Annual Report 2019–2020

insurance europe

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Glossary

EC	European Commission
EIOPA	European Insurance & Occupational Pensions Authority
ESAs	European supervisory authorities
IAIS	International Association of Insurance Supervisors
NGOs	non-governmental organisations
OECD	Organisation for Economic Co-operation & Development
SMEs	small and medium-sized enterprises
UN	United Nations

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Foreword

Andreas Brandstetter
President

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Director general

Insurance is built on "What if?". Insurers and reinsurers think not only the thinkable but also the unthinkable, seek to measure the unthinkable's size and likelihood, and then look for ways to deal with it.

(Re)insurers were modelling the risks of passenger planes hitting skyscrapers long before the terrorist attacks of 11 September 2001 and they have been studying the risks of global pandemics for decades. "The pandemic threat is a question of when, not if," said broker Aon in a publication on pandemic influenza back in 2005. Products offering cover for insurable aspects of pandemic risk have therefore been on offer, although customers weighed the likelihood of the risks against the high cost of insuring them and largely chose not to buy the policies.

So, while a global health threat did not come as a surprise to the European insurance industry when COVID-19 began its spread, what was not predicted was the commendable willingness of governments to impose stringent lockdowns to protect lives and prevent health systems becoming overwhelmed. That immense humanitarian effort has also led to widespread disruption to global businesses, trade and societies. As we write, in late August 2020, it is still too early to assess all the impacts of the global recession we are now entering.

Like all sectors, the insurance sector has been affected by the pandemic and the measures to contain it. The impact is not only in terms of claims — in non-life business lines such as travel, event cancellation, business interruption, credit and mortgage, as well as in mortality in life insurance — but also on the value of insurers' invested assets and from likely falls in new business volumes as recession bites. It is too soon to put a reliable figure on the full impact on the insurance industry, but the solvency ratios of European insurers — which were strong pre-crisis — remain healthy, ensuring they can continue to support their customers and the economy.

What is clear, though, is that the insurance industry cannot cover the enormous economic costs to businesses of such widespread lockdowns. Indeed, the sums already injected by governments to support businesses far exceed the entire market value of the world's listed insurers. Business interruption risks due to the pandemic were therefore not included in almost all insurance policies. This also means, of course, that customers were not charged for such risks in their premiums and insurers did not set aside reserves for them.

And now, how are we starting to move on? Firstly, there is now clear political will to find ways to manage the risks of future pandemics, and the insurance industry is playing its part in supporting those efforts. Europe's insurers, like their global counterparts, are providing risk management expertise and ideas to policymakers. You can read about this work in the article on p10.

Secondly, such a huge global event has brought home to many the need for protection for a whole variety of risks, so it is likely that awareness of risk management and insurance will rise. However, the questions over what elements of pandemic risk are covered by existing policies have revealed that much work still needs to be done to ensure that customers understand the products they buy. Europe's insurers must rise to this challenge.

Insurance Europe and its members will build on their existing financial literacy initiatives (see p43) and are seeking improvements to the key information document for consumers in the EU PRIIPs Regulation (see p46). We will continue to call for product information requirements that are thoroughly tested on consumers and result in clear, user-friendly documents. And it is clear that customers need more help and encouragement to consider and compare cover and services, and not only price, when choosing a financial product.

Even while the pandemic continues, efforts are underway on recovery efforts and insurers are helping to "build back better". Building resilience has long been a mantra for our industry, and Europe's insurers have a proud history of working with governments and other stakeholders to mitigate and prepare for, say, the increasing physical damage resulting from changes in climate or, more recently, the possibility of crippling cyber attacks.

And insurers have their own initiatives to stimulate behavioural changes to reduce risk; take for example the insurers that help clients reduce their potential exposure to cyber incidents or offer lower premiums to property owners who make their buildings more resilient to flooding.

The European insurance sector is also committed to investing sustainably, so it fully supports economic recovery plans and actions that are aligned with the EU sustainability and Green Deal objectives. We likewise remain committed to supporting the wider objectives set by EU policymakers in initiatives such as the capital markets union and the digital strategy. Insurance Europe's actions and positions in all these areas are covered in this Report.

Last but by no means least, for Europe's insurers to be able to support EU and national recovery efforts, the base prudential regulation for insurers must be fit for purpose. Insurance Europe is providing its technical expertise and market experience to policymakers to ensure that the current review of Solvency II (see p23) results in a regulatory framework that makes that possible.

Many questions remain about the shape of the post-COVID future. What is certain is that insurers, with their vast "What if?" experience, will help provide the answers.

Michaela Koller
Director general, Insurance Europe

COVID-19 PANDEMIC

Insurance in the time of corona

Europe's insurers have been active and innovative in their support for customers and the economy

In early 2020, the COVID-19 virus spread to virtually every corner of the globe. As this Annual Report went to press, it had infected over 23 million people and taken over 800 000 lives.

The economic impact of the pandemic has likewise been widespread and devasting, as lockdowns and quarantines have curtailed or stopped business and social activity for many weeks. That economic fall-out will be felt for years to come. The OECD was already forecasting in June that global growth could fall by 6% in 2020; even more with second waves of the virus.

Continuity & flexibility

Europe has been badly affected, albeit to different levels in different countries. In late June, the International Monetary Fund predicted a 10.2% contraction of the eurozone economy in 2020, while two weeks later the European Commission forecast that the economy of the 19-country zone would shrink 8.7%.

Europe's insurers, who have a long history of serving their customers during adverse events, showed that an event on the scale of the COVID-19 pandemic was no exception to their ability to continue operating. Despite national lockdowns and movement restrictions, insurers have maintained business continuity across the continent — often by the smart use of digital tools — while still taking all the required precautions to minimise customers' and employees' exposure to the virus.

Just three examples of many European insurer actions

The French insurance industry has pledged over €3bn in exceptional measures: €1.75bn of non-contractual measures to support small businesses, specific business sectors and medical staff affected by the crisis, and a €1.5bn global investment programme to support economic recovery.

Over 100 Spanish insurers joined together to provide complimentary life insurance and a subsidy for hospitalisation for medical staff treating patients with COVID-19.

Germany's trade credit insurers formed an emergency alliance with the federal government to maintain global supply chains and support Germany's export sector during the pandemic.

Europe's insurers and their associations have kept customers informed about virus-related issues by creating dedicated portals and websites and engaging in targeted communications. At European level, Insurance Europe did the same, creating a section of its website dedicated to frequently asked COVID-19 questions. And many insurers have taken steps to alert customers to the increased risk of fraud, and of online fraud in particular.

Insurers' day-to-day focus throughout the pandemic has been on responding fairly and responsibly to their customers and on offering flexibility to those most adversely affected by COVID-19 or the lockdowns. Often on a case-by-case basis, insurers have agreed delays in premium payments for a variety of policies and periods, depending on the national situation and individual needs. Switching between tariffs and allowing policy cancellations and suspensions has likewise been permitted where possible and appropriate. Insurers have also been flexible over the practical consequences of the crisis — taking into account that customers might not be able to fulfil certain contractual obligations, such as submitting paper documents, submitting claims by a certain deadline or renewing tests, certificates or licences.

Support & assistance

European insurers have taken many — and extremely wide-ranging — additional steps to support their customers, society in general and the economy, both at the height of the pandemic and as countries started moving to recovery from it. These actions have been tailored to the severity of the virus and lockdown measures in different areas, as well as to the differing local role of insurers that results from variations in national social security, unemployment and health systems (see box above for just three examples).

The industry's nationwide and company-level voluntary goodwill actions have spanned three areas.

- Insurance premiums or contracts, including:
  - Offering temporary extension of cover and services beyond contractual obligations, for example providing free health cover to medical staff.
- Support for the economy, including:
  - Participating in government-backed trade credit schemes to ensure commercial supply chain continuity.
  - Making swifter payments to service providers.
  - Mobilising long-term investment capacity to support customers and the wider economy by accelerating recovery and boosting growth.
- Non-insurance initiatives, including:
  - Donating medical equipment.
  - Contributing financially to charities, public health bodies and health research initiatives.
  - Amplifying government health messages.

A commitment to best practice

In late May 2020, the European Commission brought together consumer and business representatives and financial services industry organisations, including Insurance Europe, to discuss the COVID-19 relief measures offered to consumers and businesses by insurers, banks and non-bank lenders. As a follow-up to those discussions, the Commission drew up a set of best practices to facilitate the implementation of convergent temporary relief measures, where relevant and required. They were published in July 2020.

Insurance Europe and its members endorsed the EC's best practice recommendations for insurers, which very much reflected the actions that the European insurance industry had already been taking since the start of the COVID-19 outbreak in terms of treating customers fairly and flexibly.

Every insurer's first duty is, of course, to ensure it can honour its promises to its customers, both now and in the future. This means prudent management of its capital, particularly during times of economic turbulence. All the goodwill actions of insurers, therefore, have been developed taking into account their financial capacity. For that reason, it is important that solidarity actions that go beyond contractual commitments remain voluntary.

Impact on insurers

Of course, the insurance industry itself has not been untouched by the effects of this vast global crisis. Estimates for the total global claims on (re)insurers as a result of the pandemic still vary considerably and it will be some time before the final figures are known. Currently, the claims remain manageable for the industry — indeed, a global pandemic is one of the many test scenarios that (re)insurers use to assess their resilience. (See next article on p10 for more on pandemic cover and future solutions.)

Insurers have also seen falls in new business as a result of decreased economic activity, while at the same time facing even lower interest rates and hits on investment income on the asset side of their business as a result of the economic disruption (although by mid-2020 investment markets were already showing signs of recovery). Nevertheless, as the IAIS stressed in March 2020, globally "insurers are generally well capitalised with sophisticated risk management capabilities".

Within Europe, the industry has remained strong and EIOPA stated in March that the "the sector is well capitalised and able to withhold severe but plausible shocks to the system". Good risk and capital management is core to the insurance industry and the European regulatory framework sets consistent, high standards across Europe and has built-in mechanisms to ensure that companies can cope with crisis periods and extreme events (see Solvency II article on p23).

Insurance Europe's active engagement

At European level, Insurance Europe has been engaged on four fronts since the very start of the pandemic. It identified challenges emerging across markets; working closely with its members in the national markets and other industry groups to build up a picture of the developments affecting insurers and their clients to see if there were areas in which European coordination of action by national authorities was required. It also provided a platform for its members to share best practices; raising issues and sharing solutions to the challenges the industry faced.

Thirdly, it has been discussing solutions for future pandemics; working to explore how insurers can best engage with

Supervisory advice on dividend payments

Insurance companies recognise the importance of dividends to their shareholders, who often include pension funds that need dividends to meet their commitments to pay pensions. Insurers also recognise the need to ensure their own financial strength for the benefit of their customers, especially in times of uncertainty.

Companies set their dividend policy and make dividend decisions very carefully, taking into account their solvency levels, business plan, risk profile and risk appetite, as well as any significant events that could have a material impact, such as COVID-19. Solvency II requires that they do this and that they include it in their own-risk and solvency assessment (ORSA), where they must ensure their solvency will remain strong for the next three to five years, taking into account their business plans and expected dividend payments. Solvency II also provides for a suspension of dividends if a company's solvency capital requirement (SCR) is breached or if the distribution of dividends would lead to non-compliance.

Given the requirements in Solvency II and the overall strength of the insurance industry, a blanket ban on dividends by supervisors is not necessary or appropriate. Instead, a case-by-case approach in line with the strong, risk-based Solvency II framework is the right approach to any dividend restrictions.

national and European authorities to increase resilience (see next article).

Lastly, Insurance Europe has been liaising very closely with EIOPA, the Commission (see box opposite) and — latterly — MEPs in the European Parliament to ensure a clear understanding of developments in national markets and to provide feedback on the responses coming from supervisors. Insurance Europe appreciated EIOPA's statements in March and April 2020 underlining the strong solvency position of the industry and acknowledging the various steps insurers had been taking to show flexibility to their customers.

Insurance Europe also welcomed the fact that EIOPA highlighted that imposing on insurers retroactive coverage of claims not envisioned in contracts could create solvency risks and threaten policyholder protection and the market's stability. It was also positive to see EIOPA acknowledging in its supervisory expectations of July 2020 that assessments of the ongoing value and utility of insurance products should not be driven by short-term fluctuations, but instead take a medium- to long-term perspective.

And at international level, Insurance Europe is providing input to an IAIS consultation on the impact of COVID-19 that will inform the IAIS's next work plan.

Social partner pledge

In March 2020, Insurance Europe issued a joint statement with the other social partners in the European financial services sector — trade union federation UNI Europa Finance and five financial services federations. The statement pledged the sector's commitment to maintaining key services to customers during the crisis, while always protecting employees and respecting the restrictions imposed by public authorities. The joint statement also committed the partners to supporting economic activity and called for the European institutions, regulatory and supervisory authorities and financial services sector to work together to seek to neutralise the effects of COVID-19 on the economy.

What next?

As stated in the Foreword to this Report, the implications of the pandemic will be long-lasting and far-reaching. Swiss Re, in a June 2020 assessment of the longer-term implications of COVID-19, predicted several paradigm shifts to the global economy, including greater roles for governments, accelerated digital transformation and a restructuring of supply chains. While it sees these together as creating a "very challenging" environment for (re)insurers over the next two to three years, it also sees new (re)insurance opportunities in those evolving supply chains and the accelerated digitalisation. There will be a very different future for the world and its insurers.

Frédéric de Courtois
Vice-president, Insurance Europe
General manager, Generali Group, Italy

PANDEMIC RISK

Preparing for the future

Work is already under way to find innovative solutions to cover the risks of future pandemics

As the COVID-19 pandemic took hold in Europe and the continent scrambled to respond to the unprecedented public health crisis that ensued, governments announced lockdown measures in an effort to limit the spread of the disease. As a result, economic and social activity in many sectors ground to a halt, with many businesses forced to cease their activities and a widespread cancellation of events and travel.

This, in turn, led to debate over the extent to which the insurance industry covers the pandemic-related losses incurred by these industries and individuals, as well as discussion more generally over the extent to which insurance can cover pandemic risk. This debate has since matured into a discussion — taking place at both national and supranational level — about possible solutions to cover the economic losses and other risks linked to future pandemics.

A challenge to insurability

Pandemic risk poses a challenge to insurability, as it is — by definition — global and potentially affects many individuals and economic sectors at once. This sets pandemic risk apart from risks that are insurable — ones that do not materialise everywhere and all at once — as it prevents the diversification and pooling mechanisms at the heart of insurance (see box opposite).

In practical terms, this means that while it is possible to cover a

> **"While it is possible to cover a limited number of policyholders against pandemic risk in well-defined circumstances, insuring a very large group cannot be done relying exclusively on the principles of insurance and on the resources of the insurance industry alone."**

limited number of policyholders against pandemic risk in well-defined circumstances, insuring a very large group cannot be done relying exclusively on the principles of insurance and on the resources of the insurance industry alone. Pandemic risk therefore takes its place among similarly potentially large risks, such as natural catastrophes or terrorism, which require partnerships between public bodies and the private insurance industry in order to devise innovative solutions. It is important to note, however, that even natural catastrophes and terrorism do not share the same global nature intrinsic to pandemic risk; their potential losses are much lower and diversification can be achieved.

Pandemic risk on paper

Despite posing a challenge to the principles of insurability, modelling the risks created by pandemics is not uncharted territory. Pandemic risk has been modelled by the insurance industry by using risk assessment tools to map certain scenarios and their expected consequences, allowing for the spread of a disease to be predicted with relative accuracy.

What is insurable?

To assess the insurability of a risk, it must be weighed against a set of conditions. The risk is insurable if:

- It is definable and financially measurable.
- It is random and independent.
- It is possible to build a risk pool in which the risk can be shared and diversified (mutualised) at economically fair terms.
- The insurer can calculate a fair premium for the risk, ensuring that the premium is sufficient to cover future claims on its pool of risks and that it is also affordable for consumers.
- The likelihood of the risk is calculable, implying notably that there is a reasonably large history of losses and sources of data from which to calculate the average severity and frequency of future losses.
- There is limited risk of catastrophically large losses and the financial impact of such losses is not so significant that an insurer/the insurance sector cannot afford to pay it.

Pandemic risk in practice

Pandemics are not isolated events, however, as they are accompanied by government efforts to reduce their negative effects. Preventive measures put in place by governments in the interests of public health — such as full or partial lockdowns of the economy and society — while effective in limiting the spread of a disease, significantly affect the insurance industry's ability to assess, mitigate and price pandemic risk.

In the case of COVID-19, the economic losses have not arisen primarily from the pandemic itself but from government action to mitigate the impact of the virus on the population. Besides a pandemic's global nature, it is this factor that also sets pandemic risk apart from other catastrophic risks, as it is closely linked to — and can be exacerbated by — political decisions.

While the main focus on insurance during the COVID-19 pandemic has been the economic losses associated with the widespread interruption of business activity, the extent to which pandemic risk is covered or not in other lines of business has also been discussed. While pandemic risk does raise insurability challenges across the board, European insurers do cover certain elements of the risk in a number of business lines. Pandemic risk can appear on the balance sheet of insurers offering the following insurance lines:

- general liability
- medical, professional and directors & officers liability
- travel
- event cancellation
- trade credit
- life

Searching for solutions

The insurance industry is committed to playing its part in the search for a workable solution to help societies and economies to better prepare for future pandemics. For insurers, tackling the challenges associated with insurability will be the precondition for participation in any such solution.

At European level, Insurance Europe has been involved in discussions on future pandemic solutions since the early days of the current outbreak, providing a platform for markets to share information on developments at national level and forming part of a workstream established by EIOPA to explore pandemic and shared-resilience solutions. Through this workstream, Insurance Europe contributed to an issues paper published by EIOPA in July 2020, which sets out possible solutions and explores their feasibility.

"For insurers, tackling the challenges associated with insurability will be the precondition for participation in any pandemic solution."

The economic impact of the measures taken to mitigate the effects of the pandemic will be borne by governments for many years to come. Given the sheer scale of the losses and the challenges it poses to insurability, it is clear that pandemic risk cannot be borne by the private insurance industry alone. Neither will it be possible to devise solutions in time to cover second or subsequent waves of the current pandemic.

Looking ahead to future pandemics, governments and insurers in some member states have begun to explore the possibility of public-private partnerships, drawing on experience of existing partnerships for other — notably less global and potentially catastrophic — risks, such as natural catastrophes or terrorism. For the time being, these initiatives have not moved beyond the national level. This may be because, despite its global nature, COVID-19 has a strong national component, be it the extent and evolution of the pandemic, government responses or the resilience of healthcare systems.

Given the pan-European nature of a pandemic, there may also be a need to discuss a potential role for the EU. If there is such a role — whether in the form of an added financial layer supplementing national risk-transfer solutions or limited to central coordination of, for example, prevention measures — it will require strong and broad political support at the highest level.

For now, many of these questions remain open. Indeed, as the pandemic continues to rage, it remains too early to fully assess all its economic consequences; the full effects of the COVID-19 pandemic may not be evident for many years to come. What is clear, though, is that pandemic risk poses a huge challenge to governments, society and the insurance industry alike. Moving forward, whatever the role for the insurance industry may be, helping society to be better prepared for future pandemics will require new and innovative solutions, drawing on experience from the current pandemic. The insurance industry stands ready to play its part.

