Directives

of Federal Office of Private Insurance FOPI

31 December 2006

13.4/2006 – on Solvency I for Insurance Groups and Insurance Conglomerates

Legal basis:	**Articles 69 and 77 ISA** **Article 22 SO** **Articles 23 - 36 SO** **Article 39 SO** **Article 198 SO** **Articles 199 - 200 SO** **Article 202 SO** **Article 204 SO** **Article 206 SO**
Decision of:	**21 November 2006**
Entry into force:	**31 December 2006**

Schweizerische Eidgenossenschaft
Confédération suisse
Confederazione Svizzera
Confederaziun svizra

Swiss Confederation

Swiss Federal Department of Finance FDF
Federal Office of Private Insurance FOPI

1 Background

This Directive states the minimum requirements for the calculation and reporting of the required and the available Solvency I for insurance groups (groups) and insurance conglomerates (conglomerates) to be submitted to the responsible supervisory authority.

This Directive is based on article 69 ISA and articles 198 to 200 SO for groups and on article 77 ISA and articles 204 and 206 SO for conglomerates with respect to the choice of method and the calculation as well as the required and available solvability margin. Article 202 SO is the basis for determining the manner of reporting to the supervisory authority.

According to article 198 and article 204 SO, the solvency of groups and conglomerates must also be evaluated according to the two methods set out in article 22 SO. This Directive exclusively refers to the first method under article 22, paragraph 1(a) SO, Solvency I, the determination of the required equity capital taking into account the business volume (required solvability margin) and the allowable equity capital (available solvability margin).

According to article 199, paragraph 1 SO, the **required** solvability margin of a group must be calculated on the basis of the consolidated financial statement. According to paragraph 2, the required solvability margin corresponds to the sum of the required solvability margins for the individual areas such as life insurance, non-life insurance, reinsurance, etc. According to paragraph 3, the area-specific solvability margins of a group are calculated mutatis mutandis in accordance with articles 23 et seq. SO. According to paragraph 4, the supervisory authority may permit other calculations or exclude certain undertakings of a group/conglomerate.

According to article 200, paragraph 1 SO, the **available** solvability margin of a group pursuant to a financial statement compiled in accordance with internationally recognized accounting standards corresponds to the consolidated equity capital, adjusted by the minority shares, all intangible assets, anticipated dividends and repayments of capital, and deferred acquisition costs in non-life. Other elements with the character of equity capital may be permitted by the supervisory authority upon application. According to paragraph 3, the supervisory authority determines the allowable equity capital if no internationally recognized accounting standard is used.

According to article 204 SO, articles 198 and 200 SO shall be applied mutatis mutandis when calculating the required and available solvability margin for conglomerates. This is also true of article 202 SO with respect to reporting. The specific differences are governed by article 206 SO for conglomerates. According to article 206, paragraph 1 SO, the calculation of the **required** solvability margin of a conglomerate is based on the consolidated financial statement. According to paragraph 2, the required solvability margin corresponds to the sum of the required solvability margins in the insurance and finance sectors as well as of the solvability margins for undertakings without equity capital requirements under supervision law for the finance sector. For the latter, the supervisory authority shall determine the calculation of the solvability requirement. Article 206, paragraph 4b) allows the supervisory authority to exempt undertakings without requirements under supervision law from the equity capital requirements, provided that inclusion would be inappropriate or misleading.

2 Purpose

Solvency I serves to demonstrate sufficient minimum capitalization of a group / conglomerate relative to its business volume.

3 Scope

This Directive applies to all groups/conglomerates that have been placed under supervision by means of an order pursuant to the following legal foundations:

- insurance groups pursuant to article 65 ISA;
- insurance conglomerates pursuant to article 73 ISA.

4 Terminology

4.1 Solvency I

According to article 22 SO, the solvency evaluation is performed on the basis of 2 methods: Solvency I and the Swiss Solvency Test. **Solvency I** refers to the relationship between the required equity capital taking the business volume into account (required solvability margin) and the allowable equity capital (available solvability margin).

The supervisory authority considers the Solvency I of a group/conglomerate to be sufficient if at least 100% of the required solvability margin is covered by the available solvability margin.

The Directive on the Intervention Levels governs the measures arising from this calculation and, if the solvability of a group or conglomerate is less than 150%, provides for intensified monitoring by the supervisory authority.

4.2 Required solvability margin

The **required** solvability margin of a **group** is calculated on the basis of the consolidated financial statement of the group and corresponds to the sum of the required solvability margins for the areas of life insurance, non-life insurance, and reinsurance, plus the group undertakings without equity capital requirements under supervision law. All consolidated group undertakings must be included in the calculation of the required solvability margin of the group. For consolidated group undertakings without equity capital requirements under supervision law, the supervisory authority determines the calculation of the solvability margin.

