Insurers of Europe





Annual Report 2010–2011

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CEA

The CEA is the European insurance and reinsurance federation. Through its 33 member bodies — the national insurance associations — the CEA represents all types of insurance and reinsurance undertakings, eg pan-European companies, monoliners, mutuals and SMEs. The CEA, which is based in Brussels, represents undertakings that account for around 95% of total European premium income. Insurance makes a major contribution to Europe's economic growth and development. European insurers generate premium income of over €1 100bn, employ one million people and invest almost €7 500bn in the economy.

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Contents

Foreword	6
European insurance in figures	8
Solvency II	10
Accounting rules	14
Pensions	16
Systemic risk and stability	18
Global standard-setting	20
International issues	22
Taxation	24
Financial education	27
Anti-discrimination	28
Insurance guarantee schemes	30
Consumer information	32
Distribution	34
Natural catastrophes	36
Insurability	38

The CEA

Member associations	42
General Assembly & 2nd International Conference	45
Publications 2010–2011	46
Executive Committee	48
Strategic Board	51
Committees and steering groups	53
Staff	56

The CEA publications and position papers mentioned in the Annual Report can be downloaded from the CEA website, www.cea.eu.

Foreword

Solvency II. Europe's new regulatory regime has been the common strand running through much of the CEA's most important work in the last 12 months. The new prudential regime, which is due to come into force at the start of 2013, should create more harmonised insurance supervision across Europe, be more sensitive to the risks faced by (re)insurers and result in greater security and fairer prices for policyholders and beneficiaries.

Unsurprisingly, preparations for the regulatory framework itself have been the most significant workstream for the federation this year (see p10), and this will continue to be the case for the foreseeable future. The CEA has been closely involved at all stages and in all areas of the development of the Level 2 implementing measures that flesh out the Solvency II Framework Directive. In the past year our members also engaged fully with the European Commission's fifth study of the likely quantitative impact of Solvency II, QIS 5, despite the exercise's obvious difficulties and limitations.

As the protracted and difficult negotiations over the implementing measures near completion, our attention is turning to the related Omnibus II Directive and to the Solvency II Level 3 measures and guidance. Much work still needs to be done to ensure that the economic principles enshrined in the Framework Directive are maintained. Solvency II is a brave and positive step in insurance regulation. Its sophisticated approach of combining quantitative and qualitative elements of supervision, rather than just imposing crude capital requirements, is the future for insurance supervision in a global and complex world.

As such, Solvency II must inform the debate in many other areas of regulatory and supervisory reform, both at European and at global level. The issue of systemic risk, "too big to fail" companies and financial stability (see p18) have been high on political agendas in recent months. While insurers' core activities have not been identified as a source of systemic risk, for the small number of non-core activities that could potentially pose a risk, it is clear that the high supervisory standards and ladder of potential regulatory intervention introduced by the Solvency II regime obviate the need for any further regulatory action on systemic risk in insurance. This is all the more true when one considers that, unlike in banking, there is no international regulatory standard in insurance but a patchwork of regulations of different depths. The CEA will continue to work to ensure that this message is understood.

In the debate over a financial services tax, too, the value of Solvency II should not be overlooked. The Commission has initiated a consultation on a potential tax on the financial services sector (see p25) so that the industry contributes to the cost of past and future crises. Yet here again, efficient supervision and appropriate regulation — as enshrined in Solvency II — are by far the best way to ensure financial stability.

Likewise in the debates over the Commission's proposals to introduce insurance guarantee schemes (see p30), we believe that the strength of the forthcoming Solvency II regime must be taken into account. The package of measures that includes guarantee schemes and was published by the Commission in July 2010 has the laudable aim — fully supported by the CEA and its members — of ensuring maximum consumer protection and confidence in financial services. While the CEA supports the EC's objective of

protecting consumers and beneficiaries in the unlikely event of an insurer insolvency, it is again convinced that the Solvency II regime provides the necessary level of security for consumers.

Last but by no means least, Solvency II affects the current debate on pension reform. When it is introduced, Solvency II will apply risk-based valuations and regulatory capital requirements to insurers offering occupational pensions, while pension funds will continue to be subject to a non risk-based approach. The CEA is therefore calling for the principle of "same risks, same rules, same capital" to be respected in the review of the EU's IORP (Institutions for occupational retirement provision) Directive.

Clearly, therefore, the correct implementation of Solvency II is vital for Europe's insurers, economy and consumers. In light of this, the March 2011 ruling by the European Court of Justice against the use of gender-based differentiation in insurance pricing (see p28) is particularly troubling, striking as it does at the heart of the fair and accurate risk assessment that is the cornerstone of the Solvency II regime. While the insurance industry accepts the ruling, its imprecise nature will decrease legal security and might expose insurers to greater compliance risk.

In order to reduce the risk of policies and rulings that give rise to such negative consequences for the industry, the CEA has done — and will continue to do — its utmost to raise the understanding of policymakers, interest groups and the public of how insurance works. Increased understanding among policymakers of the fundamental principles that govern the way insurers assess and price risk is vital if we are to avoid unintended harm to the security and future of the insurance industry.

The CEA's role in explaining the principles of private insurance goes beyond the anti-discrimination debates around the EU's Gender Directive and proposed Anti-Discrimination Directive (see p29). It is also essential in the discussions on the best ways to reduce the impact of natural disasters and to tackle the effects of climate change (see p36). And it is equally important in all broad debates on insurability, particularly where policymakers are considering compulsory insurance schemes (see p38).

Common themes such as Solvency II and the explanation of risk assessment only serve to underline how important it is that Europe's insurers speak with one strong voice. As the representative voice of the industry, the CEA is well placed to ensure that this is the case.

Tommy Persson

CEA President

Michaela Koller

CEA Director General

European insurance in figures

Growth in life and non-life premiums in 2010

After the serious recession that hit the EU in 2009 — when real GDP decreased by around 4% — 2010 was in general a year of slow recovery for many European countries. According to Eurostat figures, real GDP grew 1.8% in the EU. The capital markets experienced some volatility as a consequence of the sovereign debt crisis, but in general they did not lose the 2009 rebound. Against this background, European insurers, who are among the largest institutional investors, saw their investment portfolios grow.

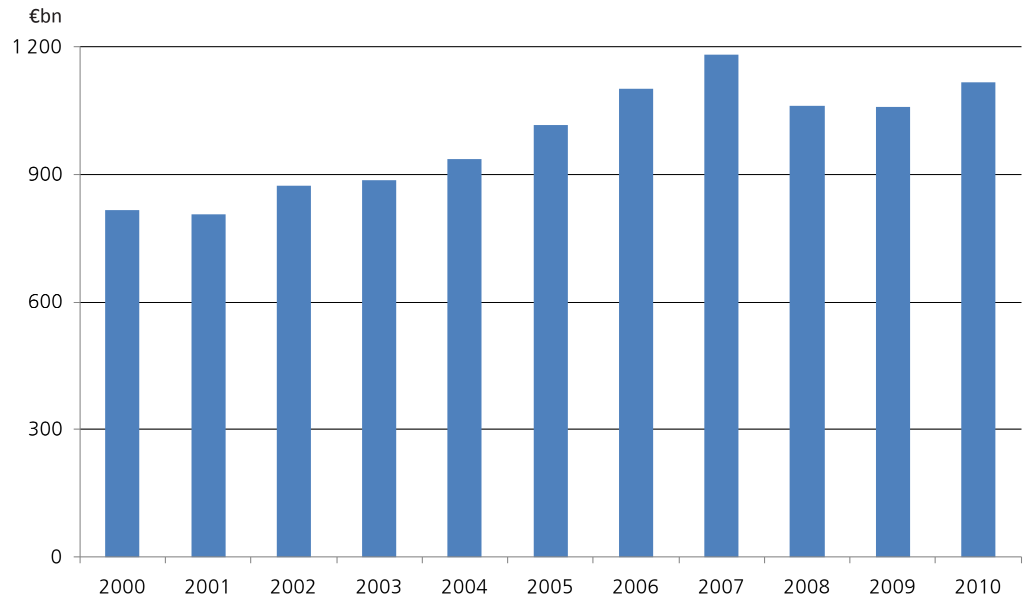
Provisional figures for 2010 show that European insurers weathered the economic crisis well, as total gross written premiums increased by over 3.5%, at constant exchange rates, to reach €1 115bn.

This growth is higher than that experienced in 2009, which was 3% at constant exchange rates. While the 2009 growth was mainly driven by the life sector, 2010 shows a rather different picture since similar growth is seen in both the life and non-life sectors.

Life keeps growing

With an estimated 4% increase at constant exchange rates over the previous year (versus a 5% increase in 2009), European life premiums are estimated to amount to €688bn in 2010. The largest markets continue to be the UK, France, Germany and Italy, which jointly account for almost 75% of overall European life premiums. The four countries all experienced growth; of 2%, 4%, 6% and 11% respectively. For the UK and Germany, the growth is mainly seen as a consequence of customers' need for security and has been reflected in a rise in new business for traditional products. For France and Italy, the growth appears to be more the result of a favourable financial environment, since unit-linked products experienced the strongest growth.

Total gross written premiums in Europe — 2000–2010 (€bn)



Note: 2010 figures are provisional

Health drives non-life

After two successive years of relatively stable premium income, there appears to be a strengthening in the non-life sector in 2010, since provisional figures show a growth of almost 3% at constant exchange rates to a total of €428bn. This overall increase is mainly the result of economic recovery, with households and companies showing a renewed interest in insurance products.

Within the non-life sector, motor insurance continues to be the largest business line, with almost 30% of the market. Germany and Italy are the main players, with a market share of 16% each. These two countries, together with France and the UK, represent 65% of all Europe's motor premiums. In 2010, motor insurance premiums are estimated to have grown over 1% at constant exchange rates to €125bn, against a 2% decrease the previous year.

Similarly, health insurance remains the second largest non-life business line, with a market share of around 25% in terms of premiums. This sector is led by the Netherlands and Germany, which together account for nearly two thirds of the European market. It seems that the health sector resumed growth in 2010 after the slowdown observed in 2009, with early estimates indicating an increase of around 6% at constant exchange rates, with premiums amounting to €108bn.

In order to strip out the effects of exchange rate changes and better reflect economic reality at the aggregate level, 2008/09 and 2009/10 growth rates have been calculated on the basis of 2010 exchange rates.

Property insurance is the third largest non-life business line, accounting for nearly 20% of non-life premiums. According to early estimates, this sector experienced modest growth of less than 1% at constant exchange rates in 2010, with premiums totalling €83bn. The leading markets are the UK, Germany and France, with around €15bn of gross written premiums each.

Investments keep recovering

Following the rebound of capital markets that began in 2009, and despite the significant level of volatility experienced in 2010, European insurers' total investment portfolio is estimated to have recovered further to around €7 500bn in 2010. This corresponds to an increase of 5% at constant exchange rates.

European insurance premiums and growth — 2008–2010

	Gross written premiums (€bn)			Nominal growth (at current exchange rates)		Nominal growth (at constant exchange rates)	
	2008	**2009**	**2010**	**2008/09**	**2009/10**	**2008/09**	**2009/10**
Life	**642**	**648**	**688**	**1%**	**6%**	**5%**	**4%**
Non-life	**418**	**411**	**428**	**-2%**	**4%**	**0%**	**3%**
Motor	127	121	125	-4%	3%	-2%	1%
Health	99	101	108	2%	7%	3%	6%
Property	81	81	83	0%	3%	3%	1%
Other non-life	112	108	112	-3%	4%	-1%	2%
Total	**1 060**	**1 060**	**1 115**	**0%**	**5%**	**3%**	**4%**

Note: 2010 figures are provisional

Solvency II

The countdown to implementation

The last year has seen the CEA heavily involved in the crucial preparations for the implementation of the new regulatory regime for the EU's (re)insurers, Solvency II.

