

**Final assessment of V3 EP draft compromise texts - SII 2020 review**

The table below contains the key elements of the V3 compromise texts – further detail on each section is provided below.

Topic	Key positive aspects	Key negative aspects	Key neutral aspects
<b>LTG/LTE</b>	<ul style="list-style-type: none"> <li>• Reduction in <b>risk margin</b> via 4.5% Cost of Capital and lambda factor.</li> <li>• Reduced impact of change to <b>RFR extrapolation</b> changes by a c.15% convergence parameter vs 10% COM (but negatively no specifics for non-Euro currencies).</li> <li>• Simplified <b>LTE criteria</b></li> <li>• No change to <b>risk correction</b> for VA</li> <li>• <b>Symmetric equity</b> adjustment not to apply to unit-linked policies.</li> </ul>	<ul style="list-style-type: none"> <li>• Optional <b>undertaking-specific adjustment</b> for VA remains but is capped at 120% and subject to application criteria.</li> <li>• Removal of EP proposals to expand use of <b>duration-based equity risk category</b>.</li> <li>• Widen corridor <b>of the symmetric adjustment</b> (+/- 17%).</li> </ul>	
<b>Macroprudential</b>		<ul style="list-style-type: none"> <li>• Extension of NSA powers to restrict dividends, buybacks etc before SCR breach where liquidity risks exist.</li> <li>• Reintroduction of <b>NSA powers before SCR breach</b> in case of exceptional sector-wide shocks.</li> </ul>	
<b>Sustainability</b>	<ul style="list-style-type: none"> <li>•</li> </ul>	<ul style="list-style-type: none"> <li>• <b>SFCR disclosure requirements</b> for climate sensitivity analysis.</li> <li>• <b>'Transition' planning</b> requirements introduced. These are broadly consistent with CRD but lacking text on</li> </ul>	<ul style="list-style-type: none"> <li>• Requirement to consider previous analysis when doing <b>sensitivity analysis</b> in ORSA.</li> <li>• EIOPA mandated to assess and report to the Commission on whether and to what</li> </ul>

		proportionate application for LRPV.	extent <b>biodiversity risks</b> are considered in companies ORSA.
<b>Cross border supervision</b>	<ul style="list-style-type: none"> <li>Extended use of <b>collaboration platforms</b> to share data between NSAs for undertakings deemed to be doing significant cross border activities.</li> </ul>	<ul style="list-style-type: none"> <li>Definition of <b>significant cross border</b> supervision remains quantitative and is reduced to 15% of GWP or €30m.</li> </ul>	<ul style="list-style-type: none"> <li>EIOPA to report on continued appropriateness of <b>ban on composites</b> by 28 June 2024.</li> </ul>
<b>Proportionality</b>	<ul style="list-style-type: none"> <li>Captives automatically defined as LRPV</li> <li>Change in traditional investment criteria</li> </ul>		
<b>Reporting and external audit</b>	<ul style="list-style-type: none"> <li>No mandatory reporting of SF SCR for <b>internal model</b> users.</li> </ul>	<ul style="list-style-type: none"> <li><b>External audit</b> requirement for balance sheet</li> <li>No reduction in <b>SFCR</b> burden</li> <li><b>Directive transposition timeline</b> <ul style="list-style-type: none"> <li>Jan 26 – transposition</li> <li>Jan 27 – application</li> </ul> </li> </ul>	
<b>Group supervision</b>	<b>Trigger inversion/Group MCR</b> (Art 230) reverts to Commission proposal	<ul style="list-style-type: none"> <li></li> </ul>	<ul style="list-style-type: none"> <li><b>FICOD review</b> by 31 Dec 2024.</li> </ul>
<b>Other areas</b>	<ul style="list-style-type: none"> <li>Removal of <b>UK data</b> from the calibrations of SCR/MCR parameters.</li> </ul>		

## LTG/LTE Compromise

### **Risk margin**

- **Maximum Lambda** set at 0.925, as stated in recital 33a (*"The parameter should be set as to ensure that the cost of supporting long-term risks beyond 8 years are reduced by at least 50% from the current levels."*).
- **CoC** set at 4.5%, explicitly stated in amendment to Article 77d, 5a.

