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Report to the European Commission on the Application of Group Supervision under the Solvency II Directive

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1 Executive summary

- 1.1. From its inception in 2011, EIOPA has been involved in supporting the establishment of colleges of supervisors for cross-border groups and promoting consistency between colleges in their activities. Last year, the focus of EIOPA's actions moved from ensuring that each college was operating effectively to a more tailored and risk-based approach.
- 1.2. The definition of groups within the Solvency II Directive has generally worked well. Where there are difficulties, it is usually related to the ease of access to relevant information about ownership and relationships between entities in the upper levels of a structure. Getting the information can be more difficult when supervisors need to rely on the cooperation of non-EEA supervisory authorities.
- 1.3. One important practical limitation is consistency between the definition of a group and the scope of supervisory powers. In certain cases a group might exist, but the supervisor might not be able to take appropriate action against a holding company.
- 1.4. Colleges generally function well, but there is scope for colleges to develop further in the direction of collaboration and even sharing of tasks within the college. Sub-group supervision is a case in point, where EIOPA foresees that further maturity of colleges could remove the need for formal sup-group supervision in many cases.
- 1.5. There are many areas of the implementation of Solvency II, where different approaches by different national authorities are seen when the college meets. This underlines the importance of EIOPA's role in leading towards greater supervisory convergence across Europe.
- 1.6. The need for greater consistency is seen for internal models. In the run up to Solvency II, EIOPA tackled some of the highest priority areas of inconsistency and promoted common approaches to making joint decisions in colleges. Even so, EIOPA noted that there were several cases where a group chose to remove one or more countries from the scope of the group internal model application where the group had concerns that a joint decision would not be reached in time for a Day 1 approval.
- 1.7. Following approval of the first wave of internal models, EIOPA is now running consistency projects to identify and address areas of continuing inconsistency.
- 1.8. EIOPA's limited role in the assessment and approval of cross-border internal models has sometimes hampered its work in assessing and promoting convergence.
- 1.9. Capital add-ons have been used by very few supervisory authorities and only one authority has used a group capital add-on. EIOPA has published a more detailed analysis of capital add-ons in December 2017.

2 Background

- 2.1. This report is addressed to the European Commission and is in response to a request from the Commission for a Report on the Application of Title III (Supervision of Insurance and Reinsurance Undertakings in a Group) of Directive 2009/138/EC ("Solvency II").
- 2.2. The background to the Commission's request is Article 242 (1) of Solvency II: *By 31 December 2017, the Commission shall make an assessment of the application of Title III, in particular as regards the cooperation of supervisory authorities within, and functionality of, the college of supervisors and the supervisory practices concerning setting the capital add-ons, and shall present a report to the European Parliament and to the Council accompanied, where appropriate, by proposals for the amendment of this Directive.*
- 2.3. The Commission's request clarified that "EIOPA is not invited to formulate proposals for amendment of the Solvency II Directive at this point in time."
- 2.4. The Annex lists the 29 issues which the Commission asked EIOPA to pay particular attention to.

3 EIOPA's involvement in promoting supervisory convergence in group supervision

- 3.1. The concept of a college of insurance supervisors was introduced in the year 2000, in the form of coordination committees set out in the Helsinki Protocol. Solvency II, from January 2016, introduced explicit rights and responsibilities for the group supervisor and other members of the college of supervisors. The founding regulation of EIOPA (No. 1094/2010) brought in rights and responsibilities for EIOPA in respect of colleges.
- 3.2. With the formation of EIOPA in 2011, EIOPA staff worked with NCAs to establish colleges for each cross-border group. In the lead up to Solvency II the focus was on establishing the college as a vehicle for information exchange and cooperation, underpinned by a written coordination arrangement between college members, and for preparation for Solvency II. For groups which intended to apply to use an internal model, EIOPA supported preparation for the joint decision that would be made on the internal model application.
- 3.3. EIOPA staff have attended the majority of the colleges of supervisors for cross-border groups in recent years. EIOPA has produced annual reports on the functioning of colleges, which provide further insight into the development of colleges since EIOPA's formation in 2011.
- 3.4. The 92 colleges currently in existence vary considerable in their size (i.e. number of NCAs who are members and the relative sizes of subsidiaries in each country) and nature of the underlying group. Following a review of the strategic approach to colleges in 2016, the focus of EIOPA's participation in colleges has moved from establishing the colleges and their effective operation to a focus on the content of group supervision and the specific risks and issues faced by each group.
- 3.5. Risk-based choices are made about EIOPA's engagement in each college; this can result in one of three levels of engagement: involvement in the college on an ongoing basis, or only at a certain frequency, or where EIOPA in principle will not attend college meetings but follow developments using a desk-based review approach.

