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Solvency II review

Introduction

On 14 December 2023, the European Council and the European Parliament reached an agreement on amendments to the Solvency II Directive. The amendments reflect mainly the European Insurance and Occupational Pensions Authority's (EIOPA) Opinion on the 2020 review of Solvency II.[1]

The proposed texts were approved by the Parliament on 23 April 2024 and adopted by the Council on 5 November 2024[2]. The amending Directive is expected to enter into force in Q4 2024 and Member States will have two years to transpose it.

The Solvency II review's main objectives are to:

- Improve the framework's efficiency by promoting long-term investments;
- Enhance the supervision of (re)insurers with cross-border activities;
- Simplify regulations for smaller (re)insurers through proportionality;
- Address new risks, such as climate-related financial risks; and
- Integrate macroprudential tools to prevent systemic risk.

The Solvency II review also includes several mandates for EIOPA, which will support bringing further changes to the Commission Delegated Regulation and other second and third-level texts. As a result, EIOPA has already launched two batches of consultations on regulatory technical standards (RTS), implementing technical standards (ITS) and guidelines.[3].

This report provides an in-depth analysis of the key changes introduced by the Solvency II review and their potential impact on (re)insurance companies. It examines how the revisions affect each of the framework's three pillars:

Pillar I: solvency capital requirements (SCR), long-term guarantee measures, risk margin and the relevant risk-free rate;

Pillar II: governance, climate change and macroprudential considerations: and

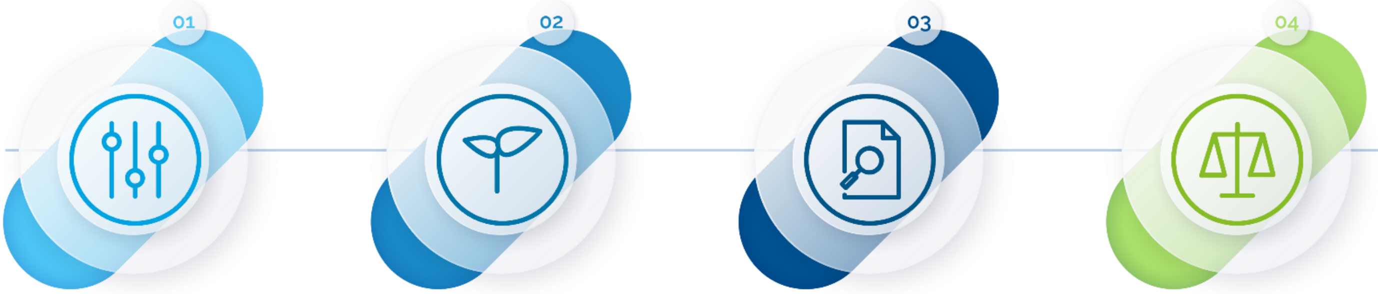
Pillar III: reporting and transparency requirements.

This report will also cover changes that encompass all three pillars, such as the new proportionality measures designed to reduce regulatory burdens for smaller (re)insurers and captives.

[1] EIOPA, *Opinion on the 2020 review of Solvency II*, 17 December 2020.
[2] Solvency II and IRRD: Council signs off new rules for the insurance sector - Consilium
[3] EIOPA opens first batch of consultations on technical standards after Solvency II Review - EIOPA and EIOPA opens second batch of consultations on legal instruments after Solvency II review - EIOPA

Executive summary

This report summarizes the key amendments of the Solvency II Directive, describes the expected amendments to the Commission Delegated Regulation and second-level texts, and presents an industry impact analysis regarding SCR. The report is structured in four topics:



Pillar I changes

- Risk margin
- Extrapolation of risk-free interest rates
- Volatility adjustment
- Long-term equity investments (LTEI)
- Symmetric adjustment
- Interest rate risk

Pillar II changes

- Own risk and solvency assessment (ORSA) requirements
- Liquidity risk management plan
- Pre-emptive recovery plans
- Cybersecurity in operational risk
- Sustainability risk management
- Climate risk change scenario analysis
- Cross-border and group supervision

Pillar III changes

- Differentiating information within the solvency and financial condition reports (SFCR) by recipients
- External audit of the SFCR (covering at least the balance sheet)
- Deadlines for submission of quantitative reporting templates (QRT), regular supervisory reports (RSR) and SFCR

Proportionality measures

- Increase of the scope exclusions
- Specific arrangements and release of requirements for small and non-complex undertakings and captives (e.g: reporting, ORSA, audit requirements…)

This report is not exhaustive. Only topics seemingly relevant to (re)insurance undertakings in the Luxembourgish market have been briefly outlined, while others have not been covered at all.

Pillar I:

Compared to the current rules, the Solvency II review is expected to create an excess of own funds of approximately €30 billion for the entire EU insurance market.[4] Its key changes include:

- Adjustments to lower the cost of capital in the risk margin;
- Long-term guarantee measures to reduce volatility; and
- Adjusted criteria for long-term equity investments (LTEI) to encourage long-term funding in the economy.

