



ACTUARIAL ASSOCIATION OF EUROPE

Solvency II

Insurance Committee

Vilnius

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18 April 2024

Preliminary remarks

- Upon completion of the amended Directive, AAE's position paper on the solvency II review is outdated. A review is necessary to consider the amendments.
- The Directive contains some guidance regarding issues addressed in the position paper.
- But Commission is empowered to lay down crucial technical specification in the Delegated Regulation or in Technical Standards.
- Some of these will be addressed in this presentation.
- The Working Group aims at drafting an update of the position paper short-term.
- Comments from IC-members preferably by end of April would be appreciated.

Agenda

- a) Background
- b) LTG-related measures
- c) Sustainability and macroprudential tools
- d) The IRRD
- e) Supplementing information

Interplay Directive and Delegated Regulation

View of co-legislators on the role of Delegated Regulation

- What is an “essential element” of the legislative act?
- What is a political issue and should be reflected in the Directive?

EU-Council suggestions: (Addendum to the compromise paper, 14 June 2022)

...- invite the Commission to present the current state of play of envisaged amendments to the Delegated Regulation in order to ensure the **balance and the consistency of the whole review of the SII framework**;

Rapporteur Markus Ferber: (Draft report from 6 June 2022)

Delegated acts are **not the appropriate instrument to deal with political issues.**

...

For these reasons your rapporteur proposes in this draft report amendments to provide more details and political guidance directly into the Directive in relation to:

- **the risk-free interest rate curve, including extrapolated part;**
- **the Risk Margin;**
- **the Volatility Adjustment;**
- **long-term equity investments**

Considered
in Directive!

Role of legislators: preparation of Delegated acts

Clarification of roles based on Interinstitutional Agreement on Better Law-Making (13 April 2016)

Recital 82b

The power to adopt delegated acts should be delegated to the Commission in respect of

- the criteria for identifying **small and non-complex undertakings** (SNCU) and groups,
- the treatment of risk posed by **crypto assets** in the market risk sub-module,
- clarifications concerning **long-term investments**,
- the criteria for limited supervisory reporting for captive insurance and reinsurance undertakings,
- the prudent **deterministic valuation of the best estimate** (SNCU!),
- the application of the simplified approach for the purpose of calculating group solvency,
- the information to be included in the group regular supervisory report, and
- **extending reporting deadlines** in exceptional circumstances.

Important: Commission shall carry out appropriate consultations during its preparatory work

In particular: **ensure involvement of Parliament and Council in preparation of delegated acts**

Outcome of the review: view of politics

Source: Press release of the European Commission 13-12-2023 - 20:58



The **main aim of the review** of the SII directive is to strengthen European insurers' contribution to the financing of the recovery, progressing on the Capital Markets Union and the channeling of funds towards the European Green Deal.

It is estimated that the rule changes could allow the insurance sector to invest around another **EUR 100 billion** into the economy, equal to around 0.6% of the EU's GDP.

The aim of the IRRD is to ensure that insurers and the relevant authorities in the EU are better prepared in cases of significant financial troubles.

Until now: Only amendment of the Directives available

- relevant technical details shall be laid down in Delegated Regulation
- reliable quantification of impact only possible, on the basis of these details
- Visionary power at politicians' disposal?

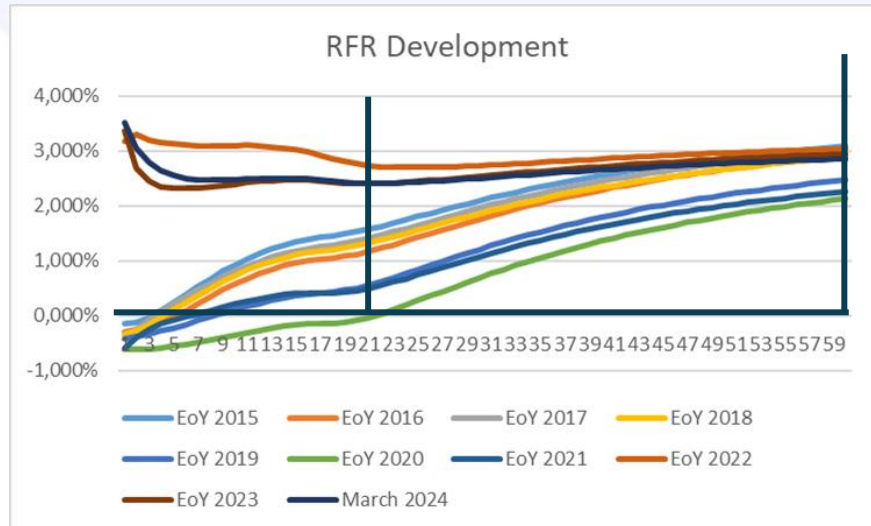
Basis for this impact assessment: presumably EIOPA's technical advice, provided in 2020

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Significant changes in capital markets

Significant change of interest environment
Inverse interest rate term structures indicate uncertainty



9 March 2024: 10-year CMS Swap rate
<https://www.finanzen.net/zinsen/cms-swap-satz-eur>

Extrapolation: New methodology

Current method (Euro)

Omnibus II-Directive: **Recital 30**

...the starting point for the extrapolation in particular for the euro, should be at a **maturity of 20 years**.

