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CONFERENCIA

¿POR QUÉ ES NECESARIA UNA REGULACIÓN COMO SOLVENCIA II?

a cargo de la SRA. JUDITH PUJOL, socia FAAS EY.

Barcelona, 30 de abril de 2020

¿Porque es necesaria una regulacíon como SII?

Judith Pujol

30 de abril de 2020

La regulación en el sector asegurador

Todos hemos sido testigos de un incremento exponencial de la regulación en el sector financiero en la última década.

En concreto en materia de seguros:

- ❑ Directiva 2009/138/CE del Parlamento Europeo publicada el 25 de noviembre de 2009,;
- ❑ Posteriormente desarrollada por el Reglamento Delegado (UE) 2015/35 de la Comisión Europea,

Solvencia II obliga desde el 31 de diciembre de 2016 a medir la solvencia de las entidades de seguros en base a los riesgos asumidos, haciendo públicos sus resultados, y siendo estos sometidos a procesos de auditoria (con diferente alcance depende de las jurisdicciones)

¿Por qué una regulación Global?

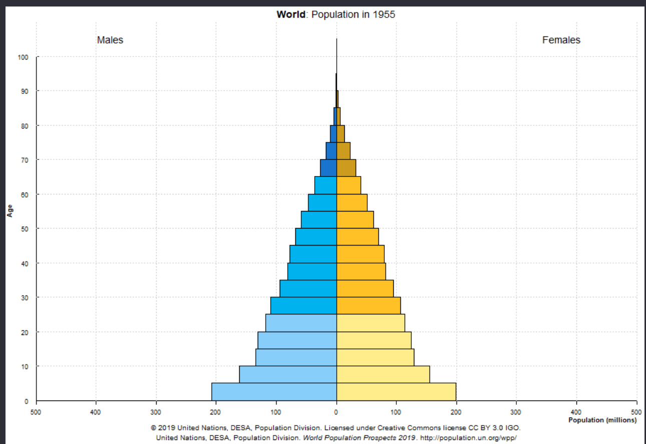
Al inicio del SXX la población mundial era de un total de 1.650m de personas.

A mitad del SXX, la cifra había crecido un 70%,

En el año 2000 la población mundia había crecido 4.420m, es decir un 267% alcanzando 6.070m de personas.

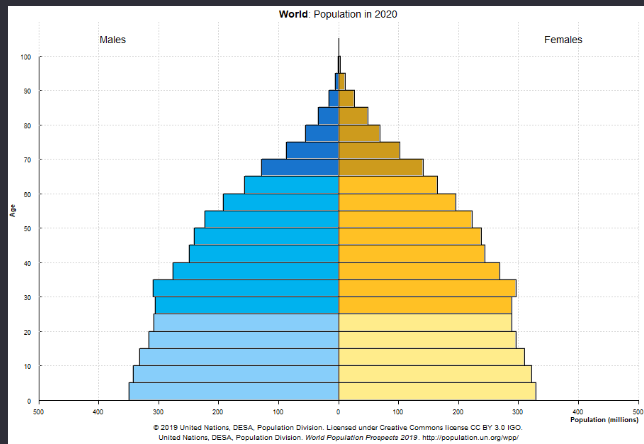
Año 1950

Población mundial: 2.773m de personas



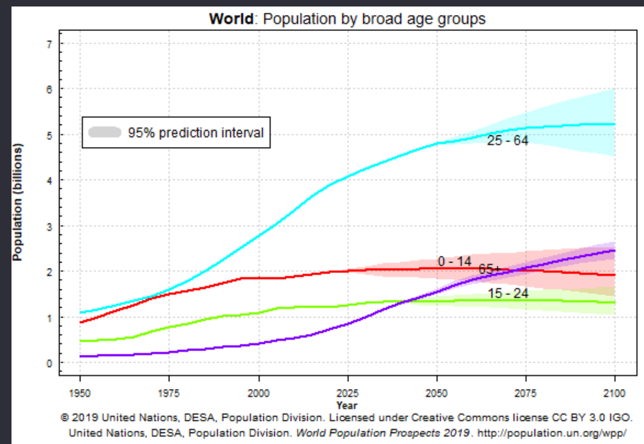
Año 2019

Población mundial: 7. 713m de personas



Proyección 2100

Población mundial: 10.875m de personas



Source UN
Population division
Departament of
Economic adn social
affairs

Los tratados de Roma, la prehistoria de Solvencia II

El 25 de marzo de 1957, 6 países europeos deciden firmar el Tratado de Roma constituyendo la Comunidad Económica Europea, con el objetivo y esperanza de que el incremento de interdependencia económica entre países del territorio europeo minimizará los conflictos bélicos y por tanto asegurará la estabilidad y el crecimiento de los territorios.

Firmantes del Tratado de Roma:

- Francia
- Alemania Occidental
- Bélgica
- Italia
- Luxemburgo
- Paises Bajos

EY

La union europea en la actualidad

La Unión Europea:

446m de personas

27 países

Paises candidatos:
Turquia
Bosnia
Serbia
Macedonia del Norte
Albania
Kosovo y Montenegro)

¿EIOPA ….DGSFP?

EIOPA, European Insurance and Occupational Pensions Authority - **Autoridad Europea de Seguros y Pensiones de Jubilación**)es una institución de la Unión Europea que,, reemplazó al Comité de Supervisores Europeos de Seguros y Planes de Pensiones (CEIOPS, Committee of European Insurance and Occupational Pensions Supervisors).

El sector financiero y la primera década del SXXI

2002-2006
Burbuja inmobiliaria alentada por el auje de las nuevas tecnoloigas

Prestamos concedidos a personas con un alto perfil de riesgo

2006
Los tipos de interés de la FED alcanzan el 5,75% (tres años antes eran del 2%)

15 de Septiembre 2008
Quiebra de Lehman Brothers

El Informe Laròsiere

A finales del año 2008, la Comisión Europea encargó a un grupo de expertos financieros y economistas, que estudiará el marco regulatorio y supervisor que existía en ese momento en la Unión Europea y que derivado de ese estudio, dictará recomendaciones concretas para su mejora.

Esta revisión del marco regulatorio y supervisor, se publico el 25 de Febrero de 2009 y es el conocido **Informe Laròsiere** (*The high-level Group on financial supervision in the EU, chaired by Jacques de Larosière , Brussels February 25th, 2009)*

Como todos los informes, el Informe Laròsiere tiene defensores y detractores, pero innegablemente aporta varias ideas, que ahora nos parecen lógicas y básicas, pero que a principios del siglo XXI no eran muy comunes:

- Las entidades financieras necesitan más capital (no olvidemos que el informe es del año 2009) y de mejor calidad.
- La regulación no debe promover comportamientos procíclicos (cuando las circunstancias son buenas, los agentes financieros actúan con optimismo y se minusvaloran los riesgos, y al revés)
- Debe incrementarse la transparencia sobre los riesgos asumidos por las entidades financieras.
- La regulación y supervisión no solo deben afectar a las entidades bancarias, también debe afectar a otras instituciones financieras como entidades aseguradoras, fondos de inversión colectiva, etc.…
- Debe mejorarse el Gobierno Corporativo de las empresas
- Debe mejorarse la coherencia en materia de regulación en los estados miembros de la Unión.

Y por fin la Directiva de Solvencia II

Por fin el 17 de diciembre de 2009 se publica en el Diario Oficial de la Unión Europea:

La Directiva 2009/138/CE del Parlamento Europeo o Directiva de Solvencia II

Desarrollada posteriormente por:

El Reglamento Delegado (UE) 2015/35 de la Comisión.

Transposición en España:

LOSSEAR Ley 20/2015 de 14 de julio, de ordenación, supervisión y solvencia de las entidades aseguradoras y reaseguradoras

Desarrollada posteriormente por

ROSSEAR (Reglamento publicado por Real Decreto 1060/2015 de 20 de Noviembre de ordenación, supervisión y solvencia de las entidades aseguradoras y reaseguradoras

De forma paralela a la publicación del Reglamento 2015/35, EIOPA puso en marcha un proceso de evaluación de Solvencia II, que se iniciaría en el mismo momento de la entrada en vigor de la norma, y que en el fondo perseguía no cometer los mismos errores del pasado, asumiendo la obligación lógica de un regulador de realizar revisiones y actualizaciones de la normas a lo largo del tiempo.

Proceso de evaluación de Solvencia II, un proceso vivo y en marcha

Estas revisiones estarían basadas tanto en los datos reportados por parte de las entidades aseguradoras a partir del primer informe público de 31 de diciembre de 2016, como en la evaluación en general de las circunstancias económicas.

El proyecto de revisión fue estructurado en dos "Sets of Advice" o conjuntos de consejos, persiguiendo 3 objetivos básicos que son:

- La simplificación y proporcionalidad de los requerimientos cuantísimos de calculo del Capital de Solvencia Requerido (SCR)

- Eliminación de inconsistencias técnicas (ej. Recalibración de determinados riesgos)

- Eliminación de restricciones injustificadas a la financian de las entidades.

Proceso de evaluación de Solvencia II, un proceso vivo y en marcha

El primer resultado de estas consultas técnicas por parte de la Comisión Europea ha sido la publicación el pasado 18 de junio 2019 en el Diario Oficial de la Unión Europea del Reglamento Delegado (UE) 2019/981 del 8 de marzo de 2019, por el que se modifica el Reglamento Delegado (UE) 2015/35.

Las modificaciones en los cálculos e información a desglosar sobre los niveles de Solvencia de las entidades detallados en el nuevo Reglamento, entraron en vigor 20 días después de su publicación, excepto aquellos que hacían referencia a la documentación de métodos e hipótesis e información a desglosar sobre la capacidad de absorción de pérdidas de los impuestos diferidos (Art. 50, Art. 59, Art. 60, Art. 61 del Reglamento 2015/35) y determinadas modificaciones en parámetros de la formula standard (desviaciones típicas en los cálculos del submódulo de riesgo de prima y del submódulo del riesgo de reserva para los ramos de crédito y caución, defensa jurídica y asistencia *-anexo II del Reglamento 2015/35-* y desviaciones típicas en Modulo del riesgo de salud no similar a vida en el seguro de enfermedad *-anexo XIV del Reglamento 2015/35-*).

Modificaciones mas significativas (RD 2019/981)

Las modificaciones más significativas del Reglamento delegado (UE) 2019/981 de la Comisión por el que se modifica el Reglamento Delegado (UE) 2015/35, agrupadas por riesgos afectados o por determinados aspectos relevantes son las siguientes:

Riesgo de mercado:

Con el objetivo de contribuir por parte del sector asegurador a la dinamización de la economía europea y, sobre todo, con el objetivo de favorecer la inversión en pequeñas y medianas empresas a través de bonos, préstamos o capital de inversión, así como de inversiones a largo plazo en acciones, se modifican determinados aspectos de los siguientes submódulos:

- Submódulo de riesgo de acciones: se mejora el tratamiento de la renta variable no cotizada
- Submódulo de riesgo de diferencial: se mejora el tratamiento de bonos y préstamos sin rating limitando su aplicación a ciertas condiciones.
- Submódulo de riesgo concentración de mercado: se mejora el tratamiento de bonos de administraciones locales y de compañías de seguros que alcancen un determinado de solvencia mínima.

Modificaciones mas significativas (RD 2019/981)

Riesgo de No Vida

Las principales modificaciones en este módulo se deben a la recalibración de determinados parámetros derivados de la revisión de las cifras de solvencia de las entidades durante estos últimos 3 años, en concreto:

Módulo de suscripción de no vida:

- se modifican los parámetros de desviación típica del cálculo del submódulo de riesgo de prima y del submódulo del riesgo de reserva para los ramos de crédito y caución, defensa jurídica y asistencia
- se mejora el tratamiento del riesgo de suscripción, para las primas futuras las primas futuras, en concreto en el riesgo de caída (modificación también para el submódulo de riesgo de salud no similar a vida)

Modulo del riesgo de salud no similar a vida:

- se modifican los parámetros de desviación típica del submódulo de riesgo de prima y de reserva del seguro de enfermedad.

Submódulo de riesgo de catástrofe provocada por el hombre:

- los riesgos marítimos, de aviación y de incendios, podrán calcularse con exposiciones netas de los importes recuperables de reaseguro.

Submódulo de riesgo de catástrofe natural:

- en el caso de los riesgos por tormenta de viento, riesgo de terremoto y riesgo de incendio se podrán realizar los cálculos en agrupaciones de zonas de riesgos.

Modificaciones mas significativas (RD 2019/981)

Enfoque de transparencia (art. 84 del Reglamento 2015/35)

Cuando las entidades no puedan aplicar el enfoque de transparencia a un organismo de inversión colectiva o a inversiones en forma de fondos, se permite utilizar un enfoque implicado basado en la última asignación de activos notificada por el organismo de inversión.

Adicionalmente se excluyen del límite del 20% que plantea el Art.84 para la utilización de datos agrupados, aquellos activos subyacentes o inversiones en forma de fondos que formen parte de las carteras de inversión en donde el riesgo de mercado es asumido por el tomador del seguro (Unit Link)

Utilización de parámetros específicos (Sección 12 del Reglamento 2015/35)

Se incorporan los contratos de reaseguro de exceso de siniestralidad (stop loss) en la utilización del factor de ajuste por el reaseguro no proporcional (el reglamento 2015/35 solo permitía la utilización de este factor de ajuste en el caso de los contratos de reaseguro de exceso de perdida excess loss)

Técnicas de reducción de riesgos (Sección 19 del Reglamento 215/35)

Se introducen modificaciones en las condiciones para poder utilizar determinadas prácticas de reducción del riesgo con el objeto de reflejar la evolución de las prácticas de gestión del riesgo en el ámbito asegurador tanto a través de productos estructurados como a través de contratos de reaseguro.

Entre otras, no se permitirá utilizar técnicas de reducción de riesgo a través de contratos de reaseguro durante un plazo superior a 6 meses con entidades que hayan dejado de cumplir los requerimientos de capital mínimo.

Modificaciones mas significativas (RD 2019/981)

Capacidad de absorción de pérdidas de los impuestos diferidos

Como se ha puesto de manifiesto, la capacidad de absorción de pérdidas de los impuestos diferidos tiene un impacto significativo en el cálculo del ratio de solvencia de las entidades, por lo que:

- se incrementa la justificación y documentación de las hipótesis subyacentes utilizadas para la proyección de los beneficios imponibles futuros, implicando a las funciones claves de la entidad, en la selección y evaluación de los métodos e hipótesis para demostrar el importe y la recuperabilidad de la capacidad de absorción de pérdidas de los impuestos diferidos, notificando y por tanto involucrando a su vez en todo el proceso de selección de métodos e hipótesis al órgano de administración.

