

## NEW CIRCULAR LETTER ON GOVERNANCE ISSUED BY THE LUXEMBOURG INSURANCE REGULATOR CAA

On 26 July 2022, the Luxembourg insurance sector supervisory authority Commissariat aux Assurances ("**CAA**") issued its Circular Letter 22/15 on the board of directors of insurance and reinsurance undertakings. The new CAA Circular Letter amends and consolidates the requirements applicable to the board of directors of (re)insurance undertakings and insurance group holding companies supervised by the CAA. Looking forward, these entities will need to ensure compliance with this new set of rules before its entry into force. The concerned persons and entities will have to comply with most provisions regarding changes in the composition of the board of directors already by 30 September 2022, while certain requirements will apply as of 31 March 2023. Assessments of governance systems must be documented by 31 March 2023. The following briefing provides an overview of the new rules, key issues and points calling for action.

### SCOPE

The Circular Letter is addressed to all Luxembourg insurance and reinsurance undertakings as well as insurance holding companies and mixed financial holding companies heading a group supervised by the CAA. Exempted are however captive insurance or reinsurance undertakings, as well as non-captive reinsurance undertakings with gross annual premiums of less than 100 million euros. In the following we will for ease of reference refer to '(re)insurers' only, but the reference shall be read so as to cover *mutatis mutandis* also the before mentioned holding companies and so as to exclude exempted entities.

The Circular Letter concerns more particularly the administrative, management or supervisory bodies ("**Board**") of (re)insurers and any members of such bodies ("**Director**"). The Circular Letter does not concern managers (*dirigeant*), approved managers, and executive managers as such, where the legal form of the company and its system of governance distinguish between a supervisory body and a management body, e.g., in case a

### Key issues

- Amended and consolidated requirements for boards of directors of (re)insurance undertakings and insurance group holding companies
- Replaces CAA Circular Letters 96/1, 99/1 and 02/8
- Clarified typology of different types of directors
- New and clarifying rules and requirements on quality and conduct of directors, composition, functioning and competencies of the board and interaction with the CAA
- New requirements call for review of and, where needed, changes in the organisation and governance of (re)insurers and holding companies
- Assessment of governance systems to be documented until 31 March 2023

(re)insurer has in place a two-tier system with a supervisory board and a management board. The before-mentioned types of managers will in their manager capacity be subject to the rules and requirements of the CAA's circular letters for managers.

## **QUALITIES AND CONDUCT OF DIRECTORS**

The CAA reminds the requirements of article 258(1) of the Delegated Regulation (EU) 2015/35 on collective and individual qualifications, competencies, skills and professional experience present in the Board.

The CAA expresses its preference that the collective competencies of the Board shall be based on Directors which have each of them a very good level in several areas, rather than being based on Directors having each expert competencies in one area only. The relevant areas are listed in the Circular Letter.

In addition, the CAA clarifies that each Director (and not only non-executive or independent Directors) must demonstrate independence of judgment, good repute, character strength and objectivity in the exercise of their mandate.

Furthermore, the CAA recommends (re)insurers to comply with the definitions of the Circular Letter when using the terms non-executive director (*administrateur non-exécutif*) or independent director (*administrateur indépendant*) in their communications and reportings. The Circular Letter provides further details on the definition of these terms, such as clear guidance on cool-down periods for certain relationships with the (re)insurer, its controlling shareholder or affiliates and their respective management after elapsing of which the person can be considered being 'independent'.

## **COMPOSITION OF THE BOARD**

The CAA states that in any case a Board must have at least three members, while the number of members must be sufficient for it to carry out its duties effectively and to supervise the undertaking in a professional manner.

(Re)insurers are further reminded that the Board is responsible for signing powers and their coherence with governance principles as well as with the notifications and authorisation requests to be made with the CAA.

The CAA reminds in this context that the function as a delegated director (*administrateur-délégué*) is one of the most important executive functions and that only a person authorised as manager of a (re)insurance undertaking may be appointed for that function.

Further, it is recommended to appoint a natural person amongst the non-executive directors as president of the Board and to notify such decision to the CAA in order to facilitate communication.

The CAA requires (re)insurers to document (i) for each Director its classification as executive, non-executive or independent Director and its assessment of good repute, (ii) situations likely to lead to conflicts of interest, and (iii) the collective competence of the Board. The assessment of the collective competence has to be carried out at the departure of a Director and at least every three years as well as upon a major change of the business plan.

Directors need to monitor that their mandate in the (re)insurer is and remains compatible with their other employments, mandates or potential interests and need to inform the Board in writing of other mandates.

The CAA finally requires undertakings to comply with several further principles (which are subject to certain exceptions), including, amongst others, a requirement to appoint an independent director for public interest entities (i.e., (re)insurance undertakings) supervised by the CAA, and a requirement for having a majority of non-executive Directors in the Board.

## **LEGAL ENTITIES AS DIRECTORS**

It is reminded that a legal entity can, subject to certain requirements, be a Director of a (re)insurer. If such legal entity is neither a direct or indirect shareholder or strategic partner of the undertaking, or the management company of a captive undertaking, of an insurer in run-off or of a reinsurer, a detailed justification for the appointment of such legal entity must be presented to the CAA.

