Delivering on the agreed ambitions for the Solvency II review

Insurance Europe's views on the development of Level 2 and Level 3 texts

Introduction

Insurance Europe welcomes the Solvency II Directive review agreed in December 2023. In particular, the insurance industry welcomes the improvements made by the EU co-legislators in the areas of capital and volatility. The improvements on proportionality for Small and non-complex undertakings (SNCUs) is also welcome but overall the review will result in higher operating burdens and costs, which is disappointing.

If implemented appropriately, the changes can help insurers better serve customers, unlock more investment for the green and digital transitions, and support progress towards completing the EU's Capital Markets Union, while maintaining the high level of policyholder protection of the framework.

However, in order to realise the potential benefits, the technical details in Level 2 and 3 implementing regulation and guidelines need to be fully aligned with the high political ambition resulting from the Level 1 Directive review. While the upcoming Level 2 empowerments likely cover mostly technical details, they can have a significant impact and getting them right is essential for the overall outcome of the review. In developing the Level 2 and 3 details, the industry also urges the legislators to always keep in mind its commitment to reduce the overall reporting burden.

A timely publication of the amending Directive, alongside the Level II (and III) texts is also crucial. These documents are relevant for insurers as they prepare for the implementation. It is equally important for insurers to gain insights in a timely manner, well before the new rules take effect, into the quantitative impacts of the review, for example in terms of the Solvency II ratio.

In the following paper, Insurance Europe outlines the key priorities for the development of Level 2 and Level 3 regulations and the necessary steps to ensure alignment with the overarching goals of the Solvency II Directive review.

Improving the treatment of long-term business

Extrapolation of RFR curves

Stability of the illiquid part of the Risk Free Rate (RFR) curves is paramount to avoid introducing even more artificial volatility.

The technical parameters of the new extrapolation methodology which determine the starting point (the FSP) and the convergence to the UFR (the speed of convergence) should be chosen to minimise artificial balance sheet volatility, avoid incentives for procyclical behaviour, and avoid pushing insurers towards extensive derivative usage.

DO

- Set the convergence parameter to be at least 15% (and 70% for the SEK).

The Directive sets a minimum value for this parameter at 11% but a higher parameter is needed to ensure stability of the framework. It is important to ensure an appropriate treatment of the extrapolation parameters also for other non-euro currencies (such as SEK and NOK), based on the local market conditions.

DO

- Set the residual volume criterion above the existing 6% for the Euro to ensure stability of the extrapolation.

The residual volume criterion is one of two the criteria which determines the first smoothing point (FSP) of the extrapolation. It is set as the percentage of bonds outstanding of that or a longer maturity among all bonds outstanding in that currency (Art 77 para 1b) which are of a greater maturity than deemed to be sufficiently high.

The rationale behind this criterion is the fact that insurers primarily use bonds and loans to hedge their liabilities. For maturities where bonds and loans are less available a stable extrapolation methodology is necessary to avoid unnecessary volatility.

The stability of the extrapolation methodology and ability of insurers to hedge using bonds was fundamental in the development of the LTG measures. To supplement the residual volume criterion, an additional criterion called the matching criterion was also agreed to be used to determine the starting point of the extrapolation. In the development of the new extrapolation methodology, EIOPA proposed to retain this criterion but to implement it via the residual volume criterion . This intention for stability should be reflected in the determination of the residual volume criterion.

Equally significant is the requirement to align with the FSP parameters established in the Directive. Specifically, the FSP for the euro is set to 20 years at the date of entry into force of the amended Solvency II Directive and it is crucial to choose the parameters in such a way that the FSP remains consistent over time to avoid introducing volatility. It should be avoided that a significant change of the FSP only short-term after the entry into force cancels out this deliberate political commitment at Level 1.

In addition, it should be recognised since Delegated Regulation 2015/35 came into force, the proportion of bonds held by the ECB has risen sharply. These bonds held by the ECB are no longer available for insurers to hedge their liabilities and could impact the outcome of the residual volume criterion.