- se incrementa toda la información a desglosar sobre los impuestos diferidos, debiendo desglosar una descripción detallada de las hipótesis subyacentes utilizadas para la proyección de beneficios imponibles futuros probables, así como un análisis de la sensibilidad de los activos por impuestos diferidos netos a los cambios de hipótesis subyacentes.

Modificaciones esperadas para el 2020…

Por último, y por concluir, no debemos olvidar que el proceso de revisión y evaluación de Solvencia II sigue su curso. La directiva 2009/138 ya establecía que determinadas áreas debían haber sido revisadas por la Comisión Europea como muy tarde el 1 de enero de 2021.

Esto implica que, durante el año 2020, se espera una modificación de la directiva, que abordará diversos temas que se agrupan en las siguientes 3 categorías:

- Medidas sobre garantías a largo plazo (variación en los métodos para la extrapolación de las curvas libre de riesgo utilizando un punto inicial más lejano en el tiempo, variaciones en cálculo del ajuste de volatilidad que tengan en cuenta las características de iliquidez de los pasivos de seguros, etc…)

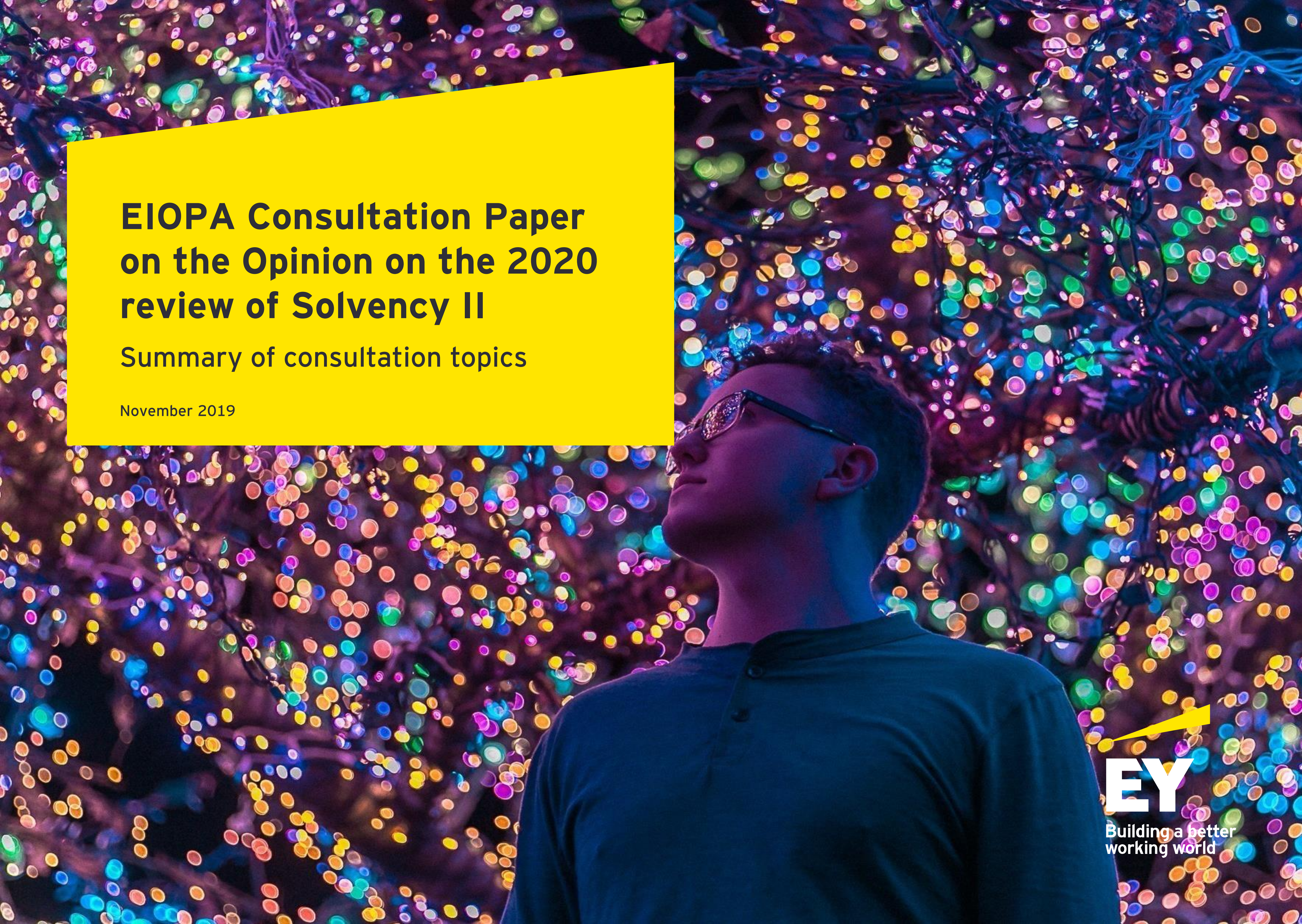
- Posible introducción de nuevas medidas de regulación macro prudenciales (dotar a los reguladores locales con la potestad de requerir un capital adicional para el riesgo sistémico o requerir planes de resolución de insolvencia preventivos, etc…)

- Revisión del marco general de Solvencia II en cuanto a la libre prestación de servicios, medidas de reporte y desgloses de información y en general, revisión de métodos, hipótesis, y parámetros utilizados en la formula estándar

EIOPA Consultation Paper on the Opinion on the 2020 review of Solvency II

Summary of consultation topics

November 2019



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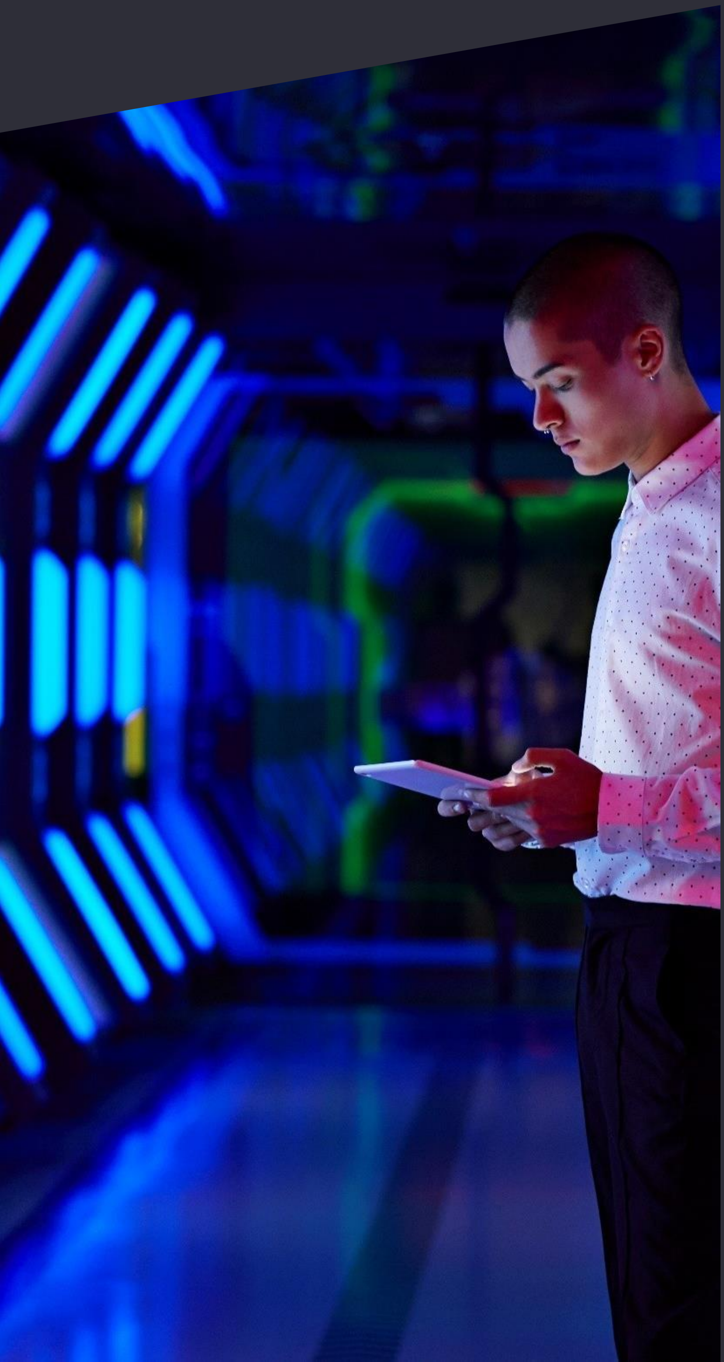
Building a better working world



Introduction

On 15 October 2019, the European Insurance and Occupational Pensions Authority (EIOPA) released their public consultation paper (CP) [1] on the 2020 review of Solvency II (SII). This consultation paper has been long anticipated by industry as several key topics will be assessed for the first time since SII was implemented on 1 January 2016, including the long term guarantee (LTG) measures and the issue of proportionality in terms of how SII is applied.

EIOPA's CP was published in response to the European Commission (EC)'s formal request dated 11 February 2019 for technical advice on the review of the SII Directive. The submission deadline for responses to this CP is 15 January 2020. EIOPA will collect data and assess the impact of its proposals before setting out its final advice by 30 June 2020.

The topics under consultation are broadly categorised as follows:

1. LTG measures and measures on equity risk.
2. Introduction of new regulatory tools on macro-prudential issues, recovery and resolution and insurance guarantee schemes (IGS).
3. Revisions to the framework based on supervisory experience since the introduction of SII, with a focus on proportionality and consistent application of requirements.

Please note that EIOPA had released separate CPs on two topics (reporting and disclosure / IGS) on 12 July 2019, with a deadline of 18 October 2019 for responding to these CPs.

[1]https://eiopa.europa.eu/Publications/Consultations/EIOPA-BoS-19-465_CP_Opinion_2020_review.pdf

This report summarises the topics under consultation in the CP and sets out EY's insights and commentary on these topics. Please note that our comments reflect our observations of the market and do not represent our views on whether any of the proposals are appropriate or not. Whilst the Brexit outcome is uncertain, UK policy is currently that SII will continue to apply in the UK through domestication of EU legislation. It is expected that the UK will remain close to the SII regime in at least the short to medium term, and will to that end consider reflecting changes made to the SII regime in the UK framework. Hence, we have included UK perspectives in this report.

This report was prepared by EY's Finance, Risk, and Actuarial Change team.

The information in this pack should not be regarded as comprehensive or sufficient for making decisions, nor should it be used in place of professional advice.

Accordingly, Ernst & Young LLP accepts no responsibility for loss arising from any action taken or not taken by anyone using this pack.

If you require any further information or explanations, or specific advice, please contact us and we will be happy to discuss matters further. Please contact your usual EY contact, or alternatively one of the contacts listed below.

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Executive summary

EIOPA's 2020 review includes a large number of proposals, some of which could have a significant impact for certain firms. Ultimately, the European Commission will need to make decisions balancing political considerations against EIOPA's proposed amendments

EIOPA's consultation on the 2020 review has been eagerly anticipated by industry as it represents the first major review of several important elements of the SII framework. The CP includes a large number of proposals, some of which have the potential to significantly impact certain firms.

Overall, EIOPA's consultation does not contain many surprises in terms of the topics covered. The proposals on LTG measures, macro-prudential supervision and standard formula solvency capital requirement (SF SCR) had been widely anticipated by industry.

While some firms will be disappointed that no changes are proposed to the risk margin, this is also anticipated by industry, particularly in light of earlier communications by EIOPA.

Some stakeholders (including regulators) had publicly expressed a desire for balance sheet impacts arising from this review to be broadly neutral. Whilst there are some proposals which would increase both technical provisions and SCR for some firms. In particular the proposed changes to the extrapolation of risk-free rates for the Euro currency and the revised strengthening of the SF interest rate risk calibration, there are no proposals which obviously appear likely to offset the impact of this proposal.

No fundamental changes have been proposed to the matching adjustment (MA) which will be welcomed by firms who had concerns that the MA may be discontinued. However, this may be disappointing for those who were looking for the scope of the MA to be widened. The MA is currently only utilised in the UK and Spain, and does not apply to the majority of European firms.

There is significant discussion of the VA within the consultation, EIOPA are proposing 8 variations to reform the VA. Whilst firms are likely to welcome the broad ambition of reducing the volatility caused by the current design, firms may be concerned that these changes could come at the cost of increased complexity, a potentially reduced VA and/or a reduction in the overall protection provided by the VA against crisis or stress scenarios. In particular, it is not clear how the EC will decide between the number of options proposed by EIOPA.

In advance of the paper's publication, many industry bodies and some regulators had stated that they hoped to see a greater focus on proportionality. While EIOPA has made some proposals that may reduce some of the reporting burden, there may be firms disappointed that the proposals do not go far enough and there are also proposals that would increase certain requirements for some firms.

It is worth remembering, these proposals are EIOPA's view and not the final proposed regulation. The EC will balance political considerations against this when deciding which elements of the final advice to adopt in June 2020. In some cases EIOPA has presented the same proposals that the EC has previously rejected, such as the allowance for negative interest rates in the SF SCR. It is unclear whether the same rationale will be used by the EC to adopt or reject these proposals a second time.

Topics under consultation

LTG measures – extrapolation of risk-free interest rates (RFRs)

Summary of EIOPA proposals

- EIOPA's proposals relate to the Euro currency and the point from which RFRs are extrapolated, i.e. the last liquid point (LLP) and the method used to extrapolate.

- EIOPA proposes the following options to amend the LLP:
  - Option 1: no changes, i.e. LLP of 20 years for the Euro and Smith-Wilson extrapolation.
  - Option 2: keep the LLP at 20 years for the Euro and introduce additional pillar 2 and 3 safeguards. These safeguards include requiring firms to:
    - Perform sensitivity analysis on setting the LLP to 50 years for the Euro and including the results in regular supervisory reporting (RSR).
    - Report this sensitivity analysis in their solvency and financial condition report (SFCR).
    - Where firms breach their SCR or MCR in the sensitivity analysis, they would have to provide evidence (if requested by supervisors) that dividend payments or voluntary capital distributions do not risk policyholder protection. Supervisors can limit capital distributions if they are unsatisfied with this evidence.
  - Option 3: increase the LLP to 30 years for the Euro. Undertakings would be required to perform sensitivity analysis on an extension of the Euro LLP to 50 years and include the results in the SFCR and the RSR (similar to option 2).
  - Option 4: increase the LLP to 50 years for the Euro.
  - Option 5: adopt an alternative extrapolation method which allows for market data beyond the LLP (the LLP is referred to as the "first smoothing point" under this alternative extrapolation method). This would affect the RFR term structure for all currencies.

