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EU Insurers Must Act Now to Meet Solvency II Deadline

Juergen Weiss

The European Parliament has taken a first step toward harmonizing risk management for insurers in the European Union by approving the Solvency II framework. But delegates quashed stronger plans for cross-border regulation.

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NEWS ANALYSIS

Event

On 22 April 2009, the European Parliament approved the Solvency II directive with an 87% majority. Solvency II is designed to protect policyholders and beneficiaries in the European Union (EU) by defining a set of capital and reporting requirements for insurance companies. It addresses quantitative and qualitative risk management, as well as market transparency and guidelines for disclosure to regulatory authorities. Each EU member state must make Solvency II a part of national law before the end of October 2012.

Analysis

Solvency II is a first step toward the harmonization of financial supervision in the EU. Insurers will have to establish more advanced internal risk management systems or possibly face having their licenses revoked by regulators. This will lead to further consolidation in the European insurance sector, as smaller insurers merge to reduce the cost of compliance. Increased financial transparency will "level the playing field," improving the international competitiveness of many European insurers. (See "How Solvency II Will Transform European Insurance Markets by 2018, and How IT Can Respond" for more implications.)

While Solvency II supports the current trend toward improving risk management standards, the European Parliament missed the opportunity to establish stronger cross-border regulation. The European Commission's initial proposal for Solvency II included "group support" measures that would have increased supervision of multinational groups. Resistance from EU member states meant that these measures were removed from the final directive. Although the parliament will review this decision in 2015, Gartner is concerned about the protectionist spirit it reveals.

October 2012 is an ambitious deadline for IT departments to support the new framework, considering the major investments required. Insurers will have to:

- Harmonize and normalize relevant data.
- Establish a rigid risk management system.
- Re-engineer business processes such as underwriting and product development.
- Prepare documentation for the Own Risk Solvency Assessment (ORSA.)

For more detail on the requirements, see "Much More Than Compliance: How Solvency II Will Impact Insurance Business Processes and IT Systems."

Insurers in other regions will also be affected, because Solvency II will create a de facto global risk management and financial-transparency standard. Rating agencies, global reinsurers and regulators will base their decisions on these rules, which will create a competitive disadvantage for international insurers and potentially also other insurance markets. The Bermuda Monetary Authority has already introduced its own Solvency II-compliant regulations and Gartner expects that other non-European countries will follow its example.

RECOMMENDATIONS

European insurers focused on domestic markets:

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- Accelerate your compliance efforts. Although Solvency II might not be part of national law until October 2012, complying will be technically complex and time-consuming.
- Build cross-functional compliance teams involving business and IT users. IT project structures must be flexible to deal with changes in implementation details.

Pan-European insurers:

- Continue your harmonization efforts. Even though group support supervision is no longer part of the directive, unifying data and processes will improve your competitiveness.

RECOMMENDED READING

- "How Solvency II Will Transform European Insurance Markets by 2018, and How IT Can Respond" — Regulation will fundamentally transform how European insurers compete. **By Juergen Weiss**
- "Solvency II: Insurers Can Learn From Basel II Implementations" — Banks' experience with risk management has shown which approaches work best. **By Juergen Weiss**

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