

Insurance & Reinsurance – Ireland

The insurance industry has endured challenging times recently, as companies have to contend with heightened competition, global catastrophes causing large scale loss, and increasingly complex regulation. Extensive regulation, such as the impending Solvency II directive, due to be implemented in early 2013, along with structural changes in the industry creates various challenges for both legal advisors and companies as they try to keep pace with local regulation and try to integrate new demands into their business models. To find out about the insurance and reinsurance sector in Ireland and the legal issues affecting it currently, *Lawyer Monthly* speaks to Tom Carney and Matthew Ryan from one of Ireland's leading law firms, Dillon Eustace.

Q Please introduce yourself, your role and your firm.

Headquartered in Dublin, Dillon Eustace has international presence in Tokyo, New York and Hong Kong. Dillon Eustace enjoys a strategic alliance with Arendt & Medernach, Luxembourg, with its practice focusing primarily on financial services, banking and capital markets, insurance, corporate and M&A, litigation and dispute resolution, real estate and taxation.

Dillon Eustace offers a highly qualified and motivated cross-disciplinary team dedicated to providing its clients with effective and commercially focused legal advice.

Q What effects will Solvency II have on the insurance and reinsurance industry in your country?

The Solvency II Framework Directive (2009/138/EC) ("Solvency II") will be implemented (possibly on a phased basis) from 1 January 2013. Solvency II seeks to enhance integration and competition in the European insurance and reinsurance markets whilst strengthening the protection of both policyholders and beneficiaries through reduction of the risk of firm failure.

The key changes for Irish insurers and reinsurers ("Insurers") as a result of Solvency II (i.e. insurers with an annual gross premium income exceeding €5m or gross technical provisions in excess of €25m) are as follows:

(i) **Revised Quantitative Capital Requirements (Pillar 1)**

Currently, the amount of capital that insurers are required to maintain is based on premium income. When Solvency II is transposed, an insurer's capital adequacy requirement will instead be based on a minimum capital requirement ("MCR") and a supervisory capital requirement ("SCR").

The MCR will be largely based on premium income, a breach of which will lead to supervisory intervention. The SCR will cover all of the quantifiable risks faced by an entity, calculated using (a) Solvency II's standard formula; or (b) an insurer's internal model (which requires pre-approval from the Central Bank of Ireland ("CBoI")). Failure to maintain an adequate SCR will result in regulatory intervention.

(ii) **Increased Corporate Governance Requirements (Pillar 2)**

Under Pillar 2, insurers will be required to formalise their risk management, governance systems and operational controls and demonstrate prudential management of their businesses. These qualitative requirements will compliment the quantitative requirements of Pillar 1. Insurers will be obliged to conduct an own risk and solvency assessment ("ORSA"), an assessment of its capital needs by reference to its specific risk profile and strategy. This ORSA must be submitted to the CBoI.

(iii) **Increased Disclosure Requirements (Pillar 3)**

Insurers will be required to make an annual public report on their solvency and financial positions additional to a private report currently made to the CBoI.

Combined, the three pillars will have a considerable effect on the management of insurance and reinsurance entities. EIOPA has conducted several quantitative impact studies relating to the introduction of Solvency II, the most recent of which attracted a response rate of over 80 per cent from insurers. Two thirds of respondents considered that they had issues with either one or both of the data or methodologies required to produce the required calculations. Almost every insurer believed that it would have to ensure adequate financial resourcing prior to Solvency II's implementation. Approximately 20 per cent of insurers did not meet the SCR from existing resources. Approximately 5 per cent failed to meet the lower MCR.

The main challenges facing insurers on the introduction of Solvency II appear to be the requirement to raise additional capital, establishing adequate corporate governance structures and demystifying the data and methodologies required to comply with Solvency II.

Q With the changing and fluid nature of insurance law, how can clients avoid the potential pitfalls?

In order to avoid any potential pitfalls, it is imperative that insurers keep abreast of legal and regulatory developments in the insurance sphere. Dillon Eustace issues quarterly insurance legislative updates and offers client staff training on a wide range of issues. Guidance is also available from the CBoI.

Q Do you foresee the need for any further legislative change in the next 12-24 months, if so why?

Aside from Solvency II, significant legislative development is likely in the Irish private health insurance market. The Irish Government is expected to seek to introduce a new risk equalisation scheme so as to facilitate a true community-rated private health insurance market. Developments in this field are expected in 2013.

Q What are the common challenges faced by your clients when involved in the insurance and reinsurance sector?

Access to capital and increased regulatory supervision

are amongst the common challenges facing (re)insurers in the Irish market.

Irish private health insurers face the additional challenge of a lack of a level playing field. Aviva Health and Quinn Health must compete with VHI Healthcare, the state-owned insurer in circumstances where the latter enjoys a derogation from the requirements of the EU insurance directives. The derogation bestows on VHI Healthcare a significant competitive advantage over its competitors in terms of reduced capital requirements and lack of CBoI supervision. Despite the judgment of the ECJ in *European Commission v Ireland*, the Irish State continues to bestow preferential regulatory status on VHI Healthcare.

Q Has the increased severity and frequency of both natural and man-made disasters had an impact on insurance law?

Regulatory intervention has increased in order to reflect the challenges faced by both insurers in today's volatile market. Of course, such intervention affects the way insurers do business. Solvency II, once implemented, will reduce the risk of firm failure following a catastrophic event. By imposing more stringent capital requirements, Solvency II will limit the impact of another financial downturn. **LM**

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