ECON/Solvency II review: Questions to Commission ahead of the meeting on 27 October 2022

As a preamble, it has to be noted that Solvency II is a whole where the different pieces interact with each other (e.g. a change to the extrapolation methodology affects not only the best estimate of technical provisions, but also the risk margin, the interest rate risk submodule, and even the treatment of deferred taxes). It is therefore not possible for us, nor for EIOPA, to conduct in a short timeframe a multitude of simulations of the impact of the various changes.

Most quantitative assessments addressed to the Commission have in practice to be carried out together with EIOPA which has the ownership of the quantitative data. Please also note that the data allow assessing various impacts at reference dates end-of-2019 and mid-2020, which correspond to market environments different from current ones where inflation and interest rates are rising. Therefore, it is expected that changes on interest rates would have a lower impact under current market conditions than under 2020 conditions. However, absent new comprehensive data collection exercises, it will not be possible to provide quantitative assessments under the current market conditions. We generally refer to the Commission's impact assessment where the justification of key parameters has been explained.

Proportionality and Low-risk profile undertakings

- **Thresholds for the application of Solvency II: With a view to proposals to raise or to lower the application thresholds, an evaluation of the COM proposal and the various suggested changes is needed. What would be the implications in terms of the number of companies being covered under different scenarios (COM proposal/ draft report/ AMs by different groups/ Council GA)?**

The EP amendments imply various combinations of thresholds in relation to gross written premiums (GWPs) and technical provisions (TP) at both solo and group level. Our understanding is that the following ideas have been put forward:

	Solo GWP	Solo TP	Group TP
Current Directive	5 million	25 million	25 million
McManus (The Left)	Threshold defined by MS but lower than 25 million	25 million	25 million
Heinäluoma Fernandez Lalucq (S&D)	10 million	40 million	25 million
Commission	15 million	50 million	25 million
Hahn (The Greens) Yon-Courtin Boyer (Renew) Council General approach	15 million	50 million	50 million
Eroglu (Renew)	15 million	50 million	100 million
Rapporteur Zanni Grant Rinaldi (ID)	25 million	65 million	65 million

It is also our understanding that setting a fixed threshold of e.g. 25 million euros or allowing Member States to discretionarily set their thresholds with a ceiling at 25 million euros would have the same outcome. Indeed, as already the case currently, the fact that the Directive sets a threshold below which insurers are not expected to be in the scope of Solvency II does not preclude that Member States apply Solvency II to some or all of their insurers below the thresholds. From the 16 Member States that have insurance undertakings excluded from the scope of the Directive, 5 apply a regime similar to Solvency II but with some exemptions, 6 apply Solvency I and 5 have a regime different from Solvency I or Solvency II. **Finally, it has to be underlined that insurers that want to benefit from the single EU passporting will remain in the scope of Solvency II despite possibly being below the (revised) thresholds of exclusions.**

Based on EIOPA's inputs, we are able to provide the following overview of the various proposals (which are maximum values, as i) insurers which operate cross-border would continue being subject to Solvency II regardless of their size and ii) Member States can continue extending the scope of the Directive to some or all insurers below the (revised) thresholds):

- There are approximately 2441 firms in the scope of Solvency II
- Under currently applicable rules 261 firms are excluded (10,7 % of the firms currently in the scope of Solvency II)
- The Commission's proposal would result in474 firms excluded (19,4 % of the firms currently in the scope of Solvency II)
- Depending on the scenario chosen, the number of firms excluded would range from 390 firms (16 % of the firms currently in the scope of Solvency II; S&D's proposal) to 588 firms (24 % of the firms currently in the scope of Solvency II, Rapporteur's proposal)

You can find the full overview of the results and the country specific allocation in Annex 1. Beyond the question of the actual figure, it is important to have a clear view of what the policy choice is. The Commission's assessment is that Solvency II has overall worked well but that proportionality can be further enhanced. Therefore, the Commission proposal aims at avoiding excluding too many firms from the scope of the EU prudential framework and at the same time enhance proportionality for those firms that remain in the scope of Solvency II.

- **LRU definition: What would be the benefits and drawbacks of moving to a market share based size threshold?**

In line with EIOPA's opinion, the Commission proposals introduces a series of criteria to assess easily the eligibility as LRU. Those criteria rely on absolute thresholds in order to ensure a level-playing field in the Union.

Introducing a market-share based size threshold would imply that the same insurer would or would not be eligible as a low-risk profile insurer depending on the Member State where it has its head office. In other words, a small undertaking registered in a small Member State could be above the size threshold, whereas it would not be in a large Member State. This could result in regulatory arbitrage opportunities by incentivising relocations in large Member States.

Depending on other changes proposed by the Rapporteur, this could also raise issues of competitive advantages in smaller Member States. For instance, under the Rapporteur's proposal, an insurance undertaking can have 25% of its business cross-border (compared with the 5% threshold of the Commission proposal).

Take the following example:

- Consider two Member States: Member State 1 has a size of 88 000 M€ (of premiums); Member State 2 has a size of 500 M€ (of premiums)
- Company A is located in Member State 1. It has 1000 M€ of premiums among which 20% (200 M€) are in Member State 2
- Company B is a local insurer of Member State 2 with 100 of premiums.

