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Abstract

Lieve blogs for the Risk & Compliance Platform Europe. In her blogs, focused on the EU's insurance legislation, Lieve Lowet informs or questions, always in the interest of promoting the rule of law, legal consistency and clarity of regulations. Like the work of Albert Szukalski, Dialogue, 1974 (open-air museum Middelheim, Antwerp, Belgium), these blogs intend to give food for thought and invite for dialogue. This overview is a selection.

Lieve Lowet
Schuman European Affairs

Guidelines again: The Opinion of Advocate-General Bobek in the case of the Féderation bancaire française (FBF) against the French Prudential Supervision and Resolution Authority (ACPR)

28 April 2021

On 15 April 2021, advocate-general Michal Bobek delivered his Opinion in a request for preliminary ruling from the French Conseil d'Etat in case C-911/19. On the dissecting table are the Guidelines on product oversight and governance arrangements for retail banking products which the European Banking Authority (EBA) issued in 2016. The ACPR in 2017 in a notice decided to comply with them, '*thus making them applicable to all financial institutions under its supervision*'. A month later, the FBF lodged an application seeking the annulment of the ACPR's notice before the French Conseil d'Etat, citing the EBA's lack of competence. The Conseil d'Etat decided to seek a preliminary ruling from the European Court of Justice (ECJ) on several questions, one of which was whether the EBA had exceeded its power.

As stated by Bobek, the present case has several layers and not all legal questions can be treated in this blog. We will focus on these questions: did the EBA go beyond its scope? Did the EBA have the power to adopt the contested guidelines? If yes, can the ECJ declare the guidelines invalid? Can this be done in a preliminary ruling procedure? Bobek writes that the specific example of the EBA guidelines provides a good illustration of the structural issues relating to the review of soft-law measures before the ECJ.

Before answering the question of power, Bobek dives into a preliminary issue: are the contested guidelines genuinely non-binding, i.e. not producing binding legal effects as all parties are arguing? It is established case law, according to Bobek, that any provision adopted by the institutions irrespective of their form, intended to have binding legal effects, are regarded as challengeable acts for the purposes of Article 263 TFEU. The traditional test is to examine the substance of the act and assess its effects based on objective criteria. While it is true that the guidelines are worded in non-mandatory terms ('should' as opposed to 'shall'), that there is no obligation on NCA to comply with them, and that the EBA had no intention to adopt anything that would be binding, one can only conclude that the contested guidelines do not in themselves produce binding legal effects.

BUT…. given that Article 16(3) of the EBA regulation provides that NCAs and addressees must make '*every effort to comply*', it can be presumed that guidelines are not adopted with the intention for them to be disregarded by the addressees, especially given the duty placed upon them. In a way, Bobek argues, the financial institutions are the genuine addressees. It is not even clear whether, if the NCAs formally decided not to comply, that the financial institutions would be exempted from complying and from making '*every effort*'. "*Those guidelines may have a life of their own vis-à-vis financial institutions irrespective of the position adopted by competent authorities*". But the ACPR decided to comply with the EBA guidelines, making the content of the guidelines de facto obligatory through its ACPR notice. It made compliance with those guidelines enforceable in that Member State with that NCA becoming the effective enforcer.

However, as the traditional standard approach of the ECJ is to look exclusively at EU level, the contested guidelines are unlikely to be considered by the ECJ as binding, and consequently be reviewable under Article 263 TFEU. Bobek finds that approach problematic: "*what may perhaps still be construed as soft law when looking only and exclusively at the EBA and the competent national authorities, becomes something very different one level down within the Member States. At that level, 'soft law' is 'no longer so soft' or may even turn into proper 'hard law'. It should be pointed out that EU* *law certainly does not preclude that from happening. Quite to the contrary in fact: the entire system is designed to function in precisely that way."* He regrets that the Court remains focused on the act and its authors, going around in circles while carefully pleading for a hybrid remedy for this hybrid form of governance.

For the core question – has the EBA exceeded its powers given to it by the EBA Regulation, and if yes, what should be the formal result of such a finding – Bobek examines to which extent the guidelines go further than what Regulation No 1093/2010 allows for. Key is the reading of Article 1(2) of the EBA Regulation, stating that the Authority shall "act within the powers conferred by that regulation *and* within the scope of a number of legislative acts laid down therein *and* of any further legally binding Union act which confers tasks thereon", completed by Article 1(3)"… provided that such actions… are necessary to ensure the effective and consistent application of *those* acts" (his emphasis). The acts mentioned in Article 1(2) constitute therefore the Authority's ultimate horizon. But is such a formal test sufficient?

