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Response to EIOPA's consultation paper on liquidity risk management plans

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Introduction

Q1. *Do you have general comments on the consultation paper?*

Insurance Europe appreciates the opportunity to provide input on EIOPA's draft technical advice.

The industry supports the development of company specific liquidity risk management plans (LRMPs). The management of liquidity risk is already a requirement of Solvency II (Article 44 2d) and is already very well managed, as evidenced through existing liquidity reporting, EIOPA liquidity stress tests, IAIS liquidity metrics, etc.

- Insurance Europe supports the introduction of LRMPs which are proportionate to the risks and sufficiently flexible to allow the integration of existing liquidity risk management approaches across the industry. LRMPs should remain strategic documents outlining principles, governance, processes and a proportionate level of data aligned with the company's practices, demonstrating how liquidity risk is managed. Insurers and supervisors can agree on a process to inform the supervisor of the outcomes of liquidity analyses. However, a clear distinction must be maintained between the plan and its execution, by means of detailed data reporting to the supervisor. In the industry's view, there is limited value in prescribing a common approach to liquidity risk management. This could actually result in increased systemic risks, contrary to the intended outcome.

Over the past few years, there have been a number of regulatory and supervisory initiatives to assess and monitor liquidity risk, beyond the Solvency II requirements of Article 44 2d. These include financial stability reporting, EIOPA liquidity stress tests, national ad-hoc liquidity reporting and the IAIS Global Monitoring Exercise including the IAIS ancillary liquidity risk indicators. As the introduction of the LRMPs is designed to satisfy the regulatory and supervisory requirements on liquidity risk going forward, Insurance Europe would support a review of these additional requirements at the European level to avoid duplication and unnecessary burdens. This would align with the Commission's intention to reduce operational and reporting burdens by 25%.

The comments below set out Insurance Europe's high-level views. These are supported by further explanation and suggestions in the answers to the detailed questions.

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Criteria for medium- and long-term analysis in LRMP

Insurance Europe supports a fully qualitative approach to identifying the undertakings required to complete the additional medium- and long-term analysis in the LRMP. For the majority of undertakings, the short-term analysis will provide sufficient information for supervisors to monitor liquidity risks and the medium- and long-term analysis should be limited to exceptional cases with a clear supervisory rationale.

In the industry's view, the quantitative threshold of €12bn should be deleted. It is noted that these are consistent with the threshold for providing financial stability reporting but these lack empirical justification. If the threshold is retained, national supervisory authorities (NSAs) must widely apply the exclusion option in Article 1(4) to ensure proportionality and avoid unnecessary administrative burdens.

If EIOPA decides to maintain a threshold:

- Insurance Europe would support a threshold in line with the IAIS Insurance Core Principles (ICP 16.9) and ComFrame (CF 16.9d), which specify that more detailed liquidity risk management processes, including the submission of a liquidity risk management report to the supervisor, are particularly mandatory for International Active Insurance Groups (IAIGs), which are required to have more than $50bn in assets (among other criteria).
- In addition, it is crucial that NSAs will largely apply the possibility to exclude undertakings from the scope. Without exclusion, the proposed threshold could lead to disproportionate and unnecessary administrative burden and costs.

Group requirements

Insurance Europe supports Regulatory Technical Standards (RTS) requirements which align with the principle of managing liquidity risk "at the level at which it occurs", as applied in the last two EIOPA stress tests on liquidity. This avoids artificially consolidating liquidity risks at the Group level in cases where liquidity is managed at the level of legal entities or portfolios.

Each group should be given the flexibility to derive the group-level liquidity analysis tailored to their group corporate structure and business model. Artificial group monitoring metrics are to be avoided, notably where liquidity is managed predominantly on solo level.

The Directive (Art 246a) provides for an exemption whereby the existence of a group LRMP at the parent entity level shall exempt subsidiaries within the scope of group supervision from having to draw up an LRMP, provided they are covered by the group LRMP. This exemption does not appear clearly in Article 10 of the Regulatory Technical Standards (RTS).

