

FEEDBACK STATEMENT

Consultation Paper on the Supervisory
Statement on exclusions in insurance products
related to risks arising from systemic events

EIOPA-22/421
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1. INTRODUCTION

EIOPA would like to thank all the participants in the public consultation for their comments on the draft Supervisory Statement on exclusions in insurance products related to risks arising from systemic events.

The input received provided important guidance for EIOPA to finalise the Supervisory Statement. All of the comments submitted were given careful consideration by EIOPA. The individual comments received and EIOPA's response to them are published as a separate document (see Resolution of Comments).

2. DETAILED OVERVIEW OF THE RESPONSES

2.1. SCOPE AND AIM OF THE SUPERVISORY STATEMENT

- ▶ **Stakeholder's comments welcomed the overall message conveyed through the Supervisory Statement. Nevertheless, some stakeholders argued that it would be desirable to substitute systemic term with catastrophic or market-wide as the former could be overly broad and overused in the insurance sector.**

EIOPA carefully assessed the Supervisory Statement and the clarity of events in scope. Systemic as opposed to stakeholder-proposed alternatives (i.e. catastrophic, system-wide, etc.) has been deemed as the most suitable term to cover supervisory expectations while keeping consistency with recent work carried out in light of the Covid-19 situation (i.e. EIOPA staff paper on measures to improve the insurability of business interruption in light of pandemics¹, and EIOPA issues paper on shared resilience solutions for pandemic risks)². EIOPA considers that whilst capturing the severity of events at stake, the term catastrophic does not cover their wide dimension (i.e. pandemics) as well as the systemic concept. In addition, the use of catastrophic adjective might lead to a restrictive understanding of the events in scope due to its customary usage in the context of natural

¹ EIOPA staff paper on measures to improve the insurability of business interruption in light of pandemics, 12 February 2021. Available at: [EIOPA publications](#).

² Issues paper on shared resilience solutions for pandemic risks, 27 July 2020. Available at: [EIOPA publications](#).

catastrophe. As for system-wide, the term notably shares commonalities with the adjective systemic and the benefits argued (i.e. overuse of systemic term in the context of financial services) are not material enough to allow for divergence of this Supervisory Statement from the wording used over the past years by the Authority.

For further clarification, the Supervisory Statement contains a definition of systemic events prepared in the context of the aforementioned and cited EIOPA papers by an exploratory group involving European Commission and industry representatives. To illustrate this definition, the Supervisory Statement also includes some examples of systemic events that would be in scope of the Supervisory Statement.

Acknowledging the limits to capture systemic events not yet emerged, EIOPA is of the opinion that the current definition, supporting examples and context section will serve as an appropriate basis to identify and determine systemic events and risk arising from them for the purpose of the Supervisory Statement. Despite this and for the sake of clarity, the definition included in the Supervisory Statement has been complemented with a clarification footnote providing further examples.

- ▶ **Some stakeholders questioned the scope of the Supervisory Statement and whether this applies to Small and Medium Enterprises (SMEs). In this regard, respondents' feedback was varied: on one hand, some stakeholders highlighted the need to clearly include SMEs and more broadly corporates as they are also subjected to detriment when exclusions are unclear. On the other hand, other stakeholders highlighted that the definition of consumer in the Directive 2011/83/EU covers natural persons who are acting outside their trade, business, craft or profession.**

EIOPA clarifies that the Supervisory Statement covers natural persons and SMEs, as key issues in relation to exclusions related to risks arising from systemic events triggering the development of this Supervisory Statement were related to both groups. For instance, as revealed during COVID-19 crisis, a systemic event can affect both individuals (e.g. travel insurance) and SMEs (e.g. non-damage business interruption) in a substantial manner. Hence, it is appropriate to promote supervisory convergence and enhanced transparency in relation to both groups. Moreover, the Supervisory Statement is based on IDD requirements, which do not exclude SMEs, but only “large risks” in the case of POG requirements.