The extrapolated part of the relevant RFR, in particular for the euro, should converge in such a way to the UFR that

for maturities 40 years past the starting point the extrapolated forward rates do not differ **more than three basis points from the ultimate forward rate**.

New: Article 77a extended

As of the first maturity ('**first smoothing point-FSP**') where markets for those financial instruments are not DLT, the relevant RFR shall be extrapolated.

Extrapolated part shall be based on forward rates converging smoothly from the **applicable forward rate** at FSP to the UFR.

The extrapolated forward rates shall be equal to a weighted average of a liquid forward rate and UFR.

The liquid forward rate shall be based on forward rates in relation to the longest maturities for which the relevant financial instrument can be observed in a DLT market.

For maturities of at least 40 years past the first smoothing point **the weight of the UFR shall be at least 77,5%.**

"Political issue"

Extrapolation: Empowerment for Commission

Source article 86

The Commission shall adopt delegated acts laying down the methodologies, principles and techniques for the determination of the relevant RFR to be used to calculate the best estimate of the technical provisions, in particular

- i. the formula for the extrapolation, including the parameters that determine the convergence speed;
- ii. the method for the determination of the depth, liquidity and transparency of bond markets
- iii. currency related percentages below which the share of bonds with maturities longer than or equal to a given maturity among all bonds shall be regarded as low
- iv. the phasing-in mechanism

Topics affected

- alpha, last liquid forward rate (LLFR), formula for extrapolation
- Residual volume criterion, determination of threshold (currently 6%)
- Determination of RFR during phasing-in period

Weight of the UFR

The extrapolated forward rates shall be equal to a weighted average of a liquid forward rate and the UFR. For maturities of at least 40 years past the first smoothing point **the weight of the UFR shall be at least 77.5%.**

Objective:

Setting guardrails for convergence tolerance (based on EIOPA's proposed formula).

$$f_{FSP, FSP+h} = \ln(1+UFR) + (LLFR - \ln(1+UFR)) * B(a, h)$$

$$= \ln(1+UFR) * (1 - B(a, h)) + LLFR * B(a, h)$$

Weight of the UFR ($1-B(a, h)$) affects the determination of alpha in level 2.

$B(a, h) = (1 - e^{-ah}) / ah$, h = Duration post FSP

$a = 10\%$: $B(a, 40) = 0,2454 \rightarrow (1 - B(a, 40)) = 75.46\%$ proposed by EIOPA

$a = \mathbf{11\%}$: $B(a, 40) = 0,2245 \rightarrow (1 - B(a, 40)) = \mathbf{77.55\%}$ **minimum weight**

($a = 17\%$: $B(a, 40) = 0,1469 \rightarrow (1 - B(a, 40)) = 85.31\%$ low interest rate environment)

Volatility adjustment(VA): risk correction

VA based on spread (S) between interest rate that could be earned from assets in the reference portfolio and the respective rates of the RFR.

Risk correction (RC) aims at eliminating risk inherent in S

Risk-corrected spread (RCS): **$RCS = S - RC$**

$VA = 0.65 * RCS$

Separate consideration of risk correction (RC) for

a) Government bonds (RC_{gov}), ratio w_{gov} of value in the reference portfolio

b) Bonds other than governance bonds, loans and securitization (RC_{corp}), ratio w_{corp} of value in the reference portfolio

As to a) $RC_{gov} = 30\%LTAS_G$, (35% for non-EEA states)

As to b) $RC_{Corp} = \max(35\%LTAS_C, PD+CoD)$

LTAS: long-term average of the spreads over the RFR,

PD+CoD: probability of default, cost of downgrade

$$RC = w_{gov} * \max(RC_{gov}, 0) + w_{corp} * \max(RC_{corp}, 0)$$

Identified risk: Overshooting in case of widening spread:

Increase of RFR not justified by own assets; undervaluation of technical provisions possible

VA: revised formula

Proposed change: $VA = 85\% \cdot CSSR \cdot RCS$

"Political issue"

- Risk-correction de-coupled from fundamental spread, current spread considered
- Undertaking-specific credit spread sensitivity ratio (CSSR) with $0 \leq CSSR \leq 1$.

Spread underlying the VA: weighted sum of the average spread on government bonds (S_{gov}) and on bonds other than government bonds, loans, and securitisations (S_{corp}) in reference portfolio.