In his Opinion, Bobek dives one stage deeper, arguing that there is a clear mismatch between the subject matter of the three specific legislative acts, mentioned in Article 1(2), provisions of which were used as legal basis for the guidelines. The subjects regulated by the contested guidelines and by the legislative acts referred to in Article 1(2) are different. Product governance is not corporate governance. The EBA could not lawfully adopt guidelines on the governance of banking products.

In addition, one provision of a fourth directive, Article 7(1) of Directive 2014/17, was also used as legal basis for some sub-guidelines. Could this Article constitute a proper legal basis? Bobek argues that although a few provisions of Directive 2014/17 empowers the EBA to adopt certain rules, none of these provisions specifically concern product governance rules, nor do they refer to the adoption of guidelines in the matters concerned. In addition, Directive 2014/17 does not deal with product governance in the same sense as the contested guidelines.

Therefore, the only sensible option, according to Bobek, is that the guidelines must stand or fall as a whole. They do not fall within the scope of the legislative acts referred to in Article 1(2) or the ones conferring specific tasks on the EBA. The "*EBA has (…) exceeded its competences in adopting guidelines the subject matter of which is not covered by those legislative acts*". Bobek's advice on this question is to reply to the Conseil d'Etat that the guidelines are invalid.

But that is an interim conclusion as it uses the methods used for a normal scrutiny to examine the validity of measures with a binding legal effect. Is it appropriate to use the same degree of intensity of review for measures allegedly not generating any binding legal effects? The ACPR and EBA both argued for a lower scrutiny, and added that the guidelines could still be seen as falling within the EBA's mandate because the EBA Regulation is expressly aimed at consumer protection. Bobek opines that he cannot subscribe to these arguments, neither in this specific case nor in general. Article 9(1) of the EBA regulation sets out specific tasks related to consumer protection: justifying the scope of the EBA's guidelines based on vague overall consumer protection aims is not tenable compared to the rather circumscribed role of EBA in that article. He further extensively argues that the judicial review of non-binding legal acts adopted by EU agencies ought to be a normal standard type of review, at least with regard to their competences, so that those agencies do not unlawfully interfere with the competence of other EU bodies or institutions.

The full Opinion can be read here.

Lieve Lowet

Source: Guidelines again: The Opinion of Advocate-General Bobek in the case of the Féderation bancaire française (FBF) against the French Prudential Supervision and Resolution Authority (ACPR) | Risk & Compliance Platform Europe (riskcompliance.biz)

Lieve Lowet

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What's in a name? Who knows the difference between EIOPA's supervisory statements and statements?

19 August 2020

EIOPA has recently issued several statements. For the attentive reader, there is a difference when such a statement is called a supervisory statement or simply a statement. Surprised? So, what's in a name? Let us first focus on Supervisory Statements. EIOPA issued in 2017 its first Supervisory Statement. EIOPA defines on its website today Supervisory Statements as follows: "*Supervisory Statements often aim to present finding on current practices observed and indicate areas for improvement. The statements are directed to National Supervisory Authorities (NSAs) as well as insurance and reinsurance undertakings*."

The legal basis according to EIOPA is Article 29(2) of the EIOPA Regulation. Article 29(2) has been revised in 2019 and reads as follows:

The Authority may, as appropriate, develop new practical instruments and convergence tools to promote common supervisory approaches and practices.

For the purpose of establishing a common supervisory culture, the Authority shall develop and maintain an up-to-date Union supervisory handbook on the supervision of financial institutions in the Union, which duly takes into account the nature, scale and complexity of risks, business practices, business models and size of financial institutions and of markets. The Union supervisory handbook shall set out best practices and shall specify high-quality methodologies and processes.

The Authority shall, where appropriate, conduct open public consultations regarding the opinions referred to in point (a) of paragraph 1, tools and instruments referred to in this paragraph. It shall also, where appropriate, analyse the related potential costs and benefits. Such consultations and analyses shall be proportionate in relation to the scope, nature and impact of the opinions or tools and instruments. The Authority shall, where appropriate, also request advice from the relevant Stakeholder Group referred to in Article 37."

