

Existing tools in Solvency II of potential relevance for the current COVID-19 situation

Measure	Comment
<b>Recovery period in case of SCR breach</b>	
<p>Article 138 Directive</p> <p>Non-Compliance with the Solvency Capital Requirement [...]</p> <p><b>4.</b> In the event of exceptional adverse situations affecting insurance and reinsurance undertakings representing a significant share of the market or of the affected lines of business, as declared by EIOPA, and where appropriate after consulting the ESRB, <b>the supervisory authority may extend, for affected undertakings, the period set out in the second subparagraph of paragraph 3 by a maximum period of seven years</b>, taking into account all relevant factors including the average duration of the technical provisions.</p> <p>Without prejudice to the powers of EIOPA under Article 18 of Regulation (EU) No 1094/2010, for the purposes of this paragraph EIOPA shall, following a request by the supervisory authority concerned, <del>declare</del> the existence of exceptional adverse situations. The supervisory authority concerned may make a request if insurance or reinsurance undertakings representing a significant share of the market or of the affected lines of business are unlikely to meet one of the requirements set out in paragraph 3. Exceptional adverse situations exist where the financial situation of insurance or reinsurance undertakings representing a significant share of the market or of the affected lines of business are seriously or adversely affected by one or more of the following conditions:</p> <p>(a) a <b>fall in financial markets which is unforeseen, sharp and steep</b>;</p> <p>(b) a <b>persistent low interest rate environment</b>;</p>	<p><b>Extension of recovery period up to 7 years in case of SCR breach</b> in case of “exceptional adverse situations” (normal timeframe: 6 months).</p> <p>Only one of the following conditions has to be met for EIOPA to consider using this possibility:</p> <p>(a) a <b>fall in financial markets which is unforeseen, sharp and steep</b>;</p> <p>(b) a <b>persistent low interest rate environment</b>;</p> <p>(c) a <b>high-impact catastrophic event</b>.</p> <p>No such extension in the regulation when MCR is breached.</p> <p><b>Questions for discussion:</b></p> <ul style="list-style-type: none"> <li>• <b>Is it justified to say conditions are met?</b></li> <li>• <b>Is there a need now for us to seek confirmation this is in place?</b></li> <li>• <b>Are there cases where this is expected to be needed in practice?</b></li> </ul>

(c) a **high-impact catastrophic event**.

EIOPA shall, in cooperation with the supervisory authority concerned, assess on a regular basis whether the conditions referred to in the second subparagraph still apply. EIOPA shall, in cooperation with the supervisory authority concerned, declare when an exceptional adverse situation has ceased to exist.

The insurance or reinsurance undertaking concerned shall, every three months, submit a progress report to its supervisory authority setting out the measures taken and the progress made to re-establish the level of eligible own funds covering the Solvency Capital Requirement or to reduce the risk profile to ensure compliance with the Solvency Capital Requirement.

The extension referred to in the first subparagraph shall be withdrawn where that progress report shows that there was no significant progress in achieving the re-establishment of the level of eligible own funds covering the Solvency Capital Requirement or the reduction of the risk profile to ensure compliance with the Solvency Capital Requirement between the date of the observation of non-compliance of the Solvency Capital Requirement and the date of the submission of the progress report.

See Follow-up articles in Delegated regulation: criteria

Article 288 Delegated acts -  
Assessment of exceptional adverse situations

Article 289 Delegated acts -  
Factors and criteria to determine the extension of the recovery period

<p>Article 138 Directive</p> <p>Non-Compliance with the Solvency Capital Requirement</p> <p><b>5. In exceptional circumstances, where the supervisory authority is of the opinion that the financial situation of the undertaking concerned will deteriorate further, it may also restrict or prohibit the free disposal of the assets of that undertaking.</b> That supervisory authority shall inform the supervisory authorities of the host Member States of any measures it has taken. Those authorities shall, at the request of the supervisory authority of the home Member State, take the same measures. The supervisory authority of the home Member State shall designate the assets to be covered by such measures.</p>	
<p><b>Potential pro-cyclical effects of supervisory actions</b></p>	
<p>Article 28 Directive</p> <p>Financial stability and pro-cyclicality</p> <p>Without prejudice to the main objective of supervision as set out in Article 27, Member States shall ensure that, in the exercise of their general duties, <b>supervisory authorities shall duly consider the potential impact of their decisions on the stability of the financial systems</b> concerned in the European Union, in particular in emergency situations, taking into account the information available at the relevant time.</p> <p><b>In times of exceptional movements in the financial markets, supervisory authorities shall take into account the potential pro-cyclical effects of their actions.</b></p>	<p>May be a ground to justify a deviation or forbearance from some legal texts.</p> <p>Note: no follow-up text in the Delegated Acts.</p> <p><b>Question for discussion:</b></p> <ul style="list-style-type: none"> <li>• <b>Are supervisors allowed to apply forbearance and not take action when company not complying with some requirements?</b></li> </ul>
<p><b>Reporting</b></p>	
<p>Delegated Acts - Art 35</p> <p><b>Information to be provided for supervisory purposes</b></p>	<p>Supervisors are allowed to grant waivers for reporting on an item by item basis, but it cannot represent more than 20% of a MS life and non-life reinsurance market.</p>

