

Equivalence under Solvency II

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Overview: equivalence under Solvency II

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What is equivalence under S2?

- EC & EEA SA have the authority to decide about the equivalence of the solvency and prudential regimes of a non-EEA country (a.k.a 3rd country)

EC : European Commission

EEA : European Economic Area

SA : Supervisory Authority

Areas of equivalence under Solvency II

Equivalence under S2 Directive: Article 172



- 3 main areas of equivalence under the Directive 2009/138/EC (S2 Directive):
 1. Article 172
 - Whether the **solvency regime** of a 3rd country applied to **reinsurance activities** of undertakings with their head office in that 3rd country is equivalent to S2 regime
 - Decision by **EC only**

Equivalence under S2 Directive: Article 227



2. Article 227

- Whether the **solvency regime** of a 3rd country applied to all domestic **(re)insurance undertaking** in that 3rd country is equivalent to S2 regime
- Decision by **EC or EEA group supervisor**

Equivalence under S2 Directive: Article 260



3. Article 260

- Whether the **prudential regime** in a 3rd country for the supervision of groups is equivalent to S2 regime
- Decision by **EC or EEA group supervisor**

Implications of positive equivalence finding

Implications of positive equivalence finding : Article 172



1. Article 172

- RI contracts concluded with such 3rd country undertakings to be **treated in the same manner** as RI contracts with EEA undertakings reinsurers – **no more favourably**
- In particular, EEA SA **shall not require pledging of assets** to cover unearned premium reserves and outstanding claims provisions

RI : reinsurance

Implications of positive equivalence finding : Article 227



2. Article 227

- Relevant to **EEA groups only**
- Where **D&A method** is used, may use the **local SCR & EOF** for such 3rd country (re)insurance undertakings that are related entities of an EEA group, in the group solvency calculation

D&A : Deduction & Aggregation (a.k.a. method 2)

SCR : Solvency Capital Requirement

EOF : Eligible Own Funds

Implications of positive equivalence finding : Article 260



3. Article 260

- Relevant to **groups headquartered in a 3rd country** with related EEA (re)insurance undertakings
- EEA SA **shall rely on the equivalent group supervision** exercised by such 3rd country SA

Implications of lack of positive equivalence finding

Implications of lack of positive equivalence finding : Article 172 EIOPA

- No positive finding from equivalence assessment, or no equivalence assessment

1. Article 172

- RI contracts concluded with such 3rd country undertakings **treated differently** from RI contracts with EEA undertakings reinsurers – potentially different treatment by each EEA SA - eg. limited risk mitigating effect recognised in solvency calculations of EEA cedant, collateral requirements.


Implications of lack of positive equivalence finding : Article 227 EIOPA

2. Article 227

- Where **D&A method** is used, use **S2 rules for the SCR & EOF calculations** of such 3rd country (re)insurance undertakings that are related entities of an EEA group, in the group solvency calculation

Implications of lack of positive equivalence finding : Article 260 EIOPA

3. Article 260

- Apply **S2 group supervision** to the whole group ⇒  jurisdiction issue
- Apply **other methods which ensure appropriate supervision** of the EEA (re)insurance undertakings in a group – eg. require establishment of an EEA subgroup and apply group supervision to the subgroup

Main criteria for equivalence assessment

Main criteria for equivalence assessment – 3rd country SA



1. Powers & responsibilities of 3rd country SA [Art172 & Art 260]
2. Requirements for prior authorisation of reinsurance business [Art172]
3. Requirements for ladder of timely supervisory intervention [Art172, Art227 & Art 260]
4. Requirements for professional secrecy obligations [Art172, Art227 & Art 260]
5. Ability to exchange of information [Art172, Art227 & Art 260]

Main criteria for equivalence assessment – solvency



1. Requirements for economic valuation of all assets & liabilities [Art172, Art227 & Art260]
2. Requirements for adequate financial resources of sufficient quality & prudently managed to cover policy liabilities & capital requirements [Art172, Art227 & Art260]
3. Requirements for risk based capital requirements or other supervisory mechanisms covering all significant risks [Art172, Art227 & Art260]

