Minutes of the meeting of the Expert Group on Banking, Payments and Insurance (Insurance formation)

Brussels, 1st July 2013

Opening and welcome.
The meeting was opened and chaired by Mr Klaus WIEDNER, Head of the Insurance and Pensions Unit at the European Commission’s Directorate-General for Internal Market and Services, since March 16 2013.

The Chairman explained that following the institutional changes introduced by the treaty of Lisbon (articles 290 and 291 of the consolidated Treaties, with Declaration 39 on article 290), the EIOPC, although it still exists, will henceforth only deal with draft implementing acts of the Commission; draft Delegated Acts of the Commission, and all matters related to level 1 legislation, will be discussed by the new expert group on banking insurance and payments (EGBIP). The membership of the group will vary according to the subject under discussion. This is therefore the first meeting of the Insurance formation of such group.

The Chairman welcomed the Croatian delegation on the day of Croatia’s accession to the EU.

1. Agenda
The draft agenda was adopted.

2. Minutes of the 23rd meeting of the EIOPC held on 27 November 2012
No requests for changes to, or comments on, the draft minutes were raised and the minutes of the 23rd meeting of the EIOPC, as submitted by the Commission, were adopted.

3. Solvency II/Omnibus II — Recent Developments, Next Steps
   i. Update on the technical assessment on the long-term guarantees package
      The Chairman recalled that Omnibus II/Solvency II is a top priority and should be concluded in the shortest possible delay. The protraction of the negotiations is causing considerable uncertainty in the industry and among supervisors. It is also detrimental to policy holder protection as Solvency I is outdated.
The Chairman then updated the members on the most recent developments concerning the proposed Omnibus II Directive. He stated the EIOPA LTGA Report had been adopted on 14 June 2013 and gave the representatives of EIOPA the floor to present its main conclusions.

Representatives from EIOPA outlined the main points from EIOPA’s LTGA report mentioned above.

A representative from EIOPA stressed that the Report is basically an impact study of different ways to mitigate the effects of volatility in the insurance market. It contains observations and advice to help the trilogue parties in taking decisions on the way forward in Omnibus II. The Report followed the terms of reference set by the trilogue parties and was approved by EIOPA’s Board of Supervisors comprising the supervisory authorities of each member state, which also took the necessary decisions on the key steps and on the outcomes thereof.

Another EIOPA representative presented the Report in detail. The Report seeks to be an EU wide effort and to take on board the views of experts from different backgrounds (ESRB for instance) and from stakeholders and to make a positive contribution to the forthcoming Trilogues.

The guiding principles of the assessment are:

- Alignment with the Solvency II framework and the balance sheet concept;
- Full transparency and comparability;
- Efficient linking of all 3 Pillars;
- Proportionality and simplicity; and
- Adequate treatment of transitional issues.

The Report fully took into account and followed the underlying principles of Solvency II and the need to ensure a high degree of policy holder protection as well as effective supervisory processes.

On the five measures EIOPA was asked to test the advice is (in summary terms) the following:

1. Countercyclical premium (CCP)/Volatility Balancer

Replace the CCP with a predictable volatility adjustment mechanism, the Volatility Balancer, which is to be permanent, based on a representative asset portfolio, currency specific with a national top-up in exceptional market circumstances, applicable to all insurance obligations apart from unit-linked, is a pure own funds adjustment and could turn negative under certain conditions (similarly to the Matching adjustment).
2. Extrapolation

Select a convergence period significantly longer than 10 years for the Euro (e.g. 40 years);

For other currencies take account of the characteristics of the local bond and swap markets;

Foresee dedicated Pillar 2 measures such as sensitivity analysis.

3. Matching Adjustment (MA)

For the classical MA include the strict criteria relating to CQS 3 (the 33% portfolio limit excluding government bonds and the MA cap) plus implement some minor amendments to the measure: inclusion of immaterial mortality risk; ability to manage the credit quality of portfolios in case of downgraded risk; maximum levels of MA for CQS 3 investment to be provided by EIOPA; appropriate criteria and conditions to deal with “cliff effect situations” to be provided by EIOPA via guidelines.

For the extended MA, exclude it from the LTGA package.

4. Transitional measures

Implement the transitional measures and accompany the tested transitional measure with a second transitional measure that can address different issues to the transitional challenges that arise in undertakings with long term guarantees. Both measures should result in Own Funds adjustment only (no impact on capital requirements or technical provisions).

