

Consultation on Draft Level 2 Implementing Measures for Solvency II: Summary Feedback Statement on the Outcome of the Public Consultation

Introduction

1. In its letters of 19 July 2007 and 12 June 2009, the European Commission requested CEIOPS to provide final, fully consulted advice on the vast majority of Solvency II Level 2 implementing measures for October 2009 (a third set to be finalised by January 2010), and recommended CEIOPS to develop Level 3 guidance on certain areas with the aim of fostering supervisory convergence.
2. This note summarises the main feedback received from stakeholders on the public consultation of the first and second sets of Consultation Papers that took place between 26 March 2009 and 11 September 2009, and the major changes made to the "Draft advice for Level 2 Implementing Measures on Solvency II" as a result of these comments.
3. The full list of comments received, together with resolutions taken by CEIOPS, is available on CEIOPS' website, except where respondents specifically requested that their comments remain confidential (see CEIOPS' [Statement of Consultation Practices](#)).
4. CEIOPS provides summary resolution templates per Consultation Paper. The resolutions range from "agreed" to "partially agreed" and "not agreed", accompanied where relevant by a short explanation. Various comments are also being addressed with "noted", to point out that CEIOPS has taken up the comment, but this does not necessarily lead to a change in its advice or would require some further consideration. Revisions were made to the papers, which after approval by CEIOPS' Members have been renamed as "CEIOPS-DOC-XX-09" to indicate the papers contain final advice. The final advice is being submitted to the European Commission. The final advice has been amended to reflect the latest version of the Level 1 text, which includes a renumbering of some Article references.¹
5. CEIOPS encourages stakeholders to read the published advice, and not to rely exclusively on the feedback statement in order to get a full view of the changes made to the paper. The feedback statement only reflects on those changes that CEIOPS' considers to be key; other changes have been made

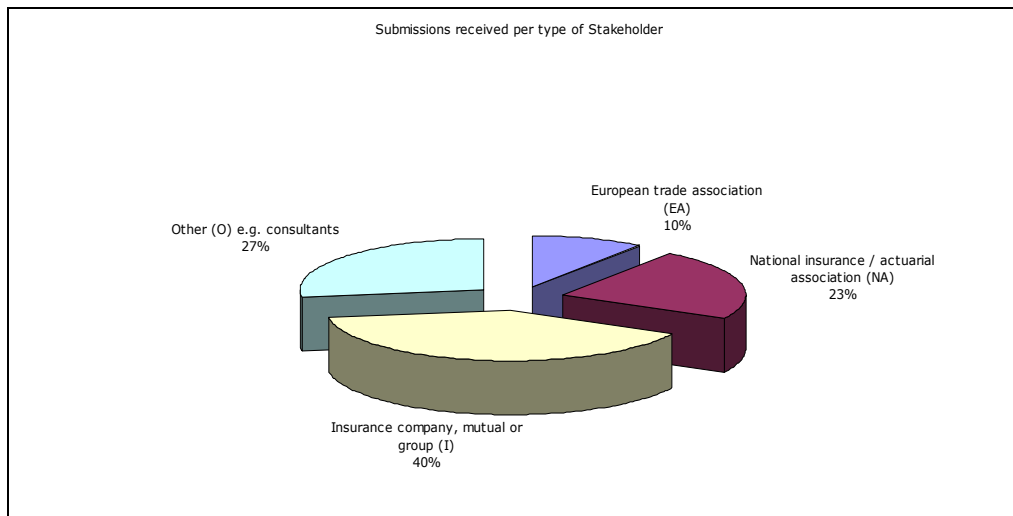
¹ Latest version from 19 October 2009 available at
<http://register.consilium.europa.eu/pdf/en/09/st03/st03643-re01.en09.pdf>

which are not reflected in this feedback statement which could have a large impact on specific stakeholders.

Facts and key figures

6. CEIOPS published a total of 37 Consultation Papers comments from 110 stakeholders. More than 3.600 comments were received during the first wave of consultation (CP 26 – 37) and close to 20.000 comments during the second wave (CP 39 – 62).
7. Consultation Paper No. 58 - Draft Level 2 advice on Supervisory Reporting and Disclosure received comments from most of the stakeholders (50% of the total number of stakeholders). Consultation Papers 39, 40, 42, 46, 47, and 53 also received a large number of comments (ranging from 40% to 48% of the total of stakeholders).
8. Most of the submissions were provided by insurance undertakings, mutuals and insurance groups (40%) and other (for example consultants, legal practitioners, academia...; 27%). 23% of the submissions were provided by national trade associations or actuarial associations while the remaining 10% of submissions were made by European trade associations (see Chart 2).

Submissions received per type of stakeholder



General remarks following consultation

9. CEIOPS thanks the stakeholders for having actively participated to the consultation. Many valuable comments were made and have helped CEIOPS to improve its advice. CEIOPS would also like to thank the stakeholders for observing the strict consultation schedule and formats.
10. CEIOPS would like to encourage stakeholders to further coordinate at European level in order to improve a common understanding and the efficiency of the consultation by avoiding submitting identical comments by members of associations or insurance groups.
11. A recurring comment from stakeholders on some proposals made by CEIOPS is the need to consider the principle of proportionality. CEIOPS is conscious that the principle of proportionality is a general principle underlying the Level 1 text and has already provided the European Commission with advice on this.² Taking this into account, wherever CEIOPS does not explicitly mention the application of the principle, the principle will apply nevertheless. CEIOPS has taken care that where its advice would be obviously disproportionate today, this has been remedied (for example on some aspects of disclosure or valuation of technical provisions). One needs to bear in mind that the principle of proportionality should not lead to measures which would not give the proper incentive for improving the risk management of (re)insurance undertakings.
12. As an example CEIOPS would like to point out one of the basic elements of Solvency II where the principle of proportionality is of particular relevance: the standard formula. As the standard formula should be applicable by small and medium sized undertakings, CEIOPS is bound not to accept particular calculations or treatments in the SCR standard formula, which would unduly make the standard approach more complex.
13. Further, during the consultation stakeholders expressed the concern that due to the large number of papers, not enough time was left for CEIOPS to consider the overall impact of its advice. CEIOPS considers this as an important comment and wants to emphasize that even though several separate pieces of advice have been drafted, the focus of CEIOPS ultimately is on the overall system of Solvency II. Therefore, CEIOPS did not only consider comments and changed Consultation Papers accordingly, as it outlines in the paragraphs below, but also gave careful consideration to the impact of all advice combined. Today, based on the analysis carried out, the assumptions made and the evidence available, CEIOPS is of the opinion that the overall advice, given in many different papers, reflects the underlying philosophy and key principles of Solvency II. However, CEIOPS realises that a full quantitative impact analysis will be required to obtain a measure of the overall impact. Therefore, CEIOPS welcomes the QIS5 exercise that will take place in 2010 and encourages stakeholders to participate.

² http://www.ceiops.eu/media/docman/public_files/publications/submissionstotheec/AdviceProportionality.pdf

Main changes made to the draft advice following the consultation

Main comments and revisions to CP 26 – Elements of actuarial and statistical methodologies for the calculation of the best estimate

14. In general, the principles-based approach set out in CP 26 was largely welcomed by respondents. In some areas respondents asked for more details, particularly on criteria, examples and concrete proposals for application of the principles. However, there were also some warnings against excessive prescription.
15. CEIOPS aims to keep the advice as principles-based as possible. However, it is necessary to give clear and accurate advice in respect of what is expected when estimating the best estimate. The best estimate calculation should not be mechanical, but a thoroughly followed process that needs to take into consideration the variability that exists in businesses and markets.
16. The most common criticism was that CP 26 appeared to be focused on life insurance, and that the advice could benefit from a distinction between techniques suitable for life insurance as compared to non-life insurance. Stakeholders underlined that in general a deterministic approach would be considered more appropriate than a stochastic approach, for non-life insurers. They further stressed that deterministic approaches are not necessarily less sophisticated than simulation techniques.
17. For the purpose of the advice, CEIOPS considers it unnecessary to split the paper into life and non-life. However, CEIOPS agrees with stakeholders that deterministic techniques are an appropriate method for estimating the best estimate as this was stated in the original CP 26. CEIOPS has amended the text to emphasise this.
18. Even where stochastic techniques are considered to be appropriate (especially for life insurance) stakeholders felt that some aspects of the advice could lead to rather demanding requirements, such as for example stochastic-in-stochastic modelling. Some felt that it might be hard to meet the “ideal” of modelling all future scenarios. One recurring comment in this regard concerned proportionality. Simpler techniques may well be more appropriate in some circumstances, although several stakeholders underlined that the use of a more or less complex simulation technique should depend on the complexity of the business rather than on the capabilities of the undertaking. CEIOPS agrees with these points and has clarified its advice accordingly.
19. Finally, the use of the word “prudent” generated several comments. Although this term is used in the Level 1 text (Article 76.4), several respondents felt that prudence is incompatible with the concept of a best estimate. Stakeholders understand that the best estimate should correspond to the mean and not to a prudent estimation. Similar comments were made on the use of “uncertainty” as this is understood to be the purpose of the risk margin and not the best estimate.