To address these concerns, it is recommended that for the residual volume criterion the percentage of bonds outstanding with higher maturity be revised upwards to provide the stability of the extrapolation which is needed for insurers with long-term liabilities.

Volatility adjustment

The co-legislators agreed to several improvements to the design and functioning of the volatility adjustment including improved reference portfolios, the macro-VA, an increased general application ratio (GAR) and the credit spread sensitivity ratio.

However, these improvements would be undermined by a poor design and calibration of the risk correction parameter, particularly in a crisis period when the efficient functioning of the VA is most critical.

DO

- Avoid adding procyclicality to the framework, by designing and calibrating the risk correction parameters which provide a realistic assessment of the default and downgrade risk associated with the reference portfolio.

In the calculation of **risk corrected spreads,** it is crucial that the portion of the spreads attributed to expected losses and unexpected risks does not exceed a realistic size. This ensures the effectiveness of the VA. Thus, in its sectional calculation, the respective percentages and the foreseen cap of the risk correction should be set such that they have a significant effect in periods of volatility, such as those observed in the last decades, in particular the short-term spread widening at the onset of the COVID- 19 pandemic and during the great financial crisis.

Regarding the **spread calculation,** it is not supported to remove the zero floors applied to government and corporate bond spreads. Bonds that exhibit a negative spread to the risk-free rates are assessed as extremely safe by the market. Therefore, there should either be no further deduction for risk correction or a zero floor for the spread in the VA calculation.

Risk margin

The co-legislators have set the cost of capital rate at 4.75% in the Directive which is welcomed as a key change that reduces currently excessive capital requirements for all the undertakings.

This should be complemented with a lambda parameter which further mitigates excessive and volatile capital requirements for long-term products.

DO

- Set the lambda parameter below a maximum of 0.975, without a floor.
- Allow for a risk margin that is either diversified or that is calculated at group level.

A lambda calibration of 0.975 was supported by the Commission outlined in its Communication on the review of the EU prudential framework for insurers and reinsurers in the context of the EU's post pandemic recovery. A similar calibration was supported by EIOPA's analysis and included in its advice.

Those proposals will help reduce the unnecessarily high costs of long-term liabilities and reduce volatility. However, further improvements on the calibration for the lambda parameter remain needed and justified so that, in conjunction with the changes to the cost of capital, they would reduce the overall size and volatility of the risk margin by at least 50%.

Furthermore, regarding groups, the risk margin should be either diversified or calculated at group level to be consistent with the reality of how insurance groups are managed in practice and with the treatment of diversification within the SCR.

[1] See EIOPA background document on the opinion on the 2020 review of Solvency II, para 2.95

Interest rate risk SCR

The industry welcomes the agreed amendments to Art 111 to extrapolate the illiquid part of the yield curve also for the interest rate risk and to introduce a term-dependent floor to the interest rate risk scenarios. A floor is necessary to reflect the economic reality of an effective lower bound to the interest rate curve and to avoid excessive capital requirements in stressed environments which could result in procyclical behaviours.

DO	DON'T
Calibrate a realistic term-dependent floor to the down interest rate risk SCR scenario. Review the interest rate risk SCR calculation method to reflect the amendments to Art 111 on extrapolation of the stressed yield curves. Recognise diversification of risks between currencies by the possibility to offset respective losses. Update the correlation between interest rate risk down and spread risk to be 0.25, as per EIOPA's advice.	Introduce mandatory phasing-in of the updated interest rate risk scenarios. Stress the Ultimate Forward Rate (UFR) as a very long-term target value.

Equity investment

Long-term equity

The industry welcomes the inclusion of workable and simplified criteria for long-term equities (LTE) in the Directive. These should be complemented with Level 2 provisions that mirror the co-legislators' ambition and ensure a smooth and extensive usage of the LTE classification.

DO	DON'T
Clarify that the criteria for equity collective investment undertakings to be assessed at the level of the fund and not at the individual security level are not too restrictive and overly complicated.	Introduce overly complicated or excessive conditions in the Delegated Acts which would restrict supervisors' ability to recognise equities as long-term.

