

Directive 2009/138/EC of the European Parliament and of the Council  
of 25 November 2009 on the taking-up and pursuit of the business of  
Insurance and Reinsurance (Solvency II) (recast) (Text with EEA relevance)

TITLE I

**GENERAL RULES ON THE TAKING-UP AND PURSUIT OF  
DIRECT INSURANCE AND REINSURANCE ACTIVITIES**

CHAPTER VI

**Rules relating to the valuation of assets and liabilities, technical provisions, own funds,  
Solvency Capital Requirement, Minimum Capital Requirement and investment rules**

Section 1

**Valuation of assets and liabilities**

*Article 75*

**Valuation of assets and liabilities**

1 Member States shall ensure that, unless otherwise stated, insurance and reinsurance undertakings value assets and liabilities as follows:

- a assets shall be valued at the amount for which they could be exchanged between knowledgeable willing parties in an arm's length transaction;
- b liabilities shall be valued at the amount for which they could be transferred, or settled, between knowledgeable willing parties in an arm's length transaction.

When valuing liabilities under point (b), no adjustment to take account of the own credit standing of the insurance or reinsurance undertaking shall be made.

[<sup>F12</sup> The Commission shall adopt delegated acts in accordance with Article 301a to lay down the methods and assumptions to be used in the valuation of assets and liabilities as laid down in paragraph 1.

3 In order to ensure consistent harmonisation in relation to valuation of assets and liabilities, EIOPA shall, subject to Article 301b, develop draft regulatory technical standards to specify:

- a to the extent that the delegated acts referred to in paragraph 2 require the use of international accounting standards as adopted by the Commission in accordance with Regulation (EC) No 1606/2002, the consistency of those accounting standards with the valuation approach of assets and liabilities as laid down in paragraphs 1 and 2;
- b the methods and assumptions to be used where quoted market prices are either not available or where international accounting standards as adopted by the Commission in accordance with Regulation (EC) No 1606/2002 are either temporarily or permanently inconsistent with the valuation approach of assets and liabilities as laid down in paragraphs 1 and 2;

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- c the methods and assumptions to be used in the valuation of assets and liabilities as laid down in paragraph 1, where the delegated acts referred to in paragraph 2 allow for the use of alternative valuation methods.

Power is delegated to the Commission to adopt the regulatory technical standards referred to in the first subparagraph in accordance with Articles 10 to 14 of Regulation (EU) No 1094/2010.]

#### **Textual Amendments**

- F1** Substituted by Directive 2014/51/EU of the European Parliament and of the Council of 16 April 2014 amending Directives 2003/71/EC and 2009/138/EC and Regulations (EC) No 1060/2009, (EU) No 1094/2010 and (EU) No 1095/2010 in respect of the powers of the European Supervisory Authority (European Insurance and Occupational Pensions Authority) and the European Supervisory Authority (European Securities and Markets Authority).

## Section 2

### **Rules relating to technical provisions**

#### *Article 76*

#### **General provisions**

1 Member States shall ensure that insurance and reinsurance undertakings establish technical provisions with respect to all of their insurance and reinsurance obligations towards policy holders and beneficiaries of insurance or reinsurance contracts.

2 The value of technical provisions shall correspond to the current amount insurance and reinsurance undertakings would have to pay if they were to transfer their insurance and reinsurance obligations immediately to another insurance or reinsurance undertaking.

3 The calculation of technical provisions shall make use of and be consistent with information provided by the financial markets and generally available data on underwriting risks (market consistency).

4 Technical provisions shall be calculated in a prudent, reliable and objective manner.

5 Following the principles set out in paragraphs 2, 3 and 4 and taking into account the principles set out in Article 75(1), the calculation of technical provisions shall be carried out in accordance with Articles 77 to 82 and 86.

#### *Article 77*

#### **Calculation of technical provisions**

1 The value of technical provisions shall be equal to the sum of a best estimate and a risk margin as set out in paragraphs 2 and 3.

2 The best estimate shall correspond to the probability-weighted average of future cash-flows, taking account of the time value of money (expected present value of future cash-flows), using the relevant risk-free interest rate term structure.

The calculation of the best estimate shall be based upon up-to-date and credible information and realistic assumptions and be performed using adequate, applicable and relevant actuarial and statistical methods.

The cash-flow projection used in the calculation of the best estimate shall take account of all the cash in- and out-flows required to settle the insurance and reinsurance obligations over the lifetime thereof.

The best estimate shall be calculated gross, without deduction of the amounts recoverable from reinsurance contracts and special purpose vehicles. Those amounts shall be calculated separately, in accordance with Article 81.

3 The risk margin shall be such as to ensure that the value of the technical provisions is equivalent to the amount that insurance and reinsurance undertakings would be expected to require in order to take over and meet the insurance and reinsurance obligations.

4 Insurance and reinsurance undertakings shall value the best estimate and the risk margin separately.

However, where future cash flows associated with insurance or reinsurance obligations can be replicated reliably using financial instruments for which a reliable market value is observable, the value of technical provisions associated with those future cash flows shall be determined on the basis of the market value of those financial instruments. In this case, separate calculations of the best estimate and the risk margin shall not be required.

5 Where insurance and reinsurance undertakings value the best estimate and the risk margin separately, the risk margin shall be calculated by determining the cost of providing an amount of eligible own funds equal to the Solvency Capital Requirement necessary to support the insurance and reinsurance obligations over the lifetime thereof.

The rate used in the determination of the cost of providing that amount of eligible own funds (Cost-of-Capital rate) shall be the same for all insurance and reinsurance undertakings and shall be reviewed periodically.

The Cost-of-Capital rate used shall be equal to the additional rate, above the relevant risk-free interest rate, that an insurance or reinsurance undertaking would incur holding an amount of eligible own funds, as set out in Section 3, equal to the Solvency Capital Requirement necessary to support insurance and reinsurance obligations over the lifetime of those obligations.

### *f<sup>2</sup>Article 77a*

#### **Extrapolation of the relevant risk-free interest rate term structure**

The determination of the relevant risk-free interest rate term structure referred to in Article 77(2) shall make use of, and be consistent with, information derived from relevant financial instruments. That determination shall take into account relevant financial instruments of those maturities where the markets for those financial instruments as well as for bonds are deep, liquid and transparent. For maturities where the markets for the relevant financial instruments or for bonds are no longer deep, liquid and transparent, the relevant risk-free interest rate term structure shall be extrapolated.

The extrapolated part of the relevant risk-free interest rate term structure shall be based on forward rates converging smoothly from one or a set of forward rates in relation to

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the longest maturities for which the relevant financial instrument and the bonds can be observed in a deep, liquid and transparent market to an ultimate forward rate.

#### **Textual Amendments**

- F2** Inserted by [Directive 2014/51/EU of the European Parliament and of the Council of 16 April 2014 amending Directives 2003/71/EC and 2009/138/EC and Regulations \(EC\) No 1060/2009, \(EU\) No 1094/2010 and \(EU\) No 1095/2010 in respect of the powers of the European Supervisory Authority \(European Insurance and Occupational Pensions Authority\) and the European Supervisory Authority \(European Securities and Markets Authority\).](#)

#### *Article 77b*

#### **Matching adjustment to the relevant risk-free interest rate term structure**

1 Insurance and reinsurance undertakings may apply a matching adjustment to the relevant risk-free interest rate term structure to calculate the best estimate of a portfolio of life insurance or reinsurance obligations, including annuities stemming from non-life insurance or reinsurance contracts subject to prior approval by the supervisory authorities where the following conditions are met:

- a the insurance or reinsurance undertaking has assigned a portfolio of assets, consisting of bonds and other assets with similar cash-flow characteristics, to cover the best estimate of the portfolio of insurance or reinsurance obligations and maintains that assignment over the lifetime of the obligations, except for the purpose of maintaining the replication of expected cash flows between assets and liabilities where the cash flows have materially changed;
- b the portfolio of insurance or reinsurance obligations to which the matching adjustment is applied and the assigned portfolio of assets are identified, organised and managed separately from other activities of the undertakings, and the assigned portfolio of assets cannot be used to cover losses arising from other activities of the undertakings;
- c the expected cash flows of the assigned portfolio of assets replicate each of the expected cash flows of the portfolio of insurance or reinsurance obligations in the same currency and any mismatch does not give rise to risks which are material in relation to the risks inherent in the insurance or reinsurance business to which the matching adjustment is applied;
- d the contracts underlying the portfolio of insurance or reinsurance obligations do not give rise to future premium payments;
- e the only underwriting risks connected to the portfolio of insurance or reinsurance obligations are longevity risk, expense risk, revision risk and mortality risk;
- f where the underwriting risk connected to the portfolio of insurance or reinsurance obligations includes mortality risk, the best estimate of the portfolio of insurance or reinsurance obligations does not increase by more than 5 % under a mortality risk stress that is calibrated in accordance with Article 101(2) to (5);
- g the contracts underlying the portfolio of insurance or reinsurance obligations include no options for the policy holder or only a surrender option where the surrender value does not exceed the value of the assets, valued in accordance with Article 75, covering the insurance or reinsurance obligations at the time the surrender option is exercised;
- h the cash flows of the assigned portfolio of assets are fixed and cannot be changed by the issuers of the assets or any third parties;

- i the insurance or reinsurance obligations of an insurance or reinsurance contract are not split into different parts when composing the portfolio of insurance or reinsurance obligations for the purpose of this paragraph.

Notwithstanding point (h) of the first subparagraph, insurance or reinsurance undertakings may use assets where the cash flows are fixed except for a dependence on inflation, provided that those assets replicate the cash flows of the portfolio of insurance or reinsurance obligations that depend on inflation.

In the event that issuers or third parties have the right to change the cash flows of an asset in such a manner that the investor receives sufficient compensation to allow it to obtain the same cash flows by re-investing in assets of an equivalent or better credit quality, the right to change the cash flows shall not disqualify the asset for admissibility to the assigned portfolio in accordance with point (h) of the first subparagraph.

2 Insurance or reinsurance undertakings that apply the matching adjustment to a portfolio of insurance or reinsurance obligations shall not revert back to an approach that does not include a matching adjustment. Where an insurance or reinsurance undertaking that applies the matching adjustment is no longer able to comply with the conditions set out in paragraph 1, it shall immediately inform the supervisory authority and take the necessary measures to restore compliance with those conditions. Where the undertaking is not able to restore compliance with those conditions within two months of the date of non-compliance, it shall cease to apply the matching adjustment to any of its insurance or reinsurance obligations and shall not apply the matching adjustment for a period of a further 24 months.

3 The matching adjustment shall not be applied with respect to insurance or reinsurance obligations where the relevant risk-free interest rate term structure to calculate the best estimate for those obligations includes a volatility adjustment under Article 77d or transitional measure on the risk-free interest rates under Article 308c.

