

Consultation Paper

on

**draft Opinion on the supervision of
remuneration principles in the insurance
and reinsurance sector**

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Responding to this paper

EIOPA welcomes comments on the proposal for the draft Opinion on the supervision of remuneration principles in the insurance and reinsurance sector.

Comments are most helpful if they:

- contain a clear rationale; and
- describe any alternatives EIOPA should consider.

Please send your comments to EIOPA by 30 September 2019 responding to the questions in the survey provided at the following link:

[\[Link to EU Survey\]](#)

Contributions not provided using the survey or submitted after the deadline will not be considered.

Publication of responses

Contributions received will be published on EIOPA's public website unless you request otherwise in the respective field in the template for comments. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure.

Please note that EIOPA is subject to Regulation (EC) No 1049/2001 regarding public access to documents and EIOPA's rules on public access to documents¹.

Contributions will be made available at the end of the public consultation period.

Data protection

Please note that personal contact details (such as name of individuals, email addresses and phone numbers) will not be published. They will only be used to request clarifications if necessary on the information supplied. EIOPA, as a European Authority, will process any personal data in line with Regulation (EC) No 45/2001 on the protection of the individuals with regards to the processing of personal data by the Community institutions and bodies and on the free movement of such data. More information on data protection can be found at <https://eiopa.europa.eu/> under the heading 'Legal notice'.

Consultation paper overview and next steps

This consultation presents the draft Opinion on supervision of remuneration principles in the insurance and reinsurance sector.

The Opinion aims at enhancing supervisory convergence in the supervision of remuneration policies of insurance and reinsurance undertakings at European level without prejudice to the application of the relevant provisions of the Solvency II Directive and the Delegated Regulation.

The Opinion is addressed to the competent authorities as defined in point (i) of Article 4(2) of the EIOPA Regulation.

¹ [Public Access to Documents](#)

The draft Opinion aims to enhance supervisory convergence by focussing on a set of remuneration principles identified in the Delegated Regulation. It gives guidance to the supervisory authorities on how to challenge the application of certain principles and focuses on a reduced scope of staff identified as potential higher profile risk-takers to promote a proportionate approach. It is not EIOPA's intention to add requirements or to create administrative burden. A risk-based approach and supervisory judgement should be the basis of the supervision of such principles.

Next steps

EIOPA will consider the feedback received and expects to publish a Final Report on the consultation together with the final Opinion.

Background

It is EIOPA's task to ensure an effective and consistent level of supervision in order to guarantee a similar level of protection for policyholders and beneficiaries at European level. Therefore, it is EIOPA's goal to build a common supervisory culture through the convergence of national supervisory practices.

Convergent supervisory practices should be built upon a common understanding of Union laws and regulations, and without prejudice to the application of supervisory judgment and the proportionality principle.

The Opinion is issued under article 29(1) of Regulation (EU) No 1094/2010 (EIOPA Regulation). Due to the nature of the issue at stake EIOPA considers relevant to publicly consult stakeholders.

The draft Opinion aims to enhance common understanding among National Competent Authorities (NCAs) by focussing on a set of remuneration principles identified in article 258(1)(l) of the Delegated Regulation.

Considering that the principles defined in the Delegated Regulation are high-level and leave considerable discretion to the undertakings and supervisory authorities, divergent practices have emerged across Europe. The draft Opinion gives guidance to NCAs how to challenge the application of the principles and focusses on a reduced scope of staff identified as potential higher profile risk takers to promote a proportionate approach. It is not EIOPA's intention to add new requirements or to create administrative burden not proportionate to the risks.

The benchmarks set out in the draft Opinion gives guidance to NCAs on how to challenge the application of the principles of remuneration set out in the Delegated Regulation and should be considered for the purpose of supervisory dialogue.

