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| | **Comments Template on**<br>**Consultation Paper on EIOPA's second set of advice to the European Commission on specific items in the Solvency II Delegated Regulation** | | **Deadline**<br>**5 January 2018**<br>**23:59 CET** |
| Name of Company: | Allianz Group | | |
| Disclosure of comments: | Please indicate if your comments should be treated as confidential: | | Public |
| | Please follow the following instructions for filling in the template:<br>⇨ <u>Do **not** change the numbering</u> in the column "reference"; if you change numbering, your comment cannot be processed by our IT tool<br>⇨ Leave the last column <u>empty</u>.<br>⇨ Please fill in your comment in the relevant row. If you have <u>no comment</u> on a paragraph or a cell, keep the row <u>empty</u>.<br>⇨ Our IT tool does not allow processing of comments which do not refer to the specific numbers below.<br>**Please send the completed template, <u>in Word Format</u>, to <u>CP-17-006@eiopa.europa.eu</u>**<br>**Our IT tool does not allow processing of any other formats.**<br><br>**<u>The numbering of the reference refers to the sections</u>** of the consultation paper on EIOPA's second set of advice to the European Commission on specific items in the Solvency II Delegated Regulation. Please indicate to which paragraph(s) your comment refers to. | | |
| **Reference** | **Comment** | | |
| General Comment | We welcome the opportunity to provide feedback on EIOPA's second set of advice to the European Commission on specific items in the Soilvency II Delegated Regulation.<br><br>In general we support the the feedback provided by the German Association of Insurers (GdV), Insurance Europe and the CRO and CFO Forum. Below those items are addressed where we want to provide additional detailed feedback. | | |

| | Comments Template on<br>Consultation Paper on EIOPA's second set of advice to the European Commission on specific items in the Solvency II Delegated Regulation | Deadline<br>5 January 2018<br>23:59 CET |
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| | Please note that the track-change modus has been used deliberately to indicate where amendments to the current legal wording are proposed. | |
| Introduction | | |
| 1.1 | | |
| 1.1.1 | | |
| 1.2.1 | | |
| 1.2.2 | | |
| 1.2.3 | | |
| 1.2.4 | | |
| 1.3 | | |
| 1.3.1 | | |
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| 1.3.5 | | |
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| 2.1 | | |
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| 2.4.1 | | |

| | Comments Template on Consultation Paper on EIOPA's second set of advice to the European Commission on specific items in the Solvency II Delegated Regulation | Deadline 5 January 2018 23:59 CET |
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| 2.4.2 | | |
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| 3.4.1 | | |
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| 4.5.2 | | |
| 4.5.3 | Agree with feedback from GDV that permanent disability scenario change from 1.5% to 3.5% is too high. | |
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| 5.5.1 | | |

| | Comments Template on<br>Consultation Paper on EIOPA's second set of advice to the European Commission on specific items in the Solvency II Delegated Regulation | Deadline<br>5 January 2018<br>23:59 CET |
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| 5.5.2.1 | | |
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| 8.4.1 | | |
| 8.4.2 | | |
| 8.4.3 | We welcome that EIOPA considers providing clarification on the application of the current legal provisions and do believe that such clarifications are indeed necessary. The feedback from the discussion paper makes clear that Article 186(2) to (5) of the Delegated Act leaves room for interpretation when determining the risk factor gi.<br><br>Article 186(2) provides provisions for the assignment of gi based on the solvency ratio. Since gi is assigned on the level of the single name exposure, which is defined to represent a corporate group, in our opinion only the group solvency ratio of an insurance group can be meant here.<br><br>When suggesting changes to the current rules EIOPA should also consider an approach where the risk factor gi is assigned based on the group solvency ratio for single name exposures that represent insurance groups.<br><br>An interpretation that Article 186(2) can only be applied, if the single name exposure comprises only exposures to a single unrated solo insurer, cannot be intended in our view. This would for example mean that a EUR 100.000.000 exposure to a single name exposure comprising only a single unrated solo insurer with a solvency ratio of 200% would get assigned a risk factor of 12%, but once an additional exposure of only EUR 1.000 is entered into with another counterparty in | |