Thomas Hlatky
Chair, sustainability working group, Insurance Europe
Head of reinsurance, Grazer Wechselseitige, Austria

CLIMATE ADAPTATION

Time for a sea change

Insurers support the EU's increased focus on ways to adapt to the world's changing climate

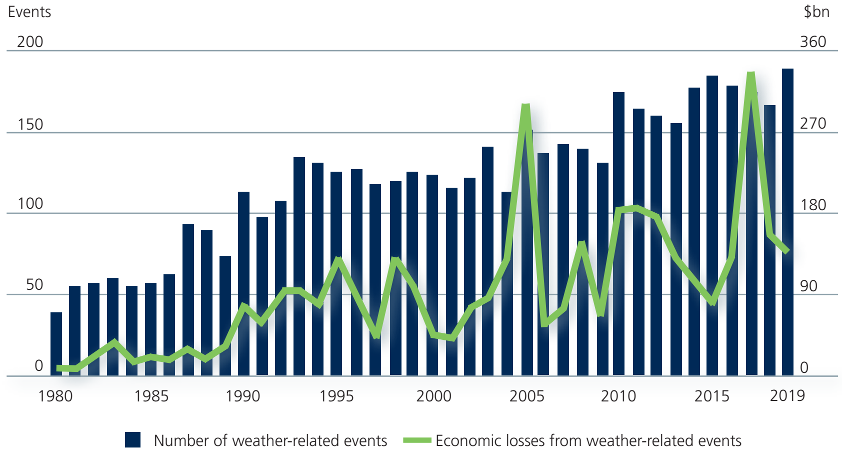
Tackling the effects of changes in climate on eco-systems and populations is arguably the world's most urgent challenge, requiring a concerted and shared global commitment. The scale of that challenge was brought into sharp relief by an analysis published in July 2020 by the World Meteorological Organisation (WMO), which showed a one-in-five chance that annual global temperatures will be at least 1.5°C warmer than pre-industrial times in the next five years. That clearly demonstrates the difficulty of meeting the 2016 UN Paris Agreement to keep the global temperature rise well below 2°C above pre-industrial levels.

The roles of (re)insurers

(Re)insurers, as providers of insurance cover and as institutional investors, are well aware of the transformation of risks brought about by climate change. They are risk carriers for increasingly destructive extreme events, as well as for higher health, mortality and political risks as a result of climate variations. And as institutional investors they face physical and transition risks for the billions of euro of assets they manage.

(Re)insurers play a pivotal role in developing the measures needed to mitigate and adapt to the effects of climate variability. They are actively engaged in climate-related discussions and actions, providing expertise in identifying, measuring and pricing climate risks, and in raising awareness of the risks and finding solutions to them (as set out in greater detail in the Opinion article by the

Weather-related events and associated economic losses — 1980–2019 ($bn, 2019 prices)



Source: Sigma 2/20, "Natural catastrophes in times of economic accumulation & climate change", Swiss Re Institute

chair of Insurance Europe's Reinsurance Advisory Board, Swiss Re's Christian Mumenthaler, on p69). Insurers contribute in a wide range of ways to enhancing adaptation to climate change. Just one example is the increasing number of insurers that offer their clients incentives to reduce the risks they face, for instance by offering reductions in premiums to those who take preventive measures such as retrofitting homes against flood or wind damage.

Adaptation or mitigation?

As defined by the UN Intergovernmental Panel on Climate Change, **adaptation** is the process of adjusting to the actual or expected climate and its effects, moderating harm or exploiting beneficial opportunities.

Mitigation, on the other hand, refers to human intervention to reduce the sources or enhance the sinks of greenhouse gases or other substances that may directly or indirectly contribute to climate change.

Both mitigation and adaptation are essential to tackle the challenges of a changing climate.

Insurers also participate in public-private partnerships to build community resilience. In these partnerships, insurers often lend their expertise in risk management and risk modelling to support and train public administrations and SMEs on integrated business risk management. In addition, insurers regularly contribute to company or municipality-level adaptation plans.

And as Europe's largest institutional investor, the (re)insurance industry is already financing the transition to carbon-neutrality, resource-efficiency and greater sustainability (see also the article on sustainable finance on p18).

Welcome EU ambitions

The European insurance industry supports the EU's political commitment to become climate-neutral by 2050, as well as the European Commission's proposal for Europe's first Climate Law to enshrine that commitment into EU law.

The WMO study shows that mitigation measures to radically reduce greenhouse-gas emissions — while of utmost importance — are no longer enough. Extreme weather events are already becoming more frequent and severe (see chart) and this will only increase. To address the economic, social and environmental implications of a changing climate, more focus is needed on adaptation. Insurance Europe therefore welcomes another element of the EU's European Green Deal package: the EC's new, more ambitious Strategy on Adaptation to Climate Change.

Adaptation enhancement is a key focus of the EC proposal for a European Climate Law, and Insurance Europe is highly supportive of the EC's ambition to step up climate-proofing, resilience-building, prevention and preparedness. Insurance Europe backs the Law's proposal that national and local authorities should enhance resilience by implementing effective prevention measures. It likewise supports the further development of national adaptation plans and strategies based on comprehensive risk-management frameworks.

Insurance Europe also welcomes work by the Commission to raise awareness of both the risks of a changing climate and of the appropriate insurance solutions. There is a key role for the EU to play in coordinating adaptation efforts, but it must be remembered that there is no one-size-fits-all solution at EU level, as member states have different risk exposures resulting from their different environments, levels of public risk-awareness, extent of government intervention, liability regimes or adaptation practices. This explains the highly diverse natural catastrophe insurance markets. In some markets, for instance, government/insurer natural catastrophe pool solutions are in place, while in others insurers provide private market solutions.

Insurers' respond to EU adaptation consultation

In its comments on the EU Strategy on Adaptation to Climate Change, published in August 2020, Insurance Europe stressed that the first step in minimising extreme-event damage should be to ensure existing adaptation measures are fully and consistently enforced.

Insurance Europe went on to insist on the need for public-private partnerships to bring coordinated action on adaptation into the mainstream. Insurers believe that effective adaption is a shared responsibility between governments (building flood defences, introducing and enforcing building codes and drawing up emergency sewerage plans, for example), the private sector, including insurers (investing, for instance, in adaptation measures) and the public (being made aware of and avoiding high-risk zones).

It is likewise vital that the EU continues to support *ex-ante* financing for extreme events by maintaining insurers' freedom

The importance of data

Data and statistics play a key role in the enhancement of climate adaptation, and Insurance Europe welcomes the Commission's recognition of this in its proposed European Climate Law and the renewed EU strategy on adaptation to climate change. Gathering, analysing and making widely available relevant climate-related data leads to a greater understanding of climate trends and risks, making it possible to meet the challenge of adapting to climate variations and to minimise future risks.

Several national insurance associations in Europe are already working with public authorities to share, systematise and analyse climate-related loss data. Such partnerships are generally tailored to local climates and geographies and national regulations.

In its response to the consultation on the EU Strategy on Adaptation to Climate Change, Insurance Europe stressed the need for more usable data on climate risks. The prerequisite for pricing climate risks is high-quality data on how such risks can occur and their effect on the economy. The EU is in the best position to support EU-wide efforts to model physical risks and to ensure the resulting data is accessible on an affordable digital platform to all interested parties.

Thought should also be given to the use of the substantial and valuable flood-risk data collected by member states as a result of the EU Floods Directive. This could contribute to enhancing the much needed research into torrential rain and the resulting flooding — a major loss factor in urban areas. Authorities could then be encouraged to base their planning decisions and building requirements on this data and research, and insurers could improve their understanding of such risks.

In view of the likely increased severity of climate risks in the coming years, Europe's insurers would like to see broader partnerships or fora for dialogue that involve all public and private stakeholders in order to build up a more holistic picture of the risks, address their causes and make decisions that create greater resilience.

Insurer/government cooperation on floods

Across Europe, insurers are working with national authorities on flood risk. One example is Austria's "HORA" risk-zoning system.

As a result of severe floods at the turn of the century, in 2002 the Austrian Federal Ministry of Sustainability and Tourism and the Austrian Insurance Association launched a nationwide risk-zoning system for natural hazards, with a special focus on floods.

HORA documents the risk of natural disasters in order to better assess the potential for damage. Data was gathered on the high-water levels of 25 000 kilometres of rivers and in 2011 HORA was updated and expanded. Since then, it has been available to use online (https://hora.gv.at) and as an application.

to negotiate terms and conditions with their policyholders directly, thus enabling the insurance industry to continue with its many market-driven solutions that are tailored to local conditions. Indeed, the EC's report on the implementation of the EU Adaptation Strategy recognises that insurance markets function as a crucial adaptation tool.

Raising public awareness of the consequences of climate change is another area in which the EU should be active. This work, along with partners such as (re)insurers and others, could be complemented by the collection and dissemination of high-quality climate-risk data (see box on p15).

And, since investment by the private sector in adaptation is essential, more projects are needed of the type in which insurers are keen to increase their investment; tying in nicely with the EU's stated "green recovery" ambition following the COVID-19 pandemic. There should also be good use of the EU taxonomy to classify investments that contribute to adaptation (see sustainable finance article on p18) and more incentives, such as tax breaks, to encourage businesses to implement adaptation measures.

Focus on floods

In 2019, Insurance Europe contributed to the Commission's public consultation on its fitness check of the 2007 Floods Directive, which requires EU member states to identify and manage zones at risk from river or coastal flooding.

Changing weather patterns and rising sea levels as a result of global warming are leading to increases in all types of flooding. European insurers already provide significant levels of compensation for flood losses; they paid out $6.9bn (€5.8bn) in 2002 alone — the year of catastrophic flooding along the Danube and Elbe rivers. Furthermore, insurers use their considerable flood-risk expertise to engage in the whole of the risk-management cycle: helping to identify risks and giving advice on reducing or adapting to them, in addition to providing services in risk transfer and recovery.

Overall, insurers believe the Floods Directive has had a positive impact on Europe's preparedness for increased flooding, but that it could still be improved. There must be an appropriate policy framework that involves public authorities and private stakeholders in flood risk management, with the proper

"The EU Floods Directive has had a positive impact on Europe's preparedness for increased flooding, but it could still be improved."

financing of — and investment in — ways to increase resilience to flooding.

While insurance is not a substitute for adaptation or mitigation measures, the Directive should require EU states to encourage the uptake of insurance in order to provide effective cover for flooding, without, however, defining that insurance cover. And the scope of the Directive should be extended to include floods caused by torrential rain and storm surges, as well as smaller rivers and streams. This could be done by introducing a threshold above which flooding has to be modelled, calibrated to the number of people who would be affected.

Some terms in the Directive, such as "frequent" and "extreme" flooding, need clarification to facilitate cross-regional comparisons. Greater clarity is likewise needed on what should be included in flood-risk modelling; for instance, whether sewerage systems should be included.

Year of action

2020 has been designated the "year of action" by the Global Commission on Adaptation, which was launched by the UN in 2018 to encourage the development of measures to manage the effects of climate change. The EU's plans in this area are wide-ranging and ambitious, and insurers are already supporting them with expertise and investment.

Sustainable ambitions for Europe

In response to the ambitions outlined by the 2019–2024 European Commission to create a prosperous, sustainable and competitive Europe, Insurance Europe published its own "Ambitions for Europe" in January 2020, setting out four key objectives and how to achieve them.

One of its four ambitions is the creation of a greener, more sustainable Europe, including enhancing climate adaptation and addressing the protection gap.

Olav Jones
Deputy director general, Insurance Europe

SUSTAINABLE FINANCE

Green shoots of recovery

Insurers support the transition to a carbon-neutral, resource-efficient & more inclusive EU economy

Despite the huge challenges created by the COVID-19 pandemic, the insurance industry remains as committed as ever to the transition to a more sustainable economy and to tackling climate change.

Just over two years have passed since the launch of the ambitious Action Plan on Financing Sustainable Growth by the former European Commission of President Juncker. They have been two years of fast-paced regulatory developments focused on the financial sector, including insurance. The new Commission of President von der Leyen has confirmed the extremely high level of ambition of that 2018 Action Plan and a focus on tackling the increasing challenges posed by climate change.

A number of regulatory initiatives on sustainability have either already been launched under the European Green Deal or have been announced. There will also now be discussions on how to put sustainability at the centre of the EC's Recovery Plan for Europe to repair the economic and social damage resulting from the pandemic and lockdowns.

Two asks from the insurance industry

Insurance Europe supports the European Green Deal objective of making the EU a net-zero greenhouse gas emissions economy by 2050. The Green Deal can address two requests made by the insurance industry during the Juncker Commission:

- To have the responsibility for sustainability shared between all relevant sectors, and not just placed on financial services. Insurance is a key part of the economy, as it provides coverage for underlying risks and funding via its investments, but the industry can only become greener if the economy overall becomes greener. All sectors need to contribute to this transition, and insurers welcome that this is exactly what the Green Deal sets out to do.
- To increase actions to create new sustainable assets in which insurers can invest. The EU has identified a yearly investment gap of about €260bn that needs to be closed in order to achieve its 2030 climate and energy targets[1]. Insurers have significant potential to help fund the investments needed and are keen to do so, but currently there is an extremely limited number of such investments and projects. Steps need to be taken by other industries, national and local governments and the Commission so that there are far more transformational and sustainable projects in which to invest. More sustainable equity, debt and sovereign bonds are also required.

As institutional investors, many European insurers have started to apply environmental, social and governance (ESG) criteria to their investment strategies and to increase their targets for sustainable investment. Insurance Europe recently estimated that the European insurance industry planned to allocate over €140bn to sustainable investments by 2020.

1 Communication of the European Green Deal

Definitions & disclosures

The EC's 2018 Action Plan saw it pushing the sustainable finance agenda via legislation that would embed sustainability in all aspects of financial services companies: in investments, in governance, in prudential rules and in consumer disclosures.

The Action Plan launched work on a much-anticipated EU taxonomy on sustainable finance and it took the EU's co-legislators almost two years to finalise a Taxonomy Regulation. While still quick for EU legislation of a highly strategic nature, this reveals the differences between member states and between national realities, and hints at the challenges that lie ahead for Europe's green transition.

The insurance industry had long called for a common definition of sustainability, to avoid "green washing" and to create a common understanding of sustainable investing. During the development of the taxonomy, it stressed that the transformation of the economy from "brown" to "green" would need to be gradual and that all efforts put into this transition should acknowledge this. The taxonomy should therefore recognise the positive impact of activities to move, or enable moves, to carbon neutrality. For example, the benefits

of investing in a bond whose proceeds would be used to finance a company's energy-efficiency should be recognised.

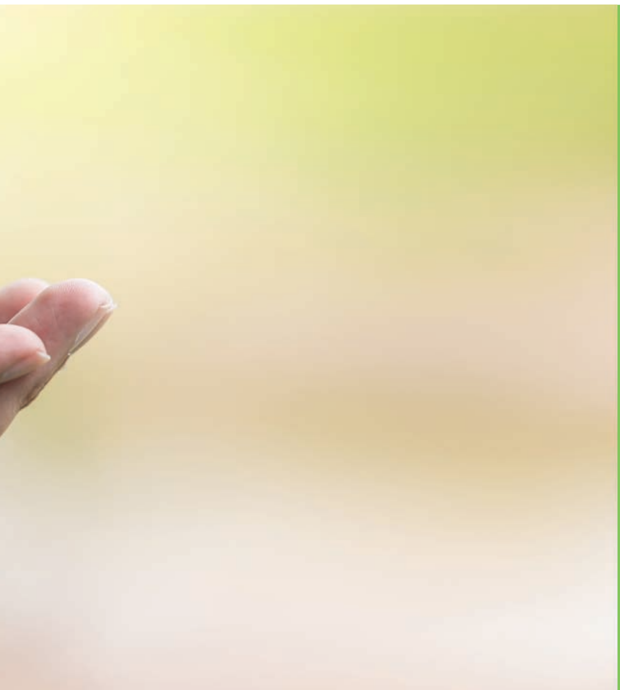
The EC Action Plan also resulted in an extensive Sustainable Finance Disclosures Regulation that requests the provision of various pieces of sustainability-related information on websites and to consumers. The insurance industry falls within the scope of this Regulation and so needs to comply with a number of new obligations.

Unfortunately, however, it has a number of implementation concerns and sees barriers that have not been addressed in the Regulation:

- The Regulation will require sustainability data for each actual and potential investment, yet reliable public ESG data is currently limited. It is therefore crucial to make it mandatory for companies to provide ESG information so that investors can manage sustainability risks, steer their portfolios towards the objectives of the European Green Deal and report on their investment portfolios in line with the Regulation. Indeed, ESG data should be made available through a centralised, electronic European register. This would aid comparability and lower costs, as well as helping data preparers by eliminating multiple requests for information.
- There is a significant risk of creating an overload and duplication of product information. While disclosures are beneficial for customers and the public, they should be needs-based and feasible. Providing too much information can have a detrimental impact on consumers and hamper their decision-making.
- The current timeline for implementing the Regulation is more than challenging and could create significant practical problems and liability risks for investors, as well as confusion for customers. Despite the urgent need to take action to promote a sustainable economy, the Level 2 measures should clarify and help determine how to deal with these challenges.

Looking ahead, a key workstream is the review of the EU's Non-Financial Reporting Directive (see box on p32), which is intended to make it mandatory for companies to report ESG data. In June 2020, Insurance Europe responded to the consultation on the Directive, strongly supporting this aim. In addition, the EC Renewed Sustainable Finance Strategy will enhance the integration of sustainability factors in business operations, while unveiling opportunities to finance sustainable investments.

The insurance industry will contribute to the work of the EC and EIOPA, seeking to address the concerns described earlier and to ensure any measures are proportionate and feasible.



No favourite colours in Solvency II

Europe's insurance regulatory framework, Solvency II, is — and should remain — risk-based. This means that any differences in the treatment of insurers' green and brown assets should be based on differences in their underlying risks, and that the insurance industry does not support artificial incentives or disincentives to hold assets on the basis of green or brown qualifications.

Instead of any green-supporting factor, the priority should be to make sure the 2020 Solvency II review results in focused changes that help insurers to play their key role in supporting investment to achieve carbon neutrality and economic growth in Europe, and that do not hinder them. Insurers are willing and able to contribute to sustainability goals, but Solvency II's capital requirements should not be used to promote them.

Sustainability & Solvency II

As part of its Action Plan, the EC also asked EIOPA to investigate what should or could be done in the Solvency II insurance regulatory framework to better reflect sustainability in areas such as the prudent person principle, companies' own risk solvency assessments (ORSAs), key organisational functions and capital requirements.

While the industry appreciates the need to assess the framework against sustainability considerations and agrees that insurers should assess their exposure to sustainability and climate change risks, Solvency II already requires all risks to be covered and therefore only small changes are needed. EIOPA itself acknowledges this and also that the assessment of the impact of climate change depends on the materiality of the risks and is subject to Solvency II's principle of proportionality.

On the ORSA, the insurance sector highlighted that the assessment should continue to reflect a company's own risk assessment and that any attempt at standardisation can undermine this.

Limited but vital improvements are needed to Solvency II to ensure the framework correctly measures insurance business and risks, in particular relating to long-term business and investments. The industry's interest in investing in long-term sustainable investment is strongly linked to its ability to continue to sell long-term products. Ensuring that the 2020 review of Solvency II reduces — and does not increase — unnecessary barriers to long-term products and investments is therefore key (see also Solvency II article on p23).

Sustainability at international level

Europe remains by far the most ambitious region in addressing climate change and supporting a sustainable financing of the economy. Nevertheless, a key milestone in sustainable finance came at international level with the establishment by the Financial Stability Board back in late 2015 of a Task Force on Climate-Related Financial Disclosures. This industry-led taskforce had the ambitious aim of creating voluntary, consistent, climate-related financial risk disclosures for use by companies in providing information to investors, insurers and other stakeholders.

The final recommendations were released in June 2017 and quickly became an international reference point for such disclosures. As a follow-up, the IAIS consulted on an issues paper on implementing the recommendations in December 2019 and released its final version in February 2020.

European insurers support the fact that the IAIS is considering implementing the recommendations through various Insurance

An EU Ecolabel for retail financial services?

The EC's 2018 Action Plan on Sustainable Finance observed that "the lack of labelled financial products may prevent investors directly channelling their funds into sustainable investments". To address this perceived problem, the Commission set its Joint Research Centre (JRC) the task of developing criteria to add financial products to its EU Ecolabel scheme, which is currently awarded primarily to consumer and household goods.

Insurance Europe has contributed to the JRC's consultations as it finalises the criteria for adoption by the EC in 2021. It has stressed that the criteria must pay due consideration to the fact that, in many countries, a large proportion of insurers' products are guarantee-based, in order to avoid any competitive disadvantage with the fund industry.

While the insurance industry supports the ambition behind the Ecolabel proposal, it believes the proposed criteria are unrealistically high, meaning that most products would not qualify. It has therefore called for better-calibrated criteria that would create a sufficiently large pool of eligible investments.