## **NOTIFICATION OF THE COMPOSITION OF THE BOARD**

Any changes in the composition of the Board must be notified to the CAA within four weeks of such change, and preferably in advance of a co-optation decision by the Board or definitive Director appointment by shareholder decision. Such appointment act cannot make the appointment subject to CAA approval or authorisation, as none of them will be required from or be given by the CAA.

Details on the information and documents required for the notification file are set out in CAA circular letter 19/5 and in forms available on the CAA website. (Re)insurers have to collect the required information and documents also for their suitability assessment of the relevant candidate. Such assessment shall be carried out and come to a positive result before the notification to the CAA and the appointment is made.

At the departure of a Director the notification should be made through separate letters of each the undertaking and the former Director within a delay of two weeks after the information of the (re)insurer of the departure and indicating the relevant details. The CAA reserves the right to hear the former Director.

## **FUNCTIONING OF THE BOARD**

It is reminded that the Board defines its own operating mode, in compliance with the applicable texts, as well as the system of governance of the undertaking, considering the nature, scale and complexity of business at both individual and group level, as well as the structure of the group. The Board shall regularly assess its operating mode and its work in order to improve it, verify its efficiency and ensure that each Director has a good understanding thereof. The assessment periodicity and results have to be documented in writing.

The excessive recourse to written Board resolutions (instead of physical meetings or, if not possible, meetings by conference call or videoconference) and the use of powers of attorney between Directors should be avoided, and in any case one Director should represent only one other Director in a Board meeting. The majority of Board meetings should be held in Luxembourg.

The agenda of a Board meeting and the relevant documents for approval and those necessary for decision taking or information of the Directors shall be communicated to them within a reasonable timeframe in advance of the meeting.

The supervision carried out and the decisions taken by the Board shall be clearly documented in writing by minutes or circular resolutions. Recurrent agenda points can be dealt with succinctly in the documentation, while points implying important risks for the undertaking or its group or points discussed contradictorily have to be documented in more detail.

## **COMITOLGY AND KEY FUNCTIONS**

In relation with the CAA, the Board is responsible for the appointment of managers and the performance of key functions in an informed, objective, and independent manner. Specialised committees with clear task and role descriptions and rules on their composition can be set up, but the Board retains its powers and full responsibility for its tasks.

Where the tasks of a specialised committee cover key functions (as defined by Directive 2009/138/EC ("**Solvency II**")), the Board organises such committee so as to respect the independence of each key function. Specific rules apply to audit committees, notably as regards their competence and composition.

It is reminded that the Board appoints and revokes the managers of the undertaking, defines individually their powers (including signing powers) within the limits foreseen in the law and the articles of association, and controls their actions. The Board clearly determines the tasks and roles of key functions. It documents any person regularly contributing thereto (including in case of outsourcing) and assesses the competence and repute of such persons.

The responsible persons for (i) each key function (as defined in Solvency II), (ii) anti-money laundering and counter-terrorist financing ("**AML/CTF**"), and (iii) distribution are assessed on their competence and good repute and are appointed by the Board and notified to the CAA. The CAA will neither authorise nor approve such persons but may at any time oppose that the relevant person remains in such function.

## **OTHER FUNCTIONS OF THE BOARD**

The CAA considers that the Board bears essential responsibilities in several areas listed in the Circular Letter. These include the compliance with the business plan, risk management, the own risk and solvency assessment (ORSA), internal controls, good governance, AML/CTF, and the good application of accounting principles and evaluation methods.

The Board is further required to formally approve or obtain knowledge of certain documents or information items listed in the Circular Letter. Additionally, the Board analyses these documents or information items and takes position as regards the risks, dysfunctions or injunctions presented in such documents. It further takes adequate preventive or corrective measures.

The Board keeps itself updated on the good repute and financial solidity of qualifying shareholders as well as on the undertaking's reputational risks and informs the CAA without delay of situations affecting such shareholders in a manner capable of being harmful to the sound and prudent management of the (re)insurer or of the facts triggering a reputational risk for the (re)insurer or its subsidiaries.

## **GOVERNING DOCUMENT CHANGES**

The Circular Letter provides that, where necessary, the Board amends its internal regulations, policies and procedures or, where relevant, proposes to the general assembly of shareholders to modify the articles of association of the (re)insurer so as to ensure that the Board approves the above-mentioned

documents and obtains the relevant information items and documents and that the Board is authorised to delegate the day-to-day management to one or more managers (to be authorised by the CAA).

## **DATE OF APPLICATION**

As of 30 September 2022, the new Circular Letter will replace CAA circular letters 96/1, 99/1 and 02/08.

It applies to changes in the composition of a Board from the same date. If necessary, instructions relating to delegated directors and executive directors are taken into consideration for 30 September 2022 by transmitting a file to the CAA requesting an authorisation as manager or notifying a new appointment or the departure of a Director.

Looking forward, the relevant provisions of the Circular Letter on the composition of the Board and on the articles of associations of the (re)insurer will apply as of 31 March 2023 and an assessment of the governance system must be documented until such date at the latest by Luxembourg (re)insurers.

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