EIOPA-CP-14/049

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Consultation Paper on the draft proposal for Guidelines on the implementation of the long term guarantee adjustments and transitional measures

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Responding to this paper

EIOPA welcomes comments on the draft proposal for Guidelines on the implementation of the long term guarantee adjustments and transitional measures.

Comments are most helpful if they:

- contain a clear rationale; and
- describe any alternatives EIOPA should consider.

Please send your comments to EIOPA in the provided Template for Comments, by email Consultation_Set2@eiopa.europa.eu, by 2 March 2015.

Contributions not provided in the template for comments, or sent to a different email address, or after the deadline will not be processed.

Publication of responses

Contributions received will be published on EIOPA's public website unless you request otherwise in the respective field in the template for comments. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure.

Please note that EIOPA is subject to Regulation (EC) No 1049/2001 regarding public access to documents and EIOPA's rules on public access to documents[1].

Contributions will be made available at the end of the public consultation period.

Data protection

Please note that personal contact details (such as name of individuals, email addresses and phone numbers) will not be published. They will only be used to request clarifications if necessary on the information supplied.

EIOPA, as a European Authority, will process any personal data in line with Regulation (EC) No 45/2001 on the protection of the individuals with regards to the processing of personal data by the Community institutions and bodies and on the free movement of such data. More information on data protection can be found at https://eiopa.europa.eu/ under the heading 'Legal notice'.

[1] https://eiopa.europa.eu/fileadmin/tx_dam/files/aboutceiops/Public-Access-(EIOPA-MB-11-051).pdf

Consultation Paper Overview & Next Steps

EIOPA carries out consultations in the case of Guidelines and Recommendations in accordance to Article 16 (2) of the EIOPA Regulation.

This Consultation Paper presents the draft Guidelines and explanatory text.

The analysis of the expected impact from the proposed policy is covered under Annex I Impact Assessment.

Next steps

EIOPA will consider the feedback received and expects to publish a Final Report on the consultation and to submit the Consultation Paper for adoption by the Board of Supervisors.

1. Guidelines

Introduction

1.1. According to Article 16 of Regulation (EU) 1094/2010 of 24 November 2010 (hereafter EIOPA Regulation or the Regulation)[2] EIOPA is issuing Guidelines on the implementation of the long term guarantee adjustments and transitional measures in accordance with Article 77b, 77d, 308c and 308d of 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 (hereinafter "Solvency II Directive")[3].

1.2. These Guidelines aim at ensuring convergence of practices across Member States and supporting undertakings in implementing the volatility adjustment, the matching adjustment, the transitional on the risk-free interest rates and the transitional on technical provisions (known as "long-term guarantee adjustments and transitional measures"). In particular, these Guidelines focus on the interaction of the Long Term Guarantee (LTG) measures with the Solvency Capital Requirement (SCR), calculated in accordance with the standard formula, and the Minimum Capital Requirement (MCR). These Guidelines also deal with the calculation of future discretionary benefits where Long term guarantee adjustments and transitional measures are used. The calculation of the risk margin where Long term guarantee adjustments and transitional measures are used is also specified in these Guidelines. The rest of the Guidelines clarifies the application of the transitional measures on risk-free interest rates and on technical provisions.

1.3. These Guidelines are addressed to supervisory authorities under Solvency II.

1.4. If not defined in these Guidelines, the terms have the meaning defined in the legal acts referred to in the introduction.

1.5. The Guidelines shall apply from 1 April 2015.

Guideline 1 – Interaction between the volatility adjustment, the matching adjustment and the transitional measure on the risk-free interest rates and the interest rate risk SCR sub-module

1.6. Insurance and reinsurance undertakings using a volatility adjustment, a matching adjustment or a transitional measure on the risk-free interest rate should ensure that the amount of these adjustments remains unchanged after the application of the shocks to the basic interest rate term structure.

