



INSURANCE

KPMG Solvency II readiness survey in Central and Eastern Europe

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ADVISORY





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Foreword

Enterprises typically seek information to help them understand their performance relative to similar companies for a variety of business issues and processes. Thus, there is a high level of interest in benchmarking information that provides insights into relevant issues, strategies and operational performance.

In light of this, KPMG's Actuarial practice has released a report outlining the results of its Solvency II readiness survey in Central and Eastern Europe (CEE). The objective of this research was to provide up-to-date qualitative research information and analysis on the impact of Solvency II implementation on the insurance industry in the markets of CEE to all interested entities and professionals.

This report is not intended to be conclusive. A company's business model is a tailor-made blueprint for that organization and its operations. There is no single formula for success in Solvency II implementation. What this report does try to achieve is to summarize information about insurance firms' current state of Solvency II implementation, and for some of them this status report could be a starting point for further debate and discussion on some of the issues that they need to be aware of and which could affect boardroom decisions across the region.

This document is the result of a significant number of contributors and in particular our foremost thanks go to the company representatives from insurance firms in thirteen CEE countries who gave so freely of their time and views in completing our questionnaire. We hope that in reading the results you will find the report a useful guide to the current state of play in our region and an insight into how the Solvency II Directive is currently performing.

With this in mind, it should come as no surprise that KPMG member firms throughout CEE have teams of professionals dedicated to helping organizations from the financial sector in implementing Solvency II. If you would like to know more about how our firms can assist your business, please contact one of our regional CEE leaders listed at the back of the publication, or inquire through your local KPMG contact.



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About this survey

KPMG's Advisory services practice carried out this Solvency II survey in the first quarter of 2010 to gain an overview of the Solvency II readiness of insurance firms operating in Central and Eastern Europe (CEE).

The survey was initiated when the Solvency II Directive and the CEIOPS final advice on Level 2 implementing measures had already been published. Following the publication of these advice papers, representatives of the insurance industry and regulators held heated discussions about the overly prudent capital requirements contained in these proposals. By the time you read this report, the industry will already be discussing the issues relating to the fifth quantitative impact study (QIS5), which was published to coincide with our work on processing these survey results.

The survey was designed to provide insights into the CEE insurance industry's initial response to the Solvency II Directive, the proposed governance arrangements and to identify those areas where there are major challenges. Respondents were asked to share their adopted approaches and describe the progress they had made in implementing Solvency II. They were also asked to consider where they believe the regime adds value and where it presents challenges.

Eighty-eight insurers in a significant section of the CEE market were surveyed, and the study involved different companies operating on this market.



We would like to thank all those who participated in this survey.



// Overall, I am very positive about the Solvency II implementation and see this as an opportunity to improve business practices across the whole insurance market

//
Survey respondent



Executive summary

Visible company autonomy in the region

Almost one-third of respondents started their Solvency II projects themselves, without any pressure from regulators or the group. A significant number of insurers, which otherwise admit group pressure on progress in Solvency II, is planning to retain a strong regional input in the process.

Quantitative impact studies as catalysts in the process

Participation in QIS4 clearly adds considerable momentum to the Solvency II preparation process. The responses to our survey indicate that where companies participated in QIS4, Solvency II projects are at a much higher stage of development, in all areas. This is in contrast to companies that did not participate in QIS4.

Leadership matters

It is encouraging that the majority of our respondents see the ultimate decision-making bodies, i.e. boards of directors both as important participants and drivers of the Solvency II preparations. Generally, companies with a stronger involvement of the board of directors are at a more advanced stage of development in the Solvency II process. In addition, boards of directors are seen as drivers of the process more often in companies which participated in QIS4 than in companies who did not participate. QIS4 and the underlying results apparently help firms gain the necessary support of senior management.

Small companies relatively intact

Surprisingly, the proportion of companies that have not started their Solvency projects is relatively large (44%). Nevertheless, this group is made up of small entities, most of which are waiting for group support, as a result of which they

“ I foresee the negative impact relating to supervisors in the sense of having less time for more reasonable things. Nevertheless, I expect a positive impact on relations with the supervisor because of more frequent and detailed contact

Survey respondent



will be included in a group-wide Solvency II project. As 60% of these companies have not participated in QIS4 at all, they may be disadvantaged in comparison to entities that have participated and were able to take advantage of their experience with QIS4 to boost their Solvency II projects. In addition, such companies may not be ready for full and sufficiently meaningful involvement in subsequent quantitative impact studies.

Resources need to be re-evaluated

The majority of our respondents (52%) expect that Solvency II will be implemented using their existing resources as part of their standard activities. Some practitioners will see this as overly optimistic, a view which we share. Utilisation of the central or regional resource teams is considered less important (27% and 14% respectively). Only one firm has allocated full resources to Solvency II. At the same time, small companies in particular appeared to be somewhat unsure when asked to specify their resource needs in implementing different areas of Solvency II. This suggests that project structures are still very much at the developing stage, and will need to be re-evaluated in light of future progress.

A narrow focus

Large companies tend to address all three pillars from the start, whereas small and medium-sized companies are starting with particular areas first. At the same time, there is a difference in the perception of Solvency II challenges between companies addressing all pillars and companies working only on particular areas. Three pillar companies are generally more worried about certain areas than companies working only on particular areas. This could indicate that a narrower focus of a Solvency II project may lead to an underestimation of the true challenges it presents. Interestingly, companies dealing only with specific areas see Solvency II as bringing a lower added value to their businesses than companies that consider all three pillars together. Few respondents expressed their concerns regarding Pillar III, which related mostly to underdeveloped implementation measures. In parallel with Solvency II activities some respondents are making visible progress in the Economic Balance Sheet area.



Areas of concern

Generally, the survey participants expect that the timing of implementation, business process redesign, documentation, Own Risk and Solvency Assessment (ORSA), data quality and IT systems will be the greatest areas of concern. QIS4 participation generally reduces concerns about most of the areas. Nevertheless, this is not true for the areas of market risk, data quality and ORSA, where we see increasing concerns of companies that participated in QIS4. It appears that work on QIS4 reveals the areas where the devil in the detail may cause some difficulty.

Implementation challenges

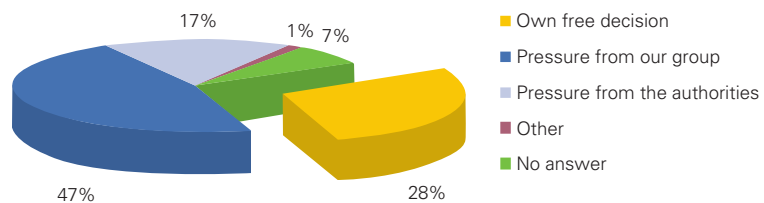
Business process redesign and the cost of compliance are the top two implementation challenges overall. The perception of other challenges is affected by QIS4 participation. Lack of understanding of the Solvency II Directive, IT system development and data capture, risk management integration and embedding are the areas considered to be a greater challenge by companies that participated in QIS4 than those that do not. From this perspective, the perception of challenges clearly depends on the company's level of experience.