Insurance Europe supports an application of this approach which would lead to the following situations:

- When a solo approach is adopted at group level, the reported overview will simply reflect the outcome for each entity.
- When a group approach is adopted, groups should be able to choose whether to use the exemption in Article 246a and submit a group LRMP to the group home supervisor. This group LRMP would combine the solo liquidity risk analysis of the parent undertaking and the related undertakings within the scope of group supervision into a single document. Or they could submit a solo LRMP to each solo supervisor without the need to derive a redundant group LRMP (i.e. without using the Article 246a exemption).

Approach, content and frequency

While the industry agrees with a principle based and proportionate approach, it considers that the amount of detail prescribed in this RTS is overly prescriptive, both in terms of content and frequency.

Insurance Europe opposes any reporting standardisation that goes beyond what is currently foreseen in the RTS, such as the introduction of dedicated templates. If any reporting requirements are considered by NSAs, the industry would ask for the following:

- Reporting should be avoided in the LRMP and instead should be agreed upon separately in a process between NSAs and undertakings.
- Any possible templates should be consulted and agreed upon with the industry and should not be overly prescriptive (eg option B.3, which is not EIOPA's preferred option).

For undertakings that participate in the quarterly EIOPA liquidity analyses using the standardised Excel sheet, a report based on principle-based requirements would impose an additional burden that should be avoided. EIOPA should limit itself to one procedure and not require both a standardised quarterly EIOPA liquidity template and then additionally demand a separate report based on principle-based assumptions.

Insurance Europe also opposes the introduction of the common liquidity coverage indicator and prescriptive list of cash flows. These are introduced by EIOPA as common approaches to be used by all (re)insurance undertakings. However, these are not comparable due to individual differences between undertakings.

- Instead of a prescriptive approach for these measures, they should be only noted as examples of approaches to measure liquidity.

Further considerations

- The minimum required quarterly reporting frequency for short-dated maturities (up to 3 months) and annually for longer-dated maturities (at a minimum 1 year) is excessive and will increase reporting burdens.
  - If reporting is required, the frequency should be fixed, eg specific figures could be provided annually. In principle, the LRMP should be prepared once and reviewed at reasonable time intervals and updated only where necessary.
- The definition of long-dated maturities as "at least one year" is not appropriate and it should be made explicit that 1 year is the maximum in order to prevent extension of the scope of the liquidity risk management plan.

Q2. *Do you have comments on the following sections in section 1 with background and rationale?*

The industry welcomes section 1 to aid the understanding of the consultation process. However, the industry would propose removing this section when publishing a finalised RTS.

The RTS states the €12bn assets threshold is based on the Guidelines on Financial Stability Reporting. It is unclear what the reasoning behind that limit was in the past and why this threshold for some reporting is valid for this RTS. In addition, it takes no consideration of inflation and similar elements as it is a fixed amount. Thus, over time more and more groups and undertakings will be above the threshold and thereby the application of the RTS will be even less proportionate. If there is a quantitative threshold, it should be adjusted over time, eg for inflation.

1.1. Amendments to the Solvency II Directive

1.2. Mandate for draft regulatory technical standards

1.2. Current requirements on liquidity risk management

1.4. Principle-based and proportionate approach

While the industry agrees with a principle based and proportionate approach, it is highlighted that the amount of detail prescribed in this RTS is excessive. For example, Articles (5) to (8) set out extensive breakdowns of liquidity sources and requirements in many sub-elements, both in normal and stressed conditions.

Insurance Europe supports a risk-oriented and proportional approach which is in line with the requirements of the IAIS (ICP 16.9.5 and ComFrame 16.9.b.2 and No. 1.4 of the "Application Paper on Liquidity Risk Management").

1.5. Detailed explanation of the draft RTS

In the case of financial conglomerates (involved in banking and insurance), the industry believes that banks should be excluded from considerations regarding (i) any quantitative threshold and (ii) the analysis and content of liquidity plans.

This is because banking undertakings are far more exposed to liquidity risks than insurance undertakings and they have their own regulations in that respect for liquidity. Liquidity indicators applicable to banks may not be adequate for insurance companies and vice versa.

Criteria for covering liquidity analysis over the medium and long term

Liquidity analysis over the short term and the medium and long term

Structure

Information on assumptions underlying the projections

Information on cash flow projections

The industry opposes the introduction of the prescriptive list of cash flows introduced by EIOPA as a common approach to be used by all insurance and reinsurance undertakings.