A more detailed analysis of these changes can be found in the first section (Pillar I) of this report.

Pillar II:

The Solvency II review's changes include a number of governance and risk management provisions, including:

- Strengthening governance and risk management processes;
- Enhancing the supervision of (re)insurers with significant cross-border activities and for large groups;
- Introducing macroeconomic analysis in the own risk and solvency assessment (ORSA); and
- Including cybersecurity in the operational risk management system.

Pillar II also includes several proportionality measures to ease its governance requirements for smaller (re)insurers and captives.

The amending Directive will require undertakings to have strategies, policies, processes and systems to identify, measure, manage and monitor sustainability risks, and develop plans to address the financial risks arising from sustainability factors. Entities will also need to assess if they are materially exposed to climate change risks and, if so, perform a climate change scenario analysis.

Finally, supervisory authorities will have the power to:

- Impose preventive measures, such as the pre-emptive recovery plan under the future Insurance Recovery and Resolution Directive (IRRD);
- Anticipate specific risks, for example, by requiring a liquidity risk management plan; and
- Take temporary measures, such as restricting or suspending dividend distribution and suspending redemption rights.

[4] EUR-Lex, *Document 52021SC0260: Commission Staff Working Document Impact Assessment Report*, 22 September 2021.

The aim is to improve the protection of policyholders and beneficiaries, and better address the potential build-up of systemic risk in the (re)insurance sector. A more detailed analysis of these changes can be found in the second section (Pillar II) of this report.

Pillar III:

The Solvency II review introduces several significant changes to Pillar III, which governs reporting and disclosure requirements for (re)insurance companies.

Its key refinements relate to the content, scope and submission deadlines of the solvency and financial condition report (SFCR) and the regular supervisory report (RSR). These updates aim to reduce (re)insurers' administrative burdens, increase proportionality in reporting requirements, and enhance transparency.

To guarantee the highest degree of accuracy of the information disclosed to the public, part of the SFCR should undergo an external audit. This audit should at least cover the balance sheet and be carried out by the statutory auditor or an audit firm in line with audit standards. Member States may extend this requirement's scope to other parts of the SFCR. A more detailed analysis of these changes can be found in the first section (Pillar III) of this report.

Proportionality measures:

One of the main objectives of the Solvency II review is to increase the proportionality of prudential rules to remove unnecessary and unjustified administrative burdens and compliance costs. A key proportionality measure is the definition of small and non-complex undertakings (SNCUs) (please see related definition in section Criteria for identifying Small and non-complex undertakings (SNCUs)) and captives, which will lighten the regulatory framework and these firm's operational burdens across the three pillars. In addition, the thresholds for exclusion from the scope of Solvency II requirements have been raised[5] to exclude a larger number of firms. A more detailed analysis of these changes can be found in the last section (Proportionality measures) of this report.

01

Pillar I

Extrapolation of risk-free interest rates

- The risk-free curves are used to calculate best estimate liabilities, as well as for the SCR for interest rate (IR) risk. The Solvency II review, considering EIOPA's recommendation[6], introduces a new method for the extrapolation of risk-free interest rates in the long term. This will result in a slower convergence to the ultimate forward rate (UFR), due to the introduction of:
  - **Liquid forward rates with maturities longer than a first smoothing point** (presumably at 20 years), to better reflect market rates; and
  - **A weighted convergence to the UFR in the long-term** (for maturities of at least 40 years past the first smoothing point, the weight of the UFR shall be at least 77.5%).
- The expected significant impact for long-term business will be smoothed using a gradual application until 2032 (subject to prior approval by the supervisory authority).

Volatility adjustment (VA)

- The **VA will become subject to supervisory authorization**, and some adjustments will be implemented, such as:
  - Increasing the application ratio from 65% to 85%;
  - Establishing a credit spread sensitivity ratio (CSSR) specific to the undertaking (between 0 and 1) to reflect the sensitivity mismatch between the technical provisions and the assets;
  - Introducing a macro VA for the Eurozone, which is based on a reference portfolio and could increase the initial VA; and
  - Including the possibility of applying an undertaking-specific adjustment to the risk-corrected spread to capture the bonds portfolio's specificities.

Risk margin

- **The cost of capital used to calculate the risk margin has been reduced** from 6% to 4.75%. This is designed to lower the overall size of the risk margin, providing capital relief to insurers. The European Commission will periodically review the cost-of-capital

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[5] The Solvency II Directive excludes from its scope undertakings that are below some thresholds in terms of Annual gross written premium (GWP) income, total technical provisions, and for undertakings that are part of a group, the group's total technical provisions.

[6] Opinion on the 2020 review of Solvency II - EIOPA

parameter but not for at least five years after this Directive is implemented. Then, it could be amended through the Delegated Regulation within a 4% to 5% corridor.

- By **introducing a tapering parameter known as "lambda"**, the Solvency II review aims to progressively decrease the risk margin, particularly for long-term risks, making it less burdensome and more aligned with actual risk exposure as time passes.

