

**Interview with  
Gabriel Bernardino, Chairman of the  
European Insurance and Occupational Pensions Authority  
conducted by Adam Cadle, Insurance Asset Management Europe  
and published on 30 May 2017**

**1. What are EIOPA's aims and ambitions within the European insurance space in 2017?**

The key ambition and challenge for EIOPA now and in the coming years is to build and put in place a common European supervisory culture. The implementation of Solvency II is **the** opportunity for the European Union's insurance supervisors to change and converge in a bottom-up process towards a European supervisory culture based on common best and effective supervisory practices. This is a longer-term process during which the European insurance supervisory community are developing common ways of thinking, understanding and working. Only a common supervisory culture will ensure a level playing field, prevent regulatory arbitrage and safeguard a similar level of protection to all policyholders and beneficiaries in the European Union. Full convergence will not happen overnight but actions need to be taken now. In this respect, EIOPA is developing a Handbook of good supervisory practices in Solvency II, building an information system based on the Solvency II data and continuously engaging in bilateral on-site activity with the national supervisors.

For insurance prudential regulation, this is the period of regulatory consolidation - a stable phase in which EIOPA is closely monitoring how the Solvency II regime is being applied and how the requirements are meeting expectations. Evidence is being collected on the efficiency and effectiveness of the measures.

Furthermore consumer protection, both through prudential and conduct of business regulation, continues to be at the centre of EIOPA's strategic priorities. EIOPA's Consumer Trends Reports, Thematic Reviews and Retail Risk Indicators provide a snapshot of existing and emerging cases of consumer detriment. At the same time they allow us to detect and take prompt regulatory and supervisory actions whenever required. For example, in our recently published Thematic Review widespread and significant payments from asset managers to insurance undertakings were detected and EIOPA is now analysing the necessity of further regulatory or supervisory actions.

Another strategic priority of EIOPA is to preserve financial stability of the pensions and insurance sectors in Europe. EIOPA uses European Union wide stress tests to assess risks and vulnerabilities and to develop common and

coordinated responses to the persistent low interest rates environment. This year EIOPA conducts its 2<sup>nd</sup> occupational pensions' stress test to assess the resilience of Institutions for Occupational Retirement Provision – so called IORPs - to an adverse market scenario and to analyse the transmission mechanisms of pension funds towards the real economy and financial markets.

## **2. How would you describe the state of the general, life and reinsurance sectors in Europe at this present time?**

Overall the European insurance sector is adequately capitalized with an average solvency ratio of 230%. Specific transition periods are used mostly by life insurance companies with long-term guarantees business. The use of transitional measures is transparent and insurance companies publish their solvency ratios with and without the application of these measures. Transitional measures form an integral part of Solvency II and are intended to limit the procyclicality and to facilitate the entry into the new regime by giving companies the time needed to adapt to the new solvency requirements.

Within a very difficult macroeconomic scenario with historically low interest rates, the application of Solvency II, a more demanding risk-based solvency regime, was carried out smoothly as a result of timely preparation and appropriate transitional periods. In an industry with € 11 trillion of assets under management and € 8.7 trillion in technical provisions, this success is remarkable and has contributed significantly to the stability of the European financial sector.

## **3. The announcement that the Ultimate Forward Rate (UFR) applied to the euro is to decrease the rate in 2018 from 4.2 per cent to 4.05 per cent, which has been met with condemnation across the insurance industry. What is your reply to this reaction of insurance companies worrying that this will require more capital in reserve balance sheets?**

According to the Solvency II legal framework the Ultimate Forward Rate (UFR) shall be stable over time and shall only change as a result of changes in long-term expectations. The currently used UFR was derived in 2010. Since then, the interest rates have drastically fallen to unprecedented levels with negative interest rates being now reality for a long period of time. As a consequence, long-term expectations of real interest rates have changed.

Furthermore it should be acknowledged, that a clearly specified methodology to derive the UFR is a legal requirement under Solvency II. EIOPA's Board of Supervisors agreed unanimously on a methodology, to be implemented as of the beginning of 2018. This methodology strikes the right balance between a stable UFR and the need to adjust it in case of changes in long-term expectations about real interest rates and inflation.

EIOPA's methodology followed a thorough impact analysis of changes to the UFR on 336 European insurance undertakings from 29 countries. The impact on capital requirements of a change of 20 basis points, i.e. more percentage points compared to the UFR to be applied as of 2018 was small. The Solvency Capital Requirement (SCR) ratio fell from 203 to 201%; even under a decrease of 50 basis points, the SCR ratio fell from 203 to 198% only.

**4. MSCI has recently argued that EIOPA should lower the SCR on real estate investment stating that the current SCR of 25 per cent exceeds the most extreme 12-month downside values at risk documented for geographically diverse real estate investments across Europe. What is your response to this?**

The result of the study by MSCI seems to be based on geographically diverse real estate investments across Europe. Before concluding on the level of the SCR for real estate investments, it would be important to assess whether insurance undertakings that are using the standard formula hold geographically diverse real estate investments across Europe. In general, one should also take into account the fact that insurance undertakings that are using the standard formula are often small and medium-sized undertakings.

At the same time EIOPA always welcomes the evidence useful for a better assessment of the risks in real estate investments and stands ready for further analysis should the need arise.

**5. How important is a macro-prudential framework for insurance?**

A macro-prudential framework is beneficial for the European insurance sector because a well-functioning sector plays an important role in achieving a stable financial system and by that supporting long-term and sustainable economic growth. A macro-prudential framework in the European Union would contribute to mitigate the likelihood and the impact of potential systemic crisis in insurance. At the same time, however, EIOPA believes that such a framework would only

work if it takes into account the specific nature of the insurance business and funding models and defines insurance specific objectives and instruments.

Furthermore, before embarking into new tools, the existing ones should be duly considered and indeed used. As we know, although Solvency II is a micro-supervisory regime, it already contains macro-prudential elements. Assessing the impact of such instruments before proposing new instruments is fundamental to ensure efficiency and to avoid unnecessary burden to both, supervisors and undertakings.

EIOPA is of the view that any potential additional macro-prudential tools or policy should be addressed in the context of the 2021 overall review of Solvency II. This approach would ensure consistency and complementarity between both the macro- and micro-prudential frameworks.

## **6. How do you see Brexit affecting the insurance industry?**

EIOPA is closely monitoring the developments linked with the Brexit negotiations. As regards the possible impact on the conduct of insurance supervision and insurance products, it is too early to form any firm position. As soon as the United Kingdom is leaving the European Union insurers based in the United Kingdom would no longer benefit from an EU "passport" to the European single market. Insurers based in the United Kingdom and seeking relocation of subsidiaries in the 27 European Union member states need to be subject to proper supervision. In order to collect evidence, EIOPA's oversight team is visiting national supervisory authorities engaged in discussions with companies in the United Kingdom. Empty shells or letter boxes are not acceptable. Sound supervision demands appropriate location of management and key functions including sound outsourcing and reinsurance policies.

EIOPA intends to publish in due course guidance for national supervisory authorities on sound principles for authorisation and supervision and will subsequently closely monitor their implementation.

EIOPA is also closely monitoring any possible effects on financial stability and consumers.