Solvency II 2020 review - overview

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22 JANUARY 2020
Background
Solvency II Directive requires that, by 1 January 2021, the Commission shall review:

- LTG measures and equity risk measures
- Methods, assumptions & parameters used in calculating standard formula SCR
- Calculation of the MCR
- Group supervision & capital management

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Background

11 February 2019 – Commission call for Advice to EIOPA:

- Risk margin
- Capital Markets Union aspects
- Macro prudential issues
- Recovery and resolution
- Insurance guarantee schemes
- FoS/FoE supervisory powers
- Reporting and disclosure
- Proportionality and thresholds
- Best estimate
- Own funds
- Reliance on external ratings

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Timeline

Source: EIOPA Fact sheet on the 2020 review of Solvency II

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EIOPA Consultation Papers – First Set

**Reporting & Disclosure**

- General Issues on Supervisory Reporting and Public Disclosure (55 pages)
- QRTs (131 pages + Annexes)
- SFCR (60 pages)
- Financial Stability Reporting (9 pages)

**To be reviewed later in 2019:**

- Group QRTs
- RSR
- Technical aspects of the reporting and disclosure process
- Data quality aspects
- Issues linked to other areas of the Solvency II 2020 review, including long-term guarantees templates.

**Insurance Guarantee Schemes**

- Harmonisation of National Insurance Guarantee Schemes (67 pages)

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**Deadline:**

Was 18 October 2019

Covered in a previous Breakfast Briefing

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EIOPA Consultation Papers – Second Set

One 878 page paper covering:
- LTG measures and measures on equity risk (258 pages)
- Technical provisions (43 pages)
- Own funds (27 pages)
- Standard Formula SCR (76 pages)
- MCR (14 pages)
- Reporting and disclosure (34 pages)
- Proportionality (37 pages)
- Group supervision (106 pages)
- FoS/FoE (11 pages)
- Macroprudential policy (41 pages)
- Recovery and resolution (48 pages)
- Insurance Guarantee schemes (1 pages)
- Other topics (16 pages)
- Annex with additional info on some of the above (151 pages)

Deadline: Was 15 January 2020

Bridget will cover aspects of these topics
Long Term Guarantees

- Changes in LLP (or at least sensitivity testing and disclosure) being considered for Euro
### Long Term Guarantees

<table>
<thead>
<tr>
<th>Matching Adjustment</th>
<th>Volatility Adjustment</th>
<th>Others</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Remove limitations on diversification benefits</td>
<td>• Other changes including undertaking specific VA being considered</td>
<td>• Possible strengthening of disclosures in relation to transitionals</td>
</tr>
<tr>
<td>• Clarification on eligibility of restructured assets</td>
<td>• Consistent approach on need for supervisory approval proposed</td>
<td>• Restrictions on new uses of transitionals</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Some changes in risk management and disclosure requirements</td>
</tr>
</tbody>
</table>
Technical Provisions

- Some changes to wording in relation to contract boundaries, FMAs and EPIFP

- Change in relation to expenses proposed
  - Suggestion that companies should consider Board’s decisions in relation to writing new business whereas as previously Delegated Regulation said to assume new business would be written

- No changes proposed for risk margin despite lobbying efforts and views on a number of potential improvements
  - But, stakeholders have been asked for views on alternative approaches not already considered
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**Interest Rate Risk SCR**
- Relative shift approach proposed
- e.g. \( r^u_p(m) = r_t(m) \cdot (1 + s^u_p(\theta m)) + b^u_p \)
- Works better with low/negative interest rates

**Equity SCR**
- Discussion but no proposals in relation to long term equity SCR – effectively saying stress is too lenient
- Proposal to phase out duration based equity stress
- Some proposals in relation to proving lower volatility to justify use of strategic equity SCR

**Other SCRs**
- Counterparty Default: some changes e.g. simplification for risk mitigating effect
- Some proposals in relation to reinsurance and other risk mitigation techniques
- Other areas looked at but no changes proposed
Some changes in non-life factors