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[2] OJ L 331, 15.12.2010, p. 48–83
[3] OJ L 335, 17.12.2009, p. 1-155

Guideline 2 – Interaction between the volatility adjustment and the transitional measure on risk free interest rates and the spread risk SCR sub-module

1.7. Insurance and reinsurance undertakings applying a volatility adjustment and/or a transitional measure on the risk-free interest rates should ensure that the amount of these adjustments remains unchanged following a SCR shock on the spreads.

Guideline 3 - Interaction between the transitional measure on technical provisions and the SCR calculation

1.8. Insurance and reinsurance undertakings applying the transitional measure on technical provisions should ensure that the amount of the transitional deduction remains unchanged following a SCR shock.

Guideline 4 – Interaction between the transitional measure on technical provisions and the operational risk SCR module

1.9. When calculating the operational risk module, insurance and reinsurance undertakings applying a transitional measure in accordance with Article 308d of Directive 2009/138/EC at the level of technical provisions should consider that technical provisions without a risk margin equal the amount of technical provisions before application of the transitional measure minus the maximum between the risk margin and the amount of the transitional deduction.

1.10. Where the amount of the transition deduction is higher than the risk margin, this amount should be apportioned across TP_{life}, $TP_{life\text{-}ul}$ and $TP_{non\text{-}life}$ according to each component's contribution to the overall amount of the transitional deduction.

Guideline 5 – Interaction between the transitional measure on technical provisions and the MCR calculation

1.11. When calculating the linear minimum capital requirement, insurance and reinsurance undertakings applying a transitional measure in accordance with Article 308d of Directive 2009/138/EC at the level of technical provisions should consider that technical provisions without a risk margin equal the amount of technical provisions before application of the transitional measure minus the maximum between the risk margin and the amount of the transitional deduction.

1.12. Where the amount of the transitional deduction is higher than the risk margin, this amount should be apportioned across the technical provisions for non-life insurance and reinsurance obligations $TP_{(nl,s)}$, $TP_{(life,1)}$, $TP_{(life,2)}$, $TP_{(life,3)}$ and $TP_{(life,4)}$ referred in Article 204 of the Implementing Measures, according to each component's contribution to the overall amount of the transitional deduction.

Guideline 6 – Effects of Long term guarantee adjustments and transitional measures on policyholders' behaviour

1.13. When calculating future discretionary benefits, insurance and reinsurance undertakings should ensure that the increase of the risk-free interest rate term structure due to the application of a volatility adjustment, a matching adjustment or a transitional measure on the risk-free interest rate does not affect the assumptions on the likelihood that policyholders will exercise contractual options.

Guideline 7 – Interaction of the Long term guarantee adjustments and transitional measures with the risk margin calculation

1.14. For the purposes of calculating the risk margin in accordance with Article 38 of the Implementing Measures, insurance and reinsurance undertakings that apply a matching adjustment, a volatility adjustment, a transitional measure on the risk-free rate or a transitional measure on technical provisions should assume that the reference undertaking does not apply any of these measures.

Guideline 8 – Combination of a matching adjustment and a transitional measure on technical provisions

1.15. Insurance and reinsurance undertakings can apply to use both a matching adjustment and a transitional measure on technical provisions on the same insurance or reinsurance obligations, in accordance with Article 77b and Article 308d of Directive 2009/138/EC.

1.16. In such a case, the amount referred to in point 2(a) of Article 308d should be calculated with the matching adjustment at the first date of application of Directive 2009/138/EC.

Guideline 9 – Application of the transitional measure on risk-free rates to the whole portfolio of admissible obligations

1.17. Insurance and reinsurance undertakings should apply the transitional measure on risk-free rate to the whole of the admissible obligations.

Compliance and Reporting Rules

1.18. This document contains Guidelines issued under Article 16 of the EIOPA Regulation. In accordance with Article 16(3) of the EIOPA Regulation, Competent Authorities and financial institutions shall make every effort to comply with guidelines and recommendations.

1.19. Competent authorities that comply or intend to comply with these Guidelines should incorporate them into their regulatory or supervisory framework in an appropriate manner.

