JOINT COMMITTEE OF THE EUROPEAN SUPERVISORY AUTHORITIES

Comments Template on EBA, EIOPA and ESMA's Joint Consultation Paper on its proposed response to the European Commission Call for Advice on the Fundamental Review of the Financial Conglomerates Directive		**Deadline: 13.08.2012 cob**
Stakeholder:	…(Name + Address)	

The question numbers below correspond to Joint Consultation Paper JC CP 2012 01

Please follow the instructions for filling in the template:

- Do **not** change the numbering in column "Question".
- Please fill in your comment in the relevant row. If you have no comment on a question, keep the row empty.
- There are in total 10 questions. Please restrict responses in the row "General comment" only to material which is not covered by these 10 questions.
    - If your comment refers to multiple questions, please insert your comment at the first relevant question and mention in your comment to which other questions this also applies.
    - If your comment refers to parts of a question, please indicate this in the comment itself.

Please send the completed template to joint-committee@eba.europa.eu, jointcommittee@eiopa.europa.eu, and joint.committee@esma.europa.eu**, in MSWord Format, (our IT tool does not allow processing of other formats).**

Comments Template on EBA, EIOPA and ESMA's Joint Consultation Paper on its proposed response to the European Commission Call for Advice on the Fundamental Review of the Financial Conglomerates Directive	Deadline: 13.08.2012 cob

CFA Questions	**Comments**
General Comments	Financial conglomerate supervision is currently set up to provide a supplementary layer between the two arms of a financial conglomerate. While we strongly believe that (re)insurance group supervision under the new Solvency II regime will be sufficiently robust, we do not believe that similar requirements are necessary at conglomerate level. The ESA's consultation raises some important issues in terms of how financial conglomerates are currently viewed at present. Much emphasis is put on a top down approach whereby at present, financial conglomerates are built first according to sectoral rules then supplementary supervision is applied according to interconnectedness between the two sectors. **Many of the ESA's proposals are simply not supported by the current framework for example full consolidation of all unregulated entities and enforcement measures against solo undertakings, particularly those cited in the supervisory toolkit.** We question the need for a fundamental review of financial conglomerates legislation given that once sectoral legislation such as Solvency II is fully implemented, supplementary supervision may not make sense. Solvency II already incorporates many cross sectoral aspects whereby group supervision and reporting requirements extends to other financial sectors and non-financial sectors within the group. While the paper does not specifically address the process of calculating capital requirements at financial conglomerate level, it does consider how unregulated entities would be consolidated at sectoral level. This issue will require further consideration as non-regulated entities are treated differently between sectors and often within each of the sectors themselves, depending on the status of the entity in terms of contribution to group capital. We believe **the first step with capital requirement calculations is to ensure that the levels determined at sectoral level are maintained according to the relevant risk types and business planning periods.** One aim of Financial conglomerates legislation is to eliminate double gearing at conglomerate level. Sectoral legislation such as Solvency II ensures that all adjustments/eliminations will be done at the (re)insurance group level. **A situation of an un-level playing field could arise should (re)insurers be obliged to fully deduct their investment in banks, whereas banks would be subject to a different approach.**

	Reference to EBA internal governance guidelines: We do not support the ESAs reference that the EBA governance requirements are a good starting point when looking at internal governance requirements for conglomerates. The Solvency II framework, and not only EBA guidelines, should be taken into account when developing overall governance requirements to ensure there are no contradictions with sectoral legislation. For example, the requirement for an "independent risk control function" would be new in comparison to Solvency II. The tasks proposed by the EBA duplicate, and may even conflict with the division of responsibilities within the Solvency II framework. For example a (re)insurer's ORSA process falls under remit of the risk management function, however the EBA propose this would fall under scope of internal control function. Given the nature and model based calculations of a (re)insurer's risks, there will likely be a lot of cross over with actuarial function therefore from a (re)insurance perspective, it is difficult to see how this 'control' function could be operationally independent as proposed by EBA. If the financial conglomerates framework intends to go beyond cross sectoral issues, then we query why sectoral legislation is required.
1.	Q1. What should be the perimeter of supervision, when a financial conglomerate is supervised on a group wide basis? Paragraph 47 of ESA's advice deals with waivers for scope of application and while we note the ESAs have made no proposals here, thresholds and waivers should be revisited in the context of other proposals which would enlarge the overall scope of application. • *ESAs Recommendation 1: the perimeter of supervision should be enlarged.* **It is important that any approach towards IORPS should aim to be consistent with achieving a level playing field between IORPs and insurance groups, and amongst member states.** The key objective of the proposal on financial conglomerates is to ensure that cross-sector financial groups are adequately capitalised and supervised, and to avoid artificial capital being created in a financial group that inflates its balance sheet. For (re)insurance groups or (re)insurance dominated financial conglomerates, the draft Level 2 requirements of Solvency II already sufficiently address this by requiring inclusion of IORPs in the group solvency capital requirements. Therefore, the inclusion of IORPs as financial institutions within a financial conglomerate is only appropriate when regulatory

