

Summary of Comments on CEIOPS-CP-44/09

CEIOPS-SEC-107/09

Consultation Paper on the Draft L2 Advice on TP - Counterparty default adjustment

CEIOPS would like to thank AAS BALTA, AB Lietuvos draudimas, AMICE, Association of British Insurers (ABI), Association of Run-off Companies (ACA), CEA ECO-SLV-09-439 (CEA), Centre Technique des Institutions de Prévoyance, CRO-Forum, Deloitte European Union member firms of Deloitte, DENMARK: Codan Forsikring A/S (10529638), DIMA (Dublin International Insurance & Management) , Federation of European Accountants (FEE), FFSA, German Insurance Association – Gesamtverband der D (GDV), GROUPAMA, Groupe Consultatif, INTERNATIONAL GROUP OF P&I CLUBS, International Underwriting Association of London, Ireland\39s Solvency 2 Group, excluding representa, Link4, Lloyd\39s, Lucida plc, Milliman, Munich RE, NORWAY: Codan Forsikring (Branch Norway) (991 502 , OAC Actuaries and Consultants, PricewaterhouseCoopers LLP, RBS Insurance, ROAM, RSA Insurance Group PLC, RSA Insurance Ireland Ltd, RSA\32\45\32Sun Insurance Office Ltd., SOGECORE, Trygg-Hansa Försäkrings AB (516401-7799) SWEDEN, and XL Capital Ltd

The numbering of the paragraphs refers to Consultation Paper No. 44 (CEIOPS-CP-44/09)

No.	Name	Reference	Comment	Resolution
1.	AAS BALTA	General Comment	<p>Our assumption is that undertakings will provide for counterparties that are already impaired as according to the process outlined by CEIOPS.</p> <p>For undertakings with counterparty exposure to a range of currently unimpaired counterparties the expected default adjustment to technical provisions is likely to be very small, perhaps less than 1% of the total reinsurance asset. The CEIOPS draft advice proposes a complex process for assessing the quantum of this adjustment. Complexities include:</p> <ul style="list-style-type: none"> - Assessing exposures to individual counterparties - Separating exposure between premium and claims provisions - Separating exposure between classes of business - Assessing loss given default recovery assumptions - Assessing probability of default assumptions if a large claim is submitted (3.9) 	Not agreed. Please refer to summary of comments.

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			<ul style="list-style-type: none"> - Allowing for collateral and other risk mitigation techniques <p>This imposes disproportionate effort on undertakings for a small adjustment to the Technical Provisions. Instead we suggest an alternative approach as follows:</p> <ul style="list-style-type: none"> - Carry out the detailed calculations initially - Determine a prudent % of the reinsurance asset as the adjustment to be made in light of the results of the previous step. This % should be a little higher than the result of the detailed calculations. - For subsequent calculations assess whether there has been any material change to the value of the reinsurance asset qualitatively - If not apply the prudent % to the reinsurance asset - The detailed calculations will need to be re- performed if there has been a material change or periodically (eg annually) otherwise 	
2.	AB Lietuvos draudimas	General Comment	<p>Our assumption is that undertakings will provide for counterparties that are already impaired as according to the process outlined by CEIOPS.</p> <p>For undertakings with counterparty exposure to a range of currently unimpaired counterparties the expected default adjustment to technical provisions is likely to be very small, perhaps less than 1% of the total reinsurance asset. The CEIOPS draft advice proposes a complex process for assessing the quantum of this adjustment. Complexities include:</p> <ul style="list-style-type: none"> - Assessing exposures to individual counterparties 	Not agreed. Please refer to comment 1.

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			<ul style="list-style-type: none"> - Separating exposure between premium and claims provisions - Separating exposure between classes of business - Assessing loss given default recovery assumptions - Assessing probability of default assumptions if a large claim is submitted (3.9) - Allowing for collateral and other risk mitigation techniques <p>This imposes disproportionate effort on undertakings for a small adjustment to the Technical Provisions. Instead we suggest an alternative approach as follows:</p> <ul style="list-style-type: none"> - Carry out the detailed calculations initially - Determine a prudent % of the reinsurance asset as the adjustment to be made in light of the results of the previous step. This % should be a little higher than the result of the detailed calculations. - For subsequent calculations assess whether there has been any material change to the value of the reinsurance asset qualitatively - If not apply the prudent % to the reinsurance asset - The detailed calculations will need to be re- performed if there has been a material change or periodically (eg annually) otherwise 	
3.	ACA	General Comment	The calculation of counterparty default risk appears more complex than all other sub modules risk (assessment of the probability at each yearly period on the whole run-off period, assessment of the recoverable cash flows at each yearly period or each LOB and each	Noted. Please refer to paragraph 3.23. Further advice on simplification methods will be provided, too

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			<p>counterparty,....).</p> <p>If an insurer is able to do all these calculations it seems that he has developed an internal model!</p>	
4.	AMICE	General Comment	<p>These are AMICE's view at the current stage of the project. As our work develops, these views may evolve depending, in particular, on the other elements of the framework which are not yet fixed.</p> <p>The comments outlined below constitute AMICE's primary areas of concern:</p> <p>AMICE believes that it would be very demanding to calibrate the LGD using a different default probability for each year, or a default probability linked to the amount to recover. This will lead to a very burdensome calculation. We suggest the one-year probability of default apply to the total amount of recoverable.</p> <p>Furthermore, special attention should be paid to reinsurers subject to Solvency II rules and equivalent. A clear distinction should be done between reinsurers covering their SCR and the others (not covering or excluded from the Solvency II perimeter). A higher recovery rate should be used for them.</p>	<p>Not agreed. Please refer to the summary of the comments.</p> <p>Noted.</p>
5.	ABI	General Comment	<p>We disagree with CEIOPS requirement of an effective 40% cap on recovery rates. We believe recovery rates will sometimes be higher (collateral, cash collateral) and this should not therefore become a benchmark. In practice, where it is well justified and documented, it should be possible to have a higher recovery rate. In addition, the 40% being proposed is the same as for the stressed conditions in CP51 and so appears to be unreasonably low. We would expect a higher recovery rate under best estimate conditions compared to stressed conditions.</p> <p>We would also highlight that for firms who offer funds from other insurers through their platform (e.g. unit linked defined</p>	<p>Noted. Higher recovery rates do not contradict with paragraphs 3.11 and 3.20 as long as the estimates are reliable.</p> <p>Noted. Please refer to the summary of the comments.</p>

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			<p>contribution (DC) pension platform), the proposed recovery rate would be particularly damaging. Such firms take the policyholders funds and pass them through to the other insurer to be invested. The liability to the policyholder remains with the firm which undertakes a reinsurance arrangement with third party fund providers who then invest into their underlying funds. Platform based models are becoming increasingly popular in the industry and the proposed restriction on recovery rates in the standard model seems inappropriately low for this type of arrangement. We would therefore like to see a distinction made between the different types of counterparty as the risk of reinsuring with a reinsurer that only conducts unit linked business is very different to the risk of reinsuring with a life insurance company that takes on risk in its day to day operations.</p> <p>We believe the approach proposed for the calculation of the adjustment for counterparty default (calculated separately at least for each line of business and each counterparty) to be too burdensome for a very limited added value. Undertakings should be able to calculate their adjustment for counterparty default at aggregate level, in particular where there is an important number of counterparties.</p>	<p>Noted. Please refer to the summary of the comments</p>
6.			Confidential comment deleted.	
7.	CEA	General Comment	<p>The paper shows a high level of prudence in the calibration, imposes a burdensome calculation and potentially generates pro-cyclical effects.</p> <p>The CEA finds the recovery rate of 40% for counterparties where no reliable estimate is available too low. We advocate for using the rate of 50% of QIS4 for such cases.</p> <p>We believe that reliable information can be derived from the solvency ratio of counterparties under Solvency II but also other</p>	<p>Noted.</p> <p>Agreed.</p> <p>Noted. Please refer to amendments in 3.12</p>

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			<p>sources. Specifically, undertakings should be able to use recovery rates higher than 50% for counterparties covering their SCR.</p> <p>A set of criteria is commonly used in order to assess the reliability of information for accounting purpose: freedom from material error and bias, faithful representation of that which it purports to represent, economic reflection of the substance of transactions and not merely of their legal form, neutrality, prudence and completeness in all material aspects. Based on the text of the Directive attempting to have the calculation of technical provision in line with developments in accounting, we urge Ceiops to consider these criteria in defining the reliability of information.</p> <p>The requirement of a very detailed segmentation generates an excessively burdensome calculation. The linking of the default probability to the amount to be recovered further increases this burden and leads also to further prudence in the calibration.</p> <p>The use of point in time estimates in the calculation of the adjustment generates pro-cyclical effects. In order to avoid such effect, the CEA opts for through the cycle estimates.</p>	<p align="center">Noted. Please refer to the summary of the comments.</p> <p align="center">Not agreed. Please refer to the summary of the comments.</p>
8.	Centre Technique des Institutions de Prévoyance	General Comment	<p>The counterparty default risk is covered by a specific SCR module in the standard SCR formula. This SCR module is calibrated against the occurrence of unexpected events.</p> <p>Concerning recoverables from reinsurance contracts, the default of a reinsurer is an unexpected event; in particular, this is literally true for reinsurers subject to Solvency II, for which the default probability is less than 0.5%.</p> <p>For this reason, the methodology presented in CP44 should be clarified in order to prevent double accounting for the same risks: one first time by a counterparty default SCR, and one second time by a reduction of recoverables from reinsurance.</p>	Not agreed. CP 44 deals with the adjustment of the Technical Provisions only

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9.	CRO-Forum	General Comment	<p>44.A Through-the-cycle estimate of default probability preferable (priority: high)</p> <p>The calibration in this CP reflects a point in time calibration. The CRO Forum believes that a through-the-cycle approach is preferable in order to avoid introducing pro-cyclical behaviour to the technical provision calculation.</p> <p>44.B Unnecessary prudence is introduced on counterparty recoverables (priority: high)</p> <p>The CRO Forum believes that a degree of prudence (inconsistent with the true underlying economics) has been introduced through the linking of default probability to claim size and the cap on the reinsurance recovery rate.</p> <p>Care is needed to ensure consistency (e.g. between default probability and recovery rate) and to avoid excess of prudence in the calculation.</p> <p>44.C Inconsistent with the IASB or CRD discussions (priority: high)</p> <p>The CRO Forum notes that the approach taken by the CP is not consistent with the expected loss model as defined by the IASB in their current discussion papers and with the definitions as used in the CRD. The basis for the counterparty default adjustment should be the measurement data. At that instance an insurer is to assess whether the counterparty will live up to its contractual requirements. That expectation is used in calculating the adjustment. In that assessment on the measurement data the possibility of default is assessed over the full duration of the asset.</p>	<p>Not agreed. The probability of default is estimated more appropriately by point in time.</p> <p>Not agreed. To our opinion PD is linked to the claim size. Furthermore the use of higher recovery rates is not excluded by paragraphs 3.11 and 3.20.</p> <p>Not agreed. We believe the approach of the CP to be in line. The probability of default is taken into account over the duration</p>
10.	Deloitte	General	As a general comment, we agree with CEIOPS' calculation of the	