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| | the same insurance group a risk factor of around 73% would need to be applied for the entire single name exposure. Consequently the risk charge would increase by a factor of 6 although the risk is still unchanged from an economic perspective.<br><br>Furthermore, we suggest that EIOPA reassesses the risk factor gi of 64.5% currently foreseen in Article 186(4) for unrated 3rd country insurance and reinsurance undertakings regulated under solvency regimes deemed equivalent. The reduced risk factor of 64.5% for such counterparties provides only for a small reduction of capital requirements (around 12%) compared to exposures with the highest possible risk factor of 73% in the module. Compared to the corresponding provisions in the counterparty default risk module where such exposures receive a PD of 0.5% instead of the maximum PD of 4.2%, the reduction of the risk factor in the concentration risk module for such counterparties appears fairly low. We suggest setting a lower risk factor gi for unrated 3rd country insurance and reinsurance undertakings.<br><br>With regard to point 573 of EIOPA’s advice we would like to point out that we do not see a need to alter the provisions in Article 199 of the Delegated Regulation, because in contrast to Article 186 Article 199(1) clearly describes how to determine a PD for a single name exposure based on the PDs assigned to the underlying exposures. | |
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| 10.4.2.2 | | |
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| 10.4.2.4 | | |
| 10.4.2.5 | | |
| 10.4.3 | In general we welcome EIOPA's work on unrated debt as part of the Solvency II review and EIOPA's proposals on how to allow for a more risk sensitive treatment of unrated debt in the Standard Model.<br><br>However, in particular the proposed "Internal assessment approach" appears to be fairly complex and burdensome to implement, especially when considering the quite limited part of the investments it may be applied to. We therefore see the risk that undertakings may not implement EIOPA's proposals for unrated debt.<br><br>With regard to the proposal on the usage of results of approved internal models, EIOPA's advice only covers the specific case of an insurer co-investing with an IRB bank. However, point 715 of the consultation paper states that similar considerations apply as well for the use of the results of an approved (partial) internal model developed by an insurer. We strongly suggest that EIOPA's advice is amended to also allow usage of internal ratings of an insurer that has received approval for a (partial) internal model. This should include the possibility of the use of such ratings when provided by regulated asset managers that originate unrated debt for insurers in a properly documented mandate. | |
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| 13.4.3 | In general we support EIOPA's proposal to amend the calculation of the loss-given-default on derivatives in order to recognize the economic effect from contractual netting agreements. A calculation of a loss-given-default for all derivatives that were concluded under a contractual netting agreement makes sense from an economic perspective and avoids issues like the artificial allocation of collateral, which is received on the level of the netted position, to individual derivatives.<br><br>With regard to the proposed adjustment of Article 107 of the Delegated Regulation we do understand that the simplification does not provide meaningful results if reinsurance recoverables are negative. However, we believe the application of the simplification should not be prevented by single reinsurance recoverables being negative. We would suggest to either restrict the use of the simplification to reinsurance arrangements with non-negative reinsurance revoverables or to introduce a floor in the formula in Article 107(1) in order to avoid that a negative risk-mitigation effect is determined in the case of negative reinsurance recoverables.<br><br>With regard to the proposed clarification of Article 110 of the Delegated Regulation we were not really able to understand the impact of the clarification proposed. In any case it should be avoided that the current scope of Article 110 is changed by adding clarifications that may only be | |

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| | reasonable for certain specific cases, but that may not be reasonable when applying Article 110 for other cases. | |
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| 14.4.3 | We strongly welcome EIOPA's proposals on how to quantify capital requirements for derivatives traded through a central counterparty in alignment with the approach applied in banking regulation. The proposals will ensure that the economic risk of such transactions is reflected in the SCR more appropriately.<br><br>Points 1161 and 1162 of EIOPA's advice are not very clear yet should be elaborated further. In particular more details on the calibration of the factors x, y and z should be provided. | |
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| 19.1 | **Allianz refers to and fully supports the comments on section 19 and 20 of the separate statements by the GDV, the CROF-CFOF, and Insurance Europe.**<br><br>To avoid repetition, Allianz focuses its comments on the wording suggestions for the relevant articles in the Delegated Regulation.<br><br>We greatly appreciate the recommended changes by EIOPA, in particular the waiver option in Article 70 bis. The waiver option reduces the risk of unintended consequences from the Principal Loss Absorbency Mechanism (PLAM) of RT1. However, we agree with the GDV, CROF-CFOF and Insurance Europe that additional changes are necessary to avoid all known risks yet.<br><br>**Two simple solutions for RT1**<br>Notwithstanding reputational and other considerations, RT1 gives the issuer the contractual right to cease all payments to investors forever. Aside from the value of RT1 from a capital point of view, such issuer rights and options and the resulting implied risks for investors (potentially in perpetuity) must be recognised. At any time, the issuer can decide to never repay the instrument, and to cancel all future coupon payments on a discretionary basis. At the same time, the issuer | |

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| | may pay equity dividends or undertake a share buy-back, as neither dividend pushers nor stoppers are allowed for RT1. While this is not how issuers will treat RT1 investors in normal situations (healthy solvency), RT1 investors do face the risk of being treated worse than equity investors, in particular if the issuer is in a crisis. This risk is especially true since the cancellation of equity dividends is economically cumulative, whereas RT1 coupon cancellation is truly non-cumulative (cancelled coupons are "lost" forever). While PLAM prohibits payments to RT1 investors, PLAM does not provide the issuer with any additional rights to stop payments beyond the rights already available. Since PLAM can have unintended consequences, and arguably does not increase the quality of capital, we see two simple alternative solutions:<br><br>***<u>Preferred solution</u>*****: PLAM should be eliminated or set at a fundamentally lower trigger level to only apply in true gone concern situations.** The trigger in Art. 71 (8) would need to be adapted accordingly. We note the risk that the Group MCR can be breached even though the group SCR ratio is still near or even above 100% (see the section on "trigger inversion " in the statements by the CROF-CFOF, GDV and Insurance Europe). Therefore, breach of the group MCR may happen in what should arguably be considered a going concern situation. It is worth mentioning in this context that Solvency II is substantially a mark-to-market regime, meaning that expectations of future losses are fully reflected in the MVBS and, consequently, in the relevant solvency ratios. This reinforces issues around "high" triggering levels and represents an important distinguishing factor compared to the regulatory regime for banks<br><br>***<u>Second best alternative:</u>*** **At a minimum, the PLAM waiver option should be extended to allow its application in any circumstances where a regulator deems a waiver as sensible.** This extension would provide flexibility for the supervisory authority to avoid unintended consequences. The waiver option should be available whenever PLAM would reduce any relevant trigger ratio. It should not matter what type of trigger has been breached, we are convinced that a further reduction of relevant solvency ratios at a time of crisis typically does not make sense. Reducing a relevant trigger ratio should be avoided potentially even where the Group MCR is breached (e.g. trigger inversion), or where the Group SCR ratio is below 75%. The waiver option should also be available for conversion. Finally, the waiver option should also allow the regulator to effect a | |