#### **Textual Amendments**

- F2** Inserted by [Directive 2014/51/EU of the European Parliament and of the Council of 16 April 2014 amending Directives 2003/71/EC and 2009/138/EC and Regulations \(EC\) No 1060/2009, \(EU\) No 1094/2010 and \(EU\) No 1095/2010 in respect of the powers of the European Supervisory Authority \(European Insurance and Occupational Pensions Authority\) and the European Supervisory Authority \(European Securities and Markets Authority\).](#)

### *Article 77c*

#### **Calculation of the matching adjustment**

1 For each currency the matching adjustment referred to in Article 77b shall be calculated in accordance with the following principles:

- a the matching adjustment must be equal to the difference of the following:
  - (i) the annual effective rate, calculated as the single discount rate that, where applied to the cash flows of the portfolio of insurance or reinsurance obligations, results in a value that is equal to the value in accordance with Article 75 of the portfolio of assigned assets;
  - (ii) the annual effective rate, calculated as the single discount rate that, where applied to the cash flows of the portfolio of insurance or reinsurance

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- obligations, results in a value that is equal to the value of the best estimate of the portfolio of insurance or reinsurance obligations where the time value of money is taken into account using the basic risk-free interest rate term structure;
- b the matching adjustment must not include the fundamental spread reflecting the risks retained by the insurance or reinsurance undertaking;
  - c notwithstanding point (a), the fundamental spread must be increased where necessary to ensure that the matching adjustment for assets with sub-investment grade credit quality does not exceed the matching adjustments for assets of investment grade credit quality and the same duration and asset class;
  - d the use of external credit assessments in the calculation of the matching adjustment must be in accordance with Article 111(1)(n).
- 2 For the purposes of paragraph 1(b), the fundamental spread shall be:
- a equal to the sum of the following:
    - (i) the credit spread corresponding to the probability of default of the assets;
    - (ii) the credit spread corresponding to the expected loss resulting from downgrading of the assets;
  - b for exposures to Member States' central governments and central banks, no lower than 30 % of the long-term average of the spread over the risk-free interest rate of assets of the same duration, credit quality and asset class, as observed in financial markets;
  - c for assets other than exposures to Member States' central governments and central banks, no lower than 35 % of the long-term average of the spread over the risk-free interest rate of assets of the same duration, credit quality and asset class, as observed in financial markets.

The probability of default referred to in point (a)(i) of the first subparagraph shall be based on long-term default statistics that are relevant for the asset in relation to its duration, credit quality and asset class.

Where no reliable credit spread can be derived from the default statistics referred to in the second subparagraph, the fundamental spread shall be equal to the portion of the long-term average of the spread over the risk-free interest rate set out in points (b) and (c).

#### **Textual Amendments**

- F2** Inserted by [Directive 2014/51/EU of the European Parliament and of the Council of 16 April 2014 amending Directives 2003/71/EC and 2009/138/EC and Regulations \(EC\) No 1060/2009, \(EU\) No 1094/2010 and \(EU\) No 1095/2010 in respect of the powers of the European Supervisory Authority \(European Insurance and Occupational Pensions Authority\) and the European Supervisory Authority \(European Securities and Markets Authority\).](#)

#### *Article 77d*

#### **Volatility adjustment to the relevant risk-free interest rate term structure**

1 Member States may require prior approval by supervisory authorities for insurance and reinsurance undertakings to apply a volatility adjustment to the relevant risk-free interest rate term structure to calculate the best estimate referred to in Article 77(2).

2 For each relevant currency, the volatility adjustment to the relevant risk-free interest rate term structure shall be based on the spread between the interest rate that could be earned from assets included in a reference portfolio for that currency and the rates of the relevant basic risk-free interest rate term structure for that currency.

The reference portfolio for a currency shall be representative for the assets which are denominated in that currency and which insurance and reinsurance undertakings are invested in to cover the best estimate for insurance and reinsurance obligations denominated in that currency.

3 The amount of the volatility adjustment to risk-free interest rates shall correspond to 65 % of the risk-corrected currency spread.

The risk-corrected currency spread shall be calculated as the difference between the spread referred to in paragraph 2 and the portion of that spread that is attributable to a realistic assessment of expected losses or unexpected credit or other risk of the assets.

The volatility adjustment shall apply only to the relevant risk-free interest rates of the term structure that are not derived by means of extrapolation in accordance with Article 77a. The extrapolation of the relevant risk-free interest rate term structure shall be based on those adjusted risk-free interest rates.

4 For each relevant country, the volatility adjustment to the risk-free interest rates referred to in paragraph 3 for the currency of that country shall, before application of the 65 % factor, be increased by the difference between the risk-corrected country spread and twice the risk-corrected currency spread, whenever that difference is positive and the risk-corrected country spread is higher than 100 basis points. The increased volatility adjustment shall be applied to the calculation of the best estimate for insurance and reinsurance obligations of products sold in the insurance market of that country. The risk-corrected country spread is calculated in the same way as the risk-corrected currency spread for the currency of that country, but based on a reference portfolio that is representative for the assets which insurance and reinsurance undertakings are invested in to cover the best estimate for insurance and reinsurance obligations of products sold in the insurance market of that country and denominated in the currency of that country.

5 The volatility adjustment shall not be applied with respect to insurance obligations where the relevant risk-free interest rate term structure to calculate the best estimate for those obligations includes a matching adjustment under Article 77b.

6 By way of derogation from Article 101, the Solvency Capital Requirement shall not cover the risk of loss of basic own funds resulting from changes of the volatility adjustment.

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#### **Textual Amendments**

- F2** Inserted by [Directive 2014/51/EU of the European Parliament and of the Council of 16 April 2014 amending Directives 2003/71/EC and 2009/138/EC and Regulations \(EC\) No 1060/2009, \(EU\) No 1094/2010 and \(EU\) No 1095/2010 in respect of the powers of the European Supervisory Authority \(European Insurance and Occupational Pensions Authority\) and the European Supervisory Authority \(European Securities and Markets Authority\).](#)

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*Article 77e*

**Technical information produced by the European Insurance and Occupational Pensions Authority**

1 EIOPA shall lay down and publish for each relevant currency the following technical information at least on a quarterly basis:

- a a relevant risk-free interest rate term structure to calculate the best estimate referred to in Article 77(2), without any matching adjustment or volatility adjustment;
- b for each relevant duration, credit quality and asset class a fundamental spread for the calculation of the matching adjustment referred to in Article 77c(1)(b);
- c for each relevant national insurance market a volatility adjustment to the relevant risk-free interest rate term structure referred to in Article 77d(1).

2 In order to ensure uniform conditions for the calculation of technical provisions and basic own funds, the Commission may adopt implementing acts which set out, for each relevant currency, the technical information referred to in paragraph 1. Those implementing acts shall make use of that information.

Those implementing acts shall be adopted in accordance with the advisory procedure referred to in Article 301(2).

On duly justified imperative grounds of urgency relating to the availability of the relevant risk-free interest rate term structure, the Commission shall adopt immediately applicable implementing acts in accordance with the procedure referred to in Article 301(3).

3 Where the technical information referred to in paragraph 1 is adopted by the Commission in accordance with paragraph 2, insurance and reinsurance undertakings shall use that technical information in calculating the best estimate in accordance with Article 77, the matching adjustment in accordance with Article 77c, and the volatility adjustment in accordance with Article 77d.

With respect to currencies and national markets where the adjustment referred to in paragraph 1(c) is not set out in the implementing acts referred to in paragraph 2, no volatility adjustment shall be applied to the relevant risk-free interest rate term structure to calculate the best estimate.

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**Textual Amendments**

- F2** Inserted by [Directive 2014/51/EU of the European Parliament and of the Council of 16 April 2014 amending Directives 2003/71/EC and 2009/138/EC and Regulations \(EC\) No 1060/2009, \(EU\) No 1094/2010 and \(EU\) No 1095/2010 in respect of the powers of the European Supervisory Authority \(European Insurance and Occupational Pensions Authority\) and the European Supervisory Authority \(European Securities and Markets Authority\).](#)



### Article 77f

#### **Review of long-term guarantees measures and measures on equity risk**

1 EIOPA shall, on an annual basis and until 1 January 2021, report to the European Parliament, the Council and the Commission about the impact of the application of Articles 77a to 77e and 106, Article 138(4) and Articles 304, 308c and 308d, including the delegated or implementing acts adopted pursuant thereto.

Supervisory authorities shall, on an annual basis during that period, provide EIOPA with the following information:

- a the availability of long-term guarantees in insurance products in their national markets and the behaviour of insurance and reinsurance undertakings as long-term investors;
- b the number of insurance and reinsurance undertakings applying the matching adjustment, the volatility adjustment, the extension of the recovery period in accordance with Article 138(4), the duration-based equity risk sub-module and the transitional measures set out in Articles 308c and 308d;
- c the impact on the insurance and reinsurance undertakings' financial position of the matching adjustment, the volatility adjustment, the symmetric adjustment mechanism to the equity capital charge, the duration-based equity risk sub-module and the transitional measures set out in Articles 308c and 308d, at national level and in anonymised way for each undertaking;
- d the effect of the matching adjustment, the volatility adjustment, the symmetric adjustment mechanism to the equity capital charge and the duration-based equity risk sub-module on the investment behaviour of insurance and reinsurance undertakings and whether they provide undue capital relief;
- e the effect of any extension of the recovery period in accordance with Article 138(4) on the efforts of insurance and reinsurance undertakings to re-establish the level of eligible own funds covering the Solvency Capital Requirement or to reduce the risk profile in order to ensure compliance with the Solvency Capital Requirement;
- f where insurance and reinsurance undertakings apply the transitional measures set out in Articles 308c and 308d, whether they comply with the phasing-in plans referred to in Article 308e and the prospects for a reduced dependency on these transitional measures, including measures that have been taken or are expected to be taken by the undertakings and supervisory authorities, taking into account the regulatory environment of the Member State concerned.

2 EIOPA, where appropriate after consulting the ESRB and conducting a public consultation, shall submit to the Commission an opinion on the assessment of the application of Articles 77a to 77e and 106, Article 138(4), and Articles 304, 308c and 308d, including the delegated or implementing acts adopted pursuant thereto. That assessment shall be made in relation to the availability of long-term guarantees in insurance products, the behaviour of insurance and reinsurance undertakings as long-term investors and, more generally, financial stability.

3 Based on the opinion submitted by EIOPA, referred to in paragraph 2, the Commission shall submit a report to the European Parliament and to the Council by 1 January 2021, or, where appropriate, earlier. The report shall focus, in particular, on the effects on:

- a policy holder protection;
- b the functioning and stability of European insurance markets;

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- c the internal market and in particular the competition and the level playing field in European insurance markets;
- d the extent to which insurance and reinsurance undertakings continue to operate as long-term investors;
- e the availability and pricing of annuity products;
- f the availability and pricing of competing products;
- g long-term investment strategies by insurance undertakings in relation to products to which Articles 77b and 77c are applied relative to those in relation to other long-term guarantees;
- h consumer choice and consumer awareness of risk;
- i the degree of diversification in the insurance business and asset portfolio of insurance and reinsurance undertakings;
- j financial stability.

In addition, the report shall build on the supervisory experience relating to the application of Articles 77a to 77e and 106, Article 138(4) and Articles 304, 308c and 308d, including the delegated or implementing acts adopted pursuant thereto.

4 The Commission report shall be accompanied, if necessary, by legislative proposals.]

**Textual Amendments**

- F2** Inserted by [Directive 2014/51/EU of the European Parliament and of the Council of 16 April 2014 amending Directives 2003/71/EC and 2009/138/EC and Regulations \(EC\) No 1060/2009, \(EU\) No 1094/2010 and \(EU\) No 1095/2010 in respect of the powers of the European Supervisory Authority \(European Insurance and Occupational Pensions Authority\) and the European Supervisory Authority \(European Securities and Markets Authority\).](#)

*Article 78*

**Other elements to be taken into account in the calculation of technical provisions**

In addition to Article 77, when calculating technical provisions, insurance and reinsurance undertakings shall take account of the following:

- (1) all expenses that will be incurred in servicing insurance and reinsurance obligations;
- (2) inflation, including expenses and claims inflation;
- (3) all payments to policy holders and beneficiaries, including future discretionary bonuses, which insurance and reinsurance undertakings expect to make, whether or not those payments are contractually guaranteed, unless those payments fall under Article 91(2).

