



EUROPEAN CENTRAL BANK

EUROSYSTEM

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ECB-PUBLIC

OPINION OF THE EUROPEAN CENTRAL BANK

of 7 April 2017

on the provision of flood insurance

(CON/2017/12)

Introduction and legal basis

On 28 February 2017 the European Central Bank (ECB) received a request from the Chairman of the Oireachtas (Irish National Parliament) Joint Committee on Finance, Public Expenditure and Reform, and Taoiseach (Irish Prime Minister) for an opinion on a Flood Insurance Bill 2016 (hereinafter the 'draft law').

The ECB's competence to deliver an opinion is based on Articles 127(4) and 282(5) of the Treaty on the Functioning of the European Union and the third indent of Article 2(1) of Council Decision 98/415/EC¹, as the draft law relates to the Central Bank of Ireland (CBI). In accordance with the first sentence of Article 17.5 of the Rules of Procedure of the European Central Bank, the Governing Council has adopted this opinion.

1. Purpose of the draft law

- 1.1 The draft law contains provisions intended to achieve fairness in the market for property and flood insurance in Ireland. In order to achieve this purpose, the draft law places certain obligations on insurance undertakings carrying out business in Ireland (hereinafter 'insurers') and confers certain powers upon the CBI.
- 1.2 There are two aspects of property and flood insurance provision that are covered by the draft law. First, the draft law prohibits insurers from discriminating, when offering property insurance policies, between (a) persons living in areas designated as being at low to medium risk of flooding (hereinafter 'affected persons'); and (b) persons living in areas which are neither at low to medium risk of flooding nor designated as being at high risk of flooding (hereinafter 'unaffected persons')². Insurers are prohibited from discriminating in their decision on whether to offer an insurance policy to an affected or an unaffected person, the price at which a policy is offered (unless the price is reasonably justified by the current risk profile of the property) and other terms on which it is offered³. The prohibition on discrimination does not appear to prevent insurers from calculating a higher premium for affected persons than for unaffected persons, subject to reasonable justification

¹ Council Decision 98/415/EC of 29 June 1998 on the consultation of the European Central Bank by national authorities regarding draft legislative provisions (OJ L 189, 3.7.1998, p. 42).

² See paragraph 3 of the draft law.

³ See paragraph 3 of the draft law.

based on the current risk profile of the property. Second, the draft law prohibits insurers from unreasonably refusing to offer an insurance policy to affected persons, or offering a policy at an unreasonable price or on unreasonable terms to them⁴. This prohibition also appears to be limited as insurers are permitted to offer a price which is reasonably justified by the current risk profile associated with a property.

- 1.3 The draft law confers upon the CBI the power to carry out an assessment of the manner in which an insurer deals with applications for insurance by affected persons⁵. This assessment may consider the extent to which the insurer in question acts in compliance with the draft law's prohibition on discrimination and the duty not to act unreasonably in its dealings with an affected person. The draft law does not set any further parameters for such an assessment or the circumstances in which the CBI might carry out such an assessment.
- 1.4 Where the CBI decides to perform such an assessment, the draft law confers upon the CBI the powers to issue directions to the insurer concerned to take steps or adopt or cease practices as it considers appropriate and necessary to ensure compliance by that insurer with its obligations under the draft law⁶.
- 1.5 With regard to enforcement, the draft law confers powers on the CBI to enforce such directions on insurers that fail to comply with them, by applying to the High Court for an enforcement order⁷. When granting the enforcement order, the High Court must also impose a fine on the insurer, unless the High Court determines that it would be unjust to impose such a fine. In such a case, it may impose a lesser fine or dispense with the requirement to impose a fine⁸.

2. General observation

This opinion does not address whether the draft law is compatible with Directive 2009/138/EC of the European Parliament and of the Council⁹. The ECB will only assess the provisions of the draft law that impact on the tasks of the CBI as a national central bank (NCB) and as a member of the Eurosystem and the European System of Central Banks (ESCB).

3. Conferral of new tasks on the CBI

- 3.1 The draft law extends the CBI's current supervisory responsibilities in relation to insurance undertakings and expands its consumer protection-related mandate to include the tasks described in paragraphs 1.3 to 1.5. In the context of a proposed conferral of new tasks on an NCB in the ESCB, it is necessary to assess such a conferral against the prohibition on monetary financing

⁴ See paragraph 4 of the draft law.

⁵ See paragraph 8 of the draft law.

⁶ See paragraph 9 of the draft law.

⁷ See paragraph 10(3) of the draft law.

⁸ See paragraph 10(5) of the draft law.

