insurance europe

Position Paper

Comments on EC proposal to amend Solvency II capital requirements for STS securitisations

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Contact person:	Ecofin	E-mail:	Ecofin@insuranceeurope.eu
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General comments

Insurance Europe welcomes the opportunity to provide comments on the European Commission consultation on revised Solvency II calibrations for STS securitisation investments.

The European insurance industry represents the largest European institutional investors, with more than €10tn of assets under management. Availability of a wide range of appropriate assets to invest in is key for the industry, in order to achieve good returns and portfolio diversification for the benefit of policyholders. While securitisations are already today and are likely to remain a suitable asset class for the insurance industry, recent actions by the European Commission in this area have the potential to further increase the attractiveness of this asset class.

Specifically, the industry supports the encouragement of sound securitisations to help fund the European economy and help achieve the objectives of the Capital Markets Union project. The recent Regulation identifying STS securitisations was a very positive step.

Equally important, over recent years the insurance industry has highlighted that the extremely and unnecessarily punitive Solvency II capital requirements represent a barrier to investing in this asset class. It has advocated for more risk-sensitive capital charges, able to better reflect the real risks that insurers are exposed to when investing. Against this background, the current EC proposal to amend Solvency II is very much welcome and its intended implementation and application in parallel to the STS securitisation framework is supported.

As a more general point, it is however worth noting that the proposed Solvency II capital requirements remain significantly high compared to the actual/historical credit risk of this asset class. For example, the actual cumulative default experience of AA securitisations during the financial crisis was 0.29% in aggregate over a 6-year period (2007-2013)[1]. While this may not be quite a 1-in-200 event, it is generally considered to have been one of the worst financial crises over the last centuries. At the same time, the proposed Solvency II capital

[1] Standard and Poor's data on European ABS

Insurance Europe aisbl
Rue Montoyer 51, B-1000 Brussels
Tel: +32 2 894 30 00 • Fax: +32 2 894 30 01
E-mail : info@insuranceeurope.eu
www.insuranceeurope.eu

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charge for a 5-year AA securitisation is 6%, which is 20x higher than the actual "worst case losses" experienced over the recent financial crisis period. The proposed calibrations are therefore more appropriate, but still too conservative.

Looking ahead, Insurance Europe would support further investigations of the methodology and results of Solvency II calibrations of this asset class, as part of the Solvency II 2020 review.

Further detailed comments

With respect to the EC proposal, Insurance Europe particularly welcomes:

- the proposed capital requirements for senior STS securitisations with credit assessment, which are now more closely aligned to the capital requirements for similarly rated bonds and loans. This would be equivalent to applying a look through approach in which loans in the pool receive, as a proxy, the same rating as the pool.
- recognition that non-senior STS securitisations with credit assessment should not automatically be considered as "highly risky" solely on the basis of their juniority status. In fact, insurers often have a keen interest in junior tranches, largely due to their often-longer maturity profiles.
- the reviewed capital requirements for senior and non-senior STS securitisation with no credit assessment, as there is now recognition that the absence of a rating should not automatically exaggerate the measurement of the actual risk exposure.
- recognition that risk exposure to a non-STS securitisation should reflect the actual credit risk assessment of the product and should not automatically lead to excessive capital charges.

However, Insurance Europe believes that:

- the differences in capital requirements between senior and non-senior tranches of a securitisation remain high. For example, the senior tranche of a 5-year AA STS securitisation receives a capital charge of 6%, while the junior tranche (assuming the same AA rating) receives a capital charge of 17%.
- non-STS securitisations remain significantly penalised, without this being justified by historical performance statistics
- there is inconsistency in treatment between a whole mortgage loans pool versus RMBS, the latter being heavily penalised in terms of capital
- the scope of allowing a risk factor of 0%, which is currently limited to the European Investment Fund and the European Investment Bank, should be expanded to all types of government and RGLAs guarantees, in line with the ongoing work on the Solvency II 2018 review

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