Stand out for the right reasons
Financial Services Risk and Regulation

Solvency II – One size fits small?

February 2016

Highlights

All insurers in Europe have to comply with Solvency II legislation. Whilst larger firms have spent significant resources preparing for Solvency II go-live on the 1st January 2016, the regime presents a different set of challenges for the smaller firms, many of which are yet to be addressed.

The moment is finally here (and gone). After over ten years of combined effort with European policy makers, regulators and insurance firms, Solvency II came into force on the 1st January 2016.

The European Insurance and Pensions Authority (EIOPA), who are responsible for the design and implementation of the legislation, started this journey with the following objectives in mind:

- ***Improved consumer protection:*** It will ensure a uniform and enhanced level of policyholder protection across the EU. A more robust system will give policyholders greater confidence in the products of insurers.
- ***Modernised supervision:*** The "Supervisory Review Process" will shift supervisors' focus from compliance monitoring and capital to evaluating insurers' risk profiles and the quality of their risk management and governance systems.
- ***Harmonisation:*** An integrated and consistent approach will promote a level playing field.
- ***Deepened EU market integration:*** Through the harmonisation of supervisory regimes.
- ***Increased international competitiveness of EU insurers***

Given the scale and diversity of the insurance business across Europe, this has been a difficult task. Understandably, the focus of regulatory and policy making efforts has been on the design and implementation of Solvency II in larger firms, or those with complex business models.

But with all the supervisory focus on the bigger firms (and a staggering €3bn spent by firms on preparations), what about the smaller firms? The smallest (predominantly run-off firms and friendly societies) have become the focus of attention from the PRA in the recent months.

The legislation is not just restricted to the balance sheet – Solvency II also applies to the risk and governance of the business, and the frequency and amount of information it reports to both the public and the regulators. These requirements provide a number of key challenges for the implementation of Solvency II in these firms.

Key Challenges for smaller firms

The last ten years have provided a long and challenging environment for firms to implement Solvency II, often requiring large change programmes to mobilise and implement organisational, systems and culture change. The regulation also presents a different set of challenges for smaller firms:

Balance sheet and capital

The new look Solvency II balance sheet contains a number of different concepts in comparison to the Solvency I equivalent. Alongside the technical challenge in the production of the Pillar 1 balance sheet, the resulting figures may look different to that produced under Solvency I. Small insurers need to pay even more attention to the risks (and resulting Solvency Capital Requirement) that most materially affect their business.

Resource

Smaller firms may not have a dedicated team that can solely focus on Solvency II implementation. It requires a multi-disciplined approach, drawing on knowledge of Actuarial, Risk, Compliance, Finance, Internal Audit and Human Resource expertise. Having all of this and ensuring it is working together is a challenging element of the design and implementation of Solvency II.

Governance and functions

Defining a sufficient governance structure needs to consider the Senior Insurance Managers Regime, the functions required under Solvency II regulation (Actuarial, Risk, Compliance and Audit), three lines of defence and the business itself; the combination of which requires careful consideration of the relevant roles and responsibilities, which if not defined correctly may lead to inadequate challenge of risk and business decision making.

Scale and breadth of regulation

The regulation itself spans a Directive, a set of Delegated Acts, a number of guideline documents and also technical specifications. Finding the relevant information and applying this appropriately requires specialised knowledge of the regulation, which may not be readily available.

Materiality, proportionality and regulatory expectation

Solvency II provides sufficient scope for firms to use techniques that are commensurate to their nature, scale and complexity. Smaller firms can therefore utilise simplifications across all three Pillars, but understanding how regulators view the application of proportionality and these simplifications is key for smaller firms to comply with Solvency II regulations in an efficient manner.

Reporting timescales and extent of information

The reporting templates required for disclosure purposes require a wide range of information of key aspects of the balance sheet and reporting. To be efficient, smaller firms will need to understand which forms will need to be completed, and the level of granularity required.

How can we help?

We have worked with a wide variety of small insurance firms to understand how the regulation will affect their business. Combined with a deep technical understanding, we can provide a Solvency II programme that simultaneously best serves your business and complies with the relevant regulation.

We offer a selection of options, ranging from reviewing existing documentation for Solvency II compliance, up to producing all the documentation required. Given the tailored nature, we would be happy to discuss our services and your requirements.

Below shows the key areas of each Pillar of Solvency II along with an example of how we could assist a small firm.

		Review and Recommend	***Review and remediate***	***Design and implement***
Pillar 1	Technical provisions	✓		
	Own Funds		✓	
	SCR calculation			✓
	Standard Formula Appropriateness			✓
	Actuarial Function Holders Report			✓
Pillar 2	ORSA			✓
	Risk Management Framework		✓	
	Senior Insurance Managers Regime			✓
	Systems of Governance	✓		
	Outsourcing	✓		
Pillar 3	Qualitative reporting templates (QRT's)			✓
	Solvency and Financial Condition Report (SFCR) and Report to Supervisor (RSR)			✓
	QRT quarterly exemptions (where applicable)			✓
	Data quality and granularity			✓

We have been able to design a pragmatic and cost effective solution to smaller firms with limited budgets. This includes tailored packages of solutions for clients, using a combination of the options in the above table. These costs depend on the requirements of the individual clients and the firm's level of maturity.

Stand out for the right reasons

Alert

Protect

Adapt

Repair

Financial services risk and regulation is an opportunity.

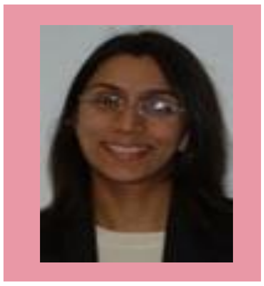
At PwC we work with you to embrace change in a way that delivers value to your customers, and long-term growth and profits for your business. With our help, you won't just avoid potential problems, you'll also get ahead.

We support you in four key areas.

- By alerting you to financial and regulatory risks we help you to understand the position you're in and how to comply with regulations. You can then turn risk and regulation to your advantage.
- We help you to prepare for issues such as technical difficulties, operational failure or cyber attacks. By working with you to develop the systems and processes that protect your business you can become more resilient, reliable and effective.
- Adapting your business to achieve cultural change is right for your customers and your people. By equipping you with the insights and tools you need, we will help transform your business and turn uncertainty into opportunity.
- Even the best processes or products sometimes fail. We help repair any damage swiftly to build even greater levels of trust and confidence.

Working with PwC brings a clearer understanding of where you are and where you want to be. Together, we can develop transparent and compelling business strategies for customers, regulators, employees and stakeholders. By adding our skills, experience and expertise to yours, your business can stand out for the right reasons.

For more information on how we can help you to stand out visit www.pwc.co.uk.



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