Figure 1: Current and proposed risk margin (RM)

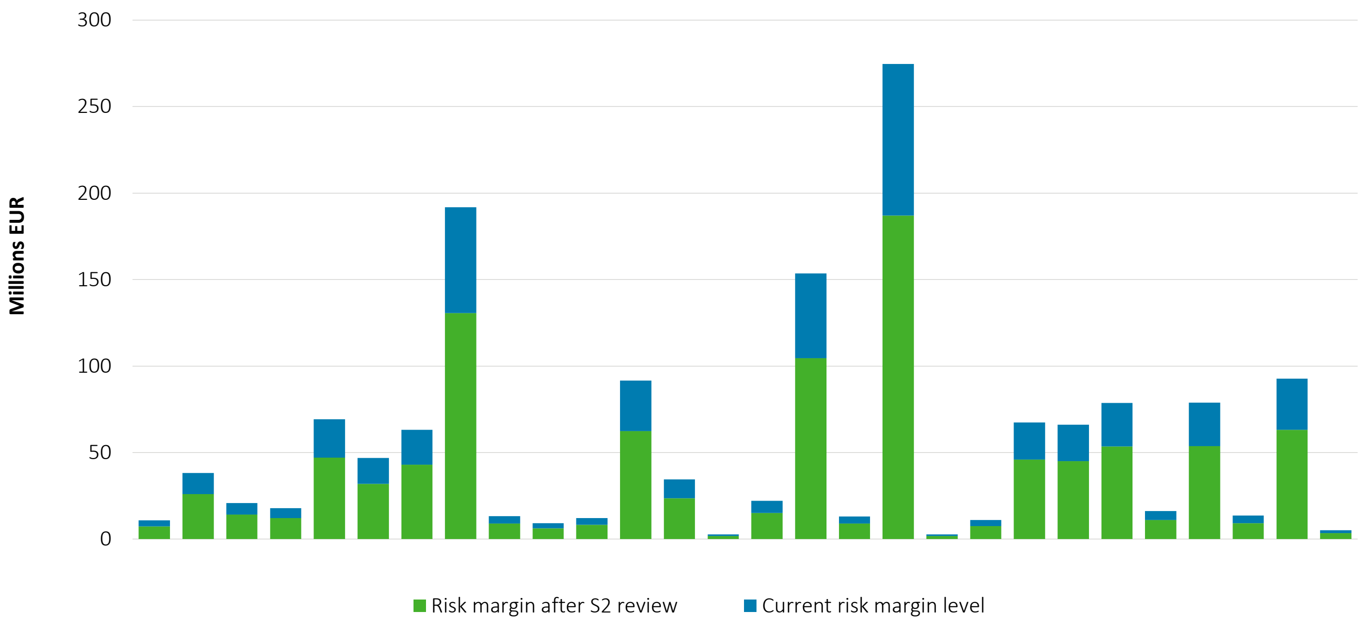
Current: $RM = 6\% * \sum_{t\geq 0} \frac{SCR(t)}{(1+r(t+1))^{t+1}}$

Proposed: $RM = 4.75\% * \sum_{t\geq 0} \frac{\lambda^t * SCR(t)}{(1+r(t+1))^{t+1}}$

In September 2021, the European Commission estimated an impact of around €30 billion of additional capital resources for the EU (re)insurance industry, arising from the proposed changes in the risk margin calculation.[7]

Figure 2 illustrates the impact of the Solvency II review on the Luxembourg life insurance market's risk margin.[8] On average, the calculation changes are expected to reduce Luxembourg insurers' risk margin by approximately 14%.

Figure 2: Risk margin for Luxembourg life insurance market (data 2023 - EUR)



Source: Deloitte calculations

Simplifications

- The amending Directive introduces **quantitative thresholds and more specific conditions** for SNCUs to apply a simplified calculation for specific risk modules. For instance, such an undertaking may use a simplified calculation when **the risk module represents less than 2%** of the basic solvency capital requirement (BSCR) and if **the sum of all** the risk modules for which the simplified calculation is intended **represents less than 10%**.
- In addition, to calculate the best estimate for life obligations with options and guarantees not deemed material, **SNCUs may use a prudent deterministic valuation**. This is instead of reflecting the present value of cash flows based on the expected outcome of future events and expected outcomes in certain scenarios.

Long-term equity investments (LTEI)

- The amending Directive updates the qualifying criteria for LTEIs, aiming to relax requirements. The new criteria for an undertaking to classify an investment as LTEIs include:

[7] EUR-Lex, *Document 52021SC0260: Commission Staff Working Document Impact Assessment Report*.

[8] The impact is based on the EIOPA opinion on the 2020 Review Of Solvency II (Opinion on the 2020 review of Solvency II - EIOPA) and was applied to the 2023 Risk Margin figures (source: Deloitte Benchmarking Tool).