This is consistent with the portfolio-level approach foreseen in the LTE criteria, i.e. (b), (d), and (f).

Symmetric equity adjustment

The current design of the symmetric equity adjustment creates basis risk for a number of countries, due to differences in currencies and equity portfolio composition. This is particularly the case for some insurers who have large unit-linked portfolios for whom the application of the symmetric equity adjustment creates, not mitigates, solvency volatility.

It is also the case for type 2 equities which includes all assets that do not fit anywhere else in the standard formula [among others, funds for which no look-through is possible, commodities and alternative investments and the two equity risk types for infrastructure (unless they are exchange-traded companies)].

These problems are increased by the widened corridor in the co-legislator's draft agreement of the Solvency II-review.

DO

- Either make it at the company's discretion to apply the symmetric equity adjustment or improve the design of the adjustment to avoid creating artificial solvency volatility for some insurers.

Proportionality

Improving proportionality was one of the core aims of the 2020 review, by raising the thresholds for the application of Solvency II and allowing small insurers – fulfilling a set of predefined criteria – to automatically benefit from simplifications and proportional measures and as such creating a more suitable framework for insurers identified as "small and non-complex" (SNCU).

- **SNCU classification:** The amended Directive allows small insurers – fulfilling a set of predefined criteria – to be automatically exempted from specific Solvency II rules and as such creates a more suitable framework for insurers identified as ''small and non-complex'' (SNCU). Given that the SNCU definition is already very narrowly defined in the Directive, when drafting the Delegated Acts (DA), the EC has to ensure that the scope of application should be as broad as possible and without additional requirements.

- **Non-SNCUs:** To make proportionality work for non-SNCUs, simple and straightforward procedures are needed for supervisory approval. Insurers narrowly missing the SNCU criteria (e.g. just over 100 Mio gross written premiums re size criterion), should receive approval for identical proportionality measures as SNCUs, including simplified reporting requirements under the new Art 19a (6) of the Accounting Directive. Refusal of proportionality measures should only be possible in exceptional cases of serious concerns regarding the insurer's risk profile.

  EIOPA will have to annually report (Dir Art 52(2)) on the utilisation of proportionality measures by insurance companies/groups in each Member State. To ensure comprehensive and consistent application of proportionality measures across Europe, it is proposed to establish a national target market share of at least 20% for granting proportionality measures to non-SNCUs in each Member State. This aligns with the current rules on exemption from quarterly reporting (Dir Art 35(7)).

- **Groups:** Many proportionality measures for SNCUs in groups, that do not meet the overall definition of a Small and Non-Complex Group (SNCG), lead to practical challenges, particularly regarding reporting and planning requirements at group level. While exempt from these requirements at entity level, SNCUs must still comply indirectly with all group-level requirements. These challenges apply to the majority of proportionality measures for SNCU, including RSR frequency (Art 35 para 5a), exemption from QRT/item-by-item reporting (Art. 35a para 2) and many more. To address these issues effectively, it should be allowed at the group level to use historical data for exempted companies or exclude them from consolidation in reports or plans.

DO

- Establish smooth transition rules for expected simplification during the transition period for entities exempted from SII and SCNUs.
- Simplify approval procedures for non-SNCUs to access proportionality measures with clear criteria and target market share.
- Enable effective application of proportionality measures for SNCUs within groups.

Macroprudential supervision

The insurance industry has shown resilience to shocks and crises of the past years, and there is very limited systemic risk in the sector that remains to be addressed. Unnecessary burdens on industry and supervisors that do not lead to a commensurate contribution to financial stability should be avoided.

While recognising the potential benefits of some of these new macroprudential requirements in monitoring systemic risk, it is crucial that implementation (e.g. level 2 provisions according to Art. 144d) is well-balanced and risk oriented.