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#### *Article 79*

### **Valuation of financial guarantees and contractual options included in insurance and reinsurance contracts**

When calculating technical provisions, insurance and reinsurance undertakings shall take account of the value of financial guarantees and any contractual options included in insurance and reinsurance policies.

Any assumptions made by insurance and reinsurance undertakings with respect to the likelihood that policy holders will exercise contractual options, including lapses and surrenders, shall be realistic and based on current and credible information. The assumptions shall take account, either explicitly or implicitly, of the impact that future changes in financial and non-financial conditions may have on the exercise of those options.

#### *Article 80*

### **Segmentation**

Insurance and reinsurance undertakings shall segment their insurance and reinsurance obligations into homogeneous risk groups, and as a minimum by lines of business, when calculating their technical provisions.

#### *Article 81*

### **Recoverables from reinsurance contracts and special purpose vehicles**

The calculation by insurance and reinsurance undertakings of amounts recoverable from reinsurance contracts and special purpose vehicles shall comply with Articles 76 to 80.

When calculating amounts recoverable from reinsurance contracts and special purpose vehicles, insurance and reinsurance undertakings shall take account of the time difference between recoveries and direct payments.

The result from that calculation shall be adjusted to take account of expected losses due to default of the counterparty. That adjustment shall be based on an assessment of the probability of default of the counterparty and the average loss resulting therefrom (loss-given-default).

#### *Article 82*

### **Data quality and application of approximations, including case-by-case approaches, for technical provisions**

Member States shall ensure that insurance and reinsurance undertakings have internal processes and procedures in place to ensure the appropriateness, completeness and accuracy of the data used in the calculation of their technical provisions.

Where, in specific circumstances, insurance and reinsurance undertakings have insufficient data of appropriate quality to apply a reliable actuarial method to a

set or subset of their insurance and reinsurance obligations, or amounts recoverable from reinsurance contracts and special purpose vehicles, appropriate approximations, including case-by-case approaches, may be used in the calculation of the best estimate.

#### *Article 83*

### **Comparison against experience**

Insurance and reinsurance undertakings shall have processes and procedures in place to ensure that best estimates, and the assumptions underlying the calculation of best estimates, are regularly compared against experience.

Where the comparison identifies systematic deviation between experience and the best estimate calculations of insurance or reinsurance undertakings, the undertaking concerned shall make appropriate adjustments to the actuarial methods being used and/or the assumptions being made.

#### *Article 84*

### **Appropriateness of the level of technical provisions**

Upon request from the supervisory authorities, insurance and reinsurance undertakings shall demonstrate the appropriateness of the level of their technical provisions, as well as the applicability and relevance of the methods applied, and the adequacy of the underlying statistical data used.

#### *Article 85*

### **Increase of technical provisions**

To the extent that the calculation of technical provisions of insurance and reinsurance undertakings does not comply with Articles 76 to 83, the supervisory authorities may require insurance and reinsurance undertakings to increase the amount of technical provisions so that they correspond to the level determined pursuant to those Articles.

#### *[<sup>F1</sup>Article 86*

### **Delegated acts and regulatory and implementing technical standards**

1 The Commission shall adopt delegated acts in accordance with Article 301a laying down the following:

- a actuarial and statistical methodologies to calculate the best estimate referred to in Article 77(2);
- b the methodologies, principles and techniques for the determination of the relevant risk-free interest rate term structure to be used to calculate the best estimate referred to in Article 77(2);
- c the circumstances in which technical provisions shall be calculated as a whole, or as a sum of a best estimate and a risk margin, and the methods to be used in the case where technical provisions are calculated as a whole, as referred to in Article 77(4);

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- d the methods and assumptions to be used in the calculation of the risk margin including the determination of the amount of eligible own funds necessary to support the insurance and reinsurance obligations and the calibration of the cost-of-capital rate, as referred to in Article 77(5);
- e the lines of business on the basis of which insurance and reinsurance obligations are to be segmented in order to calculate technical provisions referred to in Article 80;
- f the standards to be met with respect to ensuring the appropriateness, completeness and accuracy of the data used in the calculation of technical provisions, and the specific circumstances in which it would be appropriate to use approximations, including case-by-case approaches, to calculate the best estimate, as referred to in Article 82;
- g specifications with respect to the requirements set out in Article 77b(1) including the methods, assumptions and standard parameters to be used when calculating the impact of the mortality risk stress referred to in Article 77b(1)(e);
- h specifications with respect to the requirements set out in Article 77c including assumptions and methods to apply in the calculation of the matching adjustment and the fundamental spread;
- i methods and assumptions for the calculation of the volatility adjustment referred to in Article 77d including a formula for the calculation of the spread referred to in paragraph 2 of that Article.

2 In order to ensure consistent harmonisation in relation to the methods for the calculation of technical provisions, EIOPA shall, subject to Article 301b, develop draft regulatory technical standards to specify:

- a the methodologies to be used when calculating the counterparty default adjustment referred to in Article 81 designed to capture expected losses due to default of the counterparty;
- b where necessary, simplified methods and techniques to calculate technical provisions, in order to ensure the actuarial and statistical methods referred to in points (a) and (d) are proportionate to the nature, scale and complexity of the risks supported by insurance and reinsurance undertakings including captive insurance and reinsurance undertakings.

Power is delegated to the Commission to adopt the regulatory technical standards referred to in the first subparagraph in accordance with Articles 10 to 14 of Regulation (EU) No 1094/2010.

3 In order to ensure consistent conditions of application of Article 77b, EIOPA shall develop draft implementing technical standards on the procedures for the approval of the application of a matching adjustment referred to in Article 77b(1).

EIOPA shall submit those draft implementing technical standards to the Commission by 31 October 2014.

Power is conferred on the Commission to adopt those implementing technical standards in accordance with Article 15 of Regulation (EU) No 1094/2010.]

#### **Textual Amendments**

- F1** Substituted by [Directive 2014/51/EU of the European Parliament and of the Council of 16 April 2014 amending Directives 2003/71/EC and 2009/138/EC and Regulations \(EC\) No 1060/2009, \(EU\) No 1094/2010 and \(EU\) No 1095/2010 in respect of the powers of the European Supervisory Authority \(European Insurance and Occupational Pensions Authority\) and the European Supervisory Authority \(European Securities and Markets Authority\).](#)

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### Section 3

#### **Own funds**

##### Subsection 1

#### **Determination of own funds**

##### *Article 87*

#### **Own funds**

Own funds shall comprise the sum of basic own funds, referred to in Article 88 and ancillary own funds referred to in Article 89.

##### *Article 88*

#### **Basic own funds**

Basic own funds shall consist of the following items:

- (1) the excess of assets over liabilities, valued in accordance with Article 75 and Section 2;
- (2) subordinated liabilities.

The excess amount referred to in point (1) shall be reduced by the amount of own shares held by the insurance or reinsurance undertaking.

##### *Article 89*

#### **Ancillary own funds**

1 Ancillary own funds shall consist of items other than basic own funds which can be called up to absorb losses.

Ancillary own funds may comprise the following items to the extent that they are not basic own-fund items:

- a unpaid share capital or initial fund that has not been called up;
- b letters of credit and guarantees;
- c any other legally binding commitments received by insurance and reinsurance undertakings.

In the case of a mutual or mutual-type association with variable contributions, ancillary own funds may also comprise any future claims which that association may have against its members by way of a call for supplementary contribution, within the following 12 months.

2 Where an ancillary own-fund item has been paid in or called up, it shall be treated as an asset and cease to form part of ancillary own-fund items.

## Article 90

### Supervisory approval of ancillary own funds

- 1 The amounts of ancillary own-fund items to be taken into account when determining own funds shall be subject to prior supervisory approval.
- 2 The amount ascribed to each ancillary own-fund item shall reflect the loss-absorbency of the item and shall be based upon prudent and realistic assumptions. Where an ancillary own-fund item has a fixed nominal value, the amount of that item shall be equal to its nominal value, where it appropriately reflects its loss-absorbency.
- 3 Supervisory authorities shall approve either of the following:
  - a a monetary amount for each ancillary own-fund item;
  - b a method by which to determine the amount of each ancillary own-fund item, in which case supervisory approval of the amount determined in accordance with that method shall be granted for a specified period of time.
- 4 For each ancillary own-fund item, supervisory authorities shall base their approval on an assessment of the following:
  - a the status of the counterparties concerned, in relation to their ability and willingness to pay;
  - b the recoverability of the funds, taking account of the legal form of the item, as well as any conditions which would prevent the item from being successfully paid in or called up;
  - c any information on the outcome of past calls which insurance and reinsurance undertakings have made for such ancillary own funds, to the extent that information can be reliably used to assess the expected outcome of future calls.

## Article 91

### Surplus funds

- 1 Surplus funds shall be deemed to be accumulated profits which have not been made available for distribution to policy holders and beneficiaries.
- 2 In so far as authorised under national law, surplus funds shall not be considered as insurance and reinsurance liabilities to the extent that they fulfil the criteria set out in Article 94(1).

## Article 92

### [<sup>F1</sup>Delegated acts and regulatory and implementing technical standards]

[<sup>F1</sup>1 In order to ensure consistent harmonisation in relation to the determination of own funds, EIOPA shall, subject to Article 301b, develop draft regulatory technical standards to specify the criteria for granting supervisory approval of ancillary own funds in accordance with Article 90.

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Power is delegated to the Commission to adopt the regulatory technical standards referred to in the first subparagraph in accordance with Articles 10 to 14 of Regulation (EU) No 1094/2010.

1a The Commission shall adopt delegated acts in accordance with Article 301a specifying the treatment of participations, within the meaning of the third subparagraph of Article 212(2), in financial and credit institutions with respect to the determination of own funds.]

2 Participations in financial and credit institutions as referred to in paragraph 1(b) shall comprise the following:

- a participations which insurance and reinsurance undertakings hold in:
  - (i) credit institutions and financial institutions within the meaning of Article 4(1) and (5) of Directive 2006/48/EC,
  - (ii) investment firms within the meaning of point 1 of Article 4(1) of Directive 2004/39/EC;
- b subordinated claims and instruments referred to in Article 63 and Article 64(3) of Directive 2006/48/EC which insurance and reinsurance undertakings hold in respect of the entities defined in point (a) of this paragraph in which they hold a participation.

[<sup>F23</sup> In order to ensure uniform conditions of application of Article 90, EIOPA shall develop draft implementing technical standards on the procedures for granting supervisory approval for the use of ancillary own funds.

EIOPA shall submit those draft implementing technical standards to the Commission by 31 October 2014.

Power is conferred on the Commission to adopt the implementing technical standards referred to in the first subparagraph in accordance with Article 15 of Regulation (EU) No 1094/2010.]

