



5 August 2009

Ref: SII/CL/01

Dear Sir/Madam

I am writing to you to highlight the Solvency II project and to seek information on your firm's preparations for the new supervisory regime. As you are aware, the European Commission, the European Council and the European Parliament agreed, after long negotiations, on a compromise text for the Solvency II Directive. The text was passed at a plenary session of the European Parliament on 22 April 2009. Formal publication of the Directive in the Official Journal is expected in October. This now sets the stage for the implementation of the Directive at end-October 2012 and heralds the start of intensive activity at European and national level to put in place the necessary implementing measures.

Overview

Solvency II will bring about significant change in the regulation and supervision of insurance and reinsurance undertakings. The primary changes are:

- Introduction of economic risk-based solvency requirements across all EU Member States. These new requirements will be more risk sensitive and sophisticated than in the past, enabling better coverage of the real risk that insurers run. Moreover, the new regime will take a whole balance sheet approach where all risks and their interactions are covered.
- The new regime emphasises that capital is not the sole or best way to protect against company failures. New rules will compel insurers to focus fully on the identification, measurement and active management of risks. This will be done in a more prospective manner, as the new rules will require insurers to look at future risks in considering their solvency.
- A new formality will be introduced by the Own Risk and Solvency Assessment (ORSA) that firms will have to undertake on an annual basis. Another new requirement will be the Supervisory Review Process (SRP) under which supervisors will evaluate insurers' compliance with the laws, regulations and administrative provisions relating to the Solvency II Directive and its implementing measures.
- The new rules will require insurers to disclose more information publicly than is currently the case. This aim being to bring market discipline to bear on ensuring the soundness and stability of insurers.
- Lastly, the new framework will strengthen the role of the group supervisor who will have specific responsibilities to be exercised in close co-operation with solo supervisors. This will mean that the same economic risk-based approach will be applied to insurance groups that can be better managed as a single economic entity.

An excellent road map to Solvency II has been prepared by the Irish Insurance Federation, in conjunction with the IFSC Solvency II Working Group. The roadmap provides a comprehensive primer on the steps towards implementation of Solvency II and includes a checklist of key actions that firms need to take.

Implementation of Solvency II

It is planned that the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS) will complete its provision of advice to the European Commission on Level 2 Implementing Measures by the end of 2009 or early in 2010. The Commission intends to adopt the final Level 2 Implementing Measures by end-October 2011, some twelve months before the entry into force of Solvency II. For its part, CEIOPS will deliver its final Level 3 supervisory guidelines by end-March 2011 although additional Level 3 guidelines may be required for the Level 2 implementing measures.

Although these dates seem distant, the dramatic change that Solvency II will bring about for both firms and supervisors must not be underestimated. For example, firms seeking to utilise internal models for solvency purposes must pass stringent data and use tests before such a model could be recognised. In short, the message is that firms should be making effective plans now for the implementation of Solvency II. Fundamental to these plans are four key elements:

- First, firms must have, or put in place, an appropriate governance framework for the implementation of Solvency II.
- Second, an accountable individual must be appointed at executive level with responsibility for overseeing implementation of Solvency II and we would advise that a specific board member assume responsibility for Solvency II issues.
- Third, a gap analysis should be undertaken at an early stage to identify any shortfalls relative to the Solvency II requirements. While much of the detail of the Solvency II standards is still evolving, this is not a reason to delay commencement of preparations for implementation. Non-compliance in 2012 or having to undertake high cost implementation programmes at short notice can be avoided by starting now.
- Finally, firms' implementation plans should focus on all three Pillars of Solvency II, rather than concentrating on potential capital releases under Pillar 1. Failure to address properly Pillars 2 and 3 will leave firms in a position where any potential gains under Pillar 1 are forfeited.

In the context of planning for the implementation of Solvency II, I would be grateful if you could provide the Financial Regulator with the following information by end-August 2009:

- Name, contact details and position of the senior executive (and director) who will be accountable for the Solvency II project in your firm. Details should be sent to solvencyII@financialregulator.ie.
- Details of your firms intentions in relation to the use of internal models. A template questionnaire is available under 'Regulatory Requirements' in the Life, Non-Life and Reinsurance sections of the Financial Regulators website. Please download the questionnaire and email completed version to solvencyII@financialregulator.ie

Yours sincerely

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