

Response to EIOPA's consultation paper on scenarios for best-estimate valuations for life insurance obligations

Our reference:	ECO-SLV-24-415	Date:	24-12-2024
Referring to:	Consultation on scenarios for best-estimate valuations for life insurance obligations - Solvency II Review		
Related documents:	Consultation Paper		
Contact person:	Prudential Team	E-mail:	prudential@insuranceeurope.eu
Pages:	4	Transparency Register ID	33213703459-54

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.

- It is noted that the option to have a deterministic approach should be available for small and non-complex undertakings (SNCU's) and non-SNCU's.
- **Proportionality:** The industry continues to favour deterministic approaches over the prudent harmonized reduced set of scenarios (PHRSS). Historically, deterministic methods have been considered proportional, and the introduction of a strict stochastic requirement is viewed as overly restrictive.
- **Minimising burden:** The PHRSS adds significant burden to insurers using deterministic methods for time value of financial options and guarantees (TVFOG) valuations. This runs counter to the Solvency II review's aim of reducing operational burdens through proportionality.
- **Flexibility:** While the new prudent deterministic valuation and scenarios are welcomed as optional simplifications, insurers must retain flexibility to use deterministic models when appropriate.
 - Additionally, it is essential to ensure that subsidiaries eligible for proportionality rules, but belonging to a group that does not qualify, can still be consolidated with proportionality measures taken into account. This approach would allow proportionality to be applied effectively at the subsidiary level, even within a non-eligible group context.
- **Comments on proportionality consultation:** The industry also emphasises the comments submitted in the consultation on proportionality for non-SNCUs, which are closely linked to this topic. In particular:
 - Specify that the use of this simplified method must also be permitted if a stochastic method was previously used (in connection with the comments on condition no. 13).
 - Specify that obtaining an amount of less than 5% of the Solvency Capital Requirement (SCR) rate using this method, in order to be eligible, does not seem very relevant and that such a condition could be removed. If there is a desire to retain this condition, it might be more appropriate to relate it to technical provisions, of which TVOG is a part (in connection with the comments on condition no. 14).

Additionally, it is unclear whether undertakings using a Black-Scholes closed formula for TVFOG calculations fall within the scope for applying the PHRSS. Clear guidance on this point is requested.

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

Amendments to the Solvency II Directive

Mandate for draft Implementing Technical Standards

Information requests conducted by EIOPA

The industry believes that these scenarios for prudent deterministic valuation (PDV) should be optional. In particular, undertakings should not be forced to stop using stochastic valuation processes for the best estimate for life insurance obligations.

While the industry understands the exercise required undertakings with stochastic models in the context of the information requests, these undertakings should not be forced to alter their current approaches.

It is noted that all participants in the first information request used stochastic models, and the second information request included stochastic valuation for currencies other than the euro.

Approach to the draft ITS

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

N/A

Q4. Do you have comments on the following recitals in section 2?

Recital 1

Recital 2

Recital 3

Recital 4

Although the scenarios are derived using the basic risk-free interest rates, without application of a matching adjustment or a volatility adjustment, the industry highlights that **using the scenarios should not restrict SNCUs from using the volatility adjustment and the matching adjustment.**

Recital 5

Recital 6

Recital 7

Recital 8

Recital 9

Recital 10

Recital 11

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

N/A

Article 1 - Financial market parameters

Article 2 - Criteria for the set of scenarios

Article 3 - Base methodology

Article 4 - Adjustments to the set of scenarios

Article 5 - Selection of volatilities

Article 6 - Currencies

Article 7 - Entry into force

Q6. Do you have any other comments on the draft technical standards in section 2?

N/A

Q7. Do you have comments on the analysis of policy issue A?

The industry agrees with EIOPA's preferred Option A.1, to use pure stochastic trajectories instead of the more complex Options in A.2 and A.3.

Q8. Do you have any other comments on the impact assessment in Annex I?

N/A

Q9. Do you have comments on the potential mathematical implementation of the methodology?

N/A

Q10. Questions to stakeholders:

Question 1 in Annex II

The proposed interest rate model could be augmented with an additional drift term that would render its dynamics inherently risk-neutral. Under such an augmented model, the martingale equations (see section 3, subsection a.) would in theory be fulfilled.

However, the low number of scenarios would inevitably lead to deviations from martingality in practice. Moreover, the subsequent adjustments (see section 3) ensure that for the adjusted scenarios, the martingale equations are in any case fulfilled. Therefore, in order to keep the formulas as simple as possible, an additional drift term was omitted.

Do you agree with this approach? If not, what would be the advantages of an additional drift term in the interest rate evolution equation?

Q11. Questions to stakeholders:

N/A

Question 2 in Annex II

The interest rate volatility targeting is based on the standard deviation of the spot rate changes for a fixed maturity. This is a simplification to the method used for the information requests where swaption volatility prices were calculated.

Would you agree with this simplification?

Q12. Questions to stakeholders:

N/A

Question 3 in Annex II

In accordance with recital 7 of the draft ITS, the optimisation contains a penalty term for the weights. This penalty term ensures that the weights are not too low and thus all simulated scenarios contribute to the calculation of the best estimate.

Do you agree with the proposed design and parametrisation of this penalty term? If not, which alternative design would you propose and why?

Q13. Questions to stakeholders:

N/A

Question 4 in Annex II

Do you agree with this approach for the derivation of the volatility parameters used in the simulation step? If not, could you propose a better technique in order to enhance the convergence of the optimisation algorithm?

Q14. Do you have any other comments on the potential mathematical implementation of the methodology in Annex II?

N/A

Q15. Do you have any other comments on the consultation paper?

- As insurers who currently use a deterministic valuation of the TVFOG have little or no experience with a stochastic model, please also ensure that sufficient instructions are available on how to implement the PHRSS.

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.