Company A's market share at national level is far below the 10% threshold proposed by the rapporteur. Its cross-border activities represent only 20% of the total (less than the 25% proposed by the Rapporteur). Therefore, Company A is a LRU.
Company B, despite having no cross-border business and being much smaller than Company A, would not be a LRU because its market share in Member State B is 20%.
Therefore, in the small Member State 2, the local player Company B would have to compete with a much larger player which benefits from proportionality measures.

Such an undue competitive advantage would not occur under the Commission's proposal.

Note that during the Council negotiations, certain (smaller) Member States expressed concerns that too many insurers would qualify as low-risk profile because of the absolute size threshold. To address this concern, the general approach introduces a discretionary power for a supervisor to oppose the classification as LRU of an insurer if its national market share is above 5% (See Art. 29b(3) of the General Approach). This power is expected to be used only where too many insurers would otherwise be treated as LRU. **In our understanding, this criterion would ensure that in no Member State, there are more than 50% of insurers that qualify as LRU** (if the supervisor exercises its discretion not to grant the benefit of proportionality measure for insurers about 5%).

In addition, MS agreed to include a mandate for EIOPA to monitor the appropriateness and soundness of the LRPU criteria regarding policyholder protection, financial stability and level playing field (See Art. 52 (4) of the General Approach).

- **Captive insurance companies have a simple business model and few interdependencies. Does this justify a classification as LRU?**

The definition of captives, i.e. having policyholders only from the same corporate group, does not imply that captives have a simple business model or few interdependencies. In particular, a failure of a captive may affect employees of the entities of the corporate group and parties outside the captive's corporate group, notably beneficiaries or victims in the case of third-party liability insurance. Captives can also and often do access the reinsurance market directly without having to go through a supervised direct insurer. This can create interdependencies between the captive's corporate group and the wider reinsurance and insurance market. Against this background, it does not appear risk-based to classify captives *per se* as LRU.

Instead, it seems more appropriate to make the classification of captives as LRU subject to the risk-based set of criteria and it can be expected that many, if not most, captives will meet those criteria. Other captives can ask their supervisors to approve the use of proportionality measures according to the proposed Article 29d.

Moreover, regarding disclosure and audit requirements for captives, the Commission proposal takes into account the specificities of the business model. Hence, it excludes captives from disclosing the part addressed to policyholders and beneficiaries of the Solvency and financial condition report (SFCR) (Article 51 (4)). Please note that, while the Commission's proposal to exempt captives from the SFCR audit requirement is maintained in the Council General approach, a derogation is introduced to allow national supervisory authorities to extend the audit requirement to captives (See Art. 51a (2) of the General Approach).

Volatility adjustment: In the proposal the Commission deviated from the idea put forward by EIOPA. The reasons for this are not clear, could this be explained? Is there any information available on what the Council thinks about this? Can the Commission give (quantitative and qualitative) guidance on the implications of different models being proposed, such as a "quality overshooting adjustment" or an "illiquidity factor"?

The current volatility adjustment (currency VA) is calculated as the product of a general application ratio and the 'risk-corrected spread, where the general application ratio is set at 65% and the risk corrected spread is computed as a percentage of long-term average spreads. EIOPA is recommending the following four main adjustments:

- Addressing 'duration' overshooting (i.e. accounting for different durations of assets and liabilities) by introducing a reduction factor where the duration of assets is lower than the duration of liabilities – this ratio aims at avoiding situations where an insurer is 'better off' during crisis times due to unintended behaviours of the volatility adjustment;
- Reflecting the illiquidity of liabilities by introducing a reduction factor depending on how 'liquid' an insurer's liabilities. The more predictable and stable the liabilities, the lower the reduction;
- Improving the risk sensitivity of risk-corrected spreads by calculating it as a percentage of current spreads instead of a percentage of long-term average spreads.
- Because of the first three adjustments, EIOPA was proposing to increase the general application ratio from 65% to 85%.

The Commission proposal follows EIOPA's Opinion with the exception of the illiquidity factor. The choice to drop the illiquidity factor is explained in the Commission's impact assessment. You can find in Annex 2 the arguments for excluding the illiquidity factor in the Commission's proposal.

The Council supported the approach chosen by the Commission. However, in the general approach, they included an optional 'credit quality overshooting' adjustment, aiming at capturing other cases where the volatility adjustment overreacts (i.e. improves the solvency of an insurer during crisis situations) due to differences between the composition of the insurer's portfolio and that of the 'reference' portfolio based on which the volatility adjustment is calculated.

Therefore, in the Council's text, an insurer has the possibility to opt for an additional downward adjustment factor, in order to avoid such 'overshooting'. Note that the factor is capped at 100%, meaning that the optional adjustment factor should never result in increasing the solvency position of an insurer applying that optional ratio compared with another insurer not using it. This was considered as an important safeguard to preserve the level-playing field in the Union.

As this adjustment is optional and at the discretion of the insurer, it is not possible to provide quantitative impacts.

In addition, in relation to the risk-corrected spread calculation (a level 2 provision), experts of Member States supported an adjustment to EIOPA's approach so that the revised risk correction is such that it improves risk sensitivity (including to sovereign risk) while remaining an effective countercyclical tool.

It is however our understanding that Amendment 128 of the Rapporteur aims at preventing the Commission from implementing changes to risk-correction in Level 2, unless it is decided to apply the same amendments to the treatment of the so-called 'fundamental spread' for the matching adjustment.