<table>
<thead>
<tr>
<th>Segment</th>
<th>Old TP Factor</th>
<th>Old Written Premium Factor</th>
<th>New TP Factor</th>
<th>New Written Premium Factor</th>
</tr>
</thead>
<tbody>
<tr>
<td>Credit and suretyship</td>
<td>17.7%</td>
<td>11.3%</td>
<td>16.0%</td>
<td>17.7%</td>
</tr>
<tr>
<td>Legal expenses</td>
<td>11.3%</td>
<td>6.6%</td>
<td>5.2%</td>
<td>7.8%</td>
</tr>
<tr>
<td>Assistance</td>
<td>18.6%</td>
<td>8.5%</td>
<td>20.3%</td>
<td>6.0%</td>
</tr>
<tr>
<td>Accident</td>
<td>4.7%</td>
<td>4.7%</td>
<td>5.4%</td>
<td>No change</td>
</tr>
<tr>
<td>Sickness</td>
<td>13.1%</td>
<td>8.5%</td>
<td>No change</td>
<td>8.0%</td>
</tr>
<tr>
<td>Workers’ Compensation</td>
<td>10.7%</td>
<td>7.5%</td>
<td>10.3%</td>
<td>9.0%</td>
</tr>
<tr>
<td>NPR Health</td>
<td>18.6%</td>
<td>15.9%</td>
<td>15.9%</td>
<td>No change</td>
</tr>
</tbody>
</table>

Some changes in wording in relation to non-compliance or risk of non-compliance
Proportionality

- Easing of thresholds at which Solvency II applies
- EIOPA considering SCR simplifications
- Possible combination of key functions or of key functions with management/AMSB functions
- In ORSA, deviation of risk profile from standard formula assumptions only needed every 2 years
- Allowance for less frequent review of written policies (every 3 years)
Group Supervision

- Changes in definitions and wording to clarify scope of group supervision
- Changes in relation to calculation of group solvency (including minimum consolidated SCR)
- Clarifications in relation to determination of group own funds
- Clarifications on governance requirements for groups

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FoS/FoE

• Requirement as part of authorisation to disclose if application rejected or withdrawn elsewhere

• Requirement for FoS insurers to inform home supervisor immediately of material change in business and for home supervisor to notify host supervisor without delay

• New wording to facilitate collaboration between home and host supervisors:

• Host member states to be given power to request information in a timely manner
Other Topics

- **Fit and Proper Requirements**
  - Changes in wording to harmonise assessments of Board members and qualifying shareholders in SRP
  
  - Allowance for EIOPA to become involved in assessing propriety in complex cross border cases
Summary

Source: EIOPA Fact sheet on the 2020 review of Solvency II

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Risk Management Developments

Solvency II 2020 Review
Risk Management Developments
Solvency II 2020 Review

- Recovery and Resolution
- ORSA
- Systemic Risk Management Plans
- Liquidity Risk Management Plans
Recovery and Resolution Framework

- Proposal to incorporate recovery planning requirements into Solvency II
- Expected contents of a recovery plan reiterated, including
  - Strategic analysis of the group or undertaking
  - Set of possible recovery options to be used across a range of stress scenarios
  - Adverse systemic and idiosyncratic conditions; identify feasibility of options
  - Communication strategy

- Confirmation that reinsurers will also be required to produce recovery plans
Point of entry into Recovery

- Entry into ‘recovery’ defined as breach of 100% SCR
- Entry into early intervention defined as the stage of a deterioration in the financial condition of the Company in accordance with Article 136 of the Solvency II Directive
- Can be required to implement recovery plan during early intervention period, i.e. before breach of 100% SCR
- Regulators to have additional powers during early intervention period, such as to require companies to limit variable remuneration and bonuses
Resolution Powers for Regulators
Supplementing normal insolvency procedures

- Prohibit/recover variable remuneration
- Force closure to new business
- Sell or transfer shares to third party
- Sell or transfer assets/liabilities to a third party or bridge institution
- Override restrictions to transfer assets/liabilities

- Create and operate a bridge institution where to transfer assets/liabilities
- Temporarily Restrict / Suspend surrenders
- Suspend rights of reinsurers to terminate or not reinstate due to cedant’s resolution
- Suspend early termination rights of derivatives and securities lending
- Suspend payments to unsecured creditors and creditor actions

- Require other Group entities to continue to provide essential services
- Take control of and manage the Company or appoint administrator
- Restructure, limit or write down liabilities and allocate losses
Insurance Guarantee Schemes (IGS)

- EIOPA remains of the view outlined in its 2018 consultation paper regarding IGS
- Proposes minimum harmonisation with regards to policyholder protection through the establishment of a European network of national IGSs

| Status Quo | (A) Risk of contagion in insurance industry is less pronounced |
|           | (B) Sufficient protection mechanisms already in place |
|           | (C) Potential costs of IGSs |
|           | (D) Moral hazard effects |

| European network of national IGSs | (A) More equal and effective policyholder protection |
|                                 | (B) Distribution of insurance failure costs to the industry |
|                                 | (C) Increase in consumer confidence and choice |
|                                 | (D) Level playing field across Member States |
Own Risk and Solvency Assessment (ORSA)