	arbitrage is possible i.e. not in the case of (re)insurance groups or (re)insurance dominated financial conglomerates. If this is not possible because either the group cannot comprise of these entities or the risks are already appropriately captured by the relevant sectoral legislation, then such IORPs should not be included. Thus, IORPs should only be included if one of the previous two criteria are not met. As correctly indicated on page 14 of the consultation paper, the diversity of IORPs among member states currently makes it difficult to analyse the risks they may pose to the financial system and to the groups in a simple way. This makes it difficult to draw general conclusions on this issue at this stage. Furthermore, the IORP Directive is currently under revision and the outcome of it is still unclear at this stage of the process. However in the current IORP directive, the identification of structural links with related financial services entities outside the scope of the IORP directive is not required. Therefore in some markets, IORP controlled groups could be overlooked in terms of group supervision. **Solvency II SPVs will be fully funded and subject to additional governance requirements, we believe the Solvency II framework already addresses the ESAs objective.** According to Solvency II Framework Directive and draft Level 2 measures, SPVs are: • Subject to authorisation procedures; • Required to be meet specific governance requirements; • Required to be fully funded; • Subject to direct supervision; • Excluded from the group solvency requirements but are eligible for treatment as a risk mitigation technique in the solo solvency calculations of the entity which transfers the risk. Based on paragraph 41 (section 4.1.4.3) of the ESAs paper, SPVs/SPEs should be incorporated into the banking or insurance sector, depending on which sector they are most aligned with. We believe that under the Solvency II framework, this would already be sufficiently clear. We would like to highlight that securitizations of an insurance group transferring insurance risk to the capital market are in line with the definition of SPV in the Framework Directive and would thus not be considered as cross-sectorial (i.e. the consideration of SPV/SPEs should not result in a reclassification of an insurance group as financial conglomerate).

Solvency II Ancillary Service Undertakings will be incorporated into group capital requirement calculations, we believe the Solvency II framework already addresses the ESAs objective.

The draft Level 2 text (Article 1 bis (23)) requires ancillary services undertakings to be included in the consolidated balance sheet and solvency calculation, as if the participating (re)insurers held the assets/liabilities or operated the services themselves. These undertakings are included in the group SCR calculation.

Article 323 of the draft Level 2 text deals with their status regarding consolidation in group solvency requirements or proportional consolidation, whereby the undertaking's responsibility is limited to the share capital they hold. Qualitative and quantitative information would thereafter be required on the SCR and own funds of ancillary service undertakings, in so far as they are included in the group solvency requirement.

Regarding availability for group own funds, Article 323(4) continues to state that a minority interest in a subsidiary which is an ancillary services undertaking shall not be considered as available at group level.

Based on para 40 (section 4.1.4.2) of the ESAs paper, an ancillary insurance service undertaking should be included in the insurance sector which would guarantee consistency with the banking sector. We support this view but would like to reiterate that an internal investment service company where some investment activities of an insurance group's proprietary asset management have been outsourced which are (i) closely linked to the business operations of an insurance group and (ii) do not provide any support to third parties should not be considered as "cross-sectorial" activities and therefore not result in a reclassification of an insurance group as financial conglomerate.

- *ESAs Recommendation 2: Mixed Financial Holding Companies (MFHC), even if unregulated, should be made subject to supplementary supervision.*

Solvency II already contains sufficient provisions to identify the ultimate responsible entity of a (re)insurance group, this is consistent with the criteria outlined for financial conglomerates.

Directive 2011/89/EU amends Solvency II to allow that Mixed Financial Holding Companies (MFHCs) be recognised as the ultimate parent of (re)insurance groups. This brings Solvency II in line with banking sector legislation and in practice means that the same undertaking can be recognised as the ultimate parent for both sectoral and conglomerate purposes.

