

ANNEX TO DOCUMENT MARKT/2507/05 - EN

Draft Outline of a Solvency II Framework Directive

DIRECTIVE 2002/83/EC

Recitals (Revision necessary)

Title I**Definitions and scope**

- Article 1** Definitions (Possible definitions to be added; risk-oriented supervision, small undertaking, internal model, governance, internal control, risk management etc.)
Article 2 Scope
Article 3 Activities and bodies excluded

Title II**The taking up of the business of life assurance**

- Article 4** Principle of authorisation
Article 5 Scope of authorisation
Article 6 Conditions for obtaining authorisation (Revision may be needed with a view to the new supervisory approach; In Article 6.1.a, the European Company should be added; Article 6.1.e good repute should be revised in light of 2nd call no 16 Fit and Proper; Regarding the role of actuaries, Art. 9 I,(d) IORP Directive may be used as inspiration)
Article 7 Scheme of operations (Revision may be needed; add info risk management, internal control, governance, internal models, MCR, SCR)
Article 8 Shareholders and members with qualifying holdings (Revision, 2nd call no 16, Fit and proper; It should be clarified that only prudential reasons may be taken into account)

Title III**Conditions Governing the Business of Assurance****Chapter 1 General requirements**

- Article 12** Prohibition on compulsory ceding of part of underwriting
Article 14 Transfer of portfolio
Article 15 Qualifying holdings (Revision, 2nd call no 16, Fit and proper. It should be clarified that only prudential reasons may be taken into account)
Article 17 Duties of auditors
Article 18 Pursuit of life assurance and non-life insurance activities
Article 19 Separation of life assurance and non-life insurance management

Chapter 2 Internal Control and Risk Management

- Article N2** Internal Control and Administrative Organisation

Suggested wording in 1st call no 1, Internal Control and Risk Management:

“Insurance undertakings are required to have in place internal controls that are adequate for the nature and scale of their business.”

(In its draft reply to the First wave of cfa, CEIOPS supports the inclusion of a high level principle on governance, along the lines provided in Article 22 CRD; “Home Member State competent authorities shall require that every credit institution has robust governance arrangements, which include a clear organisational structure with well defined, transparent and consistent lines of responsibility, effective processes to identify, manage, monitor and report the risks it is or might be exposed to, and adequate internal control mechanisms, including sound administrative and accounting procedures.

2. The arrangements, processes and mechanisms referred to in paragraph 1 shall be comprehensive and proportionate to the nature, scale and complexity of the credit institution’s activities. The technical criteria laid down in Annex V shall be taken into account”¹.

COMMISSION STAFF PROPOSAL:

“The Home Member State shall require every insurance undertaking to have robust governance arrangements, which include a clear organisational structure with well defined, transparent and consistent lines of responsibility, and to have internal control mechanisms. The internal control mechanisms should be adequate for the nature and scale of the insurance undertaking’s business and should include sound administrative and accounting procedures.”

Article N3 Risk management

Suggested wording in 1st call no 1, Internal Control and Risk Management:

“Insurance undertakings shall identify and assess the nature and the significance of the risks they face. Insurance undertakings shall manage these risks to provide reasonable assurance of maintaining the undertaking’s overall financial soundness. In order to achieve this, insurance undertakings shall have in place effective strategies and processes, comprehensive and proportionate to the nature and scale of the risks”.

CEIOPS has suggested that insurers should be required to develop and carry out active concrete policies specially focused on the definition, follow-up and control of their solvency position, as other financial institutions, like banks have been doing during last years. Besides, CEIOPS has suggested including a high-level principal on a minimum set of general principles applicable to reinsurance management in insurance undertakings

COMMISSION STAFF PROPOSAL:

“The Home Member State shall require every insurance undertaking to identify and assess the nature and the significance of the risks it faces (risk management). Insurance undertakings shall manage their risks with a view to provide reasonable assurance of maintaining the undertaking’s overall financial soundness. In order to achieve this, insurance undertakings shall have in place effective strategies and processes, comprehensive and proportionate to the nature and scale of the risks they face.

