To: Karel Van Hulle
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Internal Market Directorate-General
European Commission

Our reference: ECO-SLV-12-171

Subject: **Insurance Europe's key issues with the Commission's Oct 2011 draft Level 2 text for Solvency II**

Brussels, 26 March 2012

Dear Karel

As we are nearing the conclusions of discussions on Omnibus II following last week's European Parliament vote, and before the implementing measures are officially tabled for adoption, Insurance Europe would like to set out its reactions to the implementing measures prepared by the Commission in October 2011.

We recognise the huge amount of work undertaken by the Commission to produce these draft implementing measures and appreciate the regular consultations carried out with insurance industry stakeholders during the process. We acknowledge that in some important areas, the Commission has been prepared to listen to the industry's views. However, while the majority of the approximately 400 articles of the draft measures form a workable basis, there are a number of areas to which we have strong concerns and, if unchanged, will lead to significant unintended and adverse consequences for consumers, the European insurance industry and the wider European economy.

We appreciate this opportunity to comment on the current draft proposals and, as always, remain open to further and regular discussions in order to ensure that the implementing measures are finalised in an appropriate and timely manner.

We note that this is the first consolidated implementing measures draft circulated since EIOPA's findings from QIS5 were published. Whilst three task forces have worked on specific areas following the outcomes of QIS5, we do have concerns that not enough has been done to adjust the implementing measures to take into account all of the lessons learnt from QIS5, the key aim of which was to provide major input into the implementing measures. Many of the points we raise now were proven to be of significant concern in the QIS5 findings.

Below we highlight the key issues we believe need to be addressed in the implementing measures. We recognise that some of these issues have also been discussed in significant detail under Omnibus II, and as such many of the issues listed below are equally relevant for those discussions. However, particularly with regards to the measures to resolve artificial volatility and pro-cyclicality, we have strong concerns with the level of detail discussed; and believe that the details of the approaches should continue to remain under the scope of the level 2 text, rather than level 1:

- **Issues related to volatility/procyclicality –** we welcome the inclusion of the package of three measures which would, if implemented appropriately, help reduce artificial volatility and procyclicality, however, the current text is not appropriate and will not achieve the intended outcomes:
  - **Counter-Cyclical Premium (CCP)** – should help avoid pro-cyclical behaviour in volatile market conditions by recognising that there are periods of distress where market spreads include risks that insurers are not directly and immediately exposed to. The text continues to fail to provide the predictability needed by the industry to carry out forward-capital-planning and risk-appetite-

setting and also to ensure appropriate rather than pro-cyclical decision making in a crisis. The measure will be rendered useless without a predictable and timely application and companies will be forced to move away from the provision of long-term products and a long-term investment strategy. A formulaic mechanism with pre-defined triggers should be proposed for corporate and government spreads. EIOPA should be able to override the formula if exceptional circumstances justify and also to have the responsibility to update the calibrations as needed, through a transparent and consultative process. This will give the industry the predictability it needs and will also give EIOPA the flexibility to deal with potential unknown future crises.

- **Matching premium** – should ensure Solvency II avoids creating artificial exposure to volatility and pro-cyclical behaviour in reaction to everyday spread movements, where spread risk is mitigated through the undertaking's investment strategy and product features. However, in the current wording, the scope of the application is inappropriately restricted and does not provide a Europe-wide solution based on sound economic principles. There are also inappropriate restrictions in its calibration. It therefore significantly exaggerates the real economic risks, penalises well-designed products and will drive companies unnecessarily away from long-term investments and the provision of long-term guarantees.

- **Extrapolation of the risk-free curve** – should be such that it avoids that the Solvency II extrapolation method itself creates significant unmanageable volatility. The methodology should extrapolate the risk-free interest rate as soon as the relevant financial markets cannot be considered as deep and liquid, taking into account the ability of the undertaking to match liabilities with bonds (e.g. from 20 years for the Euro under current conditions). Furthermore, there is still no change to shorten the time taken for the extrapolation methodology to reach the ultimate forward rate. In our view, the time to convergence should be ten years in order to avoid artificial volatility on the extrapolated part of the curve.

- **Impact on the SCR -** the impact of these measures in the SCR is currently inappropriate and, if not corrected, will potentially eliminate the effect of the measures.

- **Own Funds –** the classification criteria for Tier 1 items are now even stricter than the already unnecessarily strong requirements, e.g. we have strong concerns with the fact that in this last draft the possibility of reinstatement (write-up) has been deleted and full flexibility is now required over distributions.
  The transitional period for hybrids should be extended to give undertakings sufficient time to redeem their subordinated debt after entry into force of Solvency II. This period should either be: extended to up to 20 years; or should run until the maturity of the instruments. Furthermore, the transition should be based on existing Solvency I criteria in order to ensure a smooth transition to Solvency II.
  Finally, we have strong concerns with the new proposed requirements under Recital 42, which we believe goes beyond the level 1 text. The tiering limits should be applied to all Eligible Own Funds.

- **Contract Boundaries** - where our concerns remain that:
  - The text is very unclear and therefore companies are interpreting the text in very different ways;
  - Future premiums seems to be excluded for many savings-type contracts; and
  - Unbundling of different cash flows within contracts is required which will potentially determine different boundaries within an individual contract - this does not make sense as well as being excessively burdensome.

- **Currency risk** – there have been no changes to rectify the fact that the approach currently penalises undertakings for well managing their currency exposures to protect policyholders. Solvency II should align capital requirements with good risk management.

- **CAT risk –** strong concerns were raised during QIS5, around the complexity of the calculations and the inappropriateness of the capital requirements, which have not been resolved.

- **Group issues** – the current proposals continue not to consider groups as single economic units. Restrictions on the capital allocation (requirements around transferability and fungability) and diversification at group level (e.g. in the risk margin) introduce undue constraints for insurance groups.

- **Mass lapse risk –** the Commission has increased the calibration of the 1 in 200 year shock from 30% to 40%. However, already we have expressed strong concerns with the 30% charge, for which we have not seen a justification. We have carried out an analysis and concluded that that shock should be between 15% and 20%. We have strong concerns with the increase to this calibration, which will significantly increase an already-overstated lapse risk capital requirement.

- **Reporting –** the extent and the detail of reporting needs to be reduced as the requirements are still excessive, both for public and supervisory purposes. In particular, we have concerns around requirements for: quarterly reporting, systematic cross-checks between Solvency II and local GAAP, and excessively strict reporting deadlines. Additionally, the requirements do not currently reflect the principle of proportionality as, regardless of the nature, risk and complexity, all undertakings are obliged to quarterly reports to their supervisor. Materiality and proportionality should be reflected in an appropriate manner, e.g. the possibility to use simplifications and less granular reporting requirements for minor risks.

- **Risk Margin** – the Commission has now included residual market risk. As the Risk Margin is an approximation, this change adds significant additional complexity for little additional benefit (spurious accuracy). For practical reasons this change should be reversed. Another remaining issue is the lack of recognition of the loss absorbency of deferred taxes in the Risk Margin.

We refer to the issues attached in an annex for a complete overview of our key concerns and detailed comments.

We remain at your disposal to discuss these points in more detail.