#### Textual Amendments

- F1** Substituted by [Directive 2014/51/EU of the European Parliament and of the Council of 16 April 2014 amending Directives 2003/71/EC and 2009/138/EC and Regulations \(EC\) No 1060/2009, \(EU\) No 1094/2010 and \(EU\) No 1095/2010 in respect of the powers of the European Supervisory Authority \(European Insurance and Occupational Pensions Authority\) and the European Supervisory Authority \(European Securities and Markets Authority\).](#)
- F2** Inserted by [Directive 2014/51/EU of the European Parliament and of the Council of 16 April 2014 amending Directives 2003/71/EC and 2009/138/EC and Regulations \(EC\) No 1060/2009, \(EU\) No 1094/2010 and \(EU\) No 1095/2010 in respect of the powers of the European Supervisory Authority \(European Insurance and Occupational Pensions Authority\) and the European Supervisory Authority \(European Securities and Markets Authority\).](#)



## Subsection 2

### **Classification of own funds**

#### *Article 93*

#### **Characteristics and features used to classify own funds into tiers**

1 Own-fund items shall be classified into three tiers. The classification of those items shall depend upon whether they are basic own fund or ancillary own-fund items and the extent to which they possess the following characteristics:

- a the item is available, or can be called up on demand, to fully absorb losses on a going-concern basis, as well as in the case of winding-up (permanent availability);
- b in the case of winding-up, the total amount of the item is available to absorb losses and the repayment of the item is refused to its holder until all other obligations, including insurance and reinsurance obligations towards policy holders and beneficiaries of insurance and reinsurance contracts, have been met (subordination).

2 When assessing the extent to which own-fund items possess the characteristics set out in points (a) and (b) of paragraph 1, currently and in the future, due consideration shall be given to the duration of the item, in particular whether the item is dated or not. Where an own-fund item is dated, the relative duration of the item as compared to the duration of the insurance and reinsurance obligations of the undertaking shall be considered (sufficient duration).

In addition, the following features shall be considered:

- a whether the item is free from requirements or incentives to redeem the nominal sum (absence of incentives to redeem);
- b whether the item is free from mandatory fixed charges (absence of mandatory servicing costs);
- c whether the item is clear of encumbrances (absence of encumbrances).

#### *Article 94*

#### **Main criteria for the classification into tiers**

1 Basic own-fund items shall be classified in Tier 1 where they substantially possess the characteristics set out in Article 93(1)(a) and (b), taking into consideration the features set out in Article 93(2).

2 Basic own-fund items shall be classified in Tier 2 where they substantially possess the characteristic set out in Article 93(1)(b), taking into consideration the features set out in Article 93(2).

Ancillary own-fund items shall be classified in Tier 2 where they substantially possess the characteristics set out in Article 93(1)(a) and (b), taking into consideration the features set out in Article 93(2).

3 Any basic and ancillary own-fund items which do not fall under paragraphs 1 and 2 shall be classified in Tier 3.

### Article 95

#### **Classification of own funds into tiers**

Member States shall ensure that insurance and reinsurance undertakings classify their own-fund items on the basis of the criteria laid down in Article 94.

For that purpose, insurance and reinsurance undertakings shall refer to the list of own-fund items referred to in Article 97(1)(a), where applicable.

Where an own-fund item is not covered by that list, it shall be assessed and classified by insurance and reinsurance undertakings, in accordance with the first paragraph. That classification shall be subject to approval by the supervisory authority.

### Article 96

#### **Classification of specific insurance own-fund items**

Without prejudice to Article 95 and Article 97(1)(a) for the purposes of this Directive the following classifications shall be applied:

- (1) surplus funds falling under Article 91(2) shall be classified in Tier 1;
- (2) letters of credit and guarantees which are held in trust for the benefit of insurance creditors by an independent trustee and provided by credit institutions authorised in accordance with Directive 2006/48/EC shall be classified in Tier 2;
- (3) any future claims which mutual or mutual-type associations of shipowners with variable contributions solely insuring risks listed in classes 6, 12 and 17 in Part A of Annex I may have against their members by way of a call for supplementary contributions, within the following 12 months, shall be classified in Tier 2.

In accordance with the second subparagraph of Article 94(2), any future claims which mutual or mutual-type associations with variable contributions may have against their members by way of a call for supplementary contributions, within the following 12 months, not falling under point (3) of the first subparagraph shall be classified in Tier 2 where they substantially possess the characteristics set out in Article 93(1)(a) and (b), taking into consideration the features set out in Article 93(2).

### *[<sup>F1</sup>Article 97*

#### **Delegated acts and regulatory technical standards**

1 The Commission shall adopt delegated acts in accordance with Article 301a laying down a list of own-fund items, including those referred to in Article 96, deemed to fulfil the criteria, set out in Article 94, which contains for each own-fund item a precise description of the features which determined its classification.

2 In order to ensure consistent harmonisation in relation to classification of own funds, EIOPA shall, subject to Article 301b, develop draft regulatory technical standards to specify the methods to be used by supervisory authorities, when approving the assessment and classification of own-fund items which are not covered by the list referred to in paragraph 1.

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Power is delegated to the Commission to adopt the regulatory technical standards referred to in the first subparagraph in accordance with Articles 10 to 14 of Regulation (EU) No 1094/2010.

The Commission shall regularly review and, where appropriate, update the list referred to in paragraph 1 in light of market developments.]

#### **Textual Amendments**

- F1** Substituted by Directive 2014/51/EU of the European Parliament and of the Council of 16 April 2014 amending Directives 2003/71/EC and 2009/138/EC and Regulations (EC) No 1060/2009, (EU) No 1094/2010 and (EU) No 1095/2010 in respect of the powers of the European Supervisory Authority (European Insurance and Occupational Pensions Authority) and the European Supervisory Authority (European Securities and Markets Authority).

### Subsection 3

#### **Eligibility of own funds**

##### *Article 98*

#### **Eligibility and limits applicable to Tiers 1, 2 and 3**

1 As far as the compliance with the Solvency Capital Requirement is concerned, the eligible amounts of Tier 2 and Tier 3 items shall be subject to quantitative limits. Those limits shall be such as to ensure that at least the following conditions are met:

- a the proportion of Tier 1 items in the eligible own funds is higher than one third of the total amount of eligible own funds;
- b the eligible amount of Tier 3 items is less than one third of the total amount of eligible own funds.

2 As far as compliance with the Minimum Capital Requirement is concerned, the amount of basic own-fund items eligible to cover the Minimum Capital Requirement which are classified in Tier 2 shall be subject to quantitative limits. Those limits shall be such as to ensure, as a minimum, that the proportion of Tier 1 items in the eligible basic own funds is higher than one half of the total amount of eligible basic own funds.

3 The eligible amount of own funds to cover the Solvency Capital Requirement set out in Article 100 shall be equal to the sum of the amount of Tier 1, the eligible amount of Tier 2 and the eligible amount of Tier 3.

4 The eligible amount of basic own funds to cover the Minimum Capital Requirement set out in Article 128 shall be equal to the sum of the amount of Tier 1 and the eligible amount of basic own-fund items classified in Tier 2.

##### *[<sup>F1</sup> Article 99*

#### **Delegated acts on the eligibility of own funds**

The Commission shall adopt delegated acts in accordance with Article 301a laying down:

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- (a) the quantitative limits referred to in Article 98(1) and (2);
- (b) the adjustments that should be made to reflect the lack of transferability of those own-fund items that can be used only to cover losses arising from a particular segment of liabilities or from particular risks (ring-fenced funds).]

#### **Textual Amendments**

**F1** Substituted by Directive 2014/51/EU of the European Parliament and of the Council of 16 April 2014 amending Directives 2003/71/EC and 2009/138/EC and Regulations (EC) No 1060/2009, (EU) No 1094/2010 and (EU) No 1095/2010 in respect of the powers of the European Supervisory Authority (European Insurance and Occupational Pensions Authority) and the European Supervisory Authority (European Securities and Markets Authority).

### Section 4

#### **Solvency capital requirement**

##### Subsection 1

#### **General provisions for the solvency capital requirement using the standard formula or an internal model**

##### *Article 100*

#### **General provisions**

Member States shall require that insurance and reinsurance undertakings hold eligible own funds covering the Solvency Capital Requirement.

The Solvency Capital Requirement shall be calculated, either in accordance with the standard formula in Subsection 2 or using an internal model, as set out in Subsection 3.

##### *Article 101*

#### **Calculation of the Solvency Capital Requirement**

1 The Solvency Capital Requirement shall be calculated in accordance with paragraphs 2 to 5.

2 The Solvency Capital Requirement shall be calculated on the presumption that the undertaking will pursue its business as a going concern.

3 The Solvency Capital Requirement shall be calibrated so as to ensure that all quantifiable risks to which an insurance or reinsurance undertaking is exposed are taken into account. It shall cover existing business, as well as the new business expected to be written over the following 12 months. With respect to existing business, it shall cover only unexpected losses.

It shall correspond to the Value-at-Risk of the basic own funds of an insurance or reinsurance undertaking subject to a confidence level of 99,5 % over a one-year period.

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4 The Solvency Capital Requirement shall cover at least the following risks:

- a non-life underwriting risk;
- b life underwriting risk;
- c health underwriting risk;
- d market risk;
- e credit risk;
- f operational risk.

Operational risk as referred to in point (f) of the first subparagraph shall include legal risks, and exclude risks arising from strategic decisions, as well as reputation risks.

5 When calculating the Solvency Capital Requirement, insurance and reinsurance undertakings shall take account of the effect of risk-mitigation techniques, provided that credit risk and other risks arising from the use of such techniques are properly reflected in the Solvency Capital Requirement.

#### *Article 102*

### **Frequency of calculation**

1 Insurance and reinsurance undertakings shall calculate the Solvency Capital Requirement at least once a year and report the result of that calculation to the supervisory authorities.

Insurance and reinsurance undertakings shall hold eligible own funds which cover the last reported Solvency Capital Requirement.

Insurance and reinsurance undertakings shall monitor the amount of eligible own funds and the Solvency Capital Requirement on an ongoing basis.

If the risk profile of an insurance or reinsurance undertaking deviates significantly from the assumptions underlying the last reported Solvency Capital Requirement, the undertaking concerned shall recalculate the Solvency Capital Requirement without delay and report it to the supervisory authorities.

2 Where there is evidence to suggest that the risk profile of the insurance or reinsurance undertaking has altered significantly since the date on which the Solvency Capital Requirement was last reported, the supervisory authorities may require the undertaking concerned to recalculate the Solvency Capital Requirement.

#### Subsection 2

### **Solvency capital requirement standard formula**

#### *Article 103*

### **Structure of the standard formula**

The Solvency Capital Requirement calculated on the basis of the standard formula shall be the sum of the following items:

- (a) the Basic Solvency Capital Requirement, as laid down in Article 104;

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- (b) the capital requirement for operational risk, as laid down in Article 107;
- (c) the adjustment for the loss-absorbing capacity of technical provisions and deferred taxes, as laid down in Article 108.

#### *Article 104*

### **Design of the Basic Solvency Capital Requirement**

1 The Basic Solvency Capital Requirement shall comprise individual risk modules, which are aggregated in accordance with point (1) of Annex IV.

It shall consist of at least the following risk modules:

- a non-life underwriting risk;
- b life underwriting risk;
- c health underwriting risk;
- d market risk;
- e counterparty default risk.

2 For the purposes of points (a), (b) and (c) of paragraph 1, insurance or reinsurance operations shall be allocated to the underwriting risk module that best reflects the technical nature of the underlying risks.

3 The correlation coefficients for the aggregation of the risk modules referred to in paragraph 1, as well as the calibration of the capital requirements for each risk module, shall result in an overall Solvency Capital Requirement which complies with the principles set out in Article 101.

4 Each of the risk modules referred to in paragraph 1 shall be calibrated using a Value-at-Risk measure, with a 99,5 % confidence level, over a one-year period.

Where appropriate, diversification effects shall be taken into account in the design of each risk module.

5 The same design and specifications for the risk modules shall be used for all insurance and reinsurance undertakings, both with respect to the Basic Solvency Capital Requirement and to any simplified calculations as laid down in Article 109.

