

From Brussels with Love: A Perspective on Developing Insurance Regulation at the EU Level

Karel van Hulle

Head of Unit, Insurance & Occupational Pensions

Director-General Internal Market, European Commission

Summary

- The author provides some personal reflections on the issues facing the post-financial crisis insurance market, and the responses with the European financial regulatory architecture. He also summarises some principles underpinning insurance regulation at the EU level.
- The main focus of insurance regulation has been consumer protection, stemming from the argument that public trust and confidence in financial markets is key to financial stability. The need for a level playing field across financial markets, and the importance of recognising differences across member states are also fundamental in the process.
- Balancing costs and benefits of regulation are always central in policy development. At the same time, regulation must balance three tenets: it must be proof against possible future market developments and innovations; proportionate to the costs of compliance in the here and now; and mindful of the purpose of the regulation in the first place.
- Public consultation are the watchwords in regulatory development, and this now rings true at the European as well as any other level. Undertaking formal consultation at various stages, and creating the conditions for stakeholder feedback both individually and collectively is important not just from a political or technical standpoint. They also educate both consultant and consultees on the underpinning issues and motives.
- The author then discusses the recent progress of some of the specific briefs on the EU insurance regulatory agenda: Solvency II, Review of the Directive on Institutions for Occupational Retirement Provision, the Insurance Mediation Directive review, and Packaged Retail Investment Products.

The Chartered Insurance Institute is the world's largest professional body for insurance and financial services and is the leader in awarding qualifications to industry practitioners. Our Thinkpieces are a key part of our ongoing commitment to promoting innovative thinking and debate within the insurance and financial sectors. In 2012 we are celebrating our Centenary as a Chartered body.

This article reflects the personal opinions of the author and should not be interpreted as the opinions, views, or policies of the European Commission, or those of the Chartered Insurance Institute or its members. Mr van Hulle has asserted his right under the Copyright, Designs and Patents Act 1988 to be identified as the author and copyright owner of the text of this work, and has granted the CII worldwide perpetual licence to reproduce and distribute it in whole and in part. We welcome suggestions from potential contributors, but we are also seeking feedback from our readers. We urge you to get involved—especially as we intend some of our articles to be open to rebuttals for publication.

CII Introduction: with Solvency II implementation at the forefront of the agenda, the European Insurance & Occupational Pensions Authority (EIOPA) now firmly in place, and some key reforms imminent governing insurance distribution, the EU insurance regulation landscape is more relevant to individual firms than ever before. In this rare and special opportunity, Karel van Hulle, the European Commission's lead official on insurance & occupational pensions, and author of many of the regulatory proposals under discussion in these areas, offers his own strictly personal view of insurance regulation in the post-financial crisis world. This article should be read in conjunction with our other Thinkpiece by Mr Gabriel Bernardino, Chairman of the new European Insurance and Pensions Authority.¹

A starting point to any discussion on insurance regulation must be the initiatives at the global level following the financial crisis. The International Association of Insurance Supervisors (IAIS) has been working to develop a global approach to insurance supervision, of which a part is to define a global Systemically Important Financial Institution from an insurance perspective.

These tasks have been challenging because unlike the banking regime which has a global regime on risk-based capital in the form of the Basel Committee, insurance has not seen such harmonisation. The result is big differences in capital standards, group supervision, and regulatory treatment, all of which does not bode well for firms operating globally.

Developing Regulation at the EU Level

In the light of this global backdrop, the primary purpose of EU regulation is to create certainty for firms operating within and across the various member states. The drafting of such pan-EU rules must encompass several key principles.

Consumer protection must be paramount

Consumer protection has been the main post-financial crisis focus of EU regulation. The close link between consumer protection and solvency rules will be obvious to anyone in the industry. I would go so far as to say that lack of consumer understanding of financial products and risks was one of the causes of the financial crisis. Financial stability is linked to consumer confidence, so addressing

¹ See Gabriel Bernardino (Chairman of EIOPA), [Converging Ideas: Building a Europe-Wide Supervisory Culture in Insurance and Pensions](#), CII Thinkpiece no.75 (May 2012). Available from www.cii.co.uk/thinkpiece

consumer understanding, and therefore trust and confidence of financial markets is the key to improving financial stability.

