

**EQUIVALENCE UNDER
SOLVENCY II: THE SYSTEM OF
GOVERNANCE OF
(RE)INSURANCE UNDERTAKINGS**

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Solvency II and Hong Kong: Too far or too close?

- A Brief Overview of Solvency II
- The Assessment of Equivalence Under Solvency II: The Third Countries
- The Impact of such an Assessment on (Re)Insurers based in Hong Kong
- Focus on the System of Governance under Solvency II

Solvency II

Pillar I

Quantitative
Requirements

Pillar II

Supervisor
Review

Pillar III

Disclosure
Requirements

Pillar I

is the detailed quantification and modeling of risk and capital adequacy

- Technical Provisions
- Investment rules and ALM
- Capital requirement rules

Pillar II

is the establishment of management practices to manage risk and capital

- Internal controls and sound management
- Supervisory intervention

Pillar III

is the disclosure and reporting of risk, capital and management practices to the regulators and the market

- Information Disclosure Principles
- Information Transparency Requirements

Solvency II implementing framework

Level 1

- Framework Directive 2009/138/EC as amended by the second Quick Fix Directive (Omnibus II)

Level 2

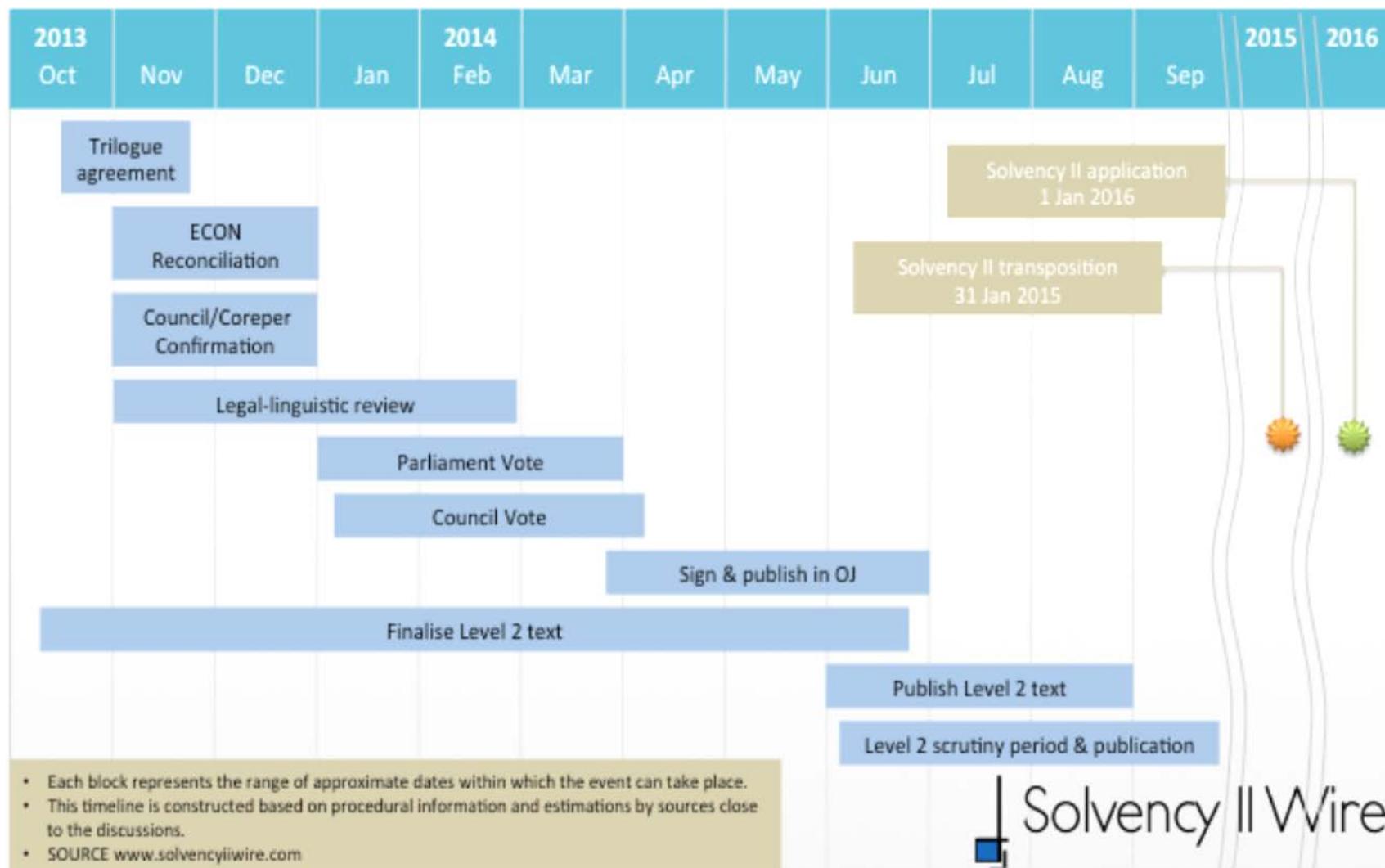
- Implementing Measures – delegated acts (EU Commission)
- Technical Standards (EIOPA)