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	European Union member firms of Deloitte	Comment	<p>counterparty default adjustment.</p> <p>Nevertheless:</p> <ul style="list-style-type: none"> - We advise that CEIOPS proposes the use of Stress Testing on the recoverable, as default and recovery levels are related to the evolution of the reinsurance company and there is, as known in the banking industry, a close relationship between one reinsurance company defaulting and other reinsurance competitors' default probabilities and recoveries rates. - Amongst information provided to assess default probability and recovery rate, we advise CEIOPS considers the use of Credit Default Spread levels, for the relevant reinsurance names, where there are listed and liquid CDS transactions. The use of CDS enables one to derive both probability of default and the recovery rate. - We disagree with the use of such adjustment without taking into account the portfolio effect (diversification and interdependency) of the difference recoverable an insurance undertaking could have in its balance sheet. We advise CEIOPS to take into consideration the correlation risk (interdependency) between reinsurance companies, which could be provided by products such as first to default or second to default, where financial institutions could provide cotes and reliable pricing. 	<p align="center">Noted.</p> <p align="center">Noted. (cf. to paragraph 3.6)</p> <p align="center">Not agreed. This approach would complicate the calculation and is already covered by the recovery rate.</p>
11.	DENMARK: Codan Forsikring A/S (10529638)	General Comment	<p>Our assumption is that undertakings will provide for counterparties that are already impaired as according to the process outlined by CEIOPS.</p> <p>For undertakings with counterparty exposure to a range of currently unimpaired counterparties the expected default adjustment to technical provisions is likely to be very small, perhaps less than 1% of the total reinsurance asset. The CEIOPS draft advice proposes a complex process for assessing the quantum</p>	<p align="center">Not agreed. Please refer to comment 1.</p>

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			<p>of this adjustment. Complexities include:</p> <ul style="list-style-type: none"> - Assessing exposures to individual counterparties - Separating exposure between premium and claims provisions - Separating exposure between classes of business - Assessing loss given default recovery assumptions - Assessing probability of default assumptions if a large claim is submitted (3.9) - Allowing for collateral and other risk mitigation techniques <p>This imposes disproportionate effort on undertakings for a small adjustment to the Technical Provisions. Instead we suggest an alternative approach as follows:</p> <ul style="list-style-type: none"> - Carry out the detailed calculations initially - Determine a prudent % of the reinsurance asset as the adjustment to be made in light of the results of the previous step. This % should be a little higher than the result of the detailed calculations. - For subsequent calculations assess whether there has been any material change to the value of the reinsurance asset qualitatively - If not apply the prudent % to the reinsurance asset - The detailed calculations will need to be re- performed if there has been a material change or periodically (eg annually) otherwise 	
12.	DIMA (Dublin	General Comment	DIMA welcomes the opportunity to comment on this paper.	

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	International Insurance & Management		<p>Comments on this paper may not necessarily have been made in conjunction with other consultation papers issued by CEIOPS.</p> <p>We would appreciate additional information and guidance from CEIOPS on bases and alternatives for assessing the probability of default as the current options are somewhat limited.</p> <p>It is an onerous and time-consuming exercise to carry out this calculation by line of business and for each counterparty. We suggest a simplified approach should be devised.</p> <p>This will be a new area and educational process for captives, which currently do not create an adjustment to recoverables for counterparty default risk. Two key technical steps will be introduced, namely calculating the average loss from a default and calculating the probability of a default.</p>	<p align="center">Noted.</p> <p align="center">Noted. Please refer to the summary of the comments.</p> <p align="center">Noted.</p>
13.	FEE	General Comment	<p>The paper proposes to provide an adjustment on a best estimate basis. In theory one would expect a deviation risk needs to be reflected as well in order to measure all assets and liabilities at current exit value or fair value. However, in practice available data on the possible default of reinsurers and SPV puts any way in question a kind of expected default approach.</p>	<p align="center">Noted.</p>
14.	FFSA	General Comment	<p>Care is needed to ensure consistency (e.g. between default probability and recovery rate) and to avoid excess of prudence in the calculation. In addition, in line with the proportionality principle, specific attention should be paid to avoid unduly burdensome methodologies</p> <p>FFSA would like to emphasize that it could be very demanding to calibrate the loss given default using a default probability different for each year, or a default probability linked to the amount to recover. This burden seems to be inadequate for standard formula calculations.(Refers to 3.15)</p>	<p align="center">Noted.</p> <p align="center">Noted.</p>

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			<p>Furthermore, special attention should be paid for counterparties subject to Solvency II rules. A clear distinction should be made between counterparties covering their SCR and the others (not covering or excluded from the Solvency II perimeter). A higher recovery rate should be used for covering their SCR.(See 3.17)</p> <p>Finally where no reliable estimate is available, FFSA suggests using a recovery rate by default of 50% (as in QIS4), rather than 40%, and a recovery rate higher than 50% for counterparties covering their SCR under solvency II. (See 3.20)</p>	<p>Noted. Please refer to the summary of comments.</p> <p style="text-align: center;">Agreed.</p>
15.			Confidential comment deleted.	
16.	GDV	General Comment	<p>GDV appreciates CEIOPS' effort regarding the implementing measures and likes to comment on this consultation paper. In general, GDV supports the detailed comment of CEA. Nevertheless, the GDV highlights the most important issues for the German market based on CEIOPS' advice in the blue boxes. It should be noted that our comments might change as our work develops. Our views may evolve depending in particular, on other elements of the framework which are not yet fixed – e.g. specific issues that will be discussed not until the third wave is disclosed.</p> <p>The paper shows a high level of prudence in the calibration imposes a burdensome calculation and potentially generates pro-cyclical effects.</p> <p>The GDV finds the recovery rate of 40% for counterparties where no reliable estimate is available too low. We advocate for using the rate of 50% of QIS4 for such cases.</p> <p>We believe that reliable information can be derived from the solvency ratio of counterparties under Solvency II but also other sources. Specifically, undertakings should be able to use recovery rates higher than 50% for counterparties covering their SCR.</p>	<p style="text-align: center;">Noted</p> <p>Not agreed. Please refer to the summary of comments.</p> <p style="text-align: center;">Agreed</p> <p>Noted. Please refer to the summary of comments.</p>

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			<p>A set of criteria is commonly used in order to assess the reliability of information for accounting purpose: freedom from material error and bias, faithful representation of that which it purports to represent, economic reflection of the substance of transactions and not merely of their legal form, neutrality, prudence and completeness in all material aspects. Based on the text of the Directive attempting to have the calculation of technical provision in line with developments in accounting, we urge CEIOPS to consider these criteria in defining the reliability of information.</p> <p>The requirement of a very detailed segmentation generates an excessively burdensome calculation. The linking of the default probability to the amount to be recovered further increases this burden and leads also to further prudence in the calibration.</p> <p>The use of point in time estimates in the calculation of the adjustment generates pro-cyclical effects. In order to avoid such effect, the GDV opts for through the cycle estimates.</p>	<p>Noted. Please refer to amendments in 3.6</p> <p>Not agreed. Please refer to the summary of comments.</p> <p>Not agreed. Please refer to the summary of comments.</p>
17.	GROUPAMA	General Comment	<p>Groupama would like to emphasize that it could be very demanding to calibrate the LGD using a different default probability for each year, or a default probability linked to the recoverable amount. This work seems to be inadequate for standard formula calculations, and we suggest using the one-year probability of default applied to the total amount of recoverables. This probability should be calculated through the cycle so as to avoid an unwanted pro-cyclical effect. (3.9)</p> <p>Furthermore, special attention should be paid to reinsurers subject to Solvency II rules. A clear distinction should be made between reinsurers covering their SCR and others (not covering or excluded from the Solvency II perimeter). A higher recovery rate should be used for them.</p>	<p>Not agreed. Please refer to the summary of the comments.</p> <p>Noted. Please refer to the summary of comments.</p>
18.	Groupe	General	Subject to considerations of materiality in the context of a	Noted. Please refer to the

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	Consultatif	Comment		summary of the comments.
			<p>particular undertaking, we agree in principle with the suggestion in this paper that probability of default and loss-given-default be considered independently as far as practicable. The suggested recovery cap of 40% may be excessively prudent, particularly when applied to undertakings themselves subject to solvency supervision.</p> <p>We note that the same level of cap is used in CP 51 in relation to consideration of SCR and we wonder whether this is consistent. 40% arguably seems a low level of best estimate, particularly for counterparties complying themselves with Solvency 2, in respect of which losses should be expected to be negligible.</p>	<p>Noted. Please refer to the summary of comments.</p>
19.	INTERNATIONAL GROUP OF P&I CLUBS	General Comment	<p>The IG is broadly welcoming of the advice set out in CP 44, in particular the allowance for risk mitigating instruments set out in 3.21. This provision should allow the IG Clubs to remove the credit risk between Clubs and their dedicated reinsurers in the Clubs' solo returns.</p> <p>The IG also has a number of observations in relation to the calculation of loss given default, referred to in 3.11 and 3.20.</p>	<p>Noted</p> <p>Noted</p>
20.	Link4	General Comment	<p>Our assumption is that undertakings will provide for counterparties that are already impaired as according to the process outlined by CEIOPS.</p> <p>For undertakings with counterparty exposure to a range of currently unimpaired counterparties the expected default adjustment to technical provisions is likely to be very small, perhaps less than 1% of the total reinsurance asset. The CEIOPS draft advice proposes a complex process for assessing the quantum of this adjustment. Complexities include:</p> <ul style="list-style-type: none"> - Assessing exposures to individual counterparties 	<p>Not agreed. Please refer to comment 1.</p>

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			<ul style="list-style-type: none"> - Separating exposure between premium and claims provisions - Separating exposure between classes of business - Assessing loss given default recovery assumptions - Assessing probability of default assumptions if a large claim is submitted (3.9) - Allowing for collateral and other risk mitigation techniques <p>This imposes disproportionate effort on undertakings for a small adjustment to the Technical Provisions. Instead we suggest an alternative approach as follows:</p> <ul style="list-style-type: none"> - Carry out the detailed calculations initially - Determine a prudent % of the reinsurance asset as the adjustment to be made in light of the results of the previous step. This % should be a little higher than the result of the detailed calculations. - For subsequent calculations assess whether there has been any material change to the value of the reinsurance asset qualitatively - If not apply the prudent % to the reinsurance asset - The detailed calculations will need to be re- performed if there has been a material change or periodically (eg annually) otherwise 	
21.	Lloyd's	General Comment	We broadly agree with the principles outlined in this paper. Our detailed comments are set out below.	Noted.