Main criteria for equivalence assessment – firms/groups



1. Requirements for effective governance [Art172 & Art260]
2. Requirements for effective risk management system [Art172 & Art260]
3. Requirements for effective risk management, compliance, internal audit & actuarial functions [Art172 & Art260]
4. Requirements for supervisory reporting & public disclosure [Art172 & Art 260]
5. Requirements for sound & prudent management of undertakings/group [Art172 & Art 260]

Main criteria for equivalence assessment – groups only



1. Scope of group supervision [Art260]
2. Solvency assessment & supervision at group level [Art260]
3. Requirements for intra-group transactions & risk concentration monitoring, managing & reporting [Art260]

About temporary equivalence (transitional)

Implications of temporary equivalence (a.k.a transitional)

- During transitional period (or until the 3rd country has been deemed equivalent whichever is earlier):
 - *same as positive equivalence treatment*
- After transitional period:
 - *If deemed equivalent : positive equivalence treatment*
 - *If not deemed equivalent or no equivalence assessment : lack of positive equivalence treatment*

Criteria for transitional equivalence assessment



1. Equivalent professional secrecy obligations
2. Public commitment for convergence towards S2-like regime
3. Robust & realistic convergence program
4. Existence of or moving towards risk-based regime
5. Willingness to engage in equivalence assessment during transitional period

 **High level gap analysis only, no onsite visit**

Initial equivalence assessment: lessons learnt & insights

Initial equivalence assessments: lessons learnt



- Living document on lessons learnt
 - Constantly developed over time to incorporate new experience gained in equivalence assessments
 - Circulated to top senior management of each EEA SA
 - Will be used widely in EIOPA including future equivalence assessments, technical inputs to EC on (transitional) equivalence assessments, development of L3 Guidelines to EEA group/individual supervisors

Initial equivalence assessments: insights (1/5)



- Team adequately staffed in size & expertise
 - Do not underestimate volume of work involved
 - ✓ Minimum of around 7 EIOPA team members per equivalence assessment – mix of SA experts & EIOPA staff
 - Required expertise includes
 - ✓ Supervisory/peer review experience
 - ✓ Actuarial
 - ✓ Legal
 - ✓ Group supervision

Initial equivalence assessments: insights (2/5)



- Lengthy process
 - At least 8 months to prepare final report for public consultation, extending to 10-11 months allowing for public consultation
 - 3rd country will be engaged all the way:
 - ✓ Questionnaire: focussed & self contained details
 - ✓ Onsite visit: preparations, presentations, discussions, wrap sessions/preliminary findings
 - ✓ Factual accuracy checks before report publication
 - ✓ Queries arising throughout

Initial equivalence assessments: insights (3/5)



- Importance of onsite visits
 - Onsite visit, not an inspection – work together
 - Adequate preparation for all parties involved: schedule, issues to be addressed, expectations
 - Ensure adequate resources and time
 - Wrap up session useful – discuss preliminary findings

Initial equivalence assessments: insights (4/5)



- Consistency between equivalence assessments
 - Rigorous exercise to ensure consistency:
 - ✓ Between different EIOPA equivalence assessment teams & assessments
 - ✓ Between findings and final conclusions – EIOPA advice to EC in the form of:
 1. meets the equivalence criteria,
 2. meets the criteria but with certain caveats,
 3. needs to undertake changes in the following areas (...) in order to meet the criteria

Initial equivalence assessments: insights (5/5)



- Possible cultural and/or language issues – e.g:
 - Different working styles
 - Same words may be interpreted differently
- Differences in terminology used and/or approach – to understand e.g:
 - Economic valuations – market consistent valuation - risk based valuation

Timeline

Current timeline (may be subject to change)



- Start 2013: EIOPA provide technical advice on identified transitional 3rd countries to EC
- Early 2013: revise & update initial equivalence assessment reports following official publication of S2 texts
- Mid 2013: equivalence decision by EC on initial equivalence assessments
- Mid-late 2013: decision by EC on final list of transitional 3rd countries



Thank you

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