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UPDATE ON PROGRESS WITH THE SOLVENCY ASSESSMENT AND MANAGEMENT (SAM) PROJECT

Introduction

This newsletter has been compiled by the SAM Communication Task Group to promote awareness amongst stakeholders of important developments in the SAM project as well as progress made by the Financial Services Board (FSB) and the SAM Task Groups on key issues.

Internal Model Approval Process

The FSB is currently conducting consultations and interviews with those insurers who have successfully completed the Pre-Application Qualifying Criteria (PAQC) Template and have become eligible to enter the Pre-Application Phase for the approval of their Internal Models.

Based on some of the proposals in the first PAQC window as well as questions which have been posed to the FSB pertaining to internal models, the FSB has identified some important principles pertaining to the use of internal models for regulatory capital purposes under the SAM framework. The following should be considered by firms who are contemplating or intending to enter into the second or third PAQC windows:

- Internal models should be built for the broader purpose of managing the insurer's own capital, and not solely for the purpose of calculating regulatory capital. This should be reflected in a history of utilising the model for decision-making purposes.
- The internal model does not allow an own assessment of technical provisions. Rather, it is used to calculate all or part (in the case of Partial Internal Models) of the Solvency Capital Requirement (SCR) under the SAM framework. Regardless of whether the standard formula or an internal model is used to calculate the SCR, the general requirements pertaining to technical provisions must be adhered to in the calculation of the technical provisions. Accordingly, assumptions used in the technical provisions pertaining to risk free rates, risk margins, contract boundaries, etc. must follow general SAM rules and are out of scope of an internal model.
- The high-level principles pertaining to the SCR should be complied with, regardless of whether the standard formula or internal model approach is being used. This means that principles pertaining to, for example, risk measure, contract boundaries, timing of the shock, new business etc. should be consistent across both the standard formula and internal model approach.

- The use of an internal model for regulatory capital purposes does not represent an opportunity to recalibrate a “standard risk”. An internal model should reflect the unique nature of the risk exposure of the insurer. As an example, an internal model should not show that a 1-in-200 event for listed equity exposure is significantly different to that in the standard formula.

In addition to the above principles, various questions were posed to the FSB regarding the independent reviews as well as the role of the independent reviewer. The FSB will therefore be releasing an updated version of the *IMAP Independent Review Guidelines* document during July 2012. This update will provide greater clarity on the timing, process and requirements of the independent reviews, as well as on the role of the independent reviewer and the types of reviews that need to be conducted.

Due to the final SAM implementation date being revised to 1 January 2015, the timeline for the approval of internal models has also been revised and is published in the SAM 2012 update available on the FSB’s website. The second window for insurers to submit their PAQC template will be open from 1 August 2012 to 31 October 2012. Once all PAQC’s have been received, the FSB will communicate decisions to the insurers by 30 November 2012. The open-ended PAQC window 3 will start from 1 January 2014.

South African Quantitative Impact Study Two (SA QIS2)

All the relevant SAM Task Groups have inputted into the drafting of the SA QIS2 Technical Specifications. The SA QIS2 timelines are as follows:

Publication of draft SA QIS2 technical specification for comment	31 May 2012
Final date for submission of comments	22 June 2012
Publication of final SA QIS2 technical specification	13 July 2012
Submission of results for solo calculations	15 October 2012
Submission of results for group calculations	5 November 2012
SA QIS2 report published by FSB	31 January 2013

The FSB would like to encourage all insurers to participate in SA QIS2 as it will provide the FSB with beneficial information as to the impact on the proposals on individual and types of insurers.

Further to this the information gathered in SA QIS2 will provide substantial input to the Economic Impact Study.

In light of the fact that SA QIS3 will be a compulsory requirement in 2013, insurers will find participation in the SA QIS2 exercise a beneficial stepping stone towards preparing for the third and final quantitative impact study. In addition, participation in SA QIS2 will aid insurer’s understanding of the potential impact that the SAM framework may have on their financial soundness position.

SA QIS2 Workshops

The FSB will be holding industry workshops on how to complete the SA QIS2 spreadsheet as follows:

Date	Venue	Participants
24 July 2012	Pretoria, FSB	Long-term insurers
30 July 2012	Pretoria, FSB	Short-term insurers
01 August 2012	Pretoria, FSB	Short & Long-term insurers
02 August 2012	Cape Town, Santam	Short & Long-term insurers

Each insurer, however, will be restricted to two participants only. Further information pertaining to the SA QIS2 Workshops including registration details was sent to SAM Co-ordinators on 2 July 2012.

Short-term insurance industry data collection

In order to help establish appropriate calibration parameters for the non-life insurance industry under SAM, the FSB will be issuing a request for information to short-term insurers. The intention is for participation to be compulsory. The structure and format will be similar to the data requested in 2011, but a number of enhancements will be made to facilitate the process, including some automated quality checks to be done prior to submission and a results tab where insurers can understand results generated from their data. SAIA and the SAM Non-Life Underwriting Risk working group will further assist insurers by conducting workshops on how to participate effectively in the exercise. The aim is to provide short-term insurers with as much time as possible to complete the data request – timelines for the release of the spreadsheet, workshops, and due dates will be sent to the industry shortly.

Pillar II Readiness Survey Update

The FSB has considered and reviewed the consolidated comments pertaining to the draft Pillar II Readiness Questionnaire, as obtained from the various SAM Task Groups.