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			<p>The proposal does not include an allowance for reinsurance disputes (either possible or actual) which can also reduce the expected recoveries from reinsurance contracts. We would expect undertakings to be required to allow for this, in a similar fashion, when considering best estimate expected reinsurance recoveries.</p> <p>We do not agree with the 40% maximum rate suggested. Market studies on recovery rates from past reinsurance failures support a maximum rate of 50% (as used in QIS4). Information on recovery rates from failed insurance\reinsurance entities must be taken into account in the derivation of expected recovery rates.</p> <p>We consider that, whilst it is desirable to calculate the counterparty default adjustment by line of business and counterparty, proportionality needs to be considered carefully and welcome the proposed simplification (which allows counterparties to be grouped).</p> <p>We would expect to see some stated consistency in estimating probabilities of default between the approaches for technical provisions outlined in CP44 and those for the SCR outlined in CP51.</p>	<p align="center">Noted</p> <p align="center">Noted. Please refer to the summary of contents.</p> <p align="center">Noted. Please refer to 3.23.</p> <p align="center">Noted. However, this is not in scope of CP 44.</p>
22.	Lucida plc	General Comment	<p>Lucida is a specialist UK insurance company focused on annuity and longevity risk business. We currently insure annuitants in the UK and the Republic of Ireland (the latter through reinsurance).</p> <p>Although the approach set out in this paper is theoretically accurate, we believe that the use of a loss given default assumption of 60% (recovery of 40%) is excessively prudent. Insurers should</p>	<p align="center">Noted.</p> <p align="center">Noted. Please refer to the summary of comments.</p>

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			also have the option of using a more approximate approach to allowing for counterparty default as the approach proposed could prove rather burdensome.	
23.	Munich RE	General Comment	<p>We fully support all of the GDV statements and would like to add the following points:</p> <p>This CP is dealing with a valuation issue. Hence, the general principles regarding valuation should be stressed. This especially applies for the market consistency of the approach and it's demand to take into account the whole cash flow pattern until maturity.</p> <p>The calibration in this CP reflects a point in time calibration. A through-the-cycle approach would be preferable in order to avoid introducing pro-cyclical behaviour to the technical provision calculation.</p> <p>It seems that a degree of prudence (inconsistent with the true underlying economics) has been introduced through the linking of default probability to claim size and the cap on the reinsurance recovery rate. In our view this overshoots the marks.</p>	<p>Noted.</p> <p>Noted. See amendments in the text.</p> <p>Not agreed. Please refer to the summary of comments.</p> <p>Not agreed. Please refer to the summary of comments.</p>
24.	NORWAY: Codan Forsikring (Branch Norway) (991 502	General Comment	<p>Our assumption is that undertakings will provide for counterparties that are already impaired as according to the process outlined by CEIOPS.</p> <p>For undertakings with counterparty exposure to a range of currently unimpaired counterparties the expected default adjustment to technical provisions is likely to be very small, perhaps less than 1% of the total reinsurance asset. The CEIOPS draft advice proposes a complex process for assessing the quantum of this adjustment. Complexities include:</p> <ul style="list-style-type: none"> - Assessing exposures to individual counterparties - Separating exposure between premium and claims provisions 	Not agreed. Please refer to comment 1.

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25.			Confidential comment deleted.	
26.	PricewaterhouseCoopers LLP	General Comment	We welcome the inclusion of guidance in the Level 2 text on allowing for reinsurer and SPV counterparty risk in the technical provisions. We caution that materiality and proportionality concepts should be applied to ensure that the method adopted is	Noted.

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			practical. We have a number of specific comments detailed below.	
27.	RBS Insurance	General Comment	We believe the calculation splits required in 3.22 would prove unduly onerous for non-life insurers, who typically have very many reinsurers on each treaty with relatively low exposure against each.	Noted. Please refer to the summary of comments.
28.	ROAM	General Comment	<p>ROAM believes that it could be very demanding to calibrate the LGD using a default probability different for each year, or a default probability linked to the amount to recover. This burden seems to be inadequate for standard formula calculations, and we suggest the one-year probability of default apply to the total amount of recoverables.</p> <p>Furthermore, special attention should be paid to reinsurers submitted to Solvency II rules. A clear distinction should be made between reinsurers covering their SCR and the others (not covering or excluded for the Solvency II perimeter). A higher recovery rate should be used for the latter ones.</p> <p>CEIOPS explains in this paper why the recovery rate has changed due to the financial crisis. ROAM wants to emphasize that during this crisis no reinsurers defaulted. ROAM thinks that there is no argument to justify a decrease for the recovery rate. Furthermore, in QIS4 Technical Specification in the footnote page 155, CEIOPS considers that "50% is a conservative choice". We suggest keeping this recovery rate by default.</p> <p>(see comment to 3.20)</p>	<p>Not agreed. Please refer to the summary of the comments.</p> <p>Noted. Please refer to the summary of comments.</p> <p>Noted. Please refer to the summary of comments.</p>
29.	RSA Insurance Group PLC	General Comment	Our assumption is that undertakings will provide for counterparties that are already impaired as according to the process outlined by CEIOPS.	Not agreed. Please refer to comment 1.

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		<p>For undertakings with counterparty exposure to a range of currently unimpaired counterparties the expected default adjustment to technical provisions is likely to be very small, perhaps less than 1% of the total reinsurance asset. The CEIOPS draft advice proposes a complex process for assessing the quantum of this adjustment. Complexities include:</p> <ul style="list-style-type: none"> - Assessing exposures to individual counterparties - Separating exposure between premium and claims provisions - Separating exposure between classes of business - Assessing loss given default recovery assumptions - Assessing probability of default assumptions if a large claim is submitted (3.9) - Allowing for collateral and other risk mitigation techniques <p>This imposes disproportionate effort on undertakings for a small adjustment to the Technical Provisions. Instead we suggest an alternative approach as follows:</p> <ul style="list-style-type: none"> - Carry out the detailed calculations initially - Determine a prudent % of the reinsurance asset as the adjustment to be made in light of the results of the previous step. This % should be a little higher than the result of the detailed calculations. - For subsequent calculations assess whether there has been any material change to the value of the reinsurance asset qualitatively - If not apply the prudent % to the reinsurance asset 	
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			<ul style="list-style-type: none"> - The detailed calculations will need to be re- performed if there has been a material change or periodically (eg annually) otherwise 	
30.	RSA Insurance Ireland Ltd	General Comment	<p>Our assumption is that undertakings will provide for counterparties that are already impaired as according to the process outlined by CEIOPS.</p> <p>For undertakings with counterparty exposure to a range of currently unimpaired counterparties the expected default adjustment to technical provisions is likely to be very small, perhaps less than 1% of the total reinsurance asset. The CEIOPS draft advice proposes a complex process for assessing the quantum of this adjustment. Complexities include:</p> <ul style="list-style-type: none"> - Assessing exposures to individual counterparties - Separating exposure between premium and claims provisions - Separating exposure between classes of business - Assessing loss given default recovery assumptions - Assessing probability of default assumptions if a large claim is submitted (3.9) - Allowing for collateral and other risk mitigation techniques <p>This imposes disproportionate effort on undertakings for a small adjustment to the Technical Provisions. Instead we suggest an alternative approach as follows:</p> <ul style="list-style-type: none"> - Carry out the detailed calculations initially - Determine a prudent % of the reinsurance asset as the adjustment to be made in light of the results of the previous step. This % should be a little higher than the result of the detailed calculations. 	Not agreed. Please refer to comment 1.

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			<ul style="list-style-type: none"> - For subsequent calculations assess whether there has been any material change to the value of the reinsurance asset qualitatively - If not apply the prudent % to the reinsurance asset - The detailed calculations will need to be re- performed if there has been a material change or periodically (eg annually) otherwise 	
31.	RSA - Sun Insurance Office Ltd.	General Comment	<p>Our assumption is that undertakings will provide for counterparties that are already impaired as according to the process outlined by CEIOPS.</p> <p>For undertakings with counterparty exposure to a range of currently unimpaired counterparties the expected default adjustment to technical provisions is likely to be very small, perhaps less than 1% of the total reinsurance asset. The CEIOPS draft advice proposes a complex process for assessing the quantum of this adjustment. Complexities include:</p> <ul style="list-style-type: none"> - Assessing exposures to individual counterparties - Separating exposure between premium and claims provisions - Separating exposure between classes of business - Assessing loss given default recovery assumptions - Assessing probability of default assumptions if a large claim is submitted (3.9) - Allowing for collateral and other risk mitigation techniques <p>This imposes disproportionate effort on undertakings for a small adjustment to the Technical Provisions. Instead we suggest an</p>	Not agreed. Please refer to comment 1.

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			<p>alternative approach as follows:</p> <ul style="list-style-type: none"> - Carry out the detailed calculations initially - Determine a prudent % of the reinsurance asset as the adjustment to be made in light of the results of the previous step. This % should be a little higher than the result of the detailed calculations. - For subsequent calculations assess whether there has been any material change to the value of the reinsurance asset qualitatively - If not apply the prudent % to the reinsurance asset - The detailed calculations will need to be re- performed if there has been a material change or periodically (eg annually) otherwise 	
32.	SOGECORE	General Comment	<p>We believe that it could be very demanding to calibrate the LGD using a default probability different for each year, or a default probability linked to the amount to recover.</p> <p>Furthermore, special attention should be paid to reinsurers submitted to Solvency II rules. Reinsurers covering their SCR should clearly be distinguished from the others (not covering or excluded for the Solvency II perimeter) as a higher recovery rate should be used for them.</p>	<p>Noted. Please refer to the summary of comments.</p> <p>Noted. Please refer to the summary of comments.</p>
33.	Trygg-Hansa Försäkrings AB (516401-7799) SWEDEN	General Comment	<p>Our assumption is that undertakings will provide for counterparties that are already impaired as according to the process outlined by CEIOPS.</p> <p>For undertakings with counterparty exposure to a range of currently unimpaired counterparties the expected default adjustment to technical provisions is likely to be very small, perhaps less than 1% of the total reinsurance asset. The CEIOPS</p>	<p>Not agreed. Please refer to comment 1.</p>

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			<p>draft advice proposes a complex process for assessing the quantum of this adjustment. Complexities include:</p> <ul style="list-style-type: none"> - Assessing exposures to individual counterparties - Separating exposure between premium and claims provisions - Separating exposure between classes of business - Assessing loss given default recovery assumptions - Assessing probability of default assumptions if a large claim is submitted (3.9) - Allowing for collateral and other risk mitigation techniques <p>This imposes disproportionate effort on undertakings for a small adjustment to the Technical Provisions. Instead we suggest an alternative approach as follows:</p> <ul style="list-style-type: none"> - Carry out the detailed calculations initially - Determine a prudent % of the reinsurance asset as the adjustment to be made in light of the results of the previous step. This % should be a little higher than the result of the detailed calculations. - For subsequent calculations assess whether there has been any material change to the value of the reinsurance asset qualitatively - If not apply the prudent % to the reinsurance asset - The detailed calculations will need to be re- performed if there has been a material change or periodically (eg annually) otherwise 	
34.	XL Capital	General	The requirement to calculate the counterparty default adjustment	Noted. Please refer to the

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	Ltd	Comment		summary of comments
			to recoverables from reinsurance contracts and SPVs separately for each line of business and each counterparty seems complex for the purposes of best estimate of technical provisions.	
35.	RBS Insurance	2.2.	We would support any requirements being in line with international developments in accounting and supervision.	Noted.
36.	CEA	3.2.	The CEA asks for more clarity on the definition of counterparties, including the context of groups.	Not agreed. Please refer to 3.1 for the scope of the CP.
37.	International Underwriting Association of London	3.2.	Does the term "counterparties" refer only to counterparties external to a group?	All counterparties.
38.	Munich RE	3.2.	It should be added that the proposed approach is aiming for a market consistent price of the recoverable.	Agreed. See revised text.
39.	ABI	3.3.	We believe that it would be more relevant if CEIOPS uses an example which covers the lifetime of the transaction with the counterparty.	Noted.
40.	CEA	3.3.	We believe that it would be more relevant if Ceiops uses an example which covers the lifetime of the transaction with the counterparty.	Noted.
41.	Milliman	3.3.	The guidance, while sophisticated, is a significant increase in complexity relative to the observed industry practice. For recoveries relative to amounts incurred to date, it is straightforward to be able to classify each future cash flow into the LOB and Counterparty component. For recoveries relative to IBNR amounts, however, this requires some significant assumptions in terms of the characteristics of the losses making up the IBNR. The approach demands that IBNR be allocated (at a minimum) to a LOB and counterparty level. Prior to this complexity, there was no material difference between 5 €1M claims and 1 €5M claim in terms of IBNR	Noted.