Weights: ratio of the value of two respective bond-classes and the value of all assets in reference portfolio.

The risk correction shall be calculated as a **percentage of spreads**.

Percentage shall decrease as spreads increase and shall at least differentiate the following three cases:

- (a) spreads \leq their LTAS;
- (b) their LTAS $<$ spreads \leq twice their LTAS;
- (c) twice their LTAS $<$ spreads

If specified conditions are met, an undertaking-specific adjustment to the RCS is possible.

Risk correction **shall never exceed an appropriate percentage of the LTAS**

VA: Empowerment for Commission

Adopt delegated acts laying down methods and assumptions for the calculation of the VA including:

- i. a formula for the calculation of the spread
- ii. a formula for the calculation of the CSSR
- iii. Calculate for **each relevant asset class**, the percentage of the spread representing the portion attributable to a realistic assessment of expected losses, unexpected credit risk or any other risk. Such percentage should decrease as spreads increase, considering at least the following three cases:
 - Where spreads do not exceed their long-term average;
 - Where spreads exceed their long-term average but do not exceed twice their long-term average;
 - Where spreads exceed twice their long-term average.

The risk correction shall never exceed **an appropriate percentage of the long-term average spreads.**

Affected topics

- methodology for the calculation of the spread undertaking-specific adjustment to the RCS
- Calculation of CSSR
- risk-component in the observed spread; e.g. default and cost of downgrade
- determination of appropriate percentage of LTAS

VA: Interdependencies – Pillar 1, Pillars 2 and 3

Art.77d:

Volatility adjustment

$$VA = 85\% \cdot CSSR \cdot RCS$$

Article 51: **SFCR**

Part addressed to market participants:

- Impact of a change of VA to zero on the financial position
- for each relevant currency, the VA and corresponding best estimates for insurance obligations

Article 44: **Risk management**

- Consider VA in **LRMP**
- Sensitivity of TP to change of risk that would affect RCS
- Consideration of VA in written policy

Article 45: **ORSA**

- Significance of deviation of own risk profile from assumptions underlying VA

Article 122: **Calibration standards**

- Use of credit spread movements on the VA only in internal model (DVA)

Article 144a (5): **Liquidity risk management**

Combination of required LRMPs possible

Possible starting point: (EIOPA's advice, supported by Commission and Council)

Risk correction considers a percentage of spreads S if higher than LTAS

$$RC_{\text{gov}} = 30\% \cdot \min(S^+, LTAS^+) + 20\% \cdot \max(S^+ - LTAS^+, 0)$$

$$RC_{\text{corp}} = 50\% \cdot \min(S^+, LTAS^+) + 40\% \cdot \max(S^+ - LTAS^+, 0)$$

Commission will consider EIOPA's advice and possibly change the DR to address overshooting due to differences in the credit spread sensitivity of assets and interest-rate sensitivity of liabilities.

Source: Communication from the Commission to the European Parliament and the Council on the review of the EU prudential framework for insurers and reinsurers in the context of the EU's post pandemic recovery (Brussels, 22.9.2021)

Long-term equity investment (LTEI)

LTEI shall contribute to the financing of Green Deal and European projects

Commission's Action plan:

Participation of insurers in long-term investments, in particular equity, can be supported by ensuring that the prudential framework appropriately reflects the long-term nature of the insurance business and mitigates the impact of short-term market turmoil on insurers' solvency.

Action 4: *The Commission will seek to remove regulatory obstacles for insurance companies to invest long-term, without harming financial stability and policyholder protection.*

(Source: https://ec.europa.eu/finance/docs/law/200924-capital-markets-union-action-plan_en.pdf)

Current framework:

Asset class LTEI introduced in 2019 (Delegated Regulation Article 171a)

The stress for this asset class is reduced to 22% for listed and unlisted equities as well.

Regulatory obstacle: eligibility of equities and administrative limitations restrained the use of this asset class.

Long-term equity investment (LTEI)

Source Article 105a

"Political issue"

LTEI is part of the equity risk sub-module with reduced capital requirement.

Requirements

- a) sub-set of equity investments clearly identified and managed separately from the other activities
- b) long-term investment management for each LTE portfolio: reflect the commitment to hold the global exposure to equity for more than five years. Regular review and reporting in ORSA required.
- c) only equities listed in EEA or OECD countries or unlisted equities of companies that have their head offices in EEA or OECD countries;
- d) demonstrate that on an ongoing basis and under stressed conditions, forced selling of equity investments can be avoided within the sub-set for five years
- e) the risk management, ALM and investment policies of the undertaking reflect the undertaking's intention to comply with b) and d)
- f) the sub-set of equity investments is appropriately diversified
- g) the sub-set of equity investments does not include participations.

The capital requirement for LTEI: stress reduced to **22 %**.