Strategic impacts

Insurance firms expect many positive strategic impacts and value creation opportunities in relation to Solvency II. The majority of respondents see value created in particular by improved management information for day-to-day and strategic decisions, as well as in relation to capital management. Interestingly, 25% of our respondents expect a negative impact on the information that they will report to supervisors. From this perspective, part of the market does not appear to be ready to share sensitive information with external stakeholders. This also coincides with the expressed concerns related to Pillar III.

1. Reasons for starting a Solvency II project

If you started a Solvency II project, what were the major reasons?



There is a strong group of proactive companies making Solvency II preparations regardless of external pressures

Although the vast majority of CEE insurance firms are part of international financial services groups, among our respondents we see a number of entities that have a commitment to starting their Solvency II preparations regardless of any group or regulatory pressure.

In fact, almost one-third of our respondents themselves took the decision to start Solvency II projects, regardless of the fact that 38% of these companies are not individual entities or ultimate owners but are part of wider groups. These respondents are clearly not waiting for group-wide approaches to emerge but want to play an active role in Solvency II preparations from the very beginning. Among other things, they consider Solvency II as a tool for increasing risk awareness in the company and an additional method for risk evaluation.

The remaining respondents, the majority, started, their Solvency II activities in response to group or regulatory pressures. This is clearly evident and in line with our observations of the CEE markets.

The responses to our survey also confirmed the unsurprising observation that the level of autonomy when deciding to start a Solvency II project increases with the size of the entity. Making a decision about starting a project is more common among large companies, but also small companies make up a significant proportion of respondents who start projects based on their own decisions.

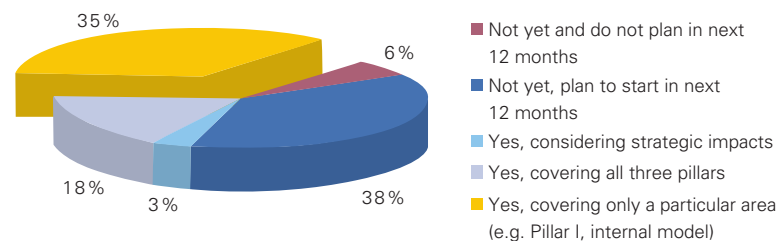
Interestingly, Slovenia has the largest number of companies that decided themselves to start Solvency II preparations. This is consistent with the active participation of this market in the Solvency II discussions in general.

“ Besides the obvious pressure from our group, our company sees the Solvency II project as an additional method for re-evaluating our risk portfolio and increasing risk awareness in the company

Survey respondent

2. Who did start implementing the Solvency II project?

Have you started a Solvency II project?



Only small entities, members of international groups, have not started their Solvency II projects

Among respondents, a relatively large group of companies had not started their Solvency II projects by the date we carried out our survey. Specifically, 8% of our respondents have not started Solvency II preparations and do not intend to do so in the next 12 months either. In addition, 38% had not started but intend to do so within the next 12 months. This may appear surprising, given the overall level of commitment across the surveyed companies and the stage of development in the Solvency II regulations.

Nevertheless, a closer examination reveals that those that have not started implementing a Solvency II project are small entities expecting to take advantage of the Solvency II project support provided by the group, which appears to be a pragmatic and appropriate approach for such companies. On the other hand, our survey indicates that these entities consider the Solvency II issues less challenging than those that have already made some progress. This could mean that companies that have not started are unable to realistically assess the real challenges of the process.

“ The main focus is on Pillar I issues, but in parallel with this we have already started the documentation and governance redesign processes related to Pillar II. Pillar III is also targeted but details will mature at a later phase ”

Survey respondent

The work carried out relates predominantly to Pillar I

Ongoing Solvency II activities relate to quantitative Pillar I issues such as calculations based on the standard formula and the development of internal models for certain risks. Some respondents also started working on Pillar II governance issues, but this area was mentioned in the survey responses to a lesser extent. Consideration of Pillar III issues is seen as too early at this stage given the underdevelopment of this area and the relevant implementation measures. Solvency II activities are sometimes coupled with work on Economic Balance Sheet, an activity predominantly visible at large entities.

A wider focus from the start helps to reveal the true challenges

Large companies tend to address all three pillars from the start, whereas small and medium-sized companies are starting with particular areas first. On the other hand, the perception of the Solvency II challenges depends on the scope of implementation across the three pillars: the wider the initial coverage, the less confidence a company has in its own resources as it progresses. This can indicate that a narrower focus of a Solvency II project may lead to underestimation of the true challenges.

Interestingly, companies addressing only particular areas see a smaller added value of Solvency II to their businesses than companies that consider all three pillars simultaneously.

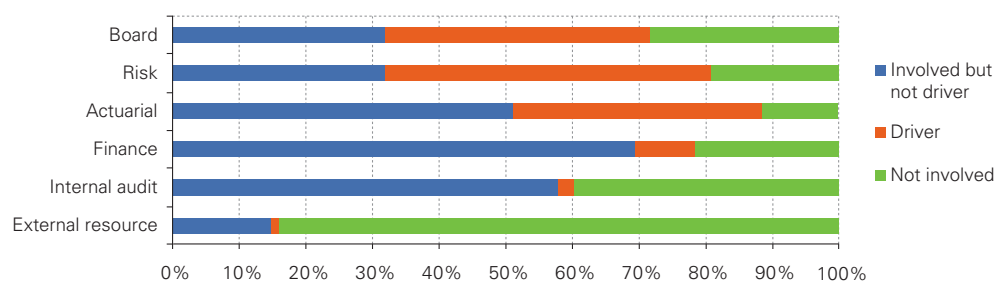


3. Drivers of the process

“ This is the current situation but as the project progresses we expect involvement of the board, finance and compliance as well ”

Survey respondent

Which functions are involved in the Solvency II project and who is driving it?



The visible involvement and commitment of top executives to the success of a Solvency II project

In line with the answers to other questions, pressures from the group are mentioned frequently among the reasons for starting a Solvency II project.

The risk and actuarial functions are the most common drivers of the preparation process

At the company level, the process drivers are clearly the boards of directors, risk and actuarial functions. The high level of commitment of the ultimate decision-making bodies, as seen from the answers provided, can be considered a positive factor. This slightly contradicts information from the national markets, where we observed complaints from supervisory bodies from time to time about a lack of involvement in and low awareness of top executives of Solvency II.

