| Comments Template on<br>Consultation Paper on EIOPA's first set of advice to the European Commission on specific items in the Solvency II Delegated Regulation | | Deadline<br>31 August 2017<br>23:59 CET |
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| Name of Company: | Gesamtverband der deutschen Versicherungswirtschaft e. V. (GDV) | |
| Disclosure of comments: | Please indicate if your comments should be treated as confidential: | Public |
| | Please follow the following instructions for filling in the template:<br>⇨ <u>Do **not** change the numbering</u> in the column "reference"; if you change numbering, your comment cannot be processed by our IT tool<br>⇨ Leave the last column <u>empty</u>.<br>⇨ Please fill in your comment in the relevant row. If you have <u>no comment</u> on a paragraph or a cell, keep the row <u>empty</u>.<br>⇨ Our IT tool does not allow processing of comments which do not refer to the specific numbers below.<br>**Please send the completed template, <u>in Word Format</u>, to CP-17-004@eiopa.europa.eu**<br>**Our IT tool does not allow processing of any other formats.**<br><br>**<u>The numbering of the reference refers to the sections</u>** of the consultation paper on EIOPA's first set of advice to the European Commission on specific items in the Solvency II Delegated Regulation. Please indicate to which paragraph(s) your comment refers to. | |
| **Reference** | **Comment** | |
| General Comment | GDV supports the review of specific items in the Solvency II Delegated Regulation and appreciates the improvements proposed by EIOPA. However, we believe that in some areas the advice could be further enhanced.<br><br>As a basic principle it has to be ensured that all requirements are proportionate to risks. The extent and complexity of requirements should not be further increased. In addition, the principle of proportionality demands that proportionate and simplified applications of the requirements | |

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| | are possible. | |
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| 2.4.4 | EIOPA wants to clarify that article 88, which specifies how to decide whether a simplified calculation is proportionate to the nature, scale and complexity of risks, only refers to simplified calculations included in the Delegated Regulation.<br><br>Instead, there should be an additional provision expressly declaring that there are two ways of simplified calculations possible:<br>- to apply the simplified calculations given in the Delegated Regulation (in fact, this does not mean to calculate the standard SCR for a certain risk in a simpler way but to replace it by an alternative definition of the SCR for this risk);<br>- to apply the standard definition of the SCR but to use a conservative estimate of its value instead of an exact calculated one. | |
| 3.1 | GDV welcomes EIOPA's initiatives to look into alternatives to external ratings. External credit ratings play an important role in the risk assessment processes of institutional investors. Despite the shortfalls of external credit ratings in some asset classes in the past, their performance and value as an risk indicator has been very good in many other asset classes. Direct regulation of | |

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| | CRAs as well as updated rating criteria have improved the overall quality and validity of external ratings. Moreover, given lack of quantitative and qualitative data, frequency of such data as well as availability of and capacities for adequate models and expertise, insurers will in most instances not come to a better assessment than external credit agencies. We therefore suggest that regulation should not aim at replacing the use of such external credit ratings altogether but rather concentrate on strengthening the voluntary development and use of own credit risk assessments. Moreover, any regulatory provisions on allowing alternatives to nominated ECAIs for supervisory purposes should not be overly complex but aim to be practicable for insurers. | |
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| 3.3 | GDV welcomes EIOPA's ongoing work on the issue of extending the framework to assessments provided by commercial and/or non-commercial third parties. The use of such frameworks could also help insurers to develop own credit risk assessment expertise and hence to reduce reliance on external ratings. We suggest that EIOPA looks into approaches followed by central banks such as the Deutsche Bundesbank by for example recognising these credit risk assessments as eligible for the purpose of the standard formula calculation. Reducing dependence on CRAs is also of particular importance for insurers since the three largest credit rating agencies have increased licensing fees substantially in recent years.<br><br>Allowing alternatives for supervisory purposes such as own credit assessments on the basis of the German investment code (Kreditleitfaden) for Schuldscheindarlehen would provide an adequate alternative to external credit ratings while at the same time ensuring prudent and standardised credit risks assessments.<br><br>Currently insurers are developing various internal credit risk measures for certain asset classes. Future guidance should therefore not restrict the various analytical approaches currently used by insurers to review external ratings or provide new mandatory requirements for the use of internal ratings but aim to encourage the voluntary development and use of proprietary credit risk assessments. | |

