

## Your contacts for Solvency II issues

PricewaterhouseCoopers has a multi-disciplinary team of specialists who can assist your organisation with the implementation of Solvency II.

Our specialists combine a broad range of experience within insurance and other financial institutions, including internal modelling, regulatory capital requirements, data management, best practice Enterprise-wide Risk Management (ERM) and project management.

To discuss the implications of Solvency II in more detail, please speak to your usual PricewaterhouseCoopers contact or one of the people listed:

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# Solvency II: It's going to change the business landscape\*



In July 2007 the European Commission issued a draft framework Directive for an entirely new, rationalised and harmonised EU-wide solvency regime for insurance and reinsurance entities. This proposes a comprehensive principles-based and risk-sensitive solvency regime. Preconditions for principles-based supervision are the responsibility of the board of directors and senior management, their integrity, adequate risk culture and transparency.

Under the Solvency II framework, companies will be expected to formalise their system of governance, risk management and operational control to ensure sound and prudent management of the business. This

will include transparent organisational structures with clearly defined allocation of responsibilities, effective reporting lines, and the requirements to maintain certain core functions (including risk management, compliance, internal audit and actuarial function)

Essentially, companies will be required to demonstrate that risk and capital management are integral to their strategic decision-making process and to provide annual, publicly available reports on their solvency and financial condition.

Solvency II will promote convergence between Enterprise Risk Management (ERM) and regulatory and compliance requirements. This convergence will impact strategic and operational decisions in all areas of the enterprise.

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## Where are you now ?

Solvency II is now entering a crucial period. We know its “spirit” - the key principles and requirements which underpin it. Beginning now to anticipate and factor Solvency II requirements into current projects and future plans – systematically – will facilitate a smooth, timely and cost-efficient transition to the new regime.

If insurers and reinsurers want to be amongst the better placed, if not the best placed, to comply with Solvency II requirements, they need to gain a clear understanding of the implications of Solvency II now and monitor developments as they occur. In tandem, internal task forces can begin to assess those implications against current operations, risk management and risk control practices, and look to minimise future efforts through exploiting synergies with other projects today.

A key consideration in defining your companies’ ambition for Solvency II is deciding whether this is primarily a compliance challenge or a business opportunity to realise the payback on this investment by setting up an ERM framework that will strengthen the governance, operations and competitive potential of the business. Table 1 outlines the key elements of compliance and what steps will be needed to achieve it. It provides not only a benchmark for your firms own preparation plans, but also enables you to compare your readiness to your competitors.

**Table 1 – Readiness for Solvency II**

Key Areas	Typical Base	Next Steps	Full Compliance
<b>Own Risk &amp; Solvency Assessment (ORSA)</b>	<ul style="list-style-type: none"> <li>Own Risk Profile well understood</li> <li>Material risks identified, documented and quantified in a risk register</li> </ul>	<ul style="list-style-type: none"> <li>Develop internal assessment / ERM framework for                             <ul style="list-style-type: none"> <li>Risk Appetite</li> <li>Solvency needs</li> <li>Compliance with capital requirements</li> <li>Managing and reporting continuously individual and aggregate risks, and interdependencies</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>ORSA forms integral part of strategic business decisions and ERM framework</li> <li>Used on a continuous basis</li> </ul>
<b>Quantitative Requirements</b>	<ul style="list-style-type: none"> <li>Solvency I and local supervisory solvency requirements</li> </ul>	<ul style="list-style-type: none"> <li>Quantify potential impact of SCR standard formula on solvency position</li> <li>Reconcile and explain internal model results (if used) with SCR standard formula</li> </ul>	<ul style="list-style-type: none"> <li>Quarterly calculation of MCR</li> <li>Annual calculation of MCR</li> <li>Ability to manage and monitor solvency position on continuous basis</li> </ul>
<b>Technical Provisions</b>	<ul style="list-style-type: none"> <li>Booked reserves under local GAAP contain implicit margin for prudence</li> <li>Actuarial/statistical methods not always used</li> </ul>	<ul style="list-style-type: none"> <li>Aware of impact of new valuation basis on balance sheet, solvency and profit &amp; loss</li> </ul>	<ul style="list-style-type: none"> <li>New reserving basis ‘business as usual’</li> <li>Technical provisions incorporate best estimate, discount and risk margin</li> </ul>
<b>Internal Model</b>	<ul style="list-style-type: none"> <li>Models used for specific purposes, e.g. pricing, reinsurance purchase, capital management</li> <li>Models may be partially integrated with business</li> <li>Models may not be used</li> </ul>	<ul style="list-style-type: none"> <li>Prepare for supervisory approval process</li> <li>Document and demonstrate compliance with:                             <ul style="list-style-type: none"> <li>Use test</li> <li>Calibration and validation test</li> <li>Statistical quality test</li> </ul> </li> <li>Develop internal governance, validation and audit procedures</li> </ul>	<ul style="list-style-type: none"> <li>Internal Model widely used in system of governance and in strategic decisions</li> <li>Model approved by Supervisor</li> <li>Regular cycle of model validation and control</li> </ul>
<b>Disclosure</b>	<ul style="list-style-type: none"> <li>Communication privately to regulator</li> <li>Limited information</li> </ul>	<ul style="list-style-type: none"> <li>Collate information</li> <li>Prepare policy on public disclosure</li> <li>Synergies with IFRS</li> </ul>	<ul style="list-style-type: none"> <li>Annual public disclosure</li> <li>Solvency and Financial Condition Report</li> </ul>

## How PwC can help

Where are you on Solvency II?	How PricewaterhouseCoopers can help
<b>We want to take advantage of the strategic opportunities Solvency II offers</b>	<p>We can work with you to exploit the opportunities presented by Solvency II to:</p> <ul style="list-style-type: none"> <li>Develop an Enterprise-wide Risk Management (‘ERM’) framework that will yield the following:                             <ul style="list-style-type: none"> <li>An optimal capital structure based on chosen risk appetite preference</li> <li>An optimal organisational structure that is fit-for-purpose and will facilitate required returns on capital</li> <li>Fulfil Pillar I and II Solvency II requirements when Solvency II comes into force</li> <li>Influence positively external perceptions of performance: rating agencies, analysts, shareholders:</li> <li>Minimise regulatory pain:</li> <li>Optimise possibilities to reduce regulatory burden</li> <li>Ensure good dialogue with key regulators</li> </ul> </li> <li>Maximise the value on the cost of Solvency II implementation</li> </ul>
<b>We have begun implementing our response to Solvency II</b>	<p>We can support you through:</p> <ul style="list-style-type: none"> <li>The QIS4 submissions</li> <li>The review and consolidation of Solvency II project plans. Checking for completeness so that you are confident that you have captured all aspects of Solvency II</li> <li>Provision of regulatory compliance, risk, actuarial, data and project management experts to assist with the implementation of your project</li> </ul>
<b>We have carried out a gap analysis / readiness assessment but are not feeling confident about the way forward</b>	<p>We can work with you at a group or divisional level to review your gap analysis to check that it:</p> <ul style="list-style-type: none"> <li>Contains all relevant business lines and products</li> <li>Is complete in its understanding of the scope of Solvency II</li> <li>Defines a realistic project implementation plan</li> </ul>
<b>We have not yet started on Solvency II</b>	<p>We can work with you to:</p> <ul style="list-style-type: none"> <li>Deliver workshops with relevant parts of the business on Solvency II</li> <li>Develop heat maps to help you understand the main impact areas</li> <li>Undertake a gap/impact analysis on Solvency II</li> <li>Develop project plans based on the impact assessment</li> </ul>