Equivalence, not duplication

Developing EU-level regulation that improves trust and confidence must balance two important principles. First, it must create a level playing field across the financial markets. In this respect, the concept of equivalence applies: the intention is not to develop an approach that everybody must follow. Instead it is to respect differences in approaches among 27 member states. Equivalence does not mean duplication.

Lack of consumer understanding of financial products and risks was arguably one of the causes of the financial crisis. Addressing consumer understanding, and therefore trust and confidence of financial markets, is the key to improving financial stability.

Some have worried that European institutions work to sweep away national rules in favour of a pan-European rulebook. In fact, the key to developing European-level financial regulation is to examine not the form but the substance of the national rules we are trying to converge. In the process we try to learn from each other the most efficient approach to regulating the industry. Rather than export national rules, it is about creating a level of regulatory certainty and efficiency in a world where more firms operate cross-border.

Better, future-proof regulation

The second important principle that applies to financial regulation is the need for longer-term thinking. It cannot be focused on the next fiscal period, or even the next election.

Regulation must take into account both the benefits to society and costs of compliance. We cannot under-regulate simply because of perceived cost of implementation. People tend to forget the financial crisis and all its costs. It took just a few poorly-managed firms to cost the world economy billions. Yet when markets recover, industries complain about being hamstrung with regulation, and call for a lighter-touch approach to spur growth. We must be vigilant of that: people are not always ready to recognise the problems, and forget that actions come with risks. The cause of the next financial crisis

might not necessarily be like the last one, but we still have to learn the lessons.

Allied to this is the better regulation agenda, to which the work of member states including the UK have been very helpful. Practices such as impact assessments and regular stakeholder consultation are now commonplace. In fact, we now get complaints that we consult too much.

We have learned a great deal, and the more effective the public consultation, the more we will learn about the nuances of the responses, including the motivations behind them. We try to meet with stakeholders, through both public hearings which we find very effective, but also on an individual basis, not just the large firms but the small local players as well.

The more effective the public consultation, the more we will learn about the nuances of the responses, including the motivations behind them. We have learnt that meetings with stakeholders are most effective at the earliest stage of the policy development process.

We have learnt from these meetings that they are best held at the earliest possible stage of the policy development process in order to understand the various points of view, before negotiations begin. We try to separate the arguments from the motivations, and prioritise the issues with a view to creating the closest we can get to a universally beneficial solution.

Liaison with EIOPA

A vital component in the development of EU regulation is convergence in the post-regulation supervisory stage. In January 2011, the European Insurance & Occupational Pensions Authority (EIOPA) came into being, and this was a significant step from the committee of supervisors (CEIOPS) that it replaced. This supervisory architecture allows national supervisors to work together and learn best practices that overcome the procedural, cultural and traditional barriers that still exist. It includes peer reviews to help maintain good co-operation between the supervisors.

The major change with the advent of EIOPA is its authority status, and these changes have been reflected in its working relationship with us at the European Commission. Directorate-General Internal Market & Services is represented in EIOPA's work, and we frequently consult with each other on supervisory and regulatory best practices.

Principles versus rules

Should European law be principle- or rule-based? Such debates about the amount of detail of EU-level regulations often arises in discussions be they at consultation or parliamentary committee stage, especially given that the dividing line between the technical and the political often gets very blurred. We had agreed that we wanted to have principle based legislation, and that Lamfalussy Level 2 would be delegated to the Commission while Level 3 would be dealt with by the supervisory authorities. However I certainly observe that people are starting to question that distinction.

Specific Insurance Initiatives

Insurance Guarantee Schemes

The White Paper on Insurance Guarantee Schemes was put out for consultation, and we have still not completely decided on the way forward. Do we need a Europe-wide system of insurance guarantee schemes? Fortunately in insurance we have had very few cases of insolvency. Should we now mount up a regulatory system? These issues are still outstanding and we intend to address them in due course.