6 With regard to risks arising from catastrophes, geographical specifications may, where appropriate, be used for the calculation of the life, non-life and health underwriting risk modules.

7 Subject to approval by the supervisory authorities, insurance and reinsurance undertakings may, within the design of the standard formula, replace a subset of its parameters by parameters specific to the undertaking concerned when calculating the life, non-life and health underwriting risk modules.

Such parameters shall be calibrated on the basis of the internal data of the undertaking concerned, or of data which is directly relevant for the operations of that undertaking using standardised methods.

When granting supervisory approval, supervisory authorities shall verify the completeness, accuracy and appropriateness of the data used.

## Article 105

### Calculation of the Basic Solvency Capital Requirement

1 The Basic Solvency Capital Requirement shall be calculated in accordance with paragraphs 2 to 6.

2 The non-life underwriting risk module shall reflect the risk arising from non-life insurance obligations, in relation to the perils covered and the processes used in the conduct of business.

It shall take account of the uncertainty in the results of insurance and reinsurance undertakings related to the existing insurance and reinsurance obligations as well as to the new business expected to be written over the following 12 months.

It shall be calculated, in accordance with point (2) of Annex IV, as a combination of the capital requirements for at least the following sub-modules:

- a the risk of loss, or of adverse change in the value of insurance liabilities, resulting from fluctuations in the timing, frequency and severity of insured events, and in the timing and amount of claim settlements (non-life premium and reserve risk);
- b the risk of loss, or of adverse change in the value of insurance liabilities, resulting from significant uncertainty of pricing and provisioning assumptions related to extreme or exceptional events (non-life catastrophe risk).

3 The life underwriting risk module shall reflect the risk arising from life insurance obligations, in relation to the perils covered and the processes used in the conduct of business.

It shall be calculated, in accordance with point (3) of Annex IV, as a combination of the capital requirements for at least the following sub-modules:

- a the risk of loss, or of adverse change in the value of insurance liabilities, resulting from changes in the level, trend, or volatility of mortality rates, where an increase in the mortality rate leads to an increase in the value of insurance liabilities (mortality risk);
- b the risk of loss, or of adverse change in the value of insurance liabilities, resulting from changes in the level, trend, or volatility of mortality rates, where a decrease in the mortality rate leads to an increase in the value of insurance liabilities (longevity risk);
- c the risk of loss, or of adverse change in the value of insurance liabilities, resulting from changes in the level, trend or volatility of disability, sickness and morbidity rates (disability – morbidity risk);
- d the risk of loss, or of adverse change in the value of insurance liabilities, resulting from changes in the level, trend, or volatility of the expenses incurred in servicing insurance or reinsurance contracts (life-expense risk);
- e the risk of loss, or of adverse change in the value of insurance liabilities, resulting from fluctuations in the level, trend, or volatility of the revision rates applied to annuities, due to changes in the legal environment or in the state of health of the person insured (revision risk);
- f the risk of loss, or of adverse change in the value of insurance liabilities, resulting from changes in the level or volatility of the rates of policy lapses, terminations, renewals and surrenders (lapse risk);
- g the risk of loss, or of adverse change in the value of insurance liabilities, resulting from the significant uncertainty of pricing and provisioning assumptions related to extreme or irregular events (life-catastrophe risk).

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4 The health underwriting risk module shall reflect the risk arising from the underwriting of health insurance obligations, whether it is pursued on a similar technical basis to that of life insurance or not, following from both the perils covered and the processes used in the conduct of business.

It shall cover at least the following risks:

- a the risk of loss, or of adverse change in the value of insurance liabilities, resulting from changes in the level, trend, or volatility of the expenses incurred in servicing insurance or reinsurance contracts;
- b the risk of loss, or of adverse change in the value of insurance liabilities, resulting from fluctuations in the timing, frequency and severity of insured events, and in the timing and amount of claim settlements at the time of provisioning;
- c the risk of loss, or of adverse change in the value of insurance liabilities, resulting from the significant uncertainty of pricing and provisioning assumptions related to outbreaks of major epidemics, as well as the unusual accumulation of risks under such extreme circumstances.

5 The market risk module shall reflect the risk arising from the level or volatility of market prices of financial instruments which have an impact upon the value of the assets and liabilities of the undertaking. It shall properly reflect the structural mismatch between assets and liabilities, in particular with respect to the duration thereof.

It shall be calculated, in accordance with point (4) of Annex IV, as a combination of the capital requirements for at least the following sub-modules:

- a the sensitivity of the values of assets, liabilities and financial instruments to changes in the term structure of interest rates, or in the volatility of interest rates (interest rate risk);
- b the sensitivity of the values of assets, liabilities and financial instruments to changes in the level or in the volatility of market prices of equities (equity risk);
- c the sensitivity of the values of assets, liabilities and financial instruments to changes in the level or in the volatility of market prices of real estate (property risk);
- d the sensitivity of the values of assets, liabilities and financial instruments to changes in the level or in the volatility of credit spreads over the risk-free interest rate term structure (spread risk);
- e the sensitivity of the values of assets, liabilities and financial instruments to changes in the level or in the volatility of currency exchange rates (currency risk);
- f additional risks to an insurance or reinsurance undertaking stemming either from lack of diversification in the asset portfolio or from large exposure to default risk by a single issuer of securities or a group of related issuers (market risk concentrations).

6 The counterparty default risk module shall reflect possible losses due to unexpected default, or deterioration in the credit standing, of the counterparties and debtors of insurance and reinsurance undertakings over the following 12 months. The counterparty default risk module shall cover risk-mitigating contracts, such as reinsurance arrangements, securitisations and derivatives, and receivables from intermediaries, as well as any other credit exposures which are not covered in the spread risk sub-module. It shall take appropriate account of collateral or other security held by or for the account of the insurance or reinsurance undertaking and the risks associated therewith.

For each counterparty, the counterparty default risk module shall take account of the overall counterparty risk exposure of the insurance or reinsurance undertaking concerned to that counterparty, irrespective of the legal form of its contractual obligations to that undertaking.



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### *Article 106*

#### **Calculation of the equity risk sub-module: symmetric adjustment mechanism**

1 The equity risk sub-module calculated in accordance with the standard formula shall include a symmetric adjustment to the equity capital charge applied to cover the risk arising from changes in the level of equity prices.

2 The symmetric adjustment made to the standard equity capital charge, calibrated in accordance with Article 104(4), covering the risk arising from changes in the level of equity prices shall be based on a function of the current level of an appropriate equity index and a weighted average level of that index. The weighted average shall be calculated over an appropriate period of time which shall be the same for all insurance and reinsurance undertakings.

3 The symmetric adjustment made to the standard equity capital charge covering the risk arising from changes in the level of equity prices shall not result in an equity capital charge being applied that is more than 10 percentage points lower or 10 percentage points higher than the standard equity capital charge.

### *Article 107*

#### **Capital requirement for operational risk**

1 The capital requirement for operational risk shall reflect operational risks to the extent they are not already reflected in the risk modules referred to in Article 104. That requirement shall be calibrated in accordance with Article 101(3).

2 With respect to life insurance contracts where the investment risk is borne by the policy holders, the calculation of the capital requirement for operational risk shall take account of the amount of annual expenses incurred in respect of those insurance obligations.

3 With respect to insurance and reinsurance operations other than those referred to in paragraph 2, the calculation of the capital requirement for operational risk shall take account of the volume of those operations, in terms of earned premiums and technical provisions which are held in respect of those insurance and reinsurance obligations. In this case, the capital requirement for operational risks shall not exceed 30 % of the Basic Solvency Capital Requirement relating to those insurance and reinsurance operations.

### *Article 108*

#### **Adjustment for the loss-absorbing capacity of technical provisions and deferred taxes**

The adjustment referred to in Article 103(c) for the loss-absorbing capacity of technical provisions and deferred taxes shall reflect potential compensation of unexpected losses through a simultaneous decrease in technical provisions or deferred taxes or a combination of the two.

That adjustment shall take account of the risk mitigating effect provided by future discretionary benefits of insurance contracts, to the extent insurance and reinsurance undertakings can establish that a reduction in such benefits may be used to cover unexpected losses when they arise. The risk mitigating effect provided by future

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discretionary benefits shall be no higher than the sum of technical provisions and deferred taxes relating to those future discretionary benefits.

For the purpose of the second paragraph, the value of future discretionary benefits under adverse circumstances shall be compared to the value of such benefits under the underlying assumptions of the best-estimate calculation.

#### *Article 109*

### **Simplifications in the standard formula**

Insurance and reinsurance undertakings may use a simplified calculation for a specific sub-module or risk module where the nature, scale and complexity of the risks they face justifies it and where it would be disproportionate to require all insurance and reinsurance undertakings to apply the standardised calculation.

Simplified calculations shall be calibrated in accordance with Article 101(3).

#### *[<sup>F2</sup> Article 109a*

### **Harmonised technical inputs to standard formula**

1 For the purposes of the calculation of the Solvency Capital Requirement in accordance with the standard formula, the ESAs through the Joint Committee shall develop draft implementing technical standards on the allocation of credit assessments of external credit assessment institutions (ECAIs) to an objective scale of credit quality steps applying the steps specified in accordance with Article 111(1)(n).

The ESAs' Joint Committee shall submit those draft implementing technical standards to the Commission by 30 June 2015.

Power is conferred on the Commission to adopt the implementing technical standards referred to in the first subparagraph in accordance with Article 15 of Regulation (EU) No 1094/2010.

2 In order to ensure uniform conditions of application of this Article and for the purposes of facilitating the calculation of the market risk module referred to in Article 105(5), facilitating the calculation of the counterparty default risk module referred to in Article 105(6), evaluating risk mitigation techniques referred to in Article 101(5), and calculating technical provisions, EIOPA shall develop draft implementing technical standards on:

- a lists of regional governments and local authorities, exposures to whom are to be treated as exposures to the central government of the jurisdiction in which they are established, provided that there is no difference in risk between such exposures because of the specific revenue-raising powers of the former, and specific institutional arrangements exist, the effect of which is to reduce the risk of default;
- b the equity index referred to in Article 106(2), in accordance with the detailed criteria established under Article 111(1)(c) and (o);
- c the adjustments to be made for currencies pegged to the euro in the currency risk sub-module referred to in Article 105(5), in accordance with the detailed criteria for the adjustments for currencies pegged to the euro for the purpose of facilitating the calculation of the currency risk sub-module, as established under Article 111(1)(p).

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EIOPA shall submit those draft implementing technical standards to the Commission by 30 June 2015.

Power is conferred on the Commission to adopt the implementing technical standards referred to in the first subparagraph in accordance with Article 15 of Regulation (EU) No 1094/2010.

3 EIOPA shall publish technical information including information concerning the symmetric adjustment referred to in Article 106 on at least a quarterly basis.

4 In order to ensure uniform conditions of application of this Article and for the purpose of facilitating the calculation of the health underwriting risk module referred to in Article 105(4), EIOPA shall develop draft implementing technical standards, taking into account the calculations provided by the supervisory authorities of the Member States concerned, on standard deviations in relation to specific national legislative measures of Member States which permit the sharing of claims payments in respect of health risk amongst insurance and reinsurance undertakings and which meet the criteria in paragraph 5 and any additional criteria established by delegated acts.

EIOPA shall submit those draft implementing technical standards to the Commission by 30 June 2015.

Power is conferred on the Commission to adopt the implementing technical standards referred to in the first subparagraph in accordance with Article 15 of Regulation (EU) No 1094/2010.