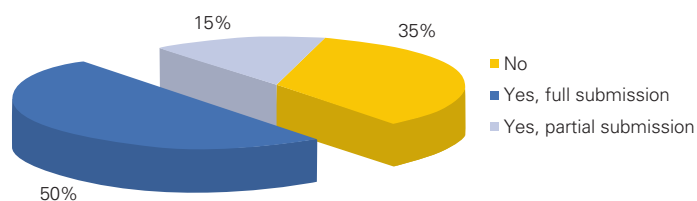
Apart from the functions mentioned above, which are both involved in and drivers of the Solvency II preparations, all key functions of an entity are involved in the process to some extent. This is expected, given the overarching nature of Solvency II. Nevertheless, the comments of certain survey participants lead us to believe that the level of involvement of functions beyond actuarial and risk is formal rather than proactive at this stage. This will probably change in the future.

Risk function is perceived as a clear driver of the process in virtually all large companies. This could indicate that they are at a higher stage in establishing key functions and their governance structures are more advanced.

The board of directors is perceived as a driver more often at small companies, where the contact of senior management with professional staff is probably more direct than at large entities. Actuaries are seen as drivers predominantly at companies that expect group support in the Solvency II preparations. This is consistent with our observation from the market that the actuarial profession is most prepared for adoption of sophisticated methodologies from the group.

4. QIS4 participation

Have you participated in QIS4?



Small companies may struggle due to a lack of QIS4 experience

The participation rate in the QIS4 exercise is clearly driven by the size of the entity. Whilst the overall participation rate was about 50%, the rate among companies classified as large was almost 100%. Three-quarters of medium-sized companies participated fully, and almost 90% of them prepared at least a partial submission. On the contrary, 60% of the companies classified as small did not participate in the QIS4 at all. This may be somewhat worrying as these companies may not grasp the full complexity of the issue and may not be prepared for using the right simplifications appropriate for their business in QIS5 and subsequently under Solvency II.

Interestingly, the participation in QIS4 appears to highlight the enthusiasm of small companies for Solvency II. Among companies participating in QIS4, we see a higher proportion of those that started implementing a Solvency II project based on their own decisions and are consequently more self-confident in using only their own resources in carrying it out. In contrast to the above, the confidence in own resources in conducting a Solvency II project is lower among large companies participating in QIS4. This is probably due to the notable differences in the complexity of a QIS submission between a large and a small entity and generalisation of the QIS experience in other areas as well. Large companies apparently may struggle with putting all the required information in place and properly capturing the complexity of their business in calculations. While we admit that doing so is easier for small companies, we are not sure whether the greater optimism of small companies stems from the fact that putting the information together is genuinely simpler for smaller companies thanks to their size or because they are compromising the quality of the submission or oversimplifying the calculations.

QIS4 participation is a clear catalyst in the Solvency II preparations

Approach to Solvency II depends on management's attitude. Whereas the management of a large insurer cannot repel dealing with Solvency II, small entities seemingly are divided according to how management considers the importance of this issue. There are some believers who participated in QIS4 and started the Solvency II project and there are some sceptics who have been following a wait and see strategy.

It is encouraging that the stage of development in Solvency II preparations clearly correlates with the level of participation in QIS4: with more involvement in QIS4, comes a higher stage of development in a Solvency II project in any area. From this perspective, the participation in QIS appears to be an important driver for gaining the necessary support and achieving the required progress in Solvency II.

QIS4 participation increases senior management support and helps in an understanding of the key challenges of Solvency II implementation

It is also positive that QIS4 participation increases the commitment of the senior management to Solvency II projects. The proportion of companies where the board is seen as one of the key drivers of a Solvency II project is the largest among companies participating in QIS4. This can be explained by the fact that boards are finding the QIS results useful for their business needs. On the contrary, companies not involved in QIS4 consider involvement of the board in the Solvency II preparation process more of a challenge.

The involvement in QIS4 generally reduces the level of concerns in all Solvency II areas. This is however not true for market risk, data and ORSA, where concerns increase with an increasing participation rate in QIS4. Small companies are generally the most concerned about embedding risk management in their businesses. The top three areas of concern, regardless of size, are: ORSA, Implementation and timing, and the supervisory review process.

Generally, QIS4 involvement also reduces the number of areas perceived as challenging. This is not true for business process redesign, cost of compliance, lack of understanding of the directive, IT system development and data, and integration of risk management and embedding it in the business. Some of these concerns can be clearly linked to practical experience with the process of preparing the QIS4 submission. The concern relating to embedding risk management probably reflects the perceived difficulties of linking quantitative information and qualitative risk management, and using them sensibly for business needs.

Whereas the majority of our respondents did not see a need for external resources in any of the Solvency II areas, participation in QIS4 appears to change this viewpoint: among companies participating in QIS4, the score for requiring external resources in most of the Solvency II areas is higher.

Companies participating in QIS4 generally have more positive expectations of the benefits of Solvency II. Differences arise when we examine the QIS4 participants per size. Large companies are generally the most optimistic in terms of capital management across the group and business unit factors; areas where small companies appear to be less optimistic.

// We have not provided all figures due to lack of modelling technology //

Survey respondent

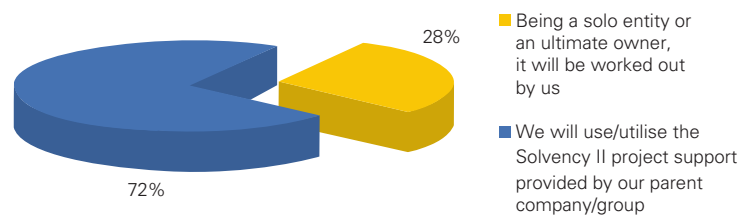


5. Approach to the Solvency II project

Our parent company will use the internal model but it is not clear when and how we will adopt it. We are developing our models together with similar entities in the region at this stage

Survey respondent

What is your approach to an existing/future Solvency II project?



The majority of the entities are conducting their Solvency II Activity as group project

Seventy per cent of our respondents intend to use group support in their Solvency II activities. The expectation that the group will provide support predominates in the answers provided, regardless of the size of the entity.

Companies running their Solvency II projects individually decided to do so based on their own decisions. These entities are progressing independently and are self-confident in their ability to prepare for Solvency II. On the other hand, in terms of details, i.e. specific Solvency II areas, approximately 50% of these entities have not started their activities in most of the areas concerned. This is somewhat worrying, and may indicate that ambition fails to be matched by reality.