As part of the risk management, a Home Member State shall require every insurance undertaking:

- to develop and carry out active concrete policies specially focused on the definition, follow-up and control of its solvency position (policy on solvency management).
- to have in place Reinsurance Management and Risk Mitigation Management, ensuring appropriate reinsurance arrangements.”

Chapter 3 Principles and methods of supervision *(It is suggested to take out ‘financial’)*

Article 10 Competent authorities *(Home state control in paragraph 1 to be kept, paragraph 2 is dealt with in N4, paragraph 3 already covered by N2.)*

Article 11 Supervision of branches established in another Member State *(Revision needed).*

Article N1 Objective of supervision

¹ CRD already covered by specific Art. N2, N3

Suggested wording in 2543/03:

“The objective of financial supervision is to act for the benefit and protection of policyholders. Supervision also promotes the maintenance of efficient, fair, safe and stable insurance markets”.

(Comment: Not commented on by CEIOPS; financial supervision probably too narrow concept; the last part of the paragraph probably controversial)

COMMISSION STAFF PROPOSAL:

“The main objective of supervision is to act for the protection of policyholders. In order to achieve this objective, the Home Member State shall ensure that the competent authorities are provided with the appropriate tools and powers.”

Article N4 Supervisory review process

Suggested wording in 1st call no 2, Supervisory Review Process (General):

“In order to achieve its objectives, the competent authorities supervise the financial soundness of individual insurers. This requires an analysis of individual insurers and insurance groups as well as the market and the environment in which they operate. The analysis of individual insurers should be both off-site and on-site.

The competent authorities receive necessary information to conduct effective off-site monitoring and to evaluate the condition of each insurer as well as the insurance market. The competent authorities carry out on-site inspections to examine the business of an insurer and its compliance with legislation and supervisory requirements.”

(In the Draft Reply to the First cfa, CEIOPS seems to suggest a wording more in line with Article 124 CRD:

“Taking into account the technical criteria set out in Annex XI, the competent authorities shall review the arrangements, strategies, processes and mechanisms implemented by the credit institutions to comply with this Directive and evaluate the risks to which the credit institutions are or might be exposed. 2. The scope of the review and evaluation referred to in paragraph 1 shall be that of the requirements of this Directive. 3. On the basis of the review and evaluation referred to in paragraph 1, the competent authorities shall determine whether the arrangements, strategies, processes and mechanisms implemented by the credit institutions and the own funds held by these ensure a sound management and coverage of their risks.”)

COMMISSION STAFF PROPOSAL:

“In order to achieve the objective of supervision, the competent authorities control all business operations of insurance undertakings within the framework of general legal supervision and specific financial supervision. The supervision shall be based on a prospective and risk-oriented approach. The analysis of individual insurers should be both off-site and on-site.

The legal supervision includes verification of the proper operation of the insurance business including observance of the supervisory provisions.

The financial supervision shall include review of the arrangements, strategies, processes and mechanisms implemented by the insurance undertakings to comply with this Directive and evaluation of the risks to which the insurance undertakings are or might be exposed. The competent authorities shall verify, with respect to the insurance undertaking's entire business, its overall state of solvency, including the establishment of technical provisions, mathematical provisions, and the assets covering them. Financial supervision also requires an analysis of individual insurers and insurance groups as well as the market and the environment in which they operate.²

The competent authorities take preventive and corrective measures that are timely, suitable and necessary to achieve the objectives of insurance supervision.”

² Article 10 (2) 2002/83/EC and Section 81 VAG (German Insurance Supervision Act)

N4a *General Powers of intervention*

(In light of the discussions in the pillar II WG it seems necessary to include an Article on General Powers of intervention in addition to Specific powers of intervention, as not all necessary powers of intervention can be explicitly mentioned in the Directive.)

