

# Public consultation on the Supervisory Statement on supervision of reinsurance concluded with third country insurance and reinsurance undertakings

Fields marked with \* are mandatory.

The European Insurance and Occupational Pensions Authority (EIOPA) published today a Supervisory Statement on supervision of reinsurance concluded with third country insurance and reinsurance undertakings. The statement aims to ensure high-quality and convergent supervision regarding insurance undertakings using reinsurance arrangements with third-country reinsurers both from equivalent and non-equivalent countries.

EIOPA invite comments on the supervisory statement and the expectations put forward there. Comments are most helpful if they respond to the question stated and contain a clear rationale.

**To submit your comments, please click on the blue “Submit” button in the last part of the present survey. Please note that comments submitted after 10 October or submitted via other means may not be processed.**

*Please clearly express in the consultation form if you wish your comments to be disclosed or to be treated as confidential.*

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## General Information

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EIOPA Insurance and Reinsurance Stakeholders Group

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Treatment of the comments provided

- Confidential
- Publicly available

## Supervisory Statement

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1. General comments on the supervisory statement

The IRSG appreciates the objective to ensure a high-quality and convergent supervision of reinsurance. However, the supervisory statement would benefit from clarity on the concrete problem EIOPA is aiming to address to avoid the risk that the consequences of this statement are disproportionate and overreaching, compared to the issues that EIOPA might be trying to address.

The draft Supervisory Statement sets out conservative expectations on NCAs and indirectly on (re) insurers, leading to additional burdens, discouraging the use of reinsurance capacity from third countries, and there is a potential risk that in the long run third country authorities impose comparable burdens on their (re)insurers, thus making the access to EU reinsurance potentially detrimental and less attractive. The impact assessment fails to consider that those elements can have social impacts in terms of affordability of insurance on the one hand, and competitive impacts of the EU-based reinsurers on the other. In so doing, the EIOPA statement may be going against the objective of the Solvency II Directive. Recital 22 of the Solvency II Directive call for a proportionate supervision of reinsurance, noting that “the supervision of reinsurance activity should take account of the special characteristics of reinsurance business, notably its global nature and the fact that the policyholders are themselves insurance or reinsurance undertakings”.

By bypassing or overriding the Art.172 equivalence decisions of the European Commission and the EU-US Covered Agreement, the EIOPA statement is threatening the effective progress made in recent years in terms of opening reinsurance markets for the benefits of the EU. The impact assessment fails to consider the negative economic and social impacts of rolling back this progress. By treating the USA (Covered Agreement) and formally (Switzerland, Bermuda) and de facto (the UK) equivalent countries the same as any third-country, it goes against the objective of the Solvency II Directive to foster greater dialogue and collaboration agreements with third country authorities. Given the global nature of the reinsurance activity, the Solvency II Directive urges the EU institutions to conclude “international agreements with a third country” (recital 89) in order to “ensure effective market access for reinsurance undertakings in the territory of each contracting party and provide for mutual recognition of supervisory rules and practices on reinsurance” (article 175). Those international agreements are meant to remove restrictions to cross-border reinsurance, such as mandatory collateral or localisation. The EU-US Covered Agreement is a successful reflection of this ambition and should serve as a template in other jurisdictions.

In any case, the supervision in third countries are likely to be guided by the IAIS’s ICPs. This means that the macro risks stemming from the use of third country reinsurance by EU (re)insurers is extremely limited. EIOPA could also focus on dialogue and collaboration agreements with third country authorities.

The statement should be reviewed to make clear and explicit that the supervisory statement does not create new requirement or supervisory expectations:

The IRSG stresses that any “good practices” that EIOPA wishes to spread through this statement should aim at phasing out arbitrary restrictions to global reinsurance to allow a greater diversification of reinsurance counterparty risk by the cedents and more capacity to be brought at a competitive rate.