1.20. Competent authorities shall confirm to EIOPA whether they comply or intend to comply with these Guidelines, with reasons for non-compliance, within two months after the issuance of the translated versions.

1.21. In the absence of a response by this deadline, competent authorities will be considered as non-compliant to the reporting and reported as such.

Final Provision on Reviews

1.22. The present Guidelines shall be subject to a review by EIOPA.

2. Explanatory text

Guideline 4 – Interaction of the transitional measure on technical provisions with operational risk SCR module

When calculating operational risk SCR module, insurance and reinsurance undertakings applying a transitional measure in accordance with Article 308d of Directive 2009/138/EC at the level of technical provisions should consider that the technical provisions without a risk margin equal the amount of technical provisions before application of the transitional measure minus the maximum between the risk margin and the amount of the transitional deduction.

Where the amount of the transition deduction is higher than the risk margin, this amount should be apportioned across TP_{life}, $TP_{life\text{-}ul}$ and $TP_{non\text{-}life}$ according to each component's contribution to the overall amount of the transitional deduction.

2.1. The first paragraph of this guideline aims at ensuring that the risk margin is not deducted twice from technical provisions.

2.2. The second paragraph provides the approach that undertakings should follow to deduct from the relevant volume measures the transitional deduction where the transitional deduction is higher than the risk margin.

2.3. This guideline only applies where insurance and reinsurance undertakings does not apply the transitional on technical provisions at the level of homogeneous risk groups in accordance with Article 308d(1) of Directive 2009/138/EC. In the latter case, the apportionment of the transitional deduction is not needed since the respective volume measures of the operational risk based on technical provisions already take into account the effect of the transitional measure.

Guideline 5 – Interaction of the transitional measure on technical provisions with MCR calculation

When calculating the linear minimum capital requirement, insurance and reinsurance undertakings applying a transitional measure in accordance with Article 308d of Directive 2009/138/EC at the level of technical provisions should consider that the technical provisions without a risk margin equal the amount of technical provisions before application of the transitional measure minus the maximum between the risk margin and the amount of the transitional deduction.

Where the amount of the transition deduction is higher than the risk margin, this amount should be apportioned across TP(nl,s), TP(life,1), TP(life,2), TP(life,3) and TP(life,4) according to each component's contribution to the overall amount of the transitional deduction.

2.4. The first paragraph of this guideline aims at ensuring that the risk margin is not deducted twice from the technical provisions.

2.5. The second paragraph provides the approach that undertakings should follow to deduct from the relevant volume measures the transitional deduction where the transitional deduction is higher than the risk margin.

2.6. This guideline only applies where insurance and reinsurance undertakings do not apply the transitional on technical provisions at the level of homogeneous risk groups in accordance with Article 308d(1) of Directive 2009/138/EC. In the latter case, the apportionment of the transitional deduction is not needed since the respective volume measures of the operational risk based on technical provisions already take into account the effect of the transitional measure.

Guideline 6 – Effects of Long term guarantee adjustments and transitional measures on policyholder behavior

When calculating future discretionary benefits, insurance and reinsurance undertakings should ensure that the increase of the risk-free interest rate term structure due to the application of a volatility adjustment, a matching adjustment or a transitional measure on the risk-free interest rate does not affect the assumptions on the likelihood that policyholders will exercise contractual options.

2.7. To ensure that assumptions underlying the calculation of technical provisions are realistic, undertakings should avoid creating an immediate link between the assumptions on lapse rates and the use of long term guarantee adjustments and transitional measures. Where, in practice, surrender models rely on the level of the relevant risk-free interest rate term structure, undertakings should ensure that assumptions on policyholder behaviour are still realistic given the increase of the relevant risk-free interest rate term structure caused by the use of long term guarantee adjustments and transitional measures. Where this is not the case, adjustments should be made (e.g. by recalibrating thresholds).

