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## **CEIOPS comments to the Lamfalussy Review**

### **I Introduction**

CEIOPS welcomes the opportunity to submit comments to the Lamfalussy Review. CEIOPS has followed the Review process with close interest. It has been pleased to contribute when invited. The present comments are made in the context of CEIOPS' previously expressed views.

In this contribution, CEIOPS first summarises its **progress to date and efforts under way** towards enhancing EU supervisory convergence. Secondly, CEIOPS offers some **successes and challenges of the Lamfalussy model**. Thirdly, CEIOPS identifies **three main building blocks** for the Lamfalussy debate.

Underpinning these are CEIOPS' mission and values set out by its founding text and the European Commission Decision establishing CEIOPS. The comments are also based on consistency between CEIOPS' roles and tasks, and the high level political vision and goals of the European economy. CEIOPS shares these objectives with the other Level 3 Committees.

### **II Progress to date and efforts under way**

CEIOPS' activities towards enhancing supervisory convergence are regularly published in detail. For a Level 3 Committee, they may be grouped into three headings.

First, **Level 3 technical Advice and resulting Level 3 Standards** are to be formed and issued. The Level 3 Committee submits its technical Advice, either as called for or on its own initiative. The resulting provisions, which take that Advice into account, need common EU implementation and observance. The Level 3 Committee therefore develops common Standards, to serve as best practices by EU supervisory authorities.

Secondly, in order to provide the necessary background approaches for that purpose, a new **supervisory cooperation and culture** have to be developed. These serve towards ensuring the operation of the legislation and standards in a similar manner across the EU. In CEIOPS' view that should not be interpreted as

seeking to eliminate diversity. Diverse markets and consequent supervisory approaches are realities and not flawed as such. CEIOPS is working to develop common EU cultures, taking legitimate diversities into account, in order to foster a new shared EU tradition and supervisory approaches under it.

Thirdly, Level 3 Committee follow-up **monitoring actual implementation and best practices** is necessary to strengthen their observance.

CEIOPS is in a different position to the other Level 3 Committees. Their situations differ between themselves. This stems from the different stages in the legislative frameworks that each have to address. CEIOPS' current progress under the three headings above, is set by its own unique position. In this perspective, CEIOPS' activities have been largely dominated by the development of its Level 3 Advice and the establishment of supervisory cooperation and culture. Its Level 3 activities on standard-setting and monitoring are expected to gain increasingly more importance in the future.

#### Level 3 Advice

Currently CEIOPS is still dominated by **the Solvency II project** for insurance. CEIOPS has provided considerable input to the Level 1 Framework Directive proposal. CEIOPS welcomes the tasks identified for it in the draft Directive. It has already offered views on the subject-matter for Levels 2 and 3 measures. These tasks and views will form CEIOPS' major work, once requirements for its Level 1 Advice are satisfied. CEIOPS is committed to the principle that the Solvency II project remains a precondition, and best opportunity, for the enhancement of supervisory convergence and cooperation in the insurance sector.

CEIOPS is presently fulfilling the **Solvency II Work Plan as set out by the Commission**. In this regard, CEIOPS' work targets and deadlines for Solvency II are established in relation to the Commission's Roadmap for the project. By the end of 2007 a future Work Plan for this project is expected from the Commission. The total period anticipated to be covered will be 2 years. In addition to Solvency II work, CEIOPS' **own Work Programme** is framed under CEIOPS' Charter. It is also influenced by the Commission. Amongst other commitments to be set for CEIOPS, a new Work Plan for **Pensions** is expected to be discussed with the Commission, leading to a Programme in 2008.

In its Advice to the European Commission on Solvency II, CEIOPS has paid particular attention to the objectives of consistent implementation of the future regime and furthering convergence in supervisory practices. An enormous number of man-days has been devoted to the project, and by all participants. On a practical level, the intense and close working between supervisory authorities in the context of preparing CEIOPS' Advice has in itself facilitated unprecedented levels of exchange of ideas between Members, as well as increasing levels of understanding of each other's regulatory approaches, frameworks and concerns. Trust and common purpose is being increasingly fostered.