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| | partial write-down or conversion where sensible. | |
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| 19.4.4 | **New Art. 71 (5) bis:**<br>*(a) When ~~the single~~ a [1] trigger event listed in paragraph 8 ~~(c)~~[2] occurs ~~is met~~[1], and write down [3] can re-establish compliance with the relevant capital requirement~~SCR~~ [2] then partial write down [3] to restore compliance is sufficient [4].*<br>*(b) In all other cases,*<br>(i) *when the trigger event listed in paragraph 8 (c) occurs, the nominal or principal amount of the basic own-fund item as determined at original issuance is written down at least on a linear basis in a manner which ensures that full write down occurs at or before 75% coverage of the Solvency Capital Requirement is reached;~~.~~*<br>*(ii) when either of the trigger events listed in paragraph 8 (a) or (b) are met, the nominal or principal amount of the basic own-fund item is written down in full.*<br><br>**Explanation of the recommended changes:**<br>*[1] Wording alignment: "occurs" and deletion of "single* | |

- The wording of Art. 71 (5) bis (1)*(b)(i)* should also be used in Art. 71 (5) bis (1)*(a)*.

*[2] Focus on paragraph 8(c) risks unintended consequences of PLAM*

- The limitation of partial write-down to a paragraph 8(c) trigger event prohibits a partial write-down in case of (i) a MCR breach or (ii) where the SCR ratio is below 75%. This prohibition can lead to unintended consequences.
- The worked example below demonstrates such an unintended consequence for the particular case of a Group MCR breach (with trigger inversion) in detail. In this example, it can be shown that partial write-down leads to a better result for the insurer's solvency than a full write-down: a sufficiently high partial write-down (in the example: 46% or more) does have the same positive impact on the Group MCR, but has a less negative impact on the Group SCR, in comparison with a full (100%) write-down.
- To allow for such partial conversion in the context of Art. 71 (5) bis requires at a minimum that partial write-down can apply for all trigger events in Art. 71 (8) (a)***-(c)**,* and also for cases where the SCR actually falls ("only" the Group MCR ratio increases thanks to the PLAM in the example)
- **However, rather than amending Art. 71 (5) bis it would be more straightforward if the waiver option would apply more broadly than currently foreseen by Art. 70 bis (and No. 1495) in that (i) it should be available to regulators irrespective of the reason of the trigger breach and (ii) it should also allow regulators to effect a *partial* write-down or conversion where sensible.** The broadening of the waiver should provide the regulator with a tool to prevent PLAM from having a negative impact in a crisis scenario.
- Please note that the proposed changes to Art. 71 (5) bis are based on the assumption that the waiver option under Art. 70 bis is available irrespective of the type of trigger breach.

*[3] Partial conversion should be allowed*

- Partial conversion is conceptually sensible for the same reasons as partial write-down and should be allowed.
- However, we are not aware of an outstanding convertible instrument that allows for the partial conversion of single bonds where the *denomination per bond* would have to be partially reduced in exchange for the delivery of shares to the RT1 investors. We are not certain whether this is legally possible in all relevant jurisdictions.

*[4] Partial PLAM in accordance with Art.71 (5) bis (a) compared to (b)*

- Please compare the following scenarios:
  - The SCR ratio is at 93% for more than three months
  - Case 1: the SCR ratio would be fully cured with a write-down amount of 97%, in line with Art.71 (5) bis (a)
  - Case 2: a write-down cannot cure the SCR ratio, and therefore Art.71 (5) bis (b) applies. The write-down amount would then be 28% (= 4 x 7%)
- In both cases, the SCR ratio will be at or near 100%, and the insurer is arguably in a going concern situation.
- It is not clear whether the windfall profit that shareholders would receive in "case 1" compared to "case 2" is justifiable as it would manifest an inversion of the hierarchy of capital (write-down of 97% implies that the RT1 investors incurs additional losses of 71% (=97% - 28%) in case 1 compared to case 2. Shareholders actually profit from the additional write-down amount and in general are potentially "only" subject to temporary valuation losses.

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| | **Worked example: assumptions and background to the calculations added below**<br><br>• The example assumes a large illustrative loss of Unrestricted Tier 1 capital, and the status immediately prior to write-down is shown after such a loss has occurred.<br>• The issuer is assumed to be loss making, with any adverse tax consequence from PLAM assumed to reduce DTA. The assumed tax rate is 30%.<br>• Immediately prior to the application of PLAM, the group MCR ratio is 98.6%, whereas the Group SCR ratio is 105% (i.e. trigger inversion).<br>• The example shows the impact of a write-down on both (i) Group MCR and (ii) Group SCR, and for both ratios the impact of a 100% and a 46% write-down are shown.<br>• In the example, a 100% write-down more than cures the group MCR breach, which increases from 98.6% to 120%. For this purpose, PLAM works as intended.<br>• However, the 100% write-down will also lead to a breach of the group SCR, which falls from 105% to 97.2%. **This cannot be an intended consequence of PLAM, in our eyes.**<br>• At the same time, a partial write-down of only 46% would increase the group MCR ratio to the same level as a 100% write-down, namely 120%, whereas the group SCR ratio would fall by less and would remain at 101.4%.<br>• **A partial write-down therefore would lead to a better result than a full write-down in this case, but we note that partial write-down (as well as the application of the PLAM waiver, see No. 1495) would be prohibited by EIOPA's currently suggested wording due to the Group MCR breach.**<br>• The group SCR is assumed to be 10,000, the group MCR is assumed to be 7,000. | |

