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FINANCIAL SECTOR ASSESSMENT PROGRAM

May 2019

TECHNICAL NOTE—INSURANCE SECTOR REGULATION AND SUPERVISION

This technical note on Insurance Sector Regulation and Supervision for the Republic of Poland was prepared by a staff team of the International Monetary Fund. It is based on the information available at the time it was completed in April 2019.

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TECHNICAL NOTE

INSURANCE SECTOR REGULATION AND SUPERVISION

Prepared by
Monetary and Capital Markets Department

This Technical Note was prepared in the context of a joint IMF-World Bank Financial Sector Assessment Program (FSAP) mission in Poland during May 2018 mission led by Michael Moore, IMF and Loic Chiquier, World Bank. The note contains the technical analysis and detailed information underpinning the FSAP assessment's findings and recommendations. Further information on the FSAP program can be found at http://www.imf.org/external/np/fsap/fssa.aspx.

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Glossary

EIOPA	European Insurance and Occupational Pensions Authority
EU	European Union
EWS	Early Warning System
FICOD	Financial Conglomerates Directive
FO	Financial Ombudsman
FSAP	Financial Sector Assessment Program
FSSA	Financial Sector Stability Assessment
FSC-M	Financial Stability Committee—Macroprudential
GDP	Gross Domestic Product
G-SII	Global Systemically Important Insurer
GWP	Gross Written Premiums
IAIG	Internationally Active Insurance Group
ICPs	Insurance Core Principles
IDD	Insurance Distribution Directive (EU Directive)
IFRS	International Financial Reporting Standards
IGF	Insurance Guarantee Fund (Ubezpieczeniowy Fundusz Gwarancyjny)
LTG	Long-Term Guarantees
MCR	Minimum Capital Requirement
MiFID	Markets in Financial Instruments Directive
MMoU	Multilateral Memorandum of Understanding on Cooperation and Information Exchange
MoF	Ministry of Finance
MoU	Memorandum of Understanding
NBP	National Bank of Poland
OCCP	Office of Competition and Consumer Protection (Urząd Ochrony Konkurencji i Konsumentów)
ORSA	Own Risk and Solvency Assessment
PAS	Polish Accounting Standards
PFSA	Polish Financial Supervision Authority (Komisja Nadzoru Finansowego)
PRIIPs	Packaged Retail and Insurance-based Investment Products (EU Regulation)
SCR	Solvency Capital Requirement
SREP	Supervisory Review and Evaluation Process (Badanie i Ocena Nadzorcza)
TPL	Third-party Liability
WSE	Warsaw Stock Exchange

EXECUTIVE SUMMARY

This technical note provides an update and an assessment of the development of regulation and supervision of the Polish insurance sector since an assessment concluded in 2012. The note is part of the Poland 2018 Financial Sector Assessment Program (FSAP) and draws on discussions in Poland from January 8 to 20 and May 8 to 21, 2018.

Most recommendations of the 2012 FSAP insurance assessment have been implemented. The current FSAP did not carry out a detailed assessment of compliance with the IAIS Insurance Core Principles (ICPs). Nonetheless, it is clear that implementation of the EU Solvency II Directive in 2016 has significantly strengthened regulation and supervision, introducing risk-based capital standards, comprehensive insurance group supervision, and new requirements on the suitability of key persons, risk management, and controls. The supervision of intermediaries has also been strengthened in line with a 2012 FSAP recommendation, and further improvements were to take effect in late 2018. Unlike in many EU countries, Solvency II was implemented without significant increases in staff numbers.

There remains a need to address issues relating to the independence, resources, and legal protection available to the Polish Financial Supervision Authority (PFSA). As recommended in 2012, there is a need to strengthen the independence of the PFSA in relation to its governance and funding (see the detailed discussion of this issue, including the impact of legislative change effective January 1, 2019, in the Financial Sector Stability Assessment). In addition, the legal protection provided for bank supervision should be extended to insurance supervision.

The Solvency II changes appear well-embedded, without significant exemptions or transitional arrangements. Implementation was thorough and proportionate. With limited long-term guarantee business, life insurers have currently no need for the special measures adopted for such business in many EU countries. Requirements for additional reporting and for audit of the key (published) Solvency and Financial Condition Report were added to the Solvency II minimum requirements. No insurer has had a model approved for the calculation of capital requirements under Polish rules, although several started discussions with the PFSA and some foreign-owned insurers have had group-level models covering Polish business approved by the home supervisor. While the PFSA is seen as relatively conservative in its approach to internal models, it has adopted Solvency II standards with no additional requirements. Nonetheless, there is scope for the authority to update the industry on its expectations with regard to internal models.

The recent emergence of the first Polish financial conglomerate, which is headed by an insurer, poses supervisory challenges. The PFSA is well-placed to carry out effective supervision of the group, most of the elements of which are PFSA-supervised, and which is already subject to the wide-ranging Solvency II group supervision framework. Nonetheless, it is important that the PFSA complete the application of its comprehensive "supplementary supervision" requirements as soon as possible (the group was exempted from these in 2017). It also needs to finalize and implement arrangements to strengthen internal coordination amongst the sectoral supervisors of the group and to plan for conglomerate-wide risk assessment and supervisory work. (Initial decisions were taken by the PFSA in November 2018 to begin a process of addressing these recommendations). There are well-established supervisory college arrangements for the group, led by the PFSA, and these have been used to trigger the important process of conglomerate-wide recovery planning.

In respect to the selected other areas of the insurance framework that were reviewed, the findings highlighted strengths in the approach, with some scope for further development:

- The supervision framework is sound, with a particularly thorough process for off-site review and early response to emerging issues; the continuing central role of broad scope on-site examinations has been supplemented with a more flexible supervisory visit tool; the supervisory risk assessment framework (SREP) is comprehensive and feeds not just risk-based supervisory planning but dividend restrictions; there is scope to sharpen key messages to management, especially in examination reports; and for an enhanced supervisory model, at least for larger insurers, which involves increased focus on key strategic challenges, the adequacy of governance and controls, etc.

- As is appropriate given the importance of foreign-owned groups, the PFSA engages actively in cross-border supervision, both in leading the college of supervisors for the large group (its only home state responsibility) and as a college member for most foreign groups.

- Instances of customer mistreatment in recent years, particularly in unit-linked and motor insurance, have been met by a coordinated response by the authorities; business conduct regulation has been strengthened and was due to be further developed, in areas such as disclosures to customers, as a result of EU legislation; there is also scope for the PFSA to develop a stronger preventative supervisory approach to business conduct, in line with its statutory objectives; this may require enhanced processes to identify and assess risks to customers rather than to insurers (the main focus of SREP), more cooperation with the Office of Competition and Consumer Protection (OCCP) and Financial Ombudsman (FO); internal organizational changes should also be considered, taking into account the needs of other sectors. Strong leadership is required to ensure that the importance of business conduct supervisory work is recognized alongside and seen as complementary to and not subordinate to prudential work.

Market-wide risk monitoring is carried out, including annual stress testing, and insurance sector issues are considered within the financial sector macroprudential supervisory framework. Aside from the initiative to begin recovery planning with the largest group, the PFSA is waiting on (and contributing to) EU developments on insurance sector recovery and resolution planning; unlike in many EU countries, policyholders benefit from a compensation scheme that is comprehensive for compulsory lines, but which could be strengthened in respect to life insurance. In the absence of explicit policyholder preference in bankruptcy law, there is also need for further work, in life and non-life insurance, to ensure that assets covering technical provisions would be available in practice for the settlement of claims.

Table 1. Poland: Main Recommendations		
Recommendation	**Responsible Authority**	**Priority**
PFSA Independence and Resourcing		
• As was also recommended in the 2012 FSAP assessment, the Government should review legislation and practice to strengthen the independence of the PFSA in relation to its governance and financing arrangements, its ability to determine its internal organization and its recruitment and remuneration arrangements; it should also extend to insurance supervision the legal protection provided for bank supervision. Such a review should also consider giving the PFSA formal status in the determination of regulatory needs and priorities (see also the Financial Sector Stability Assessment, including its discussion of the impact of legislative change effective January 1, 2019).	MoF	High
• The PFSA should review its staffing numbers and skills requirements to determine where it will need additional resources to meet the challenges of supervising a developing insurance sector and to implement the recommendations of this FSAP.	PFSA	High
Solvency II Implementation		
• The PFSA should update and expand its 2015 publication on its concerns with the use of internal models; it could consider setting out a path to approval, including conditions that would need to be satisfied.	PFSA	Medium
• In the light of the recent issuance of IFRS 17 (Insurance Contracts), the authorities should give consideration to the possibility of wider use of IFRS by insurers for statutory financial reporting, taking into account the outcome of the EU IFRS adoption process and experience of other countries.	MoF	Low
Insurance Supervision		
• The PFSA should review aspects of its supervisory approach, in particular whether there is adequate reporting by insurers to support risk assessment of conduct of business, the need for more assessment of the home supervisor in the case of foreign-owned insurers and the scope for sharpening messages to senior management.	PFSA	Medium
• The PFSA should consider whether, at least in relation to larger insurers, their supervisory approach would be strengthened by greater focus—including in discussion with insurers—on strategy, business model, risk culture, etc., and on the capacity of management to ensure compliance with regulatory requirements in the future.	PFSA	Medium
Supervision of Groups and Financial Conglomerates		
• The PFSA should complete the application of its comprehensive "supplementary supervision" requirements to the PZU conglomerate as soon as possible (taking into account decisions made on supplementary supervision in November 2018); should finalize and implement arrangements to strengthen internal coordination amongst the sectoral supervisors of the group; and should plan for conglomerate-wide risk assessment and supervisory work.	PFSA	High

Table 1. Poland: Main Recommendations (concluded)

Recommendation	Responsible Authority	Priority
• The PFSA and other authorities as appropriate should consider the scope for improvements to the extent and timeliness of publicly available data on cross-border business into Poland by insurers based elsewhere in the EU.	PFSA, MoF	Medium
Conduct of Business and Intermediary Regulation		
• The authorities should review:		
➢ the overall approach to insurance conduct of business supervision across the relevant agencies with a view to ensuring that: respective responsibilities are well understood; there is no subordination of financial to conduct supervisory objectives; coordination between agencies is adequate; and that the PFSA leads on, and is resourced further to develop its preventative supervisory work; and	MoF, PFSA	Medium
➢ the powers available to the PFSA and OCCP for consumer protection work, which could be strengthened by the addition of powers to require redress and to accept enforceable undertakings.	MoF, PFSA	Medium
• In the light of such reviews, the PFSA should consider reform to its organization and supervisory processes, as necessary to ensure even closer focus on conduct supervision; for example, they should review whether to organize and staff conduct supervisory work separately from prudential supervision (but with close coordination).	PFSA	Medium
Financial Stability and Macroprudential Supervision		
• The PFSA should give high priority to recovery planning of the conglomerate group, in line with initiatives already taken, integrating work undertaken on the group banks.	PFSA	High
• The authorities should review the approach to insolvencies: in life insurance, the level of compensation, the readiness of the compensation scheme to intervene, and the availability of its assistance function; and for all insurance, the robustness of policyholder protection arrangements in a liquidation.	MoF, PFSA, IGF	Medium

INTRODUCTION[1]

A. Scope and Approach of This Note

1. This technical note provides an update and an assessment of the development of regulation and supervision of the insurance sector since an assessment concluded in 2012. The note is part of the Poland 2018 Financial Sector Assessment Program (FSAP) and draws on discussions in Warsaw from January 8 to 20 and May 8 to 21, 2018. The FSAP's overall conclusions and recommendations are set out in the Financial Sector Stability Assessment (FSSA).

2. The note focuses on key issues, with reference to international standards but without presenting a detailed assessment of Poland's observance. As an update to the full assessment of observance of the ICPs of the International Association of Insurance Supervisors (IAIS) carried out by the World Bank in 2012,[2] the note focuses on developments such as the implementation of the EU Solvency II framework in Poland from January 1, 2016. Unless stated otherwise, references in this note to the IAIS ICPs are to the version issued in October 2011, as revised in October 2013, November 2015, and November 2017. The institutional arrangements for financial sector regulation and supervision in Poland are presented in Section B.

3. The note draws on information supplied by the authorities and extensive discussions in Poland. Meetings were held with the Chairman, one Vice-Chairman and staff of the Polish Financial Supervision Authority (PFSA), the Ministry of Finance (MoF), the National Bank of Poland (NBP), the Chancellery of the Prime Minister, the Office of Competition and Consumer Protection (OCCP), the Financial Ombudsman (FO), the Insurance Guarantee Fund (IGF), selected insurance companies and intermediaries, industry and professional bodies, an auditing practice, and a rating agency. The PFSA provided extensive statistical and other information and shared anonymized examples of supervisory work.

4. The author is grateful to the authorities and private sector participants for their excellent cooperation. The preparation of this Technical Note benefited greatly from their readiness to share insights and information. The author is especially grateful to the staff of the PFSA for their close cooperation and support for the work of the FSAP.

B. Overview—Institutional and Market Setting

The Insurance Market

5. The Polish insurance sector comprises 60 insurance companies and one specialist reinsurance company. Twenty-seven are life insurers and 34 non-life. The latter includes one

[1] This technical note was prepared by Ian Tower (IMF external expert).

[2] Republic of Poland: Insurance Core Principles, Detailed Assessment of Observance of Insurance Core Principles, IMF and World Bank, November 2012. The findings of that assessment are summarized in the report of the 2012 FSAP (Republic of Poland: Financial Sector Stability Assessment, IMF Country Report No. 13/221, July 2013).

specialist reinsurance company that writes non-life business only. Composite insurers are not permitted, but many groups offer both life and non-life insurance through separate companies, typically structured as a non-life insurance company owning the life insurer (and other financial sector activities). Primary insurers may also write reinsurance business, where authorized to do so. The largest insurance group, PZU, which is state-controlled,[3] accounts for around one third of both the life and non-life insurance markets (2017, by gross written premiums (GWP)). There are 11 mutual insurers, accounting for under 5 percent of GWP.

