



Insurance Supervisory Authority 2014 Annual Report

Remarks by the President Salvatore Rossi



Rome, 23 June 2015



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Ladies and Gentlemen,

Welcome to another edition of our Annual Report, the third since the Authority was renamed IVASS.

In the course of my remarks I will be talking about the upcoming changes in the finance sector and the insurance industry, how preparations for the new Solvency 2 regime are progressing, and the state of health of Italy's insurance sector, and I will summarize the main activities undertaken by IVASS. I will not touch on relations between insurers, brokers and policyholders or on consumer protection as I will be addressing these two highly important questions when I speak before the Annual Meeting of the National Association of Insurance Companies (ANIA) on 2 July.

Insurance permeates virtually every aspect of our advanced societies. It is one of the oldest human activities.

In the US it plays a crucial role in the financial system, also because of the sheer size of the sector. One reason for this are the traditionally limited public welfare provisions in America.

The picture in Europe is different. In the euro area last year the total assets of the banking system were on average four and a half times those of the insurance industry; six times the amount in the UK. In Italy the gap is even wider with bank assets equal to 260 per cent of GDP against about 40 per cent for insurers, i.e. six and a half times as much. Even the volume of assets handled by portfolio managers and investment funds in Italy, to mention two other major categories of institutional investor, slightly exceeds that of insurance companies. Only pension funds, a notoriously small sector in Italy, handle less business, the equivalent of 5 per cent of GDP.

These figures suggest that the insurance industry has potential for growth both in Europe and in Italy, particularly when it comes to pensions and healthcare. Meanwhile, it is also facing global forces heralding profound change.

The world is changing, financial structures are changing – what about insurance?

Technological advances are affecting all aspects of finance. An assortment of new technologies, ‘fintech’ to use the recently coined term, has gained a foothold, calling into question past and present ways of conducting finance as well as financial intermediaries’ business models.

Most of the innovations concern banks and involve all three of their main activities: lending, payment services, and advisory services. The income these activities generate (from interest, fees and various charges) is in danger of drying up.

Lending, especially to households and small firms, is already available on peer-to-peer sites, where each borrower’s credit rating is established by algorithms that optimize big data available online for each applicant. This has automated the collection and evaluation of precisely the kind of *soft* information, i.e. those based on personal acquaintance, which were once the pride and *raison d’être* of mainly small banks and their staff.

Payment services are already evolving towards forms designed primarily for tablets and smartphones, where anyone can be a provider.

Even financial consulting services, to help private individuals manage their savings and firms make investment and strategy decisions, can be performed by robo-advisers, which are now beginning to make an appearance.

These are all nascent applications, which at present account for only a minuscule part of the world market, yet their potential to overturn the current system is enormous. And we are talking only of new uses of existing, sometimes longstanding, technologies. We have no idea how the market may be further revolutionized by others not yet invented or budding only in think tanks and laboratories.

So, the banks are in for a bumpy ride. But what about insurance companies?

At first glance they seem to be more sheltered from the winds of technological innovation, but this is not the case. In the insurance sector, as in the banking industry, the new digital ecosystem in which we are all immersed is endangering the traditional, labour-intensive ways of doing core business, treating it like a commodity whose production should be automated in the interests of efficiency and profitability.

The key factor, for insurance companies as well as for banks, is knowing your customer. And this familiarity, according to some, is easier to acquire in the digital world, with its social media, through automatic procedures rather than through human contact between staff members and customers. Thorough and reliable knowledge of the customer is indeed needed not only to compile a risk profile but also to design a personalized product that is more attractive in terms of quality, and not just price, and therefore more competitive.

Of course, in comparing banks and insurance companies we must look closely at their essentially different nature. Banks, for instance, have relationships with two separate categories of customers: on the liability side are those who utilize payment and liquidity or savings management services; on the asset side are those using credit services. Insurance companies deal with only one, albeit very broad and heterogeneous group of customers, i.e. policyholders. The services they seek range from protection against unfavorable events to long-term investment of savings. On the asset side, insurance companies are themselves long-term investors.

This basic difference between banking and insurance is being eroded, however, at least as far as selling savings products and investing in assets is concerned. Two completely separate forces are working in this direction and gradually converging.

On the one hand, banks are now finding it more difficult to lend in the traditional way, especially to small and medium-sized firms, because of the increase in average risk exposure, stricter capital requirements, and reduced income from interest.