Information on buffers of liquid assets

Information on liquidity risk indicators

EIOPA compares this indicator with the commonly used liquidity metrics for banks and insurances. It is rightly highlighted that those indicators are based on standardised liquidity stresses. However, since the LRMPs outlined in this RTS would be based on individual company stresses and scenarios, the liquidity coverage indicator as defined by EIOPA would not lead to comparable results between separate undertakings. This is critical since the existence of such a standardised indicator could be misunderstood to imply such a comparability. It could also mistakenly set the focus of the liquidity risk management plan to this value which does not necessarily reflect the individual liquidity risk of the respective undertaking correctly.

The last paragraph of this section refers to Article 12, however, Article 12 contains information on the entry into force. It does not specify that undertakings are required to explain their reason not to include the liquidity coverage indicator in their liquidity risk management. Since this is instead included in Article 7 (4), the reference should be corrected.

Overall assessment of liquidity risk

Frequency of update of the liquidity risk management plan

EIOPA regularly requires a three-monthly update of the LRMP for short-term liquidity analysis and an annual update of the LRMP for the medium- to long-term liquidity analysis. The high update frequency means an excessive burden, even for larger insurance companies and insurance groups, because capacities must be created for this purpose.

In line with the EC's objective of reducing the regulatory reporting burden by 25%, it is key to ensure that any reporting standardisation does not go beyond what is currently foreseen in the RTS, such as the introduction of dedicated templates.

For companies that participate in the quarterly EIOPA liquidity analyses using the standardised Excel sheet, a report based on principle-based requirements means an additional burden that should be avoided. EIOPA should limit itself to one procedure and not carry out a standardised quarterly EIOPA liquidity template and additionally demand a separate report based on principle-based assumptions.

Content and frequency of update of the liquidity risk management plan at group level

Q3. *Do you have any other comments on the background and rationale section?*

N/A

Q4. *Do you agree that the draft technical standards achieve a proportionate implementation of the liquidity risk management plans?*

The industry believes that requiring all undertakings/groups with assets exceeding €12bn to conduct medium- and long-term liquidity analysis is not proportionate nor risk-based. As this is a fixed amount, more and more undertakings and groups will exceed the threshold over time, making it even less proportionate. If there is a quantitative threshold, it needs to be adjusted, eg for inflation.

Q5. *Do you have comments on the following recitals in section 2?*

Recital 1

Recital 2

Recital 3

As stated above, the content of this recital does not clearly justify the €12bn limit in Article 1.1.

Recital 4

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Recital 5

It is important not to create double reporting with the LRMP. If a liquidity framework and process are already in place, they should not be duplicated by putting an LRMP on top. Instead, they should be accepted as the implementation of the LRMP.

Recital 6

Recital 7

Recital 8

Recital 9

Recital 10

Recital 11

Recital 12

Recital 13

Recital 14

Additionally, the industry asks EIOPA to address possible reporting requirements through a pragmatic approach that allows undertakings and NSAs to reach suitable arrangements on the process, timing and frequency, taking into account each undertaking's liquidity framework and profile.

Recital 15

Recital 16

Q6. *Do you have comments on the following articles in section 2?*

Article 1 - Criteria for liquidity risk management plan over the medium and long term

As stated above (see comments on Q1, Q2 and Q4), the quantitative threshold of €12bn should be deleted.

As noted in answers to earlier questions, the application of Article 1 for groups is unclear. It could be interpreted that all subsidiaries in scope of group supervision are subject to medium- to long-term analysis whenever the group consolidated total assets are greater than €12bn and irrespective of the fact that the total assets of such subsidiaries could be well below €12bn. As a result, two identical insurance or reinsurance undertakings would be treated differently whether they are part of a group or not.

To address this issue, Insurance Europe suggests that the wording "and groups" is removed from the Article, with corresponding changes in Article 10 to cover group criteria (see below).

Article 2 - Time horizon of the liquidity analysis

In Article 4, EIOPA provides some requirements with respect to the starting point and the projection horizon which is confusing and unnecessarily prescriptive.

The requirement seems to indicate, that the quarters are shifted with one day, thus not 1/1 – 31/3, but 31/12 – 30/3. This results in misalignments with other information and Analysis of Change. It also involves unnecessary and easily avoidable compliance costs, as it does not align with the standard reporting of quarters, forcing insurers to implement additional reporting processes for almost the same periods.

