

EIOPA Consultation Paper on guidelines for supervisory reporting and public disclosure



November 2011

The first public consultation papers on the proposed guidelines for supervisory reporting and public disclosure look set to increase the level of disclosure required under Solvency II

INTRODUCTION

On 8 November 2011, the European Insurance and Occupational Pensions Authority (EIOPA) published a series of documents relating to the Solvency II Pillar 3 reporting requirements including:

- a consultation paper on the proposal on Quantitative Reporting Templates (QRTs);
- a consultation paper on the draft proposal for guidelines on Narrative Public Disclosure & Supervisory Reporting, Predefined Events and Processes for Reporting & Disclosure;
- Quantitative Reporting Templates for solo companies;
- Quantitative Reporting Templates for groups;
- Reporting instructions (LOG and summary files) to accompany the QRTs; and,
- an impact assessment on the Solvency II reporting package.

These documents build on the previous content of Consultation Paper 58 and two rounds of informal pre-consultation carried out with selected stakeholders from January to March 2011. The current consultation papers have been developed from feedback produced from the informal pre-consultation and aim to provide a "largely stabilised reporting package on topics that have already been extensively discussed".

The impact assessment highlights how the current consultation papers reflect the issues identified from the feedback received during the earlier pre-consultation process.

While EIOPA considers the reporting package to be largely stable, the latest text was developed in advance of the finalisation of Omnibus II and the Level 2 text. As a result, there are a number of

areas where the draft Level 2 text may be subject to change, and where the impact on reporting will need to be taken into consideration after this public consultation. The cover note to these documents lists the following areas as subject to potential future adjustment:

- Counter-cyclical and matching premiums;
- Expected Profits Included in Future Premiums;
- Participations;
- Ring-fenced Funds;
- Branches of 3rd country firms; and,
- Modification of certain SCR modules.

The cover note also sets out a number of specific questions where EIOPA is seeking further feedback from stakeholders. It notes that the additional data to be collected for financial stability purposes is not covered by this set of templates, and this will be consulted on separately in December 2011.

We note that the consultation paper on narrative reporting aims to further specify elements of the Level 1 Directive and Level 2 text to "foster convergence at the European level" and is based on the last draft Level 2 text circulated to EIOPA by the Commission.

As the draft Level 2 text has been made available in varying degrees to stakeholders, it is possible that EIOPA will receive feedback based on different levels of understanding from participants.

To assist you in digesting the draft guidelines, Milliman has provided this short summary of the content of the papers, including three annexes on detailed requirements, and a brief analysis of what we expect these documents to mean for companies.

PROPOSAL ON QUANTITATIVE REPORTING TEMPLATES

This short consultation paper and accompanying spreadsheets set out the draft proposal for the quantitative reporting requirements under Solvency II. These are aimed at defining a fully harmonised set of reporting requirements, but with country-specific reports where required to meet local market or national legal requirements.

While many companies will find the accompanying templates prescribe a similar level of disclosure to that already required under the current FSA forms in the UK, more onerous requirements are proposed around the disclosure of cashflows and the level of reporting detail required for asset holdings.

The FSA is expected to conduct an informal consultation on nation-specific templates via the ABI over the next couple of months, with a formal consultation due in 2012. One area where we would expect to see additional UK-specific reporting requirements would be around with-profits business.

Each template is accompanied by a series of LOG and summary documents. The LOG files are effectively a set of instruction manuals providing a definition, examples and purpose of each cell in the data tables and summary documents. The summary documents aim to provide information on the purpose, potential benefits and costs, application to groups, materiality thresholds, public disclosure and frequency of each template.

Solo templates are classified into 7 categories (some of which are applicable to groups where identified):

- Balance sheet;
- Own Funds;
- Capital Requirements (SCR/MCR);
- Assets;
- Technical Provisions (Life and Non-life);
- Reinsurance; and,
- Variation Analysis.

In addition, there a number of group-specific templates covering:

- Scope of the group;
- Overview of solo requirements;
- Contribution to group figures by entity (including own funds);
- Intra-group transactions; and,
- Risk concentration.

The paper sets out 6 requirements which are closely based on the guidelines set out in the pre-consultation paper published in January 2011. These make reference to the accompanying templates and provide details on how companies are expected to complete these, pointing firms to the accompanying LOG files for specific details on how to complete each template cell.

The paper explains that companies will need to complete these templates at least annually, with "core" templates required quarterly. Details of which templates are required on a quarterly basis are contained in a Technical Annex to the paper together with details of which templates are applicable to solo undertakings and groups, and which templates are required for public disclosure on an annual basis. In addition, the paper sets out a proposal requiring solo companies to submit a number of specific templates demonstrating the own funds, technical provisions and SCR requirements for each material ring-fenced fund.