- EIOPA have specified the following considerations as part of assessing these options:
  - Issue 1: avoiding the underestimation of technical provisions.
  - Issue 2: avoiding wrong incentives for risk management, in particular, incorrectly incentivising hedging against the extrapolated RFRs rather than actual risk in financial markets.
  - Issue 3: the stability of solvency positions and impact on financial stability, with concerns that certain firms (with long term liabilities not closely matched by assets) may exhibit procyclical investment behaviour when interest rates fall (by purchasing long term swaps and potentially further reducing swap rates).
  - Issue 4: maximising alignment with evidence from the deep, liquid and transparent (DLT) assessment of financial markets, for which the Euro is assessed to be DLT up to a 50 year maturity.

EY insights / commentary

- The extrapolation of RFRs is clearly a very important issue, with EIOPA's considerations highlighting the tension between a desire to be more market sensitive (i.e. aligning with the DLT assessment) and maintaining current financial stability / avoiding dis-incentives. The proposals here will require political decisions on how to balance these different considerations.

- The RFR curve methodology is a key element in the valuation of technical provisions (both the best estimate liabilities and risk margin), particularly for firms with long duration insurance business where the extrapolation period has a greater impact. The proposed changes to the RFR curve should have less impact for shorter duration insurance business, i.e. general insurance. The proposed RFR changes will have a more material effect on Continental European firms than UK insurers (who would only be impacted by the alternative extrapolation method proposal).

- EIOPA highlighted that changing the Euro LLP / extrapolation method would have the following impacts for firms with long term cash flows:
  - An LLP of 30 years would reduce the average EEA solvency capital requirement (SCR) ratio from 252% to 223%.
  - An LLP of 50 years would reduce the average EEA SCR ratio from 252% to 203%.
  - The alternative extrapolation method would reduce the average EEA SCR ratio from 252% to 240%.

- The additional sensitivity analysis proposed under options 2 and 3 is unlikely to be welcomed by firms who view existing SII operational requirements as being too onerous, since additional sensitivity analysis is likely to require additional modelling runs / resources to complete.

- The proposed revision of the RFR term structure under options 3 and 4 combined with proposed changes to interest rate risk SF SCR could potentially result in a significant decrease of the SCR ratio of SF undertakings, particularly those with significant long term business.

- In the Netherlands, there has been a strong focus on the RFR methodology from the life industry and the national supervisor, De Nederlandsche Bank (DNB). Several life firms are opposed to EIOPA's proposal to increase the LLP as it would drastically decrease their SCR ratio. The DNB noted that the extrapolation from the LLP to the ultimate forward rate (UFR) distorts the financial position of insurers and discourages cash flow matching as it leads to volatility in SII equity. Additionally, the DNB noted that the Smith-Wilson extrapolation methodology leads to high interest rate sensitivity close to LLP and that an alternative extrapolation based on the method used for Dutch pension funds should be considered.

- Under the Insurance Capital Standard (ICS), which is a global solvency framework being developed by the International Association of Insurance Supervisors (IAIS) that applies to large international insurance groups, the RFR methodology under the ICS's market adjusted valuation is similar to SII. The ICS Euro LLP is currently set as 20 years and applies Smith-Wilson extrapolation from the LLP to a UFR which begins at 60 years. The ICS RFR methodology also features a DLT assessment.

Topics under consultation

LTG measures – matching adjustment (MA)

Summary of EIOPA proposals

- EIOPA's proposals relate to the following issues:
  - Issue 1: whether to allow for diversification between MA portfolios (MAPs) and non-MAPs for standard formula (SF) firms. Currently, SF firms are not allowed to recognise diversification between MAPs and non-MAPs under article 217 of the SII Delegated Acts (DA).
  - Issue 2: the MA asset eligibility criteria for restructured assets.

- For issue 1:
  - EIOPA proposes to allow SF firms to recognise diversification between MAPs and non-MAPs.
  - EIOPA notes that there is an inconsistency in allowance for this diversification between SF firms and internal model (IM) firms, since IM firms can recognise this diversification in their SCR calculations.
  - EIOPA has argued that MAP assets only cover the best estimate liability (BEL) in the MAP and that allowing for diversification benefits in the SCR calculation does not affect / reduce the assets covering the BEL.
  - EIOPA's analysis highlights that only UK and Spanish firms currently apply the MA. EIOPA provided findings on the impact of removing the diversification restriction for 14 Spanish and 18 UK firms:
    - For the 14 Spanish firms (all SF), the reduction in SCR ranged from 0.3% to 19.6% (weighted average of 8.5%).
    - For the 18 UK firms:
      - There would be no impact for 10 UK firms on full IMs or partial IMs (PIM) as these firms already allow for this diversification.
      - For 4 PIM firms, the reduction in SCR ranged from <0.5% to 1.9%.
      - For 4 SF firms, the reduction in SCR ranged from 0.4% to 6.2% (weighted average: 2.6%).

- For issue 2:
  - EIOPA proposes that an additional requirement is introduced in the MA for restructured assets, where firms need to demonstrate that the following criteria is satisfied (in addition to satisfying the existing MA criteria) for these assets:
    1. "the underlying assets provide a sufficiently fixed level of income".
    2. "the restructured asset cash flows are supported by loss absorbency features such that those cash flows are sufficiently fixed in term and will remain so even as operating conditions change".
    3. "where the underlying assets include financial guarantees, those guarantees do not result in additional matching adjustment".
    4. "the undertaking is able to properly identify, measure, monitor, manage, control and report the underlying risks".
  - EIOPA also recognised that certain assets were constrained from inclusion in MAPs by a literal interpretation of article 77b(1h) of the SII Directive that asset cash flows are fixed. In particular, EIOPA acknowledged that certain assets which do not strictly have fixed cash flows could be suitable for backing annuity liabilities, such as callable bonds or infrastructure payments where a loan finances the construction phase. EIOPA considered a "yield to worst" approach and other alternatives to allow for the inclusion of such assets, but were not sufficiently comfortable to propose any changes to address this issue at this stage.

EY insights / commentary

- Overall, EIOPA's proposals are a mixture of positive and negative. Existing MA firms are likely to be encouraged that the MA is proposed to continue (as there had been talk of aligning the MA and VA or combining both into a single mechanism) and SF firms will welcome the diversification proposal. However as noted it is not a material change for the majority of the European insurance industry. Furthermore, non-MA firms may be disappointed that there are no proposed changes to make the MA more flexible and the potentially tighter restrictions on restructured assets may make it harder for firms who currently have MA to continue to use this.

- SF firms who apply the MA are likely to be in favour of EIOPA's proposal to remove the diversification restriction, as this generally reduces the SCR (to varying extents as highlighted by EIOPA's analysis) and eliminates an inconsistency with IM firms which had provided the IM firms with a competitive advantage.

- Whilst EIOPA introduces additional MA eligibility criteria for restructured assets, it does not propose any changes to existing MA eligibility criteria. This is unlikely to be well received by firms advocating for flexibility on both assets and liabilities:
  - There are firms from Continental European jurisdictions who would like to access the MA as they are in favour of the MA principles in terms of asset liability matching purposes. However, these firms are currently unable to access the MA due to the incompatibility of their product features against the existing MA eligibility criteria on liabilities. These firms have the view that the MA should be more flexible on the liability rules so that the MA should be available to more jurisdictions.
  - Several UK firms have argued that the MA eligibility is too inflexible on assets and that the rules have led to significant costs and resources being spent on restructuring certain assets to meet the MA requirements.

- EIOPA appears to be suggesting that the requirement introduced in the Prudential Regulation Authority (PRA)'s supervisory statement SS7/18 that assets in internal MA restructures (i.e. securitisations) satisfy the prudent person principle (e.g. firms should not internally restructure certain assets such as equity to create an MA eligible note) should be extended to cover exposures to external securitisations. This could potentially cause issues for certain assets such as some types of commercial real estate (CRE) loans, where these CRE loans are (in some cases) essentially restructured property exposures. Additionally, EIOPA notes under paragraph 2.179 of the CP that "it would not be appropriate to securitise real assets (e.g. property) that do not match the nature of MA liabilities". Firms may wish to assess that the income received on these assets is financed by lease payments, rather than sale of physical property. It should be noted that EIOPA states in paragraph 2.197 that the look-through approach to underlying assets should be implemented prospectively (and not retrospectively to assets already in MAPs) to avoid market disruption, given that MA assets were purchased with the intention to be held to maturity. It is not clear whether EIOPA considers any particular types of existing MA assets would not be allowed under their proposals. Some industry stakeholders have the view that these requirements are not intended to restrict existing UK investments, but will help to widen the PRA's approach of treating restructured assets as MA eligible to non-UK markets.

- EIOPA's additional requirement on financial guarantees appears to support the PRA's view on equity release mortgages that the spread attributable to the no negative equity guarantee (NNEG) cannot result in any MA benefit. This interpretation may be regarded as unfavourable from UK firms who are hoping to push back against the PRA's view on the basis that it is not required by SII. EIOPA's requirements may also impact other types of guarantees that could be utilised to structure MA eligible assets, such as reinvestment rate guarantees.

Topics under consultation

LTG measures – volatility adjustment (VA)

Summary of EIOPA proposals

- EIOPA's proposals to reform the VA cover five main areas: technical improvements, possible design options, general application ratio (GAR), dynamic VA (DVA) for SF and approval to use the VA.

- In terms of technical improvements, EIOPA has highlighted two technical issues:
  1. The assumptions underlying the representative portfolio (interest rates, duration of assets, market value weights) are updated on a yearly basis, so these assumptions are "frozen" during the year (the "MV-freeze" approach). This leads to overestimation of the market value weights in periods of high interest rates. EIOPA proposes an alternative approach where cash flows and durations are frozen (the "CF-freeze" approach). EIOPA's analysis shows that there is negligible difference between the two approaches, except in cases of extreme interest rate movements.
  2. Negative spreads are not allowed when calculating the spread for the government and corporate bond portfolios. EIOPA proposes to allow negative aggregated spreads to better reflect economic conditions of the spreads in the representative portfolio. EIOPA expects this change to have a small impact on the calculated VA values.

- In terms of design of the VA, EIOPA highlighted the following deficiencies that its proposals aim to address:
  - The impact of VA may over / under shoot the impact of spread exaggerations on assets.
  - The VA does not allow for illiquidity features of liabilities.
  - The activation mechanism for the country specific increase is not functioning as expected.
  - The mis-estimation of the risk correction, i.e. it is largely insensitive to credit spread changes.
  - The VA is almost always positive and does not support building up resilience in "good times".
  - The underlying assumptions of the VA are unclear.
  - Applying RFRs with the VA is not market consistent.

- EIOPA proposes the following design options to address the design deficiencies listed above (including the two technical changes above where applicable):
  1. "Undertaking-specific VA" based on undertaking-specific asset weights and market spreads.
  2. "Middle bucket" approach where the current MA and VA approaches remain and the undertaking-specific VA is introduced as the middle bucket. Firms can only apply the middle bucket to insurance liability portfolios subject to meeting certain cash flow matching criteria.
  3. "Asset driven approach": the VA would not be applied to the risk free curve. Instead, the VA would adjust the bond spreads on the asset side, where the difference in the value of bonds without and with the VA adjustment is recognised as an own funds item.
  4. Application ratio that takes into account of the undertaking's AL mismatch. The proposed formula to derive the VA under this approach (paragraph 2.363) includes applying an asset liability (AL) mismatch ratio, where this ratio is calculated as the sensitivity of the BEL to the VA divided by the sensitivity of fixed income assets to the VA. Firms are also allowed to derive the risk-corrected spread using either the VA reference portfolio or their own specific fixed income portfolio (as under design option 1).
  5. Application ratio that takes into account of the undertaking's illiquid liabilities. EIOPA suggests two approaches for this calculation: the first approach (paragraph 2.399) is similar to option 4 above, except that an illiquid liabilities ratio is applied; the second approach (paragraph 2.416) allocates liabilities to buckets of different levels of illiquidity with different application ratios.
  6. "Relative risk-corrections": the risk correction is calculated as a fixed percentage of the spread.
  7. Amendment to the trigger and calculation of any country-specific increase of the VA.
  8. Create a "permanent VA" that reflects the long term illiquid nature of insurance cash-flows, and a "macro-economic VA" that will only exist when bond spreads are wide, e.g. during crisis. The macro-economic VA would replace the existing country specific add-on.

EY insights / commentary

- Overall, EIOPA has proposed a set of wide ranging proposals with potentially different impacts. It is unclear how the EC will decide between the different proposed options. Firms impacted by the VA are likely to be concerned that addressing VA issues will come at the cost of increased complexity, a potentially reduced VA and / or a reduction in the overall protection provided by the VA against crisis or stress scenarios. It is currently unclear if these proposals will mitigate the "cliff edge" effects seen by some countries in the current VA application.

- The VA has been one of the industry's main focus areas ahead of the 2020 review. Key issues raised include: artificial volatility due to basis risk between an insurer's actual asset portfolio and VA reference portfolio; lack of flexibility in the national component trigger point; the lack of economic rational behind the 65% GAR; and reducing / eliminating perverse incentives to invest in riskier asset portfolios. EIOPA's proposals seek to address these issues.

- Design options 1-5 are likely to lead to additional complexity, which is unlikely to be welcomed by firms who view SII pillar 1 requirements as already overly complex and not proportional to their business. These firms are likely to be more content with the operational nature of the current VA. The middle bucket approach may potentially work as a compromise, as this approach allows firms to choose the middle bucket (subject to meeting the requirements) or the current VA approach.

- For design option 1, EIOPA's impact analysis (paragraph 2.539) shows that the average VA at year end 2018 (YE18) would have increased from 0.24% to 0.28%. This impact varied between different jurisdictions: the average VA changed to 0.67% for Italy and Greece; 0.36% for Spain; 0.25% for Germany; 0.24% for France and Belgium; and 0.18% for the Netherlands.

