SUPERVISORY STATEMENT ON SUPERVISION OF REINSURANCE CONCLUDED WITH THIRD COUNTRY INSURANCE AND REINSURANCE UNDERTAKINGS – IMPACT ASSESSMENT

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CONTENTS

1. ANALYSIS OF COSTS AND BENEFITS

1.1. Procedural issues and consultation of interested parties

1.1. EIOPA acknowledges the fact that reinsurance is, and should remain, an international cross-border business that is based on the global diversification of risks which offers numerous advantages to insurance undertakings. To avoid unnecessary duplication of regulation and promote open international insurance markets, the European Commission may decide on the equivalence of a third country's (in this context it refers to non-EEA countries) solvency and prudential regime. In case of reinsurers from the United States of America (US) an important achievement in the direction of simplifying cross-border market access is the EU-US Agreement (“The Agreement”) on Insurance and Reinsurance.

1.2. In 2022 EIOPA analysed the way National Competent Authorities (NCAs) regulate and supervise reinsurance practices regarding the use of reinsurance with reinsurance undertakings located in third countries[1]. The work was done in line with EIOPA’s Supervisory Convergence Plan (SCP) for 2022[2].

1.3. As a result of its work EIOPA developed a “Supervisory Statement on supervision of reinsurance concluded with third country insurance and reinsurance undertakings” (“Supervisory statement”) inspired by concrete cases shared by NCAs.

1.4. According to Article 29(2) of the EIOPA Regulation[2], the Authority conducts, where appropriate, an analysis of costs and benefits in the process of issuing opinions or tools and instruments promoting supervisory convergence. The analysis of costs and benefits is undertaken according to an Impact Assessment methodology using the data analysis performed by EIOPA in drafting of the Supervisory statement.

1.5. The “Supervisory Statement on supervision of reinsurance concluded with third country insurance and reinsurance undertakings” together with this Impact Assessment were publicly consulted during the period July-October 2023 and their current versions reflect comments received.

[1] The Supervisory Statement refers to third country reinsurance undertakings which in the context of the document comprises both third country reinsurance undertakings and third country insurance undertakings carrying out reinsurance business.

[2] The topic was also included in the Supervisory Convergence Plan for 2023.

1.2. Problem definition

1.6. The impact assessment methodology foresees that a baseline scenario is applied as the basis for comparing policy options in the estimation of the impact. This helps to identify the incremental effect of each policy option considered. The aim of the baseline scenario is to explain how the current situation would evolve without additional regulatory intervention promoting convergent supervision regarding insurance undertakings using reinsurance arrangements with third country reinsurance undertakings.

1.7. For the analysis of the potential related costs and benefits of the proposed "Supervisory Statement on supervision of reinsurance concluded with third country insurance and reinsurance undertakings", EIOPA has applied as a baseline scenario the effect from not issuing a supervisory statement towards the changes envisaged of its application.

1.3. Objective pursued

1.8. While this document is addressed to NCAs, it is expected to have also indirect effects on insurance and reinsurance undertakings.

1.9. The Supervisory statement refers mainly to insurance undertakings using reinsurance as risk-mitigation techniques.

1.10. The "Supervisory Statement on supervision of reinsurance concluded with third country insurance and reinsurance undertakings", sets out supervisory expectations regarding:

- Establishment of an early on-going supervisory dialogue;
- Assessment of insurance undertakings' risk management system on the use of third country reinsurance;
- Assessment of reinsurance contracts compliance with Articles 209-211 of the Solvency II Delegated Regulation.

1.11. The Supervisory statement's objective is to propose a risk-based approach in limiting the effect of the risks that might stem from reinsurers based mainly in not-equivalent prudential regimes[3] and to ensure a high-quality and convergent supervision.

