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EU faces Solvency II equivalency balancing act for third countries

FOR certain insurance jurisdictions, the road to third-country equivalence under Solvency II became considerably smoother on July 21, when the Committee of European Insurance and Occupational Pensions Supervisors (Ceios) released draft advice on the list of non-European Union (EU) (third) countries that will be subject to an "equivalence assessment" starting in November 2010, reports Guy Soussan, a partner at Steptoe & Johnson LLP in Brussels.

At stake is the possibility for those countries on the list (and thus groups domiciled there) to benefit from a finding of positive regulatory equivalence in terms of reinsurance, group solvency and group supervision.

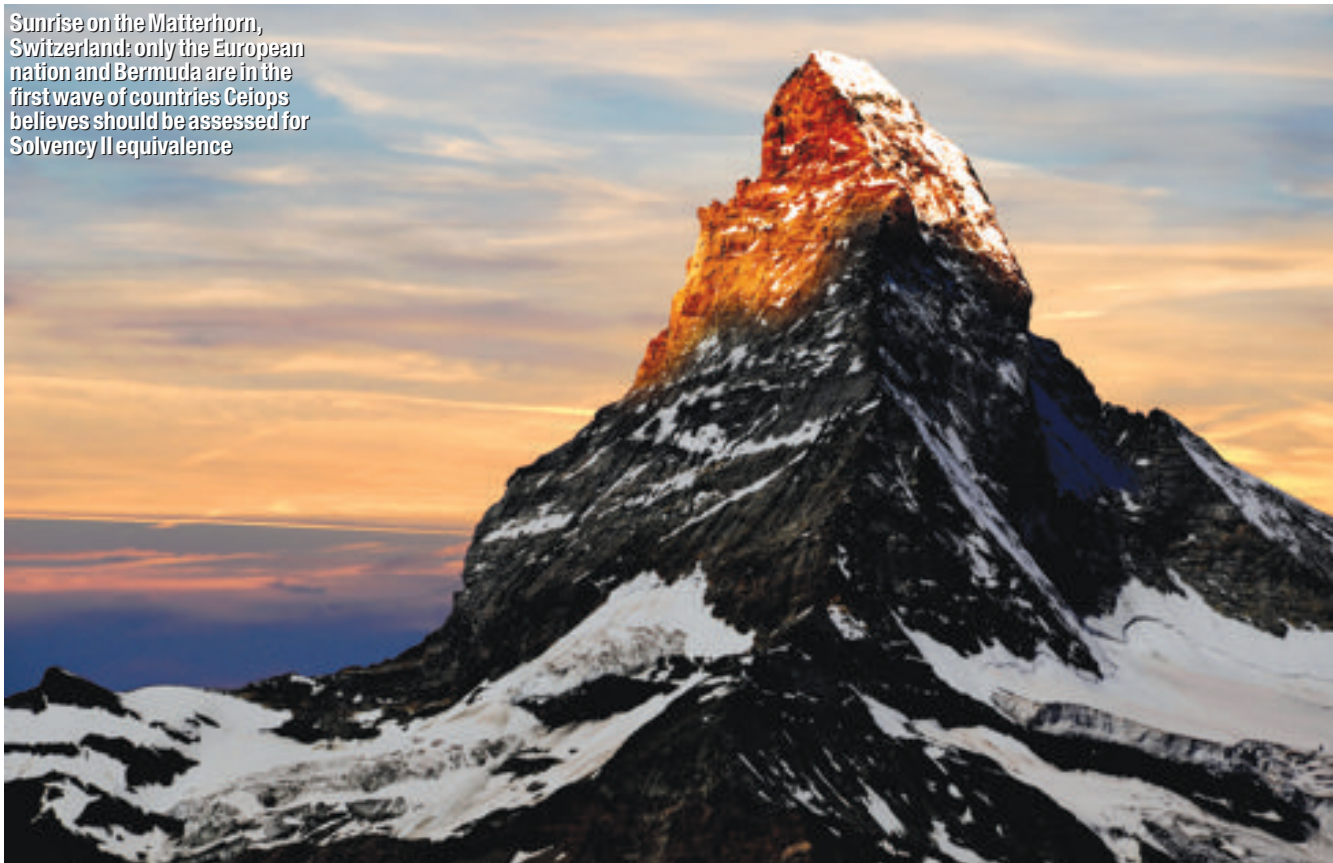
The equivalence assessment is a demanding process, as befits the EU as the global standard setter; it is, however, a process third countries can ill afford to ignore if they wish to avoid regulatory inefficiencies and additional capital and collateral requirements. In fact, on the starting line were three distinct categories of countries that share a common feature – all have significant bilateral trade in insurance with the EU. Among them are those countries – Switzerland and Bermuda in particular – that have openly implemented their commitment to aligning their prudential and supervisory regimes with EU standards.

Other countries have regimes that are moving towards Solvency II standards (China, Canada and Mexico). Finally, certain countries still vary significantly from EU standards – the US, for example.

It comes as no surprise, therefore, Ceios' draft advice identifies Switzerland, Bermuda and, to a lesser extent, Japan, as being the three main contenders for an equivalence assessment with serious prospects of being recognised as equivalent by 2013.

Bermuda in particular stands

Sunrise on the Matterhorn, Switzerland: only the European nation and Bermuda are in the first wave of countries Ceios believes should be assessed for Solvency II equivalence



out for matching emerging Solvency II standards and for its commitment to an equivalent group supervision regime.

Notwithstanding the importance of their markets, no other third country is likely to make it to the list of "first-wave" third countries. There are a number of reasons for this, not least the lack of resources at Ceios to conduct multiple equivalence assessment exercises in short order.

For reinsurance equivalence, Ceios has singled out Switzerland and Bermuda (and, more surprisingly, Japan) based on the importance of their reinsurance markets. Equivalence for the purpose of consolidating non-EU operations of EU-domiciled groups under Solvency II is also limited to these countries, even though more than 50 other third-

country jurisdictions are of importance to EU insurance groups.

For group supervision, Ceios notes Switzerland has introduced a full group supervision regime already. Bermuda's promise to deliver such a regime has been sufficient for it to be included.

There is little time for other third countries and their insurance and reinsurance sectors to seek amendment of the Ceios draft advice. The consultation process ends on August 13.

Ceios, however, only advises. It is the European Commission's prerogative to finalise the list based on the results of the "technical" selection by Ceios. The commission's final list will also have to take into account more "political" considerations.

The US is left in an awkward position – like Bermuda and

Switzerland, it is an important insurance player; however, according to Ceios, it has "no realistic chance of a positive result within the timescale of the first wave of countries".

Despite the most recent announcements of moves toward a Federal Insurance Office, Ceios concludes the absence of federal regulation and supervision, no group supervision regime and loopholes in confidentiality standards are serious drawbacks.

The EU has worked hard to be at the forefront of global regulatory standards and realises it cannot arbitrarily exclude other jurisdictions. This means while there may only be two or three first-wave contenders, other third countries will need to be considered in the next waves.

Furthermore, the EU might

have to consider transitional measures for other third countries to alleviate the consequences of deferred recognition.

Ultimately, Ceios (and its successor authority, the European Insurance and Occupational Pensions Authority) and the commission will need to address such consequences in detail – not least for EU groups with interests in third countries (in particular for group solvency purposes) – if they are to avoid inconsistent assessments of later wave third country regimes.

The EU deserves credit for setting high regulatory standards. The first-wave countries aspire to them.

The EU must, however, also recognise its responsibility, as a global trendsetter, not to neglect its other trading partners.

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This article first appeared in *Insurance Day* and can also be found at www.IDnewscentre.com