The first subparagraph of Article 29(2) allows indeed that EIOPA develops *"new practical instruments and convergence tools*" in the interest of "*common supervisory approaches and practices*". This is nothing new. This competence existed already in 2017 and was not changed in the ESA review. However, subparagraphs 2 and 3 of this paragraph 2 of Article 29 have been added in 2019, to be applied as of 1 January 2020. These subparagraphs require the Authority to conduct open public consultations regarding the tools and instruments, analyse costs and benefits, and request advice from the relevant Stakeholder Group, all this where appropriate. In addition, these consultations and analyses need to be proportionate relative to the scope, nature and impact of the tools and instruments. These additions reflect the need for more prior consultations and cost-benefit analysis.

Since the start of the COVID-19 crisis, EIOPA issued three supervisory statements. Adding the one of February 2020, four supervisory statements (see list here) have been published in 2020.

Some observations:

None of the supervisory statements published in 2020 refers to its legal base. To include a sentence similar to the one used in recommendations would have been helpful. This could read as follows: "In accordance with Article 29(2) of Regulation (EU) No 1094/20101 (EIOPA Regulation), EIOPA is issuing this Supervisory Statement…".

In two cases, the denomination "supervisory statement" has not been used, but rather the denomination "EIOPA Statement" and "Supervisory expectations". This creates confusion.

In one of the supervisory statements, titled Supervisory expectations on Product Oversight and Governance requirements amidst the COVID-19 situation, there is no EIOPA BoS reference. One might therefore presume that this communication is not a supervisory statement, also because it follows, thus EIOPA, on the *statement* issued on 1 April 2020. How can one know this document to be a Supervisory Statement?

As regards the statements, these are not the same as Supervisory Statements according to EIOPA. These have consequently not even the validity of a tool or instrument according to Article 29(2). Their content is even more light years away from guidelines and recommendations. These should consequently be treated as such.

It remains an enigma why certain statements are Supervisory Statements and other are just 'statements'. I am sorry to confess that I was unable to understand the logic. What is the defining factor?

One could argue that the distinguishing factor is the process. But the facts speak against this argument: in the case of supervisory statements, and despite the applicability of the new EIOPA Regulation since 1 January 2020, including its new Article 29(2), no public consultation has taken place, nor a cost/benefit analysis, nor has the appropriateness or inappropriateness of such a (non-)consultation and (non-)analysis been explained, despite these being explicitly foreseen in Article 29 (2) 3rd subparagraph.

Can it be that during the COVID-19 crisis these tools were the answers for replacing recommendations and opinions? Surely the COVID-19 crisis has turned a lot of organisations upside down and the times are challenging, but should we not be careful while respecting our legal framework?

One final thought: in the end, whether the statement is a Supervisory Statement or just a statement, none of these are legally enforceable.

This blog article is a short version of a longer article into this matter. For more information on the longer article, please contact the author, Lieve Lowet.

Source: https://www.riskcompliance.biz/news/whats-in-a-name-who-knows-the-difference-between-eiopas-supervisory-statements-and-statements/

Covid-19 and Solvency II – No time to lose

01 June 2020

by Lieve Lowet

This is the last part of a series of three articles about my investigation into Covid-19 and Solvency II.

We have already published two interesting blogs, which can be found in the related items section. The first part was about buying time and data and the second part was about the Covid-19 pandemic risk. In the light of the Solvency II review, one question is whether pandemic risk is adequately dealt with in the solvency capital requirements. Are the calibrations and parameters in the life and health underwriting risk submodules for catastrophic risk still in line with the (new) insights and observations of a worldwide pandemic, such as COVID-19? And if not, is an adaptation necessary? Are additional parameters required?

The next question is automatically whether pandemic risk is properly captured in the non-life underwriting risk module, and whether it matters for each line of business.

- In case pandemic risk is currently part of the framework, are there new insights which suggest further fine tuning of the existing underwriting risk framework for certain LOBs?
- Should pandemic risk be included in underwriting risk beyond the current LOBs?
- And if yes, where? Should there be a limit? Should that limit be defined EU wide?

But above all, the impact hitherto stretches beyond the risk categories that were considered relevant for a pandemic situation when Solvency II was developed more than 10 years ago. From what we observe today, a pandemic, such as COVID-19, has the potential to impact more than only underwriting and operational risks. This has come as a surprise. The pandemic has impacted financial markets and its consequences stretch beyond underwriting and operational risks into market risk, credit risk, and liquidity risk. Should the standard formula risk modules be adapted for the new insights obtained from this stressed environment?