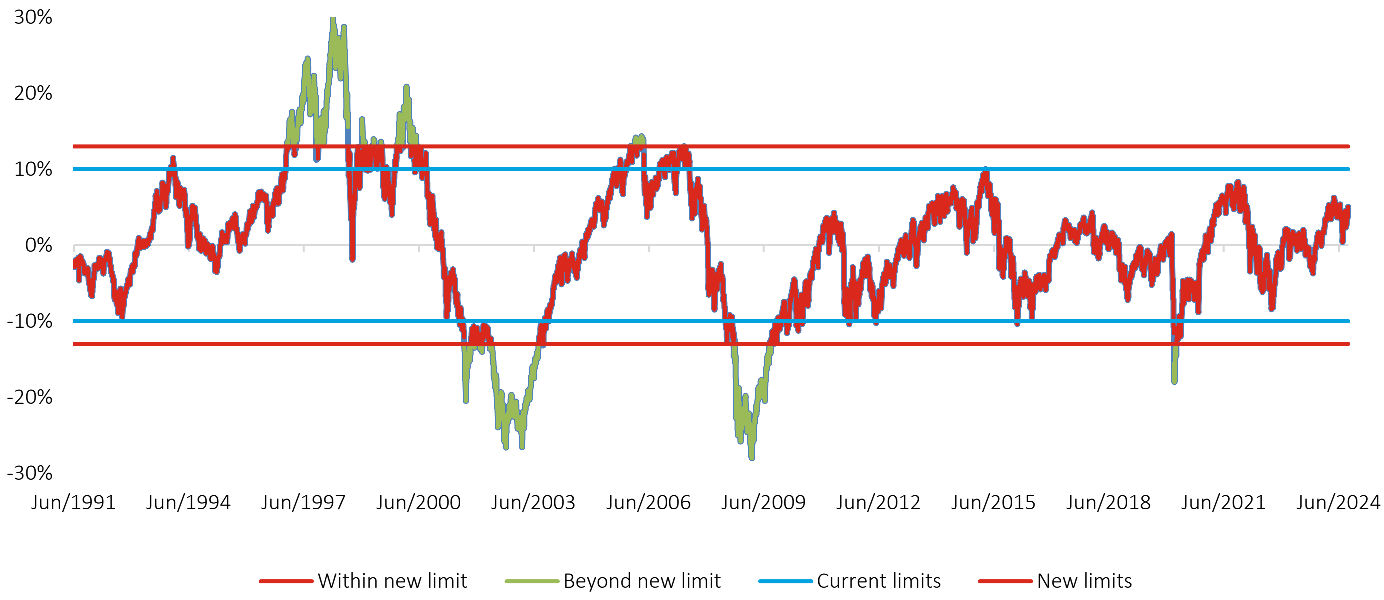
- Having set up a policy (approved by the board) for long-term investment management reflecting the (re)insurers' commitment to hold these LTEIs for a period of more than five years on average;
- Having investments consisting only of equities listed in Organisation for Economic Co-operation and Development (OECD) or European Economic Area (EEA) member countries or unlisted equities of companies with a head office in these geographies;
- Identifying and managing these securities separately from its other activities;
- Being able to demonstrate that it can avoid forced selling for five years;
- Having risk management and asset and liability management (ALM) policies reflecting the intention of holding the securities for five years;
- Having the subset of long-term equity appropriately diversified; and
- Not including participations.

- An important amendment is the **inclusion of equities held within European Long-Term Investment Funds (ELTIFs) or alternative investment funds (AIFs) having a lower risk profile**, with the possibility of being classified as LTEI if the fund meets these criteria. The criteria may be assessed at the level of the funds and not of the underlying assets held within those funds.
- Classifying equity positions as LTEIs reduces the capital burden and the capital requirements volatility for (re)insurance companies investing in these assets because:
  - The applicable capital charge for LTEIs is 22%, versus 39% and 49% for equity type 1 and equity type 2 investments, respectively; and
  - The symmetric adjustment does not apply to LTEIs.

Symmetric adjustment

- The Solvency II review increases the symmetric adjustment limit from 10% to 13% in absolute value to improve the SCR's risk sensitivity with the standard formula.
- This is expected to have a limited impact because the symmetric adjustment would only exceed the current limit of 10% (or below -10%) when the equity index deviates from its 36-month average by above 28% or below -12%.[9]

Figure 3: Symmetric adjustment under the current and new corridors (historical data 1991 – 2024)



Source: Deloitte calculations based on EIOPA insurance statistics[10].

- For example, in Figure 3, the equity risk shock in March-April 2020 would have been 26% (39%-13%) instead of 29% (39%-10%) for type 1 equities, and 36% (49%-13%) instead of 39% (49%-10%) for type 2 equities.