6. There is a high degree of foreign participation. Foreign-owned companies, all from elsewhere in the EU, USA, or Canada (the specialist reinsurance company) account for around 50 percent of total GWP and total assets.[4] In addition, a number of insurers based in other EU countries participate in the Polish market via branches or through the freedom to provide services on a cross-border basis. Such business has been reducing, but branches and cross-border business together accounted in 2016 for GWP equivalent to 8 percent of the domestic market (i.e., companies incorporated in Poland), down from 11.2 percent in 2014. A further reduction has occurred in 2017 following the transfer of some foreign insurer branches' business to domestic companies.

7. Product range is limited compared with many European markets:

- In **life insurance**, unit-linked investment products, typically linked to dedicated investment funds managed by the insurer or within its group and with low levels of insurance cover, account for almost half of life insurance premiums. The remainder is protection business (term life insurance) with a small amount of endowment policies. Life insurance is not used extensively for retirement saving, and annuity business is minimal. Group business accounted for around one third of total life insurance GWP in 2017, although the mix varies greatly by insurer. Only around 30 percent was single rather than recurring premium business.

- The **non-life insurance** market is dominated by motor insurance (including compulsory third-party liability insurance (TPL)), which accounts for 63 percent of total non-life direct GWP (TPL insurance is also compulsory for farmers) at end-2017. Property is the second largest class of non-life insurance.

- **Accident and health insurance** may be written by both life and non-life companies (but by life companies only where incidental to life insurance) and accounts for around 13 percent of total insurance sector GWP. Coverage is mostly for accident (healthcare provision is substantially state-based in Poland). Credit insurance is limited to well-established products such as insurance of trade receivables, performance bonds, surety business, etc.

- **Reinsurance** is written by a number of insurers in addition to the one specialist company, but total reinsurance GWP are around 6 percent of the non-life total and negligible in life insurance;

[3] PZU SA Group (Powszechny Zakład Ubezpieczeń), which is 34.2 percent government-owned. See Box 1.

[4] Source PFSA: share of companies not falling within the definition of "companies with a majority of domestic capital", end-2017.

and this total includes some business structured and reported as reinsurance, but which is economically co-insurance (of larger corporate risks, to spread the risk among multiple Polish insurers). Most reinsurance cover obtained by Polish insurers is from international reinsurers, including those within the same group in the case of some Polish subsidiaries of European groups.

8. **Risks written by insurers in Poland are almost entirely domestic.** Insurers write only limited international business (the one specialist reinsurance company is an exception) and they have not opened branches or provided cross-border services in other EU countries on a significant scale. PZU Group includes operations in Latvia, Lithuania, Estonia (as a branch of the Lithuanian entity), and Ukraine. All these have significant local market share. However, their total premium income, almost all in non-life insurance, accounted for only around 7 percent of the PZU Group's total premium income in 2016.[5]

9. **Investment portfolios reflect a conservative investment approach.**

- Life insurers' investments are dominated by government bonds (around 70 percent of the total, excluding assets held for unit-linked business) and interests in investment funds.
- Securities lending is minimal (only significant amounts have to be reported to the PFSA and few insurers make reports).
- Investments related to unit-linked business are around 80 percent investment funds, the underlying assets being mostly equities and government and corporate bonds.
- Non-life insurers have a similar investment profile, but their assets also include significant equity and other interests in related undertakings, reflecting the typical ownership structure (non-life companies owning life companies etc.).
- Only a minority of insurers use a relatively small range of derivative instruments (particularly interest rate swaps).

10. **Distribution of insurance products is predominantly through agents.** The agent channel, which includes bancassurance, accounts for over 60 percent of GWP in both life and non-life insurance. There are some 31,000 agents (including banks), half of which act only for one insurer and the rest for more than one in at least one line of business ("multi-agents"). Brokers operate almost entirely in the wholesale market for non-life insurance and are required to act on behalf of the customer and to offer advice, which must in principle be based on a reliable analysis of a sufficient

[5] Source: PZU Group Annual Report, 2016.

number of offers.[6] Direct sales account for 30 percent of life insurance, but only 10 percent in non-life insurance.

Table 2. Poland: Numbers and Size of Polish Insurance Companies

	2013	2014	2015	2016	2017
Life: number	27	26	27	27	27
GWP (PLN bns)	31.3	28.7	27.5	23.8	24.6
Total assets (PLN bns)	101.4	105.3	102.8	103.2	104.7
Non-life: number	31	31	30	33	34
GWP (PLN bns)	26.6	26.3	27.3	32.1	37.8
Total assets (PLN bns)	65.9	73.2	77.5	82.0	92.0
Total number of companies	**58**	**57**	**57**	**60**	**61**

Source: PFSA data (national accounting standards basis).
The one specialist reinsurance company is included in the data for the non-life sector.
The data do not include business of branches or business carried out a cross-border basis from other EU countries.

11. Penetration is low by European standards, indicating scope for significant growth. Penetration rates in 2016 (premiums as a percentage of GDP), at 0.99 percent for life and 1.92 percent for non-life, were well below average for Europe generally (3.99 percent life and 2.73 percent nonlife), but in line with those for countries in Central and Eastern Europe.[7] Table 2 sets out the development of the insurance sector in recent years. Total assets of the sector at end-2017 were almost PLN 200 billion, equivalent to around 10 percent of GDP (compared with around 80 percent of GDP for the banking sector).

12. Recent performance of the sector has adversely affected by a number of factors:

- in life insurance, by developments in the customer perception of unit-linked insurance: having displaced endowments as the major investment product (particularly as customers sought higher returns), unit-linked business has suffered in recent years from volatile investment returns and from adverse publicity resulting from regulatory actions to address high surrender charges, which themselves in part reflect high costs of new business acquisition; sales of new unit-linked policies fell sharply in 2016 and while they picked up in 2017, the volume of total outstanding unit-linked business has continued to fall as policyholders take advantage of new freedoms to surrender policies with more limited charges than were applied in the past;

- in non-life insurance by:

    - strong competition in the motor insurance market, reportedly in part from foreign insurers accessing the market on a cross-border basis; and

[6] When the Insurance Distribution Directive (IDD) is implemented in October 2018, brokers will no longer be required by law to offer advice in large risks insurance.

[7] Swiss Re, Sigma Report, Number 3/2017.

  - upward pressures on claims for bodily injury and for "pain and suffering:" changes to Article 446 of the Civil Code in 2008 made it possible for "relatives" (undefined) of a deceased beneficiary to claim for pain and suffering, leading to a number of court actions and rulings that have increased the cost of claims—in particular a Supreme Court ruling in 2010 required that valid claims be paid where the death occurred prior to 2008.

  Partly because of regulatory action focused on ensuring the adequacy of premiums, insurers moved in the second half of 2016 to increase premium levels sharply.

- across the insurance sector, by costs associated with:

  - a series of major regulatory changes, including the implementation of Solvency II and other EU directives as well as domestic initiatives to improve consumer protection;

  - more intensive supervisory work by the PFSA, which, for example, issued recommendations on claims settlement practices of motor insurers and on motor TPL pain and suffering claims and which has undertaken supervisory work to assess compliance; and

  - enforcement action, by the PFSA and the OCCP.

  These developments have had an impact on cost and business volume, although market participants noted in discussion that they are also leading to improved risk management and treatment of policyholders, repairing damage to perceptions of the insurance product.

- by reduced returns on investment portfolios due to market developments; and

- by increased taxation (a tax of 0.44 percent of the assets of all financial institutions/groups with assets of over PLN 2 billion was imposed from early 2016).

13. The insurance sector nonetheless has remained profitable, while capitalization levels are high.

- Insurers in aggregate have recorded overall positive results, more so in life insurance, which has been achieving returns on equity of nearly 20 percent.

- Non-life profitability improved from less than 10 percent return on equity in 2015–16 to nearly 15 percent in 2017, reflecting mainly the increase in premium prices (technical results for motor insurance had been sharply negative before this).

- The aggregate solvency capital ratio for the sector (coverage of the Solvency II solvency capital requirement with eligible own funds) was 256 percent at end-2017 (life 320 percent and non-life 227 percent).

- The five Polish insurers included in the European insurance stress tests undertaken in 2016 by the European Insurance and Occupational Pensions Authority (EIOPA) showed relatively low exposures to the scenarios, including the "double hit" (prolonged low interest rate environment combined with falling investment markets).

Box 1. PZU Group

PZU is the largest Polish insurance group. The Polish government has a controlling interest of 34 percent, there are no other major shareholders and PZU SA is listed on the Warsaw Stock Exchange. The top company of the group, PZU SA, is a non-life insurance company. It holds investments in the group's life insurance, investment fund and pension fund management, healthcare services and banking entities in Poland and its insurance businesses in the Baltics and Ukraine.

Since 2015, the group has increased its interests in Polish banking and now holds controlling interests in:

- Alior Bank—25.2 percent acquired in 2015 (29.6 percent with inclusion of indirect holdings); Alior Bank itself acquired in November 2016 a part of the business of the Bank BPH: the now combined operations make Alior the 9th largest bank in Poland; and
- Bank Pekao SA—a 20 percent holding in the second largest bank in Poland, acquired from the Italian bank Unicredit in June 2017 (amounting to a 32.8 percent stake held jointly with PFR, the Polish Development Fund, with which PZU has a cooperation agreement).

The group's investments in banks are fully consolidated in the group's financial statements (prepared on an IFRS basis), resulting in an increase in total group assets from PLN 67 billion in 2014 to over PLN 300 billion at end-2017 (parent company equity—on a national accounting standards basis—increased from PLN 13.1 billion to 13.9 billion in the same period, although subordinated debt of PLN 2.25 billion was also issued soon after the acquisition of the Bank Pekao SA interest). They are treated as strategic investments in the Solvency II group capital adequacy calculations.

The group's solvency ratio was 247 percent at end-June 2017 (i.e., after completion of the Bank Pekao investment) which compares with a required minimum of 100 percent and a group target of 200 percent. The group has an A–rating from Standard & Poor's.

PZU published a revised strategy for development of the enlarged group in January 2018. A major strategic aim is to increase cross-selling of financial products within the group. PZU's insurance customers by number substantially exceed those of the banks.

14. Major risks of the insurance sector differ from those in many other European countries, with much lower exposure to market risk and to low interest rates.

- Polish life insurers have not written significant amounts of traditional savings business with high guarantees, while unit-linked business is written almost entirely without guarantees.

- There is significant exposure to interest rates through the bond portfolio (and particular exposure to any developments affecting the market price of Polish government securities), but the mismatch between average duration of assets and liabilities is lower than elsewhere in Europe.[8]

- The low volume of retirement savings business has resulted in limited exposure to longevity risk. Mortality risk is significant, if partially mitigated by diversified portfolios.

- The largest risk in life insurance, accounting for most underwriting risk and over 50 percent of total solvency capital requirements (SCR) at end-2017, is related to lapses of insurance policies.

15. A key risk in non-life insurance is to further extensions in the scope of civil liability. As mentioned, changes in the Civil Code, together with a growing readiness of policyholders to challenge claims payments and a range of court judgments, have resulted in claims inflation and uncertainty over how to price business. A particular uncertainty relates to the scope of liability for pain and suffering payments to relatives. A further Supreme Court judgment in March 2018 has extended insurers' liability so as to include cases of compensation for relatives of a beneficiary suffering persistent vegetative state (the 2010 judgment mentioned above had addressed only cases of death). However, the authorities have been working to address some of the uncertainty (for example, by creating a database of court judgments and through PFSA recommendations on claims settlement and actions to develop stress tests). The Ministry of Justice has been working on clarifications to the Civil Code.

16. There have been no insurance company failures since 2000. There were several failures of non-life insurers and of one life insurer in the 1990s as the private insurance market developed (the market is relatively young—before the 1990s, insurance was provided by two state-owned companies only). Five companies, all non-life insurers, have faced acute financial challenges in recent years, but all have recovered. All were small (none had market share of more than 2 percent).

17. The main source of interconnectedness with banks is through ownership links, including major investments by the PZU Group, as well as bancassurance. Bank deposits account for a negligible and reducing share of insurers' assets—reflecting lower interest rates as well as higher capital charges under Solvency II. Most significantly, the largest domestic insurance group, PZU, has made significant investments in Polish banks in 2015 and 2017 (see Box 1 above).

18. Bancassurance is mostly organized through agreements for banks to act as agents of insurance companies. There are also two (relatively small) joint venture insurance companies established by a partnership of Polish bank and foreign insurer. Some bancassurance has been structured as group insurance (with the bank acting as policyholder on behalf of a number of customers). However, the PFSA moved in 2014 to deal with the potential conflicts of interest in this business by recommending to banks that they not act as both policyholder and intermediary in

[8] The PFSA estimates that at December 31, 2016 for the life sector, the Macaulay durations of assets was about 5 years and of liabilities about 11 years, the average duration gap therefore being about 6 years.

relation to the same insurance contract and not receive remuneration from the insurer where acting as policyholder (for example in buying group insurance for employees, etc.).[9]

Regulatory and Supervisory Arrangements

19. The PFSA is the principal supervisory agency for the insurance sector. PFSA, which also supervises banks, credit unions and cooperatives and the capital markets, has responsibility for prudential supervision and conduct of business. It also licenses and supervises insurance brokers and carries out indirect supervision of agents via its supervision of insurance companies.

20. The PFSA has the status of a public administrative body. The PFSA itself comprises eight members including a full-time Chairman and two full-time Vice-Chairmen as well as representatives of the MoF, the Ministry of Economic Development, the Minister of Labor and Social Policy, the President of the NBP, and the President of the Republic of Poland. It is supported by the PFSA Office, the executive function of the Authority, with around 950 staff in total. Unlike in the case of bank supervision, PFSA and its employees do not enjoy explicit legal protection and immunity from suit for actions taken in the course of supervisory work on insurance companies or intermediaries.[10] They have not been subject to legal action in practice.

