CONSULTATION PAPER ON THE REVISION OF THE GUIDELINES ON VALUATION OF TECHNICAL PROVISIONS

EIOPA-BoS-21/302
11 June 2021

European Insurance and Occupational Pensions Authority

Table of contents

Responding to this paper

1.1 EIOPA welcomes comments on the proposal for additional Guidelines on valuation of Technical Provisions.

1.2 Comments are most helpful if they:

a) contain a clear rationale; and

b) describe any alternatives EIOPA should consider.

1.3 Please send your comments to EIOPA by the **12th of November 2021** responding to the questions in the survey provided at the following link:

https://ec.europa.eu/eusurvey/runner/ValuationTPs

Contributions not provided using the survey or submitted after the deadline will not be processed and therefore considered as they were not submitted.

Publication of responses

1.4 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.

1.5 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].

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

Data protection

1.7 Please note that personal contact details (such as name of individuals, email addresses and phone numbers) will not be published.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 (EU) No 2018/1725 of the European Parliament and of the Council of 23 October 2018 on the protection of natural persons with regard to the processing of personal data by the Union institutions, bodies, offices and agencies and on the free movement of such data, and repealing Regulation (EC) No 45/2001 and decision No 1247/2002/EC. More information on data protection can be found at https://www.eiopa.europa.eu/legal-notice_en under the heading 'Legal notice'.

Consultation paper overview & next steps

1.8 EIOPA carries out consultations in the case of guidelines and recommendations in accordance with Article 16(2) of Regulation (EU) No

[1] Public Access to Documents

1094/2010. This Consultation Paper presents the draft Guidelines, including explanatory text.

1.9 The preliminary analysis of the expected impact from the proposed policy is covered under Section 4 Impact Assessment. This analysis will be complemented with the information request launched by EIOPA together with this consultation paper.

Next steps

EIOPA will consider the feedback received, publish a Final Report on the consultation and submit the Guidelines for adoption by its Board of Supervisors.

1. Introduction

1.10 In accordance with Article 16 of Regulation (EU) No 1094/2010[2] EIOPA issues these Guidelines to provide guidance on how insurance and reinsurance undertakings should apply the requirements of Directive 2009/138/EC[3] ("Solvency II Directive") and in Commission Delegated Regulation (EU) No 2015/35[4] ("Delegated Regulation"), on best estimate valuation

1.11 The Guidelines are addressed to competent authorities as defined in Article 4(2) of Regulation (EU) No 1094/2010.

1.12 The Guidelines apply to both individual undertakings and *mutatis mutandis* at the level of the group[5].

1.13 These Guidelines should be read in conjunction with and without prejudice to the Solvency II Directive, the Delegated Regulation and EIOPA's Guidelines on valuation of technical provisions. Unless otherwise stated in this document, the current guidelines of EIOPA's Guidelines on valuation of technical provisions remain unchanged and continue to be applicable.

1.14 During the 2020 review of Solvency II EIOPA identified several divergent practices regarding the valuation of best estimate, as presented in the analysis background document[6] to EIOPA's Opinion on the 2020 review of Solvency II. Divergent practices require additional guidance to ensure a convergent application of the existing regulation on valuation of technical provisions.

1.15 These Guidelines introduce new guidelines and amend current guidelines on topics that are relevant for the valuation of best estimate, including the use of future management actions and expert judgment, the modelling of expenses and the valuation of options and guarantees by economic scenarios generators and modelling of policyholder behaviour. EIOPA also identified the need for clarification in the calculation of expected profits in future premiums.

1.16 The section "Guidelines" provides the new and amended Guidelines. The section "Explanatory text" in addition to the explanatory text highlights the amendments to existing Guidelines.

1.17 If not defined in these Guidelines, the terms have the meaning defined in the Solvency II Directive.

1.18 These Guidelines shall apply from XX-XX-2022.

---

[2] Regulation (EU) No 1094/2010 Regulation (EU) No 1094/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Insurance and Occupational Pension Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/79/EC (OJ L 331, 15.12.2010, p. 48).

[3] Directive 2009/138/EC 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), (OJ L 335, 17.12.2019, p. 1)

[4] Commission Delegated Tegulation (EU) 2015/35 of 10 October 2014 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), (OJ L 12, 17.1.2015, p. 1)

[5] As defined in Article 212 (1) of the Solvency II Directive

[6] https://www.eiopa.europa.eu/content/opinion-2020-review-of-solvency-ii_en

2. Guidelines

Expert judgment

NEW: Guideline 24a – Materiality in assumptions setting

2.1. The insurance or reinsurance undertaking should set assumptions and use expert judgment, in particular taking into account the materiality of the impact of the use of assumptions with respect to the following Guidelines on assumption setting and expert judgement.

2.2. The insurance or reinsurance undertaking should assess materiality taking into account both quantitative and qualitative indicators and taking into consideration binary events, extreme events, and events that are not present in historical data. The insurance or reinsurance undertaking should overall evaluate the indicators considered.

NEW: Guideline 24b – Governance of assumptions setting

2.3. The insurance or reinsurance undertaking should ensure that all assumption setting and the use of expert judgement in particular, follows a validated and documented process.

2.4. The insurance or reinsurance undertaking should ensure that the assumptions are derived and used consistently over time and across the insurance or reinsurance undertaking and that they are fit for their intended use.

2.5. The insurance or reinsurance undertaking should approve the assumptions at levels of sufficient seniority according to their materiality, for most material assumptions up to and including the administrative, management or supervisory body.

NEW: Guideline 24c - Communication and uncertainty in assumptions setting

2.6. The insurance or reinsurance undertaking should ensure that the processes around assumptions, and in particular around the use of expert judgement in choosing those assumptions, specifically attempt to mitigate the risk of misunderstanding or miscommunication between all different roles related to such assumptions.

2.7. The insurance or reinsurance undertaking should establish a formal and documented feedback process between the providers and the users of material expert judgement and of the resulting assumptions.

2.8. The insurance or reinsurance undertaking should make transparent the uncertainty of the assumptions as well as the associated variation in final results.

NEW: Guideline 24d - Documentation of assumptions setting

2.9. The insurance or reinsurance undertaking should document the assumption setting process and, in particular, the use of expert judgement, in such a manner that the process is transparent.

2.10. The insurance or reinsurance undertaking should include in the documentation the resulting assumptions and their materiality, the experts involved, the intended use and the period of validity.

2.11. The insurance or reinsurance undertaking should include the rationale for the opinion, including the information basis used, with the level of detail necessary to make transparent both the assumptions and the process and decision-making criteria used for the selection of the assumptions and disregarding other alternatives.

2.12. The insurance or reinsurance undertaking should make sure that users of material assumptions receive clear and comprehensive written information about those assumptions.

NEW: Guideline 24e - Validation of assumptions setting

2.13. The insurance or reinsurance undertaking should ensure that the process for choosing assumptions and using expert judgement is validated.

2.14. The insurance or reinsurance undertaking should ensure that the process and the tools for validating the assumptions and in particular the use of expert judgement are documented.

2.15. The insurance or reinsurance undertaking should track the changes of material assumptions in response to new information and analyse and explain those changes as well as deviations of realizations from material assumptions.

2.16. The insurance or reinsurance undertaking, where feasible and appropriate, should use validation tools such as stress testing or sensitivity testing.