- Regarding market risk, EIOPA observed that the market impact of the ongoing COVID19 crisis could lead to a situation where a large share of corporate and government bonds could be downgraded. If bonds currently rated BBB would be downgraded to non-investment grade this would lead to losses of about 1,6% of total EEA (including UK) investments. What would be the impact of pro-cyclical credit downgrades on the solvency position of the sector? In addition, volatility has increased in several equity markets.
- Regarding credit risk, there are heightened and /or perceived risks of downgrades and defaults. There is talk about ballooning credit spreads. What will this do to recoverables? What is the impact of loans and mortgage payment moratoria? Will state guarantees on credits and credit lines have an impact?
- Regarding liquidity risk, excess mortality claims but also premium payment holidays combined with increased lapses and withdrawals especially in the area of life savings and pension insurance due to lack of income may be observed. Combined with potential lower new business volumes in the light of deteriorating financial conditions, and reductions in the liquidity of an insurer's portfolio's asset classes, liquidity risk might be impacted.

The key question in all the above is if and how far policymakers can reasonably extend the capital and risk management requirements of the insurance and reinsurance sector and stretch its capacity? Should pandemic risk coverage more broadly be included in the SII framework? The current storm around business interruption (BI) insurance, especially non-damage BI and event cancellation insurance definitely puts this pressing question on the table. The insurance industry (in some countries) is knocking on the door of governments and public authorities requesting a public private solution for the future in the broader area of catastrophe risk.

Stephen Davies, head of Education at the Institute of Economic Affairs, London, wrote a month ago in a Briefing Paper "*Going Viral: the history and economics of pandemics*": "Historical comparisons tell us a number of things about pandemics, which are also true in this case: they break out after prolonged periods of increasing economic integration; the initial foci are connected cities that are centres of trade and/or governance; the pattern is usually one of a series of waves, with the second one historically the most damaging…. We should be aware that, on historical precedent, the pandemic will last for about 18 months (so to summer 2021); that there will be another pandemic at some point and for structural reasons this is more likely than was the case a number of decades ago." Without waiting for the next pandemic, our reflection on incorporating into Solvency II our new insights should start. Remembering Davies' words, there is no time to lose.

The author, Lieve Lowet is an EU Affairs consultant and lobbyist since 2003, focuses on European dossiers relevant for the insurance and pension sector. From 2003 to 2008, she was Secretary-General for the international mutual insurance association AISAM (now AMICE), which accounted for 15% of the European and 6% of the world insurance market. Prior, she worked for McKinsey as a European banking and insurance expert.

Source: https://www.riskcompliance.biz/news/covid-19-and-solvency-ii-no-time-to-lose/

To pay or not to pay, that is the question

27 April 2020

by Lieve Lowet

We live in exceptional times. Right now it is good to check whether the measures announced at high speed comply with the basic principles of correct decision-making and that they are in accordance with the applicable laws and regulations. I have made an in-depth analysis and would like to share my findings in a series of three articles. The articles will be published on three consecutive days.

On 17 January 2020, in tempore non suspectu, the ECB issued a recommendation on dividend distribution policies to prepare banks for the introduction of IFRS9 and the new CRD / CRR requirements (ECB / 2020/1, OJ C30 29 January 2020). Banks, even those with "fully loaded" ratios, were recommended to distribute their net profits in dividends in a conservative manner. And then the corona crisis started to hit….

The ECB sent first a letter on 3 March 2020 to all significant banks to remind them of the critical need to consider and address the risk of a pandemic in their contingency strategies. There was no mention about dividend policy postponement yet. The first one to react on EU level was the European Banking Authority (EBA). In its 12 March 2020 statement, it urged banks to follow *prudent dividend and other distribution policies,* including variable remuneration, and use capital for ensuring continuous financing to the economy. The EBF's letter of 11 March calling for European measures did not suggest any such action.

A full two weeks later, on 27 March, the ECB withdrew its January recommendation and published a new recommendation targeted again to the significant banks it supervises. National competent authorities were invited to do the same for less significant supervised entities and groups, which for example BaFin and Banca d'Italia did. The ECB recommended to ***postpone** dividend payments* for the 2019 and 2020 financial years until *at least* 1 October 2020 (see OJ 30 March 2020). The recommendation applies both on consolidated and on individual levels.

