

<b>Comments Template on EIOPA-BoS-19-259</b> <b>Consultation Paper on</b> <b>Proposals for Solvency II 2020 Review</b> <b>Harmonisation of National Insurance Guarantee Schemes</b>		<b>Deadline</b> <b>18 October</b> <b>2019</b> <b>23:59 CET</b>
<b>Name of company:</b>	.....	
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<b>Reference</b>	<b>Comment</b>	<b>EIOPA</b>
General comments	<p>Finance Finland does not support the idea of harmonizing insurance guarantee schemes (IGS) and strongly supports the option of maintaining the status quo. IGSs are in place for some lines of business (depending strongly on the MS) but EU-wide harmonization would deliver many problems.</p> <p>The idea of harmonizing insurance guarantee schemes seems to reflect the developments in the banking sector. It should be better recognized that consumer protection needs are different in the insurance sector, and also the contagion risk is very different from the banking sector.</p> <p>The risk of moral hazard caused by IGS should not be taken lightly. Insurance market is all about assessing risks and moral hazard can influence this mechanism.</p> <p>IGSs could increase the risk of contagion since IGSs would increase the interdependence between the insurers. The introduction of IGSs to small and highly concentrated markets could lead to severe contagion risk and thus financial instability. The majority of European insurance markets show a high concentration, i.e. the top 4 insurers having 70–80 % of market share.</p>	

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Should sound companies be required to fill in funding gaps if a larger insurance company collapses, it could significantly weaken the financial position of otherwise healthy insurers, thereby exposing their policyholders to risk. So IGSs can actually have a negative effect on the financial stability.

The need for IGSs has been reduced considerably because of the introduction of Solvency II in 2016. Yet the current idea of IGS relies on an analysis based on pre-Solvency II failures and near misses. It should be remembered that even before Solvency II there were very few failures and even fewer resulting in any losses for policyholders. Before any initiative on IGS or recovery and resolution, an in-depth assessment of the effects that Solvency II has had on the risks in insurance companies and on policyholder protection is required.

Solvency II is meant to form strong protection against insolvency and it already provides very high levels of policyholder protection and safeguards. There should not be duplicative regulation on aspects which are already dealt with in Solvency II. In addition, consumers are already well protected in many Member States since they have high priority in creditor hierarchy in national legislations.

It seems extremely difficult to design even minimum harmonization of IGS since there are significant differences in insurance markets between Member States. The role of different lines of insurance business varies considerably between different Member States. These differences in insurance markets are caused e.g. by different kinds of social security systems which they are built upon. Therefore, many common lines of business (e.g. health insurance, voluntary pensions,

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	<p>workers' compensation) play very different roles in different societies and the need for IGS and their requirements are significantly different, too. Current IGSs vary significantly across Europe but work generally well within their local context and laws. What may seem to be a workable solution for one market can be detrimental to other – and can even compromise the existing national IGSs by lowering their standards if they are harmonized.</p> <p>The role of life insurance is especially different between Member States depending on how the (main) pension cover is organized. In Finland by far the biggest part of people's pension cover is delivered by statutory pension funds (statutory earnings-related pension insurance) which are not considered as life insurers – and these statutory funds already have an IGS with the protection level of 100 %. This means that life insurers play a smaller role in pensions (only supplementary pensions) and thus the need for IGS is significantly smaller for life insurance products in Finland.</p>	
Q1) Do you agree that the legal structure of policyholder protection schemes should be left to the discretion of Member States? Please explain your reasoning.	Finance Finland agrees that the legal structure of policyholder protection schemes should be left to the discretion of Member States. More generally, Finance Finland believes that national authorities should be allowed significant flexibility to choose the IGS features that best suit their market, to reflect that there are important differences between Member States regarding social welfare systems, winding-up process for insurers and insurance product lines.	
Q2) Do you see the need of a parallel development of the topics recovery and resolution framework	IGS should not be used to prevent or reduce risk of company failure and IGS should play no role in recovery and resolution. IGS should remain a "last-resort mechanism" only for providing additional protection after all resources from the insurance company have been exhausted (i.e. after	

