EIOPA final report on Guidelines for supervisory reporting and public disclosure

July 2012

The publication of EIOPA's final report on Guidelines for supervisory reporting and public disclosure provides the latest iteration of reporting requirements which firms should use as part of their Solvency II implementation

INTRODUCTION

On 10 July 2012, the European Insurance and Occupational Pensions Authority (EIOPA) published a package containing its final report on the draft Guidelines for reporting and disclosure requirements for insurance undertakings and groups under Solvency II.

The package follows the formal consultations released in November and December 2011 and includes:

- EIOPA's report on public consultations 11/009 and 11/011 on the proposal for the reporting and disclosure requirements, including Guidelines for the Solvency and Financial Condition Report (SFCR) and Regular Supervisory Report (RSR);
- Revised draft reporting templates for solo and group undertakings on annual and quarterly bases;
- Draft public disclosure templates for solo and group undertakings on annual and quarterly bases; and
- Revised draft LOG and summary files[1].

To assist you in digesting the report, Milliman has prepared this summary of the content of the report and of the changes made to the reporting package together with a brief analysis of what we expect this finalised package will mean for companies in the run up to Solvency II implementation. Previous Milliman summary papers are available covering the formal consultations on reporting requirements.

[1] LOG files describe in detail how the individual templates should be completed. Summary files give high-level details about the templates.

STABILITY OF GUIDELINES

EIOPA has commented that it believes that the revised package represents a stable view of the level of granularity expected for the reporting and disclosure requirements under Solvency II. As such, EIOPA has stressed that firms should use these templates as the basis for Solvency II implementation.

Despite this, EIOPA has identified a number of further changes that may be required due to the finalisation of the Omnibus II Directive and the Level 2 implementing measures. While these are not expected to be major changes, these may include amendments to the scope of quarterly reporting requirements and to the following templates:

- Own funds;
- Specific risk modules of the Solvency Capital Requirement (SCR);
- Life Technical Provisions (TPs);
- Activity by country; and
- Templates applicable to ring-fenced funds.

Additionally, EIOPA has outlined specific areas that will be subject to further review or clarification:

- The use of templates by firms using simplified TP and SCR calculations;
- The application of the requirements to third country branches located in the EU;
- The derivative templates, following publication of the European Markets Infrastructure Regulation consultation package in July 2012; and
- The design and structure of the templates, resulting from the development of data point modelling and eXtensible Business Reporting Language (XBRL) taxonomy.

While EIOPA has commented that any further changes to the reporting templates are not likely to be major, we note that the list of templates that may be amended represents a large proportion of the templates required for companies' liability reporting.

A number of these potential changes to the templates are expected to reflect on-going discussions within the Omnibus II trialogue, in particular in relation to provisions for products with long-term guarantees, which recent reports suggest may not be finalised by the end of 2012.

Despite this, as the templates in relation to non-life technical provisions, assets (other than derivatives) and reinsurance are not included in the list of templates requiring further amendments, companies may take comfort that these can be considered to be fairly final and ensure that, for asset reporting in particular, due processes are in place to provide the required information on a timely basis.

While EIOPA has commented that it expects that the final package on reporting and disclosure will be published during the course of 2013, a number of companies have commented that if structural changes are made to the templates during the implementation phase, the industry may require up to two years to implement and test the necessary systems, rather than the 18 months set out in the draft package.

The final package is expected to incorporate a draft technical standard setting out the reporting requirements, technical annexes containing the templates and descriptions of the items, and a section on validation rules together with two sets of Guidelines covering the reporting requirements and use of XBRL respectively.

An FSA statement, posted on its website on 25 July 2012, highlights the mandatory use of XBRL by national regulators when providing quantitative regulatory data to EIOPA.

While the FSA has stated that it only intends to collect regulatory data using the XBRL standards and format, it will also "explore the further use of XBRL for reporting by firms beyond the scope of CRD IV and Solvency II".