Since the Solvency II Framework Directive — Level 1 — was agreed in 2009, the CEA's work has been focused on the Level 2 implementing measures (future "delegated acts" — see box on Omnibus II on p12), which flesh out the technical details necessary for undertakings and supervisors to ensure harmonised implementation of the regime when it comes into force in Europe on 1 January 2013.

High QIS 5 participation

A key part of the preparations for Solvency II and a source of information to steer the ongoing discussions on the implementing measures was the European Commission's fifth quantitative impact study (QIS 5), which was carried out by (re)insurers between August and mid-November 2010.

As the last impact study, QIS 4, was carried out back in 2008, QIS 5 was an important exercise to test the effects of several proposals that had since been introduced into the Level 1 Framework Directive and also to test tentative solutions and options for the Level 2 implementing measures identified by the European Commission.

QIS 5 was equally important as a preparatory exercise for undertakings and high participation rate targets were set and achieved. The CEA encouraged and facilitated this participation by organising a string of QIS 5 workshops across Europe (in Brussels, Vienna, Warsaw, Tallinn and Athens), which included presentations by representatives from the European Commission and the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS).

The QIS 5 process was extremely complex, lacked sufficient guidance for companies and suffered from tight time pressure, so great care was needed when interpreting the detailed results. Nevertheless, when they were published in the spring of 2011, they highlighted the need for essential corrections to the tentative solutions of the Commission for the implementing measures.

While maintaining the industry's full support for the principles set out in the Solvency II Framework

European stress tests

In accordance with the requirements set out in the mandate of the new European Insurance and Occupational Pensions Authority (EIOPA), March 2011 saw the launch of the authority's annual stress tests for European insurers.

EIOPA constructed these tests in coordination with the banking sector and the assumptions underlying many of the stresses were as prescribed by the European Central Bank. The European industry had carried out a previous stress test exercise in 2009, but this second exercise saw significant changes from that earlier exercise. In particular, the new stress test was based on Solvency II balance sheets, whereas Solvency I was used previously.

The CEA raised concerns over the preliminary design of the 2011 stress tests and over the practicality of carrying out the tests in the very short timeframe allowed, and as a result many important amendments were made to the original specifications. The results are due to be presented in July 2011.

Directive, the CEA called for corrections to the implementing measures in order to ensure that the health and competitiveness of Europe's insurers are maintained.

The Commission reiterated that it does not expect the European insurance industry overall to have to raise additional capital to meet the quantitative requirements of Solvency II and it established various working groups with CEIOPS' successor, the European Insurance and Occupational Pensions Authority (EIOPA), to deliver solutions by the summer of 2011. The CEA has thus been continuing a constructive dialogue with the EC and EIOPA on the issues to be addressed (see below) to ensure the successful implementation of the new regime.

The Commission must publish an impact assessment with its proposals for the Level 2 implementing measures. At the start of 2011, the CEA responded to the Commission's consultation on the impact assessment. The CEA stressed that the complexity of the measures should be reduced in order to ensure that they can be effectively carried out by all insurance undertakings.

Also influencing the work on the implementing measures are the proposals for the Omnibus II Directive that have been published by the Commission (see box on p12).

Preparing for Level 3
Parallel to the ongoing work on the implementing measures and Omnibus II, the CEA has also started work on Level 3. Public consultations on "binding" Level 3 measures cannot take place before the implementing measures have been published in the official journal of the EU, therefore the CEA's work has been in response to informal pre-consultations with EIOPA.

A large part of the work on Level 3 so far has been on the templates for reporting under the new regime. Over the last year, the CEA has taken part in two rounds of pre-consultations with EIOPA to provide advice on them. Solvency II will enhance disclosure both to the public and also to supervisors and additionally will require supervisory transparency.

This enhanced transparency is a vital component of Solvency II. However, the CEA has been working to ensure that Solvency II will not require undertakings to disclose excessive information that would result in undue burdens and costs and would possibly not be analysed. For some issues, the CEA has argued that detailed reporting should not be required on a systematic basis.

The CEA has also submitted responses to numerous other pre-consultations for Level 3, covering areas such as the own risk and solvency assessment (ORSA), the system of governance, own funds and internal models.

Key outstanding issues
Disappointed with the implementing measure proposals, the CEA intensified its efforts to provide explanations and suggestions in the first half of 2011. EIOPA's original advice for Level 2 and, as a result, several areas of the ensuing draft of the implementing measures, were characterised by a systematic injection of excessively conservative and prescriptive elements.

The CEA reiterated both publicly and to the EC and EIOPA that the implementing measures should be workable for all insurers and should not be too burdensome, complex and expensive to be complied with, especially for small and medium-sized companies. It also stressed that they should still largely meet the objective of avoiding massive average increases in capital requirements. The Commission aims to finalise its technical work on the implementing measures in June 2011.

Long-term guarantees
The results of QIS 5 highlighted the sensitivity of the Solvency II framework to market volatility. While some sensitivity is to be expected under a market-consistent regime, the impact of artificial volatility

in the regime should be avoided. Therefore, the CEA has called for anti-cyclical technical measures to be maintained and even further developed to ensure the correct treatment of short-term market volatility, to avoid unwarranted supervisory or market reactions and to remove the risk that insurers are driven out of the provision of long-term business. The Commission has reacted by setting up a joint insurance industry, EIOPA and member state taskforce to work on the treatment of long-term guarantees in the implementing measures.

As part of the work of this taskforce, the CEA has proposed amendments in several areas such as the discount rate and design and calibration of the market risk capital requirements. In particular, the CEA has expressed strong concerns over an application of the illiquidity premium component of the discount rate on the basis of a subjective assessment of EIOPA that there is a period of "stress". Rather, the illiquidity premium should be applied via a formulaic mechanism in order to allow a pragmatic, independent and predictable approach. The CEA has also supported amendments to allow for a "matching premium" adjustment to the discount rate, in place of the illiquidity premium, for specific business that satisfies stringent requirements.

Cat risk

QIS 5 highlighted the need to adjust the design

The impact of Omnibus II

In January 2011 the European Commission published its draft Omnibus II Directive. Omnibus II proposes changes to how rules and standards will be formulated under Solvency II, reflecting developments since the adoption of the Framework Directive such as the entry into force of the Lisbon Treaty. One significant change will see the current implementing measures that are required under a Lamfalussy-type principles-based directive become "delegated acts".

Omnibus II also makes the expected amendment to move the date of the entry into force of Solvency II to 1 January 2013 and sets out the transitional measures that should be applied to ease the change to the new regulatory regime. Omnibus II also grants extended powers to the strengthened European regulator, the European Insurance and Occupational Pensions Authority.

The CEA released its position paper on Omnibus II in April, supporting transitional measures to ensure that the introduction of Solvency II does not result in market disruption. The CEA sees a need for transitionals particularly in the recognition of hybrid capital, the use of internal models, the recognition of non-European Economic Area subsidiaries as Solvency II equivalent and supervisory reporting requirements.

Transitional measures will need to be set out in more detail under the implementing measures. However, the CEA has insisted that transitional measures should not be seen as an alternative to getting the basic framework of Solvency II right and is looking to finalise work on the implementing measures before determining a list of areas requiring transitional provisions.

The CEA also expressed concerns over the timeframe for the adoption of Omnibus II, since prolonged political negotiations would delay negotiations on Solvency II's Level 2 implementing measures and Level 3 measures and guidance, in turn reducing the amount of time available for undertakings to implement the necessary changes to be able to comply with the new regime. It is of the utmost importance that the quality of legislative drafting is not compromised.

and the calibrations of the catastrophe risk sub-module. The CEA has continuously expressed concerns about the complexity and limitations of the structure for catastrophe risk, which produces a capital level that does not appropriately reflect the underlying risk of each type of man-made or natural catastrophe.

In early 2011, the CEA issued a paper setting out the possible solutions to these issues and arguing for the re-introduction of the allowance for the use of undertaking-specific scenarios under the cat risk sub-module, as was the case in QIS 4. EIOPA and the insurance industry are now working to resolve these issues in a taskforce.

Non-life premium and reserve risk

The QIS 5 exercise provided an opportunity to carry out a non-life data collection exercise as the basis for work to improve the calibrations of the non-life premium and reserve risk capital requirements. The calibration of non-life underwriting risk is a key concern for the industry and it has been addressed by a joint EIOPA/industry taskforce. In a sector that has weathered the crisis well, the CEA would not wish to see large increases in capital requirements.

Complexity

QIS 5 highlighted areas of unnecessary complexity in the default approach for some risk modules and the disproportionate burden that this will place on insurers, in particular when compared to the relative materiality of their capital charge.

The CEA has therefore called for the complexity of certain calculations and requirements to be reduced, particularly for small and medium-sized companies, and has produced a set of proposals to achieve this, while still maintaining an appropriate reflection of risk.

Expected profits in future premiums

Continuing to be a priority concern for the CEA this year has been the treatment of "future profits", which is a (still to be clearly defined) component of the excess of the value of assets backing contractual obligations measured on an economic basis over the life of contracts. EIOPA has pushed for at least part of "future profits" to be removed from Tier 1 capital, despite it being fully retained by the Commission as Tier 1 under QIS 5.

In line with the economic principles of the Solvency II Framework Directive, the CEA has, and is continuing to, support the full retention of "future profits" as Tier 1 capital. This is because in-force business is already stressed under the solvency capital requirement (SCR) calculations and so a lower tiering of "future profits" would double count this risk. It would also increase the cost for insurers to issue regular premium contracts, which would have a damaging impact on European savings markets.

Contract boundaries

The discussions on contract boundaries are causing similar concerns to those related to "future profits" in terms of increasing the cost for insurers to issue regular premium contracts.

The CEA has continuously expressed concern over the definition of the boundary of contracts for the calculation of technical provisions. The approach proposed in QIS 5 was much more restrictive than the industry believes is appropriate, leading to cash flows that are currently viewed by (re)insurers as part of their balance sheet, as well as the risks related to these cash flows, being disregarded. As it was not supported by clear economic principles, the QIS 5 definition was also very unclear, resulting in an inconsistent application across undertakings.

Parallel discussions are taking place as part of the work on International Financial Reporting Standards (IFRS) in which the CEA continues to be active (see p14), in order to ensure — as far as appropriate — that requirements are aligned between Solvency II and IFRS to reduce the burden on the industry.

Accounting rules

Seeking the best possible global standards

The CEA is a firm advocate of high quality international accounting standards for insurers. It has continued to follow closely and contribute to the work of the International Accounting Standards Board (IASB) in developing new international financial reporting standards (IFRS) for insurance contracts and for financial instruments over the last 12 months.

The IASB is due to issue a final standard on both projects by the end of 2011, having initially aimed for June 2011. The CEA has called for both standards to become mandatory on the same date and not for reporting periods before 1 January 2015.

The CEA has also closely monitored the interaction between the development of the international accounting standards and the Solvency II regulatory regime (see p10). The CEA will continue to compare the two models and assess whether any differences are justified.

Creating a global standard

The IASB, together with US standard setter the Financial Accounting Standards Board, has been working to develop a standard (IFRS 4 Phase II) for insurance contracts that aims to remove discrepancies between how insurers prepare their financial statements in different jurisdictions and to make insurers' financial statements easier for users to understand.

The CEA fully supports these aims. IFRS 4, the current interim standard, requires companies to account for insurance contracts as they do under national accounting rules, so insurers' financial statements are not comparable.

In July 2010 the IASB issued a revised proposed standard or exposure draft. This contained very significant improvements (eg, no profit at inception, use of entity-specific assumptions, etc.) compared to the previous consultations, which had been heavily criticised by the insurance industry. However, it also contained a number of flaws that would seriously damage the insurance industry and hence the value of insurance companies.

The industry's concerns were expressed in a joint CEA/CFO Forum response to the exposure draft that was submitted in November 2010. The key concerns that were raised related to the volatility introduced into the net income and to the transition requirements. Insurers also called for the model to be field tested before the final standard is issued.