Review of the Proportionality Principle and Macroprudential Policy

- Standard Formula appropriateness every 2 years
- Proportionate stress testing and scenario analysis if less complex risk profile
- Inclusion of macroprudential factors within the ORSA
Systemic Risk Management Plan (SRMP)

Macroprudential Policy

- Sources of systemic risk:
  - Excessive involvement in certain activities or products
  - Possessing high concentrations of risk
- EIOPA believes such risk taking should be discouraged, to ensure the stability of the financial sector
- Proposal to require **only certain insurers** to produce a Systemic Risk Management Plan (SRMP)
- SRMP details the measures the company will take to mitigate the systemic risk they pose to the financial system
- Scope to be based on factors such as:

  - Size
  - Interconnectedness
  - Substitutability
  - Nature, scale and complexity
Liquidity Risk Management Plan (LRMP)

Macroprudential Policy

- Proposal to require all Solvency II companies to produce a Liquidity Risk Management Plan (LRMP) – possibility to waive if less exposed to liquidity risk
- LRMP identifies potential liquidity stresses and how firms will address them

EIOPA refers to IAIS Guidance on Liquidity Risk and Management Planning:
- Specify risk tolerances
- Identify contingency funding plans
- Liquidity Gap Analysis
  - A projection over time of liquidity sources under current conditions and future stress scenarios
  - Include scenarios such as high rates of surrenders, cancellations or lapses, liquidity issues at the legal entity level and/or acceleration of liquidity needs at the group level
  - Consideration of short and long term liquidity issues
- Early warning indicators specified and regularly monitored

Possible Liquidity Indicators

<table>
<thead>
<tr>
<th>Liquid assets / technical provisions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Liquid assets / liquid liabilities</td>
</tr>
<tr>
<td>Unencumbered assets / total assets</td>
</tr>
<tr>
<td>Lapse ratios</td>
</tr>
<tr>
<td>Liquidity sources / liquidity needs</td>
</tr>
<tr>
<td>Short term liquidity resources / needs</td>
</tr>
</tbody>
</table>
Net Premium Income

Domestic Life Insurance Business

- 2016 estimate based on sample companies
- 2017 and 2018 figures based on CBI report (with some adjustments)

Figures exclude:
- Standard Life
- Royal London

Source: Blue book
Net Premium Income

Cross Border Life Insurance Business

- 2016 estimate based on sample companies
- 2017 and 2018 figures based on CBI report (with some adjustments)

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### 2018 Gross Written Premiums – Top 10 Irish insurers

**Life and Non-Life Premiums**

<table>
<thead>
<tr>
<th>Total Gross Written Premiums</th>
<th>2018</th>
<th>2017</th>
<th>Type</th>
</tr>
</thead>
<tbody>
<tr>
<td>€ million</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Zurich Insurance</strong></td>
<td>7,738</td>
<td>7,671</td>
<td>Non-Life (Domestic)</td>
</tr>
<tr>
<td><strong>Irish Life Assurance</strong></td>
<td>6,132</td>
<td>7,268</td>
<td>Life (Domestic)</td>
</tr>
<tr>
<td><strong>Intesa Sanpaolo Life</strong></td>
<td>5,748</td>
<td>7,941</td>
<td>Life (Cross Border)</td>
</tr>
<tr>
<td><strong>SCOR</strong></td>
<td>4,103</td>
<td>4,179</td>
<td>Reinsurer</td>
</tr>
<tr>
<td><strong>Zurich Life Assurance</strong></td>
<td>3,383</td>
<td>3,233</td>
<td>Life (Domestic)</td>
</tr>
<tr>
<td><strong>Hannover Re</strong></td>
<td>3,023</td>
<td>2,766</td>
<td>Reinsurer</td>
</tr>
<tr>
<td><strong>Partner Re</strong></td>
<td>2,600</td>
<td>2,485</td>
<td>Reinsurer</td>
</tr>
<tr>
<td><strong>Darta Saving Life Assurance</strong></td>
<td>2,304</td>
<td>3,075</td>
<td>Life (Cross Border)</td>
</tr>
<tr>
<td><strong>New Ireland Assurance</strong></td>
<td>2,175</td>
<td>1,792</td>
<td>Life (Domestic)</td>
</tr>
<tr>
<td><strong>Allianz Re</strong></td>
<td>1,885</td>
<td>1,937</td>
<td>Reinsurer</td>
</tr>
</tbody>
</table>