The paper indicates that the following templates would be required quarterly (although possible exceptions apply to a number of items as set out in the summary documents):

- Balance sheet;
- Own funds;
- Minimum capital requirement;
- Premiums, claims and expenses;
- Investment data;
- Derivatives data;
- Investment funds (on a look-through basis);
- Technical provisions; and,
- Outgoing reinsurance.

In addition, the paper sets out a proposal requiring solo companies to submit a number of specific templates demonstrating the own funds, technical provisions and SCR requirements for each material ring-fenced fund.

A summary of the high level changes to the QRTs is contained in annex 1 to this summary paper.

We note that although the latest QRTs are broadly consistent with those released in January 2011, there are a number of changes to both the solo and group-specific QRTs which firms will need to consider. These are expanded upon in Annex 1.

While most of these changes appear to be intended to add greater clarity around the information required, we note there are a number of areas where the reporting requirements have increased. This includes the need to report investment funds on a look-through basis in both the balance sheet and quarterly asset templates.

It is currently unclear how groups using the deduction and aggregation method should include results from subsidiaries in equivalent third countries in the QRTs. Further guidance may be needed on whether local figures should be used in these cases.

PUBLIC DISCLOSURE, REGULAR SUPERVISORY REPORTING AND PREDEFINED EVENTS

This paper expands upon the matters set out in Articles 35, 51, 53-55, 254 and 256 of the Solvency II Directive aimed at harmonising public and supervisory reporting across Europe. The paper also provides guidance on the minimum content acceptable for selected sections of the public Solvency and Financial Condition Report (SFCR) and the private Regular Supervisory Reporting (RSR). It also provides guidance on the nature of pre-defined events which may trigger additional reporting to the supervisor.

Companies will be required to create policies in respect of reporting and disclosure and the paper provides some guidance on the general principles to be adopted.

The paper sets out 55 guidelines, 21 of which relate to the narrative of the SFCR, 8 to the narrative of the RSR and the remainder to the requirements for reporting and the pre-defined events. It is noted that the guidelines relate to solo companies, groups and, in some cases, companies which are part of a group.

Groups have two options for the structure of their SFCR: an SFCR can be produced covering the group itself with separate SFCRs for each solo entity; or, the group can submit a single SFCR covering the aggregate group position. Where a

single SFCR is prepared for a group, the information for each subsidiary must be easily identifiable and the group must provide information on how the subsidiaries are covered and the involvement of the subsidiary Boards.

The guidelines which relate to the SFCR or to the RSR are considered under the broad headings:

- Business and Performance;
- Systems of Governance;
- Risk Profile;
- Valuation for solvency purposes; and,
- Capital Management.

While the structures of the reports are broadly similar, the guidelines are not the same for the SFCR and the RSR. Detailed breakdowns of the required contents of the SFCR and RSR are set out in annexes 2 and 3 to this summary paper.

We note that the latest consultation paper contains 55 guidelines, significantly more than the 38 guidelines set out in the pre-consultation text released in January 2011.

Furthermore, a number of the guidelines carried across have been extensively re-worded reflecting the need for companies to report new content or additional information. Notably, while the reporting requirements within the SFCR appear to have increased significantly, particularly around the level of disclosure relating to own funds, the requirement to report on the ORSA in the RSR has been removed.

New guidelines include:

- additional disclosure of asset and liability information relating to valuation for solvency purposes for the SFCR;
- significantly increased disclosure around own funds in the SFCR; and,
- new requirements to disclose information on assets and technical provisions in respect of the valuation for solvency purposes in the RSR.

SUPERVISORY REPORTING FOLLOWING PRE-DEFINED EVENTS

The paper states that companies should consider 'pre-defined events' as those events that could reasonably be expected to lead to material changes in the business and performance, governance procedures, risk profile or solvency and financial position of the company or the group. Firms would

be required to report to the supervisor if such an event occurred. The guidance indicates that the need to undertake an additional ORSA would constitute such an event.

The background discussion outlines some events which EIOPA suggests may constitute pre-defined events. These include:

- changes in business strategy;
- mergers, takeovers and acquisitions;
- internal reorganisation;
- significant lawsuits or claims;
- material changes in the level of own funds, technical provisions or SCR;
- new or emerging risks of a material nature;
- governance or operational failures; and,
- a very significant intra-group transaction.

REPORTING AND DISCLOSURE POLICIES

Companies should maintain a disclosure policy identifying:

- who is responsible for setting and maintaining the policy; and,
- how its requirements are met in the preparation and review of information within the business organisation prior to disclosure.

Companies may outline information which is believed to be in the public domain and therefore need not form part of the reporting requirements. Such information must be cross-referred to the specific point of usage, not just by document. However, the RSR must be a free-standing document and should not contain cross references to other documents.