Unacceptable volatility

The model proposed in the exposure draft is based on a balance-sheet approach: the performance of the year (the net income) is simply taken to be the difference between the opening balance sheet and the closing one. However, the recent financial crisis has shown that there could be significant variations in market prices and discount rates. Some of those variations are short-term compared to the long-term nature of much insurance business. Insurers therefore do not believe that booking short-term changes in the profit and loss of a year adequately reflects their business model.

As a result, the industry asked the IASB to investigate a way to properly reflect the performance of insurers, making suggestions for how a solution could be found. The IASB and other interested parties have acknowledged this issue and the IASB is trying to find a solution. Volatility in net income could seriously harm the stock price of insurers and could damage policyholders' confidence in their insurers.

Similarly, the proposals for transition requirements would require insurers not to recognise any profit on their existing business at the date of transition.

This means that the performance of insurers would be extremely low for a long period, as it would only be generated by new business. Moreover, the future profit generated by existing business would flow directly to shareholders' equity and would never pass through the net income of the company.

Analysts and auditors also expressed concern over this, and the problem was acknowledged by the IASB. The insurance industry has made proposals for a more acceptable transition requirement, which the IASB has committed to consider.

Finally, it is essential that there is a full field testing exercise before the standard is finalised. The building-block approach (ie, the calculation of the insurance liabilities as the sum of the best estimate, the risk margin and the residual margin, taking into account the effect of the time value of money) of the new standard is a tremendous change from current reporting rules.

Companies therefore need to ensure that the model proposed by the IASB will deliver results that make sense and that are coherent over several consecutive reporting periods for both the balance sheet and the profit and loss account. In addition, the new standard will require significant changes to IT systems and companies will need to test their updated systems to ensure they can produce the required information.

Accounting for financial instruments

The IASB has also undertaken to replace IAS 39 (now IFRS 9), which determines how to account for financial instruments. As insurers are some of the largest institutional investors and because financial instruments account for the vast majority of the asset side of their balance sheets, this project is of the utmost importance to the insurance industry.

In 2009 the IASB decided to split the revision into three phases. One — the classification of measurement of assets and of liabilities — was completed that year. The two remaining phases relate to impairment (when to recognise a loss of value on instruments not fair-valued) and hedge accounting.

Complicated impairment model

The CEA responded in June 2010 to the IASB's exposure draft on impairment, welcoming the move towards an expected loss model but insisting that the model was overly complicated and tailored to banking books, not to the type of instruments insurers traditionally hold.

In December 2010 the IASB issued a supplementary consultation document. The key points in the CEA response were to welcome the simplification introduced in the way impairment is computed but to re-emphasise that the other changes were still very much focused on the banking book, asking the IASB to develop a principle-based standard applicable to all financial instruments rather than focusing on bank assets.

Hedge accounting welcomed

In March 2011 the CEA commented on the proposals for hedge accounting that were issued in December 2010. Under certain circumstances, hedge accounting permits insurers to present the result of their hedging strategies in their financial statements on a net basis. Only speculation or inefficiencies would be shown in the income statement.

Insurers are very supportive of the IASB's move to a more principle-based standard and to a much simpler standard than the current requirements. Indeed, insurers do not currently apply hedge accounting very often because the rules are very stringent and require constant monitoring.

The CEA also welcomed the fact that more instruments will be eligible as either hedging instruments or hedged items. However, the new proposals from the IASB still need to be improved, as risks such as credit or inflation will not be eligible for hedge accounting. This is important, as insurers often protect themselves against these risks.

Pensions

Same risks, same rules, same capital

Europe's national pension systems are under increasing pressure due to ageing populations caused by the combination of increased longevity and declining birth rates. Many EU member states have been reforming their pension systems to varying degrees to face this challenge, but the economic crisis has made the situation more difficult and the need for reforms more pressing.

Europe's future growth, competitiveness and standards of living depend to a great extent on its ability to build up effective, affordable and sustainable pension systems, as pensions represents a substantial element of public finances in all member states.

A choice of design

Against this background, the European Commission launched a Green Paper, "Towards adequate, safe and European pension systems", in July 2010. In its November response to the Green Paper, the CEA welcomed the EC's suggestion that there should be no "one-size-fits-all" design for pension reforms and that member states should also be responsible for the design of their system.

The CEA urged the EC to tackle the current patchwork of regulation applicable to occupational pension providers in the EU. Specifically, the CEA stressed that any regulation on occupational pensions should take into account the concerns of both pension providers and future pensioners. From a consumer perspective, maximum security and adequate transparency regarding old-age income should be the key priority.

The principle of "same risks, same rules, same capital" should be applied to all regulatory frameworks applicable to life insurers, institutions for occupational retirement provision (IORPs) and mutual funds offering guaranteed benefits. All pension providers are in competition to provide consumers with pension solutions and therefore it is important to apply similar rules to products with similar risks.

Such a level regulatory playing field could cease to exist. While the new Solvency II regulatory regime for the insurance industry (see p10) applies risk-based valuation and regulatory capital requirements, the IORP Directive follows a

CEA welcomes European Parliament report

The CEA has welcomed the European Parliament's report on the European Commission's Green Paper that was adopted in February 2011. The report highlights that, following the economic crisis, the fragility of certain pension funds has been demonstrated and that risk mitigation and shock absorption should be included in the design of pension funds.

In line with the CEA position, the report recognises the need to create a level regulatory playing field between financial service providers and calls for the application of a "same risks, same rules, same capital" principle, while taking into account the characteristics of the different pension schemes.

The report supports the creation of a true internal market for occupational pension provision. It also acknowledges the lack of a consistent solvency regime for providers of occupational pension benefits and notes that solid prudential rules — with no exception for institutions for occupational retirement provision (IORPs) — are needed to increase confidence and trust in financial markets. Finally, the report calls on the EC "to launch an impact study on the application of a Solvency II-type solvency regime to IORPs as soon as possible".

non-risk-based approach. As a result, employees affiliated to a pension scheme provided by a pension fund potentially face higher risks than those whose employers opt for group insurance.

Applying Solvency II-type principles to IORPs, together with adequate transparency requirements that result in a clear and early overview of expected pension entitlements, would increase consumer confidence, as consumers are often not aware of the risks associated with certain products. It would also strengthen the single market for pensions, address regulatory gaps and avoid regulatory arbitrage.

The CEA's call for a level playing field between pension providers was heard by the European Parliament and reflected in its report on the Pensions Green Paper (see box).

The summary of the responses to the EC consultation on the Pensions Green Paper also demonstrated that there is broad support for a review of the IORP Directive. It showed that employees, pensioners and insurance companies all see the need to review EU legislation for funded pension schemes and products to ensure consistency in regulation and supervision. Employers and pension funds, however, did not agree with this view.

Ambitious approach

In April 2011 the EC sent a call for advice to the European Insurance and Occupational Pensions Authority (EIOPA) on a review of the IORP Directive.

An important objective of the review is to facilitate cross-border activity in occupational pensions by removing legal, regulatory and administrative impediments to the creation of cross-border pension schemes. This requires a certain level of harmonisation of prudential regulation across Europe. Ultimately, the review of the IORP Directive should lead to IORPs being subject to a risk-based supervisory and regulatory regime.

The CEA welcomes the ambitious and comprehensive approach taken by the EC in its call for advice and the clear link made between the review of the IORP Directive and the Solvency II Framework Directive.

Indeed, the CEA shares the EC's view that the Solvency II regime is sufficiently flexible to respond to the specific characteristics of pension funds, provided a satisfactory Solvency II solution is found to concerns about long-term guarantees (see p10).

The CEA would, in principle, prefer an approach under which all insurance products are covered by the Solvency II framework, while products provided by IORPs would be subject to the reviewed IORP Directive, which would incorporate many of the Solvency II principles and include risk-mitigating security mechanisms specific to pension funds. It is important that these mechanisms are evaluated in a quantitative rather than a qualititative way and that the principle of substance over form be applied.

A review of the IORP Directive along those lines would create a level playing field between IORPs and insurers and adequately protect consumers' interests. The enhancement of the requirements placed on IORPs to be transparent to both supervisors and consumers would also be an important improvement.

As a result of the different timing for the introduction of the Solvency II Framework Directive and the reviewed IORP Directive, an unlevel playing field between insurers and pension funds could arise. It is therefore of the utmost importance to also design appropriate transitional measures to bridge this gap.

The EC is expected to publish a White Paper on pensions in the autumn of 2011. EIOPA's advice to the EC on the review of the IORP Directive is due by December 2011, with the Commission's proposals for the review expected in 2012.

Systemic risk and stability

Treatment of insurers must reflect their business model

Post-crisis, the mitigation of potential risks to the financial system is high on the agenda of regulators across the world. This focus is driven by political guidance from the G-20, which has asked the Financial Stability Board (FSB) to coordinate the work of the sectoral standard-setting bodies including the International Association of Insurance Supervisors (IAIS) and national financial authorities to identify global systemically important financial institutions (G-SIFIs).

Europe's insurers recognise the need to close any gaps in financial services regulation. The CEA has therefore engaged in the systemic risk debate, contributing to the discussion of a systemic risk framework and its suitability for the insurance sector through the work of the IAIS.

The CEA has a number of significant concerns about the approach to SIFIs currently envisaged at international level. An overarching concern for European insurers is that, increasingly, rules are being designed to address risks arising in the banking sector and are then proposed to be applied to the insurance sector, without adaptation, even though the business models, underlying risks and existing regulation are very different. This difference is particularly clear in the "too big to fail" debate, since unlike in banking, the winding-up of insurance companies can be done in a slow and orderly manner.

Here it should be kept in mind that the financial crisis saw no systemic risk stemming from the insurance sector. Far from being a source of systemic risk, the insurance sector played a risk-absorbing role as a stable long-term investor and a provider of liquidity. Insurance remained stable and with sufficient capacity due to its business model of funding primarily through premiums paid upfront and liabilities triggered by pre-defined loss events.

Discussions on derivatives

In September 2010 the European Commission presented a legislative proposal, the European Market Infrastructure Regulation, aimed at increasing transparency and stability in the market for derivatives that are not traded on a stock exchange, ie, over-the-counter (OTC) derivatives. The two main features of the proposal are the creation of a register of all transactions and a clearing house to reduce counterparty risk.

In its December position paper, the CEA welcomed the objective of the proposals and supported insurers' inclusion within their scope, but raised concerns that the proposals do not distinguish long-term investors, such as insurers, from others, such as speculators. In particular, the requirement to transfer margin in the form of cash only to the clearing house would force insurers to divest a significant part of their portfolio. This would significantly lower their investment return, with a resulting impact for policyholders on products such as pensions. Another issue is the suggestion that pension funds could be exempt from the future legislation. European insurers instead support adaptations to collateral requirements that take into account the long-term nature and low risk profile of institutional investment business. This would prevent insurers offering similar products being put at a significant competitive disadvantage.

In May 2011, during discussion of the proposed legislation in the European Parliament and Council, the CEA shared its concerns with some MEPs and member states. The Hungarian EU Presidency aims to conclude the project by the end of its Presidency.

Bail-ins and cocos

Work is being carried out to design mechanisms to write down the claims of unsecured creditors of a failing institution and to convert debt claims into equity in certain circumstances. The Basel Committee on Banking Supervision is developing capital instruments that absorb losses at the point of non-viability (contingent convertible bonds or "cocos") and the FSB is working on bail-in bonds.

Cocos convert into equity if a certain capital trigger, defined in the instrument itself, is breached. Bail-in bonds are generally seen as being part of resolution mechanisms designed specifically for "too big to fail" institutions. With bail-in bonds, the conversion or write-down is imposed by a supervisory authority as part of the resolution process. As institutional investors, European insurers have expressed little appetite for such products. They carry the risk of suffering losses if the instruments are turned into equity, but do not grant the holder a share of a company's profit if it performs well. In addition, the uncertainty embedded in the bail-in bonds (the trigger is at the discretion of the supervisor) creates problems evaluating the instrument.

Core insurance activities are not a source of systemic risk. Only certain non-core activities carried out by insurers, namely the use of derivatives for speculative purposes and the mis-management of any short-term funding, could — under certain conditions — be a source of risk. This is where any supervisory attention related to systemic risk should be focused, if required.