1.4. Policy issue and options

1.12. In the impact assessment of the "Supervisory statement on supervision of reinsurance concluded with third country insurance and reinsurance undertakings", EIOPA has duly

3 Considering the existing Agreements and Memorandum of Understanding with third countries that might exist and might be considered applicable.

analysed the costs and benefits of the main supervisory expectations included in the paper as well as the effectiveness of the options against:

- Objective 1: Effective and efficient supervision of (re)insurance undertakings;
- Objective 2: Improving assessment of the risk management and internal control systems, including assessment of the risks arising from contracts with a third country reinsurer and principles for the selection of reinsurance counterparties;
- Objective 3: Improving transparency and better comparability.

1.13. The section below reflects the policy options that have been considered and analysed.

Policy issue	Options
1. Supervision of reinsurance concluded with third country insurance and reinsurance undertakings	1.1 No change 1.2 Issue an internal document to be used only by the National Competent Authorities (NCAs) 1.3 Publication of a supervisory statement on EIOPA's expectations on supervision of reinsurance concluded with insurance and reinsurance undertakings from third countries

1.14. The costs and benefits of each option have been further assessed and included in the following table.

Policy issue: Supervision of reinsurance concluded with third country insurance and reinsurance undertakings		
Option 1.1: No change		
Costs	Policyholders	No additional costs are expected as the framework is kept as of today. However, potential costs might arise in case of issues in supervision of reinsurance with third country reinsurance undertakings that otherwise might have been mitigated by the clear communication of EIOPA's expectations.
	Industry	No additional costs are expected as no additional expectations are communicated to the market. As with the policyholders, some potential costs might arise in case of issues of reinsurance with third country

		insurance and reinsurance undertakings which might have been mitigated by EIOPA's expectations.
	Supervisors	No additional supervisory convergence as the status will be kept of today. There might be different supervisory practices on supervision of reinsurance with third country insurance and reinsurance undertakings. As with the other areas some potential costs might arise in case of issues in supervision of reinsurance with third country insurance and reinsurance undertakings which would have been otherwise mitigated by EIOPA's expectations.
	Other	N/A
Benefits	Policyholders	No material benefit is expected
	Industry	No material benefit is expected.
	Supervisors	No material benefit is expected.
	Other	N/A
Option 1.2: Issue an internal document to be used only by the NCAs		
Costs	Policyholders	No material costs are expected.
	Industry	The Statement does not introduce new requirements and as such it is not expected to lead to material costs. In the area of collateral, the Statement also does not introduce requirement for collateral nor is encouraging its use but rather looking at the cases when there is a collateral in place (which is an existing practice). As such no significant costs to reinsurers by way of reduced efficiency of capital are expected. However, some potential costs might occur due to the lack of clarity on supervisory expectations.
	Supervisors	Some potential costs are expected in case any of the national competent authorities decides to follow on the Internal document.
	Other	N/A
Benefits	Policyholders	Some benefits are expected stemming from the possible follow up on the internal document increasing the market harmonization and the level of policyholders' protection.
	Industry	Possible harmonization and improvement in the assessment of the risk management and internal control systems (including strategies, processes, and reporting procedures necessary to continuously identify, measure, monitor, manage and report on the risks to which the insurance

