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INTERNATIONAL AFFAIRS

World class

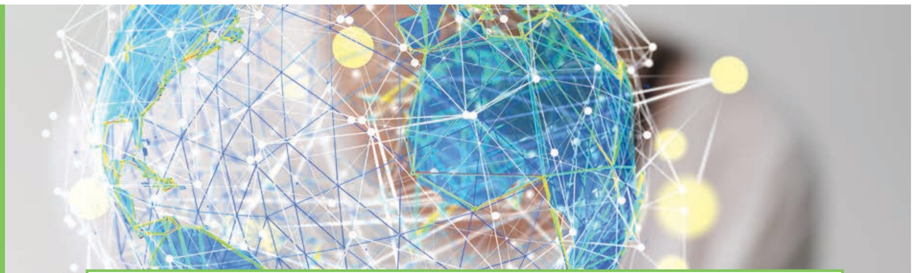
Insurance Europe has been working to preserve the international success that is the European (re)insurance industry

Insurance and reinsurance are global businesses, and European (re)insurers are an international success story. Today, around a third of all internationally active insurance groups are headquartered in the EU, and Europe is the global leader in reinsurance, writing around half of the world's reinsurance business (see table on p28).

In a tough and fast-changing world, Europe's (re)insurers therefore need the right EU regulatory environment and international agreements to allow them to maintain their competitiveness on the world stage. Over the last year, Insurance Europe has continued to engage strongly with the IAIS on its long-running project to create a global insurance capital standard (ICS) while also, within Europe, urging the new European Commission to support the competitiveness of European insurance companies on the global stage (see box on p29).

Testing the ICS

As planned, the IAIS adopted the second version of its ICS in November 2019, ready for five years of monitoring and comparability assessment. The five-year monitoring period began in January 2020, during which the ICS will be used by internationally active insurance groups (IAIGs) for confidential reporting to their group-wide supervisors, discussion in supervisory colleges and further analysis by the IAIS.



"Europe is the global leader in reinsurance, writing around half of the world's reinsurance business."

European reinsurers assume a large proportion of global risks

Reinsurance-ceding region	% assumed by Europe
Africa, Near & Middle East	96.7%
Europe	93.4%
Latin America	78.5%
Asia & Australia	77.5%
North America	15.8%

Source: Data from IAIS Global Insurance Market Report 2019

At its adoption, the IAIS clarified some important issues that had been raised by Insurance Europe. For example, it made clear that the purpose of the five-year period is to monitor the performance of the ICS over time and not the capital adequacy of IAIGs. This means that the ICS results will rightly not be used to trigger supervisory action. In addition, the IAIS acknowledged that ICS 2.0 is only one milestone in the long process of creating a global standard that achieves substantially the same outcome across jurisdictions.

The IAIS also committed to using the monitoring period to correct flaws in ICS 2.0. The European insurance industry agrees that more time and effort are needed to improve the ICS. For Europe's (re)insurers, the discussion is closely linked to similar discussions on its Solvency II regulatory framework that either took place ahead of finalising Solvency II in 2013 or are taking place now as Europe works to address certain flaws (see Solvency II article on p23).

Internal models are essential

One cannot ignore the fact that while the technical design of the ICS is similar to that of Europe's Solvency II, it is not identical to it. For example, while the ICS does include the option for groups to use their own internal models rather than a standard formula for calculating their regulatory solvency capital requirements, these internal models are not yet recognised as a key and permanent part of the standard, as they are in Solvency II.

Internal models are a key risk management and capital measurement tool and a fundamental part of the total Solvency II framework. Without such internal models, the framework would have been developed in a different way, since they allow the target capital to be set at the very high 99.5% level while keeping the standard formula relatively simple. They also ensure that even complex risks can be correctly measured.

As with Solvency II, internal models are necessary for the ICS to work in practice by ensuring the correct measurement of more complex risks and structures not addressed by the standard method. In Europe, they have already proved to be of significant benefit to supervisors. Including them as a permanent and integral element of the global framework is a key priority for the European industry.

Long-term business requires attention

Similarly, ICS 2.0 requires improvement in the way it treats long-term business. This issue has been acknowledged by a number of IAIS members. Unsurprisingly, the topics under discussion at the IAIS in this area are similar to those in

Promoting Europe's global competitiveness

Insurance Europe supports the stated ambition of the European Commission to promote Europe's competitiveness on the global stage. Indeed, maintaining a globally competitive EU (re)insurance industry is one of the four ambitions set out in Insurance Europe's January 2020 publication "Ambitions for Europe".

Insurance Europe, together with a group of EU financial services federations, wrote to EC President von der Leyen in March 2020 to express support for the EC's ambition and to ask the Commission:

- To explicitly include the global competitiveness of European businesses as a key objective in policymaking.
- To give priority to ensuring a level international regulatory playing field, with a focus on eliminating the potential for regulatory arbitrage between Europe and other jurisdictions arising from significant divergences in regulatory and supervisory approaches.
- To rigorously implement the EC's "one in, one out" approach to new regulation in order to avoid the increasing regulatory overload and compliance burden on the EU financial services industry.

In its response, the EC recognised the "utmost importance" of a robust, well-regulated and competitive financial sector for the European economy.

Solvency II, namely the valuation of long-term business, the calibration of capital requirements for long-term assets and the design and calibration of the margin over current estimate (which is a concept similar to the Solvency II risk margin). As Europe is currently working to improve these areas during its Solvency II review, similar discussions will likely take place at international level, where a number of European supervisors are engaged.

The European industry ultimately has similar objectives for the ICS as it does for Solvency II. Given the impact that prudential rules have on insurers' business models and investments, it is key that the ICS does not:

- endanger the availability and raise the cost of products that are highly valued by consumers;
- threaten the ability of insurers to continue to invest in long-term economic growth; or,
- create macroprudential and financial stability risks, including pro-cyclical investment behaviour.

This is why Insurance Europe believes that the technical elements of the ICS should in fact be tested against broader macro-economic and social objectives, such as the availability of long-term savings products and long-term investment in the economy. The IAIS should make sure that the ICS works well and does not hamper these macro objectives not only during normal times but also during times of significant stress on financial markets.

The COVID-19 pandemic has been a prime example of a global crisis triggering enhanced exchanges between supervisors in different jurisdictions. As the ICS aims to create a "common language" to assess risks and levels of solvency, this language should be calibrated for both normal and exceptional economic circumstances.

Consistent implementation is key

Equally important for Europe is that the ICS does not create competitive disadvantages for European (re)insurers vis-à-vis other jurisdictions. Given that it is likely that one third of the IAIGs that must comply with the ICS are headquartered in the EU, the coming years will be crucial in the efforts of IAIS members to agree on a global standard that works for Europe.

Yet, looking ahead, it is difficult to be confident about future developments in the political and regulatory landscape. If the relationship between the ICS and Solvency II does not develop as the European industry hopes, then the ICS should be considered for implementation in Europe only if all major jurisdictions commit to implementing it consistently. This is the only way to guarantee a level global regulatory playing field for the European industry.