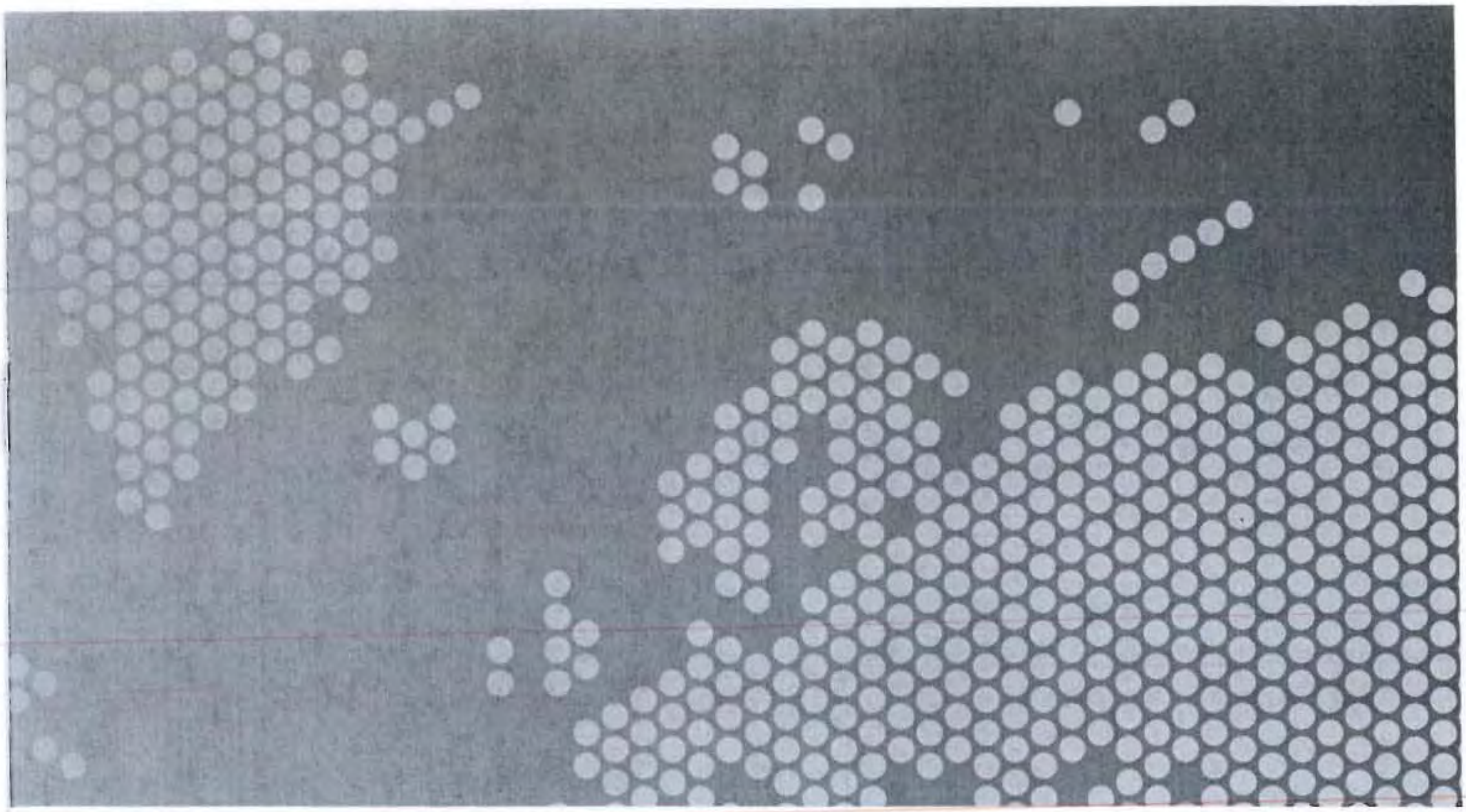

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GETTING TO THE BOTTOM OF SOLVENCY II

Günter Dröse of the European Captive Insurance and Reinsurance Owners' Association (ECIROA) discusses some of the issues surrounding the implementation of Solvency II

The much anticipated Solvency II legislative programme, which was originally due to take effect in 2012, continues to be an area of concern across the whole European captive industry. With indications pointing to 2016 as the new implementation date, significant work and preparation will be needed to ensure compliance once the fog has fully cleared surrounding the directive. To find out more, *Captive Review* spoke with Günter Dröse, of ECIROA, which has played a key role in representing the captive sector during Solvency II consultations.

Written by
Günter Dröse

Günter Dröse works as an independent insurance and risk management consultant since retiring as managing director from Deutsche Bank AG, where he was responsible for running Deukona, their in-house broker. He is chairman of ECIROA as well as an EIOPA Insurance and Reinsurance Stakeholder Group (IRSG) member.

Captive Review (CR): With 2016 now the likely implementation date for Solvency II, how prepared do you believe the captive industry currently is?

Günter Dröse (GD): I don't assume that in 2013 any of the captives have no clue as to how to proceed. There are two different areas of concern for captive owners:

a) the strategy and the purpose of the captive. This has to be internally discussed and considered, if and when Solvency II becomes problematic capital-wise (if an increase in capital is necessary) and cost-wise (a huge increase in workload is expected); and

b) the actual technical preparation to follow the Solvency II requirements in the three pillars as far as possible. This has been done by the captive manager and must be presented to the captive board or the captive owner.

In both areas the captive owners will test their ability to survive with their existing strategy or decide to adjust their concept in one parameter or another. The major captive management companies are proactively encouraging their clients to engage in this process.