21. The PFSA is principally a supervisory authority and the MoF is responsible for preparing regulation. The PFSA does not issue regulations or other forms of binding requirements (although it may issue recommendations and guidelines—see below). The MoF leads on insurance regulation and is responsible for presenting government-proposed legislation to Parliament and for secondary legislation. Requirements are set out in laws or in MoF ordinances made under the relevant law.[11] The MoF has ten staff working on insurance sector policy issues. There is close cooperation between MoF and the PFSA. As well as working with the PFSA on major regulatory changes such as Solvency II implementation, MoF has incorporated PFSA initiatives into legislation (see footnote 9 for an example).

22. Other bodies share responsibility with the PFSA for insurance business conduct regulation:

- The Office of Competition and Consumer Protection (OCCP), an authority with responsibilities for economy-wide consumer protection, has enforcement powers in respect of insurance companies' and intermediaries' compliance with marketing and unfair contract terms

[9] See PFSA Recommendation U, 2014, addressed to banks. The key provisions of this recommendation in respect of the remuneration of the policyholder were subsequently incorporated into the 2015 Act on insurance and reinsurance activity (Article 18), which introduced a prohibition on such remuneration (excepting policies taken out by an employer on behalf of employees) and applied it not just to banks but generally.

[10] Under Article 133 of the Banking Law 2009, the PFSA and "persons carrying out banking supervision activities" are not liable for damage resulting from legitimate actions or omission of action connected with bank supervision.

[11] While there is a professional body for actuaries, the Polish Society of Actuaries, it has not issued technical standards in the area of insurance regulation.

requirements. The President of the Office may issue opinions for consideration by the Court in relevant proceedings.

- The Financial Ombudsman (FO) handles complaints against insurance companies (as well as other financial institutions) and has powers to impose financial penalties where an insurer is found not to be handling complaints fairly. It may also submit opinions to the Court hearing a relevant case, at the request of consumer or of the Court itself; and it may make a petition to the Supreme Court (as it did in the cases referred to above) where it has identified inconsistencies in case law.

23. Insurance work is carried out by various departments of the PFSA, reflecting in part a division of off-site and on-site supervisory work. The organization of resources aims to balance the need for an insurance-specific focus with the benefits of PFSA-wide functional areas.

- There are separate functions for licensing, off-site supervision, risk management and inspection. The licensing department also covers supervision of intermediaries.

- The PFSA-wide Legal and Enforcement and Market Practices Departments cover legal and enforcement work and surveillance and certain activities in relation to conduct risks.

- Unlike for banking supervision, there is no insurance regulation function. Responsibilities for regulatory policy, including cooperation with the MoF, are shared amongst departments.

Total staff involved in insurance supervision, including in PFSA-wide functions such as Legal, have increased from around 99 in 2011 to an estimated 106 at end-2017.

24. The PFSA is responsible to the Prime Minister[12] and its budget is approved by the MoF and Parliament. The PFSA's operating expenses are determined by government and funded from the budget, although expenditure is financed in full from fees levied from the regulated companies rather than from general taxation. Staff remuneration follows requirements set out by the Prime Minister rather than the PFSA itself. They should take account of market salary levels, but remuneration is in practice not aligned to private sector levels. PFSA must also obtain consent from government to its internal organization.

[12] Article 3 of the Act of 21 July 2006 on Financial Market Supervision. On January 1, 2019 an amendment to the Act entered into force enabling the PFSA to establish its budget independently. See the FSSA.

25. An insurance guarantee scheme provides compensation (limited to compulsory and life business) in case of an insurer's insolvency. On insolvency, the Insurance Guarantee Fund (IGF) (or Ubezpieczeniowy Fundusz Gwarancyjny), an independent agency,[13] satisfies claims:

- for compulsory motor and farmers TPL insurance and compulsory insurance of farm buildings: 100 percent up to the sum insured;[14] and
- for life insurance and "other compulsory insurance resulting from separate acts or international agreements ratified by the Republic of Poland:" 50 percent of eligible receivables up to EUR 30,000.

Compensation for life insurance and compulsory non-life insurance in case of insolvency is financed on an ex post basis, although writers of compulsory TPL also pay levies to fund other IGF functions. IGF also has an assistance role: to enable continuation of protection in case of risk of insolvency, it can make a loan to another insurer interested in taking over a portfolio; however, it can do so only for motor and farmers TPL insurance and only where the transferee insurer would comply with solvency requirements after the transfer.

26. There are arrangements for cooperation among the authorities. The Financial Stability Committee (FSC), established in 2008, coordinates actions related to financial stability and (since 2015) macroprudential supervision of the financial system, meeting as FSC-Macroprudential (FSC-M). FSC-M members are the President of NBP as Chairman, the Minister of Finance, Chairman of the PFSA and President of the Management Board of the Bank Guarantee Fund. The NBP provides support for the FSC. It has no direct responsibilities for the insurance sector, but under the Act on the National Bank of Poland has responsibility for the stability of financial system as a whole. It monitors and assesses potential stability risks related to insurance in its half-yearly published Financial Stability Review and in its reports to the FSC.

27. The PFSA is an active participant in European Union (EU) insurance regulatory work. Much of the insurance regulatory framework derives from EU legislation, including the solvency requirements (Solvency II) and the regulation of intermediaries, including the Insurance Distribution Directive (IDD), to be implemented in October 2018. The European Insurance and Occupational Pensions Authority (EIOPA) issues technical standards at the request of the European Commission as well as guidelines on a wide range of issues, including on the supervisory approach and the functioning of colleges of supervisors in cross-border supervision. EU legislation and EIOPA material also covers an increasing range of issues related to business conduct.

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[13] IGF also provides compensation in case of liability for personal injury or damage incurred by uninsured drivers or farmers and in case of liability for personal injury or damage (where there is also severe personal injury) by unidentified drivers.

[14] In the case of motor and farmers TPL, up to the minimum amount of the guarantee sum, i.e., in the case of personal injury the PLN equivalent of EUR 5 million per event and, in the case of damage to property, EUR 1 million per event—whatever the number of victims; both individuals and legal entities are covered under the IGF's protection.

FINDINGS AND RECOMMENDATIONS

A. Overview of the Implementation of the 2012 Recommendations

28. With the exception of issues relating to the independence and resources of the PFSA itself, most recommendations of the most recent assessment have been implemented. The 2012 assessment of insurance sector regulation and supervision noted that there was a high level of observance of the ICPs.[15] Most were assessed as observed or largely observed and only ICP 3 (the powers, resources and independence of the supervisory authority) was rated as partly observed. Most of the recommended changes in regulation and supervisory practice have been implemented, but there has been less progress on issues related to ICP 3.

29. The implementation of Solvency II has addressed many of the gaps identified in regulation, while intermediary supervision and regulation have also been upgraded.

- Solvency II has transformed the approach to capital adequacy, valuation of assets and liabilities, the regulation of investments, insurance group supervision, risk management and internal controls. All these issues were the subject of recommendations in 2012 (see also Section B).

- The PFSA has extended its on-site supervisory work on intermediaries, as recommended in the 2012 assessment. New EU legislation (the Packaged Retail and Insurance-based Investment Products (PRIIPs) Regulation) has introduced new, more extensive disclosure requirements attaching to the sale of relevant policies (see Section E below). An overhaul of EU legislation applying specifically to insurance intermediation was to take effect in October 2018.

30. There has been mixed progress in relation to the ICP3 recommendations, however. The finding was that the PFSA would benefit from the addition of further staff directed toward insurance supervision and more independence in setting budgets, salaries and organizational structure. The absence of a rule-making power and limits on legal protection were also noted.

- The governance and financing arrangements for the PFSA had not changed at the time of the detailed assessment. While the PFSA appears to be operationally independent from government, its governance and financing arrangements continue to expose it to the risk of undue political influence.[16] Together with its lack of freedom to determine its internal organization, they also potentially constrain its effectiveness, particularly because of the limitations on its ability to recruit and retain the staff it identifies as necessary to meet its objectives.

[15] The 2003 version of the ICPs was used in the assessment.

[16] However, on January 1, 2019 an amendment to the Act on Financial Supervision enters into force enabling the PFSA to govern its budget and exempting PFSA employees, but not the Chairman and Vice-Chairman, from the remuneration requirements set by the Prime Minister. See the FSSA for detailed discussion.

- The PFSA continues to lack rule-making powers. Under changes introduced by the 2015 Act on insurance and reinsurance activity, it may now make generally-applicable recommendations (Article 365), issued on a comply-or-explain basis, and is required to publish where an insurer declines to comply, together with the management's explanation of how it intends to achieve the objectives (Box 2 gives examples of recommendations issued to date.) However, the PFSA was already active in issuing non-binding guidelines, statements/positions and circular letters to insurers setting out its expectations. It appears to obtain a high degree of compliance with its expectations in practice, in part because of its general authority and because it also has a long-established power (now in Article 361 of the 2015 Act on insurance and reinsurance activity)[17] to impose enforceable recommendations[18] on an individual insurer. Nonetheless, the PFSA remains dependent on government for the establishment of generally-applicable binding requirements. While requests relating to insurance regulation have generally been met, this has not been the case for all PFSA requests for legislative change across the range of its responsibilities.

Box 2. Major Insurance Regulatory Developments (up to May 2018)

The Polish insurance sector has been subject to many regulatory changes in recent years, partly reflecting EU legislation but also domestic initiatives. Some major changes remain in course of implementation.

EU legislation (and implementing instrument in Poland):

- Solvency II Directive 2013: overhaul of valuation and solvency requirements and changes in governance, group supervision, reporting requirements etc. (Act on Insurance and Reinsurance Activity 2015)
- Insurance Distribution Directive 2016 (Act on insurance distribution 2017), effective October 1, 2018
- Packaged Retail and Insurance-based Investment Products (PRIIPs) Regulation (direct effect, from January 1, 2018)
- General Data Protection Regulation 2016 (GDPR) (direct effect, from May 25, 2018)

Domestic legislation:

- Act on insurance and reinsurance activity 2015
- Act on complaints handling procedures by financial service providers and Financial Ombudsman 2015
- Act on insurance distribution 2017 (to take effect 1 October 2018)

PFSA measures:

- Principles of Corporate Governance for Supervised Institutions 2014
- Guidelines on the Management of Information Technology and ICT Environment Security 2014
- Guidelines on Motor Vehicle Insurance Claims Settlement 2014

[17] While English translations of the law use the term "recommendations" in both cases, Article 361 and 365 use different Polish language terms, reflecting the different nature of the power.

[18] This power has in practice been used mostly for enforcement of findings of on-site examinations. The wording of Article 361 of the 2015 legislation gives the PFSA wider scope than the previous legislation for applying this power.

Box 2. Major Insurance Regulatory Developments (up to May 2018) (concluded)

- Guidelines on flood risk management in the insurance sector 2014
- Recommendation U on good practices in the field of bancassurance 2014 (addressed to banks)
- Guidelines on reinsurance/retrocession 2014
- Guidelines on insurance distribution 2014
- Guidelines on the process for technical provisions 2015
- Recommendations regarding the process of determining and paying compensation for non-pecuniary damage from contracts of third-party insurance of vehicle owner 2016 *
- Recommendation regarding the product management system 2016 *
- Recommendations on assessing product adequacy 2016 *

** issued under Article 365 of the Act on insurance and reinsurance activity 2015.*

- There has been no change in the position of the PFSA in respect of protection of the agency or its staff from legal action resulting from actions (or inactions) taken in the course of insurance sector supervision.

- Staff numbers have increased somewhat but not as much as might have been expected to meet the demands of the implementation of Solvency II and other major regulatory developments. Other EU insurance regulatory agencies have seen much larger increases in staff over a similar period. The PFSA is finding it hard to recruit staff with expertise related to Solvency II and has to rely on recruitment and training of graduate entrants to a greater extent that it would choose. Equally, as discussed below, the PFSA has successfully managed the transition to Solvency II, while also delivering its targeted supervisory program and stepping up its enforcement work.

31. **Recommendations related to powers to require the transfer of portfolios and to issues in relation to the winding-up of insurers have not been addressed.** Powers to enforce transfers are not a requirement of the ICPs. Their use in practice is constrained by the need for availability of a willing transferee. The issues with insolvency, where processes in Poland have not been tested by a recent failure, continue to require some attention—as discussed below in Section F below.

32. **A summary of the FSAP 2012 recommendations and the actions taken since then are set out in the Annex to this note**. It is recommended that:

- the Government of Poland review relevant legislation and practice to strengthen the independence of the PFSA in relation to its governance and financing arrangements,[19] its ability to determine its internal organization and its recruitment and remuneration arrangements; and that it also extend to insurance supervision the legal protection provided in law for bank supervision; such a review should also consider giving the PFSA formal status in the

[19] See also footnote 16 above and the FSSA for developments subsequent to the timing of the main work of this assessment.

determination of regulatory needs and priorities (see also the Financial Sector Stability Assessment);

- the PFSA review its staffing numbers and skills requirements, as it has done in respect of other areas of its responsibilities, to determine where it may need additional or different resources to meet the challenges of a developing insurance sector and to implement effectively the recommendations of this FSAP.

B. The Implementation of Solvency II

33. The implementation of Solvency II has changed most aspects of prudential regulation, aligning it more closely to the IAIS ICPs. It has resulted in more risk-based capital standards, extensive new requirements on the valuation of assets and liabilities, a new approach to the regulation of insurers' investments, a comprehensive new approach to group supervision and new requirements on the suitability of key persons and on risk management and internal controls. Box 3 maps the changes to relevant ICPs (at a high level, as observance of the ICPs is not being assessed).

34. The changes appear to be already well-embedded, without extensive exemptions or transitional arrangements. Although the main EU requirements were enacted only in 2014 (taking effect on 1 January 2016),[20] both the PFSA and insurers benefited from the EU-wide preparatory arrangements put in place by EIOPA[21] as well as aspects allowing for a proportionate approach.