### **Extrapolation:**

- **First Smoothing Point (FSP) for the Euro** remains at 20 years, as per previous version.
- **Convergence parameter** set at around 15% (UFR weight past 40 years shall be at least 82% instead of 85%).

### **Volatility adjustment**

- **Optional undertaking-specific adjustment remains, subject to supervisory approval, with a cap of 120% and application criteria.**
- **No changes to the calculation of the risk correction.**

### **Interest rate risk**

- Calculation of stressed curve to be aligned with the **extrapolation of interest rates** as per Article 77a.
- Negative term-dependent **floor** whose calibration shall ensure a sufficiently small likelihood of interest rates not being at all times above it.
- Mandatory phasing-in over a period of up to five years for all undertakings.

### **Long term equity**

- **Removal of the requirement for the long-term equity portfolio to be assigned to cover best-estimate of portfolio of liabilities.**
- **Removal of the requirement to identify the assigned portfolio of assets and liabilities.**
- Requirement for the undertaking to demonstrate that it can maintain the sub-set of equity portfolio over the holding period which should exceed 5 years on average.
- Removal of any diversification requirements.

### **Symmetric equity adjustment**

- **Unit-linked life insurance policies excluded.**
- **Corridor of the symmetric adjustment set to +/-17%.**

### **Other areas**

- **Removal of amendments on the duration-based equity risk sub-module.**
- EIOPA review of all standard formula parameters by 2025 and every 5 years thereafter.
- **New recital 43b - Co-legislators should be consulted beforehand on any proposal amending the Delegated Acts (Recital 43b).**
- **Recital (n.83) requires the removal of UK data from the calibrations of the SCR/MCR parameters.**
- Recital 3a directing any freed-up capital to productive investments, and not to shareholder distributions and bonuses, is maintained.

## Macroprudential

### **Article 144a: Liquidity risk management**

- Not many changes compared to the previous version, according to which, undertakings shall maintain and keep up to date a liquidity risk management plan to ensure that they are able to meet their financial obligations even under stressed conditions.

- The draft regulatory technical standards, to be developed by EIOPA, will not be required to specify the format of the LRMP nor the nature of the stressed conditions.

#### **Article 144b: Supervisory powers to remedy liquidity vulnerabilities in exceptional circumstances**

- **Compromise text broadly reverts to Commission original idea but now includes additional powers for NSAs to restrict dividends, buy-backs, bonuses and suspend redemptions rights in exceptional circumstances and in case of imminent risk of non-compliance with SCR where extreme liquidity risks are identified.**
- Some additional safeguards and restrictions on supervisory powers of application are included vs the Commission proposal including
  - Restriction of NSA powers to affected undertakings (rather than the entire market)
  - **EIOPA or the ESRB can issue an opinion in case a supervisory power is considered as excessive.**
  - Member States shall ensure proper coordination and close cooperation between appointed authority and the supervisory authority.
  - Removal of requirement to notify EIOPA/ESRB, and receive their positive opinion, before suspending policyholders' redemption rights.

#### **Article 144c: Supervisory measures to preserve the financial position of undertakings during exceptional sector-wide shocks**

- **Article 144c is reintroduced.**

#### **Other**

- **Extension of recital 21 to require u/kings to consider macroprudential analysis in their underwriting activities (as well as investment and risk management activities proposed by Commission).**

### Sustainability & governance

#### **Transition plans**

- New requirement – broadly similar to the one introduced in the banking package/CRD art 76(2) - to have transition plans, without using the label 'transition'.
- A description of the implementation of the 'transition' plan is to be included in SFCR.

#### **Climate scenario analysis**

- Requirement to consider the performance of previous climate change scenarios.
- **Description of results of the analysis to be included in the SFCR.**

#### **EIOPA mandates on prudential treatment of sustainability-related assets and activities**

- Added 'fossil fuel related assets' and 'biodiversity-related risks' to EIOPA mandate
- **Other changes maintained from the previous version of the compromise**
  - Requirement for ESAs to develop guidelines on ESG stress test and ESAs shall investigate how social and governance related risks can be part integrated into stress test.
  - Simplified reporting for LRPUs is proposed, including amendment of CSRD (DIR 2013/34/EU)
  - New recital noting that numerous legislative initiatives have recently been proposed and adopted to improve resilience and contribution to sustainability, in particular in relation to sustainability reporting.
  - LRPUs – written policies may perform a less frequent review every 5 years (instead of 3 years)
  - Prudent Person Principle includes explicit reference to long-term impact on ESG factors.