20. On this aspect, CEIOPS disagrees with the statements that the terms “prudence” or “uncertainty” are not applicable to the valuation of the best estimate. In the context of the advice, allowance for uncertainty or prudence refers to the consideration of the variability of the cash-flows necessary to ensure that the best estimate represents the mean of the cash-flows. Allowance for uncertainty or prudence does not suggest that additional margins should be included within the best estimate.
21. Further advice on the use of expert judgment is included in CEIOPS’ advice in CP 39.

Main comments and revisions to CP 27 – Segmentation for the calculation of technical provisions

22. CEIOPS’ proposed advice on segmentation was generally well received. Stakeholders broadly agreed with CEIOPS’ statement that the segmentation for technical provisions is not necessarily the same as for other components of the Solvency II framework, such as SCR, MCR or statutory reporting. The segmentation should best fit the purpose. At the same time, CEIOPS aims at minimizing divergences between segmentations and mirroring to the extent relevant the structure of the SCR. Therefore the advice proposes a high-level split among life, health and non-life insurance.
23. Regarding comments received asking for a more granular segmentation in certain types of non-life business (e.g. Maritime-Aviation-Transport or accepted reinsurance) CEIOPS would like to point out that the lines of business listed in the advice represent the minimum segmentation. Insurance and reinsurance undertakings should further segment the prescribed lines of business into more homogenous risk groups according to the risk profile of the obligations as required. In order to strengthen its proposal, CEIOPS provides a definition of the term ‘homogeneous risk group’ in its revised advice.
24. Regarding non-life segmentation, three lines of business are proposed in respect of personal risks: accident, sickness and workers’ compensation. Further adjustments have been introduced to follow comments received (for example inclusion of marine and aviation liability in MAT).
25. Regarding life segmentation, stakeholders generally considered the first level of segmentation to be appropriate. Some suggested however to change the second-level segmentation based on “risk drivers” into a “product-based” segmentation. CEIOPS considers that one of the key aims of defining segmentation is to guarantee a harmonized segmentation in practice, in such a manner that data from different undertakings and different markets may be quickly compared or aggregated. CEIOPS has decided to maintain the minimum required segmentation based on risk drivers, since it seems the best way to achieve the highest harmonization of data. Nevertheless, some considerations have been added to introduce elements of the product approach, and therefore approximate both approaches in practice.

26. The proposed measures for unbundling have been adapted to fit the three high-level categories, and CEIOPS has aimed to further elaborate on the cases for applying unbundling.

Main comments and revisions to CP 28 – SCR standard formula - Counterparty default risk

27. Following strong criticism of the QIS4 approach to counterparty default risk, CEIOPS proposed a new structure in CP 28, differentiating between two kinds of exposures. This was seen as a significant improvement by a large majority of stakeholders.
28. Recurring comments on the advice referred to the absence of treatment of internal reinsurance and the lack of diversification between the two kinds of exposures. CEIOPS has introduced a correlation between both exposures of 75 %.
29. Stakeholders further sought clarity regarding the treatment of financial reinsurance. CEIOPS confirms that this should be covered under the counterparty default module, not under the spread risk module. Further, the treatment letters of credit, segregated assets and collaterals have been further analysed.
30. In the final advice, CP 28 and CP 51 have been merged.

Main comments and revisions to CP 29 – Supervisory approval of ancillary own funds

31. The majority of respondents was opposed to CEIOPS' proposal for a 12-month approval period of ancillary own funds (AOF), based on the consideration that annual re-approval could generate too much uncertainty. Some stakeholders suggested a longer period (18 months), a one-off approval or linking the approval to the duration of AOF.
32. CEIOPS has amended its advice to partially take this view on board. The final advice will require (re) insurance undertakings to submit an annual confirmation signed by the administrative or management body that there have been no changes to the structure of the arrangement, contractual terms, status of the counterparties or any other event that could affect the recoverability of the own funds should a call be made. The annual confirmation is also required where a methodology has been approved to determine the amount if the time period granted for the approval is longer than 12 months.
33. In addition, CEIOPS has introduced the possibility that where a supervisory authority approves an amount of ancillary own funds it may make its approval subject to conditions, including considering an approval for a specified period of time.
34. Stakeholders further asked for specification of the time frame in which supervisory approval of ancillary own funds should be given. It was also

- suggested that no response from the supervisor within this timeframe should be interpreted by the undertaking as approval.
35. CEIOPS has reviewed its advice in light of these comments and has suggested that once Solvency II is fully implemented this issue should be revisited with a view to introducing an appropriate time for supervisory approval of between 3 and 6 months. CEIOPS has further clarified that in no case should silence on the part of the supervisor be interpreted as approval.

Main comments and revisions to CP 30 – TP – Treatment of future premiums

36. The feedback of the stakeholders focused on the part of the paragraph where it is stated that future premiums relating to renewal options or similar options were considered to belong to the existing contract only if they increase the best estimate.
37. The vast majority of stakeholders rejected this proposal and asked for an inclusion of all future premiums in the existing contract irrespective of the impact on the best estimate. CEIOPS has analysed the arguments of the stakeholders, but the vast majority of CEIOPS' Members still believes that the exclusion of certain future premiums is economically sound, consistent with the Level 1 text and necessary to achieve the objectives of Solvency II.
38. Guidance from the Commission also pointed out the inconsistency of this treatment with the economic approach of Solvency II. CEIOPS stands ready to lead further work on this issue on the basis of clear guidance from the European Commission. In light of such guidance, CEIOPS stands ready to do further work on the consequences for own funds and SCR..

Main comments and revisions to CP 31 – SCR standard formula – Allowance of financial risk mitigation techniques

39. For a full picture of the treatment of mitigation techniques and the scope for financial mitigation and reinsurance mitigation, the advice has to be read in connection with CEIOPS' advice in CP 52.
40. In dealing with the allowance for (financial) risk mitigation techniques, CEIOPS underlines the importance of a true risk transfer. Therefore CEIOPS advises that the standard calculation of the SCR shall not allow for those financial mitigation techniques that generate material risks, because they are not explicitly or sufficiently captured in the standard calculation of the SCR and for which CEIOPS has provided examples. Such techniques shall be allowed in the calculation of the SCR with the standard formula only if the undertaking can demonstrate that the basis risk is not material compared to the mitigation effect and, furthermore, that the allowance of the financial risk mitigation technique is in line with the 99.5% confidence level of the SCR.

41. Stakeholders asked for the recognition in the standard formula of processes, such as for example dynamic hedging strategies. CEIOPS has clarified the rationale for excluding the mitigating effect of processes which have not materialized in already existing financial contracts providing protection at the date of reference of the solvency assessment. In the SCR calculation according to the Level 1 text, shocks should be considered as “unavoidable”, so any protection that is not in place before the shock occurs is not taken into account.
42. Furthermore, the advice clarifies explicitly the treatment of the specific financial risk mitigation techniques mentioned by stakeholders. In particular, when the coverage period of the technique is shorter than the stress period or the one-year time horizon, a partial recognition is allowed, based on a simplified pro rata calculation.