- The PFSA notes that with some continuing exceptions, which are being addressed, the quality and timeliness of reporting is adequate.

- Although it was unclear whether all insurers would meet the new minimum solvency requirements, and one failed to do so initially, all now are compliant (as at May 2018). Given the nature of life products, no insurer needed long-term guarantees measures, i.e., the transitional and other arrangements designed to limit the impact of certain Solvency II requirements (see Box 3).

- Only one insurer benefits from the exemption from certain requirements (mainly capital adequacy but excluding governance) available to smaller mutual insurers. The PFSA has not granted exemptions to individual insurers on either the scope or frequency of reporting requirements.

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[20] The main implementing legislation, the Act on insurance and reinsurance activity, was enacted in September 2015.

[21] These covered (i) business organization and risk management; (ii) forward-looking assessment of own risks (FLAOR)—now ORSA (Own Risk and Solvency Assessment); (iii) pre-application for internal models; and (iv) reporting.

- Regarding proportionality, the PFSA has not objected to smaller insurers meeting requirements on key functions by having the same person hold more than one function (except for the internal audit function, which may not normally be combined, in line with Solvency II).[22]

35. The authorities have added to the minimum requirements of Solvency II in some areas.

- Insurers are required, for example, to report compliance with the SCR quarterly rather than annually as in Solvency II (which requires quarterly reporting on compliance only with the Minimum Capital Requirement (MCR)).

- The key report that all insurers covered by Solvency II must publish annually—the Solvency and Financial Condition Report (SFCR)—is subject to an audit requirement.

- The PFSA also published guidance and recommendations on various issues related to or interpreting Solvency II requirements, including 31 detailed recommendations on insurers' approach to product management[23] and guidance on reporting requirements.

36. In addition, minimum solvency requirements are supplemented by dividend restrictions. Minimum required levels of coverage of SCR and MCR have been set in line with Solvency II. However, the PFSA also sets expectations each year on the levels of coverage which it expects (although cannot legally require) insurers to meet if they are to pay dividends. These are treated by insurers as the effective minimum. For 2018, they are 150 percent of SCR for non-life insurers and 175 percent for life.[24] In common with supervisory authorities in most EU countries, the PFSA has not to date required any insurer (or insurance group) to hold additional resources as a capital add-on, as provided for in the defined circumstances set out in Solvency II and the Polish legislation.[25]

37. No insurer is yet using a model to calculate solvency under Polish requirements, at solo or group level. The PFSA entered into discussions with many insurers during the preparations for implementation of Solvency II (under EIOPA's pre-application process) and there were seven open discussions as at May 2018.[26]

[22] Article 271 of the Commission Delegated Regulation (EU) 2015/35 of 10 October 2014 supplementing Directive 2009/138/EC of the European Parliament and of the Council on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II)

[23] See: Recommendations for insurance companies regarding the product management system, PFSA, March 2016.

[24] See PFSA publication: PFSA's position on the dividend policy of cooperative banks and associates, insurance and reinsurance companies, pension funds, brokerage houses and investment fund companies in 2018 (December 2017).

[25] Articles 270 and 376 of the Act on insurance and reinsurance activity 2015.

[26] No insurer has applied for use of undertaking-specific parameters in the calculation of its SCR under the standard approach (Article 252 of the Act on insurance and reinsurance activity 2015).

Box 3. Solvency II and the Insurance Core Principles (ICPs)

Solvency II implementation is relevant to compliance with many of the ICPs:

- ICP 9 (Supervision): Solvency II greatly extends the range of reported financial information available to the PFSA for supervisory purposes; it has also required the PFSA to extend its supervisory toolkit with a more flexible approach to on-site supervisory work.
- ICP 14 (Valuation): valuation of assets and liabilities for solvency purposes must now be undertaken on a consistent, whole balance sheet and (reflecting the generally market consistent approach of Solvency II) economic basis; no insurer needed the transitional and other arrangements designed in particular to dampen the impact of a market consistent approach on long-term guarantee business*.
- ICP 15 (Investments): a "prudent person approach" is now required rather than detailed limits on types of investments; detailed reporting of actual portfolios is required and, while there has not been migration to higher risk investments, the PFSA has challenged insurers on particular investments and is working with EIOPA on issues with the interpretation of the scope of permitted derivatives.
- ICP 19 (Enterprise-Wide Risk Management): Solvency II has introduced new risk management standards and a requirement on insurers to develop Own Risk and Solvency Assessments (ORSA).
- ICP 17 (Capital adequacy): the approach is now substantially based on the impact of stress (by each risk category), with new requirements for operational risk capital, solvency control levels (SCR and MCR) and the application of solvency requirements at group level.
- ICP 20 (Disclosure): there is now a requirement for annual publication by all insurers of a Solvency and Financial Condition Report covering specified information with an audit opinion.
- ICP 23 (Group supervision) and 25 (Supervisory cooperation): Solvency II establishes an extensive regime for insurance group supervision and strengthens prior arrangements for supervisory colleges.

In addition, Solvency II has helped address the standards on governance and controls in ICPs 5, 7 and 8—insurers must now have control functions (risk, actuarial, compliance, internal audit) headed by fit and proper persons, with appropriate oversight by management and supervisory boards. Role holders must be notified to PFSA, and chair and risk management member of the management board are subject to prior PFSA approval.

* Without special measures for such business, many EU life insurers had been expected not to meet Solvency II requirements. Adjustments were developed, some temporary, as well as measures on equity risk. Poland is one of only eight EU countries not making use of any of these measures (See: EIOPA Report on long-term guarantees measures and measures on equity risk, 2017).

38. The PFSA provided early feedback to potential model applicants. It also fed back (at a high level) to the insurance sector generally[27] on its reservations over the ability of insurers to meet Solvency II requirements on the use of models in the Polish context. Broadly, its concerns related to the adequacy of available data, taking into account the relatively short history of private insurance in

[27] PFSA publication: List of critical errors in internal models of insurance undertakings, 2015.

Poland and the extent of reliance proposed by insurers on expert judgment and on proprietary models, for example for catastrophe risk.

39. Some foreign-owned insurers have nonetheless been permitted by their group supervisors to use internal models for the group SCR, including their Polish business. As at end-2017, four groups had such models approved and one other group planned to apply mid-2018. So far, no foreign group has applied to extend its application to include the use of a group model also to meet local Polish requirements. In the case of applications to use a model at group level, decisions are taken jointly by the group supervisor and other concerned supervisors (those supervising insurers proposing to use the model to meet local requirements). The PFSA has therefore not been a party to the four decisions made to date, although it has been kept informed and given an opportunity to provide input.[28] However, one insurance group was (at the time of the FSAP) in the early stages of preparing an application to extend use of a group model to the Polish insurer.

40. The PFSA's approach to internal models is prudent but comes with some potential costs. The PFSA is open in principle to the use of internal models. It participates in EIOPA expert work on models and maintains a small team of staff, now integrated with its on-site inspection function, with expertise. There are advantages in setting the bar high and learning from the experience of others in the early stages of model usage. However, there may also be downsides:

- The PFSA may be disadvantaged by not working closely with insurers to address its concerns over models, using the approval process to incentivize improved risk measurement and management.

- Lacking active engagement on models, it has been unable to retain all the expertise in risk measurement and management practices that will benefit its general supervision as well as potential future models' approvals.

- It may also be disadvantaged by lack of involvement in the decision-taking process for groups, a key dimension to Solvency II's emphasis on improved group supervision and cross-border supervisory cooperation.

- From Polish insurers' perspective, the PFSA's approach, perceived as conservative, may have resulted in extra cost, including for the foreign-owned insurers the need to maintain parallel systems for local and group requirements. Equally, there are costs in development and maintenance of a model and a key driver for insurers is whether there are savings on solvency capital requirements from using an internal model, which may not always be the case depending on the nature of the business.

[28] Exceptionally in the case of the application planned for mid-2018, the PFSA was being closely consulted on the issues at the request of the group supervisor (because of the materiality of the Polish business); however, PFSA will not be involved in the decision-making.

41. It would be appropriate for the PFSA to update its expectations of internal models and even to establish a path to future model approvals. The PFSA already writes annually to insurers remaining in the pre-application process seeking updates to their plans. It is open to discussions with insurers considering the use of models covering Polish business, at local or group level. However, on the evidence of the FSAP team's discussions with industry, the PFSA is seen as more antipathetic to internal models than it may actually be. It would be appropriate and timely for the PFSA to update and expand its 2015 publication on its concerns with internal models. It could consider setting out a path to approval, including conditions that would need to be satisfied.

42. The PFSA has been reviewing insurers' Own Risk and Solvency Assessments (ORSAs) and is planning increased feedback. Under the legislation implementing Solvency II, insurers are required to develop an ORSA.[29] The PFSA reviews these in the course of its supervision. Results, as in other EU countries, have been mixed so far with over-reliance in many cases on regulatory requirements at the expense of the development of the insurer's own view of risk and solvency. The PFSA rightly wants to avoid prescribing how ORSAs should be developed and to avoid deterring insurers from recognizing in ORSAs where higher capital is required. It has nonetheless been providing feedback to individual insurers, starting with those whose ORSAs have the most significant shortcomings. The process was to be extended to all insurers. In addition, the PFSA was planning general feedback in a letter to all insurers. It is advised to consider publication of such material.

43. The impact of Solvency II implementation appears generally positive. While, as in other EU countries, costs were high, the improvements in risk measurement and management appear to have been appreciated by insurers. Risk governance standards have been raised, including through the requirements on control functions. There has not been a major impact on public perceptions of insurance, which have been dominated, as mentioned, by the issues in motor and unit-linked insurance. The publication in mid-2017 of the first set of insurers' SFCRs, including for many the first solvency numbers on the new basis, did not attract significant press or other stakeholder discussion.

44. Solvency coverage ratios were substantially changed, indicating the limitations of the previous approach as a risk-based measure of capital adequacy. As Table 3 shows, the impact differed between life and non-life insurance, although the aggregate data also hide differences in the impact on individual companies, while for all mutual companies, solvency coverage ratios declined significantly as they became subject to the same regime as corporate insurers. Generally, for life insurers, lower technical provisions were the key driver of increased aggregate coverage ratios. In non-life insurance, higher capital requirements offset the effect of lower technical provisions leading to reduced coverage ratios.

[29] Article 63 of the Act on Insurance and Reinsurance Activity 2015.

Table 3. Poland: Solvency Ratios Before and After Solvency II Implementation
(percentage coverage of minimum requirements, in aggregate)

	End-2015	2016 (January 1)	End-2017
Life insurers	274	338	320
Non-life	380	222	227
Total	**328**	**266**	**256**

Source: Polish Financial Supervisory Agency.

45. There have also been changes in business model but more particularly in the use of risk management techniques. Increased reinsurance (in non-life insurance) has been accompanied by reductions in investment risk, including through greater diversification of assets such as bank deposits. Capital quality remains high: while 17 insurers had subordinated debt included in their own funds in the calculation of capital adequacy as at the end of 2017, including subordinated bonds issued by PZU Group, the total share of such debt in own funds was only 4.6 percent and common equity continued to account for most own funds.

46. For statutory reporting, insurers continue to use Polish Accounting Standards (PAS) and International Financial Reporting Standards (IFRS) are used only at group level. All Polish insurers choose to use PAS for statutory accounting at company level, including audited financial statements, even where IFRS are used for group level reporting (by PZU, which is subject to Warsaw Stock Exchange (WSE) listing requirements, and many parents of foreign-owned insurers.) The PFSA continues to monitor insurers' financial information on a PAS as well as a Solvency II basis. The PAS numbers differ significantly from the Solvency II measure, which generally results in lower technical provisions.[30] The reasons for the differences and the amounts are, however, disclosed in SFCRs, helping stakeholders with their interpretation and there is no evidence yet of confusion due to the differing approaches.

47. Wider use of IFRS by insurers should be considered for the future. With issuance of IFRS 17 (Insurance Contracts), due for implementation in 2021, there is now a final set of IFRS applying to insurers.[31] The issues and implications of extending the use of IFRS for statutory reporting are complex, however. The divergence between regulatory and statutory reporting would be narrowed: like Solvency II, valuation under IFRS (including IFRS 9) is generally based on current market prices, while IFRS 17 shares with Solvency II a prospective approach to valuation of insurance

[30] For example, as at end-September 2017, life technical provisions were 30.2 percent lower on a Solvency II basis, nonlife 50.7 percent lower and the total 37.7 percent lower. As noted, capital requirements are substantially higher on a Solvency II basis.

[31] Issued by the International Accounting Standards Board in May 2017, IFRS 17 sets out principles for the recognition, measurement, presentation and disclosure of insurance contracts. It takes effect in January 2021 (with restated 2020 accounts). Its use in Poland is subject to adoption at EU level, the process for which is under way.

liabilities. The experience of implementing Solvency II, including that resulting from the requirement for audit of the SFCR, arguably equips Polish insurers well for wider use of IFRS.

48. However, transitional costs could still be disproportionately high, especially for smaller insurers. It would also be important to explain to stakeholders the impact, including the implications of reduced technical provisions, if this were to be the result. There would be wide-ranging tax implications. Nonetheless, given the potential benefits, the authorities should in due course give consideration to the issues, taking into account the experience of countries where IFRS are already more widely used.

49. It is recommended that:

- the PFSA update and expand its 2015 publication on its concerns with internal models; it could consider setting out a path to approval, including conditions that would need to be satisfied; and
- in the light of the recent issuance of IFRS 17, the authorities give consideration to the costs and benefits of wider use of IFRS by insurers in Poland, taking into account the outcome of the EU adoption process and experience of other countries.

