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To:	Mr Jeppe TRANHOLM-MIKKELSEN, Secretary-General of the Council of the European Union
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Subject:	COMMISSION STAFF WORKING DOCUMENT EXECUTIVE SUMMARY OF THE IMPACT ASSESSMENT REPORT Accompanying the documents Proposal for a Directive of the European Parliament and of the Council amending Directive 2009/138/EC as regards proportionality, quality of supervision, reporting, long-term guarantee measures, macro-prudential tools, sustainability risks, group and cross-border supervision and Proposal for a Directive of the European Parliament and of the Council establishing a framework for the recovery and resolution of insurance and reinsurance undertakings and amending Directives 2002/47/EC, 2004/25/EC, 2009/138/EC, (EU) 2017/1132 and Regulations (EU) No 1094/2010 and (EU) No 648/2012

Delegations will find attached document SWD(2021) 261 final.

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COMMISSION STAFF WORKING DOCUMENT

EXECUTIVE SUMMARY OF THE IMPACT ASSESSMENT REPORT

Accompanying the documents

Proposal for a Directive of the European Parliament and of the Council amending Directive 2009/138/EC as regards proportionality, quality of supervision, reporting, long-term guarantee measures, macro-prudential tools, sustainability risks, group and cross-border supervision

and Proposal for a Directive of the European Parliament and of the Council establishing a framework for the recovery and resolution of insurance and reinsurance undertakings and amending Directives 2002/47/EC, 2004/25/EC, 2009/138/EC, (EU) 2017/1132 and Regulations (EU) No 1094/2010 and (EU) No 648/2012

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Executive summary sheet

Impact assessment of the Proposal for a Directive amending 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)

A. Need for action

Why? What is the problem being addressed?

The Solvency II Directive, which has applied since 2016, introduced a harmonised, sound and robust prudential framework for insurance firms in the EU. It is based on the risk profile of each individual insurance company in order to promote comparability, transparency and competitiveness.

The evaluation has concluded that, overall, the Solvency II framework functions effectively, but that certain elements need to be improved.

1. Solvency II still includes disincentives to long-term investment in equity, and does not capture the longer-term sustainability risks;
2. Solvency II does not appropriately reflect the low interest rates environment, and may unduly generate high volatility in solvency ratios;
3. Solvency II can prove to be overly complex for small and less risky insurers;
4. recent failures of insurers operating across borders highlighted shortcomings in supervision and confirmed that policyholders are not consistently protected across the EU if their insurer fails;
5. the supervisory toolkit to prevent systemic risks may prove to be insufficient.

What is this initiative expected to achieve?

Taking into account the above-mentioned problems, the review of Solvency II aims to go further in achieving the Commission's initial objectives for Solvency II, namely:

1. increasing insurers' contributions to the long-term and sustainable financing of the economy;
2. preserving the international competitiveness of EU insurers and improving their efficiency;
3. enhancing the protection of policyholders;
4. contributing to financial stability.

What is the value added of action at EU level?

The review will amend existing EU legislation and will introduce new elements, notably on environmental risks, resolution, macro-prudential tools and, possibly, insurance guarantee schemes (IGSs). These amendments are justified by the cross-border nature of the insurance business. It is more efficient for insurers to be subject to a single set of rules than to various national frameworks. Similarly, only EU-level action can ensure that all consumers benefit from equal treatment.

B. Solutions

What legislative and non-legislative policy options have been considered? Is there a preferred choice or not? Why?

The baseline scenario for all problems is "do nothing".

Regarding long-term and green investments, the preferred options are to facilitate long-term investments in equity by loosening the eligibility criteria for preferential treatment of such investments, and to strengthen risk management requirements for climate and sustainability risks. Other options that were considered include proceeding to a general reduction in capital requirements for all equity investments and/or lowering capital requirements for green investments.

Regarding risk sensitivity and volatility, a first option was to fix all technical flaws. However, the preferred option is to proceed to such fixes while ensuring that the cumulative impact of all changes remains moderate in terms of capital requirements.

Regarding proportionality, one approach is to follow EIOPA's advice; this implies very significant increases in thresholds of exclusion from the scope of Solvency II and the identification of "low risk profile" insurers, which would be subject to automatic proportionality measures. The preferred approach is to proceed to a lower increase in exclusion thresholds, but to go further than EIOPA in enhancing proportionality within Solvency II, including for public disclosure.

Regarding quality of supervision and policyholder protection, the choice is to cumulatively improve the quality of cross-border supervision and to introduce minimum harmonising rules that aim to ensure policyholders are adequately protected in cases of insurance (near-)failure.

Regarding financial stability, while EIOPA and the ESRB propose to introduce an extensive macro-prudential framework, similar to what exists in the banking sector, the preferred option is to make targeted amendments to ensure supervisors have sufficient tools to prevent financial stability risks, in line with international standards.

This combination of preferred options is the most cost-effective, and is consistent with the main objectives of Solvency II (policyholder protection, financial stability) and with the current political priorities (CMU, European Green Deal).

Who supports which option?

Support from stakeholders varies between the different issues.
Among the proposed options, the majority of stakeholders would support the proposed way forward on *long-term and green financing*, and on *risk sensitivity and volatility*.
On *proportionality*, policyholders would support the preferred option. Insurers that would benefit from the proportionality measures would generally support the proposed approach, although they would go further than this approach regarding the scope for excluding insurers from Solvency II.
Consumers/NGOs would support the preferred option on *quality of supervision and policyholder protection*, and highly value the need to preserve financial stability. Insurers would prefer limited changes in those two areas.

C. Impacts of the preferred option

What are the benefits of the preferred option (if any, otherwise main ones)?

The combination of preferred options is expected to:

- facilitate insurers' ability to fund businesses;
- incentivise insurers to take better account of sustainability risks;
- foster long-termism in insurers' activities, by better mitigating the impact of market volatility;
- enhance policyholder protection by
    i. better incorporating the low-yield environment;
    ii. strengthening coordination and consistency of supervision;
    iii. introducing minimum harmonising rules to mitigate the impact of insurance (near-)failures.
- help preserve financial stability.

The initiative would result in an increase of up to EUR 30 billion in the amount of own funds in excess of capital requirements, depending on market conditions. As the changes that would reduce insurers' solvency ratios would only be gradually implemented over several years, in the short term the initiative would release up to EUR 90 billion of capital that insurers could use to support the economic recovery.

What are the costs of the preferred option (if any, otherwise main ones)?

Some individual changes, notably in relation to interest rates, would on their own reduce insurers' capital resources. However, as stated above, the cumulative effect of all changes would be an increase in insurers' own funds in excess of capital requirements.
The cost of introducing IGSs would be around EUR 21 billion, which would be partly passed on to policyholders through increased premiums.
The review would generate moderate implementation and administrative burdens.

How will businesses, SMEs and micro-enterprises be affected?

The review could waive the mandatory application of Solvency II for up to 186 insurers. In addition, at least 249 insurers that would remain within the scope of Solvency II would benefit from simpler and more proportionate rules, which would reduce their compliance costs. Moreover, the review would facilitate insurers' capital funding of SMEs.

Will there be significant impacts on national budgets and administrations?

No

Will there be other significant impacts?

No

D. Follow up

When will the policy be reviewed?

The legislation will be subject to a complete evaluation 5 years after its implementation deadline, to assess how effective and efficient it has been in achieving the objectives presented in this report and to decide whether new measures or amendments are needed.