Olav Jones
Director Economics & Finance/Deputy Director General

Annex – Detailed comments on consolidated level 2 text of 31 October 2011

Risk-Free Rate

Topic	Article	Commission text	Insurance Europe View
Counter-Cyclical Premium	37	Predictability - EIOPA has discretion on application.	✘ This should be the key element to avoid pro-cyclicality. The text continues to fail to provide the predictability needed by the industry, despite our strong view that uncertainty in the application of this mechanism will render it useless and will encourage undertakings to move away from the provision of long-term products. We continue to stress that the known issues of the corporate illiquidity premium and the government spread should be included in a formula with predictable triggers. We recognise that EIOPA should be able to adjust the formula over time based on new information and also to have the discretion to override the formula and triggers when unexpected and unusual conditions justify this. This will give the industry the predictability it needs in order to be able to use the CCP in its forward planning and so avoid being forced to exit long term products and, during a crisis, to allow them to avoid pro-cyclical behaviour. It will also give EIOPA the flexibility to deal with potential unknown future crises.
	41	Components - The 3 components of the CCP (Illiquidity Premium component, government spread component, discretionary component) are not clearly set out.	✘ In order to ensure predictability, Level 2 should clearly set out the 3 components (the illiquidity premium, the government spread premium and a third discretionary component). Additionally, Level 2 should specify that formulas for the illiquidity premium and the government spread premium will be defined in Level 3.
Matching Premium	42bis	Scope - Only applicable in some Member States due to the restrictive application.	✘ The matching premium should be a mechanism when spread risk is mitigated through the undertaking's investment strategy and product features. At this stage, the scope is too narrow and is inappropriately restricted to very specific products, which therefore does not provide a Europe-wide solution based on sound economic principles. Also, we see no reason why the matching premium proposals apply only to single premium products and limit the types of risks (longevity and expense risk). The key objective should be that, through the application of the Matching Premium, Solvency II does

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			not charge undertakings for risk they are not exposed to (in this case, the part of spread risk which is not related to defaults).
	42ter Recital 25 Recital 27	Calculation - The calculation is still insufficiently detailed and applies unjustified restrictions (e.g. contains the requirement for a 75% floor.)	✗ Certainty is required on the calculation method for the MP within level 2. The calculation is insufficiently detailed and assumptions are insufficiently justified at this stage. Arbitrary restrictions on the calculation of the MP should be removed, such as: - The calculation of the fundamental spread is based on market data, but then floored by 75% of the long term average spread. - The restriction on assets rated below credit quality step 2, which goes against the principle that firms have discretion to choose the type of assets appropriate for their business model, with risk reflected in the level of capital held. This restriction constrains innovation and produces a pro-cyclical cliff-edge effect.
Extrapolation	Recital 20	Starting point - extrapolation starts at 20 years for the EURO and the criterion that undertakings must be able to match their cash-flows with bonds is clearly mentioned.	✓ We welcome that the starting point of 20 years for the EURO under current market conditions and that consideration of the matching possibility for cash-flows with bonds is specified in L2. Although, we also note that the starting point for some other currencies (e.g. Sweden, Norway) would be far sooner than 20 years. We also welcome the recognition that artificial volatility should be avoided in the determination of the risk-free interest rate term structure and therefore appreciate the further clarification.
	39(4) Recital 21	Requires extrapolation over a 40 year period before reaching ultimate forward rate.	✗ It should be mentioned that the extrapolation method should not introduce artificial volatility, e.g. by magnifying small market disruptions in the last points of the liquid part of the interest rate curve (e.g. in Article 39 and in Recital 21). Furthermore the ultimate forward rate should be reached ten years beyond the beginning of extrapolation, as this convergence period would ensure a stable interest rate term structure over time for those maturities which are ten years or more beyond the beginning of extrapolation.

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	40(2)	Exclusion of a term premium in calculation of ultimate forward rate.	✘ The current Level 2 text is based on the assumption that the "term premium" is zero. In our view, this assumption is not appropriate; the Insurance Europe rather supports the breakdown of forward rates put forward by a number of academic papers (for example, Cochrane and Pianezzi, 2006) as the expected future short rate plus a term premium. We believe that the term premium should be derived from observed market data in order to provide compensation for the uncertainty in whether both real rates and inflation will materialise at the assumed level.

Contract Boundaries

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Contract Boundaries	13	Unit-linked/Savings contracts - does not recognise future premiums under unit-linked business	✘ The current text treats a significant portion of the contracts underwritten by insurance companies as short term as opposed to long term (i.e. effectively as paid-up contracts). We have real concerns that this would apply to unit-linked products, and even to traditional savings products in some cases.
	13	Unbundling requirements - Undertakings are still required to unbundle their contracts and determine separate contract boundaries for each part.	✘ A requirement to unbundle contracts is not consistent with the economic approach of Solvency II and can present significant and unnecessary practical difficulties. For example, the valuation of unit-linked products with mortality guarantees would lead to incoherent results: the part of future premiums related to mortality would be projected until the end of the contract, whereas the part of future premiums related to pure savings would not be taken into account. This example shows clearly the inconsistency of this proposal with an economic approach, as embedded guarantees in future premiums cannot be sold separately in practice.
	13(2bis)	Requirements around "no scenario" existing.	✘ Requirements do not make sense! The requirement requires the portfolio to be profitable under any possible scenarios. This would mean in practice that a premium has to be at least equal to the highest possible compensation amount for each policy. Such contract would not include any risk transfer and would not be recognized as insurance.

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			A better approach would be: "*Premiums shall be regarded as fully reflecting the risks covered by a portfolio of insurance or reinsurance obligations, only where the expected amount of the premiums payable under the portfolio exceeds the expected amount of benefits and expenses payable under the portfolio".*

Own Funds

Topic	Article	Commission text	Insurance Europe View
Eligibility of own funds	Recital 42	Tier 2 and tier 3 own funds that exceed 50% of the SCR are not eligible own funds.	✘ We disagree with this recital that goes beyond the requirements as set out in the Level 1 Directive. We urge the Commission to retain an interpretation that is consistent with Level 1 – meaning that there is no reason why the tiering limits (min 50% Tier1, max 15% Tier3) should not be applied to all Eligible Own Funds including the surplus. Tier 2 and Tier 3 items should also be allowed for the coverage ratio above 100% of the SCR, provided that they are still in the proportions defined by the tiering limits. The recital states that the tiering is not applied to all own funds otherwise it would create a pro-cyclical effect. However, this effect would incentivise undertakings to hold high quality (Tier 1) own funds - which would in fact be a positive outcome. Additionally, we note that the current recital would create counter-intuitive results given that own funds are increasing at the point that the undertaking's risk has increased (assuming an undertaking has excess own funds). It would also misrepresent the actual own funds the undertaking holds.
Reconciliation reserve	58bis (3)	Reconciliation reserve is not subject to permanent availability and subordination criteria.	✓ The excess of assets over liabilities should be considered as a whole and should not be subject to tiering which should only apply to subordinated debt items. Classification criteria should only apply to the items referred to in Art. 58 (1c),(1e) and (2) as it would otherwise result in double counting of risks with the SCR.
Tier 1 criteria	59(1f)	Supervisory approval required to redeem or repay.	✘ It is unjustifiably burdensome to require supervisory approval of repayments and redemptions on a going concern basis, particularly at maturity.
	59(1f)	No allowance for any incentive to redeem.	✘ Instruments with moderate step-ups should be allowed in Tier 1 (e.g. the higher of 100 basis points or 50% of the initial credit spread). The existence of step-ups does not mean that an instrument will be called. Indeed, the call is optional, and would only be exercised if market conditions allow undertakings

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			to refinance at a lower cost than the new stepped-up coupon, which under stressed conditions is unlikely to be the case. We have seen under the recent stressed market conditions that insurers have not called their transactions despite the presence of step-ups.
	59(1g, 1h)	No recovery period allowed – repayment or redemption should be suspended immediately on breach of SCR.	✗ These paragraphs appear to be introducing automatic triggers for the suspension of repayments and cancelation of coupons. We believe that introducing an automatic trigger is inconsistent with the purpose of the ladder of supervisory intervention. In our view, 1(g) should allow for a recovery period of 6 months or another longer period which is agreed with the supervisor according to Article 138 (4) of the L1 Directive ("Pillar 2 dampener"). The suspension of repayment of the instrument and the cancellation of coupons should be a contractual option which is exercised at the discretion of the undertaking according to the appropriate action, as set out in their recovery plan. There should be no automatic requirement for this. Additionally, whilst it would seem appropriate that this requirement can be waived, this should not be subject to supervisory discretion and rather it should be up to the undertaking.
	59(1i) & (5)	Full flexibility required over distributions	✗ Insurance Europe opposes a requirement for full flexibility over the distributions since this: - Is in breach of shareholders law; - Excludes dividend pushers and stopper mechanisms; - Could limit the use of ACSM -Alternative Coupon Settlement Mechanism- (especially points 5(b) (iii) to (vi)). We also note that the term "distributable items" is not clear.
	59(2)	Maturity for Tier 1 items - 5 year call now allowed. Minimum maturity at 30 years instead of 10 years.	✓ We support this since hybrid securities are often expected to incorporate a first call date at around 5 years after the initial offering, often without a coupon step-up, and the fact that these first call dates demonstrably do not create "general maturities". There are numerous bank and insurance retail hybrids (fixed coupon, no step-up) which had their first call date in 2008, 2009 and 2010, but have not been called by the issuer. In addition, not allowing 5-year first calls would have unfairly disadvantaged insurers vs. banks, by denying them access to the retail markets, which are such a good source of high quality non-equity capital.
	59 (6)	The possibility of reinstatement	✗ We strongly oppose this change and we see no reason for it. Once the company has recovered and SCR