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			for a LOB. With this complexity, such additional assumptions (with little to no reliable data to base this assumption on) will become necessary.	
42.	Deloitte European Union member firms of Deloitte	3.4.	We agree with CEIOPS' calculation, taking into consideration discounted effects for the different cash flows (C1, C2 and C3)	Noted.
43.	Deloitte European Union member firms of Deloitte	3.5.	<p>Amongst information provided to assess default probability and recovery rate, we advise CEIOPS to use Credit Default Spread levels, for the relevant reinsurance names, where there are listed and liquid CDS transactions. The use of CDS enables one to derive both probability of default and the recovery rate.</p> <p>The new regulations in Europe and US which are leading to the emergence of a liquid and transparent CDS market could help the definition of "Counterparty Default adjustment to recoverable".</p>	Noted. See revised text.
44.	ABI	3.6.	<p>We believe this should be interpreted in a flexible manner as it might be excessively burdensome to require current, credible and reliable information in this context, in particular for smaller insurers.</p> <p>In particular, it may be particularly problematic assessing the information used by a third part in their assessment is current, reliable and credible. There may be commercial sensitivity about opening up the third party approach to this level of scrutiny.</p>	Noted.
45.	CRO-Forum	3.6.	The current text suggests a very burdensome process to follow when assessing the counterparty default risk for each counterparty. Care should also be used when looking at the information credit ratings are with respect to the willingness and ability of counterparties to repay their amounts due to policyholders.	Noted.

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46.	DIMA (Dublin International Insurance & Management	3.6.	The reliance on credit rating agencies is not undisputed. As no alternative to credit rating agencies seems to be readily available and the use of credit ratings is increasingly important for regulatory purposes, we would urge to introduce regulation and supervision of the credit rating agency sector at the earliest possible date in advance of Solvency II.	Noted.
47.	Groupe Consultatif	3.6.	CP 51 provides more detail on the assessment of the probability of default. We assume that the same methodology should apply to the calculation of the technical provision.	Not agreed. This is not in scope of Level 2.
48.			Confidential comment deleted.	
49.	ROAM	3.6.	The need for reliable and credible information is excessively demanding: it is burdensome, if not impossible, to assess that the information provided by a third party is current, reliable and credible. Such a requirement could lead in case of smaller undertakings to the creation of specialized credit departments. Consequently this requirement should be interpreted in a flexible manner.	Noted.
50.	SOGECORE	3.6.	The need for reliable and credible information is excessively demanding: it is burdensome, if not impossible, to assess that the information provided by a third party is current, reliable and credible. Such a requirement could lead in case of smaller undertakings to the creation of specialized credit departments that would be too costly. Consequently this requirement should be interpreted in a flexible manner. We nevertheless value the possibility of several sources of information to make this assessment of risk. We also would like to address the possible distortion of information depending on the time it is gathered/collected for instance for the ratings during the	Noted. Noted.

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			current crisis. It is difficult in the process to update values daily.	
51.	ABI	3.7.	We agree with CEIOPS that the sophisticated analysis of the time dependence of the probability of default may be disproportionate in most cases.	Noted.
52.	CEA	3.7.	We agree to Ceiops statement that the sophisticated analysis of the time dependence of the probability of default may be disproportionate in most cases. Point-in-time calibration leads to pro-cyclicality. In addition, even the best point-in-time PD models are not able to react in time before a turn in the cycle. Therefore we are in favour of through-the-cycle estimates since point-in-time estimates are not available on a comprehensive basis.	Noted. Not agreed. Please refer to the summary of the comments.
53.	CRO-Forum	3.7.	Point-in-time calibration leads to pro-cyclicality. In addition, even the best point-in-time PD models are not able to react in time before a turn in the cycle. It would therefore be more prudent to use through-the-cycle calibrations.	Noted. Please refer to the summary of comments.
54.	Deloitte European Union member firms of Deloitte	3.7.	We advise CEIOPS proposes the use of Stress Testing on the recoverable, as default and recovery levels are related to the evolution of the reinsurance company and there is, as known in the banking industry, a close relationship between one reinsurance company defaulting and others reinsurance competitors' default probabilities and recoveries rates.	Noted. As the assessment is done on best estimate level, the dependence is appropriately taken into account.
55.	DIMA (Dublin International Insurance & Management	3.7.	"For example, the credit ratings of rating agencies are usually based on trough-the-cycle assessments" should read "through-the-cycle assessments".	Agreed.
56.	Munich RE	3.7.	Point-in-time calibration leads to pro-cyclicality. In addition, even the best point-in-time PD models are not able to react in time	Not agreed. Please refer to the summary of the comments.

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			before a turn in the cycle. It would therefore be more prudent to use through-the-cycle calibrations.	
57.			Confidential comment deleted.	
58.	PricewaterhouseCoopers LLP	3.7.	We agree that conceptually "point in time" estimates of the probability of default is more preferable than a "through the cycle" estimates. However, we caution that this may not be practically possible.	Noted.
59.	ABI	3.8.	Note- no text in original comment	
60.	CEA	3.8.	The CEA considers that the demonstration of the reliability, objectivity and prudence of the point-in-time estimates is burdensome. Consequently, we propose the use of through-the-cycle estimates as the preferred approach. Such estimates would also avoid potential pro-cyclical effects.	Not agreed. Please refer to the summary of the comments.
61.	Lloyd's	3.8.	We agree.	Noted.
62.			Confidential comment deleted.	
63.	ROAM	3.8.	ROAM considers that the demonstration of the reliability, objectivity and prudence of the point-in-time estimates is burdensome. Consequently, we propose the use of through-the-cycle estimates as the preferred approach. Such estimates would also avoid potential pro-cyclical effects.	Not agreed. Please refer to the summary of the comments.
64.	ACA	3.9.	In order to take into account the impact of catastrophe risk on the probability of counterparty default, we could use this reasoning, but in practice, it is really hard to estimate the threshold value which will lead to the default.	Noted. See revised text.
65.	AMICE	3.9.	We agree with this principle on a theoretical basis. However, it is very demanding to calibrate the probability of default of a	Noted. See revised text.

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			counterparty according to the amount payable by such a counterparty. This issue should be linked to the dependencies with catastrophe risk.	
66.	ABI	3.9.	Whilst we understand in principle that the probability of default should have regard to the variability in the amount payable, we note that in practice there is little evidence on this dependency and it may be difficult – especially for smaller insurers to practically apply this level of sophistication.	Noted. See revised text.
67.	CEA	3.9.	<p>While we understand in principle the recommendation that the probability of default should have regard to the variability in the amount payable, we note that in practice there is little evidence on this dependency.</p> <p>If the credit-quality of a reinsurer would depend materially on the size of a possible claim against it, the insurance company would potentially never accept it as a viable reinsurer. It will be burdensome or even impossible to calibrate the probability of default of a counterparty according to the amount payable by that counterparty. Further, ratings of credit rating agencies potentially include the type of extreme events mentioned in the paragraph and thus this method could become confusing.</p> <p>The CEA recommends removing this assessment.</p>	Noted. See revised text.
68.	CRO-Forum	3.9.	<p>The CRO-forum notes that in practice the probability of default almost never depends materially on the size of the exposure: if the credit-quality of the counterparty would depend materially on the size of a possible claim against it, the insurance company would not accept this and seek a more viable counterparty.</p> <p>Example is not realistic. Reinsurance credit risk exposure is measured per counterparty (aggregation of individual contracts) after which expected loss can be calculated using LGD and PD. Defining different LGD's parameters per line of business per</p>	Noted. See revised text.

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			<p>reinsurer per amount of exposure creates a lot of extra work, besides the fact that it is statistically not possible (also due to lack of data) to determine these parameters.</p> <p>Furthermore it is unlikely that a single exposure would be transacted that jeopardizes the health of counterparty and in turn the ceding party. This is due to the fact that both parties have an interest in this not being the case.</p>	
69.	Deloitte European Union member firms of Deloitte	3.9.	<p>We agree with the calculation proposed by CEIOPS if the 100 recoverable is paid before 10,000, where the reinsurance company is supposed to be under risk of defaulting.</p> <p>If the time frame of 10 000 is payable before the 100, we advise that the calculation to be $100 \times 99\% \times (1-50\%) + 10000 \times 1\% \times (1-50\%)$. As in the case of the payment of 10,000, the reinsurance company should be in default and therefore will only pay for it all claims the same recovery rate level</p>	Noted. See revised text.
70.	FFSA	3.9.	<p>CEIOPS recommends that the variability in the amount payable should be taken into account in the assessment of the probability of default.</p> <p>FFSA considers that:</p> <ol style="list-style-type: none"> 1. The probability of default should reflect already the overall outstanding amount payable. 2. This requirement is burdensome for the undertaking and it could be impossible to implement. Also, the undertaking needs to collect the different engagements of the counterparty to reflect it in the default probability as stated in the paper. <p>Therefore, FFSA considers that this approach is confusing and not consistent. FFSA recommends removing this assessment all together</p>	Noted. See revised text.

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71.	GDV	3.9.	<p>While we understand in principle the recommendation that the probability of default should have regard to the variability in the amount payable, we note that in practice there is little evidence on this dependency.</p> <p>If the credit-quality of a reinsurer would depend materially on the size of a possible claim against it, the insurance company would potentially never accept it as a viable reinsurer. It will be burdensome or even impossible to calibrate the probability of default of a counterparty according to the amount payable by that counterparty. Further, ratings of credit rating agencies potentially include the type of extreme events mentioned in the paragraph and thus this method could become confusing.</p> <p>The GDV recommends removing this assessment.</p>	Noted. See revised text.
72.	GROUPAMA	3.9.	<p>Groupama would like to emphasize that it could be very demanding to calibrate the LGD using a different default probability for each year, or a default probability linked to the recoverable amount. This work seems to be inadequate for standard formula calculations, and we suggest using the one-year probability of default applied to the total amount of recoverables. This probability should be calculated through the cycle so as to avoid an unwanted pro-cyclical effect.</p>	Not agreed. Please refer to the summary of the comments.
73.	Groupe Consultatif	3.9.	<p>We recognise the arithmetic here, but question whether it is relevant to the real world in which reinsurers and counterparties manage their activities so as to be able to meet claims by individual cedants and counterparties without increased default risk.</p> <p>For example, in the case of applying the proposed calculation for a reinsurance contract this implies knowledge about the existence or non-existence of retrocession agreements of the counterparty, which is not necessary available.</p>	Noted. See revised text.
74.	Lloyd's	3.9.	<p>We agree but note this can become complex in practice and thus</p>	Noted. See revised text.

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			may be disproportionate.	
75.	Milliman	3.9.	The guidance, while sophisticated, is a significant increase in complexity relative to the observed industry practice. The scenario uncertainty presented exists in the IBNR portion of the unpaid loss. This approach requires significant assumptions in terms of the characteristics of the losses making up the IBNR. The approach demands that IBNR be allocated (at a minimum) to a LOB and counterparty level. As in 3.3, we are unconvinced that data supporting such an approach exists in a reliable form and that the result of such an approach adds value.	Noted. See revised text.
76.	ROAM	3.9.	We agree with this principle on a theoretical basis. However, it is very demanding to calibrate the probability of default of a counterparty according to the amount payable by such counterparty. This issue should be rather linked to the dependencies with catastrophe risk.	Noted. See revised text.
77.	CEA	3.10.	<p>There is an inconsistency in the definition of PD_t, which is defined in par. 3.3 as "the probability that the counterparty defaults <u>during year t</u> ", and in par. 3.10 as "the probability of default <u>during the next t years</u>".</p> <p>To be consistent with the approach followed under par. 3.3 and 3.4 and if only PD is known (probability of default during the first year to be considered constant over time), then PD_t should be calculated as $PD \cdot (1 - PD)^{t-1}$.</p>	Not agreed. However, see amendments in the text.
78.	Deloitte European Union member firms of Deloitte	3.10.	<p>We do believe that an exponential extrapolation for the time horizon Default Probability is more relevant than the proposed formula.</p> <p>The reason behind the use of an exponential extrapolation came from the fact that the default risk, in addition to increase, accelerated over time. We do believe that the use for the Credit Default Swaps Bid quotes for the time horizon, with an</p>	Not agreed.