The term "not be shorter than 1 year" in paragraph 2 should be rewritten into "up to 1 year". This would be in line with the IAIS "Application paper on Liquidity Risk Management".

Any timelines for new requirements should be aligned with existing reporting requirements.
Paragraph 3 stated, that "*where other time horizons for the liquidity analysis over the short term or the medium and long-term are appropriate with regard to the liquidity risk exposures and to the timing of the liquidity needs of the undertaking, the liquidity analysis shall also consider these time horizons.*"

While it is right that the time horizons should be flexibly aligned with the risks, this paragraph is redundant with paragraph 2 (which essentially allows for any appropriate time horizons between three months and infinity) and therefore confusing. Paragraph 3 should be removed. At the very least "also" should be removed in the last sentence of paragraph 3 as the "other time horizons" should be considered as alternative.

Furthermore, in this article it should be clarified that short term may mean '*up to*' 3 months.

Nevertheless, time horizon definitions should be left up to the insurer. It is crucial to maintain sufficient flexibility to address the diverse needs of different insurance groups. As demonstrated by the CROF's 2019 survey, different time horizons are being used, and firms have their own definitions of short-, medium- and long-term. This variation is also related to the types of business, where the time horizons noted in the CROF paper may not apply to all business lines.

For example, one insurer might define a short horizon as one week due to the short-term nature of the assets or liabilities on the balance sheet (eg when using derivatives), while another insurer might define the short-term (or the most relevant time horizon) as extending beyond three months (eg for natcat business). For insurers with multiple lines of business and entities, this could result in not having a single time horizon across the group, but rather the most relevant time horizon for each line of business or entity. The key is that liquidity risk monitoring should be sensible and lead to relevant assessments.

Article 3 - Structure, including Annex I

Article 4 - Assumptions underlying the projections

The liquidity cash flows should be aligned as much as possible with the balance sheet items, where relevant, in order to ensure consistency between the LRMP requirements and the company's internal processes. In the list, EIOPA combines and re-names some items.

The proposed subcategories for the cash flow projections are not appropriate and a risk-based approach here (eg stress of major losses, etc.) would be more appropriate.

Article 5 - Cash flow projections

Article 5 requires minimum elements to be considered in the cash flow analyses (paragraph 3 and 4 states: "at least distinguish the following items"). A risk-based approach should also be adopted here. Non-material or immaterial elements should not be taken into account.

The minimum requirements on flows to be reported are too prescriptive. In particular, the level of granularity required in paragraph 4 (g) to (j) is neither fit for an "at least" list of mandatory items nor proportionate to the low level of liquidity risk that they embed (all but coupon payments are discretionary). One reporting item for those should be sufficient; differentiation can be appropriately covered in the qualitative part of the LRMP.

Therefore, it is suggested to replace paragraph 4 (g) to (j) by a new 4(g):"distributions to basic own-fund items". This does not prevent undertakings to cover buybacks, bonuses, etc., where material from a liquidity risk standpoint.

In any case, the industry would request clarification of the following:

- Article 5(4)(c) - other technical outflows, including operating expenses:
    - Why are operational expenses included as part of other technical expenses?
- Article 5(4)(f) - financial outflows, including margin requirements:
    - EIOPA includes margin calls. The expected cash flows related to margin calls are mostly contingent on the development of the underlying economic variable (such as the interest rate).
    - How does EIOPA expect the insurer to apply this requirement? Do they have to assume a certain movement in market value?

Article 6 - Buffers of liquid assets

Article 7 - Liquidity risk indicators

The industry has concerns with the implementation of a liquidity coverage indicator, which consists of narrowly predefined components and specified calculations.

The industry asks for general freedom to adopt an approach to manage liquidity in line with the risk profile of each undertaking. As part of overall risk management, insurers may also use defined liquidity risk indicators for other requirements, eg for the pre-emptive recovery plan. For unit-linked and investment-linked business, as well as matching adjustment portfolios, insurers in scope should be free to define the significance of liquidity risk, taking into account the nature of the underlying business.

