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Solvency II: Brexit and other legal uncertainties

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Brexit – general impacts on the sector

- Impact on asset values and interest rates
- Potential loss of passporting rights:
  - New business/ increments and options
  - Use of local subsidiaries/ third country branches
  - Special deal?
- Loss of mandatory recognition of Part VII transfers

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Brexit – changes to regulation?

- Working assumption is that Solvency II will be largely retained, at least initially
  - Fundamental framework is consistent with UK regulatory approach
  - Less disruption for industry
  - Less resource intensive than replacing the regime with something new
- Not entirely automatic – some aspects are directly applicable at the moment so will need to be incorporated into UK law or regulation
- Treasury committee inquiry

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Brexit – future evolution of regulation

- Incentives for maintaining the status quo
- Equivalence under Solvency II
- Possible areas for change?
  - Risk margin
  - Treatment of sovereign debt
  - Matching adjustment
  - Volatility adjustment
- Big brother is no longer watching you (no more EIOPA oversight)

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Risk transfer

- Trigger points in pre Solvency II agreements
  - Mathematical reserves vs best estimate/ best estimate + risk margin
  - CRR vs SCR
- Reinsurer termination rights
  - Change in tax law?
- Ratings requirements for financial risk mitigation techniques

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Long-term insurers – distributable profits

- Special regime under Section 843 Companies Act 2006
  - Unallocated surpluses in the long-term fund can be treated as realised profits
  - No longer applies as there is no requirement to maintain a long-term fund under Solvency II
  - Application of general rules could create balance sheet volatility and potentially restrict distributions
- Proposed changes
- Distributions based on December 2015 year ends

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Matching adjustment

- Transformation of non compliant assets using SPVs
  - Tranching of cash flows
  - Treatment in group solvency calculation
- Liability eligibility
  - Deferred premium buy-in arrangements
  - No splitting of liabilities
  - Use of reinsurance

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Own funds

- Restrictions on use of subordinated debt in the group solvency calculation
  - Insurance subsidiaries
  - Intermediate holding companies
  - Financing vehicles
- Tier 2 debt and insolvency
- Repayment of grandfathered own funds

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