Review of the Directive on Institutions for Occupational Retirement Provision

This is a subject of some debate and we recently ran a public hearing. The Commission does not want a one-size-fits-all approach. When you use the words 'pension fund' in the UK, please, when you talk about the German pension fund, consider that this is a different vehicle. The way they operate is different, and we need to take that into account. We also do not want to – as some people say – “copy and paste” Solvency II into pension funds. To the extent that pension funds are different from insurance companies you have to take account of that fact. It is probably not so much the institution but the products. The pension promise may be very different from an insurance contract. Therefore the solvency rules of the institution that is selling these products should, logically, be different. This is some of the logic that we have in mind.

Solvency II

There is much to discuss on Solvency II, and such a detailed discussion is not within the scope of this article.

However I will say that it is an important issue not just for Europe but the global insurance markets. We need a risk-based solvency regime in the interest of the insurance industry and its customers, and Solvency II is essential for European insurers, but should also provide a blueprint for a risk-based solvency regime for other regions as well. Such a regime allows insurance products to be better priced and if all economies in the world signed up to this approach, we would have achieved a level playing field.

Insurance Mediation Directive Review

There are no simple insurance products that I know of, which is why I think intermediaries have an important role to play. We are planning an amendment of the Insurance Mediation Directive to ensure the same rules to apply to everyone who sells insurance products: extending the scope of application from intermediaries to direct writers. We want to have more transparency, clarifying the relationship between the intermediary and the insurance company, and providing more disclosure about the intermediary's remuneration.

Packaged Retail Investment Products

We want a specific regime for Packaged Retail Investment Products where we want to apply the MiFID rules. Facilitating cross-border business: we are trying to find some answers to all the discussions we have had over the years between home and host supervisors when people cross borders. The debate has spanned the following:

- should all sales of insurance products be covered by the directive?
- what kind of disclosures should there be concerning remuneration: direct disclosure or on request?
- should MiFID rules apply to insurance PRIPs, and indeed some people say to all insurance products?
- how can we avoid excessive complexity in the rules?

We intend to publish a proposal in May 2012.

Health Insurance and Pensions

We have a lot of questions today about health insurance. People sometimes talk about pensions – not always, and probably too little. It is very funny, people say it is a challenge, a problem, that people get so old. I think it is fantastic, but people say it is a problem! When people grow old they go to the doctor more often and they go to hospital, so we have to find ways to deal with the costs of that. For the insurance sector, one of the challenges is to find good health insurance products.

We should realise at some stage that we have huge liabilities for the future of pensions. If we want our children and grandchildren to retire at the age of 80 there will have to be some money for them. That is an issue that maybe we older people tend to forget.

Not everything can or should be regulated

In conclusion, I honestly believe in the statement that not everything can or should be regulated. Finding out what needs to be regulated is a huge challenge for the regulator. That is why the approach we are trying to follow – which we call the better regulation agenda – is based on a strict discipline of consulting before acting. That will in the end convince us whether or not we need to regulate and to what extent we should regulate on a rules based or principles-based approach. There will never be good regulation unless the people who in the end will be regulated feel they have played a part in developing those rules. That is what I wish there to be at the EU and national level.

If you have any questions or comments about this Thinkpiece, and/or would like to be added to a mailing list to receive new articles by email, please contact us: thinkpiece@cii.co.uk or by telephone: +44 (0)20 7417 4783.

This article is loosely based on a presentation by Mr Karel van Hulle to the Insurance Institute of London at Lloyd's of London on 8 March 2012. A podcast of his speech is available [here](#), or by searching www.knowledge.cii.co.uk.



Karel Van Hulle has been Head of Unit at the European Commission (EC)'s Insurance and Occupational Pensions Unit since 2004, and has led the development of EU-level regulation for the life and non-life sectors including Solvency II, Occupational Pension Funds, and Insurance Mediation. He is a lawyer by training, and worked for 8 years at the Belgian Banking Commission before joining the EC in 1984. Prior to taking up his present role, he served as Head of Unit for Accounting Standards, later Financial Reporting & Company Law, and most recently Accounting & Auditing.



Qualified CII members: reading and reflecting on this Thinkpiece can count as *Structured CPD* under the CII CPD Scheme. To help you with this, we have published a set of Learning Outcomes and Reflective Questions linked to this article. Click here or copy to your browser: www.knowledge.cii.co.uk/system/files/TP74_Reflective_Questions_0.pdf