<p>...</p> <p>(7) The supervisory authorities concerned may limit regular supervisory reporting or exempt insurance and reinsurance undertakings from reporting on an item-by-item basis, where:</p> <p>(a) the submission of that information would be overly burdensome in relation to the nature, scale and complexity of the risks inherent in the business of the undertaking;</p> <p>(b) the submission of that information is not necessary for the effective supervision of the undertaking;</p> <p><b>(c) the exemption does not undermine the stability of the financial systems concerned in the Union; and</b></p> <p>(d) the undertaking is able to provide the information on an ad-hoc basis.</p> <p>Supervisory authorities shall <b>not exempt from reporting on an item-by-item basis insurance undertakings that are part of a group</b> within the meaning of Article <b>212</b> paragraph <b>1(c)</b>, unless the undertaking can demonstrate to the satisfaction of the supervisory authority that reporting on an item-by-tem basis is inappropriate, given the nature, scale and complexity of the risks inherent in the business of the group and taking into account the objective of financial stability.</p> <p>The exemption from reporting on an item-by-item basis shall be granted only to undertakings that do <b>not represent more than 20 % of a Member State's life and non-life insurance or reinsurance market</b> respectively, where the non-life market share is based on gross written premiums and the life market share is based on gross technical provisions.</p> <p>Supervisory authorities shall give priority to the smallest undertakings when determining the eligibility of the undertakings for those exemptions.</p>	<p>In addition, priority has to be given to smaller undertakings, and insurance undertakings that are part of a group are not supposed to be exempted.</p> <p>This could be of use for some exemptions in reporting, but there are drawbacks, as these articles were designed more for proportionality purposes.</p> <p><b>Question for discussion:</b></p> <ul style="list-style-type: none"> <li>• <b>Do members agree that these provisions are of limited use?</b></li> </ul>
<p><b>Equity risk sub-module: symmetric adjustment mechanism</b></p>	
<p>Article 106 Directive</p> <p>Calculation of the <b>equity risk sub-module: symmetric adjustment mechanism</b></p>	<p>The standard formula has inbuilt capital relief for equity charges when there is a downturn in the market via the symmetric equity adjustment.</p> <p>The symmetric equity adjustment is an adjustment to the standard formula equity shock parameter.</p>

The symmetric adjustment...shall not result in an equity capital charge being applied **that is more than 10 percentage points lower or 10 percentage points higher than the standard equity capital charge.**

- It decreases the capital requirement for equity risk in market downturns (falling equity prices) and increases it during upturns (increasing equity prices).
- **However, there is a cap and floor of +/-10% points that arguably restricts its effectiveness in a crisis.**

**The removal of the floor would increase effectiveness in a crisis but would be considered to be a more significant change as it requires a change to the Directive.**

**It would also likely result in the removal of the cap which may increase capital charges during periods of market exuberance.**

**2020 Review:** EIOPA consulted on the symmetric equity adjustment as part of 2020 Review. However, it consulted on the constituents of the EIOPA index underlying the adjustment, proposing to retain the status quo. It did not consult upon the parameters.

Industry provided no response to this part of the consultation.

**ESRB [Enhancing the macroprudential dimension of Solvency II Report](#):** The ESRB support the removal or increase of the 10% cap on the value of the symmetric adjustment so that the mechanism is more efficient. They note that this may be necessary to reduce the risk of fire sales in a crisis.

It also supports the extension of the symmetric equity adjustment to use in internal models.

**Art 172 DR** gives some criteria and the formula underlying the adjustment...

Symmetric adjustment of the equity capital charge

[...]

$$SA = \frac{1}{2} \cdot \left( \frac{CI - AI}{AI} - 8\% \right)$$

....4. The symmetric adjustment shall not be lower than – 10 % or higher than 10 %.

**Question for discussion:**

- **Would the (now theoretical) removal of the -10% have a significant impact on Solvency ratios?**

#### Transitional measure on technical provisions

##### Article 308(d) Directive

##### Transitional measure on technical provisions

Insurance and reinsurance undertakings may, subject to prior approval by their supervisory authority, apply a transitional deduction to technical provisions.