Draft Opinion on the supervision of remuneration principles in the insurance and reinsurance sector

1. Legal basis

- 1.1. The European Insurance and Occupational Pensions Authority (EIOPA) provides this Opinion on the basis of Article 29(1)(a) of Regulation (EU) No 1094/2010.² This article mandates EIOPA to play an active role in building a common Union supervisory culture and consistent supervisory practices, as well as in ensuring uniform procedures and consistent approaches throughout the Union by providing opinions to competent authorities.
- 1.2. EIOPA delivers this Opinion on the basis of Directive 2009/138/EC (Solvency II Directive)³ and Commission Delegated Regulation (EU) 2015/35 (Delegated Regulation)⁴ in line with the relevant provisions of Directive 2017/828/EC⁵ on remuneration.
- 1.3. This Opinion is addressed to the competent authorities, as defined in paragraph (i) of Article 4(2) of Regulation (EU) No 1094/2010.
- 1.4. The Board of Supervisors has adopted this Opinion in accordance with Article 2(7) of its Rules of Procedure.⁶

2. Context and objective

- 2.1 The Solvency II framework acknowledges that remuneration policies and practices which provide incentives to take risks that exceed the approved risk tolerance limits of insurance and reinsurance undertakings (collectively “undertakings”) can undermine the effective risk management of such undertakings. Therefore, it provides for requirements on remuneration for the purposes of the sound and prudent management of the business and in order to prevent remuneration arrangements which encourage excessive risk.
- 2.2 In this context, Article 258(1)(l) of the Delegated Regulation requires all undertakings to adopt remuneration policies. Article 275 of the Delegated Regulation defines the remuneration principles undertakings have to comply with when establishing and

² Regulation (EU) No 1094/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Insurance and Occupational Pensions Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/79/EC (OJ L 331, 15.12.2010, p. 48).

³ Directive 2009/138/EC of 25 November 2009 of the European Parliament and of the Council on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II) (OJ L 335, 17.12.2009, p. 1).

⁴ Commission Delegated Regulation (EU) 2015/35 of 10 October 2014 supplementing Directive 2009/138/EC of the European Parliament and of the Council on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II) (OJ L 12, 17 January 2015, p.1).

⁵ Directive 2017/828/EC of 17 May 2017 of the European Parliament and of the Council amending Directive 2007/36/EC as regards the encouragement of long term shareholder engagement (OJ L 132, 20.5.2017, p.1).

⁶ Decision adopting the Rules of Procedure of EIOPA’s Board of Supervisors available at: https://eiopa.europa.eu/Publications/Administrative/EIOPA-BoS-11-002_EIOPA-BoS-Rules%20of%20Procedure-Rev3.f.pdf.

- applying their remuneration policies. Articles 294 and 308 of the Delegated Regulation set out the information on remuneration practices that should be reported to the supervisory authorities and published in the Solvency and Financial Condition Report.
- 2.3 Considering that the remuneration principles defined in the Delegated Regulation are high-level and leave considerable discretion to the undertakings and supervisory authorities, divergent practices have emerged across the European Union.
- 2.4 This Opinion aims to enhance supervisory convergence by focussing on a set of remuneration principles identified in the Delegated Regulation. This Opinion gives guidance to the supervisory authorities on how to challenge the application of certain principles and focuses on a reduced scope of staff identified as potential higher profile risk-takers to promote a proportionate approach. It is not EIOPA's intention to add requirements or to create administrative burden. A risk-based approach and supervisory judgement should be the basis of the supervision of such principles.
- 2.5 EIOPA's task is to ensure an effective and consistent level of supervision in order to guarantee a similar level of protection for policyholders and beneficiaries at EU level. This Opinion aims at promoting the convergence of national supervisory practices and contributing to the improvement of the functioning of the internal market.
- 2.6 Convergent supervisory practices should be built upon a common understanding of Union laws and regulations, and without prejudice to the application of supervisory judgment and the proportionality principle.
- 2.7 Risk-based supervision of the remuneration policy means that the supervisory authorities should have a two-dimensional approach when assessing the risk: the first dimension being the undertakings' overall risk profile and the second dimension being the design of the concrete remuneration policy which might be identified as being more risky than others.
- 2.8 Proportionality works two-ways: it justifies simpler and less burdensome ways of meeting the requirements for 'low risk' considering the two dimensions above, but it also increases the likelihood that undertakings will need to apply more sophisticated methods and techniques for 'higher risk'. In this context, supervisory authorities may adopt a proportionate and more flexible approach in the supervision of the remuneration principles when undertakings are categorized as 'low risk', including the design of the remuneration policy.
- 2.9 For the undertakings' staff that is not covered by this Opinion supervisory authorities may also adopt a proportionate and more flexible approach. As a result, supervisory authorities may choose to apply EIOPA's guidance to the undertakings' staff below the thresholds defined in paragraph 3.1, taking into account aspects such as remuneration practices in the relevant national market, the responsibilities and job profile of those staff members or the size and risk profile of the undertaking.
- 2.10 For members of the administrative, management and supervisory body (AMSB) and the most highly paid employees of global systemically important undertakings (G-SIIs) besides the guidance provided in this Opinion supervisory authorities should take into

account the FSB Principles and Standards for Sound Compensation Practices if these principles and standards apply in the respective jurisdiction⁷.

