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UK

House of Commons Treasury Select Committee publishes a report on the Solvency II Directive and its impact on the UK insurance industry

On 27 October 2017, the House of Commons Treasury Select Committee published a [report](#) on the Solvency II Directive and its impact on the UK insurance industry.

Specific areas explored in the report include:

- the risk of procyclicality and market distortion;

- the potential impact on long term savings and investment, and the function of the matching adjustment;
- the calibration of the risk margin;
- the approval of internal models and subsequent model change;
- the volume and complexity of data required from firms;
- the usability of the volatility adjustment;
- the working of the transitional measure on technical provisions; and
- the rigidity of Solvency II's approach to contract boundaries.

The Select Committee says that evidence submitted to the previous Select Committee highlighted problems both with the legislation as drafted and with the way it has been implemented in the UK by the Prudential Regulation Authority (PRA). It says that while some differences of opinion are to be expected, the current Select Committee is as concerned as its predecessor at the extent of disagreement between the PRA and industry on matters that should be relatively factual, for example, around the availability of investment grade long-term assets. Such disagreements do not foster good policymaking.

The Select Committee understands that the PRA can act on its own initiative in a number of policy areas, whereas in others it currently has to act within the EU legal framework. However, the PRA and industry differ as to precisely where this line is drawn. The Select Committee strongly encourages the insurance industry and the PRA to come to an understanding on what aspects of Solvency II can be changed unilaterally while the UK remains an EU Member State.

The Select Committee notes the views of many of those who gave evidence to the previous Select Committee that the PRA's approach is overly focused on solvency, to the detriment of its secondary competition objective, and to the ability of the industry to meet the savings and protection needs of consumers. Many respondents had advocated a clear competition objective for the PRA, to act as a counter balance to the solvency objective. The Select Committee advocates a review of this alleged conflict by HM Treasury.

Given the complexity of the task and the importance of the industry, both domestically and internationally, the Select Committee would like to see the development of a clear agreed strategy designed to provide a roadmap for:

- what changes to insurance regulation can be implemented by the UK authorities now, unilaterally, without the need for a change in the Solvency II Directive (to include consideration of what steps would be required to allow regulatory forbearance to limit systemic risks in the event of market turbulence);
- what steps the UK regulator would like to see taken to refine the Solvency II Directive or its applicability to the UK post-Brexit, as a contribution to the Brexit negotiations;
- what action can be taken post-Brexit to foster innovation, competition and competitiveness for the benefit of UK consumers and the standing of the UK's place in the international insurance industry; and
- how UK insurance regulation will harmonise with international capital standards and emerging accounting standards.

House of Commons Treasury Select Committee announces a new inquiry into the UK's economic relationship with the EU

On 20 October 2017, the House of Commons Treasury Select Committee [announced](#) the launch of a new inquiry into the UK's economic relationship with the EU.

The inquiry will consider, among other things, transitional arrangements, preparedness for "no deal", and the long-term economic relationship. The inquiry will consider the progress of the negotiations to date, the design and governance of transitional arrangements, and the shape of the long-term economic relationship.

Solvency II implementation: PRA launches series of improvements

On 25 October 2017, the PRA [announced](#) the publication of the first in a short series of consultation papers on reform to the implementation of Solvency II starting with the matching adjustment (see below on PRA CP21/17).

The series of targeted improvements will support the PRA's February 2017 commitment to the House of Commons Treasury Select Committee to explore reform of some areas of the PRA's implementation of Solvency II, which came into force on 1 January 2016. The PRA says that it has worked closely with firms and the Association of British Insurers in developing these measures.

The series is intended to improve the implementation of certain aspects of Solvency II, consistent with the PRA's role in this framework and its statutory objectives. Over the coming months, further consultation papers will follow in the series:

- **December 2017 - model change process:** the PRA will consult on proposals on the minor model change process with the aim of reducing burden on firms and making better use of supervisory resources in pursuit of the PRA's objectives; and
- **January 2018 - reporting:** the PRA will consult on proposals to reduce the reporting burden on firms. This will include reducing the content required in the PRA's national specific templates, and a revised approach to how the PRA grants quarterly reporting waivers.

In parallel, the PRA says that it is continuing to work on a number of other areas for potential improvements which include:

- **recalculation of the transitional measure on technical provisions:** the PRA is continuing to assess the feasibility of further simplification to the recalculation process; and
- **external audit of solvency and financial condition report:** the PRA is gathering evidence from firms to support its review of whether the policy remains proportionate, particularly for smaller firms.

PRA publishes CP21/17: Solvency II - matching adjustment

On 25 October 2017, the PRA published a consultation paper, [CP21/17](#), which sets out its proposed expectations of firms in respect of the application of the Solvency II matching adjustment (MA). The MA allows firms to adjust the relevant risk-free interest rate term structure for the calculation of a best estimate of a portfolio of eligible insurance obligations.