Risk margin: change of calculation

Source: Article 77:

Calculation of the risk margin:

“Political issue”

Determination of the cost of providing an amount of eligible own funds equal to the time-adjusted SCR necessary to support the insurance obligations over the lifetime thereof.

The adjustment of the SCR consists of an exponential and time-dependent element.

The Cost-of-Capital (CoC) rate shall be assumed to be equal to **4,75 %**.

Periodical review by Commission: not earlier than 5 years after the date of application

Source: Article 86:

Depending on the result of periodical review:

Value of the CoC rate can be amended by a delegated act. But: **$4\% \leq \text{CoC rate} \leq 5\%$**

Risk margin: significant reduction expected

Two components of risk margin: the cost of capital-rate and the present value of future SCR_s

$$\mathbf{RM} = \mathbf{CoC} \cdot \sum_{t \geq 0} \frac{SCR(t)}{(1+r(t+1))^{t+1}}, \text{ where}$$

- SCR(t): SCR after t years;
- r(t+1): basic risk-free rate for the maturity of t+1 year
- CoC = **6%** (cost of capital-rate) Delegated Regulation, Article 39

Possible implementation of new requirements (proposed by EIOPA)

$$\mathbf{RM} = \mathbf{CoC} \cdot \sum_{t \geq 0} \frac{SCR(t)}{(1+r(t+1))^{t+1}} \times \mathbf{max}(\lambda^t, \mathbf{floor}), \lambda=?$$

$$\mathbf{CoC} = \mathbf{4.75\%} \quad \text{Directive, Article 77}$$

To be laid down in delegated regulation: The factor lambda and the floor.

Source: Communication from the Commission to the European Parliament and the Council on the review of the EU prudential framework for insurers and reinsurers in the context of the EU's post pandemic recovery (Brussels, 22.9.2021)

The Commission will consider building on the lambda approach proposed by EIOPA, but without a floor parameter, to allow for more effective mitigation of volatility than under EIOPA's proposal.

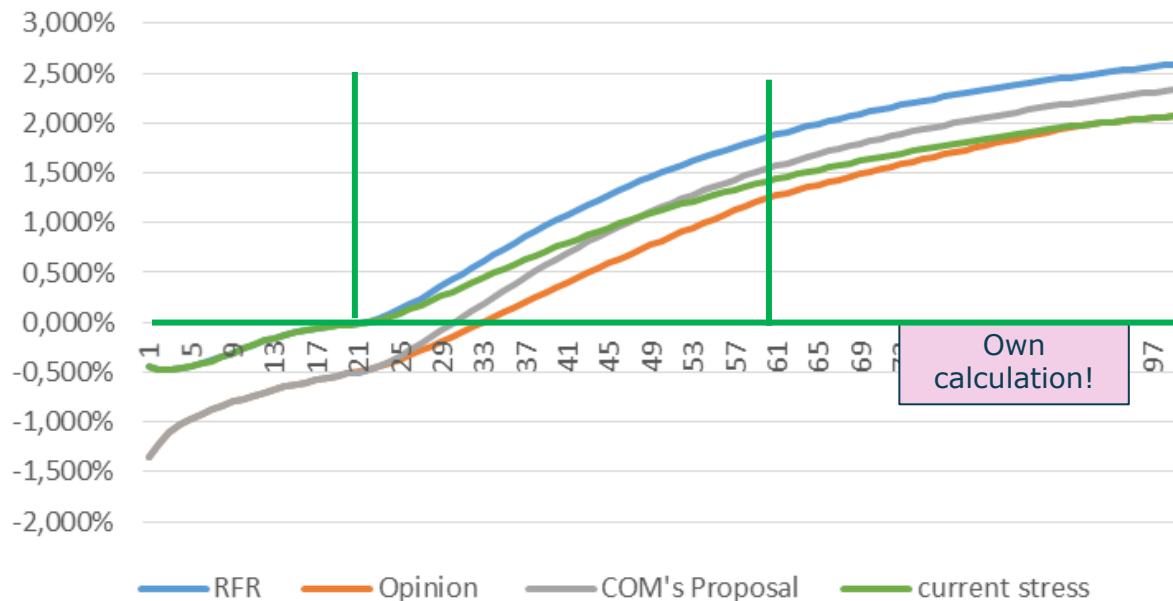
Interest rate risk sub-module

Details to be laid down in delegated regulation

"Political issue"

Interest rate down stress

Reference date
30 June 2020: Euro



Commission considers to build on EIOPA's advice.

EIOPA proposed the shift-approach:
Proportional Stress + Additive component, linearly decreasing after FSP to 0 after 60 years.

