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EUROPEAN INSURANCE
AND OCCUPATIONAL PENSIONS AUTHORITY

EIOPA's first set of Implementing Technical Standards for Solvency II

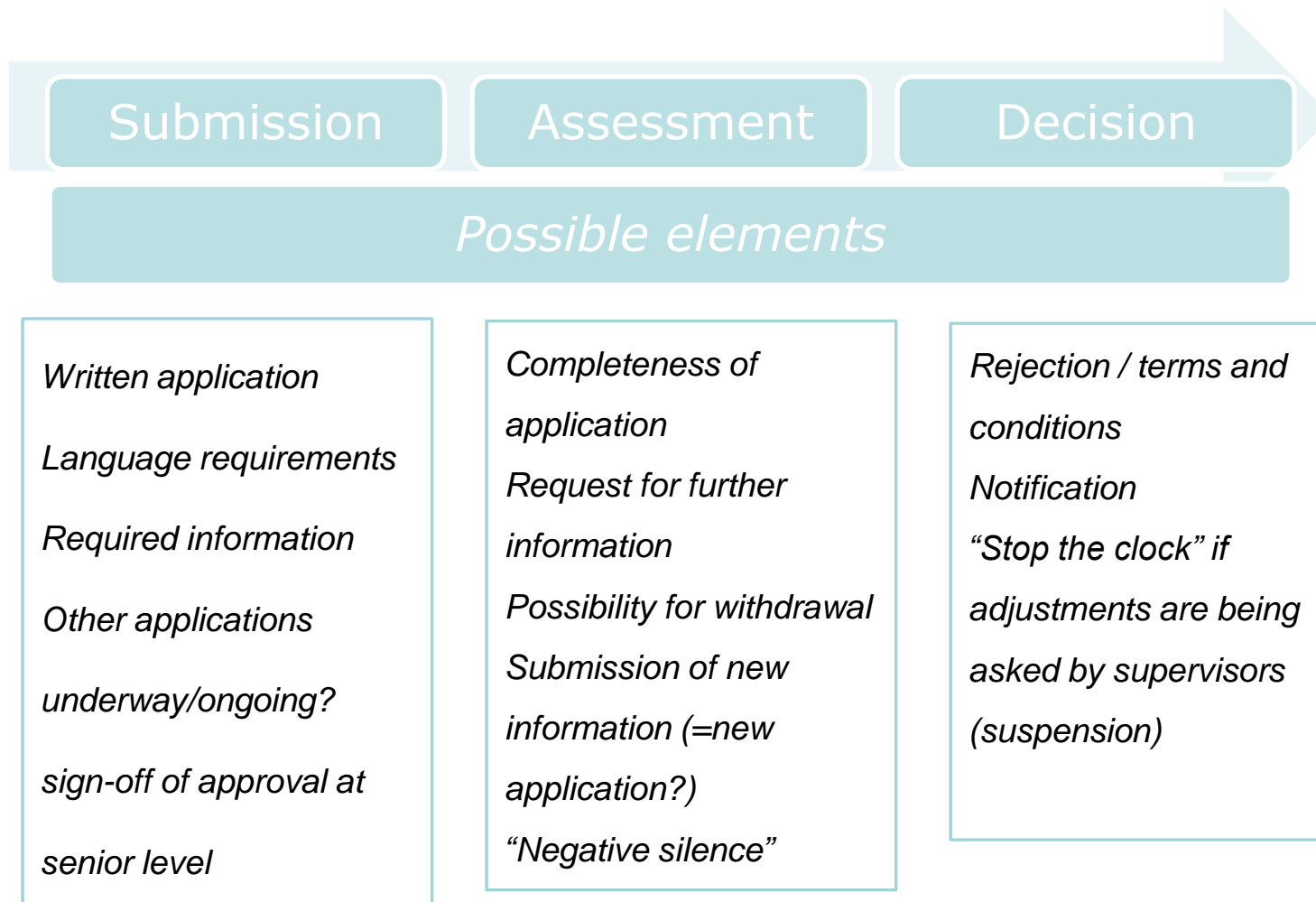
IRSG meeting 21 February 2014, Frankfurt

- What are “approval processes”
- What are “ITS”
- Preview of the content of the draft ITS and areas of attention for the IRSG in forming its opinion
 - Introduction by the experts!
- Reminder of the timeline

- What is an “approval process”:
 - the process through which undertakings shall go in order to obtain the approval by their supervisor of (the application of) particular elements of the prudential framework

- Why is an approval process necessary?
 - Prior scrutiny of the quality and admissibility by the supervisor
 - Importance of the elements, their complexity, their non-standard nature,...

