

Through the looking glass

What are the key impacts and challenges of 'look through' in Solvency II, asks Paolo Brignardello of Fundsquare

European insurance undertakings have been among the most important investors in the EU. This represents about 50 percent of the total assets under management in Europe and 54 percent of the European Gross Domestic Product.

Investors and policyholders are pressuring insurers to deliver attractive returns at the same time that regulators are pushing them to reduce their exposure. This, in turn, is putting pressure on asset managers, which, in the post-Solvency II world, will be under increasing scrutiny from their insurer clients, as they will want asset managers to maintain optimum allocation as conditions change.

What will asset managers do? Data management will be an integral part of the solvency capital requirements calculation and reporting.

one being in place to allow regulators to independently evaluate the insurer.

Industry consequences

A comprehensive look-through to gather the required information will lead to a lower capital charge being applied to an insurer under Solvency II. This has created new requirements for the provision of asset data in the form of new data fields, new data coding conventions, greater granularity of data and increased frequency of reporting.

Insurers will typically have no more than six weeks at each quarter-end to complete their Solvency II reporting and will usually be running some comparable form of Solvency II process at each month-end. There will be very short op-

communication flow, with the proliferation of formats, intermediaries and communication models. This will cause additional inefficiencies and costs on top of all the other burdens that Solvency II generates.

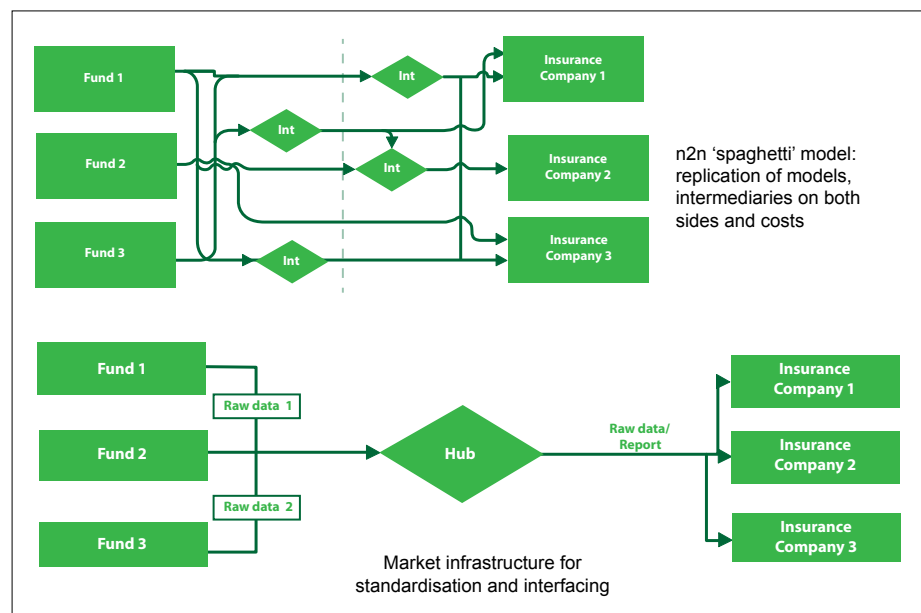
Solvency II states that 'external data', ie, data provided to the insurer by a third party, must also be held to these standards, so insurers will expect their data providers to assure them that these standards have been met.

To avoid potential issues, there is a need to be less reliable on intermediaries and in the long run aim to use a central hub that can centralise IT developments and data management. Such an industry model will guarantee efficient standardisation and cost mutualisation, while ensuring that insurers comply with regulatory requirements.

Funds in Europe also need to evolve their fund distribution models to make them more cost-effective and a strong, streamlined operating model will be key to success. This will allow for a single point for data dissemination, as well as shared operational services and harmonised and systematic controls.

From a conceptual standpoint, the reasons for a creating a central utility for look-through and reporting are self-evident. Nevertheless, centralising is easier said than done. Data dissemination and new standard implementations are a complex area and there issues remain that need to be settled before the industry can move on to mutualising efforts.

At Fundsquare, we are convinced that the only way forward is via a central hub. Based on our past experiences with data and information repositories, we believe these challenges can be met and a centralised hub is the way forward for the fund industry. **AST**



Market risk related to investments in funds will have to be assessed based on a 'look-through' approach, considering the risks related to each underlying asset.

The essence of Solvency II is to require insurers to provide transparency of their risk and the levels of capital held to cover that risk. All investments held by insurers fall under the market and default risk modules of Solvency II. A look-through methodology is required to measure market risk inherent in any fund.

Under Solvency II, European insurers and reinsurers must have multiple systems in place that are proportionate to the risks in their businesses. These include systems for governance, risk management, and information, with the last

erational windows for asset managers to ensure quality and deliver data to support these cycles.

The alternatives to the look-through approach are penalised in terms of capital charge. So, Solvency II will be applied at the level of each underlying asset line. Any quality default in delivering required information may cause delays in the solvency capital requirement calculation—even conflicts between the insurer and the supervisor.

Possible solutions

The risk for asset managers is the use of overlapping and divergent models that will add inefficiencies and costs to all of the other burdens that Solvency II generates. There could be a rise in a 'spaghetti' model, an n2n



Paolo Brignardello
Head of product management and marketing
Fundsquare