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Portugal: Trends & Developments

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Trends and Developments

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Abreu Advogados is an independent law firm with more than ten locations and more than 28 years of experience in the Portuguese market. As a full-service law firm, Abreu is one of the largest law firms in Portugal and works with some of the most prestigious legal firms in the world on cross-border projects. The insurance team collaborates with many well-known and respected companies in the insurance sector, advising throughout the entire life cycle of insurance products and via litigation or arbitration in dispute resolution cases. Abreu has partici-

pated in some of the largest transactions in the insurance sector in Portugal, as well as advising international insurance companies on the legal and regulatory aspects of their cross-border activities. The team also plays an important role in the insurtech segment, having assisted Habit Analytics in its entry into the Portuguese market and advised on the acquisition of Drivit (a pioneering Portuguese telematics company) by Zego, one of the most well-known insurtechs in the world.

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Nuno Luís Sapateiro is a professional partner at Abreu Advogados and co-head of the insurance team. With more than 15 years of experience in this sector, he has provided strategic

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PORTUGAL TRENDS AND DEVELOPMENTS

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Introduction

The insurance market in Portugal has been confronted with various challenges and changes over the past few years – the causes of which can be divided, very briefly, into:

- successive legal and regulatory changes;
- the technological revolution, the COVID-19 pandemic;
- the implementation of the IFRS 17 reporting standards; and
- the coverage of natural catastrophes and emerging risks.

The response of the Portuguese insurance sector to the above-mentioned events has strengthened its reputation and people are becoming more consciously aware of the importance of private insurance when dealing with the insufficiencies and general lack of response of the public system – notably, when they are exposed to high healthcare costs and long waiting lists.

The pandemic crisis, health service difficulties, the increase in cyber-attacks and data breaches and climate change events have awakened Portuguese consumers to the importance of a series of risks that used to be almost unnoticed, such as the risk of business interruption, cyber-risk and climate risk. On the other hand, a number of other themes have gained increased importance – namely, the level of health protection guarantees and the levels of savings for retirement.

On the regulatory side, 2023 was marked by the introduction of new rules and principles applicable to market conduct, governance, reporting and disclosure duties towards the supervisory authority and clients.

This article will attempt to analyse the current situation in the insurance sector in Portugal, pre-

dict the main trends and opportunities in 2024 and provide some guidance for foreign investors, insurers and insurance distributors in terms of the Portuguese legal and regulatory environment.

Overview of the Portuguese Insurance Market

According to the report prepared by the Insurance and Pension Funds Supervisory Authority (Autoridade de Supervisão de Seguros e Fundos de Pensões, or ASF) for the third quarter of 2023, there was a decrease of 5% in the production of direct insurance in Portugal when compared with the same period in 2022. There was a decrease of 20.7% in the life sector and an increase of 10% in the non-life sector. During this same period, the costs with claims increased 12.2% as result of an increase of 12.7% in the life sector and 11.2% in the non-life sector.

The coverage ratios for the Solvency Capital Requirement (SCR) and the Minimum Capital Requirement (MCR) in September 2023 were 204% and 552%, which reflects an increase of 7% and 35% respectively when compared with December 2022.

According to the FY 22 Annual Report prepared by the ASF, 63 insurers were established in Portugal. There were 26 branches from foreign countries (all EU countries) and 540 insurers operating under the “freedom to provide services” regime. As of 31 December 2022, the top three insurers in Portugal take around 55.9% of the market share in premiums and the top ten insurers take around 85.7%.

Although the vast majority of insurance consumers in Portugal still prefer direct interaction with a human in the insurance placement process, generational renewal and ongoing technological evolution indicate a rapid transition to

selling insurance through digital solutions. The reduction of around 10% in the number of active insurance intermediaries in Portugal in December 2022 when compared to the same period in the preceding year can be explained by various factors, with the digitalisation of the relationship between insurers and clients being one of the main causes.

Health insurance

The health insurance market in Portugal has been developing since the 1980s. Gross direct written premiums in 2012 were around 524 million euros, rising to 1.1 billion in 2022 – ie, more than doubling in a decade. In the same period, the number of insured people increased by 66.2%, with all authorised insurance companies registering around 3.7 million insured people in 2022.

The accumulated figures for the third quarter of 2023 point to a production of 22.8% of non-life business as a whole in health, which – together with motor insurance – is the most representative business segment in the Portuguese insurance market. This growth in the health sector is associated with the saturation level of the national health system (which is leading people to seek a wider choice of health services), the ageing of society and the growth in health costs, as well as a greater willingness on the part of employers to include this type of product in their employees' social benefits package.

