

EIOPA Consultation Paper on proposals for Solvency II 2020 review

Package on Supervisory Reporting and Public Disclosure – Financial Stability Reporting



This is one of five briefing notes that Milliman has produced summarising the consultation papers produced by EIOPA in June 2019 in relation to the Solvency II 2020 review. EIOPA has requested stakeholders to provide feedback on these papers by 18 October 2019.

Overview

On 11 February 2019, the European Commission (**EC**) issued a formal Call for Advice¹ to the European Insurance and Occupational Pensions Authority (**EIOPA**) on the review of the Solvency II Directive. This relates to the full review of the Solvency II rules required by the end of 2020 (**2020 Review**) as required by the Solvency II Directive.

As part of the 2020 Review, EIOPA has been asked to assess the current supervisory reporting and public disclosure requirements. On 19 December 2018, EIOPA issued a Call for Input² to provide the opportunity for the industry and other stakeholders to give input on areas that could be further improved regarding Solvency II reporting and disclosure.

Taking into consideration the responses and feedback from stakeholders, on 25 June 2019 EIOPA published a Consultation Paper (the **CP**) on its proposals for the 2020 Review regarding supervisory reporting and public disclosure. EIOPA has included a summary of the feedback it received from various stakeholders in the CP.

The consultation comprises four separate papers³ looking at:

- General issues on supervisory reporting and public disclosure
- Individual Quantitative Reporting Templates (**QRTs**) for the submission of information to the supervisory authorities and supporting annexes with additional details on proposed changes;
- Solvency and Financial Condition Report (**SFCR**) and Narrative Supervisory Reporting; and
- Financial Stability Reporting

This summary focuses on EIOPA's proposals regarding Financial Stability Reporting (**FSR**). It should be read in conjunction with our summaries of the other papers listed above.

EIOPA has requested stakeholders to provide their feedback on the proposals set out in the CP by **18 October 2019**. The result of this consultation will be included in an EIOPA Opinion to be submitted to the EC by June 2020. After this date, some

of the proposals will need to be considered by the EC and will eventually be reflected in the Level 1 Directive and/or Level 2 Delegated Regulation amendments, or in Implementing Technical Standards (**ITS**) without any legislative amendment. The actual implementation date for changes to the Solvency II rules following the 2020 Review remains unclear.

Background

On a biannual basis, EIOPA carries out economic analyses of risks and vulnerabilities facing the insurance sector in order to assess their financial stability (**FS**). The reports (so called Financial Stability Reports) draw on a range of qualitative and quantitative data drawn from supervisory and market sources, which are based partially on the FSR.

The FSR refers to the quarterly and annual FS reporting for Solo undertakings, Groups & Third-Country Branches. The data from the FSR is also used as the primary source for EIOPA's Risk Dashboard and is an important component of the preliminary analysis underlying the insurance stress tests. The data is currently received from around 95 groups and 22 solo undertakings, domiciled across 16 different European countries.

The CP focuses on the following two areas, which are described in more detail in the sections below:

- Information insurers need to provide as part of the FSR.
- FSR deadlines.

The deadline for submission of information remains unchanged with two weeks after the individual deadline for reporting.

Financial Stability Reporting information

Regarding the experience gained since the implementation of Solvency II, EIOPA has identified some gaps in the scope of the information but also identified information/entry points which could be removed to reduce the reporting burden on

¹ Formal request to EIOPA for technical advice on the review of the Solvency II Directive

² Call for input on the Solvency II reporting and disclosure review 2020

³ EIOPA consultation on supervisory reporting and disclosure

insurers. The primary gaps identified in the collection of FSR data can be summarised as follows:

- Lack of supplementary statutory account-based information;
- In *S.38.01 Duration of technical provisions*, the template contains only information on Macaulay Duration which does not allow comparability with modified duration of assets reported in *S.06.02 List of assets*.
- The Macaulay duration and the modified duration assume a fixed cash-flow structure, which might be a reasonable assumption for the majority of non-life business but fails to take into account some features of traditional life business, e.g. when discretionary benefits exist. For this reason, the use of effective duration was also discussed and EIOPA asks stakeholders to give input to the feasibility of using the effective duration.
- In *S.05.01 Premiums, claims and expenses*, there is no information on net premiums earned preventing the calculation of the net combined ratio based on quarterly FSR.
- In *S.39.01 Profit and loss*, there is no high-level P&L information.

In addition to these gaps identified by EIOPA, industry representatives raised concerns regarding FSR information during the regular dialogue and as part of the Call for Input performed by EIOPA:

- Remove the solo FSR as the quarterly information is provided earlier and it does not provide any advance information or information additional to that provided by the quarterly SII submission.

