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**Fast-track Reinsurance Supervision project**  
**– Overview and issues for consideration**  
**by the Insurance Committee**

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*Questions to the Members of the Insurance Committee:*

*Part 1:*

- *Do Members have comments on the Services' general conclusions in part 1 of this note?*

*Part 2:*

- *Which of the outlined alternatives for quantitative requirements in part 2 of this note do Members generally prefer (alternative 1, alternative 1b or alternative 2)?*
- *Do Members have comments on specific requirements or levels outlined in the grid?*
- *Do Members prefer life reinsurance requirements to be approximated by non-life reinsurance rules, or should direct life rules be used?*

**Purpose of the note**

The purpose of this note is to serve as basis for an orientation debate in the Insurance Committee on the fast-track reinsurance project. Written comments by Member States [subject to IC approval: "and interested parties"] on the note are welcome.

## **Part 1 Overview of the fast-track reinsurance project**

### ***Background***

In 2000, Member States and the Commission Services agreed to start a project in order to assess the possibility of establishing a harmonised framework for reinsurance supervision in the EU. After discussions and hearings in 2000-2002, it was decided that a focus should be given to a “fast-track” approach. This approach will necessarily to a large extent have to be based on current direct insurance supervision rules. It should lead to EU legislation in a reasonably short period of time, which would benefit supervisors and companies as well as enhance the EU position in future mutual recognition negotiations with non-EU countries. It is worth noticing that all major jurisdictions, which supervise reinsurance, do so on the basis of the rules for direct insurance. A fast-track approach would also be in line with initiatives from the G7 group, the World Bank and IAIS. In recent FSAP assessments, the lack of a harmonised reinsurance supervision scheme in the EU has been highlighted as an important gap in the financial services regulatory framework.

After an orientation debate in the Insurance Committee in April 2002, the Commission Services started preparing detailed proposals for the reinsurance project. A draft legal text has been discussed at several working meetings<sup>1</sup>. The Commission Services together with Member States have performed simulations to analyse the impact of certain combinations of solvency requirements, minimum guarantee funds and related quantitative issues<sup>2</sup>.

According to the Financial Services Action Plan, a Commission proposal for a reinsurance supervision directive should be presented towards the end of 2003. A further working meeting of the IC Reinsurance Subcommittee is planned for 9 September 2003.

### ***Objectives of the exercise***

The Commission Services and most Member States have agreed on the following overall objectives for the fast-track reinsurance supervision project:

- The system should establish a sound and prudent regime in the interest of policyholders.

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<sup>1</sup> 4 November and 18 December 2002, 8 May and 11 June 2003.

<sup>2</sup> The draft text version dated 28 May 2003 (MARKT/2531/02 rev 2) has been sent to Members of the Insurance Committee. Also available on the Commission website:  
[http://europa.eu.int/comm/internal\\_market/insurance/docs/2531-02-rev2\\_en.pdf](http://europa.eu.int/comm/internal_market/insurance/docs/2531-02-rev2_en.pdf)

<sup>2</sup> Summary comments on certain simulations will be included in the "extended impact assessment" that will accompany the Commission proposal for a reinsurance directive.

- The system should build on essential coordination of Member States legislation and mutual recognition of the supervision in the Member State where the reinsurance undertaking is licensed. Once licensed a company should automatically be allowed to do business all over the European Community under the freedom of establishment and the freedom to provide services. No additional supervision or checks on the reinsurance undertaking should be performed by supervisors in host Member States.
- The introduction of a harmonised system for reinsurance supervision should lead to the abolition of systems with pledging of assets to cover outstanding claims provisions.
- A recognised harmonised system for reinsurance supervision could bring an increase of the reduction factor in the solvency margin calculation for business ceded to EU licensed reinsurers.