## Cross-border activities

### **Cross-border supervision**

- Significant cross-border activities defined to be activities carried out under FoS and FoE which exceed 15% of company's GWP or €30 million.
- Mandatory collaboration platforms to be set up for undertakings (intending to) carrying out significant cross border activities.
- Power for EIOPA to issue a recommendation to NSA in case of disagreement within collaboration platform. Recommendation can be made public with naming of company if recommendation is not complied with within 2 months.
- Host member state powers to request joint on-site inspection in case of significant cross-border activities.

### **Ban on composite undertakings**

- EIOPA required to prepare a report by 28 June 2024 on whether the ban on composite undertakings remains justified or not.

## Proportionality

*Note: Only limited changes compared to the previous compromise (ie, change of the non-traditional investment criterion and captives are automatically classified as LRPV)*

### **Low risk profile undertaking (LRPV) status**

- Reinsurers cannot be LRPV
- Captives are LRPV by default
- IM companies can be eligible for LRPV status
- Proportionality shall be applied in particular to LRPV, but not exclusively.
- **Increase group threshold** to be excluded from SII to 50Mio of GWP
- Simplifications in the standard formula: LRPV should be able to use at all times a simplified calculation for a specific (sub) risk module.
- All captives are automatically classified as LRPV (Art 29a(1a)/New Recital 14)

### **Low risk profile undertaking (LRPV) criteria**

- See annex.

## Reporting & external audit

### **SFCR**

- SFCR follows EC proposal, ie SFCR is split in two parts, but the part addressed to other market participants is still very extensive.
- Art 256 was included on group SFCR. This is merely an editorial change and EP follows the EC proposal in this area

### **Internal model reporting**

- No new requirements for internal model users to report SCR based on the standard formula. Compromise proposes to revert to current text and modifies recital 44 accordingly.
- Removal of previous EP proposal to re-evaluate an approved internal model every five years.

### **Information for supervisory purposes (Art 35)**

- RSR for LRPV:
  - Every 5 years instead of every 3 years for LRPV
  - Every 3 years for other (re)insurers.

- The NSA can ask for more frequent RSR reporting, when it is duly justified
- The principle of proportionality that should be taken into account.
- EIOPA to report to Commission on how to reduce compliance costs for LRPUs as part of proposed report on developing integrated data collection.

#### **Limitations and exemptions (Art 35a)**

- Added the word collectively: *'The limitations regular supervisory reporting shall be granted only to undertakings that **collectively** do not represent more than 20% of a MS market.'*
  - A similar change is proposed for exemptions.
- Deleted text, in line with council proposal. Following the deletion, NSAs have the possibility to exempt insurers that are part of a group from reporting on an item-by-item basis. These insurers no longer have to demonstrate to the satisfaction of the NSA that reporting on an item-by-item basis is inappropriate.
- Limitations and exemptions shall not apply to undertakings that have capital add-ons set.

#### **Reporting deadlines – art 35b/256b**

- Added requirement to consult EIOPA when deadlines need to be changed due to emergencies and extension in deadlines is for a limited time period only.
- Added specification that at the request of one MS, EC shall consult EIOPA to determine whether the conditions for a temporary change of the submission deadlines have been fulfilled.

#### **External audit requirement (Art 51a/256c):**

- In line with the EC proposal, there shall be an external audit requirement for the balance sheet disclosed as part of the SFCR (both solo and group SFCR)
- The scope of the external audit seems to be limited to the balance sheet (recital 30)
- Removed from the previous compromise: *'Each year, only 10% of the undertakings identified by the supervisory authority on the basis of a random selection shall be subject to such an audit.'*
- LRPUs are also subject to external audit requirement (Deletion of recital 31)

#### **Transposition of Directive**

- A new timeline for transposition is proposed; transposition to be completed by 1 January 2026 with application to start on 1 January 2027.

