## THE FULLCOVER

NUMBER #13 SPRING 2020 · MDS MAGAZINE · ENGLISH EDITION



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## **Legal Corner**

## IDD, preventing a conflict of interest

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n January 2016, the European Parliament and Council ratified the Insurance Distribution Directive (IDD) 2016/97 which was subsequently translated into Portuguese law (ruling 7/2019, 16/01). In late November 2019, all European Union members, except Spain, had incorporated the Directive into their national legal framework. The IDD aims to regulate the way insurance products are designed and sold both by brokers and insurance carriers, enhance consumer protection, whatever the distribution channel, and

Central to this is product governance and ensuring policies meet market needs. For that purpose, the IDD has guidelines for business conduct, such as the reinforcement of requirements regarding reporting and preventing a conflict of interest, particularly relating to the distribution of insurance-based investment products (Commission Delegated Regulation (EU) 2017/2359, 21/09/2017).

further transnational commerce.

In Portugal, conflicts of interest arose following regulation about incompatibility regarding access to the activity of insurance intermediaries fullcover #13

and the provision of pre-contract information to customers of brokers with qualifying holdings in insurance companies, or an insurance carrier's qualifying holdings in the broker's registered capital.

To demonstrate impartiality and remove any conflict of interest, brokers are required to provide pre-contract information which is non-binding and based upon unbiased, personal analysis. Any advice must relate to the situations brokers are presented with. Brokers should also inform whether they are contract-bound to work exclusively for one or more insurance carriers.

One of the more relevant and most debated regulations is the rules of conduct on remuneration.

The IDD adopts a broad definition of remuneration: direct payments from the customer to the broker, fees that form a part of the insurance premium and any other economic benefit gained as a result of the insurance contract, or a combination of the three.

The Directive rules insurance distributors must not be remunerated nor remunerate or assess their employees' performance in ways incompatible with their duty to act in the customer's best interest. An insurance distributor must not recommend schemes for remuneration that depend on sales objectives being met or any others of such kind that would constitute an incentive for the broker or its employees, nor recommend a particular product to a customer when a different product might have been more suitable.

Before an insurance contract is signed, the broker must inform the customer on the remuneration package, the fees owed by the customer or, if not possible, the calculation methods. The broker must also advise about the customer's right to inquire about any non-fee remuneration and provide such information if requested to do so.

The new demands of the IDD require insurance companies to go to great lengths to adapt their remuneration policies.

Stricter rules also govern insurance-based investment products, due to the risks they may pose to customers.

To identify conflicts of interest, insurance distributors must assess whether they, or any other relevant persons, including where they have an element of control, are biased in the outcome of distribution activities which may fail to meet the customers' requirements and be to their detriment.

The minimum criteria to evidence a conflict of interest with insurance-based investment products are:

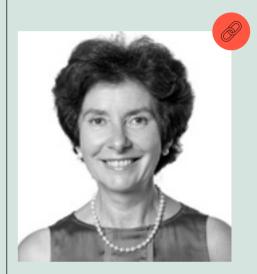
- . envisaged financial gain or avoidance of financial loss to the customer's detriment
- existence of financial incentive, or any other incentive, so as to favour the products provided by another person or group of people to the detriment of the customer
- . the distributor, or relevant person, actively participates in the management or development of insurance-based investment products, particular in connection with product pricing or related distribution costs.

The distribution of said products demands regulations to cover the prevention, reporting and handling of conflicts of interest, and in turn, they must also take into account the distributor's scope, business volume, products distributed and customer risks. These must be reviewed annually and operate under the principles of fairness.

Preventing a conflict of interest is fundamental, therefore informing customers of a conflict of interest appears a last resort measure, only for occasions where the policies in place prove to be incompatible with the customers' needs. Distributors therefore have a duty to be fully transparent with customers about the nature of a conflict of interest before contracts are entered into. •

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