2.17. The insurance or reinsurance undertaking should review the assumptions chosen, relying on independent internal or external expertise.

2.18. The insurance or reinsurance undertaking should detect the occurrence of circumstances under which the assumptions would be considered false.

Biometric risk factors

AMENDED: Guideline 25 – Modelling biometric risk factors

2.19. Insurance and reinsurance undertakings should consider whether a deterministic or a stochastic approach is proportionate to model the uncertainty of biometric risk factors.

2.20. Undertakings should take into account the duration of the liabilities when assessing whether a method that neglects expected future changes in biometrical risk factors is proportionate, in particular in assessing the error introduced in the result by the method.

2.21. Undertakings should ensure, when assessing whether a method that assumes that biometric risk factors are independent from any other variable is proportionate, and that the specificities of the risk factors are taken into account. For this purpose, the assessment of the level of correlation should be based on historical data and expert judgment.

Expense allocation

NEW: Guideline 28a – Investment management expenses

2.22. Insurance and reinsurance undertakings should take into account administrative and trading expenses related to and amount of investments at least equal to Solvency II technical provisions plus the Solvency Capital Requirement.

2.23. Reimbursements of investment management expenses that the fund manager pays to the undertaking should be taken into account as other incoming cash flows. Where these reimbursements are shared with the policyholders or other third parties the relevant cash out flow should also be considered.

AMENDED: Guideline 30 – Apportionment of expenses

2.24. Insurance and reinsurance undertakings should allocate and project expenses in a realistic and objective manner, and should base the allocation on their long-term business strategies, on recent analyses of the operations of the business, on the identification of appropriate expense drivers and on relevant expense apportionment ratios.

2.25. Without prejudice to the proportionality assessment and the first point of this guideline, insurance and reinsurance undertakings should consider using, in order to allocate overhead expenses, the simplification outlined in Technical Annex I, when the following conditions are met:

a) the undertaking pursues annually renewable business;

b) the renewals must be reputed to be new business according the boundaries of the insurance contract;

c) the claims occur uniformly during the coverage period.

AMENDED : Guideline 33 – Changes in expenses

2.26. Insurance and reinsurance undertakings should ensure that assumptions with respect to the evolution of expenses over time, including future expenses arising from commitments made on or prior to the valuation date, are appropriate and consider the nature of the expenses involved. Undertakings should make an allowance for inflation that is consistent with the economic assumptions made and the dependency of expenses on other cash-flows of the contract.

Treatment of financial guarantees and contractual options

NEW: Guideline 37a - Dynamic policyholder behaviour

2.27. Insurance and reinsurance undertakings should base their assumptions on the exercise rate of relevant options on:

- statistical and empirical evidence, where it is representative of future conduct, and
- expert judgment on sound rationale and with clear documentation.

2.28. The lack of data for extreme scenarios should not be considered alone to be a reason to avoid dynamic policyholder behaviour modelling and/or the interaction with future management actions.

NEW: Guideline 37b – Bidirectional assumptions

2.29. When setting the assumptions on dynamic policyholder behaviour, insurance and reinsurance undertakings should consider that the dependency on the trigger event and the exercise rate of the option is usually bidirectional, i.e. both an increase and a decrease should be considered depending on the direction of the trigger event.

NEW: Guideline 37c – Option to pay additional or different premiums

2.30. Insurance and reinsurance undertakings should model all relevant contractual options when projecting the cash flows, including the option to pay additional premiums or to vary the amount of premiums to be paid, where the undertaking should estimate the amount of voluntary premiums expected to be received and the related obligations within the contract boundaries.

Future management actions

NEW: Guideline 40a – Comprehensive management plan

2.31. Insurance and reinsurance undertakings should ensure that the comprehensive future management actions plan that is approved by the administrative, management or supervisory body is either:

- a single document listing all assumptions relating to future management actions used in the best estimate calculation; or
- a set of documents, accompanied by an inventory, that clearly provide a complete view of all assumptions relating to future management actions used in best estimate calculation.

NEW: Guideline 40b – Consideration of new business in setting future management actions

2.32. Insurance and reinsurance undertakings should consider realistic assumptions on new business in setting future management actions and duly consider the consequences on other related assumptions. In particular, the application of contract boundaries should not influence such assumptions, for example regarding asset allocation, bond reinvestment or profit sharing.

Methodologies for the valuation of contractual options and financial guarantees

NEW: Guideline 53a – Use of stochastic valuation

2.33. Insurance and reinsurance undertakings should use stochastic modelling for the valuation of technical provisions of contracts whose cash flows depend on future events and developments, in particular those with material options and guarantees.

2.34. When assessing whether stochastic modelling is needed to adequately capture the value of options and guarantees, insurance and reinsurance undertakings should in particular, but not only, consider the following cases:

- Any kind of profit sharing mechanism where the future benefits depend on the return of the assets.
- Financial guarantees (e.g. technical rates, even without profit sharing mechanism), in particular, but not only, where combined with options (e.g. surrender options) whose dynamic modelling would increase the present value of cash flows in some scenarios.

Economic Scenario Generator

NEW: Guideline 57a – Market risk factors needed to deliver appropriate results

2.35. When assessing whether all the relevant risk factors are modelled with respect to the provisions of Article 22(3) and Article 34(5) of the Delegated Regulation, insurance and reinsurance undertakings should be able to demonstrate that their modelling adequately reflects the volatility of their assets and that the relevant sources of volatility are appropriately reflected.

2.36. In particular and among others, undertakings should consider:

- whether the value of the assets backing the liabilities and the assets return might depend on the level of the spread risk or default risk. If so, undertakings should analyse the relevance of modelling stochastic spread and default risk;
- using models that allow for the modelling of negative interest rates.

Expected Profits In Future Premiums ("EPIFP")

AMENDED: Guideline 77 – Assumptions used to calculate EPIFP

2.37. For the purpose of calculating the technical provisions without risk margin under the assumption that the premiums relating to existing insurance and reinsurance contracts that are expected to be received in the future are not received, undertakings should apply the same actuarial method used to calculate the technical provisions without risk margin in accordance with Article 77 of the Solvency II Directive, with the following changed assumptions:

- policies should be treated as though they continue to be in force rather than being considered as surrendered;
- regardless of the legal or contractual terms applicable to the contract, the calculation should not include penalties, reductions or any other type of adjustment to the theoretical actuarial valuation of technical provisions without a risk margin calculated as though the policy continued to be in force.

2.38. All the other assumptions (e.g. mortality, lapses, expenses…) should remain unchanged. This means that the undertakings should apply the same projection horizon, future management actions and policyholder option exercise rates used in Best Estimate calculation without adjusting them to consider that future premiums will not be received. Even if all assumptions on expenses should remain constant, the level of some expenses (e.g. acquisition expenses or investment management expenses) could be indirectly affected.

2.39. The actuarial function should always validate EPIFP calculation with specific reference to the methodology and underlying assumptions used by the undertaking.

NEW: Guideline 78 – Alternative approach to calculate EPIFP

2.40. Where the calculation as described in Guideline 77 would be too complex, a possible alternative approach is to identify EPIFP as the part of present value of future profits that relates to future premiums, which may be implemented using a formula design. This calculation should be subject to actuarial function validation.

3. Explanatory text

Expert judgement

All guidelines on expert judgement are identical to the guidelines on expert judgement included in the Guidelines on the use of internal models except for Guideline 24a – Materiality in assumptions setting, which has been slightly adapted to best estimate valuation.