Being an active participant in the project

Regardless of whether a company is a sole entity or part of a group, we see a relatively strong commitment of local entities to proceed with Solvency II, regardless of the activities of the group. Several respondents noted that whilst they require group support in developing internal models, entities are willing to start their own activities, which will apparently be included in the group activities later on.

Regulators in CEE are committed to pushing forward Solvency II preparedness

A considerable part of the small companies that do not expect group support attributed the reason for starting the Solvency II project to regulatory pressures. This shows that some regulators in CEE are proactive in pushing forward Solvency II preparations.

Interestingly, both large and small companies tend to make better progress in Solvency II preparations if they started doing so themselves, without group involvement and support. This is, however, not true for medium-sized companies, which make less progress if they start Solvency II preparations alone. We believe that large companies can benefit from their more advanced resources and small companies can benefit from their size. Medium-sized companies do not appear to enjoy such benefits.

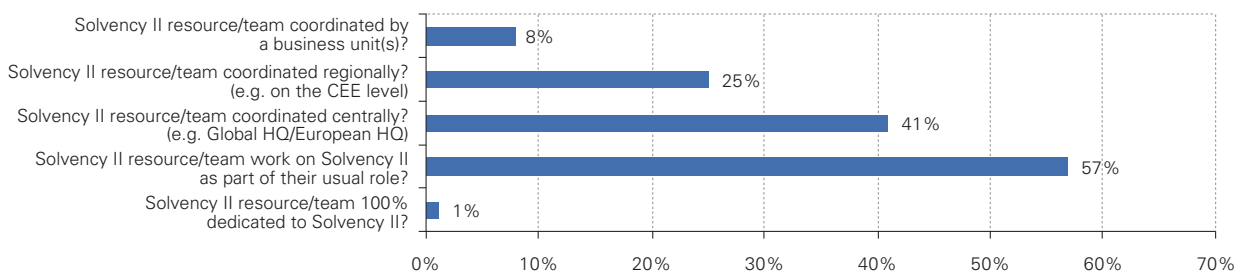
Again, this effect may be a consequence of the fact that large insurers must deal with Solvency II whereas small entities, if started, i.e. having a devoted management, have made a good progress due to management buy in.

6. Who will do the Solvency II work?

Our resource needs are expected to increase significantly after 2010

Survey respondent

If you have a Solvency II resource/team, please tick all that apply from the following:



The Solvency II requirements will be met through existing resources as part of firms' standard activities

Only one out of the eighty-eight respondents has a specific Solvency II team, which is fully dedicated to the Solvency II agenda. The vast majority of our respondents expect the Solvency II requirement to be met with existing teams, as part of their standard activities. Such a perception is stronger among large and medium-sized companies, where the overwhelming majority (80%) relies on existing teams in relation to addressing the Solvency II agenda. Small companies appear to be different. Only 29% of small companies expect to meet Solvency II requirements with existing teams, as part of the firms' standard activities.

QIS4 participation apparently increases self-confidence in Solvency II related work and eliminates certain concerns about future progress. The proportion of companies that expect to meet Solvency II requirements through existing teams, as part of standard company activities, is much larger among the companies that participated in QIS4 than among those that did not.

Whilst admitting that progress with QIS4 can increase the optimism of many participants, we note that the reliance on existing resources in meeting the Solvency II requirements may be too optimistic. This may stem from the fact that most of the Solvency II projects are only in their early stages of development. We assess that many industry practitioners will reassess their resource needs in line with the progress made in Solvency II preparations.

Small companies lack clarity about their resource needs for Solvency II

We also note that only few small companies which, among other things, did not participate in QIS4 have assigned Solvency II preparations to an accountable individual. This can also contribute to the perception that the Solvency II preparations will not need extra resources.

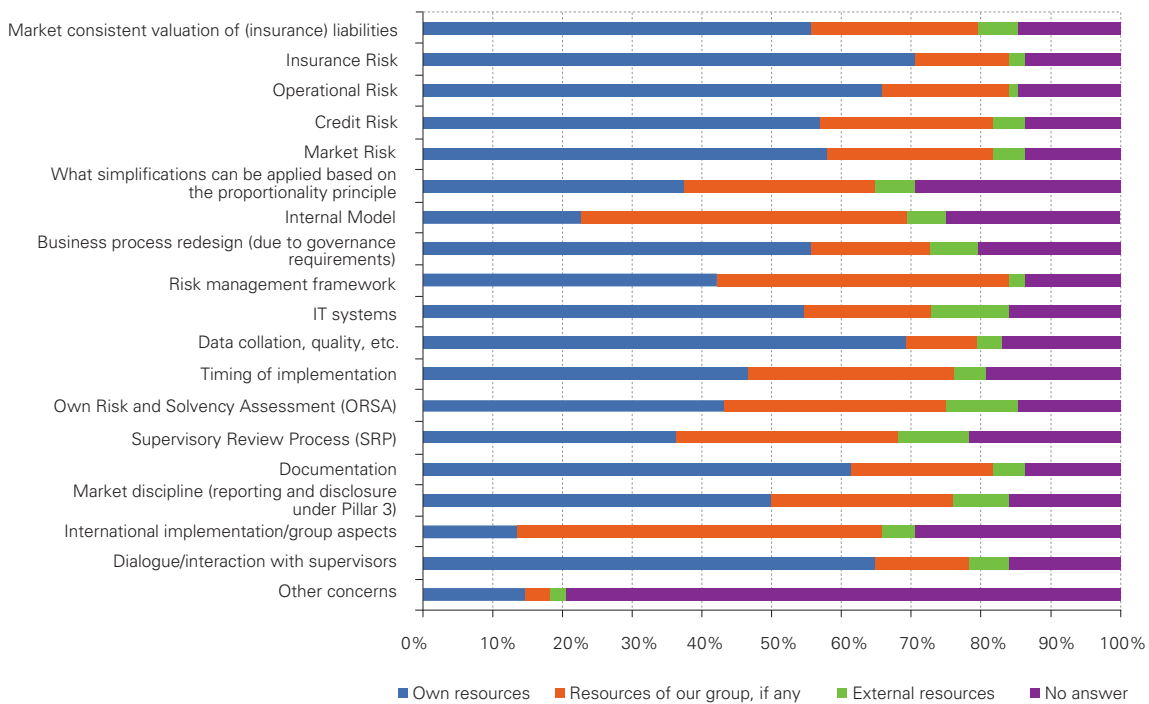
A relatively large number of respondents did not provide answers to specific questions regarding their resource needs. We understand that these blank responses may reflect that at this relatively early stage of development these companies do not know which resources they need. They should start planning for meeting their resource needs as soon as possible.