The term 'dividend' according to the ECB refers to any type of cash pay-out that is subject to the approval of the general assembly, and it adds that this is also valid for mutuals, cooperatives and savings institutions (in line with, but without referring to, Article 27 of the Capital Requirements Regulation (CRR) which defines common equity tier 1 items for these banks). After October, the ECB said it would further evaluate the situation. Banks should also *refrain from share buy-backs* aimed at remunerating shareholders. The move according to the ECB is estimated to retain approximately €30 billion of capital. This recommendation followed earlier relief measures for banks issued on 12 and 20 March including a decision of the ECB to relax capital requirements for banks good for € 120 billion, and the release of buffers valued at € 22 billion. Banks are expected to use the positive effects resulting from these measures to support the economy.

EBA stepped up its actions

On 31 March, EBA stepped up its actions. Following the ECB's move, it urged in a statement *all banks **to refrain** from dividends distribution or share buybacks* which result in a capital distribution outside the banking system, in order to maintain its robust capitalization, and to review remuneration policies. So EBA added the element 'distribution outside the banking system' unlike the ECB's recommendation. It however acknowledged that already many competent authorities communicated to banks their general expectations or engaged in bilateral dialogues in order to limit or refrain from dividend distribution and share buybacks.

To underline the importance of these actions, and the need for a level playing field among Member States, the EU's Ministers of Finance in light of the recommendations from supervisory authorities, urged on 16 April "*all banks that have not already decided to do so to refrain from making distributions during this period and to use the freed capital and available profits to extend credit or other urgent financing needs arising from the ongoing crisis to their customers in a way that helps to ensure preserving* econ*all banks that have not already decided to do so to refrain from making distributions during this period and to use the freed capital and available profits to extend credit or other urgent financing needs arising from the ongoing crisis to their customers in a way that helps to ensure preserving economic activity"*.

The ministers did not refer to distribution outside or inside the banking system. There was also no reference to the extensive state support packages which several Member States had put together, a link which for example BaFin made explicitly in its Opinion of 30 March : *"Die durch das umfangreiche Maßnahmenpaket der Bundesregierung und die aufsichtlichen Anpassungen erlangten Freiräume sollen die Institute daher nach Ansicht der BaFin nicht für die Zahlung von Dividenden nutzen.*"

At no point in time did either EBA or the ECB, as supervisor of the most significant eurozone banks, refer to the capital conservation measures of Article 141 of the Capital Requirements Directive (CRD). The ECB referred quite remotely to it by referring to 'EU law' in the last footnote of its 12 March press release titled "ECB Banking Supervision provides temporary capital and operational relief in reaction to coronavirus". But it did not refer to it in its recommendation of 27 March. Why? According to Linda van Goor, independent banking consultant, Article 141 gives a clear legal base for the 'urge not to distribute'.

It goes even further, as it states that an institution that meets the combined buffer requirement if it would distribute in connection with Common Equity tier 1 shall not make such distribution to an extent that would decrease its Common Equity Tier 1 capital to a level where the combined buffer requirement is no longer met. In other words, banks who use their buffers may not distribute their distributable amount, according to van Goor. More, CRD further determines the maximum distributable amount of an institution in Article 141 CRD. Was this considered when releasing the recommendations?

EIOPA and EBA statements

On 17 March, EIOPA in its "Statement on actions to mitigate the impact of Coronavirus/COVID-19 on the EU insurance sector insurance companies" (point 9) followed in the footsteps of EBA's first statement. Insurers should take measures to preserve their capital position in balance with the protection of the insured, following *prudent dividend and other distribution policies, including variable remuneration*. On 2 April, a few days after EBA's second statement, EIOPA also stepped up its action, with a new statement, urging (re)insurers at the current juncture *temporarily to suspend all discretionary dividend distributions and share buy backs* aimed at remunerating shareholders.

This suspension should be *reviewed* as the financial and economic impact of the COVID-19 starts to become clearer. The statement also urged this prudent approach to be applied by all (re)insurance groups at the consolidated level including significant intra-group dividend distributions or similar transactions, whenever these may materially influence the solvency or liquidity position of the group or of one of the undertakings involved. The materiality of this impact should be monitored jointly by the group and solo supervisors.