5. Extension of the Recovery Period

This measure should be maintained but extended to provide for possible Pillar 2 solutions for other sort of crisis situations. The strict link to liability duration should be reduced and 7 years should be the maximum extension of the recovery period.

The representatives from EIOPA further added that the LTGA package is very complex in terms of implementation and interpretation of its results. There should therefore be full transparency (public disclosure) of the impact of the measures in question. Furthermore an Own Funds adjustment approach for transitional measures and volatility balancer should be implemented, since the two measures do not directly relate to the economic reality of the undertakings.

Finally, on the Single Market impact of the LTGA measures and on their consistency, EIOPA’s advice is to have no link of LTGA measures to Member states options and no exclusion of cross-border business from any measure (apart from the exceptional national top-up to the Volatility Balancer). Furthermore the principle of substance over form should be fully incorporated in the LTGA package.
The Chairman and representatives from Member states thanked EIOPA for its report. It was considered a valuable and important contribution to the forthcoming negotiations on Omnibus II.

Representatives from several Member States pointed out that the scope, meaning and terms of the Volatility Balancer needed to be better, more clearly and more transparently established. They inquired as to how EIOPA reached the advice given on this issue, considering that in their opinion the calibration of the volatility balancer was too low.

A representative from one Member State indicated that the volatility balancer has not been fully tested by EIOPA and further calibration thereof is necessary, especially as regards short-term volatility. The Member State in question conducted its own internal test and the Volatility Balancer as put forward by EIOPA was not at all sufficient on its domestic market and a further (higher) calibration thereof was thus necessary in its view.

A representative from another Member State pointed out that the classic matching adjustment as set up by EIOPA cannot be applied in that Member State, the scope would have to be considerably extended in order for there to be any effect. As to the volatility balancer it should be more geared for short term volatility.

As regards the recovery period, a representative from the same Member State considered it should not exceed seven years at most.

On the transitional measures, representatives from two Member States considered that the transitional period foreseen (7 years) had not been sufficiently tested by EIOPA and should be quite considerably extended in order to reach a solution which would work in all Member States.

The representatives from EIOPA replied, as concerns the volatility balancer, that the CCP had been duly tested but it would lead to sub-optimal solutions and considerable uncertainty. The volatility balancer was duly tested and is technically effective to reduce volatility on own funds. In certain exceptional circumstances EIOPA’s advice includes the possibility of national top-up.

As regards the issue of the Matching Adjustment, the representatives from EIOPA stated that EIOPA’s advice endeavours to reach a balanced and prudentially sound solution and to strive for an efficient protection of policy holders.

On the transitional measures the representatives from EIOPA stated that the widening of the scope of transitionals could be envisaged but in a way that leads to both a realistic and reasonable solution.

On the recovery period in case of exceptional fall they stated that, as envisaged in EIOPA’s report, seven years should be the maximum length thereof.

The Chairman then referred to the Commission’s services’ report of 24 June 2013 (sent to the co-legislators on 28 June 2013) generally endorsing the EIOPA assessment, and
to the non-paper sent to the Presidency in view of the Council Financial Services Working Group meeting of 4 July 2013, both proposing that negotiations on Omnibus II’s LTGA package should take EIOPA’s recommendations as a starting point (the EIOPA Report should therefore be the basis for negotiations) and that the focus should be on improving the design and the calibration of the measures proposed in EIOPA’s report.

Representatives from several Member States took the floor to present their main issues in the forthcoming negotiations as regards the LTGA (calibration of the volatility balancer, length of transitional measures, scope of the Classical Matching adjustment). The Chairman stated those remarks were duly noted and that negotiations proper would (re)start only on 4 July 2013 in the Council.

The Chairman added that the LTGA package is the main item for the Trilogues but there are some other outstanding issues: 3rd country equivalence, treatment of sovereign debt and the official sending by Member States of explanatory documents (formerly known as correlation tables) accompanying the official notification of the transposition measures. On all these points, in his view, agreement is well within reach once there will be agreement on the LTGA package which is by far the main issue on the table.

The Commission’s services have sent non-papers proposing a way forward on these issues to the Presidency in view of the discussions in the Council on 4 July 2013.

On 3rd country equivalence the solution would be to leave open the possibility for the transitional period to be extended by a further 5 years where it is shown that a third country has made progress towards convergence.