⁹ Directive 2009/138/EC of 25 November 2009 of the European Parliament and of the Council on the taking-up and pursuit of the business of Insurance and Reinsurance (OJ L 335, 17.12.2009, p. 1).

under Article 123 of the Treaty. For the purposes of that prohibition, Article 1(1)(b)(ii) of Council Regulation (EC) No 3603/93¹⁰ defines ‘other type of credit facility’, inter alia, as ‘any financing of the public sector’s obligations vis-à-vis third parties’.

- 3.2 As one of the objectives of the monetary financing prohibition, which may not be circumvented, is ensuring a sound budgetary policy of Member States¹¹, the task of financing measures, which are normally the responsibility of the Member States, and financed from their budgetary sources rather than from the NCBs’, must not be entrusted to NCBs by law. In order to decide what constitutes a form of financing of the public sector’s obligations vis-à-vis third parties, which can be translated as the provision of central bank financing outside the scope of central bank tasks, an assessment of whether the task to be undertaken by an NCB is a central bank task or a government task, i.e. a task within the responsibility of the Member States, needs to be carried out on a case-by-case basis. In other words, sufficient safeguards must be in place to ensure that circumventions of the objectives of the monetary financing prohibition do not take place.
- 3.3 As part of its discretion in the exercise of its duty, on the basis of Article 271(d) of the Treaty and Article 35.6 of the Statute of the European System of Central Banks and of the European Central Bank (hereinafter the ‘Statute of the ESCB’), to ensure that NCBs honour the obligations laid down by the Treaty, the Governing Council has endorsed safeguards of that kind in the form of criteria for determining what may be seen as falling within the scope of a public sector’s obligation within the meaning of Article 1(1)(b)(ii) of Regulation (EC) No 3603/93 or, in other words, constitute a government task as follows:

First, central bank tasks are in particular those tasks that are related to the tasks that have been conferred upon the ECB and the NCBs by the Treaty and the Statute of the ESCB. These tasks are mainly defined in Article 127(2), (5) and (6) and Article 128(1) of the Treaty, as well as Article 22 and Article 25.1 of the Statute of the ESCB.

Second, as Article 14.4 of the Statute of the ESCB allows NCBs to perform ‘other functions’, new tasks, i.e. tasks that are not related to tasks that have been conferred upon the ECB and the NCBs, are not precluded per se. However, new tasks that are undertaken by an NCB and which are atypical of NCB tasks or which are clearly discharged on behalf of and in the exclusive interest of the government or of other public sector entities should be considered government tasks.

Third, an important criterion for qualifying a new task as atypical of an NCB task or as being clearly discharged on behalf of and in the exclusive interest of the government or other public sector entities is the impact of the task on the institutional, financial and personal independence of that NCB.

In particular, the following aspects should be taken into account:

¹⁰ Council Regulation (EC) No 3603/93 of 13 December 1993 specifying definitions for the application of the prohibitions referred to in Articles 104 and 104b(1) of the Treaty (OJ L 332, 31.12.1993, p. 1).

¹¹ Article 123 of the Treaty also serves the objective of maintaining price stability and reinforces central bank independence.

- (a) whether the performance of the new task creates conflicts of interest with existing central bank tasks which are not adequately addressed and does not necessarily complement those existing central bank tasks. If a conflict of interest arises between existing and new tasks, sufficient safeguards to mitigate that conflict should be in place. The complementarity between a new task and the existing central bank tasks should not be interpreted broadly, so as to lead to the creation of an indefinite chain of ancillary tasks. Such complementarity should also be examined in relation to the financing of those tasks;
 - (b) whether without new financial resources the performance of the new task is disproportionate to the NCB's financial or organisational capacity and may have a negative impact on the capacity to perform properly the existing central bank tasks;
 - (c) whether the performance of the new task fits into the institutional set-up of the NCB in the light of central bank independence and accountability considerations;
 - (d) whether the performance of the new task harbours substantial financial risks;
 - (e) whether the performance of the new task exposes the members of the NCB decision-making bodies to political risks which are disproportionate and may also have an impact on their personal independence and, in particular, on the guarantee of term of office set out in Article 14.2 of the Statute of the ESCB.
- 3.4 On the basis of the criteria set out above, the following paragraphs assess whether the CBI's new tasks are in line with the monetary financing prohibition.

3.4.1 *New tasks related to the tasks conferred upon the ECB and the NCBs by the Treaty and the Statute of the ESCB*

The prudential supervision of insurance undertakings, and the terms on which they provide insurance policies, and the protection of consumers of financial services are not expressly mentioned among any of the basic central banking tasks listed in Article 127(2) or (5) of the Treaty or otherwise conferred upon the NCBs by the Statute of the ESCB. Indeed, under Article 127(6) of the Treaty, the Council may confer specific tasks upon the ECB concerning policies relating to the prudential supervision of credit institutions and other financial institutions with the exception of insurance undertakings. While Article 127(5) of the Treaty provides that the ESCB shall contribute to the smooth conduct of policies pursued by the competent authorities relating to the stability of the financial system, the ESCB contribution in this respect does not imply the conferral of any original competences on the ECB. Against this backdrop, the new tasks conferred on the CBI under the draft law are not related to the tasks conferred upon the ECB and the NCBs by the Treaty and the Statute of the ESCB. Consequently, as a next step, the conferral of these tasks by the draft law on the CBI must be closely scrutinised to assess whether they constitute government tasks and whether the related funding gives rise to monetary financing concerns.