7. Where do the resource needs lie?

As we are at the very beginning of the Solvency II project, we may not see areas where we will need external resources

Survey respondent

Please identify the areas where you think the implementation of the Solvency II project will require (own resources, resources of the group, external resources):



High reliance on own resources for most of Solvency II areas

In virtually all of the surveyed areas the majority of companies do not expect to use external resources but their own and group resources. On the other hand, small companies appear to be unable to assess which resources they would need in particular areas of Solvency II at this stage.

The expectation that external resources will be provided is generally very low, which respondents admitted in areas of IT systems, supervisory review process and ORSA. Overall, no more than 5% of respondents stated that they expected involvement of external resources.

Very limited expectation of external resources at this stage

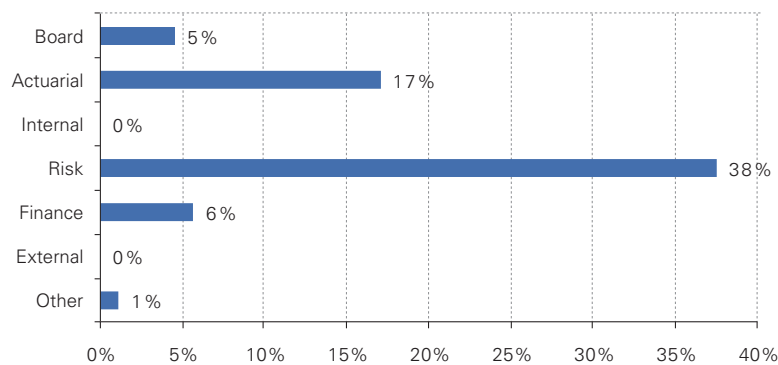
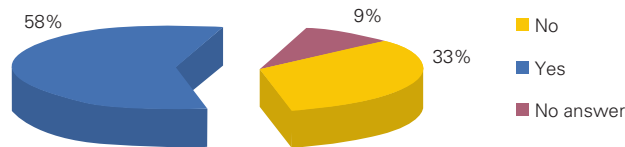
As a Solvency II project develops, both confidence in a company's own resources and the perception of a need for external and group resources grow. Part of the respondents appear more confident about advances in their Solvency II projects, whereas others appear to need support from the group or an external party when coming to the detail. Companies admitted they need group support in international implementation and group aspects, internal model, risk management framework, supervisory review process and ORSA.

8. Project management

// Risk management is guided at the group level; we locally nominated an accountable individual for Pillar I

// Survey respondent

If you have a Solvency II project, have you nominated an Accountable individual / Project Manager?



There are more risk managers than actuaries leading the Solvency II project

The majority of companies, around 60%, have already nominated individuals accountable to manage the whole project. The remaining 40% are mostly firms that have not yet started the project and therefore have not appointed a project manager. A small number of companies that have already started implementing Solvency II requirements are now in the initial stage but without a project leader. In other cases, as some answers indicated, there is not a single project leader but rather different project leaders for each pillar.

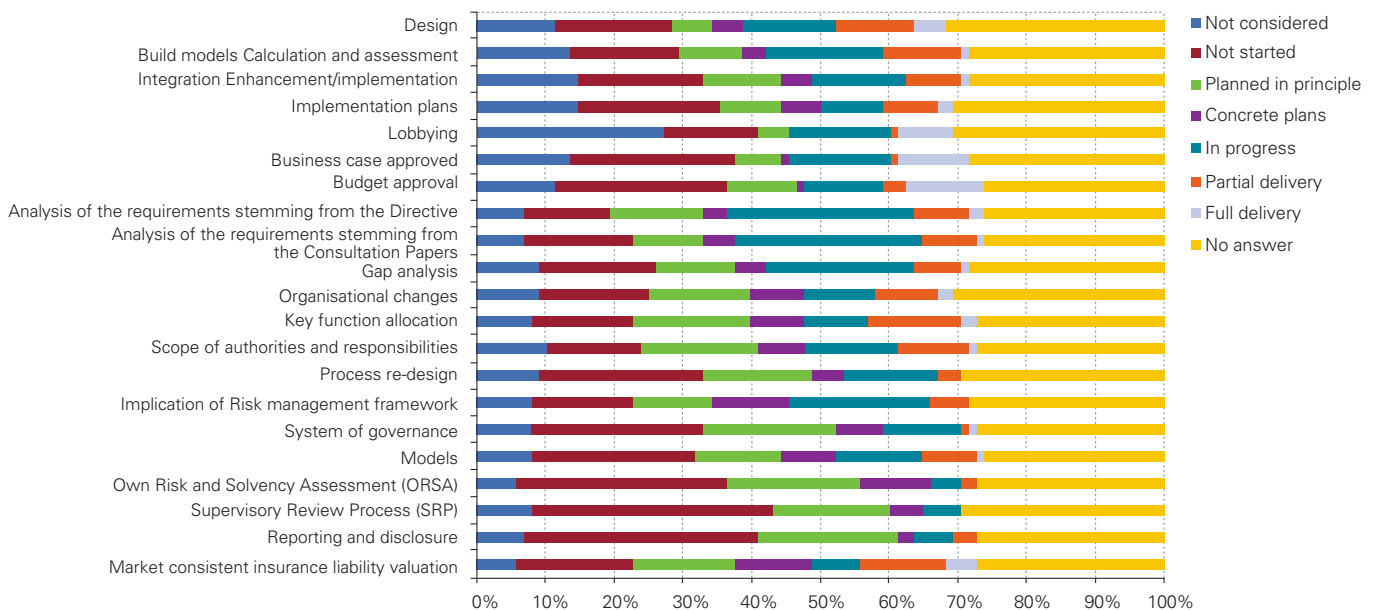
The position of the project leader also depends to a great extent on group support. In smaller companies without a risk officer, the Solvency II project is managed by actuaries or the finance department, but, as some responses stated, on a group level it is usually the risk function that has overall responsibility.

We can conclude that companies have a clear view of key areas of expertise required for a successful project leader for Solvency II. Forty-five per cent of companies that started implementing Solvency II requirements appointed their risk managers as project managers, followed by 30% who appointed actuaries. The remaining 25% chose the finance department or a member of the board to manage the project. We can see that there was progress in considering Solvency II only as another actuarial exercise. Appointing risk managers as project leaders gives a clear signal that companies are now considering Solvency II primarily as a method for better understanding and managing risks.

9. At what stage is your Solvency II project?

// We will be able to give more precise information three months later //
 Survey respondent

If you have a Solvency II project, what phase is it at, on average?



Strong correlation between the size of the company and stage of preparedness

As requirements are not fully described no company has completed all of the requirements.

Larger companies are more advanced in preparation

As no company has even partially gone through the Supervisory Review Process (SRP*) it could be the case that Supervisors in the CEE region are not yet prepared to review the new solvency regime at insurers although some of them started the assessment process of the local market players and they have also begun working together with other European supervisors responsible for the big European insurance groups.

