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23 October 2025

## AAE Note on the Review of the Solvency II Delegated Regulation

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### AAE Solvency II Working Group

#### Introduction

Solvency II has proven its effectiveness as a robust, risk-based framework that ensures policyholder protection and financial stability across Europe, even during periods of historically low interest rates and through recent market stresses. Insolvencies among insurers have remained rare within the EU, demonstrating the framework's resilience.

Regular reviews are nevertheless essential to keep the regime fit for purpose – to recalibrate risk parameters and models, to incorporate emerging risks, and to reflect evolving political and economic priorities. Following the agreement on the revised Solvency II Directive in January 2025, the European Commission published its **draft Delegated Regulation for consultation in July 2025**, setting out the detailed Level 2 measures that will determine how the updated framework operates in practice. The AAE has responded to this consultation [providing its views](#) on the proposed review.

The review represents a further step in the Solvency II development process. The scope of Solvency II is gradually extended beyond the mandatory assessment of long-term guarantee (LTG) measures to encompass several broader policy objectives and macroprudential considerations, including:

- enhancing insurers' contribution to long-term financing of the European economy and to the EU's Savings and Investments Union,
- introducing macroprudential tools, particularly for liquidity-risk management,
- embedding sustainability and ESG considerations,
- strengthening proportionality, and
- reducing unnecessary administrative burden in reporting and disclosure.

The AAE recognises and supports these objectives. At the same time, the profession emphasises that the credibility of Solvency II rests on its **evidence-based calibration** and **principles-based application**.

The Commission's proposed Delegated Regulation will play a decisive role in shaping the revised framework. Despite the broadening of the scope and the aim to remove overly conservative elements while enabling insurers' to invest in the economy for the long-term, it remains essential that policyholder protection and financial stability continue to prevail as primary objectives.

*The Actuarial Association of Europe (AAE) was established in 1978 under the name Groupe Consultatif to represent actuarial associations in Europe. Its primary purpose is to provide advice and opinions to the various organisations of the European Union - the Commission, the Council of Ministers, the European Parliament, the European Supervisors and their committees – on actuarial issues in European legislation. The AAE currently has 38 member associations in 37 European countries, representing nearly 30,000 actuaries. Advice and comments provided by the AAE on behalf of the European actuarial profession are totally independent of industry interests.*

*The Actuarial Association of Europe is registered in the EU Transparency Register under number 550855911144-54*

## 1. General Observations

### **Balance between competitiveness and prudence**

Capital released through the calibration of the risk margin may support long-term investments in the economy as stipulated by the broader policy objectives of the European Commission, but it can reduce insurers' buffers against stress. The AAE emphasises that policyholder protection and financial stability must remain the overriding objectives. Even when the adaptation of risk parameters can be substantiated by market conditions, it is indispensable to analyse the extent to which these are appropriate for undertakings without compromising their resilience. Policyholder protection, the ability to meet, at any time, the obligations resulting from insurance contracts, must not be impaired.

### **A principles-based framework for effective governance**

Solvency II's credibility rests on the evidence-based calibration of capital requirements and the professional judgement and governance of insurers. Especially for users of the standard formula, technical standards should complement—not replace—the responsibility of undertakings to apply sound actuarial and risk-management judgement through their key functions and the Own Risk and Solvency Assessment (ORSA). For this purpose, actuarial work combines historical experience with a forward-looking analysis of all material risks when deciding on the calculation method.

### **Role of risk management and data**

The Delegated Regulation introduces a requirement to avoid over-reliance on past data for climate-related risks. The AAE agrees that forward-looking analysis is essential, but this principle should apply to all material risks, not only to climate change. Actuarial work already combines historical experience with expectations about future developments, as foreseen by Article 34(2) of the existing Regulation.

## 2. Key Technical Issues

### **Risk margin**

We welcome the proposed introduction of a time-dependent exponential factor ( $\lambda$ ) in the risk-margin formula. This change appropriately reflects the natural decline of risk over time and reduces undue volatility linked to interest-rate movements. The combined effect of the  $\lambda$  adjustment and the lower cost-of-capital rate can significantly affect undertakings' resilience, especially for long-term business where capital requirements are significantly reduced.

We note that the proposed revision could result in a significant reduction in the risk margin and therefore a reduction in technical provisions. It is important to strike a balance between reducing capital requirements and ensuring the continued protection of policyholders.

The AAE encourages evidence-based calibrations and supports these measures insofar as they remain consistent with policyholder protection. We recommend that undertakings assess the impact carefully within their ORSA.

### **Extrapolation of the risk-free interest-rate term structure**

The extrapolated risk-free curve is fundamental to the valuation of long-term liabilities. We support the stability objectives of the new methodology but note that the minimum convergence-speed parameter ( $\alpha = 11\%$ ) may still produce excessive volatility in certain market conditions. A higher  $\alpha$  could provide greater stability and ensure that the phasing-in mechanism is only triggered in cases of sustained low-rate environments.