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		(write-up) has been deleted.	compliance has been re-established, there is no reason why there could not be a write-up if there has been a write-down.
	59(8)	Definition of a trigger event: - The SCR has been breached for more than 3 months; or - Breach of 75% of the SCR.	✗ The period of the SCR breach should be 6 months at least or a recovery period settled by the supervisor according to Article 138 (4) of the Level 1 Directive. ✗ Any automatic trigger is inconsistent with the purpose of the ladder of supervisory intervention and the "Pillar 2 dampener". How an undertaking best recovers its SCR should be assessed on a case-by-case basis and should be part of the recovery plan approved by the supervisor. Automatic write downs or conversions may prove not to be the best actions to take in all situations. On the contrary they may have pro-cyclical consequences.
Tier 2 criteria	61(1f)	Tier 2 coupons for some instruments are cancelled (no longer deferred as was previously the case) if there is a breach of the SCR.	✗ It does not make sense that 1f(i) deals with deferral of dividends whereas 1f(ii) introduces cancellations of distributions relating to hybrids. By changing from deferral to cancellation, the new draft L2 text goes beyond the Level 1 directive (Art. 93, 94) which states that Tier 2 items should only have a loss absorbency capacity in case of winding-up. As a potential compromise, we would better accept if the deferral were for hybrids and the cancellation for items that are similar to shares.
Tier 3 items	64(1c)	Net deferred tax assets are classified as Tier 3	✗ We disagree with the treatment of deferred taxes as tier 3 items. Net deferred taxes should be classified in Tier 1.
Transitionals	73	Transitionals for hybrids - transitional period of 10 years with a specific set of eligibility criteria.	✗ Whilst we welcome grandfathering of these items, it should be based on existing (Solvency I) criteria for simplicity and to ensure smooth transitioning. We recommend the retention of a longer transitional period. This period should either be extended to up to 20 years or transitional provisions should run until the maturity of the instruments to give sufficient time to undertakings to redeem their subordinated debt before the entry into force of Solvency II.
Expected profits in future	1bis (37)	Definition - Amended to refer to "*cashflows*" rather than "*profits*".	✓ We agree that the reference to "profits" (representing positive margins only) was not appropriate.

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premiums (EPIFP)			Indeed, this definition was asymmetric whereas economic balance sheet principles should not result in an asymmetric treatment of inflows and outflows for undertakings. However, the definition is not carried out in the rest of the L2 text since the treatment is asymmetric and therefore all benefit is removed by the EC requirement of HRGs.
	58bis(2)	Treated as Tier 1 capital	✓ We strongly support this. As this amount is already stressed under the SCR, the risk that the value does not materialise would be double-counted if it was also subject to tiering restrictions.
	252	Calculation is per Homogeneous Risk Group (HRG), with no netting between HRG.	✗ Causes huge practical difficulties (e.g. to define a HRG given that EPIFP are proxies), and does not allow netting of profit and loss making cash flows outside of HRG. Therefore the calculation should be done instead at the level of the whole portfolio.
	286 (4bis)	Public disclosure required.	✗ We continue to believe that disclosing this information could be misleading for financial statements readers. It is a technical input which does not need to be disclosed, as economically speaking it is a basic element of the Best Estimate. Disclosing it makes it appear as a weaker own funds element for the public.

Risk Margin

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Residual market risk	31(1)	The Risk Margin should include material residual market risk other than interest rate risk.	✗ Residual market risk is extremely hard to define and calculate. For practical reasons, this change should be reversed, given the Risk Margin is already an approximation it adds significant additional complexity for little additional benefit. In our view, Pillar II would be the appropriate place to make any required consideration of residual market risk, rather than requiring a specific allowance in the Risk Margin.
Diversification	31(1)	Diversification allowed up individual entity level, but not up	✗ It is inappropriate to ignore intra-group diversification as this would unfairly penalise diversified portfolios. This is not in line with the spirit of the Framework Directive. A market consistent valuation

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		to group level.	requires the recognition of diversification effects at all levels.
Loss absorbency of Deferred Tax	31(1)	No loss absorbency of DT taken into account.	✘ In contrast to the provisions for the original undertaking, the current text does not recognize the loss absorbency of Deferred Tax as to the reference undertaking. Nonetheless, after a portfolio has been transferred, the reference undertaking will incur similar cash in and outflows as the original undertaking. In particular, the reference undertaking will generate deferred tax liabilities in the same way as the original undertaking. As a consequence, the loss absorbing capacity of these deferred taxes should be taken into account. Setting the loss absorbency of deferred taxes to zero is, in our view, not in line with the economic framework and is not a requirement of the Level 1 text.
Complexity	31(1)	Default approach is a full projection of SCRs.	✘ The risk margin calculation under a full projection of the SCR is very burdensome. In our view, A simplified method should be standard and insurers should not have to prove, under the proportionality principle, that it is appropriate for them to use simplifications for this calculation. We note that the Risk Margin calculation in itself is an approximation in order to arrive at a market consistent valuation and it rests on many assumptions (e.g. the 6% Cost of Capital rate) which are approximate. Therefore a requirement to project forward each future SCR accurately would result in a significant burden and spurious accuracy.
Cost of Capital rate	32	6%	✘ We have concerns that the 6% is too high and has not been sufficiently justified.
Risk Margin calculation for internal model users	33(2)	Internal model users are restricted to the use of the most complex method to determine the risk margin	✘ An undertaking that has an approved internal model should not be subject to extensive new requirements in calculating the risk margin, compared to undertakings using the standard formula. Especially the requirement to determine the SCR at each point of time is overly burdensome and requires additional modelling. Therefore, the same requirements should apply for internal model users and standard formula users when calculating the risk margin. The current requirement could in addition disincentivise the use of (partial) internal models, which is certainly not the aim of a risk-based framework.

SCR

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Procedure for updating parameters	201 202	The current text only deals with the update of correlation parameters.	✘ As more Solvency II compliant data will become available, all parameters that are used in the standard formula should be updated. Hence there should be a procedure to update variables which are used to represent shocks (1 in 200). Therefore the update procedure should not be limited to only correlation parameters as it seems currently to be the case.
Non-life lapse risk	85 Recital 44	Non-life lapse risk sub-module	✘ This sub-module adds unnecessary complexity for a risk that is immaterial for non-life business and should be removed.
CAT risk	87-103	Design – In the main, the requirements are aligned with QIS5, however there have been some important changes: - Factor based approach: allowance for geographical diversification - Liability scenario: redesign excluding frequency scenario	✓ We support the allowance for geographical diversification included in the capital requirement for non-EEA exposures (Factor based approach) which is essential for an economic approach. We also welcome the deletion of the frequency liability scenario since it made the reinsurance allowance impossible so the net SCR, that had to be the maximum of the two liability scenarios, would have always corresponded to the second scenario. Moreover, we think that this type of scenario is already captured in the non-life premium risk module so it would have lead to a double counting of the risks. ✘ We have strong concerns around the complexity of the calculations and the inappropriateness of the capital requirements which were issues raised during QIS5 and which have not been resolved. In particular, regarding the Scenario-based approach, the design for Nat Cat risk is not in line with current standard practice for managing this risk (done by line of business) and as such presents a number of practical issues. Also, the design and calibration of the Scenario-based approach for Man Made events should be improved. As for the factor based approach, the factors are still overestimated and need recalibration. Therefore a reconsideration of the total design is still needed.
	96	Man-made scenario, Motor liability risk sub module: formula not	✘ The formula to calculate the capital requirement for motor liability is very complex and filled with numbers that have been introduced without justification. We believe that for all man-made risks a non-