Source article 111

Requirements:

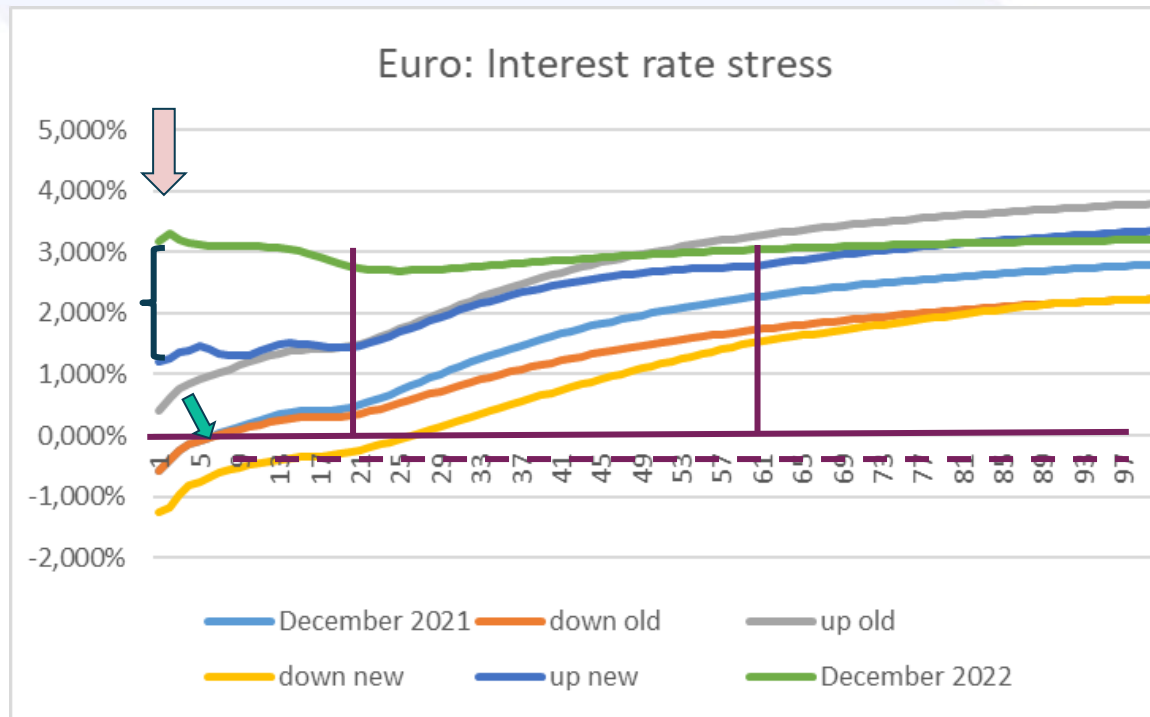
- Determination of a negative floor
- **Consistency** with extrapolation of interest rate.
- Consider a phasing-in over up to 5 years.

EIOPA-approach: first extrapolate – then stress <-> now required: "first stress – then extrapolate"

https://ec.europa.eu/info/publications/210922-solvency-2-communication_en

Recalibration of interest rate risk

Risk parameters in Delegated Regulation (Article 166 - increase, Article 167 - decrease)
Current proposal developed in low-risk environment, focussing on risk of decrease



Possible further analyses:

- Risk of increase in RFR

Adaptation required because of inflationary tendencies?

→ Risk underestimated in 2022

- Brexit: impact of UK-data

Eliminate UK-data, review calibration

(source recital 83a)

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Sustainability in risk management

New requirements concerning sustainability in risk management

Requirements: Assessment of sustainability risks over the short, medium and long term.

For this purpose: develop strategies, policies, processes, and systems for the identification, measurement, management and monitoring of these risks over the short, medium and long term.

Undertakings shall develop and monitor the implementation of

- specific plans,
- quantifiable targets, and
- processes to monitor and address the financial risks arising in the short, medium, and long-term from sustainability factors
- Include those factors relevant for the achievement of regulatory objectives.
(in particular to consider: the European Climate Law).

Macroprudential risks in the ORSA

Undertakings shall consider and analyse

- the macroeconomic situation and possible macroeconomic and financial markets development
- **upon a reasoned request** of supervisor (SNCU exempted), concerns that may affect
 - the specific risk profile,
 - the approved risk tolerance limits,
 - the business strategy,
 - the underwriting activities or the investment decisions, and
 - the overall solvency needs
- activities that may affect the macroeconomic and financial markets' developments, with potential to turn into sources of systemic risk
- the overall capacity to settle its financial obligations even under stressed conditions

Macroprudential risks in the ORSA

Regarding macroeconomic and financial markets' developments: this shall include, at least the following:

- (a) the level of interest rates and spreads;
- (b) the level of financial market indices;
- (c) inflation;
- (d) interconnectedness with other financial market participants;
- (e) climate change, pandemics, other mass-scale events and other catastrophes, which may affect insurance and reinsurance undertakings.