A “generic” approval processes



- Legal instrument that can be drafted by EIOPA, but requires the endorsement by the Commission
- Can be developed only in areas specifically set out in legislative acts (e.g. SII Directive as amended by the OMDII)
- EIOPA Regulation art. 15: *“The content shall be technical, shall not imply strategic decisions or policy choices and [...] shall determine the conditions of application of [legislative] acts (e.g. SII Directive and its implementing measures)”*
- *Ratio legis*: “forms, templates and procedures”

- Endorsement by COM: COM decision within 3 months of receipt
- Information to Parliament and Council (no formal scrutiny)
- Endorsement in part or with amendments “where the Union’s interests so require”
 - Send back to EIOPA with explanation; EIOPA has six weeks to amend and resubmit in the form of a “formal opinion to the COM”, with copy to the European Parliament and Council
 - In absence of reaction by EIOPA, COM may adopt with the amendments or reject
- In case EIOPA does not submit within the time frame
 - COM may request a draft within a new time limit,
 - If EIOPA does not comply with new time limit, COM may adopt without a draft from EIOPA, but with duty to consult and with review by EIOPA within 6 weeks of COM draft

- Why ITS on approval processes?
 - Ensure convergence of supervisory practices in a binding manner
 - Ensure legal certainty, transparency and accountability of decision-making
- OMDII requires ITS for the approval processes for Matching Adjustment, Ancillary Own Funds, Undertaking-Specific Parameters, Internal Models, Special Purpose Vehicles
- Start of launch of approval processes on 1 April 2015 (art. 308a OMDII)

Key features of the first set of ITS

Legal quality

- Alignment with legal empowerment of the OMDII
- Quality of the drafting required for a legal text

Consistency

- Differences between the approval processes shall be justified

Proportionality for supervisors

- Amount of applications to be expected?
- Can the process be managed with resources available?

Proportionality for undertakings

- Administrative burden regarding timing, requests for further information, documentation, formalities ...?
- Relevance of the requirements for appropriate risk management

Protection of policyholders

- Do the requirements ensure that undertakings duly consider the risks they take?
- What are the safeguards (rejection of application, conditions,...)

Overview of the ITS and their key features

1. Procedures for the approval of the matching adjustment

- What is a matching adjustment?

The cash flows of assets and liability have similar characteristics to maturity, so these assets are not exposed to spread risks in short-term.

The matching adjustment is used to adjust the relevant risk-free interest rate term structure for the calculation of the best estimate in line with the spread movements of their assets, in order to avoid that changes of assets spreads impact the amount of own funds of these undertaking

- Why approval procedure ITS on matching?

- ✓ To ensure the cash-flows of assets and liabilities are matched and assets can only be replaced for the purpose of retaining the matching where the expected cash-flows have materially changed such as in the case of the downgrade or default of a bond.
- ✓ To ensure that the insurance undertakings can hold their assets to maturity
- ✓ To ensure adequate transparency by ensuring the impact of the matching adjustment on their financial position will be publically disclosed

Procedures for the approval of the matching adjustment (cont'd)

- Key elements of the ITS:
 - o Application should contain evidence that the assets and liabilities meet the criteria set out in the Directive/DA
 - requirements related to assigned portfolios of assets, the portfolio of insurance or reinsurance obligations and the cash-flow matching
 - o Application should be made on existing portfolio level
 - Asset by asset reporting
 - o Supervisor assessment procedure
 - 30 days to issue a receipt of application completeness
 - 6 months to complete approval decision with 'freezing clock' required by undertaking