		undertaking is or could be exposed in case of reinsurance with reinsurance and insurance undertakings from third countries considering their different domiciles) as well as in the areas to be considered in the assessment of the reinsurance contracts with insurance and reinsurance undertakings from third countries.
	Supervisors	Increase awareness of the risks stemming from prudential regimes that are not Solvency II based and implementation of the proposed risk-based approach in limiting their effect e.g. in the assessment of the risk management and internal control systems as well as in the assessment of the risks arising from reinsurance contracts with insurance and reinsurance undertakings from third countries.
	Other	N/A
Option 1.3: Publication of a supervisory statement on EIOPA's expectations on supervision of reinsurance concluded with insurance and reinsurance undertakings from third countries		
Costs	Policyholders	No material costs are expected.
	Industry	No material impact as risk management implies an adequate management of the risks. In addition, as the Statement does not introduce requirement for collateral nor is encouraging its use but rather looking at the cases when there is a collateral in place (which is an existing practice) no significant costs to reinsurers by way of reduced efficiency of capital are expected. Furthermore, in general the Statement does not introduce new requirements and as such it is not expected to lead to material costs. However, some potential costs might occur due to potential negative implications of the Supervisory Statement if it leads indirectly to a decrease in reinsurance purchase by EU insurers and/or increasing level of under-insurance (protection gap). Such costs are expected to be outweighs by the potential benefits of the Statement in limiting the effect of the risks stemming from small number of reinsurers. The content is not expected to impact all (re)insurance undertakings having reinsurance with third country reinsurers but rather to be limited to the market share of the non-equivalent reinsurers from third country which for 2021 represents 16,76% of the total recoverables of the European market.
	Supervisors	Same observations as those highlighted in Option 1.2.
	Other	N/A

Benefits	Policyholders	Policyholder protection is enhanced by communicated expectations in the management of reinsurance and reinsurance contracts with reinsurance undertakings from third countries.
	Industry	More transparency regarding supervisory expectations on the management of reinsurance. Alignment with the expectations in the supervisory statement in the assessment of the risk management and internal control systems, including assessment of the risks arising from contracts with a third country reinsurance undertakings and principles for the selection of reinsurance counterparties.
	Supervisors	As with Option 1.2. Enhanced supervisory convergence in supervision of reinsurance risks related to the use of reinsurance with third country reinsurers.
	Other	N/A

1.15. With regards to option 1.1 neither additional material costs nor cost reductions are expected as it keeps the status quo. Both option 1.2 and 1.3 are considered to bring additional costs while also additional benefits.

1.16. As far as impacts of possible changes are concerned, options 1.2 and 1.3 might lead to changes mainly in the NCAs on-going dialogue with insurance undertakings on their Reinsurance Strategy and its impact on the solvency position, in the assessment of the risk management and internal control systems of insurance undertakings (including strategies, processes, and reporting procedures necessary to continuously identify, measure, monitor, manage and report on the risks to which the undertaking is or could be exposed considering the different domiciles of third country reinsurers used) and in the assessment of the risks arising from contracts with reinsurance undertakings from third countries. Some potential costs might occur also due to potential negative implications of the Supervisory Statement if it leads directly or indirectly to a decrease in reinsurance purchase by EU insurers and/or increasing level of under-insurance (protection gap). Such costs are expected to be outweighs by the potential benefits of the Statement in limiting the effect of the risks stemming from small number of reinsurers. The impact of the costs is not expected to impact all (re)insurance undertakings having reinsurance with third country reinsurers but rather to be limited to the market share of the non-equivalent reinsurers from third country which in terms of total recoverables represents 16,76% (including US which falls under the EU-US Agreement).

1.17. As the Statement does not introduce requirement for collateral nor is encouraging its use but rather looking at the cases when there is a collateral in place (which is an existing practice) no significant costs to reinsurers by way of reduced efficiency of capital are expected.

1.18. In terms of expected benefits, option 1.1 is not anticipated to bring such benefits because it keeps the status quo. Option 1.2 is expected to improve the assessment of the risk management and internal control systems as well as the assessment of the risks arising from contracts with a third country reinsurer. However, under this option supervisory expectations will only be known as part of the regular supervision process. Option 1.3 is expected to bring the same benefits of option 1.2, plus the benefits stemming from the clear communication to the market on the expectations on supervision of reinsurance concluded with third country insurance and reinsurance undertakings and the increased supervisory convergence.

