EUROPEAN INSURANCE
AND OCCUPATIONAL PENSIONS AUTHORITY

KEYNOTE AND WELCOME SPEECH

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Exploring new horizons for the benefit of the citizens in the European Union

Check Against Delivery
Seul le texte prononcé fait foi
Es gilt das gesprochene Wort

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Ladies and Gentlemen,

On behalf of EIOPA, I am delighted to welcome you to our sixth Annual Conference here in Frankfurt. I am very pleased that once again the conference programme attracted such a huge audience interested in the debate of important key issues in the insurance and pension's world.

Reflecting the new vision and strategy of EIOPA, this year's conference theme is "Exploring new horizons". While at first sight our three panels deal with very different subjects, they actually have in common the need to explore new horizons and frontiers.

In my today's intervention I will address the following four topics:

- *First,* **EIOPA's comprehensive approach to supervisory convergence**
- *Second,* the **evolution of the Pan-European Personal Pension Product (PEPP) in the context of the Capital Markets Union**
- *Third*, the **priorities of EIOPA's consumer protection agenda from the implementation of the Insurance Distribution Directive (IDD) to digitalisation**
- *Fourth*, the **next steps on the regulatory front** and **the challenges therein**

To my first topic, EIOPA's comprehensive approach to supervisory convergence

Along the years many times we debated the risks and opportunities of Solvency II for the insurance industry. But the implementation of Solvency II brings also challenges to supervision.

First of all, in order to ensure the protection of policyholders and beneficiaries, all supervisory authorities in the European Union should be provided with the necessary means. They need the relevant expertise, capacity and mandate to execute this mandate in full independence. In a single market, where cross-border business plays an increasing role, it is fundamental to ensure that the supervisory system has no weak links.

So, the key challenge for EIOPA in the coming years is to build and put in place a **common European supervisory culture**. To ensure supervisory convergence in the European Union internal market, the insurance supervisory community needs to develop common ways of thinking, behaving and working. This implies a common interpretation of the laws and regulations, a common understanding of supervisory objectives and a common view on the key characteristics of good and effective supervision. This is a journey and EIOPA is working together with all National Supervisory Authorities (NSA's) to deliver the desired outcomes.

Only a **common supervisory culture will ensure an equal level playing** field, **prevent regulatory arbitrage** and **safeguard a similar level of protection** to **all policyholders** and **beneficiaries in the European Union**.

Let me mention a number of EIOPA initiatives in this area:

- EIOPA is **developing a Handbook of good supervisory practices in Solvency II.** This handbook will come into life through a comprehensive training programme for national supervisors.
- We are **building an information system based on the Solvency II data** which will allow the development of reliable risk analysis and early warning indicators at individual, group and system-wide level and provide the National Supervisory Authorities with peer group comparisons, increasing supervisory capabilities at a national level. This will reinforce the quality of both micro- and macro-supervision in the European Union.
- EIOPA is **prioritising the on-going monitoring of internal models**, by working on consistency reports on the treatment of sovereign debt and the modelling of the volatility adjustment as well as market and credit risks. We are conscious that potential material differences due to diverse interpretations by National Supervisory Authorities could have a huge impact in the level playing field and policyholder protection.
- 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.

- EIOPA will continue to **engage in bilateral on-site activity with the National Supervisory Authorities**, by providing independent feedback on and by challenging supervisory practices. Following recent failures with high impact on cross-border business, EIOPA is reinforcing the exchange of information between National Supervisory Authorities and has a key and crucial coordinating role to ensure proper cooperation and effective supervision. Cooperation and exchange of information should be reinforced starting at the authorization process.
- EIOPA is **supporting improvements in national supervision** in exercises such as the conduct of Balance Sheet Reviews as it was the cases of Romania and Bulgaria. We have been instrumental in setting up and designing these reviews, providing in-depth sector expertise and knowledge and continuously following its implementation. These exercises add credibility to the market and ultimately enhance consumer confidence.
- EIOPA is i**mplementing a strategy on preventive risk-based conduct supervision** to spot outliers, investigate the root causes and develop supervisory responses. EIOPA uses tools such as Consumer Trends Reports, Thematic Reviews and Retail Risk Indicators to provide a snapshot of existing and emerging cases of consumer detriment. This allows targeting issues that go beyond one national market, building a coordinated understanding.