- 3.6. EIOPA's Oversight Strategy is to lead towards greater consistency and quality in national authorities' supervision of insurance undertakings across Europe. Specific initiatives taken by EIOPA in order to further supervisory convergence in the supervision of groups include:
- developing a supervisory handbook including the practice of group supervision,
 - providing a uniform format for coordination arrangements in colleges (this being a document which sets out the functioning of a college) and coordinating their signing for all colleges,
 - producing standard reports based on data reported at group and solo level, which can be shared among college members via the group supervisor,
 - sharing best practices on group supervision on the EIOPA extranet,
 - running annual training events for group supervisors, and
 - carrying out Peer Reviews on relevant topics, for example on national supervisory authorities' governance of their participation in colleges of supervisors and on internal model pre-application processes.
- 3.7. EIOPA's colleges and groups experts have provided advice, especially to smaller authorities, and in several cases fulfilled a facilitation role when the college members could not reach an agreement.
- 3.8. Since the start of 2014, EIOPA staff have conducted bilateral visits at the national supervisory authorities responsible for insurance supervision. This has included discussion and feedback on the authorities' supervision of cross-border and domestic groups and undertakings in groups within the context of the authorities' overall approach to supervision. This year these bilateral visits have been extended to include the approach to on-going supervision of internal models after approval.
- 3.9. The issue of cross-border business activities provided by groups and solo undertakings through the freedom to provide service (FoS) regime came to the fore this past year. EIOPA detected increasing issues in relation to this business model which ultimately in few cases even lead to failures of insurance companies writing cross-border insurance business, following unsatisfactory cooperation between the home and host supervisory authorities. EIOPA and its members agreed via a BoS Decision to reinforce supervisory cooperation related to cross-border business. This involves information and data exchange in areas such as authorisations, cross-border business, and recovery plans. To facilitate this, EIOPA sets up cross-border platforms of collaboration for the supervisory authorities involved. These platforms provide a forum to discuss the supervisory issues and common supervisory actions for specific cases. The exchange of information in this case is not based on Article 249 (which is relevant for information exchange within colleges), but on Article 65 ("Exchange of information between supervisory authorities of Member States") of Solvency II.
- 3.10. EIOPA's role in internal models is set out in section 6 below.

4 Definitions and scope of group supervision

Definition of group supervision

- 4.1. EIOPA notes that many of the Commission's issues for particular attention relate to cross-border groups and colleges, whereas Title III of Solvency II also applies to "domestic" groups, that is groups where all undertakings are located in the same country and supervision is carried out by the relevant national supervisory authority.
- 4.2. EIOPA has never been officially requested to assist in delimiting the scope of group supervision, although there are regular bilateral exchanges of views between EIOPA and some national authorities on the scope of group supervision.

