19 December 2011

Our ref: ICAEW Rep 121/11

Your ref:

Karel van Hulle
Head of Unit
Insurance and Pensions, Financial Institutions
European Commission
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Dear Mr van Hulle

Solvency II Implementation

ICAEW is writing to highlight our members' continuing concerns regarding the approach and timetable for implementation of Solvency II.

ICAEW is a world-leading professional accountancy body, which works in the public interest. We provide leadership and practical support to over 136,000 member chartered accountants in more than 160 countries, working with governments, regulators and industry in order to ensure that the highest technical and ethical standards are maintained. ICAEW is listed in the Commission's Interest Representative Register (ID number: 7719382720-34).

ICAEW members operate across a wide range of areas in business, practice and the public sector, including within the insurance industry. In 2007 ICAEW established a Financial Services Faculty to be a world class centre for thought leadership on issues facing the financial services industry. It draws together professionals from across the financial services sector including the 25,000 ICAEW members specialising in the sector.

The European Parliament is not expected to consider the Omnibus 2 Directive in plenary until mid-April 2012. Particularly against that background, we are writing to highlight our members' continuing concerns in relation to the continued lack of clarity over:

- when the detailed Solvency II requirements will be approved,
- when they will be made available to all parties (not just key stakeholders),
- when they will come into force and
- what the effect of transitional provisions will be.

We recognise that the expansion in scope of Omnibus 2 has made the process of developing the detailed implementing measures extremely difficult. However we urge that priority is given to planning the overall implementation approach and timetable and to setting out a fully transparent roadmap for the insurance industry and for regulators.

The recent positions expressed in the various Omnibus 2 drafts appear to result in Solvency II implementation being split, with some regulatory requirements coming into effect from 1 January 2013

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and others on the date on which firms need to comply fully, being 1 January 2014. However, the planned approach to Solvency II implementation remains lacking in transparency. There is a lack of clearly defined milestones and no visible implementation planning. We believe the situation has been exacerbated by the on-going use of key stakeholders to consider material that is not shared with the wider insurance community, which has led to a two tier approach being applied within Europe.

The result is that the bulk of the industry and its professional advisers still have no tangible basis on which to plan their own implementation strategies. Despite this, firms across Europe (including international businesses) have no choice but to proceed with establishing internal governance, calculation and reporting processes, with a view to the bulk of this being completed next year. The benefits of the (substantial) pan-European investment to achieve the significant changes required properly to implement Solvency II are at risk of being significantly diminished while firms remain in a position of not knowing the full set of requirements that will apply to them. This is also hindering efforts to explain Solvency II impacts clearly and credibly to investors, analysts, regulators and, of course, customers. This seems entirely contradictory to one of Solvency II's key aims of increasing market transparency.

There are a number of particular areas with a direct impact on our members that we would like to emphasise as requiring rapid and fundamental attention, including:

- Transitional arrangements
- Technical provisions
- Investor relations.

We have set out the key issues we would like to highlight in relation to each matter below.

Transitional arrangements

Firms require a clear understanding of the approach to the transition from the current solvency regime to Solvency II and, in particular, what may be required from national regulators in relation to the transitional period. In this respect, the UK FSA and HM Treasury, by both releasing consultation papers addressing the transition of Solvency II within UK legislation, are well ahead of their other EU colleague organisations, and we have yet to see anything from other regulators. However, the FSA paper is limited in that it notes that a second consultation will be required in 2012 to address those areas that are still being considered within Europe.

The approach to transition will have a very significant impact on firms' existing and developing strategic plans, going far beyond the immediate application of Solvency II. This includes, but is not limited to:

- Potential mergers and acquisitions activity
- Product development and product pricing
- Management of accounting and reporting processes and functions
- Balance sheet management including risk re-balancing activities.

A lack of clarity on the final form of the requirements could lead to uneconomic decisions being made, potentially increasing the cost burden on the wider economy at a time when this is particularly undesirable.

We would request that the Commission sets out clearly how it expects the transitional period to operate and what should be expected of firms and regulators during that period. A particular matter that needs addressing is the form of any 2013 reporting requirements – an area where the European Parliament and Council proposals under Omnibus 2 currently differ significantly. We also seek confirmation that any such requirements will be adopted consistently across the EEA, and that this will not be at Member State discretion.

Technical provisions

The continued lack of clarity over the approach and requirements for a number of fundamental aspects within the calculation of technical provisions remains of great concern. In particular we would highlight matching premium, the construct of the countercyclical premium, contract boundaries and grandfathering for annuities as areas where our members have expressed significant concern.

As the Commission is aware, there is potential for very real damage to be done to the wider economy if certain types of otherwise successful and valuable products are rendered uneconomic due to overly conservative capital requirements, leading to their withdrawal from the insurance market.

Furthermore, we are concerned that the ability to make further revisions to the technical standards through to 2016 (as proposed in relation to EIOPA's role in drafting technical standards under the Council's version of Omnibus 2) leaves open the possibility of further adjustments and revisions to existing standards, in turn creating further uncertainty and potential rework for firms.

We would request the Commission to reconsider the approach that is proposed during this period and consider establishing very strict criteria regarding the areas where technical standards can be delayed to avoid the possibility of rolling revisions being required to be implemented by firms until 2016.

In addition, while uncertainty remains in relation to these issues, core strategic and management decisions (such as product development, pricing and approaches, customer support and advice) are extremely difficult to make.

Investor relations

For the reasons noted above, the current uncertainty has resulted in a situation where firms are currently unable to explain thoroughly and effectively to their investors the impact of Solvency II on their businesses. As stated above, this is very unhelpful from a market transparency perspective.

As might be expected, this level of uncertainty over the strength of capital of a firm (or insurance group); their ability to develop new, profitable products; and the reliability of their distributable cash flows is creating a degree of discomfort within the wider investment community, with the potential for market instability. In the short term, the ability of insurers to raise capital from the market and/or deliver strategic plans could be limited.

We would request that the Commission considers the points raised above. In particular, as a priority we would like the Commission to set out and effectively communicate a clear and full roadmap for implementing the Directive with the minimum of further uncertainty.

I am copying this letter to Sharon Bowles and Burkhard Balz (European Parliament), Gabriel Bernardino (EIOPA), Michaela Koller (CEA), Bridget Micklem (HM Treasury), Victoria Raffé (UK FSA) and Alan Ball (Bank of England).

Yours sincerely

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