

Response to EC consultation on integration of sustainability factors and preferences into the IDD

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Summary

■ Scope and legal instruments

The proposed amendments of 2017/2358/EU are inappropriate. This Delegated Regulation applies to all insurance products not only to insurance-based investment products (IBIPs). Amending product oversight and governance requirements for risk insurance (eg, home, health, motor) is unworkable in many instances.

Equally the references to the Sustainable Finance Disclosure Regulation (SFDR) are to a Regulation that applies only to products with an investment purpose (eg, IBIPs, pension products). Including references in 2017/2358/EU extends the scope of SFDR definitions to also cover other products for which they are not applicable.

It should be noted that the requirement to include sustainability considerations should only apply to products intended to be designed as sustainable. The current drafting does not make this distinction clear and implies that sustainability considerations should always be taken into account even where there are none.

■ Definition of sustainability preferences

The new definition of sustainability preferences based on the SFDR lacks the necessary flexibility to allow insurers to react to the needs of their customers. We understand the desire to reflect product categorisation under the SFDR, but the creation of additional categories of products through this initiative is unhelpful. Further consideration of the impact of this definition on product offering is necessary.

■ Conflicts of interest

The Insurance Distribution Directive (IDD) – and its delegated regulations – already establish appropriate criteria for determining different types of conflicts of interest. Any conflicts of interest that may arise from taking into account the sustainability objectives of customers would be captured by these criteria, and would be handled in the same way as any other conflicts of interest under the IDD. The detailed additions to the IDD regarding conflicts of interest are as such unnecessary.

■ Target market

Insurance undertakings are not required to consider sustainability factors in the product approval process of all insurance products. We are supportive of EIOPA's original approach that makes clear that an insurer should only take into account the sustainability profile of the product where it is relevant with regard to the respective target market, as this better reflects insurers' obligations under the IDD. The legislator has specifically limited

mandatory screening with regard to sustainability factors to large providers of products in the scope of the SFDR (Article 4 (3) and (4) SFDR). Provisions on level 2 should not create legal uncertainty in this regard.

■ Implementation timeframe

Insurance Europe welcomes the implementation period of 12 months starting with the entry into force of the Act. Insurers and intermediaries need sufficient time to implement the rules once they are finalised.

Detailed Comments

■ Legal instrument

While the amendment of the delegated act specific to insurance-based investment products seems appropriate, the amendment of the delegated act concerning the product oversight and governance (POG) requirements for all insurance products is problematic.

According to the IDD, POG requirements apply to all insurance undertakings regarding the distribution of their products, and thus, to risk insurance as well as insurance-based investments. This means that without any additional precision, this proposal would make the references to “sustainability factors” and “sustainability preferences” applicable to every insurance product, such as home, health or motor insurance, which would rarely be relevant.

The proposed amendments to 2017/2358/EU should only apply where they are relevant and this should be reflected in the legal text.

We would propose that the European Commission reverts back to the drafting provided by the European Insurance and Occupational Pensions Authority (EIOPA) in its final advice, as this provides much needed legal clarity.

Since the definition in Article 2, point (4) of Commission delegated regulation (EU) 2017/2359 only applies to IBIPs and could not be related to pure risk insurance products, it would be more relevant to **amend article 4(3)(a), point (i) of the delegated Regulation (EU) 2017/2358** as follows: “(i) it takes into account the objectives, interests and characteristics of customers, including any sustainability preferences as defined in Article 2, point (4), of Commission Delegated Regulation (EU) 2017/2359 where relevant*;”

Article 5 of the delegated Regulation (EU) 2017/2358 could be replaced by the following:

“1. The product approval process shall for each insurance product identify the target market and the group of compatible customers. The target market shall be identified at a sufficiently granular level, taking into account the characteristics, risk profile, complexity and nature of the insurance product, as well as the sustainability-related profile of the product where relevant.

2. Manufacturers may, in particular with regard to insurance-based investment products, identify groups of customers for whose needs, characteristics and objectives, including any sustainability preferences as defined in Article 2, point (4), of Commission Delegated Regulation (EU) 2017/2359 where relevant, the insurance product is generally not compatible.

3. Manufacturers shall only design and market insurance products that are compatible with the needs, characteristics and objectives, including any sustainability preferences where relevant, of the customers belonging to the target market. When assessing whether an insurance product is compatible with a target market, manufacturers shall take into account the level of information available to the customers belonging to that target market and their financial literacy.”

■ Definition of Sustainability Preferences

The reference to sustainable investments and the consideration of principal adverse impacts on sustainability factors for products that promote environmental or social objectives is potentially damaging.

We acknowledge the need for clarification on the difference between “Article 8” and “Article 9” products of the SFDR. However, introducing yet another category of sustainable products would, in our view, not resolve this problem.

The definition of sustainability preferences should refer to the existing categories of sustainable products in Article 8 and 9 of the SFDR, without adding the further qualifications proposed as sub-points (i) and (ii) of Article 2 (4). The legislator has devised Article 8 and 9 of the SFDR in order to take account of the variety of sustainable products available on the market (Recital 21). Introducing a third (i) and fourth (ii) category of sustainable products in the context of the IDD would, in our view, raise further legal uncertainties, without apparent benefit to the customer.