Main comments and revisions to CP 32 – TP – Assumptions about future management actions

43. Stakeholders generally support the allowance of future management actions in the projection of cash-flows. Further development in the form of Level 3 guidance would be welcome in order to specify the choice of management actions. At the same time, stakeholders underlined the need to adopt a principles-based approach in the assessment of management actions. CEIOPS provided some examples in the revised advice in order to show how the requirements of objectivity, verifiability and realism can be met.
44. Some stakeholders also mentioned that allowance should be made for the application of dynamic hedging strategies. Consistent with its advice on the allowance for financial and reinsurance mitigation techniques in CP 31 and CP 52 , CEIOPS does not allow assuming in the calculation of the technical provision that management actions can be taken over the course of the scenario. For more detailed explanation on the reasons for not allowing processes to be taken into account for risk mitigation, see feedback to CP 31.
45. Finally, some stakeholders interpreted the draft advice as a requirement to take management actions into account in the calculation of technical provisions. CEIOPS clarifies in this respect that once the undertaking has decided to consider the effect of management actions in the calculation of technical provisions, the advice provides the circumstances in which it is appropriate to take them into account.

Main comments and revisions to CP 33 – System of governance

46. This paper attracted the highest number of comments from stakeholders. The sections related to the actuarial function and the risk management system were most commented upon.
47. CEIOPS aimed at taking into account the comments made, notably when these contributed to a better clarification of the contents of the document.

- Other concerns raised by stakeholders, however, could not be taken into account as some of the proposals made were considered not to be in line with the Level 1 text. Consequently, not many changes were made to the advice itself (i.e. the “blue boxes”) but more clarifications were made in the explanatory text.
48. In the section on general governance requirements CEIOPS clarified the inclusion of the “four eyes principle”, the requirement for the key functions to have an “appropriate standing” within the undertakings’ organisation and the requirement of direct access to the administrative or management body by the personnel that are responsible for the key functions.
 49. With regard to fit and proper requirements, further details for the assessment of the fitness and propriety of a person have been included. A further clarification on the general requirement for the members of the administrative or management body to collectively be able to provide for the sound and prudent management of the undertaking was also made.
 50. On the risk management system, CEIOPS elaborated further on the requirements for the ALM policies. It was also clarified that the internal quantitative limits should include off-balance sheet exposures and take into account what type of asset is considered eligible by the undertaking.
 51. For risk mitigation techniques the requirements on the reinsurance and similar risk mitigation techniques were clearly separated from the financial mitigation techniques. Requirements on SPV’s have been included with a clear link to CEIOPS’ advice on SPV’s (CP 36) and should be read in conjunction with CP 31 and 52.
 52. Stakeholders provided comments on the actuarial function and the development of European actuarial guidelines. CEIOPS decided to take a more general and open approach in its advice on European actuarial guidelines, in order to allow further discussion on this issue.
 53. On outsourcing, CEIOPS stressed that it is the responsibility of the undertaking to ensure that the terms of the outsourcing agreement are consistent with the undertaking’s obligations following the Level 1 text. Furthermore, CEIOPS underlined the need for the undertaking to prevent undue increase of operational risk.

Main comments and revisions to CP 34 – Transparency and accountability

54. Stakeholders were divided on the level of detail provided by the paper. While some stakeholders agreed with CEIOPS that the details could be left to Level 3, others considered that more details should already be given at Level 2, such as a comprehensive list of all aggregate statistical data and more information about the SRP and the criteria supervisors will employ when exercising their supervisory tasks.
55. The list of aggregate statistical data was adapted to include further information, in particular with regard to data on group supervision but also with regard to data on the supervisory authority where in some instances a distinction between the solo and group level was introduced. As the

- distribution of capital add-ons will be extensively published by CEIOPS in the future, the advice does not provide for the disclosure of data on capital add-ons at national level. CEIOPS also decided not to take up suggestions to include the number of simplifications used since this could serve to promote their use whereas simplifications should be avoided if possible. Notwithstanding the review after the consultation, the list of aggregate data will still be reassessed and completed at Level 3.
56. Some of the criteria supervisors employ when exercising their supervisory tasks will be covered by both Level 2 implementing measures and Level 3 guidance and consequently will be disclosed under "laws, regulations and administrative rules and general guidance". This applies for example to criteria to approve an internal model, to approve ancillary own funds or to set a capital add-on. The general criteria and methods used in the SRP to be disclosed will be sufficient to give an overview so that stakeholders are able to broadly understand what is relevant to supervisors in conducting the SRP.
 57. Given that most of the information to be disclosed under Article 31 is not about undertakings and that the information which will not be on individual undertakings but in aggregate form, stakeholders surprisingly focused on confidentiality issues. CEIOPS has taken these concerns into account by further clarifying that even aggregate data will not be disclosed if the information pool is too small to ensure that individual undertakings cannot be identified and if the relevant information is not yet in the public domain.
 58. Comments stressed that the disclosure requirements should not put an additional burden on undertakings. With the aggregate information on undertakings to be derived from data collected by the supervisory authority from and about undertakings in the exercise of supervision, supervisory disclosure requirements have no impact on undertaking's reporting requirements.
 59. Regarding the language of the disclosure, cost/benefit considerations have lead CEIOPS to decide against changing the advice to include other languages than English and the official national language(s) for disclosure purposes as wider interest in cross-border comparisons is expected to be limited to persons with a professional interest in insurance issues. These professionals will be adequately served by a translation in English.
 60. The proposals for the improved accessibility of historical data were included with the number of previous years for which data is to be kept on the website increased to at least four in order to allow for meaningful comparisons.
 61. The change in the Level 1 text after publication of the paper has been taken into account by explaining that reference to tools in Article 31(2)(b) relates to mandatory stress tests.

Main comments and revisions to CP 35 – Valuation of assets and "other liabilities"

62. Overall, stakeholders welcomed CEIOPS proposal to adopt IFRS as reference framework for building an economic balance sheet under

- Solvency II principles as well as the general principles recommended for Solvency II valuation purposes.
63. Nevertheless, some concerns were raised in relation to the practical application of these principles. While CEIOPS aims at keeping the advice principles-based, partly to allow for flexibility, clarification and explanation have been further added in the resolution templates and in the final advice to address these concerns (i.e. the principle of materiality, the link between Solvency II valuation principles and accounting principles used to draw statutory financial statements, adjustments to take into account further risks in the valuation, how to deal with ongoing changes in IFRS, recognition of items in the Solvency II balance sheet).
 64. Finally, on the general principles section a further principle has been added following a clarification of the Level 1 text from the European Commission, namely that the advice was prepared on the assumption 'that the undertaking will carry on its business under going concern and not under a "stressed scenario" assumption. Where necessary, the advice has been amended according to this principle.
 65. Some stakeholders did not support the requirements for an external verification in addition to the auditor's verification. CEIOPS has decided to keep this principle since it improves the reliability and accuracy of data related to specific items, such as assets for which there are no homogenous markets, and in situations where the application of different models is possible. CEIOPS highlights that it will be required only under these very limited circumstances. It has also clarified that audit requirements are outside the scope of this advice.
 66. Regarding specific items, CEIOPS did not agree with the comments from some stakeholders that goodwill should have a positive value. Consistent with an economic valuation, further arguments were added to the advice to justify and clarify CEIOPS' view on goodwill and also to limit the recognition of intangible assets to very specific circumstances.
 67. On participations, CEIOPS asked for the opinion of stakeholders on two approaches. Comments show that mixed views exist on this topic. Some stakeholders proposed that participations should be treated in a more comprehensive way, by dealing together with valuation and treatment as own funds and consideration at group level. CEIOPS explained that a more comprehensive approach will be adopted in this area in the third set of draft advice (see CP-67/09).
 68. Regarding the valuation of participations, most of the insurance industry supported the use of market value (based on the rationale that this ensures a market consistent valuation) while recognizing the potential inconsistency in the allowance for goodwill embedded in the market value of the participation and not allowing for recognition of goodwill on acquisition. Some audit firms also supported the use of the net equity method (depending on the availability of information on individual assets and liabilities). The current advice, intensively amended and based on three different views, is the result of further discussions held within CEIOPS, where Members expressed different opinions on the valuation of this item.