Annex I: Impact Assessment

I. Procedural Issues and Consultation of Interested Parties

Introduction

1. The objectives of the Guidelines on long term guarantees (hereinafter LTG) are to increase consistency and convergence of professional practices for all types and sizes of undertakings across Member States and to support undertakings with respect to the application of so-called Long term guarantee adjustments and transitional measures (Transitional on Technical Provisions, Transitional on the Interest Rate, Matching Adjustment and Volatility Adjustment) in the context of the calculation of technical provisions under Directive 2009/138/EC and Directive 2014/51/EU. In particular, guidance is provided to clarify the interaction between assumptions underlying the technical provisions calculation and Long term guarantee adjustments and transitional measures in the calculation of technical provisions and in the context of Solvency Capital Requirement (hereinafter SCR) calculation.

2. In order to analyse the impact of the Guidelines, EIOPA will analyse the potential related costs and benefits in accordance with article 16 of the EIOPA Regulation. The analysis of costs and benefits is undertaken according to an Impact Assessment methodology.

Public Consultation

3. The draft Guidelines and its Impact Assessment are subject to a public consultation. Stakeholders' responses to public consultation will serve as a valuable input in order to revise the Guidelines.

II. Problem Definition:

4. The European Commission has defined the rules to set the assumptions for the calculation of technical provisions in articles 17 - 61 of the Implementing Measures for which the mandate is given in Article 86 of Directive 2009/138/EC. The Implementing Measures provide mostly principles for the calculation of technical provisions. Further requirements are defined for the calculation of the so called long term guarantee adjustments and transitional measures in Omnibus II. EIOPA's intention is to provide further guidance on how specific items in the calculation of technical provisions are influenced by the Long term guarantee adjustments and transitional measures on a standalone basis as well as in the context of SCR scenarios.

Baseline

5. When analysing the impact from proposed policies, the Impact Assessment methodology foresees that a baseline scenario is applied as the basis for comparing policy options. This helps to identify the incremental impact of each policy option considered. The aim of the baseline scenario is to explain how the current situation would evolve without additional regulatory intervention.

6. The baseline scenario is based on the current situation of EU insurance and reinsurance markets, taking account of the progress towards the implementation of the Solvency II framework achieved at this stage by insurance and reinsurance undertakings and supervisory authorities.

7. In particular the baseline includes:
   - The relevant content of Directive 2009/138/EC as amended by Directive 2009/51/EC.
   - The relevant Implementing Measures.

8. To measure the additional effects created by these Guidelines, EIOPA used the baseline described above. With respect to this baseline, EIOPA analysed which topics may be resolved/enhanced by the introduction of new Guidelines. These Guidelines should assure a common interpretation of the provisions defined in the baseline.

III. Objective Pursued

9. The objectives of the Guidelines are:
   - Objective 1: To ensure convergence of practice across Member States as regards the implementation of Long term guarantee adjustments and transitional measures.
   - Objective 2: To support undertakings in implementing the volatility adjustment, the matching adjustment, the transitional on the risk-free interest rates and the transitional on technical provisions (known as "long term guarantee adjustments and transitional measures").

10. These objectives are consistent with the following objectives for the Solvency II Directive:
    - advance supervisory convergence;
    - improved risk management of EU undertakings;
    - better allocation of capital resources; and
    - harmonised calculation of technical provisions.

IV. Policy Options

Policy Issue 1: Interaction between Long term guarantee adjustments and transitional measures and relevant SCR sub-modules (Guidelines 1-3).

11. For the scenario-based SCR standard formula sub-modules, the impact of a stress on basic own funds needs to be estimated and thus a recalculation of the technical provisions is required.

12. The spread risk sub-module assumes a change in market spreads which impacts the market value of assets. The volatility adjustment and the transitional measure on the risk-free interest rates are assumed not to change. For the calculation of the risk charge with respect to the respective sub-modules, undertakings need to take into account either the basic or the relevant interest rate term structure. For the interest rate risk sub module, it is assumed that the shocks apply to the basic risk free rate term structure only.

