	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**
Name of Company:	Lloyd's	
Disclosure of comments:	Please indicate if your comments should be treated as confidential:	Public
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Reference	**Comment**	
General Comment	This is a response on behalf of Lloyd's. Lloyd's is a society of members that operates as an insurance market in London. It is recognised in the Solvency II Directive as "the association of underwriters known as Lloyd's" and is subject to prudential regulation by the Prudential Regulation Authority (PRA). We are firm supporters of the Solvency II insurance regime and believe that it is a model for insurance regulation worldwide. At the same time, we recognise that some of its detailed	

	provisions do not work precisely as intended and sometimes impose unnecessary costs and resource allocation on insurers, without commensurate benefits to policyholder protection or financial stability. Consequently, there is scope for the existing rules to be improved and we therefore welcome the reviews that the European Commission is conducting. They provide opportunities for Solvency II to be enhanced in the light of experience. We are commenting here only on the small number of issues raised in the advice that we consider to be directly relevant to Lloyd's and the Lloyd's market. At the same time, Lloyd's is a member of Insurance Europe and of the Reinsurance Advisory Board. We have seen their submissions, which comment on the advice in much greater detail, and agree with them.	
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5.4.1		
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5.4.2.2	We agree that the 200m radius for exposure inclusion is not unreasonable, albeit a little conservative. Amending the scenario to enhance risk sensitivity would result in unnecessary complexity in the standard formula.	
5.4.2.3	We believe that the recommended simplification is appropriate and will reduce the calculation burden whilst retaining an adequate level of risk sensitivity.	
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5.5.2.3	The proposed change from “tanker” to “vessel” appears sensible. The change necessitates introduction of a threshold, as is proposed. We suggest that the threshold is fixed at an amount greater than EUR 100,000, say EUR 250,000 or EUR 500,000, to achieve the objective of removing very low exposures from consideration. Many pleasure craft have insured hull values above EUR 100,000: although it is appropriate to include high value pleasure craft in the calculation, there is no need to include medium or low value vessels.	
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5.7.2.3	We support EIOPA’s recommendation that identification of the largest risk exposures within the Marine, Fire and Aviation risk sub-modules are carried out net of reinsurance.	
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6.5.3.3	We note the proposed adjustment, allowing an undertaking to take into account its specific exposure if it sells contracts with policy conditions which differ from those of the "average undertaking". In principle, we do not disagree with the suggested approach. Nevertheless, it adds complexity to the calculation, which may well dissuade many undertakings from adopting it.	
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9.1	We welcome the European Commission's request to EIOPA to investigate the approach to currency risk in relation to group SCR. Deficiencies in the approach also apply to solo entities and questionsabout the adequacies of the standard formula treatment of currency risk need to be considered overall. The standard formula penalises groups and solo entities covering their local SCRs in local currencies, which is intuitively wrong. We continue to believe that this should be corrected by application of a different approach.	
9.2		
9.3	Unfortunately, we do not think that the assessment provided addresses key criticisms of the current approach to currency risk: - It does not reflect real currency risks faced by insurers. - It incentivises poor currency risk management. This is because, as recognised by paragraph 577, it encourages groups and solo entities to hold capital in the reporting currency even though this increases risk. Paragraph 580 says: *"EIOPA does not find the argument referred to above convincing as it is not clear that holding assets in the group reporting currency to back local capital requirements and liabilities would reduce the capital because SCR for the solo undertakings would increase in such cases".* Operating subsidiaries are always likely to hold assets to back local capital requirements and liabilities in the local currency rather than the group reporting currency. It is also sensible for the group to hold excess assets in local currencies as well, so that they are better placed to meet	

	stress events at the local level should they occur. The current standard formula approach incentivises exactly the opposite approach, of holding excess assets in the group reporting currency. Paragraph 580 recognises that "*Holding all surplus assets in the group reporting currency…would expose the group to the risk of having the surplus assets in the wrong currency in the event of a stress*", but the paper does not draw the obvious conclusion: that the current approach to currency risk is not appropriate and that modifications should be introduced. Paragraph 581 notes EIOPA's concerns that "*the requirements of the Prudent Person Principle may not be satisfied if assets are not held locally*". This exactly replicates concerns expressed by industry about the approach to currency risk, communicated to EIOPA and the European Commission before and after Solvency II implementation. The current approach is fundamentally at odds with the Prudent Person Principle, as it actively discourages the localisation of assets, by incentivising the holding of surpluses in the group reporting currency, which does not ensure asset availability when foreign currency liabilities arise.	
9.4.1	We think that the analysis presented by EIOPA is disappointing. The Call for Advice asks for information on currencies chosen by insurance groups to hold their own funds in a context where the calculation of currency risk "may" penalise holding the own funds of a subsidiary in the subsidiary's local currency. It goes on to ask for an investigation into whether the approach to group currency risk " adequately" covers risk, "*taking into account the incentives given to the group's risk management*". Unfortunately, we do not think that the account set out in paragraphs 584 to 587 materially assists assessment of the currency risk sub-module. It is unclear from the information provided how groups are choosing to hold their own funds; the extent to which they are thereby incurring a "penalty" because their subsidiaries hold own funds in their local currencies; the incentives that the currency risk sub-module is giving to group risk management; or whether group currency risk is "adequately" covered or not. We note that the exercise does not appear to have excluded groups without foreign currency	

	exposure. The issue of currency risk applies to a limited number of groups and solo entities in the EU: those conducting material quantities of business in more than one currency. To those groups and solo entities who do not have foreign currency exposure, the current standard formula may well appear, as paragraph 602 says, “appropriate”. EIOPA should therefore assess how application of the currency risk sub-module works for those groups and solo entities who have significant exposure. If this would take more time, EIOPA should inform the European Commission accordingly. We note the formula proposed by Insurance Europe, as set out in paragraph 579. We are unclear about the reasons why EIOPA has rejected this formula and why it is not given detailed consideration in the section on “Options for amending the standard formula”, including assessment against the current approach. As it is, EIOPA has only considered a couple of options, neither of which entails significant change to the approach it has already adopted.	
9.4.2	We support the suggestion that groups be given the flexibility to select a currency other than the group reporting currency for calculation of their currency risk sub-module. This option must also be extended to solo entities that meet the same criteria as groups. Otherwise, there will be a difference in calculation of currency risk that does not represent any difference in the underlying risk to undertakings. At the same time, we recognise that this option is limited in its application. As paragraph 597 notes, it will only benefit groups with significant exposure to one currency, which use a different currency to prepare their consolidated financial statements. It would have been helpful if EIOPA’s assessment of how groups hold their own funds provided an estimation of the number of groups that would benefit from this. We believe that EIOPA’s conclusion, as set out in paragraph 602 that the standard formula is an inappropriate trade-off between simplicity of calculation and risk sensitivity warrants a mor extensive reassessment of the standard formula approach.	

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