On the other hand, insurance companies have seen the profit on their traditional investments (government securities, property) eaten away by a long economic crisis and the consequent monetary policy measures, which have brought interest rates down to their lowest ever levels. They have turned, cautiously but with growing interest, towards alternative investments, including debt, especially securitized debt. At the same time, life insurance is moving towards policies with lower guaranteed returns, or none at all, because fully guaranteed returns are now more costly for the company owing to low interest rates and the capital absorption required under the new rules.

The border between banking and insurance is about to grow dim, under the watchful, and on occasion concerned, gaze of regulators the world over. The insurance authorities, in particular, worry that insurers may not be properly equipped for the job of direct lender, which is certainly not part of their traditional remit. And all the while the sector is in the midst

of a regulatory revolution, with the adoption of the Solvency 2 regime in the EU and the growing global debate under way within the International Association of Insurance Supervisors (IAIS).

Solvency 2: not yet out of the woods

Solvency 2 comes into force at the beginning of next year. In accordance with the European Directive and related delegated acts, we are now gradually receiving 17 technical standards from the European Commission and 702 guidelines from the European Insurance and Occupational Pensions Authority (EIOPA). The numbers give some idea of the complexity of the new regulatory framework.

As one of the 11 countries that have already transposed the Solvency 2 Directive, Italy has made substantial amendments to its current Insurance Law. IVASS provided the Government and Parliament with technical assistance during the transposition and is in the process of reviewing much of the secondary legislation that is part of its mandate.

All of us, insurance companies and supervisory authorities alike, are working at full speed on the tools needed to calculate the new capital requirements for the different risk categories, the main novelty of Solvency 2; these include internal models, specific parameters, and standard formulas. This technically very complex task has to be completed in a matter of months.

Some aspects are still under discussion at international level. The main two are the prudential treatment of sovereign debt securities and the double accounting that companies will need to produce.

On 14 April, EIOPA issued an Opinion recommending that national supervisory authorities ensure sovereign exposures do not continue to figure as risk-free securities in the internal models of insurance companies. The Opinion was approved by a majority of EIOPA's Board of Supervisors, with IVASS and a number of other national authorities voting against it.

We voted against the Opinion not because we were inappropriately defending national interests but because we believed that the assumptions underlying it were not necessarily analytically correct. The value of the government securities of some euro-area countries became volatile at the time of the sovereign debt crisis mainly as a result of widespread fears of a euro break-up. The markets overestimated the likelihood of such an event; even the assessments of rating agencies tend to produce pro-cyclicality.

A similar discussion on banks is taking place within the European institutions, where the macroprudential risk of sudden massive sales of securities in order to avoid greater capital absorption is causing concern.

Nonetheless, we are aware of the problem surrounding the large share of assets that our companies have invested in Italian government bonds. Last March we asked them to consider sovereign risk in their own risk and solvency assessments (ORSA). We will evaluate any implications on a case by case basis, including in terms of capital ratios.

We now come to the accounting issues. Starting next year companies will have to produce two balance sheets: one for supervisory purposes based on the new Solvency 2 standards (including market consistency), the other prepared according to the current accounting principles. Remember that today the accounting balance sheets are already drawn up in two different ways. National standards are applied to the annual accounts, while the consolidated financial statements are instead subject to the principles set by the International Accounting Standards Board (IASB), known as the International Financial Reporting Standards (IFRS).

More information will be available to anyone looking at a company in order to understand its situation and performance – be they a supervisor, market analyst or director of the company. But this comes at the price of great complexity, possible confusion, and higher costs for entities.

We believe that too much complexity is in nobody's interest. We are therefore considering whether we should move over to the IFRS also for the annual accounts in the medium term. This would reduce the gap between supervisory balance sheets and accounting balance sheets, because the IFRS closely resemble the Solvency 2 standards. An agreement with the fiscal authorities and, above all, a new law are required, which will take some time. In the immediate future, parts of the accounting regulations need to be revised to eliminate any conflicts with Solvency 2. We are aiming to revise a series of our regulations by the end of 2015.

However, implementing Solvency 2 is not simply a question of capital requirements and accounting standards. It requires considerable adjustments to company governance and organization. In the first place, boards of directors must increase their interest in and their understanding of the risk profiles inherent in company activities. This does not mean that boards should only comprise technical experts or that market strategies need not be discussed – for insurance companies, understanding risk is the basis for any informed strategic decision and, to a large extent, it is their business.

