Assessing the impact of SAM on asset managers and service providers

Solvency Assessment and Management (SAM) is bringing Solvency II principles to South Africa. While most South African insurers are gearing up for compliance, few asset managers and service providers holding insurer mandates have assessed the potential impact of SAM on their business operations, let alone commenced with implementation activities.

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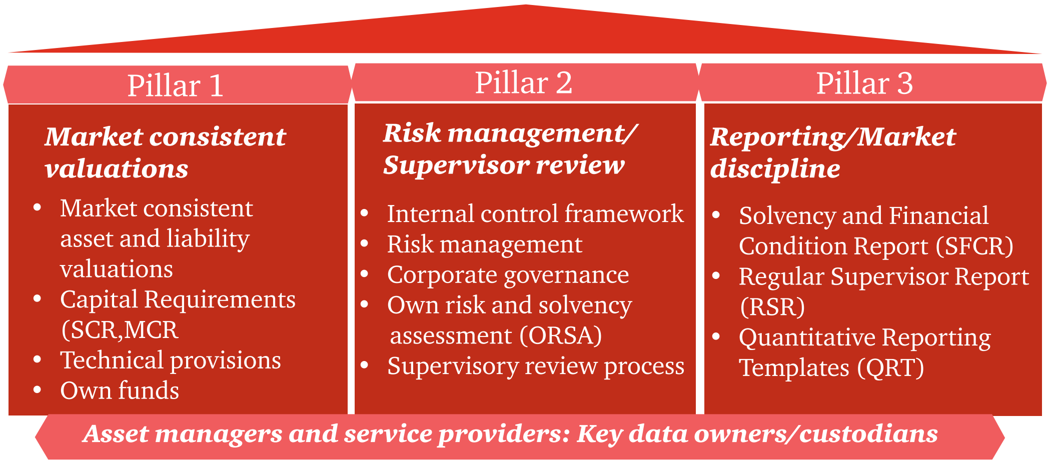
Setting the scene

SAM comprises a fundamental review of the prudential regulatory requirements for the South African reinsurance and insurance industry, and will establish a revised set of solvency capital requirements, risk management standards and disclosure requirements. The implementation of SAM is based on a 3-pillar approach, shown below:



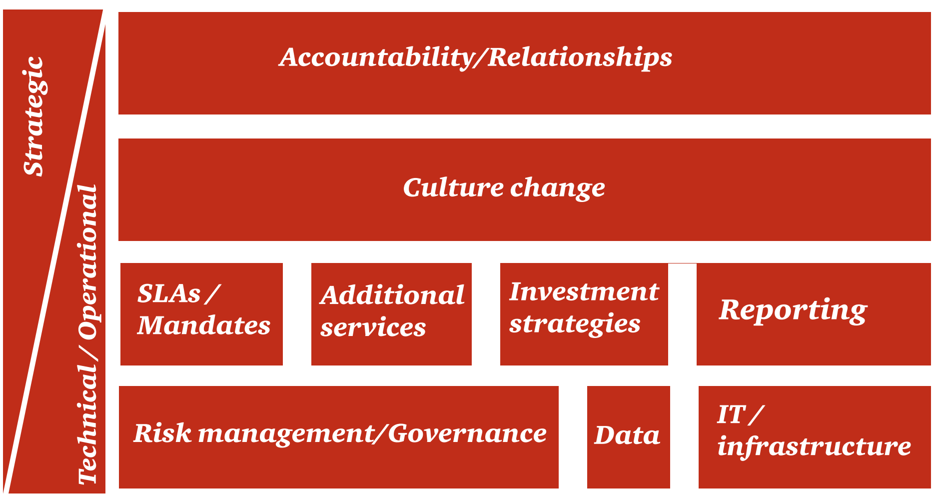
The Solvency Capital Requirement (SCR) is a risk responsive capital measure and consists of the following sub-risk modules: market risk, default risk, life underwriting, non-life underwriting, health underwriting, intangible assets risk and operational risk, of which market risk affects asset managers and other service providers the most.

An analysis of the first Quantitative Impact Study in South Africa shows that market risk as a percentage of the undiversified basic SCR comprises 70% for life businesses and 30% for non-life. The most significant components of the market risk sub-module are equity and interest rate risks.

Assessing the anticipated impact

SAM will have an impact on the entire value chain of insurers' activities including delegated asset management activities, custody and /or fund administration as well as middle office services.

As much as SAM will present significant technical challenges, it also presents strategic opportunities. The anticipated impact of SAM on the asset management industry can be depicted as follows and is explained below:



Asset data requirements:

- All assets are in scope for SAM.
- Asset data required in respect of SAM is twofold: firstly, for the SCR calculations and secondly, for reporting and disclosure requirements.
- The breadth and depth of the data required is at a level of granularity that is greater than that currently provided.
- There are potential differences between the proposed asset categorisation under SAM and other relevant standards, for example IFRS.
- A look-through principle applies to all assets and data therefore needs to be supplied at an individual instrument level.
- It is anticipated that the Financial Services Board (FSB) will allow for some simplifications in terms of using investment mandates or applying standardised shocks where no look-through information is available.
- SAM requires evidence that data is accurate, appropriate and complete – this will require a robust data governance framework and well defined controls.

Changed reporting timelines:

- New regulatory reports are relevant for all insurers and represent an increase in both qualitative and quantitative disclosure requirements.
- Timelines for quarterly and annual reports are reduced, resulting in a re-assessment of the reporting calendar.

Investment mandates:

- Anticipated capital requirements (or SCR) will provide an incentive for insurers to reduce concentration risk and volatility, and therefore insurers may choose to re-evaluate their investment strategies.
- This provides an opportunity for asset managers to assist insurers in achieving an appropriate balance between risk and return and to reduce balance sheet volatility.

Service level agreements (SLAs) with insurers:

- Existing SLAs will need to be revised due to the anticipated SAM reporting calendar and granularity of the data requirements.
- The process of providing assurance over the quality of data needs to be considered.

In conclusion

Asset managers and service providers will need to deliver more data, more frequently, within shorter time frames; and be able to demonstrate its quality.

The entire value chain of the insurer's activities should anticipate potential change to: products, mandates, systems, SLAs, processes and controls.

We believe that those asset managers and service providers that can develop SAM-ready offerings in terms of data, governance and investment services will benefit from a competitive advantage. Now, more than ever, asset managers and service providers need to consider how to respond to change and make the most of the opportunities triggered by SAM.

Where to begin

1. Increase your understanding of the proposed SAM regulatory environment and the relevant requirements, with specific focus on:
   - The granularity of asset data requirements;
   - The categorisation of assets under SAM; and
   - Data quality – what it means for your clients and how you will be able to demonstrate it.

2. Understand the gap between the status quo and the target state required under SAM. This will include an assessment of your internal operational processes to ensure that the SAM reporting timelines can be met.

3. Start to assess the impact on service level agreements.

If you wish to discuss how we can help you, speak to your regular PWC contact or, alternatively, contact any of the following people:

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