Problems concerning the definition of a group

- 4.3. In most cases the definition of a "group" in Article 212(1)c of Directive 2009/138/EC works well. EIOPA is aware of three cases of difficulty.
- 4.4. In the first case, where the individual insurance undertakings acted in consort, the "centralised coordination" condition in the Article was difficult to prove, even though the individual insurance undertakings offer the same insurance products and conditions, and present themselves on the internet as one group. The individual companies also make the same investments and have the same investment strategies, employees work for several subsidiaries in consecutive roles. In this case EIOPA believed that the national supervisory authority needed to carry out further research and information gathering to establish the existence of a group.
- 4.5. The second case is of third country groups operating in the EEA through multiple-entry points rather than using a holding company for their operations in the European market. As NCAs are mainly sighted on the operations of the subsidiary they supervise, it is quite difficult to know that there is another EU subsidiary which triggers group supervision. A further practical complication is how to decide which of these authorities meets the criteria in Article 247 (2) letter b) – paragraph v) for becoming group supervisor as it requires comparison of balance sheet sizes for all EEA entities.
- 4.6. In the case of insurance groups with major non-EEA operations, the Directive could benefit from further clarity as to what are the expectations for supervisory action in relation to the risks within the EEA from the non-EEA parts of the business.
- 4.7. The third case relates to non-EEA structures with related investment funds investing in several otherwise unconnected insurance undertakings across the EEA. The structures cannot be identified as groups and EEA supervisors are reliant on non-EEA supervisory authorities to provide information on the construction and ownership of the structure.
- 4.8. EIOPA's activities in this third area include setting up of so-called proto-colleges, which result in meetings and conference calls between the relevant EEA national authorities with the focus on information exchange and assessment of potential risks stemming from activities and uncertainties on the strategy of the ultimate parent based in a non-EEA country. As a next step EIOPA envisages to start up cooperation between EEA supervisors and the non-EEA supervisor of the ultimate parent.

Consistency in the definition of a group and scope of group supervision

- 4.9. Article 214 of Directive 2009/138/EC states that, "The exercise of group supervision in accordance with article 213 shall not imply that supervisory authorities are required to play a supervisory role in relation to the third country insurance undertaking, (...) the insurance holding company, the mixed financial holding company, mixed activity holding company(...)"
- 4.10. Some NCAs have stated that this leads to an absence of legal basis for supervisory measures against the holding company, except in the case of the fit and proper requirement set out in Article 257. For example in the case where the group solvency capital includes the (mixed financial) holding's participation in other (non-insurance companies) and the valuation of these participations is considered inadequate, no measures can be taken against the group. Another example is that, when the governance and control at group level required under Article 246 is poor, no supervisory measures can be taken directly against the holding company.
- 4.11. One way to resolve this issue would be to ensure the types of undertaking potentially excluded from group supervision under Article 214 were not those undertakings referred to in other Articles for which specific supervisory action are required in certain cases; for example Article 218 ("Supervision of group solvency").

5 Functionality of the colleges of supervisors and cooperation of authorities within them

Cooperation and information sharing among members of the college

- 5.1. Material supervisory actions taken at solo level which are relevant for other college members are usually reported to the group supervisor and shared as part of the regular information exchange in the college. If actions are of immediate importance the group supervisor is notified ad-hoc and normally informs other supervisory authorities in the college who are affected.

Degree of convergence within colleges

- 5.2. In nearly all aspects of the implementation of Solvency II there is scope for greater consistency in the approaches taken by different national authorities. This is especially the case in areas that require the exercise of judgement, for example in the calculation of Technical Provisions.
- 5.3. The group supervisor and the solo supervisor review and assess that the regulatory criteria are met for the undertakings within a group for which they have responsibility. Internal model approvals are an exception, where the approval of a group model is by a joint decision of the relevant members of the college.
- 5.4. The college is a forum for exchanging information about assessments and outcomes, and identifying issues of inconsistency. EIOPA investigates and addresses these issues on a risk-based basis. It also raises the issues with the Board of Supervisors, encouraging Members to share the approach of their authority. In the past year discussions have been held about Technical Provisions, limiting the allowance for deferred tax in the solvency capital requirement (SCR) and approaches to deciding when to implement sub-group supervision.

