

Chief Risk Officer Forum



12 January 2007

Henrik Bjerre-Nielsen
Chairman
Committee of European Insurance and Occupational Pension Supervisors

Dear Mr Chairman,

CRO Forum comments on Draft advice on Consultation Paper no. 18 “Supervisory Powers – further advice”

We welcome the opportunity to comment on this draft advice.

The CRO Forum believes it is key to have appropriate harmonisation of supervisory powers, next to an adequate solvency system.

The CRO Forum agrees with the observations as stated in paragraph 1.3 of the advice that supervisory authorities are far from being completely harmonised across Europe, either in structure or in powers. This observation is supported by the outcome of the survey as included in the Annex to the draft advice.

As a result, the CRO Forum welcomes this further advice containing preliminary thoughts about the required level of harmonisation of supervisory powers within the framework of Solvency II.

Overall, we agree with the general gist of the draft advice. However, we have some concerns on parts of the advice which may result in different application in jurisdictions or even in different applications to companies in one jurisdiction.

Our main concerns relate to:

1. The ability to lay down further standards, recommendations and guidelines by supervisory authorities for two reasons:
 - a. The EU new Solvency requirements are to be developed applying a principles based approach. As such developing further standards, recommendations and guidelines may ultimately result in a more rules-based approach which we believe is in contrast with the intention of the EU.
2. Overall, we believe there is a need to further develop harmonisation in supervisory powers to overcome possible differences in interpretations,



acceptance of different methods and/or gaining waivers on specific requirements.

In both cases establishing an Implementation committee and an Interpretation committee within the EU might be of support.

- An implementation committee should be assigned with providing further implementation guidance to Member States and supervisory authorities to ensure an appropriate harmonisation. This committee may cease to exist once Solvency II has been fully implemented.
 - An Interpretation committee should be assigned with providing further guidance as necessary to ensure the principles adopted in the Solvency II directive are interpreted in a harmonised way.
3. Our third main comment relates to the powers of the group supervisor. We strongly believe that the group supervisor should have the ultimate decision to approve (or disapprove) internal models. In that respect we also refer to the recent FSA/HMT discussion document "Supervising insurance groups under Solvency II". We believe this document contains very useful principles for prudential supervision of groups in Solvency II, if properly implemented. As you know, the CEA and the CRO Forum have already expressed support for a number of these proposals in the joint response to CEIOPS CP14 on group issues. The CRO Forum also supported other aspects of these proposals in our paper on diversification benefits from 2005.
4. We recognise the practical necessity of a principle of proportionality. However, we believe that more work is needed to define the principle of proportionality for effective application under the Solvency II framework. At this moment we wish to express two concerns:
- a) While we recognise that there might be cases that the general rules laid down in the directive may not cover all specific cases, we believe the competency of local supervisory authorities to interpret the principle of proportionality should be limited as far as possible, and
 - b) Granting of waivers to specific aspects of the principles should be coordinated such as to ensure an appropriate level of proportionality.

We have included specific responses to the draft advice in the attached Annex "CRO Forum detailed response to draft advice CP 18"

The CRO Forum notes that these comments are consistent with the comments made by the CEA.

We appreciate that further work is needed to achieve the goal of complete harmonisation and the CRO Forum will be happy to assist the Commission and CEIOPS in this work.

Yours sincerely

Thomas C. Wilson
Chairman, CRO Forum
Chief Insurance Risk Officer
ING Group



Annex: Detailed comments to CEIOPS Consultation Paper no. 18 “Supervisory Powers - further advice”