However, the CEA believes that the high regulatory standards of the EU's new Solvency II regulatory regime (see p10) already create a risk-based capital approach that enables supervisors to appropriately identify and treat potential risks from non-core activities. Solvency II introduces a ladder of potential regulatory interventions starting at an upper threshold (the solvency capital requirement) which, if breached, requires companies to submit a plan for prompt corrective action and ending at a lower threshold at which the regulator steps in (the minimum capital requirement). The second and third pillars of Solvency II have also been designed to contribute to the management of risks. Any additional regulatory requirements placed on European insurers as a result of the systemic risk debate are therefore unnecessary and prejudicial for the industry.

On the issue of systemic risk more generally, the CEA strongly supports the recent creation in Europe of the European Systemic Risk Board (ESRB), which will monitor macro-economic developments and issue warnings and recommendations when necessary. It believes the ESRB is an appropriate complement to Solvency II, the micro-level framework.

Inappropriate criteria

The CEA considers the criteria envisaged by the FSB for identifying potential SIFIs not to be appropriate when applied to core insurance activities. Rather than a source of risk, the large size of a company is generally a stabilising factor in the insurance sector. Substitutability and interconnectedness are equally inappropriate criteria, since substitutability between insurers is high and their interconnectedness is low. The CEA expressed these views in letters to the G-20 leaders in advance of their June and November 2010 meetings, and in a report published in June 2010 outlining the differences between insurance and banking.

The CEA has also commented on the criteria for identifying SIFIs being developed by the Financial Stability Oversight Council in the US (see p22).

Global standard-setting

Raising the bar for insurance standards

Both 2010 and 2011 are important years for the standard-setting activities of the International Association of Insurance Supervisors (IAIS) and the CEA has been commenting on its work.

In 2011 the IAIS will approve a completely revised set of its insurance core principles (ICPs). For the first time, all ICPs will apply to supervision not only at the level of each insurance entity but also at group level.

In 2010 the IAIS also started to develop a common framework for the supervision of internationally active insurance groups, the so-called ComFrame. This framework will only be applicable to the largest global insurance groups. In spite of its more limited scope of application, the CEA believes that the ComFrame represents an important opportunity for the IAIS to lift international insurance supervision standards to a higher level and encourage the convergence of supervisory practices around the world.

Revising core principles

Over the last year, the CEA has provided comments to the IAIS on the draft requirements for a significant number of ICPs: corporate governance, risk management and internal control, reinsurance and other forms of risk transfer, anti-money laundering and combatting the financing of terrorism, information exchange, supervisory cooperation and coordination, group-wide supervision and macro-prudential supervision.

The CEA welcomes the fact that the IAIS ICP framework is moving in the same direction as the EU's new Solvency II regulatory framework (see p10) in that it requires supervisory regimes around the world to establish risk-based solvency requirements that reflect the risks on both the asset and the liability sides of the balance sheet of an insurer.

Furthermore, the recognition that companies' own internal models may be used to calculate regulatory capital requirements — subject to supervisory approval — and the introduction of own risk and solvency assessment (ORSA) requirements are also welcome developments. Under the ORSA process, undertakings conduct a forward-looking self-assessment of their specific risks and corresponding capital requirements.

What are ICPs?

The revised insurance core principles (ICP) framework of the International Association of Insurance Supervisors is a set of 26 internationally agreed principles that outline the key elements that should be present in an insurance supervisory regime. The ICPs deal with all aspects of insurance supervision, such as prudential requirements and conduct of business standards, but also include criteria relating to the powers and responsibilities of the supervisory authorities themselves.

Each ICP is complemented by standards, which set out high-level requirements that are fundamental to the implementation of the respective ICP, and by guidance, which describes in more detail how the ICP or standard can be implemented.

Observance of the ICPs and standards (but not the guidance) is assessed when the International Monetary Fund and the World Bank review a country's compliance with international standards as part of their Financial Services Assessment Programme.

In response to a request from the Financial Stability Board, IAIS members will conduct a self-assessment of their observance of the standards on the "mandate and powers of insurance supervisors" and "group-wide supervision" immediately after the adoption of the revised ICPs in early October 2011. The aggregated results will then be submitted to the FSB in early 2012.

A new framework for groups

The CEA has long advocated the introduction of effective supervision of insurance groups that takes their economic reality into account. It therefore welcomed the decision of the IAIS in January 2010 to start developing the ComFrame in June 2010.

The ComFrame aims to put the ICPs into a more practical, principles-based framework by creating a common language among the supervisors of internationally active insurance groups and by setting out more narrowly defined common requirements for their supervision. Although the ComFrame will only be applicable to the largest insurers that operate on a global basis, many of its requirements will be equally relevant for other insurance groups. The CEA therefore believes that the ComFrame represents a unique opportunity to achieve more consistency in, and better comparability of, insurance group supervision across jurisdictions.

Key aspects in the development of the ComFrame will be: how to define an internationally active group; the identification process; the quantitative and qualitative requirements that such groups will be expected to meet; and the definition of the different but equally important roles of the group-wide and solo-entity supervisors. The IAIS is also considering the inclusion of crisis management and contingency planning measures in the framework.

In order for the ComFrame to be developed within the projected timeframe, the CEA believes that IAIS members should focus on achieving convergence in the key areas of group-wide supervision. The CEA has outlined its preliminary views on this to the IAIS, emphasising the need to look for pragmatic solutions to ensure that all international groups become subject to a sound and comparable level of group supervision, even if certain differences in regulatory approaches remain.

The challenges in developing the ComFrame should not be underestimated. The current approaches to and experience of group-wide supervision across the world differ significantly, resulting in differing expectations and objectives for the ComFrame among IAIS members.

Indeed, it is important to bear in mind that the ComFrame has not been initiated to address systemic risks in insurance. Group-wide supervision is a natural regulatory development in an environment in which insurance groups operate across borders while supervision remains at national level.

Group-wide supervision can nevertheless make a valuable contribution to strengthening the resilience of the financial system. For example, comprehensive risk-based supervision of insurance groups that covers their entire balance sheet, as well as relevant off-balance sheet items and unregulated entities, should ensure that all material risks are adequately captured within micro-prudential oversight.

A first "concept paper" outlining the ComFrame will be released to IAIS members and observers for consultation in mid-2011. The full framework should be ready for an impact assessment and final calibration by June 2013.

International issues

A current strong focus on the Americas

The EU-US relationship is more influential than ever in financial services. Its importance will only increase since reforms called for by the G-20 are moving towards implementation, work is reaching a crucial stage on the common framework for the supervision of internationally active groups (see p20) being developed by the International Association of Insurance Supervisors (IAIS) and discussions are heating up over the transitional rules for the regulatory regimes of non-EU countries to be recognised as equivalent to the EU's Solvency II (see p10).

The CEA has continued to closely track EU-US dialogues at all levels, from the political discussions at the Transatlantic Economic Council and regulatory dialogues to informal contacts between the administrations. There has been a marked increase in the frequency of the conversations, especially at the more technical level. The CEA has taken every opportunity to ensure that insurance remains high on the agenda. Of particular interest are the frequent discussions of the National Association of Insurance Commissioners with the European Insurance and Occupational Pensions Authority and the European Commission, at which issues such as differences in the approach to solvency capital requirements and the supervision of insurance groups are discussed.

To discuss the convergence of global solvency standards, on 3 March 2011 the CEA co-organised the 2nd Transatlantic Insurance Symposium in Washington DC with the American Council of Life Insurers and the US Chamber of Commerce. It was attended by over 130 delegates.

A welcome federal office

The US Dodd-Frank Act of July 2010, creates a Federal Office of Insurance (FIO) within the US Treasury. Although regulation of insurance will remain the responsibility of state commissioners,

Brazilian reinsurance restrictions

The CEA and other international insurance associations have been vocal in their opposition to two new Brazilian reinsurance regulations that will have a detrimental impact on the Brazilian market.

The resolutions were published in December 2010 without prior consultation and came into effect in March 2011. One requires the placement of at least 40% of each reinsurance cession with local Brazilian reinsurers, who previously only had the right of first refusal. The other prohibits local (re)insurers from ceding more than 20% of each placement to members of the same group outside Brazil. This rule does not apply to guarantee, export credit, rural credit, internal credit and nuclear risk business and will be applied to existing policies at renewal or as of 31 March 2012, whichever is soonest.

The CEA has repeatedly brought European insurers' concerns over the resolutions to the attention of the Brazilian government, the European Commission and other interested parties and continues to seek their revocation. In both January and April 2011 the CEA and a coalition of 17 insurance associations wrote to the Brazilian government, pointing out that the regulations depart from international regulatory standards and will severely restrict the ability of international (re)insurers to provide coverage for Brazilian risks, ultimately having a negative effect on Brazil's consumers and economy. The changes could affect (re)insurance coverage for big events in Brazil, such as the football World Cup in 2014 and the Olympic Games in 2016, as well as planned offshore oil production projects.

Argentina limits cross-border reinsurance

On 11 February 2011, with no prior consultation, Argentina enacted a reinsurance regulation to come into force on 1 September 2011 effectively banning cross-border reinsurance. Following strong opposition from the CEA and others, on 19 May a further resolution slightly relaxed the restriction.

Under the resolutions, cross-border reinsurance is only allowed for risks of over $50bn and retrocessions or with approval granted by policy on a case-by-case basis. Risks of under $50bn must be placed with fully capitalised Argentinian reinsurers. These can include branches of foreign reinsurers, which are expected to be required to maintain capital equal to the greater of ARS 20m ($5m) or 16% of net earned premiums. These local reinsurers must retain a certain proportion of their risks and capital in Argentina and cannot transfer more than 40% of the premiums per transaction to companies in the same group.

The CEA will continue to express concern over the new resolution and to urge the European Commission to continue raising the industry's concerns during the EU-Mercosur Free Trade Agreement negotiations and in discussions with Argentina.

the CEA welcomes the ability of the FIO to represent the US with one voice in international fora, develop federal policy on prudential aspects of international insurance matters and assist the US Treasury Secretary in negotiating agreements with foreign governments, entities or authorities on prudential insurance measures. Once agreements are in place it can also pre-empt state laws that are inconsistent with the agreement and treat non-US insurers less favourably.

With the new FIO director only just in place, much remains to be done to shape the FIO's role. Of particular interest will be the report due by the end of January 2012 on modernising the US system of regulation. The director of the FIO is empowered "to make any legislative or regulatory recommendations he determines appropriate to give effect to the findings of the report".

The Dodd-Frank Act also created the US Financial Stability Oversight Council (FSOC), which has the task of recommending whether certain non-bank financial holding companies, which would include US subsidiaries of European insurers, should be considered systemically important (see p18) and hence supervised by the US Federal Reserve and subject to enhanced prudential standards.

The CEA has expressed its concerns over this development in its responses to the FSOC's consultations on the criteria to be used to identify such companies, emphasising that core insurance business does not pose a risk to the financial system and that any additional supervision/ regulation should therefore focus on risk activity not on individual institutions. It has also called for recognition of the strong supervision of consolidated groups under the EU's new Solvency II regime, which would cover US subsidiaries.

The CEA has also joined those calling for the FSOC's rulemaking process to be delayed until it has the necessary insurance expertise in place and until the international debate on the identification of systemic risk is concluded.The FSOC is due to publish its criteria for identification at the end of June 2011, while the IAIS is only planning on formally consulting on its methodology towards the end of 2011.

Taxation

Concerning issues on both sides of the Atlantic

The CEA has been involved in a number of taxation issues with significant implications for the insurance industry over the last year. The European Commission is looking into a tax on the financial sector to pay for past and future economic crises (see box) and the CEA continues to have concerns over the EC's draft Directive on Savings Taxation and the draft Directive and Regulation on VAT on insurance and financial services.

From the US, the forthcoming Foreign Account Tax Compliance Act could impose a significant compliance burden on EU insurers, while the re-emergence of the affiliated reinsurance tax proposal is bad news for European (re)insurers with US operations.