NEW: Guideline 24a – Materiality in assumptions setting

The insurance or reinsurance undertaking should set assumptions and use expert judgment, in particular taking into account the materiality of the impact of the use of assumptions with respect to the following Guidelines on assumption setting and expert judgement.

The insurance or reinsurance undertaking should assess materiality taking into account both quantitative and qualitative indicators and taking into consideration ~~extreme losses conditions~~ **binary events, extreme events, and events that are not present in historical data**. The insurance or reinsurance undertaking should overall evaluate the indicators considered.

Explanatory text:

3.1. It is necessary to consider all potential events, including 'events not in data' and extreme events, also known as binary events within a financial context, to ensure that the best estimate reflects an expected value of the outcomes of all possible scenarios, as opposed to something less, such as an expected value of the outcomes of all reasonably foreseeable scenarios.

3.2. Examples of such events would include environmental issues such as global warming; and legislative or political changes that might impact the sustainability of the business model – either by increasing claim amounts or by reducing the volumes of new business.

3.3. Where there is a short history of representative data, the expert judgment as to the amount of weight to be placed on events that are not in that data is more likely to be material.

Biometric risk factors

AMENDED: Guideline 25 – Modelling biometric risk factors

Insurance and reinsurance undertakings should consider whether a deterministic or a stochastic approach is proportionate to model the uncertainty of biometric risk factors.

Undertakings should take into account the duration of the liabilities when assessing whether a method that neglects expected future changes in biometrical risk factors is proportionate, in particular in assessing the error introduced in the result by the method.

Undertakings should ensure, when assessing whether a method that assumes that biometric risk factors are independent from any other variable is proportionate, and that the specificities of the risk factors are taken into account. For this purpose, the assessment of the level of correlation should be based on historical data and expert judgment~~, as set out in the guidelines on expert judgement~~.

Expense allocation

NEW: Guideline 28a – Investment management expenses

Insurance and reinsurance undertakings should take into account administrative and trading expenses related to and amount of investments at least equal to Solvency II technical provisions plus the Solvency Capital Requirement.

Reimbursements of investment management expenses that the fund manager pays to the undertaking should be taken into account as other incoming cash flows. Where these reimbursements are shared with the policyholders or other third parties the relevant cash out flow should also be considered.

Explanatory text:

3.4. Investment management expenses could include administration expenses (expenses of recordkeeping of the investments' portfolio, salaries of staff responsible for investments, remunerations of external advisers, expenses connected with an investment trading activity and in some cases also remuneration for custodial services) and trading expenses (buying and selling of the portfolio securities).

3.5. The investment management expenses include all expenses to be incurred in servicing insurance and reinsurance obligations, which means that at least investments backing SCR requirement should be taken into account.

3.6. The calculation of the exact amount of expenses of technical provisions in accordance with the Guideline may require burdensome calculations because of the circular reference to technical provisions. Bearing that in mind, a proportionate methodology to calculate the investment expenses should be used. One simplification is that the undertaking takes into account all investment expenses.

3.7. Sometimes the fund manager pays back commissions to the asset manager (often called kick-backs). If the kick-backs are left to the undertakings and not directed further to e.g. policyholders or sales organisations, the kick-backs should be netted and considered as other incoming cash flows of the policy.

AMENDED: Guideline 30 – Apportionment of ~~overheads~~ expenses

~~Insurance and reinsurance undertakings should allocate overhead expenses in a realistic and objective manner, and should base the allocation on recent analyses of the operations of the business, on the identification of appropriate expense drivers and on relevant expense apportionment ratios.~~

Insurance and reinsurance undertakings should allocate and project expenses in a realistic and objective manner, and should base the allocation on their long-term business strategies, on recent analyses of the operations of the business, on the identification of appropriate expense drivers and on relevant expense apportionment ratios.

Without prejudice to the proportionality assessment and the first paragraph of this guideline, insurance and reinsurance undertakings should consider using, in order to allocate overhead expenses, the simplification outlined in Technical Annex I, when the following conditions are met:

a) the undertaking pursues annually renewable business;

b) the renewals must be reputed to be new business according the boundaries of the insurance contract;

c) the claims occur uniformly during the coverage period.

Explanatory text:

3.8. According to article 31(2) of the Delegated Regulation "*overhead expenses shall be allocated in a realistic and objective manner and on a consistent basis over time to the parts of the best estimate to which they relate*". This provision should also be applied to all expenses where the expenses may not be directed to one single cost point. Also, the title of the Guideline is amended accordingly.

3.9. The process of apportionment of expenses between the existing and the future business should be done in realistic and objective manner. This can be achieved by analysing the operations of the business. Expenses are calculated on the assumption of an on-going business basis. Based on these factors, the identification of appropriate expense drivers and relevant expense apportionment ratios can be determined.

3.10. In order to consider expense data to be complete and appropriate, sufficient historical data should be available at a sufficiently granular level.

3.11. Regarding long-term business strategies, when setting the undertaking itself or a specific portfolio into run-off, the undertakings should amend the expense assumptions accordingly. It is also possible that the insurance market has been changed so that some insurance lines are no more sold, the change of the product portfolio should be taken into count in setting the assumptions. However, the expense assumptions should be based on recent analyses of the operations of the business. Undertakings should not consider short-term strategies to depart from recent expense analysis.

3.12. The undertakings should assume that there are extraordinary expenses every now and then. Expert judgement is needed in order to estimate and allocate extraordinary expenses in a realistic and objective manner.

AMENDED: Guideline 33 – Change in expenses

Insurance and reinsurance undertakings should ensure that assumptions with respect to the evolution of expenses over time, including future expenses arising from commitments made on or prior to the valuation date, are appropriate and consider the nature of the expenses involved. Undertakings should make an allowance for inflation that is consistent with the economic assumptions made <u>and with dependency of expenses on other cash-flows of the contract</u>.

Explanatory text:

3.13. Future expense cash flows are usually assumed to vary with assumed rates of general level of expense inflation in a reasonable manner.

3.14. Relevant market data should be used to determine expense assumptions that include an allowance for future cost increases. The correlation between inflation rates and interest rates should be taken into account. An undertaking should ensure that the allowance for inflation is consistent with the economic assumptions made, which could be achieved if the probabilities for each inflation scenario are consistent with probabilities implied by market interest rates. Furthermore, expense inflation should be consistent with the types of expenses being considered (e.g. different levels of inflation might be expected regarding office space rents, salaries of different types of staff, IT systems, medical expenses, etc.) and the characteristics of the policy (e.g. dependency of expenses on other cash-flows of the policy).

Treatment of financial guarantees and contractual options

NEW: Guideline 37a – Dynamic policyholder behaviour

Insurance and reinsurance undertakings should base their assumptions on the exercise rate of relevant options on:

- statistical and empirical evidence, where it is representative of future conduct
- expert judgment on sound rationale and with clear documentation.

The lack of data for extreme scenarios should not be considered alone to be a reason to avoid dynamic policyholder behaviour modelling and/or the interaction with future management actions.