Macroprudential concerns: shall include, at least,

- plausible unfavourable future scenarios and
- risks related to the credit cycle and economic downturn,
- herding behaviour in investments or excessive exposure concentrations at the sectoral level.

Climate change risk in the ORSA

New Article 45a

Undertakings shall consider climate change risk as potential long-term risk

1. Assess whether it has **any material exposure to climate change risks** and demonstrate the materiality in its ORSA.
2. If materially exposed, it **shall specify at least two long-term climate change scenarios**, including the following scenarios regarding global temperature increase
 - a) the increase remains below two degrees Celsius;
 - b) the increase is significantly higher than two degrees Celsius.
3. At regular intervals (≤ 3 years): Analysis of the impact on the business. The analysis shall be part of the ORSA.
4. Review of scenarios at least every three years, update if necessary. Consider the performance of tools and principles used in previous scenarios, to enhance their effectiveness.

Mandates for EIOPA related to ESG objectives

Two mandates for EIOPA in Article 304a:
EIOPA is mandated

- To assess justification for a dedicated prudential treatment of exposures related to assets or activities associated substantially with ESG objectives.

In particular, to assess the potential effects of such a treatment on the protection of policy holders and financial stability in the Union, *including fossil fuel related assets*

EIOPA shall submit a report to Commission by **30 September 2024**

Preparatory activities: Two consultations

Prudential Treatment of Sustainability Risks Discussion Paper

EIOPA-BoS-22-527 29 November 2022

Prudential Treatment of Sustainability Risks Consultation paper

EIOPA-BoS-23-460 13 December 2023

- to review regularly (at least every five years) the scope and the calibration of **parameters of the standard formula pertaining to natural catastrophe risk**.

First review: shall be completed two years after entering into force of the Directive.

Liquidity risk management

Liquidity risk is the risk that insurance and reinsurance undertakings are unable to realise investments and other assets to settle their financial obligations when they fall due.

Liquidity risk management: (Delegated Regulation Art. 260)

- (i) actions to be taken by the undertaking to consider both short-term and long-term liquidity risk;
- (ii) appropriateness of composition of assets in terms of their nature, duration and liquidity in order to meet the undertaking's obligations as they fall due;
- (iii) a plan to deal with changes in expected cash in-flows and out-flows.

Risk: Could turn to into sources of risks for the financial sector

Table 1-1 Microprudential objectives vs. macroprudential objectives

Microprudential objectives	Macroprudential objectives
<ul style="list-style-type: none"> • Measure the exposures of individual insurers to liquidity risks • Assess vulnerabilities and resilience of individual insurers to liquidity risks • Enhance risk management capabilities to assess and mitigate liquidity risks 	<ul style="list-style-type: none"> • Assess vulnerabilities and resilience of overall insurance sector and potential systemic liquidity risks • Assess potential spill-overs to other financial sectors and the real economy of liquidity risks

Liquidity risk management

Source article 144a:

Goal: Undertakings shall maintain adequate liquidity to settle financial obligations towards policyholders and other counterparties when they fall due, even under stressed conditions.

They shall

- draw up and keep up to date a **liquidity risk management plan (LRMP)** covering liquidity analysis over the short term.
- on request of supervisor: extent the LRMP to cover also liquidity analysis over medium and long-term
- develop and keep up to date a set of liquidity risk indicators to identify, monitor and address potential liquidity stress
- submit the LRMP to the supervisory authorities

Undertakings applying MA or VA: the LRMP required in this context can be combined.

SNCU not requested to draw up LRMP

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IRRD requirement

Supervisory authority

Recovery plan (solo) (source article 5)

Undertakings shall prepare and regularly update pre-emptive recovery plans (assessed by supervisory authority):

- Minimum market coverage: **60%**
- SNCUs excluded, consideration of proportionality aspects
- Assessment against a set of scenarios
- Approval of the plan by AMSB
- Regular review and update if indicated

Plans should contain a framework of qualitative and quantitative indicators identifying the points at which remedial actions should be considered.

RTS: determination of market share, ...

RTS: content of pre-emptive plans, ...

Guidelines: specification of scenarios, indicators,

Resolution authority

Resolution plan (solo) (source article 9)

Resolution authority shall prepare resolution plans setting out resolution actions:

- Minimum market coverage: **40%** (based on risk assessment)
- SNCUs are excluded if no risk on regional or national level
- Consideration of relevant resolution scenarios
- Analysis of options for resolution regarding impact and financing
- Consider a comprehensive list of aspects
- Review: at least every two years

Submit plans to supervisory authority

RTS: content of pre-emptive plans, ...

Guidelines: criteria for the identification of critical functions.