69. For the valuation of 'other liabilities' more than one approach was proposed in the advice. The majority of stakeholders expresses support for the use of the market rate (i.e. the risk free rate plus the own credit risk at inception) whereas some went beyond this by proposing further methods based on a so-called "combined approach". Consistent with the stakeholders' comments, the advice has been amended and it now includes only one recommended valuation principle based on the combined approach (a diverging view is also reported).
70. While recognising the high level of complexity of the valuation of deferred taxation, stakeholders generally disagreed with CEIOPS attributing by default an economic value of zero to unused tax losses and tax credits. After further reflection, CEIOPS advice has been amended to allow for the recognition of these items, based on the specific criteria set in IAS 12.
71. On post-employment benefits, CEIOPS agreed with the majority of stakeholders that IAS 19, while not necessarily a suitable proxy for an economic valuation of all post employment benefits, could be used until its foreseen revision, also considering the complex task of preparing separate valuation rules on this topic. Following the requests of some undertakings to be allowed to use their own internal model for post-employment benefits calculation, the advice has been redrafted to include the principle that undertakings shall not be prevented to use internal economic capital models, provided that they are based on Solvency II principles.

Main comments and revisions to CP 36 – Special purpose vehicles

72. Most stakeholders agreed with the approach taken by CEIOPS in developing the advice on SPV's. Stakeholders generally asked for more details or clarification, which CEIOPS has provided where it considered appropriate - considering that these transactions may take a number of different forms at the moment and in the future.
73. Stakeholders mainly objected to the level of documentation for the authorization of an SPV. Consequently CEIOPS has reviewed the list of mandatory requirements and established a smaller mandatory list, the other documents being required on a case-by-case basis as appropriate. More details on the processes to be followed for authorization have been provided.
74. The narrow scope for SPV's established in CP36 was questioned by stakeholders and CEIOPS has clarified the rationale and broadened the scope to take account of other types of SPV's, i.e. parametric or model-based triggers, as well as including some details around the level of basis risk within the transactions.
75. A number of stakeholders asked questions about the envisaged re-use of SPV's (i.e. use of an existing SPV set-up for another SPV business). CEIOPS has tried to clarify in the paper that if the proposed re-use was not planned and discussed with the supervisor at initial authorisation – which should remain an exceptional situation – or if initial authorisation was granted subject to a provision that a potential re-use would have to be approved by the supervisor, the anticipated re-use of an SPV needs prior

- approval from the supervisory authority where the SPV has been established.
76. A new section on SPV's to be used by more than one undertaking has been introduced following stakeholders questions. CEIOPS has clarified its position by pointing out that CEIOPS considers that an SPV should only be used by one group and not by a number of undertakings from different groups as SPV's can involve complex transactions and the use of SPV's should be kept transparent.
 77. Where stakeholders asked for more flexibility concerning the fully-funded principle, by removing the requirement for the contract between the undertaking and the SPV to have an aggregate limit, CEIOPS has confirmed the requirement of an aggregate limit as a crucial element for proving that the SPV is fully funded.
 78. Some stakeholders requested for the allowance of contingent funding to meet the fully-funded principle. CEIOPS would only envisage the allowance of contingent funding (e.g. future premiums or investment income) for future expenses to be incurred by the SPV (i.e. not for meeting its obligations).
 79. A new section on intra-group SPV's has been added. Finally, the principle of a bankruptcy-remote vehicle has been deleted as CEIOPS agreed with stakeholder feedback that this was for the investors to dictate in entering into the transaction.

Main comments and revisions to CP 37 - Procedure to be followed for the approval of an internal model, including the addendum on group specificities

80. The proposals included in CP 37 on the procedure to be followed for the approval of an internal model are broadly welcomed by the stakeholders. The introduction of a non-mandatory pre-application phase is especially supported.
81. One of the most important concerns is the limitation of the 6 month-period, in particular for group internal models. On this, CEIOPS emphasises the importance of a pre-application phase, considering it to be beneficial both for supervisors and undertakings, at solo and in particular at group level. In particular, the phase has following merits:
 - Allows to overcome the limitations of the 6-month period;
 - Allows supervisors to better plan their resources;
 - Undertakings engage with supervisors while developing and implementing their internal models;
 - Early identification and communication of supervisors' concerns;
 - Cost/benefits – Prevents firms from developing models which would eventually not be approved.
82. To this end, a joint task force on pre-application has been created between CEIOPS' Expert Groups, on internal models and groups. CEIOPS will issue

- draft guidance in January 2010. This has been reflected and highlighted in the revised advice.
83. Furthermore, CEIOPS received comments on the interplay and the timing of the different phases of the approval process (pre-application, application, assessment, decision and the policy for changing the model), which in stakeholders' view is not entirely clear. In particular, with regard to the policy for changing the model, the lack of a specific time frame for the approval of the model change was criticised by some stakeholders. CEIOPS considers that according to Article 115 of the Level 1 text, the approval of a major change is to be treated like a new application, for which Article 112 sets a timeline of six months.
 84. Clearer principles for the differentiation between minor and major changes were requested by stakeholders. As a result, CEIOPS has stressed in its advice that further Level 3 guidance may be developed on the categorisation of changes, including representative examples to clarify the difference between major and minor changes.
 85. In general, references to potential Level 3 guidance to further elaborate on the requirements, have been inserted in the advice.
 86. Some stakeholders were concerned that the rejection of a model by the supervisor might be publicly disclosed. CEIOPS has clarified in the paper that the rejection or any information about the rejection of an application for approval of an internal model will not be published.

Main comments and revisions to CP 39 – TP – Actuarial and statistical methodologies to calculate the best estimate

87. In general, stakeholders supported the proposals made by CEIOPS with regard to the methodologies to calculate the best estimate. Comments received often related to the need to apply the principle of proportionality (see general remarks following the consultation). CEIOPS provides simplifications for the calculation of the best estimate in its third set of advice released for consultation in November 2009.
88. Stakeholders underlined the importance of the application of expert judgment in the valuation of the best estimate. CEIOPS has further elaborated on this issue, as it agrees that the calculation of the best estimate is not a mere "mechanical" process.
89. CEIOPS clarified that the projection of cash-flows should be based on going-concern assumptions. Building on CP 26, CP 39 underlines that CEIOPS does not express a preference for a certain method for calculating options and guarantees. The relation between policyholder behaviour and the solvency position of the undertaking was clarified and a simplified method for the calculation of amounts recoverable from reinsurance contracts and SPV was inserted. With regard to the use of implied or historical volatility to calibrate asset models, CEIOPS has not decided on one method as the default approach, pointing out that the appropriate volatility assumption should be applied considering the market conditions. CEIOPS further suggests that validation of the calculation of technical provisions should be carried out once a year, and in any case where there

are indications of substantial changes, proportionate to the nature and purpose of the calculation.

Main comments and revisions to CP 40 – TP – Risk free interest rate

90. The majority of stakeholders criticised CEIOPS' choice for the AAA government bond rate as a reference rate for determining the risk-free discount rate. In its revised advice, CEIOPS underlines that the approach it has developed for defining a risk free rate uses the AAA government bond rate as a benchmark. This does not imply that government bonds with a lower rating cannot be used to derive the risk-free rates. However, depending on the materiality of the credit risk included in the rates compared to the AAA benchmark, an adjustment for credit risk needs to be made to derive the risk-free rate.

Stakeholders pointed out the possibility to include an illiquidity premium in the risk-free rate. The vast majority of CEIOPS believes that the relevant risk-free interest rate term structure should not include any illiquidity premium to discount (certain) insurance obligations. However, CEIOPS is aware that the application of the new framework derived from Solvency II may have a significant impact in some types of business and certain segments of some concrete national insurance markets. The vast majority of CEIOPS' Members considers that the solution to this situation should not be based on a disruption of the coherent framework contained in this advice.

