

IVASS consults again to review the regulatory framework governing unit and index linked products

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On 28 March 2024, IVASS launched a second public consultation on a draft regulation regarding unit and linked insurance products. The purpose of the draft regulation is to lay down the rules aimed at updating, in line with regulatory changes occurred at the European and national levels, the provisions governing this kind of insurance policies. The new draft is intended to reflect the high number of comments raised by the market in the context of the previous public consultation held in 2022 on the same subject, during which the following topics, among others, were heavily commented: (i) the extension of the scope of application of the new rules to EU insurers marketing linked-type policies in Italy; (ii) the alignment of the rules governing limits to investments of assets underlying unit-linked policies to the Italian regulation on UCITS; (iii) the rules on costs and management fees in the case of funds investing in linked CIUs; (iv) the rules on the coverage of a demographic risk.

Following a first public consultation launched in March 2022 (please click [here](#) to access our previous news in this regard), on 28 March 2024 the Italian insurance regulator (“**IVASS**”) published for consultation a new draft of the regulation (the “**Draft Regulation**”) containing the rules governing unit-linked and index-linked insurance contracts (i.e. contracts with benefits directly linked to the value of units of a collective investment undertaking (“**CIU**”) or to the value of assets contained in an internal fund held by the insurance undertaking and contracts with benefits directly linked to a share index or other reference value) which are aimed at updating, in line with the regulatory changes that have taken place from time to time at a European and national level, the provisions currently in force contained in IVASS Circular no. 474 of 21 February 2002 and in IVASS Regulation no. 32 of 11 June 2009 respectively governing unit-linked and index-linked insurance products.

The review of the current regulatory framework on linked products was long-awaited from the market given that the regulations currently in force are no longer aligned with Solvency II Directive and related implementing rules. In accordance with Solvency II inspiring principles, including the freedom of investments of insurance undertakings to be exercised according to the prudent person principle, with the Draft Regulation IVASS confirms its power to limit by regulation the types of underlying assets or reference values of linked products in case the investment risk is borne by a policyholder who is a natural person.

IVASS evaluated the comments received in the context of the first consultation, which involved a high number of participants (including Hogan Lovells), and in some cases the provisions consulted have been amended welcoming the observations raised, in other cases IVASS decided to confirm its regulatory choices. Also, some new provisions have been introduced in the Draft Regulation compared to the first draft.

The main topics affected by changes compared to the first public consultation concern the following:

- **Application to EU insurance undertakings**

The Draft Regulation identifies the provisions that also apply to European players with the aim of ensuring a level playing field between Italian insurance undertakings and insurers from other Member States marketing linked products on the Italian market where compatible with the European regulatory framework. In partial acceptance of the comments we raised in the context of the first public consultation, insurance undertakings based in other Member States operating in the Italian territory have been excluded from the application of some of the provisions of the Draft Regulation, concerning in particular the Product Oversight and Governance (“POG”), corporate governance and the internal organisations of undertakings in light of the circumstance that the indiscriminate application of the whole regulatory framework to EU insurance undertakings would infringe the “home country control” principle. However, as to the remaining provisions, and in particular those on quantitative and qualitative investment limits, the Draft Regulation provides that they would apply to EU insurers as well. In this regard, according to IVASS rationale, an application limited to insurance companies with their registered office in Italy would not allow a real and adequate protection of Italian consumers.

- **Demographic risk requirement**

Pursuant to the Draft Regulation, insurance undertakings would be required to have a sufficiently structured and adequate internal process for assessing and determining the coverage of demographic risk for unit and index linked products.

In light of the comments that we also raised in the context of the first public consultation and also taking into account the comments received from the market with respect to the discussion paper on preliminary considerations for future regulatory actions of IVASS on life insurance products also published for consultation in March 2022, the provision under the first draft in this regard has been reworded in order to better clarify that the value of the insurance benefit shall depend on the demographic risk assessment appropriately calibrated to the policyholder's insurance coverage needs. In other words, the assessment of demographic risk would be in any case left to the insurance company on the basis of the policyholder's insurance coverage needs. The revised rule, with the exception of the POG and governance profiles, would be applicable also to companies with registered offices in other Member States, as it is to be considered a general good provision. Otherwise, according to IVASS, the applicability to Italian companies only would result in an unlevel playing field.

Lastly, the Draft Regulation specifies - for Italian companies - that: (i) the congruity assessment in relation to demographic risk must be consistent with both the characteristics of the product and those of the target market, taking into account elements such as the amount of the premium paid, the age of the insured and the duration of the contract as identified within the company's internal POG procedure; (ii) the benefit payable by the insurer shall not be less than an appropriate percentage of the premium invested.