C. Insurance Supervision

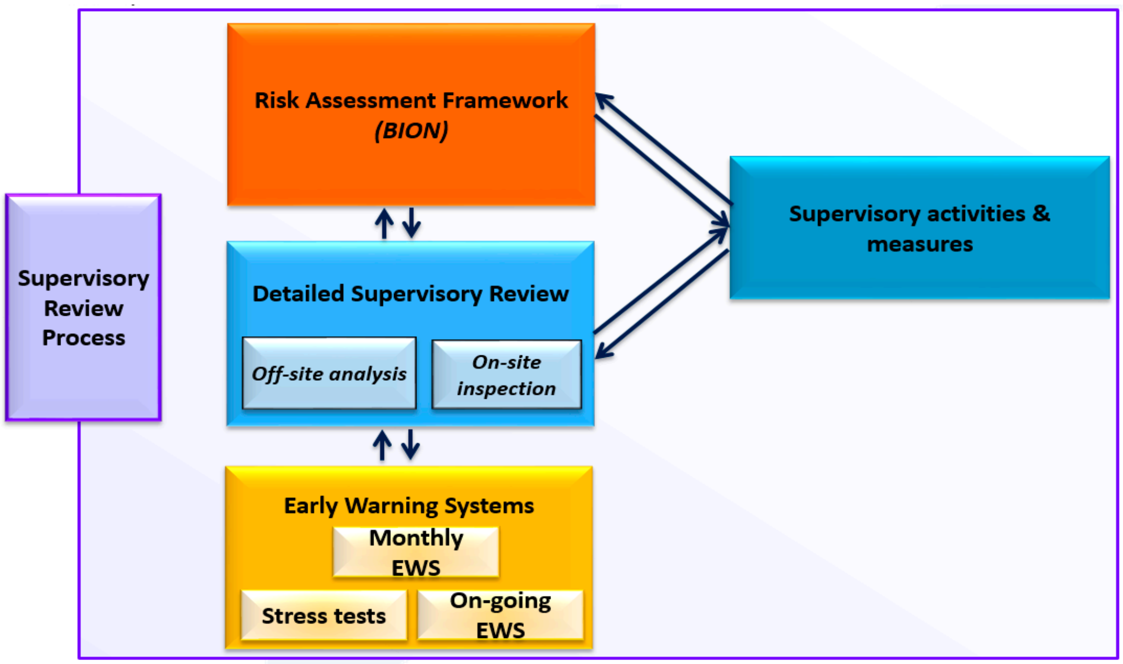
50. The PFSA has a well-established, transparent and thorough approach to insurer and intermediary supervision, which has been further strengthened by the implementation of Solvency II. There are separate processes (and staff) for reviewing and responding to insurers' regular reports (and for other off-site work) and for inspections. As mentioned, the PFSA now undertakes supervisory visits (shorter focused on-site work) in addition to full inspections. The overall process for insurers is set out in the Figure below. The main elements of the approach are published.

51. The off-site supervisory approach involves regular thorough analysis, reporting upwards within the PFSA and supervisory action, geared in part to triggers aimed at promoting early intervention.

- A key output is an internal report evaluating the extensive quarterly reported information at group and solo insurer levels, including financial information on a PAS basis and solvency. There is monthly reporting also—referred to as the Early Warning System, EWS. The monthly information received is less detailed and covers individual insurers only and not groups. The PFSA nonetheless estimates the likely change in SCR coverage based on changes in key financial information since the most recent quarterly report.
- Reports have to be produced on each insurer according to set templates and deadlines and with identified supervisory actions for higher risk issues, some based on specific triggers (including SCR coverage).

- The reports are escalated and discussed at regular management meetings, including the weekly senior management meeting of all senior staff involved in insurance supervision across the PFSA, which is chaired by the PFSA's Vice-Chairman responsible for the departments undertaking off-site insurance supervision.

Figure 1. Poland: PFSA's Supervisory Framework



Source: Polish Financial Supervisory Agency.

The approach is extensively automated, but supervisors are expected to make judgments on the significance of developing risks. Examples of where they have done so were reviewed as part of the FSAP work.

52. Other off-site supervisory work includes regular stress tests and cross-firm analysis.

- The PFSA's Risk Monitoring Department carries out annual cross-firm SCR reviews (in 2017 such a review concerned mainly Loss Absorbing Capacity of deferred taxes, lapse risk and the look-through approach to investments).

- It also manages stress tests, which supplement the SCR regime with a range of annual tests, including at least one particularly severe scenario (such as in 2017, for non-life insurers, incidence of a major catastrophe combined with a reinsurer failure).

- Results of stress tests, which are applied as relevant to all insurers, and cross-firm analysis are taken into account in the supervisory review and risk assessment (SREP).

- They are used mainly to inform discussions with management on risk management and how they would respond to stress. The PFSA, for example, has also required additional stress tests for insurers which had not passed a particular stress test or has entered into dialogue with an insurers' management which has led to actions such as insurers planning to raise additional capital in stress situations.

- Stress testing has also been used to evaluate the impact of business conduct regulatory action (in the case of the surrender penalties on unit-linked insurance—see Section E below).

53. On-site inspections are similarly carried out on a structured basis with immediate feedback to management as well as a detailed report. Inspections are scheduled for up to 60 days (the maximum prescribed by law). They cover quantitative issues, for example in-depth reviews of reserves adequacy, as well as management and controls. Feedback is provided at a closing meeting. The inspection report itself focuses in large part on identifying areas of non-compliance, but also highlights broader areas of risk where action is required, but no requirements have as yet been breached. The main areas of concern and required actions are in addition sent separately to management in a recommendations letter as is notification of sanctions to be imposed by the PFSA.

54. A key part of the process is the preparation of a risk assessment under the SREP framework.[32] Comprehensive risk assessment is carried out once a year, again following a structured process and a methodology that is reviewed and updated annually and published on the PFSA's website (it applies, on a tailored basis, to all sectors supervised by the PFSA and is generally referred to as by the Polish name BION—Badanie i Ocena Nadzorcza). The approach draws on both financial reporting, applying a large number of ratios, and on information about the insurer's management and controls. A key input is a detailed self-assessment which insurers themselves are required to develop, in response to an extensive questionnaire, and submit to the PFSA. Market participants commented that this is a thorough process that highlights areas of non-compliance with key regulatory requirements.

55. The final output of SREP is a scored assessment that takes into account the impact of the insurer in case of failure and which is shared with insurers, with required actions identified.

- Risks are scored individually taking into account both the exposure and the quality of risk management, as are capital adequacy and governance (covering business model, control functions etc.). There are four scoring categories: High, Medium High, Medium Low and Low; individual elements are weighted in the calculation of overall scores.

- Impact is separately scored using the same four-point scale, measured in the first instance by market share, but subject to override for the particular features of the individual insurer, where

[32] This discussion is based on the PFSA publication: Methodology of supervisory review and assessment (SREP) for insurance and reinsurance undertakings (Assessment for 2016).

the PFSA considers that the score would otherwise not reflect the possible influence of financial problems and potential bankruptcy of the insurer on the wider financial market.

- The product of impact and risk assessment drives the intensity of the supervision to be applied to the insurer (again, four categories from High to Low); there are guidelines on supervision action for each category. There was only one insurer in the High category as at the start of 2018.
- There are no peer groups for risk assessment purposes (the PFSA has not identified useful groupings). For the one major domestic group PZU, the group-wide risk assessment is developed through the process of the EU college of supervisors (see below).
- The PFSA shares the SREP assessment and required actions with management and may hold meetings with them, at least in the case of higher risk insurers. Insurers may also request information on the justification of SREP grades. SREP assessments are not published.

Insurers confirmed in discussions with the FSAP team that management give close attention to the SREP output, in part because the PFSA's dividend policy (see Section B above) links dividend payments to minimum SREP scores as well as to the level of capital adequacy and performance.

56. In relation to insurance intermediaries, there are separate approaches to agents and brokers.

- The PFSA at present follows an indirect approach to agent supervision (see Section E on changes from October 2018). Issues relating to insurers' selection of and controls over agents are covered in the insurer supervision framework, including SREP, but for on-site supervision, the PFSA undertakes special visits to those insurers (the large majority) which use agents.
- Similarly, for brokers, which are subject to direct PFSA supervision, there are specialist on-site inspections, aimed at verifying compliance with regulatory requirements. Brokers in addition have to submit regular reports to the PFSA but are not covered by the SREP risk assessment framework.

57. The PFSA's supervisory work includes the assessment of whether key individuals are fit and proper, although insurers have the main responsibility of assessing individuals.

- While the PFSA does not prior approve the appointment of key persons generally, it does approve the chairman and risk management member of the management board of insurers (i.e., the chief executive and chief risk officer).
- All defined role-holders have to be notified to the PFSA and it checks on qualifications etc. and assesses suitability for the particular role. It may also meet with appointees, as it did with many actuaries on the introduction of the Solvency II requirement for an actuarial function headed by a fit and proper function holder.

- Proposed chairs of the management board are invited to a meeting of the PFSA board to respond to questions before the approval decision is made. The PFSA has in practice issued decisions to refuse approval to appoint an individual as a member of the management board.

- The PFSA has a power to dismiss all key function holders, including members of the management board or supervisory board.

- Issues with key persons are also considered in the SREP assessment.

58. Various issues were discussed during the FSAP on the PFSA's supervisory approach:

- Whether it provides for sufficient coverage of on-site inspection work, taking into account limited PFSA resources. There is no minimum required frequency of inspections. An annual inspection plan is prepared on risk-based principles, taking into account off-site findings (including the SREP assessment), stress tests, the insurer's impact, etc.; 12–15 inspections are being carried out annually on insurers and around 10 supervisory visits; some 15 inspections related to agent oversight; and about the same number of broker inspections. Each insurer has a 40 percent chance of a visit each year. There is no impact override—i.e., no provision for the largest insurers receiving a minimum coverage of on-site work each year, simply to reflect their impact, whatever the risk assessment.

- Whether the approach, including SREP, covers business conduct issues as extensively as prudential. The two dimensions are integrated, reflecting the scope of the PFSA's responsibilities. Reflecting its origins, the SREP framework is structured around financial risks (for example, conduct risk is generally considered under operational risk, defined as risk of loss to the insurer rather than detriment to customers); and there is no overall score identifying the extent of net risk to customers posed by an individual insurer based on inherent risks (the insurer's products, customers, choice of distribution channel etc.) and relevant processes, controls, governance etc; nonetheless, it was clear from FSAP discussions that PFSA supervisors do assess conduct risks in some depth, drawing on information from other PFSA departments and using the SREP framework to trigger detailed review.

- Whether there is sufficient reporting by insurers to PFSA, on conduct risks in particular: there are extensive data on complaints (to the insurer, to the FO and to the PFSA itself), while the detailed new reporting required under Solvency II gives some insights into conduct risks. More specific reporting on insurers' products, customers, choice of distribution channel, etc., should be considered.

- Whether there is sufficient scope for judgment in formulating the risk assessment: in addition to many quantitative elements, there are a number of rules in SREP which constrain scoring (for example, the overall operational risk score is constrained by the score for relations with customers); there is, however, scope for adjustment of scores as part of the development of the SREP output, the work on which includes extensive internal discussions and challenge, including at decision-taking panels.

- Whether there is enough emphasis on the quality and extent of home supervision and PFSA's relationship with the home supervisor (taking into account the importance of foreign-owned insurers in Poland). SREP covers assessment of the owner's oversight of the Polish insurer, but there is no assessment of the home supervisor, taking into account EIOPA's assessments of non-EU supervisors.

- Whether the messages to the senior management of insurers which result from the PFSA's extensive supervisory processes distinguish clearly enough the major concerns on which the PFSA expects senior management to focus. In particular, the reports and recommendation letters from inspections, list large numbers of issues, mostly relating to compliance with detailed requirements, without any weighting or indication of what are the most important areas, especially in relation to risks that the insurer may fail to comply with requirements in the future.

59. More generally, there is scope for the PFSA to supplement its approach, especially to larger insurers, with additional forward-looking supervisory work on key risks. Insurers which met with the FSAP team all expressed the view that the PFSA's approach, while thorough on compliance with regulatory requirements, could include more discussion of issues which pose longer term risk, including strategy and business model. The FSAP assessor observes that many supervisors increasingly focus on the longer-term sustainability of financial soundness and fair treatment of customers by assessing strategy, business model and high-level governance, including risk culture and the culture of customer treatment. The aim is to assess how far the supervisor can rely on management to ensure future compliance rather than assessing themselves (or requiring management to self-assess) compliance with current detailed requirements. As insurers grow in Poland, or develop as financial conglomerates, such an approach may help PFSA to continue to use its supervisory resources most effectively.

60. It is recommended that the PFSA:

- review aspects of the supervisory approach discussed above, in particular whether there is adequate reporting by insurers to support risk assessment of conduct of business, the need for more assessment of the home supervisor in the case of foreign-owned insurers and the scope for sharpening messages to senior management resulting from supervisory work; and

- consider whether, at least in relation to larger insurers, their supervisory approach could be strengthened by even greater focus, including in discussion with insurers, on strategy, business model, risk culture etc. and on the capacity of management to ensure compliance with regulatory requirements in the future.

D. Conglomerate and Cross-Border Supervision

61. The PFSA's role relates to group and home supervision of the one major domestic financial conglomerate and significant responsibilities as a host supervisor of foreign-owned insurers:

- PZU Group (see Box 1 above) is the only domestic insurer with operations outside Poland. These are, however, not significant enough, nor are the insurance operations large enough, for PZU to qualify as an Internationally Active Insurance Group (IAIG) for the purposes of the IAIS's developing approach to insurance group supervision. PZU Group is also the only financial conglomerate in Poland (as defined by EU law and the Joint Forum Principles of Financial Conglomerates).[33]

- As noted in paragraph 6, there are also many foreign-owned insurers operating in Poland. Fourteen of these are parts of European financial conglomerates (seven in total) for which the group supervisor is outside Poland.

- In addition, a number of insurers have as parent a "mixed activity holding company" (effectively an owner which has significant non-financial interests, itself or in its subsidiaries). Reporting and monitoring of the insurer's intra-group exposures and transactions apply in these cases,[34] as required by EU legislation (Poland has not gone as far as some other countries who have given supervisors powers to obtain information directly from a mixed activity holding company).