The entire way that businesses are organized must change in order to introduce the new approach to risk assessment, which should neither be reduced to a cosmetic exercise for supervisory purposes, nor relegated to the office of the chief risk officer. The evidence gathered so far from inspections and the initial ORSA findings are not entirely comforting, especially as regards smallest firms. We know that the transition will not be easy, but we are ready to work together with the companies, each assuming our own responsibility, to facilitate change.

The state of health of the Italian insurance sector

Premium income and investment. – Last year Italian insurance companies fared considerably better than the European average, with premium income of almost €150 billion, 20 per cent more than in 2013, a year in which revenue had already grown; it represents almost 9 per cent of GDP. The 2011-2012 crisis is behind us. Nevertheless the increase is entirely in the life insurance sector, while non-life policies, particularly motor vehicle third-party cover, continue to decline.

What can we expect for this year? In the life insurance business, the data for the first four months of 2015 indicate stagnation for traditional policies but a doubling of unit-linked insurance policies compared with a year earlier; these policies are financial products that tend to place the burden of risk on the insured party.

In the non-motor vehicle non-life sector, Italians' chronic under-insurance shows no signs of abating. In 2014 premiums amounting to just 1 per cent of GDP were paid, much less than half those paid in France and Germany. We are seeing worrying phenomena, such as the withdrawal of national insurers from the medical malpractice segment, associated with greater recourse either to self-insurance or to products sold by operators with the legal form of companies from other EU countries, but which are actually managed from Italy, and sometimes not very reliable.

These are risks of great social consequence, thus the use of market instruments to cover them should be encouraged. We have recently begun a fact-finding inquiry, the preliminary results of which confirm the existence of problems on both the demand and supply side. On the inquiry's conclusion we plan to provide the market and the institutions involved with some suggestions as to solutions, possibly also as regards legislation.

Investment by insurance companies also increased in 2014, reaching €630 billion overall at the end of the year, almost 12 per cent higher than a year earlier.

Companies are trying to rebalance the composition of their portfolios, which compared with the rest of Europe appear to lean too far towards government bonds. This is to reduce concentration risk but also to achieve higher returns.

One opportunity that has not yet been seized, but is contemplated by law, is that of contributing to the funding of productive enterprises also by investing in mini-bonds and in securitized bank loans, or by granting loans directly. The potential investment in these forms runs to more than €60 billion, excluding via investment funds.

Last year, IVASS promptly issued the secondary legislation required under the Competitiveness Decree (Decree Law 91/2014 converted into Law 116/2014), deeming it compatible with the prudential framework and indeed opportune in terms of the gradual diversification of assets. If the opportunities created by the new rules have not been taken up, it means that suitable products were not offered to the companies, or that prudence prevailed with companies unwilling to venture into uncharted territory. We should ask ourselves what can be done to expand the offer of financial services in our economy, while safeguarding the sound and prudent management of insurance companies.

Profitability and capital. – The 2010-2011 crisis brought the accumulated losses of Italian companies to about €4.4 billion. In the following three years there was a return to profit in the order of €5-6 billion a year. All the business segments have contributed to this positive result. The overall ROE for the Italian insurance industry rose to 9.3 per cent (from 8.2 per cent in 2013), in line with the European average.

The average solvency ratio of Italian companies, calculated according to the Solvency 1 rules, was almost twice the minimum requirement at the end of last year. But what will it look like under Solvency 2? It is too soon to say, as we are still in the midst of preparing the measurement tools. However, from the first supervisory reports coherent with Solvency 2, at 31 December 2014 the signs were reassuring overall: for the entire system, eligible own funds amounted to more than twice the solvency capital requirement (SCR), calculated using the standard formula; companies that require capital increases, according to these data, account for 3 per cent of the market in terms of premium income.

Some interesting comparative indications came from the stress tests conducted last year by EIOPA on a representative sample of the European market, based on end-2013 data.

Besides the general level of readiness for the new regime, the exercise verified the capital adequacy of individual companies calculated under the Solvency 2 rules in stress scenarios: a major financial shock, such as an increase in spreads on government securities, and a sudden worsening of the risk factors specific to the insurance industry (the core scenario); the persistence of low rates of interest (the low yield or 'Japanese' scenario).