The liquidity coverage indicator introduced by EIOPA to be used by all undertakings contradicts the narrative nature of the liquidity risk management plans. It risks the reduction of the plan into a single measure to evaluate the liquidity position of insurers. Furthermore, since the stresses on cashflows and assets are determined by each undertaking individually, the resulting indicator is not comparable between separate undertakings. The introduction of this common indicator may therefore be misleading and should not be required.

Insurance undertakings have existing liquidity frameworks which reflect the dynamics of their business activities and balance sheet structure. The draft technical standards are thereby moving away from a principles-based regulation of individual liquidity frameworks towards a regulator-specific prescribed liquidity matrix, which fundamentally differs from the currently successfully used frameworks.

This could result in insurance undertakings generating two liquidity metrics:

- one metric based on their existing approach, which is tailored to and relevant for their business activities and balance sheet structure, and by which they manage their liquidity;
- and the liquidity coverage ratio, which merely serves to generate a figure for regulators that is of limited or no use for management, supervisory or even comparative purposes.

This is particularly true when it comes to group LRMP, and the liquidity is analysed on a solo basis. The current wording of Article 10(2)(a) is inappropriate as it would require the determination of a redundant group liquidity coverage ratio based on an artificial consolidation of cashflows at group level (see a drafting suggestion for Article 10).

The additional, detailed requirements of the draft, which materially intervene in the risk management of insurance undertakings, do not increase policyholder protection but lead to parallel processes and very high complexity and implementation costs.

Finally, please note that the word "disclosed" in Article 7(3) should be replaced by "reported" as in the previous sentence to avoid any confusion with public disclosure.

Article 8 - Overall assessment of liquidity risk

Article 9 - Frequency of update of the liquidity risk management plan

Overly prescriptive requirements for LRMPs should be avoided. Unlike solvency risks, it is possible for liquidity risks to be characterised by their short-term nature. Therefore, supervisory requests to cover the medium and long term in their LRMP should be limited to exceptional cases with a clear supervisory rationale.

In addition, the short-term LRMPs should only require a yearly update or if there is a significant change in the liquidity profile of the undertaking. It is not proportionate to require quarterly updates when there is no evidence of liquidity risks.

Alternatively, if numbers are required to be reported, the industry suggests that only the short-term cashflow projections should be updated, but not the scenarios, indicators, etc. Reporting to NSAs should also be necessary only once a year.

EIOPA requires a three-monthly update of the LRMP for short-term liquidity analysis and an annual update of the LRMP for the medium- to long-term liquidity analysis. With regard to the update interval, deviating frequencies should also be permitted, provided that companies can adequately explain or justify the reasons for the deviation. Insurers exempt from quarterly reporting (Article 35a (2) SII-Directive) should also be exempt from quarterly updates of the LRMPs.

Article 10 - Content and frequency of update of liquidity risk management plans at group level

The industry's comments on frequency are also applicable for groups.

Additionally, it should also be explained how different requirements can be dealt with at the group level, for example if there is a Small and Non-Complex Undertaking (SNCU) in the group that does not have to create an LRMP. Apart from the question of whether SNCUs should be included in the group LRMP, there is also the question of which subsidiaries (only home country or all Member States or Third Countries) should be included in the group LRMP.

- According to Article 246a paragraph 2, subsidiaries which are in the scope of group supervision in accordance with Article 213 paragraph 2 points a and b are exempted from drawing up and keeping up to date a liquidity risk management plan at individual level.
- The industry suggests to clarify the implication of the exemption of solo plans where a group plan exists but the liquidity is analysed and managed at solo level.
- The industry recommends that, when a solo approach is adopted, groups are able to choose whether to use the exemption in Article 246a and submit a group LRMP to the group home supervisor. This group LRMP would combine the solo liquidity risk analysis of the parent undertaking and the related

undertakings within the scope of group supervision into a single document. Or they could submit a solo LRMP to each solo supervisor without the need to derive a redundant group LRMP (ie no use of Article 246a exemption). In any event, the top-down approach of Article 246a focuses on submission (group home supervisor vs solo local supervisors) and the number of documents to derive (single group-level document or multiple solo-level documents) but it does not equate to forcing insurers to adopt artificial group liquidity metrics where the liquidity risk is managed essentially at solo level.