The **required** solvability margin of a **conglomerate** is likewise calculated on the basis of the consolidated financial statement of the conglomerate. It corresponds to the sum of the required solvability margins in the insurance sector, plus the required solvability margins in the finance sector and of undertakings without equity capital requirements under supervision law in the finance sector. For undertakings without equity capital requirements

under supervision law in the finance sector, the supervisory authority determines the calculation of the required solvability margin.

4.3 Available solvability margin

The **available** solvability margin of **groups** is calculated on the basis of a financial statement compiled in accordance with internationally recognized accounting standards. In principle, the result of the following calculation is considered the allowable equity capital:

Reported consolidated equity capital
 plus minority shares
 plus subordinated loans and hybrid instruments approved upon application
 plus elements with equity capital character approved upon application
 minus all intangible assets
 minus anticipated dividends and repayments of capital
 minus deferred acquisition costs in non-life

Allowable equity capital

The same conditions apply to financial statements compiled in accordance with nationally recognized accounting standards.

For the **available** solvability margin of **conglomerates**, the same conditions apply as for groups.

4.4 Accounting requirements

For the calculation of Solvency I, a financial statement compiled in accordance with internationally recognized accounting standards must be used. The International Financial Reporting Standards (IFRS) and the United States Generally Accepted Accounting Principles (US GAAP) are considered internationally recognized accounting standards.

The Swiss expert recommendation on accounting (Swiss GAAP FER), which is also used nationally, may be classified as equivalent to the IFRS by the supervisory authority upon application, provided that the necessary components for calculating the required and allowable equity capital on a consolidated basis can be shown separately.

4.5 Reporting

The calculation of the required and available solvability margin for groups and conglomerates is performed half-yearly. It constitutes Group/Conglomerate Solvency I and must be submitted to the supervisory authority within three months of year-end or interim closing. Annexes 1 and 2 of this Directive are to be used.

5 Calculation principles

5.1 Interim (half-yearly) calculation of Sovency I

While the solvency calculation to be submitted as at the end of the year is based on the audited, consolidated annual statements (profit and loss and the balance sheet), an estimate of the relevant basic data on an annual basis is necessary for calculating the required solvability margin for the half-yearly report. The company must separately show the supervisory authority which method it used to perform the estimate. For the available solvability margin, however, the consolidated figures of the interim balance sheet may be used in analogy to the annual balance sheet.

5.2 Determination of Solvency I for insurance groups

5.2.1 Calculation of the required solvability margin

Consolidated figures:

For calculating the solvability margin **required** by article 199 SO, the relevant consolidated figures for the three individual main areas of life insurance, non-life/health insurance, and reinsurance must be made available. The **required** solvability margin for these three main areas is then calculated in accordance with the supervisory requirements contained in articles 23 to 36 SO. For calculating the reinsurance quotient, only the reinsurance ceded to companies external to the group is allowable.

Reinsurance business:

Only accepted reinsurance business is considered relevant reinsurance business in the context of an insurance group. Reinsurance accepted within the group is not counted. Articles 23 to 36 SO are used to calculate the required solvability margin.

Undertakings without equity capital requirements under supervision law:

In the case of undertakings without equity capital requirements in the context of an insurance group, the required solvability margin currently is 0% of the net assets.

5.2.2 Calculation of the available solvability margin

In order to achieve the greatest possible uniformity, the following list specifies the allowable and non-allowable elements for calculating the available solvability margin.

The following are allowable:

1. Consolidated equity capital: This is the reported consolidated equity capital on the basis of an internationally recognized financial statement. The same conditions apply to financial statements compiled in accordance with a nationally recognized accounting standard.
2. Minority shares: Minority shares are added if they are not contained in the consolidated equity capital.
3. Other elements with the character of equity capital are allowable:
   a. Subordinated loans and debentures and hybrid instruments according to article 200, paragraph 2 SO on application, if they meet the conditions set out in article 39 SO. The application to the supervisory authority must be accompanied by proof of fulfilment of the conditions. The relative limits set out in article 39, paragraph 2 SO apply to the hybrid instruments of a group.
   b. Acquired present value of future profits (PVFP): The present value of future profits from acquired insurance contracts (PVFP on newly acquired client bases included in the purchase price) is allowable in analogy to the limits determined by the EU.
   c. The following assets may, upon application accompanied by a justification, be allowed vis-à-vis the supervisory authority for solvability purposes, provided that they have not already been reported as equity capital in accordance with IFRS/US GAAP. They include in particular:
      i. Surplus shares not individually allocated in life insurance.
      ii. Hybrid capital in the sense of mandatory convertible bonds that must be converted into share capital by a certain time, but that are currently not or only partially converted into share capital.
   d. Upon application, the supervisory authority may permit the use of other elements with the character of equity capital in accordance with article 200, paragraph 2 SO. Upon application, the supervisory authority decides on their allowability.