Companies may apply to the supervisor if there is specific information which it does not wish to reveal, although a company should not enter into contractual confidentiality arrangements to avoid disclosure in the SFCR.

Companies should include in the disclosure policy any information which it intends to provide voluntarily but this information should not include confidential information provided by a supervisor without the prior agreement of the supervisor.

Companies should also maintain a reporting policy detailing who has responsibility for preparing and reviewing reports to the supervisor, the processes and timelines for the preparation of reporting, ensuring accuracy, completeness and consistency of reporting, and approval of reporting.

SUMMARY

This package of consultation papers and accompanying templates closely follows the layout of the pre-consultation package released by EIOPA in January 2011.

The package aims to further specify elements of the Level 1 Directive and Level 2 Delegated Acts to “foster convergence at the European level” and as such is based on the last draft Delegated Act text circulated to EIOPA by the Commission. However, as the current draft Level 2 text has only been made available to a limited number of stakeholders, firms will need to provide comment based on the latest version of the text to which they have access.

While many firms may be pleased to note that the latest QRTs are broadly consistent with the pre-consultation templates released in January 2011, there are a number of changes to both the solo and group-specific QRTs which firms will need to ensure can be met from their systems. The proposed templates require significantly increased reporting detail in relation to assets and derivative transactions compared to that required for the current FSA forms. As this level of detail is required purely for supervisory reporting purposes, and does not appear to be required for the calculation of regulatory capital, it is unclear to us how supervisors will be able to review this level of information on a regular (quarterly) basis.

The requirements surrounding the SFCR and RSR have been significantly re-developed with additional information required in a number of areas. Firms that have already made progress in designing the layout and processes for completing these reports will need to ensure any new requirements are adequately incorporated.

Any comments on this consultation paper should be provided directly to EIOPA, using the template on its website, by 20 January 2012. EIOPA has commented that it expects to finalise the reporting package in summer 2012.

ABOUT MILLIMAN

Milliman is among the world's largest independent actuarial and consulting firms. Founded in 1947, the company currently has 54 offices in key locations worldwide employing more than 2,500 people.

www.milliman.com

MILLIMAN IN EUROPE

Milliman maintains a strong and growing presence in Europe with 250 professional consultants serving clients from offices in Amsterdam, Bucharest, Dublin, London, Madrid, Milan, Munich, Paris, Warsaw, and Zurich.

www.milliman.co.uk



CONTACT

If you have any questions or comments on this briefing paper or any other aspect of Solvency II, please contact any of the consultants below or your usual Milliman consultant.

William Coatesworth
william.coatesworth@milliman.com
+44 20 7847 1655

John McKenzie
john.mckenzie@milliman.com
+44 20 7847 1531

ANNEX 1 - HIGH-LEVEL CHANGES TO QUANTITATIVE REPORTING TEMPLATES

The following annex sets out a high-level overview of the major differences¹ between the current and pre-consultation quantitative reporting templates.

Balance sheets

The accompanying summary file to balance sheet BS-C1 now states that firms would only be required to submit this template quarterly where the reconciliation reserve cannot be sufficiently explained by the asset and liability information supplied on other quarterly templates.

Solvency Capital Requirements

For firms using full or partial internal models, some additional information is required on the SCR templates, including details on the loss absorbing capacity of technical provisions, adjustments for deferred taxation, and details of the notional SCR for any ring-fenced funds (consistent with the standard formula requirements).

We note that, while the cells relating to simplifications used in the calculation of the components for the underwriting sub-modules have been removed from the current version of the templates, the accompanying LOG files confirm that these may still be used.

The information to be provided on the market risk sub-module now includes details on the counter-cyclical premium risk (in place of illiquidity risk), while the illiquidity reporting buckets have been removed from the technical provisions template. This provides further evidence of the expected inclusion of the counter-cyclical premium in the next iteration of the Level 2 text.

Assets

While most of the asset templates remain unchanged, a new template is included for historical derivative trades. This is aimed at reporting all of the derivatives trades executed over the reporting period (1 January to 31 December) on a trade-by-trade approach. Under this, each transaction should be reported separately with no off-setting.

¹ This annex should not be considered a comprehensive list of changes to the QRTs.

Variation analysis

The templates for variation analysis have been significantly re-developed with separate templates now included for analysing the change in own funds resulting from investments, technical provisions, and own debt and other items. We note that the proportionality statement on the variation analysis templates, which previously made these only applicable to larger firms, has been removed from the current set of templates. This appears consistent with the accompanying summary document which states that no materiality criteria are applicable to these templates.

Groups

Groups are required to report on both the solo templates applicable to groups and on group-specific templates.

We note that, while several new templates have been included in the solo QRT pack specifically for groups (including moving the template for group own funds from the group-specific pack), the number of group-specific templates has been reduced. The templates for inter-group transactions have been consolidated into three (rather than six), and the templates in respect of the following areas have been removed:

- G10 - Main technical data for (re)insurance undertakings; and,
- G15 - Subordinated liabilities.

