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Financial Services Commission

# New Solvency Margin Requirements for Life and Non-Life Insurance Companies – transitional arrangements

## Introduction

On 5th March 2002 the European Parliament and the Council of the European Union adopted two directives, 2002/12/EC and 2002/13/EC, relating to the solvency margin requirements of life and non-life insurance companies. The Directives entered into force on 20th March, the date of their publication in the Official Journal of the European Communities. Member States have until 20th September 2003 to pass the necessary legislation in order to comply with the requirements of the Directive.

## The Requirements Of The Directives

In broad terms, the Directives make provision for the following:-

- The absolute minimum amounts of capital required (the so-called Minimum Guarantee Fund) will be substantially increased and will be indexed in future in line with inflation. The new absolute minimum is set at €3 million (€2 million for some classes of non-life insurance where liability insurance is not involved). These compare with the previous amounts, which range between €200,000 and €800,000.
- The method of calculating the required solvency margin (where this is not done by reference to the minimum guarantee fund) remains substantially the same. However, the thresholds have been increased so that the required solvency margin on a premium basis will now be 18% of the first €50 million of premiums – increased from €10 million and to be indexed in future – and 16% above that threshold. On a claims basis, the margin will be 26% on the first €35 million, up from €7 million and also indexed in future, and 23% above €35 million.
- Supervisory bodies are required to have increased powers to intervene early to take remedial action where policyholders' interests are threatened. For example, in a situation where an insurance undertaking currently satisfies the solvency margin requirements, but its financial position is deteriorating rapidly, the supervisory authority would now be able to take action.
- For certain categories of non-life business which have a particularly volatile risk profile (marine, aviation and general liability), the "calculated" required solvency margin will be increased by 50% (subject always to the minimum guarantee fund requirement).

The Financial Services Commission will discuss with the Government of Gibraltar the implementation of the Directives in due course. However, the purpose of this Newsletter is to set out for the benefit of Gibraltar insurers the stance the Commissioner proposes to take with regard to the transitional periods.

## Companies With An Existing Licence

The transitional periods for companies with an existing licence are reasonably clear, and generous. With effect from 20th March 2002, these companies have a period of 5 years in order to comply with the new requirements. This means, we believe, that the insurer must be able to satisfy the Commissioner that it meets the necessary solvency requirements at the end of the financial year falling after 20th March 2007. (In the case of a 31st December year end company, this would mean that the company must be able to demonstrate that it meets the new requirements at 31st December 2007). There is a further period, not exceeding 2 years, in which companies failing to meet the required margin for the company to agree with the Commissioner an appropriate plan for meeting the requirements. Again with a 31st December year end company, this will mean that the company must demonstrate that it meets in full the requirements by the end of December 2009.

## Companies Not Licensed By 20th March 2002

The transition periods for companies that do not yet have a licence are not as generous as for existing companies. There is some discretion available to the Commissioner as to how the transition period is interpreted and applied before the legislation giving effect to the Directives is in place. However, the absolute requirement is that the new solvency margin measures shall first apply to the supervision of accounts for the financial years beginning on 1st January 2004 (or during that calendar year depending upon companies' financial year end). Insurers not meeting the requirements at that date will have to submit a satisfactory plan to the Commissioner, and give effect to that plan, in order to secure that the solvency margin requirements are met as soon as possible after that date. In the event that insurers cannot meet the new requirements, or produce an acceptable short-term plan to do so, they will be required to cease writing new business.

New applicants, and applicants whose licence application has not yet been determined, should bear in mind the deadline for meeting the new requirements. For the time being, the Commissioner has decided not to require new applicants to inject on licensing the full amount of capital, which will be required for solvency purposes at the beginning of 2004. However, new applicants, when presenting financial forecasts for the first three years of operation, should show the expected injection of capital at the appropriate juncture in 2004 that will enable it to meet the minimum guarantee fund. Before issuing new licences, the Commissioner will require a written undertaking from the new applicant that it understands the requirements of the Directive and will take the necessary steps at that time to inject sufficient capital into the company to enable it to meet the new requirements. Clearly, as the date for implementation gets nearer, it will become less likely that a licence will be granted to a company that is not sufficiently capitalised on the first day of its operation to meet the new requirements in 2004.

Licences will not be granted to companies that cannot adequately demonstrate compliance with the new requirements at the appropriate time.

Questions about this newsletter may be addressed to the Insurance Supervisor or the Assistant Insurance Supervisor (tel. 40283).

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