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			extrapolation of the time horizon, where the CDS is not quoted, or the liquidity is weak.	
79.	GDV	3.10.	<p>There is an inconsistency in the definition of PD_t, which is defined in par. 3.3 as “the probability that the counterparty defaults during year t”, and in par. 3.10 as “the probability of default during the next t years”.</p> <p>To be consistent with the approach followed under par. 3.3 and 3.4 and if only PD is known (probability of default during the first year to be considered constant over time), then PD_t should be calculated as $PD \cdot (1 - PD)^{(t-1)}$.</p>	Not agreed. However, see amendments in the text.
80.	Lloyd’s	3.10.	We agree.	Noted.
81.	ACA	3.11.	<p>In QIS4, it was considered that a recovery rate of 50% was compatible with the best practice.</p> <p>Now, CEIOPS recommend to settle the recovery rate with a maximum of 40%. Are there experiences in regard with the current financial crisis to justify this fall?</p>	Noted. See revised text.
82.	ABI	3.11.	See comments under 3.20	Noted.
83.	Association of Run-off Companies	3.11.	Regarding the maximum of 40% recovery which applies to counterparties in the event of default... is there any justifiable basis for this maximum recovery? We would expect more analysis of market data showing recovery rates experienced by type of counterparty (e.g. according to their ratings).	
84.	CEA	3.11.	No maximum recovery rates should be set, as very often reinsurance contracts contain provisions where an insurer can ask for collateral (sometimes cash deposits) when a reinsurer’s rating drops below a certain level. In such cases, recovery rate may be as high as 100%. In any case, a 40% cap on recovery rates is too low and is not evidenced by current market practice. For cases where there is no credit rating available, the recovery rate of 50% from	Noted. See revised text.

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			QIS4 would be more appropriate. For counterparties under Solvency II, covering their SCR, recovery rates above 50% should be allowed.	
85.	CRO-Forum	3.11.	<p>The CRO forum believes that undertakings should be allowed to take into account particulars of their contracts. For example when considering reinsurance default provisions, risk mitigating measures (such as collateral requirements) in the contract should be taken into account. Furthermore, to be consistent with CP51, it should be possible to deduct collateral from the projected recoveries before applying a recovery rate. Risks covered by SPVs need to reflect the protection provided by the fully funded criteria</p> <p>The CRO forum would like more justification for the choice of a 40% recovery rate. This is in line with our response to CP51 paragraph 3.44.</p> <p>We propose that rather than setting an arbitrary recovery rate the recovery rate should be set using similar/ related paper available in the market.</p>	Noted. See revised text.
86.	Deloitte European Union member firms of Deloitte	3.11.	<p>We agree with the fact that, when not available, recovery rate should not exceed 40%. Nevertheless we do believe that it is necessary of the use of CDS quotes (which provides both Default Probability and Recovery Rates) to be used in the assessment of the counterparty default adjustment.</p> <p>One should take into consideration the correlation risk (interdependency) between reinsurance companies, which could be provided by products such us first to default or second to default, where financial institutions could provides cotes and reliable pricing.</p>	Noted.
87.	Groupe Consultatif	3.11.	We would wish to understand the basis for the 40% recovery rate cap and the intended scope of its application. For example it would seem very pessimistic to assume that the maximum recovery from	Noted. See summary of comments.

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			reinsurers subject to the Solvency 2 framework was only 40%.	
88.	INTERNATIONAL GROUP OF P&I CLUBS	3.11.	See below under 3.20	Noted.
89.	Lloyd's	3.11.	We do not agree with the 40% maximum rate suggested. Market studies of recovery rates from past insurance/reinsurance failures support a maximum rate of 50% (as used in QIS4). Information on recovery rates from failed insurance/reinsurance entities should be taken into account in the derivation of expected recovery rates.	Noted. See summary of comments.
90.	Lucida plc	3.11.	<p>The 40% assumption appears to be arbitrary in this context and excessively prudent. Whilst corporate defaults might lead to losses of 60%, reinsurers are regulated entities and losses on this scale by such an entity would suggest an extreme failure of the regulatory regime.</p> <p>Since the 40% cap will form the standard default assumption, it would be appropriate to give examples of when this should not be the case, for example where reinsurance has been obtained from an appropriately regulated entity.</p> <p>This comment also applies to 3.20.</p>	Noted. See summary of comments.
91.	Munich RE	3.11.	We believe that undertakings should be allowed to take into account particulars of their contracts. For example when considering reinsurance default provisions, risk mitigating measures (such as collateral requirements) in the contracts should be taken into account. Furthermore, to be consistent with CP51, it should be possible to deduct collateral from the projected recoveries before applying a recovery rate. We do not see a reason to change the recovery rate from 50% to 40% and hence would appreciate much	

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			more justification for the choice of a 40% recovery rate.	
92.			Confidential comment deleted.	
93.	PricewaterhouseCoopers LLP	3.11.	In this paragraph, there is a benchmark maximum recovery rate of 40% if there is no reliable estimate for the rate. It is noted that to ensure objectivity and comparability the degree of judgement over the rate should be restricted. We understand the sentiment, however, it is unclear what evidence there is to support a 40% restriction compared to any other benchmark. We also question whether this should be specified in Level 2 text as this may not be sufficiently flexible to allow for changes in future circumstances.	Noted. See summary of comments.
94.	ROAM	3.11.	No maximum recovery rates should be set, as very often reinsurance contracts contain provisions where an insurer can ask for collateral (sometimes cash deposits) when a reinsurer's rating drops below a certain level. In such cases, recovery rate may be as high as 100%.	Noted. See summary of comments.
95.	ACA	3.12.	When the collateral is higher than the losses-given default, does that mean that the adjustment becomes negative or should it be limited to null?	The adjustment should be limited to null.
96.	CEA	3.12.	The CEA asks for further specifications on how inclusion of mitigating instruments can be done in practice. Typo: first word should be "If" instead of "It".	Noted. Agreed. See revised text.
97.	CRO-Forum	3.12.	The CRO Forum believes these mitigating instruments should be allowed for in the effective recovery rate. See 3.11	Noted. The text should be read this way.
98.	DIMA (Dublin International Insurance & Management	3.12.	Mitigation by letters of credit and collateral is provided but the credit risk of instruments should be assessed and included.	Noted.

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99.	INTERNATIONAL GROUP OF P&I CLUBS	3.12.	See below under 3.21	Noted.
100.	International Underwriting Association of London	3.12.	Whilst we agree that reliable estimates of recovery rate might be difficult to achieve, we believe the maximum counterparty recovery rate of 40% might be excessively prudent, particularly when dealing with Solvency II regulated counterparties, particularly where those entities meet their SCR.	Noted. Please refer to the summary of comments
101.	Lloyd's	3.12.	We agree. Collateral is an important consideration.	Noted.
102.	Lucida plc	3.12.	We welcome the potential allowance for loss mitigation instruments. This comment also applies to 3.21.	Noted.
103.	Milliman	3.12.	Absent from the guidance but important, is that the implementation of mitigating instruments (e.g. LOC) should take place before the application of PD in a given scenario.	Noted. This is implied in the text.
104.	ACA	3.13.	The separate calculation (per line of business, kind of provision and counterparty) is really time-demanding. We would appreciate the possibility of applying simplifications.	Noted. See summary of comments.
105.	ABI	3.13.	Contribution from counterparty credit risk may be immaterial compared to other elements, making the proposed allocation a disproportionate effort. The segmentation requirements should be applied in a proportionate manner since it does only make sense if the allocated credit risk is material.	Not agreed. Please refer to the summary of the comments.
106.	Association of Run-off Companies	3.13.	We consider that the paper should refer to materiality being considered before drilling down to line of business and counterparty.	Not agreed

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107.	CEA	3.13.	Contribution from counterparty credit risk may be immaterial compared to other elements, making the proposed allocation a disproportionate effort. The segmentation requirements should be applied in a proportionate manner since it does only make sense if the allocated credit risk is material.	Not agreed. Please refer to the summary of the comments
108.	CRO-Forum	3.13.	<p>It should be up to the insurer whether to split credit risk provisions on counterparties by line of business, or premium and reserve risk. In most cases contribution from counterparty credit risk will be immaterial compared to other elements, making the allocation a disproportionate effort.</p> <p>Why is a difference per line of business required? A reinsurer has a rating based on the risk in its total portfolio and does not have a risk rating per line of business. If a reinsurer is active on a specific line of business which could imply more risk than other lines of business (f.e. liability) this should be reflected in its rating.</p>	Not agreed. Please refer to the summary of the comments. The split into lines of businesses should reflect the risk exposure of the insurer itself.
109.	Lloyd's	3.13.	We agree that is desirable to calculate the counterparty default adjustment by line of business and counterparty. However, the principle of proportionality needs to be considered carefully and we welcome the proposed simplification (which allows counterparties to be grouped) in para 3.14.	Noted.
110.	Munich RE	3.13.	<p>There is no need to calculate the adjustment per line of business and separately for non-life premium provisions and non-life claims provisions. The dependence of the probability of default on the counterparty is driving the risk. Hence, only this dependency should be taken into account. If there are different reinsurance programs for different LoB's this is reflected in the exposure, i.e. in the loss given default.</p> <p>In most cases contribution from counterparty credit risk will be</p>	Not agreed. Please refer to the summary of the comments. The split into lines of businesses should reflect the risk exposure of the insurer itself.

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			immaterial compared to other elements, making the allocation a disproportionate effort.	
111.	ROAM	3.13.	Contribution from counterparty credit risk may be immaterial compared to other elements, making the proposed allocation a disproportionate effort.	Not agreed. Please refer to the summary of the comments
112.	ABI	3.14.	We agree with CEIOPS it should be possible to calculate the adjustment for all counterparties of equal credit characteristics as it would be unduly onerous to require a separate calculation of each counterparty.	Noted.
113.	CEA	3.14.	This is a very important statement and we do support this point, given the difficulties in calculating LGD and PD.	Noted.
114.	Deloitte European Union member firms of Deloitte	3.14.	<p>We disagree with the use of such adjustment without taking into account the portfolio effect (diversification and interdependency) of the difference recoverable an insurance undertaking could have in its balance sheet.</p> <p>We consider that such adjustment should take into consideration the correlation risk (interdependency) between reinsurance companies, which could be provided by products such as first to default or second to default, where financial institutions could provide cotes and reliable pricing.</p>	Noted. Not in scope of CP 44.
115.	GDV	3.14.	This is a very important statement and we do support this point, given the difficulties in calculating LGD and PD.	Noted.
116.	Groupe Consultatif	3.14.	CP 51 provides more detail on the simplification in case of a high number of counterparties. We assume that the same simplification may be used to the calculation of the technical provision.	Noted. See summary of comments.
117.	Lloyd's	3.14.	We strongly agree that simplifications are appropriate for splitting the adjustment between lines of business and counterparties.	Noted.
118.			Confidential comment deleted.	