<u>Part 1</u>: Impact of a 100% (2,600) write-down on the Group MCR ratio (see next page for impact on Group SCR ratio) – ratio increases from 98.6% to 120%

**Group MCR (min. consolidated Group-SCR): write-down increases Group MCR ratio from 98.6% to 120%**

**1. Group MCR ratio immediately prior to write-down**

| | Available Own Funds | in % of Group-MCR | in % of T1 | Tiering limit adjustments | Eligible Own Funds | in % of Group-MCR | in % of T1 |
|---|---|---|---|---|---|---|---|
| Excess of Assets over Liabilities | 5,900 | | | | 5,900 | | |
| ./. Net DTA | -1,500 | | | | -1,500 | | |
| = UT1 | 4,400 | 62.9% | | | 4,400 | 62.9% | |
| + RT1 | 2,600 | | 37.1% | -1,500 | 1,100 | | 20.0% |
| = T1 | 7,000 | 100.0% | | -1,500 | 5,500 | 78.6% | |
| + T2 (incl. excess RT1 if any) | 2,000 | 28.6% | | -600 | 1,400 | 20.0% | |
| + T3 (Net DTA) | n.a. | | | | n.a. | | |
| **= Total Own Funds (Group MCR)** | **9,000** | | | **-2,100** | **6,900** | | |
| **Group MCR** | **7,000** | | | | **7,000** | | |
| **Group MCR ratio *before* W/D** | | | | | **98.6%** | | |

**2. Assumed write-down details**

| | | |
|---|---|---|
| Assumed RT1 write-down amount | 2,600 | (i.e. 100% of principal amount) |
| - thereof tax (30%): | 780 | |
| - thereof net write-down | 1,820 | |

**3. Group MCR ratio immediately after write-down**

| | Available Own Funds | in % of Group-MCR | in % of T1 | Tiering limit adjustments | Eligible Own Funds | in % of Group-MCR | in % of T1 |
|---|---|---|---|---|---|---|---|
| Excess of Assets over Liabilities | 7,720 | | | | 7,720 | | |
| ./. Net DTA | -720 | | | | -720 | | |
| = UT1 | 7,000 | 100.0% | | | 7,000 | 100.0% | |
| + RT1 | 0 | | 0.0% | | 0 | | 0.0% |
| = T1 | 7,000 | 100.0% | | | 7,000 | 100.0% | |
| + T2 (incl. excess RT1 if any) | 2,000 | 28.6% | | -600 | 1,400 | 20.0% | |
| + T3 (Net DTA) | n.a. | | | | n.a. | | |
| **= Total Own Funds (Group MCR)** | **9,000** | | | **-600** | **8,400** | | |
| **Group MCR** | **7,000** | | | | **7,000** | | |
| **Group MCR ratio *after* W/D** | | | | | **120.0%** | | |
| **Impact of W/D on Group MCR ratio** | | | | | **21.4%** | | |

Part 2: Impact of a 100% (2,600) write-down on the Group SCR ratio. Note the trigger inversion (i.e. Group SCR ratio not breached prior to PLAM) – ratio decreases from 105% to 97.2%

**Group-SCR ratio: write-down reduces the Group SCR ratio from 105% to 97.2% (BREACH)**

**1. Group SCR ratio immediately prior to write-down**

| | Available Own Funds | in % of Group-SCR | in % of T1 | Tiering limit adjustments | Eligible Own Funds | in % of Group-SCR | in % of T1 |
|---|---|---|---|---|---|---|---|
| Excess of Assets over Liabilities | 5,900 | | | | 5,900 | | |
| ./. Net DTA | -1,500 | | | | -1,500 | | |
| = UT1 | 4,400 | 44.0% | | | 4,400 | 44.0% | |
| + RT1 | 2,600 | | 37.1% | -1,500 | 1,100 | | 20.0% |
| = T1 | 7,000 | 70.0% | | -1,500 | 5,500 | 55.0% | |
| + T2 (incl. excess RT1 if any) | 2,000 | 20.0% | | 1,500 | 3,500 | 35.0% | |
| + T3 (Net DTA) | 1,500 | 15.0% | | | 1,500 | 15.0% | |
| **= Total Own Funds (Group SCR)** | **10,500** | | | | **10,500** | | |
| **Group SCR** | 10,000 | | | | **10,000** | | |
| **Group SCR ratio prior to W/D** | | | | | **105.0%** | | |

**2. Assumed write-down details**

| | | |
|---|---|---|
| Assumed RT1 write-down amount | 2,600 | (i.e. 100% of principal amount) |
| - thereof tax (30%): | 780 | |
| - thereof net write-down | 1,820 | |

