

Supervision

# UNION-WIDE STRATEGIC SUPERVISORY PRIORITIES

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**eiopa**

European Insurance and  
Occupational Pensions Authority

## 1. Context

As an outcome of the ESAs Review, specific amendments to the ESAs Regulations were made effective 1 January 2020.

In line with article 29 (a) of the revised EIOPA Regulation, EIOPA shall identify, at least every three years, by 31 March, up to two priorities of Union-wide relevance **which shall reflect future developments and trends**. When defining these priorities, EIOPA shall take into consideration **the contributions** received from competent authorities, **existing work** by the Union Institutions, as well as **analysis, warnings and recommendations published by the ESRB**. The identified priorities shall be discussed in the Board of Supervisors.

National competent authorities (NCAs) shall take those priorities into account when drawing up their work programmes and **shall notify EIOPA accordingly**. EIOPA **shall discuss** the relevant activities by the NCAs **in the following year and draw conclusions**. EIOPA shall discuss possible follow up which may include guidelines, recommendations to NCAs, and peer reviews, in the respective area. The priorities of Union-wide relevance identified by EIOPA shall not prevent NCAs from applying their best practices, acting on their additional priorities and developments, and national specificities shall be considered.

2020 has been a challenging year for the global economy in general, due to the Coronavirus pandemic. The outbreak of the Coronavirus has brought huge social disruptions and unprecedented economic challenges, with **inevitable impact on the EU financial sector**.

**Valuation, liquidity, credit and solvency risks** have increased across the board. While liquidity positions of EU banks remained relatively strong, the EU investment fund industry faced a significant deterioration of asset liquidity in some segments combined with substantial outflows from investors in selected asset classes.

The COVID-19 crisis has a significant impact on the insurance and pensions sector also **from a conduct and consumer protection perspective**. At the onset of the crisis, with consumer disposable income deteriorating, loss of employment, market shocks emerging and insurance undertakings, intermediaries and pension funds shifting to remote working arrangements, significant concerns for consumers emerged.

Insurance undertakings and pension fund providers had to rapidly adapt to the new market conditions and take steps to maintain business continuity and services to customers, whilst also ensuring the safety of employees. The COVID-19 outbreak **further underlined the importance of the Solvency II** regulatory framework. The market-consistent and risk-based approach helped insurers to better align risk to capital, build-up resilience and enhance the risk management practices, while the adjustments included for long-term guarantees allowed to mitigate the immediate market volatility caused by COVID-19. The comfortable level of capital buffers as of year-end 2019 helped insurers to withstand the initial severe market shocks experienced with the COVID-19 crisis. However, **a high level of uncertainty on the magnitude of economic disruption increases downside risks going forward**. COVID-19 has further intensified the pre-existing challenges posed by the prolonged low yield environment, a fundamental risk for both insurance and pension sectors.

Mitigating the effects of COVID-19 is **the top priority for the European Union** as a whole. EIOPA, in close **cooperation with the other ESAs and the ESRB** has been monitoring the COVID-19 situation very closely as the outbreak continues to cause

disruption to households and businesses. EIOPA, like the other ESAs has also been tasked to monitor the implication of the COM's Good Practices aimed at mitigating the impact of the crisis on consumers.

In addition, EIOPA has been working closely with the NCAs to ensure financial stability, market integrity and consumer protection, including addressing conduct risks stemming out of the Coronavirus pandemic crisis. In particular, EIOPA and NCAs have shared information and also collected data and engaged with stakeholders at different levels.

Furthermore, EIOPA has been closely monitoring the COVID-19 developments in relation to the occupational pensions sector, including from a conduct perspective, as part of the consumer trends work. As long-term investors, Institutions for Occupational Retirement Provision (IORPs) can play a stabilising role in current volatile markets given their objective of providing adequate retirement benefits to members and beneficiaries. Close monitoring of the COVID-19 impact on IORPs and their sponsors is also essential to clarify any lessons to be learned and collect evidence for strengthening the regulatory framework as part of the scheduled review of the IORP II Directive.

## 2. Supervisory measures

In September 2020, the three ESAs – EBA, EIOPA and ESMA – issued their first **Joint Risk Assessment Report** of the financial sector since the outbreak of the COVID-19 pandemic. In light of the ongoing uncertainties on the recovery from the COVID-19 pandemic, the ESAs highlighted the need to implement policy actions such as: **monitor risks and perform stress testing; foster flexibility where and when needed; support the real economy; stay prepared; supervise digital transformation.**

Furthermore, since the outbreak of the Coronavirus crisis, EIOPA has put in place a number of **supervisory measures** aimed to support insurers to focus on ensuring business continuity and continuing to serve their customers. EIOPA has set out its expectations from the insurance sector in a number of **statements** comprising actions to mitigate the impact of the Corona crisis on the EU insurance sector and its consumers.

These supervisory measures, statements, calls for actions etc. related to business continuity, supervisory reporting and public disclosure, deadline extensions for requests for information, consultations, impact assessments etc., measures to be taken in order to preserve solvency and capital position in balance with the protection of the insured, etc.

In addition, EIOPA issued specific guidance for the insurance sector and the occupational pensions sector respectively as well as for consumers.

In addition, EIOPA performed a detailed quantitative and qualitative assessment of the key risks identified for the insurance and occupational pensions sectors in the EEA area. Results of the assessment revealed the top 6 key risks and challenges in terms of materiality for insurers: **profitability of investment portfolio, solvency position, exposure to banks, underwriting profitability, concentration to domestic sovereign** and **cyber risk**.