Joint on-site inspections

- 5.5. With the exception of internal models (see section 6.), joint on-site inspections were only used in a limited way as a tool before the introduction of Solvency II. The number of inspections on Pillar 2 issues has started to grow this year. EIOPA is normally invited to join inspections.
- 5.6. National authorities and EIOPA have generally been in good cooperation when planning and conducting joint on-site inspections. The planning and running of on-site inspections has improved over the past few years. One occasional practical issue that needs additional effort to solve is the language used during an inspections. In some cases, according to the local law, the management of the undertaking only needs to answer questions and provide information in the local language.
- 5.7. The main findings of joint on-site examinations will normally be shared by the group supervisor with the college of supervisors where deemed relevant for the other NCAs in order to conduct their supervision.

Sub-group supervision

- 5.8. 3 countries conduct sub-group supervision on 8 cross-border groups. One of these countries has a further 3 cases for sub-group supervision under review.
- 5.9. Within the current 8 cross-border group subject to sub-group supervision, there are cases of one group having two sub-groups and one case where the sub-group contains undertakings from more than one country (that is, a cross-border sub-group).
- 5.10. The statistics in the preceding paragraphs are based on information received by EIOPA up to the end of August 2017.
- 5.11. There are two challenges surrounding sub-group supervision:
 - Firstly, Delegated Regulation Article 358 sets out only in very broad terms the circumstances in which sub-group supervision is allowed (“only [be taken] in circumstances justified by objective differences in the operations, the organisation or the risk-profile between the subgroup and the group.”). EIOPA has sought to promote consistent interpretations of this text, but has been able to achieve only limited convergence.
 - Secondly, the text of the Directive could further clarify expectations supervisors are required to meet when engaging in sub-group supervision and remove the potential for significant duplication of tasks. Article 216.1 of Directive 2009/138/EC requires that Art. 218 – 258 of the Directive are applied *mutatis mutandis* subject to provisions on group solvency stated in paragraphs 2 to 6 of the same article.
For cross-border sub-groups this requirement results in the set-up of an additional college for each sub-group including a separate coordination arrangement, emergency plan and double information exchange, as well as overlap in the reporting to supervisors by the group and its sub-group(s).
- 5.12. EIOPA is of the view that, unless there is a particular reason for needing sub-group supervision, it is possible to achieve effective supervision of the group using a specialised team within the group college to focus on particular parts of the group with significant differences from the group as a whole. Any specific requirements for reporting or the thresholds for reporting intra-group transactions and risk concentrations needed by the specialist team could be put into the annexes of the group coordination arrangement.

EIOPA's formal mediation role for colleges

- 5.13. To date there has not been a request to EIOPA under Article 19 of the EIOPA Regulation.
- 5.14. As mentioned in paragraph 3.7, EIOPA has provided advice and facilitation to group supervisors and college members.

Application to be subject to Articles 238 and 239

- 5.15. EIOPA is not aware of any cases of centralised risk management agreements reached with an explanation of reasons argued by the entities to submit the application for permission to be subject to Articles 238 and 239 of Solvency II.

6 Group internal models

EIOPA's role in promoting supervisory convergence

- 6.1. From the end-2016 reporting templates, 11 Member States have approved group internal models (both cross-border and domestic group models) and solo internal models are used in 17 Member States. Although the proportion of undertakings by number using a full or partial internal model is very low, these undertakings tends to be the larger undertakings in their markets and so make up a significant part of the total industry risk exposure.
- 6.2. Starting in 2013, staff in EIOPA's Centre of Expertise in Internal Models (CoEIM) attended selected on-site inspections of cross-border groups' internal models and worked with members to improve consistency in how the models were assessed in the pre-application and formal application phases. The number of national authority staff involved in assessing internal models, before and since approvals, is many times greater than that of EIOPA's CoEIM. EIOPA has to apply its limited resources on a risk-based approach as it is only able to attend a fraction of the on-site inspections and specialist college meetings for cross-border groups internal models.
- 6.3. EIOPA, working closely with technical experts from its members, took the following actions in respect of internal models for cross-border groups, where the approval of the application to use an internal model and of subsequent major changes is taken jointly by the relevant members of the college:
 - issuing an Opinion on External Models and Data, which ensured that supervisors received sufficient information to assess internal models that included components from third-party models,
 - developing the Common Application Package, with its use recommended in an EIOPA Opinion; this contributed to the efficiency of the application processes across Europe,
 - issuing an Opinion on the modelling of sovereign exposures and the use of comparative studies within and across countries, both of which are intended to increase convergence,
 - developing Good Practice papers on the Joint Decision process within colleges and on various quantitative and qualitative aspects of model assessment, again with the aim of promoting consistent approaches by different supervisory authorities,
 - writing chapters on internal models for the supervisory handbook, and