Non-life companies

As expected, the template for the non-life catastrophe risk sub-module has been extensively reworked to provide greater breakdown and clarity around the components of the capital calculation. Further changes may be made to this once the Delegated Acts are finalised.

Further information is required on annuities stemming from non-life obligations on template TP-F4, while the template requiring information on non-life insurance premium and expense information (TP-E5) has been removed. We note a greater level of information is now required on the peak and mass underwriting risks (now based on net retention).

Reinsurance

Additional information is required on companies' reinsurance programs and SPV arrangements.

ANNEX 2 –BREAKDOWN OF SFCR

Business and Performance

- holders of qualifying holdings, including details of proportion of ownership interest/voting power held;
- name and location of parent and ultimate parent entity;
- material subsidiaries and significant investments in joint controlled entities;
- a simplified structure chart and information on organisational structure; and,
- qualitative and quantitative information on intra-group transactions and operations.

Systems of Governance

- how the risk management, actuarial, compliance and internal audit functions are integrated into the structure and decision making process of the business, including how they have the authority and resources to undertake their tasks;
- the position of the risk management function in the organisational structure, and the role of committees and personnel in the governance and validation of the internal model and processes to calculate the SCR; and,
- the processes by which it is ensured that management information is timely and delivered accurately.

Valuation for solvency purposes

- qualitative and quantitative information for each material asset class on the Solvency II balance sheet on the recognition and valuation basis (and any changes to this), assumptions and judgement, methods and inputs for calculating the economic value and any use of expert judgement;
- explanation of any material differences between the valuation of assets in the Solvency II balance sheet and the financial statements;
- information on intangible assets, financial assets, lease assets, holdings in related undertakings, and deferred tax assets;
- information on technical provisions including any simplifications used, and an explanation of the general approach to contract boundaries;
- information on other liabilities, lease liabilities, provisions other than technical provisions and contingent liabilities, employee benefits, and deferred tax liabilities; and,
- a description of the processes and procedures employed for ensuring timely delivery of reliable financial and non financial information.

Capital Management

- the solvency ratio as the ratio of the value of own funds to the SCR;
- information on the objectives, policies and processes for managing own funds;
- information on the structure, amount and quality of own funds at the end of the reporting period (and analysis of any significant changes in each tier over the period);
- information covering the value and extent of subordination of specific own fund items;
- disclosure of eligible own funds to cover the SCR and MCR, including explanation of any restrictions and limits;
- an explanation of key elements of the disclosure reserve;
- information on transitional arrangements for each own fund item including the assigned tier and call dates;
- disclosure of any methods used to determine amount of ancillary own fund items including variations in valuation over time and key drivers of variations;
- information on the excess of assets over liabilities in ring-fenced funds;
- description of each material ancillary own fund item including information on the form of the arrangement, nature of the basic own fund item it would become and details of supervisory approval;
- additional information in relation to own funds of participating companies including which items have been issued within the group, information on local tiering of items where issued in an equivalent third country, and any restrictions on transferability and fungibility;
- justification that the simplifications used to calculate the SCR are proportionate to the nature, scale and complexity of risks;
- information on the differences between any Internal Model and the standard formula covering the structure, scope and methodologies;
- high level description of the operational performance of any internal model; and,
- a description of the process for checking data quality.

ANNEX 3 –BREAKDOWN OF RSR

Business and Performance

- information on the number of employees;
- a list of subsidiaries and a structure chart;
- information on distributions to shareholders;
- the effectiveness of risk mitigation techniques and its impact on underwriting performance;
- information on significant related party transactions; and,
- qualitative and quantitative information on intra-group transactions.

Systems of Governance

- the company's governance structure and an organisational chart showing the position of the key function holders;
- information on how remuneration policies and practices promote sound and effective risk management;
- details of compliance with Centralised Risk Management requirements (where applicable); and,
- the procedures used for each material category of risk, including management, documentation, monitoring and enforcement.

Risk Profile

- the risk exposure and the methods used to ensure that the use of derivatives contributes to the reduction of risks or efficient portfolio management; and,
- detailed qualitative and quantitative information on significant risk concentrations at group level for participating companies.

Valuation for Solvency Purposes

- methods for asset valuations other than quoted market prices or adjusted equity method;
- details of deferred tax assets;
- information on technical provisions including methodologies and assumptions, simplifications, application of contract boundaries, details of options and guarantees, overview of material changes, details of data deficiencies and adjustments, and details of any economic scenario generator used; and,
- information on preparation of group accounts.

Capital Management

- the allowance for reinsurance, financial mitigation techniques or future management actions in the calculation of the SCR, and how these satisfy the criteria for recognition.