1.5. Evidence

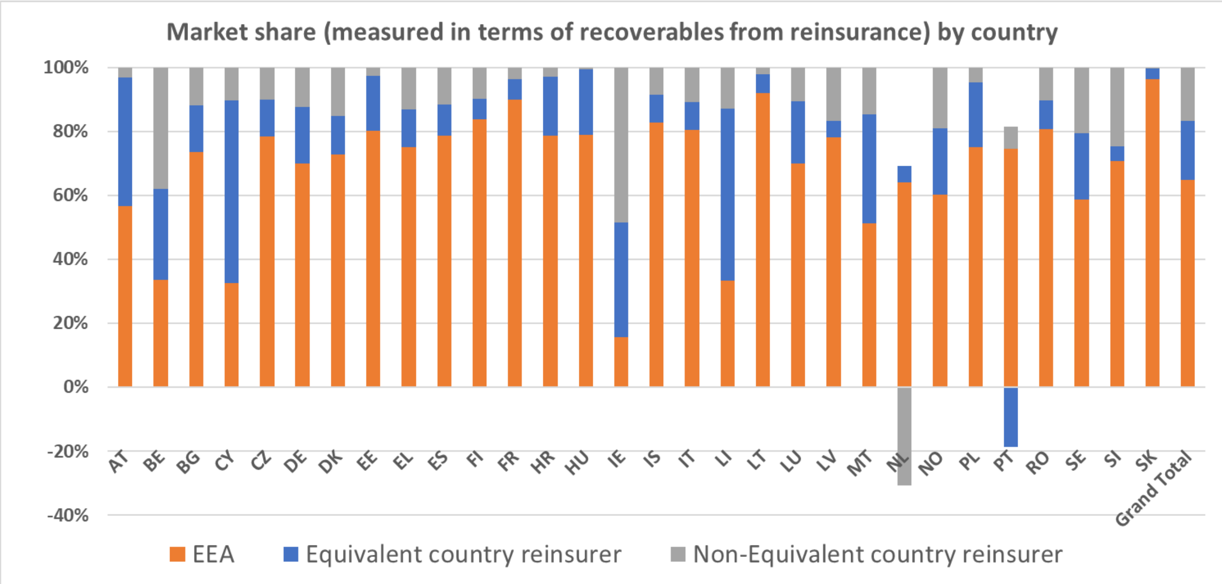
1.19. The analysis is based on the work done in 2021 and 2022 by EIOPA on the way National Competent Authorities (NCAs) regulate and supervise reinsurance practices regarding the use of reinsurance with insurance undertakings having their head office located in third countries. The work was done in line with EIOPA's Supervisory Convergence Plan (SCP) for 2021 and 2022 and is based on real cases. The following evidence was used:

- Survey to the NCAs on supervision of reinsurance with third country reinsurance undertakings (October-November 2021);
- Bilateral exchange of information with some NCAs (April 2022);
- Discussions in EIOPA's Expert Network on Reinsurance on the practices observed on supervision of reinsurance with third country reinsurance undertakings (2022-2023).

1.20. The "Supervisory Statement on supervision of reinsurance concluded with third country insurance and reinsurance undertakings" has been developed considering the use of reinsurance with third country reinsurance undertakings by country and major third countries.

