Any views provided in this presentation are tentative views at working group level and should not be understood as EIOPA positions.

EUROPEAN INSURANCE AND OCCUPATIONAL PENSIONS AUTHORITY

MA approach 2

Workshop on 2020 review
Frankfurt, 5-6 June 2019

MA approach 2

Call for Advice

EIOPA is asked to assess the efficient functioning of the volatility adjustment and the matching adjustment as mechanisms to prevent pro-cyclical behaviour on financial markets and to mitigate the effect of exaggerations of bond spreads, in view of a level playing field in the EU and policyholder protection.

The Commission services are envisaging to assess possible approaches to review the design, calibration and functioning of the adjustments, whilst not precluding the possibility of a single adjustment mechanism.

EIOPA is asked to provide an assessment of the quantitative impact on the calculation of the best estimate and the solvency position of insurance undertakings of the following approaches for the calculation/application of the matching adjustment: […]

-Approach 2: *a review of the criteria for eligible assets for the use of the matching adjustment, including their cash-flow characteristics and credit quality*.

MA approach 2

Description

The purpose of the MA is set out in recital 31 of the Omnibus II directive. It is based on assumptions such as:

- Undertakings with matched asset and liability cash flows are able to obtain additional risk-free returns via a buy-and-hold strategy.
- Undertakings will earn the MA so long as the fundamental spread allows for the costs of default and managing the portfolio to maturity.

Solvency II sets out only a few criteria for asset eligibility :

- They must be “bonds or other assets with similar cash flow characteristics” (Article 77b(1a)); and
- They have to have “fixed cashflows” as defined in Article 77b(1h).

The literal application of those requirements can result in unintended outcomes in that assets that may be suitable to back MA-eligible business cannot be allowed in the MA portfolios, and conversely, that it may be possible to engineer for assets that are not suitable to meet these requirements.

MA approach 2

Options under discussion

- **Option A**: allow a '**yield-to-worst**' treatment for assets that have a finite configuration of cash flows (but the cash flows are otherwise fixed once a configuration is determined). Specifically, undertakings would be required to use (in the matching analysis and in the calculation of MA) the configuration that resulted in the lowest possible MA benefit.
- **Option B**: clarifying a **look through principle** for MAP assets whose cash flows depend on the performance of other underlying financial assets. This principle would allow NSAs to exclude structured assets from the MAP where the underlying assets are not suitable to match MA liabilities, in particular because they are not sufficiently fixed in term (e.g. real assets such as equity etc.)

Questions to stakeholders

- What do you think about the options?