We welcome the proposed approach to setting a threshold for the residual-volume criterion by considering a safety margin to immunise against changes of the data source and to help preserve the

20-year first smoothing point for the euro curve on 30 January 2027, avoiding unnecessary changes over time. This can add stability to the valuation of long-term business.

### **Volatility Adjustment (VA)**

We acknowledge the intention to make the VA more risk-sensitive through a revised risk-correction formula and the introduction of the Credit Spread Sensitivity Ratio (CSSR). However, greater sensitivity may also amplify volatility in solvency positions, particularly during short-term spread widenings. The reliance on a currency-specific reference portfolio remains a methodological weakness, as this may be materially different to an undertaking's actual asset mix which is updated only once per year. The CSSR is intended to mitigate the risk of overshooting by requiring undertakings to compare the sensitivity of their assets to credit spread changes with the sensitivity of their best estimate liabilities to interest rate movements.

Despite the rather complex calculations, the proposed VA cannot fully resolve structural limitations. We therefore suggest that the CSSR is determined and monitored within the ORSA rather than through frequent recalculations for reporting purposes. Overall, the prudent use of the VA should continue to be supported primarily through sound governance and risk management, rather than through increasingly complex formulae.

The requirement to include the VA in undertakings' liquidity-risk management plans, combined with strengthened risk-management obligations, can provide an effective safeguard if applied proportionately.

### **Interest-rate risk sub-module**

The methodological change required by the Directive—to stress the risk-free interest-rate curve before extrapolation rather than stressing the extrapolated curve—is in line with earlier AAE recommendations and provides a more coherent treatment of long-term guarantees. The inclusion of a maturity-dependent floor appropriately ensures that extremely negative interest rates are excluded from the calibration.

However, the calibration itself was developed during a prolonged period of low or even negative interest rates and has not been re-evaluated in light of the sharp and sustained increases in yields observed since 2022. In this year, actual rate movements exceeded the assumed up-shock in the standard formula.

The AAE therefore recommends that EIOPA and the Commission undertake a comprehensive recalibration of the interest-rate risk module, incorporating data up to 2024 and considering alternative yield-curve shapes. We note the analytical work undertaken by the *Institut des Actuaire*s in France as a valuable reference point for this reassessment.

### **Long-term equity and investment incentives**

The AAE supports efforts to facilitate long-term equity investment and recognises insurers' potential contribution to the EU's Savings and Investments Union. However, the current liquidity criteria for long-term equity portfolios remain overly restrictive and out of reach for most insurers, despite their proven ability to hold equity investments over extended periods. A qualitative assessment within the ORSA would provide a more effective and proportionate means of assessing liquidity than the very complex proposed liquidity test. Furthermore, the exclusion of investments in equity funds—despite their similar risk characteristics to direct equity holdings—can serve to undermine the practical relevance of the current framework. Any application of the long-term equity investment (LTEI) regime should therefore remain proportionate to the actual scale of exposures and consistent with sound risk management principles.

### **Proportionality and simplification**

The AAE strongly supports the clearer articulation of proportionality through explicit conditions for small and non-complex undertakings (SNCU) and at group level. The regulation concerning the use of proportionality measures by non-SNCUs can promote consistency and a level playing field across Member States. However, proportionality should not be undermined by parallel new requirements such as the calculation of expected profits in future fees (EPIFF), which adds complexity without proven benefit.

### **3. Reporting, Disclosure and Governance**

The AAE welcomes the Commission's proposal to restructure the Solvency and Financial Condition Report (SFCR) into two parts: a concise summary directed at policyholders and beneficiaries, limited to five pages, and a more detailed section aimed at market professionals and supervisory users. This reform can enhance readability, improve the accessibility of information for the public, and reduce unnecessary reporting burden for undertakings.

However, some of these benefits may be offset by additional requirements for undertakings deemed relevant to the EU financial system under Article 297 of the draft Delegated Regulation. The obligation to perform and disclose supplementary scenario analyses for these firms could significantly increase complexity. The AAE recommends that materiality criteria be applied to ensure that such exercises remain proportionate and meaningful.

The AAE also anticipates that forthcoming sustainability reporting obligations are likely to expand disclosure requirements further, potentially exceeding the intended simplification. Coordination between prudential, resolution, and macro-prudential authorities will be essential to prevent duplication of requests and uncoordinated supervisory initiatives. Effective cooperation at both national and European levels is needed to maintain coherence, proportionality, and focus on information that truly supports policyholder protection and financial stability.

### **4. Concluding Remarks**

The AAE welcomes the Commission's efforts to modernise Solvency II and supports the broad direction of travel. The revised Delegated Regulation can strengthen the framework if it preserves its key characteristics:

- evidence-based calibration,
- principles-based application, and
- strong governance and professional judgement through the key functions.

Actuaries have a central role in ensuring that these principles are upheld in practice. The AAE stands ready to contribute its technical expertise to policymakers and supervisors as they finalise the Level 2 text and its implementation.

*This note reflects views from the AAE Solvency II Working Group. Any views expressed in this note are views to stimulate and inform further discussion and should not be read as being representative or an agreed position of the Actuarial Association of Europe.*