The transitional deduction shall correspond to a portion of the difference between the following two amounts:

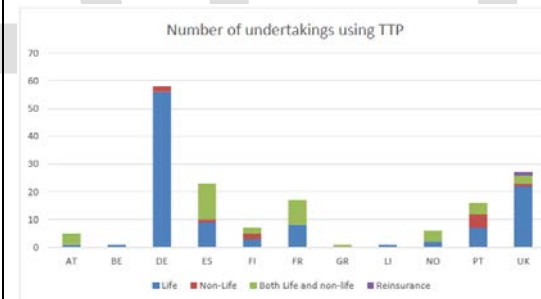
- the technical provisions after deduction of the amounts recoverable from reinsurance contracts and SPVs;
- the technical provisions after deduction of the amounts recoverable from reinsurance contracts calculated under Solvency I.

The maximum portion deductible shall decrease linearly at the end of each year from 100 % during the year starting from 1 January 2016 to 0 % on 1 January 2032.....

##### Application for approval of TMTP

TMTP is used by 162 undertakings from 11 countries (2018 LTG Report).

Its application is subject to supervisory discretion and only impacts liabilities which relate to pre-2016 business.



**There are two aspects to the TMTP would could provide a mitigating effect**

1. **Undertakings which do not currently apply the measure could make an application for its use.**
2. **Undertakings who do apply the measure could request a**

**recalculation of the TMTP (in line with Article 308d (3)).**

The UK NSA, the PRA, has acknowledged that movements in risk-free rates (and consequent increase in the Risk Margin) since the end of 2019 have passed its threshold for a TMTP recalculation. It also points out that the current coronavirus pandemic means that firms can request a recalculation based on a material change in their risk profiles. The PRA is therefore willing to accept applications from firms to recalculate TMTP as at 31 March 2020

**2020 Review:** EIOPA consulted on the transitional measures as part of the 2020 Review.

EIOPA assessed the practice of NSAs regarding new applications in the LTG report 2016.

- 8 NSAs agreed that they would allow undertakings to apply at a later date
- 4 would not allow that application at a later date.
- Several NSAs also agreed that they would allow undertakings to reapply after exiting.

EIOPA advised to restrict the new application of Transitional measures only in specific cases (transfer of portfolio, new application of SII for insurer).

Industry disagreed with EIOPAs proposals and supported the continued application of the transitional as foreseen in the Directive ie. no restrictions on application.

**Question for discussion:**

- **Are there other transitional measures which could also provide a mitigating effect?**

<p><b>Update of the UFR</b></p> <p>EIOPA <a href="#">Report on UFR 2020</a> proposes a UFR of 3.75% for 2020. This is the parameter applicable from 1/1/20.</p> <p><b>DR Article 43:</b> EIOPA must inform EC of any substantial change in the data used to calculate the RFR including the UFR.</p> <p><b>DR Article 47:</b> UFR should be stable and shall only change as a result of changes in long-term expectations.</p>	<p>The first time the revised UFR (of 3.75%) will officially be published is when the EC publishes the Q1 RFR curves. Usually, this happens in May 2020.</p> <p><b>Question for discussion:</b></p> <ul style="list-style-type: none"> <li>• <b>Would a (now theoretical) delay in changing the UFR have a material impact to address the current situation?</b></li> </ul>
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<b>Tools of lesser relevance</b>	
<b>Suspension of distribution of dividends</b>	
<p>Article 71 Delegated acts</p> <p>Tier 1 — Features determining classification</p> <p>1. The features referred to in Article 69 shall be the following:</p> <p>[...]</p> <p>(l) the basic own-fund item meets one of the following criteria: (i) <b>in the case of items referred to in points (a)(i) [<i>paid-in ordinary share capital and the related share premium account</i>] and (ii) [<i>paid-in initial funds, members' contributions or the equivalent basic own-fund item for mutual and mutual-type undertakings</i>] of Article 69(1), either the legal or contractual arrangements governing the basic own-fund item or national legislation allow for the cancellation of distributions in relation to that item where there is non-compliance with the Solvency Capital Requirement or the distribution would lead to such non-compliance until the undertaking complies with the Solvency Capital Requirement and the distribution would not lead to non-compliance with the Solvency Capital Requirement;</b></p>	<p>To be allowed as Tier 1, shares must allow (through national legislation or contractually) suspension of the distribution of dividends when there is non-compliance with the SCR or distribution would lead to non-compliance.</p> <p>The same provisions apply for Tier 2 own fund items (art 73 DA).</p> <p>NSAs can exceptionally allow for distribution if it does not weaken the solvency position and MCR would still be complied with.</p>