No agreement on savings tax

The CEA has been vocal in its opposition to a proposal by the Commission in its draft Directive on Savings Taxation, which governs the taxation of cross-border interest payments. The CEA opposes the proposal to extend its scope to include the benefits from certain life insurance contracts. This is on the grounds of the disproportionate administrative costs to insurers given the low level of cross-border sales, the exchange of information obligations for life insurance products that are already in place, and the differences in national tax regimes for life insurance.

While the EU Council has not yet been able to reach an agreement on the draft Directive as a whole, the latest Council compromise text, which dates back to November 2009, included life insurance contracts within the scope of the Directive. Since then, political negotiations on the Directive as a whole have been stalled, notably due to opposition from Luxembourg and Austria to agree to a text without having ensured a similar agreement with non-EU countries such as Switzerland. The Hungarian EU Presidency attempted to move negotiations forward, organising several high-level working party meetings. Political opposition remains and the dossier is likely to be passed on to the Polish Presidency. Unfortunately, it is likely that life insurance will remain within the scope .

VAT exemptions under scrutiny

Under the EU VAT Directive, insurance services are generally exempt from value added tax (VAT) but this exemption dates from 1977 and the legislation has not kept abreast of subsequent developments.

The EC therefore launched a proposal in 2007 comprising both an amendment to the existing Directive to clarify certain legal issues and to tackle the question of non-recoverable VAT and a new Regulation that clarifies the definition of exempt services. The Commission's proposal comprises three types of measures: the redefinition of the scope of the exempt services; the introduction of the possibility for the banking and insurance industries to opt to tax their services; and the introduction of an industry-specific exemption from VAT for cost-sharing arrangements. The CEA's main concern is to ensure that the exemption covers the key functions of an insurance contract.

The Belgian EU Presidency of the second half of 2010 and the Hungarian Presidency of early 2011 focused on the scope of exempt services. The CEA sent letters to the Council in January, February and April 2011 arguing that exemptions should better reflect the complexity of insurance business and should ensure that there is a level playing field between the banking and insurance sectors. The CEA is in favour of: a broad definition of insurance based solely on risk, the explicit exemption of the transfer and management of (re)insurance contracts, a broad definition of outsourcing exemption comprising specific and essential

parts of insurance (eg, claims-handling), as well as a broad definition of intermediation based on the nature of the service and not the means by which it is provided. Further compromise texts are expected, on which the CEA will comment.

Consolidated tax returns

The CEA will also be closely following the proposal published by the Commission in March 2011 for a common consolidated corporate tax base (CCCTB) for businesses operating in the EU. Under this proposal, companies and groups could opt to file their returns under the single CCCTB system, thus consolidating all their profits and losses across the EU. Member states would retain their full sovereign rights to set their own corporate tax rate. The CEA is currently preparing its position on the proposal.

Opposing FATCA's burden

On the other side of the Atlantic, the US Foreign Account Tax Compliance Act (FATCA), which was passed by Congress in March 2010, is intended to ensure that the US tax authorities obtain information on investments by US residents in foreign financial institutions. It is due to come into force on 1 January 2013.

CEA argues against financial services tax on insurers

In Europe, and as a direct response to the economic crisis, the European Commission has begun to consider ways to ensure that the financial services industry contributes to the cost of past and future crises. With this aim — and in the absence of a coordinated effort at global level — in February 2011 the Commission initiated a public consultation on the potential design and scope of a tax on the financial sector.

In its April response to the consultation, the CEA argued that subjecting the insurance sector to a new tax is not the right way forward. The insurance sector was neither the source of the crisis nor the main recipient of subsequent government funds.

The core business of insurers — risk-taking and asset management — does not cause problems such as those that materialised during the financial crisis, but rather contributes to stabilising markets. According to OECD estimates, G-20 governments and central banks provided more than $11 000bn of direct and indirect support to the financial services sector to stabilise the financial system, of which less than $10bn went to the insurance sector. Any financial sector taxation initiative should therefore appropriately distinguish between financial institutions and activities, their role in the economy and in the crisis and the risk they represent to financial stability.

The CEA believes that efficient supervision and appropriate regulation are the best way to ensure financial stability. For the insurance sector, this will already be strengthened by the new Solvency II regulations due to come into force at the end of 2012 (see p10). Furthermore, insurance companies are not under-taxed compared to other sectors. Insurance companies are already subject to national insurance premium taxes, whereas a comparable tax does not exist in the banking sector. Insurers are also currently subject to non-deductible VAT on their activities.

The European Commission is conducting an impact assessment and will present policy options in a Communication in July 2011.

The US Treasury/Internal Revenue Service (IRS) are required to define the scope of the legislation in the implementing guidance. The CEA wishes to ensure that FATCA is designed in a way that meets the legitimate concerns of the US regulator without imposing an undue burden on non-US insurers. It has opposed the application of FATCA in the shape proposed by the IRS on the grounds that the reporting requirements are overly burdensome and conflict with EU data protection laws. European life insurance companies present a low risk of US tax evasion because of the nature of life products and the small proportion of US residents with European life policies.

More specifically, the CEA has argued for the exclusion of existing policies from the scope of FATCA because of data protection issues and the lack of availability of information, and for the exclusion of insurance contracts that are highly unlikely to be used for tax evasion (eg, term life policies, health insurance, low value policies, etc.). The CEA has also argued that the requirement to comply with the regulation should be at individual company level to avoid classification and compliance problems at group level. It further believes that the agreement between a foreign financial institution and the IRS/US Treasury should contain a "best-efforts clause", which would ensure every effort to perform the obligations but would not imply any specific goals.

The Commission and the Hungarian EU Presidency have acknowledged the insurance industry's concerns over FATCA and the CEA welcomes their efforts to engage with the US tax authorities on the issue. The CEA therefore supported the joint letter sent by the Commission and Council to the IRS in April 2011 pointing out the severe financial burden, legal complications and potential penalties that FATCA would impose on Europe's financial services industry. As strongly advocated by the CEA, the letter raised questions of conflict with EU data protection law, worldwide affiliated groups and the availability of information.

However, the CEA has opposed the EU's proposal to use its Savings Taxation Directive to achieve FATCA's objectives, underlining to the EC and the Hungarian Presidency that the Directive will not solve the data protection or worldwide affiliated group issues.

Affiliated reinsurance tax reappears

Another US tax issue of concern to Europe's insurers is the affiliated reinsurance tax proposal that was revived again in President Obama's 2012 budget proposal of February 2011. Its objective is similar to legislation introduced by Representative Richard Neal to the US House of Representatives in 2009 and a proposal in the administration's 2011 budget, namely to tax reinsurance premiums ceded by US subsidiaries of non-US (re)insurers to international affiliates.

If enacted, the proposal would create unequal treatment for EU insurers that internally reinsure substantial parts of their US business to EU entities, which are already paying substantial tax in their home states and cannot be considered as low tax countries. The CEA believes that substantial unintended and negative consequences would result as the increased costs could lead to higher premiums and reduced insurance capacity in the US. The proposal would also violate longstanding US tax and trade policies.

In July 2010 the CEA submitted written comments to the House of Representatives Subcommittee considering the Neal Bill. The Bill has since not progressed further. The CEA also wrote to both the House of Representatives and the Senate in March to oppose the inclusion of the US affiliated tax proposal in the Budget. In addition, the CEA highlighted its concerns about the revival of the proposal to the European Commission, which has publicly spoken out against the proposal. It remains to be seen whether the reinsurance tax could become law in 2011, either as a revenue-raising amendment to a tax or spending bill or as part of corporate tax reform.

Financial education

Insurance industry initiatives raise financial awareness

Policymakers throughout Europe and beyond recognise the vital importance of improving the public's level of financial literacy. Consumers need easy access to relevant information and guidance, as well as a grounding in financial matters that gives them the ability and the confidence to make the choices that best suit their circumstances.

The European insurance industry is committed to playing its part in raising financial awareness. As well as the many initiatives by insurance companies to improve financial knowledge, the national insurance associations undertake a wide variety of financial education activities. In 2011 the CEA published a booklet showcasing just some of the many initiatives by its member associations, along with a number of recommendations for policymakers.

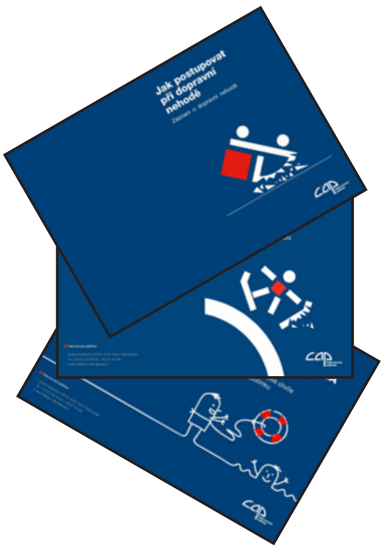
A poster for the Turkish association's play for children

Insurance associations have an important role to play in financial education because they can provide neutral information on insurance products; raise awareness of new or emerging risks and the possibility of being covered against them; and carry out research and surveys to monitor consumers' needs and understanding.

Associations use a wide variety of means to increase consumers' financial knowledge and risk awareness and to promote retirement saving. These include brochures and website material, consumer advice services, and public events and media campaigns. The CEA booklet, "Financial education and awareness", highlights everything from web-based pension calculators in Denmark, Sweden and the Netherlands, through Czech booklets explaining how to have a safe holiday, to a series of Hungarian television programmes about insurance.

Key to moving from raising awareness of financial issues to actually changing consumers' behaviour are education initiatives, especially for young people. The Turkish association, for example, has staged a play in 28 cities that teaches children the importance of being insured and the Dutch association's innovative "Geldkoffer" of financial education teaching materials includes a board game about risks.

In Belgium the association has created a website with information specifically for secondary school teachers and pupils and the German association's online consumer information centre includes a wealth of multimedia teaching materials. Details of all these initiatives and many more are set out in the CEA booklet.



The Czech association's information booklets

The CEA's financial education booklet is available to download free of charge at www.cea.eu

Anti-discrimination

ECJ ruling on use of gender in insurance pricing

The CEA has followed closely the action brought by Belgian consumer association Test-Achats before the Belgian Constitutional Court that was referred to the European Court of Justice (ECJ). Test-Achats challenged the legality of the Belgian law transposing Article 5(2) of the EU Gender Directive, which allows member states — as an exception to the prohibition principle set out in Article 5(1) — to permit gender-based differentiation in insurance pricing based on relevant and accurate data.

In an opinion published in September 2010, the Advocate General to the Court recommended that the ECJ declare Article 5(2) invalid, arguing that it infringes the EU principle of equal treatment between men and women. The ECJ then ruled on 1 March that the article should be declared invalid with effect from 21 December 2012. The judges did not follow the Advocate General's reasoning but mainly focused on the structure of the Directive, stating that the derogation granted to member states could not persist indefinitely.

Bad news for consumers

The CEA expressed serious concerns that the effect of the judgment on insurance prices and benefits and on the choice of insurance products for consumers could be significant. In particular, any increase in the cost and decrease in the choice of pension products could reduce levels of retirement saving at a time when state pension schemes are already under financial pressure (see p16). Adapting systems and products to reflect the ruling will also be challenging for the industry —for small and medium-sized insurers in particular — given the short transition period.

The CEA's detailed arguments for the use of gender in insurance pricing and a description of the potential consequences of a ban on the use of gender for consumers were set out in a policy paper it published at the time of the judgment.

Following the ECJ ruling, the CEA began to assess its implications for insurance contracts and activities. The judgment is not precise, so legal clarification is still needed. According to the CEA's initial analysis, which is in line with that of the EC, the ruling only applies to new contracts concluded after 21 December 2012.

The CEA's analysis of the judgment will serve as the basis for its contribution to the EC report on the implementation of the Gender Directive. The report was initially planned for the end of 2010 but is now postponed to the end of 2011 or even to early 2012. The publication of the report will follow an EC Gender Forum meeting in June in which the CEA will participate, and a meeting between EC Vice-President Viviane Reding and insurance industry leaders scheduled for September. The report should clarify the EC's interpretation of the ruling and describe its next steps.