- Design option 2 appears to be based on the ICS's three-bucket discounting approach which also features a "middle bucket", with similar design and eligibility criteria to EIOPA's proposals. Whilst EIOPA notes that the middle bucket option was not assessed further in view of its disadvantages (paragraph 2.350), it is worth highlighting that the IAIS views the three-bucket approach as a viable option for ICS. In particular, there has been significant focus in recent ICS field tests on refining the design and eligibility criteria of the middle bucket to allow additional liabilities to qualify (firms are currently allocating mostly participating products to the middle bucket).

- Design option 3 is less common in other major solvency frameworks, where most frameworks apply an adjustment to the RFR curve used to discount insurance liabilities (rather than adjusting the asset side). The requirement to revalue bond holdings for the VA may require firms to modify their systems and processes. On the hand, this proposal may lead to simplifying the calculation of liabilities which would only refer to the RFR (without the need to generate different adjustments to the RFR). It may be interesting to assess the solvency impact of this approach.

- For design options 4 and 5, EIOPA's analysis shows that the average VA at YE18:
  - Would have increased from 0.24% to 0.27% under option 4 (paragraph 2.541).
  - Would have been broadly unchanged from 0.24% under option 5 (paragraph 2.544).

  The figures above reflect the impact across all jurisdictions, but the impacts do vary by jurisdiction. EIOPA's analysis showing an increase in VA may come as a surprise since the AL mismatch ratio and illiquid liabilities ratio do not replace the 65% GAR, but are applied to the GAR. Both the AL mismatch and illiquid liabilities ratios are subject to a maximum value of 1, which means that these ratios can only reduce the 65% GAR and therefore should lead to a lower VA. However, EIOPA has noted for jurisdictions where these options increase the VA that it is due to the currency part of the VA increasing as it is weighted by total spread sensitive assets rather than total investments.

Topics under consultation

LTG measures – volatility adjustment (VA) (cont'd)

Summary of EIOPA proposals

- EIOPA also proposes 2 approaches which are based on a mix of the design options (described on the previous page):
  - Approach 1: permanent VA calculated as a combination of options 4, 5 and 6; and macro-economic VA based on option 8.
  - Approach 2: permanent VA calculated as a combination of options 1, 4 and 5.
- For approaches 1 and 2, EIOPA's impact analysis shows that the average VA at YE18 decreases from 0.24% to 0.19% under both approach 1 (paragraph 2.548) and approach 2 (paragraph 2.550). However, the impacts at a jurisdiction level vary more widely under approach 2.

- EIOPA considered three options for the general application ratio (GAR) used in the VA calculation:
  1) Keep the ratio unchanged at 65%.
  2) Increase the ratio to 100%.
  3) Increase the ratio to a value between 65% and 100%.
- EIOPA's advice is to keep the GAR unchanged at 65%.

- EIOPA advises that the SF should not be changed to allow for the DVA. EIOPA notes under paragraph 2.588 that allowing for a DVA under the SF would result in consistent treatment between SF and IM firms and potentially encourage investment in corporate bonds and loans. However, EIOPA also noted a number of disadvantages, including: creating an uneven playing field in favour of SF firms as government bond risks are not fully captured in the SF; that the spread risk SCR would not fully reflect the risk of spread widening observed in markets; reduce the level of policyholder protection if capital requirements are reduced; and increase the complexity of SCR calculations for firms applying the DVA.

- EIOPA highlights that countries are inconsistent in terms of requiring supervisory approval to use the VA, which leads to unequal treatment between firms in different jurisdictions. EIOPA notes that 10 countries require approval for firms to use the VA and 17 countries do not require approval. EIOPA's view is that all member states should be consistent in terms of whether supervisory approval is required for the VA. However, EIOPA notes that the design of the VA will influence whether supervisory approval is required, so prefers to decide on its preference after the consultation.

EY insights / commentary

- For design option 6, EIOPA's impact analysis (paragraph 2.546) shows that the average VA at YE18 decreases from 0.24% to 0.22% for all individual European regions. The MA and VA currently share the same risk correction, however, it is unclear whether EIOPA would apply the proposed change for option 6 to the MA.

- Design option 7 is intended to address the issue most recently experienced by Italian firms at YE18. They noted that the spread widening experienced on Italian government bonds was not sufficiently / adequately offset by the corresponding increase in VA when the country-specific trigger was not activated. Some firms noted that if the YE18 Italian government bond spread was higher by only 0.02%, then the country-specific VA would have been activated and increased the VA applied. The market is expected to welcome the review of the country-specific trigger.

- Several stakeholders have highlighted the lack of economic rationale behind the 65% GAR. EIOPA provides details on the risks inherent in VA which support the inclusion of a GAR in their view. However, there remains no clear explanation of how the figure of 65% has been derived. Under the ICS framework, the application ratio for the "general bucket" (broadly equivalent to the SII VA) is 80%, although it is also unclear how 80% has been derived. Some firms have argued that the application ratio should be 100% on the basis that anything less is uneconomic.

- It is unclear whether there is a strong demand from the industry to allow for the DVA in the SF, particularly given the complexity of a potential DVA calculation and given that SF capital requirements for credit spread risk are generally less onerous than under an IM (which has partly driven some IM firms to apply for a DVA). However, similar to other risks the fact that IM firms can apply for DVA creates a further difference between SF and IM firms. Furthermore, the application process and the level of benefit received across Europe in utilising the DVA varies significantly. Therefore, introducing this to the SF would also likely cause large differences in approach across Europe.

Topics under consultation

LTG measures – dynamic volatility adjustment (DVA) for internal models (IMs)

Summary of EIOPA proposals

- EIOPA is asked to assess whether the modelling of the DVA by IM firms sets disincentives for undertaking's investment and risk management strategies, and whether diverging practices are detrimental to achieving a level playing field. EIOPA is also asked to assess the appropriateness of dynamic modelling in IMs in light of the assumptions underlying the VA. EIOPA is also asked to advise on how to harmonise dynamic modelling in IMs (if it advises to maintain this modelling).

- EIOPA identifies the following issues in respect of the DVA:
  - Potential disincentives for risk and investment management, i.e. incentives to invest in riskier assets for the sole purpose of lowering the SCR.
  - Impacts on level playing field, due to different modelling approaches adopted.
  - Appropriateness of the DVA in light of the lack of clarity around the assumptions underlying the VA.

- EIOPA advises the following:
  - The use of the DVA for IM firms could be maintained, if disincentives are resolved in the VA ("at source"). EIOPA concludes that the DVA does not in itself introduce disincentives for insurers' investment and risk management strategies, but that it transports and amplifies potential disincentives from the base VA, particularly for firms exposed to overshooting.
  - If the VA itself is not reformed, EIOPA advises that regulatory measures would be needed to avoid disincentives and ensure that the DVA is risk sensitive and protects a level playing field.
  - EIOPA does not propose any concrete changes to the DVA on the basis that the proposed changes to the base VA are under consultation.

- EIOPA notes in paragraph 2.619-2.620 that 62 solo entities are using an IM including a DVA as at YE18, with all 62 solo entities belonging to 8 insurance groups. The majority of these solo entities are from Germany, France and the Netherlands.

- EIOPA notes that they observe eight DVA modelling approaches in the market, of which:
  - Four approaches are classified as "direct approaches", which aim to replicate the EIOPA VA methodology.
  - Four approaches are classified as "holistic" approaches, which do not replicate the EIOPA VA methodology and vary conceptually in approach and technical specification.
- EIOPA notes in paragraph 2.638 that the impacts of using the DVA do not appear to depend on the approach used, but depends more on the type of business.

- EIOPA's analysis (paragraph 2.637) shows the impact (for the sample of 47 DVA firms) of implementing a DVA under IMs compared to a situation in which the IM has a constant VA:
  - If the DVA is adopted and sovereign bond risk is considered, the SCR reduces by 18.2%.
  - If the DVA is adopted and sovereign bond risk is not considered, the SCR by 3.3%.
- The impact of 3.3% indicates that implementing a DVA in IMs has a limited impact compared to having a constant VA (if modelling of sovereign exposures is not enforced).

EY insights / commentary

- As EIOPA's analysis demonstrates, the DVA is generally only applied by a limited number of large insurance groups (and the solo entities of these insurance groups). These firms (as well as other firms considering applying for the DVA) may wish to carefully assess the proposals to the base VA given EIOPA's comments on the need to introduce regulatory measures to the DVA, if the base VA is not reformed to address deficiencies.

- The DVA is utilized by many European firms in place of MA, therefore EIOPA's recommendation to retain the DVA will be welcomed.

- As with VA approvals there is a wide variety of approaches to DVA implementation across Europe. EIOPA's proposals do not intend to harmonise the approach to implementation, meaning the benefit received by firms will continue to vary materially by country.

- In the event that the VA is reformed, it is likely that DVA firms would need to adjust their existing DVA methodology and carefully consider how to allow for the different proposals on the base VA (see page 7) in an appropriate manner. For example:
  - If either design option 1 ("undertaking specific VA") or 2 ("middle bucket") is chosen, DVA firms would need to update their DVA methodology to reflect that the VA would be calculated based on the firms' own asset portfolio composition under each stress scenario.
  - If design option 3 ("asset driven approach") is chosen, it is unclear whether the current DVA would continue. However, if the DVA remains, then option 3 should result in significant changes to existing DVA models since fixed income assets are revalued under this option (rather than insurance liabilities) which may have a significant impact on solvency if sovereign bond risk is enforced.
  - If either design option 4 or 5 is chosen (application ratios allowing for asset liability mismatch and illiquid liabilities respectively), DVA firms would need to update their DVA methodology to allow for the different application ratios.
  - If design option 6 is chosen ("relative risk correction"), this would also require a change to DVA models but potentially simplifies the DVA calculation as the same relative risk correction would be applied under all DVA stress scenarios.
- Further detailed analysis would need to be performed to assess the impact of proposed base VA on the DVA, in particular, whether the effectiveness of the DVA is reduced and results in higher capital requirements relative to the current position.

Topics under consultation

LTG measures – transitional measures on risk-free interest rates and technical provisions

Summary of EIOPA proposals

- EIOPA proposes that insurance and reinsurance undertakings should only be allowed to start applying the transitional on the risk-free interest rates and on technical provisions in the following cases:
  - An undertaking newly falls under SII because it has passed the thresholds of article 4 of the SII Directive.
  - An undertaking transfers a portfolio that is subject to the transitional to another undertaking.
- EIOPA proposes better disclosures on the use of these transitionals, and advises that firms should set out in the SFCR following information:
  - The reason for applying the transitional. EIOPA notes that it is acceptable to disclose that the firm would not comply with the SCR without the transitional.
  - The dependency of the undertaking on the transitional.
  - The prospect to reduce any dependence on the transitional by the end of the transitional period.
- EIOPA's analysis highlighted that as at YE17, 168 EEA insurance undertakings applied transitionals, of which 139 meet the SCR without the transitionals. The undertaking that apply the measures cover a broad span of solvency positions. For example 53 users of the transitional on technical provisions have an SCR ratio above 200% without that measure.

EY insights / commentary

- Overall, EIOPA's proposals appear to restrict the use of these transitional measures for existing SII firms and increases disclosure requirements on transitionals.
- EIOPA's proposals on eligibility for transitionals are unlikely to be welcomed by some firms who have currently not applied for transitional measures due to their scale, as these proposals would prevent these firms from being able to apply in future. The proposal also potentially allows firms who previously have not applied transitionals to acquire business (which had applied a transitionals) and the other way around, potentially causing a non-level playing field.
- A large number of firms do make use of these transitionals and the new disclosure requirements will therefore impact them. As EIOPA noted, the majority of firms who do apply these transitionals would in fact comply with the SCR even without the transitional measures. These firms may need to consider how to fulfil this disclosure requirement.

LTG measures – risk management provisions on LTG measures

Summary of EIOPA proposals

- EIOPA states that although risk management is not specifically addressed in the call for advice, the pillar 2 provisions on the LTG measures are subject to the overall LTG review and impacted by potential modifications on the design of the measures in pillar 1.
- EIOPA identified 5 issues around the use of VA with the following proposals:
  - Role of the liquidity plan for the VA: EIOPA advises that firms applying the VA should fall under the requirement to establish a liquidity risk management plan (LRMP). In particular, the LRMP should allow for the use of the VA and assess whether there are any liquidity constraints that could result in forced sale of assets and endanger the VA that could be earned.
  - Sensitivity analysis for the VA: EIOPA suggests requiring firms to perform sensitivities on different economic (spread) situations instead of referring to the assumptions underlying the VA. Firms should report the results in the regular supervisory report.
  - Forced sale of assets for the MA and VA: EIOPA advises to delete this requirement (article 44 para 2a(c)(i) of the SII Directive).
  - Policy on risk management for the VA: EIOPA advises to remove the requirement of a VA policy, specifying that the risk management policy should include reference on the use of VA.
  - Analysis of measures restoring compliance for the MA and VA: firms who do not comply with their SCR by not applying the LTG measures should demonstrate that their dividend payments / other voluntary capital distributions do not place the protection of policyholders and beneficiaries at risk (if requested by their NSA). Firms should regularly report the impact of not applying the LTG measures to their NSA.

EY insights / commentary

- Overall, EIOPA's proposals may necessitate additional work for firms applying LTG measures, as some firms may need to establish a LRMP (although our observation is that LMRPs are increasingly common in industry) and some firms may need to update their risk management policy to reference the VA. Additionally, EIOPA proposes firms to perform sensitivity analysis which would require additional work for some of these firms.
- EIOPA has already assessed the adequacy of the risk management requirements connected to LTG measures within the 2018 LTG report. The 5 issues under review are based on feedback received by NSAs on their experience in supervisory practice. EIOPA's recommendation on risk management provisions will take into consideration the evolution and potential reform of the overall LTG package.
- For the proposal around measures to restore compliance for the MA and VA, it should be noted that EIOPA proposes that NSAs should be able to ask firms to limit or withhold capital distributions to ensure that the solvency position of the undertakings concerned is sustainable.