It is apparent that large companies that are more advanced in their preparation for Solvency II are less concerned about risk. This could be due to the fact that the level of risk management required by Solvency II reduces risk. However, it could also be because larger companies are more advanced in their preparations, and they stand to benefit the most from Solvency II changes. However, in some aspects companies that are more advanced in project analysis have more concerns, e.g. data availability or ORSA.

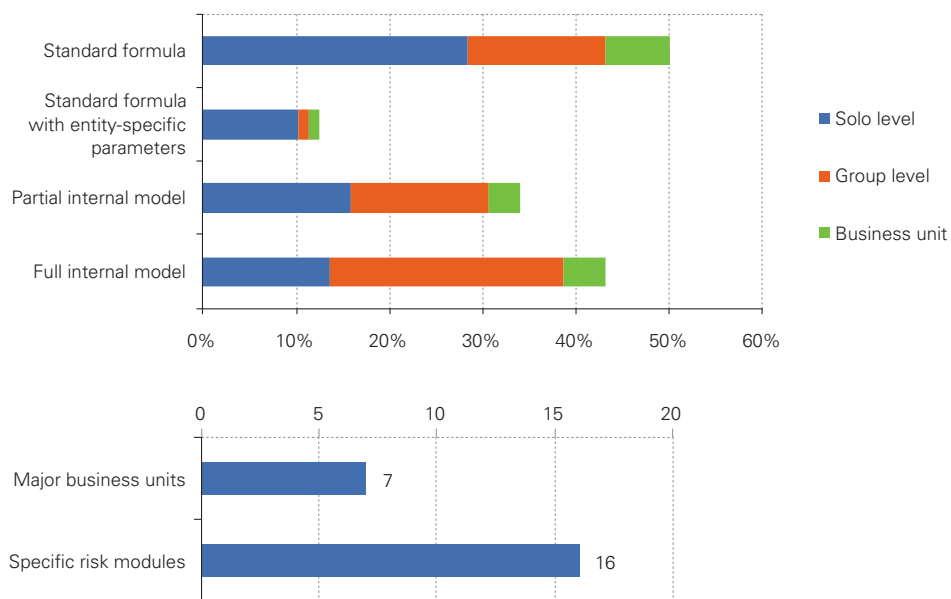
* SRP covers the entire process of how insurers are supervised; it consists of ORSA (self assessment) and a consultation between the entity and the supervisor.

10. Planned approach within Pillar I

// We will use the standard formula at the beginning, and later the internal model since the group is developing it

// Survey respondent

For which approaches for calculating your capital requirement are you likely to seek regulatory approval for the Solvency II implementation date (assuming this will be 2012) and across which organisation?



Both Pillar I initial approaches appear equally popular: the standard formula, selected mainly by smaller firms, and internal models, clearly preferred by large players

Even though a considerable number of the survey respondents intend to confine themselves to using a standard formula at the Solvency II implementation date, a significant number of entities are aiming for a more advanced strategy at the start. This approach is particularly popular if regulatory approval is to be sought on the group level: fewer than one in four firms in this group is planning to base their capital calculation exclusively on the standard formula and more than 40% are targeting implementation of the full internal model only.

This shows that for many insurers future benefits of entity-specific strategies are expected to outweigh the challenges recognised (both expected value added and expected issues are discussed further in this report). In addition, it should be noted that in the long-term perspective (after the Solvency II implementation date) some companies may choose to develop internal models, even though due to time, resource or other constraints they may find it unrealistic to complete this process in the coming years. On the other hand, other companies could find out that they had underestimated the challenges and change their approach accordingly.

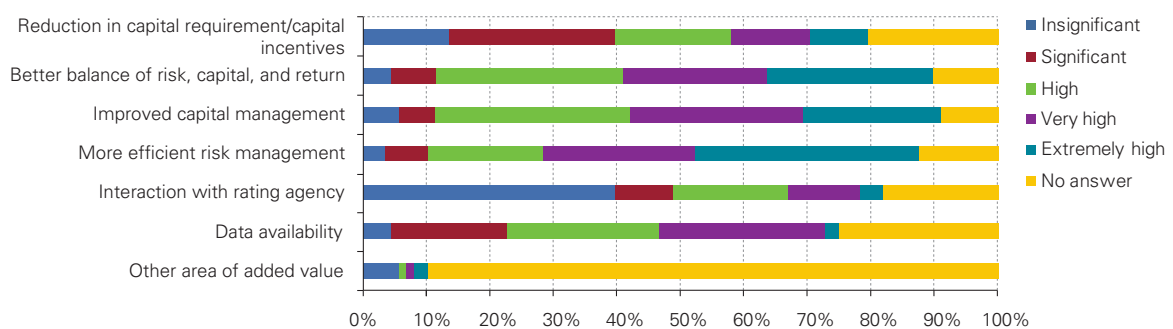
It is clearly evident that large firms have more ambitious plans for Pillar I than medium-sized and small firms. Two-thirds of these companies intend to use at Solvency II implementation the full internal model exclusively (regardless of the level of regulatory approval).

11. Value added from selected approach to Solvency II

// We will better understand the risks to which we are exposed, and maybe we will find better approaches for managing them //

Survey respondent

Where do you consider the adoption of your preferred approach will add the most value?



Solvency II benefits are recognised by most insurers especially in the areas of risk and capital management

The majority of CEE insurers participating in our survey expect that adoption of their preferred approach will bring significant added value. They are particularly optimistic about more efficient risk and capital management, as well as a better balance of risk, capital and return. Over 75% of our respondents expect high added value in these areas. This is despite more cautious expectations concerning a reduction in capital requirement, indicating that insurers perceive risk and capital management benefits from Solvency II projects in a broader context.

On the contrary, there is relatively high scepticism about the impact on interaction with rating agencies. Almost 40% of companies participating in our survey consider the value added in this area insignificant. This is probably not a surprise as only few companies from our region maintain direct and regular communication with rating agencies.