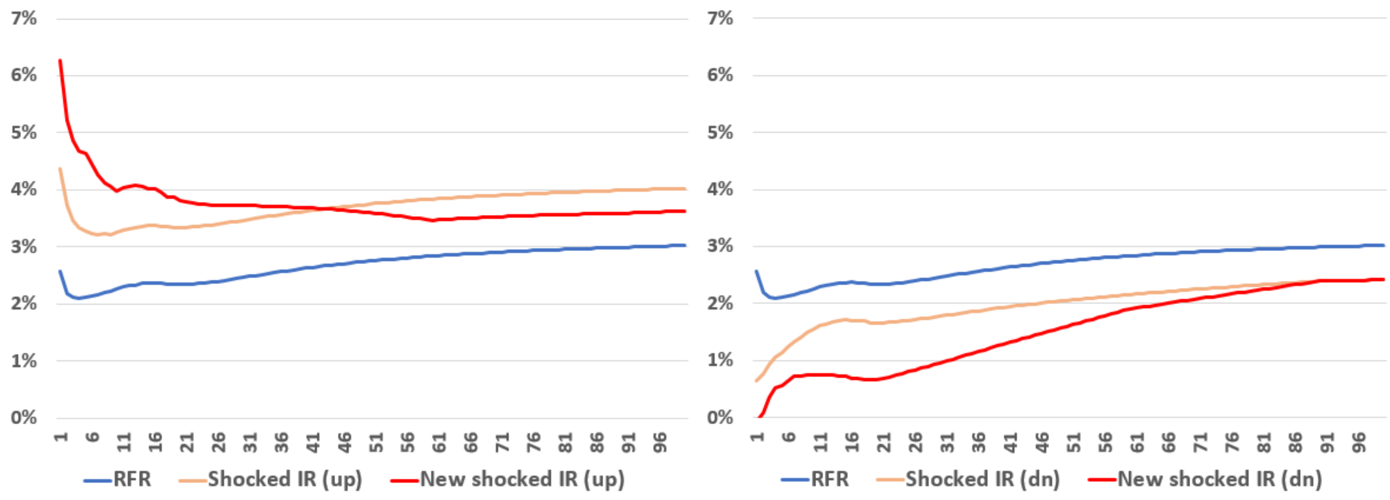
Interest Rate risk

- The current methodology for computing Interest Rate (IR) risk can underestimate the capital requirements, particularly in low interest rate environments. In fact, the actual IR shocks observed in the markets have been stronger than those assumed by the prescribed stress scenarios. In addition, the current method limits the stress impact in case of negative interest.

[9] $\text{Symmetric Adjustment} = \frac{1}{2} * \left(\frac{\text{CI}-\text{AI}}{\text{AI}} - 8\%\right)$, where CI is the current level equity index and AI is the 36 – month average
[10] Insurance statistics - EIOPA

- As a countermeasure, EIOPA recommendeds[11] introducing an additive shock component on top of the relative interest shock, independent from current interest rates, to help preserve the shocks' severity under periods of expansive monetary policy. Additionally, EIOPA proposed eliminating the 1% floor on the IR upward shock and better recognizing the existence of negative yield environments by allowing the simulation of negative shocks up to an explicit floor of -1.25% for the downward scenario.
- Considering these recommendations, the Solvency II review specifies that the European Commission shall adopt a Delegated Regulation providing the methods, assumptions and standard parameters to calculate the IR risk sub-module. Therefore, **the EIOPA's proposed methodology and shocks are not yet legally binding and will need to be implemented by this Delegated Regulation in the upcoming months,[12] which is expected to be aligned with EIOPA's initial recommendation**.
- The estimated impact of these changes would be an increase of approximately 6.5% in the SCR on IR risk (based on an illustrative exercise, considering a zero-coupon bond with a time to maturity of six years). Figure 4 illustrates the changes in the IR shocks.

Figure 4: Risk-free curve in EUR and IR shocks (current and recommended) as of September 2024



Source: Deloitte's calculations based on EIOPA Risk-free interest rate term structures.[13]

- This change will be progressively phased in over five years after the amendments are adopted.

Catastrophe risk

Climate change is affecting the frequency and severity of natural catastrophes, with both expected to increase due to ongoing environmental degradation and pollution. This shift could alter the exposure of insurance and reinsurance companies to natural catastrophe risk, potentially rendering the current standard parameters for assessing this risk inaccurate.

To address this, the amending Directive mandates EIOPA to examine (at least every five years) the scope and calibration of the standard parameters in the non-life catastrophe risk sub-module under the standard formula (Article 105[2]). If any discrepancies are identified, EIOPA should submit an opinion to the European Commission.

For example, EIOPA's *2023/2024 reassessment of the natural catastrophe standard formula*,[14] published in April 2024, concluded that a 0.13 country factor for flood risk in Luxembourg would be relevant and that the existing factor for hail risk should be increased.

Prudential treatment of sustainability risks

In its final report on the recommendations for prudential treatment of sustainability risks,[15] EIOPA found that bonds and equities linked to fossil fuels present a higher risk than those exposed to other activities, justifying specific prudential treatment. Based on EIOPA's findings, the industry can expect the introduction of differentiated SCR for equities and bonds linked to fossil fuel sectors.

These requirements would be introduced after the publication of the Solvency II review in a Commission Delegated Regulation, presumably as follows:

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[11] Opinion on the 2020 review of Solvency II - EIOPA

[12] The new proposed IR shocks that include an additive term are defined as: $r_t^{up}(m) = r_t(m) * (1 + s_m^{up}) + \boldsymbol{b_m^{up}}$ and $r_t^{down}(m) = r_t(m) * (1 - s_m^{down}) - \boldsymbol{b_m^{down}}$, respectively. Being $r_t(m)$ the relevant risk-free rate curve s_m the relative component of the shock and b_m the additive component of the shock.

