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Mr Gabriel Bernardino
Chairman of EIOPA
Westhafenplatz 1
60327 Frankfurt am Main
Germany

Dear Mr Bernardino,

I would like to thank you for your letter of 14 March 2011 and the attached report on the fifth quantitative impact study (QIS5). I would like to express my sincere thanks to you and the team at EIOPA for the hard work and enormous efforts that you have gone to in running the QIS5 exercise and analysing the results. The publication of this report is a major step in the finalisation of the level 2 implementing measures and a key milestone in the Solvency II project as a whole.

The Commission is pleased that the QIS5 results are positive and show that insurance and reinsurance undertakings are well-positioned to meet the new Solvency II capital requirements. The high participation of undertakings, including SMEs, also illustrates that the industry has invested significant time and effort to make sure they are ready in time for the introduction of the new regime.

The Commission has always stressed that QIS5 was a test. It is important now that we reflect on the results and make refinements to take into account the lessons learnt from the exercise and to reduce the complexity of the system. The QIS5 results show that refinements to the level 2 implementing measures are still needed on the requirements for technical provisions and own funds and the design and calibration of the Solvency Capital Requirement standard formula. Specifically, in the area of calibration we look forward to the further input EIOPA will provide on health and non-life catastrophe risk and health and non-life premium and reserve risk, which we expect to receive in the coming weeks.

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The fact that parts of the Solvency II Framework have become too complex was an early message coming out of QIS5. My services have already discussed with representatives from EIOPA, as well as from Member States and industry a long list of suggestions that can be implemented at level 2 to make the solvency regime less complex. The Commission has also proposed introducing additional simplifications that can be used by undertakings as an alternative to the standard calculations, where this can be justified based on the size, nature and complexity of the risks inherent in undertakings' businesses.

I very much welcome the willingness expressed in your letter to further work on this issue based on the practicability issues identified in the QIS5 report. The concerns on complexity also reinforce the importance of the application of the proportionality principle to the requirements. It is clear that further guidance will be needed at level 3 so that this is done properly and consistently and EIOPA will play a key role in ensuring that this is the case.

Another message coming out of QIS5 is the potential impact of the Solvency II regime on the providers of insurance products with long-term guarantees. These problems 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. As you know, my services have set up a working party, of which EIOPA is a part, to thoroughly analyse these issues and take the necessary measures to ensure that the characteristics and risks of these products are adequately reflected in the implementing measures. Although it is too early to say what the final outcome of this working party will be, the Commission will need EIOPA's technical input when developing solutions and analysing their impact. It is likely that the timeframes for delivering these inputs will be short. However, I hope that I can count on your support in helping to resolve this important issue.

I am also aware that aside from the issues relating to long-term business with guarantees there are concerns more generally about volatility. The Commission takes this issue very seriously. Measures have already been introduced in the Framework Directive to address pro-cyclicality, such as the Pillar 1 and 2 dampeners, which you mention in your letter. The Commission will further analyse the issue to see whether further changes to the level 2 implementing measures are necessary.

Your letter indicates that EIOPA will, at its own-initiative, undertake further work on the issue of expected profits included in future premium. The Commission acknowledges that there are diverging views on this issue and that there is a need to clarify the concepts. However, the Commission continues to believe that these expected profits should in principle be included in tier 1. We will carefully analyse any input EIOPA provides. I would like to point out that the input from EIOPA on this issue should be provided soon, as the last meeting of the Solvency Expert Group will take place at the beginning of May.

I would like to conclude by thanking you again for the report. I am aware that the QIS5 exercise and the analysis of the results coincided with the transformation of CEIOPS into EIOPA and your delivery of a high-quality report on time is greatly appreciated.

Yours sincerely,

Jonathan Faull

Copies : Ms Sharon Bowles, Chairwoman ECON, European Parliament
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