5 The implementing technical standards referred to in paragraph 4 shall apply only to the national legislative measures of Member States which permit the sharing of claims payments in respect of health risk amongst insurance and reinsurance undertakings and which meet the following criteria:

- a the mechanism for the sharing of claims is transparent and fully specified in advance of the annual period to which it applies;
- b the mechanism for the sharing of claims, the number of insurance undertakings that participate in the health risk equalisation system (HRES) and the risk characteristics of the business subject to the HRES ensure that for each undertaking participating in the HRES the volatility of annual losses of the business subject to the HRES is significantly reduced by means of the HRES, both in relation to premium and to reserve risk;
- c health insurance subject to the HRES is compulsory and serves as a partial or complete alternative to health cover provided by the statutory social security system;
- d in the event of default of insurance undertakings participating in the HRES, one or more Member States' governments guarantee to meet the policy holder claims of the insurance business that is subject to the HRES in full.

The Commission shall adopt delegated acts in accordance with Article 301a which set out the additional criteria that the national legislative measures arrangements shall meet, and the methodology and the requirements for the calculation of the standard deviations referred to in paragraph 4 of this Article.]

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#### **Textual Amendments**

- F2** Inserted by [Directive 2014/51/EU of the European Parliament and of the Council of 16 April 2014 amending Directives 2003/71/EC and 2009/138/EC and Regulations \(EC\) No 1060/2009, \(EU\) No 1094/2010 and \(EU\) No 1095/2010 in respect of the powers of the European Supervisory Authority](#)

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(European Insurance and Occupational Pensions Authority) and the European Supervisory Authority (European Securities and Markets Authority).

### *Article 110*

#### **Significant deviations from the assumptions underlying the standard formula calculation**

Where it is inappropriate to calculate the Solvency Capital Requirement in accordance with the standard formula, as set out in Subsection 2, because the risk profile of the insurance or reinsurance undertaking concerned deviates significantly from the assumptions underlying the standard formula calculation, the supervisory authorities may, by means of a decision stating the reasons, require the undertaking concerned to replace a subset of the parameters used in the standard formula calculation by parameters specific to that undertaking when calculating the life, non-life and health underwriting risk modules, as set out in Article 104(7). Those specific parameters shall be calculated in such a way to ensure that the undertaking complies with Article 101(3).

### *f<sup>1</sup> Article 111*

#### **Delegated acts and regulatory and implementing technical standards concerning Articles 103 to 109**

1 The Commission shall adopt delegated acts in accordance with Article 301a providing for the following:

- a a standard formula in accordance with Articles 101 and 103 to 109;
- b any sub-modules necessary or covering more precisely the risks which fall under the respective risk modules referred to in Article 104 as well as any subsequent updates;
- c the methods, assumptions and standard parameters to be calibrated to the confidence level referred to in Article 101(3) and to be used when calculating each of the risk modules or sub-modules of the basic Solvency Capital Requirement laid down in Articles 104, 105 and 304, the symmetric adjustment mechanism and the appropriate period of time, expressed in the number of months, as referred to in Article 106, and the appropriate approach for integrating the method referred to in Article 304 in the Solvency Capital Requirement as calculated in accordance with the standard formula;
- d the correlation parameters, including, where necessary, those set out in Annex IV, and the procedures for updating those parameters;
- e where insurance and reinsurance undertakings use risk-mitigation techniques, the methods and assumptions to be used to assess the changes in the risk profile of the undertaking concerned and to adjust the calculation of the Solvency Capital Requirement;
- f the qualitative criteria that the risk-mitigation techniques referred to in point (e) must fulfil in order to ensure that the risk has been effectively transferred to a third party;
- fa the method and parameters to be used when assessing the capital requirement for counterparty default risk in the case of exposures to qualifying central counterparties, those parameters ensuring consistency with the treatment of such exposures in the case of credit institutions and financial institutions within the meaning of Article 4(1)(1) and (26) of Regulation (EU) No 575/2013;

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- g the methods and parameters to be used when assessing the capital requirement for operational risk set out in Article 107, including the percentage referred to in Article 107(3);
- h the methods and adjustments to be used to reflect the reduced scope for risk diversification of insurance and reinsurance undertakings relating to ring-fenced funds;
- i the method to be used when calculating the adjustment for the loss absorbing capacity of technical provisions or deferred taxes, as laid down in Article 108;
- j the subset of standard parameters in the life, non-life and health underwriting risk modules that may be replaced by undertaking-specific parameters as set out in Article 104(7);
- k the standardised methods to be used by the insurance or reinsurance undertaking to calculate the undertaking-specific parameters referred to in point (j), and any criteria with respect to the completeness, accuracy, and appropriateness of the data used that must be met before supervisory approval is given together with the procedure to be followed for such approval;
- l the simplified calculations provided for specific sub-modules and risk modules, as well as the criteria that insurance and reinsurance undertakings, including captive insurance and reinsurance undertakings, shall be required to fulfil in order to be entitled to use each of those simplifications, as set out in Article 109;
- m the approach to be used with respect to related undertakings within the meaning of Article 212 in the calculation of the Solvency Capital Requirement, in particular the calculation of the equity risk sub-module referred to in Article 105(5), taking into account the likely reduction in the volatility of the value of those related undertakings arising from the strategic nature of those investments and the influence exercised by the participating undertaking on those related undertakings;
- n how to use external credit assessments from ECAs in the calculation of the Solvency Capital Requirement in accordance with the standard formula and the allocation of external credit assessments to a scale of credit quality steps referred to in Article 109a(1) which shall be consistent with the use of external credit assessments from ECAs in the calculation of the capital requirements for credit institutions as defined in Article 4(1)(1) of Regulation (EU) No 575/2013 and financial institutions as defined in Article 4(1)(26) thereof;
- o the detailed criteria for the equity index referred to in Article 109a(2)(c);
- p the detailed criteria for the adjustments for currencies pegged to the euro for the purpose of facilitating the calculation of the currency risk sub-module referred to in Article 109a(2)(d);
- q the conditions for a categorisation of regional governments and local authorities referred to in Article 109a(2)(a).

2 In order to ensure uniform conditions of application of this Article, EIOPA shall develop draft implementing technical standards on the procedures for supervisory approval of undertaking-specific parameters referred to in point (k) of paragraph 1.

EIOPA shall submit those draft implementing technical standards to the Commission by 31 October 2014.

Power is conferred on the Commission to adopt the implementing technical standards referred to in the first subparagraph in accordance with Article 15 of Regulation (EU) No 1094/2010.

3 By 31 December 2020, the Commission shall make an assessment of the appropriateness of the methods, assumptions and standard parameters used when calculating

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the Solvency Capital Requirement standard formula. It shall in particular take into account the performance of any asset class and financial instruments, the behaviour of investors in those assets and financial instruments as well as developments in international standard setting in financial services. The review of certain asset classes may be prioritised. The Commission shall present a report to the European Parliament and to the Council, accompanied, where appropriate, by proposals for the amendment of this Directive, or of delegated or implementing acts adopted pursuant hereto.

4 In order to ensure consistent harmonisation in relation to the Solvency Capital Requirement, EIOPA shall, subject to Article 301b, develop draft regulatory technical standards to specify quantitative limits and asset eligibility criteria where those risks are not adequately covered by a sub-module.

Power is delegated to the Commission to adopt the regulatory technical standards referred to in the first subparagraph in accordance with Articles 10 to 14 of Regulation (EU) No 1094/2010.

Those regulatory technical standards shall apply to assets covering technical provisions, excluding assets held in respect of life insurance contracts where the investment risk is borne by the policy holders. They shall be reviewed by the Commission in the light of developments in the standard formula and financial markets.]

#### **Textual Amendments**

- F1** Substituted by [Directive 2014/51/EU of the European Parliament and of the Council of 16 April 2014 amending Directives 2003/71/EC and 2009/138/EC and Regulations \(EC\) No 1060/2009, \(EU\) No 1094/2010 and \(EU\) No 1095/2010 in respect of the powers of the European Supervisory Authority \(European Insurance and Occupational Pensions Authority\) and the European Supervisory Authority \(European Securities and Markets Authority\).](#)

### Subsection 3

#### **Solvency capital requirement full and partial internal models**

##### *Article 112*

#### **General provisions for the approval of full and partial internal models**

1 Member States shall ensure that insurance or reinsurance undertakings may calculate the Solvency Capital Requirement using a full or partial internal model as approved by the supervisory authorities.

2 Insurance and reinsurance undertakings may use partial internal models for the calculation of one or more of the following:

- a one or more risk modules, or sub-modules, of the Basic Solvency Capital Requirement, as set out in Articles 104 and 105;
- b the capital requirement for operational risk as set out in Article 107;
- c the adjustment referred to in Article 108.

In addition, partial modelling may be applied to the whole business of insurance and reinsurance undertakings, or only to one or more major business units.

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3 In any application for approval, insurance and reinsurance undertakings shall submit, as a minimum, documentary evidence that the internal model fulfils the requirements set out in Articles 120 to 125.

Where the application for that approval relates to a partial internal model, the requirements set out in Articles 120 to 125 shall be adapted to take account of the limited scope of the application of the model.

4 The supervisory authorities shall decide on the application within six months from the receipt of the complete application.

5 Supervisory authorities shall give approval to the application only if they are satisfied that the systems of the insurance or reinsurance undertaking for identifying, measuring, monitoring, managing and reporting risk are adequate and in particular, that the internal model fulfils the requirements referred to in paragraph 3.

6 A decision by the supervisory authorities to reject the application for the use of an internal model shall state the reasons on which it is based.

7 After having received approval from supervisory authorities to use an internal model, insurance and reinsurance undertakings may, by means of a decision stating the reasons, be required to provide supervisory authorities with an estimate of the Solvency Capital Requirement determined in accordance with the standard formula, as set out in Subsection 2.

#### *Article 113*

#### **Specific provisions for the approval of partial internal models**

1 In the case of a partial internal model, supervisory approval shall be given only where that model fulfils the requirements set out in Article 112 and the following additional conditions:

- a the reason for the limited scope of application of the model is properly justified by the undertaking;
- b the resulting Solvency Capital Requirement reflects more appropriately the risk profile of the undertaking and in particular complies with the principles set out in Subsection 1;
- c its design is consistent with the principles set out in Subsection 1 so as to allow the partial internal model to be fully integrated into the Solvency Capital Requirement standard formula.

2 When assessing an application for the use of a partial internal model which only covers certain sub-modules of a specific risk module, or some of the business units of an insurance or reinsurance undertaking with respect to a specific risk module, or parts of both, supervisory authorities may require the insurance and reinsurance undertakings concerned to submit a realistic transitional plan to extend the scope of the model.

The transitional plan shall set out the manner in which insurance and reinsurance undertakings plan to extend the scope of the model to other sub-modules or business units, in order to ensure that the model covers a predominant part of their insurance operations with respect to that specific risk module.

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### *F1* Article 114

#### **Delegated acts and implementing technical standards concerning the Solvency Capital Requirement internal models**

1 The Commission shall adopt delegated acts in accordance with Article 301a setting out the following:

- a the adaptations to be made to the standards set out in Articles 120 to 125 in light of the limited scope of the application of the partial internal model;
- b the manner in which a partial internal model is to be fully integrated into the Solvency Capital Requirement standard formula referred to in Article 113(1)(c) and the requirements for the use of alternative integration techniques.

2 In order to ensure uniform conditions of application of this Article, EIOPA shall develop draft implementing technical standards on the procedures for:

- a the approval of an internal model in accordance with Article 112; and
- b the approval of major changes to an internal model and changes to the policy for changing an internal model referred to in Article 115.