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		appropriate.	linear relation between size of business and risk is evident.
	102	Credit and suretyship risk: recession scenario	✘ The approach for Credit and Surety scenario (Man Made events) with the inclusion of a recession scenario is inappropriate. In our view, capital requirements are double-counted with non-life premium and reserve risk. Therefore, the recession scenario should be deleted.
	87-103	Factor-based approach: overstated proxy for exposure to each Nat Cat peril	✘ The current approach uses gross written premium for a LoB as a proxy for exposure to each peril. As policies can be exposed to multiple perils, this methodology produces multiple-counting of exposures, with no allowance to split premiums according to perils before the application of each stress. It is essential that the multiple-counting of exposures is removed by the split of premium based on the relative exposure to the different perils
	87-103	Scenario-based approach: frequently high country factors compared to market experience	✘ There is strong evidence that the country factors of many EU countries should be lower than proposed. For example, the proposed country factor for flood risk in Poland still does not reflect the information provided by the polish supervisor The same concern is raised by Czech republic. Similarly, the valid concerns raised regarding the factors for Slovakian and Cyprus earthquake risk were ignored by the Task Force based on a subjective assessment.
Non-life underwriting risk	83(2)	Error was previously included which negated the allowance for geographical diversification. Now the geographical diversification effect has been re-included in line with the QIS5 formula.	✓ As per Insurance Europe proposal.
Non-life underwriting and health underwriting risk	81,119 Recital 68	Solvency 2 only recognizes additional premium calls for mutuals (under Own Funds), and not the ability to reduce benefits for non-life business (under the	✘ Some undertakings (e.g. Polish Mutuals) have the ability to reduce claims payable under non-life contracts to absorb losses. However, the loss absorbency capacity is explicitly excluded for non-life contracts.. We strongly oppose this exclusion: recognition of the loss absorbency capacity should be based on an

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modules		loss absorbency of technical provisions).	economic approach and thus non-life business should not be excluded arbitrarily. We also refute the additional calculation burden referred to in Recital 68: in only in a few cases does it seem that undertakings have this discretion over the payments under non-life contracts, therefore the majority of undertakings would be unaffected by the amendment. Additionally, there should always be a proportionality consideration – so if an undertaking would not like to allow for the loss absorbing capacity of their non-life business, it would be more prudent to ignore it, and so there should be no reason to disallow them from doing so.
Longevity risk shock	107	Stress at 20%.	✗ The current 20% shock is far too high. Longevity risk is a key risk for insurers providing pension business and so it is essential that no level of excessive prudence is factored into the calibration over the 99.5% VaR. A study published by the Danish Insurance Association concludes that a 10%-15% longevity risk charge would be more appropriate. Furthermore, a longevity risk charge which is modelled via a "one size fits all" immediate shock will always be a simplification of the realistic effect of longevity risk. We understand that for practicality reasons the immediate shock approximation for longevity risk is proposed. However, we would expect that Undertaking Specific Parameters should be available for those insurers for whom longevity risk is material, so that this can be modelled appropriately.
Lapse risk	113 (6(b))	Life retail mass lapse shock has now increased from 30% to 40%	✗ The 40% shock is unjustified and far too high. An Insurance Europe paper ("*ECO-SLV-09-504-Additional input to CEA comments on Ceiops' CP49 on the Mass Lapse Risk Calibration")* analysed some examples of mass lapse data (company specific events) and came to the conclusion that a calibration between 15% and 20% would be more appropriate. Already the previous 30% shock was not justified and was too hgh.
	113 (6(a))	Life non-retail mass lapse shock at 70%	✗ The 70% shock is unjustified and far too high. An analysis of the lapse experience from institutional business (Insurance Europe paper "*ECO-SLV-09-504-Additional input to CEA comments on Ceiops' CP49 on the Mass Lapse Risk Calibration")* failed to find evidence supporting a 70% mass lapse assumption.
	113 (6)	Lapse Definition (Life) - "surrender" has been replaced by "discontinuance" and shocks are only applied to policies with	✗ It is not clear why there has been a change to now use "discontinuance" compared to what was tested in the previous QIS exercises and what is the expected impact of this.

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		resulting increases in Technical Provisions.	Also, we note that when policyholders decide to terminate their contracts by either deciding to receive the surrender value (usually the case under a savings contract) or simply by stopping to pay premiums without a surrender payout (usually the case under a protection contract), Technical Provisions will move to zero. Except from those policies with negative Best Estimates (which we would expect to be the case only in a minority of contracts e.g. saving's contracts at inception before TPs have accumulated), lapses would generally lead to decreasing technical provisions. Therefore a large proportion of policies which previously were shocked under this sub-module, will no longer be shocked under the lapse risk sub-module. Is this what is intended?
Life CAT risk	115(2)	The shock is only applied to policies for which the shocked mortality rates lead to an increase in technical provisions	✘ Biometric shocks should be applied to the whole portfolio. Pandemic risk would not choose victims according to their insurance contracts. The same remark applies to the mortality and longevity modules. It is not realistic or technically sound to assume that the stress would only affect those policies for which mortality risk would create capital requirements; while having zero effect on those policies for which mortality risk would create profit.
Health NSLT premium and reserve risk	121, Annex HUR1	The calibration has been changed back to QIS 5.	✘ We believe this is by mistake and support instead the final results stated in the report of the JWG on Non-Life and Health non SLT calibration.
Health Lapse Risk	133	The permanent increase/decrease shock in lapse rates increased from 20% to 50% - in line with life risk shocks. The mass shock in lapse rates increased from 30% to 40%	✘ We do not support this evolution - no evidence is provided to justify those changes.
Health Cat risk	136	Art. 136, Paragraph 3. Definition of the largest concentration in terms of number of people, this may lead to a wrong result	✘ The use of "number of persons" does not necessarily capture the largest concentration of "risk". A more accurate description would be "the largest total insured benefits". There will be situations where a large number of insurances with a small average sum insured will have lower insured benefits than a smaller number of insurances with high average sum insured. We do not understand why the EC did not use "the total insured benefits" instead of number of people, as recommended by the Cat TF.
Counter-Cyclical Premium shock	143	Zero correlation with other market risks, 100% shock.	✘ Conceptually, the CCP risk module should be negatively correlated with other market risk modules to reflect the fact that the CCP is a counter-cyclical tool which is activated when financial markets come

Topic	Article	Commission text	Insurance Europe View
			under stress. Therefore zero correlation is not appropriate. Additionally, a 100% shock would not be consistent with the data observable in the market. Following the conclusions of the Insurance Europe Paper "ECO-SLV-11-542 Calibration and correlations of the Counter-Cyclical Premium", we propose that the stress to the counter-cyclical premium set in the implementing measures should be reduced considerably. For simplicity reasons, we suggest considering removal of the CCP risk sub-module altogether.
Interest rate risk	146	Minimum shock - The shock is required to be at least one percentage point up or down.	Arbitrary constraints should be removed: the minimal shocks of at least one percentage point should be deleted (up and down) – there is no economic justification for a minimum shock. If the concern was to have minimal shocks for short term rates, we recall that ECB rates generally move in 25bps steps and cannot be compared to movements of the whole interest rate term structure. We therefore suggest deleting this requirement.
	146/147 40 Recital 54	Shock for extrapolated part of the curve is higher than 20%	The interest rate curve should be shocked as far as there is observable market data and then be extrapolated as per Insurance Europe paper "ECO-11-270 Avoiding artificial volatility in extrapolation". This would adequately reflect the relative invariance of the ultimate long-term forward rate. Therefore we agree with Article 40 and Recital 54 stating that the ultimate forward rate should only change *"because of changes in long-term expectations".* However, it should be clarified that this implies that the UFR should be subject to a significantly lower shock in the SCR calculations, which is not currently set out in the related articles.
Property risk	154	Shock is set at 25%.	The shock should be reduced to no more than 15%, in line with the findings of a study carried out by INREV, see *"The IPD solvency II review-15th April 2011", available here: http://www.abi.org.uk/Publications/55864.pdf.* The current calibration is not representative of the European real estate market.
Spread Risk	159	Repackaged loans - Capital requirement for repackaged loans remains high compared to covered	Solvency II assesses the risks with comparable credit worthiness ratings differently. The requirements imply that insurers must have greater solvency for investment in residential mortgage backed securities (RMBS) also known as repackaged loans. It now looks as if insurers will have to have four to eight times