GENERAL COMMENTS

A number of changes have been made to the reporting package in order to revise and clarify the application of materiality principles and the requirements around exemptions from quarterly reporting. However, the report highlights the significant concerns raised by firms in relation to the costs of implementing and maintaining compliance with the reporting requirements, including the initial IT-related costs of adopting the reporting templates, as well as the permanent human costs associated with on-going compliance.

While EIOPA acknowledges these costs, it believes the requirements represent an "*appropriate balance between costs for the undertakings and the needs of the supervisory authorities to ensure the protection of policyholders and the assessment of financial stability*". Furthermore, EIOPA has pointed out that a proportion of these costs is necessary to ensure the adequate calculation of figures and proper management of firms under Solvency II and should not be considered purely reporting costs.

Respondents were in favour of giving national supervisors the flexibility to exempt companies with stable risk profiles from quarterly reporting requirements. However, EIOPA has stated that it views quarterly reporting as crucial for the adequate supervision of undertakings and, as such, has not permitted exemptions from quarterly reporting in the revised package. Despite this, EIOPA has retained the allowance of exemptions from the quarterly reporting of detailed investment and derivatives data, with high-level information reported instead if certain requirements are met.

We note that the level of detail required in certain quarterly asset templates is still significantly higher than is required for the current FSA forms.

While we would agree with EIOPA's comments that this level of quarterly asset data is generally needed for internal risk management purposes, the value of disclosing information to supervisors at this level is not immediately clear.

Furthermore, we would question the ability of supervisors to adequately review this volume of detailed data on a quarterly basis such that the perceived benefits to supervisors offset the added reporting burden to companies.

Furthermore, the need to report some templates both in the fourth quarter and again weeks later as part of the annual reporting package was seen as duplicating effort and unnecessarily increasing reporting costs. As a result, EIOPA has removed the need to report certain templates both annually and quarterly – although the Q4 results for these templates must be resubmitted if material valuation changes occur before the annual reporting deadline.

STANDARD REPORTING CODES

Respondents welcomed the possible introduction of standard reporting codes for asset holdings but expressed doubts as to how the many codes will be maintained.

While many respondents have called for the introduction of standard entity codes and Complementary Identification Codes (CICs) for asset reporting purposes, EIOPA has stated that full harmonisation is not currently possible for either set of codes.

While EIOPA will develop and maintain an entity codification system for reinsurance undertakings, for other entities, codes available in the market are to be used. Significantly, harmonisation of the CICs is not envisaged in the short term as the aim of these codes is primarily to assess an undertaking's ability to identify the risks associated with its own investments.

EIOPA has commented that the short-term harmonisation of CIC codes is not a priority as the use of these to perform cross-sector and market analysis is only a secondary aim which can be achieved through adequate supervision and use of financial information from service providers.

We note that while the impact of this on firms may be limited, the potential use of a wide range of different identifiers may unnecessarily add further complexity to supervisors' responsibilities.

Furthermore, while EIOPA has indicated that harmonisation may be achieved at a later date, the systems changes that this would necessitate will represent a further burden to firms.

REPORTING THRESHOLDS

In a number of cases, respondents proposed that reporting thresholds be revised or additional thresholds introduced. Requests included:

- New materiality thresholds for reinsurance reporting;
- A new threshold for EEA branches reporting;
- The introduction of thresholds for the level at which the variation analysis should be split by line of business; and
- Revised thresholds for the split of the run-off triangle for non-life TPs by material currencies.

EIOPA did not accept any of these changes in the draft package. Furthermore, both the materiality threshold for reporting non-life RBNS[2] claims by currency and the reporting threshold for non-EEA branches have been removed. With respect to non-EEA branches, EIOPA has stated that the impact to firms is either minor, or significant enough to be crucial for supervisory purposes. As such, all EEA and non-EEA branches will now need to be reported.

In a positive move, the materiality threshold for the reporting of structured product information has been raised from 5% to 10%[3]. Additionally, firms are now only required to complete the 'securities lending and repos' template if the Solvency II value of these assets, for contracts maturing after the reporting date, is greater than 5% of total Solvency II investments or 5% of total off-balance sheet collateral.

