

Reinsurance

2004/0097(COD) - 21/04/2004 - Legislative proposal

PURPOSE : to lay down the legal framework for prudential supervision of reinsurance activities in the Community. **PROPOSED ACT :** Directive of the European Parliament and of the Council. **CONTENT :** This paper discusses the key features of reinsurance and highlights the difference between the latter and primary insurance. It also discusses the international nature of the reinsurance business and points out that there are currently no harmonised reinsurance supervision rules in the EU. The lack of an EU regulatory framework for reinsurance has resulted in significant differences in the level of supervision of reinsurance undertakings in the EU. The different national rules have created uncertainty for direct insurance companies (and their policyholders), barriers to trade within the internal market, administrative burden and costs as well as weakening the EU position in international trade negotiations: - the selection of reinsurers is of decisive importance for an insurance company, and could also affect the company's ability to pay claims towards policyholders; - certain EU countries use systems where assets of the reinsurer must be pledged (collateralised) in order to cover outstanding claims provisions. This makes optimal investment management more difficult and thus results in higher operational costs for reinsurance undertakings. This could in fact increase the price the reinsurer charges for taking over risks from direct insurance companies. Reinsurance companies may also decide not to be active in markets where the posting of collaterals is required, and consequently the availability of reinsurance protection will be more restricted. - the lack of mutual recognition between EU supervisory authorities in reinsurance in certain cases means that reinsurance undertakings are subject to different supervisory rules in several Member States. For reinsurance companies this could lead to significant double work and increased administrative burdens. Examples of burdensome administrative measures are the multiple fit and proper checks of the group's highest management, double requirement for auditors' confirmation of balances as well as the obligation for branches to issue financial statements according to local GAAP (generally accepted accounting principles) for the whole group. - it is argued that the lack of a harmonised EU system makes international mutual recognition agreements more difficult. The absence of such agreements means that European reinsurers are confronted with important barriers to entry into foreign markets, such as the requirement of posting collateral for the value of their commitments in the foreign market where the reinsurer intends to conduct business. If no actions are taken at EU level, there is a risk that the internal market for reinsurance services would continue to work in a sub optimal way, which would harm the EU reinsurance industry. Negotiations with third markets on mutual recognition agreements could be significantly more difficult. The Commission's proposal has the following features: - a supervisory approach based on harmonisation and mutual recognition; - fast-track approach for a directive based primarily on current direct supervision rules; - mandatory licensing system; - solvency margin requirements in line with those of direct insurance, however with the possibility to increase this margin up to 50 % through comitology for non-life reinsurance when this is objectively justified. The proposed Directive requires reinsurance undertakings - like direct insurance companies - to be licensed in order to conduct reinsurance business. The proposal lays down the minimum conditions necessary to obtain the official authorisation. This system will increase the responsibility of the Home Member State's supervisory authorities, as they become the sole competent authority for the prudential supervision of the reinsurance undertaking within the Community. Enhanced cooperation between Member States' competent authorities will also be required. In order to ensure a level playing field between reinsurance undertakings and insurance undertakings carrying on reinsurance activities, the proposal also provides for the subsequent adaptations to the non-life insurance Directive 73/239/EEC and life assurance Directive 2002/83/EC. Accordingly, insurance undertakings that conduct reinsurance by way of acceptances activities will be subject to the provisions of the reinsurance directive in respect of the required solvency margin, where the volume of their reinsurance activities represents a significant part of their entire business. These provisions will only be applicable when the Commission has adopted the decision adjusting the required solvency margin for non-life reinsurance activities. In order to take account of a very special situation that might arise in a Member State where it is not possible to obtain reinsurance cover in the commercial market, the proposal does not apply to the

provision of reinsurance cover conducted by a Member State, when it acts as a reinsurer of last resort for reasons of public interest. However this provision does not exempt the Member State from complying with Community provisions concerning competition rules and state aids. An example is the situation that arose in the air insurance sector after the attacks of 11th September 2001, where the reinsurance market failed to provide reinsurance cover for some risks. Member States were prompted to provide such a reinsurance cover. The schemes set up were examined under EU law and in particular state aid rules before being authorised.