



# Solvency II

## Summary and update

November 2009



International Centre for  
Financial Regulation

# Contents

1. Background
2. Solvency II three pillar approach
3. Process for adoption of Solvency II
4. Lamfalussy process overview
5. Lamfalussy process regarding Solvency II
6. Solvency II – scheduled timetable

# Background

## **Solvency I**

- The solvency margin is the amount of regulatory capital an insurance undertaking is obliged to hold against unforeseen events. Solvency margin requirements have been in place since the 1970s and it was acknowledged in the third generation Insurance Directives adopted in the 1990s that the EU solvency rules should be reviewed
- The Directives required the Commission to conduct a review of the solvency requirements and following this review, a limited reform was agreed by the European Parliament and the Council in 2002. This reform is known as Solvency I

## **Solvency II**

- The Solvency I process illustrated that a further review of the overall financial position of an insurance undertaking was required, taking into account current developments in insurance, risk management, finance techniques, international financial reporting and prudential standards
- This project became known as Solvency II
- Solvency II is based on a three pillar approach which is similar to the banking sector (Basle 2) but adapted for insurance

# Solvency II's three pillar approach

## Pillar 1 Quantitative Requirements

- There are two capital requirements, (i) Solvency Capital Requirement (SCR) and (ii) Minimum Capital Requirement (MCR) - representing different levels of supervisory intervention
- SCR is a risk-based requirement and the key solvency control level. Solvency II sets out two methods for SCR calculation: the European Standard Formula or firms' own internal models. SCR covers all the quantifiable risks an insurer or reinsurer faces and takes into account of any risk mitigation techniques
- MCR is a lower requirement and its breach triggers the ultimate supervisory intervention: the withdrawal of authorisation

## Pillar 2 Qualitative Requirements

- The second pillar contains qualitative requirements on undertakings such as risk management as well as supervisory activities

## Pillar 3 Reporting & Disclosure

- Firms will need to disclose certain information publicly, which will bring in market discipline and help to ensure the stability of insurers and reinsurers (disclosure)
- In addition, firms will be required to report greater amount of information to their supervisors (supervisory reporting)

# Process for adoption of Solvency II

The new Solvency II provisions are to be adopted under the Lamfalussy process:

- (i) Level 1 Framework Directive setting out the key principles of the new system
- (ii) following adoption of the Solvency II Directive, detailed implementing measures will be introduced at Level 2. However, implementing measures will only be introduced in relation to the new Solvency II Articles and
- (iii) the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS <http://www.ceiops.eu/>), a Level 3 Lamfalussy committee and consisting of representatives from the various insurance supervisory authorities across Europe, will give advice to the Commission on the implementing measures

# Lamfalussy process overview

	What is it?	What are contents?	Who develops?	Who decides?
<b>Level 1</b>	Solvency II Directive	Overall framework principles	European Commission	European Parliament & European Council (co-decision process)
<b>Level 2</b>	Implementing Measures	Detailed implementing measures	European Commission	European Commission (consented by European Parliament)
<b>Level 3</b>	Supervisory Standards	Guidance regarding day-to-day supervision	CEIOPS	CEIOPS
<b>Level 4</b>	Evaluation	Monitoring compliance and enforcement	European Commission	European Commission

# Lamfalussy process regarding Solvency II

## Level 1 Directive

- Contains the broad framework and core political principles as decided by the Parliament and the Council on the basis of a proposal from the European Commission

## Level 2 Implementing Measures

- Technical measures are adopted by the Commission with the assistance of a regulatory committee and an advisory committee
- These committees help to ensure the provisions are up to date with market developments

## Level 3

- Implementation of Level 1 & 2 in Member States
- National regulators work on coordinating new regulations with other states and the "level 3 committees" such as CEIOPS

## Level 4

- Enforcement of the Solvency II regime

# Solvency II – scheduled timetable

April 2009

Publication of Level One Directive in the Official Journal

July 2009

CEIOPS released a further set of consultation draft advice on Level Two Implementing Levels (following its March 2009 consultation)

Autumn 2009

CEIOPS plans to release a further set of consultation draft advice on Level Two Implementing Levels (following its March and July 2009 consultations)

Sept 2009

FSA Stage 1 Thematic Review published

2010

European Commission drafts/consults on Level 2 measures

Q3 2010

FSA Stage 2 Thematic Review will be published

2011

Adoption of the Level 2 Implementing Measures

2011

Member States and industry prepare for implementation

Oct 2012

Solvency II comes into force (18 months after implementation)



This publication is produced by the ICFR and is intended for general guidance only.

***The ICFR grants permission to:***

- Download, display or print material for personal use or use within an individual organisation and for non-commercial use only.
- Create weblinks to these pages.
- Reproduce extracts provided the source is stated as being the “International Centre for Financial Regulation ([www.icffr.org](http://www.icffr.org))”.



International Centre for  
Financial Regulation

## ABOUT THE ICFR

The ICFR is a global collaboration between key players in the private and public sector with backing from major international financial institutions and professional services companies, as well as the UK Government and the City of London Corporation. Its mission is to address the critical issue of international financial regulation by creating new thought leadership, research, scholarship and training for the financial industry. While based in the City of London the ICFR serves a global constituency.

Further information may be found at: [www.icffr.org](http://www.icffr.org).

**The International Centre for Financial Regulation is incorporated as a company limited by guarantee in England and Wales**

**Company Number 6625422**

**Registered Office 5<sup>th</sup> Floor, 41 Moorgate, London EC2R 6PP, United Kingdom**



International Centre for  
Financial Regulation