WHY DOES GETTING SOLVENCY II RIGHT MATTER?

Why is the 2020 Solvency II review important?

- **Solvency II is a risk-based regime that is strongly supported by the European insurance industry, but it creates unnecessary constraints for long-term business and investment and is overly burdensome**. It was introduced not because of a solvency problem, but to harmonise diverging local regulations, align regulatory practices to the modern capital and risk management approaches used by many companies and ensure consumers are given consistent, high levels of protection. Solvency II has largely achieved its objectives, so what is required is a limited set of focused changes and not an overhaul.
- **The 2020 review of Solvency II provides a key opportunity to improve the design and calibration of the framework**. Beyond this, the Solvency II review has to be regarded in the context of the broader economic and environmental realities that Europe is facing, including challenges related to achieving economic growth and technological innovation, global competitiveness and addressing climate change and the ageing society.
- **Making improvements to Solvency II matters for the role insurers play in society and the economy. This will ensure that the industry can**:
  - support greater economic growth;
  - provide a diversified and affordable choice of insurance products, including guaranteed and pension products;
  - be the source of capital for long-term and sustainable investments; and
  - continue to be competitive internationally.

Why does getting Solvency II right matter?

The link between Solvency II and insurers' role in society and economy

Solvency II has a major impact on the insurance industry. Capital and other requirements drive the industry's capacity to cover risks, the ability to offer guarantees and the level and type of investments that can be made.

- Solvency II has a number of issues that lead to inflated capital requirements overall and artificial volatility, including cliff-edge effects. This creates constraints on the industry, unnecessarily limiting its ability to write long-term business and invest long-term and its capacity to cover risks for customers.
- In addition, from a global regulatory level playing field perspective, Solvency II is an extremely conservative and costly framework. Other jurisdictions appear to have taken much greater account of their economic and social goals in the design and calibration of their regulatory frameworks.

The 2020 review should address the issues related to long-term business and reduce the overall burden the framework creates, while maintaining its strong, risk-based foundations.

This will result in a justified reduction in overall capital requirements and thereby increase the industry's capacity to support Europe's needs. Freeing capital resources from non-economic requirements will make it possible to finance the EU's agenda strengthen the leadership of the European insurance industry and further expand the boundaries of insurability, thus reducing the insurance protection gap without undermining the resilience and solvency of the sector.

The review should result in focused changes that help, and do not hinder, insurers in playing a key role in supporting Europe's need for investment to achieve carbon neutrality and economic growth.

SOLVENCY II

Key problems: Solvency II does not measure long-term business correctly and is too burdensome

Solvency II currently leads to:
- Inflated capital requirements
- Artificial volatility, including cliff-edge effects

As a result, Solvency II is an unnecessarily conservative and costly framework.

In turn, this creates constraints on the industry:
- It unnecessarily limits the ability to write long-term business and invest long-term in the economy
- It affects the capacity to cover risks for customers
- It damages the European insurance industry's global competitiveness

Key opportunity: Introduce focused improvements

The 2020 review should:
- Improve the measurement of insurers' liabilities
- Improve the capital treatment of long-term assets
- Make proportionality work in practice
- Reduce the reporting and disclosure burden

An improved Solvency II can help ensure:
- More long-term investment and greater economic growth
- Guarantees and right investments are available to citizens (eg pensions)
- The increased ability of insurers to make sustainable investments
- A competitive European insurance industry internationally

The 2020 Solvency II review — what should and should not change

The 2020 review should:
- **Improve the measurement of insurers' liabilities**, to better support the link between assets and liabilities.
- **Introduce focused improvements** to:
  - reduce the Risk Margin
  - improve the Volatility Adjustment (VA) so that it is higher and better at reducing artificial volatility
  - allow the Dynamic VA for standard-formula users
  - improve the calibration of long-term assets, such as equity and real estate
- **Reduce the burden of reporting** and disclosures.
- **Enhance proportionality** and make it work in practice.

At the same time, the review should definitely:
- Not introduce changes to the Euro Last Liquid Point or extrapolation methodology and transitional measures.
- Not introduce new requirements relating to best estimate and group supervision or new supervisory powers of intervention.
- Not result in any new macro-prudential measures beyond the scope requested by the European Commission.
- Not introduce an uneconomic calibration to the interest rate risk module. EIOPA's proposals on interest rate risk are excessive and they must be reviewed and include a reasonable limit.