#### **Group supervision**

##### **Min Group SCR/Trigger inversion Art 230:**

- Revert to Commission solution proposed for trigger inversion, and definition for minimum consolidated group SCR.
- However, this proposal does not solve the double counting issue

##### **FICOD review**

- Art 228 - EC mandate for a FICOD review by 31 Dec 2024

##### **Compromise proposes a number of other changes, including but not limited to:**

- Deletion of recitals related to scope (recital 61 on de facto groups and NSA powers to change organisational structures)
- Reversion to COM proposal on calculation of currency risk in group solvency (Art 233a)
- Reversion to COM proposal on system of governance (Art 246)

##### **Several amendments are maintained from previous version of the compromise:**

- On Definitions - Deletion of 212 (4)-(6):

- a parent undertaking/subsidiary undertaking of that group is also the ultimate participating undertaking of another group, this group would also be considered in the scope of group supervision
- factors for NSAs to take into account when identifying a relationship within a group
- when a group fails to designate a parent undertaking, NSAs shall designate a parent undertaking which is to be responsible for complying with this Title. The other undertakings in such group shall be considered as subsidiary undertakings.
- On Scope of group supervision - Article 213 (3a-3c)
  - Deletion of 3b: no additional powers for NSAs to require the change of internal arrangements and requirement to restructure groups.
  - Deletion of 3c: no additional powers for NSAs to require the establishment of an IHC/MFHC with head office in EU...
- On proportionality of groups – Art 213a
  - Condition added to be eligible as LRPV: “the consolidated group Solvency Capital Requirement is complied with and a capital add-on in accordance with Article 232 has not been set “
  - 25% cross border criterion/deletion of the 1bn and 100Mio/30% for non-traditional invest criterion.
  - IM companies also eligible for LRPV status, subject to NSA approval

#### Annex: Criteria for LRPU status

- Life:
  - IRR submodule < 5 % of TP
  - 1Bn TP as proposed by the EC
  - cross border activity should be non-significant
  - the gross market risk module referred to in Article 105(5) is not higher than 20 % replaces the previous non-traditional investments criterion of max 30%
  - Reinsurance business accepted does not exceed 50 % of annual GWP income
  - SCR is complied with and no capital add ons set
- Non-life
  - Average combined ratio of the last 3 years < 100%
  - cross border activity should be non-significant
  - Annual GWP <= 100Mio
  - Sum of annual GWP in classes 4 to 7, 14 and 15 < 30% of total annual non-life GWP
  - the gross market risk module referred to in Article 105(5) is not higher than 20 % replaces the previous non-traditional investments criterion of max 30%
  - Reinsurance business accepted does not exceed 50 % of annual GWP income
  - SCR is complied with and no capital add ons set
- Composites:
  - IRR submodule < 5 % of TP
  - Average combined ratio of the last 3 years < 100%
  - Max 1Bn of TP
  - Annual GWP <= 100Mio
  - cross border activity should be non-significant
  - Sum of annual GWP in classes 4 to 7, 14 and 15 < 30% of total annual non-life GWP
  - the gross market risk module referred to in Article 105(5) is not higher than 20 % replaces the previous non-traditional investments criterion of max 30%
  - Reinsurance business accepted does not exceed 50 % of annual GWP income
  - SCR is complied with and no capital add ons set
- **Traditional investments** include real estate, loans including private loans, promissory notes and mortgages and exclude investments covering unit-linked contracts
- Process:
  - NSA may oppose the classification as LRPU if the undertaking represents more than 5% of the life or, where applicable, non-life insurance market of the home MS of the undertaking.
  - In case of serious concerns, NSAs may ask, in exceptional circumstances, undertakings to refrain from using one or more proportionality measures. And NSAs need to duly justify this in writing
- **Prop measures:** LRPU can benefit from all prop measures, except the exemption from Climate change scenario analysis
- Criteria for application of proportionality for non-LRPU
  - Removal of requirement to have declaration that the undertaking does not plan any strategic change that would have an impact on the risk profile of the undertaking within the next three years.
- Monitoring use of proportionality measures: art 29e was deleted