62. There is a regulatory framework for financial conglomerates, based on EU legislation.

- Relevant EU legislation has been implemented (the 2002 Directive on Financial Conglomerates, as amended up to 2013, also known as FICOD).[35]

- The Polish implementing legislation[36] and related MOF ordinances reflect the directive's requirements on identification of financial conglomerates and application of "supplementary supervision," covering capital adequacy, significant intra-group transactions, risk concentration, conflicts of interest between entities in a conglomerate, risk management and internal controls at conglomerate level.

- The legislation applies to conglomerates headed by a regulated entity or otherwise including regulated entities in Poland and makes provision for mixed financial holding companies—those with interests in more than one financial sector. In practice, group structures in Poland have not to date included insurance holding companies, nor are there other significant unregulated entities.

[33] There are also several other groups containing banks and insurance companies, but one sector is predominant in these cases.

[34] Article 374(4) of the Act on insurance and reinsurance activity 2015.

[35] Directive 2002/87/EC of The European Parliament and of The Council of 16 December 2002 on the supplementary supervision of credit institutions, insurance undertakings and investment firms in a financial conglomerate.

[36] Act of 15 April 2005 on supplementary supervision over credit institutions, insurance undertakings, reinsurance undertakings and investment firms which form part of the financial conglomerate.

63. The framework will now be applied to the PZU Group following its recent expansion. The conglomerates regulatory framework has not so far been applied in practice. In 2017, before completion of the (already planned) significant further expansion of PZU's interests in the banking sector (see Box 1), the PFSA decided, in response to an application from the group itself, that although PZU had previously been assessed to be a financial conglomerate as defined, on materiality grounds[37] it met the conditions for exemption from supplementary supervision. The fact that the large majority of its operations are PFSA-supervised, and the broad scope of group supervision already exercised under Solvency II (see below) were also taken into account. As of May 2018, PZU was therefore not subject to the full requirements of the 2005 Act. However, following the latest PZU expansion, the framework will now be applied, once the relevant legal instruments are issued.[38] (In November 2018, i.e., after the main assessment work was undertaken, the PFSA formally acknowledged that the conditions for the exemption from supplementary supervision no longer exist and started the procedure of issuing administrative decisions, which will be processed in 2019, in order to fully enforce the supplementary supervision.)

64. Certain relevant provisions have nonetheless been applied under the Solvency II arrangements and in the PFSA's internal arrangements.

- As an insurance group, PZU has been subject to the Solvency II group solvency requirements which take into account interests in other financial sectors (the Solvency II implementing legislation explicitly recognizes the Solvency II Method 1 approach to group solvency of an insurance-led conglomerate, based on a calculation of consolidated own funds, as equivalent to the same methodology set out in FICOD).[39] PZU Group also reports on this basis in its quarterly published financial statements and SFCR. However, the group has not been subject to requirements in relation to intra-group transactions[40] or risk concentrations on a full conglomerate-wide basis.

- The PFSA has established a senior level working group to coordinate oversight of the PZU Group's activities across the sectors; with representatives of all relevant PFSA departments at director level and led by the director of Insurance Supervision Department, the working group meets quarterly to discuss significant changes in the group such as the group structure, its latest financial situation, risk assessments and key supervisory actions. Ad hoc cooperation, led by the Insurance Supervision Department, also takes place among departments responsible for the different parts of the group as well as the legal department.

[37] i.e., the scale of its business outside the insurance sector (banking and investment business) was too small, taking into account its minority holding in banking.

[38] The formal assessment of whether a group is to be subject to supplementary supervision is based by law on audited annual financial statements - in this case for 2017, which were available by mid-2018.

[39] Article 8 of the Commission Delegated Regulation No 342/2014, 21 January 2014.

[40] Coverage of the Solvency II requirements is limited to those where one party to the intra-group transaction is an insurer.

- PFSA has also periodically extended the college of supervisors which it leads for PZU (see below) to include PFSA bank supervisors, although the college has focused mainly on coordination of insurance sector supervision.

65. The PFSA is nonetheless reviewing all aspects of the supervision of the group in the light of its recent expansion. In particular, it is considering:

- alternative approaches to the organization of resources: approaches that could be considered include creating a dedicated team to cover all aspects of the PZU Group's business and stronger lead supervision arrangements with the insurance supervisor taking the lead in practice; at the time of the FSAP Mission, PFSA staff were considering a hybrid of these approaches: the creation of a small, dedicated team to carry out supplementary supervision and support the coordination of supervisory work across the group from within the Insurance Supervision Department; and

- supervisory outputs: these would ideally include a conglomerate-wide risk assessment that would draw on, but be more than the sum of, the separate sectoral SREP assessments; SREP differs by sector and an appropriate degree of harmonization of the different methodologies would also be useful in the context of conglomerate supervision and more generally; and a supervisory strategy and plan that would draw out supervisory issues that could be addressed, and work programs delivered, at the conglomerate level.

It will clearly also be appropriate that any changes in approach to larger insurance companies addressing the recommendations in Section C above is applied to PZU Group.

66. As group supervisor, the PFSA also leads the college of supervisors for PZU Group under a well-established process:

- A college has been in place since 2011 for the PZU Group with annual meetings and exchange of information and other activities between meetings.

- Lithuanian, Latvian and Estonian supervisory authorities participate in meetings (the Ukrainian supervisor is invited but chooses not to participate in the college; it does, however, contribute the information needed to ensure that the PFSA has a comprehensive overview of group-wide risks).

- The PFSA leads on the group risk assessment (the other supervisors' approaches to risk assessment are similar to the PFSA's) and work plan resulting from the risk assessment.

- Group management are involved in the college meetings and the PFSA provides feedback to the group.

All this is in line with EU directives and EIOPA guidelines. There has been limited joint supervisory work so far.

67. Given that PZU is state-controlled, the FSAP also reviewed the particular challenges associated with state ownership and control in the financial sector. The issues, covering banking sector state interests as well as insurance, are set out in Box 4. While recently increased state ownership and control in Poland is not currently a concern (for example because there is no observable improper influence on regulation and supervision), it reinforces the need for decisions about the PFSA's budget and internal organization to be demonstrably free from potential future conflicts of interest arising from the state's role as both owner and supervisor.

68. The PFSA participates actively as host supervisor in colleges of supervisors of foreign-owned insurers.

- It is a member of the supervisory colleges for 16 insurance groups based outside Poland and attends most but not all college meetings, taking into account the scale of the Polish business.
- Only one group is based outside the EU. The PFSA is a member and attends both the EU college and the college led by the global group-wide supervisor (in the USA).

Box 4. State Ownership in the Polish Financial Sector: Recent Developments and Implications

The financial system is characterized by significant state ownership. At end-2017 there were eight banks with some degree of state interest, accounting for 40 percent of total deposit-taking institutions' assets, eight non-life insurers (around 39 percent of total non-life GWP), three life insurers (37 percent of GWP) and seven capital market firms. The Warsaw Stock Exchange (WSE) is also state-controlled. Most significantly, the state is the controlling shareholder of both the largest commercial bank (BKO BP, a 29.4 percent interest) and the largest insurance company, which is also at the head of the only financial conglomerate (PZU, 34.2 percent).

Policy on state ownership in general changed in 2015. Since 1989, when much of the economy was in state hands, the government has been reducing state interests. In the financial sector, for example, PKO BP was listed on the WSE through an Initial Public Offering in 2004 and PZU in 2010. It is the policy of the government which took office in 2015 to limit further privatization to peripheral state interests and to focus on strategic management and maximizing the value of core state assets, which include the interests in PKO BP and PZU. Ownership supervision has been reformed under 2016 legislation and oversight of state interests in the major institutions transferred to the Prime Minister. New arrangements have been put in place for managing key decisions on state interests and for making appointments to supervisory boards based on skills and expertise. The 2016 law also includes a bar on disposals of shares in the largest companies, including PKO BP and PZU.

At the same time, state interest in the financial sector has increased owing to PZU's expansion. As noted in Box 1, PZU has acquired controlling interests in Polish banks. One acquisition, of Pekao Bank SA from the Unicredit Group, also transferred control from foreign to domestic ownership, furthering a related government objective to rebalance ownership in the financial sector in favor of domestic capital, aligning Poland more closely to most other EU countries. (These transactions also closely reflected expressed PZU objectives to develop into an integrated financial services provider).

Box 4. State Ownership in the Polish Financial Sector: Recent Developments and Implications (concluded)

State control of financial institutions is a feature of many countries' financial systems, but raises policy challenges, in particular:

- Maintaining clarity over the objectives of state control: while state interests include the 100 percent-owned National Development Bank, most entities (including PKO BP and PZU) are commercial operations, competing with wholly privately-owned institutions. From FSAP discussions, including with the Chancellery of the Prime Minister, there is no evidence of the government using state control to direct or to influence the business of the institutions other than with normal ownership objectives, for example by prescribing lending or investment targets; nor has the state sought the payment of excessive dividends (which, as noted above in respect to insurance, are subject to supervisory limitations, applying to all financial institutions).
- Rigorously separating state ownership supervision from other government policy, including regulation and supervision: centralizing ownership supervision in the Prime Minister's office, although the framework is still developing, appears to be supportive of clear separation. There are no special provisions in regulatory laws etc. in respect of state-owned institutions and the lead government department for regulation (MOF) has no role in ownership supervision. Supervision and the enforcement of regulations (by the PFSA), on the evidence of FSAP discussions, is carried out in the same way for all institutions regardless of ownership.
- Ensuring that effective governance of the state-controlled institutions is not compromised by government appointments driven more by political than by suitability considerations: state ownership affords the government wide scope to make appointments, directly to a supervisory board (appointed by shareholders) or indirectly to the management board (appointed by the supervisory board). The new arrangements for ownership supervision provide a check on political appointments but have not eliminated them (it appears from FSAP discussions). Some state-owned institutions have experienced significant turnover in senior management.

Overall, the risks from significant state ownership are assessed to be largely mitigated at present, but they further underline the need for independent regulation and supervision. The integrity of the regulatory process and empowerment of the supervisor are important checks on potential adverse impacts or even abuse of state control. The PFSA evidenced instances where it has resisted the appointment of a management board member, imposed financial penalties (including on the state of Poland itself), and restricted dividend payments by state-controlled banks without interference. The WSE-listed status of all the large state-controlled institutions, including the WSE itself, contributes to discipline in corporate governance and transparency. The apparent professionalism and strong performance in practice of these institutions is to be noted. Nonetheless, there remain risks and they reinforce the need for the PFSA is to be appropriately independent of government and adequately resourced in line with international standards.

- In the case of 9 of these 16 groups, non-EU supervisors are members of the college. The PFSA relies on a variety of arrangements, including equivalence assessments undertaken under an established EU process, to enable sharing of confidential information with such supervisors in the college framework. In some cases, there are college-specific confidentiality agreements in place. In no cases is the PFSA unable to share information.

69. The PFSA also takes action to work with home supervisors of EU insurers operating as branches or on a cross-border basis into Poland. It is not a member of any college in respect of such groups (under the EU framework, it may be invited to become a member in respect of a branch, but only where the branch accounts for a significant share of group business). Nonetheless, the PFSA does contact home supervisors where it identifies issues, including in cross-border services business. In practice such issues have arisen in recent years in relation to pricing practices in the motor TPL insurance market. The PFSA is able to monitor activity in that market by branches and on a cross-border basis through data that must be submitted by all market participants to the compensation scheme IGF, which shares it with the PFSA.[41]

70. There is scope to improve available data on cross-border business. In discussion with the FSAP team, industry representatives raised some concerns over the opportunities for insurers based elsewhere in the EU to access the Polish market on unequal terms. Others noted that, while this may be the case, the share of such cross-border business is low. It was noted that information on actual amounts is available to the market only after a significant lag, which reflects time lags under the EU directives between reporting and sharing the relevant data.

71. Overall, there is a strong framework for insurance group supervision, but it needs to be further developed to meet the challenges of supervising the one financial conglomerate. The implementation of Solvency II, as noted, has greatly strengthened the regulation and supervision of insurance groups and provides a strong starting point for the supervision of the enlarged PZU financial conglomerate. Effective conglomerate supervision requires a balance between sectoral with group supervision and effective team-working across supervisory functions.

72. It is recommended that:

- the PFSA complete the application of its comprehensive “supplementary supervision” requirements to the domestic financial conglomerate as soon as possible; finalize and implement arrangements to strengthen internal coordination amongst the sectoral supervisors of the group; and plan for conglomerate-wide risk assessment and supervisory work; and

- the PFSA and other authorities as appropriate consider the scope for improvements to the extent and timeliness of publicly available data on cross-border business into Poland by insurers based elsewhere in the EU.

[41] The financial supervision of such insurers, whether they operate as branches or under the EU freedom to provide services, is the sole responsibility of the home Member State under EU law.

E. Insurance Conduct of Business and Intermediary Regulation

73. The supervisory authorities have taken high profile supervisory and enforcement action in recent years in response to evidence of customer mistreatment. Most significantly:

- They responded to contractual provisions in life insurers' unit-linked policies that provided for high surrender penalties (also known as liquidation fees). The OCCP identified the issue and cooperated with the PFSA to assess the implications of various levels of regulatory response.

    - The OCCP initially issued a decision imposing one penalty on an insurer and reached agreements with 16 insurers imposing an obligation to reduce the exit fees in <u>new</u> sales of certain products.

    - In December 2016, 17 agreements were then made between insurers and the OCCP to reduce exit fees on a range of <u>existing</u> contracts and even to provide partial refunds to certain older policyholders who had incurred high exit fees in practice. The Polish Insurance Association was engaged in negotiating these voluntary agreements.

    - OCCP undertook not to bringing action before the courts under the legislation on unfair or abusive contract terms.