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| | We welcome EIOPA’s conclusion that market implied ratings are an inappropriate risk indicator for supervisory purposes. Using a methodology based on market implied ratings for the standard formula has a number of shortfalls. Pricing information can be very volatile due to market sentiment and rumours and not reflect the fundamental risk situation of investments and markets. Moreover, pricing information on credit default swap spreads is only available for a limited number of instruments an insurer typically invests in. Finally, pricing of such instruments is often (and increasingly) impaired by illiquidity in the market which is devaluing such pricing information as a meaningful indicator.<br><br>Accountancy-based measures in the standard formula are seen as the more adequate approach given the experience with such ratios in the market. To give an example, accountancy-based financial ratios have been used for many years with good success in the German market in order to assess the credit quality of private placements (Schuldscheindarlehen) for which market implied indicators are difficult to gain. Meaningful covenants can mitigate the shortfalls (e.g. assessment of business prospects) of accountancy-based measures. | |
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| 4.4.2 | **Paragraphs 174 to 177**<br>GDV strongly supports EIOPA’s efforts in developing a more risk-adequate recognition of | |

guarantees given by RGLAs in the spread and concentration risk sub-modules. The planned amendments to the delegated regulation need to create a level playing field with banks. In addition, refinancing conditions for institutions benefitting from such guarantees can be improved as the insurance industry is an important financing source for them.

**Paragraphs 178 to 183**

GDV welcomes the idea that the RGLA list of Implementing Regulation 2015/2011 needs an update allowing more flexibility on the question which RGLA qualifies for equivalence with central governments. However, any changes to the list should be subject to a close collaboration with the insurance industry as the convergence of the two lists from the insurance and banking industry could be challenging.

GDV agrees that the differences between the RGLA list of Commission Implementing Regulation (EU) 2015/2011 and the RGLA list in the banking framework are not justified and need to be removed. However, the alignment of both lists must not lead to the lowest common denominator but instead consider at least all RGLAs already covered by either the insurance or the banking framework. As mentioned earlier such a list always comes with the caveat that it needs regular updates and that there might be situations in which an undertaking invests in an RGLA not yet covered by the list. Consequently, the undertaking would then be unable to benefit from a lower capital requirement. Same is true for an instrument guaranteed by such a RGLA. To eliminate the disadvantage of a quite inflexible list we propose that the new list should be non-exhaustive and there should be the possibility to add RGLAs in close collaboration with the national competent authority. Going forward, EIOPA should regularly update the list with RGLAs that have been approved by national competent authorities in the meantime.

As the list in the Commission Implementing Regulation (EU) 2015/2011 currently only covers RGLAs within the EEA undertakings should be allowed to add non-EEA RGLAs as well. This could also be achieved by the introduction of a non-exhaustive list as described above where undertakings are referred to their national competent authorities for an individual assessment of each added RGLA. As things develop EIOPA should supplement the list with non-EEA RGLAs within

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| | the scope of regular updates. Excluding non-EEA RGLAs would unnecessarily restrict undertakings' investment options and hamper further diversification of assets. Besides, the delegated regulation does not explicitly exclude non-EEA RGLAs and that's why these need to be considered in the European Commission's current call for advice. In addition, non-EEA RGLAs of e.g. Canadian provinces benefit from the same treatment as Canadian government bonds under the banking regulation. No change would leave the insurance sector with a disadvantage compared to banks.<br><br>**Paragraphs 184 to 191**<br>Based on the delegated regulation and EIOPA's proposal we assume RGLAs not on the list, either EAA or non-EEA, will be subject to the intermediate treatment and therefore benefit from a lower capital requirement as proposed by EIOPA. Please provide clarification on the treatment of non-EEA RGLAs with respect to supplements of the list and intermediate treatment.<br><br>**Paragraphs 192 to 208**<br>GDV fully agrees with EIOPA that the recognition of full and partial guarantees from central governments and RGLAs in ITS (EU) 2015/2011 should be extended to Type 2 exposures in the counterparty default risk module. Nevertheless, there are also good reasons to recognise partial guarantees in spread risk module. Partial guarantees are the only contract design which is allowed for state agencies in, e.g., the Netherlands and Italy. Even if there is currently no liquid market for bonds with partial guarantees by member states or RGLAs, this might change, in particular if EIOPA decides to introduce a recognition of partial guarantees for these instruments. This would further foster the success of infrastructure project bonds which are partially guaranteed by the European Investment Bank (EIB) as well as other initiatives aimed at improving the financing of the real economy. Recognizing partial guarantees is a prerequisite that these bonds can benefit from a more risk-sensitive valuation under Solvency II and rise in investor preference. EIOPA should therefore put more emphasis on the positive effect the recognition of partial guarantees can have on the future growth of such asset classes and arising new investment opportunities for undertakings. Referring to the currently relatively low volume of instruments with partial guarantees in undertakings' investment portfolios therefore seems to be no valid argument. | |