The very issues that CEIOPS is advising on will form the basis for convergence in the prudential supervision of insurance undertakings. For example, in addition to helping put together an appropriately harmonized capital requirements regime, CEIOPS' work also focuses on establishing common approaches in the requirements and assessment of internal control and risk management; creating

an appropriately harmonized framework for the supervisory review process, both in terms of fundamental principles and tools; harmonizing the measurement of technical provisions, and in particular their margin of prudence, and, as a consequence, the approach in their supervisory assessment. CEIOPS is also aiming to introduce qualitative and quantitative rules on investments at EU level which avoid the use of unjustified differences in the supervisory treatment of similar operations; to create a level playing field across Europe with regard to the use and the validation of internal models; and to introduce a harmonized framework for solvency control levels and consequent scales of supervisory interventions.

To summarize, the work leading to the adoption of the new prudential regime is itself already fostering a joint understanding of the objectives, concepts and tools that will form the bedrock of supervision under the new regime, thus paving the way for the successful deployment of eventual Level 3 measures. It should be underlined that even though the Solvency II Calls for Advice issued by the European Commission were mainly aimed at preparing the Framework Directive, CEIOPS has also been discussing the scope and purpose that should be given to supervisory measures. Work is still in hand to find the right balance between Levels 2 and 3. The preparation of CEIOPS' Advice is accompanied by a healthy discussion on this particular topic.

The legislative and supervisory position with **Occupational Pension funds** is also at a different stage from other EU financial services sectors. There is a new Directive. The IORP Directive has been framed to legislate in the light of a very varied market, which displays strong differing regional characteristics and cultures. The Directive's level of harmonization is relatively limited. Considerable effort has been needed from CEIOPS to evolve initial agreed new supervisory approaches. This work is naturally continuing. CEIOPS is rapidly deepening its surveys and proposals to progress this important activity.

#### *Supervisory cooperation and culture*

CEIOPS has a number of achievements and initiatives towards fostering cooperation and a common culture between its Members. It considers this activity crucial to its success as a Level 3 Committee. Without it, CEIOPS believes there can be little realistic expectation for sound day to day implementation of best common supervisory practices across the EU. With it, considerable changes are already apparent. CEIOPS is aware that affecting all such daily practices, to the visible perception of stakeholders including the industry, is a longer term objective. CEIOPS can meanwhile point to its current achievements and ongoing efforts in this light.

Principally, CEIOPS has developed new **supervisory networks** in the framework of its supervisory cooperation Protocol, the Helsinki Protocol. One example is for the supervision of insurance groups. In addition to work on groups under the Solvency II project, CEIOPS Coordination Committees have been established for each insurance group with cross-border activity in different EEA Member States. There are 100 such Committees already formed and 10 more nearly completed. Their number and constitution is dynamic. CEIOPS has a current list which it will maintain. They now cover all relevant EU insurance groups. The initiative started in 2001. It predates a number of other initiatives in this direction. CEIOPS Guidelines for Coordination Committees were issued in 2005. This has enabled the network to have been almost fully implemented by the supervisory

authorities concerned. It has been achieved ahead of Solvency II and therefore within the context of the present regulatory regime. CEIOPS' supervisory networks will continue to be developed. Once the framework has become bedded in, shared practical experience will be applied to refine converged approaches in greater detail and to oversee their adoption for more specific uniform supervisory practices towards their groups.

Also in the present legal structure, CEIOPS is completing the appointment of lead supervisors for each cross-border insurance group. Their tasks have been defined in a published CEIOPS Statement of their roles. Obvious benefits follow, such as arrangements for joint off-site and on-site supervisory inspections. CEIOPS is now seeking to evolve an agreed Risk Assessment System for insurance groups. It also aims to examine supervisory requirements and practices in reporting intra-group transactions, in order to develop an agreed framework for reporting as soon as possible. Finally for groups, CEIOPS is to define a common list of items of information that are essential to be exchanged within a CEIOPS Coordination Committee.

An ongoing area in which CEIOPS actively participates is **EU crisis management** initiatives. Recent events in financial markets have raised their profile. CEIOPS is pleased to join leading crisis management exercises to help evolve a coordinated supervisory approach, and to analyze and report to EU political bodies on the effects of crises on the insurance and occupational pensions sectors.

In addition to the Helsinki Protocol mentioned above, several other **Protocols** direct CEIOPS' framework for the operation of cross-border supervisory convergence. They generally provide a common approach in their sectors for cooperation and exchange of information between supervisory authorities. The new Budapest Protocol achieves this for **occupational pension funds**. The new Luxemburg Protocol serves a similar purpose for **insurance mediation**. The revised Siena Protocol covers **insurance**.