3.4.2 *Tasks which are atypical of NCB tasks*

The draft law's conferral of tasks in relation to a specific area of insurers' activity may not be atypical of NCB tasks based on the understanding that these tasks do not interfere with the NCB's ESCB-related tasks and provided that those tasks are a complementary specification of:

(a) an NCB's existing role as prudential and conduct of business supervisor of insurance undertakings, a role which is currently fulfilled by numerous ESCB NCBs¹²; and/or (b) existing consumer protection tasks in the area of financial services, a role which is currently also fulfilled by numerous ESCB NCBs¹³. In this regard, it may be observed that a central bank's pursuit of legislative mandates in several areas may lead to inherent tensions between the multiple objectives it is bound to pursue, and require the central bank to balance competing interests in a manner more appropriate for a government.

The CBI is already responsible for the prudential supervision of insurance undertakings as well as supervision of their business conduct. It also has a broad consumer protection mandate in the field of financial services, including insurance¹⁴. Its responsibilities in this regard include ensuring compliance with, inter alia, the Consumer Protection Act 2007, the European Communities (Unfair Terms in Consumer Contracts) Regulations 1995 and 2000, European Communities (Distance Marketing of Consumer Financial Services) Regulations 2004 and the Non- Life Insurance (Provision of Information) (Renewal of Policy of Insurance) Regulations 2007. The Consumer Protection Code 2012, which the CBI adopted pursuant to section 117 of the Central Bank Act 1989 and section 61 of the Insurance Act 1989¹⁵, imposes binding obligations on, inter alia, insurance undertakings with respect to the manner in which they deal with customers and consumers. The Central Bank Acts 1942 – 2015 provide the CBI with investigatory, supervisory and enforcement powers designed to ensure that it can carry out its prudential and consumer protection mandates. In the case of the draft law, it specifically confers powers upon the CBI to monitor and take action in relation to insurers' conduct vis-à-vis consumers, i.e. potential discrimination or unreasonable actions, albeit in the particular sphere of property insurance.

Therefore, it follows that, given the CBI's mandate under national law for consumer protection in the field of financial services, and, more broadly, for financial stability, roles which are currently also fulfilled by numerous ESCB NCBs, the CBI's new tasks under the draft law may be argued to be not atypical of a central bank. For the same reasons, the tasks conferred by the draft law appear to be so closely related to the CBI's existing tasks and mandates that the overall objectives and interests to be pursued by the CBI remain largely unchanged. The new tasks would therefore not be regarded as being discharged in the exclusive interest of the government. The CBI is the sole supervisory authority for insurance undertakings and there is no indication that, in carrying out this function, the CBI would be acting exclusively in the interest of another public authority. Furthermore, the powers assigned to the CBI are in the

¹² See for example, paragraph 3.1 of Opinion CON/2012/61, paragraph 2.2 of Opinion CON/2011/46, paragraph 2 of Opinion CON/2010/33, paragraph 2 of Opinion CON/2010/4, and paragraphs 6 to 8 of Opinion CON/2003/23. All ECB opinions are published on the ECB's website at www.ecb.europa.eu.

¹³ See also paragraph 3.3.4.2 of Opinion CON/2016/54, paragraphs 4.3 and 4.4 of Opinion CON/2016/34, paragraphs 3.3 and 3.4 of Opinion CON/2015/54 and paragraph 3.1 of Opinion CON/2015/21.

¹⁴ See, in particular, sections 5A(1)(f) and 6A(2)(b) of the Central Bank Act 1942 (as amended).

¹⁵ In addition to the Investment Intermediaries Act 1995 and the Consumer Credit Act 1995.

interest of consumers buying financial products, i.e. property insurance in relation to properties at a low-to-medium risk of flooding, which the CBI also has a statutory mandate under Irish law to protect.

3.4.3 *Impact of the tasks on the independence of the CBI*

It must also be considered how the new tasks that the draft law confers upon the CBI may have an impact on the institutional, financial and personal independence of the CBI.

