

Reinsurance

2004/0097(COD) - 21/04/2004 - Document attached to the procedure

COMMISSION'S IMPACT ASSESSMENT

1- PROBLEM IDENTIFICATION

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's position in international trade negotiations. This legislation will affect reinsurance, insurance undertakings and insurance supervisors directly, and policy-holders indirectly.

For more information regarding the context of this problem, please refer to the complementary summary of the Communication (COM(2004)0443).

2- OBJECTIVES

Three guiding objectives for reinsurance supervision work have been identified:

- The system should establish a sound and prudent regime in the interest of policyholders. Strong and well-supervised reinsurers contribute to a stronger internal market and international financial stability;
- 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 conduct reinsurance business throughout the EU under rules regarding freedom of establishment and freedom to provide services. No additional supervision of - or checks on - the reinsurance undertaking would be performed by supervisors in host Member States. This approach has shown its suitability during many years in the direct insurance field;
- The introduction of a harmonised system for reinsurance supervision should lead to the abolition of systems with the pledging of assets to cover outstanding claims provisions.

3- POLICY OPTIONS AND IMPACTS

Five main issues have been identified.

3.1- Issue 1: Overall approach.

The objectives outlined in point 2 could be addressed in three different ways: maintaining the status quo, introducing a market mechanism solution/voluntary disclosure of reinsurance-related information, or alternatively a recommendation concerning indirect supervision practice; and, lastly, supervisory solutions.

Most interested parties believe that there are problems in the internal market for reinsurance that must be addressed. **Thus, a status quo solution does not seem applicable.**

Most believe there is a need for supervisory action in the field: as in the direct insurance field, whose experience is relevant and instructive, the Commission believes that reinsurance legislation at EU level is necessary given the significant difference in approaches between Member States. Insurance supervision is a public concern and requires public regulation. A voluntary, disclosure-based approach would not provide sufficient trust in the supervisory system.

The supervisory alternative offers the most positive market and economic impacts (reduced administrative burden, single European licence, facilitated market access, etc.), although there will be compliance costs for reinsurance companies, and, in some cases, capital increases may be needed. Social impacts (i.e. primarily the policyholders) would be best served by this alternative. **There is unlikely to be any material impact on the employment situation in the sector and there is no evidence that premium levels would rise as a result of the introduction of supervision.**

3.2- Issue 2: *Fast-track solution or long-term, comprehensive project.*

While both alternatives could fulfil the objectives outlined in point 2, most who were consulted felt there is a clear need for swift action and thus a fast-track solution is preferred.

Under the fast-track approach, the perceived benefits - as well as certain implementation costs - will come earlier than the longer term Solvency II project. **On balance, it is considered that the swift introduction of a reinsurance supervisory scheme will give advantages to EU reinsurers.** Insurance undertakings and policyholders are likely to benefit from the rapid introduction of reinsurance supervision.

3.3- Issue 3: *A voluntary passport or a mandatory licensing system.*

Member States have expressed their support for a mandatory licensing system at several occasions. The insurance industry has reiterated their preference for a voluntary passport solution. The Commission believes that a mandatory licensing system would be more likely to fulfil the set objectives of the EU reinsurance supervision project. Such a system would cover the whole market and thereby better serve financial stability and internal market concerns (obj. 1). A mandatory licensing system would furthermore lead to increased coordination between Member States' treatment of all reinsurers (obj. 2). Concerning the objective to abolish collateralisation requirements (obj. 3), the Commission considers that the mandatory licensing solution is more efficient as it has the support of most supervisors in the EU and internationally.

After broad consultation, **a mandatory licensing system was considered to be more likely to fulfil the set objectives of the EU reinsurance supervision project.** Such a system would cover the whole market and thereby better serve financial stability and internal market concerns. It would, furthermore, lead to more coordination between Member States' treatments of all reinsurers (obj. 2). With respect to the abolition of collateralisation requirements (obj. 3), it would be more efficient as it has the support of most supervisors in the EU and internationally.

3.4- Issue 4: Quantitative solvency requirements for non-life reinsurance.

These rules relate to issues like the solvency margin requirement, the level of the minimum guarantee fund, reinsurance reduction factor and investment rules. The study looks at two possible approaches to designs and levels for solvency requirements: 1) alternatives where the solvency requirements for reinsurance are close to those of direct non-life insurance, possibly combined with comitology powers to increase the requirements in particularly risky lines of insurance, and 2) alternatives where the solvency requirements for reinsurance are higher than those for direct non-life insurance, for example 50% or 100% higher. Also looked at was a hybrid of the two alternatives (1b) that builds on 1) but includes elements of comitology for future amendments to the reinsurance regime.

Although several of the proposed solutions could fulfil the objectives set, **alternative 1b gives supervisors an important function in assessing the need for further capital for certain lines and is therefore better adapted to reinsurance business than a general increase of the solvency requirement with a certain percentage.**

3.5- Issue 5: Quantitative solvency requirements for life reinsurance.

For life reinsurance, certain other considerations than in non-life have to be made. The life reinsurance business is sometimes very similar to direct life business, but often it has another character as normally only risk-bearing elements (i.e. not the savings part) are reinsured. Two distinct solutions have been discussed for life reinsurance: 1) in principle use direct life rules for life reinsurance, and 2) approximate through use of direct non-life rules also for life reinsurance. Both alternatives could include certain adjustments such as class enhancement.

Both solutions could fulfil the objectives but quantitative requirements are only one part of the supervisory system and must also be seen in the light of other supervisory measures. Among insurance companies and Member States divergent views prevail. **Thus, the Commission has decided to propose that life reinsurance should be subject to direct life rules and non-life reinsurance to direct non-life rules.** This would lead to higher requirements in life reinsurance than those currently used in Ireland and the UK.

CONCLUSION: The Commission has therefore decided to present a proposal based on harmonization and mutual recognition. It has opted for a fast-track approach based primarily on current direct supervision rules with a mandatory licencing system. Collateralisation requirements would be abolished. Solvency requirements would be in line with those of direct insurance, however with the possibility of class enhancement up to 50% through comitology for non-life reinsurance.

4- FOLLOW UP

The proposal is expected to follow normal implementation procedures (i.e. transposition in Member States within 18-24 months). As in other insurance fields, implementation may be facilitated through cooperation between Member States' ministries and supervisory authorities. The Insurance Committee will follow how the directive is implemented and used. The ongoing long-term project, Solvency II, will also at a later stage deal with reinsurance-related issues, and to that end work in this project would need to take the working of this reinsurance directive into account. As the Solvency II system will come into place in the EU within a number of years, no formal evaluation clause has been included in the proposed fast-track reinsurance directive.