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| 4.4.3 | **Paragraphs 221 to 222**<br>GDV strongly supports EIOPA's advice, however, undertakings and national supervisors need more flexibility on deciding which RGLAS qualify for a lower capital requirement. The new list should therefore be non-exhaustive. Treatment of non-EEA RGLAs needs to be clarified (see further comments in 4.4.2).<br><br>**Paragraph 223**<br>GDV welcomes EIOPA's idea of introducing an intermediate treatment. Especially with exhaustive RGLA lists that still exclude non-EEA RGLAs undertakings could at least benefit from a certain degree of capital requirement relief. However, the more up-to-date the list is and the more flexibility undertakings and national supervisors will have in adding new RGLAs the less there is the need for an intermediate treatment. As a next step EIOPA should therefore extend the list by including non-EEA RGLAs and develop a non-exhaustive list (see further comments in 4.4.2).<br><br>**Paragraph 225**<br>GDV appreciates the recognition of partial guarantees. Nevertheless, restricting these to type 2 mortgage loans in the counterparty default risk module seems too strict. EIOPA should consider extending the recognition to the spread risk module where appropriate, e.g., infrastructure bonds partially guaranted by the European Investment Bank (see further comments in 4.4.2). | |
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| 5.3 | **Paragraphs 265 to 278**<br>GDV welcomes EIOPA's admission that a decomposition of risk transfer components would contribute to a more accurate measurement of premium and reserve risk. Therefore, it is not appropriate that finite reinsurance, or similar arrangements, where the lack of effective risk transfer is comparable to that of finite reinsurance, shall definitely not be taken into account for the purposes of determining the volume measures for premium and reserve risk. We understand | |

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| | that there may be practical impediments to implement a scenario-based approach for the calculation of the premium and reserve risk as a default method. However, it should be up to the insurer to decide whether it is capable and willing to establish a more sophisticated process to determine the components attributable to risk transfer. Hence, the Delegated Regulation should at least provide for an exception clause, subject to the supervisor's approval. | |
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| 5.4.2 | **Paragraphs 281 to 302**<br><br>GDV supports the overall direction of the clarifications and amendments proposed to the treatment of rolling hedge arrangements.<br><br>In general, GDV also supports EIOPA's approach to exclude dynamic hedging strategies from the scale of the deductible risk-mitigation techniques. But it **seems essential to clearly differentiate between rolling hedge arrangements and dynamic ones**. Otherwise paragraph 302 could lead to the result, that every strategy where an instantaneous risk-mitigation differs from a risk-mitigation over a longer period is dynamic. For example the results of option strategies rolled once or twice a year can already differ from an option with a year's maturity depending on the development of its underlying.<br><br>We therefore propose a legal definition of "dynamic hedging strategies". Dynamic hedging could for example be defined as a hedging strategy<br>i. which would require a frequent adaption (e.g. on a daily basis) of the hedging instruments (e.g. exchange traded equity options and futures) according to the hedge target (e.g. a portfolio of equity index-linked insurance contracts) and<br>ii. where the risk of the hedge target together with the hedging instruments would be substantial for an instantaneous shock calibrated on a longer term horizon (e.g. equity – 40%, calibrated on 1 year horizon). | |