Topic	Article	Commission text	Insurance Europe View
		bonds.	as much capital for an RMBS with AAA status in comparison to a AAA corporate bond and even six to twelve times as much capital in comparison to AAA Covered Bonds. We are of the opinion that (RMBS) are a major instrument to keep the European housing market going. Investment in RMBS must not result in an unnecessary capital requirement since the risks on the European market are limited and issuers of RMBS are subject to supervision. Securitisation has acquired a bad image through the packaging and selling on of American junk mortgages. However, a distinction has to be made between the European mortgage market and the American subprime market as in the thick of the credit crisis, the European average mortgage portfolio encountered very low default rates on payments. Thus the formula should therefore be amended as follows: SCR spread = SCRbonds + SCRrpl + SCRcd **+ SCR rpl rmbs**
	163(1)	Covered bonds	✘ The spread risk of covered bonds should be amended in order to ensure consistency with the treatment of vanilla corporate bonds. The ECBC (European Covered Bond Council) has carried out a calibration study for Solvency II ("ECBC Note on Covered Bonds in the Solvency II Spread Risk Sub-Module – Empirical Evidence"), showing, amongst other things, that the restrictions on ratings could introduce instability and pro-cyclicality into an otherwise stable, long-term asset class.
	163(3&4)	Exposures to Member States' central government and central banks, denominated or funded in another currency that the domestic currency of that central government and the central bank, are treated as corporate bonds.	✘ Article 163 SR7 (3 & 4) should be extended to also apply to exposures denominated in the currency of another Member State. The special treatment for exposures to Member States' central government and central banks is currently limited to exposures denominated or funded in the domestic currency of these institutions.
	156(1)	Mortgage loans which meet the requirements in Art 174ter are treated under counterparty default risk – which now allows for collateral.	✘ Mortgage loans which do not meet the requirements in Article 174ter are penalised in their treatment in the Spread Risk module. It is not clear whether collaterals on mortgage, which often mitigate away a large part of the risk, can be taken into account as a risk mitigation instrument. Therefore we ask for clarity on collaterals; in our view it is vital that collaterals are reflected in spread risk. Furthermore,

Topic	Article	Commission text	Insurance Europe View
		The remaining mortgage loans are treated under the spread risk module as unrated instruments. Also it is not clear whether collaterals can be taken into account.	mortgage loans without an external rating are treated as unrated corporate bond exposures. In order to solve those issues, we suggest alternatively to broaden the scope of Article 174ter and to treat all mortgage loans in the counterparty default module. We also note that the current requirements under 174ter are in general so restrictive that they will apply to very few mortgage loans (e.g. for example para 7 (collecting file-by-file documentation is very costly and has zero added benefit)).
	163bis	Application of the spread risk scenarios to the fundamental spread of the matching premium – current proposals seem to be wrong.	✗ The current text states that where companies apply the matching premium the fundamental spread should be increased by an absolute amount (calculated as the relevant FUP factor multiplied by a reduction). We think there is an error in the current wording of the text, because the "FUP" factors in the spread risk module are designed to be applied to market values as percentage shocks (and not to spreads as absolute shocks). As a consequence, the current wording would lead to excessively high and inappropriate risk charges: If one assumes an A rated bond with a duration of 10, Article 163bis requires adding 10.5% *.6 = 6.3, i.e. 630 bps to the fundamental spread; this would lead to a shock of around 45% on the assets (compared to a 10.5% spread shock if no matching premium is applied). In general, complete reconsideration needs to be given to this issue. Where companies apply the matching premium because they have mitigated spread risk, capital requirements related to spread risk would seem inappropriate. However, undertakings would still be exposed to default risk, which would be more appropriately dealt with in the counterparty default risk module.
Use of ratings/solvency ratios	169, 178, Recitals, 3, 4 and 6	Changed so that solvency ratios are used only when ratings are not available. (concentration risk, counterparty default risk)	✓ As per Insurance Europe proposal. We welcome this change as the approach using the counterparty's solvency ratio presents some practical difficulties. For instance, it may be the case that information on the counterparty's solvency ratio is not available when it is needed and that the last available solvency ratio may have to be used as a proxy. ✓ We welcome Recital 3 stating that own credit assessments should only be made for the larger and more complex exposures. However, according to the integrated risk management approach of Solvency II, credit risk should be assessed at entity level rather than at the level of an individual instrument. ✗ However, Recital 6 seems to imply that those measures are only temporary ("at the inception of the new

Topic	Article	Commission text	Insurance Europe View
			regime") and could change in the future. We strongly oppose any future change and suggest that Recital 6 should be amended in this sense.
Currency risk	172	Based on currency of the basic own funds.	✗ The approach to currency risk penalises undertakings for holding a surplus of assets over liabilities in any currency other than the domestic currency, even though this is appropriate and good risk management. The problem was recognised in EIOPA's QIS5 report: "*The currency risk module was noted to contain counterintuitive incentives to hold assets in excess of liabilities in the reporting currency rather than in the currencies of the underlying liabilities*." We suggest that a more logical proposal to calculating the group currency risk capital charge would be to apply the currency risk shock to the sum of the local surpluses net of the SCR (pre-currency risk). For solo entities, where no currency-specific SCR is available, a consistent approach could be achieved by weighting the currency risk capital charge by the proportion of assets and liabilities held in foreign currencies. For more evidence and examples, please refer to the Insurance Europe paper *"ECO-SLV-11-308 Issues with and solutions for QIS5 Currency Risk treatment"*
Counterparty default risk	175	Complexity - Per counterparty calculations are required for calculating LGD, with the exemption (Art. 175bis) that the loss-given-default may be calculated for a group of single name exposures. In this case, the group of single name exposures has to be assigned the highest probability of default included in the group.	✗ The current text, although allowing for a simplified way to calculate the loss-given default (LGD) for a group of single name exposures, still requests per counterparty calculations for the LGD. While we support this simplification, grouping of counterparties should not only be allowed between single name exposures, but should be possible within and across rating classes, where the weighted average of the probabilities of default should be used instead of the highest one in the group. Moreover, other features of the counterparty default module are still too complex resulting in a burdensome calculation with little impact.
	175(4)	Mortgage loans - A potential double counting reduces the impact of collaterals for mortgage	✗ Article 175(4) applies a factor of 80% to the risk-adjusted value of mortgages (which already accounts for property and currency risk, see Article 177ter). The risk adjustment leads to a reduction of around

Topic	Article	Commission text	Insurance Europe View
	177ter	loans	25% of the mortgage, which results in a total factor of around 60%. We see no rationale for the additional 80% factor introduced in Article 175(4), especially as it does not apply for other types of collaterals.
Non-proportional reinsurance	196,83, Annex NLUR4	Art 196 allows USPs to calculate the adjustment factor for NP reinsurance. Art 83 for the standard formula sets an 80% adjustment factor for some LoBs and 100% for the remaining LoBs, which replaces the formulaic approach, which was previously set out in Annex NLUR4.	✓ We support the allowance for USPs that we have requested as the NP factor in standard formula does not appropriately reflect all types of non-proportional reinsurance agreements. ✗ The current text, setting a fixed NP adjustment factor of 80 or 100% depending on the line of business, does not consider whether the undertaking has effective non proportional reinsurance. This approach is not risk sensitive at all and therefore not consistent with Solvency II principles. We believe that a risk-based standard formula is essential.
Scope of USPs	196	Changed to include a NP reinsurance adjustment factor. But scope is still too restrictive.	✗ The current text restricts the scope of risk sub modules for which the use of undertaking specific parameters (USPs) is allowed. The scope should be extended to all (sub) modules, except market risk, in line with the Framework Directive e.g. CAT risk,. Indeed, many SME's and monoliners specialise in certain areas leveraging their historic ties, their specific understanding of their customer base, or their expertise within products. This specialism normally forms part of their business plans. The ability to reflect this via the use of USPs is therefore very important to many SMEs and monoliners. As a result, the scope of USPs should not be restricted to some areas as it is currently set out in the Level 2 proposal but rather expanded.
Data requirements for USPs	197-200	Incorporates only minor changes.	✗ The current text sets extremely onerous data requirements to be able to use USPs. We welcome that the requirements to use USPs no longer request undertakings to justify that the standard formula parameters do not appropriately reflect their risk profile. Nonetheless, we still believe that the approval procedure and data criteria should not counterproductive by setting much too high barriers and thereby limiting the use of USPs (e.g. Time series of historical data should be long enough to be able to is too long)