Broader implications

The CEA is concerned that the ECJ judgment could lead to attempts to limit the legitimate use by insurers of other determining rating factors such as age and disability, particularly in view of the proposed Anti-Discrimination Directive (see opposite). Any ban on these factors would endanger the insurance business model as it currently exists and thus have highly detrimental consequences for consumers. The CEA is therefore reinforcing its efforts to explain to policymakers and the public at large how private insurance works to ensure that insurers can continue to assess risks accurately and thus cover as many people as possible in a fair way at a reasonable price.

Anti-discrimination

Explaining the value of risk assessment

The CEA is heavily engaged in promoting a better understanding among policymakers and the general public of how private insurance works. A key focus is to explain how accurate risk assessment can enhance consumer choice and lead to fairer pricing.

As part of its work in this area, the CEA participates in the Dialogue on the use of age and disability in financial services that was set up by the European Commission following its draft Anti-Discrimination Directive of 2008.

The Dialogue was launched to improve understanding of how age and disability factors are relevant to the design and pricing of financial services. It brings together the Commission, the financial services sector and consumer representatives and non-governmental organisations such as AGE Platform Europe and the European Disability Forum.

At the Dialogue meetings, the CEA has explained the fundamental principles of insurance and presented market-led initiatives by niche insurance providers. It has explained the way consumer complaint mechanisms improve both complaints management and the communication between policyholders and insurers and it has outlined the way disputes are settled through ombudsmen.

Few discrimination complaints

The CEA has also voiced concerns about the study of the use of age and disability in financial services that was published by the EC in July 2010. The study aimed to identify and analyse potential discrimination issues, but referred to alleged cases of discrimination without clarifying whether the complaints were justified. The CEA believes that the low number of registered complaints and court cases suggests that the insurance market is functioning well and that insurers endeavour to provide cover to as many people as possible, within the limits of insurability. While in essence the study describes correctly the way the private insurance market functions, its recommendations do not match its findings and are based on assumptions and estimations.

Outside the EC Dialogue, the CEA also engages in informal discussions with AGE Platform Europe to exchange views and information. Possible cooperation in areas such as pensions and financial education have been discussed, as well as joint initiatives at European or national level as part of the European Year of Active Ageing in 2012 and the encouragement of cooperation between the national members of both federations.

Directive debate

Meanwhile, the protracted negotiations over the wording of the EC's draft Anti-Discrimination Directive continue in the European Council. The CEA met the incoming Hungarian EU Presidency at the end of 2010 to raise its concerns. Firstly, it reiterated that there should be no option to allow EU member states to decide whether "differences in treatment" in the provision of financial services are allowed, as this would create legal uncertainty and be an obstacle to cross-border business.

Secondly, the Directive should not allow restrictions on the sources of information used in the risk-assessment process, which would hamper correct risk assessment and pricing. Thirdly, there should be no data publication requirements, which would contravene insurers' intellectual property rights and affect their competitiveness without benefiting consumers.

The Hungarian EU Presidency did not produce any further compromise texts but it is expected to publish a progress report at the end of its term.

Insurance guarantee schemes
Ensuring the workability of any EU proposal

In July 2010 the European Commission published a package of measures to boost consumer protection and confidence in financial services. It included a White Paper proposing that there should be a directive to ensure that all EU member states have an insurance guarantee scheme (IGS) that complies with a set of minimum requirements.

The CEA supports the EC's objective of protecting insurance policyholders and beneficiaries in the unlikely event of an insurer becoming insolvent and being unable to fulfil its contractual commitments.

However, the CEA is convinced that an adequate level of policyholder protection is already ensured through the existing and forthcoming European insurance prudential regulatory frameworks. The Solvency II regulatory regime that will come into force at the end of 2012 (see p10) and the new European Insurance and Occupational Pensions Authority (EIOPA) that was created by the new EU supervisory structure provide a ladder of intervention measures to ensure that consumers are well protected.

Insurers have to match expected future claims (technical provisions) with sufficient and securely invested assets that have similar characteristics to their underlying insurance liabilities (eg, duration, liquidity and currency). In addition, the new Solvency II framework sets two levels of capital requirements for individual insurance undertakings and insurance groups. This is a unique intervention mechanism, which allows the detection of any financial difficulties at an insurer at an early stage.

Legislation likely

In its response to the EC's White Paper on IGS in November 2010, the CEA argued that there is no case for an EU-wide IGS initiative. It believed, and believes, that before any additional protection levels are considered, the new prudential and supervisory rules should first come into force and then be evaluated after a reasonable time period.

Nevertheless, the EC is likely to go ahead with a legislative proposal on IGS. The CEA is therefore now concerned to ensure the workability of any proposal. It calls for a minimum harmonisation of national schemes as last-resort mechanisms. This would accommodate established national systems that are adapted to local market conditions and consumer needs and allow existing efficient systems to continue to operate.

Support for minimum harmonisation

This support for minimum harmonisation is shared by the EC, the European Parliament and EIOPA. Equally, all agree that national IGS should follow the home state approach, in accordance with the EU supervisory framework. IGS based on this approach would cover the policies issued by domestic insurers, including those written cross-border and those sold by their branches in other EU member states.

The European Commission is considering widening the scope of its proposal from just covering consumers to including some small companies. This suggestion is supported by some members of the European Parliament, who voiced their opinion in the European Parliament's own-initiative report on IGS.

The CEA is in favour of identifying eligible claimants as consumers, meaning any person acting outside his trade, business, craft or profession. Since consumer protection is the European Commission's primary aim, the claimant group should not be extended to micro and small companies. In contrast to consumers, such undertakings are able to assess their chosen insurers' soundness or seek professional advice on it. Furthermore, any extension of IGS to include

undertakings would lead to legal uncertainty, as these are defined differently in different EU member states. In addition, such an extension would result in an administrative and financial burden, since an annual assessment of the eligibility of companies would be necessary.

In the discussion of the European Parliament's own-initiative report, an extension of the scope to losses from insurers' and/or intermediaries' mis-selling or fraudulent activities was proposed. The CEA strongly opposes this idea, since insurers are fully responsible for the behaviour of their employees and intermediaries hold professional indemnity insurance.

Furthermore, such an extension of the scope risks creating moral hazard, as supervisory authorities could become less vigilant in monitoring insurers' and intermediaries' activities and abstain from using supervisory tools to enforce business conduct rules. Besides, fraudulent behaviour should be treated as a criminal and not a prudential matter.

Focus on life

The CEA argues that any EU initiative on IGS should focus only on life insurance policies. Life insurance policies involve large amounts and long-term commitments, often with a retirement perspective. In contrast, non-life insurance policies are often short duration contracts. Should a non-life insurer become insolvent, the consumer can easily switch from the insolvent insurer to another since, in contrast to life insurance, there is no deterioration of the insured risk over time.

The EC, EIOPA and some MEPs, in contrast, want national IGS to cover all life and non-life insurance products except motor third-party liability insurance, recognising that the latter covers the victims of accidents rather than consumers.

Should the EC, however, confirm its intention to include non-life insurance in the scope of its Directive, the CEA believes that it should explicitly allow member states to maintain well-functioning existing IGS covering non-life insurance, without interfering with the way they were designed. Existing IGS have been established and developed with local market and economic environments in mind, with the aim of best addressing local consumer protection needs. Any interference with their management, functioning and organisation would only prevent those schemes from performing effectively and achieving their objectives.

Need for national choice

The CEA strongly believes that both the funding and the design of national IGS should be left to member states, in consultation with local stakeholders. As insurance markets differ significantly across Europe in terms of size, concentration and business written, it is impossible to decide at European level whether an IGS should be funded *ex-ante* (before the event) or *ex-post* (after the event).

Moreover, the funding method and amount depend very much on whether national authorities give preference to compensation or portfolio transfer. Thus, it is preferable that the member states choose the funding that will guarantee long-term consumer protection at all times.

The setting-up of IGS entails specific challenges for smaller, concentrated markets. In those markets, should financially sound companies be required to fill IGS funding gaps in the case of a large insurance company's collapse, inappropriate funding mechanisms could create interconnectedness between insurance companies and produce an environment in which systemic risks could develop.

The financial stability of a national IGS is paramount for effective consumer protection. Depending on the scope of a future IGS suggested by the Commission, caps and compensation limits will therefore need to be considered.

The EC is expected to present its legislative proposal before the end of 2012.

Consumer information

Promoting user-friendly disclosure

Consumers can find it difficult to understand the financial products they are purchasing. The economic crisis made this clearer than ever. And yet experience has also shown that too much and too technical information can confuse consumers and can even discourage them from reading pre-contractual details. This can mean that consumers are not in a position to compare the different financial products that are on offer. It can also mean that they fail to understand the key features of a product, sometimes leading to misplaced expectations about a product's performance or guarantees.

The CEA decided to tackle this issue and took up the challenge of developing a user-friendly format in which to disclose information that would make it easier for consumers to make decisions.

To ensure that the format provides the information that buyers deem essential in order to understand and compare products, the CEA worked from the consumer's perspective to produce a key information checklist (KIC) for unit-linked life insurance (see opposite). This consists of a short list of simple, clear information headings on the key characteristics of a product, addressing consumers' main demands and expectations. It contains what the CEA considers to be the minimum information that should be provided for these products.

The information categories in the KIC are presented in a preferred order and are standardised. They are general and not personalised to the particular circumstances of an individual consumer. The way the KIC is designed therefore makes it easier for consumers to compare different unit-linked life insurance products, while still highlighting the differing features and objectives of unit-linked life insurance compared to other financial products. Moreover, using the KIC will help consumers to compare products across Europe and will allow them to take advantage of opportunities to buy products from other EU markets.

Comprehensive but flexible

Since it is a checklist, the CEA KIC is sufficiently flexible to make it possible to adapt the information contents to local consumer needs, expectations, preferences and levels of financial understanding, or to local laws and product features, as well as to any changes in these areas. The CEA recognises that different markets are at different stages of development in terms of such disclosure formats and that what is viewed as essential information for consumers in one market may not be in another. The checklist format also avoids interference with any existing national self- or co-regulatory models that have proven to work effectively. For this reason, flexibility is allowed in the content of each of the categories of the KIC, while at the same time maintaining a user-friendly format and a limited size.

It is important to stress that the KIC should not be merely another document added to existing client documents. It should form part of the pre-contractual information package rather than be an addition to it, in order to ensure that there is no duplication of disclosure requirements. It is crucial, therefore, that existing information requirements are scrutinised and updated when the KIC is introduced.

The CEA KIC formed the basis for the CEA's January 2011 contribution to the European Commission's consultation on packaged retail investment products (PRIPs), which the Commission will follow with a proposal for a regulation on disclosures for PRIPs by mid-2011.

