

# EC Consultation on insurance guarantee schemes

## Response of the Slovak Insurance Association

### 1. Have new insurance guarantee scheme arrangements been introduced in your Member State or is the situation currently under review?

No new insurance guarantee scheme arrangements have been introduced in Slovakia, although underlying documents (*Intent on the consumer protection in the financial market*) for recently proposed Act on financial mediation and financial consulting do not exclude possibility to introduce guarantee scheme in the Slovak insurance market.

### 2. Given that neither the current nor the future solvency regime create a zero-failure environment and that many MS have not established IGS, which is your preferred option?

- a. The status quo, i.e. adopting a caveat emptor approach possibly linked with enhanced policyholder information
- b. Case-by-case intervention as and when problems arise
- c. Mandating the establishment of IGS in all Member States
- d. Introducing a single EU-wide IGS that covers all relevant policies written and purchased within the EU
- e. other options

Slovak market has never recorded an insolvency in the insurance sector. The abovementioned proposal of the Act on financial mediation and financial consulting should enhance the amount of information provided to clients. We fully understand that aspect of consumer protection is of the utmost importance. But unlike other operators in the financial market, insurance companies must hold a solvency margin as a buffer against unforeseen losses.

On the basis of article 20 of currently valid directive 2002/83/EC concerning life assurance, insurance companies are obliged to establish sufficient technical provisions. Technical provisions serve exclusively for coverage of future policyholders' claims, what means that they must be used exclusively for all future liabilities as determined by the policy conditions for each existing contract. These reserves cannot be used for any other purpose. Creation, administration and using of technical provisions are strictly regulated by European directives (*i. e. art. 20 – art. 25 of directive 2002/83/EC concerning life assurance, similarly by directive on non-life insurance*) and national primary and secondary legislation. Insurance companies are obliged to provide national supervisory authority with a proof of technical provisions sufficiency performed on the basis of test of technical provisions' sufficiency (*Regulation of European Parliament and Council 1606/2002 from 19 July 2002 on international accounting standards and Regulation of European Commission 1725/2003 from 29 September 2003*). No such a requirement exists in other sectors of financial market.

Supervisory authorities are primarily responsible for safe functioning of the market, what from insurance perspective means, that national authority supervising insurance market controls sufficiency of technical provisions on regular basis.

According to opinion of the Slovak Insurance Association, establishment of IGS is not necessary due to the following reasons:

- 1.) Firstly, such a guarantee in the form of technical provisions to meet policyholders' claims exists **neither in banking nor in securities sectors**.
- 2.) Secondly, in several member states, insurance companies need to pay for their supervision. As national supervisory authorities are paid for performing of qualified and prudent supervision by

the sector itself (to certain extent), and provided the fact that supervisory authorities should make supervision properly and prudently, then no IGS are needed.

If IGS were introduced, then the role and responsibilities of supervisory authorities could lower. Establishment of IGS could potentially lead to moral hazard on the side of supervisory authorities resulting from the existence of additional safety net in the form of IGS.

***If IGS are established, insurance companies will have to pay double contributions - Firstly contributions for performing supervision and secondly to IGS because there might be a potential threat of insolvency which would result from improper supervision performed by the supervisory authorities. IGS will not enhance consumer protection, but will make supervision easier and not so prudent.***

In our opinion, potential establishment of any form of a guarantee fund should be left upon market forces. For that reason choice „**e – other options**“ appears to be the most suitable from the Slovak perspective. Nevertheless, IGS establishment has its reason only in life insurance business due to short term nature of non-life insurance contracts.

**3. Do you agree with the conclusion that, costs can to a certain extent be adjusted through scheme design and that if properly designed, introducing an IGS can be pro-competitive and improve the operation of the market?**

We agree with the opinion that design of a guarantee scheme itself can have substantial influence on costs. Costs on IGS establishment and administration will consequently reflect to certain extent on level of premium, what will make companies contributing to IGS less competitive compared to companies in another member state where i. e. contributions to IGS would not be required. Moreover, IGS could increase market entry costs. So we are not of the opinion that introduction of IGS can improve competition in the market. Furthermore, insurance companies, that assessed risks carefully and made every effort to protect clients and meet their requirements will pay for the bad performance of those companies that have not introduced any or small measures on risk mitigation.

**4. Do you consider the presence or absence of IGS to be an important factor in the development of cross-frontier insurance business in the single market and, in your view, which aspects of the current uncoordinated situation already or potentially constitute obstacles to the further development of the single insurance market?**

No, we do not think that presence (or absence) of IGS is an important factor in the development of cross-frontier insurance business in the single market. Retail financial services (including insurance services) are predominantly sold on the local basis and retail clients will always tend to buy insurance in the environment they are familiar with.

**5. Which are the key considerations (for and against) in the trade-off involved in the decision on whether or not to establish an IGS and what relative weight do you attach to these key considerations?**

Primary aim of IGS establishment is policyholders protection. Slovak market is a rather concentrated market and that's why it is highly improbable that IGS would be able to cover policyholders' claims in case of insolvency of one of the biggest insurers. From the point of view of Slovak insurance companies, IGS will not guarantee a sufficient protection for policyholders.

**6. Is the case for establishing an insurance guarantee scheme in insurance weaker than in the banking and securities sectors and which lessons, if any, can be learned from the banking and securities sectors?**

From the point of view of Slovak insurance sector definitely yes.