The Protocols are particularly important to CEIOPS for supervisory convergence. Like the occupational pension funds sector, insurance mediation also has a new Directive. It similarly provides limited harmonisation. Its markets are again significantly diverse. Agreed supervisory working relationships help to fill gaps in Member authorities' application of the legislation. With insurance for example, the original Siena Protocol is ten years old. It has been considerably updated by CEIOPS. It now includes current arrangements for the licensing of insurance undertakings, the setting up of branches, the provision of cross-border services, ongoing supervision, on-site inspections, supervisory measures, and supervisory avenues for consumer complaints. CEIOPS' Protocols are preceded by in-depth analyses, surveys and reports on current interpretations of Directives and supervisory practices under them. These activities directly foster supervisory convergence.

Convergence projects have been framed by CEIOPS' recently formed Convergence Committee. Managed by that Committee, an ambitious CEIOPS sectoral programme of **training** for supervisory staff is well under way. More than 10 Seminars, Workshops, Discussion fora and Case Studies have already been conducted in 2007, with the active support of the European Commission. Further events are in formation. They have covered both insurance and

occupational pensions. Some sessions are being opened to industry participants. In 2007, CEIOPS' previous year's work on training and exchange of staff in the insurance and occupational pension sectors was continued, with four training sessions dedicated to supervisors so far. A first CEIOPS Seminar on Occupational Pensions was held in April 2007, with more than 60 persons attending. A seminar on Solvency II for beginners followed at the end of June, a two day session on insurance groups will be held regionally in Poland shortly, and another seminar on Solvency II for advanced supervisors will take place in December.

In addition to sector-specific training, a joint 3 Level 3 Training Platform is being developed together with the other Level 3 Committees. The Level 3 Committees are also jointly exploring tools to overcome existing practical barriers to **staff exchanges**. Obstacles include costs, tax issues, and understaffing. The Committees are completing the formation of networks of Members' Human Resources Departments to develop practical ways round them.

CEIOPS will convene its **Third Annual Conference** in November 2007. That always provides a forum for convergence ideas, proposed initiatives, updates on existing activities, and informal networking between contributors, supervisors and stakeholders. Top Speakers and Panellists this year will cover the Lamfalussy model, the Solvency II project, Occupational Pensions, and will hear concluding views from the Commissioner for Internal Market and Services.

CEIOPS' **website** is a more short-term tool to improve exchange of information and cooperation between Members, and also to benefit training. It now has the additional facility of serving as a discussion board. This allows Members to enter postings to be read and to reply on. Information is exchanged by way of limited surveys on specific issues of concern to local supervisory practice and requiring convergence. There have been 18 questions entered to date. Separately, information can be posted on training courses available in individual supervisory authorities and other bodies. A directory can be created, with contact points in each authority for training and staff exchange. A new webpage for Members titled "Supervisory culture" has been created to foster these initiatives, with two sub-pages for training and staff exchange. CEIOPS will develop this 'forum' tool further.

### Level 3 Standards

CEIOPS has stated that it regards Level 3 activities in particular as the true mission of a Level 3 Committee in the Lamfalussy model. In this view, the development of supervisory best practices as well new practical supervisory tools forms an important challenge. However, for CEIOPS, that stage is still in the future. CEIOPS is confident that when reached, it will work well on Level 3 measures as an increasingly convergent Committee. It very much looks forward to focussing on those activities.

### Level 3 monitoring.

CEIOPS' supervisory intent to pressure convergence in actual implementation and observance of best practices has also been mandated to CEIOPS' Convergence Committee to effect. The main tools being refined for this purpose are **Peer Review** and a **Mediation Mechanism**. These schemes are consistent with the equivalent arrangements of the other Level 3 Committees. They will

apply to both insurance and pension funds supervision. A supplementary approach towards the uniform adoption of Level 3 Standards is that of '**comply or explain**'. The merit is supported in CEIOPS, together with other internal procedures enhancing Members' decision-taking and observance of the results.

