

Solvency II Equivalence FAQs

April 2016



What is Solvency II?

The aim of any solvency regime or system is to ensure a company is able to meet its financial obligations when they fall due – essentially, to guarantee a company's assets can provide for long-term financial stability.

The Solvency II Directive (Solvency II) is a harmonised framework aimed at ensuring there is a single market, utilising a single set of rules for insurance services. The requirements under Solvency II apply to (re)insurance companies and European Union (EU) insurance groups operating in the EU with the exception of those (re)insurers covered under Article 4 of the Directive. These (re)insurers and groups are now required to comply with requirements under Solvency II, effective 1st January 2016.

Solvency II aims to ensure (re)insurers and groups can survive difficult periods, including catastrophic events and financial market turbulence, which could adversely affect their books of business and claims-paying abilities. Solvency II encompasses requirements surrounding risk sensitive solvency, governance and risk management, and public disclosures.

How and why did Solvency II come about?

Solvency II is an EU directive which was first introduced in November 2009. It replaced the 14 insurance and reinsurance directives, previously known as "Solvency I", and was transposed into national law in each of the 28 EU Member States. Solvency II's overall objective is to protect (re)insurers' policyholders and provide for a stable financial system as a whole.

The European Insurance and Occupational Pensions Authority (EIOPA) is one of three EU supervisory authorities, with specific oversight over the insurance and occupational pensions sector. It is an independent advisory body to the European Commission (EC), the European Parliament and the Council of the EU.

Part of EIOPA's mandate is to develop regulatory standards that support Solvency II and to ensure EU Member States comply with Solvency II and the regulations. EIOPA also conducts the assessment of non-EU countries which may seek equivalence to Solvency II.

What does Solvency II equivalence mean?

Solvency II equivalence for third countries means a non-EU jurisdiction has an insurance regulatory regime that

achieves the same outcomes as those determined under the Solvency II framework.

Solvency II empowers the EC to adopt delegated acts reflecting the equivalence decision of a third country's solvency and prudential regime.

EIOPA is responsible for the technical assessment for equivalence which is based on principles such as a third country's risk-based regime, risk-based capital requirements and enhanced group supervision.

Solvency II equivalence enables (re)insurers and insurance groups from third countries (i.e. not EU), to conduct business in the EU as though they were EU-domiciled entities. Equivalence will also benefit the EU and its citizens, by increasing the provision of well-regulated, stable insurance capacity. Equivalence also substantively strengthens the level of cooperation and trust between international insurance supervisors, as well as the cross-border efficiencies and effectiveness of supervision between jurisdictions.

What does Solvency II equivalence mean for Bermuda?

Solvency II equivalence acknowledges that Bermuda's enhanced commercial insurance regime has achieved the same outcomes-based results as the Solvency II framework. This formal recognition means Bermuda's

commercial (re)insurers and insurance groups will not be disadvantaged when competing for, and writing, business in the EU. Solvency II equivalence also means that EU Member States recognise Bermuda as the group supervisor for its insurance groups that operate in the EU.

Has Bermuda reached Solvency II equivalence?

Bermuda's enhanced commercial insurance regime reached full equivalence on 24th March 2016 following a multi-year effort by the Bermuda Monetary Authority, and public and private sector stakeholders. A Delegated Act recommending full equivalence for Bermuda was adopted by the EC on 26th November 2015, following which the European Parliament (EP) and Council were entitled to object to the EC decision for a three-month period. No objections were received.

In the Delegated Act, the EC announced its approval of Bermuda's commercial (re)insurance regime which it accepted as being fully equivalent to regulatory standards applied under Solvency II. The Delegated Act entered into force on 24th March and was applied retroactively to 1st January 2016.

Are there any other non-EU countries who have reached Solvency II equivalence?

Yes, Switzerland – a non-EU country – was declared Solvency II equivalent in June 2015 for an indefinite period, and there was no objection by the European Parliament or the Council of the EU.

Bermuda achieved full equivalence under all three Articles in Solvency II: Article 172, which relates to Bermudian reinsurance contracts being treated the same as European Economic Area (EEA) reinsurance contracts; Article 227, which relates to group solvency requirements for Bermuda (re)insurers with an EEA parent; and Article 260, which relates to group supervision of EEA insurers with parents outside of the EEA.