Topics under consultation

LTG measures – disclosure on LTG measures

Summary of EIOPA proposals

- EIOPA identifies three main issues identified in terms of disclosures on LTG measures and proposes the following options:
  - There is a lack of qualitative information, including SFCRs not regularly outlining information on the use / impact of LTG measures; insufficient disclosure on the motivations behind using the LTG measures; the composition of MA assets and the yields earned on those MA assets. EIOPA advises that there should be a definition and prescription of minimum information requirements to improve the disclosure of qualitative information on the use of LTG measures.
  - There is insufficient quantitative information on the impact of the LTG measures on the SCR ratio and MCR ratio and the relative impact of the measures on the SCR, eligible own funds and technical provisions. EIOPA proposes that the SFCR template on the impact of the LTG measures should also show the impact on the SCR and MCR ratio, and no additional ratios need to be included.
  - The results of sensitivity analysis around the LTG measures are not included, such as the impact of the risk-free rate (RFR) extrapolation. EIOPA recommends that firms should disclose in their SFCR the outcome of a sensitivity analysis regarding the ultimate forward rate (UFR) used in the extrapolation of RFRs on technical provisions, own funds, SCR and MCR.

EY insights / commentary

- Overall, the proposals will increase disclosure requirements for firms applying LTG measures with some of the proposals requiring additional modelling. These proposals are unlikely to be welcomed by firms who view existing SII disclosure requirements as being too onerous.
  - The prescription of minimum criteria for disclosure of qualitative information should provide greater overall transparency, comparability and support a level playing field. Firms who apply the transitionals may need to update their SFCRs to additional these disclosure requirements (where they do not do so already).
  - In terms of the proposal to show the impact on SCR and MCR ratio, this will make the information more accessible, although it can be derived from other SFCR figures. Given the importance of the SCR and MCR, it is expected that providing these additional disclosures would not take significant additional effort.
  - The sensitivity analysis around the UFR involves shifting the UFR by a fixed amount of -1%. This proposal will require additional effort for firms to complete.

Topics under consultation

Measures on equity risk – long term and strategic equity investments / symmetric adjustment / transitional measure

Summary of EIOPA proposals	EY insights / commentary
Duration-based equity risk (DBER): ▸ EIOPA proposes to phase out the DBER sub-module (article 304 of the SII Directive) and that no new approvals for the DBER are granted. ▸ EIOPA states that 11 NSA's reported in 2016 that the DBER is not implemented in their national legislation. Immediate removal of the DBER would result in one undertaking in France having its SCR ratio reduced from 159% (without TMTP and VA) to 139%.	▸ This will help to reduce the complexity of having both a DBER risk module and a LTE class module. EIOPA points out that the calibration for the latter (which was proposed by the European Commission and implemented in March 2019) was, in part, justified by the European Commission based on the DBER.

Strategic equity investments:
▸ EIOPA proposes:
  ▸ To maintain the 20% control threshold and the "low volatility" requirements as it considers these to be critical for justifying the strategic nature of the equity investment.
  ▸ To provide further clarification on how to assess that the investments have lower volatility in order for the reduced charge of 22% to apply. EIOPA recommends an optional method (called the "beta method") to justify the volatility criteria, by demonstrating a "beta" below 22/39 (for type 1 strategic equity) or 22/49 (for type 2).
  ▸ To amend article 171 of the SII Delegated Acts to be more explicit and refer to participations rather than to equity investments.
	▸ Firms may wish to consider whether they have sufficient justification for lower volatility for any current strategic equity investments, and assess whether the "beta" calculation supports their inclusion in this module.
	▸ EIOPA clarifies that the treatment of strategic participations assumes that their valuation does neither significantly depend on the performance of the insurance undertaking, nor that its valuation is significantly correlated with the changes in own funds of the undertaking. EIOPA asks firms to provide views on whether the correlation of risks between the participation and the participating undertaking should be allowed for in the strategic equity investment module. The correlation of risks is likely vary between different firms as the correlation will depend on the nature of the strategic participation and the insurance undertaking.

Long term equity (LTE) investments:
▸ EIOPA advises the following:
  ▸ Favourable treatment only applies to "well" diversified LTE portfolios. EIOPA considers that the requirement which only enables EEA equities to be eligible for inclusion in LTE portfolios does not prevent a portfolio from being insufficiently diversified, and that firms can achieve sufficient diversification in terms of sector and / or issuers from EEA equities.
  ▸ Intra-group investments to be excluded from the LTE scope.
▸ EIOPA questions the following issues:
  ▸ The calibration of the 22% capital charge on LTE based on their investigation of value at risk over extended investment durations. In particular, EIOPA notes in paragraph 2.843 that "it is not possible to corroborate the assertion that investment for a longer duration justifies a lower capital charge" based on their analysis. However, EIOPA does not propose any changes to the SII Directive for this point.
  ▸ The adequacy of the current equity correlation methodology regarding LTE (where LTE risk is correlated with other risks in the same way as type 1 and type 2 equities). EIOPA notes that the correlation matrices were defined based on a 1-year time horizon, whereas LTE should be considered over a multiple year time horizon.
	▸ EIOPA has proposed some additions to the text for article 171a of the SII Delegated Acts. However, it is not clear that this is likely to have a material impact on the SCR, unless firms are unable to demonstrate their LTE portfolio is well diversified, or firms are currently including controlled intra-group equity investments in the scope of long term equity. Firms may wish to assess their current LTE approach against these new thresholds.
	▸ EIOPA's consultation specifically asks firms for evidence to support the current diversification assumptions between LTE and other risks. This may indicate that a more prudent approach may emerge after the CP responses are assessed, particularly given EIOPA's criticisms of the LTE calibrations.
	▸ The proposal around a well diversified LTE portfolio appears to attempt to exclude certain private equity investments that an insurer could otherwise make. The proposal around excluding intra-group investments could also potentially exclude certain private equity investments, although there could be an argument that these fall into strategic equity, so there may be no impact.

Symmetric adjustment: ▸ EIOPA proposes that the symmetric adjustment (article 172 SII Delegated Acts) is also maintained, with no change to the underlying composition of the equity index. EIOPA's analysis (paragraph 2.982) highlighted that there was a high level of correlation among the main stock markets in Europe, so updating the equity index composition was not a priority for the symmetric adjustment. ▸ EIOPA proposes no changes to the "standard" type 1 and type 2 equity SCR calibrations, i.e. the stresses remain at 39% and 49% respectively (before symmetric adjustment).	▸ Some stakeholders view the capital treatment of equity investments as too onerous. For example, the French supervisor, Autorité de contrôle prudentiel et de résolution (ACPR), has publicly stated that SII penalises equity investments (despite the introduction of lower capital charges for LTE in the 2018 SII review). The ACPR stated that a reduction in capital charges for equity investments would allow insurers to invest more in equities, as well as potentially benefit clients with better guarantees and benefit the economy.
Transitional measure on equity risk: ▸ EIOPA proposes no change to the equity transitional (article 308b(13) of the SII Directive).	▸ EIOPA's analysis suggests that use of the equity transitional is limited and that the impact is generally reported to be immaterial by NSA's. Only the Finnish FSA considered that the existence of this transitional might generate a "slight difference" in investment behaviour.

Topics under consultation

LTG measures – extension of the recovery period

Summary of EIOPA proposals

- EIOPA notes that, to date, it has not received a request to declare an exceptional adverse situation, which would increase the recovery period of article 138(3) by up to 7 years.
- EIOPA proposes to clarify the role of the European Systemic Risk Board (ESRB) with respect to the extension of the recovery period.

EY insights / commentary

- The proposed new wording makes it clearer that the ESRB is to be consulted, where appropriate, before the declaration of an exceptional adverse situation.
- It is unlikely that this proposal will cause concern for firms, as it simply clarifies that EIOPA will consult with the ESRB before declaring an extension, rather than individual NSAs.

Technical provisions – best estimate liabilities (BEL)

Summary of EIOPA proposals

- A number of areas have been identified where divergent practices are currently adopted in terms of the BEL. In some cases, EIOPA proposes wording changes to the regulations to clarify EIOPAs preferred approach, including:
  - Contract boundaries (CBs):
    - CBs should relate only to obligations in respect of future premiums.
    - Extension of contract boundary reliant on underwriting at contract level and not having the right to repeat that risk assessment.
    - "Other" future profits (notably investment management fees) should be included within future profits where relevant.
  - Future management actions (FMAs) definition clarified.
  - Expected profits in future premiums (EPIFP) presentation clarified.
  - Expense recognition:
    - New business volumes should reflect reasonable expectations (particularly for businesses closed to new business).
    - Clarification that overheads should be assessed on a prospective basis.
- In other areas no changes to regulation are considered necessary albeit there is a suggestion that additional (currently unspecified) EIOPA guidance may be desirable:
  - Calibration of ESGs, particularly in respect of external service providers.
  - Valuation of options and guarantees, particularly in respect of dynamic policyholder behaviour.
- More generally closer alignment with IFRS 17 is rejected due to differing objectives and granularity and absence of a finalised IFRS 17 framework.

EY insights / commentary

- None of the changes identified appear to reflect a change in EIOPA's view on the manner in which the BEL should be assessed, rather all areas appear to reflect a desire to harmonise market practice across Europe.
- The interpretation being set out by EIOPA generally is expected to reflect more common market practice. As such, the changes are likely to lead to increased harmonisation in some areas and make it more difficult to justify certain alternative approaches.
- The practical examples provide helpful reference points against which participants and their advisers might assess current approaches.
- However, even where the regulations include proposed wording changes these may not prevent continuation of certain divergent practices, e.g.
  - The definition of FMA and requirement that new business volumes should reflect management decisions would not necessarily prevent divergent practices in terms of level of formality.
  - Few insights are provided on the nature of existing management actions and those which might be considered anomalous.
- In other areas the identification of examples of divergent practice provides useful background without significant insights being provided on the potential guidance which EIOPA might be considering, for example:
  - ESG calibrations performed by service providers.
  - Unbundling.
  - Requirements for recognising dynamic policyholder behaviour.

Topics under consultation

Technical provisions – risk margin (RM)

Summary of EIOPA proposals

- No changes to the RM are proposed. EIOPA provides context on their overall conclusion, mainly that their scope under consideration did not extend to challenging the cost of capital (CoC) approach or other alternatives such as varying the CoC rate for different types of business, which would require a change to the SII Directive.
- EIOPA's assessment covered: design of the RM; asset mix assumptions including the use of RFRs rather than recognising MA or VA; and the use of a fixed CoC including the assumptions underpinning that fixed rate. EIOPA identified areas for consideration including concerns of market participants and sets out some context for the decisions taken on these areas:
  - Design of the RM:
    - The design was tested by considering actual transfer experience, including the CoC rate implied within those transfers.
    - Of 44 transfers for which data was gathered, only 7 were deemed appropriate to use in comparative analysis. Even for this restricted dataset, the implied CoC varied from <3% on a transfer of annuity business to 46% for a unit-linked business.
  - Asset mix assumption:
    - Consideration on whether to apply the MA or VA in the RM calculation (where firms use MA or VA to discount the BEL), rather than just applying RFRs.
    - While pros and cons are listed, making any changes has been rejected inter-alia due to this being inconsistent with the assumption that the reference undertaking de-risks on transfer.
  - Fixed CoC:
    - EIOPA concluded that reduced interest rates over recent years does not constitute a convincing argument to decrease the CoC, but provide no insights into what it might consider as a scenario where the CoC rate might change.
    - It was considered unnecessary to repeat the underlying analysis given this had been reviewed by EIOPA in 2018.

EY insights / commentary

- A number of firms are likely to be disappointed with the lack of change being proposed. In particular, many market participants have loudly voiced concerns over the magnitude of the RM (especially for annuity business) and its sensitivity to interest rates.
- The magnitude of the RM and the transitional measures on technical provisions (which largely offset the RM) that are running off over the next 12 years means that firms across Europe are actively looking for ways to reduce the impact of the RM on their balance sheet. Many UK firms utilise reinsurance from outside the EU to reduce the magnitude of the SCR thus reducing RM.
- In general the rationale offered within the consultation relies more on the absence of evidence to change rather than evidence to positively justify the current framework in relation to other potential designs. In particular, some firms will be disappointed by the rejected possibility of applying the MA or VA to the discount rate.
- It should be noted that some proposals relating to the Euro LLP in the discount rate (see page 5) would have a potentially material impact on the RM as well as the BEL, as a lower risk-free rate curve would increase the risk margin (all other things being equal).
- Under the ICS framework, the latest technical specifications feature a percentile approach for its equivalent RM (although this approach is not confirmed yet). The ICS percentile approach appears to result in a lower amount of RM held relative to SII and some firms have noted that there may be uneven playing field issues in favour of ICS firms if SII firms have to hold a higher RM.

Own funds – tiering and ancillary own funds / undue volatility / availability criteria / attribution of items

Summary of EIOPA proposals

- The only change proposed by EIOPA is in respect of "double leverage" which occurs when a parent entity in a group provides tier 1 capital support to a subsidiary which is financed by externally issued parental non-tier 1 capital. EIOPA proposes that the group supervisor should assess the level of double leverage and take action when it is 'excessive (e.g. leverage ratio > 100%). No other significant changes are proposed.
- EIOPA proposes no changes to the SII tiering, whilst considering the following issues:
  - Differences between banking and insurance.
  - Undue volatility within own funds generated by current tiering limits. EIOPA noted that most NSAs were not in favour of change and EIOPA therefore aligned its position to NSAs.
  - Appropriateness of attribution of items between tiers, including the attribution of expected profits in future premiums (EPIFPs).

EY insights / commentary

- EIOPA rejects closer alignment between banking and insurance, including reduction of insurance to two tiers, due to differences between business models for banking and insurance undertakings.
- Various options are considered in respect of tiering, notably:
  - Changing of the calculation basis for restricted tier 1.
  - Restriction on EPIFP as tier 1.
- In these areas no changes were proposed. While this is in part attributed to lack of support for change from NSAs or lack of consensus from NSAs, limited information is provided by EIOPA to support its conclusions.

