

To: Economics and Finance Committee

From: ECOFIN Team

Meeting: 6 March 2019

Reference: ECO-19-012

Subject: Solvency II - 2020 review – Insurance Europe Survey

## Objective

For information

## Comments

The aim of this background note is to provide feedback on the recent members survey (ECO-19-002) on the 2020 review. Please note that this survey was launched by the secretariat before the EC published its call for advice and its aim was to improve the understanding of members' views at this stage on the various topics.

Following the Ecofin discussion, the secretariat will begin a process of identifying priorities and an agreed "package" of improvements for the 2020 review – this process will make use of this survey – but also allow sufficient time for discussion between members and companies, especially in light of the EC call for advice and the ongoing developments in the Joint Industry Technical Workshops.

The secretariat received responses from 15 members, as follows:

AT; BE; CH; CZ; DE; DK; ES; FI; HR; IT; NL; NO; SE; SK; UK

## Summary

<b>Which of the following are priority issues for the 2020 review in your market?</b>				
Issue	Not sure yet	High priority	Low priority	Not a priority
LTG - Volatility adjustment		11	2	2
LTG - Matching adjustment		5	2	8
LTG - RF curves – Ultimate forward rate (UFR)	1	6	7	1
LTG - RF curves – Last liquid point (LLP)		9	5	1
LTG - RF curves – Convergence point	1	6	6	2
LTG - RF curves – SW extrapolation methodology	3	1	7	4
LTG - RF curves – Credit Risk Adjustment	1	2	9	3
LTG - Duration-based equity risk submodule	1	1	3	10
LTG - Symmetric adjustment to equity risk	1	3	5	6
LTG - Extension of recovery period	3	1	3	8
LTG - Transitional measures (TRFR/TMTP)	1	4	1	9
Risk margin		15		
Recalibration of market risk SCR (including DVA)		12	3	
Improvements to reporting	1	13	1	
Making proportionality work in practice	2	10	3	
Other issues	4	4	2	2

Note that agreement on priority issues does not necessarily mean that members' positions are aligned.

A summary of the feedback received is provided below.

### **LTG measures**

#### *Volatility adjustment*

- Generally support for further investigation of both the recalibrated VA and the redesigned VA.
- The functioning of the national market component should be improved.
- The illiquidity of underwriting cash flows should be considered in the calculation of the VA.
- Some members support the inclusion of non-fixed income spreads in the calculation.

#### *Matching adjustment*

- There should be no erosion of the current benefit provided by the MA and, if any changes, these should only be targeted at expanding the current scope of application.
- Certain criteria should be reviewed, such as ring-fencing requirement, eligible assets and cashflow matching.

#### *Risk-free curves*

- Majority of members support no change to derivation of risk-free rates curves (ie no change to LLP, extrapolation, convergence). However, there are views that it is not credible to fight the change in LLP.

#### *Transitional measures*

- No detrimental changes to the transitional measures eg. early removal of the measures (in particular the transitional measure on technical provisions (TMTP)).

### **Risk margin:**

- CoC should be recalibrated to a lower value.
- Support for a review of design and assumptions.
- Some members made suggestions on how the actual formula should be updated including how diversification is accounted for in the formula and the design of the cost-of-capital rate.

### **Recalibration of market risks:**

- Some members support no change to the current design of the interest rate risk submodule. Others request refinements to EIOPA's proposed shifted approach eg. calibration and extrapolation methodology.
- Members also noted that extensive testing of any interest rate proposal and its interaction with other changes, eg. VA, is required.
- Any further changes to equity risk is dependent on the final drafting of the EC's 2018 long-term equity proposal.
- Broad support for the improved recognition of insurer's long-term investment in corporate bonds through a recalibration of the spread risk submodule or the inclusion of a dynamic volatility adjustment.
- Property risk is widely considered to be too high and in need of recalibration. Some members support increased granularity (eg. different capital charges for geography/property type) .
- The criteria for exemptions within the concentration risk submodule do not work properly.
- Some support for the recalibration of the market risk correlation matrix.

### **Liquidity testing**

- Members noted interest in a more detailed understanding of how the test would work in practice.

### **Improvements to reporting:**

- Redesign and simplification of the SFCR/RSR.
- Quantitative reporting needs to be more risk-oriented instead of one size fits all. Well capitalised companies with stable risk exposure should have to report less information less frequently.
- Remove redundancies.
- Reduce burden of reporting requirements for smaller insurers.

**Making proportionality work in practice:**

- Inclusion of a proportional Solvency II regime for small insurers with a simple risk profile, based on risk oriented criteria.
- The requirements to apply proportionality could be simplified.
- Should have a clear commitment on proportionality and complexity within colleges for groups.
- Increase of thresholds for the exclusion from the scope of Solvency II.

**Other issues** that were raised by members in the survey include:

1. *Issues that are already reflected in the EC's Call for Advice:*
  - Calibration of the mass lapse scenario (and use of USP for mass lapse)
  - Calibration of longevity scenario.
  - Recognition of non-proportional non-life reinsurance.
  - Opposition to EIOPA's ambition to include insurance guarantee schemes (IGS), recovery and resolution and macro-prudential issues/tools in the 2020-review.
  - Own funds: change of sub limits (apply 33% for tier 3; relate to own funds instead of SCR).
  - Treatment of non-equivalent insurers.
  - Treatment of intra-group transactions.
  - Group consolidated Minimum Capital Requirement.
  - The need for a holistic and comprehensive impact assessment.
  
2. *Issues that are not reflected in the EC's Call for Advice:*
  - Inclusion of climate risks in the SCR (heavy rain and cloud bursts).
  - Inclusion of LAC TP in the non-life underwriting SCR calculation.
  - Recalibration of CAT risks.
  - Treatment of currency risk for groups.
  - Geographical diversification within premium and reserve risk.
  - Contract boundaries.
  - Group: Treatment of Other entities
  - The risk measure in the fire risk submodule.
  - Extending the recovery period after SCR breach.
  - Removing interest rate dependency in some calculations (like RM, SCR Longevity).
  - Intra-group outsourcing should not be subject to the same requirements as outsourcing to third parties.
  - Transition to the new risk-free rate in the euro area, from IBOR to ESTER.
  - Design of the operational risk submodule.
  - LAC DT.
  - Exclusion of unit-linked assets from look-through approach (inc. reporting obligations).
  - Underwriting risks for multiyear contracts.
  - Netting arrangements should be excluded from the absolute precedence of insurance claims (Art. 275 (1) (a)).
  - Recognition of expected profits/losses for Non-Life and Health-NSTL underwriting risk.