Explanatory text:

3.15. The most commonly modelled dynamic policyholder behaviour relates to surrender options. For example, in this case, undertakings can measure the financial gain/loss that the policyholder would face by surrendering the contract early or keeping the contract on, by comparing the current credited return with the benchmark return after recognizing any surrender penalties and future discretionary profit sharing. It should be acknowledged that the average policyholder may not actively manage their insurance products as part of an investment portfolio under such a purely economic view. On the other hand, the projection horizon for savings product can be relatively long (several tens of years) and the hypothesis that the future behaviour will remain identical to the past might be subject to discussion.

3.16. Dynamic lapse is path-dependent and so varies within the stochastic scenarios, where it is particularly relevant. The benchmark return should be defined with reference to the investment conditions that prevail in the given scenario being considered.

3.17. At the same time since there is usually little or no evidence in terms of the experienced reaction of policyholders to extreme financial conditions as the ones included in the set of stochastic scenarios, the lack of this data should not be considered alone to be a good reason to avoid dynamic policyholder behaviour modelling. In such cases, expert judgement can complement the available data to model the dynamic behaviour.

3.18. Moreover, as part of an adequate dynamic modelling, undertakings should properly consider the interaction between the relevant future management actions and the policyholder behaviour (e.g. policyholder behaviour in terms of surrender levels can be linked to the comparison between contract return and a return offered by the market, where contract return is directly influenced by management actions).

Future management actions

NEW: Guideline 40a – Comprehensive management plan

Insurance and reinsurance undertakings should ensure that the comprehensive future management actions plan that is approved by the administrative, management or supervisory body is either:

- a single document listing all assumptions relating to future management actions used in the best estimate calculation; or
- a set of documents, accompanied by an inventory, that clearly provide a complete view of all assumptions relating to future management actions used in best estimate calculation.

Explanatory text:

3.19. The comprehensive management plan mentioned in Article 23(2) of the Delegated Regulation should provide to the administrative, management or supervisory body all the needed information to evaluate the consequences of the retained assumptions for each future management actions and the interaction between those actions.

3.20. To guarantee that requirement, the administrative, management or supervisory body should have a comprehensive view of all future management actions. For that purpose, the approval of such plan should be done including a single document listing all assumptions relating to future management actions or providing a set of documents that clearly provide a complete view of all future management actions. In the latter case, a summary listing all assumptions and pointing to the detailed documents that provides all the necessary information should be established.

NEW: Guideline 40b – Consideration of new business in setting future management actions

Insurance and reinsurance undertakings should consider realistic assumptions on new business in setting future management actions and duly consider the consequences on other related assumptions. In particular, the application of contract boundaries should not influence such assumptions, for example regarding asset allocation, bond reinvestment or profit sharing.

Explanatory text:

3.21. Future business can be split into three categories: Future business within contract boundaries (i.e. included in best estimate), future business related to current contracts but falling beyond contract boundaries (e.g. premiums to be received after the contract boundary and therefore no included in best estimate) and future business related to new contracts. Even if only the first category is included in best estimate, all of them may need to be considered when setting best estimate assumptions and, in particular, future management assumptions.

3.22. If the assumption of writing new business (linked to existing contracts or linked to new contracts) in the future leads to different investment profits than the assumption of having no business after the contract boundary, undertakings should project investment profits based on the assumption of writing new business. This does not mean that undertakings need to estimate and project future profits linked to new business.

3.23. For example, in case an undertaking still commercializes a with profit portfolio. The undertaking matches the duration of its investments and liabilities and assumes that the return on the assets grows proportionally to its duration. If the undertaking does not consider any new business, future projections would be based on a decreasing duration of the obligations and, considering its matching policy, a decreasing duration of the assets. Therefore, the undertaking would project decreasing profits and underestimate the future profit sharing. However, if the undertaking adapts its assumptions to realistic expectations on future business, the undertaking would base its assumptions on realistic expectations on future business, e.g. assume that the duration of the liabilities and the assets will remain stable and, therefore, the return on assets will not decrease and future profit sharing will not be underestimated. It should be noted that this never requires projection of profits linked to new business, which only needs to be considered to set the assumptions, in this case, constant duration of assets and liabilities.

Methodologies for the valuation of contractual options and financial guarantees

NEW: Guideline 53a – Use of stochastic valuation

Insurance and reinsurance undertakings should use using stochastic modelling for the valuation of technical provisions of contracts whose cash flows depend on future events and developments, in particular those with material options and guarantees.

When assessing whether stochastic modelling is needed to adequately capture the value of options and guarantees, insurance and reinsurance undertakings should in particular, but not only, consider the following cases:

- Any kind of profit-sharing mechanism where the future benefits depend on the return of the assets.
- Financial guarantees (e.g. technical rates, even without profit sharing mechanism), in particular, but not only, where combined with options (e.g. surrender options) whose dynamic modelling would increase the present value of cash flows in some scenarios.

Explanatory text:

3.24. Stochastic modelling of options and guarantees intends to capture their time value, which is not captured following deterministic valuation. The time value of options and guarantees can be captured in any case using simulation methods, but, in some simple cases, it can also be measured with closed-formula approaches.

3.25. Profit sharing usually woks under asymmetric basis: profits are shared with the policyholders while losses are completely assumed by the undertaking. Under such circumstances, stochastic valuation is particularly relevant, since a set of scenarios might lead to a significantly higher best estimate than a single average scenario under a deterministic approach.

3.26. The combined effect of financial guarantees and surrender options might also be particularly relevant. A guaranteed rate might increase the value of surrender option: the policyholder would keep its policy in unprofitable low interest rates environment and surrender it in high interest rates environment. Therefore the average present value of the liabilities may significantly increase compared to a deterministic calculation.

Calculation of Expected Profits in Future Premiums (EPIFP)

AMENDED: Guideline 77– Assumptions used to calculate EPIFP

For the purpose of calculating the technical provisions without risk margin under the assumption that the premiums relating to existing insurance and reinsurance contracts that are expected to be received in the future are not received, undertakings should apply the same actuarial method used to calculate the technical provisions without risk margin in accordance with Article 77 of the Solvency II Directive, with the following changed assumptions:

a) policies should be treated as though they continue to be in force rather than being considered as surrendered;

b) regardless of the legal or contractual terms applicable to the contract, the calculation should not include penalties, reductions or any other type of adjustment to the theoretical actuarial valuation of technical provisions without a risk margin calculated as though the policy continued to be in force.~~;~~

~~c) the other assumptions should be left unchanged.~~

All the other assumptions (e.g. mortality, lapses, expenses…) should remain unchanged. This means that the undertakings should apply the same projection horizon, future management actions and policyholder option exercise rates used in Best Estimate calculation without adjusting them to consider that future premiums will not be received. Even if all assumptions on expenses should remain constant, the level of some expenses (e.g. acquisition expenses or investment management expenses) could be indirectly affected.

The actuarial function should always validate EPIFP calculation with specific reference to the methodology and underlying assumptions used by the undertaking.

Explanatory text:

3.27. As stated in Article 260(2) of the Delegated Regulation, EPIFP are determined as the difference between the official calculation of technical provisions without risk margin and a calculation of technical provisions without risk margin under the assumption that future premiums (and related benefits) expected to emerge from existing contracts will not occur.

3.28. The methodology described is based on a difference between two different calculations of technical provisions without risk margin, so it is crucial that both terms of the subtraction are calculated following same approach and technical hypothesis, with the only exception that in the additional technical provisions without risk margin calculation no future premiums will be included.

3.29. As written above, the technical hypothesis should remain unchanged to guarantee coherence among the official technical provisions without risk margin and technical provisions without risk margin under the assumption that future premiums (and related benefits) expected to emerge from existing contracts will not occur.

