insurance europe

Position Paper

Proposals to improve EIOPA's framework on proportionality

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Introduction

The principle of proportionality is embedded into the Solvency II Directive and aims to preserve a diversified and efficient insurance market, which is directly beneficial for European consumers.

However, currently, proportionality is hardly ever applied in practice. The 2020 review of Solvency II is a key opportunity to make proportionality work and to reduce the unnecessary operational complexity and burden.

EIOPA has made some helpful proposals but they need refining and extending if proportionality is to really work in practice.

Industry proposals to make proportionality work as intended and needed

- On NSAs' role and powers:
  - Insurance Europe agrees with EIOPA that it must be made clear in the Directive that NSAs have the power to allow for a proportionate approach. However, it also needs to be clear that it is their **duty to apply proportionality**.
  - Insurance Europe disagrees with EIOPA's position that proportionality cannot lead to an exemption from a requirement. In fact, it must be made clear that an exemption from a specific requirement is allowed under proportionality.
    - **Exemptions must be allowed** when needed for proportionality reasons and where there is no material impact on customer protection.

- On the new proportionality framework:
  - **Add new proportionality measures:**
    - The fact that EIOPA proposes to add some new proportionality measures as part of a toolbox, as it was proposed by the industry, is welcome.
    - However, some of EIOPA's proposed measures need improving and additional measures are also needed. The toolbox of proportionality measures should cover all three pillars (see table below).
  - **Allow automatic application of certain proportionality measures where an entity meets one of two types of criteria:**

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1. **It is a low-risk undertaking** (LRU) — based on EIOPA's approach, which allows an LRU to apply a set of identified proportionality measures automatically (see toolbox example below). However, the following important changes relating to two of the seven criteria that EIOPA sets out to define a LRU are needed:
   - EIOPA's **cross-border business criterion should be deleted** because it is not risk-based and goes against the objectives of the CMU and an integrated market.
   - EIOPA's **size criterion should be deleted.** This is also not risk-based; a company does not have to be very small to be an LRU.

   The industry agrees with EIOPA that NSAs should be allowed to define an insurer as an LRU even if it does not meet all the criteria based on an assessment of the risk profile.
2. **It does not have material exposure to a risk or activity**
   - Specific risk-based criteria should be defined for some proportionality measure so that they can apply where a risk is immaterial (see toolbox example below).

- The industry agrees with EIOPA that **the list of predefined proportionality measures should not be considered exhaustive.** This needs to be made clear in the legal texts to ensure that:
  - Supervisory dialogue would remain for companies and activities that do not meet the criteria for automatic application but still have grounds to apply one of the proportionality measures of the toolbox, or additional proportionality measures.
  - As proposed by EIOPA, for such cases a harmonised application process should be designed with a reasonable timeframe for the NSA to object.
- It needs to be made clear that **being part of a group does not exclude an insurance entity from proportionality**, both when criteria for automatic application are met at solo level and on the basis of supervisory dialogue**.**
- **The toolbox of proportionality measures, with the pre-defined criteria for automatic application, could be included as an ITS.** This would be one way to allow flexibility while — as a binding regulation — still ensuring minimum harmonisation and clarity for insurers.

- On the annual report on proportionality to be prepared by EIOPA:
  - The report is a key part of the proportionality framework and should be used to **monitor and improve NSAs' and insurers' use of proportionality** across the three pillars.
  - The required reporting by insurers on the use of proportionality measures must be simple and easy to complete. The EIOPA proposal appears to achieve this.

Proposed improvements to EIOPA's proportionality toolbox

The industry is sharing this table as an example, and will remain available for discussions on the measures and their corresponding criteria.

Colour coding used in the table:

- ☐ Proportionality measures existing in the regulation
- ☐ New proportionality measures/criteria for automatic application proposed by EIOPA
- ☐ New proportionality measures/criteria for automatic application proposed by the industry

	Criteria to qualify for automatic application of proportionality measures. *Note: A general criteria needed to qualify for automatic application would be that the entity's solvency ratio is 100% and projected to remain so under ORSA projections*	
Proportionality measures	Low-risk undertakings	Predefined risk-based criteria for all companies (cumulative)
Pillar 1		
Simplifications for the calculation of **technical provisions** listed in articles 57 to 61 of the Delegated Acts - Quarterly calculations: allow simplified update - Allow greater aggregation of the granularity of technical cash flows: - Allow use of the same external model, for example an Economic Scenario Generator (ESG), across multiple companies by having supervisor validate it once	Allowed	No changes in the risk profile that have a material[1] impact on SCR
Simplifications allowed for the calculation of the **SCR** listed in articles 90 to 112 of the Delegated Acts	Allowed	No changes in the risk profile that have a material[1] impact on SCR
Simplified calculation of **own funds**: - Amounts recoverable from insurance: no adjustment for the expected default of the reinsurer - Deferred taxes: possibility to use IFRS approach, simplifications should be explicitly allowed	Allowed	Where amounts involved (either recoverable insurance or deferred taxes) are <5% of Own Funds
No calculations for negligible exposures: report zero for the **SCR** component		SCR component <1% total BSCR Market share of the company <10%
Conservative estimate for small but not negligible exposure in the **SCR,** including for market risk sub-modules		Each sub-module <5% of the BSCR All sub-modules concerned <10% of the BSCR Sub-module to have a stable pattern over the last 3 years Sub-module to have a consistent pattern with regard to the business model/strategy
No calculations for negligible components of the **balance sheet**: report zero in the balance sheet		BS component <1% total BS* Market share of the company <10%