13. In order to ensure a harmonised application, guidance is needed on how the interest rate or spread risks interact with the Long term guarantee adjustments and transitional measures.

14. Taking into account the relevant legal background, it is considered that the Solvency II Directive and the Implementing Measures only allow for one option in the context of the standard formula.

15. **Option 1.1**: Under this option undertakings are required to assume no change in amounts of adjustments under SCR scenarios.

Policy Issue 2: **Interaction between the transitional measure on technical provisions and volume measures depending on technical provisions (Guidelines 4-5).**

16. The operational risk sub-module and the Minimum Capital Requirement (hereinafter MCR) are calculated on the basis of volume measures. Those volume measures are based on the amount of technical provisions. The transitional measure on technical provisions is assumed to be an adjustment to the amount of technical provisions. It is not specified in the baseline, whether or not the transitional measure on technical provisions needs to be incorporated in the aforementioned volume measures.

17. **Option 2.1:** Under this option undertakings are required to take into account the transitional in the respective volume measures according to their contribution to the transitional deduction.

18. **Option 2.2:** Under this option undertakings are not required to take into account the transitional on technical provisions in the respective volume measures.

19. **Option 2.3:** Under this option undertakings are required to take into account the transitional on technical provisions in the respective volume measures on a pro rata approach.

Policy Issue 3: **The effect of Long term guarantee adjustments and transitional measures on the assumptions underlying the technical provisions calculation (Guideline 6).**

20. According to the Implementing Measures, the projection of the asset returns should be consistent with a risk-free curve including, where relevant, a matching adjustment, a volatility adjustment or a transitional on the risk-free interest rates. The inclusion of those adjustments aims at ensuring that the same time value of money is applied for both the projection of asset returns and the discounting of liabilities. Nonetheless, assumptions on expected future developments and on policyholder behaviour should not be distorted where it is not realistic to assume an impact of the inclusion or not of the Long term guarantee adjustments and transitional measures in the risk-free curve used for the projection of asset returns on expected future developments and policyholder behaviour.

21. **Option 3.1:** Restrict undertakings to assume a direct impact of the Long term guarantee adjustments and transitional measures on policyholder behaviour's assumptions.

22. **Option 3.2:** Set additional requirements for undertakings to validate and explain assumptions on policyholder behaviour on request.

Policy Issue 4: Interaction of the Long term guarantee adjustments and transitional measures with the risk margin calculation (Guideline 7).

23. As described in Policy Issue 1 the Long term guarantee adjustments and transitional measures may impact the SCR, thus there may be an impact on the projected SCR which is the basis for the risk margin calculation as well in case the reference undertaking also applies the Long term guarantee adjustments and transitional measures.

24. For the risk margin calculation it is assumed that the reference undertaking invests in assets in order to minimise the market risks. In case the basic risk free rate applies, it is assumed that the reference undertaking invests in risk free assets. In case a Long term guarantee adjustments or transitional measure was applied, this assumption may need to be re-assessed.

25. Neither the impact on the balance sheet of the reference undertaking and thus as a consequence on projected SCR (which are necessary in the calculation of the risk margin) nor the assets the reference undertaking holds are specified in the baseline.

26. **Option 4.1:** The reference undertaking does not apply the Long term guarantee adjustments and transitional measures of the original undertaking, consequently the projected SCRs to be used for the purpose of the risk margin calculation does not take account of the impact of Long term guarantee adjustments and transitional measures. It is assumed that the reference undertaking invests in risk free assets.

27. **Option 4.2:** The reference undertaking applies the matching adjustment when the original undertaking applies a matching adjustment. For other Long term guarantee adjustments and transitional measures it would be assumed that those are not applied by the reference undertakings.

28. As a consequence when a matching adjustment would be applied, the SCR to be used in the projections takes into account the impact of Long term guarantee adjustments and transitional measures, as the balance sheet would be impacted. It would be assumed that the reference undertaking would be invested in risky assets included in the matching portfolio to receive the matching adjustment and therefore the undertaking would be exposed to market risks (e.g. spread risk).