CP 18 paragraph	CRO Forum response
1.3	<p>We agree with the observation that supervisory authorities are far from being completely harmonised across Europe, which observation is supported by the outcomes of the survey included in the Annex.</p> <p>The CRO Forum highly appreciates the survey undertaking to assess current supervisory powers and whether or not Member States believe further harmonisation is needed. We believe the outcome of this survey as included in the Annex provide good insight in further work needed to achieve complete harmonisation.</p> <p>Overall, we note that apart from how a harmonised approach should look like there are significant hurdles to take in respect of different legal traditions. Nevertheless, the CRO Forum believes that in making the new Solvency requirement to work appropriately the EU Member States and Supervisory Authorities would achieve a minimum level of harmonisation between European supervision regimes.</p>
2.10	<p>We agree with the observation that even having the same rules does not necessarily render the same results, since rules are often subject to interpretation. We also appreciate the observation that this is inevitable and therefore hardly possible for legislation to be so precise in the wording as to avoid some differences in interpretations.</p> <p>However, the CRO Forum’s view is that to achieve appropriate harmonisation to minimise possible difference in interpretations. Particularly it is important that any interpretation should be consistently applied across Member States.</p> <p>As a result, the CRO Forum is concerned with the comment that in the absence of interpretations, the supervisory authorities should be able to adopt interpretations for insurance related rules. We believe leaving interpretations to supervisory authorities may result in different applications of approaches between Member States (or even between companies in one Member State), which will make solvency requirements not comparable between Member States and does not support transparency.</p> <p>Particularly for groups different interpretations between Member States may be complex to deal with.</p> <p>As a result, we believe there is a need for coordination between member States and supervisory authorities to provide further interpretations a needed. We believe establishing an Interpretation committee will facilitate such coordination and provide transparency.</p> <p>The implementation committee should in our favour include a combination of representatives from EU, Member States, supervisory authorities and of the industry to provide further guidance to implement harmonised supervisory powers. The inclusion of industry representative is on an advisory basis, so as to provide insight in the issues and items that need further implementation guidance. This committee may cease to exist when Solvency 2 is completely implemented.</p> <p>The Interpretation committee’s task will be to provide guidance to Member States and supervisory authorities on the interpretation of the principles included in the Solvency 2 framework. This committee should include representatives of the EU, Member States and supervisory authorities.</p>

CP 18 paragraph	CRO Forum response
2.11	<p>We completely agree that supervision can be considerably more effective if the competent authorities are empowered to actively influence standards and procedures of the supervised entities instead of being limited to a reactive role. Also, the CRO Forum highly appreciates the comment that Supervisors should tell the industry upfront what is expected from them.</p> <p>However, the CRO Forum has two concerns:</p> <ol style="list-style-type: none"> 5. The EU new Solvency requirements are to be developed applying a principles based approach. As such developing further standards, recommendations and guidelines may ultimately result in a more rules-based approach which we believe is in contrast with the intention of the EU. As a result, there is need to establish a process governed by the EU, to determine whether additional standards are necessary. 6. We believe it is very important that any standards, recommendations a guidelines are consistent across jurisdictions and across companies. Particularly, we fully support the comment in 2.16 that concerning financial supervision material differences could result in considerable discrepancies in the capital requirements of undertakings across Europe and ultimately result in serious competitive distortions. As a result, we do not agree that a supervisor in a Member State should have the power to issue standards, recommendations and guidelines, rather that such power should be organised on pan EU basis. <p>To address both concerns we believe a central EU coordination committee is needed. Such a committee probably is most needed in the implementation phase. This committee should include a combination of representatives from EU, Member States, supervisory authorities and of the industry to provide further guidance to implement harmonised supervisory powers and to establish further standards, recommendations and guidelines. The inclusion of industry representative is on an advisory basis, so as to provide insight in the issues and items that need further implementation guidance. Also the industry needs to be represented to discuss the need for additional standards, recommendations and guidelines. This committee may cease to exist when Solvency II is completely implemented.</p>
2.17	<p>We recognise the practical necessity of a principle of proportionality. However, we believe that more work is needed to define the principle of proportionality for effective application under the Solvency II framework. At this moment we wish to express two concerns:</p> <ol style="list-style-type: none"> 1. While we recognise that there might be cases that the general rules laid down in the directive may not cover all specific cases, we believe the competency of local supervisory authorities to interpret the principle of proportionality should be limited a far as possible. 2. Granting of waivers to specific aspects of the principles should be coordinated such as to ensure an appropriate level of proportionality.
2.20	<p>We agree with the observation that powers with regard to the use of internal models for the calculation of the regulatory solvency requirements are new to all supervisory authorities and that this is an opportunity for full harmonisation from the outset.</p> <p>The CRO Forum in fact believes that full harmonisation on the use of internal models is a must as this would ensure a consistent approach to the assessment on internal models.</p> <p>We agree with 2.25 regarding the important role of the group supervisor and as a result we do not agree with draft advice that “Every</p>