With regard to the regulatory framework, EIOPA Regulation (EU) No 1094/2010 prescribes the enhancement of “customer protection” as an objective of the Authority and emphasises that this role must aim the protection of policyholders and beneficiaries. The notion of customer has a broader meaning than consumer as it covers all clients of financial institutions, regardless of whether they are natural or legal persons.

Finally, considering the divergence in comments with some stakeholders advising on expanding coverage of this Supervisory Statement to all policyholders and other stakeholders suggesting to limit it to consumers, the proposed approach strikes a balance. It limits the coverage of this Supervisory Statement to all individuals and entities which, because of their contractual situation (i.e. information asymmetries, contractual imbalances, financial literacy etc.), may not be able to openly negotiate terms and conditions and/or require further protection because of those imbalances.

Based on stakeholders' feedback and bearing the considerations above, further information has been incorporated into the Supervisory Statement for clarification purposes.

- ▶ **A number of respondents to the public consultation suggested to increase clarity on whether the expectations contained in the Supervisory Statement apply to exclusion arising from systemic events only.**

Without limiting supervisory expectations of full compliance with existing rules in the area of all exclusions (i.e. Product Oversight and Governance - POG), EIOPA clarifies that the Supervisory Statement focuses on exclusions related to risks arising from systemic events. References to "exclusions" across the Supervisory Statement as opposed to "exclusions in insurance products related to risk arising from systemic events" are made for brevity and simplicity purposes. Based on stakeholders' feedback, EIOPA has further clarified the scope of the Supervisory Statement including the wording used when referring to exclusions.

2.2. SELECTION OF POLICY OPTION

- ▶ **Some stakeholders did not question the importance of clear and unambiguous communication and the importance of applying POG requirements in a consistent manner. They argued, however, that there is already a set of rules, guidance and statements in the area of POG. These stakeholders equally expressed doubts over the selection of policy option, noting that Policy Option 1 (Maintain the status quo) would have been more appropriate than Policy Option 2 (Issuing a Supervisory Statement). Other stakeholders identified Policy Option 2 as the most appropriate option.**

Whilst the existent regulatory framework provides clear rules, EIOPA is of the view that the issues and detriment which emerged over the past years in relation to exclusions related to risk arising from systemic events has accentuated the need for setting clear supervisory expectations in relation to existing regulatory requirements. This with the view of ensuring a convergent approach to their implementation and consistent outcomes across Europe.

In view of this, the option of maintaining the status quo was discarded given the actual or potential cost for customers, industry and supervisors of not taking action (i.e. denied claims, legal disputes, reputational costs, etc.) outweigh the benefits for all stakeholders. In fact, rather than duplicating existing rules, the purpose of the Supervisory Statement is to promote common supervisory approaches and practices in relation to exclusions related to risk arising from systemic events as per Article 29(2) of Regulation (EU) No 1094/2010 and not promoting such convergence could result in court disputes and uncertainty raising costs for all market participants.

The Supervisory Statement aims to ensure that National Competent Authorities (NCAs) apply high quality and convergent supervision on the treatment of exclusions of risks arising from systemic events in insurance contracts, taking into account the need to ensure a customer-centric approach to product design. This includes ensuring that coverage is as clear as possible and also by providing guidance on key considerations to determine whether, in case of doubt following a systemic event, as risk is covered or not. This does not aim at mandating the level of protection on risks arising from systemic events offered by insurance undertakings, as they are free to determine the coverage offered as long as this is clear and aligned with the target market's needs, objectives and characteristics. It further does not seek for retroactive coverage of risks arising from systemic events, which can pose significant risks to the sector.³

2.3. COMMUNICATION WITH INSURANCE DISTRIBUTORS AND EXISTING AND POTENTIAL CUSTOMERS

- ▶ **Some stakeholders highlighted the need for enhanced communication to distributors. In particular, these stakeholders argued that unclear, complex or ambiguous exclusions have an impact on distributors' duties, noting the appropriateness of sound guidance in the area of exclusions supporting distribution activities.**

EIOPA agrees on the importance of clear communication to distributors for the benefit consumers. As per Article 8 of Commission Delegated Regulation (EU) 2017/2358 (POG Delegated Regulation) insurance undertakings shall provide insurance distributors with all appropriate information on the insurance products, the identified target market and the suggested distribution strategy, including information on the main features and characteristics of the insurance products, their risks and costs, including implicit costs, and any circumstances which might cause a conflict of interest to the detriment of the customer.