* SCOR Global Life Reinsurance and SCOR Life Ireland (established in 2018)
### 2018 SCR – Top 10 Irish insurers

The total solvency ratio for all undertakings **INCREASED** from **176%** in 2017 to **187%** in 2018

*(179% to 189% for Life undertakings)*

<table>
<thead>
<tr>
<th>Company</th>
<th>SCR 2018</th>
<th>Ratio 2018</th>
<th>SCR 2017</th>
<th>Ratio 2017</th>
<th>Type</th>
</tr>
</thead>
<tbody>
<tr>
<td>Zurich Insurance</td>
<td>1,704</td>
<td>143%</td>
<td>1,933</td>
<td>135%</td>
<td>Non-Life (Domestic)</td>
</tr>
<tr>
<td>SCOR Life Ireland</td>
<td>1,602</td>
<td>222%</td>
<td></td>
<td></td>
<td>Reinsurer</td>
</tr>
<tr>
<td>Partner Re</td>
<td>1,321</td>
<td>144%</td>
<td>1,374</td>
<td>135%</td>
<td>Reinsurer</td>
</tr>
<tr>
<td>SCOR Global Life Re</td>
<td>1,314</td>
<td>230%</td>
<td>1,654</td>
<td>174%</td>
<td>Reinsurer</td>
</tr>
<tr>
<td>Irish Life Assurance</td>
<td>1,019</td>
<td>175%</td>
<td>1,189</td>
<td>160%</td>
<td>Life (Domestic)</td>
</tr>
<tr>
<td>MetLife Europe</td>
<td>702</td>
<td>171%</td>
<td>813</td>
<td>148%</td>
<td>Life (Cross-Border)</td>
</tr>
<tr>
<td>Allianz Re</td>
<td>639</td>
<td>184%</td>
<td>487</td>
<td>181%</td>
<td>Reinsurer</td>
</tr>
<tr>
<td>Beazley Insurance</td>
<td>573</td>
<td>247%</td>
<td>542</td>
<td>246%</td>
<td>Non-Life (Cross-Border)*</td>
</tr>
<tr>
<td>New Ireland Assurance</td>
<td>572</td>
<td>147%</td>
<td>583</td>
<td>154%</td>
<td>Life (Domestic)</td>
</tr>
<tr>
<td>Zurich Life Assurance</td>
<td>565</td>
<td>138%</td>
<td>705</td>
<td>129%</td>
<td>Life (Domestic)</td>
</tr>
</tbody>
</table>

* Beazley Insurance converted from a reinsurance company to a non-life insurance company in 2017

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Solvency Ratio distribution by country

Life insurance companies (sample only)

The average European SCR Coverage ratio for year-end 2018 is 226%.

The average European SCR coverage ratio has IMPROVED over the year from 218% to 226%.

Impact of LTG Measures on Solvency Ratio

Life insurance companies (sample only)

Over 50% of German companies in our report apply the TMTP.
Harmonisation

Solvency II 2020 review

Aisling Barrett
22 JANUARY 2019
Solvency II regime

Solvency I

Solvency II

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Harmonisation?

- Ireland
  - Head of Actuarial Function role
  - External audit of Solvency II balance sheet
  - National Specific Templates
  - Reporting exemptions
  - Prior approval for use of Volatility Adjustment
  - Use of LTG and transitional measures

- UK – Pillar 2 additions already in place (liquidity risk management, R&R); post Brexit changes? (Risk margin, MA)

- The Netherlands – impact of UFR considered in ORSA and dividend payments; R&R

- Germany – strongly defending position of 20 year LLP

- France – internal models pressure

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Divergent practices identified

- EIOPA identifies divergent practices in Best Estimate calculation in relation to:
  - ESG calibration
  - Contract boundaries
  - Future Management Actions
  - Expenses
  - Expense inflation
  - Valuation of options & guarantees
Solvency II 2020 review

- EIOPA considers the following objectives in evaluating options:
  - Improved transparency & better comparability
  - Ensuring a level playing field through sufficiently harmonised rules
  - Effective & efficient supervision
    - Market consistent, promoting good risk management, limited procyclicality and artificial volatility of TPs and Own Funds

- Areas where proposals would improve harmonisation
  - LTG
  - Pillar 2 – macro prudential aspects, recovery & resolution etc.
  - Audit
  - FoE / FoS
  - Fit and proper requirements
  - Insurance guarantee schemes

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