As is widely known, given the preliminary and highly uncertain nature of the estimates, EIOPA decided not to publish the results for individual companies, but only at national level. As we reported at the time on our website, the Italian insurance sector was found to be better capitalized overall than the European average both in the absence of stress and in the Japanese scenario; it fared slightly worse only under the hypothesis of an increase in spreads.

In the meantime, the Japanese stress scenario has now almost become a reality. This poses problems in particular to life insurance companies by reducing the spread between the yields obtained and the financial guarantees promised to the holders of traditional policies. In Italy, the margin according to EIOPA data was still positive at 55 basis points; in Germany, on the other hand, it was negative (-43 points), and more so in France (-56 points). Further aggravating the situation of Germany and France's insurance sectors was another differential: that between the financial duration of assets and liabilities, which was close to 11 and 5 years respectively in the two countries. In Italy, this second differential was almost nil, in part due to the regulatory framework that was attentive to this risk already under the previous Solvency 1 regime.

Nevertheless persistently low returns are conditioning the choices of companies in Italy as well. They are moving away from traditional life insurance policies, which guarantee a minimum return, towards products with no guarantee, which do not affect their income statement and also absorb less capital.

In this way, we are moving away from the true nature and mission of insurance companies, that of transferring and mutualizing the risks of individuals, protecting their savings and reducing uncertainty about the future. Two and a half centuries ago, Adam Smith wrote that 'The trade of insurance gives great security to the fortunes of private people, and by dividing among a great many that loss which would ruin an individual, makes it fall light and easy upon the whole society'.¹

¹ A. Smith, *The Wealth of Nations*, Part IV Chapter 1, Part III.

We cannot blame those who make rational choices in the interests of a company's accounts. And yet we cannot but cogitate on trends that could ultimately deprive our society of a highly valuable service: the investment of savings for the purposes of insurance and social security. I think that we should all – government offices, IVASS, businesses and consumers – explore new ways of achieving this objective.

Insurance and social security

I would like to dwell briefly on the connection between insurance and social security, an issue of steadily increasing importance, especially in Italy.

Social security provides pensions to the retirees. 'Provides' derives from the Latin *providere*, meaning 'to foresee', to see in advance what will happen in the future. Insurance means 'securing' what is by nature not secure, because it is uncertain. And nothing is more uncertain than a future event. This simple etymological parallel demonstrates the intimate connection between modern pension systems and insurance systems.

Of the two concepts, insurance is the older and the more general. Very long ago, the adverse events against which one could insure oneself comprised not only harvest failure and shipwreck but also the premature end of life and the consequent difficulties of survivors, and even the fact that at some point advancing age itself deprives one of the ability to work and produce income. In the course of the nineteenth century a collective consciousness arose ensuring that a minimum of social security, in particular in the form of pensions, was a public responsibility. Public pensions came into being in Europe and the United States. In Italy, the pension system reached its maximum advantage for retired employees during the 1970s both in the size of pensions (not calculated on the basis of contributions paid in) and in age at retirement. Even under normal demographic conditions this was clearly an unsustainable system.

As we know, since then successive reforms – making pension benefits commensurate with the contributions paid in by workers over the course of their career, raising the retirement age and linking it with life expectancy – have shaped a public pension system that weighs less heavily on the active labour force and on taxpayers in general. Italy now has a pension system that international organizations judge to be one of the world's most advanced in terms of public finance equilibrium. On the other side of the coin, younger generations can no longer rely on the public system, alone, to offer them a standard of living in retirement that approximates what they had during their working lives.

Private finance should compensate for the necessary withdrawal of public pension systems from levels of protection that were financially unsustainable. Private finance comprises retirement products strictly speaking – pension funds, distinguished according to whether or not they offer defined benefits. In addition there are insurance products whose purposes are broadly retirement-related: with-profit life policies, unit-linked policies, individual retirement plans, and ‘open’ pension funds.

A protracted period of low interest rates makes the guarantee of defined benefits problematical, both for pension funds and for insurance companies.

Yet regardless of how interest rates move in the future, a larger contribution on the part of the insurance industry to retirement provisions can only be to the advantage of the public pension system. Insurers have always been well equipped to provide demographic/financial guarantees. IVASS monitors both the level of the guarantees and the adequacy of the reserves built up against them, hence long-term sustainability also as a function of the coverage assets. At the same time, at least in continental Europe, pension systems have historically been conceived as containing some element of guarantee, albeit primarily public in nature. It seems to me that the conditions now obtain for strengthening, on the supply side, the intimate connection between pensions and the insurance industry that I mentioned earlier.

