

Commissioner McCreevy

The Internal Market in financial services and insurance – Future Directions and Priorities

The Insurance Leaders Summit 2007

"Face to face with the Future"

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Mr Cassells, Mr Hevey, Ladies and Gentlemen

Introduction

Thank you for inviting me to speak at this meeting today. I commend the Insurance Institute of Ireland for its commitment to promoting insurance education and enhancing competency within the industry. The events of this summer have clearly demonstrated the essential need for scrupulous ethical behaviour, high standards of professionalism on the part of market participants and well-enforced regulation.

I would like today to give you a general overview of the progress we are making in integrating EU financial markets and on the agenda for the coming years. I will then focus on the insurance market and, in particular, on the Solvency II proposal.

The internal market for financial services: what has been achieved?

In recent years, we have made significant progress in delivering a Single Market for financial services, particularly at the wholesale level. The measures included in our Financial Services Action Plan have almost entirely been adopted and transposition into national legislation is going quite smoothly, although some countries are lagging behind. The EU has now principles-based regulations and a modern prudential framework in place. Landmark legislation like the Capital Requirements and Prospectus directives as well as the introduction of IFRS have revolutionised the financial markets landscape in Europe. In a few weeks, we will reach the deadline for the application of the MIFID directive, which will boost competition on regulated markets, lower costs and foster product innovation.

Where possible, we have also tried to stimulate market-led solutions, where these were more effective than legislative measures. An important initiative in this regard is the voluntary Code of Conduct on Clearing and Settlement, signed last year by all major European trading and post trading companies. It sets standards to increase price transparency, to improve access and interoperability and to foster accounting separation and unbundling of clearing and settlement services across the EU. Had we tried to achieve the same with legislation this would have taken us many years, if not decades. We are now monitoring closely how this Code is being put into practice.

Next steps: what remains to be done?

The integration of EU financial markets has progressed albeit at different speed depending on the segment. Our studies show that in some markets competition is not efficient, particularly in areas like payments

and retail services. We still have a lot to do to make EU consumers more confident in buying financial services beyond their own national borders!

In May, the Commission issued a consultative document on Retail Financial Services. This "Green Paper" aimed to highlight the objectives of our policy and the planned initiatives in the retail area. We also wanted to learn more about the obstacles faced by market participants.

The level of engagement from all stakeholders in this consultation has been remarkable. The input we have received will be important for any possible new initiatives, some of which could be included in the wider review of the Single Market to be published in November.

Some measures targeted at consumers and retail investors are already underway or will be put forward soon. The directive on consumer credit is heading for adoption in the Parliament and in the Council. We will set out our policy orientations in the field of mortgage credit in a White Paper that will be published towards the end of this year. We are working on the legal framework for investment funds, and will be bringing out our policy proposals in early 2008.

The current turbulence in the financial markets has underlined again the need for good and strong financial supervision. Pan-European groups play an increasingly important role in the European financial landscape and with them comes the potential for cross-border and cross-sector spill-over effects. The supervisory landscape in Europe needs to develop in such a way as to keep pace with these developments. We need to achieve greater co-operation between supervisors and greater convergence in supervisory practices if we are to enhance the efficiency and competitiveness of our markets. We are not talking about a

revolution here, but rather capitalizing on the existing Lamfalussy architecture in securities, banking, and insurance and strengthening the existing committees of supervisors. The Commission will be coming forward with fresh proposals on supervision before the end of the year.

A modern legal framework for the insurance business: Solvency II

Now, let me turn to the developments in the insurance regulatory regime. After years of preparation, study, consultation and analysis, the Commission launched the "Solvency II" proposal as scheduled on 10 July this year. The proposal aims to establish a modern regime that is based on sound economic principles, to ensure the financial solidity of insurers in Europe. Insurance is one of Europe's success stories globally. European insurers are world-leaders. If we are to maintain our position and to build on it, Europe needs to be prepared to step up its game and take the lead globally when it comes to the regulation of financial services. One cannot achieve this without being ambitious.

Reform is overdue as the current regime is over 30 years old and the financial sector has developed dramatically during that time. Techniques for risk management have undergone a revolution in the past three decades. This has resulted in a great gap between the way in which insurance firms measure and manage their risks, and the basis on which they are regulated. Furthermore, the present EU framework only sets out minimum standards that are often supplemented by additional rules by Member States. These national differences distort and undermine the Single Market, as well as hinder effective competition. This results in increased costs for EU insurers, in particular pan-European groups, and higher premiums for European consumers and businesses, thus hampering growth.

The Solvency II proposal puts forward a comprehensive and far-reaching package to reform the prudential supervision of insurance in Europe. It will remove obstacles to the functioning of the internal market in insurance and improve the supervision of insurers. Consumers, the industry and the EU economy as well as financial stability should all benefit.

The new framework will also turn the spotlight on the accurate identification, measurement and management of risk. An accurate reflection of an insurer's realistic financial situation is an essential prerequisite for sound risk management and timely management action.

For the new framework this means a shift to market consistent valuation of assets and liabilities, as well as giving due recognition to the economic impact of modern risk mitigation techniques.

The Solvency II proposal also introduces measures designed to streamline the supervision of insurance groups. Groups are increasingly managed in an integrated way and the current supervisory view of groups does not fit in well with the modern world. A dedicated group supervisor will be appointed for each group, with real decision-taking powers and coordination responsibilities. Groups will need to demonstrate robust systems and controls and effective group-wide risk-management before being allowed to take advantage of group-wide diversification benefits, a lower capital burden and streamlined supervisory and reporting requirements.

This reform is a real opportunity to improve the international competitiveness of European insurers. It is already evident in other sectors that the sensible and modernising regulatory approach of the

EU is paying dividends. The same will be true for insurance. We have a chance of creating a true global benchmark. We are already seeing great interest from the US, Japan and China in this project.

There is growing nervousness in the US about the EU surging ahead while the US itself is stuck with a highly fragmented insurance regulation. Let's make sure we use this opportunity to give EU insurers a head start in the global economy.

Conclusion

To sum up, ladies and gentlemen, our mission is to provide the framework for thriving and competitive EU financial markets. The signs are that we are progressing but we have still a lot to do. State-of-the-art financial regulation is key to ensuring that European markets, European companies and citizens can reap the benefits of financial integration. We must be ambitious and be ready to ditch old habits. We need to be courageous in seeking new approaches. Solvency II is part of this effort. It will benefit the European industry, policy holders and the EU economy.

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