29. In case other measures apply as well, the SCR to be used for the purpose of the risk margin calculation does not take account of the impact of other Long term guarantee adjustments and transitional measures.

30. **Option 4.3:** It would be assumed that the reference undertaking applies the Long term guarantee adjustments and transitional measures of the original undertakings as well. Consequently it would be assumed that the Long term guarantee adjustments and transitional measures are applied in order to calculate the projected SCR's. There would be need to modify the assumption that the reference undertaking would minimise its market risks, this could result in the assumption that the undertaking is invested in assets which are not risk-free.

Policy Issue 5: **Clarification of the scope of the transitional measure on technical provisions in connection with matching adjustment (Guideline 8).**

31. It has not been clarified in the baseline whether and how the matching adjustment and the transitional measure on technical provisions can be combined.

32. **Option 5.1:** The simultaneous application of transitional measures on technical provisions and matching adjustment is allowed to the same insurance and reinsurance obligations.

33. **Option 5.2:** The application of the matching adjustment does exclude the application of transitional measures on the same insurance and reinsurance obligations.

34. **Option 5.3:** No clarification on the application of matching adjustment and transitional measures is given.

Policy Issue 6: **Application of the transitional on risk-free interest rates (Guideline 9).**

35. It has not been clarified in the baseline whether undertakings have discretion for the choice on which obligations they want to apply the transitional on risk-free rates.

36. **Option 6.1** (only option): In case the transitional measure on risk-free interest rate is applied it needs to be applied to the whole admissible portfolio.

V. Analysis of Impact

37. The selected options are now analysed with regard to their expected impacts. A more detailed analysis will be done for the chosen options in regard to predefined stakeholder groups:

- Policyholders,
- Undertakings,
- National supervisory authorities (hereinafter, NSAs) and EIOPA,
- Financial Stability.

Impacts on policyholders

38. No direct impact on policyholders is to be expected. A clarification of the use of the Long term guarantee adjustments and transitional measures may lead to a broader application of these measures by insurance undertakings as the risk of a wrong use by the undertaking is reduced. As a consequence this may lead to reduced costs and a decrease of premiums.

Impacts on undertakings

39. Insurance undertakings get a higher level of clarification for the application of Long term guarantee adjustments and transitional measures. This may help to avoid frustrated costs for insurance undertakings as these measures are new to many undertakings. This always bears the risk of high implementation costs. In general the usage of Long term guarantee adjustments and transitional

measures will generate additional costs (e.g. additional systems, additional calculations) but it is expected that a wide application of Long term guarantee adjustments and transitional measures may lead to better solvency ratios.

Impacts on NSA's

40. No costs to be expected for NSA's. Furthermore, NSA's may benefit from a higher level of clarification and convergence. This also allows group supervision to be more efficient.

Impacts on financial stability

41. Generally no impacts on financial stability are to be expected. There may be an increase in systemic risk in case the undertaking make extensive use of Long term guarantee adjustments and transitional measures and would underestimate their technical provisions or other quantities.

42. No direct social impact is to be expected from those guidelines, therefore it is not analysed further.

VI. Comparison of Options

Policy Issue 1: Interaction between Long term guarantee adjustments and transitional measures and relevant SCR sub-modules.

43. **Option 1.1** (assuming no change in amounts of adjustments under SCR scenarios) does not result in additional costs for insurance and reinsurance undertakings and national supervisory authorities as the Guidelines only clarifies which is considered the sole possible option in the context of the standard formula.

Policy Issue 2: Interaction between the transitional measure on technical provisions and volume measures depending on technical provisions.

44. The preferred policy option is Option 2.1 (taking into account the transitional in the respective volume measures according to their contribution to the transitional deduction). The choice of this option does not lead to additional costs for undertakings as the calculations only need data which are available to the undertakings. Under this option the approach for the calculation is clarified. **Option 2.1** guarantees high convergence in the application of the transitional on technical provisions, therefore it reduces legal risks for insurance and reinsurance undertakings and national supervisory authorities.

