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Public consultation on Insurance Guarantee Schemes

Summary feedback statement

1. INTRODUCTION

This note summarises the feedback from the public consultation on insurance guarantee schemes that took place between 7 May and 7 July 2008¹. The European Commission received 30 contributions, from European and national associations, insurers, supervisors, ministries, a consumer panel, an insurance guarantee scheme and the Committee of European Insurance and Occupational Pension Supervisors. The comments and contributions received during the public hearing on 2 June 2008 are also integrated into this summary feedback statement.

1. Have new insurance guarantee scheme arrangements been introduced in your Member State or is the situation currently under review?

The following developments were reported. Bulgaria has recently introduced a guarantee scheme covering all classes of life insurance. The scope of the Financial Services Compensation Scheme of the United Kingdom has changed in July 2008 so that EEA risks written through EEA branches of UK insurers are now also covered by the scheme.

The situation is currently under review in Greece, Spain and Slovakia. The UK-FSA plans to consult on a review of the compensation limits for the Financial Services Compensation Scheme, including the limits for insurance, later in 2008.

Some respondents call for alternative safeguards, such as winding-up law or reinsurance or alternative arrangements such as the Austrian premium reserve funds (Deckungsstock) for life and health insurance, to be further explored.

¹ Available at: http://ec.europa.eu/internal_market/insurance/guarantee_en.htm#cons.

2. *Given that neither the current nor the future solvency regime create a zero-failure environment and that many MS have not established insurance guarantee schemes, which is your preferred option?*

a. *The status quo, i.e. adopting a caveat emptor approach possibly linked with enhanced policyholder information*

b. *Case-by-case intervention as and when problems arise*

c. *Mandating the establishment of insurance guarantee schemes in all Member States*

d. *Introducing a single EU-wide insurance guarantee scheme that covers all relevant policies written and purchased within the EU*

e. *Other options*

Most respondents prefer option (e) *other options*. Examples include voluntary solutions sought by the industry, such as portfolio transfer, a modern solvency regulation such as Solvency II or reinsurance arrangements. A guarantee fund for pan-European groups supervised under the group support regime under Solvency II is also suggested.

Views are about equally split between options (a) *status quo, i.e. adopting a caveat emptor approach possibly linked with enhanced policyholder information* and (c) *mandating the establishment of insurance guarantee schemes in all Member States*. Those respondents in favour of option (a) refer for example to past experience. They underline the importance of effective insurance supervision to minimise the possibility of insurance failures which would be the primary means of protecting policyholders. Moreover, it is felt that the introduction of an insurance guarantee scheme may have adverse effects on the behaviour of market participants and may distort competition. Those respondents in favour of option (c) also refer to their past experience, the differences in national market conditions (potentially linked with cross-border issues), the importance of a level playing field for undertakings and consumers, as well as consumer protection considerations.

There is little or no support for the other options. Options (a), (b) and (d) are clearly ruled out by some respondents.

3. *Do you agree with the conclusion that, costs can to a certain extent be adjusted through scheme design and that, if properly designed, introducing an insurance guarantee scheme can be pro-competitive and improve the operation of the market?*

Most respondents agreed that the costs of an insurance guarantee scheme can to a certain extent be mitigated through scheme design and that, if it is properly designed, introducing an insurance guarantee scheme can be pro-competitive and improve the operation of the market. However, a number of respondents contested such a conclusion.

4. Do you consider the presence or absence of insurance guarantee schemes to be an important factor in the development of cross-frontier insurance business in the single market and, in your view, which aspects of the current uncoordinated situation already or potentially constitute obstacles to the further development of the single insurance market?

A number of respondents consider that the presence or absence of insurance guarantee schemes has little or no impact on the development of cross-border business. Others perceive the presence or absence as an obstacle to the development of a single market in insurance. For some respondents it is difficult to evaluate the impact of an insurance guarantee scheme on cross-border insurance business.

A large number of respondents believe that other factors are likely to be more important determinants of consumer choice between insurance products than the existence of an insurance guarantee scheme. Such factors are the general strength of an insurer and its presence in the market, differences in national legislation and supervision, taxation, information provided by intermediaries, limited awareness of consumers of the existence of an insurance guarantee scheme or its coverage and hence little effect on the purchasing decision as well as cultural differences affecting insurance needs, supply and demand and language barriers.