While reinsurers have an important role to play in closing the protection gap, the statement may have negative implications if it leads (in)directly to a decrease in the purchase of reinsurance. Reinsurance is made possible through global diversification of risks, and without capacity sourced in the EU from third country reinsurers, the natcat protection gap would be even wider. When EU-based insurers cede risks outside of the EU, global reinsurers contribute to absorbing losses occurring in the EU. In that sense, third country reinsurance is similar to a capital injection in the EU when it is most needed, and therefore it contributes to its resilience. EIOPA’s work on addressing the protection gap cannot be considered in isolation of the supply of reinsurance capacity. Both EU-based and foreign-based reinsurance capital is needed to close the EU protection gaps, while discriminatory practices are not.

## Section 2: Context and objective

Please include any general comment you might have on this section of the statement

The statement should be reviewed to make clear and explicit that the supervisory statement does not create new requirement or supervisory expectations:

- It should systematically specify whether its recommendations to the NCAs apply to all third country reinsurers, or to a subset, and why.
- The statement should refrain from potentially encouraging practices which have no ground or are even prohibited in Solvency II for equivalent jurisdictions, such as pre-approval of reinsurance programs, collaterals, localisation of assets. These cannot be viewed as “good practices” for routine conduct of business and supervision. These are effectively impediments to the ability of reinsurers to move capital exactly where there are claims in real-time, e.g. after a natural disaster. This is detrimental to the social benefits of reinsurance while decreasing the reinsurance capacity and fostering higher rates.
- The statement should be clearer when considering who it is addressed to: while it is presented as being addressed to NCAs, and to ensure the convergence of supervision, a number of elements of the supervisory statement present recommendations consisting of expectations for undertakings, eg how undertakings should assess reinsurance agreements. In addition to creating additional burden on undertakings, this creates an undesired ambiguity in terms of addressees that should be clarified – for example by removing wording such as “undertakings are expected”.

Retroceding of risks is an important risk mitigation technique to diversify risk exposure, which enables reinsurers to manage and transform risks from primary markets effectively and efficiently while staying within the limits of their risk appetite: the wider the geographical scope of retrocession, the lower the risk of accumulation in a single reinsurer and in a single jurisdiction. Through retrocessions, EU reinsurers taking on EU-authorized insurers allow global capital to absorb losses occurring in the EU, and by doing so, contribute to an economic allocation and use of capital which benefits the region. Retrocessions are pursued by highly specialised risk professionals and therefore should be excluded from the scope of this statement.

2.1. Please include any comment you might have on paragraph 2.1. of the document

EIOPA should highlight the reasons underpinning the recognition of reinsurance equivalence in Solvency II, i. e.: limiting national restrictions to use cross-border reinsurance. Therefore, EIOPA should clarify how each paragraph of the statement is applicable to equivalent vs non-equivalent jurisdictions.

2.2. Please include any comment you might have on paragraph 2.2. of the document

2.3. Please include any comment you might have on paragraph 2.3. of the document

EIOPA should highlight that the EU-US Covered Agreement is meant to limit the restrictions to use cross-border reinsurance. Therefore, EIOPA should clarify how each paragraph of the statement accounts for the Covered Agreement. Cooperation between jurisdictions can bring significant benefits to the supervision of cross-border reinsurance, as demonstrated by the EU-US Covered Agreement.

Overall, the EIOPA supervisory statement should not threaten the implementation of the Covered Agreement, which benefits both the EU and the US (re)insurance markets, by issuing blanket expectations that do not consider its clauses and intent properly. The Covered Agreement strengthens regulatory certainty and ensures a level playing field for EU and US (re)insurers by eliminating the imposition of any local presence and collateral requirements on a company that is not based in the same jurisdiction as the primary insurer, under certain conditions. The agreement also promotes the cooperation and exchange of information between EU and US supervisors.

#### 2.4. Please include any comment you might have on paragraph 2.4. of the document

This paragraph combines different aspects: legal conditions for the authorisation of third country reinsurers to pursue business in the EU, of which there are none in Solvency II (but national provisions could apply), Solvency II conditions for the recognition of third country reinsurance in capital requirements (in particular based on creditworthiness), and the supervision by NCAs and the related observed good practices. These three aspects should be covered in different paragraphs to avoid any ambiguity.

There is a concern that national legislation might set further barriers to access markets within the EU. “Good practices” should aim at ensuring that restrictions to global reinsurance are phased out to allow a greater diversification of reinsurance counterparty risk by the cedents and more capacity to be brought at a competitive rate, not the opposite.