Significantly, EIOPA has removed the proposal to include a threshold for the quarterly reporting of the Solvency II balance sheet, so all firms will now be required to produce this on a quarterly basis.

We note that while the requirement for all firms to produce quarterly balance sheets will increase the reporting requirements for many firms, the information required for this should already be produced at least quarterly, both for internal purposes and to provide own fund information in order to ensure continuing compliance with capital requirements.

[2] Reported But Not Settled.
[3] Total value of investments in structured products as a % of total Solvency II assets, excluding unit and index-linked.

TEMPLATE-SPECIFIC COMMENTS

Balance sheet

EIOPA agreed with comments that public disclosure of both the statutory accounting balance sheet and the Solvency II balance sheet may be misleading while providing no additional benefit. As such, under the revised requirements, only the Solvency II balance sheet needs to be publicly disclosed for both solo firms and groups (although the statutory accounting balance sheet information is still required for annual supervisory purposes).

We note that there is no longer a requirement to split the 'investment funds' balance sheet entry by investment type for non-public reporting. However, this requirement has been retained for public disclosure.

Where an item does not exist under local GAAP a nil value may still be used for the statutory accounts value. However, the LOG files have been adjusted to cover the situation where an item is reported differently under local accounting standards; in such cases it should be reclassified for inclusion, where possible, rather than being assigned a nil value.

Own Funds

In response to concerns around the complexity of the own funds templates, EIOPA has amended the solo and group templates to better reflect the requirements and added a specific template on participations.

The quarterly own funds requirement for groups has been retained as EIOPA deemed this reporting to be relevant at group level.

As mentioned above, these templates are likely to be subject to further changes following finalisation of the Omnibus II Directive and the Level 2 implementing measures.

Assets

EIOPA rejected proposals to remove the reporting of information that can be sourced from other financial sources, and of assets backing unit-linked products, in both cases citing the need for such information in order to assess the application of the prudent person principle. It did, however, agree with the request for groups to be able to report assets on a consolidated, group-level basis and the scope of the group templates has been amended accordingly.

The consultation raised a number of concerns relating to the availability of, and cost of providing, detailed asset information, particularly in relation to the look-through requirements for investment funds. EIOPA continues to require such information, and stated that this is "*needed by undertakings if they are to properly manage their investments under Solvency II",* whilst highlighting that the look-through is only to an asset category, geographical exposure and currency level rather than the full look-through required for the SCR calculation.

Despite this, reporting this information on a look-through basis will now only be required for solo firms and groups if the ratio of investment funds to total investments at the previous year end is more than 30% (up from a previous threshold of 20%).

We note that while EIOPA has relaxed the requirement for firms to disclose their holdings in investment funds on a look-through basis, this information will still be required for the SCR calculation. As such, the increase in the reporting threshold for this information is likely to have a minimal impact on firms.

While supervisors retain the power to exempt individual solo firms from the requirement to report detailed quarterly asset information, groups are no longer permitted to receive such exemptions and must report detailed investment and derivative information every quarter.

Furthermore, the criteria have been adjusted such that national supervisors may only grant exemptions to solo firms provided that, for a given quarter, the total investment or derivatives value[4] reported at a detailed level across all firms covers at least 90% of the total value across all European firms, and 75% of the value within an individual country, at the previous year end. These limits apply separately to the life and non-life sectors. Furthermore, the exemption criteria for quarterly derivative reporting now consider open and closed derivative positions individually (although, if exemption is not granted for one it cannot be taken for the other).

[4] Value = notional holding for derivatives and Solvency II value for all other assets.

We note that, while the criterion ensuring at least 75% coverage of detailed investment or derivative reporting at a national level was included in previous reporting packages, application of this criterion was at the discretion of the national supervisors and, if applied, would override the European-level criterion. In the updated package, the discretion has been removed and both criteria apply equally.