The **prolonged low-yield environment** has already been a fundamental risk for both insurance and pension sectors and the COVID-19 outbreak further increased its potential.

The **Insurance Stress Test 2021** will consider the adverse unwinding of the COVID-19 crisis such as a slower than planned recovery of the economy or double dip

evolutions. The narrative and shocks are developed in cooperation with the ESRB taking into account the latest macroeconomic and market developments. Liquidity risk will be included in the Insurance Stress test 2021.

In terms of consumer protection and conduct of business aspects, regular quantitative and qualitative monitoring activities revealed that **possible risks for consumers may** materialise with regards to:

- Business continuity, for both insurance and occupational pensions sectors;
- Exclusions and product design;
- Lack of clarity in terms and conditions;
- Changes in coverage for active contracts or at renewal;
- Product design and pricing not adequately reflecting the risk levels;
- Structural issues in the retail investment market, with a particular focus on the unit-linked market, which may be heightened by the crisis due to early surrenders and/or the prolonged low interest rate environment;
- Issues with regards to travel insurance products.

These risks and challenges further raise the question on the sustainability of the current business models in terms of financial viability but also in terms of the availability of adequate coverage expected or required by the target markets.

Against this background, EIOPA identifies the following two priorities of Union-wide relevance:

### 3. Union-wide strategic priorities

#### ***(1.) Business model sustainability***

In the context of the COVID-19 crisis and of the prolonged low-yield environment, EIOPA expects NCAs to focus their supervisory activities on monitoring the impact of the prolonged low-yield environment as well as of the COVID-19 crisis on the **business model sustainability and development** of insurers and institutions for occupational retirement provision (IORPs).

Concretely, supervisory activities should focus on assessing the impact of both the COVID-19 crisis and the prolonged low interest rate environment on the **financial viability** i.e. the solvency, profitability and liquidity positions of insurers and IORPs, on short, medium and long term.

The potential spill-over of risks coming from the interconnectedness of insurers with banks as well as potential spill-overs from the sectors of the real economy should also be considered. Furthermore, EIOPA expects NCAs to consider an enhanced market monitoring of Low Interest Rate (LIR) via **stress tests**.

EIOPA further expects NCAs to give due consideration to the **forward-looking risk assessment** insurers and IORPs perform in their ORSA and ORA processes respectively, as well as to the **measures insurers and occupational pensions providers take in order to preserve their capital position** in balance with the protection of the policyholders and beneficiaries, e.g. by following prudent dividend and other distribution policies, including variable remuneration.

The crisis is likely to accelerate emerging trends in industry, especially in the area of digitalisation, sustainability, new insurance and pension products and services or product transformations (e.g. simplification of products, simplification of the product portfolio, structural changes in the products portfolio). Digitalisation is raising significant risks and opportunities from a supervisory perspective; therefore, a proper understanding of the direction of the future transformations is crucial.

EIOPA expects NCAs to **monitor the impact of emerging trends and risks** on insurers' and occupational pensions providers' business models as well as on the future solvency capital and liquidity needs combined with capital generation capabilities on medium-long term.

#### ***(2). Adequate product design, including via a close monitoring of product oversight and governance (POG)***

In the context of the COVID-19 crisis and of the prolonged low-yield environment, EIOPA expects NCAs to focus their supervisory activities on monitoring the impact of the COVID-19 crisis on products and ensuring that POG requirements and other relevant consumer protection and conduct of business related requirements are adequately implemented to address the deficiencies which emerged in the crisis. This will include an analysis of product and contract complexity as well as an assessment if the insurance undertakings and occupational pension funds have adequately assessed changes in product risk profiles both as a result of consumer behaviours and market shocks.

Profitability, for both insurers and occupational pensions providers, is likely to be impacted and as such, it is necessary that products are reviewed to ensure on one hand sustainability of business models and on the other hand customer centricity. In this context, EIOPA expects NCAs **to assess whether product manufacturers have**

**adequately implemented customer-centric product design and product approval processes.** Further, EIOPA expects NCAs to assess product sustainability and test whether these products offer value for money to consumers and savers.

Concretely, for existing products, EIOPA expects NCAs **to assess whether, in cases where market shocks have led to significant changes in risk levels, the products are still aligned with the relevant target market** and whether impacting returns are adequately mitigated. In practice, EIOPA expects NCAs to monitor whether manufacturers assess the design of the products to ensure that they are easily understood and offer value by/to the relevant target market.

Changes in consumers' habits and behaviours as a result of the COVID-19 crisis have led to significant changes in risk profiles of products with pricing often not fully reflecting the actual risk level. EIOPA expects NCAs **to assess whether insurance manufacturers have adequately performed product monitoring and review activities** focusing on the products whose features and target markets' needs, objectives and characteristics have been impacted by the COVID-19 crisis, leading to a significant change to the risk profile and raising questions on fair treatment of consumers. This will also include a close monitoring of claims ratios and mitigating actions taken.

EIOPA further expects NCAs **to monitor and mitigate consumer detriment with regard to the way exclusions have been dealt with amidst the crisis and poor value for money risks which have been further elevated by the Coronavirus crisis.** Insurers should ensure a sound and holistic approach by avoiding for instance the risk of retroactive coverage.

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