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	supervisory authority should have the power to test and back test the model before approving it, e.g. by changing the parameters and trying some extreme scenarios.”
2.21	<p>The CRO Forum fully agrees that “Supervisory authorities need to ensure that all undertakings are treated equally in the calculation of the SCR under the standard formula. If any leeway is given to authorities to approve that undertakings deviate from rules, the scope of this supervisory power should be clearly defined and the acceptable reasons for permitting deviation from general rules prescribed for all authorities in the implementing measures, so as to avoid unequal calculation of the SCR across jurisdictions. “</p> <p>In that respect we do agree that “All supervisory authorities should have the power to correct an undertaking’s use of incorrect entity-specific parameters within the standard formula for the calculation of the SCR.” However, we believe care should be taken that these corrections do not result in inconsistencies across jurisdictions.</p>
2.22	<p>Regarding the powers to set limits on assets in general we refer to our response to the draft advice on Safety measures (Limits on Assets – CP 19).</p> <p>On a case by case basis we have some concern that providing powers to local supervisors may result in inconsistent application across the EU and across companies. As a result, we believe there is a need for further guidance on when and how local supervisors can set limits (or waive limits) on a case-by-case basis.</p>
2.23	<p>With regards to the calculation of the technical provisions we agree that with the aim to abolishing existing considerable discrepancies in the calculation across Member States.</p> <p>In that regard we refer to our earlier submission (jointly with the CEA) on the approach to value insurance liabilities on an economic sound basis, applying a cost of capital approach¹.</p> <p>We believe the principles for the valuation of insurance liabilities should be included in the Solvency II directive and as such as a matter of principle we believe there should not be an ability to accept different calculation rules.</p>
2.24	<p>We agree fully with the statements as provided in this paragraph. Particularly, we agree with the statement that “While some degree of flexibility is necessary to deal appropriately with SCR breaches on a case-by-case basis, this needs to be finely balanced with guards against supervisory arbitrage where some Member States generally react more leniently when undertakings are in breach of requirements.” For further more detailed comments on the concept of supervisory ladders we refer to our response to Pillar I issues - further advice (CP20).</p>
2.25	<p>We refer to our comment provided on paragraph 2.20.</p> <p>In addition we have a comment on the sentence “Solvency II will call for the group supervisor to coordinate the approval process between the</p>

¹ Solutions to major issues for Solvency II - Joint submission by the CRO Forum and CEA, 23 December 2005, with further details provided in A market cost of capital approach to market value margins – Discussion paper ; CRO Forum, 17 March 2006.