In the medium to long term, mutuality among generations of workers and of investors of savings, realized through insurance-retirement asset management, can reconcile the various needs of security, economy, market compatibility and the solvency of intermediaries.

A related consideration concerns insurance against the loss of self-sufficiency in old age. This is a phenomenon logically and psychologically connected with retirement and pensions that is becoming more common as life expectancy lengthens, and one that the public health service has difficulty coping with. This is creating a substantial potential market for private insurers.

Tax incentives for this kind of insurance are to the Treasury’s advantage insofar as they prompt the conclusion of contracts that would otherwise not be made, while also offering savings in budget expenditure. Employer and labour organizations and insurance companies should all get involved, the former by extending collective bargaining on retirement matters to these specific instruments and the latter by making supply conditions more attractive with a view to a rapidly growing market.

It is essential that younger generations fully realize that they will have to save more than their parents did and invest their savings with a view to retirement.

There is great responsibility for all concerned: for policymakers and politicians, who must actively promote such awareness; for those with administrative, regulatory and supervisory functions, who must oversee market operators that offer retirement-related financial products and work so that they are stable, efficient, transparent and correct; and last but not least for insurance companies, which must creatively adapt products and marketing practices to the needs of the customers whose future they are managing.

The 'case' of motor vehicle liability insurance

We now come to motor vehicle compulsory liability insurance. That this is truly a special case is notorious. For many years motor insurance premiums in Italy have been among the highest in Europe. A variety of factors are at work here, one of which is the abnormal rate of insurance fraud perpetrated by a not inconsiderable and aggressive minority of policyholders.

This Authority, since it was reconstituted as IVASS, immediately realized that it was not only its institutional duty but also an intriguing intellectual challenge to offer an effective technical contribution to the solution of this intricate, festering problem. We have allocated many resources to it and will continue to do so, working together with the Government and Parliament and engaging in constructive dialogue with other authorities, with trade associations and with consumer organizations.

Market data show that the first signs of improvement in 2013 were followed last year by considerable further progress, little short of an outright turnaround.

According to our IPER survey of *actual* motor vehicle liability policy costs (not companies' formal list prices, which are somewhat misleading) the average policy price fell by nearly 8 per cent in 2014, continuing the previous year's downward trend. Just as a working hypothesis, if this trend continues at the same pace and prices in the other countries hold at their 2012 levels, the gap between average premiums in Italy and in the rest of Europe will be closed by 2020. This simple exercise in arithmetic shows the extent of the initial divergence but also suggests how close to a solution the problem is.

Why, one wonders, are policy prices coming down? First of all, because the number of accidents and the cost of indemnity are diminishing. The accident rate – the ratio of claims to the number of vehicles on the roads – declined further last year to 6 per cent, owing in part to the recession; in 2011 it was 7.4 per cent. The average cost of compensation decreased by 1.5 per cent in 2014. The most impressive decline has been that in minor personal injury claims, which fell by 17 per cent and are now a third of what they were in 2011.

Moreover, gains have also been made in two problem areas that we mentioned last year, namely competition and product diversification.

The concentration of the market, as measured by the Herfindahl-Hirschman index, was reduced by 15 per cent compared with 2013. Policyholder mobility between companies has increased, exerting significant downward pressure on prices. One policyholder out of six changed insurer last year, obtaining an average price reduction of 22 per cent on their old policy; those who stuck with the same company also benefited from price reductions, but only of 5 per cent. About one contract in ten now provides for ‘settlement in the form of repairs’ (in cases of claims for which the policyholder is not liable, the vehicle is repaired at a workshop designated by the insurer) or for the installation of a ‘black box’ (an electronic device that records the essential data on the utilization of the vehicle).

We shall continue our work to create conditions that can further these tendencies. We recently reviewed the functioning of the direct indemnity system and its fixed compensation amounts, introducing mechanisms to stimulate competition.

In the crucial area of combating insurance fraud, we have completed the first phase in the construction of the Integrated Antifraud Database (IAD), which we described in last year’s report. However, effective anti-fraud action means more than the intelligible collation of the wealth of data available, as we are trying to do with IAD. Insurance companies, for their part, need to be technologically equipped first to feed in the relevant data and then to exploit the information effectively. Our inspections have found that this is not always the case: the companies that are lagging behind in adapting their information technology to this purpose need to get up to speed as soon as possible.