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| | The decision whether a substantially different risk-mitigation effect would be reachable over a longer period (no instantaneous shock) could be taken in a mandatory backtesting assessment before implementing the respective rolling hedge arrangement. | |
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| 6.1 | GDV largely supports the criteria and definition of an "investment related undertaking" proposed by EIOPA. However, from our point of view some further changes and clarifications are needed, in particular to ensure a proportionate (and not mandatory) application of the look through approach. It is likely that the extension of the look-through results in additional costs and challenges regarding data availability. Therefore proportionate exemptions of the look-through-requirement should be implemented so that undertakings have the option to apply the existing equity capital charge to investment related undertakings. This should at least be possible, if the exposure is not material.<br><br>Our detailed comments on EIOPAs considerations, analysis and advice can be found in sections 6.3 to 6.4.<br><br>We are looking forward to EIOPA's further considerations in this regard and its further proposals on simplifications of the look-through approach, which are announced by EIOPA for its second set of advice. In regard to the review of the look-through requirements of article 84 (3) Delegated Regulation GDV considers the 20% threshold as inappropriate for undertakings, which have a strong focus on unit-linked products and therefore a high amount of UCITs in its portfolio, because the collection and processing of data always involves a high effort whereas the impact of such unit-linked-funds on the SCR is negligible. GDV therefore suggests, that this threshold should not apply to assets of unit-/index-linked products, where the risk is borne solely by policy holder or at least to increase the threshold substantially. | |
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| 6.3 | **Paragraph 337**<br>GDV agrees that common criteria should be developed to identify related undertakings which are used as investment related vehicle. The existence of an investment mandate can be one relevant criterion for the identification of such undertakings. However, the demands on the existence of an investment mandate should not be too high. Such mandate should not only be sufficiently proved by a (precise) defined investment mandate. Rather the requirement should also be fulfilled by other indicators, such as e. g.<br>- the purpose outlined in the partnership agreement or the statute of the investment related undertaking,<br>- the context of its incorporation (as investment vehicle) or<br>- internal investment guidelines of the (parent) insurance company.<br><br>Ancillary activities which are related to investment activities should also be covered by an appropriate definition, because investment relating undertakings fulfill their investment role not only in holding assets on behalf of the (parent) insurance undertaking, but also by ancillary services which support the operations of the insurance undertaking in regard to investment activities.<br><br>**Paragraph 342 and 343**<br>GDV does not consider the level of financial leverage as an appropriate criterion and therefore supports the approach not to pose specific conditions regarding the financial leverage of such undertakings. The nature of liabilities does not appear as appropriate criterion, too.<br><br>**Paragraphs 344**<br>As stated above, the existence of an investment mandate is seen as one relevant criterion for the identification of such undertakings. However such mandate should not only be sufficiently proved by a (precise) defined investment mandate but also by other indicators (for further details see our comment to paragraph 337).<br><br>**Paragraphs 345 and 346** | |

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| | The application of the look-through approach generates costs in its own rights and is also likely to result in additional costs and challenges regarding data availability. To ensure that the application of the look-through on investment related undertakings does not lead to a disproportionate effort, it is necessary to allow undertakings as an option to apply the existing equity capital charge to investment related undertakings, e. g. in cases where the exposure is not material.<br><br>**Paragraph 349**<br>GDV strongly supports optionality in the application of the look-through to investment related undertakings. As proposed in our comments to paragraphs 345 and 346 above, optionality should apply when justified from a prudential perspective. | |
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| 6.4.2 | **Paragraph 355**<br>The feedback given to NSAs regarding the relevance of these investment vehicles confirms that exposures to investment related undertakings in some markets are immaterial. This reiterates the need to allow undertakings not to apply the look-through for immaterial exposures.<br><br>**Paragraph 369**<br>As stated above, the existence of an investment mandate is seen as one relevant criterion for the identification of such undertakings. However such mandate should not only be sufficiently proved by a (precise) defined investment mandate but also by other indicators (for further details see our comment to paragraph 337). | |
| 6.4.3 | **Paragraph 375 and 376**<br>GDV supports the definition of "investment related undertaking" provided by EIOPA subject to the following clarifications:<br>- The investment mandate should not only be sufficiently proved by a (precise) defined investment mandate. GDV proposes the following clarification in regard to the second condition: | |

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| | "it supports the operations of the insurance undertaking related to investment activities, following an investment mandate. The existence of a corresponding investment mandate can be proven also be by other indicators, such as e. g.<br>- the purpose outlined in the partnership agreement or the statute of the investment related undertaking,<br>- the context of its incorporation (as investment vehicle) or<br>- internal investment guidelines of the (parent) insurance company.<br><br>Investment related undertakings fulfill their investment role not only in holding assets on behalf of the (parent) insurance undertaking, but also by ancillary services which support the operations of the insurance undertaking in regard to investment activities. In regard to the third condition it therefore should be clarified that ancillary activities which are related to investment activities are covered by an appropriate definition.<br><br>In addition it should be clarified, that strategic investments are excluded from the definition of "investment related undertakings". Such investments should continue to be treated as strategic participations.<br><br>**Paragraph 376**<br>As stated in the response to paragraphs 345 and 346 GDV proposes that optionality should be integrated into the framework to enable undertakings to use the existing equity risk capital charge for immaterial exposures. | |
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| 7.3 | **Paragraph 387**<br>We wonder why a change in standardized methods may implicate that all approved USP would need to be resubmitted. Our understandig of legal circumstances is that, once approved, USP last until they legally terminate. This includes that they have to be assessed in regular intervals so that | |

there is not more work for NSAs.