It is also noted that to the extent that market evolution and policy initiatives, notably Solvency II, lead to a more integrated single market, differences in insurance guarantee schemes, including the absence of an insurance guarantee scheme, may become a relatively more substantial impediment than it appears to be at present.

5. Which are the key considerations (for and against) in the trade-off involved in the decision on whether or not to establish an insurance guarantee scheme and what relative weight do you attach to these key considerations?

The respondents list the following key considerations in favour of the establishment of an insurance guarantee scheme: enhanced consumer protection, increased consumer confidence in the settlement of insurance claims and market confidence, increased financial stability, industry reputation benefits, equal treatment of policyholders across the EU as well as a level playing field within the sector and with the banking and the securities sectors. Moreover, the current diverse landscape would be sub-optimal. A coordinated EU-wide approach would help to encourage the development of a single market.

The following key considerations are listed against the establishment of an insurance guarantee scheme: moral hazard, practicality, contagion risk and distortion of competition. Other protection mechanisms (e.g. insurance supervision, in particular Solvency II, portfolio transfer, winding-up law and the premium reserve funds (Deckungsstock) such as in Austria) would be equally effective. Moreover, costs would outweigh the benefits. Insurance guarantee schemes would be too costly for small and/or highly concentrated markets. Furthermore, insurance guarantee schemes would have an aspect of unfairness towards the majority of policyholders and insurers who would in the end pay the costs incurred by those not behaving responsibly. It was also questioned whether an insurance guarantee scheme could bear the costs of a major failure or a systemic crisis.

Several respondents state that any EU legislative initiative should be subject to an impact assessment. It is also noted that, if only very few aspects of scheme design were to be harmonised, the relevance of regulating the issue at EU level would be questionable.

6. Is the case for establishing an insurance guarantee scheme in insurance weaker than in the banking and securities sectors and which lessons, if any, can be learned from the banking and securities sectors?

The majority of respondents respond that the case for establishing an insurance guarantee scheme in insurance is not weaker than in the banking and securities sectors. It is pointed out, that it would be easier to provide a workable insurance guarantee scheme in insurance, than to provide for a credible deposit guarantee scheme. There are economic similarities between life insurance savings products and products from other sectors such as the fund and banking industries, which could make it difficult for consumers to understand why, for example, a bank deposit is guaranteed, whereas a life insurance product which has comparable features is not.

It is also noted, that there would be substantial differences between insurance and the banking and securities sectors. These differences relate to regulatory and risk environments (e.g. insurance has less concern with liquidity management), the nature of products, related timeframe and cost aspects. While some consider, that these differences would make it difficult to draw comparisons, others consider that these differences should be recognised in the scheme design, for example in the compensation arrangements. It is also stated that policyholders should benefit from at least the same level of protection as the creditors in the banking and securities sectors.

As lessons to be learnt from the banking and securities sectors, respondents mention, inter alia, the home state principle as well as the introduction of limits on compensation in order to confine moral hazard. While some consider the minimum level of harmonisation in the other financial sectors as positive, others consider that the Directive on Deposit Guarantee Schemes falls short on achieving a level playing field and has implications for financial stability and competition. It is also suggested that the Directive on Deposit Guarantee Schemes would deal with cross-border insolvencies in an unsatisfactory manner.

If an insurance guarantee scheme were to be implemented in all Member States to address cross-border problems, the following questions would have to be addressed:

7. What should be the geographic scope of the insurance guarantee scheme – i.e. should the national insurance guarantee scheme be based on the home or the host state principle?

The vast majority of respondents prefer the home state principle. The key consideration is that the home state principle is consistent with the EU supervisory framework. This would appear to be the best method for ensuring that regulatory authorities in the home Member State operate a strong prudential regime and that the costs of the failure of such a regime do not fall on other Member States. Moreover, the administration of an insurance guarantee scheme is closely linked to rules regarding insolvency and

liquidation, which are the responsibility of the home Member State. The home state principle would be consistent with the regulation in the banking and securities sectors.

