



# FSO Legal & Regulatory Update IDD - ESG Impact

September 2022

# How to integrate the client's sustainability preferences in the suitability assessment of an insurance-based investment product?

On 20th July, EIOPA published a guidance with the objective of helping insurance distributors, namely insurance firms and intermediaries, to integrate the new requirements on customer's sustainability preferences in the suitability test required under IDD (1). Indeed, since the amendments (2) to Commission Delegated Regulation (EU) 2017/2359 with regard to information requirements and conduct of business rules applicable to the distribution of insurance-based investment products (3) ("IDD Delegated Regulation"), which came into force on 2th August 2022, distributors of insurance-based investment products ("IBIPs") are now required to integrate sustainability preferences into the suitability assessment of an IBIP when advice is given on its distribution. Under Belgian law, this guidance applies more generally to all savings and investment products (except for second-pillar pension products), given the extension of the IBIP concept to these products by the Belgian legislator.

The EIOPA guidance addresses the integration of customer's sustainability preferences by contextualising these in the different stages of the operational scheme of insurance distribution. More particularly, the document addresses:

- ▶ information to be provided to the client on the objectives and scope of the collection of the client's sustainability preferences as part of the suitability assessment of an IBIP;
- ▶ the modalities of the collection of the customer's sustainability preferences;
- ▶ the modalities of the (periodic) evaluation of the customer's sustainability preferences;
- ▶ the integration of sustainability requirements into the continuous education of insurance distributors.

Based on this new guidance, a distributor of IBIP can use the following roadmap including **6 key actions** to ensure that its operational framework and due diligence process, and more specifically the so-called 'suitability test', are in line with the regulatory requirements for sustainability preferences.

(1)EIOPA, [Guidance on the integration of sustainability preferences in the suitability assessment under IDD](https://www.eiopa.europa.eu/media/news/eiopa-publishes-guidance-integrating-customer%E2%80%99s-sustainability-preferences-suitability_en), 20 July 2020, [https://www.eiopa.europa.eu/media/news/eiopa-publishes-guidance-integrating-customer%E2%80%99s-sustainability-preferences-suitability\\_en](https://www.eiopa.europa.eu/media/news/eiopa-publishes-guidance-integrating-customer%E2%80%99s-sustainability-preferences-suitability_en).

(2) These changes stem from Commission Delegated Regulation (EU) 2021/1257 of 21 April 2021 amending Delegated Regulations (EU) 2017/2358 and (EU) 2017/2359 as regards the integration of sustainability factors, sustainability risks and sustainability preferences into the supervisory and product governance requirements applicable to insurance undertakings and insurance intermediaries, and into the conduct of business rules and rules governing investment advice applicable to insurance-based investment products.

(3) Commission Delegated Regulation (EU) 2017/2359 of 21 September 2017 supplementing Directive (EU) 2016/97 of the European Parliament and of the Council as regards information requirements and conduct of business rules for the distribution of insurance-based investment products.



## 1<sup>st</sup> key action

### Include explanation of 'sustainability preferences' in the interview with the customer

Before asking the customer to make a choice about his sustainability preferences, the insurance distributor should be able to explain in a clear manner the different options available and what these are.

The insurance distributor is thus expected to be able to explain the three sustainability preference choices foreseen by the IDD Delegated Regulation, namely that of an IBIP:

- ▶ which is invested in sustainable investments as defined under Regulation (EU) 2019/2088 on sustainability-related disclosures in the financial services sector ("SFDR") (4), i.e. investing in economic activities contributing to an environmental or social objective provided that the investment does not significantly harm any other environmental or social objective and that the investee companies follow good governance practices (**choice 1**);
- ▶ which is invested in environmentally sustainable investments within the meaning of Regulation 2020/852 on the establishment of a framework to promote sustainable investment (5) ("Taxonomy Regulation") (**choice 2**);
- ▶ which takes into account principal adverse impacts on the sustainability factors (**choice 3**).

In particular, these explanations can be provided on the basis of the ESG standardised information document (6).

(4) Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on sustainability-related disclosures in the financial services sector.