On sovereign debt, reference was made by the Chairman to the CRD IV solution. Recital (84) of CRD IV states that sovereign risk be captured in written policies and procedures on concentration risk, with the Commission producing a report at an appropriate point in time on any desirable changes to the prudential treatment of sovereign bonds of concentration risk. A similar recital should be included in Omnibus II, appropriately tailored to the Solvency II regime.

On explanatory documents, the Chairman considered the compromise should respect the Joint Declaration on this issue by the EP, the Council and the Commission in 2011. Consequently Article 3 of Omnibus II and Article 309 of Solvency II should not include provisions on explanatory documents. Instead, the model recital in the Joint Declaration of the three institutions should be included in Omnibus II.

The Chairman stressed once again that the forum for negotiations was the Council. There were no follow-up questions.

Representatives from two Member States pointed out that the Council needs adequate time to reach a position on the LTGA package (plus the other outstanding issues) and
pleaded against an early restart of Trilogues in July, which could in their view be counter-productive as long as the Council Presidency has no mandate, as past experience clearly showed.

The Chairman stated those remarks were duly noted.

ii. Legislative procedure and Trilogues

The Chairman announced that the Commission had replied to a letter from a Member State (also on behalf of most Member states) concerning the transposition of Solvency II (for which the deadline was 30 June 2013). Due to the delay in the adoption and entry into force of Omnibus II no infringement procedures will be launched at this stage against Member States. In view of the current application date for Solvency II of 1 January 2014 (which is also the date of repeal of Solvency I) the situation will be reassessed in September 2013 in view of the progress made in the Omnibus II negotiations. Discussions will restart in the Council on 4 July 2013 and a Trilogue will take place on 10 July 2013 (mainly to debrief on the LTGA Report). The following trilogue is in principle scheduled for 10 September 2013.

As to the new date of application for Solvency II the Chairman stated there are two options, either a short term “quick-fix 2” delaying the application date by about six months in order to avoid a legal vacuum on 1 January 2014 and to allow for the publication and entry into force of Omnibus II (which would have been agreed in the autumn of 2013 and entered into force in the first half of 2014 and contain the final dates for transposition and first application of Solvency II as well as of repeal of Solvency I) or a long-term “quick-fix 2” containing the final dates of transposition and application of Solvency II and of repeal of Solvency I, which would have to be agreed in the trilogues at an early stage.

Representatives from most Member States welcomed the fact that there would probably be a second quick-fix Directive proposed by the Commission. Representatives from two Member States expressed their preference for a short-term “quick-fix 2” Directive.

iii. Green Paper on Long term investment

The Chairman informed the members of the Expert Group that the Green Paper on long-term investments was adopted by the Commission on 25 March 2013. It launched a three-month public consultation on how to foster the supply of long-term financing and how to improve and diversify the system of financial intermediation for long-term investment in Europe. The public consultation ended in late June 2013.

The Green Paper discusses several measures facilitating long-term financing in the European economy. It covers areas such as corporate governance, taxation, financial market infrastructure, public procurement, and financial regulation.
The Commission is also dealing with long-term financing in the context of its impact assessment on long-term guarantees, specifically in relation to the assessment of the impacts of long-term guarantee measures on long-term financing.

A representative from EIOPA stated that EIOPA shares the goals of the Green Paper and will issue its report on the issues in question in principle later in the year. Solvency II will favour long-term investment, for example by removing the possibility of limitations on investments by Member States.

A representative from a Member State mentioned that the needs of SMEs, which rely heavily on bonds, do not seem to be sufficiently taken into account. It asked EIOPA for its position on whether this could or should be taken into account in the Delegated Acts under Solvency II.

The EIOPA representative stated that Delegated Acts is rather a matter for the Commission when that stage is reached. In any case EIOPA is also looking at the issue mentioned by the Member state in question.

The Chairman noted that the Delegated Acts can only be finalised and adopted once Omnibus II will have entered into force.

4. Update on the preparation of the IORP II Proposal

A representative of the Commission provided an update on the state-of-play of the IORP II preparation, recalling that Commissioner Barnier had announced on 23 May 2013 that the IORP II proposal will focus in a first instance on governance, reporting and transparency. That representative congratulated EIOPA for having delivered the first QIS ever for the IORP industry. This has provided a European-wide framework to assess the financial position of IORPs operating defined benefit schemes. There is now a greater understanding about how different valuation methods, security mechanisms and benefit adjustment mechanisms interact.

