) ensure that all information addressed to their customers (or prospective customers) is fair, clear and not misleading.

☐ **Pre-contractual information**. First of all, insurance distributors (and insurance companies, when directly distributing their products) are required to provide a series of pre-contractual information to potential policyholders relating to them. Any potential conflict of interest must also now be clearly disclosed to the potential policyholder. Finally, before entering into an insurance agreement, the distributor is required to provide the customer with relevant information on the insurance product in an intelligible form (such information must be provided as a standardised "key information document" for non-life insurance products) with the objective to enable customers to make an informed decision while such products. All pre-contractual information must be provided in a durable medium.

Additional information must be provided in case of cross-selling (*i.e.* when an insurance product is offered together with an ancillary product or service which is not insurance, as part of a package or the same agreement).

Finally, similar obligations apply to insurance distributors on an ancillary basis.

☐ **Provision of advice in relation to insurance products.** Prior to the sale of insurance products, the insurance distributor is required to carry out a customer's demands and needs test. In addition, a personalised recommendation must be provided to the customer regarding the insurance product, and explaining why a particular product best meets the customer's insurance demands and needs. The Luxembourg legislator took the option that Luxembourg customers are to be automatically provided with such advice but that a customer can, however, accept to renounce to such advice.

☐ **Product oversight and governance arrangements.** Two sets of obligations have now become applicable: on the one hand, obligations applicable to manufacturers of insurance products and on the other, obligations applicable to persons who advise or offer insurance products.

☐ **Requirements in relation to insurance-based investment products.** On top of the obligations as stated above (information, advice, internal organisation, etc.) and the obligations pursuant to PRIIPS[2], the distribution of insurance based investment products ("**IBIPs**") is subject to additional requirements such as, *i.a.* the prevention and management of conflicts of interest, information requirements and, where applicable, suitability or appropriateness assessments.

☐ **Inducements.** Although there were many discussions at Luxembourg level in this respect, Luxembourg chose the option offered by IDD not to include provisions regarding inducements. However, depending on the applicable law, the local laws and regulations regarding inducements may be applicable.

[2] Regulation (EU) N°1286/2014 of the European Parliament and of the Council of 26 November 2014 on key information documents for packaged retail and insurance-based investment products (PRIIPS) (OJ L 352/1, 9.12.2014, p.1)

In addition to the above rules, IDD, and thus now the 2015 Law, is completed by a series of implementing and delegated acts, in particular in relation to (i) the standardised presentation format for the insurance product information document, (ii) product oversight and governance requirements and (iii) information requirements and conduct of business rules applicable to the distribution of insurance-based investment products.

2. New regime of preferential rights granted to insurance creditors

Prior to the 2018 Law, all policyholders had a first ranking privilege over all the assets underlying technical provisions of a given insurance company in case of the liquidation of an insurance company, irrespective of the type of insurance contract held by each policyholder.

Via the Law the Luxembourg legislator, with the objective of better protecting the different classes of insurance creditors taking into account their specific situations, has reshaped such regime. Indeed, the new Articles 253-1 to 253-6 of the 2015 Law now provide for the evaluation of the insurance receivables (which shall be carried out on the basis of different criteria for life insurance and non-life insurance, with a distinction between standard life insurance and unit-linked insurance), and then a privilege shall be applicable only on the assets representing a particular type of insurance (e.g. a unit-linked policy holder will have a first ranking privilege only over the assets representing the technical provisions relating to unit-linked insurance contracts, and not generally over all assets representing the technical provisions of the relevant insurance company). In case the total number of units which are part of a given category of assets is not sufficient, then the first ranking privilege shall be proportionally reduced.

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