91. CEIOPS is willing to analyse and develop, through a duly fully-consulted procedure, the points still pending and necessary to put into practice a methodology aimed to ensure objectivity and reliability for the purposes of solving this issue. To this end CEIOPS has provided its current state of analysis on this matter in annex to the advice. Further work would have to be carried out with a clear concept and mandate in light of the framework contained in the advice. CEIOPS is prepared to take the lead in this area and continue to involve all the relevant stakeholders in a transparent process.
92. On the possible methodologies for extrapolating the risk-free curve, CEIOPS concluded that there is no agreement today on which extrapolation technique would be best for all currencies in all circumstances. CEIOPS has further elaborated on the techniques, but does not prescribe a method at this stage and foresees to further work on this during the Level 3 process.

Main comments and revisions to CP 41 – TP – Calculation of TP as a whole

93. A majority of stakeholders considered CEIOPS' approach to the calculation of technical provisions as a whole to be too strict.
94. For example, stakeholders commented that the unbundling of financial and insurance cash-flows arising from a contract should be kept optional and

subject to the proportionality principle. Stakeholders asked for flexibility and more practical applications of the criteria.

95. In line with the Level 1 text, CEIOPS considers that it is essential that only where reliable replication can be obtained, technical provisions can be calculated as a whole. The calculation as a whole should not be seen as a simplification, but as a means to obtain an accurate calculation. Furthermore, additional clarifications have been added to the list of examples and criteria provided in this advice

Main comments and revisions to CP 42 – Risk margin

96. Stakeholders criticized the lack of diversification between lines of business when calculating the risk margin. CEIOPS position is directly based on the requirement set out in Article 80 of the Level 1 text. Furthermore, the criticism is based on different views from CEIOPS and stakeholders on the reference undertaking (RU). While stakeholders agreed that the RU should be another undertaking, they understand/interpret it as a mirror of the undertaking itself. Stakeholders did not propose how the overall risk margin should then be distributed among the individual lines of business in a “full diversification regime”, nor did they put forward thoughts on the impact this would have for market risk. Finally, it may be argued that a transfer to a “mirror undertaking” is more or less the same as a transfer to the undertaking itself – and this represents an interpretation of the transfer concept that according to CEIOPS’ understanding is not line with Article 76 of the Level 1 text.
97. The assumption that the SCR of the RU should comprise “unavoidable” market risk is mainly criticised for the increased complexity in the calculations while the impact on the overall Cost-of-Capital margin is likely to be small. CEIOPS has provided a simplified method for calculating the capital charge related to “unavoidable” market risk in its advice on simplifications (third set of advice, see CEIOPS-CP-76/09).
98. With regard to the calculation of the Cost-of-Capital rate, CEIOPS has duly considered the comments which pointed out that the rate should not only be based on equity funding. CEIOPS elaborates its view on the funding with equity and debt based on what is currently seen in the market place , but considers that assuming 95-100 per cent equity funding (based on QIS4 data) would not lead to different conclusions for the purpose of the calculation of the rate.
99. Simplifications for the calculation of the risk margin are being provided in the third set of advice (CEIOPS-CP-76/09).
100. CEIOPS noted the support from stakeholders for the review of the rate and provided some thoughts but did not make a proposal on this in the advice.

Main comments and revisions to CP 43 – TP – Standards for data quality

101. Stakeholders commented on the need to underline the application of the principle of proportionality in judging the quality of data along with the practical application of the appropriateness, completeness and accuracy criteria. CEIOPS in this regard indicates that the principle of proportionality applies throughout the Directive and will be judged against nature, scale and complexity of the risks. CEIOPS has elaborated on the role of proportionality for assessing the accuracy, appropriateness and completeness of data, while at the same time it is convinced that the quality of the data collection, which lies at the basis of the valuation of the undertaking's liabilities, is of primary importance.
102. Where stakeholders mention that the proposed standards would focus on internal data, CEIOPS points out that although there is generally a higher scope for the undertaking to control and analyse internal data than external data, these external data should also meet in any case a sufficient level of quality, as described in the advice.
103. Consistency with the data quality requirements under internal models is being achieved in the advice. CEIOPS underlines that the advice only contains general principles with regard to documentation.

Main comments and revisions to CP 44 – TP – Counterparty default adjustment

104. The feedback of the stakeholders was mainly positive on the overall methodology of the calculation. However, issues raised were the burden of the calculation, the estimate of the probability of default by a point-in-time approach and the threshold of the recovery rate.
105. The general comment was made at various occasions that the effort for the calculation is disproportionate, especially for small undertakings. Some stakeholders therefore proposed the use of simplifications, which would require calculating once the adjustment in detail and work with a derived percentage rate in the following calculations. The detailed approach should be applied only in the case of material effects. CEIOPS considers that the industry's proposed approach represents a slight simplification, but increases uncertainty.
106. Furthermore, for specific situations CEIOPS has provided some simplifications in the paper and additionally methods on simplifications for the adjustment analysed in CP 44 have been provided in more detail as part of the third set of consultation papers (CEIOPS-CP-76/09).
107. The size of the recovery rate was also discussed intensively. The implementation of a threshold of 40% where no reliable estimate is available, has been revised to 50 %. Furthermore, the advice foresees that if no reliable estimate of the recovery rate of a counterparty is available, no rate higher than 50% should be used. Thus, the advice does not

- exclude the possibility for higher recovery rates; they would have to be justified reasonably.
108. The majority of stakeholders prefers to use through-the-cycle assessments for the probability of default as default approach. According to comments received, point-in-time estimates might generate pro-cyclical effects and would be too burdensome, especially considering the time dependence. CEIOPS considers the risk of default to be better characterized by point-in-time estimates, hence these should be the default approach which would meet the economic and market consistent approach required by the Level 1 text to value assets and liabilities for solvency purposes. However, it is stated in the advice that if their calculation would not be in line with the proportionality principle, through-the-cycle estimates can be used.
 109. Finally, CEIOPS has identified areas for further work on Level 3, including the determination of the probability of default or the split of recoverables between lines of business for some concrete risk-transfer arrangements..

Main comments and revisions to CP 45 - simplified methods and techniques to calculate technical provisions

110. Overall, stakeholders expressed support on CEIOPS' draft advice. CEIOPS was asked to clarify the link between the role of proportionality and the concrete simplifications. In CEIOPS-CP-76/09 on simplifications for TP calculations (third set released for consultation in November), CEIOPS has included the revised and approved advice from CP 45. This should allow stakeholders to have a holistic view on the role of proportionality in the calculation of technical provisions (CEIOPS will understandably not be consulting for a second time on the advice originating from CP 45).
111. The three-step approach for assessing the application of proportionality in the calculation of technical provisions was supported by a majority of stakeholders. CEIOPS however took into account the concern expressed by some stakeholders that some elements of the approach may be too burdensome when revising its advice (e.g. the assessment of model error or backtesting).
112. CEIOPS further clarified its position on the implications of the degree of model error: where the use of a valuation technique results in a material increase in the level of uncertainty associated with the best estimate liability, the insurer should include a degree of caution in the exercise of the judgement needed in setting the assumptions and parameters underlying the best estimate valuation. However, it was clarified that this exercise of caution should not lead to a deliberate overstatement of the best estimate provision. To avoid a double-counting of risks, the valuation of the best estimate should be free of bias and should not contain any additional margin of prudence.