Core Principles (ICPs). It is worth making a comparison with Solvency II, where sustainability risks are being explicitly embedded in the prudential framework to facilitate the identification and management of all material risks by insurance companies. Similarly, introducing clarifications on how sustainability can be integrated explicitly in interpreting the IAIS ICPs will help strengthen the integration of material sustainability risks in insurers' operations in a consistent and efficient manner. In addition, this could be an effective way of ensuring minimum standards globally, which is an objective supported by the European industry.

From this perspective, it is helpful that the IAIS is taking a coordinated approach across jurisdictions, which reflects the global nature of insurers' operations and especially the cross-border nature of climate risks. Coherent policymaking across jurisdictions will avoid duplicative or contradictory standards, while contributing to an understanding of sustainability risks and strengthening the overall stability of the financial system.

Global data gap

A key issue emerging in the global discussions is the availability of data on the sustainability profile of each entity, from the perspective of both a company's performance and the external environmental and social impact of its activities. As mentioned earlier, sustainability-related information is a prerequisite for insurers to be able to perform sustainable investing and underwriting activities, and to produce robust and efficient disclosures, but quality sustainability data is currently lacking.

In general, regulatory support is needed to enhance the quantity and quality of ESG data available worldwide. Even within Europe there are significant interactions between various pieces of EU regulation that need to be addressed for consistency; at international level, the issue only becomes more complicated and solutions will take time. It is important to acknowledge the scale of the challenge and take this into account in any assessment of progress on sustainability disclosures.

Looking ahead, the European industry will continue to bring to the IAIS its extensive knowledge in the area of sustainable finance and use the recent regulatory discussions in Europe to contribute to the even more challenging international ones.

"Coherent policymaking across jurisdictions will avoid duplicative or contradictory standards, while contributing to an understanding of sustainability risks and strengthening the overall stability of the financial system."

Alban de Mailly Nesle
Chair, economics & finance committee, Insurance Europe
Group chief risk & investment officer, Axa Group, France

SOLVENCY II

Few flaws, big impact

COVID-19 and the economic challenges faced by the EU make it vital to correct the flaws in the EU's prudential framework for insurers

Major challenges lie ahead for the EU in achieving economic growth, technological innovation and global competitiveness and in addressing the risks created by climate change, ageing societies, cyber activity and pandemics. So, now more than ever, it is crucial that insurance regulation and supervision preserve insurers' capacity to play the significant role they do in addressing all these issues.

For over four years, European insurers have been supervised under the Solvency II framework, one of the most sophisticated risk-based regulatory frameworks in the world. Experience has shown that it works well overall, as the industry has demonstrated its resilience during the current COVID-19 crisis, and it has brought significant benefits in terms of risk and business management to both insurers and supervisors. Yet, experience has also shown that there are some key shortcomings that need to be addressed. In fact, although the shortcomings are few, their impact is great.

From the outset, European co-legislators acknowledged that adjustments could be necessary for long-term products and investments. They therefore embedded in the framework explicit requirements for its performance to be reviewed. Specifically, two reviews were foreseen: a limited one, which took place in 2018–19, and a more extensive one, which is happening now.

The 2018 review was narrow in scope and — disappointingly — the fixes it led to were even narrower. Indeed, some important issues

> **"The effects of the pandemic should be used to inform the review, so that Solvency II becomes fit for purpose in both normal and stressed market conditions."**

from that initial review were left to the current one, which is why the industry characterised the 2018 review as a missed opportunity in some areas. The 2020 review is therefore the opportunity to instigate the improvements that are much needed to make Solvency II work as intended, for the benefit of consumers, society and the economy at large.

While the COVID-19 pandemic has led to some delays in the review process, it has also confirmed some of the industry's concerns over flaws in the design of Solvency II in the context of a crisis. With the pandemic, the regulatory framework is being put to the test. Understandably, the solvency ratios have experienced a decrease overall, but this is entirely normal as a result of such an event. Although the industry remains strong and well capitalised, with average solvency well above the solvency capital ratio (SCR), the flaws in the framework are exacerbated in these times of stress, as the industry warned several times would be the case.

The effects of the pandemic should therefore be used to inform the review, using the delays to investigate the problems and find the right solutions, so that Solvency II becomes fit for purpose in both normal and stressed market conditions.

Three priorities

The industry has three key priorities for the 2020 review:

- The treatment of long-term business needs to be improved to ensure the industry has the capacity and ability to continue to provide affordable, long-term products and to remove disincentives so that insurers can fully play their role as long-term investors.
- Simplification should be sought through the rationalisation of reporting requirements as well as a better application of the principle of proportionality.
- An efficient, effective and credible EU system of financial supervision needs to be ensured.

Addressing long-term business flaws

Improving the treatment of long-term business in Solvency II is crucial, given the leading role that insurers play in the provision

Solvency II & insurance guarantee schemes

At the request of the European Commission, EIOPA launched a consultation on the European harmonisation of insurance guarantee schemes (IGS) in July 2019. In its response, Insurance Europe opposed an EU initiative on IGS because national schemes vary significantly across Europe but generally work well within their local context and laws. Even a minimum level of harmonisation would create significant costs and pose complex challenges for which there may not be acceptable solutions.

The priority for policymakers should instead be to ensure that Solvency II is applied appropriately in all EU member states and that there is coordinated supervision of insurers working cross-border under the EU principles of the freedom to provide services (FOS) and the freedom of establishment (FOE).

National authorities should be allowed significant flexibility to choose the IGS features that best suit their markets and to reflect the significant differences between member states' social welfare systems, winding-up processes for insurers and insurance product lines. And it should be the home supervisory authority, rather than the host, that should be held accountable should there be a failure of an insurer operating under FOS/FOE.

Should the EC nevertheless provide evidence that minimum harmonisation of IGS at European level is required, Insurance Europe's preference would be for a "home" approach, combined with "host" elements.

Under such an approach, the home country would provide the funding, which would align with how companies are supervised, and the host country would provide the "front office" customer interface to facilitate customer, policy and claim identification, as well as communication in the local language. There would, however, be significant and potentially intractable operational challenges in applying this, or indeed any, harmonised approach across the EU.

Insurers are not alone in seeking improvements to Solvency II

In its June 2020 final report on the capital markets union project to bring about a single EU market for capital, the EC's High-Level Forum made five recommendations for the Solvency II review to encourage insurers to provide more financing for EU capital markets, all of which Insurance Europe supports:

- Better consider the long-term nature of insurance and assess if the risk of forced selling of assets at adverse market prices is being estimated realistically when reviewing the treatment of equity and debt capital charges.
- Change the criteria for the current long-term equity capital calibration to address the problem that almost no equity investment would currently qualify.
- Assess whether the risk margin is too high and volatile for its policy purpose, reducing capacity for investment risk in capital markets.
- Ensure that insurers' own funds are appropriately valued and not too volatile, in particular looking at what improvements can be made to the volatility adjustment to avoid exaggerating either way the valuation of projected long-term liabilities and reduce artificial volatility.
- Propose Level 1 legislative changes and make the necessary Level 2 changes to improve the mitigation of procyclical effects that requirements may have on insurers' investment behaviour.

of long-term savings products and long-term investment in the European economy. There are a number of areas that create problems today for long-term business.

First, Solvency II currently creates artificial volatility in insurers' solvency positions and leads to an overestimation of the value of long-term liabilities. The volatility adjustment (VA) is a widely used measure that was introduced as part of the long-term guarantee package in the Omnibus II negotiations that finalised the Solvency II framework. Insurance Europe strongly supports the VA, but focused improvements are needed to ensure it properly reflects the ability of insurers to earn returns above risk-free rates and mitigate artificial balance-sheet volatility.

EIOPA's proposals, as part of its quantitative impact study, would certainly not achieve this objective. As they stand, they actually make the VA less effective, especially in times of crisis when it is most needed. The industry remains in dialogue with EIOPA and the European Commission to find solutions that would achieve the necessary outcomes without introducing undue complexity.

Second, the risk margin[1] is unreasonably high, especially for long-term business. According to EIOPA, the risk margin can reduce the industry's available capital by a staggering €189bn[2]. This unnecessarily increases liabilities and thus reduces available capital and risk-taking capacity. The current risk margin's excessive sensitivity to interest rates is yet another source of artificial volatility and makes it inherently procyclical. An excessive risk margin also has an impact on the cost and availability of certain products, particularly long-term ones, to the detriment of policyholders.

In spite of the industry's extensive technical evidence during the 2018 review that the risk margin should be lower and can be safely reduced, its revision was left to 2020. This is an area in which the EC recognises that changes should be considered, yet EIOPA so far seems to have very little ambition to address the flaws in the risk margin in a comprehensive way.

Last but not least, the capital requirements for long-term assets remain, in many cases, exaggerated and do not reflect the actual risks to which insurers are exposed. These long-term assets include the infrastructure and investments to fund the sustainable transformation that Europe needs to meet its 2050 goal of carbon neutrality. It is extremely important that

1 The risk margin is an amount over and above funds needed to pay claims and benefits. Its prudential purpose is to ensure that, should an insurer fail, there are additional funds above the best estimate of liabilities to make those liabilities transferable to another undertaking.
2 Based on EIOPA data for solo undertakings in the European Economic Area for Q3 2019

work in this area also takes a holistic approach, with either the reduction of specific capital requirements investigated or alternative mechanisms considered (such as the dynamic VA) that lead to the same outcome.

Increasing proportionality

Another fundamental area that needs addressing is the unduly onerous operational burden of Solvency II. Achieving improvements by making proportionality a real tool rather than a theoretical principle and streamlining the reporting requirements is vital to ensure that supervision is effectively risk-based and to avoid that, ultimately, policyholders have to bear unnecessary costs.

Currently, companies report little or no application of proportionality. This issue was also highlighted by the EU co-legislators as a priority in early 2020. While the framework requires that scale, nature and complexity must be taken into account in the exercise of supervision, it appears that national supervisors feel that they lack the legal background and tools to deviate from or waive a requirement. Consequently, EIOPA's proposal to add new simplifications — while welcome — is not enough to ensure that these will be effectively applied. Discussions with EIOPA in recent months confirm its greater openness to take an ambitious stance in the area of proportionality. The challenge is now to put in place some tools that will work effectively in practice.

Furthermore, with up to 95 Solvency II reporting templates for each company to complete and several qualitative reports both for the public and for supervisors, the burden of reporting is extremely onerous and overly costly. This is why the industry fully supported EIOPA's intention to create "a material reduction in the scope of quarterly reporting" and "an increased proportionality of supervisory reporting and public disclosure".

EIOPA's follow-up proposals did include some potentially helpful concepts, such as the introduction of a set of core and non-core templates and the split of the solvency and financial condition reports (SFCRs) into a policyholder and professional part. However, the way these have been introduced is not workable, as the reporting requirements are still onerous. For example, a written report would still be required for the professional SFCR section and the new standardised templates are excessive. In addition, the non-core templates are not automatically exempt from reporting. Moreover, the significant additional reporting and many proposed changes would in fact increase the overall burden — notably the new requirements relating to external audits and standard formula reporting for companies that use their own internal model.

Ensuring a stable & efficient supervisory system

To ensure an efficient, effective and credible system of financial supervision at EU level, any amendments to the current regime must be based on sufficient evidence of the need for change.

The ultimate responsibility of supervision is and should remain with national supervisors to ensure that the principles of subsidiarity and proportionality are not undermined. The role of national supervisors should not be compromised, as they are vital elements in the supervisory system thanks to their local expertise, direct contact with (re)insurers and, crucially, local accountability.

Insurance Europe remains of the view that EIOPA and national supervisors do not need any further significant changes to their powers to be able to fulfil their mandate. National supervisors need to apply Solvency II in a consistent and proportionate way and EIOPA needs to make greater use of its existing powers to enhance supervisory cooperation and convergence before any changes to EIOPA's governance or mandate are considered.

In addition, the very comprehensive, risk-based system is designed to require boards and supervisors to take a risk-based approach based on each company's risks and capital situation. It is vital that this remains so. In this respect, the industry regrets some actions taken during the pandemic to mimic reactions in the banking sector — notably bans on dividends (see box on p9) — which disregard companies' solvency situation and hence undermine the Solvency II framework in the eyes of the investor community.

Finally, it is important to note that the industry is not alone in calling for some of the key changes outlined above. The EC's High-Level Expert Group on Sustainable Finance made similar recommendations in 2018 and the High-Level Expert Forum on the Capital Markets Union set up by the Commission (see box on p25) has also highlighted the need for Solvency II improvements. It is now time to take heed of those recommendations to achieve an efficient review of the Solvency II framework.

Cristina Mihai
Head of prudential regulation & international affairs, Insurance Europe

INTERNATIONAL AFFAIRS

World class

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

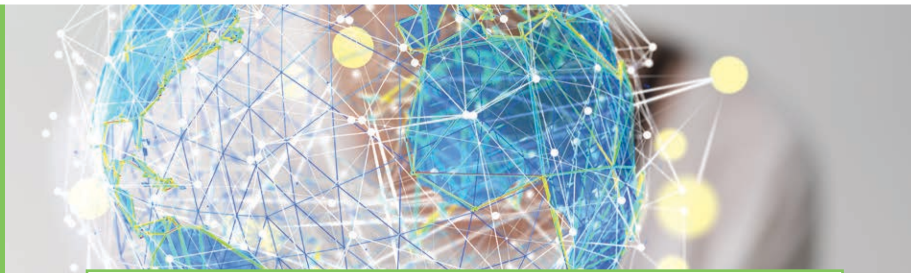
Insurance and reinsurance are global businesses, and European (re)insurers are an international success story. Today, around a third of all internationally active insurance groups are headquartered in the EU, and Europe is the global leader in reinsurance, writing around half of the world's reinsurance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

Olav Jones
Deputy director general, Insurance Europe

FINANCIAL REPORTING

Need to raise standards

Insurers still have concerns about their two key International Financial Reporting Standards

As both preparers and users of financial reports, Europe's insurers understand the value and importance of meaningful, consistent and reliable financial reporting. And since the International Financial Reporting Standards (IFRS) drawn up by the International Accounting Standards Board (IASB) are used in the consolidated reporting of all the EU's listed (re)insurers and a large proportion of the unlisted ones, getting the IFRS right is crucial.

Two standards particularly affect insurers: IFRS 17, which applies to insurance liabilities; and IFRS 9, which applies to the assets that insurers hold to back those liabilities. The IASB — and hence Insurance Europe — have been active on both in the past year, as well as two other projects. These are the IASB's late-2019 proposed improvements to the way information is communicated in financial statements, through a consultation on general presentation and disclosure, and an early 2020 discussion paper on possible improvements to the information companies report on goodwill and impairment.

IFRS 17: last stages of a long journey

After a 20-year international debate around insurance contract measurement, IFRS 17 was published in May 2017, then re-opened following concerns raised by Insurance Europe and others, with the final version only published in June 2020.

While the industry broadly supports the goals of the IASB, the standard published in 2017 had not been good enough to achieve suitably high-quality global financial reporting and to avoid excessive implementation costs. The industry therefore welcomed the IASB decision to re-open the standard and provided significant input into the consultations and discussions that followed about potential improvements.

Six key concerns were highlighted in feedback to the IASB by the European Financial Reporting Advisory Group (EFRAG) — a private association, of which Insurance Europe is a member, which was established with encouragement from the European Commission to serve the public interest on financial reporting by providing independent advice to the EC and technical input to the IASB. The insurance industry also raised the points identified by EFRAG, as well as a number of others, as important issues that the IASB needed to address. Insurance Europe proposed solutions to all the issues the industry raised. Insurers also called for implementation of the standard to be postponed to January 2023 to allow time for the IASB to make the necessary improvements to it and to allow enough time for affected insurers to implement it.

Annual cohort concern

One of the issues that was of widespread concern was the requirement to split product portfolios into annual cohorts. This is because it significantly increases the cost and complexity of IFRS 17. In addition, it does not adequately reflect the true economic nature of insurance contracts, with their risk-sharing between customers and between different generations of customers over time (together often referred to as "mutualisation").

"The lack of any changes to the annual cohort requirement is an area of particular frustration."

The industry appreciates that in the updated and final standard issued in June 2020 the IASB has made a number of important improvements and that it has postponed the standard's effective date to 2023. However, Insurance Europe was disappointed that the IASB left a number of important issues unaddressed. The lack of any changes to the annual cohort requirement is an area of particular frustration.

In Europe, the standard still requires endorsement. The first stage of this, expected by the start of 2021, is EFRAG's advice to the Commission on whether it should be endorsed. Following this, the Commission will form its view and then the European Parliament and Council will take the final decision. The issue of annual cohorts will be one of the main areas of discussion.

IFRS 9: a key issue remains

Insurance Europe welcomed the decision by the IASB to align the application date for IFRS 9 with the IFRS 17 application date of 1 January 2023. This alignment ensures more meaningful accounting information, avoids insurers having to explain two separate changes to users and reduces costs.

There remains, however, one area of ongoing discussion in Europe. This is known as the "recycling" issue. IFRS 9 provides a welcome mechanism to avoid temporary share-price volatility from distorting the profit and loss account. This is achieved through the use of a feature called FVOCI (fair value through other comprehensive income) and works by keeping that short-term volatility fully transparent, but held within the OCI part of the accounts.

Recycling is good

Using the FVOCI option is a very important mechanism but, currently, IFRS 9 will not allow insurers to recognise any of the actual realised gains from FVOCI equity investments in their profits.

Allowing realised capital gains to flow from OCI into profits and loss is allowed for bond investments and is called "recycling". Without it — given that capital gains typically represent 60% of overall equity returns — IFRS profits will not reflect the true financial performance or correctly represent insurers' long-term business model. As a result, an unnecessary disincentive for insurers to invest in equities is created.

Insurers have been calling for the reintroduction of recycling for FVOCI instruments under IFRS 9 for many years. Insurance Europe therefore welcomed the Commission's letter to the IASB in March 2020 calling for an expeditious review of the non-recycling requirement for equities measured at FVOCI.

"Insurers have been calling for the reintroduction of recycling for FVOCI instruments under IFRS 9 for many years."

A non-financial reporting role for EFRAG

In January 2020, as part of the EC Action Plan on Financing Sustainable Growth, Executive Vice-President Valdis Dombrovskis announced proposals for two mandates that would significantly expand the role of EFRAG in developing non-financial reporting standards.

The Commission has since mandated EFRAG to start the technical preparatory work on EU non-financial reporting standards. Insurance Europe supports this mandate, since EFRAG's European Corporate Reporting Lab — which was started in 2018 with a remit to stimulate innovation in corporate reporting by identifying and sharing good practices — had already begun work in this area and there are clear benefits from having a link to financial reporting work.

By early 2021, the EC is expected to propose to mandate EFRAG to become Europe's standard-setter for non-financial reporting standards. Its proposals will need to also cover how EFRAG's governance and funding might need to change to accommodate such a role.

While global standards would be the ideal and ultimate goal, Insurance Europe would support this mandate, given the urgency arising from the need to tackle climate change, the need to comply with the EU's Taxonomy Regulation and its Sustainable Finance Disclosures Regulation, and the time it would take to reach international agreement on any global body and standards.

In developing environmental, social and governance (ESG) reporting standards for Europe, it will nevertheless be important to take into account international developments and in the longer term seek international alignment.

William Vidonja
Head of conduct of business, Insurance Europe

BETTER REGULATION

Quality not quantity

When it comes to EU insurance regulation, there is significant room for improvement

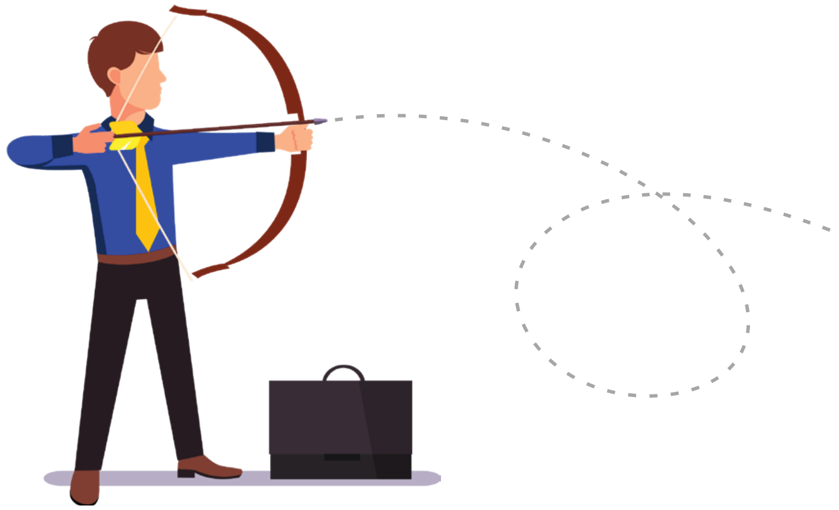
EU financial services regulation has not always been successful in achieving its core aim of benefiting consumers. The EU legislative process includes several shortcomings that affect both the competitiveness of the insurance sector and consumers' access to top-class services. This is due to the complexity of the current EU legislation, its instability in terms of frequent changes and its failure to properly address certain insurance specifics and to respond to consumers' actual needs.