- 2.11 The benchmarks included in this Opinion should be considered for the purposes of supervisory dialogue and not as hard targets for the practical implementation of the remuneration principles. The indicative thresholds mentioned in this Opinion do not preclude the supervisory authorities to have stricter requirements if it is deemed appropriate.

3. Supervision of the remuneration policies

Scope of application

- 3.1 This Opinion, in line with the proportionate and risk-based supervisory approach mentioned above, applies for the remuneration of the staff from the categories listed below, whose annual variable remuneration exceeds EUR 50,000 and represents more than 1/4 of that staff member's total annual remuneration:

- a) AMSB members;
- b) other executive directors who effectively run the undertaking;
- c) key function holders as defined in EIOPA's Guidelines on the system of governance⁸; and
- d) categories of staff whose professional activities have a material impact on the undertakings' risk profile (material risk takers or MRTs).

Fixed and variable components of remuneration have to be balanced (Article 275(2) (a) of the Delegated Regulation)

- 3.2 Where remuneration schemes have fixed and variable components, these components should be in such a proportion that the employees do not become overly dependent on the variable components. When employees are overly dependent on variable remuneration this could encourage behaviours that are not in line with the undertakings' business and risk management strategy, endanger sound and prudent management, and encourage risk taking in order to maximise remuneration.
- 3.3 If an undertaking exceeds the threshold of a 1:1 ratio regarding any AMSB, other executive directors who effectively run the undertaking, key function holders or MRT, the supervisory authority should engage with the undertaking and investigate whether the remuneration policy is balanced with regard to the proportion of variable remuneration.
- 3.4 In addition to the fixed/variable remuneration ratio, supervisory authorities are recommended to pay specific attention to very low fixed remunerations, considering the context of national remuneration practices.

⁷FSB Principles for Sound Compensation Practices – in particular Implementation Standards Nr.6.

⁸ Paragraph 1.4 of EIOPA's Guidelines on the system of governance (BoS-14/253): "At least the four functions included in the system of governance, namely the risk management, the compliance, the actuarial and the internal audit function, are considered to be key functions and consequently also important or critical functions. Furthermore, persons are considered to be persons having key functions if they perform functions of specific importance for the undertaking in view of its business and organisation. These additional key functions, if any, are identified by the undertaking, but the determination of whether such functions should be considered key or not may be challenged by the supervisory authority."

A substantial portion of the variable remuneration has to be deferred (Article 275(2)(c) of the Delegated Regulation)

- 3.5 According to the Delegated Regulation the length of the deferral period shall not be less than three years and shall be correctly aligned with the nature of the undertakings' business, its risks and the activities of the employees in question. This implies that the undertakings' remuneration policies should contain different deferral periods depending upon the risks they enter into.
- 3.6 The deferral of 40% of the variable remuneration is considered a substantial portion for variable remuneration. Supervisory authorities should use their supervisory judgement to consider the need for a deferral rate higher than 40% and/or a longer deferral period as part of their risk-based approach. When the deferral is lower than 40% supervisory authorities are recommended to engage with the undertakings to better understand the specific situation. The deferral should apply to all the variable component, both linked to short term and long term performance horizons.
- 3.7 The deferral rate is recommended to be higher than 40% in case of a particularly high variable remuneration, e.g. in case of a ratio higher than 1:1.

