SPEECH

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EIOPA, Solvency II and the Loss Adjusting profession

Check Against Delivery
Seul le texte prononcé fait foi
Es gilt das gesprochene Wort

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Ladies and Gentlemen,

It is a privilege and pleasure to be here at the General Assembly of the European Federation of Loss Adjusting Experts.

I would like to start with a thank you to the organizers and to the President of FUEDI Mr. Rui de Almeida for inviting me to participate in this event.

In my presentation today, I will touch on <u>three</u> main issues:

I. What is EIOPA, the European Insurance and Occupational Pensions Authority for whom I have the privilege to serve as chairman;
II. How Solvency II can contribute to the improvement of risk management;
III. The loss adjusting profession, its relevance for the insurance market and the overall society.

What is EIOPA?

EIOPA is the European supervisory authority for the insurance and occupational pensions sectors. We are a young organisation: in January, we completed our first year as a European agency, one of the three European Supervisory Authorities in the financial system.

We are an independent Union body with legal personality, accountable to the European Parliament and the Council.

We clearly see our mission, tasks and responsibilities. We see EIOPA's mission in protecting public interest by contributing to the short, medium and long-term stability and effectiveness of the financial system, for the EU citizens and economy. This mission is pursued by promoting a sound regulatory framework and consistent supervisory practices in order to protect the rights of policyholders, pension scheme members and beneficiaries and contribute to the public confidence in the European Union's insurance and occupational pensions sectors.

This is a very important mission if we realize the relevance of insurance and occupational pensions in the daily life of citizens and on the development of the economy.

The objectives of the new European supervisory authorities, and particularly of EIOPA, are extremely relevant:

- Contribute to a stable and effective financial system;
- Promote sound regulation and supervision;
- Enhance customer protection;
- Ensure the transparent, efficient and orderly functioning of the markets;
- Contribute to international supervisory co-ordination;
- Avoid regulatory arbitrage;
- Ensure equal conditions of competition; and
- Implement appropriate regulation and supervision of risks.

In order to fulfil these objectives, EIOPA has important powers. We develop technical standards that become binding for all insurance undertakings in the EU and issue guidelines and recommendations that national supervisors apply on a "comply or explain" basis. We settle disagreements between national supervisory authorities in cross-border situations and have a coordinating role in crisis situations.

EIOPA monitors the correct application of the EU law in the different Member States, by using, if necessary, its powers of investigation in local markets.

EIOPA and national supervisors are independent from one another, but closely co-operate with one another. EIOPA does not substitute local authorities. It has its own powers and responsibilities, but day-to-day supervision remains a task of the national authorities.

The key decision organ of EIOPA is the Board of Supervisors, where the heads of the national supervisory authorities are represented. However, it is very important to mention that the EIOPA Regulation provides that members of the Board of Supervisors must act with independence and within the sole interest of the European Union.

Most of our decisions are taken by simple majority, some by qualified majority.

EIOPA wants to represent an added value to European consumers and to the European supervisory landscape. In order to fulfil its mandate, EIOPA is building up its own resources and exploiting the knowledge and experience of its Members.

This is a very important element. We want to create a truly European supervisory culture. A culture based on best and robust practices. In order to create this culture, I want to bring together all the national supervisory authorities. All of them have an important contribution to make.

EIOPA's regulatory tasks

EIOPA has been working on Solvency II, advising the EU Commission on the Level 2 implementing measures. We have also been developing draft technical standards and guidelines on around 40 different areas of Solvency II. We are doing this in a transparent way by informally consulting with key stakeholders. We plan to publicly consult as soon as the legal framework will allow us to do that.

In order to facilitate the preparatory work of insurance undertakings for Solvency II, we launched a number of important public consultations in areas such as the Own Risk and Solvency Assessment (ORSA) and Supervisory Reporting and Public Disclosure, including the Solvency II XBRL Taxonomy. We continued to work on the Solvency II specifications for example by issuing a joint report on calibration of non-life risk factors in the standard formula.

EIOPA also provided input into the Commission's revision of the Insurance Mediation Directive (IMD) by carrying out an extensive survey of national laws providing for sanctions (both criminal and administrative) for violations of the provisions of the IMD. The Commission's legislative proposal (IMD2) is expected soon and I am aware that the Commission intends to capture loss adjusters under the scope of IMD2.

Also, on the regulatory side, we delivered our advice to the Commission on the revision of the IORP Directive. Stability and consumer protection were at the core of our advice. We advocate the use of a consistent and realistic measurement of all assets and liabilities and proposed the adoption of a Key Information Document (KID), containing the fundamental elements about performance, costs, charges and risks of defined contribution schemes. I believe that this will help to increase the confidence of consumers in this type of plans.

Oversight

At EIOPA, we are committed and motivated to contribute to the creation of a truly European supervisory culture: a culture that promotes stability, enhances transparency and fosters consumer protection. A culture based on intelligent and effective regulation which does not stifle innovation. That is why in the area of oversight we took as a priority our participation in the colleges of supervisors, contributing to a more consistent practice.