Only very few respondents are in favour of the host state principle. Arguments in favour of the host state principle include an equal level of protection for all policyholders in the same Member State and a level playing field for all undertakings operating in the same market. The host state principle would allow the insurance guarantee scheme to meet the particular requirements of the local market and it would be more convenient for claimants to work with a scheme based in their own jurisdiction.

It is also noted that the host state principle would be desirable from the point of view of the consumer, whereas the home state principle would be preferable from the point of view of the supervisor. Another possibility would be a mixture of home and host principles. The principle of geographic scope might also depend on the type of insurance class.

8. Should subsidiaries participate in and be covered by the insurance guarantee scheme of the Member State in which the group supervisor is located under the group support regime under Solvency II?

Some respondents support the idea that subsidiaries should participate in and be covered by the insurance guarantee scheme of the Member State in which the group supervisor is located under the group support regime. Others consider it too early to take a decision given that the group supervision regime under Solvency II is currently being negotiated in Council and European Parliament. One possibility might be an option for subsidiaries to opt-into the system of the parent undertaking. The majority of respondents are however not in favour of the idea that subsidiaries should participate in and be covered by the insurance guarantee scheme of the Member State in which the group supervisor is located under the group support regime.

9. What degree of harmonisation across Member States would be required between national insurance guarantee schemes and which features of an insurance guarantee scheme should be harmonised? Should they be harmonised, please indicate your preferred approach.

a. Geographic scope (home v host state principle)

b. Organisational structure (single or multiple insurance guarantee schemes, cooperation with insolvency practitioners and supervisory authority, staffing arrangements/outsourcing)

c. Funding arrangements (in particular ex ante or ex post funding, risk-weighted contributions and contribution limits)

d. Policies covered - What classes of insurance should be covered by the insurance guarantee scheme and which insurance classes could be excluded?

e. Claimant eligibility - Which claimants should benefit from the insurance guarantee scheme, and which claimants could be excluded?

f. Protection amounts and limits (caps or maximum compensation levels, deductibles, etc.)

g. Nature of intervention (in particular the payment of compensation or portfolio transfer)

h. Payout timing and information to policyholders/beneficiaries

Most respondents are in favour of minimum harmonisation, though some prefer maximum harmonisation. Others consider that there is no need for harmonisation at all.

The vast majority of respondents are in favour of harmonising the geographical scope of an insurance guarantee scheme (on the basis of the home state principle). A large number of respondents are also in favour of harmonising the policies covered by an insurance guarantee scheme, the claimant eligibility, protection amounts and limits and payout and timing. Fewer respondents support harmonisation of the organisational structure, nature of intervention and funding arrangements.

ANNEX. List of respondents

- (1) ABI (Association of British Insurers)
- (2) Association of International Life Offices (AILO)
- (3) Assuralia
- (4) AXA Brussels office for Institutional and European Affairs
- (5) BaFin (Federal Financial Supervisory Authority Germany)
- (6) Bipar
- (7) Canada Life Assurance Europe Limited
- (8) CEA (European insurance and reinsurance federation)
- (9) CEIOPS (Committee of European Insurance and Occupational Pension Supervisors)
- (10) Consumer Consultative Panel, Ireland
- (11) Czech Insurance Association
- (12) Department of Finance, Ireland
- (13) Federation of Finnish Financial Services
- (14) Fédération Française des Sociétés d'Assurance
- (15) Financial Regulator Ireland
- (16) Financial Services Ireland
- (17) FSA HMT United Kingdom
- (18) GDV (German Insurance Association)
- (19) Irish Insurance Federation (IIF)
- (20) Ministry of Finance Netherlands
- (21) Ministry of Finance Norway
- (22) Ministry of Health and Social Affairs Finland
- (23) Ministry of Finance Poland
- (24) Ministry of Finance Sweden and the Swedish Financial Supervisory Authority (joint reply)
- (25) Protektor Lebensversicherungs-AG
- (26) Slovak Insurance Association
- (27) Swedish Insurance Federation
- (28) Swiss Insurance Association (SIA)
- (29) The Dublin Insurance & Management Association (DIMA)
- (30) Zurich Financial Services