CP21/17 has been developed by the PRA as part of its work on adjustments to the insurance prudential framework in the light of experience following the UK introduction of Solvency II, including in areas recommended for reform by the Association of British Insurers and discussed with the House of Commons Treasury Select Committee (see above).

In addition to the adjustments mentioned above, the consultation paper proposes to consolidate and update material previously set out in directors' letters, executive director's letters and feedback statements published in the period 1 April 2013 to 15 February 2016 in a new supervisory statement (see appendix 2 to the consultation paper). The consultation paper will allow firms to provide feedback to the earlier published material and new guidance, provide greater clarity on the PRA's expectations in relation to the MA, and help firms realise the intended benefits of MA.

CP21/17 is relevant to all UK Solvency II firms and to the Society of Lloyd's and its managing agents where they are applying or have applied to use the MA.

The PRA proposes additional guidance in the following areas (with references to the relevant chapter in the draft supervisory statement):

- asset eligibility - demonstrating cash flow fixity (see chapter 2);
- criteria for assessing "sufficient compensation" (see chapter 2);

- restructuring asset cash flows using special purpose vehicles (see chapter 2);
- trading in the MA portfolio (see chapter 7);
- consequences of breaches of MA requirements (see chapter 8); and
- changes to MA portfolio approval (see chapter 9).

Comments are requested by 31 January 2018.

PRA publishes PS25/17: Solvency II: Data collection of market risk sensitivities

On 18 October 2017, the Prudential Regulation Authority (PRA) published a policy statement, [PS25/17](#), which provides feedback to responses to its June 2017 consultation paper, [CP7/17](#), "Solvency II: Data collection of market risk sensitivities" and includes a link to the final Supervisory Statement (SS) [SS7/17](#).

SS7/17 sets out the PRA's expectations in respect of the reporting of sensitivities of solvency position to various changes in market conditions by firms with material exposure to market risk. It is relevant to Solvency II insurance and reinsurance firms holding, or intending to hold, material quantities of assets exposed to market risk.

The PRA received ten responses to CP7/17. Overall, the PRA considers that the responses require no material changes to its proposals. The PRA has made amendments to the draft SS to provide further clarity to firms. The amendments concern the scope of firms, timeline of data submission (including the regularity of data requests), and date of the first formal data submission. Chapter 2 of the policy statement explains these changes and provides further minor clarifications in light of feedback received.

Firms in scope can report sensitivities to various changes in market risks half-yearly using this [template](#) and associated [instructions](#). The SS refers to the year end 31 December 2017: firms' submissions of the completed templates will be the solo quantitative reporting template reporting deadline plus four weeks, that is, 18 March 2018 for the first submission.

The PRA will inform firms individually through their usual supervisory contacts whether they fall within the scope outlined above. Out of scope firms that would like to submit the information may do so after discussion with their usual supervisory contact.

Solvency and financial condition report roundtables

During September 2017, the PRA hosted three roundtables with insurers, investors, credit analysts, and equity analysts to discuss the first round of solvency and financial condition reports (SFCRs) published by EU insurers in 2017. SFCRs are publicly disclosed narrative reports, alongside data in standardised reporting templates, which form part of insurers' Pillar 3 disclosure obligations under Solvency II.

On 18 October 2017, the PRA published a [summary](#) of the roundtables which sets out the feedback from both the preparers and users of these reports. The initial feedback on the 2016 SFCRs shows that, among other things:

- most insurers had published stand-alone SFCRs rather than cross-referring to other publications. As a result, SFCRs were often lengthy, with a lot of material duplicated in other publications;
- insurers did not regard SFCRs as a primary mechanism for providing data to investors;
- insurers had received little feedback on their SFCRs. None had evidence that policyholders were reading SFCRs;
- some analysts said that disclosure of financial information by insurers was inadequate and inconsistent. This reduced the attractiveness of the sector to investors;
- analysts and investors were focused on the financial data included in SFCRs. The narrative reporting was seen as providing little additional valuable information.

Investors and analysts said that two areas were priorities for increased disclosure: sensitivity analysis and analysis of movements in Solvency II solvency capital requirements. Analysts said that they regretted the loss of some valuable disclosures from previous PRA returns, particularly around general insurance reserving and claims development.

FCA publishes update on implementation of insurance renewal transparency rules

On 18 October 2017, the FCA published a new [webpage](#) which summarises how general insurance firms have implemented its transparency in insurance renewals which came into effect in April 2017.

The FCA says that it has identified a range of concerns and reminds those accountable that they need to ensure that they effectively manage regulatory change. The areas where firms have failed to meet the rules fall into four broad categories:

- providing incorrect premium information;
- failing to present the premiums and shopping around message clearly, accurately and in a way which draws the reader's attention;
- not implementing the rule changes for all products and customers;
- failing to properly identify a "renewal" as defined by FCA rules.

The FCA expects firms to review their current processes and documentation (both direct to consumer and on-line) to ensure they are compliant and have captured all necessary renewals. It reminds firms that they are required to ensure that the last year's premium and additional shopping around messages are presented as key information in a clear prominent position and in a way which draws attention.

