Increasing regulatory efficiency – enhancing proportionality and streamlining reporting requirements

Many of the amendments agreed by the co-legislators will increase the operational and reporting burdens for many undertakings. This is at odds with the European Commission's commitment and efforts to streamline and reduce reporting requirements for EU business. To prevent a further increase in reporting requirements and operational burden, it is essential to draft Level 2 and Level 3 legislation appropriately, in particular in the areas of proportionality and reporting.

As the implementation of Level 2 and 3 approaches, the industry emphasises the importance of a cautious approach by the European Commission (EC) and EIOPA. This paper presents key ideas and suggestions for consideration, in line with the EC objective of rationalisation of requirements for companies.

Further enhancing proportionality

Enhancing proportionality was one of the central objectives of the Solvency II 2020 review. This was pursued by raising the thresholds for Solvency II application and allowing smaller and less risky insurers, meeting predefined criteria, to automatically access simplifications and proportional measures and as such creating a more suitable framework for these 'small and non-complex' (SNCU) insurers. Simultaneously, the continued application of the proportionality principle to all insurers, irrespective of nature, size or risk profile was maintained.

While the automatic SNCU proportionality classification, which is based on clear criteria represents an improvement, only a restricted number of insurers are likely to benefit from this designation. This is particularly evident in larger markets due to the absolute nature of the size criteria.

With the ever-increasing operational burden in mind, it is key that also non-SNCUs are able to benefit from proportionality measures based on simplified approval procedures and clear criteria and target market share.

In drafting the Level 2 and Level 3 legislation, emphasis should be placed on enhancing proportionality in the following areas:

- Transposition period
- Non-SNCUs
- Groups

Transposition period

The transposition period following the amendments to the Solvency II Directive is a critical phase, during this period, Member States are tasked with incorporating the amended Directive into their national laws. It is imperative that insurers potentially exempt from Solvency II (following increased thresholds Dir Art 4) or classified as SNCUs are not unduly burdened with new regulatory requirements. This includes not only the direct requirements of Solvency II but also any other horizontal legislation, such as the Digital Operational Resilience Act (DORA) and Corporate Sustainability Reporting Directive (CSRD). Ensuring a smooth transition period is essential for minimising disruptions to insurers' operations, otherwise there is a risk that companies will incur implementation efforts and costs that become sunk costs shortly after the transposition period.

The discrepancies in the timelines between the implementation dates of Solvency II and the CSRD/DORA provisions, could potentially lead to small undertakings to first have to adhere to the entirety of the legislation before benefiting from proportionality measures.

- **Digital Operational Resilience Act (DORA):** Some insurers currently in scope of SII application following Dir Art 4 may have to comply temporarily with DORA, specifically between its application date (17 January 2025) and the application date of the Solvency II review amendments (foreseen for end 2026/early 2027). DORA Article 2(3)(b) states it does not apply to (re)insurers as per Article 4 of Solvency II (limitation of scope based on size). This implies insurers falling under the SII review-amended version of Article 4 would have to comply with DORA for approximately a year, based on the existing version of Article 4 before becoming out of scope based on the amended Solvency II Directive.

- **Corporate Sustainability Reporting Directive (CSRD):** The Solvency II review agreement includes amendments to the CSRD. The proposed amendment in Article 19a of Directive 2013/34/EU suggests replacing paragraph 6 with new provisions that allow certain types of undertakings to limit their sustainability reporting requirements. Specifically, small and medium-sized undertakings, small and non-complex institutions, captive (re)insurers, and SNCUs meeting specific criteria may streamline their sustainability reporting. These entities opting for the derogation will be required to adhere to the sustainability reporting standards designated for small and medium-sized undertakings as specified in Article 29c. It is important to note that these SME-ESRS standards are not yet in place and preparations for their implementation could require a year or two.

DO

- For entities that would be exempted under Solvency II and SNCUs, establish smooth transition rules while avoiding sunk costs for the expected simplification during the transition period, in particular as regards the DORA and CSRD.

SNCU classification

Considering that the SNCU definition is already very narrowly defined in the Directive, when drafting the 'DA specifying the criteria and the methodology to be used when classifying SNCUs for SNCU eligibility' (Amending Dir Art 29(5)), the EC must ensure that the scope of application is as broad as possible, without imposing additional requirements.

Most criteria required to obtain SNCU-status cannot be assessed based on publicly available information such as QRTs or SFCRs. Consequently, it becomes challenging to assess or estimate the number of insurers that might qualify for this status.

The prescribed methodology should be straightforward and transparent, avoiding additional burden for companies.

DO

- Draft DA so that:
  - the scope of application for SNCUs is as broad as possible and without additional requirements.
  - the prescribed methodology is straightforward and transparent without additional burden for companies.

Non-SNCUs

While the industry welcomes the introduction of automated proportionality, based on SNCU criteria, there is a need to also address proportionality for non-SNCUs. Pursuant to the amended Dir Art 29(5)(c), the Commission is tasked with adopting a 'DA specifying the conditions for granting or withdrawing supervisory approval for proportionality measures to be used by undertakings not classified as small and non-complex undertakings (non-SNCUs)'.