To deliver this supervisory convergence programme, which is at the end beneficial to both, to the industry and to consumers, the **forthcoming review of the European System of Financial Supervision should guarantee a proper financing mechanism for EIOPA and strengthen the supervisory convergence area with a clearer mandate to ensure common supervisory culture and practices.** EIOPA's independent assessment and challenge of supervisory practices should go beyond the situations of potential threats to the stability of the financial system. In this sense, some governance adjustments are necessary to provide the needed independence as well as checks and balances to this reinforced process.

The question of further integration of supervision in the European Union insurance sector is eminently a political one. History tells us that decisions of this nature are usually prompted by critical events. As Jean Monnet once said, "People only accept change when they are faced with necessity and only recognize necessity when a crisis is upon them". But progress can and should be made without waiting for a crisis. The implementation of Solvency II gives all European Union insurance supervisors a tremendous opportunity to change and converge in a bottom-up process towards an European supervisory culture based on common good and effective supervisory practices. EIOPA is fully committed to lead the way forward.

Now let me turn to my second topic, the Pan-European Personal Pension Product and the Capital Markets Union

One of the major challenges for countries in the European Union is the provision of safe, adequate and sustainable pensions to their citizens. While there is a broad consensus that both private occupational and personal pensions can play an important role in diversifying the sources of retirement income on top of the public pension regimes, the context of labour and demographic changes and the prolonged low interest rate environment creates particular challenges also to private regimes.

At the same time, particularly in the area of long-term retirement savings, it is evident that the European Union internal market is far from delivering its full potential. There is a huge fragmentation of products available to consumers, from low-performing deposits, to very often too complex and costly life insurance and mutual funds, many of them not truly retirement saving products. Also consumer protection rules are very different in the various European Union Member States. This fragmentation is a serious obstacle to cross-border business, increases the costs, reduces the average returns for savers and ultimately undermines consumer confidence in private pension provision.

This year, in February, EIOPA submitted to the European Commission **its final technical advice on a Pan-European Personal Pension Product, the PEPP**, **a safe, transparent and cost-effective personal savings product.** In our view the PEPP could be the catalyst for efficiency gains through economies of scale and opportunities for risk diversification as well for competition and innovation for the benefit of consumers.

We proposed a number of standardised and flexible features for the PEPP:

- **Standardised information provision** based on the proposals of the Key Information Document within the Packaged Retail and Insurance-based Investment Products, the PRIIP's framework
- **Standardised limited investment choices**, with one core „default" investment option, where the investment strategy takes into account the link between accumulation and decumulation
- **Regulated, flexible caps on costs and charges**
- **Flexible biometric and financial guarantees**

The PEPP should have a **long-term perspective in its investment policy** to better reflect the long-term nature of retirement savings. This is particularly welcomed from a macro-perspective because long-term investors are needed to provide stable funding to the European Union economy. In order to allow this long-term investment horizon, the **PEPP should envisage minimum holding periods to mitigate the surrender risk**. **Sustainable investment in illiquid assets should match liabilities with a correspondent illiquid profile**.

The analysis conducted brought us to the conclusion that the PEPP, enacted through a 2nd regime, is a powerful tool to close the pension savings gap in Europe. This conclusion has been supported by the vast majority of stakeholders that responded to our public consultation.

From the development of a Capital Markets Union the PEPP can be one of the most tangible outcomes and benefits for European Union citizens Together, we have to do everything to regain the trust of Europe's citizens in the European Union and its financial services industry. Europeans request concrete solutions to their very pertinent problems such as the lack of adequate retirement savings. With the PEPP European citizens could see the benefits of building a true single market for capital.