**3. Group SCR ratio immediately after write-down**

| | Available Own Funds | in % of Group SCR | in % of T1 | Tiering limit adjustments | Eligible Own Funds | in % of Group SCR | in % of T1 |
|---|---|---|---|---|---|---|---|
| Excess of Assets over Liabilities | 7,720 | | | | 7,720 | | |
| ./. Net DTA | -720 | | | | -720 | | |
| = UT1 | 7,000 | 70.0% | | | 7,000 | 70.0% | |
| + RT1 | 0 | | 0.0% | | 0 | | 0.0% |
| = T1 | 7,000 | 70.0% | | | 7,000 | 70.0% | |
| + T2 (incl. excess RT1 if any) | 2,000 | 20.0% | | | 2,000 | 20.0% | |
| + T3 (Net DTA) | 720 | 7.2% | | | 720 | 7.2% | |
| **= Total Own Funds (Group SCR)** | **9,720** | | | | **9,720** | | |
| **Group SCR** | 10,000 | | | | **10,000** | | |
| **Group SCR ratio *after* W/D** | | | | | **97.2%** | | |
| **Impact of W/D on Group SCR ratio** | | | | | **-7.8%** | | |

<u>Part 3</u>: Impact of a <u>*46%*</u> (1,200) write-down on the Group MCR ratio for the same issuer – same impact on Group MCR ratio as for a 100% write-down

**Group MCR (min. consolidated Group-SCR): write-down increases Group MCR ratio from 98.6% to 120%**

**1. Group MCR ratio immediately prior to write-down**

| | Available Own Funds | in % of Group-MCR | in % of T1 | Tiering limit adjustments | Eligible Own Funds | in % of Group-MCR | in % of T1 |
|---|---|---|---|---|---|---|---|
| Excess of Assets over Liabilities | 5,900 | | | | 5,900 | | |
| ./. Net DTA | -1,500 | | | | -1,500 | | |
| = UT1 | 4,400 | 62.9% | | | 4,400 | 62.9% | |
| + RT1 | 2,600 | | 37.1% | -1,500 | 1,100 | | 20.0% |
| = T1 | 7,000 | 100.0% | | -1,500 | 5,500 | 78.6% | |
| + T2 (incl. excess RT1 if any) | 2,000 | 28.6% | | -600 | 1,400 | 20.0% | |
| + T3 (Net DTA) | n.a. | | | | n.a. | | |
| **= Total Own Funds (Group MCR)** | **9,000** | | | **-2,100** | **6,900** | | |
| **Group MCR** | **7,000** | | | | **7,000** | | |
| **Group MCR ratio before W/D** | | | | | 98.6% | | |

**2. Assumed write-down details**

| | |
|---|---|
| Assumed RT1 write-down amount | 1,200 (i.e. 46% of principal amount) |
| - thereof tax (30%): | 360 |
| - thereof net write-down | 840 |

**3. Group MCR ratio immediately after write-down**

| | Available Own Funds | in % of Group-MCR | in % of T1 | Tiering limit adjustments | Eligible Own Funds | in % of Group-MCR | in % of T1 |
|---|---|---|---|---|---|---|---|
| Excess of Assets over Liabilities | 6,740 | | | | 6,740 | | |
| ./. Net DTA | -1,140 | | | | -1,140 | | |
| = UT1 | 5,600 | 80.0% | | | 5,600 | 80.0% | |
| + RT1 | 1,400 | | 20.0% | | 1,400 | | 20.0% |
| = T1 | 7,000 | 100.0% | | | 7,000 | 100.0% | |
| + T2 (incl. excess RT1 if any) | 2,000 | 28.6% | | -600 | 1,400 | 20.0% | |
| + T3 (Net DTA) | n.a. | | | | n.a. | | |
| **= Total Own Funds (Group MCR)** | **9,000** | | | **-600** | **8,400** | | |
| **Group MCR** | **7,000** | | | | **7,000** | | |
| **Group MCR ratio <u>after</u> W/D** | | | | | **120.0%** | | |
| **Impact of W/D on Group MCR ratio** | | | | | **21.4%** | | |

**Part 4: Impact of a *46%* (1,200) write-down on the Group SCR ratio – the post PLAM Group SCR ratio is higher when write-down is only partial (46%) rather than 100%**

**Group-SCR ratio: write-down reduces the Group SCR ratio from 105% to 101.4% (NO breach)**

**1. Situation immediately prior to write-down**

| | Available Own Funds | in % of Group-SCR | in % of T1 | Tiering limit adjustments | Eligible Own Funds | in % of Group-SCR | in % of T1 |
|---|---|---|---|---|---|---|---|
| Excess of Assets over Liabilities | 5,900 | | | | 5,900 | | |
| ./. Net DTA | -1,500 | | | | -1,500 | | |
| = UT1 | 4,400 | 44.0% | | | 4,400 | 44.0% | |
| + RT1 | 2,600 | | 37.1% | -1,500 | 1,100 | | 20.0% |
| = T1 | 7,000 | 70.0% | | -1,500 | 5,500 | 55.0% | |
| + T2 (incl. excess RT1 if any) | 2,000 | 20.0% | | 1,500 | 3,500 | 35.0% | |
| + T3 (Net DTA) | 1,500 | 15.0% | | | 1,500 | 15.0% | |
| **= Total Own Funds (Group SCR)** | **10,500** | | | | **10,500** | | |
| **Group SCR** | **10,000** | | | | **10,000** | | |
| **Group SCR ratio prior to W/D** | | | | | **105.0%** | | |

**2. Assumed write-down details**

| | |
|---|---|
| Assumed write-down amount | 1,200 (i.e. 46% of principal amount) |
| - thereof tax: | 360 |
| - thereof net write-down | 840 |