Key Information Checklist (KIC) for unit-linked insurance

Information categories	Possible contents
Title	Key Information Document — unit-linked life insurance
Explanatory statement	*"This document provides you with non-personalised key information about this product. It is not marketing material. The information is required by law to help you understand the nature and the risks of this product. You are advised to read this document and any complementary information to which it refers so you can be in a better position to make an informed decision about whether to purchase this product."*
Name of the product	—
Name of the insurance undertaking	This may also include the company head office address and legal status
Type of product	Summary of the product
Insurance benefits [or cover]	• Risk coverage description (death, life, disability, sickness, etc.) • Pay-out method (lump sum and annuities)
Objectives and investment policy	• General description of the investment objectives • Risk coverage (if any) without any further description • Hyperlinks/references to underlying funds KIDs/ pre-contractual information
Risk and reward profile	• Narrative explanation describing risks, risk mitigation elements, guarantees not reflected in the SRRI (synthetic risk and reward indicator) (eg maturity guarantee) and the existence of Solvency II requirements • No SRRI at product level (SRRI methodology at underlying funds' level to be revised)
Charges	• Entry fees • Exit fees • Recurring charges • In % (because standardised format) or euros where necessary (fixed amount); indication that other charges exist at underlying funds' level or display all underlying funds' costs
Premium	• Minimum entry or investment requirement • Premium payment modalities and flexibility (single or periodic payment)
Duration of the contract	• Minimum or specific period or "no specific period" • Existence of a cancellation right
Consequences of early termination	• Deductions • General warning (in case the consequences of early termination are too long to be detailed in the KIC). The general warning can consist of a reference to the general policy conditions for further detailed information
Practical information	Examples: • Mediation mechanisms • Information that insurer will communicate to policyholder regularly • Further information on underlying funds on request from insurer or at sale point • Insurance guarantee scheme coverage or not • Hyperlinks/references to underlying funds KIDs/ pre-contractual information
Authorisation details	[name of insurance undertaking] is authorised by [name of EU member state] on [date] and is supervised by [identity of competent authority] to provide products
Date of publication	The information contained within the KID is accurate as at [day/month/year]

Distribution

Protecting consumers while maintaining diversity

European insurers sell products to customers in different ways. The distribution structures in EU markets are diverse, complex and constantly adapting to consumer needs and demands. This diversity of channels benefits consumers, whose cultures, needs and preferences are the drivers of the differences. The diversity also increases consumers' choice of products and stimulates competition between different product providers and distributors.

In July 2010 the CEA published a briefing note on insurance distribution, highlighting the wide variety in insurance distribution markets and outlining the important points to consider when regulating insurance distribution. In its paper, the CEA also proposed a series of high-level principles to govern the selling of insurance. These are tailored to the insurance business model and aim to provide a high level of consumer protection.

Review of the IMD

In November 2010 the European Commission published a consultation on the review of the EU Insurance Mediation Directive (IMD), seeking views on its current functioning and suggesting a number of possible changes to the legislation. The Commission aims to achieve effective regulation of insurance distribution by improving the single market for insurance and reinsurance intermediaries. It aims to ensure a level playing field between all parties involved in selling insurance products and to strengthen policyholder protection.

The Commission identified a number of areas where improvements to the legislation may be necessary, including the provision of information to consumers, conflicts of interest and transparency, and professional requirements for distributors of insurance products. The CEA contributed to the Commission's work by addressing each of these issues and putting forward suggestions of ways to ensure a high level of consumer protection.

In December 2010 the Commission held a public hearing on issues relating to the review of the IMD, at which the CEA was represented by two speakers. The CEA stressed the need for a minimum harmonisation directive that allows for national difference, for greater transparency in "general good" rules, for any approach to be proportionate and for the diversity of distribution channels to be recognised.

Diversity in distribution

The CEA has always maintained that any future legislation on insurance mediation must recognise the diversity of insurance distribution markets across the EU, since the differences reflect differing consumer needs and demands, and local market conditions. The CEA is concerned that any attempt to introduce EU-wide, "one-size-fits-all" legislation would not be capable of capturing the differences between the existing national distribution structures. It has long argued that future rules on insurance mediation should follow a minimum harmonisation approach, since this would be flexible enough to address the diversity of products and existing distribution channels, as well as different local consumer needs.

Risk-based and proportionate

The Commission is seeking to harmonise the regulatory landscape to ensure that the same level of consumer protection and a level playing field apply across the whole range of distribution channels. The CEA stresses, however, that the future rules should be proportionate to both the type of distribution channel and the nature of the product, and should recognise the fact that the risks are different between distribution channels. For example, the risks of conflicts of interest

when insurance is sold by intermediaries are very different to those in the direct-selling channel.

High-level principles

The CEA outlined in its response to the Commission consultation that future European legislation on the distribution of insurance should take the form of high-level principles that are flexible enough to accommodate the diversity of existing distribution structures, to adapt to evolving consumer needs and demands, and to avoid having any adverse effects on distribution markets.

To this end, the CEA elaborated on its July briefing note and proposed a set of six high-level principles for selling practices for all insurance contracts and all distribution channels that would ensure a proportionate approach.

To guarantee a level playing field between distribution channels, the CEA holds that these principles should apply to all insurance products and should be adjusted according to the demands and needs of the customer, the level of financial risk to the customer, the complexity of the product, and the distribution channel.

Improving transparency

The Commission is currently considering how to improve transparency for consumers and to avoid situations of conflict of interest in the sale of insurance products.

In its position paper, the CEA identified key ways to address potential conflicts of interest and highlighted the need to adapt future regulation in this area to the particularities of different distribution structures.

The CEA believes that the current IMD provisions provide a good starting point to mitigate conflicts of interest, but also offers some suggestions to the Commission in case it decides to build on these rules in the future. The CEA holds that conflicts of interest can be prevented by making the status and role of the distributor clear to the customer from the outset, so that consumers are always aware of the distributor's exact role in the selling process. This creates a high level of transparency, while at the same time respecting the importance of consumer choice.

A single market

The CEA calls for greater transparency in general good rules, since the lack of information on national general good rules is one of the biggest barriers to cross-border insurance business. The provision of such information would increase legal certainty and transparency for insurance intermediaries and companies operating on a cross-border basis.

The CEA put forward a number of proposals in its response to the Commission consultation as to how improvements can be made to the transparency of general good rules across the EU, including the publication of national rules on a single website, categorised into different areas of law, and the establishment of a single contact point responsible for providing information on general goods rules in each member state.

The CEA believes that high-level principles on knowledge and ability for all insurance intermediaries, adjusted to suit their status and the nature of their activities, would guarantee a uniform approach in raising the level of professionalism and consumer protection. These principles would aim to ensure that intermediaries have the appropriate knowledge and competences to perform their duties adequately; possess appropriate, relevant professional experience; and update their knowledge and competences through continuous professional development.

Professional requirements should be outcome-oriented; targeting concrete learning results and competences, rather than prescribing inputs such as a certain number of training hours.

Natural catastrophes

Working with policymakers to minimise the impact of disasters

When it comes to protecting the public against natural catastrophes, the role of insurers goes well beyond risk sharing and risk transfer. Insurers are an integral part of the entire risk management cycle. They help to improve risk identification methods for areas at high risk of natural catastrophes, such as mapping tools to identify flood-prone regions. They also help public authorities to set up appropriate risk management frameworks, including risk modelling initiatives to predict the economic cost posed by catastrophic risks. European insurers have therefore been playing an increasingly important role in enhancing the understanding of natural catastrophes and in developing sustainable solutions to cover them effectively.

At various EU seminars and meetings over the past year the CEA has explained the conditions needed if insurance schemes are to cover natural catastrophes effectively and efficiently. These are: the sharing of responsibility between public authorities, private companies and insured parties; the coordination of action between stakeholders and government bodies to increase the data available on catastrophic events; and the promotion of *ex-ante* (before the event) financing schemes, such as insurance, as a more effective way to compensate those affected by natural disasters than *ex-post* (after the event) financing, such as state/EU funds. All three principles underpin the CEA's position that preparedness — via greater cooperation and dissemination of information — is key to minimising the economic impact of natural catastrophes.

Steering group role

As well as speaking at various events, the CEA is a member of the European Commission's Adaptation Steering Group, an invitation-only working group consisting of EU member state environmental experts and key stakeholders in climate change adaptation. Launched in September 2010, the group supports the Commission's work on adaptation by giving guidance on EU adaptation policies, identifying key challenges for adaptation action and sharing technical information.

Shared responsibility

The CEA's activities aim to increase understanding that insurance cannot be the sole solution for natural catastrophe losses, as insurability also depends on actions taken by other parties. Responsibility for minimising the impact of natural catastrophes and adapting to catastrophic conditions must be shared between private and government bodies and the public.

Effective risk management requires all those involved to coordinate the distribution of data in order to produce more accurate predictions of natural catastrophes. With the higher frequency of major floods, hurricanes and earthquakes in the last 40 years, as well as growth in populations and asset values, it is important to invest in risk-mapping tools and in building more advanced information-sharing databases, such as the EC proposal for a Clearing House Mechanism on climate change impacts, vulnerability and adaptation.

The development of such tools can aid policymakers in identifying high-risk areas, which helps them determine the building codes or land-use planning regulations necessary for minimising the public's exposure to risks. In turn, this data can help insurers to design appropriate insurance cover to complement any government measures that help minimise the impact of natural catastrophes.

Insurers can provide an efficient "buffer" to the effects of natural catastrophes, as contributions are collected in advance through insurance

premiums so payouts under insurance policies are not affected by administrative and budgetary concerns, as is often the case with state or EU solidarity funds. In areas where insurance is not commercially developed, public-private partnerships to share the cost of premiums can be of assistance in making a very high exposure to natural catastrophic risk more affordable, thereby enlarging the pool and further stimulating insurance capacity.

Public expectation of some state intervention in the event of a major natural disaster tends to lower the incentive to take preventive measures and the demand for *ex-ante* protection, such as that provided by insurance. The CEA believes that pure *ex-post* compensation, such as state relief and EU solidarity funds, should therefore be restricted to those cases where the necessary prevention measures have been taken and to those losses that are not insurable. This creates a greater incentive to use *ex-ante* financing schemes, which promote efficiency in claims management and provide quicker compensation of the affected parties.

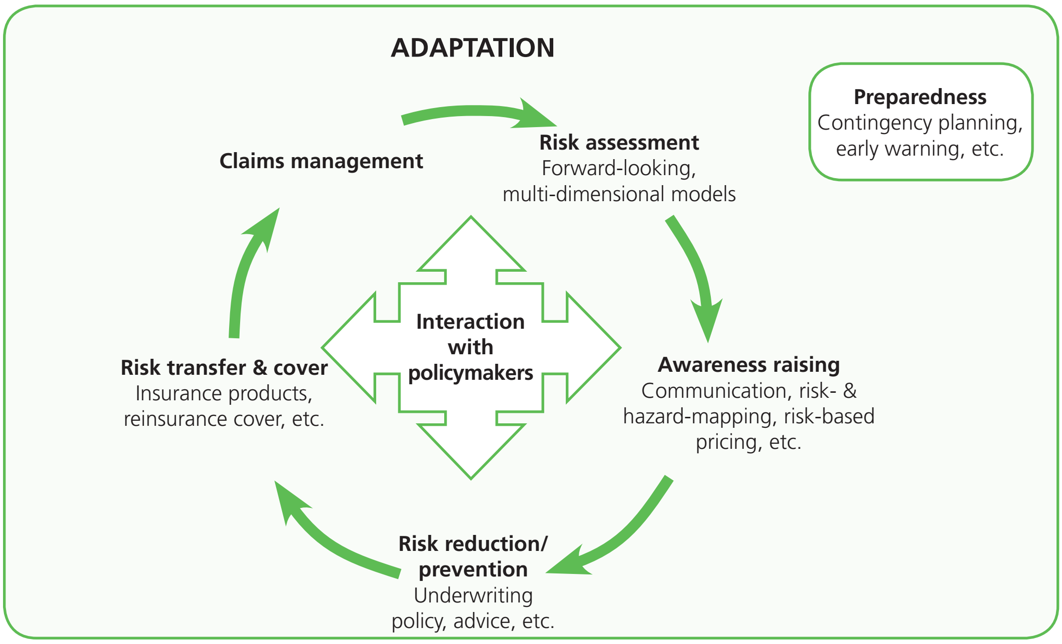
Key information provider

The CEA works closely with the European Commission to provide policymakers with information and data related to insurance and natural catastrophes.

Following the devastating earthquake and tsunami that struck Japan in March 2011, the CEA was able to provide the Commission with an early assessment of the likely impact on European insurers, showing that the terrible events were not likely to trigger problems in the European insurance market.

In preparation for a planned EC conference on insurance and natural catastrophes in October 2011, the CEA has been responding to requests from the EC for advice on the various insurance schemes in place for natural catastrophes, the differences between the compulsory and optional insurance regimes across Europe, the general take-up of insurance against natural catastrophes in various EU member states and the cover of past catastrophic events.