Macroprudential considerations as part of own risk and solvency assessment (ORSA) and investment strategies (Art. 45, Art. 132)

Regarding the drafting of the Regulatory Technical Standards (RTS) (Art. 144d) on the criteria to be taken into account by supervisory authorities when defining the (re)insurance undertakings and groups subject to the additional macroprudential requirements, a proportionate and risk-oriented approach is crucial. Application of the additional macroprudential requirements should remain limited to exceptional cases with a clear supervisory rationale.

DO

- Limit the scope of undertakings which will have to provide additional macroprudential analyses under the ORSA or Prudent Person Principle (Art 45 (e) and Art. 132 (6)).

Liquidity Risk Management Plans (LRMP, Art. 144a)

Regarding the drafting of the RTS (Art. 144d) a proportional and risk-oriented approach is crucial when specifying the content and frequency of update of liquidity risk management plans and the criteria to be taken into account when defining the insurance or reinsurance undertakings and groups which shall be requested to cover the medium and long term in their LRMP.

With respect to the content and frequency of update of LRMPs, flexibility is needed, e.g. regarding the scope, form and granularity to ensure that the LRMP requirement is risk-oriented and proportionate to an undertaking’s liquidity risk.

Liquidity risk for most insurers is very moderate and already well managed. Therefore, extensive requirements on liquidity planning should be limited to exceptional cases with a clear supervisory rationale.

DO

- Avoid overly prescriptive requirements for liquidity risk management plans and limit the scope of undertakings with additional requirements regarding their LRMP (Art. 144a (2))

Sustainability

European insurers strongly support the drive towards sustainability and are ready to build on their current actions to contribute further to the transition to a more sustainable society and to play their role in achieving the targets of the EU Green Deal.

The industry supports the integration of climate change scenario analysis in the ORSA. Beyond this, the focus of specific plans to monitor and address the financial risks arising from sustainability factors should be limited to the risk management aspects of the transition, such as the strategic risks associated with not implementing transition strategies.

DO

- For the sustainability risk requirements to be developed, avoid creating overlaps and inconsistencies with other cross-sectoral regulation that can create confusion and unnecessary costs and operation burdens.
- Avoid excessive and complex requirements which go far beyond the risk management tools for transition risks which have already been established, e.g. ORSA climate change scenario analysis.
- Restrict the requirements to material financial risks.
- While distinct from requirements for net-zero GHG transition plans, in terms of content it is important to avoid duplications with other regulatory requirements, inconsistencies, unnecessary reporting burden and legal risks. It is also important to allow flexibility for insurers to meet new Solvency II requirements on management of sustainability risks through integrated risk management or transition plans.
- Ensure that group-level plans can be used to satisfy any subsidiary-level requirements.

DON'T

- Do not introduce changes to capital requirements that are not risk- and evidence-based.

Group supervision

Numerous changes were made to the group supervision requirements and extensive additional powers were granted to group supervisors. In particular a solution was implemented to address the issues regarding the scope and the calculation method of the minimum consolidated group SCR, which lead to trigger inversion and double counting.

However, despite the changes double counting will remain an issue due to the extension of the group floor to non-EEA subsidiaries.

DO

- Clarify in the Delegated Regulation (or at a minimum via EIOPA's Guidelines on Group Solvency) that local requirements of third-country undertakings do not have to be factored in if the related risks are already part of the balance sheets of European companies, to the satisfaction of supervisory authorities.

Reporting and disclosure

Standard Formula reporting for internal model users

The agreed SII amendments foresee that internal model users shall provide every two years an estimate of the Solvency Capital Requirement determined in accordance with the standard formula.

The proposals give misplaced recognition and credibility to standard formula results for internal model users. A standard formula comparison for internal model users is an arbitrary tool for such ongoing monitoring because as a capital measure for the average risk profile, it will not appropriately capture changes in atypical risk profiles and give a misleading measure of the change.

DO

- ✓ Ensure that the standard formula <u>estimate</u> is required in a manner that addresses the individual needs of the respective NCAs. Therefore, the format and content should be agreed directly between them, independently from the RSR and Solvency II QRTs processes.

