The latest estimate for the date on which Solvency II will come into force for insurers across Europe is now January 1, 2016. The size of the task ahead is reflected by the fact that this date has been postponed several times since the directive’s adoption by the European Parliament and Council of the European Union in 2009, and by the fact that implementation is still some way ahead.

Solvency II imposes challenging requirements regarding assets. For insurers, it is thought that market risk accounts for around 60% of total basic Solvency Capital Requirement (SCR) across all risk types. Data on assets is distributed across many different managers, firms and data vendors, and collating reliably all of these disparate sources to generate a unified picture is an enormous challenge. Some firms still see delivery on Solvency II ‘Pillar II’ requirements (see page 2) as something they can achieve via evolution of existing risk management systems, however the reality is rather different. Both the scope and granularity of requirements are far beyond anything currently seen.

Current market conditions exacerbate the risk management challenge, as insurers are forced to look at less familiar investment routes to seek acceptable returns. A Chief Investment Officer (CIO) survey¹, conducted in May 2012 by GSAM Insurance Asset Management, shows that insurers are increasing allocations to high yield, bank loans and mezzanine debt, and also looking to increase allocations to asset classes such as real estate, emerging market debt and private equity. Movement into such investments will be enabled by reduced positions in cash and short-term instruments.

Across the globe, 26% of insurers expect to increase their overall investment risk. The same GSAM survey reveals that more than 80% of insurers around the world anticipate more investment in risk management, risk modelling and risk reporting, thanks to regulatory reform. Perhaps thanks to Solvency II, the EMEA figure was even higher, with 95% planning more risk system investment ‘to some extent’ and half planning ‘significantly more’. Solvency II includes the need to implement a highly demanding ‘look through treatment’, and this means understanding all underlying risks including those from pooled investment vehicles.

Introduction

The new regulatory regime is designed to put risk management at the heart of the insurance process. It will change the way all of the data used to calculate risk is collected, how risk is assessed and how the Solvency Capital Requirement (SCR) is determined and reported. Solvency II will integrate the European insurance market, harmonizing approaches and boosting competitiveness. Global regulation will improve thanks to a new benchmark for international regulatory regimes.

All insurers in Europe now face very significant new requirements, involving large volumes of highly complex data on liabilities and assets. Risk governance is moving out of individual business units, and becoming a company-wide activity. Solvency II means that more data will need to be sourced, processed, stored and disseminated to management and the regulator, and to higher levels of consistency and quality. Such ‘gold standard’ data management has moved beyond ‘nice to have’ and is now a regulatory necessity.

80% of Insurers reported gaps where required data were unavailable or where the quality and completeness were under question.

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1 ‘Seeking Return in an Adverse Environment’ – Insurance CIO Survey, Goldman Sachs Asset Management (GSAM), July 2012
The three ‘Pillars’ of Solvency II

The Solvency II directive has three ‘Pillars’: Pillar I (quantitative), Pillar II (supervisory and risk governance) and Pillar III (reporting). Together, these Pillars impose a very difficult set of requirements. Complying with all Solvency II provisions will involve a very substantial step up in terms of capability, thanks to the levels of complexity involved and the need to harmonize disparate data sources.

To give an example, the SCR mandated by Pillar I is based on aggregated results from six high-level risk modules: market risk; counterparty default risk; life underwriting risk; non-life underwriting risk; health underwriting risk; and intangible risk. In turn, every module has its own secondary modules for particular types of risk. For every module, asset and liability values are first projected forward before making a value-at-risk calculation and then assessing a capital allocation for a required survival probability of 99.5%. Module results are finally aggregated to allow calculation of a Basic SCR, and this is then refined to take account of an Operational Risk charge and the risk-absorbing consequences of deferred taxes and any Technical Provisions. Further complexity comes from the fact that many firms prefer to avoid using a ‘standard model’ for SCR calculation (which takes no account of a particular business’s circumstances) in favor of developing an internal model that imposes less conservative capital requirements.

To take another example, Own Risk and Solvency Assessment (ORSA) requirements in Pillar II go well beyond any conventional ‘reporting’ expectations that insurers might typically have. The 2011 QIS5 survey by EIOPA showed that 75% of firms surveyed were not yet in a position to deliver a comprehensive ORSA. An ORSA requires a very detailed and documented analysis of key areas such as overall business strategy, appetite for risk and consequent capital requirements – and it must relate back to the calculations in Pillar I. All of this must be summarized in a consistent format and must capture the solvency band risk implications of a firm’s entire business strategy. In fact, an ORSA should be seen as a fundamental business tool that is not only up to date at all times but which is also a foundation stone of future business strategy development.

75% of firms surveyed were not yet in a position to deliver a comprehensive ORSA

3 The three ‘Pillars’ of Solvency II

1 Quantitative

2 Supervisory and Risk Governance

3 Reporting

Forming a strategy

Effective data management is at the root of most Solvency II requirements. Until now, insurers have usually generated risk reporting internally, albeit while relying to some extent on externally provided data. Without modification, this internal-only strategy is looking less and less sustainable in the face of emerging Solvency II requirements. The UK FSA’s IMAP Thematic Review Findings explicitly identify data management as an area where firms still need to undertake significant work to achieve compliance.

Reporting and analysis requirements outlined in Solvency II are fundamentally more demanding than any existing reporting framework. Establishing and monitoring the provenance of key data, assigning ownership and implementing quality metrics remains a substantial challenge. The specialist skills required to implement such changes, from both actuaries and program managers, are also in short supply. In practice, this means that continued in-house development can often involve relying on external consultants and contractors.