The ‘competition’ bill now before Parliament sets a series of reasonable objectives relating to motor vehicle liability insurance: enhancing the transparency and comparability of the policies that insurers offer, containing system costs, and countering insurance fraud. This is an opportunity to resolve the problem once and for all. In the hope that legislators will enact a

sufficiently innovative text, ignoring vested interests that run counter to the public interest, we stand ready to provide our technical contribution to the Parliament.

IVASS in 2014

What did IVASS do last year? It is hard to sum up the activity of an institution such as ours in a few lines. To do so using only quantitative indicators can be misleading, because quantitative measures do not take full account of quality. However, purely by way of example, let me give you a few numbers.

In 2014 we conducted 34 prudential supervision and anti-money laundering inspections, taking 3,700 person-days, and 46 on-site visits to the undertakings that were preparing the risk evaluation models envisaged by Solvency 2, taking 800 working days. We processed just under 800 reports of problematic cases involving insurance intermediaries (agents and brokers) and managed 120 appeals against our decisions. I will return later to our activities in the area of sanctions and winding-up procedures. We responded to some 26,000 claims relating to consumer protection and logged 43,000 calls to our call center. The Joint Directorate, which deliberates on matters of external relevance, met on 26 occasions and examined about 200 items.

The work of the Authority intensified in part owing to the adoption of new methods, in some cases replacing obsolete ones, such as those governing the internal audit, in others introduced for the first time, such as the Inspection Guide (completed) and the Off-site Supervision Manual (forthcoming). The Bank of Italy's experience and best practices provided further guidance, in the spirit of the law that established IVASS.

One noteworthy practice imported from the Bank consists, for example, in interacting directly with the boards of directors of the supervised companies. For the time being this has mostly coincided with the delivery of the inspection reports but in the future Solvency 2 will require it at all stages.

We have accorded a prominent place in our supervisory activities to the delivery of the inspection reports, as a good opportunity for assessing the general situation of insurance undertakings. We do not stop at signalling failures of compliance with the rules: we bring to the attention of management the organizational inefficiencies identified and, based on detailed technical analyses, indicate the areas where management and internal controls need strengthening. The inspected companies themselves have had occasion to

gauge the usefulness of the findings and recommendations made by the inspectors.

More generally, we are rethinking our supervisory practices. We sense the need for an 'adult' relationship with the undertakings, based on a shared approach to risk assessment. Solvency 2 implies as much: it provides a metric for risk assessment based on economic criteria and therefore a common language in which to communicate. It does not settle for a mere compliance approach.

We would like to be able to devote more resources to the component of supervision that is most socially useful, i.e. the one aimed at problem prevention. The main tools for this are on-site inspections and data analyses. Many of our best resources are, however, absorbed by 'punitive' supervision: sanctions and winding-up procedures. This situation is imposed on us by decidedly outmoded legislation; up to a short while ago, internal practices that we are now changing were also contributory factors.

The law obliges us to sanction even minor infringements but for all of them, including the most serious, it only sets pecuniary sanctions for undertakings and not for individual directors or managers, what is more for amounts (€23 million for the system in 2014 or 0.02% of premiums) that the sanctioned firms have little difficulty absorbing in their company accounts, at most shifting them onto prices. Save for loss of reputation, the deterrent effect is very modest. Every year the Bank of Italy handles 100 sanction procedures against banks, involving 900 individuals, while IVASS handles 3,000 procedures against insurance companies. The difference is striking: IVASS works very hard but obtains little.

The compulsory liquidations of insurers also suffer from laws that produce paradoxical results: at the time of writing there are still 58 open procedures, 14 of which were begun over 30 years ago! It is one of those Italian anomalies that is always very difficult to explain to foreign observers. We are taking steps to improve and speed up the management of these procedures whenever it is in our power to do so: we have written guidelines for the appointment of crisis management bodies and a code of ethics to which these bodies must adhere; we have amended our regulations to make liquidators more independent, for the ultimate purpose of shortening the length of procedures; we have replaced 25 liquidators, several of whom are over 75 years of age, and 60 members of supervision committees, around half of the total; we are conducting trials of alternative settlements or agreements to close out ongoing procedures more rapidly. Last year 15 procedures were closed or entered their final stages and 8 more are expected to be concluded this year. By 2016 more than half of those started two years ago will be closed.