Roles of the insurance industry in tackling natural catastrophes



Source: CEA

Insurability

Balancing consumer protection and sustainable insurance

EU policymakers often look at EU-wide compulsory insurance as a way of protecting European citizens and residents against risks. This tendency has become particularly prevalent following recent large-scale loss events, such as the April 2010 US Deepwater Horizon oil spill in the Gulf of Mexico (the largest marine oil spill in history), the October 2010 Hungarian toxic mud spill and the ash cloud from the volcanic eruption in Iceland in March 2010, which caused widespread disruption to air travel.

The CEA has on many occasions provided advice and recommendations on the most effective action. Given that insurance capacity can be severely strained by compulsory insurance proposals, especially for large-scale risks, the CEA has explained the limited situations in which compulsory insurance schemes can work (see box) and why these solutions are not the most effective way to address the protection of consumers against such widespread losses.

Spotlight on environmental liability

In October 2010 the CEA welcomed the European Commission's long-awaited report on the effectiveness of the EU's 2004 Environmental Liability Directive (ELD) and related financial security issues, as the report concluded that there was insufficient justification at that time to introduce a harmonised system of mandatory financial security, such as compulsory liability insurance.

In the years leading up to the report, the CEA had explained that an EU-wide compulsory liability scheme for environmental liability risks was unfeasible, not only because of the current lack of statistical data on ELD claims due the late transposition of the Directive into national law in most EU member states, but also because of differences in liability cultures and environmental threats between member states. The CEA maintained that a voluntary scheme that permits insurers to develop and price products

The difficulties with compulsory liability

Before any compulsory insurance scheme can be considered there are five key preconditions that must be met:

- market stability established by sufficient claims data;
- sufficient supply of insurance capacity to manage and cover claims;
- a variety of insurers to ensure adequate competition;
- uniform risk characteristics that can aid in standardisation; and,
- an adequate reinsurance market.

Where these preconditions are not met, undesired effects are likely to result for consumers, including premiums that do not accurately reflect risks, a shortage of insurance capacity and a lack of insurers and products to adequately address consumers' needs.

The preconditions alone may also not be sufficient, depending on the nature of the liability. Some liabilities may be so difficult to cover (ie, have such a high risk) that they require certain predefined filters for the risk to be insurable (eg, a cap on insurance cover or the possibility to introduce policy exclusions and/or coverage restrictions). Insurers must be free to use these filters to adapt their products to the needs under any given liability regime.

according to the needs of their customers is more appropriate for the development of sustainable and innovative solutions and helps to ensure that an appropriate level of insurance capacity for potential liabilities can be maintained.

Shortly after publication of the report, however, the EC's Energy Directorate General issued a Communication that proposed amendments to extend the ELD to cover all marine waters and called for a legislative framework to govern the financial capability to handle the consequences of unforeseen events (eg, offshore oil spills), such as insurance schemes or risk-coverage instruments.

The CEA again stressed to the EC the infeasibility of a mandatory financial security scheme for major environmental disasters such as the Deepwater Horizon oil spill or the Hungarian mud spill. The scale of these events far exceeded the financial capacity of the insurance industry, as the damages are extremely high and there is only a limited number of highly specialised insurers covering ELD liabilities.

In the case of oil companies in particular, most have far more financial capacity to cover their environmental liability risks than the insurance industry. As oil spills do not respect national borders, any solution must also be developed within international conventions that already exist for oil sector liability rather than through EU legislation.

The EC will re-examine the option of mandatory financial security, possibly before the next review of the ELD that is planned for 2014.

Protecting air passengers

In late 2010, the EC commissioned a study of possible ways to improve passenger protection in the event of airline insolvency, with compulsory airline insolvency insurance one of the options considered.

The CEA contributed to the work of the study during November 2010, advising that EU-wide compulsory airline insurance would not be feasible as the market is very limited and the simultaneous filing of numerous claims could well surpass the financial capacity to deliver cover. Without a more diverse insurance market and an adequate reinsurance base, insurers cannot effectively spread the risk to cover airline insolvency under a compulsory insurance measure.

The consultancy performing the EC's study issued its final report in March 2011. While it concluded that compulsory insurance was indeed not feasible at present, it indicated that such insolvency cover could perhaps be generated under a compulsory measure.

In its comments on the final report, the CEA explained that the lack of a reinsurance market for airline insolvency cover would make it highly unlikely that such a market could be generated on a compulsory basis. In contrast to the global reinsurance market for natural catastrophes, the reinsurance market for airline insolvency is almost non-existent. This leaves the currently small number of insurers covering airline insolvency without sufficient resources to fall back on in the event of a major insolvency.

The CEA also presented its position at an EC stakeholder hearing at the end of March 2011. The airline industry expressed support for the CEA's views at this hearing and agreed that a voluntary insurance solution would be more appropriate.

The EC will carry out an impact assessment on this issue and align the process with its review of the Package Travel Directive, which is scheduled for the end of 2011. It will also perform a "fitness check" or evaluation of the European aviation market throughout 2011, which will include further study of the issue of airline insolvency and a possible study on the cover of terrorism within the airline sector.

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Lloyd's
Chairman: Lord Levene of Portsoken
www.lloyds.com, tel: +44 2073271000

Observers:

Russia — All Russian Insurance Association (ARIA)
President: Andrey Kigim
www.ins-union.ru, tel: +7 4952321224

Ukraine — The League of Insurance Organisations of Ukraine (LIOU)
President: Nataliya Gudyma
www.uainsur.com, tel: +380 445168230

General Assembly & 2nd International Conference

London, 10–11 June 2010

As part of the 2010 General Assembly events that were held in central London, the CEA hosted its second full-day international conference for both members and non-members.

At the conference, CEA president Tommy Persson called on regulators and policymakers to ensure that any initiatives in response to the financial crisis are appropriate for the sectors to which they apply. "The assumption that what is valid for banking must be valid for insurers is too simplistic," he insisted.

CEA president Tommy Persson introduces the day's debate

Keynote speaker Peter Skinner MEP

The conference, entitled "Insurance in a changing world", attracted around 300 delegates and featured panel debates with CEOs, consumer representatives and regulators.

Keynote speaker Peter Braumüller, chairman of the executive committee of the International Association of Insurance Supervisors

Speakers at the conference included Recaredo Arias, secretary general of the Inter-American Federation of Insurance Companies (FIDES); Steven Weisbart, senior vice-president of the Insurance Information Institute; Low Kwok Mun, executive director of the insurance supervision department at the Monetary Authority of Singapore and Peter den Dekker, president of the Federation of European Risk Management Associations (FERMA).

At the CEA's General Assembly held the day before the conference, Sergio Balbinot, managing director of Generali, was elected vice-president of the CEA. He serves a term of one year, before taking over from Tommy Persson as president in June 2011 for a mandate of three years.

Swiss supervisor Monica Mächler moderates a panel of CEOs: Generali's Sergio Balbinot, John Keogh of Ace, Geoff Riddell of Zurich Financial Services and Aegon's Alex Wynaendts

CEA publications 2010–2011

All these CEA publications, and more, are available free to download at www.cea.eu

Annual Report 2009–2010
(June 2010)

Review of the CEA's key activities between June 2009 and June 2010, together with details of the CEA's structure and organisation.

CEA Briefing Note: Insurance distribution
(July 2010)

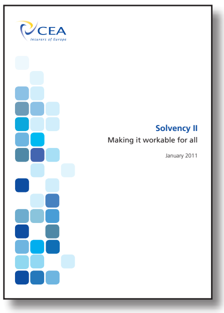
Points for policymakers to consider when regulating insurance distribution and proposals for high-level principles on selling practices for insurance.

European Insurance — Key Facts
(September 2010)

Facts and figures about the European insurance market and the contribution of European insurance to society and the economy.

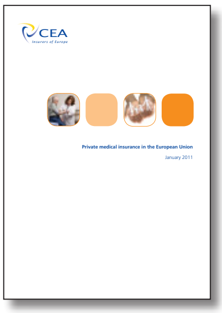
European Insurance in Figures
(November 2010)

A CD-Rom of key 2009 data on the life and non-life premiums and investment portfolios of Europe's insurers and on market operators.



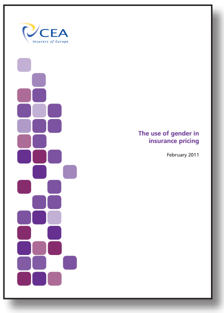
Solvency II: Making it workable for all
(January 2011)

Proposals for ensuring that the implementation of Solvency II is workable for all (re)insurers, particularly small and medium-sized companies.



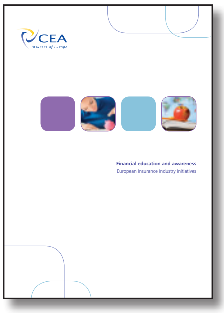
Private medical insurance in the European Union
(January 2011)

Explanation of the main types of private medical insurance (PMI) schemes operating alongside public healthcare systems in Europe and how PMI can help states to manage the burgeoning costs of providing adequate healthcare.



The use of gender in insurance pricing
(February 2011)

Explanation of why insurance companies take account of gender in their pricing process and the effect of a prohibition of the use of gender.



Financial education and awareness: European insurance industry initiatives
(May 2011)

Showcase of some of the many financial awareness programmes carried out by national insurance associations, along with a number of policy recommendations to change consumers' behaviour.

Indirect taxation on insurance contracts in Europe — 2011
(June 2011)

Overview of the taxes applicable to insurance premiums as well as the various declaration and payment procedures in most European states.

CEA Executive Committee

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Versicherungsverband
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Hrvatski ured za osiguranje

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CEO
Schweizerischer Versicherungs-verband (ASA/SVV)

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Türkiye Sigorta ve Reasürans Şirketleri Birliği

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Association of British Insurers (ABI)

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Unión Española de Entidades Aseguradoras y Reaseguradoras (UNESPA)

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Senior advisor
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Generali, Italy

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Chairman & CEO
Axa Group, France

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Chairman
CRO Forum
CRO
Zurich Financial Services, Switzerland

Asmo Kalpala
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CFO
Zurich Financial Services, Switzerland

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Reinsurance Advisory Board (RAB)
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Vice-president
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HUK Coburg, Germany

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Uniqa, Austria

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Eureko, Netherland

Simon Lee
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RSA Insurance Group, UK

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International Underwriting Association of London

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Group casualty director
RSA, UK

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Victoria General Insurance, Greece

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Roland Rechtsschutz, Germany

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Axa Cessions, France

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Nordic product manager, private division
TrygVesta, Norway

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Lloyd's, UK

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Arbeitgeberverband der Versicherungsunternehmen, Germany

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Axa MPS, Italy

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Association of British Insurers

Vice-chair: Lorenzo Savorelli
Head of research & development
Generali, Italy

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UNIPOL, Italy

Vice-chair: Peter Eichler
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Uniqa Personenversicherung, Austria

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Vice-chair: Fabio Dal Boni
Head of communication & public relations
Allianz, Italy

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Danny Dehaes
Executive secretary

Dorothy Straw
Executive assistant

Public Affairs

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Head of department

Frida Bergman
Policy advisor

Ecaterina Matcov
Policy advisor

Katerina Huljakova
Secretary

Communications & Public Relations

Janina Clark
Head of department

Annemarie Bos
Policy advisor

Mareike Post
Policy advisor, information & documentation

Amélie Chantrenne
Event coordinator/secretary

Economics & Finance

(situation vacant)
Deputy director general/ director, economics & finance

Prudential Regulation

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Head of unit

Catherine Munt
Senior manager, actuarial issues

André-Philippe Sende
Policy advisor

Natalie Stevenson
Policy advisor

Accounting & Investments

Benoit Malpas
Head of unit

David Ogloza
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International Affairs & Reinsurance

Hannah Grant
Policy advisor (secondee)

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Anne Halbardier

Laetitia Molina

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Catherine Goislot
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Policy advisor, life & health

Daniel Madejski
Policy advisor, taxation

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Single Market & Social Affairs

William Vidonja
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CEA Annual Report 2010–2011 is available on the CEA's website: www.cea.eu

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