### **III Successes and challenges of the Lamfalussy model**

Over the last three years the Lamfalussy process and its defined roles for supervisors have been a great stimulus for the 3 Level 3 Committees. There has been good progress in achieving a higher level of supervisory convergence notwithstanding quite diverging views, traditions and practices among European authorities and Member States, which had been developed over many decades. Considering the increasingly ambitious expectations from stakeholders, CEIOPS and the other Level 3 Committees will publish a 3L3 medium term work programme that will also further strengthen convergence and cooperation across financial sectors. These will take into account the Francq Report's objectives, namely that the current challenges to improve supervisory arrangements in the EU include the further development of supervisory co-operation and convergence, enhancing the cost-efficiency of the EU system, and establishing a coordinated approach to cross-border supervision.

The Lamfalussy process naturally involves four Levels. They comprise the Commission, the Council and the Parliament at Level 1, implementing measures by the Commission, on the advice of the Level 3 Committees, at Level 2; Level 3 Committees comprising competent authorities; and Level 4 which concerns enforcement by the European Commission. While CEIOPS' comments are mainly concerned with the Level 3 Committees, it is important to stress that other aspects of the Lamfalussy process influence the Committees' ability to perform satisfactorily. Some obstacles to reach an even higher level of convergence have proved over the last three years to be technical as well as political.

For instance, the current distance to go towards a **higher level of harmonization** of the EU regulatory framework represents one of the most fundamental challenges to increased supervisory convergence. Within that, there remain a number and range of national discretions introduced at Levels 1 and 2. They represent political compromises and national positions. Divergencies at these Levels need considerable smoothing, and where possible eliminating. National options require international EU-wide substitutes. Supervisory authorities cannot and should not be expected to find solutions where the political process has not led to clear and reliable results. In insurance, CEIOPS is using the Solvency II project to target areas where lack of harmonization prevents supervisory convergence. One example is the valuation of assets and liabilities for insurance undertakings. This will lead in consequence to further convergence in supervisory reporting.

Another obstacle might be the nature of the **separation of legislative powers and technical expertise** between Level 2 and Level 3. The division does not accelerate the actual development process for higher convergence. A thorough evaluation is desirable of any clarification and improvement of the respective roles and priorities of Levels 2 and 3 going forward.

**Enforcement by the Commission** against breaches of the Directives and implementing measures needs to be speedier. The Level 4 reinforced infringement procedure has yet to be put in place. CEIOPS' reports and comments to its political bodies tend to prioritize other considerations. It should be clarified on this occasion that without prompt and penal enforcement actions, there is no disincentive to improper implementation of European rules.

Having said that, CEIOPS Members are convinced that convergence must continue as a comprehensive project for the European Union beyond 2007. Clearly, the promotion of a common supervisory culture remains an important objective of the Lamfalussy Process. Such a project should include the political as well as technical level of the Lamfalussy structure, in order to increase its potential for delivery. At the same time there should be clear distinction between regulatory and supervisory convergence. Therefore, CEIOPS suggests deciding on a number of practical improvements to be forwarded to the ECOFIN meeting in December 2007.

#### **IV Main building blocks, Lamfalussy debate**

If the Lamfalussy debate continues beyond 2007, it could take the form of "**Lamfalussy II**". It should at least cover **three main building blocks**:

##### *1. Objectives of supervision*

##### ***Are Supervisors doing the right things?***

CEIOPS strongly welcomes initiatives at the political level towards helping the Level 3 Committees. It encourages a renewed commitment to the principle of cooperation at EU level and support for the EU convergence process. In respect of this issue, CEIOPS believes that the incorporation of a European political mandate in the mission statements of national regulatory and supervisory authorities and/or the production of an annual Level 3 Committee work plan, would not solve pending problems without a corresponding analysis of the obstacles to the creation of the European mandate. It is important to discuss what the main objectives and mandates for supervisors on the European level should be and what natural tensions might arise between national objectives and a possible European mandate. Consideration should also be given to how those tensions could be settled to achieve clear priorities for European supervisors. In this context CEIOPS recalls that the Solvency II Directive proposal, for instance, includes numerous and varying objectives, from consumer protection to financial stability and competitiveness of the European industry.

It goes without saying that these questions touch on basic responsibilities and the balance between the European Union and its Member States, including a possible delegation of national tasks. They are therefore highly political, rather than technical.