Main comments and revisions to CP 46 – Classification and eligibility of own funds

113. This paper attracted a lively debate with regard to three main issues: the inclusion of hybrids in Tier 1, the increase of the quality and quantity of capital, sufficient duration of Tier 1 own funds and excess over liabilities with restricted loss absorbency.
114. With regard to hybrids, CEIOPS recognises that there may be a role for high quality hybrids in Tier 1 provided that in stressed situations they convert or write down to provide higher quality capital in the form of equity. However, CEIOPS advises to restrict the inclusion of high quality hybrids in Tier 1 to 20% of Tier 1. As stated in the advice, CEIOPS continues to see an inherent trade-off between the requirements for the quality of own funds eligible to cover capital requirements and the limit structure applicable to the Tiers to which those own funds are allocated. Therefore, the limit for Tier 1 should not be lowered below 50% and the characteristics for hybrids should be such that they continue to absorb losses first or rank *pari passu*, in going concern, with capital instruments that substantially absorbs first losses.
115. Furthermore, CEIOPS has taken industry comments into account and reconsidered its view that the term "substantially" in Article 94(1) must be construed narrowly. CEIOPS appreciates that in times of stress hybrid capital instruments convert into ordinary shares or are written down upon breach of the SCR. Therefore, in effect, hybrid capital instruments may be deemed to "fully" meet the loss absorption characteristics required by the Level 1 text as they will be fully available when needed – in times of stress.
116. The majority of stakeholders was opposed to the proposed limits to the Tiers. Having regard to the comments made, CEIOPS does not consider that convincing arguments have been put forward as to why the proposed limits are inappropriate given the need for the SCR and MCR to be met with own funds of an appropriate quality and so CEIOPS proposes to retain the limits set out in its advice.
117. With regard to the Tier 1 limit for the SCR, CEIOPS recommends that the proportion of Tier 1 items in eligible own funds is at least 50% of the total amount of eligible own funds. Further, CEIOPS confirms its view that 80% Tier 1 is needed to meet the MCR.
118. CEIOPS has revised its advice following stakeholder comments with regard to the definition of the duration of Tier 1 elements. According to the revised advice, the sufficient duration of own funds instruments called for by the Level 1 text can be achieved through benchmark minimum maturities at issue date i.e. 10 years for T1, 5 years for T2, and 3 years for T3.
119. With regard to the excess over liabilities with restricted loss absorbency, CEIOPS has provided further clarification on the "profits at inception" (the wording has been adapted into "expected future profits" in accordance with the Level 1 text) which are classified as Tier 3. Further details on the "winding-up gap" have been added in annex to the paper, in line with CEIOPS' understanding that basic own funds should be tested against the criteria of Article 93, which means that they should be available to absorb losses in going concern and winding-up.

120. In line with the interpretation of the Level 1 text, CEIOPS has revised the advice to reflect that any asset recognised with a value for solvency purposes contributes to the excess of assets over liabilities. Under this approach, basic own funds shall allow for (i.e. increase with) the value of intangible assets, although this does not prejudge the classification of the corresponding own funds into Tiers, according to the criteria set out in Articles 93 and 94 of the Level 1 text. For the time being risks inherent to intangible assets were not considered in the calculation of the SCR, which might lead to an inconsistency with Level 1 regulations at this respect. Therefore to solve this CEIOPS advises (see annex to the final advice) with regard to intangible assets to develop a module for the calculation of an adequate capital charge for intangible assets.

Main comments and revisions to CP 47 – SCR standard formula – Market risk

121. Generally, stakeholders supported the proposed structure and design of the market risk module.
122. On concentration risk, many stakeholders commented on the stricter calibration compared with QIS4. This was particularly noted for higher rated (AAA-A) securities. Additionally, some stakeholders found the options provided for the thresholds for covered bonds too harsh, preferring a higher threshold than those offered. CEIOPS has revised its advice, recommending a threshold of 15% in the final advice for covered bonds and thresholds of 1,5%/3% instead of 1% and 2% for AAA-A rated securities and other/non-rated securities. CEIOPS continues to consider that a look-through approach is important for effective management of concentration risk, including for investment funds. Debt issued by multilateral development banks or specific international organizations should also be exempted from concentration risk.
123. In the currency risk sub-module, some stakeholders suggested grouping currencies and introducing a method of capturing diversification between currencies. However, CEIOPS considers this would be too complex for the standard formula.
124. Further clarifications have been made regarding the treatment of investments held in respect of contracts where the policyholder bears the investment risk. In such cases, the market risk module applies only to the extent that the undertaking bears a market risk on these contracts.

Main comments and revisions to CP 48 – SCR standard formula – Non-life underwriting risk

125. Stakeholders strongly requested the inclusion of expected future profits in the non-life underwriting risk module. However, this is not in line with the Level 1 text, which states that this module should take into account "uncertainty in the results of insurance and reinsurance undertakings related to the existing insurance and reinsurance obligations as well as to

- the new business expected to be written over the forthcoming twelve months", and would therefore by definition not cover expected profits and losses.
126. Stakeholders wondered why geographical diversification is not included. Whilst CEIOPS recognises that this would be an improvement and more risk-sensitive, it is seen as introducing unnecessary complexity at solo level in the standard formula, in view of the materiality of the reduction in capital requirement most undertakings could obtain from the calculation. CEIOPS includes an average level of geographical diversification implicitly in the calibration.
 127. Stakeholders favoured the QIS4 Method 3 for designing catastrophe scenarios (personalized scenarios), since they believe this method provides for the best way of taking accurately into account CAT risk. CEIOPS recognises that personalised scenarios are a good albeit sophisticated way of estimating the catastrophe charge, closer to a partial internal model than to a standard formula. Furthermore, this approach is not harmonised between undertakings nor between Member States. CEIOPS believes the work carried out since September by a CEIOPS Task Force with a number of stakeholders regarding standardised scenarios will provide an adequate and robust framework for this sub-module.

Main comments and revisions to CP 49 – SCR standard formula – Life underwriting risk

128. Stakeholders commented on the limited risk-sensitiveness of one-off shocks in the design of the life underwriting risk and questioned rationale for the calibration of some sub-modules.
129. For the purpose of the standard formula, CEIOPS considers that the proposed design of the risk module is balanced between the need for risk sensitiveness and the need for avoiding undue complexity.
130. However, further clarification on the design was made (e.g. on the morbidity definition and scope, lapse risk...).
131. CEIOPS also agreed with stakeholders comments on the reduction of the mortality catastrophe charge, which it implemented in its revised advice (reduction to 1,5 per mille).

Main comments and revisions to CP 50 – SCR standard formula – Health underwriting risk

132. Some stakeholders suggested a change in the definition of health insurance obligations. The definition proposed was considerably narrower than the current CEIOPS definition (with exclusion of accident insurance, disability insurance, critical illness insurance/dread disease insurance or permanent health insurance). After having examined the potential impact, CEIOPS has decided to uphold its initial definition. CEIOPS proposes a non-

- exhaustive list of examples, the aim not being to deal with every kind of guarantee sold across national markets.
133. Stakeholders asked for more clarification with regard to the criteria that should be used to determine whether the health component of a contract can be unbundled from other components. CEIOPS clarified that where obligations can be unbundled but are not material, the unbundling should not be required, in line with CEIOPS advice.
 134. Some stakeholders considered that the calibration of the health module should take into account specificities of the different public (and consequently private) health systems in the EU. Moreover, they considered that such specificities would be best captured by the allowance for specific parameters linked to the level of protection provided by the social security system in the calculation of the health underwriting risk charge. CEIOPS considers that, to be consistent with the Level 1 text, country-specific parameters as such should not be allowed, except where the risk is of a different nature. It is clarified that undertakings are allowed to use undertaking-specific parameters for health obligations (see CEIOPS-CP-75/09 on undertaking specific parameters released for consultation in November). Further advice on calibration and correlation is being included in the third set of consultation papers.
 135. Finally, CEIOPS maintained the segmentation between accident/sickness/workers' compensation. Based on suggestions made by stakeholders, clarifications on mortgage insurance and workers' compensation have been added.

Main comments and revisions to CP 51 – SCR standard formula – counterparty default risk

136. The main comments received from stakeholders on the further advice on counterparty default risk (see also CP 28), related to the calibration and to the options proposed by CEIOPS as simplifications for the calculation.
137. The calibration was considered by the stakeholders to be too high. CEIOPS partially agrees to these comments, and has amended the assumed recovery rate for reinsurance, the losses for past-due receivables, the quantile factor for type 1 exposures, and will allow an implicit rating of BBB for unrated reinsurers under equivalent supervision and for unrated banks under the Capital Requirements Directive.
138. Stakeholders were divided on which of the three options to prefer for the inclusion of simplifications for the type 1 exposures. CEIOPS has decided to use option 3. This means that the sophisticated calculation remains the default calculation for life and for derivatives, and for non-life a simpler approach becomes the default calculation method. Simplifications remain available for life, non-life and derivatives. CEIOPS believes that this option leaves the choice between accuracy and simplicity to the undertaking and adequately addresses the complexity concerns regarding non-life.
139. In the final advice, CP 28 and CP 51 have been merged.