The ASF has already noted the existence of a protection gap in which people's health insurance cover does not meet their interests or needs and recently announced that a legislative initiative is underway to introduce a standard health insurance policy covering check-ups, hospitalisations and outpatient care in order to

improve the level of consumer comparison of products.

Cyber-risk

The increase of cyber-risks in Portugal arising from the high connectivity of companies and populations, combined with remote work, have led to a “perfect storm” for cyber-insurance. According to reports made available in the market, the threat of cyber-attacks is considered the main risk for Portuguese companies and the acceleration of companies' digital transformation is leading to an increase in cyber-attacks and data breaches.

It is now clear that cyber-insurance shifted to a hard market and companies are finding it more difficult to get coverage owing to the significant increase in the frequency and severity of ransomware attacks and cybercrime involving reputed Portuguese companies and State institutions.

The legal obligation to publicise security breaches, the reinforcement of the sanctioning framework, and the new approach of self-accountability for organisations that resulted from the General Data Protection Regulation (GDPR) have placed greater emphasis on the reputational risks that can arise from a cyber-attack and on the importance of properly measuring and hedging this risk.

The major insurance groups are natural targets for cyber-attacks because they possess substantial amounts of confidential policyholder data and the ASF has recently issued specific rules on cybersecurity and outsourcing arrangements with cloud computing service providers. Pursuant to this regulation, the board of directors is responsible for establishing an effective system for managing information and communi-

cations technology and security risks as part of the company's overall risk management system.

Natural catastrophes and the protection gap

Portugal continues to experience heatwaves that cause massive forest fires in the summer period. These are followed by severe flooding due to heavy rain in the autumn and winter.

According to the dashboard on insurance protection gap for natural catastrophes that was recently published by the European Insurance and Occupational Pensions Authority (EIOPA), Portugal has the sixth worst protection gap in Europe. Also, according to the dashboard, the historical protection gap score in Portugal is high as a result of very low levels of insurance penetration across all risks.

Insurance companies are facing increasing pressure to take action to combat climate change. It is inevitable that there will be a considerable increase in the level of investment dedicated to this area, as the ability or inability of the insurance market to respond to this new reality could have a considerable reputational impact.

As detailed in the EIOPA dashboard, earthquake risk could present the main concern in the future. There are possible systemic repercussions for Portugal, due to the potential for devastating events in areas that experience a very high level of vulnerability and exposure with very low insurance penetration levels (notably Lisbon).

Back in October 2023, the Portuguese government finally instructed the ASF to carry out – in co-ordination with the relevant bodies – the necessary work to create a system to cover the risk of seismic phenomena. The work to be carried out by the ASF will comprise (but is not limited to) the preparation of a preliminary draft of a law

creating and regulating the system for covering the risk of seismic phenomena and a proposal to extend the system in order to cover risks arising from other natural disasters. The ASF will have to present a preliminary report proposing a model for a seismic risk coverage system by the end of the first quarter of 2024.

Savings

The increase in average life expectancy and the fragility of the Portuguese social security system have awakened consumers to possible shortages of resources at the end of their working lives and the need to find complementary solutions for their retirement.

The Portuguese government recently approved the draft law for the Pan-European Personal Pension Product (PEPP), which will be subject to the same rules applied to pension funds. One aspect that was essential for the success of the existing retirement savings plans (PPR) and which remains unanswered in the case of the PEPP is the tax benefits applicable to subscribers.

The potential of complementary retirement and investment products is growing and the insurance industry can play an active role in strengthening complementary savings schemes (in particular, individual savings). The restoration of tax benefits for savings products is a key part of this solution.

Business interruption

Another important issue that is still on the agenda is the possibility of activating an insurance portfolio to cover the so-called operating losses arising from the COVID-19 restrictions and also from the war in Ukraine. These are largely the result of the forced closure of establishments and the lack of raw materials, fossil fuels and

other key items. The coverage of operating losses arising from forced business interruption will remain a key issue but there is still no clear response from the insurance market on the solutions that will be available to deal with this risk.

The lack of manpower, the dependence on imports of strategically important raw materials, as well as the shortage of suppliers and customers, has in many cases led to a long interruption or reduction of activity with resulting economic losses. Experience shows that most of the coverage for operating losses that exist in the Portuguese market is not designed for this type of circumstance and that, as a rule, it figures as complementary coverage of indemnity insurance (the so-called all risks). This complementarity means that, as a general rule, cover for business interruption losses can only be activated in the event of interruption or reduction of activity as a result of an insured event linked to the destruction of or physical damage to insured property – ie, damage to a property and/or its contents. This is definitely not the case for business interruption losses resulting from a pandemic.