3.30. In order to avoid divergent practices on expenses projection applied on technical provisions without risk margin without future premiums, it is important to underline the following considerations:

- expenses directly related to future premiums should be excluded since the underlying assumption is that no future premiums will be received (e.g. some acquisition expenses);
- fixed costs should remain unchanged (e.g. no hypothesis on lower costs – such as salaries - can be accepted for the fact that no future premiums will be received);
- variable expenses will be only indirectly influenced according to the fact that, without future premiums, the invested reserve will not increase as planned (e.g. for investment management expenses, the same management fee percentage used in the official technical provisions without risk margin, but applied to lower amounts).

4. Impact assessment

4.1. Procedural issues and consultation of interested parties

4.2. In accordance with Article 16 of EIOPA Regulation, EIOPA has conducted an analysis of costs and benefits during the policy development process. The analysis of costs and benefits is undertaken according to an impact assessment methodology.

4.3. This impact assessment covers the impact of the revision of the Guidelines as a whole plus the most relevant areas individually, in particular expert judgement, investment management expenses and EPIFP calculation. It is based on the qualitative assessment of the potential impacts done by EIOPA with some quantitative analysis based on prudential reporting data (QRTs) and data gathered in the information request for the 2020 review.

4.2. Problem definition

4.4. Following the entry into force of the Solvency II Directive, especially the publication of the Delegated Regulation, EIOPA has adopted several sets of Guidelines that aim at clarifying expectations of the supervisors towards a correct implementation of the regulation by insurers. However, those Guidelines were not issued after a review of actual practices, as the time between application and implementation of Solvency II was not sufficiently long to study the industry's practices and the industry's understanding of the regulation.

4.5. During the preparation of EIOPA's Opinion on the 2020 review of Solvency II, EIOPA has identified several divergent practices among insurers and supervisors regarding the calculation of technical provisions. Those issues have been presented in the consultation paper, published in October 2019, and were especially explained in the Annex 3 of that document.

4.6. Globally, those divergent practices were mainly due to lack of clear explanations regarding the appropriate application of some provisions of the Delegated Regulation, mainly regarding stochastic valuation, future management actions, policyholder behaviour, expenses, expert judgement and EPIFP.

4.7. In some cases, divergences arise from the penetration of more sophisticated techniques, e.g. stochastic valuation or dynamic policyholder modelling. In other cases divergences arise from a lack of clarity of some detailed assumptions, as for example the investment management expenses that should be allocated to the best estimate or the delimitation of the scope of future management actions. Overall, these divergent practices have an impact over the best estimate, which could lead to an unlevel playing field if not properly addressed.

4.8. Expert judgement guidelines do not introduce new guidance since their content is the same than the Guidelines on expert judgement already existing in the Guidelines on the use of internal models and, according to the introduction of the Guidelines on valuation of Technical provisions, these guidelines on expert judgement are also applicable for best estimate valuation purposes. However, this reference via the introduction is not straightforward and visible enough, which led to some confusion and divergent interpretations in the past.

4.3. Objectives pursued

4.9. The main objective of these Guidelines is to ensure a convergent approach regarding the calculation of technical provisions across (re)insurance undertakings. This proposal sets out additional principle-based guidance complementing and amending the current guidelines in order to provide clarity on how the insurance and reinsurance undertakings should implement the requirements laid down in the Delegated Regulation. In particular, the assumptions underlying the use of economic scenario generators, the implementation of future management actions, expenses, policyholder behaviour and the calculation of EPIFP are addressed. It also provides explicit guidance on the use of expert judgment instead of a reference to the Guidelines on the use of internal models, as it is currently the case. This additional principle-based guidance aims at fostering convergence on practices within European Union.

4.10. The mentioned objectives for the Guidelines are connected to the general objectives of the Solvency II framework (deepen the integration of the EU insurance market, enhance the protection of policyholders and beneficiaries and promote better regulation) and in particular they are connected to:

- improving the governance and risk management of insurance and reinsurance undertakings;
- the convergence of supervisory methods.

4.11. The objectives of the Guidelines are also consistent with the following objectives of EIOPA, as reflected in the founding Regulation of EIOPA:

- to ensure a sound, effective and consistent level of regulation and supervision;
- to ensure the transfer of risks related to (re)insurance activities is appropriately regulated and supervised; and
- to foster consumer protection.

4.4. Policy Options

4.12. With the aim to meet the objectives to clarify the application of assumptions and management actions, as set out in the previous section, EIOPA has analysed different policy options throughout the policy development process.

4.13. The section below reflects the most relevant policy options that have been considered in relation to the different aspects of valuation of technical provisions. We have also listed relevant options which have been discarded in the policy development process.

4.4.1 Policy issue 1: Introduction of additional Guidelines versus the status quo

4.14. The following policy options have been identified:

1. **Policy option 1.1** Introduction of additional Guidelines to provide clarity on how the calculation of technical provisions shall be applied by insurance and reinsurance undertakings.

2. **Policy option 1.2** Keeping the status quo of the current Guidelines.

4.4.2 Policy issue 2: Consistent approach regarding use of expert judgments for both technical provisions and internal model

4.15. The following policy options have been identified:

1. **Policy option 2.1** Introduction of a full set of guidelines on Expert judgment for valuation of technical provisions.
2. **Policy option 2.2** Introduction of a reference to the guidelines on Expert judgment for internal model purposes in a specific guideline
3. **Policy option 2.3** Reference to the guidelines on Expert judgement for internal model purposes in the recitals (current situation)

4.4.3 Policy issue 3: Proportion of investment management expenses to be considered

4.16. The following policy options have been identified:

1. **Policy option 3.1** Expenses relating to all assets
2. **Policy option 3.2** Expenses relating to investments backing Solvency II technical provisions and the solvency capital requirement
3. **Policy option 3.3** Expenses relating to investments backing Solvency II technical provisions
4. **Policy option 3.4** Expenses relating to investments backing Solvency II Best Estimate
5. **Policy option 3.5** Expenses relating to investments backing the local GAAP technical provisions

4.4.4 Policy issue 4: Management of expenses that the fund manager reimburses to the undertaking

4.17. The following policy options have been identified:

1. **Policy option 4.1** Reimbursement should be considered as decrease of expenses
2. **Policy option 4.2** Reimbursement should be considered as other cash inflow
3. **Policy option 4.3** Reimbursement should not be taken into account

4.4.5 Policy issue 5: Detailed guidance on the calculation of EPIFP

4.18. The following policy options have been identified:

1. **Policy option 5.1** Clarification on the assumptions to be used to calculate EPIFP
2. **Policy option 5.2** No further clarification

4.5. Analysis and impact of policy options

4.5.1 Policy issue 1: Introduction of new Guidelines vs status quo

Policy option 1.1 *Introduction of additional EIOPA Guidelines to provide clarity on how the calculation of technical provisions shall be applied by insurance and reinsurance undertakings.*

4.19. On the basis of the analysis performed by EIOPA during the preparation of the consultation paper on the Opinion on the 2020 Review of Solvency II, EIOPA has identified a lack of convergent practices among several topics regarding the calculation of technical provisions. Those divergent practices are described especially in Sections 2, 4, 5 and 6 of the Annex 3 of the aforementioned document and mainly affect interpretation of the legal provisions regarding economic scenarios generators, future management actions, expenses and valuation of options and guarantees.