Main comments and revisions to CP 52 – SCR standard formula – Reinsurance mitigation

140. Stakeholders expressed their concern about the exclusion of finite reinsurance under the allowance for reinsurance mitigation effects.
141. There exists a wide variety of contracts, in particular in non-life (re)insurance. It is not possible to capture them all under the standard formula SCR, especially as no-one could not expect the standard formula to accurately capture tailor-made instruments.
142. However, CEIOPS agrees that there may be contracts that are notionally separable into an insurance contract and a financial contract (or an insurance contract and a contract with both insurance and financial elements). If so, the insurance contract could be included in the standard formula SCR, at least if the other notional contract does not materially increase risk that is not covered in the SCR. The financial elements should be addressed in the SCR because the relevant components of the SCR are scenario tests.
143. Furthermore, stakeholders felt it to be disproportionate to exclude instruments with basis risk in their entirety. There may be a few contracts where one might safely ignore basis risk. However for some instruments where the trigger for recovery is different from the size of the reinsured's loss, then there is the possibility that the instrument will not respond (sufficiently), despite a significant loss for the reinsured from the event. It is also possible that the recovery is greater than expected. For such a contract there is no obvious way to deal with it in the standard SCR. Therefore it is necessary under the standard formula to restrict the level of basis risk allowed. CEIOPS advice on this is in line with the treatment of financial mitigating tools (see also CP 31).
144. There is wide-spread disappointment from stakeholders that the standard SCR does not appropriately deal with non-proportional reinsurance. CEIOPS has duly considered this concern but has not been able to address this issue in a satisfying manner in the context of the non-life standard formula. Therefore, at this stage the non-life calibration assumes that an average level of non-proportional reinsurance has been purchased.

Main comments and revisions to CP 53 – SCR standard formula – Operational risk

145. Stakeholders generally considered the proposed increase in calibration of the operational risk charge to be too high. These views have been partially taken into account by CEIOPS by deleting additional charges it had proposed relating to future management actions and the external management of financial investments.
146. Furthermore, stakeholders requested for allowing for the recognition of diversification effects between operational risk and other risk charges, as well as the consideration of qualitative aspects of operational risk management in the standard formula. With regard to the diversification

- effects, the Level 1 text does not allow for diversification between operational risk and other risks. Furthermore, CEIOPS advised not to include reductions for risk management due to high degree of subjectivity inherent to such indicators in the standard formula.
147. A number of comments were also received regarding the recognition of the mitigating effect of reinsurance contracts over operational risk. For the time being, CEIOPS considers that there is no clear link between reinsurance and operational risk, as both an increase and a decrease of operational risk when a part of the risk is ceded can easily be argued.
 148. The doubling of the cap from 30% to 60% of the BSCR was also highly criticized by stakeholders. Considering additional feedback from the European Commission on the interpretation of the Level 1 text on this point, CEIOPS has decided to revert it back to the original proposal included in the Level 1 text.

Main comments and revisions to CP 54 – SCR standard formula – loss absorbing capacity of TP

149. Some stakeholders proposed a new definition of "gross" SCR calculation for the purpose of assessing the mitigating effect of profit sharing, which CEIOPS has taken up in its revised advice.
150. CEIOPS recommends in its advice to test both the "modular approach" and the "single equivalent scenario" approach in QIS5, and not to eliminate one method before the results of QIS5.
151. Deferred tax assets are now also recognised, provided that they are available in a winding-up situation.

Main comments and revisions to CP55 – MCR calculation

152. Stakeholders commented extensively on the quarterly calculation of the MCR. They expressed concern about the complexity and potential burden of quarterly calculations, and argued in favour of more simplifications, including simplifications for insurers using SCR internal models.
153. The need for simplification has to be balanced against the need for the legal certainty when it comes to the ultimate intervention by supervisors across jurisdictions. Because of this need for legal certainty, the calculation cannot rely on simplifications when the breach of the MCR is imminent. Additionally, CEIOPS considers that, due to the potential volatility of capital requirements under Solvency II, the calculation should aim for sufficient sophistication, proportionally to the resources of the undertaking (e.g. in the case of internal modelling). Therefore, in its advice CEIOPS agreed only to lower one of the thresholds for simplifications.
154. A majority of stakeholders argued that the MCR linear formula should include an allowance for deferred taxes. It is noted however that a number of stakeholders expressed support for CEIOPS' approach on this point.

- Following the results of QIS4, CEIOPS is concerned that including a deferred taxes factor would lead to significant difficulties of interpretation and lack of comparability between undertakings, which would negatively impact the legal certainty of the calculation. As the basis for a reliable calibration of a deferred taxes factor is currently lacking, the benefits as to the increased risk sensitivity are also questionable. This issue might be revisited in the future, when sufficient experience will have been gathered about the functioning of the Solvency II treatment of deferred taxes.
155. Changes were made concerning the granularity of capital at risk and the absolute floor for new composites.

Main comments and revisions to CP 56 – Tests and standards for internal model approval

156. The principle-based proposals included in CP 56 were broadly welcomed by the stakeholders. Nevertheless some requirements were seen by the industry as burdensome, in particular regarding the documentation standards and the use and documentation of expert judgement. CEIOPS received some comments stressing that the advice in the blue box had too much detail and was overly prescriptive on many of the tests.
157. CEIOPS has clarified that it developed advice that, in its view, reflected good practice in insurers' models.
158. Furthermore CEIOPS' view is that, following the proportionality principle, the requirements should be proportionate to the complexity of the model. In particular regarding the documentation standards, proportionality does not exempt any insurer from adequately documenting its internal model. For simpler internal models this might result in smaller amounts of documentation. However this should be a consequence of the level of complexity of the model, and not of the thoroughness of its documentation, as set out in CEIOPS' advice on proportionality. This has been inserted in the advice.
159. Some stakeholders requested more clarification of the requirements set out in the advice. In general, references to Level 3 guidance which may be provided by CEIOPS, have been inserted..

Main comments and revisions to CP 57 – Capital add-on

160. While some of the comments on the advice were generally supportive of CEIOPS' views and considered the proposed approach sensible and well balanced, a number of respondents expressed divergent views on several issues. After duly considering these comments, the advice was amended by including further explanations where comments indicated that this would be helpful but introduced no major changes.
161. Following stakeholders comments clarification of the expression of "following the Supervisory Review Process". Further, additional explanation

- is provided why procyclicality should not be a consideration in the decision of whether to set a capital add-on.
162. An explanation on why CEIOPS is not in favour of a special appeal process for capital add-ons was provided.
163. On the assessment of a capital add-on CEIOPS clarified the following:
- Overestimated and underestimated risks are being considered in the assessment of the significance of a deviation where (partial) internal models are used (netting). This is similar to when the standard formula is used;
 - For solo undertakings, a reference value for a significant deviation of the risk profile for standard formula and internal model users was fixed at 10% of the SCR, with the possibility for the supervisory authority to consider different values based on harmonised criteria. A deviation of 15% will by default always be considered significant;
 - A “within 5 years” review clause was introduced for the reference value of 10% and the 15% limit;
 - Further explanation of rationale for the maximum 6 months timeframe in relation to governance capital add-ons was provided.
164. For groups, CEIOPS clarified that non-EEA entities will have to be taken into account when the group SCR is being assessed and provided an approach for addressing group-specific risks. Finally, a clarification that group capital add-ons are neither automatic nor disregard risk mitigation, was made.