2. Procedures for the approval of Ancillary Own Funds

- What are ancillary own funds?
 - *Ancillary own funds are items other than basic own funds that can be called up to absorb losses.*
 - *Examples are; unpaid share capital or initial fund that has not been called up; letters of credit and guarantees; any other legally binding commitments received by insurance and reinsurance undertakings (future claims for mutuals).*
 - *The amounts of ancillary own fund items are subject to prior supervisory approval.*
 - *Ancillary own funds can cover part of the solvency capital requirement, but not the minimum capital requirement.*
 - *Where an ancillary own fund item has been paid in or called up, it is treated as an asset and ceases to form part of ancillary own fund items.*

Procedures for the approval of Ancillary Own Funds (cont'd)



- Key elements of the ITS:
 - o Separate written application for each ancillary own fund item
 - o Application for approval of either (1) a monetary amount for each ancillary own fund item; or (2) a method to determine the amount of each ancillary own fund item
 - o Actions to be taken by the undertaking before applying for approval
 - o Evidence that the item meets the criteria set out in the Directive and delegated acts (e.g. status of counterparties and ability to pay, legal form and enforceability, information on past calls).
 - o Procedures to ensure ongoing satisfaction of the criteria necessary by the undertaking and the supervisor

3. Procedures for the approval of USP - approval process

- What are Undertaking Specific Parameters?

Certain risk parameters that can be used by the undertaking in the calculation of the solvency capital requirement, where this allows for the true underwriting risk profile of the undertaking to be better reflected.

The solvency capital requirements for these USP are calculated by standard methods using the undertaking's data. These standardised methodologies to derive these parameters will be included in the delegated acts.

Procedures for the approval of USP - approval process (cont'd)

- Key elements of the ITS:
 - Justification on choice of the parameters, segments and methods to calculate the parameters
 - Assessment of how the criteria for completeness, accuracy, and appropriateness of the data are fulfilled
 - Reversion to standard formula parameters – only in duly justified circumstances and subject to the approval of the supervisory authorities .
 - Requirement from the supervisory authority to use undertaking-specific parameters

4. Procedures for the approval of IMs and of major changes to an IM and changes to the policy for changing an IM

- What are internal models and why a policy (and approval process) for changing the internal model:

An internal model is a risk management system developed by an insurer to analyse the overall risk position, to quantify risks and to determine the economic capital required to meet those risks. (SII Glossary CEA/GC 2008). The purpose of an internal model is to fully integrate processes of risk and capital management within the insurer. It is the responsibility of undertakings to update their internal models in order to keep the model and its methodologies accurate and up-to-date. Supervisors shall approve major changes to the internal model and be satisfied that the model still complies with the test and standards for model approval after any changes have been applied. For changes a policy should be approved as part of the initial model approval. Changes to this policy shall also be approved by supervisors.

Procedures for the approval of IMs and of major changes to an IM and changes to the policy for changing an IM (confidential)

- Key elements of the ITS:
 - o Application package should contain evidence that the internal model meet the criteria set out in the Directive/DA
 - o rules for the assessment of the application by supervisors
 - o content of decision
 - o transitional plan provisions to extent scope of model

5. Joint decision process for group internal models

- What is a group internal model:

A group internal model is an internal model which is used by a group to calculate both the Group Consolidated SCR and the solo SCR of at least one related undertaking.

- Key elements of the ITS:
 - o provisions to ensure uniform conditions of application of the joint decision process by supervisors concerned in the college, with a view to facilitating joint decisions

- What is an SPV

SPVs are independent legal entities that are established by one or more sponsors. The establishment of separate legal entities shall create an independent third party to which insurance risks and assets can be transferred. After the establishment and the transfer of assets, portfolios or insurance risk, the sponsor will not have any control over the SPV and the SPV will not have any rights against the sponsor. In an insurance environment SPVs would assume risks from insurance or reinsurance undertakings. The structure of the SPV has to accommodate that this risk transfer is effective.

- Key elements of the ITS: ensuring the transfer's risk effectiveness and policyholder protection:
 - Analysis of the transfer itself and the structure, i.e. independence, of the SPV
 - Timelines and minimum documentation requirements
 - Details on the fully funded requirement
- Other ITS empowerments for SPVs:
 - the cooperation and exchange of information between supervisory authorities regarding SPVs
 - formats and templates for accounting, prudential and statistical information to be reported by SPVs

Timeline for the ITS set 1 and the IRSG