To ensure the effectiveness of proportionality for non-SNCUs, it is essential to establish simple and straightforward procedures for supervisory approval. **Insurers narrowly missing the SNCU criteria** (e.g. just over 100 Mio GWP regarding size criterion), **should be granted approval for identical proportionality measures as SNCUs,** including simplified reporting requirements under the new Art 19a (6) of the Accounting Directive. **Refusal of proportionality measures should only be possible in exceptional cases of serious concerns regarding the insurer's risk profile.**

EIOPA will be required to annually report (Amended Dir Art 52(2)) on the utilisation of proportionality measures by insurance companies/groups in each Member State. To ensure comprehensive and consistent application of proportionality measures across Europe**, it is proposed to establish a national target market share of at least 20% for granting proportionality measures to non-SNCUs in each Member State.** This proposal aligns with the current rules on exemption from quarterly reporting (Dir Art 35(7)).

DO
✓ Simplify approval procedures for non-SNCUs to access proportionality measures with clear criteria and target market share of at least 20%.

Groups

Many proportionality measures for SNCUs in groups that do not meet the overall definition of a Small and non-Complex Group (SNCG) lead to practical challenges, particularly regarding reporting and planning requirements at group level. While exempt from these requirements at entity level, SNCUs must still comply indirectly with all group-level requirements. These challenges apply to the following proportionality measures for SNCU:

- Five yearly RSR: a five-year interval for the provision of the Regular Supervisory Report (RSR) is not very useful if the group has to submit an RSR for the entire group annually.
- Exemption from external audit requirements (Art. 51a para 1): an exemption from external auditing of the Solvency II balance sheet disclosed as part of the SFCR offers no real added value if the auditor has to audit a consolidated version at group level.
- The exemption from QRT and the item-by-item reporting (Art. 35a para 2),
- The frequency and simplification in the Own Risk and Solvency Assessment (Art. 45 para 1b, 5; Art. 45a para 5),
- The SFCR frequency (Art. 51 para 6),
- Liquidity risk management plan (Art. 144a para 4)
- Sustainability reporting (Art. 19a para 6 of the Accounting Directive).

In order to enable an effective approach here, it should be permissible at group level to use historical data for the exempted companies (e.g. for RSR) or to exclude them from the consolidation in the reports or plans (e.g. SFCR).

DO
✓ Enable effective application of proportionality measures for SNCUs within groups.

Reporting and disclosure

Since the implementation of Solvency II in 2016, insurers have invested significantly to meet its reporting requirements, with standard reporting already being highly comprehensive. NSAs have extensive powers and tools to request additional necessary data and information from insurer. Moreover, insurers have recently implemented the significant changes following the extensive amendments to the ITS on reporting and disclosure (Taxonomy 2.8.0).

Given this context and the European Commission's ambition to reduce the reporting burdens by 25%, **it is vital to ensure that any increase in the burden of Pillar 3 reporting is minimised.** Specifically, the **following areas require attention when drafting Level 2 and 3 legislation:**

- Standard formula reporting for internal model users
- External audit requirement
- Design of the SFCR
- Appropriate implementation of the RSR
- Development and revision of the ITS on reporting and disclosure
- Addressing inconsistencies in timelines

Standard Formula reporting for internal model users

The agreed SII amendments foresee that internal model users shall provide every two years an estimate of the Solvency Capital Requirement determined in accordance with the standard formula.

The proposals give misplaced recognition and credibility to standard formula results for internal model users. A standard formula comparison for internal model users is an arbitrary tool for such ongoing monitoring because as a capital measure for the average risk profile, it will not appropriately capture changes in atypical risk profiles and give a misleading measure of the change.

DO
Ensure that the standard formula estimate is required in a manner that addresses the individual needs of the respective NCAs. Therefore, the format and content should be agreed directly between them, independently from the RSR and Solvency II QRTs processes.

External audit requirement

The SII amendments include a minimum external audit requirement of the balance sheet disclosed as part of the SFCR. These external audit requirements will be very resource-intensive and entail significant costs for insurance companies. The data to be audited is already subject to a significant safeguard mechanism through the supervisory process of regulatory authorities (see, inter alia, Article 36 of the Solvency II Directive).

Although the industry appreciates the exemption for SNCUs, there are concerns about having national discretion. These concerns encompass both the content and scope of the extension. In terms of content, there is apprehension about expanding the requirement beyond the balance sheet, which could affect not only SNCUs but also non-SNCUs. Additionally, expanding the scope to include SNCUs may exacerbate the already significant resource burdens and costs faced by these smaller entities.

In addition, when auditing the balance sheet, the auditor should consider the SCR as a given input. Any detailed examination of the SCR falls under the responsibility of the NSA.

DO	DON'T
Accept a limited level of assurance in the audit.	Extend audit requirements to Small and non-complex Undertakings (SNCUs) or other sections of the SFCR.