Main comments and revisions to CP 58 – Supervisory reporting and disclosure

165. Most of the stakeholders agreed with the approach taken by CEIOPS in developing the advice for supervisory reporting and public disclosure. However, there were a number of areas of concern expressed by stakeholders, particularly relating to the perceived burden that the reporting requirements would put on undertakings especially where CEIOPS suggested that:
- All the SFCR information should be duplicated in the RTS;
 - The SFCR and RTS should be stand-alone documents and should not include references or hyperlinks.
166. Regarding the reporting burden, CEIOPS majority view is that the RTS should contain all the information within the SFCR, and that the reports should be stand-alone documents. It was agreed that this aided the review by stakeholders and supervisors at little extra effort for undertakings. Hence, CEIOPS maintains its position by not agreeing with stakeholder concerns with regard to on duplication.
167. Concerns around disclosure of sensitive information in the SFCR were raised which should be avoided especially concerning internal models and risk management. CEIOPS has reviewed the SFCR and moved some

- requirements to the RTS where it felt this was appropriate (e.g. around risk mitigation or the administrative or management body's discussions).
168. Most stakeholders highlighted that the timeframes CEIOPS had established (3-4 months for annual reporting and 3-4 weeks for quarterly reporting in CP58) were attainable in the long term for the SFCR, the RTS and quantitative templates but unrealistic in the first few years of Solvency II (especially if the Level 3 deadline is Q4 2011).
 169. CEIOPS reviewed the timeframes established and proposes two points in its advice:
 - The deadlines are 14 weeks for annual reporting and 4 weeks for quarterly reporting; and
 - A scaling of the timeframes over the first two years after the implementation of Solvency II should occur where in the first year of implementation, the annual deadlines for the qualitative and quantitative reports shall be extended by 6 weeks, and the quarterly deadlines for the quantitative reports may be extended by 2 weeks. In the second year of implementation, the annual deadlines may be extended by 4 weeks, and the quarterly deadlines may be extended by 1 week.
 170. A number of respondents questioned the supervisory role in disclosure and reporting, for example, if supervisors should be expected to sign-off the disclosure requirements before publication. One idea suggested was to have retrospective review. CEIOPS intends to maintain the position as in CP 58 where supervisors have a role in ensuring compliance with Pillar 3 and has clarified that supervisors would not be expected to 'sign-off' disclosure requirements in advance of their publication or submission but could go back to undertakings after publication.
 171. Respondents asked for greater clarity on group reporting requirements, especially on timeframes. CEIOPS created a new section on group requirements to address some of the confusion that stakeholders experienced and also added explanation on the timeframes for group reporting. Further, CEIOPS also clarified issues on the language to be used for group reporting.
 172. Some stakeholders asked to develop proportionality and materiality further throughout the paper. CEIOPS discussed this and considered that it had provided sufficient information on these concepts in the paper. CEIOPS however made some drafting changes but found it difficult to address stakeholder comments in more detail as there were no drafting suggestions or concrete examples from stakeholders. CEIOPS nevertheless included the principle of proportionality and materiality in the blue box to try and enforce its importance (see also general remarks following consultation at the beginning of this document).
 173. Stakeholders had a number of comments on the quantitative reporting templates stating that CEIOPS needed to cut down the level of data and that the templates should be harmonised. CEIOPS will consider this work further at Level 3 and this is one of the priorities for CEIOPS work in the coming months.

Main comments and revisions to CP 59 – Remuneration

174. While stakeholders declared themselves to be supportive of the principle-based and sector-specific approach adopted by CEIOPS and agreed that the remuneration issues and related best practices should be an integral part of the governance of (re)insurance undertakings, most stakeholders were against all but the most high-level regulation with regard to remuneration in the insurance sector.
175. As CEIOPS agrees with the European Commission that having implementing measures on remuneration is in line with the Level 1 text – which was denied by some stakeholders – and will foster harmonisation, the final advice does not incorporate any major change with regard to the contents of the proposals. CEIOPS has however sought to clarify some points where the comments indicated that the draft proposals were not sufficiently precise. The more important clarifications or changes include the following.
176. The scope of application for remuneration principles is limited to personnel performing activities that involve significant risk-taking. An explicit inclusion of non-financial performance factors as relevant objective for the performance of individuals was included.
177. The principles have been amended as follows:
- Clarification of the factors which are important for the remuneration of personnel in key functions;
 - Recommendation for shareholder participation was worded more generally in order to avoid inconsistencies with national law;
 - Specification was made that expertise in the field of remuneration means knowing how a remuneration policy with due regard to risk management issues is to be designed;
 - If a third party advises on remuneration, conflicts of interests of these third parties should be disclosed;
 - Disclosure requirements exclude decision-taking processes of the administrative or management body and senior management.
178. For supervisory authorities it has been clarified that their task is not only to evaluate remuneration policies but remuneration practices as well.

Main comments and revisions to CP 60 – Group solvency assessment

179. CEIOPS confirmed in the revised advice that it did not intend to question the use of the accounting consolidation method as the default method for the group calculations.
180. CEIOPS has clarified that, in general, the scope of a group for the purpose of assessing group solvency will be the same as for the consolidated

accounts. Nevertheless, there may be cases where it is necessary to adjust the scope of the group for assessing group solvency.

181. In relation to the concern of some stakeholders on the inclusion of third countries in the group calculation, CEIOPS confirmed that the Level 1 text provides for this and hence recognises diversification that may exist with third country entities. However, there may be factors that restrict the recognition of that diversification, including insufficient information. CEIOPS recognises that these issues may also affect undertakings within the European area and are not unique to third countries. For these reasons, the equivalence of the third country regime is not the only issue to consider when assessing diversification. CEIOPS will publish a Consultation Paper on equivalence in December 2009.
182. CEIOPS has also clarified the section on the assessment of available group own funds. As considered in the Level 1 text, certain items of own funds may not be available to cover all risks of the group and this should be taken into account when assessing the solvency position of groups.
183. Some stakeholders indicated that they consider that no additional risks arise at the level of the group (group-specific risks). CEIOPS disagrees and considers that group-specific risks (e.g. risks from unregulated holding companies) and group benefits have to be addressed as part of the assessment of group solvency.

Main comments and revisions to CP 61 – Intra-group transactions and risk concentration

184. Stakeholders highlighted the importance of consistency with the Financial Conglomerates Directive (FCD) and the findings of the FCD Review.
185. Stakeholders commented that there should be convergence in the thresholds used for the reporting of intra group transactions (IGT) and risk concentration (RC). CEIOPS considers that there should be a common methodology for determining thresholds to promote harmonisation across the EEA. CEIOPS considers that this should be done in Level 3 guidance.
186. Some stakeholders considered that the scope of the reporting of IGT and RC was too large. CEIOPS view is that its proposals are consistent with the Level 1 text and reflect the need for a holistic approach to group supervision, encompassing all the entities that influence the risk profile of groups.

Main comments and revisions to CP 62 – Cooperation and colleges of supervisors

187. Stakeholders considered that the advice might be too high level to provide a clear overview of how the supervisory framework for groups will work in practice. For example, some stakeholders considered that the advice did not provide enough detail on the specific role of the group supervisor and the decision-making process within the college of supervisors. CEIOPS

considers that it is appropriate to maintain a flexible and pragmatic approach at Level 2.

188. The advice highlights the Level 1 Articles where the final decision is taken by the group supervisor or by the solo supervisor. CEIOPS also clarified that under the Level 1 text, a college is a forum for the exchange of information and cooperation, but has no legal character and therefore can not itself take decisions. Any decision following discussions within the college is made by the relevant supervisory authority.
189. Some stakeholders also considered that the advice should be more precise on the nature, format and frequency of information exchange among the participants within the college. CEIOPS has clarified that the group Report to the Supervisors (RTS) should be the basis for the regular exchange of information between supervisors.
190. Stakeholders considered that the importance of data protection was not stressed enough in the advice. CEIOPS further clarified that supervisors, including non-EEA supervisors, shall ensure the safe handling of confidential information and professional secrecy. Supervisors shall also have appropriate systems and structures in place, as well as written policies, to ensure compliance with these requirements.