It is therefore encouraging to see that this has been recognised by the European Commission that took office in December 2019.

The plans presented for the Commission's mandate include applying a "one in, one out" principle to new laws and regulations "to make life easier for people and businesses". The plans stress that any new legislative proposal must be evidence-based, widely consulted upon and subject to an impact assessment.

These proposals are a welcome start, as there is a lot more that needs to be done to address all the shortcomings of the EU regulatory process. In light of the COVID-19 pandemic, now more than ever European consumers and insurers need a regulatory framework that is fit for purpose and digital-friendly. So how can policymakers ensure that regulation proposed with the best intentions is not detrimental to consumers? Insurance Europe would propose six broad areas of focus.

"The EU's 'Lamfalussy' process for creating financial services regulation [...] has led to legislation that fails to meet its intended objectives and often has to be revised or supplemented."



Avoid continual regulatory changes

Under the EU's "Lamfalussy" process for creating financial services regulation, basic laws and principles are proposed by the EC and adopted by the European Parliament and Council.

But the technical details are worked out at "Level 2" by the Commission with input from the European supervisors, and through "Level 3" measures developed — sometimes separately — by the Commission and the supervisors. This has led to legislation that fails to meet its intended objectives and often has to be revised or supplemented.

Insurers have been facing a significant increase in the amount of regulation in recent years, a decrease in its quality and frequent reviews and amendments — sometimes before they have adjusted to the new rules and before there is evidence of a need for change. The successive changes to the Packaged Retail and Insurance-based Investment Products (PRIIPs) Regulation and its key information document (see p46) are a prime example of this.

To improve the regulatory process, in-depth analysis should be undertaken to ensure that any new legislation is fit for purpose from the start. And the regulatory framework should be kept as stable as possible, avoiding "quick fixes" and interim solutions.

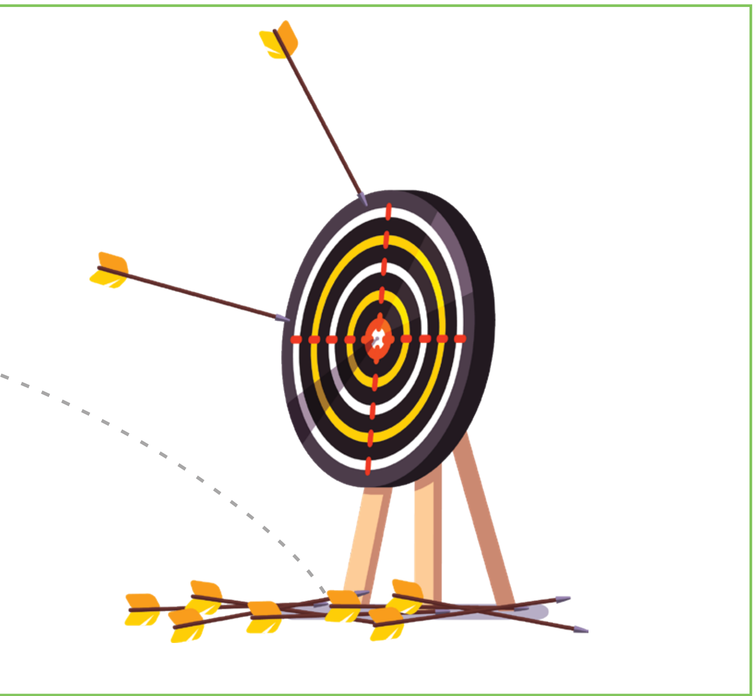
Avoid legal uncertainty

The fall in the quality of EU legislation — perhaps due to the number of initiatives — has led to a proliferation of outdated and unfit rules and to cases of legal uncertainty.

Let us take two examples: firstly, insurers' use of promising blockchain technology — which has the potential to reduce costs, increase transparency and increase trust — could be jeopardised by potential incompatibilities with the General Data Protection Regulation (GDPR).

How can the GDPR's "right to be forgotten" and "right to rectification" (see p58) be reconciled with the fact that blockchain technology is designed to be an immutable and permanent record of all transactions?

Secondly, the key pillar of the EC's legislative package on sustainable finance is an EU-wide taxonomy (classification system) for the sustainability of investments (see p18). Given that all other proposed transparency measures refer back to this concept, its development should have been prioritised by policymakers to avoid legal uncertainty. This was not, however, the case, as the proposal for a Regulation on sustainability-related disclosures was agreed back in March 2019 and work on the development of its Level 2 measures started before finalisation of the taxonomy.



To provide maximum legal clarity, the legislative process must not be rushed, and more time and attention needs to be dedicated to aligning texts.

Avoid inconsistencies, overlaps & duplication

When preparing legislation, the cumulative impact of individual rules and the coherence of the entire EU regulatory framework are frequently not taken into account, resulting in inconsistencies, overlaps and duplication between different pieces of legislation.

To take just one example: the 2019 Regulation introducing a pan-European personal pension product (PEPP), combined with legislation such as the GDPR, the Distance Marketing Directive for financial services and the e-Commerce Directive, could result in an insurance broker who sells a PEPP online having to make between 145 and 189 information disclosures at the precontractual stage. This number will increase further with the new Regulation on sustainability-related disclosures.

To ensure coherence and consistency across EU legislation, the cumulative impact on consumers of proposed and existing rules should be assessed — with thorough consumer-testing — and legislation should not be developed in silos. Indeed, the distribution of certain insurance products is going to be subject to seven different EU regulations and directives in the near future, with no specific clauses that solve the cases of duplicative or inconsistent requirements. The burden to properly interpret and apply the different provisions in conjunction is passed on to insurance companies and consequently to consumers, who are overwhelmed by repetitive or confusing information.

Avoid unfit rules & misleading disclosures

Regulation needs to take full account of the unique features of insurers' products and their distinctive value proposition to customers looking for protection, investment and the peace of mind of minimum guarantees.

Rules that are unfit for insurance or copied from another sector should be avoided, as they can have unintended negative consequences for consumers and the market as a whole.

For example, it is impossible to make a meaningful comparison between the costs of products that contain unique insurance features and those that do not; premiums for protection against biometric risk, for example, are not investment costs, but are premiums for which the consumer receives an insurance protection or benefit.

Regulation must reflect the profound differences between

"The COVID-19 crisis provided a clear demonstration of the importance of digital communication for business continuity and accelerated consumers' expectations of being able to carry out paperless transactions."

financial service products and markets, and disclosures must be clear, meaningful and reflect insurance specifics.

Avoid outdated rules & obstacles to innovation

Some EU regulation requires, for example, information to be provided to consumers on paper by default, preventing further development of the internet as a distribution channel for insurance products and failing to recognise that consumers are increasingly demanding and using online services. In this respect, the COVID-19 crisis provided a clear demonstration of the importance of digital communication for business continuity and accelerated consumers' expectations of being able to carry out paperless transactions.

For instance, the Insurance Distribution Directive (IDD) and the PRIIPs Regulation require pre-contractual information to be provided to consumers on paper by default. It may only be provided another way — such as on a website or in digital format — "by way of derogation". This is highly unsuitable for our digital age. Moreover, the additional disclosures that must be provided (from the Solvency II Directive, GDPR, Distance Marketing Directive for financial services, eCommerce Directive, etc.) do not make the disclosures digital-friendly.

Likewise, certain GDPR rules and the guidelines adopted by the European Data Protection Board (EDPB) create legal uncertainty that may discourage insurers from introducing new automated processing and profiling techniques.

Avoid short implementation timelines

Deficiencies in the EU law-making process often leave companies with insufficient time to implement the changes they need to make to their processes and to train staff or with increased implementation costs because of frequent changes to the legislation.

For example, companies would have had just two months, once all the Level 2 measures had been developed and adopted, to implement the changes needed to comply with the IDD and its delegated regulations. Only after repeated, strong requests by the insurance industry was a seven-month delay to the implementation date eventually secured.

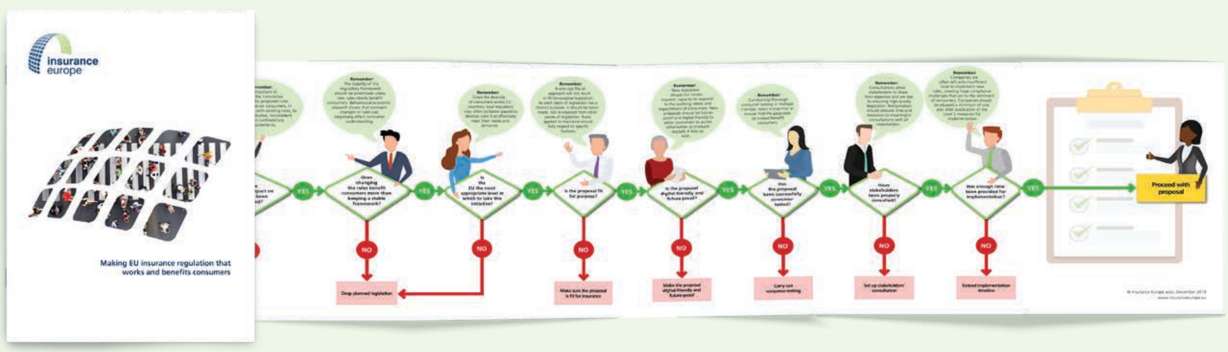
It is unrealistic to expect the industry to begin implementation based on draft texts without the legal certainty of the final regulatory outcome. Instead, there need to be separate timeframes for developing Level 2 and 3 measures and for industry implementation. The industry needs to have at least a year for implementation after final Level 2 texts are published.

Time for a fresh start

While insurers have to deal with the immediate negative consequences of the current "trial and error" approach to EU legislation, the ultimate losers are consumers, since the increase in compliance costs and risks has a negative effect on insurers' ability to provide the variety and quality of services that consumers expect.

A fresh approach by European legislators would be welcome in which: regulation delivers on its intended objective of better protecting consumers; insurers can serve their customers fairly; and compliance costs and risks are kept to a minimum.

Insurance Europe therefore welcomes the 2020 launch of the Fit for Future Platform, a high-level expert group that will help the Commission in its efforts to simplify EU laws and to reduce unnecessary costs as part of the regulatory fitness and performance (REFIT) programme. The insurance industry also appreciates that this new group will examine whether existing laws are digital-friendly.



For more on improving EU financial services regulation, see "Making EU insurance regulation that works and benefits consumers", with its fold-out decision tree "European regulation: how to achieve better quality", December 2019, in the publication section of Insurance Europe's website.

Xavier Larnaudie-Eiffel
Chair, personal insurance committee, Insurance Europe
Deputy CEO, CNP Assurances, France

PENSIONS

It takes two

The Level 2 measures will be crucial to the success of the PEPP pan-European pension product

While the full impact of the COVID-19 crisis is yet to be measured, it will most certainly confirm the need for people to better prepare for their retirement, further emphasising the need for good pension products.

Crucially, therefore, EU policymakers' work on a pan-European personal pension product (PEPP) is not just a theoretical initiative at the heart of the EU plan for a capital markets union; if successful, it could be part of the answer to Europe's ageing challenge.

The PEPP, which is intended to complement national pension regimes and be portable between EU states, was agreed on by EU policymakers in early 2019. At the time of writing, it is reaching another important milestone, as EIOPA submitted to the European Commission in mid-August 2020 the Level 2 measures that will flesh out the details of the Regulation.

A lot depends on Level 2

The development of standards specifying the technical details of the PEPP is a real challenge. This is not only because the text of the PEPP Regulation is unclear, but also because such a long list of standards covering many technical issues is required. The fact that some of these are completely new at EU level — such as the definition of rules to apply to risk-mitigation techniques or the introduction of the requirement for a fee cap — makes EIOPA's task even more challenging.

Digital is desirable

In Insurance Europe's recent survey of what Europeans want from their pensions (see p40), there was a clear preference for receiving information about pensions digitally rather than on paper.

67% of all respondents preferred digital information, rising to 70% of 18 to 35-year-olds. The insurance industry believes a digital-friendly approach to distribution and disclosures is therefore essential for PEPPs and that EIOPA's Level 2 measures are a missed opportunity to develop practical solutions to foster digitalised information documents.

There is also concern that the tight timeline for developing the Level 2 measures foreseen by the Regulation is hampering a smooth and transparent process as well as a sufficient degree of quality for the technical standards, not least because it resulted in EIOPA not submitting fully finalised work.

Danger of complex solutions

Insurance Europe is also concerned by EIOPA's tendency to opt for excessively complex solutions that have not yet been tested. For instance, EIOPA suggests introducing inflation-adjusted performance projections and a completely new cost indicator "reduction in wealth" (RIW) in the PEPP benefit statement. The RIW indicator would provide savers with the difference between projected maturity values with and without costs. The concern is that such an approach would result in figures that do not take into account the extent of the service provided, the length of accumulation and the performance achieved, and are therefore likely to discourage people from making additional contributions to their PEPP.

Along the same lines, EIOPA also wants to introduce "return ambitions", requiring that PEPPs outperform the annual rate of inflation with a probability of at least 80% over 40 years. This goes beyond the letter of the Regulation, which requires a PEPP to ensure "nominal capital protection" and raises the practical questions of how to predict inflation over such a long period of time and whether this could be achieved, especially given the current economic environment.

Another key aspect of the measures is EIOPA's work on the economic stochastic model that it suggests using to support its holistic approach to risk, reward, performance and risk-mitigation techniques. Methodologies to measure PEPP risks and performance, as well as rules governing the eligibility of investment options in the PEPP are a key element in assessing EIOPA's proposals. Insurance Europe understands that EIOPA will now continue work on these preliminary proposals. However, all elements must be made available to policymakers before they decide whether to endorse the PEPP technical standards.

Last but not least, the definition of the fee cap's scope is one of the main issues that will determine distributors' ability and willingness to offer PEPPs. EIOPA proposed an all-inclusive fee cap, meaning that all costs and fees — except biometric, switching and guarantee costs — would not exceed 1% of the capital invested per annum.

Insurance Europe strongly welcomes the fact that EIOPA acknowledged the specific nature of guarantees. Guarantees are not a cost, but a price paid for a particular service, and that price is partly driven by sectoral legislation. However, the inclusion of the cost of advice remains problematic, particularly in the early years of the accumulation period, when upfront costs are added on top of ongoing costs and based on the expected level of contributions to the PEPP. An exclusion of advice costs, even if partial and temporary, as well as the possibility to consider average costs instead of annual costs, seem necessary conditions for providers to be able to design and launch high-quality PEPPs on the market.

All in all, the impression is that while the end of the legislative process is in sight, the PEPP discussions are far from over. Insurance Europe appreciates EIOPA's intense work and efforts, and acknowledges how difficult a task PEPP is, but it urges authorities and policymakers to take the time needed to get this important legislation right. Insurers, as major providers of personal pensions products, stand ready to continue to contribute to this.

Juan Fernández Palacios
Vice-chair, personal insurance committee, Insurance Europe
CEO, Mapfre Vida, Spain

PENSION SURVEY

Glass half full

With nearly half of Europeans not saving for retirement, Insurance Europe's pension survey contains clear messages for policymakers

With an estimated €2trn a year needed in additional retirement savings in Europe, pensions are high on the political agenda and individuals are increasingly being called on to take responsibility for their future retirement income. As the European federation representing major providers of pension products, Insurance Europe carried out a survey of over 10 000 people in 10 countries to find out how they are preparing financially for retirement and what they expect from their pensions.

It discovered that a staggering 43% were not saving for their retirement. Although nearly two-thirds of those said that they were interested in saving, a worrying 42% felt they could not afford to. More women than men were not saving, as were more younger people and people with lower educational qualifications. These results clearly show that there is a pressing need to raise awareness of the need for pension saving and to improve levels of financial literacy so that individuals can make the most appropriate decisions for their circumstances.

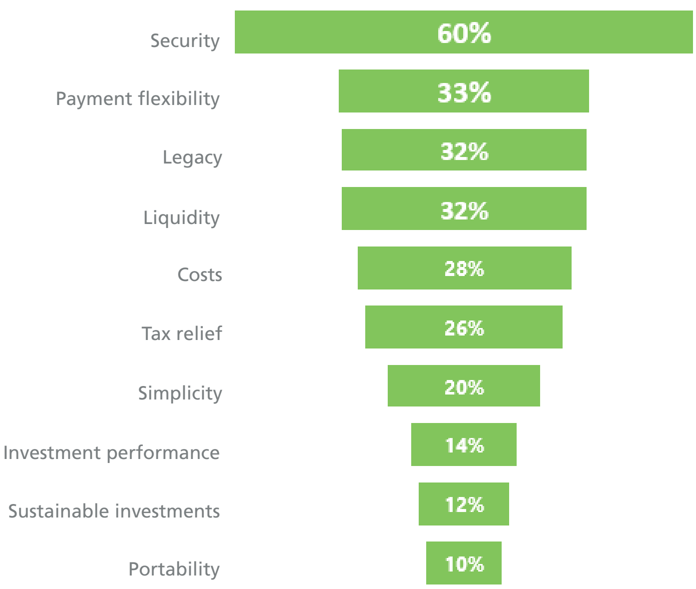
Pension priorities

Among the survey respondents, by far their highest priority when saving for retirement was the security of the money they had invested. Also important were being able to increase or stop contributions (flexibility), to leave savings to descendants (legacy) and to transfer or access savings (liquidity). Least important to those surveyed was being able to move savings between European

Key survey findings

1. Almost half of respondents are not saving for retirement
2. Security is by far the most important priority when it comes to retirement
3. Pension savers prefer to receive information digitally rather than on paper
4. In all the survey areas, there are significant differences between countries
5. Responses are also influenced by personal circumstances such as age, gender and employment

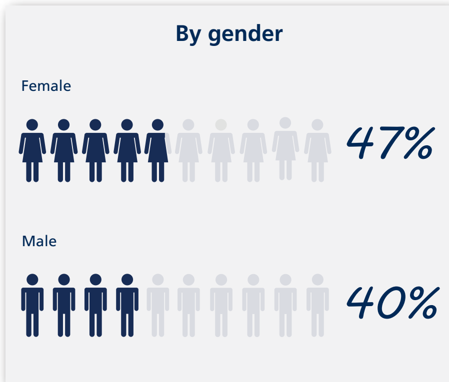
Pension saving priorities

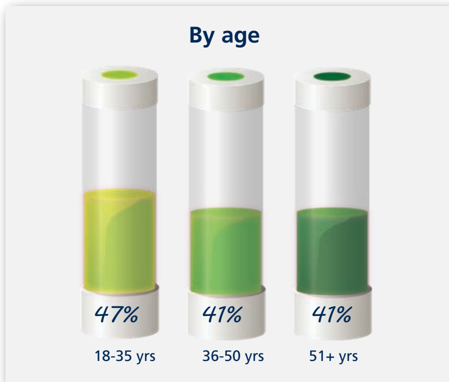


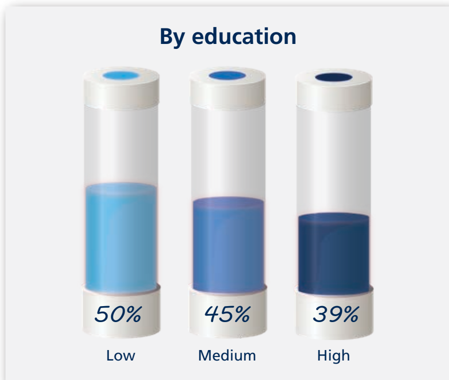
About the survey

- Date: August 2019
- 10 142 respondents
- 10 countries: Austria, France, Germany, Hungary, Italy, Luxembourg, Poland, Portugal, Spain, Switzerland
- A representative sample:
  - 49% female, 51% male
  - Aged from 18 to 65
  - Different employment statuses
  - Different education levels
  - Different marital statuses

Respondents not saving





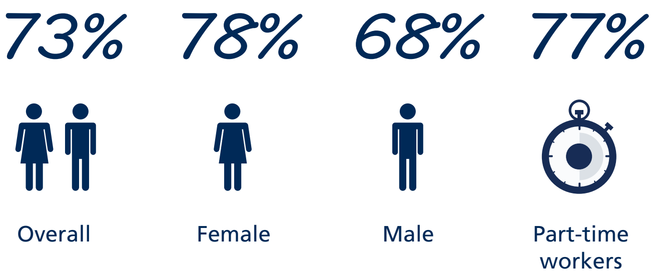


countries (portability). These priorities were, of course, affected by individual circumstances, such as age, employment status or gender. The survey thus confirms the need for pension policies to be consumer-centric, based on evidence of users' demands and needs.