What is the Authority's involvement in obtaining Solvency II equivalence?

As regulator of Bermuda's financial services industry the Authority had a dedicated core team working for six years to achieve equivalence.

The Authority has worked on – and been assessed – on the following EIOPA criteria:

- Powers and responsibilities of third country supervisors
- Taking-up of business
- System of governance
- Public disclosure
- Changes in business, management or qualifying holdings
- Solvency assessment
- Professional secrecy, exchange of information
- Group supervision

This achievement marks not only the Authority's supervisory expertise but the calibre of commercial (re)insurers and insurance groups operating from Bermuda and the quality of their regulatory environment.

Which Bermuda insurers are impacted by Solvency II equivalence?

Solvency II equivalence applies to Bermuda's groups and commercial (re)insurers including the island's Classes 3A, 3B and 4 (re)insurers, and Long-Term (life) Classes C, D and E (re)insurers.

The Authority's focus for gaining equivalency has been on Bermuda's commercial insurers due to the significant business conducted within Europe by these classes and the risk that they could be competitively disadvantaged if Bermuda's enhanced commercial insurance regime was not deemed equivalent to Solvency II.

Are Bermuda's captives affected by Solvency II equivalence?

Bermuda's captives or limited purpose insurers (i.e. Class 1, Class 2, Class 3, Class A and Class B (re)insurers) and Special Purpose Insurers (SPIs) are not impacted by Solvency II equivalence.

However, as part of Bermuda's continuing work on developing a quality regulatory environment for all insurance entities, Bermuda's limited purpose insurers will soon be required to provide consolidated annual electronic filings. The E-SFR is designed to create efficiencies in the process for both the market and the Authority.

The E-SFR consolidates previous submissions received by the Authority, including a risk self-assessment, and compiles aggregated data to support the Authority's statistical analysis of the characteristics and trends within

Bermuda's captive market. The data collection will ensure an appropriate level of supervision is maintained for this sector.

Why has it taken Bermuda so long to achieve Solvency II equivalence?

The equivalence process and its deadlines were driven by EIOPA and the EC, under the direction of the EU Parliament and Council. The Authority has worked closely with both EIOPA and the EC to ensure it met the requirements of Solvency II equivalence. This work was extensive, and included consideration of the powers and responsibilities of third country supervisors, systems of governance, solvency assessments and group supervision.

In 2015 alone, the Authority consulted on implementing the Economic Balance Sheet regime for commercial (re)insurers, and finalised legislation for agreed amendments to the Bermuda Solvency Capital Requirement (BSCR).

These aspects were significant and had to be carefully planned. Regime changes were executed to support the dynamics of a multi-licence Bermuda market and on a schedule which enabled insurers to transition to the enhanced requirements on a phased basis, where appropriate.

What were some of the challenges Bermuda faced on the road to achieving equivalence?

Challenges included striking a balance between assessing and implementing revisions to reflect international regulatory standards, while at the same time doing so in a risk-based manner appropriate for Bermuda's market.

Equivalence has raised the bar for Bermuda's (re)insurance industry; how will the Authority respond to expectations in a post-equivalent era?

The Authority regularly reviews its (re)insurance regimes to ensure they are appropriately protecting policyholders and are credibly viewed by regulators in key trading jurisdictions. In this way, the Bermuda (re)insurance industry is not placed at a competitive disadvantage. Where possible, this includes entering into recognition or equivalence arrangements.

The Authority has invested substantially in recruitment and training to ensure its staff is able to continue effective transition to a proactive and forward-looking risk-based approach. Having highly-skilled staff allows the Authority to appropriately implement international standards in a credible and

pragmatic way, in accordance with the principle of proportionality.

What's next for Bermuda?

As outlined in our 2016 Business Plan, the Authority continues to focus efforts on various critical areas for Bermuda.

For example, our asset management supervisory activities include working towards developing an opt-in system for the Alternative Investment Fund Managers Directive (AIFMD) to assist with marketing Bermuda funds in the EU.

In addition, we are preparing for the Caribbean Financial Action Task Force (CFATF) assessment of Bermuda's Anti-Money Laundering/Anti-Terrorist Financing systems expected to take place in 2018.