According to EIOPA's assessment, the impact of the different proposals on the capital relief are the following:

	EIOPA's approach	COM proposal	Rapporteur's approach
End of 2019	22 bn €	48 bn €	11 bn€
Mid of 2020	18 bn €	57 bn €	77 bn €

It can be noted that the value of the Volatility adjustment can therefore be very low under certain market conditions under the Rapporteur's approach, in comparison with EIOPA's or Commission's proposal.

Risk margin and cost of capital: Various amounts for the lambda factor (0.9, 0.975 and 0.995) and the cost of capital (4%, 4,5%, 5% and 6%) are discussed. Could the COM provide an analysis of the impact the different values would have?

This is an example of area where a large number of options which have been put forward on the table. There are three variables which influence the actual outcome:

- The value of the lambda factor
- The value of the floor to the lambda factor (EIOPA proposed 0.5, the Commission proposed to remove the floor provided that the lambda is not changed, and the Rapporteur removed the floor);
- The cost-of-capital rate.

Therefore, only the combination of the three can allow assessing the impact of the changes on risk margin. According to EIOPA's assessment, the amendments to the risk margin were resulting in the following capital relief:

- Around +25 billion euros in EIOPA's proposal
- Around +45 billion euros in Commission's proposal
- Around + 90 billion euros in the Rapporteur's proposal.

Further data on the various options are provided in Annex 3.

Long-term equities: What are the implications in terms of capital relief of the different options suggested in the draft report and via amendments? What are the diversification

benefits of extending the pool of investable assets? Should the long-term equity framework be leveraged to support other Union policy objectives?

The treatment of long-term equity investments is not like the treatment of listed equity. While the latter only depends on the nature of the asset itself (quoted on the market), the former requires proactive actions from the insurer, notably the willingness and intention to make a long-term investment and the ability to avoid forced selling at a deteriorated market price. Therefore, it is not possible to provide an estimation of the impact of each amendment.

As part of the Commission's impact assessment, it was indicated that the review could thus result at least in a doubling of the number of insurance firms which are willing to use the long-term equity asset class, and a multiplication by almost six of the amount of equities eligible to a preferential treatment (from € 4.2 billion to € 26 billion). This implies that at least € 3 billion in capital would become available for covering capital requirements for further investments in equity (or further distributions of dividends).

The design of the appropriate criteria is complex and their effectiveness depends, as indicated above, on willingness of insurers to adjust investment behaviour For this reason, we are still of the view that they would better fit into level 2, both in order to be directly applicable without transposition – hence warranting the level-playing field – but also because the criteria can more easily be amended if they prove to still be inappropriate.

In this regard, the Commission Services have transparently presented during Expert Group meetings possible ways to revise the criteria, with the view of making them clearer. It can be noted that such revisions do not result in less legal text, but probably more prescriptive one, guaranteeing more certainty for stakeholders and more EU-wide level-playing field. The Commission services intend to further discuss during Expert Group meetings adjustments to current drafts. We remain at the disposal of the Rapporteur and shadow Rapporteurs should they want to organise dedicated discussions on level 2 topics.

As a complementary remark, please note that Amendment 197 from the Rapporteur related to the review of the duration-based equity risk submodule set out in Article 304. Such an article was deleted in the Commission's proposal, in line with EIOPA's proposal, due to the regulatory developments for long-term equity investments and the limited application of Article 304 (only one firm in Europe is using it). It is the understanding of both the Commission staff and EIOPA that the revised Article 304 would result in almost all equities of life insurers eligible for the 22% capital charge.

Sustainability: Does the European Commission have evidence that (re-)insurance undertakings are systematically underestimating sustainability risk? What was the Commission's rational to only include sustainability aspects in a few selected articles of the Solvency II review.

As stated in the European Green Deal, the Commission aims to ensure that climate and environmental risks will be managed and integrated into the financial system. For this purpose, we want to integrate such risks better into the EU prudential framework. Solvency II requires insurers to consider in their system of governance, risk management system and own risk and solvency assessment (ORSA) all risks they face in the short and long term and to which they

are or could be exposed, including when these risks are not (fully) included in the calculation of the Solvency Capital Requirement (SCR). However, EIOPA concluded that at most 13% of the ORSA reports made a reference to climate change risk scenarios based on an analysis of ORSA reports from 1682 insurance companies representing more than 80% of the EU insurance market[1]. Moreover, where undertakings performed a quantitative analysis of climate change risk, most assessments took a short-term perspective. While this does not provide conclusive evidence on potential underestimation of risks by insurers, it demonstrates that supervisors may not be able to assess whether an insurer takes climate change-related risks into account the Commission considered it necessary to introduce clear references to climate change risks in the rules on the ORSA.

As pointed out in the Commission's impact assessment, climate and environmental risks will typically materialise beyond the one-year time horizon and thus it is essential to promote a forward-looking management of these risks, also in the long term. On the basis of EIOPA's findings and its Opinions issued in 2021[2] and 2019[3] respectively, the Commission proposed a requirement on insurers to regularly assess the impact of longer-term horizon scenarios of climate change. The new Article 45a aims to strengthen the management of climate-change related risks in the risk management framework of insurers, and more, specifically in their ORSA.

The Commission's impact assessment concludes that, in addition to finding merits in strengthening Pillar II requirements in relation to the management of climate change risks through the ORSA, more evidence is needed in order to assess the need for amendments to the Pillar I rules regarding sustainability risks. Thus, the Commission proposed a mandate to EIOPA to explore by 2023 a dedicated prudential treatment of exposures related to assets or activities associated substantially with environmental and/or social objectives and to review regularly the scope and the calibration of parameters of the standard formula pertaining to natural catastrophe risk.

