

Supervisory Statement on the use of governance arrangements in third countries to perform functions or activities

1. OBJECTIVE

- 1.1. The European Insurance and Occupational Pensions Authority (EIOPA) provides this Supervisory Statement on the basis of Article 29(2) of Regulation (EU) No 1094/2010¹. This Article mandates EIOPA to play an active role in building a common Union supervisory culture and consistent supervisory practices, as well as in ensuring uniform procedures and consistent approaches throughout the Union.
- 1.2. EIOPA delivers this Supervisory Statement on the basis of the Solvency II Directive², in particular Articles 18, 29, 35 and 41 thereof, and the Insurance Distribution Directive (IDD)³, in particular Articles 1(6), 10 and 16 thereof.
- 1.3. The aim of this Supervisory Statement is to ensure appropriate supervision and monitoring of the compliance of insurance undertakings and intermediaries with the requirements of the relevant EU legislation in relation to their governance arrangements in third countries.
- 1.4. This Supervisory Statement is addressed to the competent authorities, as defined in Article 4(2) of Regulation (EU) No 1094/2010⁴.
- 1.5. The Board of Supervisors has adopted this Supervisory Statement, after a public consultation procedure, in accordance with Article 2(8) of its Rules of Procedure⁵.

¹ Regulation (EU) No 1094/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Insurance and Occupational Pensions Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/79/EC (OJ L 331, 15.12.2010, p. 48).

² Directive 2009/138/EC of 25 November 2009 of the European Parliament and of the Council on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II) (OJ L 335, 17.12.2009, p. 1–155).

³ Directive (EU) 2016/97 of the European Parliament and of the Council of 20 January 2016 on insurance distribution (recast) (OJ L 26, 2.2.2016, p. 19–59).

⁴ Notwithstanding the fact that specific points of this Supervisory Statement describe supervisory expectations for insurance undertakings and intermediaries, they are required to comply with the regulatory and supervisory framework applied by their competent authority based on Union or national law.

⁵ Decision adopting the Rules of Procedure of EIOPA's Board of Supervisors, available at: https://www.eiopa.europa.eu/sites/default/files/publications/administrative/bos-rules_of_procedure.pdf.

2. CONTEXT OF THE STATEMENT

Introduction

- 2.1. EIOPA has stressed in the past the need for insurance undertakings to demonstrate an appropriate level of corporate substance, proportionate to the nature, scale and complexity of their business⁶.
- 2.2. Undertakings should not display the characteristics of an empty shell that could arise, among others, from situations where the undertakings use third country branches to perform disproportionately functions or activities.
- 2.3. Corporate substance includes an appropriate presence of the administrative, management or supervisory board (AMSB) members and key function holders in the Member State of the head office who dedicate sufficient time to fulfil their duties, as well as a level of staff established in the European Economic Area (EEA) commensurate to the nature and amount of regulated business being underwritten or undertaken by the entity in the EEA.
- 2.4. The presence of an appropriate level of corporate substance applies to undertakings that are conducting business and to those that are planning to launch operations.
- 2.5. The presence of an appropriate level of corporate substance should allow for an appropriate oversight and assessment of the undertakings' governance to guarantee effective decision-making and risk management and to allow for proper supervision.
- 2.6. These issues were initially identified in the context of the discussion on the risks arising from the UK withdrawal from the EU. However, they are equally relevant for any third country and it is, therefore, important to address them in a convergent manner as regards any establishment of a governance structure (such as a branch) in any third country jurisdiction.

Application of this Supervisory Statement to insurance intermediaries

- 2.7. EIOPA also includes intermediaries⁷ in the scope of this Supervisory Statement since some relevant activities in the product lifecycle usually attributed to insurance

⁶ For example, Recommendation 9 of EIOPA Recommendations for the insurance sector in light of the United Kingdom withdrawing from the European Union (EIOPA-BoS-19/040) of 19 February 2019.

⁷ The term "intermediaries" is used in this Supervisory Statement to collectively capture insurance intermediaries, reinsurance intermediaries and ancillary insurance intermediaries, which are legal persons and take up or pursue the activity

undertakings, such as underwriting/placement of risks, may be carried out by intermediaries, which are not subject to the same level of regulation of third country activities as insurance undertakings under Solvency II. The IDD provides for restrictive direct access (via freedom to provide services and without recourse to an EU registered intermediary) for intermediaries established in third countries to the EU market based on compliance with national laws of the Member States⁸. On this basis, the legislative intention of the IDD can be understood as not providing unfettered direct access for third country intermediaries to EU markets.

2.8. Therefore, this Supervisory Statement aims to facilitate the supervision of situations where an intermediary registered in the EU is, or becomes, disproportionately dependent on services provided by a branch in a third country in order to carry out distribution activities which target EU27 policyholders and coverage of EU27 risks falling under the scope of the IDD (e.g. the potential for direct underwriting of insurance contracts/placement of EU27 risks for EU27 policyholders taking place outside the EU). This reflects the approach already taken by EIOPA in Recommendation 9 of its Recommendations for the insurance sector in light of the United Kingdom withdrawing from the European Union⁹.