	We support this initiative however it should not be the case that an ultimate parent should repeatedly perform duplicate tasks in order to comply with sectoral and supplementary conglomerate legislation. If sectoral legislation addresses requirements at financial conglomerate level, waivers should apply to eliminate repetition of tasks. We believe that this will be the case under the Solvency II framework. • *ESAs Recommendation 3: MAHC and MAIHC should not become direct addressees of FICOD. Supervisors should have ability to access information via their supervisory toolkit.* **The ESAs should not seek to artificially create intermediate financial holding companies for supervisory purposes only.** It is the undertaking's responsibility and discretion to determine its organisational and legal structure and to designate the appropriate point of entry for the supervisor. There should not be mandatory requirements over group and financial conglomerate structures which may not be in line with the way a financial conglomerate performs its business. An additional layer in the corporate structure of the conglomerate could result in reduced transparency and may also negate the benefits of Solvency II group supervision. The purpose of the financial conglomerate quick fix review was to align definitions to ensure the same entity could be identified as the ultimate parent undertaking under sectoral and financial conglomerate legislation. We find that the ESAs recommendation attempts to unwind recent legislative amendments adopted under the quick fix review. **The motivation to create legally enforceable liability structures, in the form of a 'common chapeau' is not clear.** It is not clear to us the motivation of the ESAs to create multiple lines of communication within financial conglomerates and in particular, the emphasis on the legal liability of "individuals/teams". **If ultimate parent/responsible entities are correctly identified, there should be no need to designate a specific regulated entity as point of entry for supervisors.** We believe that this provision heavily overlaps with the objectives of ESAs recommendations 3 (comments above) and 4 (comments follow in following section). It is not clear to us why financial conglomerates should be required to set up multiple reporting/communication lines at different levels. It should ultimately be the decision of the financial conglomerate to determine

	the legal structure of their business. We also have some strong concerns with the proposed supervisory toolkit as outlined below: • Apply notional capital amount to cover supplementary risks: financial conglomerate legislation itself constitutes a supplementary requirement therefore we are not clear what is meant by "supplementary" in this context; • Enforcement measures via ultimate parent to regulated entities: it should not be the case that, for example, a banking led conglomerate has the power to enforce sanction type actions on a (re)insurance undertaking. This kind of activity could have consequences on the solvency situation of the (re)insurance undertaking under sectoral legislation which might ultimately result in their authorisation being revoked. • Limits on intra-group transactions (IGTs): Solvency II has an advanced mechanism for reporting IGTs and RCs consisting of systematic annual reporting and ad-hoc reporting upon occurrence of a significant IGT. Reporting of a very significant IGT triggers a broader analysis relating to pre-defined events. As long as IGTs are properly understood, given the nature of the transfers and overall impact on the group, it should not be required to impose quantitative limits. • Withdrawal of all or part of a license: business is written at a sectoral level, it should never be the case that a supervisor, other than the one responsible for granting a license or establishing authorisation under sectoral legislation, can revoke the legal basis for any of these activities. Such powers could jeopardise the solvency situation of sectoral undertakings.
2.	Q2. Which legal entity in a conglomerate should be responsible and qualify for compliance with group wide requirements? • *ESAs Recommendation 4: the EC should identify and define an ultimate responsible entity.* **Solvency II already contains sufficient provisions to identify the ultimate responsible entity of a (re)insurance group, this is consistent with the criteria outlined for financial conglomerates.** As previously mentioned, 2011/89/EU amends Solvency II to allow that Mixed Financial Holding Companies (MFHCs) be recognised as the ultimate parent of (re)insurance groups. This brings Solvency II in line with banking sector legislation and in practice means that the same undertaking can be recognised as the ultimate parent for both sectoral and conglomerate purposes. We support this initiative however it should not be the case that an ultimate parent should repeatedly perform duplicate tasks in order to comply with sectoral and supplementary conglomerate legislation. We propose that supervisors of a financial conglomerate be part of a college to ensure the underlying sectors of the financial

	conglomerate are well understood. This is particularly important considering the differences in nature between insurance and banking businesses. It should always be the case that group/solo (re)insurance supervision is carried out by the responsible (re)insurance supervisor, as defined under sectoral legislation.
3.	Q3. Which requirements should be imposed on this qualified parent entity in the context of group wide supervision? • *ESAs Recommendation 5: The ultimate responsible entity should be responsible for compliance with group wide requirements.* **Financial conglomerate supervision should focus only on cross over issues between sectors, if not already captured by sectoral legislation.** Financial Conglomerate supervision is currently set up to provide a supplementary layer between the two arms of a financial conglomerate. We strongly believe that (re)insurance group supervision under the new Solvency II regime will be sufficiently robust and we do not believe that similar requirements will be required at conglomerate level. The upcoming Solvency II framework will provide for extensive regulation of (re)insurance groups. Intra-group transactions (IGTs) and risk concentrations will be continuously monitored and reported in detail to supervisors. "Significant IGTs" will trigger more frequent reporting and deeper analysis of the solvency situation of a group. 2011/89/EU foresees that if sectoral legislation sufficiently covers supervision of IGTs and risk concentrations for financial conglomerates purposes then the supervisory requirements may be carried out only once. We strongly support the use of waivers as it should be possible for supervisors and undertakings to perform these tasks only once, it would be inefficient for the same task to be performed multiple times. Under a system of enhanced cooperation and information sharing, supervisors will be able to maintain a sufficient level of oversight at conglomerate level.
4.	Q4. Which incentives (special benefits or sanctions) would make the enforcement of the group wide requirements more credible? • *ESAs Recommendation 6: the EC should develop an enforcement regime towards the ultimate responsible entity.* • *ESAs Recommendation 7: Supervisors should be able to administer sanction measures addressed at the MAHC or MAIHC.*