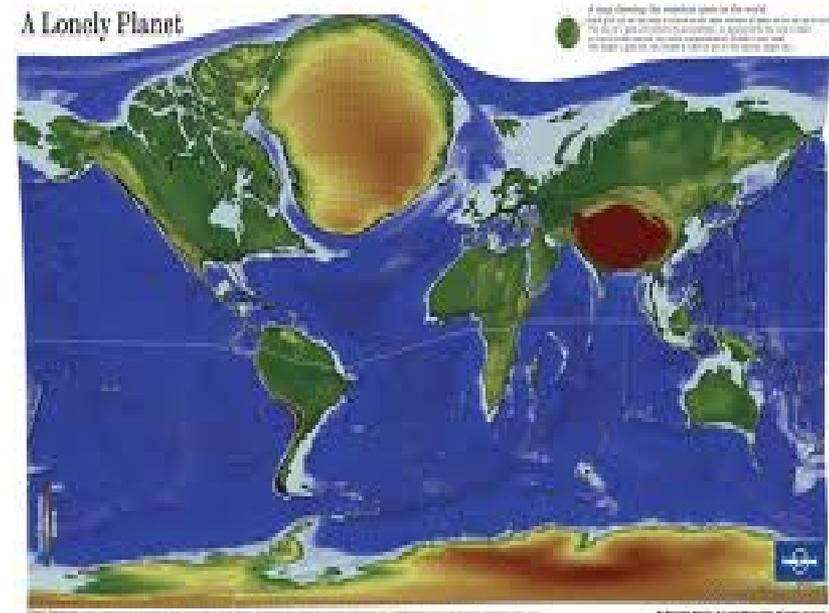
Level 3

- Guidance by EIOPA to ensure consistent implementation and cooperation between Member States

Solvency II: potential legislative path

(As at 6 Oct 2013)





Equivalence Assessment of Third Countries: Who's next?

All created equal?

Countries seeking equivalence	Countries seeking transitional equivalence	Initial talks on equivalence	Different approach needed
Japan	Australia	Brazil	US
Bermuda	Chile	China	
Switzerland	Hong Kong	Turkey	
	Israel		
	Mexico		
	Singapore		
	South Africa		

Source: European Commission, Eiopa

The Principle of Equivalence

- The overarching principle of equivalence is to ensure that a third country supervisory regime ensures a similar level of policyholder and beneficiary protection as Solvency II.
- There are three tests for equivalence:
 - Reinsurance** (Article 172)
 - Group solvency calculation** (Article 227)
 - Group supervision** (Article 260)

Reinsurance

- A test of whether a **third country's solvency regime** applied to **reinsurance activities of third country undertakings** is equivalent to that laid down in the Solvency II Directive.

Group Solvency Calculation

- A test of whether an **insurer in a third country owned by an insurer in the EU** is subject to a solvency regime equivalent to that laid down in the Solvency II Directive

Group Supervision

- A test of **group supervision**, not of a third country's supervision of solo entities

Reinsurance

- A determination of equivalence will allow reinsurance contracts **to be treated in the same way** as reinsurance contracts within the EEA.

Group Solvency calculation

- A determination of equivalence will allow groups to take into account the local third-country calculation of capital requirements and available capital **rather than calculating on a Solvency II basis** for the purposes of the deduction and aggregation method.

Group Supervision

- A determination of equivalence will allow **member states to rely on the group supervision exercised by the third country supervisor**, if EU insurers have a parent undertaking in a third country.
- Member state supervisors will form a college **led by the third country group supervisor**

The assessment of equivalence

Who will make the assessment?

How will the assessment be made?

Who will make the assessment?



EIOPA's QUESTIONNAIRE FOR EQUIVALENCE - GAP ANALYSIS

- Powers and responsibilities of third country supervisory authorities
- Professional secrecy, exchange of information and promotion of supervisory convergence
- Taking up of business of reinsurance
- System of Governance; Supervisory Review and Public Disclosure
- Changes in business, management or qualifying holdings
- Solvency Assessment
- Parent undertakings outside the Community: group supervision

The assessment of equivalence

We have the entities charged of the assessment.

.... Do we find the EU rules with which the rules of the Third Countries should be assessed?

... Solvency II is only a framework directive ...