Relevant Updates for Foreign Investors, Insurers and Distributors

Acquisition of qualified shareholding in a Portuguese insurance undertaking

Although the regime for the acquisition of qualified shareholdings has not been subject to recent changes (the last amendment dates back to 2021), the ongoing process of consolidation of the insurance market justifies a brief reference to the regime in force in Portugal.

Pursuant to law, any natural or legal person who – directly or indirectly – proposes to acquire a qualified shareholding in an insurance undertaking or who proposes to increase its quali-

fied shareholding so that the proportion of its voting rights or share capital would reach or exceed 10% or 20%, one-third or 50%, or so that the undertaking would become their subsidiary should give prior notice to the ASF of the envisaged transaction. The terms and conditions of such notice as well as the list of information and supporting documentation that must be enclosed therewith are duly regulated in the Regulatory Standard No 3/2021–R of 13 April 2021 published by the ASF. This Regulatory Standard further regulates the communication of encumbrances or charges on qualifying holdings in insurance or reinsurance companies.

It is worth mentioning that this Regulatory Standard also aims to harmonise the regulatory framework with the Joint Guidelines of the European Supervisory Authorities – in particular, with regard to:

- the existence of qualified shareholdings through concerted action or indirect holdings; and
- the acquisition of holdings (regardless of the thresholds reached or exceeded), provided that they enable the proposed acquirer to exercise significant influence over the management of the insurance undertaking, whether or not such influence is exercised.

Market conduct rules applicable to insurers carrying out their business under the freedom to provide services regime

As detailed earlier, the FY 22 Annual Report prepared by the ASF makes reference to 540 insurers operating in the Portuguese market under the freedom to provide services regime. Bearing this in mind, it is important to make a brief reference to the ASF Regulatory Standard No 7/2022-R on market conduct and complaints management. Some provisions of this Regula-

tory Standard are applicable to insurers carrying out their business in Portugal under the freedom to provide services regime.

It is worth highlighting the obligation to maintain a web page, written in Portuguese, with a specific section – entitled *Informações Relevantes para o Cliente* (relevant information for the customer) – dedicated to market conduct. The referred information must be presented in a structured manner and include:

- the conditions and available sources for lodging a complaint before the insurer and the Client Ombudsman and the applicable eligibility criteria;
- recommendations issued by the Client Ombudsman;
- conditions for lodging a complaint before the ASF and the applicable eligibility criteria; and
- customer treatment policy.

Insurance distribution

The Portuguese legislator gold-plated the Directive (EU) 2016/97 of the European Parliament and of the Council of 20 January 2016 on insurance distribution (the “Insurance Distribution Directive”, or IDD) in certain areas – for example, the qualification requirements and the information duties to be observed by the insurance distributor towards the client, the insurer and the ASF. Nevertheless, Law 7/2019 of 16 January (the “Insurance Distribution Law”) is pretty much in line with the IDD and therefore insurance distributors registered in other EU countries must be generally compliant with Portuguese law when acting in accordance with the IDD and the Commission Delegated Regulation (EU) 2017/2359 of 21 September 2017 supplementing the IDD.

Pursuant to the Insurance Distribution Law, the pre-contractual documents must be drafted in

Portuguese. However, a different language may be used if such alteration is requested by the policyholder and is agreed between the parties.

As detailed in Article 23.1(c) of the IDD and duly transposed into the Insurance Distribution Law, all information provided to the customer must be communicated in the official language of the EU member state in which the risk is situated or of the EU member state of the commitment (or in any other language agreed upon by the parties).

Insurance Sector Challenges

Emerging risks

It is inevitable that the insurance market will be forced to adapt its product offering in order to offer some coverage guarantees associated with epidemics, pandemics, climate change effects and war. This need for adaptation has already been felt but there is still a long way to go.

There are different variables that may be considered by the industry in order to build solutions and delimit its level of exposure before emerging risks – whether in terms of reinsurance, premiums, deductibles, or the time limit of coverage (namely, in the case of operating losses) –when it comes to exclusions or in the way the solution is presented (complementary/voluntary coverage).

It is important to take advantage of the current experience to reassess the catastrophic and pandemic risks. The insurance industry has an opportunity to analyse, together with the government and the reinsurance sector, the solutions that can be put forward to respond to these risks.