4.20. The existence of those divergent practices is often due to the lack of clarity of the existing guidelines or the absence of guidelines explaining expectation of supervisory authorities when (re)insurance undertakings implement the principle-based regulatory requirements of technical provisions.

4.21. As a consequence, EIOPA has an opinion that the introduction of additional and amended Guidelines on calculation of technical provisions:

a) supports the (re)insurance undertakings in setting up their assumptions, and therefore, ensures an enhanced level playing field among the undertakings;

b) does not modify the current expectations of supervisors but provide more clarity and more transparency on the application of regulatory requirements;

4.22. In terms of cost of compliance with the new Guidelines, it is reasonable to expect that (re)insurance undertakings shall slightly modify their assumptions, methodologies and documentation package related to the calculation of technical provisions. However, as all those assumptions and methodologies shall be regularly reviewed by (re) insurance undertakings, it is expected that the implementation of the additional Guidelines will lead to no material additional costs.

4.23. For competent authorities, those new guidelines should ease the process of reviewing the calculation of technical provisions by providing a better clarity on practices to be implemented, leading to less administrative costs.

Policy option 1.2 *Keeping the status quo of the current Guidelines.*

4.24. EIOPA believes that, without the introduction of additional guidelines, the current set of Guidelines on technical provisions fail to provide a sufficient regulatory framework for the insurance and reinsurance undertakings and the competent authorities in the field of calculation of technical provisions as shown by the current divergent practices (re)insurance undertaking.

4.25. Moreover, without the issuance of new guidelines it could lead to a situation of unlevel playing field among insurance undertakings, especially in case of activities performed through freedom of establishment of freedom of services. Indeed expectation regarding the calculation of technical provisions might differ from the Home supervisor and the host supervisor, that could lead to different own funds assessment for the same insurance obligations.

4.5.2 Policy issue 2: Consistent approach regarding the use of expert judgments for both technical provisions and internal model

Policy option 2.1 *Introduction of a full set of guidelines on Expert judgment for the valuation of technical provisions*

4.26. Expert judgment is widely used by insurance and reinsurance undertakings when setting assumptions for valuation purposes. Currently Recital 1.3 of the current guidelines refers to Chapter 4 of the Internal Models Guidelines. It is then in contradiction with internal model guidelines for which a detailed set of guidance has been provided.

4.27. Because the guidance and clarification of the application of expert judgement is equally important for the valuation of technical provisions, EIOPA believes that the introduction of the full set of guidelines regarding expert judgment in the Guidelines on the valuation of technical provisions will promote consistency and a level playing field across insurance and reinsurance undertakings.

4.28. In terms of cost of compliance with the guidelines on expert judgment, it is reasonable to expect that (re)insurance undertakings will not be significantly affected, because the recitals of the current Guidelines already refer to the same provisions in the Guidelines on the use of internal models. Indeed, insurance and reinsurance undertakings already apply specific governance and control on expert judgment, as they need to ensure the adequacy of the general governance and control systems related to the valuation of technical provisions. However, they will probably need to slightly amend existing practices to ensure alignment with the detailed guidance provided. As the general governance system is regularly reviewed by (re)insurance undertakings, it is expected that the implementation of the additional Guidelines will lead to no material additional costs.

4.29. For competent authorities, these new guidelines are expected to ease reviewing the calculation of technical provisions by providing better clarity on practices to be implemented, leading to less administrative costs.

Policy option 2.2 *Introduction of a reference to the guidelines on Expert judgment for internal model purposes in a specific guideline*

4.30. This option is quite similar in terms of costs and benefits to option 2.1. It also provides the advantage to ensure a full consistency between the Guidelines on internal models and the Guidelines on the valuation of technical provisions. However, it cannot ensure the full consistency of the entire set of Guidelines on the valuation of technical provisions, which means that insurance and reinsurance undertakings that are not using internal models have to refer to guidelines that are not directly applicable to them.

Policy option 2.3 *Reference to guidelines on Expert judgement for internal model purposes in the recitals (current situation)*

4.31. EIOPA believes that, taking into account the current situation, the status quo is not enough to ensure sufficient harmonisation among the industry because the recitals cannot enforce an obligation.

4.5.3 Policy issue 3: Proportion of investment management expenses to be considered

4.32. In June 2019, EIOPA surveyed the practices of how investment management expenses are considered in the calculation of technical provisions. Several different approaches were used, also within the same country, and EIOPA believes that there is need to harmonise the practices.

4.33. Altogether 287 undertakings took part in the survey, of which 150 were life, 48 non-life and 79 composite undertakings. 10 undertakings were reinsurance undertakings. According to the survey results, different calculation approaches could be observed:

	Life		Non-life		Composite		Reinsurance		All	
	Companies	Models	Companies	Models	Companies	Models	Companies	Models	Companies	Models
AT	2	1	4	2	11	3	0	0	17	3
BE	10	5	0	0	13	5	0	0	23	5
CY	3	1	0	0	2	2	1	1	6	2
CZ	0	0	0	0	4	3	0	0	4	3
DE	40	5	1	1	0	0	0	0	41	5
DK	8	5	4	3	3	3	0	0	15	6
EE	1	1	3	2	1	1	0	0	5	4
ES	2	2	0	0	8	3	1	1	11	4
FI	4	4	4	2	1	1	0	0	9	4
FR	8	3	0	0	1	1	0	0	9	3
GR	1	1	1	1	3	2	0	0	5	2
HR	0	0	2	1	4	4	0	0	6	4
HU	2	2	2	2	3	2	0	0	7	4
IE	15	4	11	3	0	0	7	3	33	5
IT	13	4	0	0	9	2	0	0	22	4
LI	7	3	3	3	2	2	0	0	12	4
LT	2	1	1	1	0	0	0	0	3	2
LU	6	2	2	1	0	0	1	1	9	3
LV	1	1	1	1	1	1	0	0	3	3
NL	4	2	0	0	0	0	0	0	4	2
NO	1	1	0	0	2	1	0	0	3	1
PL	7	3	6	4	0	0	0	0	13	6
PT	5	2	1	1	3	3	0	0	9	3
RO	4	4	0	0	4	2	0	0	8	4
SE	4	2	2	1	4	3	0	0	10	5
Total	**150**		**48**		79		10		287	

4.34. The following table shows the percentage of undertakings that considered certain investment management expenses in their calculations:

Investment management expenses considered	Life	Non-life	Composite	Reinsurance	All
All	50 %	50 %	50 %	60 %	50 %
Local GAAP	20 %	10 %	30 %	10 %	20 %
SII TP	20 %	10 %	10 %	10 %	10 %
None or n/a	0 %	20 %	10 %	10 %	10 %
SII TP and SCR	0 %	10 %	0 %	0 %	0 %
SII BE	0 %	0 %	0 %	10 %	0 %
Other	10 %	0 %	10 %	0 %	10 %
Total	100 %	100 %	100 %	100 %	100 %

4.35. Because all options would allow the undertakings to use more prudent approaches than defined in the guidelines, the harmonisation of practices would, depending on the chosen option, require the following share of undertakings to modify their practices:

Option	Life	Non-life	Composite	Reinsurance
3.1 Expenses of all assets	50 %	50 %	50 %	40 %
3.2 Investments backing Solvency II technical provisions and the solvency capital requirement	50 %	40 %	50 %	50 %
3.3 Investments backing Solvency II technical provisions	50 %	30 %	40 %	40 %
3.4 Investments backing Solvency II best estimate	50 %	30 %	40 %	30 %
3.5 Any option that backs also at least the local GAAP technical provisions	80 %	90 %	70 %	90 %

4.36. Undertakings may gather required information easily from their accounting data, but option 3.2, Investments backing Solvency II technical provisions and the solvency capital requirement, requires typically an approximation method to be used because there is a circular reference to SCR.