Topic	Article	Commission text	Insurance Europe View
			The use of USPs should be flexible.
Non-life premium and reserve risk	Annex NLUR1	Calibrations have been amended in line with the joint EIOPA/Industry Task Force recommendations	✓/✗ Significant improvement compared to EIOPA's original proposals. However, data and methodologies used in the calibration were not fully Solvency II compliant as they were based on the on-going Solvency I framework. Therefore, a new calibration, carried out after the entry into force of Solvency II and thereby using more appropriate Solvency II compliant data and methodologies should be performed. This should be enshrined in the Level 2 text by a review clause. Also, the final factors result in an increase in capital requirements (relative to QIS5) for 'Workers compensation', 'Legal Expenses', 'Motor Other', 'Credit & Suretyship' and 'Assistance'. As these lines of business are conducted mainly by monoliners in many EU markets, these factors could have damaging social and economic consequences. Therefore, it is vital to consider the findings of EIOPA's impact assessment before concluding on these issues.
Non-life / NLST health premium and reserve risk	81 119	The capital charge for non-life premium and reserve risk, as well as for NLST health premium and reserve risk, has increased.	✗ The parameter to project the premium and reserve risk to a 1 in 200 event has been increased from 2.56 (in the QIS5 spreadsheet) to 3. No justification has been given for this change which has a huge impact on the capital charge for non-life premium and reserve risk and NLST health premium and reserve risk. We would suggest keeping the parameter tested in QIS, as the use of 2.56 exactly reflects the 99.5% quantile.
Health risk equalisation systems	122(e)	The treatment for health risk equalisation systems is now subject to further constraints (ring-fencing).	✗ In order to be allowed to apply the adjusted health calibrations which reflect the specific nature of health risk equalisation systems, undertakings are now subject to even stricter constraints. A new requirement of ring fencing (which does however not seem to imply the creation of ring-fenced fund) was added; this could damage the development of health insurance as well as policyholder protection. If applied, this strong requirement will seriously hamper the use of the equalisation systems and subsequent development of new health products with such a system. Therefore we suggest remove this requirement from the sufficiently extensive list of current requirements.

Participations

Topic	Article	Commission text	Insurance Europe View
Participations in financial and credit institutions	71	Requires deduction of participations in financial and credit institutions over 10% of Tier 1 Own Funds.	✖ The current text requires deduction of participations of financial and credit institutions over 10% of Tier 1 Own Funds. We disagree with the deduction of these participations in financial and credit institutions. We see no reason for a specific treatment for these participations, which creates and unlevel playing field with banks. Participations in financial and credit institutions will normally be included in group supervision in accordance with Articles 228 or 229 of the Framework Directive. Therefore, at group level double-gearing is eliminated. At solo level, however, participations in regulated undertakings included in group supervision should in our view not be subject to any measure for eliminating double-gearing. Instead, for the purpose of calculating the solo SCR, participations in financial and credit institutions should be treated as equity investments. There is no need to eliminate double-gearing at solo level when it is already carried out at group level. Furthermore, not eliminating double gearing at solo level is consistent with the treatment of credit institutions' participations in insurance undertakings in accordance Art. 60 of Dir. 2006/48/EC (CRD): *"Member States may provide that for the calculation of own funds on a stand-alone basis, credit institutions subject to supervision on a consolidated basis in accordance with Chapter 4, Section 1,or to supplementary supervision in accordance with Directive 2002/87/EC, need not deduct the items referred to in points (l) to (p) of Article 57 which are held in credit institutions, financial institutions, insurance or reinsurance undertakings or insurance holding companies, which are included in the scope of consolidated or supplementary supervision."* This option, applied by a majority of Member States, allows them to decide not to deduct certain holdings and participations in institutions included in the scope of their consolidation from solo-level own funds. Moreover, in groups with insurance and banking activities of a similar size, the solo solvency of the insurer with deducted non-insurance participations will not reflect the economic reality. The path towards an internal model is not possible, because of the use test requirements – modelling only the insurance part is not sufficient for internal management. Thus, deduction is not appropriate and we

Topic	Article	Commission text	Insurance Europe View
			suggest use of the 22% equity stress. Additionally, we note that the wording is not clear: for participations in a credit and financial institutions exceeding 10%, it is not clear whether undertakings have to deduct the full value of the Basic Own Funds or only the part exceeding 10%.
Definition of strategic participations	152	A different treatment applies for strategic (22% shock) and non-strategic (equity risk shock) participations.	✘ Level 1 defines all participations as strategic, therefore the current proposal in the implementing measures is inconsistent with Level 1. In our view, all participations should have a 22% shock. An investment by an insurance or reinsurance undertaking in more than 20% of the equity of a company is a substantial commitment and not one that is made with the intention of selling the stake. Such investments are intrinsically of a long term nature. Also, we note that the requirements in Level 1 for the definition of a participation (>20% holding) are higher than in common corporate laws (usually >10%), which reinforces the strategic nature by default for all participations defined under Solvency II. Given that participations which are subject to group supervision are treated properly at group level, only a simple approach needs to be adopted at solo level. The detail required to prove that a participation is strategic seems excessive and disproportionate given the end use. A single shock for all participations is simple to apply and can be applied consistently across undertakings and Member States. Applying a 22% shock to participations should be seen as parallel to the fact that a 22% shock has been considered appropriate for the duration based equity shock, which is a shock applied to equities held for a long time.

Valuation of assets and other liabilities

Topic	Article	Commission text	Insurance Europe View
Valuation of contingent	8	Undertakings are required to value their material contingent liabilities	✘ This was against the advice of CEIOPS (Final advice as presented to the EC in 2009). CEIOPS only proposed an explicit disclosure in line with the requirements of IFRS. We supported this approach. The

Topic	Article	Commission text	Insurance Europe View
liabilities		on balance sheet	valuation of a contingent liability is extremely difficult and will require expert judgement.
Valuation of holdings in subsidiaries	9(2)	Undertakings are required to use the adjusted equity method as the default approach	✘ The current text requires that the valuation of the subsidiary holding should be carried out through the adjusted equity method. We disagree with this proposal and instead believe that a mark-to-model approach based on observable market input provides a valuation that better reflects the economic value of the holding in a subsidiary and therefore is more in line with the market consistent requirements of the Framework Directive. A mark-to-model approach based on observable market input should therefore be possible.
Non-Life insurance obligations - Lines of business	Annex I (A)	The numbering seems to be wrong.	✘ The numbering of the lines of business from 1 to 12 has been changed to 14 to 25, but afterwards the text stills refer to them as lines of business 1 to 12. This should be corrected.

Risk mitigation techniques

Topic	Article	Commission text	Insurance Europe View
Duration of techniques	184 (2)	The risk mitigation effect of contracts with a duration of which is shorter than 12 months is fully taken into account in BSCR only if very strict requirements about the replacement of these contracts are met. In particular, the replacement of the RM contract shall not take place more regularly than 3	✘ The current text sets out conditions that are extremely problematic especially with regard to the recognition of dynamic hedging. Indeed, the requirement, that the replacement of the risk-mitigation technique shall not take place more regularly than every three months, is unrealistic, especially in case of dynamic hedging where hedges are adjusted daily based on equity index development (i.e., event outside the control of a company) which can trigger a hedge adjustment. The current best practice and usual duration of dynamic hedging contracts (currency hedging derivatives) is less than 1 month as more frequent settlement reduces counterparty default risk. With longer positions the volatility would increase to an unacceptable level for both insurance company and the bank providing the derivative (or conditions would worsen) implying a huge risk of disruption on the market, lowering the revenues for

Topic	Article	Commission text	Insurance Europe View
		months.	the undertaking and consequently for the policyholders.
Finite reinsurance	186 (6)	No allowance for Finite reinsurance as a risk mitigating technique in the calculation of the SCR.	✘ The general exclusion of "Finite Reinsurance" contracts from being recognizable in the calculation of the SCR is not appropriate. By definition (Art. 210 (3)), finite reinsurance contracts need to transfer *"significant underwriting risk that exceeds the premium over the lifetime of the contract by a limited but significant amount"*. To the extent underwriting risk is transferred a recognition in the BSCR should be allowed. While for finite reinsurance contracts in the sense of Art 210 (3) the mitigation effect in the non-life premium and reserve risk is typically quite limited, such contracts can have a significant effect on the risk of loss in the life, health and the non-life catastrophe risk module. Moreover it should be possible for undertakings to take account of the effect of these risk mitigation techniques in their SCR using Internal Models, provided that the risks arising from the use of such techniques are properly reflected in those models.