It is not clear how supervisors will assess the level of coverage on a national and European level or how they will decide which firms to exempt based on this information. For example, it is not clear how the criteria will be applied in the case of insurers with branches, or operating under Freedom of Services, in multiple European countries. We expect EIOPA to publish further guidance on this in due course.

This aside, it would appear that significant cooperation will be required between national supervisors and EIOPA in order to ensure that the 90% Europe-wide coverage target is achieved.

Where exemptions are granted, firms will only be required to report detailed investment or derivative information in Q4. Exempted firms must produce investment information in the other three quarters but at a summary level only. Exempted firms will not have to produce any derivatives data in the other three quarters.

Additionally, the requirement to produce quarterly as well as annual investment and derivative information has been removed. However, this has been replaced with the need to resubmit Q4 results if material valuation changes occur before the annual reporting deadline.

Technical provisions

While no changes have been made to the templates for Life TPs, the report notes that the simplifications to be used for quarterly reporting are those foreseen in legislation and which will be further developed in the Actuarial Guidelines.

With respect to non-life, while the need for reinsurance triangles has been retained, the requirement for 'salvages and subrogation' triangles has been removed.

While high level information on TPs must be reported quarterly to supervisors, this now only needs to be publicly disclosed on an annual basis. In addition, a simplified version of the future best estimate cashflow projection for non-life business must now be disclosed publicly each year.

We note that while no changes have been made to the Life TP templates at this stage, these have been identified by EIOPA as potentially requiring changes once the final requirements of Omnibus II and the Level 2 text are known. As such, any changes would be expected to reflect the final position of the requirements surrounding the matching adjustment and the potential need to report technical provisions with and without this adjustment.

The report notes that the simplifications that may be used for quarterly reporting are "those foreseen in legislation". The draft Level 2 implementing measures, as at October 2011, set out a number of simplifications that may be employed by firms in the calculation of technical provisions for areas including:

- *recoverables from reinsurance contracts and special purpose vehicles;*
- *the risk margin;*
- *the best estimate for insurance obligations with premium adjustment mechanism; and*
- *the counterparty default adjustment.*

Variation analysis

A number of changes have been made to the Variation Analysis templates addressing many of the stakeholder comments including:

- Revising the templates to provide a better link to other templates;
- Confirming that both accident and underwriting basis are allowed (in line with the TP templates);
- Removing the requirement for a detailed breakdown of reinsurance recoverables;
- Changing the order of calculation for the roll-forward of the best estimate; and
- Requiring the information on technical flows to be on an accrual, rather than cashflow, basis.

Despite requests to remove the requirement to provide the analysis by line of business for non-life business, EIOPA commented that it considers this split to be crucial given the very different types of business present and has retained this requirement.

SCR/MCR

A number of comments were received in relation to the SCR and MCR reporting templates. In particular, these queried the level of detail required for the catastrophe risk sub-module and the applicability of these templates to internal model firms who are still required to report an estimate of the SCR under the standard formula as per Article 112(7) of the Solvency II Directive.

While EIOPA commented that the level of detail required for catastrophe risk was needed so that supervisors can understand the risk exposure and challenge undertakings as appropriate, it clarified that, for internal model firms, only template SCR-B2A should be used for reporting the estimate of the SCR.

In relation to the group templates, doubts were expressed on how they should be completed when a combination of methods is used. EIOPA has clarified that groups are only required to complete the SCR templates if they use consolidation, or combination, methods to determine group SCR (as opposed to deduction and aggregation methods).

In addition, EIOPA made the following points in relation to the MCR and SCR templates:

- The counterparty default risk SCR template has been adapted to better reflect the SCR calculation rationale;
- The templates will only be partially applicable to most undertakings as undertakings will usually not be exposed to all types of risk;
- The applicability of the SCR templates to RFFs has been kept; and
- Reporting requirements for undertakings that use simplifications will need to be addressed after the Omnibus II Directive and implementing measures are known.

EIOPA has commented that a tool may be considered in the future to help undertakings calculate the SCR but will not be used for reporting purposes.

Reinsurance

No material changes have been made to the content of the reinsurance templates, although the two templates have been split into four for increased clarity.