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<p>and IGSs? Please explain your reasoning.</p>	<p>insolvency or resolution). It should be up to the national supervisory/resolution authorities (who have the power to initiate liquidation procedures) and for the Member State to decide how the cost of financing resolution (including any losses generated by a reduction of insurance obligations) should be covered. Therefore, Finance Finland agrees with EIOPA's position, stated in Paragraph 86, that the mission of IGS should not include the prevention of insurance failures.</p> <p>Before proceeding with any initiative on IGS or recovery and resolution, an in-depth assessment is required on the effects that Solvency II has had on the risks in insurance companies and on policyholder protection.</p>	
<p>Q3) Do you agree that the primary objective of an IGS can be achieved by means of the two options proposed (i.e. paying compensation and ensuring the continuity of policies)?</p>	<p>National IGS should be solely designed to provide compensation to policyholders for their losses in liquidation. But also here, the role of an IGS depends on the realities of the market in which it is embedded and therefore determining the role of national IGS should be a matter of national discretion.</p>	
<p>Q4) Do you agree that the continuation of the policies should take precedence in case of life and some long-term-life policies? Please explain your reasoning.</p>	<p>National IGS should be solely designed to provide compensation to policyholders for their losses in liquidation. But also here, the role of an IGS depends on the realities of the market in which it is embedded and therefore determining the role of national IGS should be a matter of national discretion.</p>	

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	<p>It might be extremely detrimental to transfer the portfolio of the failed insurer to another insurer. If the risks involved are too significant (e.g. high interest rate guarantees in life insurance policies with a savings component, aggravated health risks in life insurance policies covering death), a portfolio transfer may actually jeopardise the financial soundness of the insurance company that takes over the portfolio.</p>	
<p>Q5) What aspects are relevant to be taken into consideration for the effective implementation of the home-country principle?</p>	<p>The main argument in favour of the home-country principle is that because the financial supervision of insurance and reinsurance undertakings, including business under FoS and FoE, is the sole responsibility of the home Member State (Article 30 of Solvency II), it must therefore also be the responsibility of the home Member State to deal with the consequences of an insolvent insurer, wherever its activities are located. The home country should provide all the funding, because this ensures alignment with the model of the EU supervision. The home country would be responsible for deciding on how the IGS is funded e.g ex-ante/ex-post funding, how contributions are allocated to each insurer in their market, contribution caps, etc.</p> <p>Even though the home-country principle is logical it has proven very difficult to be carried out in practice in cross-border situations. These difficulties stem from the principle itself and all the work and especially costs related to resolving those problems cannot be avoided even if there was some kind of front office etc.</p>	
<p>Q6) Specifically, should the following options be added to</p>	<p>The home-country principle is logical when deciding which IGS should bear the ultimate financial burden because in cross-border situations the solvency supervision remains the home country's</p>	

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<p>the principles of the home-country approach:</p> <ul style="list-style-type: none"><li>• the possibility of the IGS of the host-country to function as a “front office” for the identification of the affected policyholders and beneficiaries?</li><li>• the possibility of the IGS of the host-country to make payments to the affected policyholders and beneficiaries (in their country of residence), and then have a right of recourse against the IGS of the home-country (“back office”)?</li></ul>	<p>responsibility. Yet also some aspects of the host-country principle are extremely important. Especially in cases where there already are IGSs which offer 100 % protection level (usually statutory “social security-like” insurances) businesses operating in the same geographical area within the field of social security-like insurance cover should have the same obligation to offer 100 % protection level.</p> <p>About the possibility of the host IGS operating as a “front office”: Even if the host-country IGS was to operate as a “front office” that would not make the practical difficulties associated with the home-country principle disappear. All the burdensome work and costs related to resolving those problems cannot be avoided even if there was some kind of front office etc.</p> <p>About the possibility of the home IGS operating as a “back-office”: The “back office” would be much too burdensome and unfeasible to implement due to its complexity and the financial risks involved for the host-contry IGS and host-country policyholders.</p>	
<p>Q7) Do you have any other comments on the geographical coverage? For instance, are there any cases, especially in statutory lines of</p>	<p>Under the host-country principle, all policyholders within the same Member State are evenly protected regardless of the insurer’s location. The host-country principle is thus most suitable when determining the level of compensation for statutory (“social security-linked”) lines of business - especially in those countries where the coverage level already may be as high as 100 %</p>	