No bankruptcy occurred throughout the whole existence of privately held insurance market (19 years). Slovak banking sector recorded several bankruptcies in the past, that's why deposit guarantee fund has its justification in the banking sector.

On the basis of article 20 of currently valid directive 2002/83/EC concerning life assurance, insurance companies are obliged to establish sufficient technical provisions. Technical provisions serve exclusively for coverage of future policyholders' claims, what means that they must be used exclusively for all future liabilities as determined by the policy conditions for each existing contract. These reserves cannot be used for any other purpose. Creation, administration and using of technical provisions are strictly regulated by European directives (*i. e. art. 20 – art. 25 of directive 2002/83/EC concerning life assurance, similarly by directive on non-life insurance*) and national primary and secondary legislation.

Insurance companies are obliged to provide national supervisory authority with a proof of technical provisions sufficiency performed on the basis of test of technical provisions' sufficiency (*Regulation of European Parliament and Council 1606/2002 from 19 July 2002 on international accounting standards and Regulation of European Commission 1725/2003 from 29 September 2003*). Supervisory authorities are primarily responsible for safe functioning of the market, what from insurance perspective means, national authority supervising insurance market controls sufficiency of technical provisions on regular basis.

According to opinion of the Slovak Insurance Association, establishment of IGS is not necessary due to the following reasons:

- 1.) Firstly, such a guarantee in the form of technical provisions to meet policyholders' claims exists **neither in banking nor in securities sectors**.
- 2.) Secondly, in most of the member states, insurance companies need to pay for their supervision. As national supervisory authorities are paid for performing of qualified and prudent supervision by the sector itself (to certain extent), and provided the fact that supervisory authorities should make supervision properly and prudently, then no IGS are needed.  
If IGS were introduced, then the role and responsibilities of supervisory authorities could lower. Establishment of IGS could potentially lead to moral hazard on the side of supervisory authorities resulting from the existence of additional safety net in the form of IGS.
- 3.) Moreover, Solvency II rules should enhance policyholder protection and should contribute to more precise risk assessment.

***From the point of view of Slovak insurance sector, if IGS are established, insurance companies will have to pay double contributions - Firstly contributions for performing supervision and secondly to IGS because there might be a potential threat of insolvency which would result from improper supervision performed by the supervisory authorities  
IGS will not enhance consumer protection, but will make supervision easier and not so prudent.***

**If an IGS were to be implemented in all Member States to address cross-border problems, the following questions would have to be addressed:**

**7. What should be the geographic scope of the IGS – i.e. should the national IGS be based on the home or the host state principle?**

If IGS are to be introduced then **host state** principle should be chosen.

Reasons for such a response:

- 1.) There is a trend of transforming insurance companies operating in the Slovak market to branches. Lately already highly specialized that operate in the field of non-life insurance did so, It cannot be excluded that composite companies with high market share will transform to branches in the future.

As Slovak market is highly concentrated and 99 % of companies are subsidiaries of insurance companies based predominantly in Germany and Austria then in the case of home state principle, companies operating in the Slovak market will have to pay to IGS administered abroad. In case of insolvency, it is highly improbable that Slovak policyholders claims would be fulfilled in the beginning. Credibility of Slovak insurance sector would be at stake.

- 2.) The question which needs to be taken into consideration when applying home state principle is which law would be used in the case of collection of claims if insurance company goes bankrupt. For example - Applicable law - *Article 32 of the currently valid directive 2002/83/EC* concerning life assurance – it was transposed to Slovak legislation as following: In non life insurance – Member State of the commitment. And in life insurance – where natural person and has his/her habitual residence. If IGS will be based in other MS (the case of Slovakia when companies transform to branches and when applying home state principle), which law should be used?
- 3.) Host state principle is used in MTPL insurance where insurance companies operating in the area of one member state (no matter what is their form – if branch, FOS or regularly licenced company) must contribute to guarantee fund administered by local insurers' bureau.

#### **8. Should subsidiaries participate in and be covered by the IGS of the Member State in which the group supervisor is located under the group support regime under Solvency II?**

Because Solvency II directive proposal is still being discussed in the Council and final wording of the articles on group support and group supervisor have not been approved yet, it is too early to respond to that question.

#### **9. What degree of harmonisation across Member States would be required between national IGS and which features of IGS should be harmonised? Should they be harmonised, please indicate your preferred approach.**

- a. Geographic scope (home v host state principle)
- b. Organisational structure (single or multiple IGS, cooperation with insolvency practitioners and supervisory authority, staffing arrangements/outourcing)
- c. Funding arrangements (in particular ex ante or ex post funding, riskweighted contributions and contribution limits))
- d. Policies covered - What classes of insurance should be covered by the IGS and which insurance classes could be excluded?
- e. Claimant eligibility - Which claimants should benefit from the IGS, and which claimants could be excluded?
- f. Protection amounts and limits (caps or maximum compensation levels, deductibles, etc.)
- g. Nature of intervention (in particular the payment of compensation or portfolio transfer)
- h. Payout timing and information to policyholders/beneficiaries

Potential establishment of any form of a guarantee scheme should be left upon market forces, If IGS are to be harmonized then only minimum harmonisation should be required.