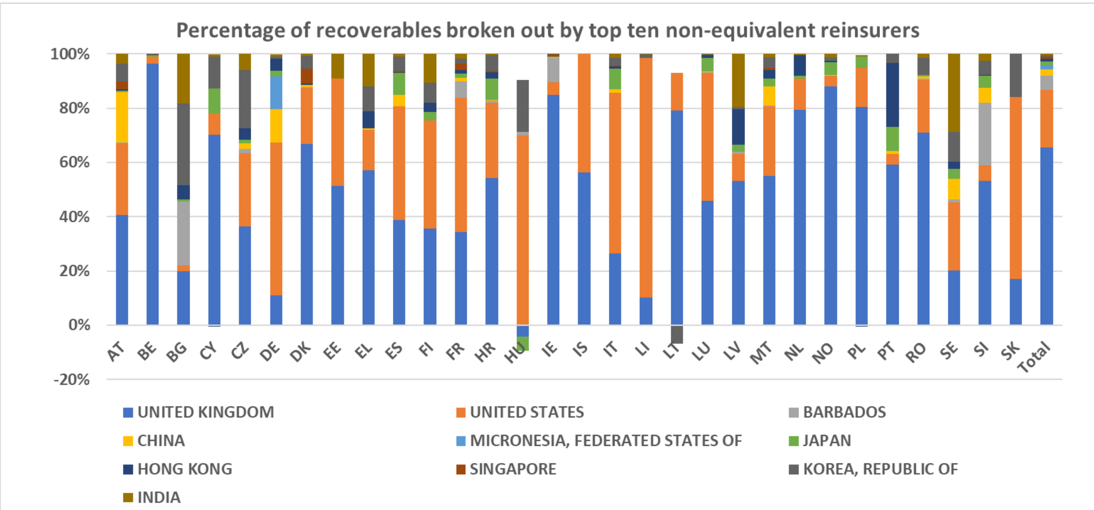
1.21. The following graphic shows, for each EU country, the proportion of reinsurance from EU, equivalent 3rd countries and nonequivalent third countries, as measured by market share. The market share is calculated with the amount of reinsurers recoverables.

***Graphic 1**: Source of reinsurance for each EU country measured by market share (2021)*



1.22. For the total European market, reinsurers from EEA countries represent 64,85% of total recoverables, reinsurers from equivalent third countries 18,39% and reinsurers from non-equivalent third countries 16,76% (all third countries represent 35,15%).

Graphic 2: *EU countries exposure to the top 10 non-equivalent third countries as measured by proportion of recoverables*



1.23. The countries with the highest amount of recoverables with reinsurers from non-equivalent third countries are IE, DE, BE, LU and FR. From those for IE and BE the origin is mainly from the UK, while for DE, FR and LU the origins vary more with a material share from the US in both cases.

Table 1: *The 10 most material non-equivalent third countries in terms of recoverables*

Top 10 non-equivalent country	Total amount of EEA recoverables
UNITED KINGDOM	46,410,125,230 €
UNITED STATES	15,063,507,863 €
BARBADOS	3,618,091,719 €
CHINA	1,673,754,348 €
MICRONESIA, FEDERATED STATES OF	1,261,593,799 €
JAPAN	880,918,240 €
HONG KONG	729,896,247 €
SINGAPORE	485,171,323 €
KOREA, REPUBLIC OF	389,922,516 €
INDIA	381,319,263 €

1.24. Overall, the UK is the main country of origin for the reinsurers classified as reinsurers from non-equivalent countries, followed by US. The UK leading role is mostly due to being a historical global center for reinsurance, but also because of its former EU membership and a legacy of Solvency II implementation.

Table 2: *Credit quality rating of third country reinsurers by amount of recoverables, market share and number of reinsurers*

	Recovable Amount	Percentage of recoverables	Number of reinsurers
Credit quality step 0	105,852,773.79 €	0.15%	44
Credit quality step 1	49,189,752,338.30 €	68.19%	225
Credit quality step 2	16,068,583,867.53 €	22.28%	525
Credit quality step 3	692,762,943.56 €	0.96%	215
CQS btw 0-3 included	***66,056,951,923.16 €***	***91.58%***	**1009**
Credit quality step 4	163,327,235.80 €	0.23%	97
Credit quality step 5	17,527,965.96 €	0.02%	25
Credit quality step 6	90,059,611.87 €	0.12%	26
CQS btw 4-6 included	***270,914,813.64 €***	***0.38%***	**148**
No rating available	3,376,992,014.75 €	4.68%	476
Non-reported	2,427,567,794.44 €	3.37%	299