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business, where the host-country principle should be preferred?	for those products.	
Q8) Do you believe that the criteria for selecting the eligible policies (as set out in paragraph 149) capture all relevant policies which should be subject to IGS protection? Please explain your reasoning.	<p>The criteria set out in paragraph 149 will lead to a situation in which a wide variety of insurance products within EU will be covered by IGSs because the type of insurance that fulfil the criteria differ between the Member States. This is because there are no EU-rules on what an insurance product is and what a specific insurance product should cover (bank deposits on the other hand are much more similar among the Member States).</p> <p>For example, in some countries home insurance also covers legal protection, liability and travel insurance while in others it does not. Thus, the relative importance of different types of insurance for policyholders differs between Member States. This is precisely why there are significant differences in this respect between current IGS in EU Member States.</p> <p>The lack of an analysis of the criteria in paragraph 149 in the consultation paper and its practical implications on different insurance products in different Member States makes it impossible to draw conclusions on the implications for IGS.</p> <p>The product scope should be kept as limited and focused as possible, leaving a large degree of national flexibility to ensure that the best solution is found for every market.</p>	
Q9) Which policies should at least be	Under minimum harmonisation, the product scope should be kept as limited and focused as	



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eligible for IGS protection based on these criteria (as set out in paragraph 149)?

possible, leaving a large degree of national flexibility to ensure that the best solution is found for every market. The following considerations should be taken into account when deciding what types of products should be covered by IGS:

- In general the criteria for the coverage of specific policies, which could lead to considerable social hardship seems more relevant in cases where the insurance substitutes statutory or state-based pension and/or health care systems. Especially the role of life insurance varies greatly between Member States depending on how the main pension cover is organised.
- There are also other significant differences between types of life insurance products that have to be taken into consideration. For example, the risks differ significantly between unit-linked products without guarantees and (traditional) life insurance products with guarantees. In unit-linked life insurance, the investment risk is borne by the policyholder and the insurance company does not provide any guarantee. For this reason unit-linked life insurance should be excluded from IGS.
- Non-life insurance is characterised by a short contract duration and, in the case of insolvency of a non-life insurance undertaking the consumer can easily switch from the insolvent insurer to another insurer. In non-life insurance, unlike in the case of bank deposits or investments, compensation must only be paid if the insured event occurred. Consequently, the affected number of policyholders is considerably smaller in relation to the total insured portfolio. This all reduces the need for an IGS.
- While there is a logic to including some compulsory non-life insurance in a national IGS, the reality is that the types of insurance that are compulsory vary greatly across Member

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	States. Therefore, including all compulsory non-life products under the scope of minimum harmonisation would be misguided.	
Q10) Are there any other considerations to be taken into account to select the range of policies to be covered by an IGS? Please explain your reasoning.	Since life and non-life insurance contracts differ significantly and are handled differently in the event of insolvency, life and non-life insurance should not be administered by same IGS entities.	
Q11) Which criteria should be used to determine/exclude the eligible claimants?	Should minimum harmonisation be considered and because the primary aim of harmonising national IGS is effective consumer protection, Finance Finland believes that the IGS should cover consumers that are natural persons only and that it should be at the discretion of Member States, in consultation with local stakeholders, to decide whether a wider scope is justified.	
Q12) Should coverage be extended to large legal persons where the ultimate beneficiary are retail customers (such as large corporates offering pensions for customers)?	Any minimum harmonisation should only cover consumers (natural persons) and it should be for Member States to decide, in consultation with local stakeholders, whether a wider scope is justified.	
Q13) What should be the relevant criteria to determine a minimum	Member States should decide which compensation limits are adequate for the sustainability of	

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coverage level at EU level for different types of insurances?

their national IGS. They may provide for:

- a de minimis rule (minimum threshold for IGS intervention) which avoids a disproportionate, excessive administrative burden that has only a very minor advantage for the consumer;
- a maximum limit for IGS intervention;
- within the maximum limit, a maximum percentage of the insurance claim covered by the IGS;
- absolute caps on total contributions are needed to avoid that the obligation to fund an IGS exposes the customers of the other remaining insurers in the market at a risk that would not have existed otherwise.

Q14) What should be the relevant criteria to determine the target level for national IGSs?

Finance Finland believes that decisions relating to IGS funding should be left to Member States' consideration, in consultation with local stakeholders.