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119.	ROAM	3.14.	We do support this point which we find relevant, following the difficulties in calculating LGD and PD.	Noted.
120.	ABI	3.15.	We believe mitigating instruments should also be recognised in the definition of loss given default.	Please refer to 3.21
121.	CEA	3.15.	<p>The wording is potentially confusing.</p> <p>In first sentence it is stated that the counterparty default adjustment should approximate the 'present value of losses-given default', but then in the second sentence 'loss-given default' is itself defined as a present value.</p> <p>Mitigating instruments should also be recognised in the definition of loss given default.</p> <p>The CEA recommends revising the wording as follows: "The adjustment for counterparty default should approximate the expected present value of the losses-given default of the counterparty, weighted with the probability of default of the counterparty. The loss-given default should be derived as the change in value resulting from the default at that point in time, i.e. the reduction caused by default in the value of future cash flows from the counterparty. Instruments, like collaterals and letter of credit, mitigating the loss given default should be also included in the calculation of the change in value."</p> <p>It should be finally added that the proposed approach is aiming for a market consistent price of the recoverable.</p>	<p>Agreed. See revised text.</p> <p>Please refer to 3.21</p> <p>Noted. See amendments in the explanatory text</p>
122.	GDV	3.15.	<p>The wording is potentially confusing.</p> <p>In first sentence it is stated that the counterparty default adjustment should approximate the 'present value of losses-given default', but then in the second sentence 'loss-given default' is itself defined as a present value.</p>	Please refer to comment 121

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			<p>Mitigating instruments should also be recognised in the definition of loss given default.</p> <p>The GDV recommends revising the wording as follows: "The adjustment for counterparty default should approximate the expected present value of the losses-given default of the counterparty, weighted with the probability of default of the counterparty. The loss-given default should be derived as the change in value resulting from the default at that point in time, i.e. the reduction caused by default in the value of future cashflows from the counterparty. Instruments, like collaterals and letter of credit, mitigating the loss given default should be also included in the calculation of the change in value."</p> <p>It should be finally added that the proposed approach is aiming for a market consistent price of the recoverable.</p>	
123.	Munich RE	3.15.	It should be stressed that the market consistent value of the recoverable is the ultimate goal of the exercise.	Noted. See amendments in the explanatory text
124.	RBS Insurance	3.15.	Agreed. To avoid doubt we believe that loss given default should be net of expected payments due to the counterparty, if any. (eg- if the reinsurer is expected to default on the loss recovery, then the corresponding reinstatement premium would not be paid to the reinsurer).	Noted.
125.	ROAM	3.15.	<p>The wording is potentially confusing.</p> <p>In first sentence it is stated that the counterparty default adjustment should approximate the 'present value of losses-given default', but then in the second sentence 'loss-given default' is itself defined as a present value.</p> <p>Mitigating instruments should also be recognised in the definition of loss given default.</p>	Please refer to comment 121

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			<p>ROAM recommends revising the wording as follows: "The adjustment for counterparty default should approximate the expected present value of the losses-given default of the counterparty, weighted with the probability of default of the counterparty. The loss-given default should be derived as the change in value resulting from the default at that point in time, i.e. the reduction caused by default in the value of future cash flows from the counterparty. Instruments, like collaterals and letter of credit, mitigating the loss given default should be also included in the calculation of the change in value."</p> <p>It should be finally added that the proposed approach is aiming for a market consistent price of the recoverable.</p>	
126.	ACA	3.16.	<p>First, taking into account the whole run off period seems contradictory with a one year horizon for the standard model. Secondly, a multiyear horizon needs very complex calculations to project cash flows and to estimate the probability of default at each period.</p>	Not agreed. The approach is in line with the best estimate.
127.	CEA	3.16.	<p>Following from valuation principles, we agree that the whole run-off period needs to be considered.</p>	Noted.
128.	FFSA	3.16.	<p>Note- no text in original comment</p>	
129.			<p>Confidential comment deleted.</p>	
130.	GDV	3.16.	<p>Following from valuation principles, we agree that the whole run-off period needs to be considered.</p>	Noted.
131.	Lloyd's	3.16.	<p>We agree.</p>	Noted.
132.	Munich RE	3.16.	<p>Valuation principles demand that the whole run-off period is</p>	Noted.

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			considered.	
133.	RBS Insurance	3.16.	We agree that assessing a credit risk during the whole run-off period (to ultimate) is logical.	Noted.
134.	ROAM	3.16.	We agree that the whole run-off period needs to be considered.	Noted.
135.	ACA	3.17.	How to estimate a default probability from these informations? A table for the default probability corresponding to each rating already exists, but what about "the financial reporting of the counterparty" for example? Many interpretations are possible. We also note a lack of precision about the particularity of inter-group reinsurance and non-proportional treaties, especially in non-life activity.	Noted. See summary of comments.
136.	ABI	3.17.	We believe the requirement for 'current, reliable and credible information' need to be applied with flexibility. In particular, it may be particularly problematic assessing whether the information used by a third party in their assessment is current, reliable and credible. There may be commercial sensitivity about opening up the third party approach to this level of scrutiny. In IFRS 4 a set of criteria has been introduced in order to assess the reliability of information for accounting purpose. Based on the text of the Directive attempting to have the calculation of technical provision in line with developments in accounting, we urge CEIOPS to consider these criteria in defining the reliability of information. See comments under 3.6	Noted. Please refer to the summary of comments.
137.			Confidential comment deleted.	
138.	CEA	3.17.	The assessment for reliability and credibility of information needs further specification while respecting the proportionality principle. The current form of this assessment is overly burdensome. For example, the requirement, as presented by the paper, could lead in	Noted. See amendments in the text.

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			<p>case of smaller undertakings to the creation of specialized credit departments which would be too costly.</p> <p>A set of criteria is commonly used in order to assess the reliability of information for accounting purpose: faithful representation, economic reflection of the substance of transactions, neutrality, prudence and completeness in all material aspects. Based on the text of the Directive attempting to have the calculation of technical provision in line with developments in accounting, we urge Ceiops to consider these criteria in defining the reliability of information.</p>	
139.	CRO-Forum	3.17.	<p>The current text suggests a very burdensome process to follow when assessing the counterparty default risk for each counterparty. Care should also be used when looking at the information credit ratings are with respect to the willingness and ability of counterparties to repay their amounts due to policyholders.</p> <p>'The undertaking should not rely on information of a third party without assessing that the information is current, reliable and credible'. This could potentially place considerable burden on companies to constantly check ratings applied by the rating agencies - a realistic approach is needed here.</p>	Noted. Please refer to the summary of comments.
140.	FFSA	3.17.	<p>CEIOPS says that "the undertaking should not rely on information of a third party without assessing that the information is current, reliable and credible."</p> <p>FFSA asks for a clarification of the criteria companies have to check before using third party information. Either the check can be based upon information publicly disclosed, or it may require more complex studies. This clarification would also help the main information providers to set their information publications to an appropriate level.</p> <p>Furthermore, special attention should be paid for counterparty subject to Solvency II rules. A clear distinction should be made</p>	Noted. Please refer to the summary of comments.

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			between counterparties covering their SCR and the others (not covering or excluded for the Solvency II perimeter). A higher recovery rate should be used for covering their SCR.	
141.	GDV	3.17.	<p>The assessment for reliability and credibility of information needs further specification while respecting the proportionality principle. The current form of this assessment is overly burdensome. For example, the requirement, as presented by the paper, could lead in case of smaller undertakings to the creation of specialized credit departments which would be too costly.</p> <p>A set of criteria is commonly used in order to assess the reliability of information for accounting purpose: faithful representation, economic reflection of the substance of transactions, neutrality, prudence and completeness in all material aspects. Based on the text of the Directive attempting to have the calculation of technical provision in line with developments in accounting, we urge CEIOPS to consider these criteria in defining the reliability of information.</p>	Noted. See amendments in the text.
142.	Groupe Consultatif	3.17.	There could be a wide range of interpretations in deriving the needed parameters	Noted.
143.	Lloyd's	3.17.	We agree and suggest there is consistency in approaches when estimating probabilities of default for technical provisions outlined in CP44 and those for the SCR outlined in CP51	Noted. Please refer to the summary of comments.
144.			Confidential comment deleted.	
145.	RBS Insurance	3.17.	It is onerous to assess each counterparty individually, particularly for prior treaty years and less significant counterparties. Materiality needs to be applied so that, for example, the use of rating agency default probability assessment is allowable without independent individual verification for small counterparties.	Noted.
146.	ROAM	3.17.	The need for reliable and credible information is excessively demanding: it is burdensome, if not impossible, to assess that the	Noted. Please refer to the summary of comments.

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			<p>information provided by a third party is current, reliable and credible.</p> <p>Such a requirement could lead in case of smaller undertakings to the creation of specialized credit departments. Consequently this requirement should be interpreted in a flexible manner.</p> <p>ROAM asks for a clarification of the criteria companies have to check before using third party information. Either the check can be based upon information publicly disclosed, or it may require more complex studies. This clarification would also help the main information providers to set their information publications at an appropriate level.</p> <p>Furthermore, special attention should be paid to counterparties subject to Solvency II rules. A clear distinction should be made between counterparties covering their SCR and the others (not covering or excluded for the Solvency II perimeter). A higher recovery rate should be used for those covering their SCR.</p>	
147.	SOGECORE	3.17.	<p>We strongly support this article as insofar it should give ground to the CEIOPS to state that undertakings that respect their solvency requirements under Solvency II should be entitled to claim for a set probability of default, even if not having a rating.</p> <p>Should also be added the possibility, if the rating of a counterparty can not be found, that the rating of the mother company can be used if available.</p>	<p align="center">Noted.</p> <p align="center">Not agreed, as the mother company could have a different rating.</p>
148.	ACA	3.18.	<p>Could you better explain the terms "point-in-time" and "through-the-cycle"?</p>	<p align="center">Noted. Please refer to clearer structure in the text.</p>
149.	AMICE	3.18.	<p>This consultation paper does not make any reference to the simplification used in the QIS4. AMICE members wonder whether CEIOPS will include such simplification in Level 2.</p> <p>AMICE members would prefer to have "through-the cycle</p>	<p align="center">Noted. Please refer to the summary of comments.</p>

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			estimates" rather than point-in-time estimates.	
150.	ABI	3.18.	See comments under 3.8	Noted.
151.			Confidential comment deleted.	
152.	CEA	3.18.	<p>The CEA preferred approach is the use of through the cycle estimates.</p> <p>Point-in-time estimates may be distorted by crisis conditions (see current crisis) that will not persist over the longer term. For example, most commentators expect defaults to be significantly higher than in normal conditions over the next few years but then revert to historic average levels. The use of such estimates would thus introduce more volatility compared to through-the-cycle probabilities and would generate pro-cyclical effects.</p>	Noted. Please refer to the summary of comments.
153.	CRO-Forum	3.18.	<p>Point-in-time calibration leads to pro-cyclicality. In addition, even the best point-in-time PD models are not able to react in time before a turn in the cycle. It would therefore be more appropriate to use through-the-cycle calibrations</p> <p>We would question whether 'point-in-time' estimates are ever reliable, objective and prudent?</p>	Not agreed. Please refer to the summary of the comments.
154.	FFSA	3.18.	<p>CEIOPS states that the point-in-time estimates should be the default approach for the calculation of the probability of default but acknowledges that it shall be possible to use the through-the-cycle estimates if the first approach is not possible to calculate in a reliable, objective and prudent manner.</p> <p>FFSA considers that the preferred approach should be the through-the-cycle estimates, as it uses a long term historical data which is more appropriate. Besides the fact that the point-in-time approach is burdensome, it introduces more volatility.</p>	Not agreed. Please refer to the summary of the comments.
155.	GDV	3.18.	The GDV preferred approach is the use of through the cycle	Not agreed. Please refer to the

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			<p>estimates.</p> <p>Point-in-time estimates may be distorted by crisis conditions (see current crisis) that will not persist over the longer term. For example, most commentators expect defaults to be significantly higher than in normal conditions over the next few years but then revert to historic average levels. The use of such estimates would thus introduce more volatility compared to through-the-cycle probabilities and would generate pro-cyclical effects.</p>	summary of the comments.
156.	Lloyd's	3.18.	We agree.	Noted.
157.			Confidential comment deleted.	
158.	PricewaterhouseCoopers LLP	3.18.	See comment under 3.7.	Noted.
159.	ROAM	3.18.	<p>ROAM preferred approach is the use of through the cycle estimates.</p> <p>Point-in-time estimates may well be distorted by the conditions then applying that may not persist over the longer term. For example, most commentators expect defaults to be significantly much higher than usual over the next few years but then revert to historic average levels. The use of such estimates would thus introduce more volatility compared to through-the-cycle probabilities and would generate pro-cyclical effects.</p>	Not agreed. Please refer to the summary of the comments.
160.			Confidential comment deleted.	
161.	CEA	3.19.	<p>It would be clearer to refer to cumulative probability increasing as the time horizon increases.</p> <p>In 3.5 Ceiops correctly explains that multiplying a single probability of default to the sum of future cash-flows is inappropriate as the probability of default is an annual rate and if the time horizon of the reinsurance is longer than this it will not capture the risk of default</p>	Agreed. See revised text.