[13] EIOPA, "Risk-free interest rate term structures," accessed 21 November 2024.

[14] EIOPA, *2023/2024 reassessment of the natural catastrophe standard formula*, April 2024.

[15] EIOPA, *Prudential Treatment of Sustainability Risks*, November 2024.

- **Equity risk module:** a dedicated supplementary capital requirement to the current equity risk calibration for fossil fuel-related stocks (+17%?).
- **Credit spread risk:** a dedicated supplementary capital requirement to the current spread risk calibration for fossil fuel-related stocks.

02

Pillar II

Own risk and solvency assessment (ORSA)

- The Solvency II review introduces new elements to the ORSA, such as an analysis of the macroeconomic situation, possible macroeconomic and financial markets' developments, and the capacity to settle financial obligations even under stressed conditions.
- The analysis of macroeconomic and financial markets' developments should include at least the following:
  - The level of interest rates and spreads;
  - The level of financial market indices;
  - Inflation;
  - Interconnectedness with other financial market participants; and
  - Climate change, pandemics, other mass-scale events and other catastrophes that may affect insurance and reinsurance undertakings.
- If requested by a supervisory authority, (re)insurance undertakings should also consider analyzing the macroprudential concerns that may impact the undertaking, as well as how its activities may affect the macroeconomic and financial markets' developments, and have the potential to turn into sources of systemic risk. If requested, this analysis must include, at least, plausible unfavorable future scenarios and risks related to the credit cycle and economic downturn, herding behavior in investments, or excessive exposure concentrations at the sectoral level. However, the analysis of the macroeconomic conditions is not required for SNCUs.
- The ORSA will still be required annually, except for SNCUs and captives (under certain conditions), where it will be required every two years.

Implications of the macroprudential tools

- A new chapter (Chapter VIIA) in the amending Directive establishes a legal basis for the (re)insurance sector's use of macroprudential tools. It aims to address risks that affect the broader financial system, rather than just individual (re)insurance companies. Chapter VIIA ensures that supervisory authorities have the power to, among others:
  - Require firms to prepare and maintain pre-emptive recovery plans;
  - Implement additional capital requirements, and restrict or prohibit certain business activities;
  - Limit or suspend dividends and other payments to shareholders;
  - Require changes in liquidity management to cover short-term liquidity needs; and
  - Require additional macroprudential analysis.

1. Liquidity risk management

Member States must ensure that insurance and reinsurance undertakings draw up and regularly update a liquidity risk management plan covering liquidity analysis over the short term, projecting the incoming and outgoing cash flows regarding their assets and liabilities.

If requested by supervisory authorities, insurance and reinsurance undertakings must extend their liquidity risk management plan to also cover liquidity analysis over the medium and long term. Member States must ensure that insurance and reinsurance undertakings develop and update a set of liquidity risk indicators to identify, monitor and address potential liquidity stress.

In this regard, EIOPA has already launched a consultation (within the first batch[16]) on the **RTS regarding the criteria for defining which undertakings and groups should include medium- and long-term analyses** in their liquidity risk management plans, as well as these plans' content and update frequency. During 2025, **EIOPA will issue an RTS specifying this information**.

SNCUs **are exempted from this requirement**.

2. Pre-emptive recovery plans

The amending Directive will increase supervisory authorities' power, specifically regarding the deterioration of the solvency position. This is linked to the future IRRD,[17] which should enter into force in parallel to the Solvency II review.

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[16] EIOPA opens first batch of consultations on technical standards after Solvency II Review - EIOPA

[17] EUR-Lex, *Proposal for a directive of the European Parliament and of the Council establishing a framework for the recovery and resolution of insurance and reinsurance undertakings*, September 2021.

A pre-emptive recovery plan will be required for major undertakings (targeted at a minimum market coverage of 60%) and will contain:

- A summary of the plan's key elements;
- A description of the undertaking;
- An indicator framework;
- A description of how the pre-emptive recovery plan has been drawn-up, and will be updated and applied;
- A range of remedial actions; and
- A communication strategy.

If the undertaking has breached the SCR and adopted a recovery plan over the last 10 years, it should also include an assessment of the measures adopted to restore its compliance with the SCR. The drawing up, updating and application of pre-emptive recovery plans should be part of the system of governance as defined under Solvency II.

Operational risk management

- The amending Directive will oblige firms to consider **cybersecurity in their operational risk** management system.