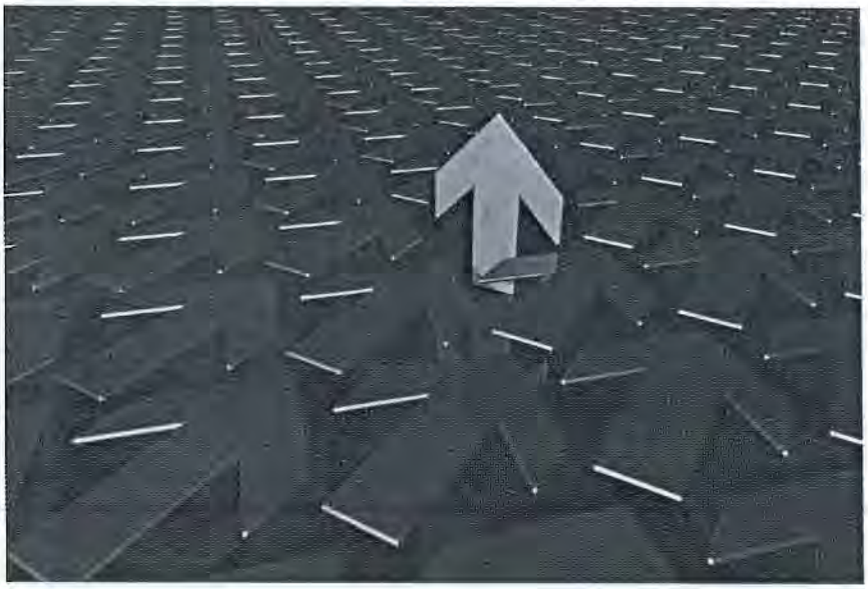
CR: Which of the three pillars of the framework will provide the greatest challenge?

GD: Pillar 1 is very technically determined but can be mastered by actuaries professionally. I don't believe Pillar 1 is the greatest challenge for well-managed captives but it could lead to a change in strategy, as mentioned above.

Pillar 2 is challenging because here the principle of proportionality has to be applied. ECIROA has produced guidelines on best practice for the level three guidance to reduce the requirements which obviously (based on the small size of captives) cannot be applied. We have sent this to the European Insurance and Occupational Pensions Authority (EIOPA) and are seeking to discuss this with them.

Pillar 3 will again increase the workload for captives, but a lot of the data to be delivered is a must under various local regulations anyway. What is new is the format and the density, but we can only report what we have. This distinguishes captives from the commercial (re)insur-

> **"Pillar 3 [of Solvency II] will again increase the workload for captives, but a lot of the data to be delivered is a must under various local regulations anyway"**



> "The requirements in the initial phase of a new principle-based regime should have been simpler, with less stringent rules and prescriptive requirements and with room to adjust and to develop over time in a gradual learning process"

ers, which have huge data sets. Again, ECIROA is proposing a proportionate reporting package for captives. It is clear that EIOPA expects that all companies submit the full set of templates in the format they require but for captives, some of these templates could be blank. It is also clear that captives do not need to report quarterly – annual reporting should be sufficient.

We have to perform some additional work, which aligns reporting for the benefit of EIOPA (and the European Central Bank is another user of this data). On the positive side, it is hoped that we will only need to change these processes once and that they can then be used going forward without the need for frequent adjustments.

CR: Andrew Bailey of the UK's Prudential Regulation Authority has spoken about the 'staggering cost' of Solvency II implementation, estimated at around £400m. Do you believe the compliance costs that captives have already incurred, and will occur, are too high?

GD: This is very difficult to judge. I assume that the cost calculations of all regulators and politicians are "big thumb" calculations. I am pretty sure that the cost per company will always be higher than predicted by officials.

CR: What role has ECIROA played in the consultation stage of Solvency II?

GD: We had and still have permanent contact with the European Commission and EIOPA (previously the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS)), in a similar way to other lobby groups. However, the impact of such connections is now reduced – the main problems around Solvency II are now connected to long-term guarantees (LTGs). Based on the market volume of our activities, we are recognized as being of minor importance in the general scheme of Solvency II development. On the other hand, we have been successful in achieving the acknowledgement that captives are valuable tools in the risk and insurance management processes of international corporations, which wasn't the common view of captives in the European Commission before.

£400M
ESTIMATED COST OF SOLVENCY II IMPLEMENTATION

CR: How much priority do you think captives have been given in discussions, in comparison to commercial insurers?

GD: As previously mentioned the public sector, politicians, parliament, ministries of finance and the EIOPA have applied the proportionality principle in our situation accordingly.

CR: There have been significant criticisms of Solvency II across the whole insurance industry. Do you believe these are justified?

GD: We have now had more than 10 years of Solvency II discussions and developments. Over the years two different groups have provided input in the preparation of the final texts. There was the group which was rather creative and driven by the firm will to structure Solvency II in a workable and easy-to-understand structure based just on principles (a challenge for all countries governed by codified law in general), and the other group, which has complicated Solvency II's development by raising a lot of complaints without providing a productive proposal on how to resolve the issues identified. The process has involved an increasing number of requests to determine a lot of small details – which, in my view, has been a rather redundant and superfluous exercise. At the same time, one of the most important questions has been postponed – relating to LTGs and the interest curve discussion. There are some other general inconsistencies which we anticipate will pop up later, once the new regime has started.

The requirements in the initial phase of a new principle-based regime should have been simpler, with less stringent rules and prescriptive requirements and with room to adjust and to develop over time in a gradual learning process. We are now seeing a more flexible attitude and perception develop in the European community due to the fact that there is no alternative – the first target is to get local supervisors on a level playing field. Nevertheless, my fears now are that local supervisors will exaggerate their requirements, with higher hurdles than anticipated by EIOPA.