

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. 19 “Safety measures (Limits on Assets)”

The CRO Forum appreciates CEIOPS’ further development of principles for the formulation and application of the supervisory tool “Pillar II capital add-on”, and welcomes the opportunity to comment on this draft advice.

We agree that “The presumption is that a more risk-sensitive approach would largely deal with a majority of risks. Where issues are too complex to be dealt with by formulae, then other solutions to cope with them need to be found.” (1.6). We understand from the paper that CEIOPS has taken this presumption as leading in defining additional safety measures such as limit on assets. However, the CRO Forum does not agree with this further conclusions as we would emphasize that any risk that is already dealt with in the SCR should not be accompanied by additional limits on assets. Also, internal models developed by companies may actually include some of the risks discussed in this draft advice.

As stated in prior submissions, the CRO Forum is a strong advocate of an economic risk based approach and as a result, we do not support the suggested use of arbitrary asset limits that are not risk sensitive. In particular, we would like to emphasize that it is important that the new Solvency regime provides appropriate incentives to good risk management and that requiring additional limits may actually hinder companies to do so, or could mean that there could be less emphasis on good investment management and risk management techniques. It is our strong belief that an appropriately designed SCR is a better approach than applying limits which may or may not capture the risks appropriately.

The CRO Forum believes that limits on assets should be consistent with banking regulation to ensure a level playing field. Asset and investment innovation has been tremendous over the last 50 years and acceleration of innovation continues to increase. Applying artificial limits may stifle innovation and creativity or worse



encourage packaging certain risks into structured assets or complex derivatives – these same exposures supervisory rules are intended to limit – thereby reducing transparency. This “packaging” risk will exist as limits will tend to focus on labels rather than characteristics and attributes which are much more difficult to articulate and interpret but labels can easily change. The CRO Forum believes that transparency and open dialogue on asset management and ALM strategies is crucial to the supervisory process and time and energy should be focused on the fit of the asset management strategy in the organization including consideration of the company’s demonstrated experience with all asset classes they are exposed to.

In addition, we expect most companies to have a good risk management in place focussed on an appropriate balance between risk taking and higher returns, and as a result, those companies will have their own exposure limits in place, however, not arbitrary limits rather economic limits based on internal model calculations, similarly like banks have limits to market risks. Therefore, we believe that verification by the regulator of companies having a good risk management in place focussed on an appropriate balance between risk taking and higher returns, and hence providing for an adequate assessment of the risk exposure from investing in assets is a more efficient and less arbitrary method. In fact risk assessment of exposures should not only deal with exposures to assets rather also to exposure to liabilities, such as the risk of concentrations etc. In particular, we would also like to stress that prescriptive limits on assets in Pillar I could introduce an element of systemic risk. Therefore, we believe this needs to be part of the Pillar 2 discussion on appropriate risk management.

We note that we understand that our position is consistent with the position that the CEA has on this matter.

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



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