External audit requirement

The agreed SII amendments include a minimum external audit requirement of the balance sheet disclosed as part of the solvency and financial condition report (SFCR). These external audit requirements will be very resource-intensive and entail significant costs for insurance companies.

DO	DON'T
✓ Accept a limited level of assurance in the audit.	✗ Extend audit requirements to Small and Non-Complex Undertakings (SNCUs) or other sections of the SFCR.

The data to be audited is already subject to a significant safeguard mechanism through the supervisory process of regulatory authorities (see, inter alia, Article 36 of the Solvency II Directive).

The industry appreciates the exemption for SNCUs. However, there are concerns about the national discretion to extend this requirement both in terms of scope and content (beyond the balance sheet). In addition, when auditing the balance sheet, the auditor should consider the SCR as a given input. Any detailed examination of the SCR falls under the responsibility of the NSA.

Design of the SFCR

By reviewing the format/content of the SFCR the intention was to enhance transparency, by aligning insurers' disclosures with recipients' – policyholders'/beneficiaries' and professionals' – needs.

While the industry appreciates efforts to improve usability, it emphasises the importance of ensuring that the content of each part of the SFCR effectively meets the information needs of its intended audience. Specifically, the DA should structure the part for policyholders and beneficiaries so that it is a compact report with a target length of not more than two pages, limited to information relevant for this group.

For market professionals, the disclosed QRTs are the most relevant, therefore, narrative information in the SFCR part for market professionals should be kept to a minimum.

DO

- Minimise the SFCR reporting burden by streamlining requirements in the Level 2.
- Ensure that each part of the SFCR effectively addresses the information needs of the intended audience, including both the group-level SFCR and single SFCR.
  - Limit the part of the SFCR for policyholders/beneficiaries to information relevant for their interests with a target length of not more than two pages.
  - Base the content of the part of the SFCR for market professionals primarily on quantitative data without the need for an extensive narrative.
- Envisaged exceptions in the amended directive SNCUs should apply without any further restrictions.
- DO: Assess the SFCR's usage and relevance for recipients within three years of implementing. In case of limited usage and/or relevance, consider limiting it to key indicators or abolishing it.

DON'T

- Extend required content of the SFCR beyond what is foreseen in the SII Directive.

Appropriate implementation of the RSR

The industry welcomes the introduction of a Single Regular Supervisory Report (RSR) for groups. According to Art. 256b paragraph 6 of the amended directive, Delegated Acts shall further specify the information which shall be reported in it.

It must be ensured that the single RSR is designed in a practicable manner. Besides this, it is necessary to reduce the content of the RSR – the single RSR as well as the group and solo RSRs. Overlaps to the ORSA report should be avoided.

DO

- Minimise the RSR reporting burden by streamlining requirements in Level 2.

Revision of ITS on reporting and disclosure

After the amendments to the Solvency II Directive and the Delegated Regulation there will be a revision of the implementing technical standards (ITS) on reporting and disclosure. It should be avoided that this revision introduces new QRTs and thereby increases the reporting burden without clear supervisory need.

DON'T

- Introduce new QRTs without clear supervisory need. Equally, the ITS should not be expanded by other regulations, such as securities holdings statistics.

Other topics

EPIFP

Expected profits in future premiums (EPIFPs) are an important part of the Solvency II framework allowing the reflection of economic reality, with respect to the principle of going concern. As such, they are a useful element, notably to encourage the offer of long-term guarantees, and changes should be avoided for EPIFP at group level and in terms of definitions.

The treatment of EPIFP at group level should remain unchanged, and not be included in the group's regular assessment. EPIFP are the result of a valuation based on economic principles and part of the reconciliation reserve. They are fully recognised as unrestricted Tier 1 items, and there is no justification apparent for a burdensome continuous assessment. Furthermore, Article 330 of the DA already provides the NSAs the power to challenge the availability of own funds items that are assumed available. Supervisors also have the power to review the best estimate calculations, knowing that EPIFPs are just an output of the economic value of insurance liabilities. Creating an availability assessment process specific to the EPIFP, on top of what is already required by Art. 330, would only add burden and uncertainty in the group capital assessment for no purpose. This is especially crucial since the artificial nature of EPIFP makes it particularly difficult for undertakings to provide concrete proof for the availability at group level.