(5) Regulation (EU) 2020/852 of the European Parliament and of the Council of 18 June 2020 on the establishment of a framework to facilitate sustainable investment, and amending Regulation (EU) 2019/2088.

(6) Annex 2 and 3 to Commission Delegated Regulation (EU) 2022/1288 of 6 April 2022 supplementing Regulation (EU) 2019/2088 of the European Parliament and of the Council with regard to regulatory technical standards specifying the details of the content and presentation of the information in relation to the principle of 'do not significant harm', specifying the content, methodologies and presentation of information in relation to sustainability indicators and adverse sustainability impacts, and the content and presentation of the information in relation to the promotion of environmental or social characteristics and sustainable investment objectives in pre-contractual documents, on website and in periodic reports.





## 2<sup>d</sup> key action

### Redesign your suitability test

The customer's sustainability preferences must be collected after the insurance distributor has properly analysed the customer's knowledge and experience, as well as his financial situation and other investment objectives. The only exception to this principle is when the customer proactively communicates his preferences in this regard at the beginning of the meeting.

### **3<sup>d</sup> key action**

#### **Include questions on sustainability preferences in your suitability test**

##### **► Assess in the first place the client's interest in sustainability aspects**

Once explanations on 'sustainability preferences' have been provided, the insurance distributor may start collecting information from the client with a binary question asking whether the client wishes to integrate certain sustainability aspects into his investment objectives more generally.

If the client does not wish to express his sustainability preferences or if sustainability aspects are not relevant to him, the insurance distributor may consider this client as 'neutral' and consequently offer him IBIPs with or without sustainability features.

However, if the customer wants to make a sustainability preference choice, the insurance distributor will have to deepen its knowledge of the customer's sustainability preferences by gathering additional information.

##### **► Get to know the customer better in relation to their sustainability preferences**

The evaluation grid for further enquiry into the customer's sustainability preferences should be based on the three sustainability aspects that an IBIP can have, which should, as a reminder, be explained to the customer before asking him to make a sustainability choice. In this respect, the insurance distributor should also allow the customer to make a combination of the three sustainability preference choices offered.

In addition, for choices 1 and 2, in order to better understand the client's sustainability preferences, questions on minimum investment proportions should also be asked. In this respect, standardised percentages can be proposed to the client to facilitate his choice in a neutral way.

In addition, with regard to choice 2, the distributor will, before asking the client to make this quantitative choice, also have to explain to the client the two types of key performance indicators ("KPIs") used to calculate the alignment and the choice that can be made by the client of one and/or the other of these KPIs. This explanation should be consistent with the information reflected in the ESG standardised information document to be provided to the client (7), which should however only be legally available from 1st January 2023.

(7) Section "To what minimum extent are sustainable investments with an environmental objective aligned with the EU taxonomy?" of the ESG standardised disclosure document set out in Annexes 2 and 3 of Commission Delegated Regulation (EU) 2022/1288 of 6 April 2022 supplementing Regulation (EU) 2019/2088 of the European Parliament and of the Council with regard to regulatory technical standards specifying the details of the content and presentation of the information in relation to the principle of 'do not significant harm', specifying the content, methodologies and presentation of information in relation to sustainability indicators and adverse sustainability impacts, and the content and presentation of the information in relation to the promotion of environmental or social characteristics and sustainable investment objectives in pre-contractual documents, on website and in periodic reports.



Finally, with regard to choice 3, information on the quantitative or qualitative aspect of the principal adverse impacts ("PAI") should also be collected. In this respect, the client may be offered a choice of categories or families of PAI, without going into an exhaustive list of all possible PAI.

► **Consider the specificities of IBIPs under branch 23**

For IBIPs under branch 23, the details collected on the client's sustainability preferences (i.e. minimum investment proportion and PAI) may, at the client's discretion, apply either generally to all or only to some of the underlying investment options offered under that IBIP and chosen by the client.