To what degree does a more prominent role for sustainability aspects need to be weighed against unintentional side-effects such as the build-up of a 'green asset bubble' or making legitimate economic activities "uninsurable"?

The Commission's impact assessments consider the benefits and the costs of the policy options. Adverse impacts on financial stability, like the build-up of assets bubbles, and undue impediments to insurability of economic activities, if material, have been and/or would have been taken into account as a cost of policy options considered under the review of the Solvency II Directive.

All the preferred sustainability related policy options and the related proposed amendments are risk-based. The amendments related to sustainability risks aim to either strengthen the already existing Pillar II requirements (i.e. by fostering a forward-looking management of climate risks

[1] EIOPA: Opinion on Sustainability within Solvency II, (EIOPA-Bos-19-241), September 2019 (link)
[2] EIOPA: Opinion on the supervision of the use of climate change risk scenarios in ORSA (EIOPA-BoS-21/127), April 2021 (link)
[3] EIOPA: Opinion on Sustainability within Solvency II, (EIOPA-Bos-19-241), September 2019 (link)

through long-term scenario analysis) or to ensure an appropriate assessment of the relevant evidence as regards the risk characteristics of exposures associated substantially with environmental and/or social objectives or the natural catastrophe risk parameters. Therefore, the proposed amendments do not provide incentives for the build-up of so called "green assets bubbles"[4]. The amendments also do not affect the insurability of economic activities, except where activities give rise to material sustainability risks (including transition risks) and where the insurer does not yet take those risks into account. Even in the latter case, insurers will be able maintain or renew existing insurance coverage provided they remain solvent after sustainability risks are sufficiently taken into account.

To what extent are sustainability reporting requirements suggested in the amendments already covered by other legislation (such as the CSRD)?

The Corporate Sustainability Reporting Directive (CSRD) will amend the existing reporting requirements of the NFRD. The proposal extends the scope of requirements on sustainability reporting to all companies listed on regulated markets and all companies, including insurers, that exceed at least two of the three following criteria:
(a) balance sheet total: EUR 20 million;
(b) net turnover [gross written premiums in the case of insurers]: EUR 40 million;
(c) average number of employees during the financial year: 250.

The CSRD introduces more detailed reporting requirements, and a requirement to report according to mandatory EU sustainability reporting standards. More specifically, the non-financial reporting should cover, inter alia:

- a brief description of the undertaking's business model and strategy, including:
    - the resilience of the undertaking's business model and strategy to risks related to sustainability matters;
    - the opportunities for the undertaking related to sustainability matters;
    - the plans of the undertaking, including implementing actions and related financial and investment plans, to ensure that its business model and strategy are compatible with the transition to a sustainable economy and with the limiting of global warming to 1.5°C in line with the Paris Agreement and the objective of achieving climate neutrality by 2050 as established in Regulation (EU)2021/1119 (European Climate Law), and where relevant, the exposure of the undertaking to coal, oil and gas-related activities;
    - how the undertaking's business model and strategy take account of the interests of the undertaking's stakeholders and of the impacts of the undertaking on sustainability matters;
    - how the undertaking's strategy has been implemented with regard to sustainability matters;
- a description of the time-bound targets related to sustainability matters set by the undertaking, including where appropriate absolute greenhouse gas emission reduction targets at least for 2030 and 2050, a description of the progress the undertaking has made towards achieving those targets, and a specification of whether the undertaking's targets related to environmental matters are based on conclusive scientific evidence;

[4] cf. Page 32 of the Commission's Impact Assessment (SWD(2021) 260).

- a description of the role of the administrative, management and supervisory bodies with regard to sustainability matters, and of their expertise and skills to fulfil this role or access to such expertise and skills;
- a description of the undertaking's policies in relation to sustainability matters;
- information about the existence of incentive schemes offered to members of the administrative, management and supervisory bodies which are linked to sustainability matters;
- a description of:
    - the due diligence process implemented by the undertaking with regard to sustainability matters, and where applicable in line with EU requirements on undertakings to conduct a due diligence process;
    - the principal actual or potential adverse impacts connected with the undertaking's own operations and with its value chain, including its products and services, its business relationships and its supply chain, actions taken to identify and track these impacts, and other adverse impacts which the undertaking is required to identify according to other EU requirements on undertakings to conduct the due diligence process;
    - any actions taken by the undertaking, and the result of such actions, to prevent, mitigate, remediate or bring an end to actual or potential adverse impacts;
- a description of the principal risks to the undertaking related to sustainability matters, including the undertaking's principal dependencies on such matters, and how the undertaking manages those risks.

It has to be noted that captive insurance undertakings and captive reinsurance undertakings would only have to report pursuant to simplified reporting standards. Small and non-complex institutions as defined in the CRR can also report pursuant to simplified reporting standards. In order to ensure cross-sectoral consistency, co-legislators may want to consider allowing insurers and reinsurers classified as low-risk profile undertakings under Solvency II to report pursuant to simplified reporting standards under the CSRD.

The rules of the CSRD will be supplemented by sustainability reporting standards that will specify the information listed above and, where relevant, the structure in which that information shall be reported.