The technical implementation of the Solvency II regime

EIOPA is going to prepare

- Two sets of Implementing Technical Standards that are legally binding and aim to ensure the uniform application of the Solvency II Directive:
 - Set 1: “Approval processes”;
 - Set 2: “Pillar 1 (quantitative basis), Pillar 2 (qualitative requirements), Pillar 3 (enhanced reporting and disclosure) and supervisory transparency”.
- Two sets of Guidelines that are necessary to guarantee convergence of the Solvency II implementation:
 - Set 1: “Guidelines relevant for approval processes, including Pillar 1 (quantitative basis) and internal models”;
 - Set 2: “Guidelines relevant for Pillar 2 (qualitative requirements) and Pillar 3 (enhanced reporting and disclosure)”.

On 31 January 2014, EIOPA has set up the timeline for the delivery of the Solvency II Implementing Technical Standards and Guidelines

Timeline:

- April – June 2014 Public consultation on the Set 1 of the ITS
- June – September 2014 Public consultation on the Set 1 of the Guidelines
- 31 October 2014 Submission to the EC of the Set 1 of the ITS
- December 2014 – March 2015 Public consultation on the Set 2 of the ITS
- December 2014 – March 2015 Public consultation on the Set 2 of the Guidelines
- February 2015 Publication of the Set 1 of the Guidelines in all the official EU languages
- 30 June 2015 Submission to the EC of the Set 2 of the ITS
- July 2015 Publication of the Set 2 of the Guidelines in all the official EU languages
- 1 January 2016 Application of the Solvency II regime

EIOPA's Guidelines on preparing to Solvency II

In October 2013 EIOPA issued guidelines for preparation for Solvency II.

These aim to ensure that the National Competent Authorities, insurance companies and groups take active steps towards a consistent and convergent implementation of key elements of Solvency II and they cover the areas of:

- Systems of governance;
- A forward looking assessment of undertakings' own risk (based on ORSA principles);
- Submission of information;
- Pre-application for internal models

Focus on the System of Governance

- Unlike the other profiles, the System of Governance is laid down almost entirely



- EIOPA's Questionnaire for Equivalence



- Guidelines on System of Governance issued by EIOPA in October 2013

EIOPA's Questionnaire: System of Governance.

The solvency/prudential regime of the third country shall require domestic insurance and reinsurance undertakings carrying out reinsurance activities to have in place

An effective **system of governance** which provides for sound and prudent management of the business, and require groups to have in place such a system at the level of the group

An effective **risk management system** comprising the strategies, policies, processes and internal and supervisory reporting procedures necessary to identify, measure, monitor, manage and report the risks to which the undertaking is or could be exposed, and their interdependencies, as well as an effective **internal control system**.

Guidelines on System of Governance under Solvency II: An Overview

In October 2013 EIOPA issued 52 Guidelines that cover

- General Governance Requirements
- Fit and Proper requirements for persons who effectively run the undertaking or have other key functions
- Risk Management system
- The “prudent person” principle
- Own Fund requirements
- Internal Controls
- Internal Audit Function
- Actuarial Function
- Outsourcing
- Group Governance Specific Requirements

Guidelines on System of Governance under Solvency II: An Overview

- The Guidelines provide direct references to the corresponding provisions set out in Solvency II Directive.
- However EIOPA acknowledges that certain parts of Solvency II Directive are to be revised by the OMDII and that delegated acts proposal have not yet been finalized by the European Commission yet

.... The yard is still open

Guidelines on System of Governance under Solvency II: An Overview

The following Guideline has been the most criticized in the public consultation and it refers to the decision making:

The undertaking ensures that at least two persons effectively run the undertaking. That implies that any significant decision of the undertaking involves at least two persons who effectively run the undertaking before the decision is being implemented

Group Governance Specific Requirements

The parent insurance or reinsurance undertaking or insurance holding company identifies the **responsible entity** and reports it to the group supervisor

the responsible entity **sets adequate internal governance requirements** across the group appropriate to the structure, business and risks of the group and of its related entities

The responsible entity considers **appropriate structure and organization for risk management** at group level setting a **clear allocation of responsibilities** between all entities of the group

Group Governance Specific Requirements

The responsible entity:

- has in place appropriate and effective tools, procedures and lines of **responsibility and accountability** enabling it to oversee and steer the **functioning of the risk management and internal control systems** at individual level;
- has in place **reporting lines** within the group and effective systems for ensuring **information flows in the group** bottom up and top down as well;
- **documents and informs all the entities in the group** about the tools used to identify, measure, monitor, manage and report **all risks to which the group is exposed**; and
- takes into account **the interests of all the entities** belonging to the group and **how these interests contribute to the common purpose of the group** as a whole over the long term.

Group risk management

The responsible entity

- **considers** in its risk management system **the risks** both at individual and group level and **their interdependencies**.
- **supports** in its risk management at the level of the group by appropriate processes and procedures **to identify, measure, manage, monitor and report the risks** that the group and each individual entity are or might be exposed to.
- ensures that the structure and organization of **the group risk management do not impair the undertaking's legal ability** to fulfill its legal, regulatory and contractual obligations.

Once again
Solvency II and Hong Kong:
Too far or too close?

Thank you for your attention

感谢您的关注！

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