    - MoF was also involved and led on an initiative to undertake legislative change that placed a 4 percent cap on surrender penalties in new business.[42]

- The PFSA investigated evidence from supervisory work and from the FO that providers of motor insurance were not handling claims fairly; as mentioned above, the PFSA published extensive feedback to the sector in 2014 on this work and used its powers to impose financial penalties on 20 individual insurers.

74. Powers of regulatory authorities have been strengthened under recent legislation.

- The FO, established in 2015,[43] offers two core services to consumers, a free of charge "intervention" procedure, under which it supports the complainant with advice and information for use in discussions with the insurer; and an alternative disputes resolution service (attracting a small charge to the complainant)[44] under which it enters into discussion and seeks settlement with the insurer. However, it cannot provide binding adjudications. It has a power to impose

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[42] Article 26 of the Act on insurance and reinsurance activity 2015.

[43] Act on the complaint handling procedures by financial service providers and FO, 2015.

[44] The FO's general costs are borne by licensed financial services providers through a levy.

financial penalties where an insurer is found not to be handling complaints fairly. As mentioned above, it may also submit opinions to the Court and petitions to the Supreme Court.[45]

- On 1 January 2018, the PFSA acquired new powers as a result of the EU PRIIPs Regulation to prohibit or restrict the marketing, distribution or sale of certain insurance-based investment products (it does not have power to require prior approval of insurance products).[46] In addition, the PRIIPS Regulation has increased the sanctioning powers of the PFSA, including providing for higher financial penalties for breaches of the Regulation's requirements.[47] The Regulation introduced new, more extensive disclosure requirements attaching to the sale of relevant policies, particularly a requirement for insurers to produce and provide to consumers before sale a key information document meeting detailed requirements.

75. However, there are some gaps in powers compared with some other countries.

- While the OCCP was able, as mentioned above, to negotiate valuable voluntary agreements with insurers in relation to surrender penalties on unit-linked business and partial refunds for some consumers, no authority has power:
    - to require insurers to pay redress to consumers who have suffered from mistreatment; or
    - to accept enforceable undertakings from financial service providers.
- There is also no provision for binding dispute resolution of complaints: in addition to the FO, there is a Conciliation Court, managed by the PFSA, which as well as mediation, provides for dispute resolution, but its decisions are binding only where both parties have agreed to be bound; case volumes are low.

76. In addition, the PFSA's capacity to monitor developments and to identify and respond to new risks to consumers has been strengthened. Its Enforcement and Market Practices Department, established in early 2018, and which covers all regulated sectors, has responsibility for:

- handling complaints against insurers received by the PFSA (i.e., using them to identify concerns with particular insurers);
- analysing contracts, standard terms and conditions, etc.; and

[45] The FO addressed nearly 19,000 complaints in total in 2017, of which 75 percent related to insurance; it also submitted 493 opinions to the Court and 20 petitions to the Supreme Court (all sectors). It has not to date used its powers to levy fines on financial institutions.

[46] Article 17 of the PRIIPs Regulation.

[47] Article 24 of the PRIIPs Regulation.

- cooperation with the FO and OCCP.

77. The PFSA could reduce its reliance on direct consumer complaints, which is resource-intensive. The capacity to identify "signals" of potential consumer detriment from the complaints it receives directly, as well as from market intelligence, etc., supplements the work of PFSA supervisors in monitoring for risks. The PFSA does not maintain a separate risk assessment process or work program on consumer protection issues nor a list of current key areas of concern. It does, however, participate in and respond to issues raised by the EIOPA process for identifying consumer risks.[48] As already considered by the PFSA, greater efforts to have more complainants go directly to the FO would save supervisory resources, albeit at the cost of loss of some useful "signals."

78. There appear to remain significant risks of misconduct related in part to the basis for remuneration in insurance distribution.

- Agent remuneration is mainly by commission, which has been high, reflecting the challenges in acquiring new business. The need to recover commission paid to agents was a key driver of the high surrender penalties on unit-linked insurance.

- As at May 2018, there are limited requirements for disclosure of remuneration. However, on implementation of the IDD in October 2018, disclosure to the customer of the basis of remuneration, although not the amount, was to be required.[49]

- Insurers are, however, already required, in respect of savings-related policies linked to investment funds or indices (most unit-linked policies), to spread commission payments over five years, limiting the impact of surrenders in the early years.[50] The new requirements on assessing the needs of consumers will also help.

79. In this context, implementation of recent EU legislation brings challenges for the PFSA as well as significant potential benefits to consumers. As mentioned, new requirements (in the IDD and PRIIPs Regulation) applying to all insurance intermediation, whether undertaken by agents, brokers or the insurer's direct sales staff, require standard disclosures (the key information document) as well as detailed assessment of customer needs.[51] There are some challenges for PFSA, including:

[48] See, for example, the regular EIOPA Consumer Trends Report.

[49] Article 22 and 32 of Insurance Distribution Act 2017.

[50] Article 23 and 24 of the Act on Insurance and Reinsurance Activity 2015.

[51] Current insurance legislation requires only that insurers examine the adequacy of insurance-based investment products (Article 21 of the Act on Insurance and Reinsurance Activities act 2015).

- the need to integrate to some extent agent and broker supervision (separate registers are maintained at present, there are separate approaches to training and competence requirements and, as mentioned, the PFSA undertakes only indirect supervision of agents);
- in broker regulation, changes in how brokers are expected to comply with the requirement to provide advice on the whole of the market, which, while not a completely new obligation, differs in detail from the current framework which has been subject to interpretation by courts;
- the need for a policy framework for implementing the new powers to prohibit or restrict the marketing, distribution or sale of relevant products, taking into account the role of EIOPA in facilitating and coordinating national supervisors' actions; and
- potential changes in market structure that may result from the impact of the new requirements, including the increase in costs of certain business models which some in the market are expecting.

The PFSA is reviewing the implications of these changes. Additional resources for intermediary regulation are likely to be required.

80. Risks to insurance consumers remain high and it will be important for the PFSA to continue to perform a leadership role in insurance consumer protection. Risks of misselling and/or unfair contract terms seem likely to remain high and it will be important for the authorities to devote adequate attention to conduct of business risks, while continuing to cooperate closely. OCCP's responsibilities span the whole economy and its resources are more limited than the PFSA's. Notwithstanding its wide range of powers, the FO's role is focused on complaints. The PFSA's objective to protect the interests of consumers encompasses business conduct and it is well-placed to exercise preventative supervision, using the SREP framework (see Section C) and its other tools.

81. Strong leadership within the PFSA and adequate resourcing are required to ensure that the importance of conduct supervisory work is recognized and seen as complementary and not subordinate to prudential work. If necessary to ensure the effectiveness of both financial and conduct supervision, the PFSA should consider organizing and staffing conduct work separately, while continuing to exploit the advantages of integrated supervision, such as ease of coordination and resolution of the conflicts that can arise. While, as noted, supervisory processes, including SREP, already address conduct issues, there may be scope for changes to enable even greater focus on conduct, taking into account the needs of PFSA supervisors of sectors other than insurance (as SREP is already a shared tool and needs to become even more so in future to facilitate conglomerate supervision, for example). This could include adding to SREP a specific conduct risk assessment process, which would be integrated at a high level with the assessment of financial risks. The PFSA's approach also needs to take account of developing EIOPA work on supervision.

82. Overall, arrangements for insurance conduct of business are well-established and increasingly effective, as shown by recent supervisory and enforcement action. However, in order to ensure continued effectiveness in a context of significant risks, **it is recommended** that:

- the authorities review the overall approach to insurance conduct of business supervision across the relevant agencies with a view to ensuring that respective responsibilities are well understood, there is no subordination of financial to conduct supervisory objectives, coordination between agencies is adequate and that the PFSA leads on, and is resourced further to develop preventative supervisory work;

- the authorities review the powers available to the PFSA and OCCP for consumer protection work, which could be strengthened by powers to require redress and to accept enforceable undertakings; and

- in the light of such reviews, the PFSA consider reform to its organization and supervisory processes, as necessary to ensure even closer focus on conduct supervision; for example, it could consider whether to organize and staff the work separately from prudential supervision, but with close coordination.

F. Financial Stability, Macroprudential Regulation, and Crisis Preparedness

83. The authorities consider stability and macroprudential issues relating to insurance to be limited at present. The PFSA leads on such issues, although, as mentioned, the NBP has overall responsibility for financial system stability. The NBP covers insurance extensively in its regular published Financial Stability Review and issues are discussed at FSC-M. The combination of NBP work and the supervisory work of the PFSA, including its regular stress tests, provides for relatively thorough and frequent analysis of market-wide developments, including those posing stability risks.

84. There are some insurance sector shared exposures, including those related to conduct and legal risks.

- As noted, there is a high shared exposure to the Polish government, but common exposures appear otherwise to be limited and interconnectedness with the banking sector is low, other than via growing ownership links, as discussed above.

- The liquidity risks associated with some forms of life insurance are limited in Poland because of the product mix and high liquidity of the investment portfolio.

- Similarly, there are limited issues related to the procyclicality of the more risk-based capital adequacy framework (and there are elements in the requirements that dampen certain effects, such as in relation to equity risk).[52]

- Exposures to the financial implications of regulatory action due to conduct issues and to legal uncertainty have been considered. As mentioned, life insurers have been exposed to the implications of past conduct and non-life insurers to underpricing of TPL insurance. Mechanisms

[52] For the calculation of the SCR standard formula, the equity risk sub-module includes a symmetric adjustment applied to cover the risk arising from changes in the level of equity prices. In rising equity markets the dampener will increase the capital charge, and in falling equity indices the dampener will reduce it. (Article 106 of the Directive).

to address these issues as described in Section E above (mainly cooperation between regulators and with the MoF) have functioned well, even if market participants mentioned that they would have preferred earlier action in some cases.

85. There is no formal framework yet for assessing the systemic importance of insurers, although FSC-M is considering the issues. Polish insurers are not engaged in forms of insurance activity or related business that has been assessed internationally as giving rise to systemic risks, including complex savings business such as variable annuities or some forms of credit insurance. There are limited issues related to substitutability (where an insurer dominates an economically significant line of business). While the foreign-owned insurers in Poland include Global Systemically Important Insurers (G-SIIs), the only significant Polish group, PZU, is not formally regarded as a systemically important insurer (with associated specified additional requirements), in the domestic context.[53] As noted, however, it is subject to relatively intensive supervision, reflecting its size, and to the developing application of the financial conglomerates regulatory framework.

86. Additionally, the FSC-M has provisionally identified non-life insurance as systemically significant. The FSC-M is empowered[54] to identify all systemically important financial institutions (not only banks). The non-life insurance sector (specifically PZU) has been judged as important in the financial system, mainly because of its interconnection with the banking sector. This assessment has not been made public. It has no immediate consequences for action, although it is consistent with the relatively intensive supervision of PZU, as mentioned. Further work on the FSC-M approach is in hand.

87. There is no resolution regime for insurance and the authorities are waiting on (and contributing to) developing policy work at the EU level. There are limited international standards in this area. The Financial Stability Board's Key Attributes report (Annex 2 covers insurers) is applicable only to G-SIIs. Solvency II implementation has strengthened the intervention framework in relation to solvency but does not provide for resolution work or even for recovery planning. Polish insurers are subject to general company bankruptcy law, which provides for court-administered insolvency proceedings (on the application of the PFSA or the insurer itself) and appointment of a bankruptcy trustee or curator.[55] As noted above, the IGF is the (limited scope) insurance guarantee scheme, with an assistance as well as compensation function. EIOPA has issued an opinion[56] supportive of the harmonization of recovery and resolution frameworks for EU insurers and is also

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[53] One of the banks in which it now has a large interest, Pekao Bank SA is treated as an "other systemically important institution" (O-SII) under the arrangements for measurement of systemic importance applied to Polish banks.

[54] Under Article 5.2 of the Act on macroprudential supervision and crisis management in the financial system.

[55] In addition, amongst other intervention powers, PFSA may order a compulsory winding-up of an insurer (with appointment of a liquidator) in a wide range of circumstances including failure to comply with a recovery plan (Article 322 of the law on insurance and reinsurance activity)—i.e., where the insurer remains solvent.

[56] EIOPA "Opinion to institutions of the European Union on the harmonization of recovery and resolution frameworks for (re-)insurers across the Member States," July 2017.

working on resolution funding and insurance guarantee schemes. As at the time of the main FSAP work, there was no timetable for a response by the European Commission.

88. It is appropriate for the PFSA nonetheless to address recovery planning. EIOPA's opinion includes support for "pre-emptive recovery planning" (distinguished from the recovery plans required of insurers which fail to meet solvency capital requirements under Solvency II). There are no explicit provisions on such plans in Polish insurance legislation, although provisions on ORSA and contingency planning require insurers to address risks of financial stress and its implications. EIOPA's view is that pre-emptive recovery plans should be taken by a broad range of insurers.[57]

89. Pending agreement and implementation of an EU approach, the PFSA is taking action in relation to the largest domestic group. While there is no fully-developed SII approach yet, the significance of PZU Group in the financial system makes at least recovery planning appropriate. The group was asked, through the mechanism of the supervisory college, to prepare a "recovery action plan" at the group level. The PFSA's review of the plan should be integrated with similar work on the banks in the group (for example, by addressing actions that could be taken in case of stress originating in either a group bank or insurance company), taking into account the structure of the group, which is headed by the non-life insurer.

90. It would be appropriate to review the operation of insolvency law in delivering policyholder preference in case of a failure. As noted in the previous ICP assessment, there is no explicit policyholder preference provision in law. Under Article 477 of the Act on Bankruptcy, in case of insolvency, the assets covering technical provisions for solvency purposes are treated as available for the settlement of claims (and certain costs). There is no provision, however, as there is in some other countries, for the relevant assets to be clearly identified by the insurer at all times (and even checked periodically by auditors), in a register or by another appropriate mechanism, to ensure that assets can in practice be readily used by a bankruptcy trustee to satisfy policyholder claims, without risk of challenge from creditors. The law has not been tested by a recent actual bankruptcy. Such work seems especially important given the limited scope of insurance guarantee scheme coverage.

