Welcome

Welcome to the first issue of our newsletter for insurers. This issue explores a number of key developments, which we will look at in more detail in subsequent issues. You may also be interested in our newsletter addressed primarily to the insurance broking community, *Broking Business*, which can be downloaded from our website – www.clblf.com.

The pace of change in regulation and reporting for insurers has been dramatic in recent years and is set to continue. To help prepare effectively, it is important for insurers to choose professional advisers who understand the issues and can provide practical and cost effective support.

CLB Littlejohn Frazer is one of very few firms of accountants outside the 'big four' with real expertise in the UK's insurance market. For many years we have had a core expertise as auditors and advisers to the Lloyd's market. We are now finding there is increasing commonality of regulation, reporting and management of different insurers. We also act for a large number of insurance brokers and companies that range from small start ups to large multinationals. We provide a wide variety of services to the insurance industry including external and internal audit, due diligence, investigations, general and taxation advice.

The firm's financial services division provides a solid core of insurance expertise with a team of five partners and some 30 dedicated staff. This team, together with the complementary insurance expertise of our taxation division, is well placed to provide the deep understanding of the insurance market essential to meet the needs of our clients.

I hope you find this issue of interest. If you have any comments or would like copies sent to colleagues, please let me know.

Neil Coulson
Partner, Insurer team
020 7369 4570
ncoulson@clblf.com

Neil Coulson is a partner in the firm's financial services division and head of the insurer services team. He is a member of the ICAEW insurance committee and a regular commentator on market activity in the insurance press.

Solvency II:

The annual regulatory requirements for UK insurers have changed significantly in recent years. What further changes does Solvency II have in store? John Perry reports.

As a concept, Solvency II has been around for some years and is seen as a framework that will level the playing field across the EU insurance industry. In essence, it replaces the historical rules-based approach with a risk-based system that will focus on principles-based regulation.

The project is complex and has continued to develop in 2007 with the European Commission publishing its proposed Solvency II Framework Directive in July for discussion in the European Parliament and European Council. This set a deadline of October 2012 for implementation of Solvency II – a deadline two years later than previously planned.

Also in 2007 the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS) undertook its third Quantitative Impact Study (QIS). This considered the calibration of the models to be used in Solvency II, the findings of which are anticipated by the end of 2007.

Although the final details of Solvency II are still to be resolved, the fundamentals have been established. Solvency II is based on a three-pillar approach, similar to that already put in place for banks under the EU Capital Requirements Directive, but which is more importantly also the framework of the FSA's Individual Capital Assessment (ICA) regime.

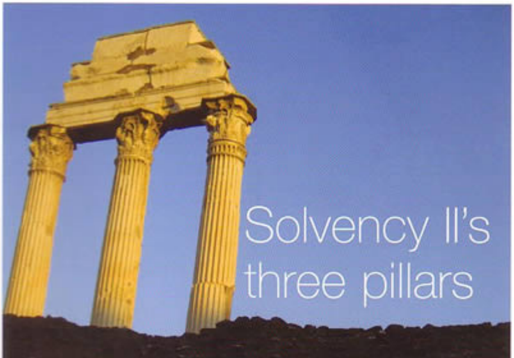
creating a level playing field in Europe

Solvency II will encompass two thresholds: a Minimum Capital Requirement (MCR) and a Solvency Capital Requirement (SCR).

The MCR is likely to be a formula-based calculation below which a firm would be considered technically insolvent. The SCR will be calculated by the firm based upon its assessment of the risk of unplanned losses. The SCR calculation is likely to be based upon a firm's internal model of risks. This will be assessed by the supervisor for suitability who will suggest changes or loadings according to the assessment of the model's appropriateness. If a firm has insufficient capital to meet its agreed SCR, a plan to address this, such as a reduction in the volume of business to be underwritten, will need to be agreed with the supervisor.

It should be noted that once Solvency II is implemented, it will form the basis under which insurers report to the FSA; the current annual regulatory returns will no longer be required.

Pillar 2 will include requirements that address the adequacy of a firm's internal systems and controls. It will require a risk and capital assessment to be produced, an approach that effectively looks for firms to adopt an enterprise-wide risk management approach, aligning their business strategy with the compliance, risk management and internal audit functions. When assessing capital adequacy issues, there will be a need to consider these together with the firm's accounting and actuarial functions so that these qualitative factors are overlaid onto the valuation of assets and liabilities and other quantitative factors that will come together in determining the firm's regulatory capital position.



Pillar 1
Qualitative capital requirements, a market-consistent basis of valuing assets and liabilities

Pillar 2
Qualitative supervisory activities including a company's approach to the management of risk

Pillar 3
Enhancement of market discipline through reporting and public disclosure of information

UK takes the lead

Ahead of Solvency II, in the UK the FSA moved forward with its own risk-based capital approach by implementing its ICA regime in late 2004. UK insurers are already required to consider the risks their businesses face and assess the impact that these will have on capital requirements. Therefore while there are distinct differences between the specific details of the ICA regime and the anticipated shape of Solvency II, the similarities put UK insurers ahead of a number of our EU counterparts in dealing with risk-based capital assessments.

There will be increased scope for firms to reduce their capital requirements. As a result, it will be important for insurers to continue to evolve sophisticated integrated approaches to identification and management of risks linked into capital assessment and operational processes.

We have assisted a number of insurers in identifying, documenting and quantifying risks and controls and developing systems to minimise risks and test the effectiveness of controls, and anticipate that firms will need to continue to develop and refine their systems as 2012 approaches.

For further information, please contact John Perry at 020 7369 3880 or email jperry@clblf.com

John Perry is a senior manager in the insurer services team who joined the firm from the insurance team of a 'big four' practice. He has extensive experience of auditing and advising a range of large insurers.