Topics under consultation

Solvency capital requirement standard formula (SCR SF) – interest rate risk (IRR)

Summary of EIOPA proposals

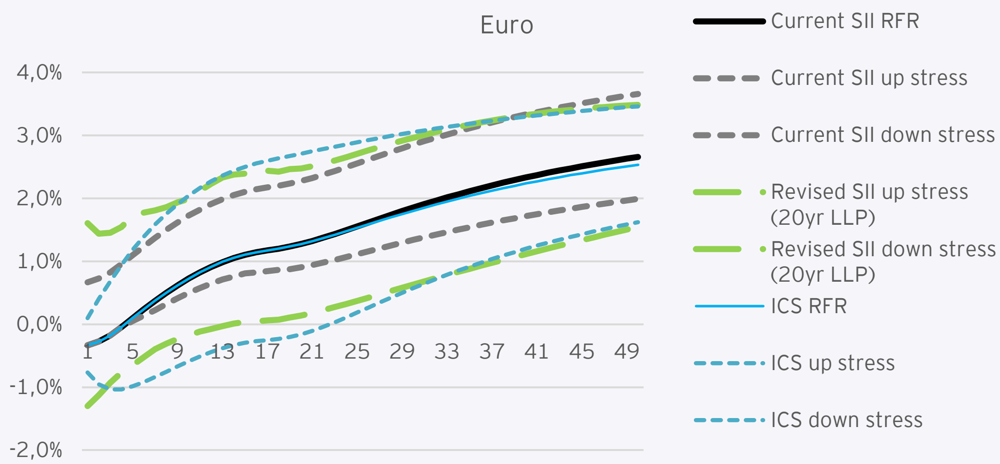
- EIOPA previously noted in its second set of advice in 2018 that there was "strong evidence that the current interest rate risk module severely underestimates the risk", and proposed a relative shift approach which would allow for negative interest rates. The material impact expected to be caused by this proposed approach would require a gradual implementation. The European Commission decided to not make any changes at that point in time.
- EIOPA re-affirms their 2018 advice in this CP and EIOPA "strongly advises" to change the calibration of the interest rate SCR.
- The previous advice suggested an implementation period of up to 3 years. EIOPA notes that it will revise the need for gradual implementation in view of the combined impact of the changes in the CP.

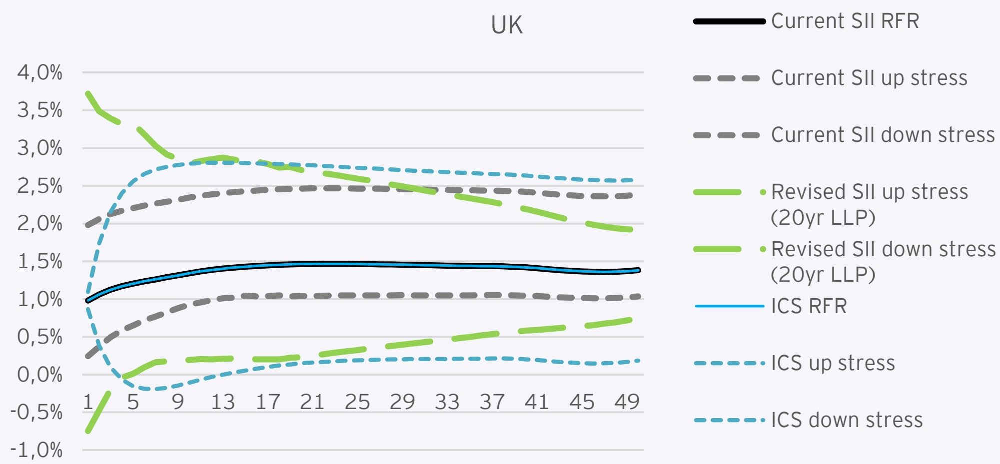
EY insights / commentary

- It is unclear whether the European Commission will accede to EIOPAs advice, but firms should be prepared for a material change to the IRR calibration. Combining the potential impact of changes in the LLP and the UFR with the proposed IRR calibration is likely to have a material impact for SF firms (particularly those with long term insurance business).
- EIOPA proposes some small modifications to the way the shock is applied. However, EIOPA will publish the stressed IRR curves so there should be little disruption to firms from an operational perspective.
- EIOPA's proposals will create a greater alignment between IM firms and SF firms, but may put further pressure on IM firms which do not currently allow for negative rates to incorporate these into their model development plans.

EY comparison of IRR curves

- The charts below compare the SII RFR spot yield curves (at year end 2018) under normal conditions ("SII RFR") and IRR stressed conditions on the current SII SF calibration ("Current SII [up / down] stress") and the proposed revised SII SF calibration where the Euro LLP remains at 20 years ("Revised SII [up / down] stress (20yr LLP)"). For comparison, we have also shown the respective unstressed and stressed ICS spot yield curves.
- The revised SF down stress is significantly stronger than the current SF calibration at all maturities, whilst the revised SF up stress is significantly stronger than the current SF calibration from shorter to medium term maturities. It should be noted that EIOPA proposes different revised IRR shocks depending on whether the Euro LLP is increased from 20 years to 30 or 50 years (see page 5) – the revised SII IRR shock is stronger under a 50 year LLP than compared to a 20 year LLP.
- It can be observed that the ICS RFR curve is broadly consistent with the current SII RFR curve and the ICS up / down stresses are generally different to the proposed SF stresses (although broadly similar for long maturities under the Euro).
- These charts emphasise that SF firms exposed to IRR are likely to be impacted regardless of the maturity profile of their business (i.e. SF firms with shorter or longer duration business will be impacted if exposed to IRR). The proposed impact is likely to be more significant for SF firms exposed to an interest rate down stress.





Topics under consultation

Solvency capital requirement standard formula (SCR SF) – other risks and correlation matrices

Summary of EIOPA proposals	EY insights / commentary
Spread risk: ▸ EIOPA advises not to modify the existing SCR spread risk sub-module. ▸ In EIOPA's (technical) view it is unnecessary and even unwarranted to introduce a separate, long term treatment of insurance and reinsurance undertakings' investments in fixed income assets, beyond the current, long term calculation of the spread risk charge of assets contained in MA portfolios.	▸ EIOPA's view appears to be that the current spread risk calibration is weak, but it does not appear to have a strong desire to challenge the EC to strengthen it. ▸ This perceived weakness will be familiar to many internal model (IM) firms, where some supervisors have pushed firms to stronger calibrations than what their models had suggested. Firms developing IMs should be aware of the regulator's perceptions of weakness in this calibration.
Property risk: ▸ EIOPA proposes no change, given the scarcity of data. ▸ It proposes to continue its analysis, but is not in a position to provide the European Commission with definitive advice for a change.	▸ EIOPA acknowledges that there are different property markets throughout Europe, and that there is a market view that the calibration using only UK data might be overstating volatility in other markets. However, the relatively low diversity of property portfolios and the scarcity of data means it is unable to justify a more geographically granular calibration. ▸ There is the potential for future granularity in the calibration, but it remains to be seen how EIOPA would manage the divergence from "pan-European" approach and investment incentives that such granularity would create.
Correlation matrices: ▸ EIOPA proposes no change. In particular, EIOPA advises that no correlation should be introduced between market risk and lapse risk.	▸ EIOPA has mainly considered market risk correlations, noting the scarcity of appropriate data for non-market correlations. ▸ Whilst EIOPA notes that an empirical market risk SCR (based on CEIOPS 2010 methodology) is higher than the SCR implied by the current correlations, it believes that this is mainly a result of a weak interest rate calibration, rather than a weakness in the correlations.
Counterparty default risk: ▸ EIOPA proposes an additional optional simplification for the computation of the risk mitigating effect of derivatives, reinsurance arrangements, special purpose vehicles and insurance securitisations. ▸ EIOPA proposes that the hypothetical SCR for the fire, marine and aviation risk, for the purpose of determining the risk-mitigating effect in the counterparty default risk module should be based on the largest gross (rather than net) risk concentration for the fire, marine and aviation risk. ▸ EIOPA proposes to amend article 189(3) such that default and forborne loans are included in the type 2 exposures, with LGD = 6.67 * max(Loan – Recoverables, 36% * Loan). ▸ EIOPA proposes additional text in article 192(4) which would allow partial guarantees to include cases where the guarantor requires the insurance or reinsurance undertaking to first pursue the obligor itself.	▸ EIOPA's proposal extends the current simplification in article 107 for derivatives only to be applicable to other counterparty risks, which may be a welcome simplification for some firms ▸ EIOPA's proposal addresses potential anomalous results where there are multiple reinsurers for the fire, marine and aviation risks. ▸ For many firms these changes are unlikely to be particularly controversial or material, as they introduce simplifications and / or correct anomalies. However, the impact will depend on the specific facts for each firm.
Underwriting risks: ▸ EIOPA has assessed the calibrations for the SLT health underwriting risk and SLT health lapse risk sub-modules, and has advised that no change is required.	▸ Although one NSA provided some data as an argument against the current pan-European 40% SLT health mass lapse risk, it is perhaps little surprise that EIOPA does not consider this to be sufficient data to change the calibration. ▸ 6 classes standard deviations were updated in the non-life and NSLT health premium and reserve risk charges announced by EIOPA on 6 July 2019. These will apply from 1 January 2020.
Catastrophe risk: ▸ EIOPA proposes no change.	▸ The calibration of NAT CAT risks was outsourced to specific model vendors, reinsurance brokers and (re)insurers to access additional expertise. ▸ It was deemed too early for EIOPA to assess the materiality of an alternative calculation but this could be carried out from 2020.

Topics under consultation

Solvency capital requirement standard formula (SCR SF) – risk mitigation techniques / external ratings / transitional on government bonds

Summary of EIOPA proposals	EY insights / commentary
Risk mitigation techniques: ▸ Following representations to recognise certain forms of non-proportional reinsurance in the SF, EIOPA has engaged in intensive dialogue with stakeholders on non-proportional reinsurance, adverse development and finite reinsurance covers. EIOPA's analysis showed that the proposals from stakeholders would allow for cases of underestimation of the real risk and considers it is important to properly address this policy issue in methodological terms. ▸ EIOPA proposes no changes, but invites stakeholders to provide further input to enable it to make any recommendations. ▸ EIOPA notes that capital contingent or contingent convertible bonds cannot be recognised in the current structure of the SF. The transfer of risk is non-existent or limited and a proper modelling is not possible with the fundamental structure of the SF: the contingent capital operation does not necessarily cover a risk accounted for in the SF and when an event triggered, it has no P&L impact for the insurer. As a consequence, EIOPA advises not to recognize these instruments as risk mitigation techniques and thus they could not be used to reduce the SCR. This non-recognition under SF could potentially create some inconsistency between SF and IMs.	▸ Whilst EIOPA notes that non-recognition of certain risk mitigation techniques could potentially create some inconsistency between the SF and IM approaches, if anything it is proposing to strengthen the wording to ensure that risk mitigation is only taken into account where the SCR / own funds benefit is commensurate with the extent of risk transfer. ▸ EIOPA considered a previous proposal to recognise specific types of non-proportional reinsurance via a formula to be applied in the premium and reserve risk sub-module. The outcome for adverse development covers and finite reinsurance covers was similar to previous advice where they identified that under-estimation of the SCR was still a possibility. ▸ The only case where this was not a risk was for mono-line insurers. EIOPA concluded that it would not be appropriate to change the recognition in the SF only for the benefit of these companies. ▸ Firms are asked to provide other proposals, otherwise they will need to consider the existing undertaking specific parameters or IM framework if they wish to make more specific allowance for such covers. Some firms seeking recognition of a wider selection of risk mitigation techniques which are not currently allowed for may be disappointed by EIOPA's proposals.
Reducing reliance on external ratings: ▸ EIOPA proposes no changes, but proposes to open an analysis table to investigate how the new alternative credit assessment methods could be tailored to some specific rated exposures and under a standard methodology.	▸ Given that the SII Delegated Acts has provided firms with the "internal assessment approach" and the "internal model approach" to assess credit risk for unrated debts, it is not surprising that EIOPA does not propose any changes.
Transitional on government bonds: ▸ Government bonds not denominated in local currency are subject to a phase-in of SF SCR stress factors for spread risk (article 180(3) of the SII Delegated Acts) and concentration risk sub-module (article 187(4) of the SII Delegated Acts). ▸ EIOPA proposes not to further extend the transitional measure.	▸ Given that undertakings are prepared for the expiration of the transitional, it is not surprising the EIOPA does not propose any changes. ▸ This is not expected to be a material issue for most firms, particularly for larger firms where many have IMs and may have sovereign bond risk capital charges included within their model.

Minimum capital requirements (MCR)

Summary of EIOPA proposals	EY insights / commentary
▸ Despite reservations that the floor and caps can undermine consistency with a 85% value at risk measure, EIOPA proposes to keep the current 25% to 45% corridor. ▸ For a limited number of non-life risk factors set out in Annex XIX of the SII Delegated Acts, EIOPA proposes some changes due to updates to the SF distributions in 2018 (and an apparent error in the CEIOPs calculations).	▸ For a majority of (mostly larger) firms, there will be no material impact from these changes. However, non-life firms will need to update the factors and there may be some case specific impacts.

Topics under consultation

Reporting and disclosure

Summary of EIOPA proposals

12 July 2019 consultation paper (CP):

- EIOPA released a CP on 12 July 2019 which we have summarised in this report for reference. Please note that the consultation period for the July CP closed on 18 October 2019.
- The July 2019 CP covered the following areas, which are not revisited in the 15 October 2019 CP:
  - General issues on reporting and disclosure.
  - Individual quantitative reporting templates (QRTs).
  - Solvency and financial condition report (SFCR).
  - Financial stability reporting.
- The most notable proposals in the July 2019 consultation were:
  - Annual QRT deadline pushed back from 14 to 16 weeks.
  - Q4 quarterly reporting retained.
  - Introduction of core QRTs without risk thresholds and non-core QRTs with risk thresholds.
  - Some new QRTs introduced: cyber risk, additional look-through for alternative investment funds and new non-life product information.
  - S.06.02 (list of assets) – additional fields (ESG compliant / sustainable investments, regional and local government guarantees, assets linked to cryptocurrencies, custodian LEI) and amendments to CIC codes and definitions for bonds.
  - Variation analysis (S.29): replacement of all current QRTs with S.29.05 (life) and S.29.06 (non-life) analysing movements in technical provisions.
  - Dedicated SFCR sections for "professional public" and policyholders.
  - The merging of the risk profile section with capital management section in the "professional public" version of the SFCR.
  - Some disclosures to be moved from the SFCR to the RSR (e.g. detailed governance information).
  - New standardised QRTs / tables to show SCR sensitivities and own funds movements from prior year.
  - Proposal to include EU wide audit requirement of the SII balance sheet in the SII Directive.
  - Reduced reporting by captive insurers.