There is a growing trend towards investment portfolio outsourcing, especially among smaller insurers, with a consequent proliferation in data. 80% of GSAM survey respondents said they outsource at least some of their investment portfolios, and firms with assets below $5 billion are likely to outsource virtually all investments. 17% percent of respondents are intending to increase their outsourcing in the near term. As outlined previously, these outsourced investments are likely to include less familiar asset classes – and larger firms are also more likely to outsource when considering non-core portfolio elements.

The 2011 QIS5 survey by EIOPA saw just 20% of firms reporting no areas where data was absent or substantially incomplete (relating to core Pillar II data such as valuations, asset reference and pricing and policyholder static). 80% reported gaps where required data was unavailable or where the quality and completeness were under question. Some data were usually managed using spreadsheets, requiring a full audit and application of governance policy.

Overall, firms responding to the EIOPA survey reported six different initiatives that were needed to deliver Pillar II requirements. These were initiatives on
data quality (validation); gap analysis (identification and mitigation); process (data governance); control (focusing on external source control); look-through (requirements on pooled fund valued position and security reference data); and infrastructure (data warehouse and workflow). Any data audits have to extend across all external providers and these include risk modelers, third-party fund managers, custodians and ex-EEA parent companies. 57% of EIOPA survey respondents said they had high or medium exposure to such third-party providers.

Good quality data is the starting point for a successful Solvency II process, and many insurers have responded by establishing dedicated teams whose remit is to focus on data quality and data governance. Compliance with Solvency II is an important outcome, but other benefits result. Even where companies already have good data management systems, more formalized control and ownership can lead to better understanding of business activities and outcomes.

### Real-world solutions

We are as yet quite some way off a ‘standard’ approach to handling Solvency II requirements. The sheer complexities are highlighted by the challenges involved in establishing a ‘look-through’ view: All of this should also be seen in the context of an environment where suitable development specialists are a scarce resource. Many of the data management and governance requirements already described are routinely addressed by asset managers working on the buy-side. Insurers will need to sustain efforts aimed at developing internal capabilities to import, process, analyze, store, retrieve and audit very large quantities of highly complex data, from many different sources. These are the core skills of RIMES Technologies Corporation.

RIMES has been meeting specialized data requirements across the buy-side since 1996, and is a pioneer provider of managed data services, using cloud-based technology to deliver highly customized financial data over the internet. RIMES serves over 240 Asset Management, Pension Fund and Custodian institutions in 36 countries. The RIMES proposition centers on delivering system-ready data management solutions that are fully compliant with the evolving regulatory landscape.

Three RIMES services are of particular relevance to insurers working on Solvency II. In combination with the development resources offered by RIMES, they offer the scope for the creation of a comprehensive solution within the insurance sector.

**RIMES Benchmark Data Service®**

RIMES BDS® This multiple award-winning service is a fully managed data service that provides bespoke benchmark data directly to in-house systems, meeting users’ needs across all business functions and addressing all regulatory criteria. RIMES BDS includes high quality data from over 100 data partners, giving complete scalability, and costs that are aligned with business success. New data sources can be added at very short notice. Used in conjunction with the RIMES Data Governance Service (DGS), it delivers a unified platform for good data processing and governance.

**RIMES Reference Data Service**

RIMES RDS®

RIMES BDS® is a single solution to the multiple challenges of building and managing a global repository of dynamic reference data. It collects, remediates, transforms, stores and distributes directly to client business processes. The operating platform has virtually unlimited storage potential, and close integration with existing workflow complements other RIMES managed services. Users can capitalize on existing sources of security and reference data across the entire business, with optimized sourcing, alignment of cost with business needs and reliable storage of growing reference data volumes without incremental investment in technology or people.

**RIMES Data Governance Service**

RIMES DGS®

RIMES DGS is designed to bring best practice management to everything from procurement – with control of all data purchase – through to provision of management information, with data that supports effective decision making. Usage is controlled, as well as decommissioning, and the service makes sure that data is used in line with compliance guidelines and restrictions. This service offers a robust platform for all regulatory compliance, giving a commanding view of data appropriateness, accuracy and completeness. It also improves index vendor management, showing who is accessing what data, where, how and why. As with RIMES BDS, the outsourced model allows tight cost management and good alignment of data acquisition and usage with business needs.

Find out more at [www.rimes.com](http://www.rimes.com)
About RIMES

RIMES Technologies Corporation was founded in 1996 in New York City specifically to meet the specialist data needs of the buy-side. The company was a pioneer provider of managed data services, using cloud-based technology to deliver highly customized financial data over the internet. Providing world-class data, supported by first-class service remains a prime focus of RIMES today.

The success of RIMES reflects a unique practical approach that combines the right technology with the best people. Our suite of services are designed, delivered, and supported by an expert team recruited from the heart of the industry. As a global company, RIMES serves over 200 institutions in 36 countries.

RIMES offers several solutions ranging from data processing to data governance. RIMES Benchmark Data Service® provides index and benchmark data in a format that is ready for use in third-party or proprietary client applications. RIMES Reference Data Service helps buy-side firms optimize data services to cut costs and boost efficiency. And RIMES Data Governance Service enables firms to monitor data use, tighten control and maintain compliance.

All our solutions are fully managed and deliver more than 500 data sources from over 100 data vendors in one single, fit-for-purpose feed. We currently feed data into more than 30 third-party data warehousing, risk, performance and compliance solutions, and many in-house systems. We enable buy-side firms to benefit from a world-class data operating platform without a major investment in people or technology. Firms that choose RIMES can achieve more with less.

RIMES has earned several industry awards over the years: the Inside Reference Data Award for Best EDM Initiative, the Banking & Finance Award for Innovation, the Best Product Implementation at a Buy-Side firm and Best Data Provider to the Buy-Side – the latter for the 7th consecutive year – at the Waters Buy-Side Technology Awards.