MCR

Topic	Article	Commission text	Insurance Europe View
MCR formula	236	Formula for MCR nl was the higher of 2 amounts under QIS5, now the sum. No recalibration of the related factors.	✘ Factors should be recalibrated as, due to the formula change, the MCR for non-life business could potentially double.
Complexity	236	Requires quarterly MCR calculations.	✘ Undertakings should be allowed to use simplified methods to update the quarterly value of Technical Provisions to use in the linear MCR calculation.

Groups

Topic	Article	Commission text	Insurance Europe View
Clarity around use of method 2	321 (1)	Method 2 for third-country entities - There is no specification that local SCRs from third-party country entities in equivalent jurisdictions can be aggregated using Method 2 (Method 1 is not feasible).	✘ Art. 227 (1) (2) needs method 2 for using equivalent local SCR in group solvency calculations (SCR aggregation). Therefore this use of method 2 should be specified in the criteria in Art 321 (1).
Restrictions around Method 2	321 (2)	Where significant intra-group transactions exist, the use of method 2 is no longer possible.	✘ Not justified. Intra-group transactions will be supervised regardless of the method (Art. 245 Solvency Directive). In general method 2 would be expected to be more conservative – why should group supervisors not allow undertakings to use it?
OF availability requirements	323 (3)	Requirements on availability of own funds at group level Some own funds are considered as not available at group level	✘ Funds can be made available at group level through the use of intra-group transactions. As such what is considered to be loss absorbent at solo level should also be considered as loss absorbent at group level. We therefore not agree with the systematic assumptions that some own funds are less likely to be available at group level.
Treatment of Group Own Funds	323a	Re-tiering required at group level	✘ We object re-tiering of own funds at group level. As solo entities issue own funds items, there should be no further constraints at group level. More generally, own funds should be considered available to cover the SCR of the participating undertaking for which the group solvency is calculated, unless non-availability is explicitly stated for those own fund items. We suggest that a new recital stating this principle should be introduced.
Diversification effects	323(6)	Restrictions on diversification effects – due to adjusted SCR, above which solo own funds cannot be recognised at group level.	✘ Reduction of eligible own funds which cannot be effectively made available for the group by a "diversification haircut" is unjustified.

Internal Models

Topic	Article	Commission text	Insurance Europe View
Application of political decision to both internal models and the standard approach	New recital	N/A	The calibration of the Standard Formula is subject to certain political decisions, e.g.: - EU-government bonds not to be backed by solvency capital in order to incentivise the funding of public debt in the EU - Equity risks from participations at solo level to be backed with lower solvency capital - cases of overarching economic policy objectives determining supervisory rules (volatility risks, inflation risks, equity dampener) It is necessary to ensure that these decisions are applicable for the use in the standard approach as well as in internal models. Thus, we suggest the addition of the following recital: *"Fundamental economic policy decisions of Solvency II that are driven for political or supervisory reasons shall be explicitly applicable to both users of internal models and standard formula without further validation requirements. Where deemed appropriate by the undertaking, other economic assumptions leading to more conservative results can be adopted."*
Use prior to approval	208	No allowance for the use an, as yet, unapproved internal model.	Given the uncertainty around timelines and the still on-going discussion on the criteria for the approval of internal models it would be crucial for undertakings to use their unapproved internal models under conditions and not being forced to use an inappropriate standard formula. Therefore, under certain circumstances, a company should be allowed to use its internal model for calculating the SCR until the supervisor reaches a decision. This would clearly need to be subject to strict conditions, but could avoid the whole model being held up because a small part is still in the process of approval.
Definition of a "major change" in internal models	Recital 79	The inclusion of new risks/new business units will indicate a major model change	The definition of "major change" is too restrictive. Reference should be made to proportionality. The inclusion of new risks/new business may have minimal impact and may not be a major model change, especially in the group context (may be material from a solo perspective but not from a group perspective). A reference to the proportionality principle would resolve this issue.

Third country equivalence

Topic	Article	Commission text	Insurance Europe View
Reporting	Recital 146	Following a finding of 'transitional equivalence' Member States are permitted to request additional reporting from the group rather than rely on 'equivalent' supervision by the third country.	✗ Additional requests of information and data by the potential EU group supervisor should be exceptional. Reliance on information provided by the third-country group supervisor should be the guiding principle. Regarding countries under transitional equivalence, care has to be taken that third-country supervisors do not request too much additional data and calculations; but should rather try to cooperate with the group supervisor and avoid duplication.
System of governance and public disclosure	358 (g), 368(h (i))	Risk management processes - Supervisory regime still needs to require undertakings to have risk management processes in place measured on a continuous basis.	✗ The requirement for companies to have a risk management process in place, under which all risks to which a company could be exposed should be measured on a continuous basis, is excessive. Regular assessment should be enough.
Solvency assessment of third country regime	358(l, iv)), 366(1,b (iv)),368(n (iv))	Level of confidence attached to capital requirements - Reference to 'at least' deleted.	✓ As per Insurance Europe comments – previous reference to 'at least' was excessive
	368(1,(r))	Calculation of group SCR - Group SCR still required to produce a result which is at least equivalent to that achieved by either of the two calculation methods set out in Article 230 and 233 of Directive 2009/138/EC.	✗ Excessive – reference should be to equivalent level of policyholder protection not to the result. It is important that the third country regime provides an equivalent level of policyholder protection, but, due to acceptable differences in methodology, the result of the group solvency calculation may differ. Thus the Solvency II SCR might not always be higher than the third country's group SCR calculation.
Transitional arrangements	365 (1(a)), 367(1 (a)), 376(1(a))	Public commitment - requires a public commitment to introduce a solvency regime capable of satisfying the criteria set out in Article RTCE1 by 31 December 2018.	✗ Excessive, we believe that such a commitment does not need to be made publically.

Topic	Article	Commission text	Insurance Europe View
	365(1(b)), 367(1(b)), 376(1(b))	Convergence programme - requires a convergence programme established for converging to a solvency regime that is capable of satisfying the criteria set out in Article RTCE1.	✗ Excessive. It should be sufficient that the third country commits to clear milestones at the outset. In any case, we believe reference to 'convergence programme' should be amended to instead refer to 'work program'. In practice, reference to work programme rather than 'convergence programme' makes no difference. However, third countries are likely to be more willing to enter into the former.
	365(2), 367(2), 376(2)	Length of transitional period - Transitional length is a maximum of 5 years.	✗ The Insurance Europe would like the transitional length to be 5 years plus a 5 year review clause on the understanding that clear milestones are set within the transitional period.

Proportionality

Topic	Article	Commission text	Insurance Europe View
Principle of proportionality		No overarching principles set out for proportionality/materiality and simplifications.	✗ Level 2 should introduce an overarching principle of proportionality and materiality, because the Regulation – in contrast to the Directive – is applicable directly to authorities as well as undertakings. This should be done as was initially the case in articles 2 and 3.
Repackaged Loans	Recitals 88-90	No reference is made to proportionality	✗ The requirements for investments in repackaged loans disregard the principle of proportionality; the former reference to nature, scale and complexity of the risks inherent should be reintroduced.

Segmentation

Topic	Article	Commission text	Insurance Europe View
Annuities arising from non-life contracts	Annex I (D)	Life (re)insurance obligations include "Annuities arising from Non-Life insurance contracts".	✗ Not all (re)insurers writing non-life annuities will have sufficiently detailed historical data, or appropriately adapted systems, to be able to use life insurance techniques as soon as Solvency II enters into force. We believe therefore that a substantial transitional period should be granted to allow insurers and

Topic	Article	Commission text	Insurance Europe View
			reinsurers to build up the necessary amount of data. During this period, (re)insurers would continue to use their existing non-life insurance techniques for non-life annuities.
Accepted reinsurance	Annex I (B)	Direct and proportionate insurance are required to the separated	✖ The requirement to split proportional reinsurance, with no allowance to merge it with direct insurance will generate unnecessary burdens for undertakings.

