EIOPA QIS 5 Report
Solvency II Breakfast briefing

Presented by
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Recap: Objectives of QIS5

- To obtain quantitative information on the impact of Solvency II on Balance Sheet
- To check that technical specifications are aligned with the Directive
- To encourage undertakings and supervisors to prepare for Solvency II
- Starting point for ongoing dialogue between supervisors and industry

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QIS5 Participation

Participation rates

- **Target:** Solo undertakings – at least 60% participation (25% targeted for QIS4)
  Groups – at least 75% participation (60% targeted for QIS4)

- **Actual:** Solo undertakings – 68% participation (↑ of almost 80% from QIS4)
  Groups – 167 groups (↑ of almost 60% from QIS4)

- Specific request for smaller undertakings to participate more actively than before resulted in a 127% increase in their participation- however believed approximately 500 small companies still excluded.
- Central Bank confirmed they received 220 submissions: 9% of total submissions

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Overview of Results: Solo Undertakings

- Caveats surround results
  - Consistency of approach: Known issues-deferred taxes, contract boundaries etc,
  - Sample sizes in some cases.

- Excess own funds of 355 billion over SCR: a reduction of 120 billion in excess funds compared to Solvency I
  - Results are not homogenous as 13 countries showed an increase in surplus
  - Ireland showed a decrease from 13.5 billion to 4.8 billion

- Overall 15% of undertakings do not meet their SCR and 5% do not meet their MCR

- However almost half of undertakings have a solvency coverage ratio of >200%

- For solo SCR calculations internal models and the standard formula on average produced similar results

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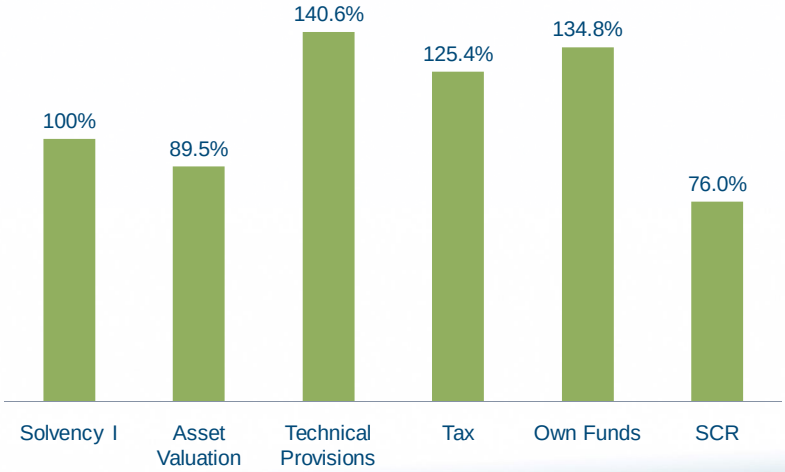
Analysis of Movement in Surplus



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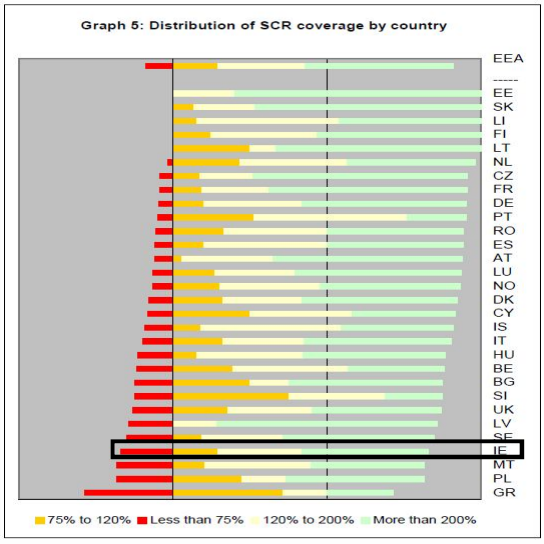
SCR Coverage by Country



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Overview of Results: Groups

- Same Caveats apply as for solo undertakings
- Excess own funds of €114 billion over Group SCR: a reduction of €86 billion in excess funds compared to Solvency I using the accounting consolidation based method with standard formula
- Groups using the accounting consolidation based method saw on average a 20% diversification benefit compared to the sum of solo SCR's - similar to QIS4
- The 29 Groups which submitted internal model results saw an increase in surplus of €6 billion compared to Solvency I
  - on average the group SCR calculated using the internal model is 80% of that calculated using the accounting consolidation approach with standard formula.