Safety or performance?

Pension saving can take different forms. What marks out the products offered by insurers is their ability to offer financial protection against a broad range of risks: investment, longevity, mortality and morbidity (ill health). For their retirement savings, respondents overwhelmingly (73%) chose investment safety over performance.

Safety favoured over performance



A significant proportion of respondents expressed interest in buying additional cover for biometric risks: 46% were interested in mortality cover, 43% longevity and 40% morbidity. There is thus a clear appetite for certain protective features traditionally offered by insurers, such as annuities and guarantees, making it crucial that pension policies enable insurers to fulfil their important role in tackling the pension savings gap.

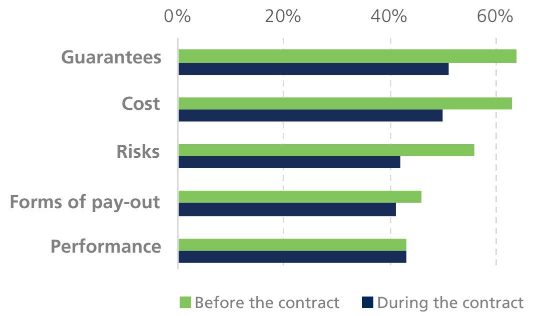
Those preferences were reflected in the information that savers wanted to receive, with survey respondents most interested in learning about the guarantees included with a particular product, both before signing the contract and once it was in force. Such information was valued even more than that on cost or risks. And over two-thirds of respondents preferred to receive information digitally rather than on paper, demonstrating that pension policies must allow providers to engage in innovative ways with their customers.

Projecting the future

Interestingly, people's responses on how they preferred to receive their pension savings at retirement varied depending on whether they were given projections of the amounts they would be likely to receive. Without projections, people preferred annuities over flexible withdrawals or lump sums, whereas with projections there was an even split between those choosing annuities and lump sums.

Overall, the survey confirmed the diversity inherent in retirement saving across Europe. Pensions come in various forms and are influenced by a broad range of factors. As a result, there is no one-size-fits-all approach that tackles all the challenges. A combined effort by both national and EU policymakers is needed if Europe's citizens are to enjoy a financially secure retirement.

Top five information priorities



Janina Clark
Editorial manager, Insurance Europe

FINANCIAL EDUCATION

Testing times

In times of economic crisis, citizens need the financial literacy to remain economically resilient

"If there is a moment for [financial education] it is now." So said Mario Nava in March 2020, when he was director of horizontal policies in the European Commission's directorate-general for EU policy on finance. He was speaking during a webinar on building financial resilience in turbulent times, which was organised by the European Banking Federation and in which Insurance Europe also participated.

It is certainly true that in the difficult economic environment created by the COVID-19 pandemic and government lockdowns it is more important than ever that individuals and companies have the skills to make appropriate financial decisions and choose the right financial products for their situation. As bankruptcies and unemployment rise and recessions loom, it is also worth remembering that it is those with low literacy skills who are more likely to have financial problems and could be more tempted to make the short-term decisions to raid pension pots or cancel insurance policies that have such serious long-term consequences.

The increasing shift to digital activities and transactions that was prompted by national lockdowns and social distancing have also dramatically altered how people access financial services, bringing into the spotlight the importance of including digital skills in any financial education efforts. Insurance Europe was therefore pleased to see the Commission referring to the promotion of financial education and digital financial skills in the April 2020 consultation

"The increasing shift to digital activities and transactions that was prompted by national lockdowns and social distancing have dramatically altered how people access financial services, bringing into the spotlight the importance of including digital skills in any financial education efforts."

on its new digital finance strategy, which is expected in the third quarter of 2020.

Not a new problem

Stark figures showing how much individuals struggle with financial matters are nothing new. "Large groups of citizens are lacking the necessary financial literacy and financial resilience to deal effectively with everyday financial management," concluded an international survey of adult financial literacy carried out by the OECD/International Network on Financial Education (INFE) in 26 countries and economies in Europe, Asia and Latin America, which was published in June 2020.

Scoring the maximum of 21 in the OECD/INFE test would demonstrate a basic level of understanding of financial concepts and the application of some prudent principles in financial dealings, yet individuals across the entire sample averaged a score of just 12.7. "These scores suggest that there is plenty of room for improvement across all the elements of financial literacy," said the OECD.

Gaps in financial literacy are clear from an early age. Around one in four of the 117 000 15-year-olds from 20 countries and economies who took part in the latest OECD PISA test[1] of financial literacy are unable to make even simple decisions on spending. And only one in 10 students from the 13 OECD countries and economies who took the test performed at the highest level of financial literacy.

Financial education should, of course, be a lifelong process and Insurance Europe's own recent pan-European survey of adults' retirement saving habits (see p40) confirmed the pressing need to improve levels of financial literacy and awareness among adults, since it revealed that nearly half of Europeans are not saving for their retirement.

And a US survey, the third annual TIAA Institute-GFLEC Personal Finance Index[2] of adults in 2019, confirmed clear variations between demographic groups, with women, the young, those with lower levels of education, the unemployed and the disabled all more likely to be less financially literate. Worryingly for the insurance industry, understanding risk was the area in which financial literacy was found to be the lowest in the TIAA Institute/GFLEC study.

New Insurance Europe publications

Insurance Europe and its member associations have long been actively engaged in efforts to raise levels of financial literacy,

1 Programme for International Student Assessment, OECD, 2018
2 "Financial Literacy in the US and Its Link to Financial Wellness — The 2019 Teachers Insurance and Annuity Association Institute-Global Financial Literacy Excellence Center Personal Finance Index"

InsureWisely campaign: new publications

specifically in relation to risk awareness, insurance and long-term saving for retirement.

Since 2018, Insurance Europe's work in this area has come under the "InsureWisely" label. December 2019 saw publication of the fourth in its thematic infographic factsheets, this time on natural catastrophes. The one-pager sets out advice on reducing risks, choosing the right policy and making a claim. And, in June 2020, Insurance Europe published a booklet entitled "Insure yourself wisely". The booklet offers useful tips on how best to insure for key life events such as buying a house or car, going on holiday or retiring.

Welcome for EU action

While education is a matter for national governments, Insurance Europe welcomes efforts at EU level to promote financial literacy. It was pleased to see in the December 2019 conclusions of the Council of the EU on the initiative to deepen the capital markets union (CMU) that to increase retail participation in capital markets the Council proposed to "promote financial literacy (for both retail investors and SMEs) and facilitate the exchange of best practices and views on national measures in this regard".

Likewise, it is pleasing that the final report that was published in June 2020 by the High-Level Forum on the CMU — which was set up by the Commission to review progress on the initiative and propose new actions — recognised financial knowledge and skills as a priority. The Forum proposed an EU framework on financial competence, suggested that the EU fund financial literacy projects and the exchange of best practices, and recommended requiring member states to promote measures to support financial education.

While it is encouraging to see such recognition of the importance of financial education, EU policymakers and regulators could play a greater role. A starting point could be a European Day of Financial Education organised by the EC, on which policymakers, citizens, the financial sector, education providers and social partners could share best practices and new approaches to financial education. EIOPA could also do more to fulfil the obligations in its founding Regulation to coordinate financial literacy and education initiatives by national authorities.

However tempting the need for budget savings might currently be, now is certainly not the time for the many players who do such great work improving financial education — among them governments, schools, international organisations, NGOs and financial services providers — to scale back their efforts. The financial resilience and well-being of citizens is too closely linked to their levels of financial literacy.

Jérôme Roncoroni
Chair, conduct of business committee, Insurance Europe
Internal audit director, Covéa, France

PRIIPS REGULATION

Information is key

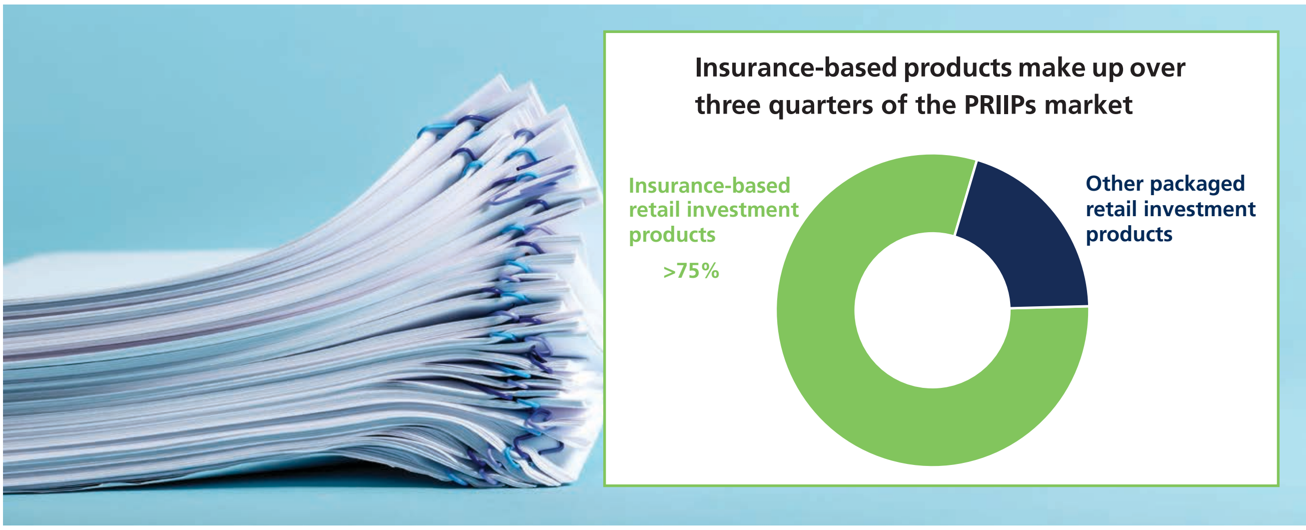
Quality must come before speed in the changes needed to make the key information documents for PRIIPs work for customers

Providing consumers with clear and accurate information is vital to help them make good investment decisions. The key information documents (KIDs) produced in accordance with the EU's Packaged Retail and Insurance-based Investment Products (PRIIPs) Regulation do not, however, always do this. KIDs can fall short of giving the "fair, clear and not misleading" information they are meant to, and it is easy to see why.

Policymakers embarked on designing the PRIIPs KID without a clear idea of the products and providers they were aiming to regulate. Insurance companies are the major providers of PRIIPs, but the Regulation was not drafted with insurers in mind. Instead, the focus was on investment funds which, for the most part, are temporarily exempted from the rules.

Not only does this make the KID unsuitable for insurance products, it also means it fails to respect the variation between insurance products and prevents insurers from providing accurate information on the range of features they can offer. Nowhere is this problem more obvious than the "what is this product?" section, which prioritises information on investment strategies over basic details of the insurance coverage included.

PRIIPs has the very simple objective of informing investors about products using language they can understand. This should have made it easier to compare products' costs, performance and risk.



Unfortunately, comparing products using the PRIIPs KID is almost impossible. The focus on creating a standardised document has led to a concerning level of prescriptiveness that puts uniformity of appearance ahead of accuracy.

The problems with the KID persist despite, or even because, of a series of measures intended to address its most serious flaws. There has been a steady stream of questions and answers, delays, guidance, supervisory statements and proposed RTS changes (see timeline on p48) that have isolated specific issues and attempted to address them individually. Throughout, policymakers and the industry have had no time to step back and look at where things went wrong in the first place.

Rushed proposals

In 2020, this culminated in a further set of flawed proposals to amend the PRIIPs KID, coming as the result of political pressure and an apparent urgency to "get something done" before UCITS funds come within the scope of the Regulation in 2022.

> **"The focus on creating a standardised PRIIPs KID has led to a concerning level of prescriptiveness that puts uniformity of appearance ahead of accuracy."**

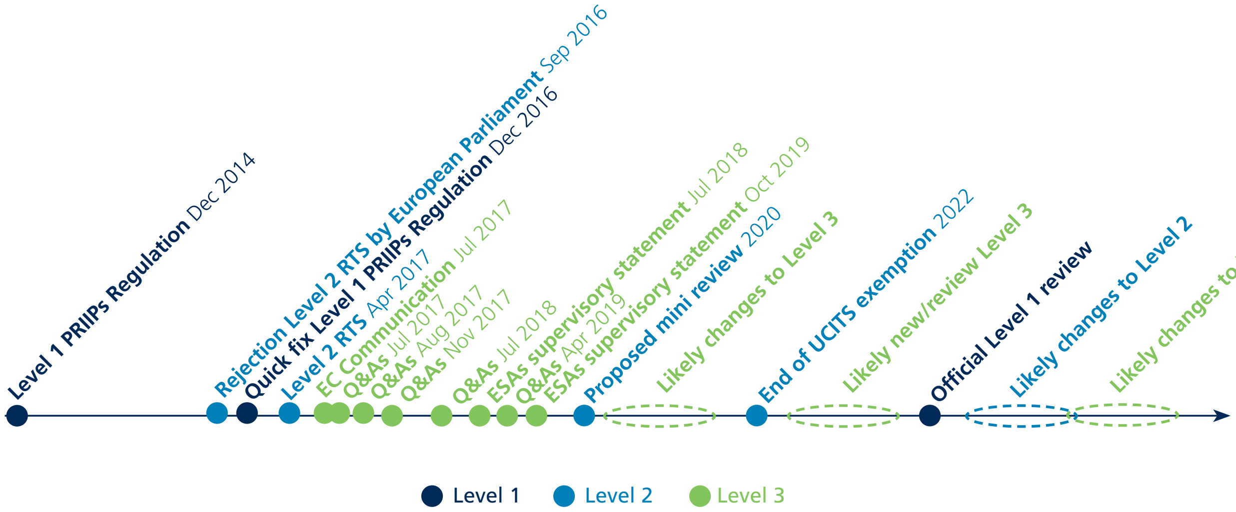
The proposed changes looked set to make matters even worse; introducing a range of new ways of presenting the likely performance of products through links to other documents, "backward-looking scenarios" and room for discretion for PRIIPs producers to use lower estimations of future returns, all while leaving the problematic existing methodology in place for insurers' non-linear and guaranteed products. On costs, the previous need for absolute comparability was set aside, but only to introduce a much weaker cost indicator for most investment funds. And again, the needs of insurance customers were sidelined, with the proposed treatment of multi-option products — a key product type in many markets — having no grounding in reality.

The EIOPA Board of Supervisors was right in July 2020 to reject these fundamentally flawed proposals. Until there is another look at how to address the tension between broad scope and comparability and to reassess the prescriptiveness in the rules, no amount of small changes will create a workable Regulation.

Flawed process, flawed outcomes

The insurance industry expressed concerns early on that the flawed process for adopting the regulatory technical standards (RTS) governing the form and content of the PRIIPs KID would lead to flawed outcomes. No new rules benefit from not being tested and to a large extent the PRIIPs RTS were not. The testing

Continual changes to the PRIIPs framework



carried out on the original KID was far too limited, excluding some markets and many variants of insurance-based investment products. The latest round of proposals for RTS changes were subject to testing that was even more limited in scope.

Had the European Commission and the supervisory authorities really looked at how their proposals worked for everything in the scope of PRIIPs, it would have been clear at every stage that they fell short. Rules that work for all products can only be devised if they are really tested. And when some ideas fail during testing, new proposals must be devised and tested. The quick fixes seen so far have been adopted in a timeframe that does not allow for this kind of evidence-based approach.

Doing the right thing

Too much time has been lost on doing the wrong thing. It is now urgent to consider how to approach the problem of the PRIIPs KID differently. The good news is that the Commission is already doing the right thing.

A study has been launched to look at the KID in its entirety and in conjunction with all other legislation covering the information provided to consumers. It will include consumer-testing, legislative-mapping and mystery-shopping exercises and will look at a broader range of products than any previous testing. It is vital that this study takes a rigorous approach to assessing the problems with PRIIPs and that it reframes the discussion to focus on consumers and their needs and experiences.

And then? The necessary time must be taken to find solutions that really work for all products before changes are made. With the current proposed changes on hold, insurers, NGOs, regulators and policymakers need to use the breathing space to go back to the drawing board and come up with new ways of presenting information that offer real benefit for consumers.

This will mean looking again at how information can be presented digitally, and at how the new digital landscape is shaping consumers' expectations. Is the idea that consumers need comparability between all product types outdated in a world where consumers expect to be digitally guided to the type of product that suits them best? If so, a rethink is needed about how best to arm consumers with useful information for making investment decisions in this digital environment.

It will also mean grappling again with the controversial issues around presenting costs and performance for each of the diverse product types covered by PRIIPs. The EC's work on assessing the current regulatory environment will be a solid foundation on which to carry this out. An evidence-based approach to fixing the KID is the only way to meet consumers' need for fair and accurate information that supports their investment choices.

William Vidonja
Head of conduct of business, Insurance Europe

DISTRIBUTION

Quo vadis?

As the EU regime for insurance distribution comes up for review, what needs to be considered?

It is almost exactly two years since the Insurance Distribution Directive (IDD) was applied across the EU. The IDD was intended to update and modernise existing rules on insurance mediation to bring about enhanced consumer protection and increased transparency. Two years on, there is now enough experience to take stock of whether these improvements have come to fruition and whether there is any more that could be done to ensure the best outcomes for consumers.

Significant improvements

The improvements in consumers' experiences when buying insurance have been significant. New processes are now in place to make sure consumers are consistently offered products that meet their needs and expectations.

The IDD's enhanced rules on cross-selling have ensured customers are made aware of when they can buy products separately; providing transparency and giving customers choices in how they purchase linked products. The new "demands and needs" test goes further than rules in any other sector in requiring insurers to match customers' requirements to the products made available to them, even for non-advised sales. This has greatly strengthened protection from the risk of mis-selling. The new insurance product information documents (IPIDs) facilitate informed decision-making, providing customers with the information they need to choose a non-life product that is right for them.

Greater governance

Beyond these improvements at the point of sale, customers are also benefiting from strengthened product oversight and governance (POG) rules. IDD product approval processes have created an environment in which the needs of a product's target market are central to product design and review. POG rules require insurers to continually evaluate their products to ensure they are still providing value to consumers. These evaluations enable insurers to adapt products and take action when external factors change the added value their products provide to customers.

The improvements brought about by the IDD have come about because it works with, not against, existing distribution systems.

Insurance is typically distributed in a very different manner to other financial services. Insurance intermediaries are often SMEs with a limited number of employees. IDD rules are not unduly burdensome for these companies, while still ensuring consumers have an appropriate level of protection.

The IDD is also workable for all insurance products — both life and non-life — and only differentiates between them where this is necessary in light of the nature of the product. Additional rules applicable only to insurance-based investment products, including introducing high standards for financial advice, are proportionate and reflect the additional support customers need when considering these products.

Suitably flexible

The IDD also respects national differences. It aligns national rules where appropriate but maintains the flexibility needed for national regulators to consider existing national practices and customer expectations when applying the rules. The result is an insurance market in which consumers can expect the same high standards of product design, transparency and conduct of business, but in which local providers are still able to provide them with the services on which they have always relied. In short, the IDD is working well.

Review time

So where do we go from here? The European Commission is currently reviewing the entire distribution regime for insurers and has commissioned an extensive external study of how the insurance market operates.