### ***General outline of the project***

At an early stage of the project it was concluded that a fast-track approach would necessarily have to ***base itself largely on existing rules*** in the direct insurance field, however taking reinsurance-specific aspects into account. This approach has also been chosen by the IAIS Reinsurance Subcommittee in their draft standard on minimum requirement for supervision of reinsurers. The discussions during the reinsurance project – as well as Solvency II – have convinced the Commission Services that too many departures from the existing rules will in fact make a fast-track approach impossible.

When the ***Solvency II proposals*** have been finalised, it is likely that the reinsurance supervision regime will be adjusted accordingly. This means that certain solutions in a fast-track approach would have a ***temporary character***. This would for example be the case for the solvency margin requirement.

International influences will be taken into account to the extent possible also in a fast-track approach. The ***international projects on reinsurance supervision, solvency and insurance accounting are not yet finalised*** and it is unlikely that we will know the clear direction before adopting a proposal for a Directive on reinsurance based on a fast-track approach.

The basic elements of a fast-track regime are outlined in the box below<sup>3</sup>. Certain issues, particularly those linked to quantitative parameters, are still under discussion (see part 2 of this note).

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<sup>3</sup> Detailed comments and reasoning behind the proposals are contained in a Commission staff note from 1 February 2002. Available at the Commission website:  
[http://europa.eu.int/comm/internal\\_market/insurance/docs/2002-02-fastrack/2002-02-fastrack\\_en.pdf](http://europa.eu.int/comm/internal_market/insurance/docs/2002-02-fastrack/2002-02-fastrack_en.pdf)

<i>Element of a fast-track regime</i>	<i>Commission Services' proposals</i>
Licence or passport solution	License
Scope of authorisation	It shall permit a reinsurance undertaking to carry out life, non-life or both kinds of reinsurance. Licensing should not be based on further specified insurance classes.
Scope of regime	Pure reinsurers and reinsurance captives. The application also to direct insurers accepting inwards reinsurance is discussed in <i>part 2 of this note</i> .
Treatment of technical provisions	Current rules in the direct insurance directives should be used.
Equalisation provisions/reserves	Equalisation provisions/reserves would be required for credit reinsurance, but there would be an option for Member States to require them also in other reinsurance lines.  The issue whether such provisions/reserves amounts could be counted against the solvency margin will be discussed in <i>part 2 of this note</i> .
Use of actuarial methods	Encouraged, but no formal legal requirement.
Solvency margin, minimum guarantee fund	<i>See part 2 of this note.</i>
Investment rules	A “prudent person” approach should be used.
Asset cover rules	The technical provisions – not the full solvency margin – should be covered by quality assets.
Accounting, financial reporting and statistics	The current requirements in the direct directives should apply also to reinsurance undertakings.
Reinsurance/retrocession reduction factor	<i>See part 2 of this note.</i>
Powers of intervention for supervisors	In principle the same as for direct insurance undertakings, incl. the Solvency I amendments.
Withdrawal of license	To the extent possible the same procedural arrangements as for revoking a direct insurance licence should be used.
Use of internal models	Should not be allowed in a fast-track reinsurance regime.

Moreover, the introduction of an EU legal regulatory framework for reinsurance will have an impact on the existing directives on insurance<sup>4</sup> (non-life, life and insurance groups' directives). Indeed, these legal instruments are the foundations of the current legal framework for insurance. To the extent that the foreseen reinsurance framework shall complete this legislative framework, it appears necessary to take account of it in order to build a consistent regulatory framework for the whole insurance/reinsurance sector. Accordingly, the existing insurance directives need to be adapted.

These adaptations are also prompted by the purpose of submitting direct insurance undertakings accepting reinsurance to the solvency requirements which would be laid down for reinsurance undertakings and ensuring a level playing field amongst different undertakings writing inwards reinsurance business.

The insurance groups' directive 98/78/EC shall also be adapted in order to take account of the fact that EU reinsurance undertakings shall be subject to supervision<sup>5</sup>.