Sustainability risk management

- The Solvency II review will require entities to explicitly consider the short, medium and long-term horizon when assessing sustainability risks. For that assessment, the amending Directive requires undertakings to have strategies, policies, processes and systems for identifying, measuring, managing and monitoring sustainability risks.
- Entities will also have to develop plans to address the financial risks arising from sustainability factors, including those from the transition process towards the climate-neutrality objective.[18]
- As a reminder, some of these elements were already included in the last amendments of the Commission Delegated Regulation (EU) 2021/1256 ("current Delegated Regulation")[19] and the taxonomy for the quantitative reporting templates (QRTs):
  - The current Delegated Regulation, which has applied since 2 August 2022, included the consideration of sustainability risks in:
    - The underwriting and reserving policy;
    - The investment risk management policy;
    - The risk management function's tasks when assessing overall solvency needs;
    - The actuarial function's opinion on the underwriting policy;
    - The remuneration policy; and
    - The application of the prudent person principle.
  - The EIOPA reporting taxonomy 2.8.0 (published 17 March 2023)[20] introduced the identification of investments exposed to climate change risks (S.06.04).

Climate risk change scenario analysis

- As part of ORSA's risk identification and assessment, entities will need to evaluate whether they have any material exposure to climate change risks and demonstrate the materiality of their risk exposure.
- If any material exposure is identified, entities will have to specify two long-term scenarios and analyze these scenarios' impact on their business:
  - The global temperature increase remains below 2°C; and
  - The global temperature increase is significantly higher than 2°C.

This analysis is not required for SNCUs.

Governance

- Entities will need to implement a policy promoting diversity in the administrative, management or supervisory body, including gender-balance. EIOPA will issue guidelines on the notion of diversity.
- For SNCUs, the persons responsible for the key functions of risk management, actuarial and compliance may also perform any other key function different from internal audit, or be a member of the administrative, management or supervisory body, provided that certain conditions are met.

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[18] EUR-Lex, *Regulation (EU) 2021/1119 of the European Parliament and of the Council of 30 June 2021 establishing the framework for achieving climate neutrality and amending Regulations (EC) No 401/2009 and (EU) 2018/1999 ('European Climate Law')*, June 2021.
[19] EUR-Lex, *Commission Delegated Regulation (EU) 2021/1256 of 21 April 2021 amending Delegated Regulation (EU) 2015/35 as regards the integration of sustainability risks in the governance of insurance and reinsurance undertakings*, April 2021.
[20] Supervisory reporting - DPM and XBRL - EIOPA

Fit and proper

- Regarding the fit and proper requirements for persons who effectively run the undertaking or have other key functions, entities will need to inform the supervisory authority of the reasons for any changes to these persons' identities. The supervisory authorities will also have the power to require the entity to remove a person from a key function if they do not fulfill the requirements.

Supervision of cross-border activities

- The Solvency II review introduces enhanced supervisory cooperation and information exchange between home and host supervisory authorities regarding **significant cross-border activities**. Cooperation must be commensurate with the risks of the significant cross-border activities and cover at least the system of governance, outsourcing and distribution partnerships, business strategy, claims handling, and consumer protection.
- In this regard, as part of its first batch of consultations[21], EIOPA published an **RTS aimed at defining the criteria and conditions to identify significant cross-border activities** based on both qualitative and quantitative information.

Pillar III

Content of the SFCR

- To meet the needs of different stakeholders, the amended Directive restructures the SFCR into two parts:
  - A part **primarily for policyholders and beneficiaries**, providing key information about the business, performance, capital management, and risk profile.
  - A part **aimed at market professionals**, including detailed information about the business' governance system, technical provisions, solvency position, and other data relevant to specialized analysts.

Audit requirements

- The Solvency II review requires that the **balance sheet** disclosed in the SFCR should be subject to an audit, **except for SNCUs and captives**. Nevertheless, Member States can still apply audit requirements to all undertakings and other parts of the SFCR. The audit shall be carried out by a statutory auditor or an audit firm, in accordance with the auditing standards applicable.[22]
- The insurance and reinsurance undertaking should submit a separate report, including a description of the audit's nature and results and prepared by the statutory auditor or the audit firm, together with the SFCR to the supervisory authority.

Deadlines for QRTs, RSR and SFCR submission

- Due to the audit requirement on balance sheet disclosed in the SFCR, the Solvency II review extends the reporting periods for submissions as follows:
  - The deadline for annual QRTs will increase from 14 to 16 weeks;
  - The deadlines for RSR and SFCR will be extended from 14 to 18 weeks; and
  - The deadline for group SFCRs will be extended from 20 to 22 weeks.

However, the deadlines for quarterly reporting remain unchanged, with five weeks for solo QRTs and 11 weeks for group QRTs.

Other proportionality in reporting requirements

- **On the SFCR: SNCUs may disclose only the quantitative data** required by the implementing technical standards (ITS) on the SFCR's content[23], consisting of information targeted to other market professionals. Under certain conditions, captives are also exempted from disclosing the first part of the SFCR and are only required to include the quantitative data in the second part.
- **On the RSR**: this report's frequency is at least every three years. However, where the supervisory authority permits, **SNCUs may only need to submit the RSR at least every five years.** In addition, supervisory authorities can limit the RSR if it is burdensome relative to the nature, scale, and complexity of risks.

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[21] EIOPA opens first batch of consultations on technical standards after Solvency II Review - EIOPA

[22] Pursuant to Article 26 of Directive 2006/43/EC. Statutory auditors and audit firms, when performing this task, shall comply with the duties of auditors set out in Article 72 of this Directive.