> **"The EC review needs to build on the successes of the IDD, not seek to amend it without good cause."**

This study will only result in meaningful improvements for consumers if it takes a holistic view of the distribution regime and focuses on the entire customer experience — from the initial sales process right through to the insurers' ongoing relationship with their customers through periodic reporting and product review.

The study needs to clearly identify the needs of customers and assess whether they are being met. And then, where there are found to be weaknesses, targeted action needs to be taken. Legislators need to avoid interfering with and altering a legislative framework that is meeting its objectives, and should instead ask whether proper application of existing rules could address any concerns. Where there are identifiable problems, these need to be solved and legislative change will be part of that. Where there are no problems to fix, that means there is no need for ineffective solutions and tinkering.

The IDD will be reviewed in 2022 in light of the findings of the study. The EC review needs to build on the successes of the IDD, not seek to amend it without good cause. It is worth bearing in mind that until now no supervisory issues with the IDD have come to light since its implementation and, in some instances, regulators have considered additional actions but then seen that there is currently no need within the market for extra intervention.

But that does not mean settling for stasis. We need to look to the future and see where the IDD can be improved to continue to meet the evolving needs of customers in the digital world. Online distribution will soon become the norm (see also article opposite) and the IDD needs to be able to meet that challenge.

This will not be achieved through prescriptive rules but through a sensitive and flexible approach. Insurance distribution rules need to continue to support consumers navigating financial markets, not restrict insurers' provision of the services their customers need.

Frédéric de Courtois
Vice-president, Insurance Europe
General manager, Generali Group, Italy

INSURTECH

Metamorphosis

The digital transformation of insurance has been given a boost by the pandemic, but the EU regulatory framework must keep pace

Insurance customers are embracing innovation in insurance and seeking out new offerings that respond to their needs and make their interactions with insurers more convenient. The insurance industry continues to strive to meet these expectations and use new technologies to better serve its customers.

However, it will be crucial to ensure an appropriate EU regulatory framework that is conducive to innovation and allows consumers, established companies and new market entrants to benefit from the opportunities that digitalisation can offer. This entails removing any regulatory barriers that hold back innovation, facilitating a data-driven financial sector and supporting greater uptake of new technologies. The more detailed or prescriptive the regulatory requirements are, the more difficult it becomes for the financial sector to innovate.

The COVID-19 pandemic has further emphasised the vital importance of digital transformation for society and the need for strong and innovative digital capacities in the financial sector. It is up to the EU institutions to lay the right foundations for European businesses to thrive, innovate and contribute to the overall goal of enhancing Europe's digital sovereignty.

Consultation on AI

Artificial intelligence (AI) has the potential to transform the modern world, and its applications in insurance are already improving

“AI is expected to help insurers to predict risk with greater accuracy, to customise products and to use enhanced foresight to rapidly deploy new products in response to emerging risks.”

customer service, increasing efficiency, providing greater insight into customers’ needs and preventing fraudulent transactions. AI is expected to help insurers to predict risk with greater accuracy, to customise products and to use enhanced foresight to rapidly deploy new products in response to emerging risks.

Any future regulatory framework for AI needs to be consistent with the overall objectives of the EU to promote and encourage innovation, while ensuring respect for European values and principles. There is a clear need to foster a principles-based approach and to avoid unnecessarily prescriptive rules, which could increase Europe’s dependence on technology and services from other regions, thereby putting European businesses at a competitive disadvantage.

Insurance Europe published a position paper on AI and responded to the European Commission consultation on its AI White Paper in June 2020. It highlighted insurers’ support for the adoption and deployment of ethical, trustworthy and human-centric AI via an appropriate and proportionate principles-based framework. It noted that the development and use of AI are already covered by a wide range of existing EU legislation that addresses many of the potential risks and challenges, and called on policymakers to examine where existing legislation, such as the General Data Protection Regulation (GDPR) creates barriers to the use or development of AI.

Insurance Europe has also been engaging with the European Parliament as it works on developing its own-initiative legislative proposals on a civil liability regime and a separate framework for ethical aspects of AI, robotics and related technologies.

Developing a data strategy

Many applications of AI depend on the availability of high-quality data or use machine-learning or deep-learning techniques to achieve their results. One of the major challenges faced by insurers when developing AI systems is the restricted or limited access to data that could improve such systems and create better service for customers. This raises questions over how access to this data should be governed, as well as technical issues of interoperability and the standardisation of data.

Insurance Europe supports actions at EU level to promote and support the development and uptake of AI, notably through facilitating the access to and use of the data that is so essential. The development of a common EU data strategy — one of the key focus areas of the Commission — will hopefully provide an opportunity for the EU to adopt a future-proof, innovation-friendly framework that supports data-driven business and enables the digital transformation of society, while ensuring appropriate protection for consumers.

Greater availability of data could help insurers to improve risk

monitoring and assessment, offer a better customer experience and increase fraud detection. The more data that is available for the common good, the better the digital solutions and analytical models will be.

Individuals should also be able to allow access to their personal data to a much greater extent than is possible today. There should, for example, be practical solutions that would allow individuals to exercise control over their own data, with appropriate consideration given to the security of sensitive data. Individuals should be able to grant other parties access to the data they generate. For instance, if a customer decides that an insurance undertaking may access their driving data, the vehicle manufacturer should grant access on reasonable terms (see article on p61).

Enhancing legislation on accessing, processing and sharing data will be important to promote innovation and competition. The insurance industry is supportive of efforts to facilitate appropriate data-sharing based on voluntary agreements and a true level playing field between different players. However, much will depend on the specific model and implementation chosen for any data-sharing framework. Insurance Europe responded to the EC consultation on its data strategy in June 2020 and stands ready to further engage in shaping the right framework.

EC digital finance strategy awaited

The EC's digital finance strategy is expected to be published by the end of the third quarter of 2020 and it will set the course for how digital finance evolves in the EU over the next five years.

In its response to the EC's consultation on its strategy, Insurance Europe highlighted the importance of ensuring that the financial services regulatory framework is innovation- and digital-friendly, technologically neutral and sufficiently future-proof to be fit for the digital age.

New technological opportunities and customer behaviour inevitably give rise to new service concepts, and new service providers have entered the market. For these providers, regulatory requirements can often be less strict than those faced by the traditional financial services industry. For the insurance sector, it is therefore crucial to respect the principle of "same activities, same risks, same rules" and strive for a true level playing field between all market players.

Maintaining a level playing field between European insurers and bigtech players will be key, particularly in terms of access to data and potential data monopolies. This not only means ensuring that any new players are brought within the insurance regulatory framework where they engage in the same activities, but also making sure that established insurers are not unduly restricted in their ability to compete due to current requirements in the European financial sector's already comprehensive regulation and supervision. For example, the impact of "existing activities" restrictions for financial institutions' non-core business (eg Article 18 of the Solvency II Directive) should be reviewed to determine whether they remain proportionate.

The crucial issue is to ensure that insurance customers enjoy the same level of protection, regardless of whether they are served by established providers or new entrants, who may be small start-ups or global bigtech companies. All elements of the insurance value chain are sufficiently regulated and serve the regulatory objective of policyholder protection. New entrants to the insurance market should therefore be brought within insurance regulation. The average customer does not differentiate between an incumbent provider or a new entrant. In both cases, the customer should be equally protected.

It will also be incumbent upon policymakers to ensure that rather than automatically looking to introduce new regulation, the application of existing rules should be reviewed to see how they could be adapted to meet digital developments without incurring major regulatory change.

For example, GDPR requirements create legal uncertainty and limit the potential use of blockchain and distributed ledger technologies (see also p58). They also create difficulties for the development of machine-learning models and the data on which they can be based. These limits on data usage do not take into account the needs of reliable AI development and may inhibit the EC's aim to make Europe a world leader in AI. It would therefore be worth considering the recommendations of the Expert Group on Regulatory Obstacles to Financial Innovation, which propose issuing guidance on the application of the GDPR in relation to the use of new technologies in financial services.

Insurers need to be able to innovate and explore the use of new technologies to respond to consumers' digital expectations and offer enhanced experience and convenience. To do this, an appropriate and proportionate regulatory framework is required. It is now for the European institutions to develop and adopt measures to ensure that the EU's regulatory and supervisory frameworks are fit for the digital world and do not hinder innovation. Initial steps are at least encouraging, but there is a lot of work ahead to ensure that insurers and customers alike can fully reap the benefits of digitalisation.

Outsourcing to the cloud

Cloud services form an important part of the digitalisation of the financial sector, but a number of barriers to their adoption still exist under the EU regulatory framework. These include uncertainty over cloud service provider compliance with EU data protection requirements (eg data location) and challenges regarding the requirements to audit the provider, creating a need to rely more than is currently possible on certification schemes or third-party audits. This means that financial institutions are not always able to avail themselves of the technology as often as they would wish.

Insurance Europe has been heavily engaged with EIOPA and the European Commission on cloud services. In February 2020, EIOPA published its guidelines on outsourcing to cloud service providers, which addressed the majority of the concerns raised by the insurance industry during the consultation. The draft guidelines had already developed positively as a result of dialogue with the industry and the final guidelines demonstrated EIOPA's awareness of the importance of the cloud for insurers, as well as its willingness to facilitate greater uptake.

Insurance Europe has also been in discussions with the EC to encourage and facilitate the development of standard contractual clauses for cloud outsourcing by financial institutions. Developing such model clauses would allow institutions to better reflect their regulatory constraints, eg Solvency II for insurance, in their contractual agreements with providers. Insurance Europe led the industry's involvement in an EC workshop for the financial sector and followed up with further input on how to develop standard clauses for cloud use in the financial sector.

Regulators and supervisors need a common approach towards cloud-computing that supports the EC's overall digital strategy to boost the use of AI and data-driven innovation. The use of standard clauses will certainly help insurers in their dealings with cloud providers, but ensuring effective supervisory oversight of cloud service providers will also be necessary.

Nicolas Jeanmart
Head of personal & general insurance, Insurance Europe

CYBER RISKS

A challenge and an opportunity

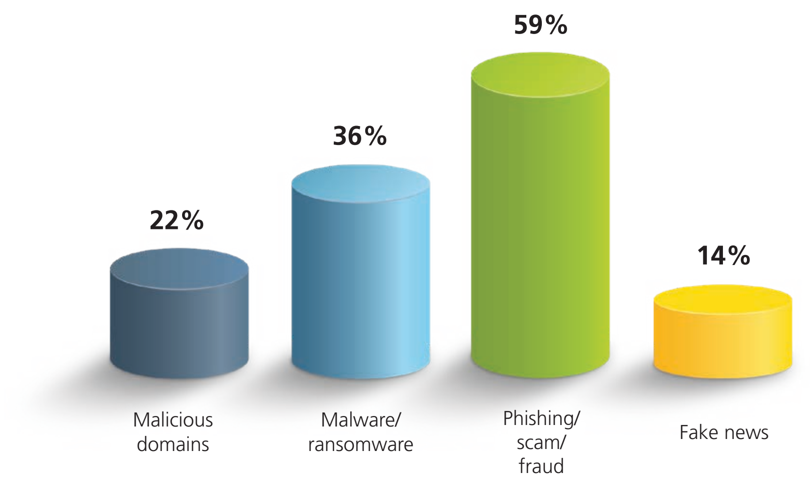
Insurers are both protectors and targets in the world of cyber risks

Many societal changes have been accelerated by the COVID-19 pandemic, but none more so than the digital transformation. Around the world, businesses large and small, including most insurers, have been forced to make the move to home-working in an effort to slow the spread of the coronavirus and protect their employees and customers, relying almost exclusively on digital technologies in order to stay in touch and keep operating. Both the capacity and security of IT systems have been brought sharply into focus, with Europol, the EU's law enforcement agency, reporting that the unprecedented shift in cyber activity has seen a corresponding rise in cyber criminality.

This comes at a time when insurance industry players and EU policymakers alike were already stepping up efforts to draw benefits from increasing digitalisation, while limiting as much as possible the associated risks.

On the side of EU policymakers, the European Commission of Ursula von der Leyen, which took office in December 2019 on a twin platform of sustainability and digitalisation, vowed to add to the patchwork of cybersecurity rules in the EU. Policymakers want to build on the General Data Protection Regulation (GDPR), which celebrated its second birthday in May 2020 (see p58), the Network and Information Security (NIS) Directive, which is heading for review at the end of 2020, and the Cybersecurity Act, which entered into force in June 2019. While these rules focus

% of Interpol countries reporting COVID-19-related cyber threats



Source: "COVID-19 Cybercrime Analysis Report", Interpol, August 2020

on businesses that process personal data (GDPR), undertake essential services (NIS) or want to certify their products, processes and services (Cybersecurity Act), policymakers are now looking directly at financial institutions, seeking to address a perceived gap in their cybersecurity and increase the "digital operational resilience" of the sector as a whole.

With this in mind, the Commission consulted on a "framework" of new information and communications technology (ICT) rules aimed at bringing all aspects of the cybersecurity of the financial sector together under one piece of legislation. The Commission's goal is to establish requirements for all organisations across the financial sector, including insurers, in the areas of:

- ICT risk management
- Incident-reporting and information-sharing
- Stress-testing of ICT infrastructure
- Oversight of critical ICT third-party service providers

No one-size-fits-all approach

If adopted, the Commission's envisaged approach could change the landscape of cyber incident management, reporting and prevention across the EU financial sector. For Insurance Europe, it is key in this process to keep in mind that the financial sector is not uniform, as organisations differ greatly — not only in their type, size and profile, but also in the risks to which they are exposed and the systems and services that need to be protected and maintained. European insurers are therefore calling for a risk-based approach to cyber resilience, distinguishing between critical and less critical functions.

Alignment of rules

The Commission is not the only body with its eye on strengthening the cybersecurity of the insurance industry, as EIOPA will also publish sector-specific guidelines on ICT security and governance for the insurance industry. Insurance Europe has therefore called for alignment between the various EU-level initiatives to avoid any multiplication of obligations and requirements placed on organisations — all of which are intended to achieve the same goal. For this same reason, insurers would also like reporting requirements, under the GDPR, the NIS Directive (where relevant) and a future Digital Operational Resilience Framework, to be streamlined.

Two sides of the same coin

In the area of cybersecurity, the (re)insurance industry occupies a unique position, both as a sector that finds itself increasingly vulnerable to cyber attacks and as a business that can offer protection through a range of cyber insurance products and services.

Insurance Europe's cyber policy recommendations

DO

- Promote awareness-raising, which is key to increasing cyber resilience
- Support public-private cooperation on catastrophic risks
- Urge member states to act to increase cybersecurity
- Support efforts to make cyber-incident data available

DON'T

- Introduce premature standardisation, which can harm both customers and insurers
- Introduce mandatory insurance for cyber risks, which would be counterproductive

Cyber insurance has a key role to play in helping European businesses to become more cyber-resilient, offering many different services, both before and after an incident. Cyber insurance can also enhance the competitiveness of European businesses — helping to foster an appetite for innovation in areas of digital technology by providing a safety net so that, if things go wrong, they do not bear the risks alone.

It is better for businesses, though, if they have less need to avail themselves of damage cover or *ex-post* support, and insurers also have a key role to play in prevention — making businesses aware of their possible exposures by assessing their "IT hygiene".

During the COVID-19 pandemic, insurers have been active in the area of prevention, and several national associations have run campaigns to raise awareness of the risks associated with home-working, including the increased vulnerability of businesses due to use of private home networks and computers. Indeed, the pandemic has confirmed the importance of cyber resilience for businesses of all sizes (see chart opposite) and has highlighted the key role of insurers in the prevention, mitigation and transfer of cyber risk.

Policy "dos and don'ts"

Though traditionally seen to be lagging behind its sister market in the US, the European cyber insurance market is growing year-on-year, thus contributing to increasing Europe's cyber resilience. In October 2019, Insurance Europe published a booklet containing recommendations — "dos and don'ts" (see box above) — for policymakers when looking to further encourage the growth of the market.

Among these recommendations, European insurers call for support from policymakers across the EU in the area of awareness-raising, public-private cooperation and increased access to data on cyber incidents.

On the subject of data, Insurance Europe is in favour of leveraging on existing data on cyber incidents, such as incident data gathered under the GDPR and the NIS Directive — and possible future data to be gathered under the Digital Operational Resilience Framework. To this end, back in 2018, Insurance Europe already developed a template for breach notifications under the GDPR, which would allow for data to be gathered in an anonymised but sufficiently granular format to be of use to the insurance industry.

In terms of policy "don'ts", European insurers advise against the introduction of premature standardisation or mandatory insurance for cyber risks, as this would hamper a market that is growing but is yet to reach its full maturity.

William Vidonja
Head of conduct of business, Insurance Europe

DATA PROTECTION

Too early to amend, not too late to improve

Although in its infancy, the EU's General Data Protection Regulation can still be improved

Without data, insurers could not operate. They would be unable to develop and price their policies, process claims or spot fraud. Insurers have therefore always been strong supporters of the objectives of the EU's General Data Protection Regulation (GDPR).

As data processing lies at the very heart of insurers' business, they are acutely aware of the value of data and the importance of protecting it. So, Insurance Europe wants the Regulation to provide the best protection for insurance customers' data and to drive businesses to compete responsibly in the digital world.

Time for a second look

Implementing one of the EU's most demanding pieces of legislation has been challenging for companies, insurers included, and they have dedicated significant time and resources to become compliant. Now that the GDPR has been in force for over two years, it has become apparent that work is also needed to address problems in some specific areas of the legislation and to ensure it meets its aims, which are to safeguard Europeans' fundamental right to have their privacy and personal data protected — and protected consistently — across the EU.

The first of the problems from an insurance perspective is the impact of the GDPR on innovation, where obstacles have unintentionally been created. The use of new technologies — blockchain technology, artificial intelligence, big data, the internet

What is the GDPR?

The European regulatory framework for data protection — the GDPR — has been in force since May 2018. Arguably the most comprehensive data protection regime in the world, its aims include:

- strengthening individuals' rights to control their personal data;
- introducing a single regulatory framework applicable in all EU member states and ending the patchwork of data privacy laws; and,
- updating privacy rules in the light of technological advances and ensuring their effectiveness in an increasingly data-driven economy.

The GDPR also created a European Data Protection Board and a European Data Protection Supervisor, which have become Europe's data protection watchdogs.

of things — creates significant opportunities for insurers to expand and improve the products they can offer consumers (see insurtech article on p51). However, such innovation could be undermined by provisions in the GDPR or in the European Data Protection Board (EDPB) guidelines because they do not entirely respect the principle of technological neutrality.

Indeed, certain rules are at odds with fast-evolving technology and may slow the pace of insurers' digital innovation. For instance, blockchain technologies have the potential to reduce costs and increase transparency, as well as to reinforce trust. Yet blockchain technology is designed to be an immutable and permanent record of all transactions, so it is hard to reconcile with the GDPR's right to be forgotten and right to rectification under which records may be removed or changed.

Likewise, due to a very narrow interpretation of the "necessity" of carrying out solely automated processes, the guidelines may discourage insurers from introducing automated processes. This may prevent the development of innovative products, such as real-time insurance offered through mobile phone apps, despite these enabling insurers to serve consumers better, faster and at lower cost. Insurance Europe would therefore like to see the European Commission work closely with the EDPB to provide the necessary legal certainty to permit the development of insurance solutions based on new technologies. Furthermore, it would like to see the legal basis for processing data in the GDPR and the Commission's proposal for an ePrivacy Regulation aligned. In particular, the latter does not currently provide an adequate legal basis for insurers to offer telematics products.

"Certain GDPR rules seem at odds with fast-evolving technology and may slow the pace of insurers' digital innovation."

EDPB needs oversight

The role of the EDPB and the impact of its GDPR guidelines on industries also needs to be reviewed. Guidelines can be useful implementation and compliance tools, which can help to clarify GDPR requirements while promoting consistent interpretations across the EU. However, areas exist in which the interpretation of the EDPB has gone beyond the text of the Regulation by, for instance, creating additional requirements or narrowing the interpretation of a GDPR provision. It must be remembered that it is the EC that is the guardian of the Regulation and that the EDPB's mandate is governed by the text of the GDPR, which was the result of a political agreement between EU policymakers.

Destroy discrepancies

In the interests of consistent, Europe-wide application of the GDPR, there needs to be an examination of the fragmentation in the Regulation's application that has been created by certain national GDPR guidelines.