Another representative of the Commission added that the White Paper on pensions announced the IORP2 proposal for 2012 as a measure to support the development of private complementary retirement savings. The Commission Services therefore consider it important to present the IORP II proposal without further delay. Greater take-up of occupational pensions requires trust and performance, as is the case for any financial product. Strengthening governance requirements aims to overcome principal-agent problems: regulation needs to make sure that those effectively running the IORP do so in the best interest of the scheme members. Better governance leads to higher risk-adjusted investment returns, which means either higher pensions or lower contributions. Moreover, greater transparency aims to reduce information inefficiencies. It is important that people take good retirement financing decisions while they are young, so that capital is build-up efficiently over a typical accumulation period of 40 years. A 2010 Eurobarometer survey suggested that one in five EU citizens has worked or studied in another Member State at some point and that this is even more so for the young generations. Having comparable information disclosures is also
important in the light of the Portability Directive in the process of being adopted. Finally, the IORP II proposal will aim to remove remaining barriers for cross-border activity. Recent consultations with companies that have actually set up cross-border IORPs or have seriously considered doing so have underlined the complications of going ahead, due to legal uncertainties and additional transaction cost.

A representative of EIOPA informed that the final QIS results would be available on 4 July 2013. At the same time a discussion paper on sponsor support would be published.

A representative from one Member State asked that the date at which Solvency 2 will apply to IORPs run by insurance undertakings (article 4 of the IORP Directive) should be synchronised with the possible introduction of solvency rules for IORPs in a subsequent phase of the IORP Directive review. A representative of the Commission suggested that this should be raised during the Omnibus 2 Directive negotiations.

Representatives from three other Member States welcomed the Commissioner's announcement of 23 May 2013. Those representatives remained to be convinced that a proposal on governance, reporting and transparency will be useful and called for proportionate regulation. Those representatives also asked for reassurance that the IORP2 proposal would not contain reporting of common quantitative requirements.

A representative of the Commission mentioned that the IORP industry (Pensions Europe) had recently carried out an assessment of the potential administrative burden of an IORP II proposal. The Commission Services are in the process of preparing an impact assessment report to set the costs against the benefits.

5. Update on the negotiations concerning the revision of the Insurance Mediation Directive 2002/92/EC

i. Discussions in the European Parliament

A Commission representative updated the Expert Group members on how the negotiations are developing.

At the European Parliament, the vote in the ECON Committee is planned for September 2013 and the Plenary vote for October 2013. The results of any possible Trilogues before the European Parliament elections of May 2014 would not be binding on the next European Parliament, if the proposal were not to be formally adopted beforehand.

The main issues being debated in the European Parliament are the lighter ancillary regime, whether transparency on remuneration should be mandatory or on demand and whether and how it could be applied to direct insurance sellers, whether professional qualification requirements should be set at Level 1 or through delegated acts and on the rules for the sale of insurance PRIPs.
At the request of the representative of a Member State a Commission representative stated that a coherent approach with the MiFID II proposal, on which the Council recently reached a General Approach, will be ensured.

At the Council there were no meetings under the Irish Presidency and the Lithuanian Presidency will concentrate first of all on the Omnibus II file and cannot at this stage guarantee it will hold any meetings on IMD 2.

**ii. Update on the adaptation of the required cover for professional indemnity insurance**

A Commission representative informed about the need to adapt the thresholds applicable to professional indemnity insurance and liquidity requirements provided under Article 4 of the existing Insurance Mediation Directive. He reminded that these thresholds need to be adapted every five years following the entry into force of the Directive and since there is no formal procedure by the Commission to undertake this exercise, this responsibility lies with the Member States. The last deadline for adaptation was 15 January 2013 (IMD1 entered into force on 15.1.2003). To ensure a harmonised approach across the Member States, the Commission had provided guidance in a note addressed to the Expert Group on 5 June 2013 (see document markt.h.5(2013) 2076153).

A representative of a Member State stated that its legislation would have to be changed by Parliament in order to comply with the new thresholds. It was agreed to discuss this bilaterally with the Commission’s services.

Any comments should be sent in writing to the Secretariat.