[1] Based on EIOPA's definition of materiality, ie <10% aggregate impact on BSCR

Conservative estimate for small but not negligible component of the **balance sheet**		BS component <5% total BS Market share of the company <10%
Estimating the future **BEL** of non-significant portfolio (annually or quarterly) by applying the ratio between the current BEL and the mathematical provision of a portfolio with similar characteristics		Portfolio weight <5% LoB Market share of the company <10%
Pillar 2		
ORSA: - Guided ORSA[2] - Three-year frequency; synchronised with RSR - No appropriateness assessment of standard formula in the ORSA - Use of last valuation (quarter or annual, instead of full recalculation) for non-material component in the ORSA	Allowed	No changes in the risk profile that have a material[1] impact on SCR
Key functions - Combination of several key functions - Key function-holders can hold the responsibility for several entities - Risk management: re-evaluation of non-material items only every three years	Allowed	
Lower requirements for intra-group outsourced activities - no cost/risk/benefit assessment currently required prior any outsourcing - no notification to supervisors - no AMSB approval - no designation of a person within the undertaking with overall responsibility for the outsourced key function Selection/tender of service providers for services to be outsourced: - simplified examination of the service provider (Art 274.3.a of the Delegated Acts) - simplified examination of the same provisions of the safety and confidentially of information (Art 274.3.f DA) - simplified terms and conditions of the outsourcing agreement (Art 274.3.d DA) Ongoing cooperation/collaboration between involved intra-group entities for outsourced services: - simplified right to issue general guidelines and individual instructions to service provider (Art 274.4.f and 274.4.j DA) - simplified reporting and disclosure obligations of the service provider (Art 274.4.c, 274.4.h and 274.4.j DA) - simplified compliance of the service provider's risk and internal control system (Art 274.5.a DA). - simplified monitoring of the service provider by the outsourcing insurance undertaking (Art 274.1 DA) - simplified coordination of contingency plans of the service provider by the outsourcing insurance undertaking (Art 274.5.d DA)		Outsourcing occurs within a group

[2] Central Bank of Ireland offers the possibility for "low and medium low undertakings" to fill a predefined template for the ORSA

Depth and recurrence of the regular review of the **governance** system		
No deferral of the payment of variable **remuneration** for very small amounts	Allowed	Variable portion of the staff member's remuneration <€50k and 1/3 of the total remuneration
Written policies - Simplified or standardised written policies - No minimum content - Review every three years (instead of annually)	Allowed	
Administrative, management or supervisory body (**AMSB**) - Regular assessment of the adequacy of the composition, effectiveness and internal governance of the AMSB considering proportionality	Allowed	
Pillar 3		
RSR: - Sections should be updated only when significant change - Simplified scenario analysis	Allowed	SCR cover over 100% plus the 1.5 times of the maximum volatility of the past 5 years
Only set of basic QRTs to be reported	Allowed	
SFCR No consumer-focused SFCR		Captives with no direct consumer exposure
Groups: solo companies within a group accounting for a negligible proportion of the entire group to be included in the group report [via, for example, roll-over methods or even be omitted entirely]		Non-material part of the group: - ≤ 3% of total GWP) - Accumulated share of all LRU/eligible entities non-material (≤ 10 % of GWP)
Exemptions of quarterly reporting for non-significant entities part of a group	Allowed	
No obligation for the **look-through** approach	Allowed	Mandatory for NSAs to apply to other than LRU up to 20% of the market
Across all three pillars		
Use of simplified results, proxies or extrapolation methods for the accumulation at group level for non-significant entities part of a group	Allowed	Non-material part of the group: - (≤ 3% of total GWP) - Accumulated share of all LRU/eligible entities non-material (≤ 10 % of GWP)
Exclusion from the definition of Public Interest Entities under the Accounting Directives	Allowed	Further appropriate size criteria to be adjusted in the accounting Directives

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 almost €1 000bn annually — or €2.7bn a day — in claims, directly employ nearly 950 000 people and invest over €10.4trn in the economy.