

Taking-up and pursuit of the business of insurance and reinsurance - Solvency II. Recast

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The Committee on Economic and Monetary Affairs adopted the report drawn up by Peter SKINNER (PES, UK) amending, under the first reading of the codecision procedure, the amended proposal for a directive of the European Parliament and of the Council on the taking-up and pursuit of the business of Insurance and Reinsurance (recast) (SOLVENCY II).

The main amendments are as follows:

Minimum Capital Requirement (MCR): the committee states that the Minimum Capital Requirement should be calculated in accordance with a simple formula, which is consistent with the risk-based approach of the Solvency Capital Requirement (SCR) and is based on the data which can be audited. MCR values must provide a proper safety net and a proper relationship with the SCR. The committee felt that the **compact approach** is the most appropriate method to achieve this goal.

Simplification of tier structure: regarding the SCR, the committee deleted the provisions regarding the limits on amounts of Tier 2 and Tier 3 items. Instead it provided that the Commission may adopt implementing measures restricting Tier 2 and Tier 3 capital to the amounts that may be demonstrated to be necessary to provide an appropriate level of protection for policyholders. Members note that some form of tiering and restrictions is desirable to prevent companies being inappropriately capitalised with capital of relatively low quality. However, the eligibility limits proposed by the Commission are excessive, arbitrary and not based on an economic rationale. Surplus funds can **only be used to cover losses** in the case of a breach of the **undertaking's SCR**, but not in the case of a breach of MCR, regardless of the tier classification.

Surplus funds: a new recital clarifies that surplus funds cannot be used as group support because of their legal nature. It notes that it is current practice in the Community that insurance companies sell life insurance products in relation to which the policy holders and beneficiaries contribute to the risk capital of the company in exchange for all or part of the return on the contributions. Those accumulated profits are surplus funds, which are the property of the legal entity in which they are generated. Within the group support regime, surplus funds are not transferable to other legal entities of the group.

Members add that in some countries, insurance groups are structured in such a way that a legal entity manages a group of undertakings linked by long-lasting financial relationships. They inserted an amendment which clarifies that **half of their own funds will be classified in Tier 2**.

A new Article on information for policyholders: surplus funds states that the use of surplus funds must be communicated to the policyholder for solvency requirement purposes before the conclusion of the life insurance contract.

Implementing measures on proportionality: the proposal notes that the Directive must be applied in a manner which is proportionate to the nature, complexity and scale of the risks inherent in the business of an insurance or reinsurance undertaking as well as with a view to maintaining financial stability in the Community as a whole, in particular in times of financial distress. The committee provides that the Commission shall adopt implementing measures relating to this matter, specifying the proportional application of the Directive, in particular to very small insurance undertakings. Those measures shall be adopted in accordance with the regulatory procedure with scrutiny.

Group supervision and group support regime: the committee broadly supported the group support regime. On group supervision, an amended provision now states that Member States shall ensure that the supervisory authorities are provided with the necessary means, and have the relevant expertise and capacity, and mandate to achieve the main objective of supervision, namely the protection of policyholders and beneficiaries in accordance with Community and national law. Members note that the supervisory requirements established under Pillars 2 and 3, such as the **approval of internal models**, their monitoring and regular review, and the consequent closer cooperation and engagement with other supervisors and companies, is likely to mean national supervisors will need more resources to fulfil their enhanced responsibilities properly.

Member States must ensure that when a supervisory authority acts as a group supervisor it is recognised as doing so in a non-discriminatory manner; consequently, legitimate actions taken as a group supervisor, including but not limited to transfers of capital, shall not be regarded, on the basis of that supervisor's national mandate, as contrary to the interests of the Member State or of policyholders in that Member State.

.A new Article states that in the event of non-compliance by a holding company or a parent company with the requirements of group support, the group supervisor may determine that supervision on a group basis is to cease.

Treatment of equity risk: again, the committee broadly supported the Commission's approach on equity risk. Members state that in order to **prevent pro-cyclicality**, in particular in equity markets during times of financial distress, supervisory authorities need to be given a greater degree of flexibility in the adoption and execution of their supervisory measures. Such greater flexibility, however, should be of exceptional nature, aiming to stabilise rather than increase the negative effects of a financial crisis.

With regard to breach of the SCR, the committee states that in order to avoid pro-cyclical effects and to prevent destabilising financial markets by requiring undertakings to comply with the Solvency Capital Requirement within nine months from the observation of non-compliance, the supervisory authorities may **extend the prescribed period** three times by an additional three months.