EIOPA stands ready to continue to work on PEPP, namely in the design of „product pilots". We intend to explore pure **individual Defined Contribution Schemes** but also **collective Profit Sharing Products**.

While pure individual Defined Contribution Schemes can be designed to adjust investment risk throughout the live of the contract, thus reducing risk for members, the development of collective Profit Sharing Products could allow the **pooling of investments** with the smoothing of returns across members of the pool, so that all members benefit from **average long-term returns** of the fund and are **protected from extremely negative outcomes** in stressed market situations.

The design of the PEPP "product pilots" need to ensure conditions to allow European Union citizens to invest in a balanced portfolio that should include assets such as **equities, property, infrastructure and green technologies**. With the appropriate safeguards, this will provide a good chance to accumulate a pension that outperforms inflation and grows to levels that can provide a decent standard of living.

Provided that by design these collective Profit Sharing Products avoid the exposure to short-term market volatility the regulatory treatment in Solvency II could be aligned to the risks effectively incurred, **resulting possibly** in **lower capital requirements**.

Finally, the PEPP "product pilots" need to be designed in a way to ensure the **highest standards in transparency, fairness, governance and risk management**.

In particular, the transparency of the PEPP towards the European Union citizens could be greatly enhanced with the development and maintenance of a centralized information system by EIOPA providing **online updated and easily accessible information of the costs, risks and returns** of **all PEPP's sold** throughout the European Union.

Very importantly, in my view, the Capital Markets Union can only succeed if we are capable of regaining confidence of the European Union citizens in the financial markets. In this sense I strongly believe that **supervisory convergence needs to be a high level priority of the Capital Markets Union**. The implementation of the PEPP needs to be accompanied with an evolution in the powers and tools available to EIOPA. To break the current market fragmentation and to increase cross-border provision of services we need to ensure that there are proper arrangements to achieve high quality supervision across the European Union. This should entail an **appropriate mix of centralised powers and tools and a clear mandate to reinforce supervisory convergence.**

Whilst the PEPP is designed as a personal product, I believe that some of its learnings can benefit occupational pensions, too.

Looking forward, a further important step would be the design of **a simple and transparent 2nd regime for Defined Contribution Occupational Pensions Schemes.** This framework should be capable to take full advantage of the potential of the European Union internal market, by providing a cross-border platform which European companies could use to manage the retirement plans of their employees, reduce costs, support long-term funding of the European Union economy and ultimately deliver better pension outcomes.

EIOPA will develop **first ideas on the components of this framework and on the design of potential scheme solutions** that, while allowing the control of costs by sponsors, would mitigate for the members the increased risks coming from the move towards pure Defined Contribution plans.

Coming to my <u>third topic</u>, the priorities of EIOPA's Consumer protection agenda from the implementation of the Insurance Distribution Directive (IDD) to digitalisation

EIOPA places consumer protection, both through prudential and conduct of business regulation, at the centre of its strategy. Misconduct by firms may not only harm individual consumers, but may also have a wider prudential impact, posing a threat to the stability of the financial sector.

In this context, the **implementation of the Insurance Distribution Directive (IDD)** is a significant step forward. EIOPA has already consulted on its draft technical advice to the European Commission on possible delegated acts on issues like **Product Oversight and Governance**, **Conflicts of Interest**, **Inducements and Assessment of suitability and appropriateness**.

Our aim is to ensure that the interests of the customers are taken into consideration throughout the life cycle of a product, that distribution activities are carried out in accordance with the best interests of customers and that customers buy insurance products which are suitable and appropriate for them.

Detrimental impact occurs when an inducement or structure of an inducement scheme provides an incentive to carry out the insurance distribution activities in a way which is **not in accordance with the best interests of the customer**. It is then fundamental to identify criteria to assess if and when inducements are considered to have a high risk of leading to a detrimental impact on the quality of the relevant service to the customer.