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			<p>in future years. However, the wording used in 3.19 is a bit ambiguous.</p> <p>The CEA recommends the following wording revision: "The assessment of the probability of default should take into account the fact that the cumulative probability increases with the time horizon of the assessment."</p>	
162.	CRO-Forum	3.19.	<p>This paragraph is redundant given the requirement of 3.16. It could be confused as implying that the annual rate of default is expected to increase over time, which is not the case. 3.10 makes this clear but the standalone advice does not.</p>	Noted. See revised text.
163.	GDV	3.19.	<p>It would be clearer to refer to cumulative probability increasing as the time horizon increases.</p> <p>In 3.5 CEIOPS correctly explains that multiplying a single probability of default to the sum of future cash-flows is inappropriate as the probability of default is an annual rate and if the time horizon of the reinsurance is longer than this it will not capture the risk of default in future years. However, the wording used in 3.19 is a bit ambiguous.</p> <p>The GDV recommends the following wording revision: "The assessment of the probability of default should take into account the fact that the cumulative probability increases with the time horizon of the assessment."</p>	Agreed. See revised text.
164.	Lloyd's	3.19.	<p>We agree.</p>	Noted.
165.	ACA	3.20.	<p>We saw that the counterparty default probability depends on the time (§3.19) and on the amount (§3.9). But the Recovery Rate is fixed although it depends also on the amount of the recoverables.</p> <p>It seems impossible to estimate the rate of recovery because of lacks of statistics. The standard model might fix these parameters (x% for insurance counterparties and y% for financial derivatives/</p>	Noted.

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			structured financial products). In QIS 4 these two rates were fixed to 50%.	
166.	AMICE	3.20.	We suggest a recovery rate by default of 60% rather than 40%. Where there is no information available, there is as much probability of being higher than being lower than 60%.	Noted. Please refer to the summary of comments.
167.	ABI	3.20.	<p>We disagree with CEIOPS requirement of an effective 40% cap on recovery rates. We believe recovery rates will sometimes be higher (collateral, cash collateral) and this should not therefore become a benchmark. In practice, where it is justified and documented, it should be possible to have a higher recovery rate. The recovery rate should depend on the level of collateral backing the treaty (as outlined in 3.12 and 3.21). Inter – group reinsurances may also require separate consideration.</p> <p>In addition, the 40% being proposed is the same as for the stressed conditions in CP51 and so appears to be unreasonably low. We would expect a higher recovery rate under best estimate conditions compared to stressed conditions.</p>	Noted. Please refer to the summary of comments.
168.	Association of Run-off Companies	3.20.	As per 3.11, can the use of a maximum recovery rate of 40% be justified?	Noted. Please refer to the summary of comments.
169.	CEA	3.20.	<p>The CEA is concerned by the absence of a clear explanation of what is considered a reliable estimate. This creates a risk that, in practice, the cap could be used systematically in an excessively prudent manner.</p> <p>The default 40% recovery rate is the same as that proposed for the loss-given-default calculations under the SCR (see 3.106 in CP51) and is lower than the 50% figure used in QIS4. Recovery rates are, as might be expected, lower during adverse economic conditions than in more benign economic conditions. The CEA reminds that the crisis has not indicated any worsening of the reinsurer recovery</p>	Noted. Please refer to the summary of comments.

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			<p>rate. Consequently for cases where there is no reliable information available, the recovery rate of 50% from QIS4 would be more appropriate.</p> <p>In practice recovery rates vary significantly depending upon the seniority of the debt. For example, average rates for senior secured debt are 60% to 70% falling to about 20% for junior subordinated debt. Also such rates are influenced by provisions triggering collateral setting following certain circumstances.</p> <p>Furthermore, special attention should be paid for counterparty submitted to Solvency II rules. A clear distinction should be made between counterparties covering their SCR and the others (not covering or excluded for the Solvency II perimeter). A higher recovery rate than 50% should be allowed for undertakings covering their SCR.</p> <p>The CEA argues for no maximum recovery rate and use of undertaking specific rates, if such rates can be well justified and documented.</p>	
170.	CRO-Forum	3.20.	<p>The CRO forum believes that undertakings should be allowed to take into account particulars of their contracts. For example when considering reinsurance default provisions, risk mitigating measures (such as collateral requirements) in the contract should be taken into account. Furthermore, to be consistent with CP51, it should be possible to deduct collateral from the projected recoveries before applying a recovery rate. Risks covered by SPVs need to reflect the protection provided by the fully funded criteria</p> <p>The CRO forum would like more justification for the choice of a 40% recovery rate. This is in line with our response to CP51 paragraph 3.44.</p> <p>We propose that rather than setting an arbitrary recovery rate the recovery rate should be set using similar/ related paper available in</p>	Noted. Please refer to the summary of comments.

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			the market.	
171.	DIMA (Dublin International Insurance & Management	3.20.	Lack of reliable data leads to conclusion that if no reliable estimate of the recovery rate of a counterparty is available, no rate higher than 40% should be used. No justification for the use of 40% as the maximum recovery rate is being given.	Noted. Please refer to the summary of comments.
172.	FFSA	3.20.	<p>CEIOPS outlines that if the undertaking cannot provide with a reliable estimate of the recovery rate, it couldn't use a rate higher than 40%.</p> <p>FFSA would like to understand how this cap of 40% was derived and would like to specifically understand the reasons for setting a figure that is lower than the 50% used in QIS4.. Furthermore, the FFSA reminds that the crisis has not indicated any worsening of the reinsurer recovery rate. In addition, FFSA is concerned by the absence of a clear indication as to what will be considered a reliable estimate. This creates a risk that, in practice, the cap could be used systematically in an excessively prudent manner</p> <p>FFSA suggests using a recovery rate by default of 50% (as in QIS4), rather than 40%, and a recovery rate higher than 50% for counterparties covering their SCR under solvency II</p>	Noted. Please refer to the summary of comments.
173.			Confidential comment deleted.	
174.	GDV	3.20.	<p>The GDV is concerned by the absence of a clear explanation of what is considered a reliable estimate. This creates a risk that, in practice, the cap could be used systematically in an excessively prudent manner.</p> <p>The default 40% recovery rate is the same as that proposed for the loss-given-default calculations under the SCR (see 3.106 in CP51) and is lower than the 50% figure used in QIS4. Recovery rates are, as might be expected, lower during adverse economic conditions</p>	Noted. Please refer to the summary of comments.

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			<p>than in more benign economic conditions. The GDV reminds that the crisis has not indicated any worsening of the reinsurer recovery rate. Consequently for cases where there is no reliable information available, the recovery rate of 50% from QIS4 would be more appropriate.</p> <p>In practice recovery rates vary significantly depending upon the seniority of the debt. For example, average rates for senior secured debt are 60% to 70% falling to about 20% for junior subordinated debt. Also such rates are influenced by provisions triggering collateral setting following certain circumstances.</p> <p>Furthermore, special attention should be paid for counterparty submitted to Solvency II rules. A clear distinction should be made between counterparties covering their SCR and the others (not covering or excluded for the Solvency II perimeter). A higher recovery rate than 50% should be allowed for undertakings covering their SCR.</p> <p>The GDV argues for no maximum recovery rate and use of undertaking specific rates, if such rates can be well justified and documented.</p>	
175.	GROUPAMA	3.20.	We suggest a recovery rate by default of 50% rather than 40%. In case of no available information there is as much probability of being higher than being lower than 50%.	Noted. Please refer to the summary of comments.
176.	Groupe Consultatif	3.20.	Subject to understanding the source data, we believe the recovery cap of 40% to be excessively prudent, particularly if applied to supervised counterparties.	Noted. Please refer to the summary of comments.
177.	INTERNATIONAL GROUP OF P&I CLUBS	3.20.	<p>The IG notes the advice that if no reliable estimate of the recovery rate of a counterparty balance is available, no rate higher than 40% should be used.</p> <p>The 40% figure is discussed in 3.11, which states that there is little</p>	

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			empirical data about rates of recovery, that estimates of such figure would be unreliable, and that for these reasons, if no reliable estimate is available, the 40% figure should be used as the maximum recovery. While we understand the temptation for supervisors to seek greater certainty in the aftermath of the recent financial crisis, the rationale for the increase in the loss given default from 50% to 60% is sketchy and the statement that credit risk was underestimated in the past is hardly justification for the reduction in assumed recovery rate. We suggest that more work should be done in this area (not just in light of the current financial crisis) and that where industry sectors have particular security or offset arrangements which reduce the loss given default and can support different factors with reliable data, industry specific loss given defaults should be used.	
178.	International Underwriting Association of London	3.20.	Please refer to our comment on Paragraph 3.12.	Noted.
179.	Ireland's Solvency 2 Group, excluding representa	3.20.	No justification is given for proposing 40% as the maximum recovery rate, where no reliable estimate of the recovery rate of a counterparty is available.	Noted. Please refer to the summary of comments.
180.	Lloyd's	3.20.	We do not agree with the 40% maximum rate suggested. Market studies of recovery rates from past insurance/reinsurance failures support a maximum rate of 50% (as used in QIS4). Information on recovery rates from failed insurance/reinsurance entities should be taken into account in the derivation of expected recovery rates.	Noted. Please refer to the summary of comments.
181.	Munich RE	3.20.	The recovery rate should be set consistent to the procedure	Noted. Please refer to the

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			outlined in CP51. There it is argued that the calibration parameters are preliminary set to 40%. However, we see no reason to change the 50% used in the QIS studies to 40% and hence advocate to set the recovery rate to 50% especially as we do not see any evidence due to the financial crisis to change this approach.	summary of comments.
182.	OAC Actuaries and Consultants	3.20.	We consider that the assumption of the maximum recovery of 40% is too low, particularly in the context of an entity regulated under Solvency 2. This may discourage firms from writing business which they wish to reinsure because of the onerous capital requirements	Noted. Please refer to the summary of comments.
183.			Confidential comment deleted.	
184.	PricewaterhouseCoopers LLP	3.20.	See comment under 3.11	Noted.
185.	RBS Insurance	3.20.	We disagree with CEIOPS requirement of an effective 40% cap on recovery rates where there is no reliable estimate.	Noted. Please refer to the summary of comments.
186.	ROAM	3.20.	<p>ROAM is concerned by the absence of a clear explanation of what is considered a reliable estimate. This creates a risk that, in practice, the cap could be used systematically in an excessively prudent manner.</p> <p>The default 40% recovery rate is the same as that proposed for the loss-given-default calculations under the SCR (see 3.106 in CP51) and is lower than the 50% figure used in QIS4. Recovery rates are, as might be expected, lower during adverse economic conditions than in more benign economic conditions. The ROAM reminds that the crisis has not indicated any worsening of the reinsurer recovery rate.</p> <p>In practice recovery rates vary significantly depending upon the seniority of the debt. For example, average rates for senior secured debt are 60% to 70% falling to about 20% for junior subordinated</p>	Noted. Please refer to the summary of comments.