EIOPA continues to require firms to provide information on reinsurers' credit ratings, stating that this level of detail is required by the supervisory authority, and that this information should already form a part of firms' proper risk management under Solvency II.

While the reporting frequency of the facultative reinsurance templates remains annual, these must now be resubmitted by the end of the year if there is any change in the top 10 most important risks in terms of reinsured exposure compared to those disclosed in the initial templates. The outgoing reinsurance templates must now be resubmitted at the half year, rather than quarterly, in respect of any new or cancelled treaties, and in the case of material changes to the reinsurance program.

Risk concentration (RC)

EIOPA maintained the view that reporting of RCs should be done quantitatively, although commented that additional qualitative information may also be reported. In response to strong concerns from the industry, EIOPA has removed the public disclosure requirement in relation to RCs.

Intra-group transactions (IGTs)

While reporting IGTs at both the sub-group and group level was deemed excessive by stakeholders, EIOPA pointed out that Article 216 of the Solvency II Directive requires that "*if a national sub-group is established it is subject to group supervision*" and, as such, reporting must be done at this level.

EIOPA confirmed that all IGTs, including those terminated during the period, should be reported, although accepted that these should be reported in the currency of the group, rather than the currency of the transaction.

Ring-fenced funds

The list of templates that must be completed for RFFs has not been altered. However, the LOGs for the SCR templates now state that they are to be completed for 'material' RFFs only.

While the definition of material RFFs has not been clarified, we note that EIOPA has flagged these templates for potential further changes following the finalisation of Omnibus II and the Level 2 text.

Furthermore, the field "Application to ring-fenced funds" has been added to certain LOG files but not to others. We would look to EIOPA to correct this apparent inconsistency and provide more clarity on the materiality criteria in the final versions of the LOG files.

FINANCIAL STABILITY INFORMATION

A separate public consultation on the financial stability reporting requirements was carried out in December 2011. Respondents' key concerns were:

- The threshold for firms required to report financial stability information being too low and liable to include insurers with no relevance to financial stability;
- The introduction of shorter reporting deadlines for groups; and
- The reporting of certain information on a quarterly basis for financial stability purposes when it is only required annually for standard reporting (specifically, TPs by line of business, statutory accounts and SCR information).

The threshold for companies required to report financial stability information has been raised from €6 billion to €12 billion of Solvency II balance sheet assets.

In order to ensure that sufficient market coverage is maintained under the revised threshold, EIOPA has specified that the companies reporting in a particular market should account for at least 50% of total Solvency II balance sheet assets in that country. In relation to the designation of undertakings in order to achieve 50% coverage, EIOPA has stated that:

- Undertakings should be designated in order of size (presumably of Solvency II asset holdings) ; and
- Guidelines will be established to enable local supervisors to assess how to reach the 50% threshold in a harmonised way.

Based on available data as at 31 December 2011, a threshold of €12 billion would result in roughly a quarter of UK life insurance companies (down from a third based on the €6 billion threshold) and 2% of UK non-life insurance companies having to provide reporting information for financial stability purposes.

While in the UK this equates to total market coverage of around 80%, in countries where the requirement for a 50% national coverage is not met through companies with Solvency II balance sheet assets of greater than €12 billion, the need to provide information for financial stability purposes looks likely to be amended to include companies falling under the revised threshold.

We believe further clarity is needed as to how the threshold for financial stability reporting will be applied in practice, particularly in cases where group undertakings have branches, or are operating under Freedom of Services, in multiple countries, and look forward to the publication of further guidelines on how the 50% national-level coverage will be reached in practice.

Recognising the added time needed to consolidate solo reports, the revised proposal extends the deadline by which groups must submit consolidated information to 6 weeks. Solo firms will need to provide information on financial stability items which are already provided under standard reporting requirements within 5 weeks, and within 6 weeks for all other items. A transitional arrangement is proposed to reduce the financial stability reporting deadlines from a starting deadline of 8 weeks for solo companies (9 weeks for groups) to the final deadline of 5 weeks (6 weeks for groups) 4 years after the implementation of Solvency II.