Another significant project within the overall work of EIOPA on the IDD is the **Insurance Product Information Document (IPID)**. Its objective is to ensure that the customer has the relevant information about a non-life insurance product to allow him to easily compare between different product offers and to make an informed decision about whether or not to purchase the product. We developed a template for the **Insurance Product Information Document (IPID)** subject to consumer testing and public consultation, which is currently on-going.

Our society is confronted with **successive technological innovations and the continued increase in the use of big data.** This **digital revolution** is transforming completely the way we interact and do business.

The insurance world is already confronted with this reality. Some will say that we have always been facing changes and that this is just another step. That’s true, but **the change coming from the digital era is different: in many aspects it is not incremental; it is disruptive.**

The entire insurance value chain will be impacted, from insurers to intermediaries, distributors and service providers. We will see some business models threatened and new entrants implementing business models that will dramatically reduce the traditional frictional costs. The use of big data and telematics, comparison websites and automated advice tools will impact the interface with consumers. The increasing amount of personal data available and the power of data analytics will inevitably change insurance underwriting models.

As we all know, **changes bring risks, but equally opportunities**.

On the positive side, this **change has the potential to produce better** outcomes for customers, through the development of more personalized services and products and better management of risks or fraud situations. But also raises several issues in terms of access to financial services for certain consumers, the transparency regarding the use of personal data and cyber security risks.

Starting next year, **EIOPA will organize a series of roundtables dedicated to "Insurtech".** Our objective is to learn from different stakeholders about the evolutions in this area, the benefits and risks for consumers and the potential obstacles to good innovation practices. Ultimately this will contribute to the development of a regulatory framework that promotes the highest standards of consumer protection while not hindering innovation.

My ***fourth*** **and** ***last topic***, the next steps on the regulatory front and the challenges therein

Going forward, **regulatory certainty** is an important value that we all should preserve. The **review of Solvency II** should follow the **structured process envisaged in the legislative texts**: by 2018, the review of the Solvency Capital Requirement (SCR) and by 2021, the overall review of the regime, including the treatment of long-term guarantees.

Following the recent call for advice received from the European Commission, EIOPA will issue a discussion paper on the review of the Solvency Capital Requirement (SCR) before the end of this year. During 2017 through a series of roundtables we will engage with all relevant stakeholders. EIOPA is committed to an **evidence-based policymaking**. **Changes must be carefully justified and clearly necessary**. We are particularly interested in concrete proposals to ensure **more simplicity and proportionality**.

While Solvency II is undoubtedly a great achievement for the European Union insurance sector and for the protection of policyholders, there are still some areas where progress is needed to complete a comprehensive European Union insurance regulatory framework. I am talking about a **macro-prudential framework**, **recovery and resolution mechanisms** and **insurance guarantee schemes**. Furthermore, in this context the evolution of **international standards** should be mentioned. Let me elaborate on these areas.

- ***The macro-prudential framework***

The insurance sector plays a relevant role in achieving a stable financial system, supporting long-term sustainable economic growth. Thus, **mitigating the likelihood and the impact of a systemic crisis in insurance should be an important policy objective.**

Work needs to be done towards **the establishment of a comprehensive European Union macro-prudential framework for insurance** that takes into account the specific nature of the insurance business and funding models and defines insurance specific objectives and instruments. We could think of a number of operational objectives, such as

- To **ensure sufficient loss absorption capacity and reserving**
- To **avoid negative interconnections and excessive concentrations**
- To **avoid excessive involvement in activities whose features may pose systemic risk**
- To **limit pro-cyclicality and risk behaviour as insurers collectively 'search for yield'**
- To **avoid moral hazard**

This work needs to consider that although Solvency II is a micro-supervisory regime it already contains macro-prudential elements. A full assessment of the macro-effectiveness of these elements needs to be made in the coming years.

Our proposal is to use the **2021 overall review to integrate in Solvency II a macro-prudential framework for insurance**. This approach would ensure the **coherence between the micro- and the macro-elements**, **avoid the emergence of conflicting incentives to insurers,** and **facilitate the implementation of the regimes by the respective authorities**. EIOPA will work in this area in close cooperation with the European Systemic Risk Board (ESRB).