Where EIOPA's statement is different from EBA's statement is the open-ended deadline regarding the end of the measures coupled with the option to review the suspension (no deadline versus 1 October 2020). Different is also the specification that the measures are also valid for intra-group dividend distribution, which however the ECB recognised in its 27 March recommendation. And the reference EIOPA added to materiality (materially influence of the solvency or liquidity position) for intra-group suspensions is completely missing in the ECB's recommendation and in EBA's statements.

The next article in this series of 3 articles by Lieve Lowet is about Solvency II and will be published tomorrow on the Risk & Compliance Platform. You can respond and ask Lieve questions via the comments button at the bottom of this article.

The author, Lieve Lowet is an EU Affairs consultant and lobbyist since 2003, focuses on European dossiers relevant for the insurance and pension sector. From 2003 to 2008, she was Secretary-General for the international mutual insurance association AISAM (now AMICE), which accounted for 15% of the European and 6% of the world insurance market. Prior, she worked for McKinsey as a European banking and insurance expert.

Source : https://www.riskcompliance.biz/news/to-pay-or-not-to-pay-that-is-the-question/

Tools allowing for flexibility within the Solvency II framework? Really?

28 April 2020

Knowledge Base

by Lieve Lowet

This is part two of the series of three articles about my investigation into the recent measures taken by European authorities as a result of the situation that has arisen. This article is more specifically about Solvency II.

For insurers, there is no equivalent measure to Article 141 CRD. There is no such legal base in the Solvency II framework directive to 'urge' not to distribute. Article 71(1)(l)(i) of the Solvency II Delegated Regulation refers indirectly to the cancellation of distribution (dividends) in case of non-compliance with the SCR or where the distribution would lead to such non-compliance when legal or contractual arrangements allow for such cancellation. But it does so in the context of the classification of tier 1 basic own funds. In the past, EIOPA has referred to the cancellation or referral of dividend distribution when the validity of the business model is at risk: this was a recommendation to national supervisors e.g. after the 2016 stress test to address the vulnerability identified in the exercise. And in its recent consultation paper on the Solvency II review (EIOPA-BOS_19-465-CP-opinion 2020), EIOPA's draft advice links the potential by supervisors to limit or withhold dividend payments and other voluntary capital distribution to a sustainable solvency position when insurers use e.g. long-term guarantee measures. It also touches upon the prohibition of payments of dividends outside the EEA as another method of group supervision or as an alternative for the capital surcharge in case of systemic risk. Pious wishes?

The ESRB in its 2018 report *Macro-prudential powers, measures and instruments for insurance* pleads for a power for supervisory authorities to impose dividend restrictions in situations where the (re)insurance market developments could generate systemic risk. Even if the ESRB's plaidoyer would have been followed, and even if the Solvency II framework directive would have such provisions, is the Covid-19 crisis a systemic risk crisis? De la Rosière (Reflections on the health and financial crisis, SUERF policy note, issue nr 148, April 2020) does not seem to think so: he does not mention the Covid-19 crisis as a systemic risk.

Nor does Felix Hufeld, BaFin's President. And EIOPA, which opens its statement of 17 March with references to close communication and collaboration with the European Systemic Risk Board and the other supervisory authorities, does not even refer to the Covid-19 pandemic as a high impact catastrophic event, qualifying as an exceptionally adverse situation, and affecting a significant share of the market or LOBs (see Article 138,4 Solvency II directive).

The ministers of finance of the EU on 16 April also welcomed EIOPA's recent statements and recommendation on EIOPA's identification of tools allowing for flexibility within the current Solvency II framework for insurance undertakings. The ministers urged insurers to follow up on EIOPA's statements to take timely and comprehensive measures to preserve their capital position, including the temporary suspension of all discretionary distributions, and to continue to act in the best interests of consumers. Tools allowing for flexibility within the Solvency II framework? Really?

Article 16 of the EIOPA regulation

There was only one recommendation, and it concerned supervisory reporting flexibility. How does one marry that recommendation of 20 March with the reporting requirements of the Delegated regulation 2015/35? Which tool did EIOPA identify? EIOPA refers to Article 16 of the EIOPA regulation as the legal basis for the recommendation. According to that Article, guidelines and recommendations shall be in accordance with the empowerments conferred in the legislative acts referred to in Article 1(2), such as the Solvency II directive, or in Article 16 of the EIOPA regulation itself. But does this mean that deadlines laid down in a regulation can be shifted by a statement from EIOPA using mere moral persuasion? With all the creativity of the world, I cannot find in the Solvency II directive competences allowing EIOPA to do accordingly, even in terms of pandemic crisis.