**3. Group SCR ratio after write-down**

| | Available Own Funds | in % of Group SCR | in % of T1 | Tiering limit adjustments | Eligible Own Funds | in % of Group SCR | in % of T1 |
|---|---|---|---|---|---|---|---|
| Excess of Assets over Liabilities | 6,740 | | | | 6,740 | | |
| ./. Net DTA | -1,140 | | | | -1,140 | | |
| = UT1 | 5,600 | 56.0% | | | 5,600 | 56.0% | |
| + RT1 | 1,400 | | 20.0% | | 1,400 | | 20.0% |
| = T1 | 7,000 | 70.0% | | | 7,000 | 70.0% | |
| + T2 (incl. excess RT1 if any) | 2,000 | 20.0% | | | 2,000 | 20.0% | |
| + T3 (Net DTA) | 1,140 | 11.4% | | | 1,140 | 11.4% | |
| **= Total Own Funds (Group SCR)** | **10,140** | | | | **10,140** | | |
| **Group SCR** | **10,000** | | | | **10,000** | | |
| **Group SCR ratio *after* W/D** | | | | | **101.4%** | | |
| **Impact of W/D on Group SCR ratio** | | | | | **-3.6%** | | |

***<u>Why PLAM increases the Group MCR ratio, but reduces the Group SCR ratio in this example</u>:***

- The Tiering limit for RT1 is identical for purposes of the Group SCR and Group MCR (i.e. 20% of total Tier 1). In the example RT1 is assumed to exceed this 20% limit prior to write-down for the purpose of both ratios.
- The resulting "excess RT1" can theoretically count as eligible T2, but only as long as the T2 headroom is not yet fully exhausted by existing T2 capital. The Tiering limit for T2 is stricter for purposes of the Group MCR (max 20% of MCR) than for the Group SCR (max 50% of SCR, limit shared with T3).
- In the example, the 20% T2 limit for Group MCR is fully utilised by available T2 and excess RT1 therefore does not count as eligible capital for purposes of the Group MCR. The PLAM increases UT1 and thus total own funds. While RT1 falls due to PLAM, too, this fall "only" reduces "excess RT1" that did not count as eligible own funds prior to PLAM. As a result, total **own funds for purposes of the Group MCR increase thanks to PLAM,** which in turn increases the Group MCR ratio.
- The limit for T2 headroom for purposes of the Group SCR is higher (50%). This means that "excess RT1" does count as eligible capital *<u>prior</u>* to PLAM for purposes of the group SCR. The increase of UT1 is compensated by an identical reduction of excess RT1 which counted as eligible T2 prior to PLAM. Since PLAM also leads to a reduction of DTA (T3), **total own funds for Group SCR purposes fall.** As a result, PLAM reduces the Group SCR ratio.

***<u>Why the impact of a 100% write-down on the Group MCR ratio is not better than that of a 46% write-down in this example</u>:***

- Prior to PLAM, the available capital for Group MCR purposes is 9,000, but because of binding Tiering limits, eligible capital is only 6,900. The ineligible difference ("excess capital") is 2,100.
- "Excess capital" consists of 600 "excess T2" and 1,500 "excess RT1". For purposes of the

Group MCR, "excess RT1" does not increase eligible T2 since the T2 headroom is already more than fully utilised by available T2.

- **PLAM can only increase solvency ratios to the extent it transforms ineligible "excess capital" into eligible capital.**
- PLAM does not impact the SCR, but "only" UT1. PLAM can therefore only increase T1 capital. The <u>*maximum*</u> benefit of PLAM is therefore limited to the amount of excess RT1 (1,500). In this example, the maximum benefit from PLAM can be realised, since PLAM cannot reduce eligible T2, given the sufficiently high amount of available T2.
- To realise the maximum benefit of 1,500, a write-down of 1,200 is sufficient. To see that, note that a write-down of 1,200 …
    - … increases UT1 by 1,200 without reducing eligible RT1 ("only" ineligible excess RT1 is reduced by 1,200 from 1,500 to 300)
    - … and this increase of UT1 by 1,200 in turn increases the maximum amount of eligible RT1 by 300 (= 1,200 *20% RT1 Limit / 80% UT1 Limit). The remaining ineligible excess RT1 of 300 remaining after the step-up therefore becomes eligible given this increase of the maximum total RT1 headroom.
    - A write-down of 1,200 is therefore sufficient to fully activate the previously ineligible excess RT1
    - If the write-down amount were increased by an additional 100 to 1,300, UT1 would increase by 100, but eligible RT1 would fall by the same amount. **Increasing the write-down to more than 1,200 does not increase the Group MCR ratio any further.**

<u>***In our view, the example supports three observations and several important conclusions:***</u>

1) **There can be situations where a <u>*partial*</u> write-down leads to an improved outcome**

**compared to a full 100% write-down even where the Group MCR is breached.** Therefore, partial write-down should not generally be prohibited in case of Group MCR breach. This can be achieved by an appropriately flexible PLAM waiver or by an adaptation of the article regarding partial PLAM.

2) **There can be situations where there is no simple answer to the question of the "optimal" write-down amount.** While a write-down of 46% leads to the best possible outcome for purposes of the Group MCR, one could also argue that the write-down should actually be smaller since this would result in a higher Group SCR ratio than the rather low 101.4% that results from the 46% W/D. A higher post PLAM Group SCR ratio requires a smaller write-down amount, but this would come at the cost of a Group MCR ratio that would be lower than the maximum of 120%. **We are not expressing a view on how to balance this trade off in this document.**

3) **Determining the "optimal" write-down amount requires that the impact of PLAM on all relevant metrics is considered.** Large groups (i.e. the most prominent expected issuers of RT1) typically will reference up to four different trigger ratios (SCR and MCR on both solo and group level). A high number of trigger ratios may make the determination of the optimal write-down amount more challenging.

