

Comments on CEIOPS Issues Paper CEIOPS-IGSRR-24/08

Implementing Measures on System of Governance

Commentator:



European Captive Insurance and Reinsurance Owners' Association

Reference

Comment

The European Captive Insurance and Reinsurance Owners' Association (ECIROA) is pleased to respond to your request for comments on the Issues Paper on Supervisory Review Process and Undertakings' Reporting Requirements. As you may be aware, ECIROA represents major industrial and financial groups owning European captives. For further information about the association and its members please visit www.eciroa.org.

General comment

Most captives are not complex operations supporting sophisticated internal functions but are primarily very small companies which are usually serviced by captive management companies. A captive is obliged to comply with the established and advanced internal control and reporting guidelines and policies imposed by the risk management functions of the parent. We therefore believe that captives should be asked to fulfil only the reasonable „minimum“ requirement as any disproportionate requirements for actions, policies and information distribution would be burdensome and would increase costs.

Please find below some detailed comments on some of the Paragraphs of your Issues Paper. The text marked in yellow is the wording from the Issues Paper and the unmarked text is our comment.

Para. 3.3

“Undertaking should at least provide for the following functions:

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- a) Risk management
- b) Compliance
- c) Internal audit
- d) Actuarial"

We think it is reasonable that, for captives, these functions be performed by the parent company's corresponding function (if existing).

Para. 4.6

..."the internal function shall be objective and independent from the operational functions...""not to create any unreasonable burden for undertakings with low risk profiles, these undertakings would not have to provide for a permanently operating function as part of their organisation but could commission a qualified party to execute these tasks within an appropriate timeframe."

For captives, a qualified party could be the internal function of the parent company.

Para. 4.7-4.8

"Insurance and reinsurance undertakings shall have written policies in relation to at least risk management, internal control, internal audit and, where relevant, outsourcing.."

Captives insure the risks of its owner and therefore the risk management function and other controls should be in line with the expectations of the parent company.

Para 6.10

A captive is obliged to obey internal guidelines, including investment policies and asset-liability management policies and thus

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	the risks are under the full control of the insured. No third party protection is needed.
Para 6.50	Operational risk management... "this definition includes legal risk, but excludes risks arising from strategic decisions and reputation risk" ... Operational risk may include legal risk but should exclude business risk. Business risk includes strategic decisions as well as reputation risk. Business risks are covered by regulatory capital following Pillar I requirements.
Para 6.70	"Undertakings should be aware that intra group exposures give rise to credit risk as any other external exposure does..." No consideration is necessary with respect to intra group exposures in monitoring the captive's credit risk exposure. The risk underwritten by a captive is group related and therefore a credit risk from intra group exposure does not result in an additional risk towards a third party.
Para 6.85	"The undertaking needs to establish a risk management function within its organisational structure that is proportionate..." ...shall ensure that the function is objective and independent from operational functions." It is clear that in a large company a risk management function is necessary. In smaller companies, entrepreneurial risk has to be carried by managers and there is no need to distinguish between the entrepreneurial risk and other risks. Earlier in the Issues Paper (Para 4.5) it is mentioned that it might be appropriate and proportionate for staff to fulfil several duties or functions at the same time (should the undertaking have a limited number of staff). This is the case for captives and for smaller insurance companies. This will not work in practice if a function is to be objective and independent from operational functions.
Para 8.12	"...the internal audit function shall at least annually produce a written report..." A captive is obviously too small an entity to establish its own internal audit function. However, captives normally fall under the controls of the internal audit department of the parent company.

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With regard to the frequency of internal audits, the proportionality principle should be applied as a small captive cannot be expected to be subject to an annual internal audit.

Para 10.5

"...As the undertaking remains fully responsible for all outsourced functions and activities it needs to have in place a system of controls of the activities taking place at the service provider and to include them in its risk management. It is not sufficient that the service provider itself has internal controls..."

Because captives are generally limited in size many functions of the captive are commonly outsourced, including the day-to-day management. Normally, a Service Agreement is produced with full documentation setting out responsibilities, including how and why actions will be carried out. We would like to discuss this point in more detail with CEIOPS and with captive management companies, as this is a central point in the daily work load of the management of captives.