³ [Call to action for insurers and intermediaries to mitigate the impact of Coronavirus/COVID-19 on consumers | Eiopa \(europa.eu\)](#)

In view of changes in the area of exclusions that may be triggered if systemic events materialise (i.e. wording amendments, incorporation of new exclusions, etc.) and the consequent effect on distributors' comprehension of the revised product, EIOPA deemed it appropriate to clarify supervisory expectations over the information provided to distributor on the insurance product. As a result, paragraph 3.16(d) of the Supervisory Statement contains elements supporting NCAs in identifying key aspects of the communication to distributors when assessing compliance with POG requirements. In the event of substantial impact on distributors' knowledge and understanding due to changes on exclusions, enhanced communication is also touched upon on the said paragraph of the Supervisory Statement

- ▶ **Some stakeholders shared views on the use of examples of exclusions related to risk arising from systemic events. In particular, they noted that the Supervisory Statement may cause confusion and create additional compliance requirements. Conscious of the difficulty of striking a balance between providing an exhaustive list of exclusions and making the terms and conditions overly complex respondents suggested to focus on clarity of wording.**

Paragraph 3.8 of the Supervisory statement does not aim to interfere with insurance undertakings decision to use examples if they deem it appropriate to ensure consumers can better understand exclusions. On the contrary, the Supervisory Statement clarifies expectations to NCAs in the evaluation of documentation on insurance product delivered to consumers so as to ensure that example(s) of events listed bring clarity rather than creating further confusion.

EIOPA does not expect that all possible examples are listed. Instead, the Supervisory Statement promotes a clear understanding of the scope of exclusions related to risk arising from systemic events, including unambiguous wording and consumer-centric approaches to presenting any supportive information such as examples of systemic events.

In relation to the suitability of the examples with the target market and insurance cover, EIOPA acknowledges the need to take into account when listing examples the coverage provided by the product and the target market's needs, objectives and characteristics. The Supervisory Statement further clarifies that expectations on examples relate to how appropriate these are for the identified target market. In the event of examples that are not relevant for the target market or too vague and broad (e.g., flooding and similar events), this may provide a false level of comfort, be misleading and/or prevent a clear understanding of the scope of the exclusion

2.4. TREATMENT OF EXCLUSIONS RELATING TO RISKS ARISING FROM SYSTEMIC EVENTS IN THE PRODUCT OVERSIGHT AND GOVERNANCE (POG) PROCESS

- ▶ **Concerns in relation to the granularity of the target market and the supervisory expectations to be proportional to the detail of the main exclusions were expressed, particularly in view of potentially increasing burden and costs for manufacturers.**

The Supervisory Statement does not create new requirements for insurance undertakings in relation to the target market granularity. Target market requirements exist as part of Art. 5 of Commission Delegated Regulation (EU) 2017/2358, among others, including the identification of the target market at a sufficiently granular level, taking into account the characteristics, risk profile, complexity and nature of the insurance product.

The Supervisory Statement solely clarifies that also exclusions related to risks arising from systemic events need to be taken into account when ensuring that the granularity of the target market is adequate to the nature and complexity of the insurance product. Given the effect of exclusions on aspects such as product complexity, among others, it is reasonable that higher granularity is expected in terms of target market definition if the product also contains a high number of exclusions. This should also assist distributors in the demands and needs process and avoid future mis-match between actual and expected coverage.

Since full compliance with the POG and Delegated Regulation is already expected of insurance undertakings and insurance intermediaries, EIOPA considers that the expectation above does not create material burden or costs.

