Brussels, March 2017

General Comments of the International Association of Legal Protection Insurance (RIAD) on the Review of the Solvency II Capital Requirement Standard Formula

RIAD, the International Association of Legal Protection Insurance, is the only body worldwide representing the unique interests of legal protection insurers and service providers in this field from Europe, Canada, South Africa and Japan. In this capacity, RIAD defends the high potential of legal protection insurance as an easy, affordable and high quality solution for access to justice and the law.

To ensure that legal protection insurers can perform their important task it is of utmost importance that they are able to calculate their solvency capital requirements appropriately, i.e. proportional, technically robust, and risk-sensitive.

But it has been known for several years that, without discernable reasons, the Solvency II rules which apply across all EU Member States as of January 1, 2016, set the standard parameters for legal expenses insurance with 7.0% for the premium risk and with 12.0% for the reserve risk disproportionately high. In their own risk assessments the majority of companies calculates these parameters significantly lower and, subsequently, these standard parameters do not show the 'real risk' of legal protection insurance companies when calculating the reserve and the premium risk. As a consequence, many legal protection insurance companies had to undergo an onerous, time-consuming, and expensive process to replace a set of standard parameters by parameters specific to them when calculating the Solvency II capital requirements in order to provide an appropriate representation of the underlying risks. For the calculation of these so-called undertaking-specific parameters (USP) companies used a number of distinct actuarial methods and had to apply for authorization with their national supervisory authorities to be able to use USP.

In order to reflect the actual risk situation, RIAD strongly supports recalibrating the standard parameters for the non-life premium and reserve risks. At the same time, RIAD urges EIOPA and the European Commission to maintain the possibility for legal protection insurance companies to develop and get permission to use their own USP. If EIOPA and the European Commission considered to rescind insurers' right to use USP they would render the enormous efforts previously undertaken, time and money already spent by the industry on developing USP and receiving authorisation null and void which would mean that all these efforts would be wasted and those insurers that have undertaken these efforts would be at a competitive disadvantage.

In a nutshell, it is essential to ensure that the standard parameters actually reflect the risks and therefore EIOPA must undertake all necessary efforts and pursue the exercise already initiated to recalibrate the standard parameters in order to assure that they approximate the real risks. At the same time, legal protection insurers must retain their right to develop and employ USP.

This being said, it is evident that the huge mismatch between the standard formula and the actual risk has already had different effects: firstly, the calculation and the approval process of USP has taken enormous efforts and tied up substantial financial as well as human resources. Secondly, the established standard parameters have counteracted the principle of proportionality, particularly for small, single line business companies with limited risks which has had a clear influence on the industry's market structures whether unintended or even intentionally: Solvency II has forced the industry to restructure and specialised (single line) legal protection insurance companies are in danger of vanishing from the market.

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