[23] Commission Implementing Regulation (EU) 2015/2452 of 2 December 2015 laying down implementing technical standards with regard to the procedures, formats and templates of the solvency and financial condition report in accordance with Directive 2009/138/EC of the European Parliament and of the Council

- **On captives:** they are **exempted from regular supervisory reporting on an item-by-item basis** (i.e., from submitting specific reports) if the predefined reporting periods are less than one year and if some conditions are met (all the insured persons are legal entities of the captive's group or natural persons covered by the group's policies).

Proportionality measures

Exclusion thresholds from the Solvency II scope

The amending Directive excludes undertakings that meet the following criteria:

- Annual gross written premium (GWP) income does not exceed €15 million (previously €5 million);
- Total technical provisions, before reinsurance and special purpose vehicles, do not exceed €50 million (previously €25 million); and
- For undertakings that are part of a group, the group's total technical provisions, before reinsurance and special purpose vehicles, do not exceed €50 million (previously €25 million).

Criteria for identifying Small and non-complex undertakings (SNCUs)

Undertakings (including captives) can be classified as SNCUs if the following conditions are met for two consecutive financial years:

- **General criteria for all undertakings**
  - Annual GWP income from business underwritten in a foreign Member State should be lower than any of the two following thresholds:
    - €20 million; or
    - Ten percent of its total annual GWP income.
  - The following sum does not exceed 20% of the total investments:
    - The gross market risk module;
    - The part of the counterparty default risk module corresponding to securitizations, derivatives, receivables from intermediaries and other investment assets, which are not covered in the spread risk sub-module; and
    - Other capital requirements applied on intangible assets and not covered by the market risk and counterparty default risk modules.
  - The reinsurance accepted by the undertaking does not exceed 50% of its total annual GWP.
  - The SCR is complied with.
- **Additional criteria for life undertakings**, whose technical provisions related to life activities represent 20% or more of the total, and annual GWP income related to non-life activities represent less than 40% of the total:
  - The IR risk submodule should not exceed 5% of the technical provisions; and
  - Technical provisions related to life activities should not exceed €1 billion.
- **Additional criteria for non-life undertakings**, whose annual GWP income related to non-life activities represents 40% or more of its total, and technical provisions related to life activities represent less than 20% of its total:
  - The average combined ratio for non-life activities net of reinsurance of the past three years is less than 100%; and
  - The annual GWP income from non-life activities should be lower than €100 million.

- On 2 August 2024, **EIOPA launched a consultation[24] on the methodology** for identifying small and non-complex undertakings and groups and to ensure consistency in applying these criteria across Member States. On classifying undertakings and groups as small and non-complex, EIOPA believes that the proposed methodology is clear and comprehensive, and that no further specifications at this point are required.
- However, regarding the conditions for permitting the use of proportionality measures for insurers not classified as small and non-complex, EIOPA is proposing a set of conditions and consulting on each one of them.

Captives

- Captive (re)insurance undertakings should also be able to benefit from the proportionality measures when classified as SNCUs. However, **points (i) and (ii) of the general criteria for all undertakings described previously do not apply to captives**.
- **Additional criteria applicable to captives:** even if they do not comply with the criteria to be classified as SNCU, captives shall also be classified as SNCUs if they meet both of the following conditions:
  - Insured persons and beneficiaries must be either:
    - Legal entities within the group; or
    - Natural persons covered under the group's insurance policies, with their business limited to 5% of technical provisions; and
  - The (re)insurance obligations must not include compulsory third-party liability insurance.

[24] EIOPA, *EIOPA consults on new proportionality regime under Solvency II*, 2 August 2024.

Summary of the proportionality measures

Measures	Applicable for SNCUs (including captives classified as SNCU)	Applicable only for (re)insurance captives NOT classified as SNCU
Calculation of technical provisions	**May use a prudent deterministic valuation** to calculate the best estimate for life obligations with options and guarantees, instead of using a full stochastic model.	
Liquidity risk management plan	Exempted	
Governance – key functions	Persons responsible for the **key functions** of risk management, actuarial and compliance **may also perform any other key function** different from internal audit, any other function, or be a member of the administrative, management or supervisory body.	
ORSA	ORSA will only be **required every two years.**	**Under certain conditions,**[25] ORSA will only **be required every two years.**
ORSA - analysis of two climate scenarios if material exposures are identified	Exempted	
ORSA - analysis of the macroeconomic conditions	Exempted	
SFCR - audit of the balance sheet	Exempted from auditing the balance sheet disclosed in the SFCR.	
SFCR - content	May disclose **only the quantitative data** required.	(**All captives**) Under certain conditions, may disclose only the quantitative data required.
SFCR for policyholders		Exempted under certain conditions.
RSR	Only required **at least every five years** instead of three years.	Only required **at least every five years** instead of three years. Also, an exemption on **an item-by-item basis is possible.**

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[25] See article 45, paragraph 5 of the Solvency 2 Review.

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