4.5.4 Policy issue 4: Management of expenses that the fund manager reimburses to the undertaking

4.37. In the same survey, EIOPA observed that 60 % of the undertakings either stated that reimbursements were not taken into account, were not relevant or the undertakings did not provide any response.

4.38. From the remaining respondents, about 35% mentioned that they netted the reimbursements with the trading costs. Others modelled the reimbursements e.g. as separate cash flows.

4.39. According to the survey results, some undertakings directed the reimbursements to policyholders in equal terms, some directed part of them to policyholders. About 67 % of the undertakings stated that they keep the reimbursements themselves.

4.40. **Policy option 4.1** *Reimbursement should be considered as decrease of expenses*, and **policy option 4.2** *Reimbursement should be considered as other cash inflow*, leading to the same best estimate. The difference between the two options is that in regard policy option 4.2 the expenses are stressed in the calculation of the solvency capital requirement.

4.41. **Policy option 4.3** *Reimbursement should not be taken into account*, which would mean that best estimate and SCR of many undertakings would increase.

4.5.5 Policy issue 5: Detailed guidance on the calculation of EPIFP

Policy option 5.1 *Clarification on the assumptions to be used to calculate EPIFP*

4.42. This option provides further clarification to (re)insurance undertakings for the calculation of EPIFP. Removing future premiums in the calculation of EPIFP may be complex and depend on several assumptions. Thus, by clarifying which assumptions are to be left unchanged, EIOPA believes that higher convergence of practices and level-playing field will be achieved.

4.43. It is reasonable to expect that (re)insurance undertakings will have to only slightly modify their assumptions, methodologies and documentation package related to the calculation of EPIFP. However, as all those assumptions and methodologies have to be regularly reviewed by (re) insurance undertakings, it is expected that the implementation of the revised guidelines will not lead to any material additional costs. Moreover, guidance on simplification might lead to less complexity and less costly calculations.

4.44. For the competent authorities, new guidelines would ease the process of reviewing the calculation of EPIFP.

Policy option 5.2 *No further clarification*

4.45. EIOPA believes that, without the introduction of clarifications regarding the EPIFP calculation, the current set of Guidelines on technical provisions fails to provide a sufficiently clear regulatory framework in the field of calculation of technical provisions for the insurance and reinsurance undertakings and for the competent authorities.

4.46. Indeed, the actual application of the current guidelines has led to divergent practices by (re)insurance undertakings, whereas EPIFP needs to be well identified in the calculation of own funds.

4.47. This option will not lead to any material additional costs on (re)insurance undertakings.

4.6. Comparison of options

4.6.1 Policy issue 1: Introduction of new Guidelines vs status quo

4.48. EIOPA believes that, without the introduction of additional Guidelines, the current set of Guidelines on valuation of technical provisions fail to provide a sufficient regulatory framework for the insurance and reinsurance undertakings and the national competent authorities as shown by the current divergent practices.

4.49. The following table shows the main costs and benefits for EIOPA stakeholders:

Policy issue 1: Introduction of new Guidelines vs status quo		
Option 1.1: Introduction of additional Guidelines		
Costs	Policyholders	None
	Industry	Some undertakings may need to do some adjustments regarding best estimate valuation to comply with the revised Guidelines. However, this is unavoidable when addressing divergent practices.
	Supervisors	None
	Other	None
Benefits	Policyholders	More consistent level of protection across Europe.
	Industry	Enhanced level playing field and consistent supervision across Europe.
	Supervisors	Clearer guidance facilitating the level playing field and a common understanding with industry.
	Other	None
Option 1.2: No change		
Costs	Policyholders	Different level of protection depending on the interpretation of SII principles in each jurisdiction.
	Industry	Different interpretations in different markets, hampering the level playing field and creating challenges for undertakings operating in several markets.
	Supervisors	Lack of clear guidance on the interpretation of some provisions complicates reaching a common understanding with the industry.
	Other	None
Benefits	Policyholders	None
	Industry	None
	Supervisors	None
	Other	None

4.50. For these reasons, Option 1.1 is preferred.

4.6.2 Policy issue 2: Consistent approach regarding the use of expert judgments for both technical provisions and internal model

4.51. EIOPA has identified that a reference in the recitals on Expert judgment for internal model purposes might not be the most suitable guidance to provide a sufficient regulatory framework for the insurance and reinsurance undertakings and the national competent authorities. Indeed it does not directly provide a full and self-functioning set of guidance to the insurance and reinsurance undertakings, leading to potentially divergent practices.

4.52. The following table shows the main costs and benefits for EIOPA stakeholders:

Policy issue 2: Consistent approach regarding use of expert judgments for both technical provisions and internal model		
Option 2.1: Introduction of a full set of guidelines on Expert judgment for valuation of technical provisions.		
Costs	Policyholders	None
	Industry	None as current guidelines on valuation of technical provisions already refer in the recitals to guidelines on Expert judgment applicable to internal models
	Supervisors	None as current guidelines on valuation of technical provisions already refer in the recitals to guidelines on Expert judgment applicable to internal models
	Other	None
Benefits	Policyholders	None
	Industry	Avoid implicit reference to other sets of guidelines and provide a full set of guidelines to the industry when assessing their compliance to valuation of technical provisions.
	Supervisors	Clearer guidance on expert judgment facilitating the review field and a common understanding with industry.
	Other	None
Option 2.2: Introduction of a reference to guidelines on Expert judgment for internal model purposes in a specific guideline		
Costs	Policyholders	None
	Industry	None as current guidelines on valuation of technical provisions already refer in the recitals to guidelines on Expert judgment applicable to internal models
	Supervisors	None as current guidelines on valuation of technical provisions already refer in the recitals to guidelines on Expert judgment applicable to internal models
	Other	None
Benefits	Policyholders	None
	Industry	Introduce an explicit guideline that reinforces the fact that guidelines applicable to internal models are also applicable for valuation of technical provisions regarding expert judgment
	Supervisors	Clearer guidance on applicability of expert judgment guidelines facilitating the review field and a common understanding with industry.
	Other	None
Option 2.3: Reference to guidelines on Expert judgement for internal model purposes in the recitals (current situation)		
Costs	Policyholders	None
	Industry	None
	Supervisors	None
	Other	None
Benefits	Policyholders	None

	Industry	None
	Supervisors	None
	Other	None

4.53. For these reasons, Option 2.1 is preferred.

4.6.3 Policy issue 3: Proportion of investment management expenses to be considered

4.54. EIOPA has identified that different approaches are currently being followed in different jurisdictions and therefore further guidance on the right approach is needed to facilitate a level playing field.

