POLISH FINANCIAL SUPERVISION AUTHORITY

Chairman
Andrzej Jakubiak

Warsaw, 3 December 2014

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Insurance companies
Reinsurance companies

Dear Sirs/Mesdames:

The regulatory authority, in a manner similar to that applied in respect of recommendations issued in the previous years regarding the payment of dividends from profits generated in the relevant year, recommends that insurance/reinsurance companies continue to apply a conservative dividend policy and allocate any profit they may have earned to enhance their capital standing. In the opinion of the regulatory authority, the conduct of a conservative dividend policy by insurance/reinsurance companies has had positive effects, in particular in the form of maintaining solvency ratios at relatively high levels, and thus developing adequate capital buffers.

The year 2014 was a period in which elevated levels of risk were observed in the external environment of the Polish economy, in particular resulting from a complex political and economic situation in the eastern part of Europe, increasing uncertainty about the future development of the economic situation in Poland. Furthermore, of great significance is the observed practice in the insurance area consisting of judicial decisions in respect of the payment of compensation, spare parts, replacement vehicles and applied withdrawal fees in unit-linked insurance which may adversely affect the financial standing of insurance/reinsurance companies. The significance of reputational risk of insurance companies keeps increasing gradually and the challenge remains to build insurance based on relational culture, i.e. good relations with clients that pay off in the long term thanks to their increased loyalty and trust.

Moreover, overlapping with the above picture of the environment surrounding insurance/reinsurance companies is the entry into force, on 1 January 2016, of new regulations of the Solvency II Directive which will imply new solvency requirements. The quantitative impact study (QIS) conducted again in 2014 for the insurance sector enabled both insurance/reinsurance companies and the regulatory authority to develop a more accurate recognition of capital needs associated with the new solvency regime.

Accordingly, bearing in mind the need to protect the interests of policyholders, insureds, beneficiaries and persons entitled under insurance agreements, it is recommended that the capital security of the insurance sector continue to be strengthened. At the same time, one factor that should not be lost from sight is the unfavorable effects of potential catastrophic events for which insurance/reinsurance companies should be adequately prepared by having appropriate capital buffers in place.

In light of the foregoing, the regulatory authority, similarly to the recommendations for the payment of dividends from profits generated in 2013 distributed among insurance/reinsurance companies by letter dated 11 December 2013, bearing in mind the length of time required for the planning of

assumptions for the financial plans for 2015 by insurance/reinsurance companies, has found it appropriate to issue a recommendation on the payment of dividends from profits generated in 2014. Therefore, the regulatory authority recommends that insurance/reinsurance companies continue their conduct of a conservative dividend policy using the generated profit to enhance their capital standing.

It is recommended that dividends be paid only by those insurance/reinsurance companies that meet all of the following criteria:

I. they received a good (1.00) or satisfactory (2.00) BION risk score for 2013;
II. in 2014, they reported no shortage of shareholder funds to cover the solvency margin or guarantee capital and no shortage of assets to cover technical provisions (in monthly or quarterly periods);
III. in 2014, they were not covered by a remedial plan or program of the kind referred to in Article 187 Sections 1-3 and 8 of the Insurance Activity Act;
IV. their capital requirements coverage ratio (understood as the lower of the ratio of shareholder funds to solvency margin and the ratio of shareholder funds to guarantee capital) as at 31 December 2014 was at least 160% in the case of life insurance companies or 200% in the case of non-life insurance companies;
V. their stress tests conducted as at 31 December 2014 for all tested risk types indicated the capital requirements coverage ratio of at least 110% and the ratio of coverage of technical provisions with pertinent assets of at least 100%;
VI. in the quantitative impact study (QIS) conducted as at 31 December 2013, they showed eligible own funds amounting to at least the minimum capital requirement and the solvency capital requirement.

Those insurance/reinsurance companies that satisfy the above criteria should limit their dividend payments to a maximum of 75% of the profit earned in 2014, while the capital requirements coverage ratio after the dividend payment should be maintained at no less than 110%.

At the same time, it is permitted to pay a dividend from the entire profit earned in 2014 (which means that it is not permitted to pay a dividend from profits earned in previous years), provided that after the payment of the dividend the capital requirements coverage will be maintained at a level higher than that specified in criterion IV and criterion V will be met, taking into consideration the status as at 31 December 2014 adjusted for the amount of the dividend.

Those insurance/reinsurance companies that satisfy the above criteria, when deciding on the level of dividends should take into account their additional capital needs within the period of twelve months from the approval date of the financial statements for 2014, which could result, among others, from an increase in costs caused by changes in the market and legal environment as well as capital needs arising from the need to prepare for the requirements of Solvency II.

Respectfully yours,

Andrzej Jakubiak

Chairman of the Polish Financial Supervision Authority