In the course of 2011, colleges of supervisors with at least one physical meeting or teleconference were organized for 69 European insurance groups. Last year, we set an annual action plan for colleges of supervisors and were monitoring its actual implementation. In February 2012, EIOPA issued the report on the functioning of colleges in 2011 and the Action Plan 2012 for colleges of supervisors. In the Action Plan, we defined clear timelines within the colleges for the setting up of an appropriate work plan to deal with the group internal model validation process.

Consumer protection and financial innovation

Consumer protection and financial innovation are priority areas for EIOPA.

We have prepared Guidelines and a Best Practices Report on Complaints-Handling by Insurers. With these Guidelines, we intend to fill an existing regulatory gap at EU level and promote convergence of regulatory practice. They were the subject of a public consultation at the end of last year and are due to be finalised in the second quarter of 2012.

At the end of last year, EIOPA published a Report on Financial Literacy and Education Initiatives by national competent authorities; it was a stock-take of existing structures/processes in Member States. This was in line with a requirement under our empowering legislation to review and co-ordinate such initiatives.

We collected data on consumer trends amongst our Members authorities. This helped us to prepare an Initial Overview, analysing and reporting on those trends. This Overview was published this year in February. The Overview identified three key trends: (i) Consumer protection issues around Payment Protection Insurance (PPI) (ii) development of unit-linked life insurance and (iii) increased use of comparison websites by consumers. This is just the start of our on-going monitoring of consumer trends.

And finally, we focused on disclosure and selling practices of Variable Annuities. This exercise was brought about by the fact that some variable annuities products may achieve outcomes that are not easy for consumers to understand. We consulted on a draft Report at the end of last year and its final version was published this year in April.

Finally, last year, we organized our first EIOPA Consumer Strategy Day where we had the opportunity to discuss important consumer issues with different stakeholders.

Financial stability

EIOPA was also active in the financial stability domain by assessing the resilience of the EU insurance sector to major shocks through the EU-wide stress test exercise and by testing different scenarios on the low yield stress test which shows that the insurance industry would be negatively affected if a scenario were to materialize where yields remain low for a prolonged period of time.

EIOPA also issues, on a bi-annual basis, Financial Stability Reports. One of the conclusions we made in our December publication is that “due to significant natural catastrophes during the examined period, reinsurers suffered above average losses. Furthermore, life insurers may be subject to the risk of having insufficient liquidity, which can be emphasised by banking-related transactions, e.g. through “liquidity swaps” and similar products as well as due to increasing surrenders”.

Furthermore, EIOPA is contributing to macro-prudential discussions and risk analysis in the context of the European Systemic Risk Board, supported by the establishment of the EIOPA Risk Dashboard.

International relations

EIOPA is fully aware of the importance of international relations in a globalized world. In this area, we provided final advice to the European Commission on the assessment of the Solvency II equivalence of the Swiss, Bermudan and Japanese supervisory systems and we have started to contribute to the development of robust international standards by actively participating in the work of the International Association of Insurance Supervisors (IAIS).

During 2011, EIOPA maintained its regulatory and supervisory dialogues with the US National Association of Insurance Commissioners (NAIC), the China Insurance Regulatory Commission, the Japanese Financial Services Authority and the Latin American Association of Insurance Supervisors. EIOPA also enhanced its regular exchanges with the US Federal Insurance Office (FIO) in the context of FIO's responsibilities for insurance law harmonisation at US federal level and in the area of international relations.

EIOPA's values

I would like to say a couple of words about EIOPA's values. In our daily activities and relations with our members and stakeholders, we are governed by the principles of Independence, Responsibility, Integrity, Transparency, Efficiency and Team Spirit.

We aim to be a modern, competent and professional organization that is aware of the expectations of European citizens and wants to ensure that they all are taken on board in our strategies and actions. Our goal is to act independently in an effective and efficient way towards the creation of a common European supervisory culture – and this should not be just empty words.

We consider it our shared responsibility to build a sound framework for the future of insurance activities; a framework that takes into account the specificities of their business models. I would like to assure you that we are ambitious in fulfilling our obligations towards EU citizens and businesses and I am confident that together we will succeed.

Solvency II

As you know, Solvency II is the new regulatory regime for the EU insurance industry and will be implemented on 1 January 2014. Solvency II will bring a better alignment between risk and capital, promoting good risk management practices and fostering transparency. Regulatory regimes are always a result of a balancing act between different objectives. Solvency II will provide an appropriate basis for increased policyholder protection and will contribute to reinforce financial stability, allowing insurance companies to continue to play their natural counter-cyclical role in times of stressed markets.

Gladly, the Solvency II regime is increasingly being perceived as more than a “check the box” regulatory exercise that determines capital requirements. It requires the European insurance industry to critically analyze its risks, and in the process, assess the true costs attached to them.

Today, I would like to talk to you particularly about risk management, which I think is of particular relevance for your profession.

Now, more than ever, insurers need to rely on strong risk management capabilities in order to deal with the different challenges posed by the economic slowdown, the financial market volatility, the stress on sovereign debt, the demographic changes and the evolving pattern of natural catastrophes.