Discrepancies have clearly arisen between national guidelines in areas such as the consent to use cookies and tracers, data protection impact assessments and legitimate interest. These create legal uncertainty and make it harder for insurers to conduct their business in multiple member states while remaining in compliance with data protection rules. The EC must pursue a unified approach to the interpretation and application of the GDPR across Europe.

Inadequate adequacy decisions

Finally, Insurance Europe would like to see action on the international transfer of personal data to non-EU countries. The GDPR currently provides different tools and solutions for international transfers. Of those, EC adequacy decisions are the most suitable for insurers, as they provide the most appropriate safeguards for both data controllers and data subjects. However, only a very small number of countries are currently covered by such decisions and this is insufficient for a sector as global as insurance. Prompt action is required to address this and make the GDPR fit for the insurance industry.

Don't touch the text

While the Regulation certainly contains challenges for businesses that need to be addressed, it would nevertheless be premature and counterproductive to amend the GDPR text itself just yet.

Like many other sectors, the insurance industry has invested significant resources in understanding the Regulation and its implications, and in implementing the new regime. Such a substantial investment of time and money could be wasted — and new costs would be incurred — if the text were changed after just a few years.

Instead, in areas in which the GDPR is found not to have achieved its objectives, the Commission should consider developing further or different guidance, together with the EDPB where relevant.

The Commission's first evaluation and review report of the GDPR, which was released in June 2020, likewise concluded that a revision of the GDPR text would currently be premature. The EC report touched upon many of the areas raised by Insurance Europe in its contributions to the review, taking stock of the strengths and weaknesses of the legislation as it reaches its second birthday and paving the way for the next evaluation of the text in 2024.

Daniel John
Chair, motor working group, Insurance Europe
Head of non-life actuarial department, HUK Coburg, Germany

MOTOR

Delays possible

This year has seen progress on access to vehicle data and the review of the EU Motor Insurance Directive, but neither is yet complete

For a number of years, the bulk of Insurance Europe's activities in relation to motor insurance have been centred on two major workstreams: the revision of the EU Motor Insurance Directive (MID) and — increasingly importantly — insurance issues related to connected and automated vehicles. On both topics, significant progress was made in the last year but, as the end goals inch closer, real obstacles still remain.

Designing the future of motor insurance

Motor insurance will change significantly in the coming decades. There are two reasons for this. Firstly, today's state-of-the-art car is connected; the car and the driver produce a lot of data. This allows for completely new concepts in insurance, such as products tailored to driving style or frequency and speedier claims-handling and claims-related services. And if the insurance industry does not use this data, others — such as the manufacturers — surely will, presenting a clear danger to traditional insurance business.

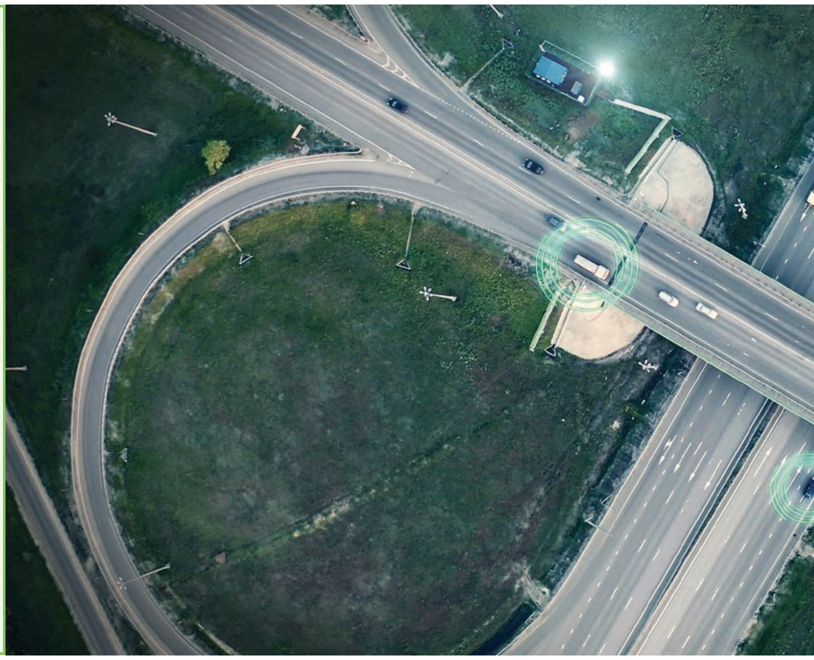
At the same time, these connected vehicles present real opportunities. Some existing telematics tariffs show that those using them become better drivers, thus contributing to the European Commission's vision of zero road accidents. Furthermore, drivers with good telematics scores have lower fuel consumption, which also supports the EC's sustainability goals.

Secondly, autonomous cars are slowly appearing on the horizon.

Communication lines open with carmakers

Vehicle manufacturers have developed their own solutions involving remote servers from which service providers can access the data generated by vehicles. Given the importance for insurers of accessing this data, insurers have been keen to comprehensively evaluate the technological solutions proposed.

This is why Insurance Europe worked together with the vehicle manufacturers for most of 2019 on a project to test the solutions they have proposed. This has been a valuable experience as it has fostered a constructive dialogue on the issues involved.



Here it is no longer the human driver who produces the risk but a system consisting of many hardware and software components. These components use artificial intelligence, require extensive testing before approval, change frequently and generate a massive amount of data while in operation. From a legal point of view, insuring an autonomous car is not very different from insuring a traditional car, but from a pricing and risk assessment perspective, it is a completely new world that requires completely new concepts.

Therefore, the two main questions are:

- How to calculate insurance premiums based on driving/sensor data?
- How to estimate and price the risk of an autonomous car?

And the basis for all of this is: data.

First moves on access to data

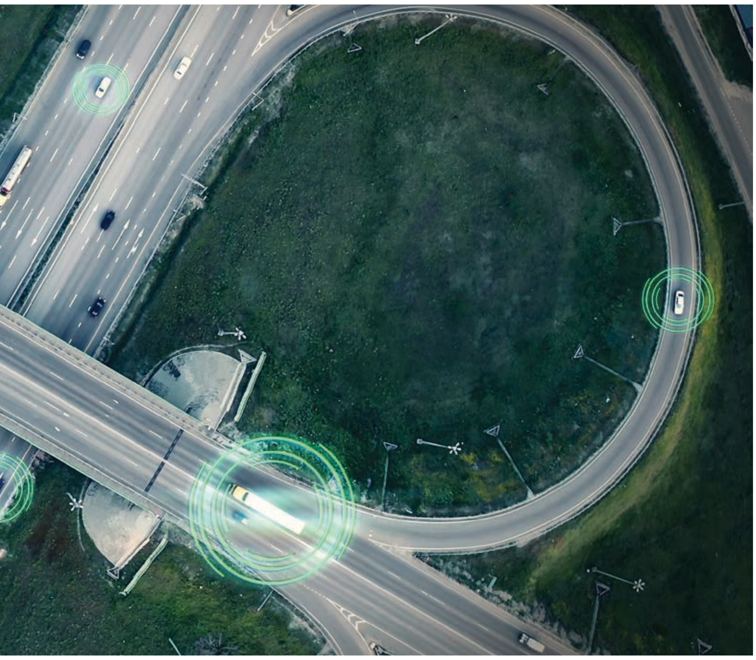
In mid-2019 the Commission's DG GROW (Directorate-General for Internal Market, Industry, Entrepreneurship and SMEs) gathered all key stakeholders in the automotive value chain — insurers included — to lay the ground for a legislative proposal on access to the data generated by automated and connected vehicles.

This, in itself, was a huge step forward and was welcomed by Insurance Europe, confirming that the idea that legislative action is necessary on access to vehicle data has gained considerable ground.

For insurers to carry out their core function of providing compensation, they need to have access to any relevant data generated by the vehicles involved. Not only does this enable insurers to apportion liability correctly, but access to the data from automated and connected vehicles also helps insurers to better understand the risks those vehicles present, to improve claims-handling and to develop innovative, tailored products and services for consumers. Vehicle manufacturers, however, have long opposed the idea of any legislative intervention in this area.

The discussions led by DG GROW were a way for the Commission to gauge stakeholders' views and, in particular, the data needs of the different parties. Insurance Europe agreed to collaborate in this exercise and provided an extensive but

"For insurers to carry out their core function of providing compensation, they need to have access to any relevant data generated by the vehicles involved."



not exhaustive list of datapoints to which insurers need access in order to offer their services in and around connected and automated vehicles.

One point Insurance Europe highlighted was that any proposal would need to be future-proof, meaning that any list of datapoints could only be used as an example, rather than an exhaustive and binding list. As vehicles evolve, so will the datapoints, and insurers will want to be able to adapt their services to this ever-evolving ecosystem. Any action by the EU must enable this.

Progress has slowed since this initial push from the Commission, and the start of the study that will form the basis for the legislative proposal from the Commission, which was originally scheduled for the end of 2020, will now more realistically be for 2021.

Insurance Europe will continue pushing for any proposal to include the necessary safeguards to ensure consumers — and society in general — make the most of the opportunities arising from connected and automated driving. Drivers must remain in control of their vehicle data and be free to share it with the service providers of their choice, without having to go through the vehicle manufacturer. To foster consumer choice and fair competition, it is essential to ensure all service providers in the automotive value-chain can access the wealth of data generated by new technologies.

Differences over the MID

The MID is a longstanding piece of EU legislation that has ensured the protection of victims of road traffic accidents and facilitated the free movement of motor vehicles throughout Europe since the 1970s. Talks of a revision started back in 2015 and the EC published its proposals in 2018. Insurance Europe strongly supports the review's objectives of increasing the protection for victims of accidents and ensuring policyholders are all treated fairly and without discrimination. It is particularly supportive of the Commission's view that autonomous vehicles fall within the scope of the Directive and of its proposal to allow new technology — such as number-plate recognition — to be used in the fight against uninsured driving.

While the European Parliament was quick to adopt its position on the EC proposals, the Council of the EU was much slower to start work. Nevertheless, the last quarter of 2019 saw an acceleration, paving the way for negotiations to begin in 2020 between all three institutions. However, progress has since slowed down, and only partly because of the COVID-19 pandemic.

The reality is that there are widely differing views between EU member states and between MEPs (sometimes within the same group) on many key aspects of the proposals. Some of the contentious issues have been known for a long time, such as the definition of the use of a vehicle, which Insurance Europe believes should be limited to vehicles used in traffic, or the standardisation of claims history statements, which Insurance Europe considers impractical and without clear benefits for consumers.

The co-legislators' discussions on other issues, however, only really began in 2020. These include, most topically, liability issues relating to light electric vehicles, such as bicycles and scooters.

It is not surprising the topic of light electric vehicles was introduced into the debate, since they seem to have taken over some European cities in the last year or two. While they are seen to bring many benefits in terms of sustainable transport, they also raise some serious questions and have turned into quite the "hot topic" that policymakers all want to discuss.

One issue in particular relates to liability for accidents and whether the MID's protection should be extended to electric vehicles. Insurance Europe has been arguing that extending the compulsory motor third-party liability (MTPL) insurance system found in the MID to them would be a disproportionate move, since they are usually more akin to bicycles and few would argue that cyclists should be required to have MTPL insurance.

Insurance Europe has therefore suggested basing the decision on whether to apply compulsory MTPL insurance at EU level to such vehicles on existing type approval rules, meaning compulsory insurance should only apply to those vehicles that can reach a speed of over 25 km/h. It is important to note here that the MID is a "minimum harmonisation" instrument, meaning member states remain free to go further and require insurance for these vehicles.

While the co-legislators' views on electric vehicles seem to generally match those of Insurance Europe, there are many other issues where no clear consensus has yet emerged, including on the wider issue of the scope of the Directive (ie, the definition of the use of a vehicle). The adoption of a revised MID by the end of 2020 as currently planned is thus anything but guaranteed.

"Compulsory insurance should only apply to those vehicles that can reach a speed of over 25 km/h."

Nicolas Jeanmart
Head of personal & general insurance, Insurance Europe

TAXATION

Big on BEPS

Welcome work by the OECD on taxing the digital economy still needs further thought

Insurance Europe is supportive of the OECD's efforts to address the challenges that digitalisation brings to the international tax system. The OECD's long-standing base erosion and profit shifting (BEPS) project, which seeks to ensure that profits are taxed where economic activity and value creation occur, has remained a key item on the G20 agenda even in these difficult times. Indeed, it could help contribute to recovery from the economic effects of the COVID-19 pandemic.

In a nutshell, the proposed global tax would have two pillars:

- Pillar 1 is new profit allocation and nexus rules to allocate taxation rights based on "significant economic presence". Automated service providers and consumer-facing businesses would be within the scope of the rules, with possible exclusions granted to financial services, including insurance.
- Pillar 2 is a set of rules (including a minimum tax rate) to prevent multinational companies from shifting profits to jurisdictions where they are subject to no or very low taxation. This is also known as the "Global Anti-Base Erosion" (GloBE) proposal.

It is generally accepted that insurers are not, and should not be, the target of this project. This is because insurers do not have profits arising from intangibles and should therefore not be impacted by a tax on digital services. In addition, they are subject to extensive prudential regulations that require them to hold capital and to do so locally, to match local risks. And, in general, taxes on insurance products, both indirect or on premiums, are levied in the country in which the risk is situated, which largely coincides with the location of the customers. Insurance Europe supports the tentatively agreed exclusion of the financial sector from Pillar 1, but still has concerns over the possible effects of Pillar 2.

Second pillar questions

First, the main goal of Pillar 2 is to impose a minimum level of taxation on profits while avoiding double taxation. The insurance industry is already subject to several tax principles that are fine-tuned with the jurisdiction of the consumer. If the proposed additional taxation rules (eg the "income inclusion" rule, the "under-taxed payments" rule and the "subject to tax" rule) are not effectively coordinated, the cross-border arrangements common in insurance to provide efficient coverage may end up subject to double taxation.

It is also important that Pillar 2 tax rules are implemented clearly and efficiently, and that their interaction (both internally and with existing local tax rules) does not require companies to assess on a case-by-case basis the effective tax rate they must pay. Tax uncertainty would lead to inefficient commercial transactions and add unnecessary compliance complexity and administration burdens to insurers.

Finally, it is crucial to give sufficient consideration to the specifics of particular sectors, such as insurance. While the principles of the new taxing mechanism are public, the details have not yet been shared. Insurance Europe urges the OECD to consult widely with interested parties on the envisaged rules.

Discussions continue in parallel at political and technical level, and important central issues, such as the minimum rate of taxation, remain open. The "blueprints" of the project are expected to be ready in late 2020, but the decisions on their adoption and whether the project should be extended beyond digital companies remain a political matter, so the meeting of G20 finance ministers in October 2020 and the G20 summit in November will be decisive if the aim of agreement by year-end is to be achieved.

National options

Though the preference continues to be for a global approach, many countries are willing to introduce their own national digital services tax if the OECD fails to reach agreement. France has temporarily postponed the levying of a tax that was introduced at the beginning of 2020. Other countries, such as Italy, have included clauses to repeal their national taxes once international taxation comes into force, while others still, such as Spain, are proposing or finalising bills to introduce digital services tax laws.

The EU has likewise been working on a proposal for a digital services tax that would focus on revenues only from the provision of targeted digital advertising services. Discussions were halted in 2019 without agreement and member states are looking with interest at the OECD's proposed global solution and continue to work towards it. Germany has said it is willing to intensify talks on a European proposal for a digital tax during its EU presidency in the second half of 2020 if there is no solid progress on a global agreement.

Insurance Europe will continue to monitor developments to ensure that approaches to a digital tax at global, EU or national level do not have unintended consequences for insurers.

Inconsistent implementation of DAC6

The implementation of the 2018 EU Directive on Administrative Cooperation (DAC6), which requires companies, intermediaries and taxpayers to report on cross-border arrangements in order to increase tax transparency, proved challenging for EU member states, especially once the COVID-19 crisis started. Some have not yet enacted domestic legislation and there has been a lack of guidance and reporting schema details.

For insurers and other financial services entities, the delays in enacting national legislation and the lack of guidance have meant that complying with the new rules has been challenging, particularly with the impact of COVID-19 on operations. For these reasons, Insurance Europe, in cooperation with other European financial services federations, wrote to the European Commission and EU finance ministers requesting a delay in implementation of the rules. While an amendment to the Directive has been proposed, it unfortunately gives member states the option not to delay. A consistent approach throughout the EU would be preferable, to bring significant relief to the financial sector.

Nicolas Jeanmart
Head of personal & general insurance, Insurance Europe

ANTI-MONEY LAUNDERING

Pick your fights

The EU's anti-money laundering efforts will be most effective if they focus on areas of real risk

Recent years have seen a steady stream of money laundering and terrorism financing scandals involving banking institutions and related failures by national supervisors. This has ensured that the topic of anti-money laundering (AML) and countering the financing of terrorism (CFT) — and particularly their supervision — have become a priority for the European institutions.

A banking authority supervising insurers?

The first major change adopted recently involved giving the European Banking Authority (EBA) a centralised role in the supervision of AML and CFT at European level for all "obliged entities", which means financial insitutions and designated non-financial businesses and professions, and therefore includes insurers.

This new responsibility for the EBA was introduced in the late stages of the review that was finalised in April 2019 of the Regulations establishing the European financial supervisory authorities. While a role was given to insurance supervisor EIOPA in assisting the EBA, this was not sufficient to alleviate insurers' concerns about bringing them under the jurisdiction of a banking authority.

Insurance = low risk

The EBA's first action as AML/CFT supervisor was to start updating the existing Risk Factors Guidelines, which are aimed at all obliged entities. This update was an opportunity for Insurance Europe to reiterate some of the key tenets of its position to the EBA. Insurance Europe particularly stressed one fact acknowledged by most institutions involved in AML/CFT, be it the European Commission at European level or the Financial Action Task Force (FATF) at international level: the insurance sector presents a very low money-laundering/terrorism-financing risk.

Indeed, the industry's only exposure to risk is in life insurance, and then only life insurance products with an investment element. In non-life insurance, the risk is nil, unless fraud is taken into account, yet fraud should be and is addressed in its own right by insurers.

The European institutions confirmed this by focusing on life insurance in the European framework and, in doing so, they followed the FATF, which clearly excludes non-life insurance from the scope of its work. Unfortunately, this approach is not followed consistently throughout Europe, with some member states choosing to leave non-life insurance within the scope of their national frameworks.

Be guided by risk

Another key principle that Insurance Europe defends is the need to take a risk-based approach to countering money laundering and terrorism financing; resources should be focused on the sectors, products, transactions and people that represent a real risk. Applying a risk-based approach means that — in most cases — life insurance transactions only require a simplified due diligence process.

A risk-based approach should be the guiding principle when considering the Commission's recent suggestion of a new EU AML/CFT supervisor. The EBA had barely started its mandate when new AML scandals in the banking sector prompted the EC to propose further and stronger reform of AML/CFT supervision in the EU. This was confirmed in 2020 when, in its Action Plan for a comprehensive EU policy, the Commission suggested a new supervisor for the cross-border activities of all obliged entities.

Since the problems that prompted this Action Plan were virtually all related to the banking sector, it would make sense for any new authority to be focused on banking. This would be consistent with the risk-based approach: focus the supervisory resources on the sector in which the risk resides.

> **"Resources should be focused on the sectors, products, transactions and people that represent a real risk."**

In any event, any such supervisor must have the skills and expertise to supervise all entities under its jurisdiction. The business models of different entities and their exposure to AML risks are very diverse and, as explained earlier, Insurance Europe is still wary of an institution with expertise in banking supervising the insurance sector.

Local knowledge is best

The allocation of supervisory powers to a new EU body must also be measured against the subsidiarity principle, meaning that powers should be transferred to EU level only if the objectives of AML/CFT supervision cannot be sufficiently achieved by national supervisors.

This important role played by national supervisors should be highlighted, as they are generally better placed to know and understand their home markets. In addition to having local expertise, they are also in direct contact with the entities under their jurisdiction. Where a supervisor fails on cases in a specific sector, this should be taken up with the supervisor concerned and within that sector, rather than leading to the creation of a new authority with EU-wide jurisdiction over all financial sectors.