**PLAM does not increase the quality of capital in our eyes. PLAM can increase some – and decrease other – triggers ratios at the same time. The Group MCR ratio is an inappropriate trigger to the extent that it can be breached prior to the Group SCR. If PLAM is triggered in situations of such "trigger inversion", this would represent a major departure from a risk-based regime and would represent a poor reason for causing significant losses to RT1 investors. Limiting the application of PLAM would reduce the complexity of RT1, and would reduce the risk of unintended consequences. PLAM should be eliminated or set at a fundamentally lower triggering level (true gone concern). At a minimum, the PLAM waiver option as currently envisaged should be broadened so that it can apply in any circumstances where a regulator deems a waiver as sensible.**

| | | |
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| | **New Art. 71 (5) ter:**<br>*Where partial write down is undertaken in accordance with Article 5 bis (b)(i), unless an exceptional adverse situation has subsequently been declared in accordance with Article 138 (4) of Directive 2009/138/EC, the Solvency Capital Requirement coverage ratio should be recalculated every three months starting from the trigger event listed in paragraph 8 (c) until the insurance or reinsurance undertaking either:*<br>*a) re-establishes compliance with the Solvency Capital Requirement; or*<br>*b) breaches either of the triggers listed in paragraph 8 (a) or (b), and in either case writes down in full.*<br>*If ~~this recalculation indicates that~~ [1] the Solvency Capital Requirement coverage ratio has deteriorated further, then the nominal or principal amount of the basic own-fund item as determined at original issuance should be written down further in accordance with Article 5 bis (i) to reflect that additional deterioration.*<br>*The supervisory authority may decide to extend a recalculation period by an additional three months in case the undertaking has already executed meaningful measures to re-establish compliance with the Solvency Capital Requirement after the last reporting date. [2]*<br><br>**Explanation of the recommended changes:**<br>***[1] "Indication" is insufficient***<br>• The application of PLAM must be legally certain and therefore requires a reliable calculation of the SCR/MCR, which in turn requires a fully fledged MVBS on solo and/or consolidated basis.<br>***[2] Extension of re-calculation period to allow consideration of capital or risk measurers***<br>• The MVBS is based on (interim) financial statements and will usually be available at reporting dates for (interim) financial statements. Therefore, measures to re-establish | |

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| | compliance with the Solvency Capital Requirements may not be reflected in case they have been executed after an (interim) reporting period. The MVBS will only reflect these changes in the report for the next (interim) financial period. To avoid a situation where a further application of the PLAM were formally required even though a significant capital or risk measure has been undertaken shortly after the last interim reporting period so that it is not yet already reflected in the next financial figures we deem the suggested extension as appropriate.<br>• The same clarification should be added with respect to the three months period in DR Art. 71 (8) (c) | |
| 19.5.1 | | |
| 19.5.2 | | |
| 19.5.3 | | |
| 19.5.4 | **<u>New Art. 70 bis</u>**<br><br>***Tax effects of <u>the principal loss absorbency mechanisms</u> ~~write down~~ of items listed in Article 69 (a)(iii), (v) and (b)***<br>*For own funds items listed in points(a)(iii), (v) and (b) of Article 69 which <u>contain a principal loss absorbency mechanism</u>~~write down~~**[1]** on trigger in accordance with Article 71 (1)(e)(i)<u>, (ii)</u> or (iii), the supervisory authority may decide ~~in exceptional circumstances~~ **[2]** to waive the <u>requirement to apply the principal loss absorbency mechanism</u>~~write down requirement~~ where at least the following conditions are met:*<br>*a) the waiver has been requested by the undertaking; and*<br>*b) when requesting the waiver the undertaking has provided the following to the supervisory authority:*<br>*(i) projections which demonstrate that <u>the application of the principal loss absorbency mechanism</u> ~~a write down~~ is very likely to lead to a tax liability that will have a significant adverse effect on S<u>olvency</u> C<u>apital</u> R<u>equirement</u> <u>or Minimum Capital Requirement</u> **[3]*** | |

| | | |
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| | *coverage; and*<br>*(ii) a certification by the undertaking's statutory auditors [4] that all of the assumptions used in the projection are realistic.*<br><br>**Explanation of the recommended changes:**<br><br>***[1]*** *Exceptional waiver for conversion RT1:*<br>• Where conversion can have adverse effects on SCR or Group MCR coverage, there is no reason why regulators should not be allowed to grant a waiver.<br>• We understand that based on current tax laws in the EEA, waivers for conversion are less likely to be required than for write-down.<br>• However, there are jurisdictions today where both write-down and conversion are subject to taxation, so that a waiver can be sensible also for conversion (and other potential PLAMs).<br>• More importantly, RT1 is perpetual, and the relevant tax law can change in the future. Even in jurisdictions where neither conversion nor write-down are subject to taxation at issuance (today), there is no guarantee that this will remain so for the entire life of the instrument.<br>• To avoid that RT1 can malfunction, the terms and conditions of *all* RT1 instruments should therefore allow for a potential PLAM waiver.<br><br>***[2]*** *Deletion of "In exceptional circumstances" is a clarification*<br>The exceptional circumstances are described as conditions under b) (i) and (ii).<br><br>***[3]*** *Exceptional waiver to avoid that PLAM reduces MCR coverage*<br>• PLAM can lead to a reduction of both SCR or MCR coverage. PLAM as currently foreseen may apply in a going concern situation. | |