In addition to the rules of the CSRD, the SFDR imposes several entity level disclosure requirements on life insurance undertakings which make available an insurance-based investment product (IBIP). Those requirements cover inter alia a requirement to publish the following on the company website:

- information about policies on the integration of sustainability risks in their investment decision-making process;
- a statement on due diligence policies with respect to principal adverse impacts of investment decisions on sustainability factors where they consider those impacts or clear reasons where they do not consider them;
- information on how remuneration policies are consistent with the integration of sustainability risks.

Capital relief: Can the Commission provide guidance on how to ensure that capital relief does not translate to higher shareholder distributions, but an actual increase in risk-taking capacity?

As already said in introductory remarks, we, based on EIOPA's inputs, have been in a position to assess the quantitative impact of EIOPA's proposal, its own proposal as well as the Rapporteur's proposal under market conditions equivalent to those at the end of 2019 and mid-2020 only.

	EIOPA's opinion	COM proposal	Rapporteur's proposal
Year-end 2019	-17.8 bn€	38 bn€	105.4 bn€
Mid-2020	-55 bn€	16.6 bn€	178.9 bn€

Annex 4 provides further details on the comparative impact of the various proposals on the overall capital requirements for insurance companies.

We understand that the Rapporteur's proposals would release between 105 billion and 180 billion euros of capital. Such significant capital relief combined with the reduced volatility stemming from the Commission's proposal is probably expected to foster investments in the real economy. However, beyond the impact of such capital relief on policyholder protection and financial stability, and as acknowledged in the Commission's impact assessment, there is no possibility to guarantee that the significant capital reliefs would not be used to distribute more dividends. We note in this respect that that several adjustments envisaged by the Rapporteur or other MEPs are indeed unconditional. Regarding the long-term equity asset class, the insurer needs to take proactive steps to really invest for the long-term in order to get a lower capital charge – which would not necessarily imply that the released capital would be used to further invest in businesses, but at least co-legislators would have the assurance that the 22% capital charge is used for long-term financing of the economy and not speculation or short-term trading – changes notably to extrapolation or the risk margin are unconditional.

As prudential rules are not the only driver of equity investments (which also depends on asset-liability management, accounting and tax considerations, as well as market volatility or the models used by rating agencies to assign a 'grading' to insurers), there is no guarantee indeed that significant relaxations of capital requirements would result in further investments. In addition, significant relaxations of prudential requirements could restrict supervisors' ability to intervene timely, as the changes would result in "tweaking" the measure of risk (the solvency capital requirement or SCR) in such a manner that a supervisor would no longer be able to intervene in cases where it would under current rules.

Note that the Commission introduced in its proposal a supervisory tool of exceptional and temporary nature aimed at preserving the financial position of individual insurers during periods of exceptional sector-wide shocks where the financial position of the insurer or the stability of the financial system may be endangered (**new Art. 144c**). In such exceptional cases, supervisors would be empowered to restrict or suspend the distribution of dividends and bonuses to preserve the financial position of an insurer in the interest of policyholders or the stability of the financial system. Therefore, during times of sector-wide shocks, the capital relief associated with certain amendments put forward by the Commission can be preserved by supervisors using this tool, thus preventing the decapitalization (or decrease of own funds) of an insurance company in times of crisis through the distribution of dividends to shareholders

or bonuses to board members. However, it is true that this tool cannot be used to prevent insurers from using the capital relief to distribute more dividends under 'normal times'.

- **Governance/gender issues: Could the COM explain what would already be covered by the upcoming 'Women on boards Directive' https://www.europarl.europa.eu/news/en/press-room/20220603IPR32195/women-on-boards-deal-to-boost-gender-balance-in-companies and which consequences this would have for the insurance sector?**

The Directive on improving the gender balance among non-executive directors of listed companies will cover companies, including insurers, whose shares are admitted to trading on a regulated market and which have with 250 or more employees.

The main elements of the gender balance directive are:

- At least 40% of the underrepresented gender must be represented in non-executive boards of listed companies or 33% among all directors. Companies shall strive to achieve this objective and those that do not achieve them must apply transparent and gender-neutral criteria in the appointment of directors and prioritise the underrepresented sex where two candidates of different sexes are equally qualified.
- Clear and transparent board appointment procedures with objective assessment based on merit, irrespective of gender. The selection procedure of non-executive directors will need to comply to the following binding measures:
  - Where two candidates of different sexes are equally qualified, preference shall be given to the candidate of the underrepresented sex, in companies where the target for gender balance is not achieved.
  - Companies must disclose their qualification criteria should the unsuccessful candidate request it. Companies are further responsible to prove no measures were transgressed, if there is suspicion that an unsuccessful candidate of the underrepresented sex was equally qualified.
  - Companies must undertake individual commitments to reach gender balance among their executive directors.
  - Companies that fail to meet the objective of this Directive must report the reasons and the measures they are taking to address this shortcoming.
  - Member States' need to put in place effective, proportionate and dissuasive penalties for companies that fail to comply with selection and reporting obligations. Penalties could include fines and nullity or annulment of the contested director's appointment. Member States shall also publish information on companies' that are reaching targets, which would serve as peer-pressure to complement enforcement ("faming" provision).

In addition to the rules of the Directive on improving the gender balance among non-executive directors of listed companies, the CSRD will amend the Accounting Directive to require undertakings with securities listed on regulated markets to report on their gender diversity policies with regard to the company board. If no such policy is applied, the statement shall contain an explanation as to why this is the case.