- running several consistency projects to assess the consistency in different aspects of internal models across NCAs. These projects cover benchmarking market and credit risk calibrations, the modelling of sovereign risk, the modelling of a dynamic Volatility Adjustment and a comparative study into the modelling of non-life underwriting risk. EIOPA will issue a public update this month on the status of first three of these projects.

- 6.4. The lack of standardisation in the reporting of granular outputs from internal models hampers the use of the data in the quantitative reporting templates to generate indicators and compare models. EIOPA is working with Members to find ways to improve the consistency of reporting for internal models.
- 6.5. EIOPA's internal models experts have provided advice, especially to smaller authorities, and in a few cases fulfilled a facilitation role when the college members could not reach an agreement.
- 6.6. EIOPA has stood ready since the second half of 2015 to fulfil its formal mediation in the case of joint decisions on internal model applications, but to date has not been called upon to do so. Although there were difficult discussions in many of the colleges, in the end joint decisions (often including Terms and Conditions) without a request for EIOPA's mediation.
- 6.7. Based on the information gathered during college meetings and visits to national authorities, EIOPA's CoEIM on several occasions during the pre-application and formal application phase in 2014 and 2015 reported its findings and recommendations on convergence for internal models to the Board of Supervisors. This included the risks to the consistency of internal model approvals.

EIOPA's role in assessing and approving group internal models

- 6.8. Based on Article 347 (3) of the Delegated Regulation, national supervisory authorities do not consider EIOPA to be a "concerned supervisor" in the joint decisions about internal models in colleges. This means that EIOPA has not in general received the formal application materials (e.g. IM documentation) or other materials (e.g. the exchange of supervisors' views). Where EIOPA has participated in the relevant college meeting or on-site inspection, presentations and draft versions of decisions have usually been available as part of the papers provided before or during the meeting.
- 6.9. As far as it knows, EIOPA has been invited to participate in all on-site inspections for cross-border internal models over the past three years. EIOPA has had to prioritise the attendance of its small number of internal model experts.

Cooperation among members of the college

- 6.10. EIOPA's observations are that the planning and running of on-site inspections and college meetings related to internal models has improved in recent years and is now without significant problems.
- 6.11. Internal models have been and continue to be an innovative and complex aspect of the supervision of undertakings and different supervisory authorities have different views on the relative importance of certain aspects of models and the range of acceptable modelling practices. In most cases, the concerned supervisory authorities were able to resolve differing views or agree how a joint decision could be made with the use of terms and conditions (Art. 231 of Solvency II Directive).

- 6.12. In the run-up to the first wave of model approval decisions at the end of 2015, EIOPA noted that there were several cases where a group chose to remove one or more countries from the scope of the group internal model application where the group had concerns that a joint decision would not be reached in time for a Day 1 approval.

7 Group capital add-ons

- 7.1. Of the four national supervisory authorities that have currently imposed a capital add-on on at least one solo undertaking, only one authority has used group capital add-ons.
- 7.2. EIOPA has published the report required under Article 52 of Solvency II in December 2017. This report includes an analysis of the use of capital add-ons at solo and group level.