It would, for instance, mean that until 30 December 2022 the customer’s desire for a product which excludes certain investments from its portfolio (eg, fossil fuels, child labour, etc.) would not constitute a sustainability preference within the meaning of the Delegated Regulation. Similarly, the French Socially Responsible Investment (SRI) label does not have sustainable investments as its objective and also does not require excluding underlying assets with significant adverse impacts. However, it promotes environmental and social characteristics since awarded funds select companies based on their ESG performance. Making references to sustainable investments and the consideration of principal adverse impacts could lead one to consider that such SRI funds cannot meet consumers’ sustainability preferences, even though this may be a very appropriate product for the target market.

It should be possible to take into account the customer's sustainability preferences where the customer would prefer a product that promotes environmental or social characteristics, even if said product would not fulfil the requirements set out in the draft regulation, Art. 2(1) points (4)(b) (i) and (ii).

To ensure consistency, “Article 8” and “Article 9” products under the SFDR should be able to meet consumers’ sustainability preferences with no further requirements.

■ Conflicts of interest

The IDD – and accompanying delegated regulation – already establishes appropriate criteria for determining different types of potential conflicts of interest given both the financial and non-financial objectives of the customer. Any potential conflicts of interest that may arise with regard to sustainability objectives will be captured by these criteria and handled in the same way as any other conflict of interest under the IDD. It is unlikely that the inclusion of sustainability factors would introduce any specific conflicts of interest that cannot be addressed within the existing IDD framework.

Insurance Europe agreed with EIOPA’s original advice that a reference only to sustainability considerations could over-emphasise and unbalance the legal drafting. The insurance sector supports a high-level principle-based approach, as suggested by EIOPA in paragraph 92 of its draft technical advice. As EIOPA pointed out (on page 42-43 of its draft technical advice), a recital could have been used to provide guidance on the application of the conflict of interest rules.

The insurance sector would also like to draw attention to the fact that neither the IDD nor the delegated acts require insurance undertakings to offer insurance products with sustainability considerations. Insurance undertakings and insurance intermediaries should therefore not be expected to include sustainability considerations in their conflicts of interest policy in general, but only where relevant. This not well reflected in the amendments to the Delegated Acts put forward by the Commission. This would also be consistent with other parts of the draft technical advice.

It is perhaps also worth noting that the more demand there is for products contributing to sustainable investment, the more insurance intermediaries will engage in distributing such products.

■ Target market

Insurance Europe was supportive of EIOPA's approach that insurance undertakings should not be required to consider sustainability factors in the product approval process of all insurance products, but only if the insurance product is to be advised or sold to customers with sustainability preferences – ie, sustainability preferences of customers should be considered in the assessment of the target market only with regard to "sustainable products". It is unfortunate that the Commission has chosen to apply these provisions more broadly.

The obligation to take into account sustainability factors in the POG processes of all products should be reconsidered. "Sustainability factors" is a legal term used in the SFDR to describe the impacts of an investment on sustainability issues. In order to avoid legal uncertainty, we propose to refer to "the sustainability profile of the product (where relevant)" in Article 5 (1) of the Delegated Regulation as proposed by EIOPA in its technical advice (EIOPA-BoS-19/172). This would be a sensible approach to integrate sustainability considerations into the product approval process where this is relevant for the respective target market.

Similarly, Article 5.3 of delegated Regulation 2017/2358 is unclear. It would be helpful to also specify here that insurers are not required to offer sustainable products, and these considerations only apply where relevant.

Article 5 of Delegated Regulation (EU) 2017/2358 on Target market

1. The product approval process shall for each insurance product identify the target market and the group of compatible customers. The target market shall be identified at a sufficiently granular level, taking into account the characteristics, risk profile, complexity and nature of the insurance product, as well as ~~its sustainability factors~~ **the sustainability-related profile of the product (where relevant)**, ~~and the consideration of principal adverse impacts on sustainability factors, if any.~~

3. *Manufacturers shall only design and market insurance products that are compatible with the needs, characteristics and objectives, including, **where relevant, for insurance-based investment product**, any sustainability preferences of the customers belonging to the target market.*

■ Further clarifications

The Commission's first draft to amend the rules on the suitability assessment in Delegated Regulation (EU) 2017/2359) regarding sustainability considerations dated January 2019 contained useful clarifications in its recitals which are, however, not included in the current draft.

The explanatory memorandum notes potential issues "should a sustainability factor take precedence over a client's personal investment objective". This is said to be reflected in a recital, but there appears not to be any references in the legal text.

The explanatory memorandum also states that a "new suitability assessment for existing contracts will not be necessary". It is also stated that, for legal certainty purposes, this would be clarified in the proposal. However, such a clear clarification does not appear in the proposed legislative amendments and should be added. Similarly, Recital 8 of the Commission's January 2019 draft provided clarification with regard to existing customers is missing in the final Delegated Acts, despite references to this in the explanatory memorandum.



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