It has to be noted that only a small share of insurers are listed and therefore subject to the rules cited above. A recent CEPS study[5] estimated that around 1% of EU insurance companies are listed (taking into account listings of shares and bonds).

In addition, the sustainability reporting standards that will be adopted by the Commission under the CSRD and that will be relevant for most insurers (see also explanation on the CSRD scope under a previous question) will specify the information that undertakings are to disclose about equal treatment and opportunities for all, including gender equality and equal pay for work of equal value, training and skills development, the employment and inclusion of people with disabilities, measures against violence and harassment in the workplace, and diversity.

Group Supervision: The Commission proposal also deals with the supervision of groups that not only include insurance companies. Why did the Commission opt to address this point in the Solvency II review and not in the Financial Conglomerates Directive? The so called "Danish Compromise" benefits banking groups with insurance holdings over insurance groups. Why did the Commission opt not to address this unlevel playing field in the Solvency II review?

The treatment of banks in the solvency calculation of insurance undertakings and groups is currently specified at several levels of legislation and guidance:

- **The Directive:** Article 228 (current directive) refers to the use of FICOD methods in Solvency II and on the possibilities to deduct banking holdings
- **The Delegated Regulation (EU) 2015/35:** Article 68 (also partly referring to FICOD) refers to the treatment at solo level of banks, and Articles 329, 335 and 336 refer to the treatment at group level
- **EIOPA guidelines on group solvency calculation and EIOPA Q&As** further specify how to handle cases of banking subgroup, or provide further specifications on the banking capital requirements to be taken into account for the purpose of group solvency.

The Commission proposal on the Solvency II review does not aim to change the rules as they currently apply but simply to put them together in the same piece of legislation in order to make it simpler for groups and supervisory authorities. This is in line with the feedback received from stakeholders during EIOPA's consultations.

Please note that at solo level, in accordance with current Article 68 of the Delegated Regulation, which would be now 'upgraded' in Article 92 of the Solvency II Directive under the Commission proposal, the treatment of banks in the SCR of an individual insurer follows the same 'logic' as the Danish compromise in banking. More precisely, there is the possibility for insurers using the standard formula not to deduct holdings in banking subsidiaries but instead to apply a "low" capital charge of 22% where conditions very similar to those applicable in CRR for the Danish compromise are met. The Commission proposal **would not be a change** compared with current rules where most insurers already apply the 22% standard parameter to their banking holdings.

[5] CEPS: "Study on the Non-Financial Reporting Directive", November 2020 (link, cf. page 44)

At group level, the treatment of banking subsidiaries is in line with that of FICOD. According to Articles 335 (e) and 336 (c) of the Delegated Regulation, which would be "upgraded" in Articles 228, 230 and 233 of the Solvency II Directive under the Commission proposal, banks are included in the insurance group solvency but are **never** consolidated in an insurance balance sheet for the purpose of Solvency II. Instead, the proportional share of the **CRR figures** for own funds and capital requirements are used for the purpose of the insurance group solvency. More precisely:

- The insurance group own funds are the sum of the consolidated own funds of the pure insurance part of the group and the proportional share of the own funds of the banking part of the group calculated in accordance with CRR
- The total group capital requirements would be the sum of the capital requirement of the insurance part of the group (the 'solvency capital requirement') and the proportional share of the CRR capital requirements for the banking part.

Please note that in this context the proportional share means the percentage of capital held by the insurer in the banking subsidiary.

The Commission proposal on the Solvency II review confirms the **existing approach at group level,** which has proved to be robust and has never been disputed by any stakeholder.

To be noted, that the expression "Danish compromise" is not used in the Solvency II context, but refers to specific CRR provisions. The Danish compromise in CRR implies that the non-deduction is correlated to the application of FICOD to the banking group. Under FICOD, the banking group has to take into account the Solvency II figures for own funds and capital requirements of the insurance business. Therefore, the FICOD ratio of a banking-led conglomerate, based on which supervisory authorities can also take remedial actions, and which is publicly disclosed in annual reports of banking groups, is the close equivalent of the Solvency II group calculation for insurance-led conglomerates. Therefore, it is possible for both supervisory authorities and analysts to compare on a similar basis, insurance-led and banking-led conglomerates' solvency position.

In conclusion, and in line with EIOPA's advice and stakeholders' feedback, the Solvency II framework has proved to be robust in relation to the treatment of banking subsidiaries of insurance undertakings and groups, and has not been challenged during the various consultation processes.
The concerns expressed by some industry stakeholders are related to the review of the banking prudential treatment of insurance holdings in CRR, which is outside the scope of the Solvency II review.

Annex 1 - Proportionality and Low-risk profile undertakings: Assessing the various proposals for thresholds under Solvency II

The EP amendments imply various combinations of thresholds in relation to gross written premiums (GWPs) and technical provisions (TP) at both solo and group level. Based on currently available data, EIOPA assessed the impact of the proposals and you can find the expected maximum number of firms exempted under the different proposals in the following. In addition, you find a country specific allocation of the exclusions below.