The legal basis for including all obliged entities under the scope of an EU-level supervisor, irrespective of their exposure to AML risks, is therefore questionable. The time and effort required to set up such a structure can also seem disproportionate when compared to the exposure to money-laundering/terrorism-financing risks of sectors such as insurance.

European insurers remain as committed as ever to the fight against money laundering. For this fight to be successful, the risk-based approach must remain the cardinal rule on which any legislative framework is based.

A single EU-level AML/CFT supervisor with jurisdiction over a low-risk sector such as insurance does not seem consistent with that approach and should therefore be avoided.

RAB OPINION

Christian Mumenthaler
Chair, Insurance Europe Reinsurance Advisory Board (RAB)
Group CEO, Swiss Re, Switzerland

SUSTAINABILITY

Green lights

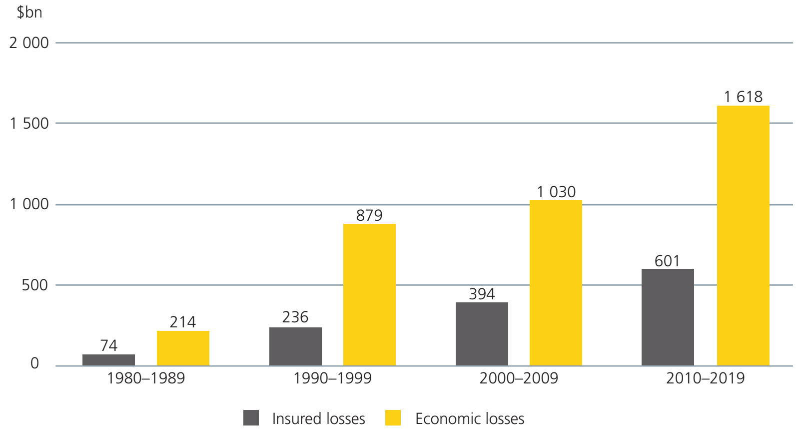
Reinsurers are natural partners in the European Green Deal

Sustainability is at the front and centre of everyone's agendas, permeating discussions with clients, investors, regulators and employees. Within the reinsurance sector, sustainability is becoming an integral part of the core business on both the liability and investment side, and companies increasingly see it from a risk perspective but also as a business opportunity.

The EU is leading the global response to climate change, setting out its ambition to be the first climate-neutral continent by 2050 in European Commission President von der Leyen's landmark European Green Deal. That Green Deal is welcome news for European reinsurers as it marks a major step in society's response to the most significant socio-economic challenge of our time. The members of Insurance Europe's Reinsurance Advisory Board (see box on p71) have been modelling the impacts of climate change on natural catastrophes since the mid-1990s. Our analysis shows that secondary peril events (such as drought, wildfire and flood) will become more extreme as a consequence of an ever-warming world.

Reinsurance acts as an enabling and protective financial mechanism that strengthens society's resilience to the effects of climate change. The insights yielded from our expertise in natural catastrophe modelling can be used to assist policymakers in identifying the most appropriate adaptation measures, which could be, for example, strengthening flood defences or improving

Global economic versus insured losses from weather-related catastrophes — 1980–2019 ($bn, 2019 prices)



Source: Sigma 2/20, "Natural catastrophes in times of economic accumulation & climate change", Swiss Re Institute

building codes, as Insurance Europe outlines in its article on climate adaptation on p13.

However, underinsurance remains a significant issue. The Commission's work on adaptation to climate change is welcome, but more action is needed to address the significant imbalances in protection levels that exist between EU member states.

Mitigation as well as adaptation

RAB companies are also strong supporters of mitigating the impacts of climate change and supporting the transition to a low carbon economy through our underwriting and investment practices.

Our companies believe that sustainable business is good business. With that in mind, some European reinsurers have already committed to stop providing reinsurance that supports the operation of new thermal coal mines or the construction of new coal-fired power plants. At the same time, reinsurers are facilitating the development of new technologies that will reduce emissions by increasing the insurance coverage of renewable energy technologies. These include risk solutions for electricity grid infrastructure, battery storage and offshore wind turbines.

"More action is needed to address the significant imbalances in protection levels that exist between EU member states."

As a natural consequence of their long-term business model, reinsurers' investment activities contribute to climate-change mitigation, predominantly by funding a more sustainable economy. Like our commitments on underwriting, the reinsurance industry as a whole has expanded commitments to responsible investing both by increasing exposures to issuers carrying out sustainable activities and by reducing exposures to carbon-intensive investments. In addition, reinsurers use different techniques to explicitly embed sustainability into their investment practices. RAB companies have provided transparency through ESG (environmental, social and governance) reporting and disclosures and some, for example, have been early adopters of the recommendations of the Financial Stability Board's Task Force on Climate-Related Financial Disclosures.

Stimulating sustainable assets

We support action that promotes and stimulates the supply of suitable sustainable assets for investment, such as the

Commission's work to develop a green bond standard. We are also supportive of an enhanced EU strategy to accelerate the energy transition by fostering the creation of viable green infrastructure projects and deepening the market of green assets. While the focus is still frequently on the environmental component of ESG, social — including human and labour rights — and governance issues must not be neglected. RAB companies have always been committed to fostering diverse, inclusive environments and societies in which individuals can meet their full potential.

Although reinsurers are not themselves major greenhouse-gas emitters, many have set ambitious targets to reduce their own carbon emissions, engaging with their employees and supply chains to increase their sustainability. As more governments pledge to become net-zero carbon emission economies by 2050, some reinsurers have also taken first steps to commit to net-zero by 2050 or sooner in their core business and investment. They are also committed to sustainable business models as employers. If anything positive is to come out of the COVID-19 crisis, maybe it is that it has reinforced that it is possible to make our operations more sustainable through, for example, more virtual meetings reducing air travel.

The EU's ambition for carbon neutrality is the right one. Concerted and globally coordinated action will be needed to reach net-zero CO_2 targets to reduce the effects of climate change and ensure that the risks associated with it remain insurable so that together we can close the natural catastrophe protection gap.

reinsurance advisory board

RAB: representing Europe's reinsurers

The Insurance Europe Reinsurance Advisory Board (RAB) is a specialist representative body for the European reinsurance industry. It is represented at CEO level by seven major reinsurers: Gen Re, Hannover Re, Lloyd's of London, Munich Re, PartnerRe, Scor and Swiss Re, with Insurance Europe providing the secretariat.

GFIA OPINION

Recaredo Arias
President, Global Federation of Insurance Associations (GFIA)
Director general, Mexican Association of Insurance Companies (AMIS)

COVID-19 PANDEMIC

Better together

A truly global challenge brings the value of a global federation to the fore

The global insurance industry is an essential stabilising force throughout the world. Insurers provide protection for the most challenging catastrophes and societal upheavals faced by individuals, businesses and governments, as well as working to develop solutions for new and emerging risks.

The member associations of the Global Federation of Insurance Associations are present in 64 countries, all of which have been touched by the COVID-19 pandemic, and they have risen to meet the challenges it has created, both individually and collectively.

Business almost as usual

As the world grappled with the public health and economic effects of the virus, insurers remained focused on honouring their promises to their customers and implementing contingency plans to protect their employees but minimise disruptions to services, often by focusing on the digital delivery of services, which required regulatory adjustments in some jurisdictions.

Some insurers implemented new, flexible solutions for premium payments and other requirements in order to respond to the changing situations faced by their customers or to transformations in behaviour (such as working from home). Many have also provided voluntary financial and material support in their communities, such as to medical personnel, either individually or collectively through their national associations.

"The rapid reaction of the IAIS was extremely helpful in supporting the industry in the face of significant challenges."

GFIA was active from the very start of the crisis: gathering and sharing experiences and best practices among its members. Throughout the pandemic, it has also been liaising closely with international bodies such as the IAIS, the Financial Stability Board and the OECD, presenting the global industry's views and positions and participating in stakeholder dialogue events. GFIA issued a public statement on COVID-19 early in the pandemic. This was welcomed by the IAIS, and the points it raised in relation to supervisory flexibility and not imposing retroactive cover for unpriced risks was reflected in the IAIS's own subsequent statements.

Liaison with the IAIS

GFIA welcomed the IAIS's own statements on insurance and COVID-19. In particular, it welcomed the IAIS's recognition of the severe negative effects that would ensue for the industry and its customers if retroactive coverage was sought for losses outside the scope of existing contracts for which premiums have not been collected. The continued financial stability of the insurance industry is vital. Without it, insurers would not be able to continue to respond to the crisis or to honour their obligations to customers under existing policies.

GFIA likewise welcomed the IAIS's call to local and regional supervisors to show flexibility to insurers over calls for data and in their supervisory measures, particularly in the early days of the pandemic. The rapid reaction of the IAIS to those concerns and others facing the industry was extremely helpful in supporting the industry in the face of significant challenges.

GFIA also applauded the many supervisors who developed innovative solutions to enable critical business functions to continue and it hopes to work with them to carry forward innovations that benefit customers and the industry.

As well as speaking at a June 2020 dialogue set up by the IAIS Executive Committee, GFIA is following up with written feedback on the short-, medium- and long-term impact of COVID-19 on the financial system and on the insurance sector in particular, as well as on the first key trends, risks and opportunities emerging from COVID-19, which the IAIS had requested ahead of finalising its work plan for 2021–22.

GFIA members also provided input to an OECD report[1]. This gives an overview of the measures taken by insurance associations and companies, governments, regulators and supervisors around the world in three main areas:

- Ensuring continuity of operations
- Managing solvency and liquidity risks
- Providing support to policyholders

For the future

Looking ahead, as set out in Insurance Europe's article on p10, insurers are already working with legislators and supervisors on future approaches to dealing with pandemic risks. GFIA's extreme events working group has been coordinating the federation's work in this area, gathering information on the various initiatives now under way worldwide.

As governments, businesses and individuals begin to emerge from the measures taken to combat the spread of COVID-19, GFIA members remain committed to working with all stakeholders to advance and develop ideas for forward-looking, long-term, government-supported solutions for future pandemic risks. Such solutions must, however, recognise the limits to the capacity of the insurance sector to assume pandemic risks and must be adjustable as data from the current pandemic becomes available.

GFIA

GLOBAL FEDERATION OF INSURANCE ASSOCIATIONS

GFIA: a global federation

Established in October 2012, GFIA now comprises 41 member associations and one observer association. It represents the interests of insurers and reinsurers in 64 countries that account for more than $4trn (€3.4trn) of insurance premiums, or 89% of the global total. GFIA's secretariat is headquartered at Insurance Europe.

1 "Insurance sector responses to COVID-19 by governments, supervisors and industry," OECD, July 2020

Insurance Europe

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Member associations

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Bulgaria		Association of Bulgarian Insurers (ABZ) Chairman: Konstantin Velev www.abz.bg tel: +359 29 80 51 24
Croatia		Hrvatski ured za osiguranje (HUO) President: Slaven Dobrić www.huo.hr tel: +385 14 69 66 00
Cyprus		Insurance Association of Cyprus Chairman: Andreas Stylianou www.iac.org.cy tel: +357 22 45 29 90
Czech Republic		Česká asociace pojišťoven (ČAP) President: Martin Diviš www.cap.cz tel: +420 222 35 01 50
Denmark		Forsikring & Pension (F&P) President: Laila Mortensen www.forsikringogpension.dk tel: +45 41 91 91 91
Estonia		Eesti Kindlustusseltside Liit President: Marek Ratnik www.eksl.ee tel: +372 667 18 00
Finland		Finanssiala ry Chairman: Timo Ritakallio www.finanssiala.fi tel: +358 207 93 42 00
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Greece	Hellenic Association of Insurance Companies President: Alexandros Sarrigeorgiou www.eaee.gr tel: +30 2103 33 41 00
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Liechtenstein	Liechtensteinischer Versicherungsverband President & director: Caroline Voigt www.lvv.li tel: +423 237 47 77
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United Kingdom	The British Insurers' European Committee (BIEC), comprising:	
	ABI	Association of British Insurers (ABI) Chairman: Jon Dye www.abi.org.uk tel: +44 20 7600 3333
	IUA of London International Underwriting Association	International Underwriting Association of London (IUA) Chairman: Malcolm Newman www.iua.co.uk tel: +44 20 7617 4444
	LLOYD'S	Lloyd's Chairman: Bruce Carnegie-Brown www.lloyds.com tel: +44 20 7327 1000

Associate members

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Serbia	УОС	Udruženje Osiguravača Srbije Secretary general: Duško Jovanović uos.rs tel: +381 112 92 79 00

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Russia	ВСС	All Russian Insurance Association (ARIA) President: Igor Yurgens www.ins-union.ru tel: +7 495 232 12 24

Events

11th International Conference "Fast forward: the future of insurance" Bucharest, May 2019

Nearly 400 delegates listened to Insurance Europe President Andreas Brandstetter open the Conference, held under the patronage of Romania's 2019 EU presidency. He focused on insurers' role in tackling three major societal challenges: natural catastrophes, cyber attacks and the lack of retirement saving.

(L to R) Elisabeth Stadler, VIG; Susan Neely, ACLI; Sue Lewis, The People's Pension; and Victoria Saporta, IAIS, were asked by director general Michaela Koller (far right) how to reduce protection gaps and boost pension saving.

Leonardo Badea, President of Romania's Financial Supervisory Authority (ASF), gave a keynote speech.

In a wide-ranging interview, Allianz chairman Oliver Bäte (right) drew on his long industry experience to give fascinating insights into the insurance world of the future: technology-driven change, business model adaptations and shifting consumer demands.

(L to R above) Paweł Surówka, PZU; Minoru Aosaki, Japan FSA; Lard Friese, NN Group; and Gabriel Bernardino, EIOPA, were quizzed by moderator Frédéric de Courtois of Generali (far right) on how to make regulation fit for the future.

Greenpeace climate and energy campaigner Adam Pawloff (right) gave an impassioned speech calling for consistency from the insurance industry in its commitments to tackle climate change.

“Cybersecurity and the role of insurance”
Brussels, October 2019

To coincide with the publication of its “Insurers’ role in EU cyber resilience” booklet (see p84), Insurance Europe hosted a breakfast debate between representatives of the EC, EIOPA and the insurance industry. Panellists discussed: how to increase awareness of cyber risks; the difficulties created by their potential scale and possible solutions for covering them; questions of contract certainty; and the problems of silent risks.

“Insuring mobility, today and tomorrow”
Brussels, October 2019

Focusing particularly on the liability questions raised by light electric vehicles — such as electric scooters — and on the issue of insurers’ access to the data of connected and automated vehicles, Insurance Europe’s half-day conference attracted around 100 delegates.

They heard speeches by Ismail Ertug MEP (right) and EIOPA chairman Gabriel Bernardino (below), as well as from panellists representing the EC, road users and the insurance industry. At the event, Insurance Europe launched an Insight Briefing setting out European insurers’ views on the two topics (see p84).

"Tackling the pension challenge"
Brussels, February 2020

To launch the results of its pan-European survey on pensions (see p40), Insurance Europe held a conference attended by over 100 delegates.

After a keynote speech by Ruth Paserman (right) of the Cabinet of EC Executive Vice-President Valdis Dombrovskis and a presentation of the survey, two panel debates featured speakers representing the OECD, the EC, insurance supervisors, consumers and the insurance industry.

The panellists responded to the survey findings and discussed the roles of the EU and its insurers in stimulating retirement saving and boosting financial literacy. They also investigated what still needs to be achieved to make the EU's pan-European personal pension product (PEPP) a success.

Publications

These Insurance Europe publications, and more, are available at www.insuranceeurope.eu

Annual Report 2018–2019
(May 2019)

Articles on the federation's workstreams and details of its structure and organisation.

Guest contributors include: Denis Kessler, chairman & CEO, SCOR; Alison Martin, group CRO, Zurich Insurance Group; and Christian Mumenthaler, CEO, Swiss Re.

Insight Briefing: EU General Data Protection Regulation: one year on
(June 2019)

A look at whether the GDPR has delivered on its aims of enhanced data protection and greater harmonisation of EU protection rules, and whether the Regulation is compatible with innovation in insurance.

European Insurance — Key Facts
(October 2019)

European Insurance in Figures
(January 2020)

2018 statistics, including information on European insurers' premiums, claims and investments.

Insurers' role in EU cyber resilience
(October 2019)

A summary of the ways insurers assist in efforts to increase cyber resilience, including examples of initiatives by national associations.

Insuring mobility — today and tomorrow
(October 2019)

A look at the liability questions raised by light electric vehicles and automated vehicles, as well as the issue of insurers' access to the data of connected and automated vehicles.

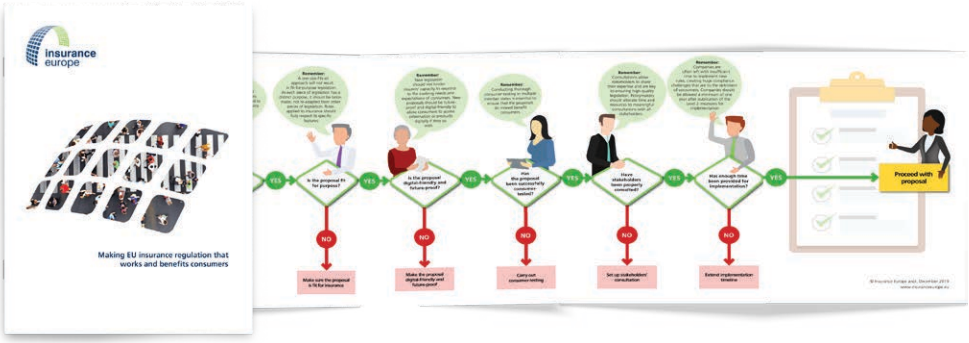
Insurance fraud: not a victimless crime
(November 2019)

Second only to tax fraud as the most common form of fraud globally, insurance fraud is constantly evolving and has many negative consequences.

Making EU regulation that works and benefits consumers

European regulation: how to achieve better quality
(December 2019)

How EU policymakers can ensure rules work for insurers and benefit consumers, plus a decision tree for designing and reviewing insurance rules.



Why insurance is unique
(December 2019)

A booklet explaining the special features that make insurance such a unique financial service requiring tailored regulation.

Insure yourself wisely: natural catastrophes
(December 2019)

The latest infographic in the InsureWisely series, providing tips on limiting the consequences of nat cat events.

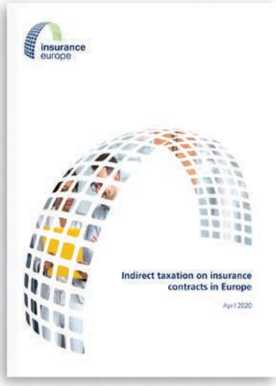
Ambitions for Europe
(January 2020)

The role of Europe's insurers in achieving four objectives:

- Create a greener, more sustainable Europe
- Respond to the challenges of an ageing society
- Finance sustainable EU economic growth
- Maintain a competitive EU (re)insurance industry

Pension Survey: What do Europeans want from their pension savings?
(February 2020)

The results of a pan-European survey to find out how citizens are preparing financially for retirement and what they expect from their pension savings.



Indirect taxation on insurance contracts in Europe 2020
(April 2020)

A full survey of tax rules, tariffs and regulations, giving an overview of taxes applicable to insurance premiums, as well as declaration and payment procedures

Insight Briefing: Two years of the GDPR — what next? (May 2020)

Insurers' views on the areas of the EU's General Data Protection Regulation that need attention.

Insure yourself wisely
(June 2020)

A booklet of useful tips on how best to insure for key life events such as buying a house or car, going on holiday or retiring.

Insight Briefing: Managing the EU's flood risks
(June 2020)

Insurance Europe believes the EU Floods Directive has had a positive impact on Europe's preparedness for increased flooding, but sees areas in which it could still be improved.

Insight Briefing: Intelligent moves
(August 2020)

A two-page summary of the European insurance industry's views on artificial intelligence and what an EU regulatory framework for AI should look like.

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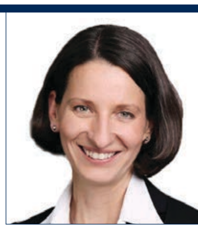

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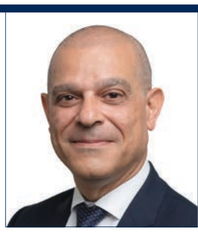

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