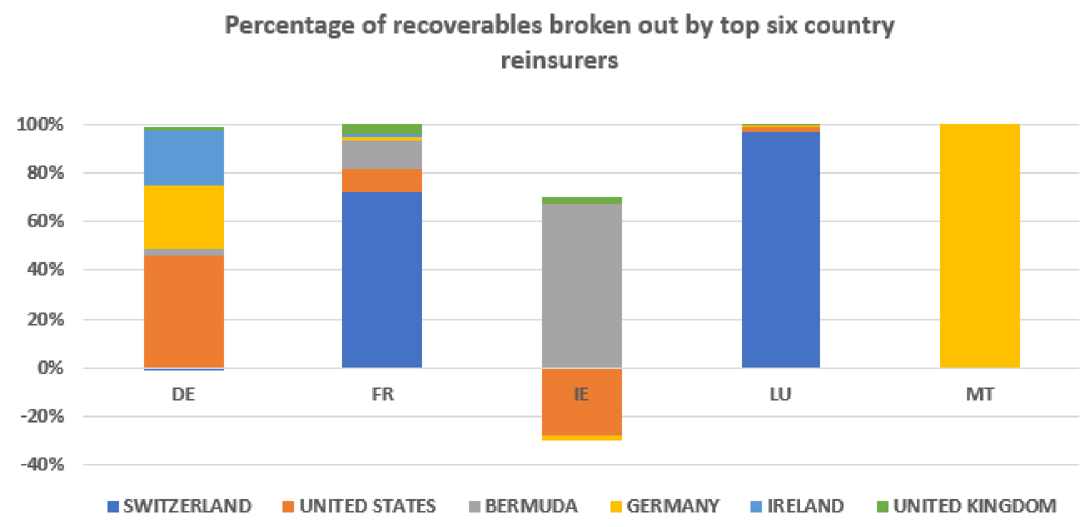
1.25. The large majority of the recoverables in case of third country reinsurance undertakings are with credit quality step 3 and better meaning that in case of non-equivalent third country reinsurance undertakings they could be considered as risk mitigation techniques in the Basic Solvency Capital Requirement according to Article 211 (2) (c) of the Commission Delegated Regulation (EU) 2015/35.

1.26. Considering that some parts of the supervisory statement might be also relevant, following a proportionate and risk-based supervision, to reinsurance undertakings retroceding their risks EIOPA also looked at the biggest EU reinsurers and their business[4].

4 SCOR, Swiss Re Europe S.A, Munich Re, Partner Reinsurance Europe SE, Hannover Re and General Reinsurance AG.

1.27. For the total European market, the biggest EU reinsurers retroceded 20% of their business to EU reinsurance undertakings and 80% to reinsurance undertakings from third country (respectively 57% from an equivalent and 23% from a non-equivalent).

Graphic 3: *Biggest EU reinsurers[5] exposure to the top 6 countries as measured by proportion of recoverables*



1.28. The main third countries towards which there is a reinsurance exposure are Switzerland, US, Bermuda and UK.

1.6. Comparison of options

1.29. The preferred policy option for this policy issue is Option 1.3: “Publication of a supervisory statement on EIOPA’s expectations on supervision of concluded reinsurance with insurance and reinsurance undertakings from third countries”. The overall balance of costs and benefits for the preferred option highlights the importance of publicly sharing EIOPA’s expectations in the supervision of reinsurance with insurance and reinsurance undertakings from third countries. The proposed option further strengthens supervisory convergence in the areas of supervision of reinsurance with reinsurance undertakings from third countries while also provides supervisory expectations for the assessment of the insurance undertakings risk management and internal control systems (including strategies, processes, and reporting procedures necessary to continuously identify, measure, monitor, manage and report on the risks to which

[5] SCOR, Swiss Re Europe S.A, Munich Re, Partner Reinsurance Europe SE, Hannover Re and General Reinsurance AG.

the undertaking is or could be exposed considering the different domiciles of third country reinsurance undertakings used), for the engagement of early dialogue in understanding undertakings' Reinsurance Strategy and its impact on the solvency position and for the assessment of the risks arising from reinsurance contracts concluded with third country insurance and reinsurance undertakings.

