Commission Delegated Regulation (EU) 2019/981 of 8 March 2019 amending Delegated Regulation (EU) 2015/35 supplementing Directive 2009/138/EC of the European Parliament and of the Council on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II) (Text with EEA relevance)

COMMISSION DELEGATED REGULATION (EU) 2019/981

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(Text with EEA relevance)

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II)[(1)] and in particular Article 35(9), point (a) of Article 50(1), Article 56, points (a) and (b) of Article 86(1), Article 97(1), points (a), (b), (c), (e), (f), (fa), (i), (j), (k) and (l) of Article 111(1), Article 211(2) and Article 234 thereof,

Whereas:

(1) Experience gained by insurance and reinsurance undertakings during the first years of application of Directive 2009/138/EC should be used to review the methods, assumptions and standard parameters when calculating the Solvency Capital Requirement standard formula.

(2) The Commission proposal for a new Regulation establishing the InvestEU Programme[(2)] focusses on addressing EU-wide market failures and sub-optimal investment situations. That proposal includes the establishment of the InvestEU Advisory Hub that should support the development of a robust pipeline of investment projects and the InvestEU Portal that should provide investors with an easily accessible and user-friendly database of investment projects. InvestEU will thereby support investments in finance for small and medium-sized businesses in the form of bonds, loans or private equity as well as other long-term investments in equity. The standard formula for the calculation of the Solvency Capital Requirement does not provide for specific rules for investments in privately placed debt, private equity and long-term investments in equity. In light of the expected improvement in the accessibility of such investments by means of the InvestEU portal, such specific rules should be introduced. In addition, in light of the Action Plan on Building a Capital Markets Union of 30 September 2015, more investments in Europe should be encouraged and access to equity and debt funding for European small and medium-sized enterprises should be facilitated. The prudential treatment of private equity and privately placed

debt should therefore be amended to remove unjustified barriers to investments in those asset classes.

(3) In order to ensure a level playing field between economic operators active in the insurance sector and economic operators active in other financial sectors, some of the provisions applicable to insurance and reinsurance undertakings should be aligned with the provisions applicable to credit and financial institutions, to the extent that such an alignment is commensurate with their different business models.

(4) Trade exposures to qualifying central counterparties (CCPs) benefit from the multilateral netting and loss-sharing mechanism provided by qualifying CCPs. Those trade exposures have lowered counterparty credit risk and should therefore be subject to lower own funds requirement than exposures to counterparties not benefiting from CCP mechanisms. In accordance with Article 111(1)(fa) of Directive 2009/138/EC, the calculation of counterparty default risk with the standard formula should treat trade exposures to qualifying CCPs in a manner that is consistent with the capital requirements for such exposures applicable to credit institutions and financial institutions.

(5) In order to contribute to the Union's objective of long-term sustainable growth, investments by insurers in privately placed debt should be facilitated. To that end, criteria should be established that allow for the assignment to credit quality steps 2 or 3 of bonds and loans for which a credit assessment by a nominated ECAI is not available, on the basis of the insurance or reinsurance undertaking's own internal credit assessment.

(6) Substantial changes in the data used for the determination of the technical information on the relevant risk-free interest rate term structures may lead to a situation where data sources that were used in the past are no longer available. Furthermore, improved data availability may render obsolete the techniques used for the determination of the technical information on the relevant risk-free interest rate term structures. A substantial change in market conditions may also necessitate a re-assessment of parameters, including the ultimate forward rate, the starting point for the extrapolation of risk-free interest rates or the convergence period to the ultimate forward rate. Conditions should therefore be laid down to assess whether potential changes to data and techniques used for the determination of the technical information on the relevant risk-free interest rate term structure are commensurate with the objectives of transparency, prudence, reliability and consistency of the methods to determine the technical information on the relevant risk-free rate term structure over time. To this end, EIOPA should submit to the Commission an assessment of the impact of modified techniques, data specifications or parameters and the proportionality of the modification with respect to the substantial change in the data.

