Article by Gabriel Bernardino, Chairman of EIOPA, for the Börsen-Zeitung

Solvency II is coming closer

Initially Börsen-Zeitung asked me to write an article entitled "Solvency II: The never ending story". While it is true that Solvency II has been a long project and that we still need some final decisions before starting its implementation, I believe that we have now a clear plan to deal with this last hurdles so I remain confident and prefer to put the emphasis on the message "Solvency II is coming closer".

The EU is currently facing an outdated and fragmented regulatory regime in insurance (Solvency I). This regime is not risk sensitive, contains very few qualitative requirements regarding risk management and governance and does not provide supervisors with adequate information on the insurers' risks. Consequently, national authorities have been introducing different elements on their regimes in order to cope with market developments.

Risk of delay

In the recent financial sector assessment program of the EU the IMF states that continued delays in the implementation of Solvency II could create vulnerabilities in the insurance sector by not having a risk sensitive regime and recognizes that weaknesses in insurance supervision in several EU member states will remain in the absence of Solvency II.

In this context, I believe that there is full recognition by the different stakeholders that 2013 is a crucial year for Solvency II.

Following the agreement by the EU political institutions, EIOPA launched the long-term guarantee assessment (LTGA) that aims to test various measures that have been discussed in the political negotiations. EIOPA supports this approach because it is essential for policyholder protection and financial stability that Solvency II appropriately reflects the long-term financial position and risk exposure of undertakings carrying out insurance business of a long-term nature.

The assessment will focus on the evaluation of the following key features (individually and in combination): adapted relevant risk-free interest rate term structure ("Counter-cyclical Premium"); extrapolation; matching adjustment

("Classic" and "Extended"); transitional measures; and extension of the "Recovery Period".

We need a robust framework that would price correctly any options embedded in the contracts and that captures the true economic reality of the asset-liability position of insurers. We need to recognise that guarantees have a price - there is no "free lunch". We are encouraged by the level of participation in the different member states: more than 500 undertakings including big, medium and smaller players are running the exercise. We plan to present the LTGA findings as well as our conclusions in June.

I am confident that EIOPA's independent supervisory assessment will provide a reliable basis for an informed political decision on the long-term guarantee measures to be included in Solvency II.

On top of the LTGA, EIOPA sees it as of key importance that there will be a consistent and convergent approach with respect to the preparation of Solvency II. So what exactly are we doing? Following our Opinion in December 2012 we will issue Guidelines that will ensure that national supervisory authorities will put in place certain important aspects of the new prospective and risk based supervisory approach from the 1st of January 2014.

The Guidelines are to be issued under Article 16 of EIOPA Regulation and support the corresponding provisions of the Solvency II Directive.

These Guidelines will cover a number of fundamental areas for the effective preparation for Solvency II: system of governance, including risk management; forward looking assessment of the undertaking's own risk (based on the ORSA principles); submission of information to National Supervisors; pre-application for internal models.

It is up to national supervisors to determine how to comply with EIOPA's Guidelines by incorporating them into their regulatory or supervisory framework in an appropriate manner. Also due proportionality should be applied during the preparation phase and that is reflected in the guidelines.

Good preparation is crucial

It is important to note that we are not anticipating Solvency II, but preparing supervisors and undertakings for the new regime in a consistent way. We are working in close cooperation with the European Commission and with EIOPA's Insurance and Reinsurance Stakeholder Group. Furthermore, all the interested parties will be able to provide their feedback on the Guidelines during the public consultation that was launched on 27 March. We plan to finalize the Guidelines in autumn 2013.

This reform is important and is needed. And by making all the necessary actions in a consistent and convergent way, we all will make another step towards an appropriate basis for increasing policyholder protection and reinforcing financial stability.