I hesitate to conclude that EIOPA's recommendations, let alone statements, can put aside by moral persuasion or 'material technocratic influence' (either by making those choice or by technical influence, see Mendes, J., EU Executive Discretion and the limits of Law, 2019) hard and long debated democratic legal frameworks, especially because Solvency II has no provision equivalent to Article 141 CRD. EBA and EIOPA dealt with the issue of dividend suspension through statements, an 'instrument' not even foreseen in the revised ESA regulations. No statement, whether it was from EBA or EIOPA, referred to any legal basis. But EBA seems to have a legal base, whereas EIOPA...

There are other questions these ESA actions raise. Would an EU coordinated approach across the different financial sectors have been useful? Why was the Joint Committee not involved 'to ensure cross-sectoral consistency'? Some national supervisors have moved cross-sectoral, which is especially relevant for financial conglomerates. This is for example the case in Belgium where the National Bank, supervising both insurers and banks, issued a circular to insurers using the ECB's "at least till 1 October 2020" deadline for (re)insurers, a deadline which EIOPA did not put forward. The NBB also translated 'other distribution policies' into rebates and profit participations. An indirect reference to Article 27 CRR?

The next article in this series of 3 articles by Lieve Lowet is about the price to be paid by the insurance sector and will be published tomorrow on the Risk & Compliance Platform. The first one was published yesterday, see related items.You can respond and ask Lieve questions via the comments button at the bottom of this article.

The author, Lieve Lowet (See photo) is an EU Affairs consultant and lobbyist since 2003, focuses on European dossiers relevant for the insurance and pension sector. From 2003 to 2008, she was Secretary-General for the international mutual insurance association AISAM (now AMICE), which accounted for 15% of the European and 6% of the world insurance market. Prior, she worked for McKinsey as a European banking and insurance expert.

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<u>The urge to act is strong. But normative integrity should be strong too</u>

29 April 2020

Knowledge Base

by Lieve Lowet

This is the last part of the series of three articles about my in-depth investigation of the aforementioned measures as a result of the corona crisis. All the above actions, mentioned in the two previous articles, although prima facie and probably well intended, carry nevertheless a very heavy price. I will focus on the insurance sector by naming five topics.

First: core principles of the Treaty are neglected. By urging despite the strong capital ratios that all insurers should stop paying dividends for the time being, without further analysis or reference to business model, LOBs underwritten, SCR level, etc.. the principles of proportionality and adequacy were not respected, even if the tool was only a 'statement' (see Article 1(6) EIOPA regulation). It should be noted that statements can become legally enforceable if Member States decide so;

Second: EIOPA didn't let the regulatory framework do its job. The Solvency II framework allows for supervisory action if and when the SCR comes into the danger zone. No link was made to the effective health of the SCR. No reference was made to the ORSA as Van Hulle commented recently here. Article 138,4 of the SII directive was not used, although EIOPA refers broadly to Article 138 and to the supervisory ladder in its first March statement. But it did not mention 'exceptional adverse situations'. By anticipatively urging to keep the cash inside, even before an exceptionally adverse situation, the supervisors killed the supervisory ladder, while at the same time saying that maybe the framework is not so solid as we think it is and that e.g. the liquidity risk as laid out in the framework was not properly calibrated. Was all our work over the past ten years in vain? Or was it just a last conservative convulsion or reflex of the old system?

Third: under the proviso that an insurance solvency position is in the danger zone, there is no equivalent provision in the Solvency II framework equivalent to Article 141 CRD. Going further down the road, there is also no equivalent provision to Article 16a of the Banking Recovery and Resolution directive (BRRD) regarding powers to prohibit certain distributions. Even if such CRD and BRRD provisions would have been foreseen for insurers, would these have been a sufficient base? As there is in the statements no reference to danger zones, nor to a recovery and resolution situation, it seems they wouldn't, so the inclusions of provisions equivalent to those in the CRD and BRRD banking legislations on the insurance side could not have been the competence base of the urge to postpone today. Preventive governance?

