

SOLVENCY II IN 2 MINUTES

Fixing the flaws in the risk margin

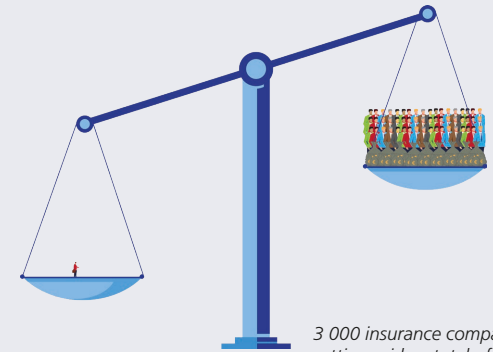
What is the issue?

The risk margin currently ties up around €190bn of EU insurers' capital, which is unnecessarily high and significantly reduces insurers' capacity to take on risks and to invest in the economy.

What is the risk margin?



The risk margin is an extra layer of capital insurers must hold on top of both the reserves that are needed to cover all expected claims and expenses and the solvency capital required to cover all risks.



Very few failures

3 000 insurance companies, setting aside a total of €190bn, while there are other buffers

It is a theoretical amount of additional capital meant to support the transfer of the insurer's liabilities in the very unlikely event of insolvency.

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The current risk margin is far too high



It reduces the risk-taking capacity of industry by **up to €190bn**



It can be another source of volatility



The risk margin should therefore be significantly reduced and redesigned

Strong justifications for lowering the risk margin



Cost of capital

Strong evidence exists that the theoretical parameter needed to calculate risk margin should be set at 3% instead of 6%.



Diversification

Many insurers have different types of business and their risks cannot all happen at the same time.



Risk changes over time

For example, a policyholder terminating a contract cannot terminate the same contract again.

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What are the consequences of a high risk margin?

For consumers

Lower benefits for pensions and other products

Less long-term investment

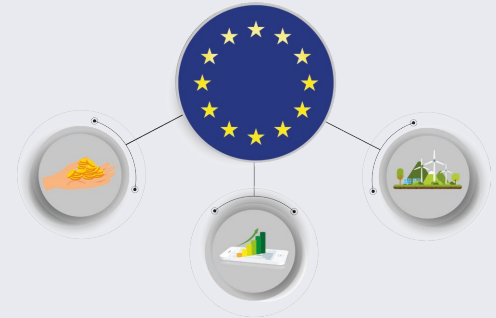
Higher premiums

Fewer products available

Unnecessary costs



For the economy



Reduces insurers' capacity to invest to support EU's recovery, growth and sustainability objectives

What could be the benefits of a lower risk margin?

Every €1 of lower risk margin could support:



€1.70 in equity investments

€3 if the capital charge for long-term equity is properly corrected



€6 investment in green bonds

€9 if the dynamic volatility adjustment is extended to the standard formula in combination with existing spread risk charges



€1 000 in windstorm protection

These estimates are based on a simplified model of an insurance company and standard formula

For more information, please see www.insuranceeurope.eu/solvency-ii