<table>
<tr><th></th><th>Solo GWP</th><th>Solo TP</th><th>Group TP</th><th>Exemption</th></tr>
<tr><td>Current Directive</td><td>5 million</td><td>25 million</td><td>25 million</td><td>261</td></tr>
<tr><td>McManus (the Left)</td><td>Threshold defined by MS but lower than 25 million</td><td>25 million</td><td>25 million</td><td>538</td></tr>
<tr><td>Heinäluoma Fernandez Lalucq (S&D)</td><td>10 million</td><td>40 million</td><td>25 million</td><td>390</td></tr>
<tr><td>Commission</td><td>15 million</td><td>50 million</td><td>25 million</td><td>474</td></tr>
<tr><td>Hahn</td><td rowspan="2">15 million</td><td rowspan="2">50 million</td><td rowspan="2">50 million</td><td rowspan="2">477</td></tr>
<tr><td>Yon-Courtin Boyer</td></tr>
<tr><td>Eroglu</td><td>15 million</td><td>50 million</td><td>100 million</td><td>479</td></tr>
<tr><td>Rapporteur</td><td rowspan="2">25 million</td><td rowspan="2">65 million</td><td rowspan="2">65 million</td><td rowspan="2">588</td></tr>
<tr><td>Zanni Grant Rinaldi</td></tr>
</table>

<table>
<tr><th>Country</th><th>Current Directive</th><th>McManus (the Left)</th><th>Heinäluoma Fernandez Lalucq (S&D)</th><th>Commission</th><th>Hahn</th><th>Yon-Courtin Boyer</th><th>Eroglu</th><th>Zanni Grant Rinaldi</th></tr>
<tr><td>AT</td><td>0</td><td>1</td><td>0</td><td>0</td><td colspan="2">0</td><td>0</td><td>1</td></tr>
<tr><td>BE</td><td>3</td><td>8</td><td>6</td><td>8</td><td colspan="2">8</td><td>8</td><td>10</td></tr>
<tr><td>BG</td><td>3</td><td>5</td><td>4</td><td>5</td><td colspan="2">5</td><td>6</td><td>5</td></tr>
<tr><td>CY</td><td>2</td><td>15</td><td>3</td><td>10</td><td colspan="2">10</td><td>10</td><td>16</td></tr>
<tr><td>CZ</td><td>4</td><td>5</td><td>5</td><td>6</td><td colspan="2">6</td><td>6</td><td>6</td></tr>
<tr><td>DE</td><td>6</td><td>29</td><td>18</td><td>26</td><td colspan="2">26</td><td>26</td><td>31</td></tr>
<tr><td>DK</td><td>8</td><td>22</td><td>15</td><td>19</td><td colspan="2">19</td><td>19</td><td>23</td></tr>
<tr><td>EE</td><td>2</td><td>4</td><td>3</td><td>3</td><td colspan="2">3</td><td>3</td><td>4</td></tr>
<tr><td>EL</td><td>5</td><td>10</td><td>7</td><td>9</td><td colspan="2">9</td><td>9</td><td>11</td></tr>
<tr><td>ES</td><td>6</td><td>26</td><td>8</td><td>15</td><td colspan="2">15</td><td>15</td><td>26</td></tr>
<tr><td>FI</td><td>3</td><td>5</td><td>4</td><td>4</td><td colspan="2">4</td><td>4</td><td>5</td></tr>
<tr><td>FR</td><td>17</td><td>72</td><td>43</td><td>56</td><td colspan="2">56</td><td>56</td><td>74</td></tr>
<tr><td>HR</td><td>2</td><td>2</td><td>2</td><td>2</td><td colspan="2">2</td><td>2</td><td>2</td></tr>
<tr><td>HU</td><td>1</td><td>1</td><td>1</td><td>1</td><td colspan="2">1</td><td>2</td><td>2</td></tr>
<tr><td>IE</td><td>31</td><td>58</td><td>47</td><td>54</td><td colspan="2">54</td><td>54</td><td>66</td></tr>
<tr><td>IS</td><td>0</td><td>0</td><td>0</td><td>0</td><td colspan="2">0</td><td>0</td><td>0</td></tr>
<tr><td>IT</td><td>0</td><td>2</td><td>0</td><td>1</td><td colspan="2">1</td><td>1</td><td>2</td></tr>
</table>

LI	4	6	5	6	6	6	8
LT	1	1	2	2	2	2	2
LU	96	128	122	130	131	131	143
LV	0	1	0	1	1	1	1
MT	15	26	19	22	23	23	29
NL	8	27	16	19	19	19	29
NO	23	27	26	27	27	27	30
PL	1	6	1	4	5	5	7
PT	1	3	1	2	2	2	4
RO	2	4	4	4	4	4	4
SE	15	41	26	36	36	36	44
SI	2	2	2	2	2	2	2
SK	0	1	0	0	0	0	1
EEA	**261**	**538**	**390**	**474**	**477**	**479**	**588**

Annex 2 – Justification for the exclusion of the illiquidity factor

First, the illiquidity factor adjusts downward the volatility adjustment. As one of the objectives of the Commission was to achieve a balanced outcome, removing the illiquidity factor was increasing the volatility adjustment, hence improving the capital relief for insurers in comparison with EIOPA's Opinion.

Second, in light of EIOPA's technical specifications, the new illiquidity component of the volatility adjustment would reward in the current low-yield environment insurers which offer unsustainably high guaranteed rates on life policies, possibly raising financial stability risks; therefore, this adjustment is not efficient.

Third, the recently adopted Regulation (EU) 2019/1238 on a pan-European Personal Pension Product (PEPP) is aimed at fostering the supply of private pensions in Europe across border. However, one of the characteristics of the PEPP is its portability (i.e. the ability to change provider). This portability feature would imply that insurers providing PEPP products would be classified as having "liquid" liabilities. Therefore, insurers would be at a disadvantage vis-a-vis insurers selling national products with no portability. This would not be coherent with the objective of developing the PEPP (also reiterated in the Capital Markets Union Action Plan).