**6. Review of certain amounts laid down in the Reinsurance Directive**

A Commission representative mentioned that the Commission has conducted the annual review of the guarantee fund for reinsurance undertakings and captive reinsurance undertakings in accordance with the methodology agreed by the European Insurance and Occupational Pensions Committee. The relevant index, the European Index of Consumer Prices, rose by 5.45% during the review period (10 December 2010 – 10 December 2012) and consequently changes are required (5.45% > 5.00%).

The required changes are outlined and explained in document markt.h.5 (2013)1916699, together with the new amounts and the procedure regarding the communication thereof and the publication in the Official Journal. Any comments should be sent in writing to the Secretariat.

A representative from a Member State enquired about the annual examination of certain amounts laid down in the EU insurance Directives. A representative from the Commission stated that the relevant review period ended on 20 March 2013 and the data is therefore not yet available but should be shortly.
7. Insurance International Issues

i. Equivalence issues

A Commission representative updated on the on-going work on transitional third country equivalence being carried out by EIOPA, which involves a professional secrecy equivalence assessment and a gap analysis for each of the eight third countries under consideration. EIOPA has already submitted some reports, which are not public, and the remaining reports are due by November 2013. The Commission intends to make further contacts with third countries in the autumn of 2013 once the criteria for transitional equivalence in Omnibus II have been finalised.

ii. EU-US Dialogue

A Commission representative outlined the work of the EU-US Insurance Dialogue project, which was set up at the beginning of 2012 and which published a Factual Report (outlining the similarities and differences between the EU & US framework in 7 key areas) and a Way Forward Document (outlining 7 common objectives in the same areas to be pursued over the next five years) in December 2012. The short term focus will be on the issues of professional secrecy and reinsurance and collateral requirements. The Chairman stressed the positive dialogue with the US and the appetite for increased convergence.

A representative from one Member State asked for further information on the discussions on reinsurance and collateral requirements and questioned why some Member States and not others were being considered for "qualified jurisdiction" status by the US authorities. The Commission representative explained that the importance of the US treating the EU as a single jurisdiction had been stressed to the US. A useful discussion took place in April 2013, where it was agreed that the National Association of Insurance Commissioners (NAIC) would share with EIOPA its proposed approach to qualified jurisdictions for comments.

iii. IAIS work

The Chairman reinforced the importance that the EU speaks with one voice in international meetings and that a common European position was essential to reinforce the single market in Europe. A Commission representative updated on the work of the IAIS Financial Stability Committee (FSC) and the recent announcement by the FSB on the forthcoming designation of nine Globally Systemically Important Insurers (G-SIIs). It was noted that some policy measures for G-SIIs would begin earlier than others, work on effective resolution and enhanced supervision would be introduced first, with high loss absorbency requirements being introduced in 2019. In order to ensure that higher loss absorbency requirements do not create an unlevel playing field, the IAIS has been
asked by the FSB to develop a straightforward backstop capital requirement by autumn 2014.

The development of a Common Framework for the Supervision of Internationally Active Groups (ComFrame) is running parallel to the work on G-SIIs. The ComFrame standards will be published for consultation in the autumn and work on field testing ComFrame has recently been launched. One Member State asked for clarity on the capital backstop, while another emphasised the importance that the work on the backstop is tied in with the work on ComFrame.

8. Consultation on the Green Paper on the prevention and insurance of disasters

A Commission representative stated that the Green Paper was adopted by the Commission on 16 April 2013 together with the Communication on the Adaptation Strategy for climate change. It covers not only natural disasters but also manmade disasters. A public consultation was launched and is still ongoing; it will end on July 15 2013. Replies have already been received from some Member States, consumer organisations and individuals.

The Chairman stressed the importance of this issue and the need to have a significant number of replies to the public consultation.

9. AOB

Solvency II – Delegated Acts

A representative from a Member State stated that the last version of the Solvency II Delegated Acts seen by Member States dated from October 2011. Member states had commented on them. It enquired about the next steps and the role Member States would play.

The Chairman replied that the first task to be done is adopting the Omnibus II Directive. The Delegated Acts will follow thereafter. Member States as well as the European Parliament will be consulted on the draft Commission Delegated Act in order to ensure its smooth adoption by the co-legislators.

Next meeting

The Chairman announced that the next meeting of the Expert Group (Insurance Formation) will take place on November 7 2013.

As no further points were raised, the Chairman closed the meeting.