Financial and non-financial criteria have to be taken into account when assessing an individual's performance (Article 275(2)(d) of the Delegated Regulation)

- 3.8 Where variable remuneration is performance related, the total amount of variable remuneration has to be based on a combination of the assessment of the individual's performance, the performance of the business unit concerned and the overall result of the undertaking or group to which the undertaking belongs.
- 3.9 Supervisory authorities should ensure that undertakings, when assessing an individual's performance ex ante, set out financial (quantitative) and non-financial (qualitative) criteria and describe the consequences on the pay-out of variable remuneration when these criteria are not met by the individual.
- 3.10 The criteria used should be linked to the decisions made by the respective staff member and should ensure that the remuneration award process has an appropriate impact on the individual's behaviour. The criteria should include achievable objectives and measures on which the staff member has some direct influence.
- 3.11 The assessment of performance should be set in a multi-year framework. The indicators on which the criteria are based and the entire decision-making process should be clear and predetermined, appropriately explained and documented. In the assessment the followings should be taken into account:
- a) financial (quantitative) criteria that should cover a period which is long enough to capture the risk taken by staff members and should be risk adjusted;
 - b) non-financial (qualitative) criteria that should contribute to the creation of value for the undertaking, such as compliance with external and internal regulations, the efficiency of customer service management, the achievement of strategic goals (e.g. Environmental, Social and Governance criteria, ethical aspects), behaviour including towards customers, turnover of staff, adhering to the values of the company, impact on the undertakings' reputation, consumer satisfaction, adherence to the undertakings' risk management policy, leadership, teamwork,

creativity, motivation and cooperation with other business units, internal control and corporate functions.

3.12 Furthermore, financial and non-financial criteria should be appropriately balanced. For instance, where the criteria is 80% financial and 20% non-financial the supervisory authority may come to the conclusion that the assessment framework is not appropriately balanced. In any case, non-financial criteria should not be negligible and should have a substantial value as indicators of the above mentioned aspects. The supervisory authorities should challenge the balance of the criteria if they are not consistent with a sound and effective risk adjusted remuneration policy or do not sufficiently reflect the undertaking's strategic views.

The measurement of performance has to include a downwards adjustment for exposure to current and future risks (Article 275(2)(e) of the Delegated Regulation)

3.13 The term downward adjustment embraces all kind of adjustments, e.g. malus, clawback and in year adjustments (e.g. by lowering the overall bonus pool, which will ultimately translate into lowering - or not awarding at all - the variable remuneration of an individual).

3.14 Variable remuneration should not only be adjusted downward when members of staff do not meet their personal objectives, but also when their business units and/or the undertaking as a whole fail to do so. Importantly, if an undertaking is likely to breach or has breached the Solvency Capital Requirement its remuneration policy should prescribe that downwards adjustment will be applied⁹.

3.15 When tailoring an appropriate remuneration scheme, this has to be aligned with the nature, scale and complexity of the risks inherent to the undertaking's business and should be reflected in the downwards adjustment.

3.16 Supervisory authorities should require a clear description of the downwards adjustment(s) from undertakings. This should at least:

- a) show how the short to long-term risks, the cost of capital, (internal) capital requirements, as well as the dividends policy have been taken into account;
- b) include examples of how the downwards adjustment works;
- c) include the rationale for the chosen downwards adjustment and the triggers used; and
- d) in any case, downwards adjustments should be designed in a way that - in the event of an individual's negative contribution to the undertakings' results in any year of the deferral period - any unvested portion of the variable part of the remuneration may be subject to malus.

Termination payments have to be related to performance achieved over the whole period of activity and be designed in a way that does not reward failure (Article 275(2)(f) of the Delegated Regulation)

⁹ In line with EIOPA 's Opinion to institutions of the European Union on the harmonisation of recovery and resolution frameworks for (re)insurers across the Member States, EIOPA believes that supervisory authorities should have as an early intervention power, the power to require undertakings to limit variable remuneration and bonuses. If this power is already available at national level, supervisory authorities should consider using this power in case of a potential breach of the SCR.