Furthermore some Member States have expressed their concern that EU law may provide a dual legal treatment for the winding-up of reinsurance undertakings depending on whether the reinsurance undertaking involved in the winding-up situation is subject to the Directive on winding-up of insurance undertakings (2001/17/EC) or not. In order to avoid such a situation, it would be appropriate to consider reviewing the existing legal framework and apply the winding-up directive also to reinsurance undertakings covered by the future directive on reinsurance.

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<sup>4</sup> Non-Life: Directives 73/239/EEC, 88/357/EEC, 92/49/EEC  
Life: Directive 2002/83/EEC;  
Insurance Groups: Directive 98/78/EEC.

<sup>5</sup> A subsequent adaptation of Directive 2002/87/EC relating the financial conglomerates will also be necessary.

## Part 2 Issues for consideration by the Insurance Committee

In the document MARKT/2523/03, the Services outlined possible solutions and alternatives for certain quantitative parameters and related issues<sup>6</sup>. After consideration of the comments made in the IC Reinsurance Subcommittee and by interested parties, the Services believe that two major alternatives can be outlined for these issues. Alternative 1 would introduce requirements that are broadly similar to those of direct insurance, whereas alternative 2 would basically mean an enhancement of the requirements by around 50%.

Alternative 1 is considered by some Members of the IC Reinsurance Subcommittee as most appropriate in a fast-track context. Since the reinsurance directive broadly aims at establishing a regulatory framework for reinsurance inspired by the existing regime for direct insurance undertakings, the solvency requirements for reinsurance undertakings should also mirror existing solvency rules. Too many deviations at this stage are not considered justified as the Solvency II process is still in progress.

Alternative 2 is preferred by other Members of the IC Reinsurance Subcommittee as it reflects the more risky nature of reinsurance business. Accordingly, reinsurance undertakings should be subject to higher solvency requirements than direct insurance undertakings. A higher requirement would also be linked to amendments of certain other rules (an increased reinsurance reduction factor, use of equalisation provisions/reserves to cover the solvency margin).

The two basic alternatives can be outlined as follows:

<i>Issue</i>	<i>Alternative 1: Requirements close to direct insurance rules</i>	<i>Alternative 2: "150%" alternative</i>
<i>Solvency margin for non-life reinsurance</i>	16% of premiums 23% of paid claims	25% of premiums 35% of paid claims
<i>Solvency margin for life reinsurance</i>	Use non-life reinsurance solvency requirements, or direct life requirements.	Use non-life reinsurance solvency requirements, or direct life requirements.
<i>Minimum guarantee fund</i>	1m EUR (reinsurance captive of industrial or commercial group)  3m EUR (reinsurance undertakings)	1m EUR (reinsurance captive of industrial or commercial group)  3m EUR (reinsurance undertakings)
Reinsurance reduction factor	50%	75%

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<sup>6</sup> This document contains detailed discussion on the issues dealt with in this part of the report. Website: [http://europa.eu.int/comm/internal\\_market/insurance/docs/2523-03\\_en.pdf](http://europa.eu.int/comm/internal_market/insurance/docs/2523-03_en.pdf)

Equalisation provisions/ reserves	Under EU law such provisions/reserves would not be considered part of the available solvency margin.	Under EU law such provisions/reserves could be considered part of the available solvency margin
Application to direct insurance undertakings	Possibly (in particular alternative 1b below)	Yes

The Services could see the possibility of an enhanced alternative 1 (*alternative 1b*) according to which solvency requirements could be enhanced by up to 50% for certain reinsurance business lines or types of reinsurance contracts. This could be done through comitology after recommendation from the interim CEIOPS (Committee of European Insurance and Occupational Pension Insurance Supervisors)<sup>7</sup>. Until such comitology decisions have been taken, direct insurance solvency requirements should apply. If solvency requirements are increased, a possibility would exist to increase the reinsurance reduction factor or use equalisation provisions/reserves for covering the solvency margin requirement. If this solution would lead to different solvency rules between insurance and reinsurance, the reinsurance rules should be applied to incoming reinsurance business accepted by direct insurers.

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<sup>7</sup> The former Conference of EU Insurance Supervisors.