#### 2.5. Please include any comment you might have on paragraph 2.5. of the document

There are several instances where EIOPA made points (e.g. on collaterals or ratings) which are inapplicable to equivalent jurisdictions by virtue of the Solvency II directive but which have not been highlighted as such in the statement.

The statement should also systematically consider the implications of the Covered agreement and should not threaten its implementation..

#### 2.6. Please include any comment you might have on paragraph 2.6. of the document

The statement should focus on its primary matter (cession of primary insurers to reinsurers) and the following sentence should be removed: “however, it might be also relevant, following a proportionate and risk-based supervision and considering the specific business models, to reinsurance undertakings retroceding their risks”.

### Section 3: Assessment of the business rationale for using third-country reinsurance and early supervisory dialogue

Please include any general comment you might have on this section of the statement.

The IRSG fully agrees with the recognition of reinsurance as an efficient risk management and diversification tool as well as a capital management tool and welcomes the reminder that AMSBs are responsible for their undertakings' reinsurance strategy. The IRSG agrees that Pillar 2 risk management is an important tool in the management of reinsurance risks, and supervisory oversight of the risk management framework can play an important role in addressing failings in an undertaking's implementation of its reinsurance strategy.

Any wording that would suggest pre-supervisory authorisation is needed to purchase reinsurance should be removed. The use of third country reinsurance - or retrocession - is fully recognised by Solvency II based on certain conditions and should not require a systematic "early supervisory dialogue". Reinsurance is under the responsibility of each undertaking's AMSB and should not be subject to prior authorisation by supervisors.

3.1. Please include any comment you might have on paragraph 3.1. of the document

See above general comments.

3.2. Please include any comment you might have on paragraph 3.2. of the document

3.3. Please include any comment you might have on paragraph 3.3. of the document

The IRSG suggests to either delete this paragraph entirely or at least clarify that prior engagement is encouraged only in very exceptional cases (if (re)insurers transfer a significant amount of risk (see paragraph 3.4) or have obvious reason to believe that NCAs are likely to raise questions in the supervisory review process at a later stage). Indeed, the provisions in the supervisory statement are disproportionate and would create a heavy burden for both undertakings and NCAs.

The supervisory statement suggests that NCAs should engage in a supervisory dialogue with the undertaking "before the conclusion of the reinsurance agreement". In addition to being unlikely to be practical, it would also be counter-productive where reinsurance solutions need to be quickly implemented to expect ex ante involvement of NCAs for in each reinsurance agreement. The additional burden does not serve a comprehensive regulatory purpose. It would also create legal uncertainty for (re)insurers if they receive no or inconclusive feedback from NCAs.

3.4. Please include any comment you might have on paragraph 3.4. of the document

See above comments.

## Section 3: Assessment of the Insurance undertakings risk management system regarding the use of third-country reinsurers

Please include any general comment you might have on this section of the statement.

3.5. Please include any comment you might have on paragraph 3.5. of the document

The end of the paragraph should be deleted (“and quantified while also including a list of the most material arrangements”) and the reference should be to material risks (“that material risks associated with third country reinsurance arrangements are appropriately captured by the risk management framework”).

Risks associated with third country reinsurance should not be singled out for quantification in the ORSA, unless those risks are material to the risk profile of the undertaking. EIOPA statistics reveal that third country reinsurance plays a minor role in the finances of most EU companies. Singling out specific non-material risks in this way would lead to a loss of ownership by the undertaking of the ORSA and could deflect attention from more material risks which an undertaking could be facing.

Furthermore, insurers are required to extensively report on reinsurance strategies and treaties in QRTs S30 and S31. This reporting should not be replicated in the ORSA.

3.6. Please include any comment you might have on paragraph 3.6. of the document

Regarding point a), it should be completed by “where this is relevant given materiality and where this information is publicly available”. Materiality should be also clearly defined.

When “taking into account the different domiciles of its third country reinsurers, including also retrocession of risks to other third country reinsurers” is mentioned, it is worth noting that it may not be possible for the insurer to obtain information on the internal risk management of the reinsurer if the information is not in the public domain. The reinsurer is unlikely to be able to share confidential internal information with ceding companies.