COMMISSION STAFF PROPOSAL

“The competent authorities shall have the power to take any measures, including where appropriate, those of an administrative or financial nature which are necessary to remedy any irregularities prejudicial to the interests of the policyholders. Any measure imposed should be based on clear and objective criteria that are publicly disclosed.

The competent authorities may, in particular:

- (a) make detailed enquiries regarding the assurance undertaking's situation and the whole of its business, inter alia, by:
 - gathering information or requiring the submission of documents concerning its assurance business,
 - carrying out on-the-spot investigations at the assurance undertaking's premises;
- (b) take any measures, with regard to the assurance undertaking, its directors or managers or the persons who control it, that are appropriate and necessary to ensure that the undertaking's business continues to comply with the laws, regulations and administrative provisions with which the undertaking must comply in each Member State and in particular with the scheme of operations in so far as it remains mandatory, and to prevent or remedy any irregularities prejudicial to the interests of the assured persons;
- (c) Member States may also make provision for the competent authorities to obtain any information regarding contracts which are held by intermediaries.

... to be continued ... ⁴³

Article 13 **Accounting, prudential and statistical information: supervisory powers**
(Revision needed, see above Article N4a and in light of 3rd call no 22, Supervisory reporting and public disclosure).

Article N5 **Transparency of competent authorities and their actions**

Suggested wording in 1st call no 4, Transparency of supervisory action:

“The competent authority conducts its functions in a transparent manner”.

(CEIOPS' suggestions in the Draft reply seem to include elements from Article 144 CRD.

Article 144

“1. Competent authorities shall disclose the following information:

(a) the texts of laws, regulations, administrative rules and general guidance adopted in their Member State in the field of prudential regulation; (b) the manner of exercise of the options and discretions available in Community legislation; (c) the general criteria and methodologies they use in the review and evaluation referred to in Article 124; (d) without prejudice to the provisions laid down in Title V, Chapter 1, Section 2, aggregate statistical data on key aspects of the implementation of the prudential framework in each Member State.

The disclosures provided for in the first subparagraph shall be sufficient to enable a meaningful comparison of the approaches adopted by the competent authorities of the different Member States.”)

³ Article 13 (2), (3) 2002/83/EC. Further measures to be added after examining advice from CEIOPS, 2nd call no 14, supervisory powers (general).

COMMISSION STAFF PROPOSAL:

“The competent authorities conduct their activities in a transparent manner. They shall at least disclose the following information:

(a) the texts of laws, regulations, administrative rules and general guidance adopted in their Member State in the field of prudential regulation; (b) the manner of exercise of discretions available in Community legislation; (c) the general criteria and methodologies they use in the review and evaluation referred to in this Directive; (d) aggregate statistical data on key aspects of the implementation of the prudential framework in each Member State.

The disclosures provided for in the first subparagraph shall be sufficient to enable a meaningful comparison of the approaches adopted by the competent authorities of the different Member States.”

Article N5b *Supervision of Groups*

(2nd call no 18, Group and cross-sectoral issues.

(Could/should Article 125 et seq. CRD be used as a starting point?)

Article N6 Co-operation between competent authorities of different Member States

Suggested wording in draft 3rd call no 21, Co-operation between supervisors of different Member States:

“The competent authorities of the Member States shall communicate to one another on request all relevant information which may allow or facilitate the exercise of supervision and shall communicate on their own initiative any information which appears to them to be essential for other competent authorities. Competent authorities must ensure sufficient cooperation in particular, when an insurance undertaking encounters financial difficulties.

Information received pursuant to this directive shall be subject to the obligation of professional secrecy.”

COMMISSION STAFF PROPOSAL

“The Home Member State shall ensure that its competent authorities communicate on request to the competent authorities of other Member States all relevant information which may allow or facilitate the exercise of supervision. On their own initiative, they shall communicate any information which appears to them to be essential for the other competent authorities. Competent authorities must ensure sufficient cooperation in particular, when an insurance undertaking encounters financial difficulties.