EY insights / commentary

- Now that both the July 2019 and October 2019 CPs on pillar 3 reporting have been published, stakeholders will have the opportunity to consider the full extent of the proposed changes. These appear to be very extensive in relation to both the QRTs and narrative reporting.
- EIOPA will set out its advice on the topics covered in the July 2019 CP in the final opinion on the 2020 review of SII.
- EIOPA will carry out voluntary field testing of the new proposed QRTs, e.g. cyber risk and alternative investment funds.
- It was noted in the EIOPA public event on 30 September 2019 that the current instructions included in the Annexes to the CP with respect to some of the new requirements were not particularly clear. EIOPA agreed and undertook to ensure that clear instructions were drafted.
- Some stakeholders are likely to be reluctant to disclose SCR sensitivities and own funds movements in the SFCR (notwithstanding that it is already a requirement under the current rules).
- Specific details of the scope of the EU audit are yet to be determined.
- Some stakeholders in countries where there is currently no audit requirement are likely to be concerned as regards the additional burden that an SFCR audit requirement will introduce.

Please also see comments included on slide 20 regarding Pillar 3 proportionality.

Summary of EIOPA proposals

15 October 2019 CP:

Regular Supervisory Reporting (RSR):

- The minimum requirement for submission of a full RSR remains unchanged at three years.
- EIOPA proposes to improve both the structure and the content of the RSR (see annex 7.1):
  - Some information identified as "static information" for which focus should be on reporting material changes. EIOPA will develop proposals for the frequency of reporting full information.
  - The merging of risk profile section with capital management section consistent with the change in SFCR format (as mentioned above).
  - Some disclosures will be moved from the SFCR to the RSR: detailed governance information and ORSA information (section B); information on capital management policies (section D).
  - Valuation for solvency purposes (section D): concrete examples to be provided on valuation information to be provided in addition to that provided in the SFCR, including: material deferred tax assets; the use of simplifications; the approach to the calculation of material reinsurance recoverables; and a description of material off-balance sheet items.
  - Capital management (section E): removal of overlaps with the ORSA.

EY insights / commentary

- The changes now proposed for the RSR include a number of rationalisations to remove repetition with information already provided in the SFCR but there does not appear to be a significant reduction in the amount of information required.
- Stakeholders are likely to welcome clarification with concrete examples of valuation information to provided in Section D, however the additional disclosure requirements appear quite onerous.

EY

Topics under consultation

Reporting and disclosure (cont'd)

Summary of EIOPA proposals

15 October 2019 CP:
Group reporting:

- Group QRTs will be amended in line with solo changes in the July 2019 CP.
- There are also some proposals for specific group QRTs, with some being deleted, some clarified and new information required in others. More significant proposed changes are:
  - S.05.01 (premiums claims and expenses by line of business) – deleted at group level.
  - S.06.02 (list of assets) - amendment of "issuer code" instructions with respect to investments issued by group entities to achieve consistency with entities in the scope of the group reported on S.32.01.
  - S.23.01 (own funds) – changes may follow after any revision of the SII Directive and Delegated Acts, in particular with regard to classification and availability of own funds.
- On the group SFCR, EIOPA proposes to make changes in line with those proposed to the solo SFCR, other points worth noting are:
  - No proposal to introduce a separate policyholder section of group SFCR.
  - Proposal to include EU wide audit requirement (of the SII balance sheet only) in SII Directive (consistent with solo SFCR).
  - Requirement to translate summary into languages of member states where any insurer or reinsurer has a head office removed.
  - No changes to group SFCR QRTs.
  - Extend the deadline of the group SFCR by 2 weeks to accommodate the proposal for audit of the SII balance sheet, i.e. from 20 to 22 weeks.
  - Single group SFCR: policyholder section to be published to solo SFCR deadline and "professional public" section to be published to group deadline.
- No proposal to permit preparation of a single group RSR.

EY insights / commentary

- Group specific QRT changes do not appear to be too onerous, however the details will need to reviewed and further considered by groups.
- Stakeholders are likely to welcome deletion of S.05.01 (premiums claims and expenses by line of business) at group level, but may be disappointed that S.05.02 (premiums, claims and expenses by country is not deleted as well.
- The specific details of the scope of the EU group audit requirement are yet to be determined. Some stakeholders in countries where there is currently no audit requirement are likely to be concerned on the additional burden that this audit requirement would potentially introduce.
- Groups that publish a single group SFCR may disappointed that it is not proposed to also permit the preparation of a single group RSR.

Other new disclosures:

- Additional new disclosures are proposed in relation to the following sections of the 15 October 2019 CP:
  - Volatility adjustment (section 2.4) .
  - Risk management provisions on LTG measures (section 2.7).
  - Expected profits on future premiums (section 3.1).
  - Extrapolation of the risk-free rate (section 2.2): impact of changes of last liquid points / first smoothing points on financial position.
  - Disclosure on LTG measures (section 2.8).

EY insights / commentary:

- Stakeholders will also need to consider these additional disclosure requirements when determining the full extent of the pillar 3 reporting changes impacting on their firm / group, with the impact also being dependent upon the result of the consultation in those areas.

Topics under consultation

Proportionality – thresholds for exclusion from SII / pillar 1 / pillar 2 / pillar 3

Summary of EIOPA proposals	EY insights / commentary
Thresholds for exclusion from SII: ▸ EIOPA proposes to double the technical provisions threshold for identifying whether a firm is excluded from SII from €25m to €50m. ▸ EIOPA also proposes to allow member states to set an appropriate threshold for premium income between €5m and €25m (vs the current level of €5m).	▸ EIOPA explicitly reinforces that the "proportionality principle is one of the overarching principles of Solvency II framework" and acknowledges that part of the market is unsatisfied by how it has been implemented by national supervisory authorities – which is evident in the public comments made by several stakeholders in advance of the publication of this consultation.

Proportionality – pillar 1:
▸ EIOPA notes that simplifications are already embedded in technical provisions calculations. EIOPA has asked stakeholders to provide concrete proposals if they feel further simplifications are required.
▸ Two options are being considered for simplifying the SF SCR for immaterial risks:
  ▸ Simplifying at individual risk level for immaterial risks, as long as the resulting capital is "at least the size of" and "not too far from the original capital requirement".
  ▸ A more integrated approach which assesses which risks are immaterial in terms of contribution to the BSCR; a simplified contribution is introduced for future calculation, for example rolling forward from one period to the next with some prudence factor; the simplified calculation is assessed against an accurate calculation periodically.
	▸ EIOPA is reluctant to introduce specific quantitative measures beyond those already included, noting that a one-size-fits-all approach is unlikely to be appropriate and that a more risk-based approach should be adopted.
	▸ The options under consideration for simplifying the SF SCR for immaterial risks is likely to be welcomed by those SF firms which will be impacted by this – EIOPA has called for feedback on the two options under consideration. The two options under consideration for immaterial risks require an assessment of the simplified approach against the more accurate, which appears to mean that firms would need to perform the more accurate calculation anyway (and therefore leads to the question of whether the simplification reduces the burden significantly or not).

Proportionality – pillar 2:
▸ EIOPA proposes to improve the proportionality of governance requirements, in particular on key functions, the own risk and solvency assessment (ORSA), written policies and the expectations of boards.
  ▸ In the ORSA, the assessment of deviation from underlying SCR assumptions needs only to be performed every two years (currently assessments are required on an annual basis).
  ▸ The ability to combine certain key functions.
  ▸ Reviews of certain policies (e.g. risk management, internal control) can be undertaken every three years (currently reviews are required on an annual basis).
	▸ In cases where the risk profile does not change significantly, assessing deviation from underlying SCR assumptions every two years may avoid significant workload for insurers, especially smaller ones.
	▸ EIOPA proposes to explicitly permit combining: key functions; a key function and an operational role; a key function and an AMSB role; provided the insurer demonstrates there are no conflicts of interest.
	▸ Board composition, effectiveness and governance have been under scrutiny from supervisors. EIOPA's proposal does not include specific instructions on these topics, but advises regular assessment of the board, in order to respect proportionality principles.

Proportionality – pillar 3:
▸ 12 July 2019 CP: EIOPA proposes the following in order to improve the proportionality in reporting and disclosure of SII framework:
  ▸ Quarterly reporting and exemptions of items in articles 35(6)-35(8) of SII Directive retained.
  ▸ Reinforce risk-based thresholds to increase proportionality while ensuring legal certainty: introduction of core QRTs without risk thresholds and non-core QRTs with risk thresholds.
  ▸ Quarterly reporting package reduced: simplification of S.08.01 (open derivatives), deletion of S.08.02 (derivatives transactions) for quarterly reporting; simplification of S.12.01 (life and health technical provisions) and S.17.01 (non-life technical provisions) by deleting transitional information.
  ▸ Separate policyholder SFCR and more focussed professional user SFCR.
  ▸ Reductions in annual reporting package (in EIOPA's view).
▸ 15 October 2019 CP: EIOPA proposes to allow for the exemption of group reporting without the condition of exemption of all the solo undertakings belonging to that group.
	▸ Whilst stakeholders generally welcome simplifications, some stakeholders have raised concerns about the number of changes that EIOPA is proposing as all changes will result in systems changes. Stakeholders who have invested heavily in developing systems to facilitate SII reporting would largely prefer minimal changes.
	▸ Some stakeholders may consider that any benefit from simplifications to the current QRTs is outweighed by the introduction of additional QRTs on cyber risk, alternative investment funds (S.06.04) and non-life product information.
	▸ Regarding the retention of Q4 reporting, some stakeholders remain concerned around the level of overlap between Q4 and annual reporting.
	▸ Where quarterly exemptions apply, the requirement to report MCR is still considered burdensome by some stakeholders as a supporting SII balance sheet needs to be prepared.

Topics under consultation

Group supervision

Summary of EIOPA proposals

- EIOPA has made several proposals aimed at achieving greater consistency of application of group supervision and addressing areas that are currently either unclear, insufficiently defined or otherwise not operating correctly. Often these are definitional, where different interpretations have led to different approaches.

- **Group definition:** the definition of the group for supervisory purposes is proposed to be extended, to capture de facto groups and clarify the scope of supervision in particular cases, with more prescriptive guidance in certain areas of judgement (e.g. the test for insurance holding companies, and criteria for exclusion from scope).

- **Group supervisory powers:** EIOPA proposes enforceable powers for group supervisors over holding companies, something that not all countries currently provide, and the ability to require changes to the group structure.

- **Non-equivalent third-country groups:** the 'other methods' provision for supervision of non-equivalent third-country groups is to be supported by more precise text.

- **Group solvency calculation:**
  - EIOPA proposes changes and clarifications to both Method 1 and Method 2, introducing a notional capital requirement for holding companies, providing clearer indication of how either Method 2 or a combination of methods is to be applied, and extending some provisions (which at present apply only to insurance or reinsurance undertakings) to apply also to other group members when included in the regulated group.
  - On the other hand EIOPA does not propose changes to the calculation of the minimum consolidated group SCR to address the problem of trigger inversion (MCR biting before SCR at group level), but proposes to add notional MCRs for holding companies to the minimum consolidated group SCR to take account of risks in those entities.

- **Other financial sector (OFS) treatment:** EIOPA proposes amendments to the treatment of OFS group members, requiring tiering of their own funds and assessment of transferability of their own funds, and making clear that their contribution to group SCR must include all buffers and add-ons. EIOPA also proposes to remove some interactions with the Financial Conglomerates Directive (FICOD) that have caused confusion or inconsistency.

- **Group governance:** greater clarity is proposed for the application of group governance requirements.

EY insights / commentary

- Overall, greater consistency in application is likely to be welcomed by firms, though some groups may face challenges under these proposals and outcomes may not always be appropriate. Some existing difficulties remain, notably trigger inversion for MCR, and applying sectoral rules for OFS entities.

- **Group definition:** the proposals would capture more group structures, and more entities, than at present. Some groups may have to restructure their capital and governance – for example if the current group perimeter stops below a debt vehicle, if two entities are effectively leveraging the same capital but are currently not consolidated, or if a classification of mixed activity is no longer valid. The impact on groups with more than one platform needs to be studied.

- **Group supervisory powers:** the proposals for enforceable powers over parent entities raise practical questions where the parent entity is in a different country – maybe even one with no group (re)insurance undertaking, so that country's regulator is not currently involved. It is also unclear how in practice the proposed requirement would read across to third-country groups where the group supervisor applies SII under article 262(1)(a). Some groups may find they would need to deal with more regulators.

- **Group solvency calculation:**
  - The removal of anomalies in the group own funds and SCR calculations is welcome, but there is a risk of unintended consequences, such as distortion of the attribution of capital (and therefore transferability) through double-counting of risks. EIOPA proposes an explicit principle in the SII Delegated Acts that there should not be double counting of risks – a significant clarification for participations in group entities under Method 2. It is not clear though whether that will apply to the notional SCR now proposed for parent undertakings, and that is important to clarify.
  - Also, EIOPA recommends not only retaining the current calculation for the minimum consolidated group SCR (straight sum of MCRs, with no adjustment for double-counting of risks) but also adding notional MCRs for holding companies. This would seem to make trigger inversion arising from double-count more likely and may disappoint affected groups.
  - The proposal for clearer guidance on applying Method 2 or a combination of methods is welcome, as some firms consider the current text to be neither clear nor intuitive. So far as concerns the combination of methods, EIOPA confirms that this means a consolidated core, and that consolidated sub-groups (except for cross-sector ones) cannot be added on a Method 2 basis.

- **OFS treatment:**
  - EIOPA recognises that problems remain with the treatment of OFS group companies under SII, even after the amendments to the SII Delegated Acts in 2019. It seems likely though that some groups will still face the difficulty of applying 'sectoral rules' implying a regulator's capital review; EIOPA appears to assume that there will always be a regulatory capital review, but that is not the case for an unregulated entity to which OFS rules must be applied.
  - EIOPA's proposal to require consideration of transferability of own funds in OFS entities means SII is catching up with FICOD. Some groups may need to consider how their capital is distributed. It is less clear how the proposed requirement to classify own funds arising in other financial sectors into SII tiers will work in practice, given the precision of tier conditions.
  - Removing some FICOD references and associated options may help groups to identify and apply the right rules and methods. Those that use FICOD methods now may need to request waiver of SII rules in order to avoid having to do both FICOD and SII calculations.