When considering the timing of funding both ex-ante and ex-post funding have their disadvantages.

Ex-ante funding easily acts the same way as a new tax, and this should be avoided. Experience has shown that funding on an ex-ante basis often leads to the multiplication of the tasks that the fund needs to run. This means greater administrative duties and costs. Unused funds (which become disproportionately large when insurance failures are infrequent or have a limited impact) would block financial resources for a long period of time, exposing them to risks of inefficient use. In the

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case of a market downturn and possible hardship for insurers caused by the downturn, the ex-ante IGS fund would face the same difficulties at the same time.

Ex-post funding reduces the abovementioned management costs and avoids investment risks. Contributions to the IGS fund will be computed according to actual need (outstanding claims/policies concerned). But also ex-post funding has severe disadvantages. In ex-post funding the failing company will not have contributed to the fund and this leads to the main disadvantage of an ex-post funding which is the risk of **moral hazard**.

In concentrated markets, as is the case for the majority of the Member States (i.e. the top 4 insurers having 70–80 % of market share) IGS will only be able to protect consumers from the failure of small insurance companies. Any failure of a medium-sized or large company in a small, concentrated market will require state assistance in order to protect consumers effectively. In the absence of state assistance, and should sound companies be required to fill in funding gaps if a larger insurance company collapses, this may significantly weaken the financial position of otherwise healthy insurers, thereby exposing their policyholders to risk.

In any case, an IGS should not be expected to guarantee to repay policyholders in full. Therefore, one would expect there to be restrictions (caps and limits – see Q13) on the amounts that can be reclaimed under this system and IGS funds cannot be expected to be equivalent to the full value of the technical provisions.

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<p>Q15) What should be the relevant criteria to determine the level of the annual contributions per individual insurer into IGSs, including the method of calculating such contributions (risk-based, fixed rate, other)?</p>	<p>The details of IGS funding should be left to Member States' consideration, in consultation with local stakeholders.</p> <p>Written premiums is not a suitable calculation basis especially for unit-linked life insurance. Calculation should be risk-based and linked to the solvency of the company. Solvency II regime includes tools for the assessment of actual risks.</p> <p>Additionally, any contributions should also be refundable, which means that some kind of “payback mechanisms” should be considered for cases where the basis of the contribution to the fund does not exist any longer or declines significantly (e.g. life insurance stock is partially/completely sold).</p> <p>Finance Finland also favours the introduction of upper limits to the annual level of contributions to the IGS, determined by national competency. The existence of upper limits in insurers’ contributions should preclude any further power of the IGS to require additional contributions from the industry.</p>	
<p>Q16) What should be the relevant criteria to determine the level of the annual contributions for the industry as a whole, including the method of calculating such</p>	<p>Finance Finland favours the introduction of upper limits to the annual level of contributions to the IGS, determined by national competency. The existence of upper limits in insurers’ contributions should preclude any further power of the IGS to require additional contributions from the industry.</p>	

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contributions (risk-based, fixed rate, other)?		
Q17) Are there any other elements that should be included in the disclosure requirements to policyholders? If so, what are those?	<p>Finance Finland believes that any IGS proposal should explicitly prohibit any type of advertising about the existence of an IGS since doing so would create moral hazard.</p> <p>Finance Finland points out that, in the case of insurance-based investment products, the PRIIPs regulation already provides for disclosure under Art 8(3)(e): <i>“(e) under a section titled ‘What happens if [the name of the PRIIP manufacturer] is unable to pay out?’, a brief description of whether the related loss is covered by an investor compensation or guarantee scheme and if so, which scheme it is, the name of the guarantor and which risks are covered by the scheme and which are not;”</i></p>	
Q18) Are there any other elements that are relevant in the context of cross-border cooperation and coordination arrangements in this field, particularly in the context of the home-country approach, please also refer to Q4 and Q5)? If so, what are those?	<p>Many of the problems related to IGSs seem to more or less relate to cross-border situations. There should be an assessment of those characteristics of cross-border business that seem to induce the need for IGS. There should be ways to tackle those problems at a much earlier stage. Solvency II toolkit promotes early intervention and requires effective group supervision through a college of supervisors. Main risk factors indicating future problems usually include: fast growth, considerably low prices, low reserve levels, unusual terms and a narrow range of products.</p>	