1.30. Option 1.1 has been disregarded because keeping the status quo would not enhance further the existing convergence between Member States.

1.31. The three foreseen options have been compared measuring efficiency and effectiveness granted by each of them.

1.32. In terms of Effectiveness, the three options are expected to have the following outcomes:

- option 1.1 means keeping the status quo regardless of the available information;
- option 1.2 is sharing of the information only with supervisors which will not have the benefit of the increased awareness of the market;
- option 1.3 fits all objectives while also grants more effectiveness in the supervision of reinsurance with insurance undertakings from third country.

1.33. In terms of Efficiency, the three options are expected to have the following outcomes:

- option 1.1 means keeping the status quo, does not generate any cost and is not foreseen to further increase efficiency;
- option 1.2, combines a positive effect of the assessment of the risk management and internal control systems, including assessment of the risks arising from contracts with a third country reinsurer and principles for the selection of reinsurance counterparties;
- option 1.3 proves to be a better fitting for all the three objectives also granting more efficiency in the supervision of reinsurance with third country reinsurance undertakings if compared to option 1.2. The estimated costs related to the implementation of the option are expected to be limited considering that for the total European market reinsurance with third countries reinsurers represent 35,15% of total recoverables, out of them 16,76% for reinsurers from non-equivalent third countries.

1.34. The above-mentioned effects are also illustrated by the table below:

Policy issue: 1. Review the adequacy of the content of the supervisory reporting package			
	Effectiveness (0/+/++)		
Options	Objective 1: Effective and efficient supervision of (re)insurance undertakings	Objective 2: Improving assessment of the risk management and internal control systems, including assessment of the risks arising from contracts with a third country reinsurer and principles for the selection of reinsurance counterparties	Objective 3: Improving transparency and better comparability
Option 1.1: No change	0	0	0
Option 1.2: Issue an internal document to be used by the NCAs	+	+	0
Option 1.3: Publication of a public document on EIOPA's expectations towards the (re)insurance undertakings using reinsurance from reinsurers of third countries	++	++	++
	Efficiency (0/+/++)		
Options	Objective 1: Effective and efficient supervision of (re)insurance undertakings and groups	Objective 2: Improving assessment of the risk management and internal control systems, including assessment of the	Objective 3: Improving transparency and better comparability

		risks arising from contracts with a third country reinsurer and principles for the selection of reinsurance counterparties	
Option 1.1: No change	0	0	0
Option 1.2: Issue an internal document to be used by the NCAs	+	+	0
Option 1.3: Publication of a public document on EIOPA's expectations towards the (re)insurance undertakings using reinsurance from reinsurers of third countries	++	++	++

1.7. Conclusion

1.35. EIOPA considered three policy options to ensure supervisory convergence in the areas of reinsurance with third country reinsurance undertakings, safeguard the effective and consistent supervision of insurance and reinsurance undertakings using reinsurance arrangements with third country reinsurers; provide insurance and reinsurance undertakings with areas of expectations to be reflected in the risk management and internal control systems regarding the use of material reinsurers from non-equivalent third country and with areas to be considered in the assessment if the reinsurance contract is in line with Articles 209-211 of the Solvency II Delegated Regulation. The Options considered are (1) No change; (2) Issue an internal document to be used by the NCAs and (3) Publication of a public supervisory statement on EIOPA's expectations towards the (re)insurance undertakings using reinsurance from reinsurers of third countries. Policy option 3 is EIOPA's preferred option in terms of cost and benefits. The principle-based approach strikes the good balance between Improving assessment of the risk management and internal control systems, including assessment of the risks arising from contracts with a third country reinsurer and principles for the selection of reinsurance counterparties and improving transparency.

EIOPA

Westhafen Tower, Westhafenplatz 1
60327 Frankfurt – Germany
Tel. + 49 69-951119-20
info@eiopa.europa.eu
https://www.eiopa.europa.eu