Equally significant is the **accounting mismatch** arising from this change. Both EPIFP and policyholder benefits arise from future gross surpluses. The mismatch arises if, on the one hand, the policyholder participation is recognized as part of the technical provisions, and, on the other hand, the shareholder share of future gross surpluses can only be partially offset. This means that treating EPIFP as not effectively available is also unreasonable from an accounting perspective

DON'T

- Change the treatment of EPIFP in the Level 2, in particular:
  - Do not include EPIFP in the availability assessment of groups.
  - Do not include a definition of gross expected future profit/loss from servicing and management of funds in the DA.

Risk mitigation techniques

Non-proportional (NP) reinsurance is an important risk mitigation instrument for the non-life sector and a crucial tool for smaller and medium-sized companies to manage peak risk.

The current standard formula approach provides only for a flat 20% reduction in the volatility of premium risk for three lines of business. This reduction does not sufficiently reflect the actual existence of reinsurance and is not available for other lines of business, nor for reserving risk.

DO	DON'T
Introduce an additional dedicated treatment for Adverse Development Covers, based on an improved version of EIOPA's proposal which applies to multiple lines of business and which would also apply to the reserving risk.	Don't modify the requirements for the use of contingent capital instruments for internal model users.

The current regulatory treatment of contingent capital in internal models correctly recognises the economic impact of contingent instruments. That this is achieved under close supervisory scrutiny via internal model approval processes is appropriate and does not need to be changed.

Contract boundaries

The current definition of contract boundaries provided by Art 18(3) of the DA is appropriate and doesn't need to change. Any limitation to the exception to extend the contract boundaries only when the undertaking doesn't have the right to perform the assessment again would substantially increase operational complexity, without providing additional clarity. However, a clarification that it is a right but not an obligation for undertakings to perform this assessment at the level of individual contracts would be helpful.

DO	DON'T
Introduce the clarification that the undertaking has the right but not the obligation to perform this assessment at the level of individual contracts	Change the definition of contract boundaries in Art. 18 of the DA to include the exception on the extension of contract boundaries

Acquisition expenses

Article 140 of the DA specifies that expenses taken into account in the calculation of the technical provisions should be shocked to determine the SCR for life-expense risk. However, there are no exceptions for acquisition expenses or other fixed expenses. This departure from a risk-based approach results in insurers being compelled to include expenses that cannot vary, such as acquisition expenses, leading to unnecessary and excessive capital requirements. A similar issue applies to Art 157.

Therefore, there is the need to modify the Delegated Regulation to address the issue of expense risk in the standard formula.

DO
Modify the wording in Art 140 and Art 157 of the DA on the life-expense risk sub-module and the health-expense risk sub-module respectively

The issue can be solved by adding text along the lines of the wording shown in red below to the existing article:

> *The capital requirement for life-expense risk referred to in Article 105(3)(d) of Directive 2009/138/EC shall be equal to the loss in basic own funds of insurance and reinsurance undertakings that would result from the combination of the following instantaneous permanent changes:*
>
> *(a) an increase of 10% in the amount of expenses taken into account in the calculation of technical provisions; Expenses which cannot vary materially or give rise to material adverse solvency development can be excluded (e.g. commission or investment management expenses which are contractually agreed and so cannot be unilaterally changed).*
>
> *(b) …*

Remuneration

Article 275 of the Delegated Regulation defines the remuneration principles undertakings have to comply with when establishing and applying their remuneration policies.

DO

- Limit the scope of the mandatory deferral of a substantial portion of the variable remuneration component in Article 275(2)(c) of the Delegated Regulation to amounts exceeding 50 000 EUR and one-third of the total remuneration.