The following are not allowable or must be deducted:

1. The following intangible assets must be deducted if they have already been included in the determination of the equity capital:
   a. Goodwill from acquisitions.
   b. PVFP in the form of present value of future profits arising from insurance contracts concluded within the group/conglomerate (PVFP on own-client base).
   c. Trademarks, licenses, copyrights, and other intangible commodity rights accounted for as assets.
   d. Internally developed computer programmes (software) with limited market value accounted for as assets and externally purchased programmes with minor resale value accounted for as assets.
   e. Tax credits from earlier losses carried forward.
2. Anticipated dividends and repayments of capital (including minority shares): These include reductions of the face value or other transactions with the same aim of capital reduction. Anticipated dividends and analogous elements must therefore already be deducted from the equity capital as a precautionary measure at the time of application to the general meeting.
3. Deferred acquisition costs non-life: Since only the legally reclaimable acquisition costs in the context of surrender-value in life insurance are permissible for Solvency I, the deferral effects of multiyear acquisition costs in non-life insurance (insurance against loss or damage, health insurance, reinsurance) already included in the equity capital must be deducted.

5.3 Determination of Solvency I for insurance conglomerates

Pursuant to article 204 SO, article 198 SO and articles 200, 202, and 203 SO applicable to the Solvency I of insurance groups also apply with respect to insurance conglomerates.

5.3.1 Calculation of the required solvability margin

In the case of insurance conglomerates, the insurance and finance sectors and undertakings without equity capital requirements under supervision law are each considered separately using the block-building approach for purposes of calculating the required solvability margin. All companies predominantly or entirely contributing to the insurance sector are included in the insurance sector. Companies that cannot be clearly classified are also included in the insurance sector.

The calculation for the insurance sector of an insurance conglomerate is based on articles 198 to 199 SO and the provisions in point 5.2.1 of this Directive above with respect to the required solvability margin of insurance groups.

For the finance sector, the calculation pursuant to article 206, paragraph 2(b) SO on the basis of internationally or nationally recognized accounting standards applies. The required solvability margin in the finance sector corresponds to the equity capital requirements for this sector. In consultation with the Federal Office of Private Insurance, the bank supervisory authority responsible for the finance sector of the insurance conglomerate determines which principles apply in this regard.

5.3.2 Calculation of the available solvability margin

The provisions set out in point 5.2.2 above concerning the calculation of the available solvability margin for insurance groups also apply to insurance conglomerates.

6 Minimum requirements for reporting

6.1 Form of reporting

For Solvency I of the group/conglomerate, the following reports must be submitted together with the relevant report elements:

- Reporting scheme for insurance group XY ➔ Annex 1
- Reporting scheme for insurance conglomerate XY ➔ Annex 2

The purpose of reporting is to explain the different elements of the required and available solvability margin in detail and to present the figures over at least three half-yearly periods, e.g., current, six months prior, twelve months prior.

Changes to the calculation method used and to the required or available solvability margin must be presented and explained in a reconciliation note. Changes to the basis for

calculation such as the calculation methods, shifts in the asset and liability items, etc., must be shown and presented in a reconciliation note.

6.2 Change to calculation approach

If the insurance group or conglomerate wishes to change its calculation approach, it must submit a justified application to the supervisory authority containing the reasons for the changes and showing the effects compared to the previous approach. These changes are subject to approval.

7 First submission and submission deadlines

7.1 First submission

The solvency calculation must be submitted for the first time in accordance with the order placing the group or conglomerate under supervision.

A reconciliation table must be submitted to the supervisory authority as part of the first report on Solvency I. This table must present the individual data points in detail and explain the source of the consolidated figures and how the required and available solvability margins were calculated in detail. Adjustments to consolidated figures must also be shown.

The supervisory authority will comment in writing on the submitted reconciliation table before the calculation approach is officially approved. Approval of the approach does not, however, confirm the correctness of the overall calculation.

7.2 Periodic reporting

The required report must be submitted to the supervisory authority simultaneously in writing and in electronic form in accordance with article 202 SO twice a year within three months of the reporting date for the annual or interim financial statement. Upon a justified application, the supervisory authority may extend this deadline.

8 Annex

The reporting scheme for Solvency I is contained in Annex 1.

Annex 1: Calculation Sheet for the Solvency of Insurance Groups
Annex 2: Calculation Sheet for the Solvency of Insurance Conglomerates

Federal Office of Private Insurance

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