Design of the SFCR

By reviewing the format and content of the SFCR it was aimed to enhance transparency by aligning insurers' disclosures with the needs of policyholders/beneficiaries and professionals. However, the current amendments imply that insurers must have two separate SFCRs, one for each audience. This approach might present challenges, potentially increasing operational burdens if not streamlined effectively at Level 2.

While the industry appreciates efforts to improve usability, given the low level of public interest in the SFCR, it emphasises the importance of ensuring that the content of each part of the SFCR effectively addresses the information needs of its intended audience.

Specifically, the DA should structure the **part of the SFCR for policyholders and beneficiaries** so that it is a compact report with a target length of not more than two pages, limited to information relevant for this group. Additionally, conducting consumer testing to assess the understanding of the information among the target audience could be beneficial.

For market professionals, the disclosed QRTs are the most relevant, therefore, narrative information in the SFCR part for market professionals should be kept at a minimum.

DO

- Minimise the SFCR reporting burden by streamlining requirements in the Level 2.
- Ensure that each part of the SFCR effectively addresses the information needs of the intended audience, including both the group-level SFCR and single SFCR.
  - Limit the part of the SFCR for policyholders/beneficiaries to information relevant for their interests with a target length of no more than two pages.
  - Base the content of the part of the SFCR for market professionals primarily on quantitative data without the need for an extensive narrative.

In addition, the industry welcomes the obligation to consider the principle of proportionality regarding information to submit to NSAs. Given the substantial efforts required to prepare the SFCR and the limited public interest it attracts, it is essential not to impose further restrictions on the exceptions outlined for SNCUs in the Directive. Furthermore, it is deemed appropriate to reassess the utilisation and significance of the SFCR for its intended recipients within three years of implementation. If its usage and relevance are found to be limited, it should be narrowed down to key indicators or completely abolished.

DO

- Envisaged exceptions in the amended Directive for SNCUs should apply without any further restrictions.
- Assess the SFCR's usage and relevance for recipients within three years of implementing. In case of limited usage and/or relevance, consider limiting it to key indicators or abolishing it.

Appropriate implementation of the RSR

The industry welcomes the introduction of a Single Regular Supervisory Report (RSR) for groups. According to Art. 256b(6) of the amended Directive, DA shall further specify the information which is to be reported in the Single RSR. It needs to be ensured that the Single RSR is designed in a practicable manner. Besides this it is necessary to reduce the content of the RSR, this includes the single RSR as well as group and solo RSR. In particular, overlaps to the ORSA report should be avoided.

Furthermore, while the industry welcomes the implementation of a five-year interval for the provision of the Regular Supervisory Report (RSR) for SNCUs, this change is not very useful if the Level 2 requirement for interim report on material changes according to Art. 312 (3) remains in place.

DO

- Minimise the RSR reporting burden by streamlining requirements in the Level 2.
- Reduce the RSR reporting burden by eliminating the interim report on material changes requirement in Level 2 for SNCUs.

Development and revision of the ITS on reporting and disclosure

Following the amendments to the Solvency II Directive and the Delegated Regulation there will be a revision of the implementing technical standard (ITS) on reporting and disclosure. This revision should not introduce new QRTs and it should not increase the reporting burden without clear supervisory need.

DON'T

- Introduce new QRTs without clear supervisory need. Equally, the ITS should not be expanded by other regulations, such as securities holdings statistics.

Additionally, EIOPA is tasked to develop an 'ITS on RSR reporting templates, including risk-based thresholds and other exemptions'. The ITS should also propose 'IT solutions, including for reporting templates and instructions for reporting' (Dir Art 35(10)). The industry highlights the **ITS should be used as an opportunity to address the numerous inconsistencies within the ITS and the related documents** such as the taxonomy, the templates and the template instructions.

It is equally important that **EIOPA makes use to a maximum extent of the 'joint ESAs report on potential measures to develop an integrated data collection** to reduce duplication/inconsistencies between financial frameworks and to improve data standardisation/efficient sharing/data usage' it has to prepare (Dir Art 35 (12)) to further reduce the reporting requirements and as such also the burden for insurance undertakings.

DO

- Minimise the reporting burden by:
  - Introducing simple and sufficiently high thresholds and exemptions.
  - Proposing feasible IT solutions when it comes to reporting templates, including a focus on clear reporting instructions
  - Using the mandates provided in the Directive, including the ITS on RSR reporting templates and the joint ESAs report on potential measures to develop an integrated data collection.
  - Swiftly addressing the inconsistencies between the ITS on reporting and disclosure and the templates, related instructions and taxonomy.

Addressing inconsistencies in timelines

While the extended timelines for annual reporting, introduced to accommodate the additional external audit requirement for the balance sheet, are welcomed, it is essential to **ensure harmonisation with the reporting deadlines for the ECB add-ons.** Consequently, the timeline for annual reporting for ECB add-ons needs to be increased accordingly.

DO
✓ Harmonise timelines with the reporting deadlines for the ECB add-ons.