MICHEL BARNIER
Membre de la Commission européenne

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Dear Sirs,

I am writing in response to your joint letter dated 29 March 2011, in which you set out the European insurance industry's concerns about the latest developments in the Solvency II project.

The financial crisis did not stem initially from the insurance sector, although some companies were very directly involved and many more suffered from the consequences.

I strongly believe we must learn all the lessons of the crisis. We need to improve regulation and supervision across the board to ensure the same mistakes are not repeated in the future.

The crisis has strengthened the need for good risk management and sound governance.

We are taking action in many different areas to ensure the financial sector will be stronger and sounder. Our work on Solvency II was not triggered by the crisis. However, the insurance sector is not immune to the necessary changes. The current regime is outdated and clearly not suitable for today's world. It is not risk-based and does not reflect economic reality of the way insurers manage their business.

That is why Solvency II is so important: It will modernise the regulatory framework and in doing so bring many benefits to the insurance industry as well as to consumers and the wider economy.

The approach chosen will reward good risk management and enhance policy holder protection.

Mr Henri DE CASTRIES, Chairman PEI
Mr Tommy PERSSON, President CEA
Mr Alex WYNAENDTS, Vice-Chairman PEIF
Mr Serge BALBINOT, Vice-President CEA
Mr Alex LEHMANN, Chairman CRO Forum
Mr Dieter WEMMER ,Chairman CFO Forum
Mr Robin SPENCER, Vice-Chairman CRO Forum

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It will allow insurers to continue to make long-term investments, which is so essential to consolidating the recovery of the European economy.

I believe strongly that these new rules will make the EU more attractive for insurers to operate in, as we are providing a secure and sound framework.

I hear much criticism, often unjustified, about the potential impacts of Solvency II. This criticism is not borne out by any of the existing facts and figures. The reality is that Solvency II has been subject to more consultation and impact studies than any other piece of legislation I am aware of! We have worked closely and constructively with all stakeholders to take on board their views throughout the process. And we will maintain this approach during the final stages.

Let me recall that the results of the fifth quantitative impact study (QIS5) published by the European Insurance and Occupational Pensions Authority (EIOPA) on 14 March 2011 have confirmed that the approach that has been tested is a workable proposition. The criticisms levied against Solvency II, particularly that the calibrations are excessively high, have not been confirmed by evidence.

The results show that the insurance industry is well-positioned to meet the new solvency requirements. Overall the industry has, at the level of individual companies, approximately €360bn more eligible own funds than the Solvency Capital Requirement (SCR), that is, the higher of the two capital requirements that insurers will be subject to. While there has been a decline in surplus capital as compared to Solvency I, this is not surprising since Solvency II requires insurers to hold capital that is commensurate with the risks inherent in their business. This will offer much greater protection to policy holders and beneficiaries.

The SCR is a target, not a hard capital requirement. Non-compliance with the SCR will trigger supervisory intervention, but Solvency II introduces a ladder of intervention and ultimate supervisory action will only occur once the Minimum Capital Requirement (MCR) is breached. Surplus eligible own funds over the MCR is €676bn. This is even higher than the Solvency I surplus.

I have publicly acknowledged that in spite of the very positive QIS5 results, there are still a number of important issues to resolve. Refinements to the implementing measures will be made in a number of areas to take into account the QIS5 results. The Services of the Commission and EIOPA have already established working parties to develop solutions in relation to several of the issues mentioned in your letter. Your organisations are represented in each of these working groups.

In particular, we take very seriously the issue of the ongoing viability of insurance products with long-term guarantees. The problems mainly relate to the volatility of own funds under a market consistent valuation framework and the measurement of the specific risks that these undertakings are exposed to. A working party is currently analysing these issues and the necessary measures will be taken in order to ensure that the characteristics and risks of these products are adequately reflected in the implementing measures. Similarly, working groups led by EIOPA have been established to refine the calibrations for health and non-life catastrophe risk and premium and reserve risk. The aim of this work will be to ensure that the 99.5% Value at Risk calibration is based on empirical data that is representative of all Member States.

The draft level 2 implementing measures have been shared with stakeholders, including your organisations, and a large number of your suggestions have been taken on board. An important example is the treatment of the expected profits included in future premiums (referred to in your letter as Value-in-Force). The inclusion of this amount in Tier 1 was the approach adopted in QIS5 and we continue to support this approach.

The Services of the Commission have also responded to concerns about complexity by proposing a long list of suggestions aimed at making the solvency regime less complex. Your associations have had an opportunity to comment on this list and we would welcome any additional suggestions you have.

The industry's position on some of the other issues raised in your letter is not shared by all those that will be responsible for making the final decisions on the level 2 implementing measures. One example is the contract boundary for technical provisions. The Commission's final proposal will take the views of all stakeholders into account and will be in line with the Framework Directive.

Solvency II will enter into force as planned on 1 January 2013. Where necessary, the Commission will introduce measures to ensure a smooth transition but I am against a delay to the introduction of Solvency II. Solvency II is a much needed Directive and it is critical that all parties ensure that they are ready in time for implementation.

I know that you share my view about the importance of Solvency II to the EU insurance industry and I would like to encourage your organisations to continue working constructively with the Commission and EIOPA as the Solvency II project reaches its final phase.

Yours sincerely,

Michel BARNIER