	The proposed sanctions and corrective actions are inappropriate and redundant given that business will be written by the authorised undertaking at sectoral level. We find the proposed sanctions and corrective actions envisaged by the ESAs inappropriate and redundant. In particular the proposals to apply an additional notional capital amount to the supplementary capital requirement and also the ability for the lead supervisor of a financial conglomerate to withdraw all or part of a solo license. This is not illustrative of how financial conglomerates are organised/supervised at present. • The supplementary capital requirement at conglomerate level is by definition already a "supplementary requirement" - the difference between sums of own funds and sum of SCRs (for each entity calculated using sectoral rules). It is unclear what additional risks might emerge to justify an additional "notional" capital add-on. • Withdrawal of all or part of license – licenses are issued in accordance with sectoral legislation as the ultimate parent entity of a conglomerate may not necessarily 'write' business. Solo supervisors are responsible for issuing licenses and establishing an authorisation according to sectoral legislation, we do not see a mandate for financial conglomerate supervision in such activities. **We strongly support that differences between (re)insurance and banking models should be appropriately considered.** In response to the ESAs advice in paragraph 112 (section 4.3) on whether sectoral-based approaches may lead to difference in the treatment of financial conglomerates, we believe that different sectoral approaches are necessary given the inherent differences between banking and (re)insurance sectors. This is due to the longer term business time horizon of (re)insurers and emphasis on the liabilities side of the balance sheet. Individual elements of the balance sheet are also different, for example issuing loans is not a major part of a (re)insurer's business. It should not be the aim of conglomerate legislation to align sectoral differences and this should not be a consideration of the ESAs when developing supplementary requirements. Alignment of capital requirements can be achieved in many ways while taking care of the fundamental differences in the prudential regimes. For example in the CRD, no weighting is given to government bonds issued by member States. Under Solvency II, no capital requirement is to be calculated for spread risk attached to government bonds.

5.	Q5. Would supervisors in Europe need other or additional empowerment in their jurisdictions? • *ESAs Recommendation 8: ESAs should draft guidelines or be asked to develop binding technical standards for a common reporting scheme on risk concentrations and intra-group transactions.* **Solvency II outlines detailed requirements for reporting of risk concentrations and intra-group transactions, this should be used as the basis of any reporting regime.** Under the Solvency II framework, binding technical standards will be introduced on reporting of risk concentrations and intra-group transactions, as part of the group supervision regime. These standards are incredibly detailed and (re)insurers are already investing heavily in their implementation plans to support this. We believe this framework should be used as the basis for any reporting regime of risk concentrations and intra-group transactions. Please refer to our Q3 response where we refer the waiver provided for in 2011/89/EU which foresees: if sectoral legislation sufficiently covers supervision of IGTs and risk concentrations for financial conglomerate supervisory purposes, then the requirements on IGTs and RCs may be carried out only once. We fully believe that Solvency II will be sufficiently robust to make use of this waiver. While we see the sense of managing risk concentrations throughout financial conglomerates, we do not support quantitative limits being placed on intra-group transactions. Reporting of these transactions should be sufficient.
Annex H Questions	Annex D *Little risk transfer* We are unclear of the ESAs meaning behind this paragraph, it is not clear to us how the ESAs conclusion is reached in the situation described. Further clarification would also be helpful on the meaning of "affiliated SPE" and how this might interlink with SPVs. This section is particularly confusing when considering SPVs that support CAT Insurance linked securities. Under these arrangements the risk transferred is CAT risk but the economics of the arrangement clearly support that there **is** economic risk

	transfer, but the risk event could be described as unlikely to crystalize. We suggest modifying as follows: "*If the firm determines that there was little economic risk transfer in the first place (for instance, the trenching is such that only catastrophic risk that is so unlikely to crystalize, that there is no discernible economic effect, has really been transferred), it may be more willing to step in and voluntarily support an affiliated SPE*."
General Comments	Insurance Europe is not in a position to provide quantitative feedback on the questions which follow. As a general comment, significant costs would arise as a result of any regulatory decision to force a sub-group breakdown of the conglomerate and any duplicate requirements to those already performed at sectoral level.
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