3.4.3.1 *Extent to which the performance of the new task creates conflicts of interest with existing central bank tasks*

The core obligations created by the draft law apply to insurers. As noted in Sections 3.4.1 and 3.4.2, the CBI is the competent authority responsible for the authorisation and prudential supervision of insurance undertakings. In addition, the CBI has a consumer protection mandate with respect to insurance undertakings operating in Ireland. Therefore, the CBI's new tasks under the draft law seem to complement its existing tasks. The CBI's exercise of its powers under the draft law would therefore not appear to create a conflict of interest with its existing central bank tasks.

3.4.3.2 *Extent to which the performance of the new tasks is disproportionate to the CBI's financial or organisational capacity*

The principle of financial independence requires that the Member States may not put their NCBs in a position where they have insufficient financial resources to carry out not only their ESCB-related tasks, but also their national tasks, from both an operational and financial perspective. Furthermore, when allocating specific new tasks to NCBs, each NCB concerned should be able to avail itself of additional financial resources so that these tasks may be carried out in a manner that will not affect the NCB's operational or financial capacity (including sufficient human resources) to perform its ESCB tasks. As such, it must be ensured that the CBI can avail itself of sufficient resources, including personnel, for the performance of assessments and the issuance of directions under the draft law, so that the CBI's capacity to perform its ESCB-related tasks is not affected. In this regard, the draft law does not specifically address how to finance additional expenses resulting from the CBI being granted additional powers. However, the ECB understands that the additional resources required by the CBI to exercise its powers under the draft law would be financed by the existing framework that finances the supervision of regulated financial service providers, i.e. by way of industry levies and, if necessary, a subvention from the CBI. It is understood that in order to fall within the existing framework, and therefore provide for the CBI to be reimbursed for the costs incurred in relation to the performance of its new tasks, the draft law will need to be categorised as a 'designated enactment' for the purposes of the Central Bank Acts 1942 - 2015¹⁶.

¹⁶ See sections 2 and 32D and Schedule 2, Part 1 of the Central Bank Act 1942.

3.4.3.3 Extent to which performance of the new task fits into the CBI's institutional set-up, in light of central bank independence and accountability considerations

The performance of the new tasks appears to be aligned with the CBI's institutional set-up. As mentioned in paragraph 3.4.3.1, the CBI is responsible for the prudential supervision of insurance undertakings and has a consumer protection mandate with respect to insurance undertakings, in the context of which the new tasks under the draft law are conferred.

3.4.3.4 Extent to which the performance of tasks harbours substantial financial risks

The draft law does not directly address the CBI's potential liability in the event of any legal action, application or other legal proceeding for damages in relation to the exercise of its powers under the draft law. Nonetheless, section 33AJ(2) of the Central Bank Act 1942 provides that specified officers and employees of the CBI are not liable for damages for anything done or omitted in the performance or purported performance or exercise of any of its functions or powers, unless it is proved that the act or omission was in bad faith. Furthermore, no appeal shall lie to the Irish Financial Services Appeals Tribunal or the High Court in respect of assessments carried out by the CBI, directions issued by the CBI or decisions by the CBI to seek an enforcement order. In that respect the CBI appears not to be exposed to substantial financial risks. However, it is for the Irish authorities to assess whether the draft law complies with Irish legal and constitutional principles in this regard¹⁷.

3.4.3.5 Extent to which the performance of the new task exposes members of the CBI's decision-making bodies to disproportionate political risks and has an impact on their personal independence

The performance of the tasks conferred under the draft law does not appear to expose the CBI's decision-making bodies to any disproportionate political risk or have an impact on their personal independence. As mentioned in paragraph 3.4.3.1, the CBI is responsible for the prudential supervision of insurance undertakings and has a consumer protection mandate with respect to insurance undertakings in Ireland.

3.4.3.6 Conclusion in relation to the draft law's effect on the CBI's independence

On the basis of the above, it may be concluded that the draft law does not adversely affect the CBI's institutional, financial and personal independence.

3.4.4 Conclusion regarding the compatibility of the draft law with the prohibition on monetary financing

The CBI's new powers to carry out assessments of the manner in which an insurer deals with applications for insurance by affected persons can be regarded as central bank tasks, in the sense that they would complement the CBI's existing mandate for consumer protection in the field of financial services. However, it should be noted that a central bank's pursuit of legislative mandates in several areas may lead to inherent tensions between the multiple objectives it is bound to pursue, and require the central bank to balance competing interests in a manner more

¹⁷ See also paragraph 3.3.4.3.4 of Opinion CON/2016/54.

appropriate for a government. It is understood that in order to ensure that the CBI is reimbursed for its costs incurred in relation to the performance of its new tasks, the draft law will need to be categorised as a 'designated enactment' for the purposes of the Central Bank Acts 1942 - 2015.

This opinion will be published on the ECB's website.

Done at Frankfurt am Main, 7 April 2017.

[*signed*]

The President of the ECB

Mario DRAGHI