This alignment is justified in terms of risk-based supervision and would be also consistent with the approach pursued in the banking framework (Article 94 of the Directive (EU) 2019/878) and EIOPA's opinion on the supervision of remuneration principles in the insurance and reinsurance sector (EIOPA-BoS-20/040).

Stress test disclosure

The co-legislators have agreed to amend Article 64 to clarify that the professional secrecy requirements do not prevent supervisory authorities from publishing the outcome of stress tests or transmitting the outcome of stress tests to EIOPA for the purpose of the publication of the results at EU level.

The insurance industry does not consider individual publication of stress test results as necessary or appropriate. To avoid that future stress test exercises setting additional capital requirements above those specified by Solvency II, it is necessary to introduce safeguards.

DO

- Introduce safeguards to ensure that stress tests do not become pass/fail exercises creating additional capital and disclosure requirements that undermine the existing Solvency II requirements and core features, such as LTG measures.
- Continue to focus on aggregated results in which EIOPA avoid that figures from individual participants can be inferred or recalculated.

Capital Markets Union aspects

As noted by the Commission in its Request for Advice to EIOPA in 2019, Solvency II should appropriately reflect the long-term nature of the insurance business. As such, it should not present an unjustified barrier to investment in CMU-related assets and standard formula capital requirements for these assets, including securitisations, should be based on the risk that they pose to insurers as long-term investors and not on short-term trading risk.

Furthermore, investments in infrastructure are generally made through acquisitions of participations in entities that manage the infrastructure. In terms of group SCR calculation, under the current wording of Article 336 of the Delegated Acts, participations between 20% and 50% do not diversify with the rest of the portfolio, as the proportional share of the capital requirements calculated according to the relevant sectoral rules must be added, while investments less than 20% (non-participation) or greater than 50% (subsidiaries) do diversify.

DO

- Recalibrate the standard formula capital requirements for CMU-related assets, such as securitisations, to reflect the correct economic, long-term risks posed to insurers.
- Correct the treatment of participations for diversification purposes in order to make it easier for insurance entities to invest in necessary infrastructure.

Recalibration of Standard Formula parameters

The Directive foresees a 5-yearly assessment of the appropriateness of the standard formula parameters. Furthermore, recital 83a requires a revision of all calibrations that are input for the SCR/MCR to determine whether they are unduly dependent on UK data and, where applicable, UK data should be eliminated from the relevant data sets, unless no other data is available.

Against this background, the industry highlights that the property risk and lapse risk calibrations should be recalibrated. An assessment should also be made of CMU-related assets, including securitisations, to ensure that Solvency II capital charges are reflective of the true risks that they pose for insurers and are not barriers to investment.

- **Property Risk**
  The current calibration of the property risk factor is based solely on the UK commercial property market, which is exceptionally volatile and not representative of a typical European insurer’s real estate investment portfolio.

  Available data for the pan-European real estate market shows that the property risk factor should be at 15% at most. A revised capital requirement for property risk could foster insurers’ contribution to the financing needs of economic recovery, to the Capital Markets Union and to the decarbonisation targeted by the European Green Deal.

DO

- Review the property risk calibration in light of more recent pan-European data

- **Lapse risk**

  The risk factors for the life and health mass lapse scenarios appear to be unreasonably high. No evidence of the veracity of the calibrations has been provided by EIOPA. In reality, even in extreme situations of individual life insurers, lapse rates of 40% (or 70%) have not occurred. The mass lapse risk factors for life and similar to life techniques health should therefore be recalibrated (or at least be re-placeable by an undertaking-specific parameter).

  Furthermore, when calculating the capital requirement for mass lapse risk the per-policy expenses should remain unchanged. This issue should be mentioned in Article 142(6) of the delegated acts to avoid interpretations going beyond the current wording (see EIOPA Q&A ID 1678 and ID 2402).

DO	DON'T
✓ The mass lapse factors for life and similar-to-life techniques health should be recalibrated.	✗ Introduce additional assumptions related to per-policy expenses after the mass lapse scenario. Lapse and life-expenses risks are already correlated through the corresponding matrix.