91. It may also be appropriate to review IGF coverage. There is no international standard on insurance guarantee arrangements and many countries, including in the EU, provide no protection. The IGF framework focuses, in relation to insolvency, on compensation for compulsory lines of business, for which the IGF is well-prepared to provide compensation in case of need, having extensive data and immediate access to finance as well as its assistance mechanism for TPL business transfers. The same is not true for life insurance or other compulsory insurance. Furthermore, the limitation of compensation to 50 percent of benefits (with a Euro 30,000 cap) seems unhelpful in the context of the usual objectives of guarantee arrangements not only to compensate for actual loss but also to support market confidence in insurance.

[57] See Box 4 of EIOPA "Opinion to institutions of the European Union on the harmonization of recovery and resolution frameworks for (re-)insurers across the Member States," July 2017.

92. Insurers are required to develop contingency planning and there is consideration of crisis preparedness in supervisory colleges. All insurers are required to develop emergency plans and to reflect these in relevant systems, including risk management. Cooperation on crisis preparedness is one of the issues covered by the EU arrangements for colleges of supervisors:[58] the group supervisor is responsible for preparing an emergency plan as an annex to the coordination arrangements governing the operation of the college. Such plans are aimed at:

- facilitating the exchange of confidential information at short notice within the college (a list of contacts is also maintained by EIOPA);
- ensuring access to current information such as group structure; and
- committing supervisors to notify college members of any potentially serious financial disturbance at group level.

93. Overall, the Polish approach of moving forward on these issues in line with the EU seems appropriate and actions already taken are well-judged. Nonetheless, it is recommended that:

- the PFSA give high priority to recovery planning of the PZU Group, in line with initiatives already taken, integrating work undertaken on the banks in the group; and
- the authorities review:
    - the current approach to life insurance insolvencies, including the level of compensation and readiness of IGF to intervene, including the possible availability of its assistance function for life insurance portfolio transfers; and
    - for all insurance, the robustness of policyholder protection arrangements in a liquidation, in the light of the continued absence of explicit policyholder preference and the lack of experience of the arrangements being tested; the possible need to action to ensure that assets covering technical provisions for solvency purposes are available in practice for the settlement of claims.

[58] EIOPA Guidelines on operational functioning of colleges: Annex 1.E—Emergency plan.

Annex I. Poland's Response to the Recommendations of the 2012 Detailed Assessment

IAIS ICP (2003 version)	Rating	Recommendations to Improve Observance of ICPs	Comments
1. Conditions for effective insurance supervision	LO	The main conclusion regarding this ICP is the importance for the PFSA to continue their current extensive effort to strengthen professional education and vocational training of those involved in the sector and to enhance financial literacy in the general public. Private and public sector initiatives will continue to be necessary to maintain the availability of high-quality professional services, including accounting and actuarial services and to further develop the sector.	PFSA's functions under the 2006 Act on Financial Market Supervision include "taking educational and informational actions related to the operation of the financial market" (Article 4). It has continued to maintain a project started in 2009 (Education Centre for Market Participants—CEDUR) promoting financial literacy. This is targeted at a wide range of recipients, from supervised entities to the general public. The PFSA also publishes educational material. Promotion and development of the financial sector, including relevant professional services, falls to other bodies including the Ministry of Finance (MoF), which for example sets examination requirements for actuaries. Supply of accounting, audit and actuarial services appears broadly adequate to the needs of the insurance sector.
3. Supervisory authority	PO	The powers, the resources to exercise them, and the operational independence in the exercise of its functions and powers, would be enhanced by the addition of further staff directed toward insurance supervision, and more independence in setting budgets, salaries and organizational structure. The absence of a rule making power envisaged in this ICP also contributes to the assessment.	Response to the recommendations has been mixed: • The PFSA's powers have been extended by the 2015 Act on insurance and reinsurance activity to enable it to issue generally applicable recommendations (Article 365), issued on a "comply or explain" basis. • However, the PFSA has not been granted general rule-making powers and all regulatory requirements continue to be set by the MoF in laws and ordinances made under the relevant laws. The PFSA cooperates closely with the MoF on the preparation of laws and ordinances applying to

IAIS ICP (2003 version)	Rating	Recommendations to Improve Observance of ICPs	Comments
			insurance, for example in the implementation of the EU Solvency II Directive through the 2015 Act on insurance and reinsurance activity. In some cases (e.g., implementation of some of requirements of IDD, the MoF has agreed to the PFSA's requests to implement key measures earlier. • The PFSA has not greatly increased its staff resources since 2012, certainly compared with the increases made by many EU insurance supervisory authorities in this period. Staff at end-2011 are estimated to have totalled 99, which compares with 106 at end-2017, although comparison is hampered by reorganization of insurance work within the PFSA during the period. • The PFSA's limited independence in setting budgets, salaries and organizational structure has not been addressed. (However, on January 1, 2019, i.e., after the main assessment work, an amendment to the Act on Financial Supervision entered into force enabling the PFSA to independently govern its budget and exempting PFSA employees, but not the Chairman and Vice-Chairman, from the remuneration requirements by the Prime Minister. See also the FSSA.)
6. Licensing	LO	There are minor issues related to the fitness and propriety requirements (see ICP 7).	See under ICP7 below
7. Suitability of persons	LO	The main issue regarding the requirements lies in the absence of explicit reach to some key functionaries that may not be management	As a result of implementation of the EU Solvency II Directive, the framework now includes suitability requirements for management (and supervisory) board members and key function holders (heads

IAIS ICP (2003 version)	Rating	Recommendations to Improve Observance of ICPs	Comments
		board members; this is addressed in the system in more indirect fashion through the warranties of board members.	of compliance, actuarial, risk management and internal audit, i.e. those functions which insurers are now required to have—Chapter 3 of the 2015 Act on insurance and reinsurance activity). The chairman of the management board and member responsible for risk management must be approved by the PFSA prior to taking up office.
10. Internal controls	LO	The PFSA holds the management board responsible for maintaining an internal control framework, assessing the adequacy of controls as part of its on-site supervision work. It includes discussions with staff in such functions and access to their internal reports (including internal audit). Although actuarial reports are generally provided to boards, the requirement is not compulsory.	There remains no binding requirement for actuarial reports to be submitted to boards of management. However, the PFSA's 2015 guidelines on establishing technical provisions state that the report prepared by the head of actuarial function should be submitted to the management and supervisory boards. The new framework of requirements on governance, including the role of the actuary, and on reporting introduced by the EU Solvency II Directive has resulted in this recommendation being met.
13. On-site inspection	LO	The PFSA has an active on-site inspection process with scope in line with the ICP regarding insurers. Inspection activity of intermediaries could be enhanced over time.	The 2012 assessment recorded that "brokers and agents are only inspected if there is a complaint". The PFSA now maintains a program of inspections of: (i) insurance companies, focusing specifically on their agents (under the indirect approach to agent supervision adopted at present)—13 insurers were subject to inspection in 2017 out of the 56 insurers which make use of agents; and (ii) brokers—14 to 18 per year, which compares with a population of 1,365 registered brokers in total (1,323 insurance brokers, 42 reinsurance brokers, many of which are small/individual practices). The PFSA's approach was under development as a result of implementation

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			of the EU Insurance Distribution Directive due in October 2018.
15. Enforcement or sanction	LO	The PFSA should be given direct and explicit powers to require business transfers. This power is currently more implicit. The PFSA should also be granted the power to bar individuals and directly require capital increases.	The PFSA has not been given powers to require portfolio transfers. The PFSA does not have general powers to bar individuals from "acting in responsible capacities in the future". It would rely on requirements for key persons to meet suitability requirements (see ICP 7 above). The PFSA has powers (Article 52 of the Act on insurance and reinsurance activity) to determine that a member of the management or supervisory board or key function holder is failing to satisfy the requirements of the Act with the result that the person is removed from the relevant position. It may also require removal of an actuary (Article 69—decision to strike an actuary off the register of actuaries). As a result of the implementation of the EU Solvency II Directive, PFSA has powers (Article 270 (1) of the Act of insurance and reinsurance activity) to impose a capital add-on (i.e., an additional capital requirement), if the conditions set out in the law are met.
16. Winding-up or exit from the market	LO	The insurance legal framework provides a trigger for the PFSA to take action in case of an insurance company becoming financially unsound. In the event of winding-up, there is no preference for insurance policyholders but, instead, a Guarantee Fund for a policyholder protection scheme that would pay out in	There has been no substantive change to the provisions on the treatment of policyholders in liquidation. Under the 2003 Bankruptcy Act (Article 477), assets covering technical provisions for solvency purposes are available for the settlement of claims arising from insurance contracts, reinsurance contracts and costs of asset liquidation. Similar provisions are set out in the 2015 Act of insurance and reinsurance activity (Article 326).

IAIS ICP (2003 version)	Rating	Recommendations to Improve Observance of ICPs	Comments
		case of policyholder loss on insurance company insolvency.	The Insurance Guarantee Fund (IGF) continues to be responsible for paying compensation in case of an insurer's bankruptcy. As in 2012, it covers compulsory insurance contracts and life insurance (subject in the case of some contracts to limits on the amounts it will pay). See Findings Section F.
17. Group-wide supervision	LO	The PFSA is principally a host supervisor. Where the PFSA is a home supervisor, there is scope to enhance current data collections to facilitate a more continuous monitoring of the overall financial position, risk profile and exposures, etc. beyond the level currently in place. Given the nature of the insurance market, this would best be advanced reflecting the specifics of the insurance groups.	Group supervision has been greatly developed as a result of implementation of the EU Solvency II Directive (see Chapter 15 of the 2015 Act on Insurance and reinsurance activity). Requirements on groups have been strengthened in the new law. Data collection in relation to the group business of the one group for which the PFSA Is group wide supervisor has been greatly extended. The PFSA continues to lead a college of supervisors for that group and to participate in colleges in respect of other insurance groups represented in Poland where it is the host supervisor. For the one Polish group, it applies its supervisory framework, including risk assessment, at group level and prepares a Joint Risk Assessment in the college of supervisors. See Findings Section D.
19. Insurance activity	LO	It would be useful to elaborate more explicitly the PFSA's expectations of insurers regarding risk management in some respects so as to develop guidance at a more specific level of detail whilst providing for variation to take into account the nature, scale and complexity of insurers and insurance groups.	The regulatory framework for risk management has been extended in recent years, reflecting Solvency II and the PFSA's response to market developments. The requirement for, and broad expectations of the risk management function are set out in the 2015 Act on insurance and reinsurance activity. The PFSA has issued Principles of Corporate Governance for supervised entities (2014) and guidance on specific subjects such as its Guidelines on flood risk management in the insurance sector (2014). Other material has included risk

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			management expectations, including the 2016 Recommendations regarding the process of determining and paying compensation for non-pecuniary damage from contracts of third-party insurance of vehicle owners.
20. Liabilities	LO	It would be useful if some more publicly available guidance on provisioning was available to enhance consistency and transparency on reserving issues.	The regulatory requirements implementing the EU Solvency II Directive include provisions on the establishment of technical provisions, for life and non-life companies, particularly Articles 224–237 of the 2015 Act on insurance and reinsurance activity. The PFSA has supplemented these with its own Guidelines on the process for technical provisions (2015), published ahead of Solvency II implementation. The established requirements in law regarding technical provisions to be recognized for accounting purposes (which before 2016 also served as requirements for solvency purposes) have been retained and continue to be used for audited financial statements and additional reporting to the PFSA in parallel with Solvency II reporting. All this material is publicly available.
21. Investments	LO	Consistent with the broader system, the PFSA's approach is principle-based and sensitive to the nature, scale and complexity of insurer risk profiles rather than overly prescriptive approach, although there are more detailed rules in many useful respects. To further enhance observance, the approach could benefit from some additional specificity and focus	Solvency II implementation has led to an overhaul of investment regulation. As reflected in the 2015 Act of insurance and reinsurance activity (Article 276), insurers' investments must now be managed in accordance with "prudent person" principle (that they invest in assets whose risks they can properly identify, measure, monitor, manage, control and report). The PFSA is able to monitor compliance with this requirement through extensive reporting by insurers of their investment

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		on the requirements of sound risk management in transparent guidance, and the reach of fitness and propriety rules to key investment officers especially those that may not be part of the management board, both being developments that are expected as Solvency II is implemented.	portfolios; and investment policy and practices are covered in both off-site and on-site supervision, including in the SREP process.
22. Derivatives and similar commitments	LO	This high level of observance can be further enhanced through more detailed transparent sector wide guidance on good practices addressing the specific risks associated with derivative use, possibly developed as part of or subsequent to the implementation of Solvency II.	Solvency II implementation resulted in changes to the approach to insurers' derivatives business. The general approach of Solvency II (as reflected in Article 276 of the Act of insurance and reinsurance activity) is to limit the use of derivatives (except in unit-linked and index-linked assets without guarantees) to the purposes of reduction of risks and efficient portfolio management. The PFSA draws on EIOPA guidance to support an interpretation of the language of the Solvency II Directive/2015 Act on insurance and reinsurance activity. There is regular reporting to the PFSA of derivatives contracts and insurers' policy and practices are evaluated in both off-site and on-site supervision, including in the SREP process. Only a minority of insurers use derivatives in practice.
23. Capital adequacy and solvency	LO	Observance of this principle will be enhanced with the full implementation of the Solvency II regime which will have the desired effect of making the capital requirements more sensitive to risk as is suggested by essential criterion (d). It is noted that the EU has stated	Solvency II, a form of risk-based capital adequacy requirement for insurance companies, was implemented in full from the start of 2016, and all insurers are in compliance with the new minimum requirements. See Findings Section B.

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		that the current solvency regime as described in the directives is not fully observant of this ICP. The efforts of the PFSA on more risk-oriented approaches go some way in this direction but will reach a full culmination with the implementation of Solvency II.	