## 4<sup>th</sup> key action

### **Reflect the client's sustainability preferences in the suitability statement**

► **Analyse the results of the suitability assessment appropriately**

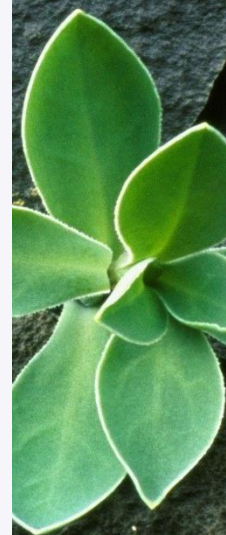
As the customer's sustainability preferences are only taken into account after the assessment of his financial situation and other investment objectives, the final selection of IBIPs to be offered to the customer can only be made from the panel of products pre-selected after this pre-assessment. If none of the 'pre-selected' products can meet the sustainability preferences expressed by the customer, the insurance distributor will have to provide the customer with an appropriate explanation in this respect before informing him of his right to adapt his initial sustainability choices.

If the customer decides to adapt his sustainability preferences, the insurance distributor will not only have to provide him with information on the insurance products that coincide with his choices, but also inform him whether or not the products offered are products distributed solely by him.

If the customer does not express a specific sustainability preference, it will be up to the insurance distributor to offer the insurance products that best match the general choice expressed by the customer. However, before reaching such a conclusion, the insurance distributor should ensure that the customer has a clear understanding of what sustainability means and, if necessary, re-explain the different concepts.

► **Ensure that the pre-contractual information provided to the customer matches with the customer's expressed sustainability preferences**

In order to define the final selection of products corresponding to the client's knowledge and experience but also to his financial situation and investment objectives, including more specifically his sustainability preferences, the insurance distributor will have to ensure in particular that the pre-contractual ESG information to be provided to the client in relation to the products in question matches the choice expressed by the client.

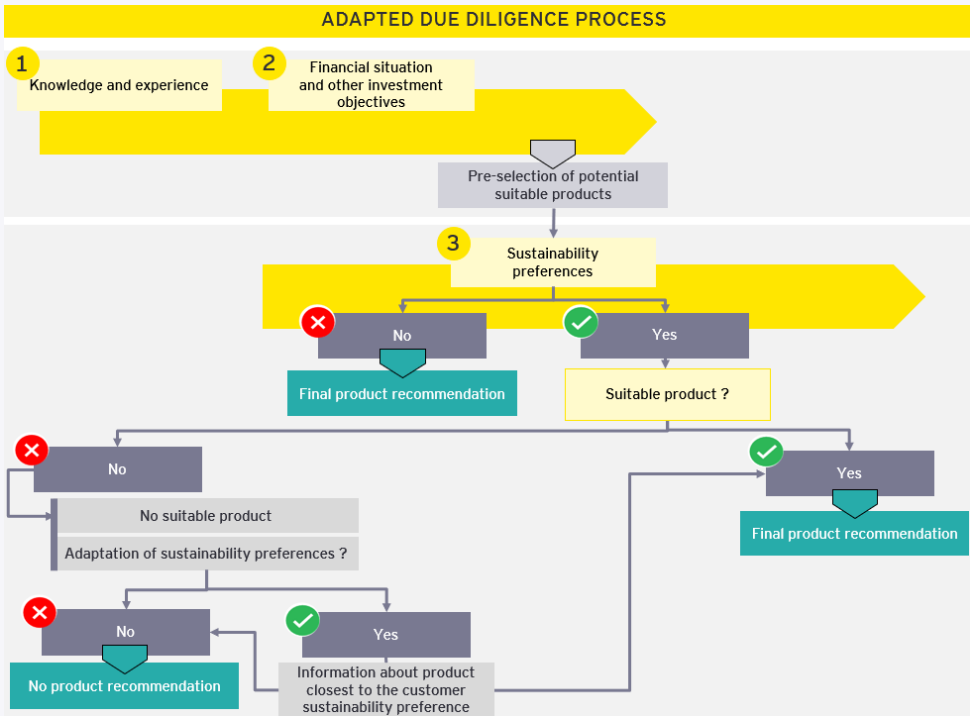


In this respect, during the transitional period from 2 August 2022 to 31 December 2022, such correspondence will in principle be limited to the pre-contractual information provided to the client and available on the insurer's website, in accordance with the provisions of the SFDR and the applicable Taxonomy Regulation.