The work that began two and a half years ago to modernize IVASS is proceeding. We operate with an absolute cap on the number of staff members established by law and we pay very close attention to costs: last year we again made a small budget saving. It is worth bearing in mind that the Institute's operating expenses do not weigh on the government budget but on that of the supervised entities. Moreover, the bulk of the fines imposed go to the national guarantee fund for road accident victims (*Fondo di garanzia per le vittime della strada*) managed by Consap, and the remainder directly to the Treasury.

There is urgent need to update IT systems, also ahead of the introduction of Solvency 2. Last year IVASS signed an agreement with the Bank of Italy for the use of its IT infrastructures and services: we will ask the Bank to help design an advanced system for managing operational risk. We are also working hard to implement in IVASS the anti-corruption and pro-transparency rules recently introduced into Italian law.

Among the general objectives we have set for the future, I would like to mention simplification and proportionality.

IVASS produces a very large volume of secondary legislation (regulations to implement laws). Aware that needlessly complicated and obscure laws are among the chief ills afflicting Italy, we wish to make our own modest contribution, insofar as it is within our power to do so, by drawing up straightforward and clear rules.

A few months ago we adopted the first measures to simplify procedures and contractual obligations between insurance undertakings, intermediaries and customers. We will not stop there: after consulting with the parties involved we will radically revise the information that must be submitted to consumers of non-life insurance products, anticipating future European initiatives.

But it is in the implementation of Solvency 2 that we aim to take a decisive step towards simplification. We are about to revise or issue around 30 regulations, an opportunity not to be missed. To avoid the classic risk of making a mountain out of a molehill, we need the cooperation of all the market players to help us understand where superfluous complexities lie.

Proportionality must be the second watchword: this means tempering the strength and burden of supervisory activities in proportion to the potential danger of the situation at hand.

The law entrusts us with the ultimate goal of safeguarding those who are insured and those who are entitled to insurance services, specifying that this must be obtained by pursuing three intermediate objectives: monitoring

first and foremost the sound and prudent management of firms, then their transparency and fairness with respect to customers, and finally systemic stability. These objectives must be pursued in synergy, not in opposition to each other: effective proportionality can do just that.

Up until now it was believed that supervision should basically be proportional to firm size. Solvency 2 instead calls on us to pay attention to the nature, breadth and complexity of the risks run by firms, which may or may not be related to size. Several other aspects must be given consideration: business sector, management and organizational aspects, and the operating context. It will be crucial to define criteria *ex ante*, several of which will come under community law while others can be set by individual countries. We are working towards this goal with the insurance industry; it will require time, implementing experience and a large dose of interpretative flexibility.

But we must be clear on one point: proportionality can never mean the non-application of laws. The Solvency 2 framework is based on principles, proportionality influences the ways in which the supervisory objectives are pursued but in no case does it render these objectives irrelevant.

Conclusions

A highly-evolved, modern and forward-looking insurance system is vital to Italy's economy. The importance of its role transcends its weight in terms of mere value added because insurance undertakings – along with the rest of the financial framework apparatus – are part of the broader economic circulatory system.

The construction site for structural reforms in Italy is vast. Now that we are emerging from the double-dip recession that had pushed our economy backwards for seven long years, let us try to pave the way for sustainable and lasting development. Every aspect of the economy and society must be considered anew. Many comforting certainties from the past can no longer guide our action. Small and large positional rents will in any event be swept aside by new technology, which is already here.

Financial reform is an integral part of that construction site. We know that in the years to come banks will evolve as will their role in funding the real economy. Insurance firms will change too, driven by innovation and the evolving needs of the market and also by the new regulatory environment.

In adhering to the mandate conferred on it by law, IVASS is determined to help steer all these changes in favour of the insured and of those who benefit from insurance services, and ultimately in favour of Italy's economy.

IVASS can rely on a lean structure with many highly-skilled professionals. At this time of complex transition in the insurance world, the Authority's staff are demonstrating a spirit of sacrifice that we can be proud of. Also on behalf of the Governor and the members of the Directorate of the Bank of Italy, as well of IVASS Directors Riccardo Cesari and Alberto Corinti and the Secretary-General Corrado Baldinelli, I extend my heartfelt thanks to all the staff at IVASS for their precious contribution.

Hard work, a sense of duty and carefully cultivated professionalism, together with openness to change, are the distinctive hallmarks of those institutions but also of those countries that do not fear progress because they pursue it every day.

Thank you for your attention.

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