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Valuation of Assets and Liabilities (other than technical provisions)

- Market consistent approach well supported
- In general few issues for those countries adopting IFRS rules
- Issues identified:
  - Treatment of Deferred Taxes
    - Area of greatest difficulty
    - Problems with assessment of whether asset realisable within given timeframe
    - Some undertakings did not report deferred tax assets/liabilities which is contrary to expectations
  - Contingent Liabilities
    - Amounts involved were immaterial but undertakings experienced difficulties using QIS5 valuation methodologies
  - Valuation methods where no active market exists

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Technical Provisions

- Overall gross technical provisions decreased by 1.4% from Solvency I.
- For life business gross technical provisions have reduced by 1% but net technical provisions have increased by 3%
- Clear support for simplifications in the calculation of the risk margin: less than 5% performed the full calculation
- Illiquidity premium accounts for 1% reduction in technical provisions

Issues Highlighted

- **Application of Contract Boundaries**
- **Application of Illiquidity Premium**
- **Valuation of Embedded Options and Guarantees**

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Solvency Capital Requirement (SCR)

- Broad support for modular approach and aggregation methodologies
- On average SCR is approximately twice the Required Solvency Margin under Solvency I
- Diversification Benefits resulted in a reduction of 35% in the sum of the individual risks modelled
- A further reduction of 24% was introduced by the loss absorbing capacity of technical provisions and taxes i.e. final SCR is around 41% of individual elements
  - But only 60% of participants calculated the loss absorbing adjustment

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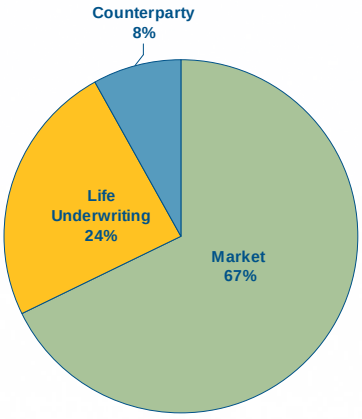
Composition of diversified BSCR for Life Undertakings



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Solvency Capital Requirement (SCR)

Issues Highlighted

- Complexity of look-through approach of funds
- Lapse risk sub-module : requirement to calculate policy-by-policy
- Loss absorbing capacity of tech provisions and deferred taxes
- Complexity of Counterparty Default risk sub-module
- Counter intuitive results of Currency Risk sub-module
- Operational Risk: does not incentivise good risk management

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Internal Models

- Due to the fact that internal models are still in development and also due to the small sample provided it is difficult to draw any firm conclusions on the comparison of the capital requirements under Internal Models versus Standard Formula
- 96% of respondents to the qualitative questionnaire on internal models plan to use a group internal model
  - however many of these did not submit any quantitative or qualitative data on their internal model
- 234 undertakings provided results calculated using an internal model
  - Saw previously that on average for solo entities this resulted in similar results compared to the standard formula whilst for groups this resulted in a 20% reduction to the SCR
- Misinterpretation of full internal model, partial internal model and undertaking specific parameters

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Own Funds

- 92% of total own funds are classified as unrestricted Tier 1 which is fully available to meet SCR and MCR
- QIS5 attempted to assess the impact of transitional arrangements but data is unreliable as undertakings were overly optimistic in their inclusion of certain items e.g. hybrid and/or subordinated debt in the figures without transitional arrangements
- EIOPA does however acknowledge that there is a clear need for transitional arrangements in this area given that hybrid capital and subordinated debt account for over 5% of own funds
- Both supervisory authorities and participants requested greater clarity on what constitutes a ring fenced fund and how they should be allowed for.

Issues Highlighted

➢ **Difficulties in calculation of Expected Profits in Future Premiums (EPIFP)**

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Going Forward

- Will be some further tests focussing on specific aspects but not a full QIS exercise
- Technical Standards, Level 2 and Level 3 will take account of feedback from QIS5. In particular EIOPA will consider those issues highlighted previously as being overly-complex e.g. contract boundaries, EPIFP, counterparty default risk, etc
- EIOPA has already commenced a technical standard on contract boundaries which will include specific examples with product mapping
- EIOPA acknowledges the need for transitional arrangement. EIOPA has specifically stated the need for transitional arrangements in the following areas:
  - Equivalence with Third Countries
  - Hybrid Capital and Subordinated debt
  - Discount rates on technical provisions

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