Fourth, currently, the volatility adjustment is a simple tool the value of which is centrally derived by EIOPA. Under the new approach, each insurer would have to calculate its own volatility adjustment. This creates undue burden for smaller and less complex insurers, which may decide to rely on the volatility adjustment anymore, even if it is at the cost of higher volatility of the solvency ratio. Therefore, the illiquidity adjustment would not be coherent with the Better Regulation agenda.

Finally, EIOPA proposes that insurers' liquidity risk is measured by calculating the standard formula level of capital requirements for increased mortality or exercise of redemption rights. Therefore, EIOPA is double counting the same risk in the capital requirement and through the level of the volatility adjustment when valuing its liabilities.

For all those reasons, the Commission decided to discard the illiquidity factor as proposed by EIOPA.

Annex 3 – Impact assessment of various approaches on risk margin – Commission's calculations

Assessing the impact of amendments to the risk margin on capital relief is not straightforward, as there are indirect interactions with tax rates in the various countries. The Commission's calculations are a bit less granular than the ones from EIOPA, in particular in relation to assumptions of tax rates (which affect the extent to which a reduction in risk margin increases an insurer's capital resources).

The below figures are Commission services' own calculations. While not exactly the same as EIOPA's figures due to slightly different hypotheses, the gap with EIOPA's approach can be considered moderate (less than 4% difference indifferences in risk margin values). Note however that the size of the risk margin also de**pends on other parameters, such as extrapolation**.

The highlighted figures represent EIOPA's approach in green, the Commission's approach in blue and the Rapporteur's approach in orange.

	Change in own funds (in bn€)			
	Cost of capital rate = 6%			
	Floor = 0	Floor = 0.3	Floor = 0.4	Floor = 0.5
Lambda = 0.9	64,3	57,6	52,8	46,8
Lambda = 0.95	42,9	41,7	39,8	36,9
Lambda = 0.975	25,7	25,7	25,5	25,5
Lambda = 0.995	6,1	6,1	6,1	6,1

	Change in own funds (in bn€)			
	Cost of capital rate = 4.5%			
	Floor = 0	Floor = 0.3	Floor = 0.4	Floor = 0.5
Lambda = 0.9	81,3	75,6	71,7	66,9
Lambda = 0.95	65,4	64,2	62,6	60,1
Lambda = 0.975	52,1	52,1	51,9	51,4
Lambda = 0.995	36,6	36,6	36,6	36,6

	Change in own funds (in bn€)			
	Cost of capital rate = = 5%			
	Floor = 0	Floor = 0.3	Floor = 0.4	Floor = 0.5
Lambda = 0.9	76,2	69,8	65,5	60,2
Lambda = 0.95	58,5	57,2	55,4	52,7
Lambda = 0.975	43,8	43,7	43,5	43,0
Lambda = 0.995	26,6	26,6	26,6	26,6

	Change in own funds (in bn€)			
	Cost of capital rate = 4%			
	Floor = 0	Floor = 0.3	Floor = 0.4	Floor = 0.5
Lambda = 0.9	86,4	81,3	77,8	73,6
Lambda = 0.95	72,2	71,2	69,8	67,6
Lambda = 0.975	60,4	60,4	60,2	59,8
Lambda = 0.995	46,6	46,6	46,6	46,6

***NB**: the figures related to the Cost-of-Capital rate of 6% (table on the top left) directly come from EIOPA.*

Annex 4 – Comparative assessment of the impact of the different proposals on capital requirements

As a reminder, from a technical perspective, the review as recommended by EIOPA consisted in remedying the underestimation of risks related to interest rates faced by insurers, both in the valuation of their liabilities towards policyholders (extrapolation method where the current methodology does not reflect market data on long-term rates) and in capital requirements (where negative interest rates are assumed not to exist). For this reason, EIOPA was recommending a review which is balanced in terms of capital excluding those two topics, but which would result – taking into account those two items – in an increase in capital requirements of up to 55 bn€.

The Commission proposal aimed to offer a balanced outcome in terms of capital requirement, by taking into account both level 1 and level 2. In this regard, the Commission proposal would result in an improvement in insurers' wealth (measured as insurers' excess capital over the SCR) of between 16 billion and 30 billion euros. The Commission services have considered those changed (notably the deletion of the illiquidity factor in the volatility adjustment or the decrease in the cost-of-capital rate by 1 percentage point from 6% to 5%) as technically justifiable, although acknowledging in the Commission Staff's impact assessment that this is already stretching EIOPA's Opinion for the purpose of supporting the EU political priorities.

Based on EIOPA's quantitative assessment, we understand that the Rapporteur's proposal would overall result in a relaxation of capital of up to 170 billion euros (i.e. an increase of between 120 billion euros and 280 billion euros compared with EIOPA's proposals, and still an increase of between 60 billion euros and 180 billion euros compared with the Commission's proposals).

As a comparison:

- Under Solvency I, during the great financial crisis in 2007, insurers lost in one year 120 billion euros of surplus
- During the Covid-19 crisis, between end of 2019 and first quarter of 2020, insurers lost 138 billion euros of capital.
- The entry into application of insurers resulted in an increase in capital cushion by insurers between 2007 and 2015 of about 187 billion euros.