2.8 Although the system of governance concept is not formally replicated in the IDD, the professional and organisational requirements for intermediaries¹⁰ provide a corresponding basis for including intermediaries in this Supervisory Statement in view of promoting ongoing supervision of their activities. The result of these obligations is similar to the system of governance of undertakings, namely that dependence on a third country branch by an EU registered intermediary should not lead to a situation where the staff of that intermediary do not possess appropriate knowledge and ability in order to complete their tasks and perform their duties adequately. In addition, the IDD provides that when using the services of intermediaries, undertakings and intermediaries must use the insurance and reinsurance distribution services only of EU registered intermediaries¹¹.

of insurance distribution under the IDD. The term “undertaking” used in this Supervisory Statement is also intended to capture insurance and reinsurance undertakings that take up or pursue insurance and reinsurance distribution.

⁸ Article 1 (6) of the, IDD. The IDD has no equivalence framework or third country branch regime.

⁹ EIOPA-BoS-19/040, 19 February 2019

¹⁰ These professional and organisational requirements are included in the Chapter IV of the IDD entitled “Organisational Requirements”, which is a notion synonymous to the system of governance

¹¹ Article 16 of the IDD

Governance arrangements that deserve particular attention with respect to the adequacy of the corporate structure

- 2.9 A particular governance arrangement where the required corporate substance may not be sufficiently present, and raises concerns, is where the undertakings or intermediaries use a branch in a third country to conduct regulated functions or activities (such as providing support with underwriting services). The branch performs that role for the undertaking or the intermediary, which ultimately serves policyholders in the EEA.
- 2.10 These governance arrangements may impair risk management and effective decision making, and have the potential to pose financial, operational and reputational risk and ultimately impair policyholder protection.
- 2.11 Furthermore, the use of these governance arrangements can affect materially the ability of the supervisory authorities to conduct proper supervision. Supervisory authorities may not have sufficient visibility of the functions performed in a third country if, for example, rights to carry out on-site inspections are impaired.

Objective

- 2.12 This Supervisory Statement sets out supervisory expectations to address supervisory practices in relation to governance arrangements where the undertakings or intermediaries use a branch in a third country to conduct regulated functions or activities.
- 2.13 To achieve clarity of supervisory expectations, the principle of substance over form is used to ensure similar risks are treated in a similar way, irrespective of the legal form of the governance arrangement, with the objective of appropriate supervisory oversight of activities and functions performed by the undertakings and intermediaries.
- 2.14 Although these governance arrangements do not qualify as outsourcing, similar risks need to be addressed and therefore supervisory actions aimed at addressing concerns related to outsourcing¹² might also be considered as relevant and appropriate.

¹² Article 49 of the Solvency II Directive.

3 SUPERVISION OF THE GOVERNANCE ARRANGEMENTS

- 3.1 EIOPA and the supervisory authorities expect that the use of a third country branch should not compromise the undertaking or the intermediary having an appropriate level of corporate substance, proportionate to the nature, scale and complexity of its business, within the EEA.
- 3.2 EIOPA is of the opinion that the purpose of a branch of an undertaking or an intermediary should be primarily to serve the market in which it was established. As a result, branches established in third countries with the sole objective of supporting undertakings and intermediaries based in the EU should be avoided.
- 3.3 To address any potential concerns regarding lack of adequate technical expertise or specialist risk coverage in the EU, supervisory authorities are encouraged to promote relocation or secondment of staff from the third country branch to the EU undertaking or intermediary and/or cede part of the insurance risk by way of reinsurance to a reinsurance undertaking headquartered and authorised in a third country¹³.
- 3.4 The third country branch should neither perform regulated functions or activities in such a way that leads to the undertaking or intermediary being disproportionately dependent on the arrangement in a third country for its activities in the EEA nor should the operation of that branch materially impair the system of governance, increase operational risk or undermine policyholder protection. An example of where the undertaking or intermediary would be “disproportionately dependent” on the arrangement in a third country for its activities in the EEA, would be an undertaking or intermediary which is unable to demonstrate to the home EU supervisory authority when requested, that, in the event of sudden loss of access to the branch, it can continue operating normally, and without undermining policyholder protection. In any event, a case-by-case assessment of whether or not there is “disproportionate dependence”, would always be necessary by the home EU supervisory authority.
- 3.5 Supervisory authorities should ensure that regulated functions or activities are appropriately overseen by and controlled from the undertaking, and distribution activities are performed by the intermediary, in a manner which ensures that the undertaking, or intermediary where relevant, is in a position to take full

¹³ In accordance with the position stated in EIOPA Opinion on supervisory convergence in light of the United Kingdom withdrawing from the European Union (EIOPA-BoS-17/141) of 11 July 2017 (see point 24).

responsibility for effective decision-making and risk management in going concern and emergency situations.

- 3.6 Regulated functions or activities should not be structured or conducted in such a way that they impair the ability of the supervisory authorities to monitor the compliance of the undertaking or intermediary with all its obligations stemming from the relevant EU legislation.
- 3.7 When authorising business and as part of ongoing supervision supervisory authorities should request that the undertakings considering or operating such governance arrangements provide sufficient justification and rationale why the proposed structuring of their activities can safeguard the ability of the supervisory authority to undertake proper supervision. This information should enable supervisory authorities to assess properly the planned operations, to conduct proper supervision and to monitor the compliance of the undertakings with their obligations as a whole and in relation to their third country branch. The same principle applies, as appropriate, for intermediaries, which are legal persons, in the context of their professional and organizational requirements under the IDD.
- 3.8 This Supervisory Statement will be published on EIOPA's website.

Done at Frankfurt am Main, on 3 February 2023.

[signed]

For the Board of Supervisors

Petra Hielkema
Chairperson