- ▶ **Some stakeholders responded that POG provisions are intended to be applied proportionately and the Supervisory Statement should avoid being overly bureaucratic.**

In light of the requirements of Directive (EU) 2016/97, POG measures should be applied in a proportionate and appropriate manner. This requirement applies regardless of the Supervisory Statement, and thus the proportionality principle is guaranteed. In this regard, expectations described across the Supervisory Statement should be read in the context of existing regulatory requirements. EIOPA clarifies that it opted to focus the Supervisory Statement on POG to ensure insurance product manufacturers have flexibility in implementing the relevant guidance.

On the other hand, EIOPA is not of the view that the supervisory instrument selected to address the issues on exclusions related to risk arising from systemic events observed is overly bureaucratic. The Supervisory Statement does not increase complexity in the treatment of such exclusions or incorporates new requirements to insurance undertakings and intermediaries. Instead, the Supervisory Statement constitutes a practical instrument to promote in the implementation of POG requirements.

To achieve consistent outcomes across Member States, the Supervisory Statement supports enhanced and proactive risk-based supervision which, by definition, prioritises riskier issues, products, and market participants.

2.5. IMPACT ON THE LEVEL OF PROTECTION OF INSURANCE

- ▶ **Some stakeholder commented on the potential impact of the work on exclusion on the level of protection.**

EIOPA agrees the importance of reducing protection gaps in the insurance sector and it has been looking into this topic by carrying out specific work (i.e. EIOPA staff paper on measures to improve the insurability of business interruption risk in light of pandemics and pilot dashboard on protection gap for natural catastrophes, etc.). EIOPA will continue to exchange with stakeholders on this subject in the future.

Nonetheless, lack of clarity in exclusions and, hence insurance cover, should always be avoided. While promoting further clarity may allow for the emergence of protection gaps, ambiguity not only hides protection gaps but also creates significant uncertainty for policyholders and for the sector. EIOPA considers that the benefits of promoting clarity in relation to exclusions bring significant benefits, for instance, in relation to ensuring that protection gaps become more apparent and so that adequate options to close them can also be explored.

In line with the Supervisory Statement, insurance product manufacturers, when designing the product and/or when reviewing the same following a systemic event should take into account the target market's needs, objectives and characteristics – i.e., needed coverage – amongst other considerations rather than just simply excluding coverage. Otherwise, the said design and/or review of the product may raise uncertainty as to the scope of the coverage. This approach, which enables manufacturers to take relevant business decisions, allows for guidance in terms of the process to be followed while ensuring that also ensure that policyholders' considerations are taken into account.

EIOPA'S FEEDBACK STATEMENT

The issues and detriment which emerged over the past years in relation to exclusions related to risk arising from systemic events has accentuated the need for setting clear supervisory expectations in relation to existing regulatory requirements. Pandemics, climate change-

related phenomena or large cyber-attacks are examples of potentially events which have the potential of being systemic event. Product complexity, unclear policy wording or product reviews after systemic events without a proper application of POG rules are examples of issues which can cause detriment to existing and potential customer in general. In this context, more customer-centric approach towards the treatment of exclusions demands is needed.

EIOPA public consultation follows previous work arising from COVID-19 pandemic and showed strong stakeholders' interest on the subject, outlining the relevance to bring more clarity to exclusions-related requirements including when certain risks become uninsurable.

The Supervisory Statement does not aim at promoting the incorporation of new coverages into insurance contracts or the implementation of retroactive protection. Insurance undertakings' ability to do so is not challenged either. Instead, this constitutes a proportionate instrument and convergence tool to address existing and future concerns on treatment of exclusions in insurance contracts relating to risks arising from systemic events and to promote clarity in an area where the non-convergence implementation of POG requirements is leading to both detriment for existing and potential customer and uncertainty for insurance undertakings and insurance intermediaries.

EIOPA re-emphasises the importance of clear communication to existing and potential customer and to insurance distributors. EIOPA will continue facilitating discussion and open dialogue on the topic and will monitor future developments in the area of exclusions.

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