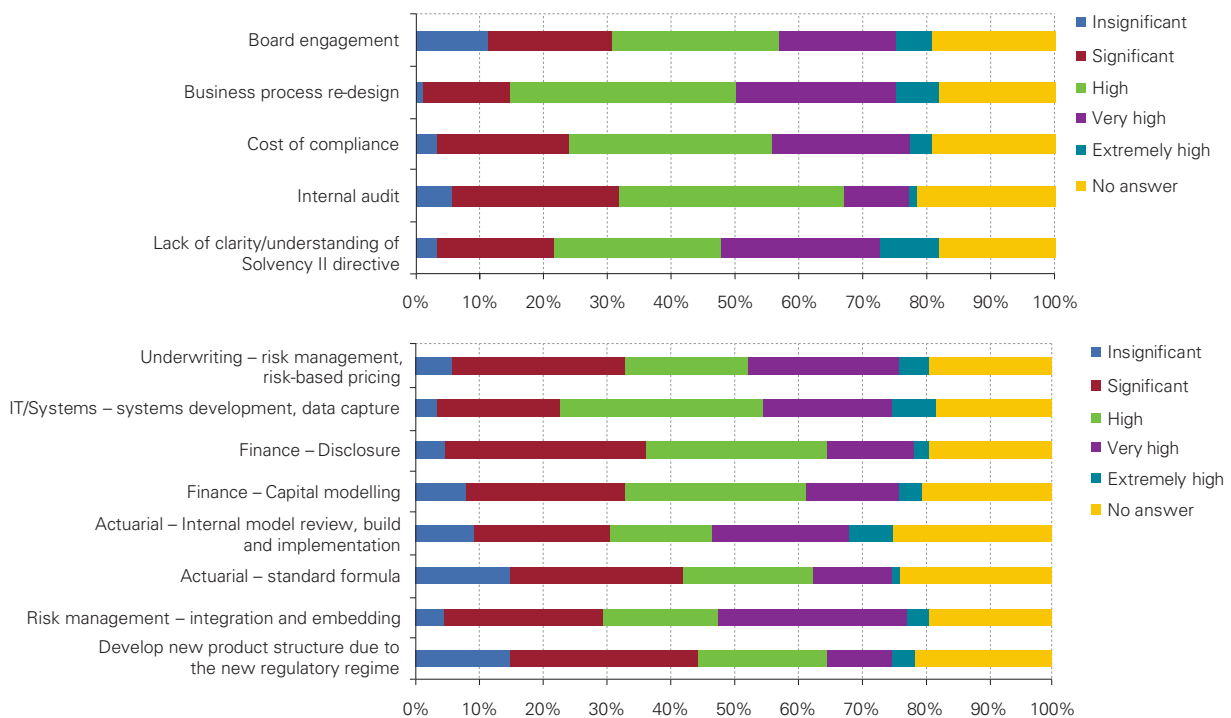
The above tendencies are driven mainly by small entities, which strongly differentiate their assessment of benefits from the Solvency II project, depending on the area. The larger the company, the smaller differences it tends to see between benefits in particular areas. Unsurprisingly, on average large insurers present the most optimistic approach. However, interestingly, small entities tend to be more enthusiastic than medium-sized entities.

The high added value expected by small entities with regard to risk and capital management aspects in contrast to their low expectations in other areas appears to result from the support they hope to receive from the group in such areas. It is noticeable that particularly optimistic answers tend to be given by small firm respondents, which intend to use the Solvency II project support offered by their parent company or group.

Large companies generally believe that there is greater added value, and their answers seem to be more positive if SII activity is part of a group project.

12. Challenges of the selected approach to Solvency II

What do you consider as the challenges to implementation of your preferred approach?



Even though Solvency II challenges are considered equally strong as benefits, a closer look reveals that they often decrease with the progress in a Solvency II project

Appreciating Solvency II benefits the survey participants also attach importance to challenges related to implementing the requirements. In most areas, fewer than 10% of entities consider the potential issues insignificant. Unsurprisingly, smaller firms tend to be less confident about their abilities and resources than larger companies.

One of the most problematic areas appears to be Solvency II Directive clarity. Although a more detailed analysis of results shows that concerns are particularly strong among those entities that have not yet started the Solvency II project, we believe that this challenge may be to some extent overestimated. Similar observations actually relate to all other types of challenges, but the dependence on the progress in Solvency II implementation appears weaker.

Another interesting observation is that life insurers tend to be more optimistic about many of the Solvency II challenges than composite or, particularly, non-life entities. This is especially visible with regard to skilled resources in such functional areas as new product structure development due to a new regulatory regime, underwriting (risk management and risk-based pricing) or finance (capital modelling), but to some extent also with regard to actuaries dealing with Pillar I issues or IT resources.

Interestingly, among life insurers the greatest optimists are those that have already been calculating European or Market Consistent Embedded Value. Since many issues arising upon implementation of the Solvency II regime are encountered also during EEV or MCEV modelling, such companies may rightly expect to draw benefits from previous investments in EV while struggling with the Solvency II project.

// We do not have sufficient information at this stage to assess these challenges

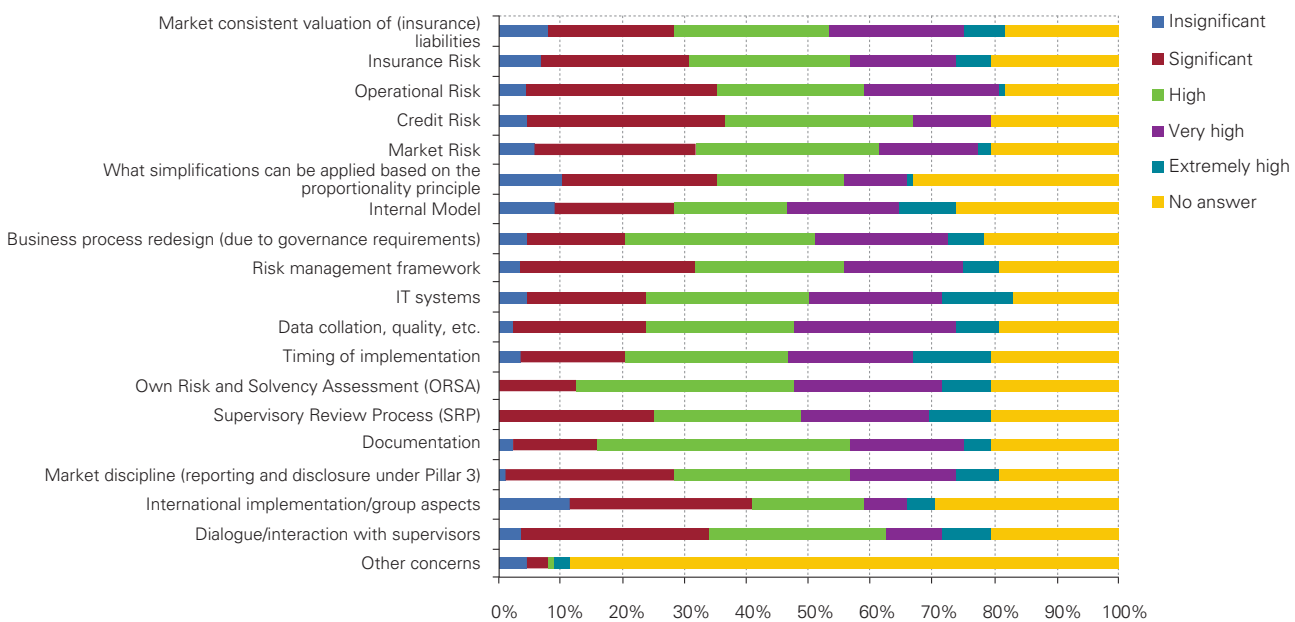


Survey respondent



13. Which areas of Solvency II are raising the most concerns?

Which areas of the Solvency II proposal are giving you the most cause for concern?