| | | |
|---|---|---|
| | • The PLAM waiver option should enable the relevant regulator to waive the PLAM where application of PLAM would have an adverse effect on either SCR or MCR (on solo or group basis – including in cases of trigger inversion).<br><br>***[4]** Direct feedback from auditors on Art. 70 bis to EIOPA and the European Commission is important*<br>• From our interaction with auditors we understand that the proposed wording in Art. 70 bis (b) (ii) works in practice. We further understand that auditors will work on standards that set out the scope of services that regulators can expect in this context. We recommend that EIOPA directly interacts with auditors on the matter to ensure all parties know what information auditors should and can deliver.<br>• Having said that, note that we understand "tax liability" for purposes of Art. 70 bis (b) (i) in the sense that it exclusively refers to the tax impact of PLAM, irrespective of the overall tax situation of the issuer at that time. That means that it should not matter for the PLAM waiver whether the significant adverse (tax) effect on solvency coverage manifests itself via a current tax (i.e. an actual increase of a liability) or via a deferred tax position (i.e. a reduction of an asset).<br><br>***[5]** The PLAM waiver should apply more broadly*<br>• We refer to the example provided in the context of Art. 71 (5) bis<br>• As outlined there, we think that the scope of the PLAM waiver should be as broad as possible to allow regulators to prevent unintended consequences from PLAM.<br>• Our preferred solution, however, would be to delete PLAM altogether or to limit its applicability to "true" gone concern situations only. | |
| 19.6.1 | | |
| 19.6.2 | | |
| 19.6.3 | | |
| 19.6.4 | ***New Article 71 (2) bis***<br>*Notwithstanding paragraph (1)(f)(ii) of this Article, the competent authorities may permit* | |

| | | |
|---|---|---|
| | *institutions to redeem a Tier 1 instrument before five years of the date of issue ~~when the undertaking's Solvency Capital Requirement is, after the redemption, exceeded by an appropriate margin~~ [1] taking into account the solvency position of the undertaking including the undertaking's medium-term capital management plan and in addition one of the following situations is met:*<br>*a) there is a change in the regulatory classification of that instrument which would be likely to result in its full or partial [2] exclusion from own funds or full or partial reclassification as a lower tier of own funds, and both of the following conditions are met:*<br>*i. the competent authority considers such a change to be sufficiently certain; and*<br>*ii. the undertaking demonstrates to the satisfaction of the competent authorities that the regulatory reclassification of the instrument was not reasonably foreseeable at the time of their issuance;[3]*<br>*b) there is a change in the applicable tax treatment of that instrument which the undertaking demonstrates to the satisfaction of the competent authorities is material and was not reasonably foreseeable at the time of their issuance[3].*<br><br>**Explanation of the recommended changes:**<br><br>*[1] Unintended signalling due to the limited applicability of the "appropriate margin" concept*<br>• All ordinary and extraordinary calls are subject to prior regulatory approval. Regulators are expected to grant approval only if the solvency ratio after redemption is sufficiently high in the view of the regulator, who can grant approval subject to prior or simultaneous replacement with equivalent (or better quality) capital.<br>• Therefore any approval of ordinary or extraordinary calls is "automatically" connected with the regulator's view on the issuer- and situation-specific **"appropriate margin"** (by "situation-specific" we mean that an issuer's risk profile can change significantly over time, and therefore the actual "appropriate margin" for a particular issuer may therefore change over time, too. As a result, the appropriate margin should not be contractually "hard-coded"). The limitation of the formal appropriate margin concept to the first five | |

| | | |
|---|---|---|
| | (or for ordinary calls: ten) years may therefore be interpreted as a confusing and arguably unintended signal to market participants.<br><br>*[2] Partial derecognition should enable issuer calls*<br>Such redemption should also be possible in case of partial exclusion or reclassification. As any redemption is subject to approval by the relevant regulator, it is not necessary to set up additional requirements from a regulatory perspective.<br><br>*[3] The "non-foreseeability" requirement introduces unnecessary litigation risk*<br>• Issuer call rights allow the issuer to save money as they allow a call typically at par even where the market price for a repurchase would be higher.<br>• Therefore, call rights may be challenged by investors, and additional complexity regarding call rights increases legal risks for insurance companies.<br>• Since any redemption is subject to prior approval, we do not see a benefit of adding this requirement.<br><br>*General remark*<br>• Where the solvency ratio after redemption is sufficiently high without replacement, a replacement should not be required<br>• Article 71 (2) bis should apply to every extraordinary calls, and replacement should not *automatically* be required.<br><br>**New Article 73 (2) bis** [please see our comments to Article 71 (2) bis]<br><br>**New Article 77 (2) bis** [please see our comments to Article 71 (2) bis] | |
| 19.7 | | |
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| | Comments Template on<br>Consultation Paper on EIOPA's second set of advice to the European Commission on specific items in the Solvency II Delegated Regulation | Deadline<br>5 January 2018<br>23:59 CET |
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| | Comments Template on<br>Consultation Paper on EIOPA's second set of advice to the European Commission on specific items in the Solvency II Delegated Regulation | Deadline<br>5 January 2018<br>23:59 CET |
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