The FCA will continue to monitor compliance to ensure the effective implementation of its rules with a view to taking appropriate action where this is not the case.

The FCA is also concerned that firms were under-prepared to implement the renewal transparency rules accurately. It considers these rules to be relatively straightforward. The FCA reminds firms of upcoming regulatory changes such as the Insurance Distribution Directive and the senior managers and certification regime which are more complex. The FCA says that under-preparation for major regulatory change is not acceptable. Based on what it has identified, it feels it is important to remind all firms of the need to ensure that regulatory changes are managed effectively in future.

Sanctions and Anti-Money Laundering Bill introduced in the House of Lords

On 18 October 2017, the [Sanctions and Anti-Money Laundering Bill](#) was introduced in the House of Lords. A set of [explanatory notes](#) on the Bill has also been published.

This is the first Bill relating to Brexit to be introduced in the House of Lords, following a public consultation on the new measures earlier this year. The new legislation will give the UK the necessary legal powers to continue to implement sanctions and introduce new measures post-Brexit. It will enable the UK to maintain existing sanctions regimes currently imposed through EU law, while providing the necessary legal underpinning for the UK to decide when and how to take action against new threats.

PRA publishes update on CP16/17

On 13 October 2017, the PRA updated the [webpage](#) on its August 2017 consultation paper, [CP16/17](#), "PRA fees and levies: model transaction fees, fees and FSCS levies for insurers and fees for designated investment firms".

In paragraph 2.36 of CP16/17 the PRA noted that it was unable at that time to provide life insurers (A4 fee block) with indicative fee rates due to data limitations. The PRA says that, although these issues have not been resolved fully, it is now able to share some indicative rates for the 2017/18 fee year

based on 2016 Solvency II reported data and the proposals set out in CP16/17 (including the current weightings between fee components).

The PRA says that it should be noted that these figures are for information only and are intended to assist life insurers in interpreting the proposals contained within CP16/17.

Insurance linked securities: draft regulations updated

On 12 October 2017, HM Treasury published updated versions of the following draft Statutory Instruments which have been laid before Parliament:

- the [Risk Transformation Regulations 2017](#): the Regulations implement a new regulatory and supervisory framework for insurance linked securities (ILS) in the UK, designed to attract ILS business to the UK. The Regulations create a new form of regulated activity under the Financial Services and Markets Act 2000 for ILS and also enable the creation of a new form of body corporate called a “protected cell company” to act as a special purpose vehicle in ILS transactions. A related [draft explanatory memorandum](#) has also been published; and

the [Risk Transformation \(Tax\) Regulations 2017](#): the Regulations make provision for the taxation of the above special purpose vehicles.

INTERNATIONAL

IAIS publishes status tables on ICPs and ComFrame

On 23 October 2017, the International Association of Insurance Supervisors (IAIS) published tables showing the status of the [insurance core principles](#) (ICPs) and the development of [ComFrame](#). The IAIS will update the tables on a quarterly basis.

IDD: EIOPA publishes guidelines on execution-only sales

On 11 October 2017, the European Insurance and Occupational Pensions Authority (EIOPA) published a [final report](#) containing guidelines on insurance-based investment products (IBIPs), where the associated risks are difficult for the customer to understand.

The guidelines have been developed in line with Articles 30(7) and (8) of the Insurance Distribution Directive (IDD) and apply to execution-only sales. These are typically IBIPs sold via telephone or online and where the insurance distributor neither provides advice nor verifies the customer’s knowledge of the product and the risks involved.

The guidelines include criteria to identify product features difficult for the customer to understand. For example, they address the nature of the charges paid by the customer and the ability for the customer to surrender the product before maturity. IBIPs including such features will not be eligible for sale via execution-only.

EIOPA [consulted](#) on the guidelines in February 2017 and the final report includes a feedback statement with a summary of the main conclusions of the consultation.

The guidelines will be translated into all the official languages of the EU. Within two months of the publication of the translated versions, national competent authorities (NCAs) will need to confirm to EIOPA whether they comply, intend to comply or do not comply with the guidelines.

According to the disclosure rules for packaged retail and insurance-based investment products, where the associated risks of an IBIP are difficult to understand for customers, a comprehension alert has to be included in the key information document provided to the customer. In order to promote a convergent approach by the NCAs in the implementation of this requirement, EIOPA intends to separately address this issue and communicate its approach accordingly.

SOLVENCY II

Corrigendum to Delegated Regulation on infrastructure corporates published in the Official Journal

On 13 October 2017, a [corrigendum](#) to [Commission Delegated Regulation \(EU\) 2017/1542](#) of 8 June 2017 amending the Solvency II Delegated Regulation concerning the calculation of regulatory capital requirements for certain categories of assets held by insurance and reinsurance undertakings was published in the Official Journal of the European Union.

The corrigendum amends one of the equations on page 18 in Article 1(4)(c) of the amending Delegated Regulation.

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