Regarding the FSR content, EIOPA prefers to simplify the reporting by removing some entry points and adding new information. Indeed, it is considered that the removal of entry points should result in:

- A net benefit for the industry in terms of reporting requirements.
- Costs to supervisors and EIOPA are considered minimal and related to the need for a change in FSR taxonomy.
- The improvement in the scope of the information (i.e. new information) collected through FSR will be beneficial to supervisors and regulators by increasing the key information gathered from FSR entities, ultimately benefitting the protection of policyholders through more complete assessment of risks stemming from the insurance industry.

Based on these three criteria, EIOPA proposes the following amendments to the Guidelines:

ADD:

- New table in *S.23.02* to the FS entry points (semi-annual frequency). Proposals are in document "Individual Quantitative Reporting Templates".

- In *S.38.01.10 Duration of technical provisions*, request the "modified duration" in order to be directly comparable with the reported asset durations and make the template a quarterly template instead of annual.
- In *S.05.01.13 Premiums, claims and expenses* request net premiums earned (R0300), in order to allow the calculation of the net combined ratio quarterly.
- In *S.39 Profit and loss*, in addition to Profit and Loss figure, add the figures of technical and non-technical account result, other income and other expenses, taxes, dividends and others (semi-annually frequency).
- Request the *S.02.01* annual entry point (with statutory accounts value) in a semi-annual frequency.

REDUCE:

- In *S.38.01.10 Duration of technical provisions*, delete "Macaulay duration" cell.
- Delete *S.14 Life obligations analysis* from FS entry points.
- Delete *S.40 Profit or loss sharing* from FS entry points.

The above results in the overall deletion of Annual FS report.

Note that there are no changes to the proportionality in the requirement for FSR from undertakings. It is considered that the additional information requested does not translate into an increased reporting burden on the groups in combination with the reduction of entry points.

Financial Stability Reporting deadlines

During their regular dialogue with EIOPA, industry representatives proposed aligning FRS deadlines with regular Solvency II reporting deadlines, as these reports are more or less similar.

This proposal has been disregarded by EIOPA as it is considered that the potential costs for supervisors (including EIOPA) and policyholders related to delayed identification of risks, largely outweigh the benefit for the industry. In addition, the quarterly FSR is key to the timely production of EIOPA's Risk Dashboard every quarter. Therefore, EIOPA considers that changing quarterly deadlines to be in line with the prudential package ones would delay the Risk Dashboard production by at least two months. Compared with other Europe Supervisory Authorities, EIOPA's Risk Dashboard is already published with some delay.

Annex: duration

1. MACAULAY DURATION

Macaulay duration is currently requested for liabilities. It can be defined as follows:

$$\text{Macaulay Duration} = \frac{\sum_{t=1}^n \frac{t * C}{(1 + y)^t} + \frac{n * M}{(1 + y)^t}}{\text{Current Bond Price}}$$

Where t is the time period, C is the coupon payment, y is the periodic yield, n is the number of periods, M is the maturity value and *Current Bond Price* is the present value of cash flows.

2. MODIFIED DURATION

Modified duration is currently available for the asset side. It can be defined as follows:

$$\text{Modified Duration} = \frac{\text{Macaulay Duration}}{\left(1 + \frac{YTM}{n}\right)}$$

Where YTM is yield to maturity and n is number of coupons per year.

Milliman is among the world's largest providers of actuarial and related products and services. The firm has consulting practices in life insurance and financial services, property & casualty insurance, healthcare, and employee benefits. Founded in 1947, Milliman is an independent firm with offices in major cities around the globe.

Milliman maintains a strong and growing presence in Europe with 250 professional consultants serving clients from offices in Amsterdam, Brussels, Bucharest, Dublin, Dusseldorf, Isle of Man, London, Luxembourg, Madrid, Milan, Paris, Warsaw, and Zurich.

milliman.com

3. EFFECTIVE DURATION

Effective duration is conceptually able to take into account the variability of cash-flows under changing economic environments. This concept is based on a full revaluation of the balance sheet positions in scope and therefore considers both aspects:

1. change in discount rates
2. change of cash flows.

More concretely, the effective duration for Technical Provisions would be calculated as follows:

$$D_{TP}^{eff} = \frac{TP_{IRdown} - TP_{IRup}}{2 * \Delta y * TP_{base}}$$

Where (TP) is the market-consistent value of Technical Provisions in the respective scenario at the reference date. Accordingly, TP_{base} refers to the baseline scenario while TP_{IRup} and TP_{IRdown} to the scenarios with parallel interest rate movements up and down, respectively.

CONTACT

PARIS

Jean-Baptiste Coulomb
Jean-Baptiste.Coulomb@milliman.com

Adeline Maulet
Adeline.Maulet@milliman.com

Eliott Pradat
Eliott.Pradat@milliman.com

Badis Zeghmar
Badis.Zeghmar@milliman.com



Follow our 'Milliman France' page:
<https://www.linkedin.com/company/milliman-france>