CP 18 paragraph	CRO Forum response
	<p>involved supervisory authorities and provide that he <u>may</u> take the final decision whether the proposed group internal model can be approved if the supervisory authorities cannot agree on a decision within an appropriate timeframe.”</p> <p>The wording of this sentence implies that no decision could be taken resulting in indecisiveness. As a result, we believe that in respect of the approval process, group supervisors should take the final decision rather than <u>may</u> take the final decision.</p>
4.4	<p>We do not agree that member state supervisory authorities on their own should have the power to lay down standards, recommendations and guidelines and to adopt interpretations.</p> <p>For more details on our concerns with this advice we refer to our comments on paragraph 2.10 and 2.11.</p>
4.5	<p>We refer to our comments on paragraph 2.17.</p>
4.6	<p>We agree that obtaining information is a key power for supervisory authorities.</p> <p>While we also do agree that there should not be a limiting list of the information available for the supervisors, we believe that, in requesting additional information a fine balance is needed to balance the costs (for the insurance undertaking to gather this information) and the benefits such additional information has to the supervisory authority. In that respect we appreciate the comment that supervisors should not ask for information that is readily available from another supervisor.</p> <p>However, there might be other requests for information that is complex together or very difficult to obtain. We would welcome some further guidance to supervisors on information requests to appropriately balance the costs and benefits.</p>
4.7	<p>We agree that supervisory authorities should be empowered to complement off-site supervision by on-site supervision and should have free access to any staff and any information relevant for the supervision of the undertaking.</p> <p>However, we have some concern on the statement “with the right to demand that documents and information are prepared or produced in readiness for the supervisor’s visit.” We agree that a visit might be more beneficial if documents and information is prepared and produced in advance, but we believe reasonability requirements and appropriate timing needs to be ensured so as too not put undue burdens to the insurance undertaking.</p> <p>In addition, we note that the practicality of how supervisory visits to the insurer’s outsourced providers would work in practice remains to be addressed.</p>
4.8 and 4.9	<p>The general rules on assets are already suggested in CP 19 (we refer to our comments on these general rules in our response on CP 19.). As stated in our comment to paragraph 2.22, we have some concern that providing powers to local supervisors on a case-by-case basis may result in inconsistent application across the EU and across companies (and in fact inconsistency with the discussions in the draft advice included in CP 19). As a result, we believe there is a need for further guidance on when and how local supervisors can set limits (or waive limits) on a case-by-case basis.</p>

CP 18 paragraph	CRO Forum response
4.11 – 4.13	Group supervision
4.11 4.12 and 2.25	<p>The CRO Forum welcomes the continued consideration of group issues, in particular around the supervision of groups. We agree with the powers for the group supervisors as provided in these paragraphs, however, we strongly believe that the group supervisor should have the ultimate decision to approve (or disapprove) internal models.</p> <p>In that respect we also refer to the recent FSA/HMT discussion document². We believe this document contains very useful principles for prudential supervision of groups in Solvency II. The CRO Forum believes that these proposals are consistent with the Commission's Framework for Consultation on Solvency II.</p> <p>As you know, the CEA and the CRO Forum have already expressed support for many of these proposals in the joint response to CEIOPS CP14 on group issues. The CRO Forum also supported other aspects of these proposals in our paper on diversification benefits from 2005³. The CRO Forum believes that, if adequately implemented, this approach will streamline prudential supervision of groups while enhancing the access of solo supervisors to relevant information about the financial position of the group and their participation in decisions about the supervision of the group through the collegiate approach to supervisory review process.</p>
4.13	<p>While we understand that the group supervisor should have the duty and the power to enforce the delivery of capital support at the solo level, we believe this power needs further definition and should be in the context of the legal relationship between the group and the solo entity.</p> <p>In addition, the requirement to a cash transfer is excessive and is likely to increase capital support charges, which would be incurred by policyholders. Unless the solo company has specific liquidity issues that cannot otherwise be resolved, other ways of meeting the needs of the solo entity should be permissible.</p> <p>In that respect the CRO Forum believes guidelines will need to be developed to ensure equitable treatment between and within jurisdictions, on what may constitute a capital injection.</p>
Annex	<p>The information provided in the Annex is very helpful and provides a lot of insight in the current powers. However, we have some concern given the wide range of powers listed. Is it CEIOPS advice to have all this powers in place? We believe also the powers of supervisory authorities may be better principle based, with any new power subject to a period of consultation, including consultation on the details and use of these powers.</p>

² FSA / HMT Discussion Document, "Supervising insurance groups under Solvency II"

³ A framework for incorporating diversification in the solvency assessment of insurers, CRO Forum, 10 June 2005