EIOPA shall submit those draft implementing technical standards to the Commission by 31 October 2014.

Power is conferred on the Commission to adopt the implementing technical standards referred to in the first subparagraph in accordance with Article 15 of Regulation (EU) No 1094/2010.]

#### **Textual Amendments**

- F1** Substituted by [Directive 2014/51/EU of the European Parliament and of the Council of 16 April 2014 amending Directives 2003/71/EC and 2009/138/EC and Regulations \(EC\) No 1060/2009, \(EU\) No 1094/2010 and \(EU\) No 1095/2010 in respect of the powers of the European Supervisory Authority \(European Insurance and Occupational Pensions Authority\) and the European Supervisory Authority \(European Securities and Markets Authority\).](#)

### *Article 115*

#### **Policy for changing the full and partial internal models**

As part of the initial approval process of an internal model, the supervisory authorities shall approve the policy for changing the model of the insurance or reinsurance undertaking. Insurance and reinsurance undertakings may change their internal model in accordance with that policy.

The policy shall include a specification of minor and major changes to the internal model.

Major changes to the internal model, as well as changes to that policy, shall always be subject to prior supervisory approval, as laid down in Article 112.

Minor changes to the internal model shall not be subject to prior supervisory approval, insofar as they are developed in accordance with that policy.



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### *Article 116*

#### **Responsibilities of the administrative, management or supervisory bodies**

The administrative, management or supervisory bodies of the insurance and reinsurance undertakings shall approve the application to the supervisory authorities for approval of the internal model referred to in Article 112, as well as the application for approval of any subsequent major changes made to that model.

The administrative, management or supervisory body shall have responsibility for putting in place systems which ensure that the internal model operates properly on a continuous basis.

### *Article 117*

#### **Reversion to the standard formula**

After having received approval in accordance with Article 112, insurance and reinsurance undertakings shall not revert to calculating the whole or any part of the Solvency Capital Requirement in accordance with the standard formula, as set out in Subsection 2, except in duly justified circumstances and subject to the approval of the supervisory authorities.

### *Article 118*

#### **Non-compliance of the internal model**

1 If, after having received approval from the supervisory authorities to use an internal model, insurance and reinsurance undertakings cease to comply with the requirements set out in Articles 120 to 125, they shall, without delay, either present to the supervisory authorities a plan to restore compliance within a reasonable period of time, or demonstrate that the effect of non-compliance is immaterial.

2 In the event that insurance and reinsurance undertakings fail to implement the plan referred to in paragraph 1, the supervisory authorities may require insurance and reinsurance undertakings to revert to calculating the Solvency Capital Requirement in accordance with the standard formula, as set out in Subsection 2.

### *Article 119*

#### **Significant deviations from the assumptions underlying the standard formula calculation**

Where it is inappropriate to calculate the Solvency Capital Requirement in accordance with the standard formula, as set out in Subsection 2, because the risk profile of the insurance or reinsurance undertaking concerned deviates significantly from the assumptions underlying the standard formula calculation, the supervisory authorities may, by means of a decision stating the reasons, require the undertaking concerned to use an internal model to calculate the Solvency Capital Requirement, or the relevant risk modules thereof.

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## Article 120

### Use test

Insurance and reinsurance undertakings shall demonstrate that the internal model is widely used in and plays an important role in their system of governance, referred to in Articles 41 to 50, in particular:

- (a) their risk-management system as laid down in Article 44 and their decision-making processes;
- (b) their economic and solvency capital assessment and allocation processes, including the assessment referred to in Article 45.

In addition, insurance and reinsurance undertakings shall demonstrate that the frequency of calculation of the Solvency Capital Requirement using the internal model is consistent with the frequency with which they use their internal model for the other purposes covered by the first paragraph.

The administrative, management or supervisory body shall be responsible for ensuring the ongoing appropriateness of the design and operations of the internal model, and that the internal model continues to appropriately reflect the risk profile of the insurance and reinsurance undertakings concerned.

## Article 121

### Statistical quality standards

1 The internal model, and in particular the calculation of the probability distribution forecast underlying it, shall comply with the criteria set out in paragraphs 2 to 9.

2 The methods used to calculate the probability distribution forecast shall be based on adequate, applicable and relevant actuarial and statistical techniques and shall be consistent with the methods used to calculate technical provisions.

The methods used to calculate the probability distribution forecast shall be based upon current and credible information and realistic assumptions.

Insurance and reinsurance undertakings shall be able to justify the assumptions underlying their internal model to the supervisory authorities.

3 Data used for the internal model shall be accurate, complete and appropriate.

Insurance and reinsurance undertakings shall update the data sets used in the calculation of the probability distribution forecast at least annually.

4 No particular method for the calculation of the probability distribution forecast shall be prescribed.

Regardless of the calculation method chosen, the ability of the internal model to rank risk shall be sufficient to ensure that it is widely used in and plays an important role in the system of governance of insurance and reinsurance undertakings, in particular their risk-management system and decision-making processes, and capital allocation in accordance with Article 120.

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The internal model shall cover all of the material risks to which insurance and reinsurance undertakings are exposed. Internal models shall cover at least the risks set out in Article 101(4).

5 As regards diversification effects, insurance and reinsurance undertakings may take account in their internal model of dependencies within and across risk categories, provided that supervisory authorities are satisfied that the system used for measuring those diversification effects is adequate.

6 Insurance and reinsurance undertakings may take full account of the effect of risk-mitigation techniques in their internal model, as long as credit risk and other risks arising from the use of risk-mitigation techniques are properly reflected in the internal model.

7 Insurance and reinsurance undertakings shall accurately assess the particular risks associated with financial guarantees and any contractual options in their internal model, where material. They shall also assess the risks associated with both policy holder options and contractual options for insurance and reinsurance undertakings. For that purpose, they shall take account of the impact that future changes in financial and non-financial conditions may have on the exercise of those options.

8 In their internal model, insurance and reinsurance undertakings may take account of future management actions that they would reasonably expect to carry out in specific circumstances.

In the case set out in the first subparagraph, the undertaking concerned shall make allowance for the time necessary to implement such actions.

9 In their internal model, insurance and reinsurance undertakings shall take account of all payments to policy holders and beneficiaries which they expect to make, whether or not those payments are contractually guaranteed.

## *Article 122*

### **Calibration standards**

1 Insurance and reinsurance undertakings may use a different time period or risk measure than that set out in Article 101(3) for internal modelling purposes as long as the outputs of the internal model can be used by those undertakings to calculate the Solvency Capital Requirement in a manner that provides policy holders and beneficiaries with a level of protection equivalent to that set out in Article 101.

2 Where practicable, insurance and reinsurance undertakings shall derive the Solvency Capital Requirement directly from the probability distribution forecast generated by the internal model of those undertakings, using the Value-at-Risk measure set out in Article 101(3).

3 Where insurance and reinsurance undertakings cannot derive the Solvency Capital Requirement directly from the probability distribution forecast generated by the internal model, the supervisory authorities may allow approximations to be used in the process to calculate the Solvency Capital Requirement, as long as those undertakings can demonstrate to the supervisory authorities that policy holders are provided with a level of protection equivalent to that provided for in Article 101.

4 Supervisory authorities may require insurance and reinsurance undertakings to run their internal model on relevant benchmark portfolios and using assumptions based on external

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rather than internal data in order to verify the calibration of the internal model and to check that its specification is in line with generally accepted market practice.

#### *Article 123*

##### **Profit and loss attribution**

Insurance and reinsurance undertakings shall review, at least annually, the causes and sources of profits and losses for each major business unit.

They shall demonstrate how the categorisation of risk chosen in the internal model explains the causes and sources of profits and losses. The categorisation of risk and attribution of profits and losses shall reflect the risk profile of the insurance and reinsurance undertakings.

#### *Article 124*

##### **Validation standards**

Insurance and reinsurance undertakings shall have a regular cycle of model validation which includes monitoring the performance of the internal model, reviewing the ongoing appropriateness of its specification, and testing its results against experience.

The model validation process shall include an effective statistical process for validating the internal model which enables the insurance and reinsurance undertakings to demonstrate to their supervisory authorities that the resulting capital requirements are appropriate.

The statistical methods applied shall test the appropriateness of the probability distribution forecast compared not only to loss experience but also to all material new data and information relating thereto.

The model validation process shall include an analysis of the stability of the internal model and in particular the testing of the sensitivity of the results of the internal model to changes in key underlying assumptions. It shall also include an assessment of the accuracy, completeness and appropriateness of the data used by the internal model.

#### *Article 125*

##### **Documentation standards**

Insurance and reinsurance undertakings shall document the design and operational details of their internal model.

The documentation shall demonstrate compliance with Articles 120 to 124.

The documentation shall provide a detailed outline of the theory, assumptions, and mathematical and empirical bases underlying the internal model.

The documentation shall indicate any circumstances under which the internal model does not work effectively.

Insurance and reinsurance undertakings shall document all major changes to their internal model, as set out in Article 115.

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## Article 126

### External models and data

The use of a model or data obtained from a third party shall not be considered to be a justification for exemption from any of the requirements for the internal model set out in Articles 120 to 125.

## <sup>F1</sup>Article 127

### Delegated acts concerning Articles 120 to 126

The Commission shall adopt delegated acts in accordance with Article 301a with respect to Articles 120 to 126 to enhance the better assessment of the risk profile and management of the business of insurance and reinsurance undertakings regarding the use of internal models throughout the Union.]

#### Textual Amendments

- F1** Substituted by [Directive 2014/51/EU of the European Parliament and of the Council of 16 April 2014 amending Directives 2003/71/EC and 2009/138/EC and Regulations \(EC\) No 1060/2009, \(EU\) No 1094/2010 and \(EU\) No 1095/2010 in respect of the powers of the European Supervisory Authority \(European Insurance and Occupational Pensions Authority\) and the European Supervisory Authority \(European Securities and Markets Authority\).](#)

## Section 5

### Minimum capital requirement

## Article 128

### General provisions

Member States shall require that insurance and reinsurance undertakings hold eligible basic own funds, to cover the Minimum Capital Requirement.

## Article 129

### Calculation of the Minimum Capital Requirement

- 1 The Minimum Capital Requirement shall be calculated in accordance with the following principles:
- a it shall be calculated in a clear and simple manner, and in such a way as to ensure that the calculation can be audited;
  - b it shall correspond to an amount of eligible basic own funds below which policy holders and beneficiaries are exposed to an unacceptable level of risk were insurance and reinsurance undertakings allowed to continue their operations;

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- c the linear function referred to in paragraph 2 used to calculate the Minimum Capital Requirement shall be calibrated to the Value-at-Risk of the basic own funds of an insurance or reinsurance undertaking subject to a confidence level of 85 % over a one-year period;
- d it shall have an absolute floor of:
  - (i) [<sup>F1</sup>EUR 2 500 000 for non-life insurance undertakings, including captive insurance undertakings, save in the case where all or some of the risks included in one of the classes 10 to 15 listed in Part A of Annex I are covered, in which case it shall be no less than EUR 3 700 000;
  - (ii) EUR 3 700 000 for life insurance undertakings, including captive insurance undertakings;
  - (iii) EUR 3 600 000 for reinsurance undertakings, except in the case of captive reinsurance undertakings, in which case the Minimum Capital Requirement shall be not less than EUR 1 200 000;]
  - (iv) the sum of the amounts set out in points (i) and (ii) for insurance undertakings as referred to in Article 73(5).