(7) The objective of transparent, prudent, reliable and consistent methods to determine the technical information on the relevant risk-free interest rate term structures over time should also apply at the level of the components, and in particular, the volatility adjustment. In order to ensure transparency, prudence, reliability and consistency over time, the method to determine the technical information on the volatility adjustment

applied by the European Insurance and Occupational Pensions Authority (EIOPA), in particular the activation of the country component as set out in Article 77d(4) of Directive 2009/138/EC, should be re-examined where evidence shows that the method fails to meet the objectives, and as part of the Commission review under Article 77f(3) of Directive 2009/138/EC.

(8) Own–fund items in the form of paid-in subordinated mutual member accounts, paid-in preference shares and the related share premium account, and paid in subordinated liabilities, may provide for a partial principal loss absorbency mechanism for cases where the Solvency Capital Requirement is breached during three consecutive months. Criteria should be established that specify to what extent such items qualify as Tier 1 own funds.

(9) Losses of basic own funds due to tax effects when the principal loss-absorbing mechanism is triggered should be avoided. Insurance and reinsurance undertakings should therefore be able to request a waiver of the application of that mechanism. Before granting the waiver however, supervisory authorities should assess whether there is a high and credible likelihood that the tax effects of the mechanism could significantly weaken the solvency position of an insurance or reinsurance undertaking.

(10) A level playing field between economic operators in the insurance sector and in other financial sectors should be ensured. Insurance and reinsurance undertakings should therefore have the possibility, subject to prior supervisory approval, to repay or redeem an own-fund item within the first five years after the date of its issuance in case there is an unexpected change in the regulatory classification of the own-fund item which is likely to result in the exclusion of that item from the own funds, or in case there is an unexpected change in the applicable tax treatment of that item.

(11) The look-through approach should ensure that the risks the insurance or reinsurance undertaking is exposed to are properly captured, irrespective of the undertaking's investment structures. That approach should therefore be applied to undertakings related to that insurance or reinsurance undertaking, that have as their main purpose the holding or management of assets on behalf of that insurance or reinsurance undertaking.

(12) Where the look-through approach cannot be applied to a collective investment undertaking or investment packaged as funds, insurance or reinsurance undertakings should be allowed to use a simplified approach based on the last reported asset allocation of the collective investment undertaking or fund, provided that that simplified approach is proportionate to the nature, scale and complexity of the risks concerned.

(13) The lapse risk sub-modules require complex calculations based on the level of single insurance policies. Where such complexity is not proportionate to the nature, scale and complexity of the risks falling under those sub-modules, it should be possible to base the calculations for those sub-modules on groupings of insurance policies, rather than on single insurance policies, unless such groupings would lead to a material error.

(14) The calculation of natural catastrophe risk with the standard formula should account for the nature, scale and complexity of the exposure of the insurance or reinsurance undertakings to that risk. The calculation of natural catastrophe risk with the standard

formula requires that insurance and reinsurance undertakings map their sum insured in risk zones. Not all insurance and reinsurance undertakings have the information on risk zone level required for that calculation in their internal systems, and for those undertakings it may be costly to produce this information. Those undertakings should therefore be able to base their calculation on groupings of risk zones where such grouping is well substantiated and proportionate to the exposure.

(15) The calculation of the capital requirement for the fire risk sub-module of the standard formula requires that insurance and reinsurance undertakings identify the largest fire risk concentration. In order to limit the calculation burden, insurance or reinsurance undertakings should be able to restrict their identification process for the largest fire risk concentration to the surroundings of their largest fire risk exposures, provided that that approach is proportionate to the nature, scale and complexity of the exposure to fire risk of the insurance or reinsurance undertakings.

(16) The simplified calculations of the capital requirement for life and health mortality risk sub-modules of the standard formula should be amended to reflect that the capital at risk of insurance policies may vary over time.