Topics under consultation

Freedom to provide services and freedom of establishment

Summary of EIOPA proposals

- EIOPA comments on observed incidents indicating a need for strengthening of collaboration between supervisory authorities and prevention of arbitrage.
- Additional context is provided by existing proposals (as part of the review of European Supervisory Authorities) for new articles in SII providing for initial notification by the home state supervisor where an applicant for authorisation plans to operate cross-border, and for either EIOPA or the supervisors concerned to have the right to initiate a 'collaboration platform' (similar in some respects to a group supervisory college).
- EIOPA proposes adding a specific requirement for an applicant for authorisation to disclose previous rejected or withdrawn applications.
- Cooperation between home and host supervisors is proposed to be strengthened, with a clear requirement for active cooperation with host supervisors in the supervisory review process, and notification when cross-border activities change materially or when home or host supervisors have prudential concerns (when EIOPA would also be informed).
- An enhanced role is proposed for EIOPA when home and host regulators are unable to agree, with EIOPA able to make recommendations, reporting publicly if the supervisors' response is inadequate.

EY insights / commentary

- The proposed obligation to disclose previous rejected or withdrawn applications in other member states may help alert national supervisors to attempts to secure regulatory arbitrage by seeking authorisation in one country with a view to writing predominantly in another, though since authorisation must be sought in the applicant's home state the impact may be limited. More consistency in interpretation would itself tend to limit incentives for arbitrage.
- EIOPA's other proposed changes indicate a greater role for both host state regulators and EIOPA, in areas traditionally reserved to the home state regulator. Whilst host state supervisors already have a duty to blow the whistle, the strengthening of these requirements suggests that home / host state interaction will be more routine than has typically been the case.
- Host state regulators will have greater visibility of business written into their state on a services basis. Firms may experience more interaction with host state supervisors as a result, and home state supervisors may feel less able to apply a lighter touch, knowing that they may be challenged by EIOPA. Firms may discover that some jurisdictions are more demanding in terms of head office substance in terms of its operations.
- For some types of business (for example, specialty business), blanket permissions under the freedom to provide services have been typically sought in case they are needed. Firms may need to be more selective about the permissions that they request because of the need for host state supervisor involvement.
- In the case of reinsurance, EIOPA's proposed changes may give supervisors of cedants a greater role in the supervision of reinsurers, due to the approach in some countries, which has also been articulated by the European Commission, that reinsurance is conducted where the cedant is, even if the reinsurance activity is entirely offshore.
- The advent of cooperation platforms and a role for host state supervisors in prudential supervisory review is likely to increase the cost burden of supervision overall.
- Overall, the move to greater involvement of host state supervisors appears to change the landscape for cross-border insurance in the single market.

Topics under consultation

Macro-prudential policy

Summary of EIOPA proposals

- EIOPA has been working towards Introducing tools to address systemic risk in the insurance sector for some time. It is proposing to do this by adding a general article to the SII Directive, rather than via separate legislation, to achieve consistency and coherence with the micro-prudential approach.
- EIOPA proposals build strongly on earlier EIOPA work regarding systemic risk and macro-prudential tools for the insurance sector, which has included the publication of various papers and consultations through 2018 and 2019.
- EIOPA notes that SII already includes some tools with macro-prudential impact, e.g. the long term guarantees measures and measures on equity risk.
- EIOPA proposes the following additional measures:
  - National supervisory authorities (NSAs) should have the power to set a capital surcharge to address activity-based, entity-based or behaviour-based sources of systemic risk. EIOPA will develop draft implementing technical standards or guidelines as to when these should be imposed or removed.
  - NSAs should have the power to define soft thresholds for action at market level if an exposure increases dramatically.
  - The ORSA and the prudent person principle will be changed to explicitly include macro-prudential concerns.
  - NSAs can require systemic risk management plans and all firms should be required to draft liquidity risk management plans, unless they obtain a waiver.
  - NSAs to be given power to impose a temporary restriction on surrender rights for policyholders.

EY insights / commentary

- EIOPA follows the IAIS in considering 3 sources for systemic risk in insurance: entity-based, activity-based and behaviour-based. This is consistent with International Monetary Fund (IMF) work on "domino view" (the failure of individual institutions and subsequent contagion) and "tsunami view" (shocks propagated or amplified even by solvent institutions). The proposed framework shall address all 3 sources of systemic risk.
- The proposal for NSA's to have the power to impose temporary restrictions on surrender rights for policyholders could potentially require a shift in legal basis for certain countries (e.g. the UK).
- Each proposed measure is linked to an operational objective, e.g. limit implication in certain activities, or discourage herding behaviour.
- EIOPA proposals are consistent with:
  - Existing measures in the banking sector (e.g. capital surcharge to account for systemic risk), even if EIOPA rejected other components of the banking sector framework, for instance countercyclical buffers, which are not deemed necessary since SII already includes countercyclical tools.
  - Financial Stability Board requirements for Global Systemically Important Insurers such as: recovery and resolution planning, systemic risk management plans and liquidity risk management plans.
  - Measures in place in certain member states, e.g. Italian insurers are already required to take economic conditions and macro-prudential concerns into account in the ORSA; French insurers are already subject to the possibility of temporarily restricting surrender rights.
- Further work is required in order to identify criteria for certain measures (e.g. scope of firms subject to systemic risk management plans) and develop guidelines (e.g. how should concentration limits be implemented, how can relevant macro-prudential information from the ORSA be extracted and used by supervisors).

Topics under consultation

Recovery and resolution

Summary of EIOPA proposals

- Following EIOPA's previously expressed concerns over the lack of harmonisation on recovery and resolution practices among member states, it proposes that a recovery and resolution framework should be established. This addresses several concerns raised by national supervisors:
  - Fragmented recovery and resolution regimes across the EU.
  - Limits to national frameworks, powers and tools available for national authorities. As a consequence, most recovery and resolution regimes in the EU for insurance do not fully meet the Financial Stability Board's key attributes for an effective resolution regime.
  - National regulations are emerging and help to reinforce resolution powers, but the lack of EU co-ordination increases the risk that application is inconsistent and inefficient.
- In this context, the proposed approach consists of minimum harmonization at EU level, whilst allowing member states to adopt additional measures at the national level.

- EIOPA believes that SII should be supplemented with a requirement for undertakings to develop and maintain recovery plans in a pre-emptive manner. To address those concerns, EIOPA is proposing these actions, among others:
  - In each member state, insurers representing a high proportion of the market should be required to develop a recovery plan.
  - Early intervention powers for NSAs should be enhanced, including additional or more frequent reporting and implementation of actions in the recovery plan.

- EIOPA believes that there should be an officially designated administrative resolution authority in each member state.

- EIOPA believes that the following resolution powers for NSAs should be introduced:
  - Prohibit bonus payments to senior management.
  - Withdraw the licence to write new business and put all or part of existing business into run-off.
  - Sell or transfer shares, assets and / or liabilities to third parties (potentially including the creation of a "bridge institution" to transfer them into).
  - Restrict the rights of policyholders to surrender policies.
  - Suspend payments to unsecured creditors.
  - Take control of the entity.

- EIOPA believes that judgement-based triggers for resolution should be introduced at EU level.

- Regarding triggers for supervisor intervention, EIOPA suggests:
  - Soft triggers (both quantitative and qualitative) for early supervisor intervention.
  - Entry into recovery when the SCR ratio falls under 100%, consistent with EU supervisors view. This does not address cases where recovery may be needed following a liquidity crisis, although these situations may be marginal.
  - Soft triggers for the entry into resolution, based on:
    - The insurer not being viable any more (or likely to become so) with no reasonable prospect of recovery.
    - Exhaustion of possible recovery measures.
    - Resolution action necessary in the public interest.

EY insights / commentary

- Recovery and resolution planning is at different stages across Europe, with some countries such as Romania and the Netherlands having a resolution authority with extensive powers and others with a framework that recommends recovery and resolution plans only.

- The introduction of recovery and resolution plans across Europe will have an increased cost to firms in production and maintenance of these plans.

- By defining the recovery and resolution framework by market share, many of the larger insurers such as the Global Systemically Important Insurers already have a recovery and resolution plan in place, therefore it is unclear how many additional insurers this proposal would apply to in reality.

- The proposals are unclear whether there will be standardised format to recovery and resolution plans across Europe and also the structure of the NSAs powers if this were to be enforced. EIOPA has previously been reluctant to prescribe powers ordinarily reserved for national governments, however the proposals contained in the CP are more far-reaching than previously.

- Operational resilience will be a core component of both recovery and resolution planning, ensuring that critical functions are appropriately considered in the context of continuity of service and mitigating actions.

- Firms may wish to consider integrating recovery and resolution plans with supporting frameworks such as the risk appetite framework, governance structures, liquidity risk management plans, systemic risk management plans and capital management plans, in order to embed these frameworks in the business.

EY

Topics under consultation

Insurance guarantee schemes (IGS)

Summary of EIOPA proposals

- EIOPA's proposals on IGSs were contained in a separate consultation, on which the response period ended on 18 October 2019.
- EIOPA believes that every member state should have an IGS in place for the protection of policyholders in the event of a failure of an insurer, and that such IGSs should meet a minimum set of harmonised features, but with flexibility in order to avoid excessive burdens on insurers and member states.
- EIOPA's proposals may be summarised as follows:
  - Role and function: IGSs in member states should concentrate on compensating policyholders and / or ensuring continuity of coverage, swiftly when insurers fail.
  - Geographical coverage: EIOPA proposes that the home-country principle should apply to IGS.
  - Eligible policies: the IGS should cover at least life and non-life policies meeting prescribed criteria, aiming at a minimum to cover policies which would cause considerable financial or social hardship to policyholders where an insurer has failed and/or lines of business with a high market share in cross-border business in Europe.
  - Eligible claimants: the IGS should cover natural persons in addition to micro- and small-sized legal entities. coverage restrictions to exclude persons close to the failed insurer should be introduced.
  - Coverage level: there should be a minimum harmonised coverage level.
  - Funding: IGSs should be funded adequately on an ex-ante basis and if required, by ex-post funding. Member states should ensure adequate funding systems are in place.
  - Disclosure: there should be requirements for adequate, clear and comprehensive disclosure about the IGS protection to consumers and policyholders.
  - Cross-border cooperation and coordination: national IGSs should cooperate including on payment of entitlements on behalf of other member states' IGSs.

EY insights / commentary

- Overall, industry could view most of the proposed principles as reasonable but the main challenge will come in designing workable minimum schemes.
- The EIOPA CP makes clear that there is currently a wide range of approaches and levels of coverage across member states. It proposes a principles-based framework to shape the core criteria for the design and operation of IGSs.
- EIOPA's advice on IGSs may increase coverage and consistency for policyholders across jurisdictions. However, given the 'minimum harmonisation' nature of EIOPA's proposals, there is a risk that jurisdictions may approach the requirements differently, which could lead to differential treatment between jurisdictions. For example:
  - Different jurisdictions may choose different levels of coverage, in excess of the minimum thresholds or triggers proposed by EIOPA.
  - The home country principle combined with minimum harmonisation principle means that policyholders' protection will be dependent on where their insurer is headquartered; this may encourage some form of arbitrage and raises important disclosure issues at the point of sale, depending on different jurisdictions' approaches to coverage or funding.
  - Insurers may seek to pass on the cost of coverage as an explicit surcharge to policyholders, potentially raising competition issues.
  - Levies that are based on premiums or technical provisions can involve a moral hazard as firms with more aggressive pricing or reserving represent higher risk of failure but pay less.
  - Despite reference to the proportionality principle, these requirements may be more onerous for countries with less developed insurance sectors.
- Where jurisdictions do not already have an IGS in place, introducing one involves additional costs of business and therefore greater barriers to entry. Where IGSs do currently exist, modifying them to conform to new minimum requirements may be costly and involve lengthy transitional periods.
- While there are potential practical issues arising from ex-post funding, EIOPA's advice to fund IGS on an ex-ante basis raises the prospect of creating a large pool of assets that is not deployed efficiently. Whilst this may be appropriate in smaller markets, large markets should be sufficiently resilient to individual failure and ex-ante funding could be an unnecessary dead weight cost for these businesses.
- EIOPA raises questions on whether funding contributions should be risk-based. Risk-based levies would reward companies that are well capitalised and penalise those that were not, potentially mitigating moral hazard (though also potentially exacerbating national differences).
- The cross-border cooperation proposal means that national schemes will be settling on each others' behalf. In some countries this will be a substantial amount of claims and "headquarter" countries will have net outflows, which could lead to calls for these countries' schemes to oversee what is being paid out to ensure there is not an uncontrollable agency problem. There may be practical issues that payers in one country will need to administer payments in line with the rules set by another country (which may not be well understood by the payer country).

Topics under consultation

Other transitionals

Summary of EIOPA proposals

- Article 308b sets out various "other transitional measures" covering reporting deadlines, recognition of Solvency I own fund items and some other matters relevant when SII was introduced. EIOPA proposes no changes to any of these.
- The only transitional considered in detail is article 308b(15), which covers exemption from SII of insurance business subject to article 4 of IORP. This has been extended from end-2019 to end-2022, by which time it is not expected to be used.

EY insights / commentary

- There should be limited impact from these proposals. Several of these measures are no longer relevant and EIOPA notes that there is extremely limited take-up of the others.
- Article 308b is used by entities in France and Slovenia to a limited extent and more widely in Sweden, but alternative arrangements are being introduced in all three countries which will end the need for this transitional before December 2022 (when it is currently defined to end anyway) so there will be no impact.

Fit and proper requirements

Summary of EIOPA proposals

- The recent peer review on fitness and propriety concluded that:
  - There is still a lack of harmonisation in the ongoing assessment of administrative, management or supervisory body (AMSB) and qualifying shareholders and the review recommended a number of national competent authorities (NCAs) to take action to avoid impediments in cross-border cases.
  - Propriety assessments of AMSB members and qualifying shareholders are completed as a one-off task with very few NCAs performing any ongoing assessment as part of their supervisory activities.
  - The compliance with the ongoing assessment requirement should be subject to supervisory examination in accordance with article 29 (which requires the NCAs to supervise the undertakings on a continuous basis and in a pro-active manner) and other related provisions of the SII Directive.
- As a result of the peer review on propriety:
  - 12 NCAs have received a recommended action to assure ongoing supervision of the propriety of AMSB in a risk-based and proportionate manner.
  - 25 NCAs are required to carry out, using a risk-based and proportionate approach, ongoing assessment of propriety of qualifying shareholders.
- Moreover, EIOPA is recommending amendments to the SII Directive to address the issues identified by the peer review.

EY insights / commentary

- The drive for a consistent application of fitness and propriety requirements across the EEA is expected to reinforce a level playing field between countries and avoid individuals or shareholders engaging in regulatory arbitrage.

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