Salvatore Rossi: The launch of Solvency II – the implementation of the new regime: open issues, implications for business models, and effects on institutional and financial communication

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Keynote address by Mr Salvatore Rossi, Senior Deputy Governor of the Bank of Italy and President of IVASS (Istituto per la Vigilanza sulle Assicurazioni), at the IVASS Conference 2016, Rome, 3 March 2016.

Ladies and gentlemen,

I am delighted to welcome you to this Conference on the launch of Solvency II.

I want to thank Victoria Saporta, Chair of the International Association of Insurance Supervisors (IAIS), Gabriel Bernardino, Chair of the European Insurance and Occupational Pensions Authority (EIOPA), Frank Grund of BaFin and all the other panelists, for kindly accepting our invitation. I also want to thank you all, the audience, for being so numerous. This is the proof that the topic we will be discussing today – namely the Solvency II implementation challenges we are facing only two months after the entry into force of the new regime – is of great relevance, for both regulators and the industry.

Indeed, this is not the first conference on Solvency II and will not be the last. Actually a lot of other conferences and seminars have already taken place since the project started. But we still need some more discussion, and a deeper and wider comprehension of the implications of this multifaceted issue.

We will start with a keynote speech by Gabriel Bernardino. Two panel discussions will follow. The first one on the most relevant and controversial aspects of Solvency II implementation. The second one devoted to a specific but crucial feature of the new framework: information disclosure. The panelists are very distinguished and well known representatives of both the supervisory community and the industry. The moderators will be Ferdinando Giugliano, former editorial writer of Financial Times, now at the Italian newspaper la Repubblica, and Fausto Parente of IVASS. Alberto Corinti, member of the board of IVASS and of the management board of EIOPA, will offer some concluding remarks.

I am sure that we will gain important insights from today's debate, also based on everybody's concrete experience in the past few weeks of the new regime.

Now a few introductory words on my part.

Solvency II was born on 1st January 2016 after a pregnancy lasting more than 10 years. We all remember the last thrilling moments when the Directive Omnibus II, essential for advancing the project, seemed for a while too hard to be agreed upon. A failure would have put the childbirth at deadly risk. But we made it.

EIOPA had a fundamental role in that delicate process. It impressed a decisive push when it adopted the interim measures for the preparation to Solvency II in 2013. That move energized the whole insurance sector (both supervisors and the industry), keeping its attention high in view of the final goal of the new regime.

Notwithstanding the long and complex preparatory works, not each and every detail is fully fixed yet, nor, I would add, fully understood. That is why we organized this Conference. Of course, we are not going to solve all our doubts today. In our ordinary work we continuously bump into new implementation problems, asking ourselves how to practically deal with this or that aspect of Solvency II. To some extent it is physiological, as it always happens when one moves from theory to practice. I am confident that at the end of the day we will be able to exploit all the benefits of the new regime, while minimizing the implementation costs.

Let me briefly touch upon what are – to my understanding – the key points we need to tackle now.

First of all, we need to stimulate and accommodate a thorough cultural change in the insurance sector. The transition from the Solvency I static/historical approach to the Solvency II forward-looking one is revolutionary. It is not rhetoric: in the banking sector the same revolution – back in the remote past by now – required years to be digested by all the stakeholders. In a risk dominated environment, supervisors are expected to systematically challenge undertakings on their risk profile/appetite and on their ability to pursue it; for instance, supervisors should periodically discuss with the board of each company its risk profile and long-term strategies.

IVASS has already taken some steps in this direction. One example: immediately after an on-site inspection we convene a dedicated meeting with the board of the company, to discuss the outcome and possible corrective measures. In our experience not all board members are always willing and able to sustain such a constructive dialogue with the supervisors, especially in small undertakings. But that is essential in the new regulatory framework. It is a cultural gap. We have to work together on it.

All cultural changes require time, effort and perhaps even some pain. What is important is to keep moving ahead – step by step but constantly – towards the main goal: a forward-looking approach in assessing risks and vulnerabilities. Both camps have to adapt their way of reasoning: supervisors when analysing data coming from undertakings, the latter when, for example, performing the Own Risk and Solvency Assessment (ORSA).

A second key point is what I consider now the top priority for the supervisory community in the EU: harmonization and convergence of supervisory practices.

We cannot consistently manage a common regulatory framework if we accept for too long a playing field which is not level, arbitrages among national supervisors, discriminations in the protection of policyholders along national borders. This was often the case under Solvency I, with so many national differences permitted by the EU directives. Solvency II allows a much more limited number of national specificities. We can more easily work on harmonizing supervisory practices, pointing to a really common approach. This means identifying the best practices and being ready, each of us, to adopt them in our national sphere even if they do not come from our own experience. It is not easy. Day-to-day supervision remains in the national supervisory authorities' responsibility, with their different stories and long years of experience. Spreading the best practices, irrespective of where they were developed, would sometimes require forgoing national pride in order to embrace the cause of rationality and efficiency.

I believe EIOPA can do a lot in this field. Not only because "enhancing convergence" is in its mandate, but also because it is in the best position to collect and compare all the different approaches, identify and recommend the best ones, promote their common adoption, while acknowledging differences on aspects that actually merit to be treated differently.

To accomplish this task the tools are already there. Let me just mention the finalization of EIOPA's supervisory handbook, which we believe is "the" essential tool. Hence, IVASS very much supports it and is actively working on it. Another important tool in order to select and share best practices is the "peer review work".

Even in this case, we will need time. From our side, I can assure that we are seriously committed to such collective effort.

A third key point is public disclosure. Solvency II will be a fantastic opportunity to better understand the risk profile and the business model of each company, for all the stakeholders: supervisors first, but also market analysts, board members and managers, journalists, politicians, and the public opinion. The market disclosure rules foreseen by the new legislative framework will really allow everybody interested to have access to the financial position of an insurer with an unprecedented level of detail. The inherent sophistication and complexity of Solvency II, however, raise issues that need to be addressed.

It is essential that such informative treasure be of high quality, that could be easily understood and used. A possible complication stems, at least in our country, from the coexistence of the Solvency II informative approach with financial statements based on accounting standards not matching the former. It may be a source of confusion and misunderstandings, possibly endangering the reputation of both supervisors and companies. It will be interesting to exchange views on that today.

Let me conclude, ladies and gentlemen, with a word of caution. Solvency II is just a regulatory framework. It designs the urban map, it imposes one-way streets and speed limits, it deploys traffic lights and traffic officers. All this infrastructure has just been changed, and today we are going to discuss how to ease the transition towards the new regime. But the traffic itself, the thousands of cars and drivers in a modern city, well, that is the market. And the insurance market, all over the world, is now facing a bigger challenge than the one posed by a change in the rules of the game, though radical.

The challenge is twofold. A structural one: technological innovation. The other one is apparently of a conjunctural nature, but it is actually persisting almost like a structural feature: that is the environment of low and volatile financial returns in which we have been living for years now. I said low, I could have said negative, in the short-term segment of financial markets.

How fast will the new technologies disrupt the traditional way of conducting the insurance business? How long will monetary policies keep interest rates at the present unprecedented levels, or even lower? Nobody knows, and every opinion is legitimate. But the whole business is rocked by these developments.

Understanding the trends and the challenges behind the current state of affairs in the insurance market should be a common endeavor for regulators/supervisors and the industry. For the time being, we have to work together in order to make the implementation of Solvency II as smooth and effective as possible, also for the purpose of strengthening the insurance sector and make it capable of resisting the present headwinds and catch the opportunities of tomorrow.

Thank you for your attention.