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SAFE Finance Blog

Towards an Integrated Market in Insurance

11/15/2017

Jens Gal and Helmut Gründl: Time for an integrated European insurance supervision has not yet come. However, the course has already been set



As the financial crisis set in motion the creation of the European System of Financial Supervision (ESFS), the imminent Brexit now serves as an impulse to rather extensively reorganize it. Pursuant to the preferences of the Commission – as revealed in its draft for a regulation amending the regulations founding the European Supervisory Authorities (ESA) – the supervision (and regulation) of the financial sectors should be further centralized and integrated and additional powers should be given to the ESAs.

To a large degree these alterations are intended to adjust the competences of the European Securities and Markets Authority (ESMA) to better meet its new objectives under the Capital Markets Union (CMU). In view that an equivalent to the CMU or the Banking Union – in the sense of a European Insurance Union –

is not yet on the horizon for the insurance sector (or the occupational pensions sector), one could *prima vista* take the view that insurance supervision and regulation is once again taken captive by the necessity of regulatory reforms stemming from other financial sectors. However, even if that is partially the case, the outcome of the intended reforms might still be advantageous for the insurance sector and an important step in the right direction. For this reason, it is important to take a closer look and examine the most prominent envisioned changes to the structure, tasks and powers of the European Insurance and Occupational Pension Authority (EIOPA):

- **Replace the Management Board by an Executive Board composed exclusively of EU-Employees:** This structural change will *in toto* result in a significant disempowerment of the national supervisory authorities (NSAs) and cause a massive Europeanization of insurance supervision. This means that EIOPA would be granted several areas of operation within which it could take insurance supervisory decisions unchecked by the NSAs, but with immediate effect for them. Whether these are happy news, is a question of perspective.
- **Increased Competences in the approval process for internal models:** This empowerment seems very appropriate since a divergence in supervisory practices concerning the allowance of internal models, especially within a principle based system, increases the risk of supervisory arbitrage. By putting EIOPA in a position of being an information juncture it is not only able to better assess deficiencies and best practices. It should also be explicitly assigned to use such information, though this power already existed implicitly in the past, to issue guidelines on the assessment of internal models.
- **Reformed Funding System:** The Commission's draft is intent on making all European insurers directly liable for funding EIOPA, replacing funding through a proportional contribution of the NSAs and a balancing contribution out of the EU budget (the EU will, however, under the new scheme still make a balancing contribution) . As it can be expected that the NSAs will collect the contributions for the account of EIOPA under the new proposal, it is difficult to see the true advantage of this procedure compared to the current system. Moreover, it seems very likely that the proposed amendment would mean a cost increase for supervised entities.
- **Possibility of imposing fines on insurers:** Whilst the EIOPA Regulation already creates an obligation for NSAs, other national authorities and insurers to appropriately respond to an appropriate request of information, it does not provide for any legal consequences where such obligation is breached. Though this has not been a problem thus far, the Commission sees fit to provide legal consequences. EIOPA shall be given the power to impose fines on insurers – *nota bene*, not on NSAs – if they neglect their duty. Currently, EIOPA may only request the provision of information directly from insurers as an *ultima ratio*-measure, meaning when the necessary information cannot be provided by the NSA or other state authorities which will hardly ever be the case. Insofar the imposition of fines in the insurance sector – other than in the sectors supervised by ESMA, where a direct supervision and thus information duty exists – will remain, for the time being, hypothetical.
- **Power of strategic planning:** Through so-called strategic supervisory plans to NSAs, EIOPA shall be enabled to identify for the NSAs with a three-year-horizon (in conjunction with the work programs of EIOPA) the specific priorities for supervisory activities. This amendment appears rather benign at first sight but might have a very pronounced impact, by potentially creating the power to (almost) directly supervise certain (big) insurance undertakings.

Other than the changes to the governance structure, i.e. the creation of the Executive Board *in lieu* of the Management Board, and the funding scheme, the proposed amendments of the EIOPA Regulation seem *in praxi* rather minor and often only of declaratory nature. In many instances, however, the alterations

seem to be intended to prepare for recalibrations of the ESFS. One might understand the proposed amendments, thus, as an effort to softly steer the EIOPA Regulation towards a future implementation of an Insurance Union with a single supervisory authority, i.e. EIOPA. Viewing reactions from many stakeholders, it appears that such a fruit is not yet ripe for plucking.

It seems contradictory that most Europeans regard the U.S.-system of state-based supervision and regulation of the insurance sector as anachronistic, yet cling onto a system of national supervision. At least concerning large undertakings and pan-European insurance groups one should entertain the idea of a centralized supervision. This would support the creation of a truly internal market in insurance and, if only by reducing supervisory expenditures, further increase the competitiveness of European insurers on a global level. For those who for one reason or another are opposed to centralized supervision, the proposed amendments should come as a warning. The EU is out to centralize, it is out to integrate and it is not taking prisoners. With Great Britain, one of the biggest opponents to centralized financial supervision, out of the European Union, the creation of a fully integrated financial market seems more feasible. Since the British financial market now enters into competition with the European Union market, centralized financial supervision and a resulting robust fully integrated financial market might be just a logical step.

More on this Topic: Jens Gal and Helmut Gründl: "The Recalibration of the European System of Financial Supervision in Regard of the Insurance Sector: From Dreary to Dreamy or Vice Versa?", SAFE Policy Letter, No. 60. (<http://safe-frankfurt.de/policy-center/policy-publications/policy-publications/detailsview/publicationname/the-recalibration-of-the-european-system-of-financial-supervision-in-regard-of-the-insurance-sector.html>)

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Leibniz Institute for Financial Research SAFE

Theodor-W.-Adorno-Platz 3
60323 Frankfurt am Main

Phone: +49 69 798 30080
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