- In light of this, Article 10 would need to be amended as follows:
  - 1. Articles 2, 3 and 9 shall apply to the liquidity risk management plans at group level.
  - 1a. Supervisory authorities shall require participating insurance and reinsurance undertakings, insurance holding companies and mixed financial holding companies, if deemed proportionate in accordance with Article 1(2) – (3), to draw up and maintain up to date a liquidity risk management plan at group level covering liquidity analysis over the medium- and long-term.
  - 2. The liquidity risk management plan at group level shall include:
    - (a) the information defined in Articles 4 to 8 for the participating insurance and reinsurance undertaking, insurance holding company or mixed financial holding company;
    - (aa) the information defined in Articles 4 to 8 for the insurance and reinsurance subsidiaries in the scope of group supervision in accordance with Article 213(2), points (a) and (b);
    - (b) a description of the mechanism for managing liquidity and for identifying and addressing liquidity needs at the level of the group or, as appropriate, the parent undertaking and the related insurance and reinsurance undertakings in the scope of group supervision in accordance with Article 213(2), points (a) and (b), on an ongoing basis and under stressed conditions. This shall contain a description of availability and transferability, including in cases of simultaneous liquidity needs within the undertakings of the groups.

Article 11 - Risk concentration and intragroup transactions

Article 12 - Entry into force

Q7. *Do you have any other comments on the draft technical standards in section 2?*

N/A

Q8. *Do you have comments on the analysis of the following policy issues?*

Insurance Europe supports EIOPA's intention for principle- and proportionate-based standards on LRMP. However, the proposed RTS could go further in reflecting this intention.

Policy issue A

The inclusion of companies using the Matching Adjustment (MA) and Volatility Adjustment (VA) would lead to too many smaller companies having to make risk plans for medium- and long-term, which would be contrary to a risk-based approach.

The industry does not agree that keeping the plans updated does not require significant resources on an ongoing basis (under Costs: Industry). Especially for smaller insurance companies required to update the short-term LRMP every three-months and submit it to the supervisors. The high update frequency also represents an excessive burden for larger insurance companies and insurance groups, because capacities must be created for this purpose.

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Any potential reporting requirements would also increase costs for the industry.

The application criteria based solely on qualitative information, ie no threshold, has not been considered. Insurance Europe believes that this could be the best policy option in terms of effectiveness and efficiency.

Therefore, as stated above:
The short-term LRMP should only be required to be submitted to the supervisors once every year.
Reporting should be avoided in the LRMP and instead should be agreed upon separately in a process between NSAs and undertakings.

Policy issue B

The industry agrees with EIOPA that Option B2 is the best option from the options provided, however, it reiterates the previous comments about the costs for the industry.

The policy options regarding the content of plans fail to consider credible alternatives, such as more limited requirements. As EIOPA is only considering increasingly prescriptive options, starting from Option B.1 to the even more prescriptive Option B3, it is incorrect to label Option B.2 as the "minimum requirement", while at the same time stating that these requirements are currently already documented by undertakings. In fact, Option B.2 would still imply extra work for undertakings.

Q9. *Do you have any other comments on the impact assessment in Annex I?*

The policy options regarding the content of plans fail to consider credible alternatives, such as more limited requirements. EIOPA's approach of progressively prescriptive options (Options B.1 to B.3) mislabels Option B.2 as the "minimum requirement", despite acknowledging that undertakings already document these requirements.

In fact, Option B.2 would still imply extra work for undertakings. In addition, for policy issue A, only qualitative criteria, ie no threshold, should be considered as this would be the most efficient option among those proposed. As stated above, it is not correct that EIOPA concludes no costs for the customers in Option A1 and A2. Any regulation that means higher costs for the companies can mean higher costs for the customer, especially in mutual companies.

Q10. *Do you have any other comments on the consultation paper?*

N/A

Insurance Europe is the European insurance and reinsurance federation. Through its 37 member bodies — the national insurance associations — it represents all types and sizes of insurance and reinsurance undertakings. Insurance Europe, which is based in Brussels, represents undertakings that account for around 95% of total European premium income. Insurance makes a major contribution to Europe's economic growth and development. European insurers pay out over €1 000bn annually — or €2.8bn a day — in claims, directly employ more than 920 000 people and invest over €10.6trn in the economy.