While many groups will welcome the one-week extension of the financial stability reporting deadline for consolidation purposes, this does not appear to accommodate sufficient time for the consolidation of the items not included in the standard reporting package, for which the solo and group reporting deadlines coincide.

EIOPA has removed the requirement for TPs to be reported by line of business for groups. TPs will now be reported quarterly by all firms in the Solvency II balance sheet split by life, non-life, health and index/unit-linked.

Quarterly SCR information is still required for financial reporting purposes. However, EIOPA reiterated that the SCR need only be updated for volatile elements and only on a best efforts basis. Statutory account P&L information is now required on a semi-annual, rather than quarterly, basis.

We note that the report makes frequent reference to the use of a "best efforts basis" in respect of the information provided for financial stability purposes (including for the quarterly SCR calculations, lapse rates and liability durations).

The report comments that while this should ensure the data provided is "exact enough to serve as an indicator on aggregate", the levels of internal governance and the exactness of the data do not need to be at the same level as is required for regular, supervisory reporting.

Specifically, for the SCR, EIOPA has specified that this can be achieved by only calculating the volatile components of the SCR (usually the market risk module).

The report comments that more Guidelines will be produced on the use of a best efforts basis, particularly on the use of estimations for particular items and the preliminary status of the figures.

OVERVIEW OF OTHER CHANGES MADE TO THE REPORTING PACKAGE

The package on reporting and disclosure also includes revised draft guidelines for the SFCR, RSR, reporting under predefined events and the process for reporting and disclosure.

While these guidelines are broadly consistent with those issued previously during the 2011 consultation process, under the latest draft guidelines, firms will no longer be required to report the following in the SFCR:

- Specific quantitative and qualitative information on the extent to which asset valuations are based on an economic value provided by an external independent valuation expert (previously under Guideline 8);
- An explanation of the general approach to contract boundaries used for TPs (previously under Guideline 14);
- Evidence in support of the recognition of deferred tax liabilities (previously under Guideline 19); and
- Information on high level differences in the methodologies used in the standard formula and any internal models (previously under Guideline 25).

A small level of additional information is required under the revised draft Guidelines, including:

- Details of the principal loss absorbency mechanism used to qualify own funds as high quality, including details of the trigger point and its effect (Guideline 19); and
- A new guideline for the RSR, in relation to structured products, requiring firms to provide at least a description of the risk factors when investing in such products, including any elements which may negatively affect the "evolution of value or return of the structured products" (Guideline 34).

SUMMARY

EIOPA's final report sets out the responses and comments raised during the public consultation of the proposed draft Guidelines for reporting and disclosure requirements for insurance undertakings and groups under Solvency II.

A number of changes have been made to the reporting templates to help address concerns around the reporting burden and compliance costs, while EIOPA has commented that it believes the package represents an "*appropriate balance between costs for the undertakings and the needs of the supervisory authorities to ensure the protection of policyholders and the assessment of financial stability*".

While many of these changes, including increases to thresholds and simplifications to reporting requirements, will help reduce the reporting burden on companies, the impact of some of the changes for companies may be limited, particularly as detailed information is still required elsewhere in the reporting process – either for financial stability purposes or in the calculation of other disclosed items. Furthermore, while thresholds have been raised or included for certain reporting areas, others have been removed completely. As such, the overall impact of these changes on the reporting burden is hard to assess.

The increased threshold for financial stability reporting from €6 billion to €12 billion of Solvency II balance sheet assets will reduce the reporting burden for many companies. However, in countries where the requirement for a 50% national coverage is not met through companies with Solvency II balance sheet assets of greater than €12 billion, the need to provide information for financial stability purposes looks likely to be amended to include companies falling under the revised threshold.

EIOPA has highlighted a number of areas where the reporting templates may change in response to the finalisation of Omnibus II and the Level 2 text. These potential changes are not expected to be major and, as such, EIOPA has stated that companies should use these templates for their Solvency II implementations.

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