Furthermore, the retrocession of risks to other (non-equivalent) third countries should not be subject to the same process as for cedents. Reinsurers have the competence and the professional means to keep the financial strength of their potential counterparties under constant surveillance. This applies even more to intra-group retrocession arrangements.

Regarding point b), international sanctions prohibit business relationships with certain counterparties. The risk arising from non-compliance with international sanctions is limited to an inadequate monitoring of sanction lists. The IRSG does not see the rationale of performing a special risk assessment nor a particular relevance of the issue for third country reinsurance assessments.

3.7. Please include any comment you might have on paragraph 3.7. of the document

The IRSG recommends deleting the reference to potential “special areas” to be considered in case of liquidation and bankruptcy of the third country reinsurer as it is unclear what EIOPA has in mind here.

It is not proportional to expect all insurers to perform a full analysis of the legal framework in specific third countries. This would also fall outside of the remit of the undertaking – instead, it would be beneficial if supervisory authorities would provide a list of the jurisdictions aimed at.

While we recognise that (re)insurers should understand the consequences of potential insolvency, winding-up procedures or recovery and resolution mechanisms, paragraph 3.7 inaccurately implies that the selection of third countries is dominated by enforceability considerations. The undertaking should focus its analysis on the qualitative elements of the relationship, such as: well-established reinsurer, geographical risk diversification, proven willingness to pay, fair behaviour, adequate governance, etc.

In addition, EIOPA should refer to the enforceability of collateral provisions in the countries which accept the majority of third country retrocessions (namely the US and the UK) and for countries which have been deemed equivalent under article 172 of the Solvency II Directive. This is even more necessary as § 2.5 makes it clear that “when relevant only to reinsurance arrangements with third country reinsurers from non-equivalent countries, this is explicitly mentioned in the text”.

It appears that this paragraph applies to reinsurers in equivalent jurisdictions and to the extent that this sets additional requirements for reinsurers in those jurisdictions, it seems to be in contradiction with Articles 172 (3) and 173 of the Solvency II Directive. Please refer to the general comments about the need for the supervisory statement to appropriately differentiate between different types of jurisdictions.

In addition, Member States shall not require pledging of assets to cover unearned premiums and outstanding claims provisions where the reinsurer is a third-country insurance or reinsurance undertaking, situated in a country whose solvency regime is deemed to be equivalent in accordance with Article 172.

3.8. Please include any comment you might have on paragraph 3.8. of the document

EIOPA should not address the issue of collateral in a way that can be understood as a promotion or encouragement of collaterals, whether potential or even mandatory.

In fact, this would be a step back from all the discussions around collateral between the EU and the US that led to the removal of collateral requirements as part of the Covered Agreement. Such a bold statement on collateral would be an unfortunate message given by the EU to the global supervisory community, with a significant risk of backfiring against EU players.

The separate chapter on collaterals suggests that EIOPA sees collateral as a regular and commonly used tool in the supervision of third country reinsurance arrangements. This perception does not reflect the reality in the EU.

3.9. Please include any comment you might have on paragraph 3.9. of the document

3.10. Please include any comment you might have on paragraph 3.10. of the document

3.11. Please include any comment you might have on paragraph 3.11. of the document

Please refer to comments to 3.7.

3.12. Please include any comment you might have on paragraph 3.12. of the document

3.13. Please include any comment you might have on paragraph 3.13. of the document

3.14. Please include any comment you might have on paragraph 3.14. of the document

3.15. Please include any comment you might have on paragraph 3.15. of the document

The wording should be reviewed to clarify that the rating is only relevant for the recognition of reinsurance arrangements with third country reinsurers from non-equivalent jurisdictions (underlined wording to be added in the paragraph), in accordance with Art.211 of the Solvency II Delegated Act.

3.16. Please include any comment you might have on paragraph 3.16. of the document

### Section 3: Assessment of the reinsurance agreement

Please include any general comment you might have on this section of the statement.