45. **Option 2.2** was rejected, because it does not help to achieve an optimal level of convergence and further clarifications for the application of the transitional measures deem necessary.

46. **Option 2.3** was rejected, because the pro rata approach, although it would help to achieve convergence in application, is an overly simplistic approach. Such an approach is inappropriate firstly because a more sophisticated approach would not be too burdensome and secondly the high relevance of the MCR from a supervisory point of view demands an accurate calculation, therefore it is inappropriate to use simplistic methods to determine it.

Policy Issue 3: The effect of Long term guarantee adjustments and transitional measures on the assumptions underlying policyholder behaviour.

47. Both **Options 3.1** and **3.2** have a cost for insurance and reinsurance undertakings compared to the situation where no harmonisation is sought.

48. However this cost is deemed unavoidable to ensure that insurance and reinsurance undertakings value their technical provisions in a prudent, reliable and objective manner, as required by the Solvency II Directive.

49. Even though both **Options 3.1** and **3.2** can achieve the objective to ensure the character realistic of assumptions where Long term guarantee adjustments and transitional measures are used, **Option 3.1** (restricting undertakings to assume a direct impact of the Long term guarantee adjustments and transitional measures on policyholder behaviour's assumptions) was chosen because it represents the simplest and the most harmonised option.

Policy Issue 4: Interaction of the Long term guarantee adjustments and transitional measures with the risk margin calculation.

50. Policy **Option 4.1** (considering that the reference undertaking does not apply the Long term guarantee adjustments and transitional measures of the original undertaking) was chosen, because it is a technically feasible solution and allows a similar treatment of all Long term guarantee adjustments and transitional measures in with regard to the risk margin.

51. The intention is that all Long term guarantee adjustments and transitional measures are treated in the same way. For this policy issue that specifically means that a consistent treatment of the matching adjustment and the volatility adjustment with respect to the risk margin should be achieved. This would be ensured by **Option 4.1** and **Option 4.3**.

52. **Option 4.2** was rejected because it does not allow for a consistent treatment between the matching adjustment and the volatility adjustment.

53. **Option 4.3** was rejected as a higher level of clarity and harmonisation compared to the baseline would not have been achieved. It was also deemed unrealistic to assume flat adjustments with respect to the Long term guarantee adjustments and transitional measures over the horizon of projection of the SCRs. Finally, defining the precise conditions under which the underlying assumptions of the Long term guarantee adjustments and transitional measures in the Directive are compatible with the assumption of the Implementing Measures according to which the reference undertaking is to minimize the market risk has been considered out of the scope of these Guidelines.

Policy Issue 5: Clarification of the scope of the transitional measure on technical provisions in connection with the matching adjustment.

54. The preferred policy option is **Option 5.1** (allowing simultaneous application of transitional measure on technical provisions and matching adjustment). This option closes a gap on the interaction of the transitional measure on technical provisions and the matching adjustment.

55. **Option 5.1** does not create additional costs for insurance and reinsurance undertakings, in contrast by this clarification higher convergence can be achieved and legal risks for undertakings are reduced.

56. **Option 5.3** was rejected because it does not provide any convergence in application. **Option 5.2** was rejected because in Directive 2009/138/EC there is no explicit exclusion of the simultaneous application of these two measures as it is done for the simultaneous application of transitional on risk free rate and matching adjustment.

Policy Issue 6: Application of the transitional measure on risk-free interest rates.

57. The preferred policy option for this policy issue is option 6.1 (application to the whole admissible portfolio). This option was chosen because it avoids cherry picking by undertakings, when those were under specific circumstances allowed to apply the transitional on the risk-free interest rate on specific parts of their portfolio. Those could result in an underestimation of technical provisions. In addition this option allows for a harmonised calculation of technical provisions.