The Pillar II Readiness questionnaire has been circulated to all insurers to complete and is due to be submitted to the FSB by the end of July 2012. The questionnaires will be followed by sample interviews with insurers in Q3 2012, with a report on the findings of the survey envisioned to be published early in 2013.

The survey is not intended to be construed as a checklist of the final Pillar II requirements as these are still being developed and refined by the relevant task groups.

Completion of the survey will be compulsory and shall require sign-off by the Chief Executive Officer (CEO) and a non-executive member of the Board.

Discussion Documents

Discussion Documents provide crucial input for consideration of technical proposals by the FSB in the drafting of legislative requirements within the SAM process. The following Discussion Documents were approved for public comment by the SAM Steering Committee:

Discussion Document	Title	Task Group
50	Detailed contents of SFCR and RSR: Quantitative, Qualitative and Supplementary internal model disclosure and reporting requirements	Reporting and Disclosure
53	Treatment of participation in financial and credit institutions in own funds	Capital Resources
85	Treatment of insurance operations (in “non-equivalent” jurisdictions) under the final measures to regulate the solvency of South African insurance groups (“groups”)	Insurance Groups
89	Calculation of SCR on total balance sheet	Capital Requirements

These Discussion Documents and a comments template can be found on the FSB website www.fsb.co.za under the Insurance Division by accessing the SAM link.

Position Papers

Discussion Documents that have been in the public domain for comment will ultimately take the form of a Position Paper before becoming input into legislation. The following Discussion Documents were recently approved by the FSB SAM Steering Committee for adoption as Position Papers:

Former Discussion Document	New Position Paper	Title	Task Group
25	25	Own Funds – Supervisory approval of ancillary own funds	Capital Resources

These Position Papers and a comments template can be found on the FSB website www.fsb.co.za under the Insurance Division by accessing the SAM link.

Final Position Papers

The following Positions Papers have been accepted and approved as “Final” Position Papers by the FSB SAM Steering Committee.

These Final Position Papers have been subjected to a comprehensive public comment process and as such do not require any further industry input. These papers will now be considered as the final input from industry into the FSB’s process of drafting the SAM Secondary Legislation.

Final Position Paper Number	Title	Committee
14	Solvency and Financial Condition Report: Undertakings using an approved internal model	Steering Committee
15	Structure of the Regulatory Return	Steering Committee
17	Report to Supervisors – Undertaking’s reporting and disclosure policy	Steering Committee
19	Level of harmonization and quantum of data	Steering Committee
34	Own Risk and Solvency Assessment	Steering Committee
42	Calculation of technical provisions as a whole	Steering Committee
43	Internal Models: Validation	Steering Committee
55	Internal Models: Statistical Quality and Calibration	Steering Committee
56	Internal Models: Documentation and Data Requirements	Steering Committee
57	Partial Internal Models	Steering Committee

Insurance Laws Amendment Bill (ILAB)

A draft Insurance Laws Amendment Bill has been submitted to National Treasury for consideration. It is hoped that the Bill will be tabled in Parliament by the end of 2012 and become effective in mid-2013.

The main objectives of the Bill are to:

- extend the provisions relating to the licensing of insurers;
- provide for explicit governance, risk management and internal control requirements for insurers;
- provide for the supervision of insurance groups; and
- enhance the powers of the Registrar to provide for effective supervision and enforcement .

The Bill forms part of the SAM Interim Measures dealing with insurance group supervision and governance, risk management and internal controls.

Insurance Bill update

The second draft of the Insurance Bill has been released for consultation within the SAM structures only. It is expected that the third draft of the Insurance Bill will be made available for comment within the SAM structure in the third quarter of 2012.

Draft 4 will be released for public comment in the fourth quarter of 2012, while Draft 5 is envisaged to be released for public comment in the second quarter of 2013. The Final draft (Draft 6) will be submitted to National Treasury by the end of the third quarter in 2013.

It is envisaged that National Treasury will provide the public with a further opportunity to comment by the end of 2013 and beginning of 2014. The SAM Roadmap envisages that the Bill will undergo parliamentary debate in the second half of 2014, providing a final opportunity for public comment before the Bill is enacted by latest December 2014.

SAM Workshop

FSB SAM Workshops, as arranged by the SAM Communication Task Group, recently took place in Cape Town and Pretoria.

The workshops were rated as providing delegates with beneficial and pertinent information relating to SAM. In particular the presentation by Professor Karel Van Hulle, the Head of Insurance and Pensions at the European Commission, was well received by those in attendance and proved to be extremely insightful.

These presentations have been made available on the FSB's website (www.fsb.co.za).

3rd Country Equivalence

An overarching principle of SAM is that the recommendations arising from the SAM project should meet the requirements of a 3rd country equivalence assessment, as established by the European Union.

The Solvency II regime is still being developed, and the requirements for 3rd country equivalence are not yet finalised. However, the European Commission is considering transitional arrangements whereby countries may be deemed equivalent for a set period of time from Solvency II implementation.

The European Commission has identified South Africa as one of seven countries where they have asked EIOPA to carry out a technical analysis on the regulatory regime for insurers. This technical analysis will assist the European Commission in making a decision on whether South Africa should qualify for the transitional arrangements.

The FSB submitted a response to a questionnaire posed by EIOPA in April 2012, as well as clarifications on follow-up questions from EIOPA in June 2012. The FSB is awaiting further feedback from EIOPA pertaining to the process of qualifying for the transitional equivalence arrangements.

It is expected that the European Commission will render their verdict as to which countries qualify for these transitional arrangements in 2013.

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