Pillar 2

Topic	Article	Commission text	Insurance Europe View
System of Governance	249(1)(c)	Definition of board - "*Administrative, management or supervisory body*" (terminology used in Level 1 text to reflect the harmonised term for 'board') changed to "*Administrative body, management body and supervisory body*".	✖ The text proposed in Level 1 provides a common definition for the 'board' that works for countries that adopt either one or two tier board systems i.e. 1-tier combines management and supervisory boards, 2-tier separates them. To ensure that Solvency II does not conflict with existing company law legislation, the EC should not deviate from the text established in the Framework Directive.
	251(4)	Use of external ratings - Own credit assessments are required for larger and more complex exposures	✖ With regard to the start of Solvency II, undertakings are unlikely to have sufficient resources to carry out due diligence of external assessments. Controlling such external institutions is not part of the (re)insurance industry's core business. As a consequence, necessary capacities as well as adequate know-how and expertise replacing an external credit assessment is lacking in many undertakings. Therefore we would suggest that own credit assessments should not be a requirement at the inception of the new regime.
	258	Functions - The wording is not sufficiently explicit to provide legal certainty that full operational independence is	✖ It is important that undertakings have the option of combining the numerous functions under the system of governance. This would allow for one person to assume more than one responsibility. The exception being the internal audit function, the level 1 directive clearly states that this must be

Topic	Article	Commission text	Insurance Europe View
		required only on the internal audit function. This is aligned with Article 47 of the Framework Directive.	operationally independent from other functions within the system of governance. The consequence being that the human resources required to run the system of governance may not be proportionate to the undertaking itself. This should be explicitly mentioned in the Level 2 text. The Level 2 text offers exclusion for smaller and less complex undertakings however the principle of proportionality should not only apply to smaller companies but also in view to the nature and complexity of risks – therefore the text should refer explicitly to the principle of proportionality. Furthermore, requiring a separate organisational unit to ensure the actuarial function is excessively prescriptive and inappropriately interferes with how undertakings are managed and organised. All references to "*organisational unit*" should be deleted.
	264(5)& (6) Recital 100	Outsourcing - The requirement has changed to confirm that the undertaking's obligation to ensure compliance of outsourced service providers, with the SII Framework Directive, only applies to the outsourced function in question, and not other activities. Broadly unchanged – undertaking required to ensure providers are compliant with art 49(2)(a)&(b) of FD.	✓ This is a positive development. It would be difficult for an undertaking to control the numerous activities taking place within outsourced service providers. ✗ Being able to control external providers to such an extent is not part of the (re)insurance industry's core business and would be impossible in practice. It is clear that the administrative, management or supervisory body retains responsibility for the outsourced function. It should therefore be sufficient to stipulate what is required of the undertaking. Furthermore, Recital 100 is ambiguous and should clarify that it deals with outsourcing only concerns *insurance* activities that are outsourced.
	265(1)(f)	Remuneration Policy - The requirement for an independent remuneration committee is linked to the size and significance of the undertaking.	✗ Any requirement which introduces fully independent committee and functions within an undertaking should be carefully considered. To achieve full independence will be incredibly burdensome.
	264	Outsourcing – the wording of	✗ The wording of this article needs some improvements:

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		this article is not clear.	- Paragraph 2 refers to a definition in Article 1bis which no longer exists. - Paragraph points (f) and (j) seem to define similar requirements with regard to the ability to obtain information and issue instructions concerning the outsourced activities and functions. - Paragraph 5 and 6 refer to outsourced functions but describe also requirements for outsourced activities. The wording should be more coherent.
Capital add-ons	272(6)	Supervisors are able to estimate capital add-on based on the risk profile of a "similar" undertaking provided that they are able to ensure that the reasons behind their decision can be disclosed.	✓ Insurance Europe is concerned about comparing data, designs, structures and methodologies between 'similar undertakings'. Comparisons would be difficult to achieve in practice and the Supervisory Authority would not be able to disclose underlying information to the undertaking. The amendment seems to recognise that this would indeed not be possible in all cases.
ORSA supervisory report	294(3)	Creates precedence for separate ORSA reporting for supervisory purposes.	✗ ORSA is a valuable tool for management purposes and reporting of ORSA results should reflect this. Internal documentation should as far as possible be accepted as information to be reported to supervisors. ORSA is an undertaking driven mechanism to fully assess the risk profile in comparison to solvency needs of the undertaking. Presentation of results will differ per undertaking and also, submission of ORSA results within a 2 week timeframe upon finalisation will be difficult if results must be presented in an additional report for supervisory purposes.
Coordination of group supervision	338-339	Insurance Europe proposed redrafting suggestions to allow that tasks and duties could be delegated by the group supervisor to other supervisors in the college. This was not taken on board by the EC.	✗ The possibility to delegate tasks and duties within the supervisory college could help to increase efficiency and ensure the group is managed effectively.

Pillar 3

Topic	Article	Commission text	Insurance Europe View
Public Disclosure	284(3)(a)	The Level 2 text requires a breakdown of information per asset class on income and expenses arising from investments.	✗ Insurance Europe believes this level of detail in a document for public disclosure is much too detailed. The SFCR already contains a section on "business and performance" based on which the reader will have sufficient information to make a judgement on an undertaking's overall business and performance. Therefore we question the value of a breakdown per asset class.
	291	Deadlines - Allow for soft launch before full entry into force of Solvency II in 2013. Confirms that the first full annual report would be delivered in 2015 based on 2014 information (assumes financial year end 31 Dec 2014). Report to be delivered 20 weeks after financial year end.	✓ We support the current proposals for deadlines.
Reporting	294(1)(c) & (3),303	ORSA will now be dealt with as a standalone process and as such, will be subject to different reporting requirements. New requirement for the ORSA to be submitted 2 weeks after concluding the assessment.	✓ This is a positive development as it will enable the ORSA to be conducted according to an undertaking's business planning time horizons and not reporting/financial year end cycles. Insurance Europe supports that ORSA results should be reported to the supervisor as soon as possible however it must be clear that the 2 week deadline begins after the ORSA report has been signed off by the management/ supervisory body.
	297(3)(d&e)	Governance - there is a new requirement for undertakings to describe how they apply the prudent person principle and also how the undertaking verifies appropriateness of external credit assessments/ratings.	✗ In level 3, EIOPA is currently setting out very detailed quantitative templates which should enable supervisors to already receive information to assess if the undertaking's applying the prudent person principle. We do not therefore see why the undertaking should have to also report its own qualitative assessment of information which will already be held by the supervisor. This is double reporting and one of these obligations should be removed. For comments external credit assessment institutions, please refer to our comments on System of Governance – use of external ratings (Art 251(4))

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	302bis	opening requirements in 2014 'Opening requirements' must now be delivered 14 weeks after first financial year end upon application of SII, this is an improvement from the previous 8 weeks. The following items are listed under 'opening requirements': full valuation of assets and liabilities, SCR and MCR and main differences between SI and SII valuations ("balance sheet" removed from list).	× We do not support required comparisons between SI and SII data. The results would not be representative of the solvency situation of an undertaking and could therefore be misleading.

General comment

Topic	Article	Commission text	Insurance Europe View
Impacts on current tax rules	New recital	N/A	× In general, insurance companies are currently taxed on the profits shown in their statutory accounts, rather than by reference to regulatory requirements. Thus Solvency II in itself should not have an impact on the liabilities used for tax purposes. Also, there is a widely held view that a tax result based on solvency returns is likely to be more volatile than at present. This kind or recitals are not new. A similar recital can be found in Council Directive 91/674/EEC of 19 December 1991 on the annual accounts and consolidated accounts of insurance undertakings. Therefore we suggest to include the following new recital: *"The compulsory disclosure and reconciliation of figures between solvency and accounting is prescribed solely for purposes of comparability and transparency and is not intended to lead to changes in the tax treatment of insurance undertakings. The purpose of the Solvency II figures will be to focus on capital adequacy of insurance and reinsurance undertakings rather than being considered within the tax regime of each Member State."*

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