- 3.17 Undertakings' remuneration policies should specify the possible use of termination payments, including the maximum payment or the criteria for determining the amount of the payment.
- 3.18 Termination payments may include redundancy payments, and may be subject to a non-competition clause. In particular additional payments made in the following situations qualify as termination payments:
- a) when the undertaking terminates contracts because of a failure of the undertaking;
 - b) when the undertaking terminates a contract following a material reduction of the undertakings' activities in which the staff member was active or where business areas are acquired by other undertakings without the option for staff to stay employed in the acquiring undertaking;
 - c) when the undertaking and staff member agree on a settlement in case of a potential or actual labour dispute, to avoid a decision on a settlement by the courts.
- 3.19 Termination payments are regularly seen as a form of variable remuneration. When defining the maximum level of these payments the fixed/variable remuneration ratio – as proposed in the section on balanced remuneration – should be taken into account.
- 3.20 The following amounts of termination payments should not be taken into account when determining the fixed/variable remuneration ratio:
- a) payments that are mandatory under national labour law, mandatory payments following a court decision or payments which are calculated through a predefined generic formula set within the remuneration policy in the cases referred to under paragraph 3.18;
 - b) settlements made for the loss of office where they are subject to a non-competition clause in the contract ('gardening leave') and awarded in future periods up to the amount of the fixed remuneration which would have been paid for the non-competition period, if staff were still employed; and
 - c) payments that belong to the category listed in paragraph 3.18, and that do not fulfil the condition in paragraph (a) above, where the undertaking has demonstrated to the supervisory authority the reasons and the appropriateness of the amount of the termination payment.
- 3.21 The following amounts of termination payments should be taken into account when determining the fixed/variable remuneration ratio:
- a) the sum of any higher amounts than the fixed remuneration for the future periods which would have been paid for the non-competition period, if staff were still employed under paragraph 3.20(b); and
 - b) any other termination payment not listed under paragraph 3.20.
- 3.22 In addition, a substantial part of the termination payment should be deferred in time, as proposed in the section on the substantial part of variable remuneration that is to be deferred in time. Termination payments identical to those listed in paragraph 3.20 should not be taken into account when determining the portion of variable remuneration that should be deferred in time.

3.23 Payments have to reflect the performance achieved over time and must not reward failures. The severity of failures will determine the level of the termination payment and – ultimately – may lead to no termination payment being awarded at all. When making this determination the undertaking has to distinguish between:

- a) failures of the undertaking – such failures have to be considered when the total amount of the termination payments for staff is determined taking into account the capital base of the undertaking; such termination payments should not be higher than the reduction of costs achieved by the early termination of contracts. Examples of such cases could include:
 - i. the undertaking benefits from government intervention or is subject to early intervention or resolution measures;
 - ii. where the opening of normal insolvency proceedings of the undertaking has been filed;
 - iii. where significant losses lead to the situation that the undertaking no longer has a sound capital basis and, following this, the business area is sold or the business activity is reduced.
- b) failures of the identified member of staff – these should lead to a downwards adjustment or non-payment of the termination payment. Examples of such cases could include:
 - i. where an AMSB member is considered to no longer meet fitness and propriety requirements;
 - ii. where the identified staff member participated in or is responsible for conduct that resulted in significant losses for the undertaking;
 - iii. where the identified staff member acts contrary to internal rules, values or procedures intentionally or by gross negligence.

3.24 Termination payments should not be made when:

- a) a failure of the identified member of staff warrants the immediate cancellation of the contract or the dismissal of staff;
- b) a member of staff resigns voluntarily in order to work for a different legal entity, unless such a payment is required by national labour law.

3.25 Supervisory authorities should ensure that undertakings are able to demonstrate the reasons for the termination payment, the appropriateness of the amount awarded and the criteria used to determine the amount, including that it is linked to the performance achieved over time and does not reward failure.

4. Composition of the variable remuneration

4.1 Supervisory authorities should ensure that undertakings award 50% of variable remuneration of the staff mentioned in paragraph 3.1 in shares, equivalent ownership or share-linked instruments, if proportionate and feasible.

4.2 These instruments should be subject to an appropriate retention policy designed to align incentives with the longer-term interests of the undertaking. This applies to the portion of the variable remuneration component that has to be deferred in time as well as the portion of the variable remuneration component that is not deferred in time.

4.3 A risk-based and proportionate assessment of the specific situation might lead a supervisory authority to conclude that the 'composition requirement' should be applied in a simpler and less burdensome manner for specific undertakings.

- 4.4 Appropriate (financial) instruments might not be available to a considerable group of undertakings due to their legal form. In those circumstances such undertakings are encouraged to consider developing equivalent non-cash instruments.

5. Reporting requirements

- 5.1 Supervisory authorities should collect qualitative and quantitative data enabling them to perform supervisory review of the remuneration principles in accordance with this Opinion. Instruments for data collection might be either the regular supervisory reporting or a specific request.

6. Monitoring by EIOPA

- 6.1 EIOPA will start monitoring the application of this Opinion by the supervisory authorities two years after its publication.
- 6.2 This Opinion will be published on EIOPA's website.