(ii) in the case of items referred to in points (a)(iii) [*paid-in subordinated mutual member accounts*] and (v) [*paid-in preference shares and the related share premium account*] and point (b) of Article 69 [*paid-in subordinated liabilities valued in accordance with Article 75 of Directive 2009/138/EC*] the terms of the contractual arrangement governing the basic own-fund item provide for the cancellation of distributions in relation to that item where there is non-compliance with the Solvency Capital Requirement or the distribution would lead to such non-compliance until the undertaking complies with the Solvency Capital Requirement and the distribution would not lead to non-compliance with the Solvency Capital Requirement;

(m) the basic own-fund item **may only allow for a distribution** to be made where there is non-compliance with the Solvency Capital Requirement or the distribution on a basic-own fund item would lead to such non-compliance, **where all of the following conditions are met:**

(i) the **supervisory authority has exceptionally waived the cancellation** of distributions;

(ii) the **distribution does not further weaken the solvency position** of the insurance or reinsurance undertaking;

(iii) the **Minimum Capital Requirement is complied with after the distribution** is made.

#### Supervision of cross border groups

Article 355 Delegated Acts

Coordination arrangements

[...]

2.The coordination arrangements shall, with regard to both going concern and emergency situations, specify the following:

[...]

(2) (e) **an emergency plan agreed by the college of supervisors.**

(3) The emergency plan referred to in point (e) of paragraph 2 shall be adapted to the specific risks of the insurance or reinsurance group. It shall include provisions covering all of the following elements:

(a) recognition of the existence of a crisis;

These coordination arrangements are meant to facilitate group supervision in the colleges of supervisors.

(b) preparation of the crisis management;  
 (c) crisis assessment;  
 (d) crisis management;  
 (e) external communication.

(4) The emergency plan shall provide that all of the following information shall be exchanged among supervisory authorities within the college of supervisors as soon as it becomes available:

(a) a description of the emergency situation, with an indication of any impact on policyholders and on the financial markets;  
 (b) an identification of the undertakings in the group which are affected by the emergency situation referred to in point (a), with relevant information on their financial situation;  
 (c) an overview of any measures taken by the group in relation to the emergency situation referred to in point (a);  
 (d) an overview of any measures taken by any of the supervisory authorities concerned in relation to the emergency situation referred to in point (a) and a description of any existing national measures relevant to the management and resolution of the crisis.

#### Relevant EIOPA reports/documents

**Crisis walkthrough exercise: approach and lessons learned** 7 February 2020 ([link](#))

The report emphasizes that authorities in charge of financial stability need to develop very flexible crisis management procedures in order to deal with unexpected events and to mitigate as quickly as possible the consequences of a developing crisis.

“Several areas of improvement were identified. In particular, some terminology currently embedded in the EU regulatory framework may be

Being in charge of ensuring financial stability, EIOPA has a central role in developing crisis management procedures.

In June 2019, EIOPA conducted, together with one NSA, its first walkthrough exercise.

This report was issued recently: it is unlikely that the “lessons learned” and “areas of improvement” have been already embedded in EIOPA’s framework.

<p>confusing or require further clarification to make them operational. Furthermore, some of the EIOPA Crisis Handbook processes established might be too rigid to cope with sudden and severe crisis. Therefore, an accelerated fast-track process could be considered for specific stress situations."</p>	
<p><b>Crisis Prevention page</b> (<a href="#">link</a>)</p> <p>One of EIOPA's key responsibilities is to <b>ensure coordinated crisis prevention and management</b>, as well as to <b>preserve financial stability in crisis situations</b>. EIOPA's crisis prevention tasks can be split into three dimensions:</p> <ul style="list-style-type: none"> <li>• The internal dimension, defining processes and procedures for EIOPA to be prepared for and act efficiently in crisis situations;</li> <li>• The micro-prudential dimension, which focuses on risks affecting individual institutions, in particular, with respect to those that may pose a systemic risk; and</li> </ul> <p>The macro-prudential dimension, which seeks to identify sources of systemic risk and potential macro-prudential measures to address them.</p>	<p>EIOPA should be more proactive in its role of coordinating a centralised EEA crisis management plan.</p> <p>The PRA already acted on its own, we need some similar measures at EEA level.</p> <p>It is also EIOPA's responsibility to communicate to avoid a market confidence crisis.</p>
<p><b>EIOPA risk and Financial stability committee</b> (<a href="#">link</a>)</p> <p><i>The Risks and Financial Stability Committee (RFSC) contributes to EIOPA's role and tasks related to preserving the stability of the EU insurance and occupational pensions sectors in accordance with the EIOPA Regulation. The RFSC identifies, assesses and prioritises financial stability risks and focuses on potential adverse developments that could impact the European insurance and occupational pension sectors.</i></p>	<p>EIOPA already has a Committee in charge of financial stability.</p>