- ***The recovery and resolution mechanisms***

One of the lessons learned from the recent financial crisis is the need to have in place **adequate recovery and resolution tools** which will enable national authorities to intervene in failing institutions and resolve failures when these materialise in an effective and orderly manner.

At present, there is **no harmonised recovery and resolution approach for insurers in the European Union**. The national frameworks in place show substantial differences and often do not capture relevant elements which the Financial Stability Board (FSB) considers to be necessary for an effective resolution regime. In the absence of a European Union regime, the emergence of national specific solutions will increase fragmentation in the internal market and create additional difficulties when dealing with cross-border cases.

EIOPA already started working in this area and will **publish a discussion paper before the end of the year, covering an overview of the national regimes currently in place, discussing the rationale for harmonisation and putting forward first ideas on the building blocks of a minimum harmonized recovery and resolution framework for insurers in the European Union**. While we should learn from the banking experience on the Banking Recovery and Resolution Directive (BRRD), we believe that **a "copy-paste approach" is not an appropriate one**. The insurance regime should build on the **already existent mechanisms and develop tools and powers appropriate to the insurance specific features.**

- ***The insurance guarantee schemes***

Although the introduction of Solvency II and, in particular, the adoption of risk-based capital requirements and forward-looking supervision should contribute to reduce the likelihood of insurance failures, **it is important to realize that Solvency II is not a zero-failure regime and eventually failures will continue to occur**. Beyond recovery and resolution regimes, **insurance guarantee schemes can contribute to increase the overall protection of policyholders and beneficiaries**. However, in the European Union this area is still a hugely fragmented, with the existing schemes differing quite substantially in terms of financing, functions, mandate and coverage. This fragmentation creates particular problems in the presence of failures involving cross-border business.

While priority should be given now to the development of a European Union recovery and resolution framework, I believe that **in the medium-term it is**

fundamental, both for consumer protection and the proper function of the internal market, to build a minimum harmonized approach to insurance guarantee schemes in the European Union.

- ***The international standards***

The 2021 review of Solvency II may benefit from the **progress achieved at international level** in particular in **systemic risk** and the **international capital standard** (ICS).

The challenge for the coming years is to develop what I call the **"third generation of systemic risk policy in the insurance sector".** Building on the progress already achieved, I believe that work needs to be done on **an activities-based assessment to complement the entity approach and deal with horizontal activities and business models that may become systemically relevant in adverse market conditions.** Furthermore, the **assessment of the transmission channels should be consistent with the risk-based measures of the international capital standards.** The **design of the policy measures should consider the mitigation factors and capital requirements** eventually included in the micro-prudential regime in order to avoid loopholes or duplications.

Regarding the international capital standards, while I agree with the step by step process of incremental convergence, due to the inherent difference in valuation standards around the globe, **it is fundamental that its version 1.0 already shows concrete examples of progress on the convergent path towards the ultimate goal of <u>one</u> international capital standard, <u>one</u> ICS**.

The global nature of insurance demands a sound and robust global group solvency regime that should be applied by all jurisdictions.

To conclude,

President Juncker recently said „our European Union is, at least in part, in an existential crisis". European citizens demand concrete responses to the challenges of our time and the European Union policy makers need to deliver.

Therefore, we all are called upon to enhance our work accordingly and without delay in our respective areas of responsibilities.

Supervisors need to work together to ensure that all policyholders are protected by high-quality supervision.

Insurance and pensions products should provide adequate protection and better returns to citizens.

Consumers and companies should benefit from the full potential of the single market.

Innovation brought by the digital revolution should deliver better outcomes to citizens.

All of this work needs to be performed in a sustainable way with a clear focus on preserving stability and enhancing consumer protection.

More than words, it is now time for action!

It is time for all of us to „explore new horizons" to deliver a better Europe for our European citizens.

I am very much looking forward to follow today's discussions.

Thank you very much for your attention.