ANNEX – issues for consideration by EIOPA in the request from the Commission

Application of Title III

1. Any problems concerning the definition of group supervision.
2. Any new structures which have emerged that could require group supervision and are not identified in Article 213 of Directive 2009/138/EC.
3. Any cases in which the participation of EIOPA to assist the National Supervisor to delimit the scope of the group supervision was requested.
4. Any cases in which Article 216 of Directive 2009/138/EC was applied or in which it was argued that the ultimate parent insurance or reinsurance undertaking, insurance holding company or mixed financial holding company should be subjected at national level to group supervision in cases of groups where the ultimate parent undertaking is in another Member State. Particular regard should be paid to any difficulties that arose during this process.
5. Any cases in which a decision under Article 217 of Directive 2009/138/EC to extend subgroup supervision to cover several Member States was taken or it was requested to take such a decision. Particular regard should be paid to any difficulties that arose during this process.
6. To what extent relevant information on supervisory action taken on solo level is shared within the college.
7. EIOPA's initiatives targeted at ensuring supervisory convergence in group supervision.

Functionality of the Colleges of Supervisors of Supervisory and Cooperation of Authorities within them

8. Any cases in which any supervisory authorities concerned referred a

matter to EIOPA in accordance with Article 19 of Regulation (EU) No 1094/2010 regarding:

- approval and major changes of internal models;
 - supervision of group solvency for groups with centralised risk management;
 - designation of the group supervisor;
 - the exercise of rights and duties of the group supervisor and the other supervisors of the college of supervisors;
 - cooperation and exchange of information between supervisory authorities;
9. Any cases in which mediation in the issues listed in the point number 68 finished with an agreement or with a decision of EIOPA, including the reasons why it was not possible to find an agreement between NSA.
 10. Any cases in which the decision of the EIOPA panel in the issues listed in point number 68 was rejected under the process established in Article 41(2) and (3) of Regulation (EU) 1094/2010, and the final decision was taken by the group supervisor.
 11. Any cases in which different criteria are observed by the NSAs of a college of supervisors in relation to the quality of own funds, subordinated debt, or other items, including the process followed to align their approaches and the way in which the colleges of supervisors deal with such cases.
 12. Any issues related to inconsistent practices of the valuation of the assets and liabilities between different group undertakings, and how these issues were addressed in the college of supervisors.
 13. Any difficulties identified by EIOPA to carry out joint on-site inspections, or where EIOPA was not invited to participate in on-site inspections.

14. Any cases in which problems of cooperation among supervisory authorities arose during the joint on-site examinations.
 15. Related to on-site examinations, any cases in which the findings were not communicated to the college of supervisors.
 16. Any cases of centralised risk management agreements reached with an explanation of reasons argued by the entities to submit the application for permission to be subject to Article 238 and 239 of Directive 2009/138/EC. Particular regard should be paid to any difficulties that arose during this process.
- a significant system of governance deviation;
 - a significant risk profile deviation following the application of the matching adjustment, volatility adjustment or transitional measures in Art 308 c) and 308 d) of Directive 2009/138/EC;
24. Any cases in which other supervisory measures were taken by supervisory authorities or the college of supervisors before taking the last recourse measure of a capital add-on.
 25. Any cases in which the supervisory authorities or the college of supervisors determined that such other measures were ineffective or inappropriate.

Group Internal Models

17. Any cases in which information relating to group internal models, including the application, was not shared with other college members.
 18. Any cases in which there were differences between the quality and quantity of information on group internal models circulated within the colleges of supervisors.
 19. Any cases of additional requests voiced within the colleges of supervisors related to the information provided by the group supervisor.
 20. Any cases in which different views on the supervision of group internal models were discussed and reconciled within a college.
26. Any practices of the group supervisors on the calculation of the capital add-on to ensure that the groups comply with Article 101(3) of Directive 2009/138/EC.
 27. Any cases of disputes related to capital add-on referred to EIOPA and their outcome.
 28. Any supervisory practices concerning setting capital add-ons where a supervisory authority considered that the risk profile of the ultimate parent undertaking at national level deviates significantly from the internal model approved at group level.
 29. The practices established within the college of supervisors to review the capital add-ons at least one a year.

Supervisory Practices concerning Setting the Capital Add-Ons

21. Any cases in which the use of capital add-ons was set at group level.
22. Any cases in which capital add-ons were imposed on undertakings which are part of a group.
23. Any cases in which the capital add-ons on group level, were set up based on:
 - a standard formula significant risk profile deviation;
 - an internal model significant risk profile deviation;