The level of insurers' concerns about Solvency II tends to be higher if more benefits are expected. Therefore, the level of concern appears linked to the overall complexity of the approach taken.

Regardless of which Solvency II Pillar areas are considered, the vast majority of our respondents appear to have significant concerns about dealing with them. For most topics listed in our survey over 70% of companies assessed their concerns as significant. In general, the larger the entity, the greater its confidence.

Obviously both Solvency II benefits and issues regarding its implementation are likely to depend on how ambitious and comprehensive approach a given company has chosen. This expectation appears to be confirmed by the results of our survey. Companies that foresee less value added from adoption of their preferred approach clearly tend to have on average fewer concerns related to this process.

We find it encouraging that in many areas insurers that are more advanced in the Solvency II project tend to be more confident than those that are less advanced. This particularly holds true for Pillar I topics, group aspects as well as some general issues (such as timing of implementation and IT systems).

Again (similarly as for Solvency II challenges), a relatively optimistic attitude is shown by life insurers in comparison to non-life and composite companies. This relates especially to Pillar I topics. However (in contrast to our previous observations regarding Solvency II challenges), in many of the Pillar I areas (including MC valuation of liabilities, insurance, credit and market risks) life insurance companies that have been calculating European or Market Consistent Embedded Value tend to have more concerns compared to those that have not. This observation leads to the conclusion that firms operating in the life insurance market that are currently less advanced in these areas may discover in the future that their relatively high confidence was not fully justified.

// Given our current knowledge of the Solvency II requirements, we believe that we will be able to comply. However, future changes to Solvency II requirements may increase the risk of being partially non-compliant

//
Survey respondent



14. Strategic impacts

An opportunity to improve business practices across the whole insurance market

Survey respondent

Which of the following areas of your business do you believe will be strategically impacted?



The positive strategic impact of Solvency II is expected in all areas, with management processes at the top.

There is no doubt that CEE insurers recognise the positive potential of the Solvency II project. In all of the areas listed in our survey expectations that it will have a positive strategic impact are therefore much more frequent than expectations of a negative impact. In addition, optimism generally appears to grow with the size of an entity. However, this does not mean that smaller entities are significantly more pessimistic – usually they have just not considered the Solvency II pros and cons to the same extent as larger firms and more frequently do not feel able to formulate their view yet.

Our respondents tend to be the most enthusiastic about the Solvency II strategic influence on the following areas:

- Management information required for business decisions (especially strategically, but also day-to-day decisions);
- Capital management both in business units and across groups.

This is no surprise, considering our findings from the most appreciated Solvency II anticipated value added, presented earlier in this report.

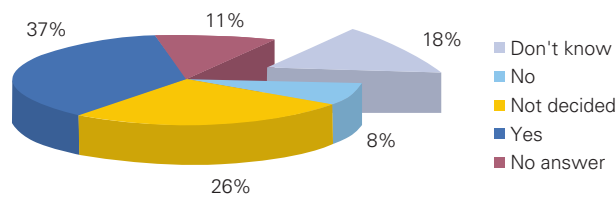
Potential negative changes resulting from Solvency II generally do not appear to be a significant threat to the vast majority of the survey participants. However, there are quite strong concerns relating to the influence on future reporting to supervisors, with particularly high rates of negative impact expectations among Slovak and Czech companies.

It is encouraging that companies already working on a Solvency II project (at least in the high-level planning phase) are generally more enthusiastic about its future strategic impact than companies that have not yet started at all (although this is not 100% true for all potential Solvency II influence areas).



15. Group support

If group support is allowed under Solvency II, do you expect to apply this option across your group?



CEE insurers would welcome group support

Companies in CEE were not sure how to deal with the group support regime. Only 50% clearly indicated whether they expect to benefit from group support or not to use it. Around 30% of companies did not know if they would use it and the remaining 20% were undecided. This uncertainty is affected by several factors. One is that at the time the survey was completed, it was not clear to all participants if group support would be permitted. It should be also considered that in most cases this is not decided on a company level but rather a group level. Last but not least, a factor to include on group support application within CEE is that many participants may not be aware of group support regime aspects and benefits, and therefore their answers could be different if they had a deeper knowledge of this issue.

Insurers would in general welcome group support regime, because 40% clearly stated their intention to make use of the group support regime and only 10% were against it. We think that the remaining undecided companies are also more likely to use the group support regime, if it would be permitted.

Almost all insurers that expect to use group support are subsidiaries in a group and therefore their responses to the survey may not express the same view as that of their parent companies. On the other hand, most replies that did not know if group support will be used are from entities that are not part of a group, for whom this issue is either not applicable or has not yet been encountered.

// This depends on the final outcome of the Solvency II Directive //
Survey respondent

Conclusion



The results of the survey undoubtedly showed that the preparations for the new Solvency II regime are a priority issue for insurers operating in the CEE region.

The survey findings clearly demonstrate that only small companies which expect group support have their Solvency II projects relatively undeveloped. Other entities are making visible progress and are conducting their Solvency II preparations regardless of external pressures. These firms expect to enjoy the benefits that can be achieved from implementing Solvency II, particularly in management of information for day-to-day and strategic decisions, as well as in relation to capital management.

The participation in QIS4 boosts project momentum and helps firms to gain the necessary support from senior management. This is a clear message which underlines the need to participate in the subsequent quantitative impact studies conducted by CEIOPS.

It is encouraging that a significant portion of our respondents see senior management as the driver of the Solvency II preparations. On the other hand, wider business functions unrelated to risk and actuarial are not yet sufficiently involved in the process.

The negative expectation of some respondents regarding the quality of information submitted to regulators could be considered an indicator that part of the market is not yet ready to share risk-sensitive information with external stakeholders. This will need to change as progress is made in Pillar III issues.

The findings of this survey indicate that firms not involved in previous QIS exercises or waiting for group support in implementation may not see the real challenges of Solvency II and may be underestimating the extent of necessary work.

To meet the currently proposed 2012 submission target date the pace of Solvency II implementation will need to quicken for all entities – a wait and see approach is no longer a sensible option.

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