3.17. Please include any comment you might have on paragraph 3.17. of the document

The wording of the paragraph should be changed to reflect that different elements may be considered as part of good risk management, depending on the specific case under consideration, and para 3.18 should be redrafted to say “In such an assessment insurance undertakings may consider”.

Paragraph 3.17 invites undertakings to assess their reinsurance contracts’ compliance with articles 209-211 of the Delegated Act, as part of their reinsurance risk management. However, the points listed in 3.18 include elements which are not specified in Articles 209-211 of the Delegated Regulation.

For example, the recognition of the reinsurance contract only depends on whether collateral is in place if the third country reinsurer is not rated. Similarly, there is no requirement for a termination clause for recognition of a reinsurance contract.

As for external reinsurance and retrocession, intragroup reinsurance and retrocession allows insurers and reinsurers to manage and diversify their risks efficiently. Restrictions on cross border reinsurance transactions, either external or intragroup, would reduce underwriting capacity and make insurance more expensive.

3.18. Please include any comment you might have on paragraph 3.18. of the document

Please refer to comments to 3.17 and 3.6.a. Downgrade only plays a role in the recognition for reinsurance from a non-equivalent jurisdiction – this should be made clear (for instance with this precision: “such as the breach of the local solvency requirement or a material deterioration of the financial situation of the third country reinsurer (including its downgrade for non-equivalent jurisdictions)”. Furthermore, an insurance undertaking is generally not informed of retrocession arrangements by its reinsurers, which is a confidential contractual information.

3.19. Please include any comment you might have on paragraph 3.19. of the document

3.20. Please include any comment you might have on paragraph 3.20. of the document

### Section 3: Tools to mitigate any additional risks

Please include any general comment you might have on this section of the statement.

3.21. Please include any comment you might have on paragraph 3.21. of the document

We suggest to replace “(or be requested by the NCA)” by “(or be recommended by the NCA as part of the supervisory dialogue with the undertaking)” as EIOPA supervisory statement should not pre-empt the content of the dialogue between the NCAs and the undertakings.

## Part II: Impact assessment

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Please include any comment you may have on Section 1.1. Procedural issues and consultation of interested parties

Please include any comment you may have on Section 1.2. Problem definitions

Please include any comment you may have on Section 1.3. Objective pursued

The concept of “good practices in supervision implemented by some NCAs” is very subjective. As explained above, there are some significant differences between domestic markets in the EEA, and requirements can also vary based on the lines of business. Therefore, it seems difficult to suggest “one fits all” solutions for an entire market, with the same level of efficiency in all sectors.

Please include any comment you may have on Section 1.4. Policy issue and options

The impact assessment should mention that the benefit of this supervisory statement is limited. It is noted in §1.16 of the impact assessment, for the total European market reinsurance with reinsurance undertakings from third countries represent 35,15% of total recoverables, out of them 16,76% for reinsurers from non-equivalent third countries.

As shown in Graphic 2, most of these exposures concern the UK and the US, whereas exposures to other third countries tend to be very limited and even “non material” to quote EIOPA (1.24). The same is also true for EU reinsurers (Graphic 3). This means that the quasi entirety of EU (re)insurers’ purchase of third country reinsurance comes from reinsurers considered, legally or de facto, well-regulated and well-supervised.

Please include any comment you may have on Section 1.5. Evidence

Please include any comment you may have on Section 1.6. Comparison of options

Please include any comment you may have on Section 1.7. Conclusion

General comment

The impact assessment fails to consider the potential negative implications of the supervisory statement if it leads directly or indirectly to a decrease in reinsurance purchase by EU insurers. The economic benefits of cross-border reinsurance for needs to be highlighted as well as the importance of phasing out restrictions to global reinsurance to increase the take-up rate of reinsurance.

When EU-based insurers cede risks outside of the EU, this means that the world contributes to absorbing losses occurring in the EU. Access to global capital will help to insure peak risks in the EU.

Please refer to the above comments on the implications of the EU-US Covered Agreement. Threatening the implementation of the Covered Agreement, which benefits both the US reinsurers doing business in the EU and the EU reinsurers doing business in the US, would be highly detrimental to the European insurance sector.

## Submission of Comments

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