4.55. The following table shows the main costs and benefits for EIOPA stakeholders:

Policy issue 3: Proportion of investment management expenses to be considered		
Option 3.1: Expenses of all assets		
Costs	Policyholders	None
	Industry	- Some undertakings may need to do some adjustments regarding the best estimate valuation to comply with the revised Guidelines. However, this is unavoidable when addressing divergent practices. - This option overestimates technical provisions compared to the requirement of the Delegated Regulation
	Supervisors	None
	Other	None
Benefits	Policyholders	- This approach would usually lead to higher technical provisions compared to other options and therefore to a higher level of protection of policyholders. - Same level of protection across Europe.
	Industry	- Clearer guidance reducing uncertainty.
	Supervisors	- Clearer guidance
	Other	None
Option 3.2: Investments backing Solvency II technical provisions and the solvency capital requirement		
Costs	Policyholders	None
	Industry	- Some undertakings may need to do some adjustments regarding best estimate valuation to comply with the revised Guidelines. However, this is unavoidable when addressing divergent practices.

	Supervisors	None
	Other	None
Benefits	Policyholders	- Same level of protection across Europe.
	Industry	- Clearer guidance reducing uncertainty. - This approach seems the most in line with article 78 (1) (1) of the Solvency II Directive that requires all expenses that will be incurred in servicing insurance and reinsurance obligations to be taken into account.
	Supervisors	- Clearer guidance
	Other	None
Option 3.3: Investments backing Solvency II technical provisions		
Costs	Policyholders	None
	Industry	- Some undertakings may need to do some adjustments regarding best estimate valuation to comply with the revised Guidelines. However, this is unavoidable when addressing divergent practices.
	Supervisors	None
	Other	None
Benefits	Policyholders	- Same level of protection across Europe.
	Industry	- Clearer guidance reducing uncertainty. - This approach leads to lower technical provisions compared to options 3.1 and 3.2
	Supervisors	- Clearer guidance
	Other	None
Option 3.4: Investments backing Solvency II best estimates		
Costs	Policyholders	None
	Industry	- Some undertakings may need to do some adjustments regarding best estimate valuation to comply with the revised Guidelines. However, this is unavoidable when addressing divergent practices. - It does not ensure all expenses that will be incurred in servicing insurance and reinsurance obligations to be taken into account.
	Supervisors	None
	Other	None
Benefits	Policyholders	- Same level of protection across Europe.
	Industry	- Clearer guidance reducing uncertainty. - This approach leads to lower technical provisions compared to options 3.1, 3.2 and 3.3

	Supervisors	- Clearer guidance
	Other	None
Option 3.5: Any option that backs also at least the local GAAP technical provisions		
Costs	Policyholders	- It does not provide the same level of protection across Europe as it refers to local GAAP
	Industry	- Some undertakings may need to do some adjustments regarding best estimate valuation to comply with the revised Guidelines. However, this is unavoidable when addressing divergent practices. - It does not ensure all expenses that will be incurred in servicing insurance and reinsurance obligations to be taken into account.
	Supervisors	None
	Other	None
Benefits	Policyholders	None
	Industry	None
	Supervisors	None
	Other	None

4.56. For these reasons, Option 3.2 is preferred. This option does not restrict the undertakings to take into account expenses of all assets, but the requirement to take all expenses into account would in general not respect the level-playing field for mutual undertakings because compared to insurance and financial groups they do not have same possibilities to optimise the solvency position.

4.6.4 Policy issue 4: Management of expenses that the fund manager reimburses to the undertaking

4.57. EIOPA has identified that insurance and reinsurance undertakings do not treat consistently reimbursement of expenses from fund managers. That leads to an unequal treatment of policyholders.

4.58. The following table shows the main costs and benefits for EIOPA stakeholders:

Policy issue 4: Management of expenses that the fund manager reimburses to the undertaking		
Option 4.1: Reimbursement should be considered as a decrease of expenses.		
Costs	Policyholders	None
	Industry	- Some undertakings may need to do some adjustments regarding best estimate valuation to comply with the revised

		Guidelines. However, this is unavoidable when addressing divergent practices.
	Supervisors	None
	Other	None
Benefits	Policyholders	- Same level of protection across Europe.
	Industry	- Clearer guidance reducing uncertainty.
	Supervisors	- Clearer guidance
	Other	None
Option 4.2: Reimbursement should be considered as other cash inflow.		
Costs	Policyholders	None
	Industry	- Some undertakings may need to do some adjustments regarding best estimate valuation to comply with the revised Guidelines. However, this is unavoidable when addressing divergent practices. - Compared to Option 4.1, it will lead to higher solvency capital requirement
	Supervisors	None.
	Other	None
Benefits	Policyholders	- Same level of protection across Europe. - With option 4.2, reimbursement will be stressed for SCR purpose; leading to higher capital requirement and thus a higher level of protection than option 4.1
	Industry	- Clearer guidance reducing uncertainty.
	Supervisors	- Clearer guidance
	Other	None
Option 4.3: Reimbursement should not be taken into account.		
Costs	Policyholders	- This approach would usually lead to higher technical provisions compared to Option 4.1 and 4.2 and therefore to a higher level protection of policyholders.
	Industry	- Some undertakings may need to do some adjustments regarding best estimate valuation to comply with the revised Guidelines. However, this is unavoidable when addressing divergent practices. - This option will lead to an increase of technical provision across Europe
	Supervisors	- Some undertakings may need to do some adjustments regarding best estimate valuation to comply with the revised Guidelines. However, this is unavoidable when addressing divergent practices.
	Other	None

Benefits	Policyholders	- This approach would usually lead to higher technical provisions compared to Option 4.1 and 4.2 and therefore to a higher level protection of policyholders. - Same level of protection across Europe.
	Industry	- Clearer guidance reducing uncertainty.
	Supervisors	- Clearer guidance
	Other	None

4.59. For these reasons, Option 4.2 is preferred.

4.6.5 Policy issue 5: Detailed guidance on the calculation of EPIFP

4.60. EIOPA believes that the current guideline does not provide sufficiently clear guidance on the calculation of EPIFP, in particular on the principle that some assumptions should be left unchanged. Moreover, due to the complexity of the EPIFP calculation, the role of the actuarial function is crucial to ensure an appropriate assessment of the calculation.

4.61. The following table shows the main costs and benefits for EIOPA stakeholders:

Policy issue 5: Introduction of new Guidelines vs status quo		
Option 5.1: Clarification on the assumptions to be used to calculate EPIFP		
Costs	Policyholders	None
	Industry	Some undertakings may need to do some adjustments regarding best estimate valuation to comply with the revised Guidelines. However, this is unavoidable when addressing divergent practices.
	Supervisors	None
	Other	None
Benefits	Policyholders	More consistent level of protection across Europe.
	Industry	Enhanced level playing field and consistent supervision across Europe.
	Supervisors	Clearer guidance facilitating the level playing field and a common understanding with industry.
	Other	None
Option 5.2: No further clarification		
Costs	Policyholders	None
	Industry	Lack of clear guidance on the interpretation of some provisions complicates reaching a common understanding on the calculation to be provided.
	Supervisors	Lack of clear guidance on the interpretation of some provisions complicates reaching a common understanding with the industry.

	Other	None
Benefits	Policyholders	None
	Industry	None
	Supervisors	None
	Other	None

4.62. For these reasons, Option 5.1 is preferred.

EIOPA

Westhafen Tower, Westhafenplatz 1
60327 Frankfurt – Germany
Tel. + 49 69-951119-20
info@eiopa.europa.eu
https://www.eiopa.europa.eu