- **Unit-linked contracts linked to internal insurance funds, eligible investments and related limits**

The Draft Regulation updates the rules on the assets in which insurance companies' internal funds to which the benefits of unit-linked contracts are linked, may be invested. The aim is, on the one hand, to

implement the primary regulatory framework for the insurance sector and, on the other hand, to take into account the legislative changes that have taken place in the broader reference context. IVASS has therefore pursued, as far as possible, the objective of ensuring maximum consistency with the provisions dictated on UCITS in the Bank of Italy's Regulation on collective investment management, which have been identified as a benchmark both with respect to the interests of the insurance company, to ensure a level playing field with other players in the financial market, and with respect to the protection of policyholders, to ensure that the policyholder as a natural person may purchase a product with a risk profile that is not higher than a UCITS intended for retail customers.

Nonetheless, in light of the comments that we also raised in the context of the first public consultation, compared to the first draft the revised Draft Regulation increases – provided that specific conditions are met – the investment limits compared to those set out by the Bank of Italy in its regulation on UCITS. In particular, less stringent investment limits (with particular respect to (i) unlisted financial instruments, (ii) parts of a same non-reserved open-ended FIAs and (iii) non-reserved open-ended FIAs taking into account the overall exposure) would apply in relation to particular categories of customers who would be allowed access to more illiquid and riskier linked contracts, where the internal fund linked to the relevant contract has all the following characteristics:

- payment of an initial non-fractional premium of not less than EUR 500,000;
- minimum investment horizon consistent with the degree/level of illiquidity of the assets (by way of example, a time horizon of not less than the maturity of the most illiquid security may be considered as such);
- suitability of distribution to policyholders who are natural persons with proven experience, also taking into account the number, type and amounts of financial investment transactions carried out over the previous 5 years, high financial knowledge and skills necessary to fully understand the illiquid nature and risks of the investments underlying the policy underwritten.

The identification of the abovementioned type of product and customers to which it may be sold, in IVASS intentions, would allow (i) insurers to broaden their product offer, (ii) to safeguard the interests of consumers with specific characteristics/profiles of greater risk appetite, financial competence and willingness to invest, as well as (iii) to pursue the objectives of a level playing field for the regulation of insurance products in the context of the broader financial market (i.e. the market that allows investments in riskier products than a UCITS (e.g. AIFs)). On the other hand, the illiquidity of products and of related investments would require insurance companies to put in place specific safeguards to protect their and the market's stability. EU insurance companies operating in Italy would be nonetheless excluded from this latter obligation.

- Management fees in the event of internal funds investing in linked CIUs

The Draft Regulation calls for insurers to pay particular attention to maintaining an adequate value of the insurance product for the policyholder when defining the costs attributable to the assets of internal funds. In view of the potential conflict of interest underlying the case of management fees in the presence of linked CIUs (i.e. funds managed by entities belonging to the same group of the insurer), IVASS considered that the insurance company is required to adopt specific safeguards also aimed at avoiding the duplication of charges borne by the policyholder. Therefore, without prejudice to the prohibition of charging to the internal fund the expenses of any nature whatsoever for the subscription and redemption

of units of linked CIUs, under the revised Draft Regulation the remuneration of the insurance undertaking would be allowed where, inter alia, the latter provides an effective additional service with respect to the one carried out by the manager of the linked CIU in which the internal fund is invested.

The original provisions have therefore been reformulated, also in light of the specificities that characterise the management of internal funds that invest in linked CIUs, enhancing the autonomy of insurance companies and entrusting them with the management of potential conflict of interest through the identification of appropriate measures to ensure the non-duplication of burdens on customers.

- Transitional regime

In consideration of the comments that we also raised in the context of the first public consultation, IVASS made changes to the draft provisions governing the transitional regime, in order to allow insurance undertakings a gradual adaptation to the new provisions set forth in the Draft Regulation. Consequently, IVASS provided for a general transitional period of 12 months from the entry into force of the Draft Regulation for insurance undertakings to adapt to the new rules.

For pre-existing internal funds, linked to contracts signed after the date of entry into force of the Draft Regulation, the same 12 months transitional period applies (compared to the 6 months period provided under the draft published for the first public consultation).

In the event of pre-existing internal funds which are not open to new subscriptions and for which, therefore, no new contracts are subscribed, the new regulatory rules would not apply, in line with the provision according to which the new legal framework would only apply to contracts concluded after the date of entry into force of the Draft Regulation, regardless of their type (multi-class or hybrid products).

The draft Regulation would repeal – among others - IVASS Circular 474/2002 (on unit-linked contracts) and IVASS Regulation no. 32 of 11 June 2009 (on index-linked contracts), which both would continue to apply to contracts concluded before the entry into force of the Draft Regulation.

Next steps

The public consultation on the Draft Regulation will be open until 27 May 2024 and we are in the process of reviewing it in detail with the aim to submit comments to the Italian regulator where needed.

We are available to assist in providing a detailed analysis of the provisions contained in the Draft Regulation as well as in submitting specific comments to IVASS on topics of interest.

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