Customised insurance

The demand for customised insurance products is definitely one of the most important challenges that the Portuguese insurance market will have

to deal with in the coming years. In fact, there is still a somewhat ingrained practice of replicating the general conditions of products in the same line of business (namely, third-party liability) in the different variants of that product, referring the specificities of the product to its particular conditions. This practice has been detrimental to insurance consumers, as they are confronted with a series of definitions and contractual provisions that, strictly speaking, have no applicability to their product. The gradual implementation of concepts such as “pay as you drive” and “pay as you live” will necessarily entail effective customisation of insurance products involving the entire contractual package (general conditions included).

Insurtech

It is clear that technology will be a consistent and fundamental enabler for the insurance market and there is a growing awareness that clients are increasingly willing to go through an experience when buying their insurance product – anytime, anywhere and with any available device.

This phenomenon has been even more striking in the Portuguese insurance sector, given that this sector has not demonstrated the same level of development as the banking sector and that insurtech’s level of penetration was clearly below that of fintech.

The lack of specific provisions in the Portuguese legal and regulatory framework governing the implementation of insurtech solutions cannot be an obstacle to the revision of the business model of local insurers in order to meet the demands of a more sophisticated insurance client. The use of tools that allow massive extraction and processing of data and information from an almost infinite number of sources will enable faster and more efficient preparation, submission and anal-

ysis of often lengthy and complex dossiers concerning cross-border activities and the transfer of qualifying holdings in supervised entities.

The speed and level of penetration of technological solutions in the Portuguese market are not compatible with bureaucratic and lengthy processes of public consultation followed by the transposition of EU Directives that still lack regulation in each member state. In line with what has already resulted from the recent amendment to the legal framework for insurance activity, it is essential to strengthen the framework for co-operation between the national supervisor and the European Insurance and Occupational Pensions Authority (EIOPA) so that there can be alignment at the level of supervision and local regulation – regardless of the timing of the revision of fundamental laws and regulations.

It is also worth highlighting the growing number of insurance solutions that have been presented as a result of partnerships between insurers, insurtechs and distributors. There is still a great margin for the entry of new insurtechs, with solutions in the areas of smart contracts, digital signatures, artificial intelligence, etc.

The ASF is working in order to meet the new market trends and support new technologies. Therefore, other insurtechs are expected to enter the Portuguese market and team up with local insurers in the launch of innovative new products.

There are provisions in Portuguese law governing distance selling of insurance (whether online or by phone) and outsourcing rules (as transposed from the Solvency II Directive) that should be sufficient to deal with the implementation of certain innovative solutions and enable the co-

operation between incumbent undertakings and insurtech start-ups.

Transition to the green economy

The national insurance sector is not indifferent to the path taken by banking and investment funds and is also betting on the transition to a green economy. Without prejudice to the need to find a balance between sustainability and the applicable prudential framework, the insurance industry and pension funds are already considering ESG criteria when selecting their investments and defining the composition of their asset portfolios.

Insurers are being called upon to respond to the challenges of sustainable development, making investments within a policy of social and climate responsibility. It is important to understand how these investments fit in with the regulatory framework applicable in the medium and long term.

The harmonised rules set forth in Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on disclosure of sustainability-related information in the financial services sector are being transposed to the internal regulation governing the insurance sector. By way of example, the ASF's Regulatory Standard No 4/2022-R of 31 May 2022 determines that the insurer's remuneration policy must include information on how it corresponds to the integration of sustainability risks, in accordance with Regulation (EU) 2019/2088.

Reference also to the ASF's Regulatory Standard No 4/2023-R of 11 July 2023 on reporting duties – pursuant to which, insurers that are subject to the Regulation (EU) 2019/2088 must communicate to the ASF on an annual basis the hyperlinks to information on:

- policies for integrating sustainability risks into their investment decision-making process; and
- the negative sustainability impacts at the entity level, all in accordance with Regulation (EU) 2019/2088.

Other notes on the Portuguese insurance sector

The current framework of technological revolution and the increased demand for reporting requirements, statutory disclosures and monitoring activities will make it more difficult for traditional small and medium-sized insurers to compete with the top ten insurers. The door to new concentration processes at the level of insurers and distribution channels will remain open but the scale of such operations will certainly be very limited when compared with previous years.

No major changes in law are expected in 2024 but reference should be made to the transposition of the new EU Directive 2021/2118 amending the Directive 2009/103/EC relating to insurance against civil liability in respect of the use of motor vehicles. Although the dissolution of the Portuguese Parliament has already been announced, there was still some expectation of the possible transposition of the Directive into national law before 23 December 2023.

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