Moreover, as the undertaking has already to do an extensive assessment of the chosen method compared to other methods including an explanation whether the chosen method is appropriate for the undertaking, we cannot see that more possible methods lead to more work for the NSAs. On the contrary: the assessment of more or other methods may help to validate the results and the reasoning why the chosen method is appropriate.

**Paragraph 388**
We don't agree with the opinion of EIOPA:
The current USP method often does not seem appropriate because of over-parametrisation (estimating 3 parameters from a 10- or 15-year time series). Therefore a robust estimating method like taking empirical standard deviation, which concentrates on 2 paramters is preferable. The second-oder effect for the variance can more likely be considered as LoB-specific than undertaking-specific. Fixing the mixing-parameter delta in advance for every LoB (e.g. delta = 0 or 1) and then taking standard deviations gives robust and stable results over the years compared to the very sensitive current method.

**Paragraph 389**
We absolutely think, that the proposed method has an additional value.
Maximum-likelihood estimation is not generally preferable to other methods of estimation. The proposed method is theoretically sound and easier to handle.

**Paragraph 390**
We don't agree with the opinion of EIOPA.
Though the method was not used to derive the standard parameters in the standard formula, it was statet in the calibration paper (Calibration of the Premium and Reserve Risk Factors in the Standard Formula of Solvency II, Report of the Joint Working Group on Non-Life and Health NSLT Calibration, 5. August 2011):

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| | ***5.4 Underwriting cycle effects in premium risk***<br>*114. Premium is a poor proxy for exposure owing to the fact that it is itself an estimate. Indeed, the main sources of misstatement of premium are the use of unreliable or unrepresentative data, errors in estimation of key parameters and the effects of commercial pressures and the underwriting cycle. The underwriting cycle is driven by results in the overall insurance market, the market segment itself and the general business cycle. Other things being equal, the effect of the cycle becomes more pronounced in lines of business where the length of claims tail and/or the capital (and risk) intensity is increased.*<br>*115. The JWG recognises the possible existence of an underwriting cycle but did not find it practicable to incorporate or embed an explicit recognition of such cycles into the calibration methodology. To achieve such an implementation, knowledge on the position of the premiums on the underwriting cycle would need to be available. Then, volatilities would become dependent on the current premium-position, in the end resulting in lower or higher undertaking-specific volatilities. The current statistical approach is more pragmatic and is based on an averaging 'look-through' analysis.*<br>*116. However, this issue should be analysed further in future calibration exercises.*<br><br>So: Existing trends and cycles are part of the systematic component of the claims- and/or premium-process, whereas the premium risk includes only the random component. Therefore our proposal seems appropriate for undertakings which are able to identify their trends or cycles (e.g. from long timeseries). Moreover, the proposed third method does not require the exact formulation of trend/cycle – only their existence is assumed.<br><br>**Paragraph 399**<br>We appreciate the opinion of EIOPA that potential USP for natural catastrophe risks are proposed to be investigated by the Catastrophe Risk Work Stream of EIOPA.<br><br>**Paragraphs 399 & 403**<br>GDV welcomes that standardised USPs methods for mortality and longevity risks may be considered at a later stage once recalibration works are over. GDV strongly believes that the | |

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| | scope of USPs should not be restricted to certain areas, as is currently set out in the Delegated Regulation, but rather expanded to life, health, non-life catastrophe and even operational risk. This enlargement to all areas permitted by the Solvency II Directive is in GDVs view necessary for Solvency II to be workable for all undertakings regardless of their size, including SMEs/mono liners.<br><br>**Paragraph 407**<br>Appreciated. GDV stands ready to discuss other methods with EIOPA. | |
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| 7.4.2 | **Paragraph 438**<br>We appreciate that the **stop loss-method** is added. | |
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| 7.4.4 | **Paragraph 453**<br>We appreciate that the **stop loss-method** is added. | |
| 8.1 | There is no need for changes in the Delegated Regulation regarding the loss absorbing capacity of deferred taxes (LAC DT). EIOPA's task asked for by the European Commission is completed with the report in this consultation paper.<br><br>In any case, the true loss absorbing capacity of deferred taxes must be fully recognized in the SCR. To limit the adjustment for LAC DT on the amount of net DTL is not justified. In addition, the projections backing DTA must not be artificially capped. Increasing uncertainty is not a bigger problem than in other pillar I calculations. Arbitrary restrictions of LAC DT would systematically distort results and, thus, be contradictory to the Directive. | |
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