2 Subject to paragraph 3, the Minimum Capital Requirement shall be calculated as a linear function of a set or sub-set of the following variables: the undertaking's technical provisions, written premiums, capital-at-risk, deferred tax and administrative expenses. The variables used shall be measured net of reinsurance.

3 Without prejudice to paragraph 1(d), the Minimum Capital Requirement shall neither fall below 25 % nor exceed 45 % of the undertaking's Solvency Capital Requirement, calculated in accordance with Chapter VI, Section 4, Subsections 2 or 3, and including any capital add-on imposed in accordance with Article 37.

[<sup>F1</sup>Member States shall allow their supervisory authorities, for a period ending no later than 31 December 2017, to require an insurance or reinsurance undertaking to apply the percentages referred to in the first subparagraph exclusively to the undertaking's Solvency Capital Requirement calculated in accordance with Chapter VI, Section 4, Subsection 2.]

4 Insurance and reinsurance undertakings shall calculate the Minimum Capital Requirement at least quarterly and report the results of that calculation to supervisory authorities.

[<sup>F2</sup>For the purposes of calculating the limits referred to in paragraph 3, undertakings shall not be required to calculate the Solvency Capital Requirement on a quarterly basis.]

Where either of the limits referred to in paragraph 3 determines an undertaking's Minimum Capital Requirement, the undertaking shall provide to the supervisory authority information allowing a proper understanding of the reasons therefor.

[<sup>F15</sup> The Commission shall submit to the European Parliament and the Council by 31 December 2020 a report on Member States' rules and supervisory authorities' practices adopted pursuant to paragraphs 1 to 4.]

That report shall address, in particular, the use and level of the cap and the floor set out in paragraph 3 as well as any problems faced by supervisory authorities and by undertakings in the application of this Article.

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#### Textual Amendments

- F1** Substituted by Directive 2014/51/EU of the European Parliament and of the Council of 16 April 2014 amending Directives 2003/71/EC and 2009/138/EC and Regulations (EC) No 1060/2009, (EU) No 1094/2010 and (EU) No 1095/2010 in respect of the powers of the European Supervisory Authority (European Insurance and Occupational Pensions Authority) and the European Supervisory Authority (European Securities and Markets Authority).
- F2** Inserted by Directive 2014/51/EU of the European Parliament and of the Council of 16 April 2014 amending Directives 2003/71/EC and 2009/138/EC and Regulations (EC) No 1060/2009, (EU) No 1094/2010 and (EU) No 1095/2010 in respect of the powers of the European Supervisory Authority (European Insurance and Occupational Pensions Authority) and the European Supervisory Authority (European Securities and Markets Authority).

### *[<sup>F1</sup>Article 130*

#### **Delegated acts**

The Commission shall adopt delegated acts in accordance with Article 301a specifying the calculation of the Minimum Capital Requirement, referred to in Articles 128 and 129.]

#### Textual Amendments

- F1** Substituted by Directive 2014/51/EU of the European Parliament and of the Council of 16 April 2014 amending Directives 2003/71/EC and 2009/138/EC and Regulations (EC) No 1060/2009, (EU) No 1094/2010 and (EU) No 1095/2010 in respect of the powers of the European Supervisory Authority (European Insurance and Occupational Pensions Authority) and the European Supervisory Authority (European Securities and Markets Authority).

### *Article 131*

#### **Transitional arrangements regarding compliance with the Minimum Capital Requirement**

By way of derogation from Articles 139 and 144, where insurance and reinsurance undertakings comply with the Required Solvency Margin referred to in Article 28 of Directive 2002/83/EC, Article 16a of Directive 73/239/EEC or Article 37, 38 or 39 of Directive 2005/68/EC respectively on [<sup>F1</sup>31 December 2015] but do not hold sufficient eligible basic own funds to cover the Minimum Capital Requirement, the undertakings concerned shall comply with Article 128 by [<sup>F1</sup>31 December 2016].

Where the undertaking concerned fails to comply with Article 128 within the period set out in the first paragraph, the authorisation of the undertaking shall be withdrawn, subject to the applicable processes provided for in the national legislation.

#### Textual Amendments

- F1** Substituted by Directive 2014/51/EU of the European Parliament and of the Council of 16 April 2014 amending Directives 2003/71/EC and 2009/138/EC and Regulations (EC) No 1060/2009, (EU) No 1094/2010 and (EU) No 1095/2010 in respect of the powers of the European Supervisory Authority

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## Section 6

### Investments

#### Article 132

#### Prudent person principle

1 Member States shall ensure that insurance and reinsurance undertakings invest all their assets in accordance with the prudent person principle, as specified in paragraphs 2, 3 and 4.

2 With respect to the whole portfolio of assets, insurance and reinsurance undertakings shall only invest in assets and instruments whose risks the undertaking concerned can properly identify, measure, monitor, manage, control and report, and appropriately take into account in the assessment of its overall solvency needs in accordance with point (a) of the second subparagraph of Article 45(1).

All assets, in particular those covering the Minimum Capital Requirement and the Solvency Capital Requirement, shall be invested in such a manner as to ensure the security, quality, liquidity and profitability of the portfolio as a whole. In addition the localisation of those assets shall be such as to ensure their availability.

Assets held to cover the technical provisions shall also be invested in a manner appropriate to the nature and duration of the insurance and reinsurance liabilities. Those assets shall be invested in the best interest of all policy holders and beneficiaries taking into account any disclosed policy objective.

In the case of a conflict of interest, insurance undertakings, or the entity which manages their asset portfolio, shall ensure that the investment is made in the best interest of policy holders and beneficiaries.

3 Without prejudice to paragraph 2, with respect to assets held in respect of life insurance contracts where the investment risk is borne by the policy holders, the second, third and fourth subparagraphs of this paragraph shall apply.

Where the benefits provided by a contract are directly linked to the value of units in an UCITS as defined in Directive 85/611/EEC, or to the value of assets contained in an internal fund held by the insurance undertakings, usually divided into units, the technical provisions in respect of those benefits must be represented as closely as possible by those units or, in the case where units are not established, by those assets.

Where the benefits provided by a contract are directly linked to a share index or some other reference value other than those referred to in the second subparagraph, the technical provisions in respect of those benefits must be represented as closely as possible either by the units deemed to represent the reference value or, in the case where units are not established, by assets of appropriate security and marketability which correspond as closely as possible with those on which the particular reference value is based.



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Where the benefits referred to in the second and third subparagraphs include a guarantee of investment performance or some other guaranteed benefit, the assets held to cover the corresponding additional technical provisions shall be subject to paragraph 4.

4 Without prejudice to paragraph 2, with respect to assets other than those covered by paragraph 3, the second to fifth subparagraphs of this paragraph shall apply.

The use of derivative instruments shall be possible insofar as they contribute to a reduction of risks or facilitate efficient portfolio management.

Investment and assets which are not admitted to trading on a regulated financial market shall be kept to prudent levels.

Assets shall be properly diversified in such a way as to avoid excessive reliance on any particular asset, issuer or group of undertakings, or geographical area and excessive accumulation of risk in the portfolio as a whole.

Investments in assets issued by the same issuer, or by issuers belonging to the same group, shall not expose the insurance undertakings to excessive risk concentration.

### *Article 133*

#### **Freedom of investment**

1 Member States shall not require insurance and reinsurance undertakings to invest in particular categories of asset.

2 Member States shall not subject the investment decisions of an insurance or reinsurance undertaking or its investment manager to any kind of prior approval or systematic notification requirements.

3 This Article is without prejudice to Member States' requirements restricting the types of assets or reference values to which policy benefits may be linked. Any such rules shall be applied only where the investment risk is borne by a policy holder who is a natural person and shall not be more restrictive than those set out in the Directive 85/611/EEC.

### *Article 134*

#### **Localisation of assets and prohibition of pledging of assets**

1 With respect to insurance risks situated in the Community, Member States shall not require that the assets held to cover the technical provisions related to those risks are localised within the Community or in any particular Member States.

In addition, with respect to recoverables from reinsurance contracts against undertakings authorised in accordance with this Directive or which have their head office in a third country whose solvency regime is deemed to be equivalent in accordance with Article 172, Member States shall not require the localisation within the Community of the assets representing those recoverables.

2 Member States shall not retain or introduce for the establishment of technical provisions a system with gross reserving which requires pledging of assets to cover unearned premiums and outstanding claims provisions where the reinsurer is an insurance or reinsurance undertaking authorised in accordance with this Directive.

### *[<sup>F1</sup>Article 135*

#### **Delegated acts and regulatory technical standards concerning qualitative requirements**

1 The Commission may adopt delegated acts in accordance with Article 301a specifying qualitative requirements in the following areas:

- a the identification, measurement, monitoring and managing of risks arising from investments in relation to the first subparagraph of Article 132(2);
- b the identification, measurement, monitoring and managing of specific risks arising from investment in derivative instruments and assets referred to in the second subparagraph of Article 132(4) and the determination of the extent to which the use of such assets qualifies as risk reduction or efficient portfolio management as referred to in the third subparagraph of Article 132(4).

[<sup>F32</sup> The Commission shall adopt delegated acts in accordance with Article 301a of this Directive supplementing this Directive by laying down the specifications for the circumstances under which a proportionate additional capital charge may be imposed when the requirements provided for in Articles 5 or 6 of Regulation (EU) 2017/2402 of the European Parliament and of the Council<sup>(1)</sup> have been breached, without prejudice to Article 101(3) of this Directive.

3 In order to ensure consistent harmonisation in relation to paragraph 2 of this Article, EIOPA shall, subject to Article 301b, develop draft regulatory technical standards to specify the methodologies for the calculation of a proportionate additional capital charge referred to therein.

The Commission is empowered to supplement this Directive by adopting the regulatory technical standards referred to in this paragraph in accordance with Articles 10 to 14 of Regulation (EU) No 1094/2010.]]

#### **Textual Amendments**

- F1** Substituted by Directive 2014/51/EU of the European Parliament and of the Council of 16 April 2014 amending Directives 2003/71/EC and 2009/138/EC and Regulations (EC) No 1060/2009, (EU) No 1094/2010 and (EU) No 1095/2010 in respect of the powers of the European Supervisory Authority (European Insurance and Occupational Pensions Authority) and the European Supervisory Authority (European Securities and Markets Authority).
- F3** Substituted by Regulation (EU) 2017/2402 of the European Parliament and of the Council of 12 December 2017 laying down a general framework for securitisation and creating a specific framework for simple, transparent and standardised securitisation, and amending Directives 2009/65/EC, 2009/138/EC and 2011/61/EU and Regulations (EC) No 1060/2009 and (EU) No 648/2012.

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*Status: EU Directives are being published on this site to aid cross referencing from UK legislation. After IP completion day (31 December 2020 11pm) no further amendments will be applied to this version.*

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- (1) [<sup>F1</sup>]<sup>F3</sup>Regulation (EU) 2017/2402 of the European Parliament and of the Council of 12 December 2017 laying down a general framework for securitisation and creating a specific framework for simple, transparent and standardised securitisation, and amending Directives 2009/65/EC, 2009/138/EC and 2011/61/EU and Regulations (EC) No 1060/2009 and (EU) No 648/2012 (OJ L 347, 28.12.2017, p. 35).]]

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- F1** Substituted by Directive 2014/51/EU of the European Parliament and of the Council of 16 April 2014 amending Directives 2003/71/EC and 2009/138/EC and Regulations (EC) No 1060/2009, (EU) No 1094/2010 and (EU) No 1095/2010 in respect of the powers of the European Supervisory Authority (European Insurance and Occupational Pensions Authority) and the European Supervisory Authority (European Securities and Markets Authority).
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