Information received pursuant to this directive shall be subject to the obligation of professional secrecy.”

Article N7 Peer reviews

Suggested wording in 2nd call no 16, Peer reviews:

“Competent authorities will aim for a convergence of their working methods through peer reviews to secure a high level of protection for policyholders.”

Article 16 Professional secrecy

Chapter 4 **Rules relating to technical provisions and their representation**

Article 20 Establishment of technical provisions

(Revision necessary: In depth analysis and ideas in 2nd call no 7, Technical Provisions for Life Assurance)

Article 21 Premiums for new business

(Revision necessary: In depth analysis and ideas in 2nd call no 7, Technical Provisions for Life Assurance)

Chapter 5: Rules on assets and general principles on investment management

(Prudent person plus approach to be introduced – inspired by Article 18 of the IORP Directive:

“Member States shall require undertakings located in their territories to invest in a prudent manner. To this end Member States shall require undertakings located in their territories to invest in accordance with the following rules [...]”)

Article 22 Assets covering technical provisions and capital requirements

Suggested wording in 1st call no 5, Investment Management Rules:

“The assets covering the technical provisions and the solvency capital requirement shall take account of the type of business carried on by an insurance undertaking in such a way as to secure the safety, yield and liquidity of its investment, which the undertaking shall ensure are diversified and adequately spread. To this end, an insurance undertaking shall have an appropriate investment plan.”

Art. 34 Reinsurance Proposal:

The assets covering the technical provisions shall take account of the type of business carried out by a reinsurance undertaking, in particular the nature, the amount and the duration of the expected claims payments, in such a way as to secure sufficiency, liquidity, security, quality, profitability and matching of its investments, which the undertaking shall ensure are diversified and adequately spread and which gives the undertaking the possibilities to respond adequately to changing economic circumstances, in particular developments in the financial markets and real estate markets or large impact catastrophic events

COMMISSION STAFF PROPOSAL

The assets covering the technical provisions and the capital requirements shall take account of the type of business carried out by an insurance undertaking, in particular the nature, the amount and the duration of the expected claims payments, in such a way as to secure sufficiency, liquidity, security, quality, profitability and matching of its investments, which the undertaking shall ensure are diversified and adequately spread and which gives the undertaking the possibilities to respond adequately to changing economic circumstances, in particular developments in the financial markets and real estate markets. To this end, an insurance undertaking shall have an appropriate investment plan.

Article N8 Requirements on asset-liability management

Suggested wording in 1st call no 6, Asset Liability Management Rules:

“To control its present and future exposure to financial and insurance risks, an insurance undertaking shall perform an asset-liability analysis appropriate for its business.”

(Revision of whole section below will be necessary -2nd call no 9, Safety measures, 3rd call no 19; Eligible elements to cover the capital requirements)

- Article 23** Categories of authorised assets
Revision will be necessary
- Article 24** Rules for investment diversification
Revision will be necessary
- Article 25** Contracts linked to UCITS or share index
Revision will be necessary
- Article 26** Matching rules
Revision will be necessary

Chapter 6 Rules relating to the Minimum Capital Requirement (MCR)

Article 27/ 28 MCR (Revision, 2nd call no 9, Safety measures, 3rd call no 19; Eligible elements for solvency requirement)

(CEIOPS working definition: “The minimum capital requirement reflects a level of capital below which an insurance undertaking’s operations present an unacceptable risk for policyholders and therefore, immediate supervisory action is needed).

Article 29 Absolute floor of MCR
2nd call no 9, 14, 15

Article N8a Powers of intervention – MCR
2nd call no 9, 14, 15

Chapter 7 Rules relating to the Solvency Capital Requirement (SCR) and Internal Models

Article N9 SCR

Suggested DRAFT wording in 2nd call no 10, SCR:

“To be able to absorb significant unforeseen losses and to give [reasonable] assurance to policyholders, an insurance undertaking shall hold at all times solvency capital which is adequate having regard to its overall risk profile. Solvency capital requirement shall cover the relevant [underwriting, credit market, liquidity, operational and other] risks. It shall be calibrated so that the probability of failure of an undertaking within [one] year is sufficiently low [0,5%?]”