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			<p>debt. Also such rates are influenced by provisions triggering collateral setting following certain circumstances.</p> <p>ROAM suggests using a recovery rate by default of 50% (as in QIS4), rather than 40%, and a recovery rate higher than 50% for counterparties covering their SCR under solvency II</p>	
187.	SOGECORE	3.20.	We also support this article but we would like to add that the judgement over reliability is subjective.	Noted.
188.	XL Capital Ltd	3.20.	<p>"If no reliable estimate of the recovery rate of a counterparty is available, no rate higher than 40% should be used"</p> <p>We support the principle of capping the rate to 40%. We also believe that recovery rates will sometimes be higher (collateral, cash collateral) and well justified and documented, and these cases, it should be possible to have a higher recovery rate.</p>	Noted.
189.	AMICE	3.21.	AMICE members disagree that when the determination of the adjustment for counterparty default allows for the effect of risk mitigating instruments (i.e collaterals or letters of credit), then the credit risk of the instruments should be allowed for. We believe that this is a marginal risk and should not be considered.	Not agreed.
190.	ABI	3.21.	Reinsurance could cover a number of lines of business (e.g. Property treaty covering Household and Commercial lines of business). It would be more appropriate to calculate the counterparty default at the treaty rather than the line of business level.	Not agreed.
191.	Association of Run-off Companies	3.21.	Many run-off companies, by their nature, may have inter-group guarantees or other arrangements group for protection. These should be considered in this paragraph.	Not agreed. Not in scope of the paper.
192.	FFSA	3.21.	CEIOPS reintroduces a credit risk on the collaterals in the calculation of the adjustment of counterparty default in the best estimate while we have mails of the Commission which had	Noted.

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			admitted our argument which was that counterparties shall have to complete their collaterals at any time if the value was reduced, there was only an extremely marginal risk of simultaneity equal to the product of the default rates.	
193.	INTERNATIONAL GROUP OF P&I CLUBS	3.21.	The IG welcomes the allowance for 'risk mitigating instruments', including collateral, in the determination of counterparty default risk. While para. 3.21 refers to the need to calculate the credit or other risk associated with the risk mitigation instrument, the CP is silent on the subject of how this should be done in practice.	Noted.
194.	ROAM	3.21.	CEIOPS reintroduces a credit risk on the collaterals in the calculation of the adjustment of counterparty default in the best estimate. Please note that in exchanges with the Commission, the Commission agreed with our argument which was that counterparties shall have to complete their collaterals at any time if the value was reduced, there was only an extremely marginal risk of simultaneity equal to the product of the default rates. ROAM asks CEIOPS to remove this paragraph.	Noted. Not agreed.
195.	ACA	3.22.	Calculating LGD for each LOB and each counterparty (or group of counterparties with a same rating class) seems too complex. The principle of proportionality should be allowed for small companies.	Not agreed. Please refer to the summary of the comments
196.	AMICE	3.22.	Splitting the capital requirements for each counterparty and for each line of business is very demanding and adds little value. We suggest this paragraph be deleted.	Not agreed. Please refer to the summary of the comments
197.	ABI	3.22.	We believe the approach proposed for the calculation of the adjustment for counterparty default (calculated separately at least for each line of business and each counterparty) to be too burdensome, and for a very limited added value. Undertakings should be able to calculate their adjustment for counterparty	Not agreed. Please refer to the summary of the comments

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			default at aggregate level, in particular where there is a significant number of counterparties.	
198.	CEA	3.22.	<p>The requirements to distinguish by each line of business and counterparty will result in a big amount of estimations and are thus burdensome, require disproportionate effort and add little value, because of the problem of deriving reliable default parameters.</p> <p>We attract attention that it may be inappropriate to split some types of reinsurance cover by line of business, e.g. stop loss reinsurance.</p> <p>Normal practice would be to combine similarly rated counterparties and do an aggregate calculation.</p> <p>It is not current practice to split the calculations for non-life between premium provisions and claim provisions In line with our answer on CP39 on para 3.216, the classification of reinsurance recoverables into premium provisions and claims provisions needs refinement in order to come up with appropriate calculation for the adjustments to these split recoverables.</p> <p>The CEA recommends the following wording revision: "Where it results in materially different results and subject to proportionality, the adjustment for counterparty default should be calculated separately for each line of business and each counterparty". Further, simplifications, like the ones based on the duration of future payoffs, could be implemented.</p>	<p>Not agreed. Please refer to the summary of the comments</p> <p align="center">Noted.</p> <p>Not agreed. The message is included implicitly.</p>
199.	CRO-Forum	3.22.	<p>It should be up to the insurer whether to split credit risk provisions on counterparties by line of business, or premium and reserve risk. In most cases contribution from counterparty credit risk will be immaterial compared to other elements, making the allocation a disproportionate effort.</p>	<p>Not agreed. Please refer to the summary of the comments</p>
200.	Deloitte	3.22.	<p>Out of proportionality, we suggest that calculation not on line of</p>	<p>Noted. (Cf. 3.23)</p>

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	European Union member firms of Deloitte		business level but for aggregated data could be allowed specially for small lines. Also applied to 3.23.	
201.	FFSA	3.22.	<p>CEIOPS states that the adjustment for counterparty default should be calculated separately for each line of business and each counterparty.</p> <p>FFSA understands that a separate calculation could better estimate the loss-given-default during the run-off period, because the payment pattern in each line of business is different. But the calculation by line of business and by counterparty is quite burdensome for the undertaking. FFSA recommends a simplification, which could be based on the duration of futures payoffs.</p>	Noted. Please refer to the summary of comments.
202.			Confidential comment deleted.	
203.	GDV	3.22.	<p>The requirements to distinguish by each line of business and counterparty will result in a big amount of estimations and are thus burdensome, require disproportionate effort and add little value, because of the problem of deriving reliable default parameters.</p> <p>We attract attention that it may be inappropriate to split some types of reinsurance cover by line of business, e.g. stop loss reinsurance.</p> <p>Normal practice would be to combine similarly rated counterparties and do an aggregate calculation.</p> <p>It is not current practice to split the calculations for non-life between premium provisions and claim provisions In line with our answer on CP39 on para 3.216, the classification of reinsurance recoverables into premium provisions and claims provisions needs</p>	<p>Not agreed. Please refer to the summary of the comments</p> <p align="center">Noted.</p>

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			<p>refinement in order to come up with appropriate calculation for the adjustments to these split recoverables.</p> <p>The GDV recommends the following wording revision: "Where it results in materially different results and subject to proportionality, the adjustment for counterparty default should be calculated separately for each line of business and each counterparty". Further, simplifications, like the ones based on the duration of future payoffs, could be implemented.</p>	Not agreed. The message is included implicitly.
204.	Groupe Consultatif	3.22.	The distinction for each line of business and counterparty could result in a big amount of estimations with only a little gain of real world information because of the problem of deriving reliable default parameters.	Noted. Please refer to the summary of comments.
205.	Lloyd's	3.22.	We agree that is desirable to calculate the counterparty default adjustment by line of business and counterparty. However, the principle of proportionality needs to be considered carefully and we welcome the proposed simplification (which groups counterparties) in para 3.23.	Noted.
206.	Munich RE	3.22.	<p>There is no need to calculate the adjustment per line of business and separately for non-life premium provisions and non-life claims provisions. The dependence of the probability of default on the counterparty is driving the risk. Hence, only this dependency should be taken into account. If there are different reinsurance programs for different LoB's this is reflected in the exposure, i.e. in the loss given default.</p> <p>In most cases contribution from counterparty credit risk will be immaterial compared to other elements, making the allocation a disproportionate effort.</p>	Not agreed. Please refer to the summary of the comments.
207.			Confidential comment deleted.	
208.	Pricewaterho	3.22.	There is a requirement in this paragraph to calculate "the	Not agreed. CP 27 also states

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	useCoopers LLP		adjustment for counterparty default separately at least for each line of business and each counterparty.” We note that reinsurance arrangement may span and interact across the lines of business (as defined in Consultation Paper 27). Consequently, it may not be appropriate to calculate the adjustment as this level of granularity.	that technical provisions of insurers have to be calculated by LoBs. So the same should be true for counterparty default adjustment.
209.	RBS Insurance	3.22.	This would be an extremely onerous calculation for very limited added value. For example, if a simulation approach is taken for reinsurance recoveries for large motor or liability claims, say, then much more information would need to be stored for each simulation in order to keep a credit risk number for each counterparty for each claim at each point in time. Also the data requirements are large, for example, for catastrophe reinsurance, probabilities of default and loss given default are required, independently verified, by reinsurer, varying by size of underlying market loss.	Noted. Please refer to the summary of the comments.
210.	ROAM	3.22.	Splitting the capital requirements for each counterparty and for each line of business is very demanding and adds little value. We suggest this paragraph to be deleted.	Not agreed.
211.	XL Capital Ltd	3.22.	The requirement to calculate the counterparty default adjustment to recoverables from reinsurance contracts and SPVs separately for each line of business and each counterparty seems complex for the purposes of best estimate of technical provisions. We would welcome an option to calculate the adjustment at an aggregate level to avoid undue burden.	Noted. Cf to 3.23
212.	ACA	3.23.	How to calculate the adjustment when our counterparty is a pool of reinsurer and we only know the rating of the leading insurer? With § 3.17 we have the same difficulty than our comment.	Noted. Please refer to simplifications.
213.	AMICE	3.23.	We agree with this paragraph.	Noted.
214.	Association of Run-off	3.23.	The text at 3.14 refers to grouping counterparties of equal credit worthiness; the advice in 3.23 does not.	Noted.

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	Companies			
215.	CEA	3.23.	<p>As per the proportionality approach companies should be able to use this approach where it does not materially distort the results.</p> <p>The CEA recommends that in conjunction with the changes suggested for 3.22 the wording is changed as follows: "Where the probability of default and the recovery rates of several counterparties coincide, in line with the principle of proportionality the adjustment for the counterparty default for these counterparties can be calculated together."</p>	Noted. However, the formulation of the paragraph remains as the "undue burden" should be pointed out.
216.	Deloitte European Union member firms of Deloitte	3.23.	See comment on para. 3.22	Noted.
217.	GDV	3.23.	<p>As per the proportionality approach companies should be able to use this approach where it does not materially distort the results.</p> <p>The GDV recommends that in conjunction with the changes suggested for 3.22 the wording is changed as follows: "Where the probability of default and the recovery rates of several counterparties coincide, in line with the principle of proportionality the adjustment for the counterparty default for these counterparties can be calculated together."</p>	Noted. However, the formulation of the paragraph remains as the "undue burden" should be pointed out.
218.	Lloyd's	3.23.	We strongly agree that simplifications are appropriate for splitting the adjustment between lines of business and counterparties.	Noted.
219.	ROAM	3.23.	We agree with this paragraph	Noted.