During the last decade, not only risk management itself but also its practical application underwent a major transformation. Improvements in modelling methodology, significant development of new internal control instruments, increasing investors’ and analysts’ pressure as well as a new generation of risk managers with a more holistic view arriving in the company’s also triggered change. Companies which invested, early and continuously, in establishing an effective and well integrated risk management are now taking the benefits from that strategic decision.

It should not come as a surprise that insurance and reinsurance undertakings are at the forefront of applying sound and robust practices of risk management. After all, insurance is in itself a risk management tool and thus the industry possess a wide range of specific know-how and experience in this area.

Nevertheless, from an historical perspective, risk management has not been viewed as a relevant element of the insurance regulatory regime. This has changed with Solvency II.

I believe that appropriate risk management is a cornerstone of any modern risk-based regulatory regime and consequently has its own role in the supervisory process.

Solvency II is mostly known for its risk-based capital requirement calculation. However, it is essential to recognize that one of the most important elements in this regime is the heavy reliance on robust risk management practices.

Under the Solvency II regime, insurance and reinsurance undertakings must have in place an effective risk management system comprising strategies, processes and reporting procedures necessary to identify, measure, monitor, manage and report, on a continuous basis the risks, at an individual and at an aggregated level, to which they are or could be exposed, and their interdependencies.

Importantly, risk management cannot be seen as a point in time procedure. It is a continuous process that should be used in the implementation of the undertaking's overall strategy and should allow an appropriate understanding of the nature and significance of the risks to which it is exposed, including its sensitivity to those risks and its ability to mitigate them.

Taking into consideration some lessons learned from the financial crisis, Solvency II identifies a number of elements which are particularly relevant for a robust implementation of a risk management system:

- First of all, it is paramount to recognize the ultimate responsibility of the management body in ensuring that the implemented risk management system is suitable, effective and proportionate to the nature, scale and complexity of the risks inherent in the business.

- Secondly, the risk management system needs to be documented and communicated to the relevant management and staff, to ensure it is embedded within the business.

- Thirdly, an effective risk management system should cover all material risks the undertaking might be exposed to.

- Finally, and significantly, the risk management system must be integrated into the organizational structure of the undertaking and its decision-making processes.

From a supervisory perspective, the insurance undertaking’s risk-management system must be comprehensive, covering at least areas like underwriting and reserving, asset–liability management, investment, liquidity and concentrations, operational risk and reinsurance and other risk-mitigation techniques.

In each of these areas, supervisors have been transparent in their expectations towards undertakings.

Let me touch particularly on the area of underwriting and reserving.

Underwriting risk is at the centre of the insurance business. The risk of loss or of adverse change in the value of insurance liabilities, due to inadequate pricing and reserving assumptions is clearly related to the quality of the information available and its management.

Consequently, supervisors expect that suitable processes and procedures will be in place to ensure the reliability, sufficiency and adequacy of both the statistical and accounting data to be considered both in the underwriting and reserving processes.

As part of the system of governance, insurance undertakings should be **required to employ personnel with the skills, knowledge and expertise necessary to discharge the responsibilities allocated to them properly**.

Furthermore, insurance undertakings should **ensure that effective systems are in place to prevent conflicts of interest** and that potential sources of conflicts of interest are identified and procedures are established in order to ensure that those involved with the implementation of the undertaking’s strategies and policies understand where conflicts of interest could arise and how such conflicts are to be addressed.

Furthermore, the undertaking should ensure that all policies and procedures established for underwriting are applied by all distribution channels of the undertaking insofar as they are relevant for them and that they **have in place adequate claims management procedures which should cover the overall cycle of claims: receipt, assessment, processing and settlement, complaints and dispute settlement and reinsurance recoverables.**

I believe that the practical implementation of these requirements is of fundamental relevance for the loss adjusting profession.

The Loss Adjusting profession

The profession of loss adjuster is crucial for the insurance business and for the society. The services provided by loss adjusters to insurers and other customers should be based on professionalism, independence and impartial and accurate assessment of claims. These are indeed the key words of your federation.

Your role is particularly sensitive in the relationship between insurers and their clients and claimants. You have a particularly relevant role when dealing with major catastrophes.

I am aware that, during the years of its existence, FUEDI made a lot of efforts in maintaining high standards of professional conduct and competence, high educational standards as well as unified standards of customer services. I believe that these efforts represent a priceless contribution to the fully integrated and reliable insurance market of the European Union and to the overall reinforcement of consumer protection.

I am sure that, in the near future, the loss adjusting profession will be further recognized at the EU level. In my opinion, it is fundamental to assure that all loss adjusters working in the EU follow strict rules of professional conduct including maintaining qualities of integrity and impartiality and are bound by sound loss adjusting practices.

It is also my belief that proper self-regulation is an important tool in this area, but nevertheless, some basic principles should be incorporated in the EU regulatory framework.

I am looking forward to work in close cooperation with your profession and with the insurance industry to ensure increased confidence for policyholders and beneficiaries in the insurance sector.

Thank you.