(CEIOPS working definition: “The solvency capital requirement should reflect the amount of capital necessary to meet all obligations over a specified time horizons (including the present value of future obligations to a defined confidence level, taking into account all significant, quantifiable risks”).)

It should be clarified that the SCR may not be lower than the MCR.

Article N9a Powers of intervention – SCR
2nd call no 9, 10, 14, 15

Article N10 Use of an Internal Risk Model for calculating the SCR
2nd call no 11

Suggested wording in 2nd call no 11, SCR: Internal models:

“The Solvency Capital Requirement may be calculated by an undertaking’s own internal model after validation and approval by the competent authorities. The risk measure, the time horizon and the scope of the risks covered must not be less prudent than in the standard approach. Detailed compliance criteria for undertakings wishing to use internal models will be established in implementing measures”

Article N10a Use of partial models

Article N10b Powers of intervention – Internal model

Article N11 Validation of an Internal Model at Group level
(Cf. above, Article N10 and 2nd call no 18, Group and Cross-sectoral issues).

Chapter 8 Solvency Control Levels

(Articles to be added at a later stage, in light of 2nd call no 15, Solvency Control Levels)

Chapter 9 Assurance undertakings in difficulty or in an irregular situation

(Revision of whole chapter needed in light of Chapters 4-8 above. Some of the provisions below will probably already be covered.)

Article 37	Assurance undertakings in difficulty
Article 38	Financial recovery plan
Article 39	Withdrawal of authorisation

Chapter 10 Contract law, conditions of assurance, disclosure, market discipline

9.1. Contract law

Article 32	Law applicable
Article 33	General good
Article 34	Rules relating to conditions of assurance and scales of premiums

9.2. Information given to policyholders

Article 35	Cancellation period
Article 36	Information for policyholders

9.3. Other disclosure requirements

(Market discipline to be included)

Possibly further amendments in light of 3rd call no 22, Supervisory Reporting and Public Disclosure

Article NI3 *Supervisory Reporting*
(3rd call no 22, Supervisory Reporting and Public Disclosure)

Article NI4 *Public Disclosure*
(3rd call no 22, Supervisory Reporting and Public Disclosure)
(Articles 145-149 CRD as starting point)

Title IV

Provisions relating to right of establishment and freedom to provide services

Article 40	Conditions for branch establishment
Article 41	Freedom to provide services: prior notification
Article 42	Freedom to provide services: notification by the Home MS
Article 43	Freedom to provide services: changes
Article 44	Language
Article 45	Conditions of assurance, scales of premiums
Article 46	Assurance undertakings not complying with the legal provisions <i>(Revision needed in light of the general changes to supervisory powers?)</i>
Article 47	Advertising
Article 48	Winding-up
Article 49	Statistics <i>(Revision may be necessary)</i>
Article 50	Taxes on premiums

Title V

Third state agencies and branches

Article 51	Principles and conditions of authorisation	<i>(Revision needed)</i>
Article 52	Rules applicable to branches	
Article 53	Transfer of portfolio	
Article 54	Technical provisions	<i>(Revision needed, cf. Article 20 et seq.)</i>
Article 55	Solvency margin and guarantee fund	<i>(Revision needed, cf. Article 20 et seq.)</i>
Article 56	Advantages to undertakings authorised in more than one MS	
Article 57	Agreements with third countries	

Title VI

Subsidiaries of third country parent undertakings

Article 58	Information to the Commission
Article 59	Third-country treatment of Community undertakings

Title VII

Final and transitional provisions

Article 30	Review of the amount of the MCR and SCR (index) .
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