

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

2007/0143(COD) - 10/07/2007 - Initial legislative proposal

PURPOSE: the reform of the EU's solvency provisions through the establishment of a single Directive: SOLVENCY II.

PROPOSED ACT: Directive of the European Parliament and of the Council.

BACKGROUND: existing solvency provisions are outdated. They are non-risk sensitive, they do not deal adequately with group supervision and they have been superseded by industry, international and cross-sectoral developments. Hence the need for a thorough reform of the EU's solvency provisions.

CONTENT: the purpose of this proposal, therefore, is a reform of existing EU solvency law and the establishment of second generation solvency provisions to be referred to as SOLVENCY II. The Solvency II project is one of the main outstanding items from the Financial Services Action Plan (1999 – 2005). Following the Commission's Better Regulation and Simplification agendas, the revision of the present solvency regime will recast 13 (re)insurance Directives into one single document, whilst simultaneously adding new requirements. The proposal applies the "re-casting" technique" which enables substantive amendments to existing legislation without a self-standing amending Directive, thereby rendering solvency provisions less complex as well as making EU legislation more accessible.

The main aim of EU solvency law is to ensure that insurance undertakings are financially sound and capable of withstanding adverse events in order to protect policy holders and to guarantee a stable financial system.

This proposal contains a number of amendments of a non-substantive nature in order to improve the proposed Directive's drafting. Articles, or parts of articles, which have become obsolete have been deleted. At the same time, however, a number of important new provisions have been inserted in order to modernise and update the EU's solvency law. In principle, the new solvency provision are based on, and follow, the four level structure of the Lamfalussy financial services architecture. This will allow the new solvency regime to keep pace with future market and technological developments as well as international development in accounting and (re)insurance regulation.

In essence, the new system will allow for more sophisticated solvency requirements for insurers, allowing them to guarantee that they have sufficient capital to withstand adverse events, such as floods, storms or big car accidents. Under existing requirements only insurance risks are covered. Under new requirements, however, future insurers will be required to hold capital against market risk, credit risk and operational risks.

Insurers will also be required to focus on the active identification, measurement and management of risks and to consider any future developments, such as new business plans or the possibility of catastrophic events that might affect their financial standing. Further, the proposed reform will oblige insurers to assess their capital needs in light of all risks by means of the "Own Risk and Solvency Assessment", whilst the "Supervisory Review Process" or SRP will shift the focus of supervisors from compliance monitoring and capital to evaluating insurers' risk profiles and the quality of their risk management and governance systems.

Moreover, the reform of the solvency provisions, will enable insurance groups to be supervised more efficiently, through a “group supervisor” in the home country that would have specific responsibilities to be exercised in close co-operation with the relevant national supervisors. This would entail a more streamlined approach to supervision that recognises the economic realities of such groups. The introduction of group supervisors will ensure that group-wide risks are not overlooked as well as enabling groups to operate more efficiently, whilst at the same time providing policyholders with a high level of protection. Groups that are sufficiently diversified may also be allowed to lower their capital requirements under certain conditions.