

To: Didier Millerot
Head, Insurance and Pensions Unit
European Commission

Our reference: ECO-19-066

Subject: Follow-up on publication of Solvency II DAs in the Official Journal of the EU

Brussels, 11 July 2019

Dear Didier,

We would like to follow up on the recent publication of the Solvency II Delegated Acts. We appreciate that some much-needed improvements and simplifications have indeed been achieved, however these are outweighed by the lack of progress on key issues impacting the insurance industry's ability to maintain and develop its long-term products and investments.

Below we set out the industry's views on three key elements of the Delegated Acts.

1. Interest rates

We welcome the new text introduced by the Commission in Article 43 regarding the determination of the risk-free interest rate term structure (which includes key elements such as the UFR and the LLP). The text brings important clarifications about the Commission's and EIOPA's roles and responsibilities.

In our reading of the new text, there are key implications for the UFR:

- First, should EIOPA pursue further changes to the UFR, we would expect it to submit such proposals to the Commission (Art 43.3), together with "*an assessment of the appropriateness and impact of proposed modifications*" (Art 43.4).
- Second, we believe there are good reasons for the Commission to reject further changes to the UFR from the current level of 3.9%.

The UFR is an extremely important factor in the determination of the Solvency II discount rate. It was defined and intended as a stable and long-term parameter (ie 100 years) in order to avoid being itself a source of artificial volatility. Under EIOPA's methodology, the current low interest rate environment has an unjustifiably high impact on the UFR, which should actually represent a long-term equilibrium rate.

Any changes to the UFR should take into account the overall level of prudence of the Solvency II framework, as well as potential unintended consequences of such changes, in particular for long-term business. We call for no further changes to the UFR.

2. Risk margin

The excessive size and interest-rate sensitivity of the risk margin ultimately impact the cost and nature of products that can be offered by insurers, and affect long-term products in particular. It is very important to investigate whether the current approach leads to appropriate and reasonable levels of risk margin. As we have noted on a number of occasions, the 2018 review was a missed opportunity to lower the cost of capital to an appropriate calibration.

The industry provided extensive evidence that a decrease from 6% to 3% can be technically justified. Nevertheless, the Commission decided to follow EIOPA's advice to retain the status quo. We would therefore like


to reiterate our findings that EIOPA's technical work made a number of assumptions that are technically not fully sound and are excessive. We naturally welcome the fact that the Commission has asked EIOPA to work on a wider review of the risk margin in the 2020 review, including both the cost of capital and the design of the risk margin. We expect EIOPA to dedicate appropriate resources to this workstream and to take a critical look at its own work in the 2018 review.

3. Long-term equity

We welcome the Commission's recognition that changes in the capital charges for long-term equity investments are justified. It now remains to be seen whether the proposal will be effective in practice and, if so, how effective. We encourage the Commission to seek practical evidence of whether and how this measure supports long-term investments, as envisaged by the CMU, and to consider what further action may be needed as part of the 2020 review to achieve the intended outcome.

Looking ahead, we look forward to engaging with you during the 2020 review. It will be important to make an overall assessment of the Solvency II calibration, which we believe is already very heavy from a capital requirements point of view, and it will be equally important to avoid a piecemeal approach. The 2020 review is a key opportunity for industry and policymakers to work together towards improving Solvency II so that it fulfils its potential as a world benchmark and a risk-based framework that protects European consumers without diminishing the industry's potential to provide protection and contribute to long-term sustainable growth.

Yours sincerely,



Olav Jones
Deputy Director General