IRRD: objectives and resolution tools

Objectives of resolution

- (a) protecting policyholders, beneficiaries and claimants;
- (b) maintaining financial stability, in particular, by preventing contagion and by maintaining market discipline;
- (c) ensuring the continuity of critical functions;
- (d) protecting public funds by minimising reliance on extraordinary public financial support.

The way to resolution: Supervisor's assessment will start the process if

- 1) an undertaking is assessed as likely to fail or in case of a failure
- 2) No reasonable prospect of recovery is identified

Resolution authority involved:

Liquidation of the undertaking or go into resolution

In resolution: Choice of an appropriate resolution tool.

General principle: "no creditor worse off than under normal insolvency proceedings" .

Five resolution tools considered:

- (a) the solvent run-off tool;
- (b) the sale of business tool;
- (c) the bridge undertaking tool;
- (d) the asset and liability separation tool;
- (e) the write-down or conversion tool

Steps to resolution

Provisional valuations (Source article 23):

A first valuation shall ensure that the conditions for resolution are met.

A second valuation when decision is taken to i.a.

- allow an informed decision on the appropriate resolution action to be taken;
- ensure that any losses of the entity are fully recognised when the resolution tools are applied;
- Provide the basis for further decisions related to the particular resolution tool

Definitive valuation required as soon as possible after resolution

The **definitive valuation** (Source article 25)

(a) allows for full recognition of any losses of the entity in its books;

(b) substantiate a decision to write back creditors' claims or to increase the value of the consideration paid,

Correction of net asset value if this is higher than in provisional valuation.

RTS: specify methodology for calculating the buffer for additional losses included in provisional valuations.

Member states shall establish **financing arrangement:** provide funds through ex-ante or ex-post contributions or combination thereof from undertakings. Goal: i.a. safeguard 'no creditor worse off'-principle (Source article 77a)

Insurance guarantee schemes (IGS)

IGS are under discussion for more than a decade.

Article 91a Insurance Guarantee Schemes (IGS)

The Commission is requested to submit a report for Parliament and Council assessing the appropriateness of minimum common standards for IGS, by **24 months** after entry into force

The report shall at least

- (a) assess the state of play of IGS in Member States (coverage level, types of insurances covered, triggers);
- (b) discuss policy options, including the different policy options such as using IGS to continue or to liquidate insurance policies, thereby considering the differences in insurance products in various Member States;
- (c) assess the necessity of introducing and, where appropriate, outline the necessary steps to introduce a minimum baseline for IGS across the Union;

The report shall be accompanied by a legislative proposal where appropriate.

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Solvency II-Review 2020

Review process: a long journey

11 February 2019	Commission's request for technical advice to EIOPA (due 30 June 2020)
17 December 2020	<div> <div>EIOPA's opinion on the 2020 review of solvency II</div> <div>Background document: Analysis (1,086 pages)</div> <div>Background document: Impact assessment (471 pages)</div> </div> <div>Delayed due to Covid-19 pandemic</div>
22 September 2021	<div>Commission proposed amendments of Solvency II</div> <div>Proposal for a new directive recovery and resolution - IRRD</div> <div>Communication on the review of the prudential framework</div>
2 June 2022	Council of the European Union: Proposed amendments SII
16 December 2022	Council of the European Union: Proposed amendments to IRRD
13 September 2023	<div>European Parliament: Proposed amendments SII</div> <div>European Parliament: Proposed amendments to IRRD</div>

Solvency II-Review 2020

Review process: finally gained momentum in trilogue negotiations

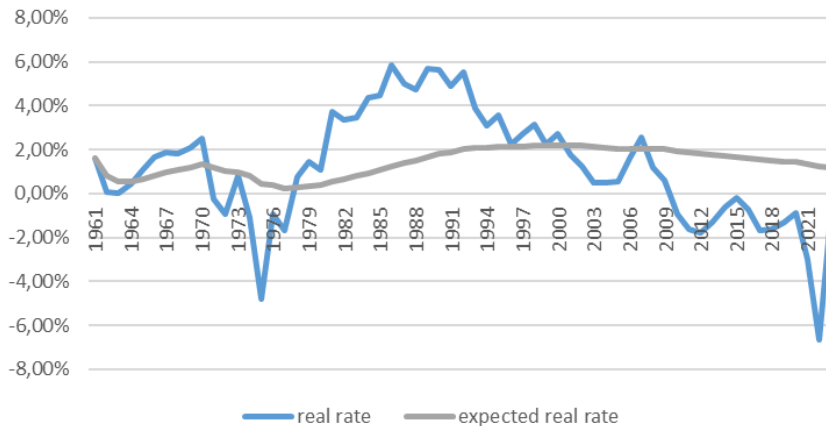
18 September 2023	Start of negotiations of trilogue parties concerning - Amendment to the SII directive and - Amendment to the IRRD	 European Commission
13 December 2023	Agreement achieved: SII Directive	 
14 December 2023	Agreement achieved: IRRD	
19 January 2024	Draft amendments of Directives published	
April 2024?	Adoption by Parliament (and Council)	

To consider:
Elections for European
Parliament in June 2024

Impact of inflation on the UFR

Delegated Regulation, Article 47: UFR shall be stable over time and shall only change as a result of changes in long-term expectations. → Methodology introduced 2016.

