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AAE Note on the Review of the Solvency II Delegated Regulation

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 and a consultation on the draft Regulation in July 2025, the European Commission published the **final Delegated Regulation on 29 October 2025**, setting out the detailed Level 2 measures that determine how the updated framework operates in practice. The AAE had responded to the July 2025 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.

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 proposed convergence-speed parameter (alpha = 11%) may still produce excessive volatility in certain market conditions.

We welcome the proposed approach to setting a threshold for the residual-volume criterion by considering a safety margin of 1.5 percentage points 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.

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. Although, we welcome the clarification that it is sufficient to perform this calculation once per year.

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.

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 Actuaires* 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. The revised framework makes some progress in simplifying the liquidity criteria and rendering them somewhat more achievable. It also seems to take into account insurers' ability to maintain equity investments over extended periods. A qualitative assessment within the ORSA would provide a more effective and proportionate means of assessing liquidity than the complex test set out in the final Regulation. The de facto exclusion of investments in equity funds because of the 500 million euros threshold, despite their broadly similar risk characteristics to direct equity holdings, may limit the practical applicability of the framework. The final Regulation also introduced a specific LTEI treatment for investments made under public legislative programmes, subject to supervisory approval and proportional capital relief, which may modestly broaden access to the regime. Any application of the 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.

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, the AAE anticipates that forthcoming sustainability reporting obligations are likely to expand disclosure requirements further, potentially exceeding the intended simplification.

The establishment of resolution authorities under the IRRD is expected to further increase the reporting burden for undertakings within its scope. At the same time, the specific roles of bodies or authorities with a macroprudential mandate have not yet been clearly defined, which may give rise to additional reporting requirements.

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.