(17) The cost for acquiring ratings for the calculation of the Solvency Capital Requirement using the standard formula should be proportionate to the nature, scale and complexity of the associated asset risk. Insurance and reinsurance undertakings that have nominated an external credit rating agency should therefore be able to use a simplified calculation for those parts of the debt portfolio for which external ratings are not provided by the that external credit rating agency.

(18) The standard formula calculation of the Solvency Capital Requirement for counterparty default risk requires insurance and reinsurance undertakings to take into account the share of the counterparty's assets that are subject to collateral arrangements. A disproportionate burden in the calculation with the standard formula should be avoided. Insurance and reinsurance undertakings using the standard formula for the calculation of the Solvency Capital Requirement for counterparty default risk should therefore be able to calculate the Solvency Capital Requirement for counterparty default risk on the basis of the assumption that more than 60 % of the counterparty's assets are subject to collateral arrangements.

(19) Insurance and reinsurance undertakings using the standard formula for the calculation of the Solvency Capital Requirement for counterparty default risk have to use a specific formula for the calculation of the capital requirement for counterparty default risk on type 1 exposures where the standard deviation of the loss distribution of type 1 exposures is lower than 7 %. Disproportionate burden when calculating that requirement should be avoided. Insurance and reinsurance undertakings should therefore be able to calculate the capital requirement for counterparty default risk on type 1 exposures using the same formula that is applied where the standard deviation of the loss distribution for type 1 exposures is between 7 % and 20 %.

(20) The calculation of the risk mitigating effect on underwriting risk is complex and may be a disproportionate burden for insurance and reinsurance undertakings operating in non-life lines of business. It is therefore appropriate to enable insurance and reinsurance

undertakings to use a simplified formula, provided that the use of that simplified formula is proportionate to the nature scale and complexity of the undertakings' counterparty risk profile.

(21) The risk charge for premiums for future contracts should not unduly penalise contracts with an initial term of more than one year in order to take into account the lower risk associated to future premiums from contracts with longer terms. Therefore, for future contracts the term of which is more than one year, the volume measure for non-life and NSLT health premium and reserve risk should account for only 30 % of future premiums.

(22) The actual risk exposure of the undertaking in the calculation of the Solvency Capital Requirement for natural catastrophe risk should be reflected in the calculation of the Solvency Capital Requirement with the standard formula. The calculation of the Solvency Capital Requirement for natural catastrophe risk with the standard formula should therefore take into account contractual limits for the compensation for natural catastrophes.

(23) The calculation of the Solvency Capital Requirement for man-made catastrophe risk should reflect the risks that insurance and reinsurance undertakings are exposed to. The scenario-based calculations of that requirement for marine, aviation and fire risk should therefore be based on the largest exposures, after deduction of amounts recoverable from reinsurance or special purpose vehicles.

(24) It is not appropriate to apply the tanker collision scenario of the marine risk submodule to pleasure craft or rigid inflatable boats. That scenario should therefore only be applicable to vessels with a minimum sum insured of at least EUR 250 000.

(25) Direct investments by insurers in unlisted equity can contribute to the Union's objective of long-term sustainable growth. Those investments should therefore be facilitated. When calculating the capital requirement for equity risk with the standard formula, portfolios of high-quality unlisted equity investments should therefore be able to benefit from the same treatment as equities that are listed in regulated markets. Criteria should be established to ensure that a high-quality unlisted equity portfolio has a sufficiently small systematic risk.

(26) Insurers have an important role as long-term investors and equity investments are important for the financing of the real economy. Long-term equity investments by insurance and reinsurance undertakings should therefore be encouraged by aligning the treatment of long-term equity investments and strategic equity investments when calculating the Solvency Capital Requirement with the standard formula including the correlation matrices. To ensure the long-term character of the investments, a portfolio of long-term equity investments and other assets matching a portfolio of clearly identified insurance or reinsurance obligations should be introduced within the equity risk sub-module. To avoid regulatory arbitrage, the portfolio of assets and the portfolio of obligations should have similar values, and each of them should not represent more than half of the total size of the balance sheet of the insurance or reinsurance undertaking.