## 2. Institutional basis for supervision

### ***Are European Supervisors doing things right?***

The Level 3 Committees are legal entities under the local law of their permanent locations, and are recognised internationally as having specific tasks and responsibilities. In this context CEIOPS would not support the concept of a traditional European “Agency”. There exists a need to clarify (and as appropriate, alleviate) the implications of certain legal and taxation requirements with which the Level 3 Committees must comply within their home jurisdictions. It is in respect of the resolution of practical issues such as these, that CEIOPS also recognise the need for strong links both with and between national authorities .

Whilst consideration must be given to the funding of the Level 3 Committees, CEIOPS acknowledge that any proposals in this respect, must serve to safeguard the status and operational independence of the Committees. Funding must be sufficient to develop for the first time a reliable medium term work plan, including a medium term financial outlook over the next 3 to 5 years. That should include covering sufficient staffing and technical support, for instance in the field of modern information technologies, data sharing, or the introduction of common reporting formats, and offering training facilities to Members. These latter are beyond the scope of current budgets.

At the same time CEIOPS also sees a need to clarify internal as well as external governance issues that might accelerate convergent practices between Members. Traditionally, CEIOPS has always strived to reach consensus between Members. It will continue to do so. However CEIOPS supports proposals for extending Qualified Majority Voting (QMV) to certain aspects of its future decision making mechanisms, such as already available to it in deciding on technical advice. CEIOPS recognises that any such extension of QMV (and its corresponding implications), cannot be viewed or developed in isolation from other initiatives currently being developed/pursued by the Level 3 Committees.

When CEIOPS is issuing Level 3 Standards and Guidelines, these will to the greatest extent possible, be based on a consensus approach. Where it is obvious that consensus cannot be achieved, and / or is followed by non-compliance, then a clear ‘comply or explain’ approach should apply. All these approaches should be combined with Peer Review, a Mediation Mechanism, and other peer pressure arrangements, which CEIOPS welcomes together with political backing. Their details will be subject to further discussions in CEIOPS.

CEIOPS would also support the idea of inviting continued concrete external feedback from all its stakeholders, including small and large groups as well as consumers, to provide information on day to day supervisory practices in Member States. CEIOPS is conscious that the process of convergence in this area has not been fully completed. CEIOPS looks forward to learning of perceived areas for improvement and addressing them as a Level 3 Committee.

CEIOPS recalls that all major European projects should be accompanied by a sound impact assessment, to illustrate the macroeconomic and microeconomic outcome as well as the impact on industry, supervisors and consumers in an evolving European internal market. This would contribute to the development of



a EU-wide supervisory framework that builds on joint responsibility and joint accountability of national supervisory authorities.

CEIOPS will continue to engage in discussions regarding the future evolution of EU financial services supervision – drawing upon the practical experience of its members, as well as thorough reflection on the real objectives of financial services policy, which must include its complex practical problems.

### 3. Future insurance group supervision

CEIOPS sees the future structure of group supervision for insurance as a separate building block, bearing in mind the extremely high expectations of pan European groups on a lead supervisor concept (the Insurance Groups Directive term, rather than the 'group supervisor' term in Solvency II). In that sense, current proposals under the Solvency II draft Framework Directive will certainly have a major impact on financial sectors and the supervisory landscape in Europe.

Given the political nature of the current Solvency II proposals, CEIOPS welcomes any clear legal basis in the future Directive on:- harmonized European supervisory processes (including supervisory reporting and data sharing); cooperation between supervisors; and responsibilities between home and host states. In respect of the latter, CEIOPS recognise that whilst clarity in relation to supervisory responsibilities is desirable, decisions on detailed allocation of tasks between home and host authorities, do not lend themselves to formulaic treatment, and that detailed decisions on these matters will, inevitably, have to be taken by the supervisors concerned on a case-by-case basis.

## **V Conclusion**

CEIOPS has strong belief in the Lamfalussy model. The model's successes are generally considered by CEIOPS to have been close to the maximum realistically possible so far. The model's full potential has yet to be realised. CEIOPS is keenly aware of certain areas open to improvement. Together with the other Level 3 Committees, it has actively debated these and offered certain conclusions. CEIOPS therefore supports some modifications to the model, in preference to others and to a different model altogether. It would welcome the continuation of a wider debate. CEIOPS is also ready to try alternative approaches to its own procedures, both on its own initiative and where adopted at the political level.

CEIOPS welcomes any comments on this contribution and giving any further input wanted.