



To:

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Dear Sirs and Madam

We appreciate the frequent engagement that we have had in order to ensure the development of proportionate implementation rules for Captive Insurance and Reinsurance Companies and their captive owners (Europe's major multinational corporations) under the Solvency II Directive. This letter and the accompanying documents present a number of outstanding issues that we look forward to resolving with the Commission and EIOPA.

We welcome and fully support the definition of a captive insurance entity as set out under Article 13 of the Solvency II Directive (2009/138/EC).

However, as currently drafted, Article 78 SCRSC1 narrows the definition of captives by placing restrictions on the types of captives that will be allowed to use the captive simplifications to calculate the solvency capital requirement. This operates against the principle of proportionality for captive insurance and reinsurance undertakings as called for in the Solvency II Directive.

Limitations under (a) and (b) (see below) are so strict that they would effectively rule out at least 8 out of 10 captives from using the simplifications for captives.

**Article 78 SCRSC1
(Art. 109 of Directive 2009/138/EC)
General provisions for simplifications of captives**

Simplified calculations that are specifically available to captive insurance and reinsurance undertakings set out in Articles 84 SCRSC2, 148 SCRSC3, 158 SCRSC4 and 171 SCRSC5, shall be considered as proportionate to the nature, scale and complexity of the risks they face where applied only to captive insurance and reinsurance undertakings as defined in Article 13 of Directive 2009/138/EC complying with Article 77 SCRSC1 and where the following requirements are met:

- (a) in relation to the insurance obligations of the captive insurance undertaking, all insured persons and beneficiaries are legal entities of the group of which the captive insurance or reinsurance undertaking is part of;
- (b) in relation to the reinsurance obligations of the captive insurance or reinsurance undertaking, all insured persons and beneficiaries of the insurance contract underlying the reinsurance obligations are legal entities of the group of which the captive insurance or reinsurance undertaking is part of;
- (c) the insurance obligations of the captive insurance undertaking and the insurance contract underlying the reinsurance obligations of the insurance or reinsurance captive undertaking do not relate to any compulsory third party liability insurance.

The problem with the current wording arises because in today's world major corporate group structures experience frequent changes. This is because major corporations (the captive owners) tend to have active mergers and acquisitions activities. This means that legal entities that are part of the group today might not be part of the group in 2 or 3 years.

However, group insurance policy issued today covers all group affiliates and, according to insurance law, these entities remain covered under the group's occurrence based Third Party Liability Insurance (TPL). Therefore, where legal entities are sold, the coverage remains a "group risk" cover in line with the captive definition under Article 13 of Solvency II. **Note that the captive is not insuring any new risks of the entity once it has been sold.**

Given the importance of captives as a risk management tool for Europe's largest multinational corporations, it is essential that Article 78 SCRSC1 is appropriately amended to reflect how the captive business model operates under the Article 13 definition and to ensure proportional treatment.

We understand and appreciate that the Commission (based on Consumer and Claimant Protection considerations) would prefer to exclude any compulsory third party liability insurance by a direct insurance undertaking from making use of the simplifications. Our suggested amendment below reflects this outcome.

In all cases of Reinsurance Captives writing TPL policies a commercial insurer is providing, via fronting policies, the necessary claims handling. In the case where a direct insurance captive writes non-compulsory TPL, this should not lead to complaints from and discussions with consumer protectionists due to the fact that corporations are not obliged to insure their liability risk as long as it is not a legal local requirement – there are companies which don't insure their liability risk due to a sound positive claims experience and a sophisticated risk management activity.

The commercial insurers diligently check the Counterparty Risk and the claims paying ability of captives with their own experienced employees. For added comfort, they may request further security measures such as Letter of Credit, collateral or similar security. Beside this Credit Risk the reinsurance policies between the fronting insurer and the captive contain insurance technical clauses such as 'Simultaneous Payment' or 'Cut Through Clauses'.

Suggested amendment to Article 78 SCRSC1

**Article 78 SCRSC1
(Art. 109 of Directive 2009/138/EC)
General provisions for simplifications of captives**

Simplified calculations that are specifically available to captive insurance and reinsurance undertakings set out in Articles 84 SCRSC2, 148 SCRSC3, 158 SCRSC4 and 171 SCRSC5, shall be considered as proportionate to the nature, scale and complexity of the risks they face where applied only to captive insurance and reinsurance undertakings as defined in Article 13 of Directive 2009/138/EC complying with Article 77 SCRSC1, except direct captive insurance undertakings writing compulsory third party liability insurance.

We look forward to further discussing the implementation of Solvency II with the Commission and EIOPA in order to develop our understanding of how the captive sector will need to apply the Directive's Pillar 2 and Pillar 3 provisions. In attachment you will find (1) ECIROA's Pillar 2 Best Practice paper for Captives (proposed Level 3 paper), (2) reporting templates overview (previously discussed with Ana Teresa Moutinho) and (3) an ECIROA letter with questions to fronting insurers and a document with their replies.

Yours sincerely,