UFR: real rate component



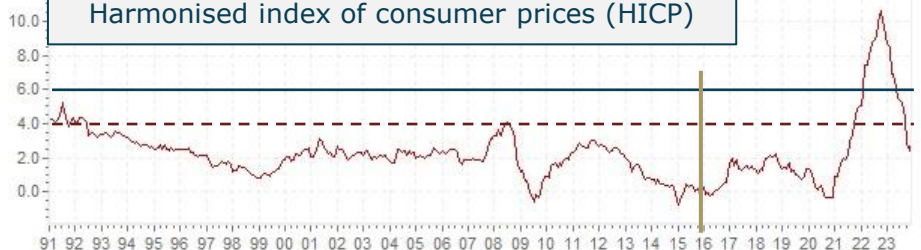
2018: New methodology to determine expected real rate introduced.

UFR still calculated as expected inflation plus expected real rate.

Expected inflation rate: ECB's target rate 2% unchanged

Year	UFR
2015	4.20%
2016	4.20%
2017	4.20%
2018	4.05%
2019	3.90%
2020	3.75%
2021	3.60%
2022	3.45%
2023	3.45%
2024	3.30%
2025	3.30%

Harmonised index of consumer prices (HICP)



Sharp increase of inflation in Europe

Historic harmonised inflation Europe – HICP inflation

<https://www.inflation.eu/en/inflation-rates/europe/historic-inflation/hicp-inflation-europe.aspx>

Extrapolation: phasing-in mechanism

Source Article 77a(2)

Goal: Mitigation of effects resulting from the new methodology

The phasing-in mechanism shall consist of the following:

- On application date: choose the convergence speed of the forward rates towards the UFR such that the RFR is **sufficiently similar** to the RFR determined with current extrapolation method.
- Until 1 January 2032: Linear decrease of chosen parameters at the beginning of each calendar year. Final parameters of the extrapolation are applied as of 1 January 2032.

Sustainability risk in risk management

To consider: the latest reports and measures prescribed by the European Scientific Advisory Board on Climate Change, in particular in relation to the achievement of the climate targets of the Union.

Consistency with disclosed plans on sustainability matters in accordance with CSRD.

In particular: Consistency of actions regarding the business model and strategy across both plans.

EIOPA shall develop draft **RTS** to further specify:

- (a) minimum standards and reference methodologies for identification, measurement, management and monitoring of sustainability risks;
- (b) Content of the requested plans

To consider: possible conflicts with requirements for sustainability reporting for undertakings concerned

- CSRD - Corporate sustainability reporting Directive (EU) 2022/2464, Article 19a (amended the Accountancy Directive (2013/34/EU))
- SFDR: Sustainable Finance Disclosure Regulation ((EU) 2019/2088)

Additional macro-prudential tools

Source Article 144d

Application of additional macro-prudential tools

EIOPA shall develop draft **RTS** to ensure consistent application of macroprudential tools on criteria to be considered when defining undertakings and groups

- requested to:
 - (i) carry out the additional macroprudential analyses in the ORSA
 - (ii) incorporate macroprudential considerations as part of the prudent person principle
- requested to draw up and maintain a medium and long term LRMP

EIOPA shall develop draft **RTS** specifying the content and frequency of update of LRMPs.

Due date: 12 months after entry into force

Criteria proportionate to nature, scale, complexity of the risks.

Liquidity risk management

Source Article 144b:

Supervisory powers to remedy liquidity vulnerabilities in **exceptional circumstances**

Supervisors shall monitor the liquidity position of undertakings and

- Inform if material liquidity risk is identified
- Undertaking shall explain how it intends to address this risk

In case of risks or deficiencies: power to require reinforcement of liquidity position

List of measures in case of imminent threat to policyholder protection or for financial system

EIOPA shall together with ESRB develop **guidelines** to provide further guidance.

Source Article 144c:

Supervisory measures to preserve the financial position of undertakings **during exceptional sector-wide shocks**

Supervisor can require undertakings with vulnerable risk profile to take at least the following measures:

- restrict or suspend dividend distribution or other payments to shareholders
- restrict or suspend share buy-backs and repayment or redemption of own fund items;
- restrict or suspend bonuses or other variable remuneration;

Application of the measures as long as the justifying reasons that are present.

Exceptional sector-wide shocks: EIOPA shall develop **draft RTS** to specify the existence.

Solvency II

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