Fourth: can company law continue to function if an Authority, using moral powers, is able to overrule a general assembly of owners of a perfectly healthy insurer as a measure of consumer protection? In addition, in the case of a mutual insurer where the members are the policyholders, the rationale of protecting customers seems odd and contradictory. Without supervisory authorities, several listed non-financial groups are moving autonomously in the same direction, suspending dividend payments.

Fifth: by urging to postpone dividend payments, the Authority not only created a waterfall effect towards other sectors of the economy counting on dividends, but also threw the child out with the bathwater. How can a Capital Markets Union and probably also the PEPP continue to be credible: *"On the Capital Markets Union, the demand side must be our next focus, so that private savers , so that private savers can benefit from capital markets"* (Bernardino, November 2019). If the purpose of the CMU is to diversify the financing base of companies, who will in the future be willing to invest in capital markets instruments if -when push comes to shove- proceeds are being blocked and pensions potentially endangered.

Dividend holders are not only institutional but also for example employees (via employee stock ownership plans), governments, public pension funds, not-for-profit organisations, retail shareholders who rely on dividends as an important part of their income, ….*"Dividends are essential to the livelihood of most pension schemes; therefore, the state should not prohibit these payments unless the company is badly hit by the Corona-crisis and has liquidity problems or has received public relief funding"* (Better Finance, press release 23 April 2020). Who will invest in the future if there is no guarantee that rightful returns can be paid out?

Lastly: how exceptional is this pandemic crisis? As it has not been labelled an exceptionally adverse situation, nor a systemic risk crisis, how will future crises be dealt with? Has this created a (dangerous) precedence? The urge to act is strong. But normative integrity should be strong too.

This is the last part of this series of 3 articles by Lieve Lowet. You can respond and ask Lieve questions via the comments button at the bottom of this article.

The author, Lieve Lowet is an EU Affairs consultant and lobbyist since 2003, focuses on European dossiers relevant for the insurance and pension sector. From 2003 to 2008, she was Secretary-General for the international mutual insurance association AISAM (now AMICE), which accounted for 15% of the European and 6% of the world insurance market. Prior, she worked for McKinsey as a European banking and insurance expert.

Source: https://www.riskcompliance.biz/news/the-urge-to-act-is-strong-but-normative-integrity-should-be-strong-too/

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EIOPA proposes further steps to close the European natural catastrophes protection gap

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In his inspired keynote speech at the opening of the 9th Annual EIOPA conference titled "Insurance and Pensions: leading the future", Gabriel Bernardino, EIOPA's chairman, called upon the sector to do right for the next generation and to show leadership. "No one should suffer because we are too complacent to act." All have a powerful role in mitigating the impact of climate change and ensuring a gradual transition to a more sustainable and resilient economy. For insurers and pension funds, this is especially true in the area of asset management. In underwriting, insurers should consider the impact of their underwriting practices. Risk mitigation and loss prevention can make a significant difference, while maintaining the fundamental principles of sound risk-pricing. However, this is only relevant if there is protection being bought. There is an important European protection gap due to climate change in the area of natural catastrophes (NATCAT) with a considerable disparity in terms of insurance penetration, catastrophe exposure and disaster preparedness. The very large majority of EU Member States don't even have a NATCAT scheme, and governments are budget tight. Will governments continue to play their role as insurer of last resort?

Any protection gap in the area of NATCAT impacts households, businesses, the financial system and ultimately governments. Better understanding the underlying causes of that protection gap across Europe is a first step. Chairman Bernardino proposed to build a European risk dashboard on natural catastrophes. Such dashboard could better inform political decisions on the national and European measures to put in place. But he also proposed to make the resilience gap part of the European Semester discussions between the European Commission and the Member States. Only a European approach will enable us to build sufficient resilience to this threat. Because climate change and weather do not stop at the borders.

This proposal, if put in place, may break the deadlock around moving towards a European solution for NATCAT. In 2013, the European Commission published a Green Paper on the insurance of natural and man-made disasters which revealed that the EU is working 'to facilitate and support increased coverage of appropriate disaster risk insurance and financial risk transfer markets, as well as regional insurance pooling (...)'. But not much seems to have happened since. Respondents were at best lukewarm, and had very limited appetite for compulsory insurance. The European Parliament adopted a resolution in 2014 which was not favourable and supportive for any European action in the field. But is such position anno 2019 still responsible? Referring to complacency, Bernardino as chair of EIOPA clearly thinks that this is no longer an option and that minds and ultimately money has to move.

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Photo courtesy: Lieve Lowet

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