As of 1st January 2023, when the Commission Delegated Regulation (EU) 2022/1288 (8) will come into force, the insurance distributor will have to ensure that the customer's sustainability preferences correspond to the pre-contractual information provided to him through the ESG standardised information document and the specific product information on the distributor's website (9). In this respect, particular attention should be paid to the possible choice of minimum proportions provided by the client. To this end, the insurance distributor can develop a matrix to classify all the products it distributes according to the various sustainability aspects included in its suitability assessment questionnaire.

► **Formalise the sustainability preferences expressed by the client**

The monitoring of the operational path, including the client's choices and decisions as well as the recommendations given by the insurance distributor, should be expressly reflected in the suitability statement to be provided to the client at the end of the suitability assessment.



(8) Commission Delegated Regulation (EU) 2022/1288 of 6 April 2022 supplementing Regulation (EU) 2019/2088 of the European Parliament and of the Council with regard to regulatory technical standards specifying the details of the content and presentation of the information in relation to the principle of 'do not significant harm', specifying the content, methodologies and presentation of information in relation to sustainability indicators and adverse sustainability impacts, and the content and presentation of the information in relation to the promotion of environmental or social characteristics and sustainable investment objectives in pre-contractual documents, on website and in periodic reports.

(9) These choices should correspond to the information in the sections 'To what extent are sustainable investments with an environmental objective aligned with the EU taxonomy?' and 'What is the intended asset allocation of this financial product?' / 'What is the asset allocation and the minimum share of investments?' of the ESG standardised disclosure document set out in Annex 2 and 3 to Commission Delegated Regulation (EU) 2022/1288 of 6 April 2022 supplementing Regulation (EU) 2019/2088 of the European Parliament and of the Council with regard to regulatory technical standards specifying the details of the content and presentation of the information in relation to the principle of 'do not significant harm', specifying the content, methodologies and presentation of information in relation to sustainability indicators and adverse sustainability impacts, and the content and presentation of the information in relation to the promotion of environmental or social characteristics and sustainable investment objectives in pre-contractual documents, on website and in periodic reports

## 5<sup>th</sup> key action

### Include questions on sustainability preferences in the eventual periodic suitability assessment

Provided that the insurance distributor has undertaken to do so in its declaration of suitability, the periodic suitability assessment to be provided will in future also have to include a review of the customer's sustainability preferences in order to ensure that the recommended products still correspond to the customer's possibly adapted sustainability preference at the time of the assessment.

Therefore, in the event of an adaptation of sustainability preferences by the customer, the insurance distributor will have to measure the impact on the product held by the customer, inform the customer appropriately, if necessary modify its recommendation and formalise this new assessment in a new or additional suitability statement.

## 6<sup>th</sup> key action

### Train your staff

In order to be able to implement these recommended adjustments to the procedural framework, it is a necessary prerequisite that the relevant employees (i.e. including persons in contact with the public and persons responsible for distribution) of every insurance company and intermediary distributing IBIPs (whether or not they are of a sustainable nature) should be provided with basic knowledge and skills about sustainability preferences in their ongoing training.

Furthermore, where the insurance distributor offers IBIPs that promote environmental or social characteristics or pursue a sustainability objective in accordance with the respective requirements of Articles 8 or 9 of SFDR, this basic foundation must be supplemented by appropriate training in relation to the sustainability characteristics of IBIPs offered by the insurance distributor.

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This roadmap has been established on the basis of the EIOPA guidance, and is not legally binding *vis-à-vis* the FSMA or insurance undertakings and intermediaries. However, as EIOPA has announced that it intends to publish guidelines following this guidance, it can only be recommended to the concerned insurance distributors to integrate the requirements for sustainability preferences into their internal processes according to this first interpretation given by EIOPA in this respect, subject to a stricter position adopted by the FSMA.





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