	Comments Template on Consultation Paper on EIOPA's first set of advice to the European Commission on specific items in the Solvency II Delegated Regulation	Deadline 31 August 2017 23:59 CET
Name of Company:	Assuralia	
Disclosure of comments:	Please indicate if your comments should be treated as confidential:	Public
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General Comment		
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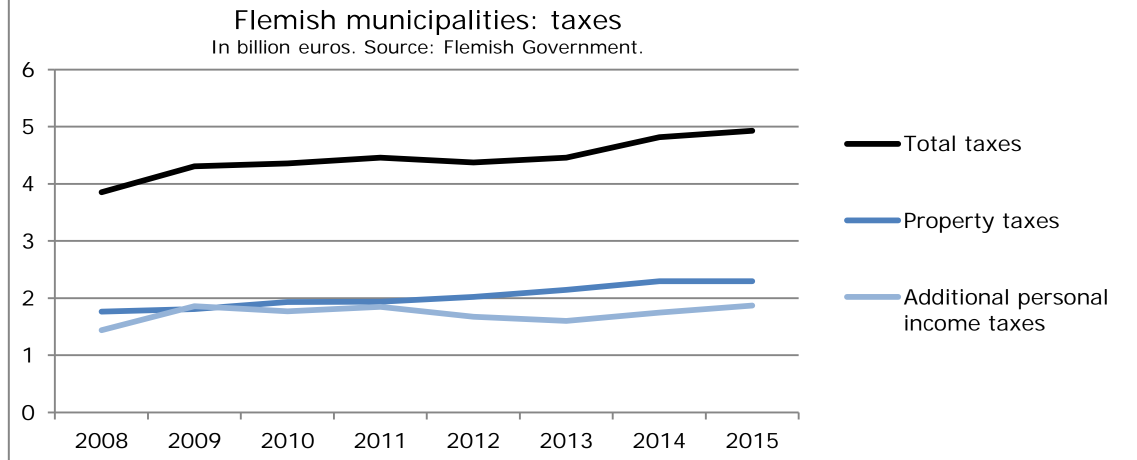
4.4.3	**Aligning the RGLA list in the Commission Implementing Regulation (EU) 2015/2011 with the list of the banking framework** In paragraph 222 of the consultation paper, the following is stated: "The list of RGLA in the Commission Implementing Regulation (EU) 2015/2011 should be aligned with the list of the banking framework… Aligning the RGLA list to the banking regulation might imply modifying the Commission Implementing Regulation (EU) 2015/2011."	

	As pointed out in table 1 of the consultation paper, for Belgium, differences exist between the lists of RGLA in Solvency II and the banking framework. Provinces ("provincie" or "province") and municipalities ("gemeente", "commune") are recognized as RGLA in Solvency II, but not in the list published by EBA regarding article 115(2) of regulation (EU) 575/2013. These differences have an impact of €575 million, as noted in table 2 of the consultation paper. As explained in the paragraphs below, Belgian provinces and municipalities fulfill the criteria of article 109a.2(a) of the Solvency II Directive, and should therefore remain listed in the Implementing Regulation (EU) 2015/2011. *Revenue-raising powers* A first criterion to be listed as RGLA is the existence of specific revenue-raising powers, as required under article 109a.2(a) of the Solvency II Directive and article 85 of the Delegated Regulation. In the final report on RGLA (EIOPA-Bos-15/119), it is stated that the RGLA should have the power to set at least one tax rate, where the RGLA itself benefits from the payments of this tax. Municipalities have the power to set tax rates. The graph below presents the amount of taxes raised by Flemish municipalities (sources: Flemish Government (1) and Flemish Government (2)). The main sources of taxes are property taxes ("onroerende voorheffing") and additional personal income taxes ("aanvullende belasting op de personenbelasting"). The total of taxes raised in 2015 amounts to €4.9 billion, representing 40.4% of the total revenue of Flemish municipalities.	



Belgian provinces also have the power to set tax rates. The data below present the revenues of the 5 Wallonian provinces, according to the budget of 2016 (source: Wallonian Government). The accompanying budget report reads: "Taxes, representing returns of more than EUR 587 million in the initial budget of 2016, are the large majority of ordinary revenues. Depending on the province, 94% up to 99.5% of the taxes emanate from additional property taxes.

€ million	Brabant Wallon	Hainaut	Liège	Lux.	Namur	Total	Total %
Taxes	74	206	182	55	69	587	59.6%
Fund for provinces	12	64	35	13	22	145	14.8%
Education revenues	6	64	28	6	6	110	11.2%
Other revenues	13	47	42	19	21	142	14.4%
Total	105	382	288	92	119	985	100.0%

Specific institutional arrangements

A second criterion to be listed as RGLA is the existence of specific institutional arrangements, as required under article 109a.2(a) of the Solvency II Directive and article 85 of the Delegated Regulation. According to the final report on RGLA (EIOPA-Bos-15/119), a sufficient condition is that the budget of the RGLA is supervised by an authority that is considered of the same risk as the central government (either the central government or another RGLA in the ITS).

The multiannual plan of municipalities, as well as their budget and modifications to their budget are supervised by the provinces and the Flemish Government (listed as RGLA in the ITS 2015/2011). This supervision is legally enacted in articles 176-178 of the Decree on Municipalities. Article 176 explains the supervision on the multiannual plan of municipalities:

> *§1 …the governor of the province can suspend the execution of the multiannual plan and the decision to modify the plan:*
> *1° if it cannot be sufficiently demonstrated, or solely demonstrated based on fictive information, that the financial equilibrium is safeguarded during the financial years of the multiannual plan;*
> *2° if the known or expected revenues or costs… of the municipality were fully or partly not taken up in the multiannual budget…*
> *§3 The Flemish Government takes a motivated decision on the multiannual plan or the modification thereof, laid down by the council of the municipality. The Flemish Government again lays down the multiannual plan or the modification thereof in the following cases:*
> *1° if it cannot be sufficiently demonstrated, or solely demonstrated based on fictive information, that the financial equilibrium is safeguarded during the financial years of the multiannual plan;*
> *2° if the known or expected revenues or costs…. of the municipality were fully or partly not taken up in the multiannual budget…*
> *In the case of 1°, the Flemish Government takes all required measures to restore the financial equilibrium. In the case of 2°, the Flemish Government registers in its official capacity all known or expected revenues or costs…*

| | In article 177 of the Decree on Municipalities, a similar procedure is provided for the budget or modifications to the budget of municipalities. In article 178 of the Decree on Municipalities, it is stated that the supervising government can appoint an external audit committee to verify decisions of the municipality with a financial impact, as well as the municipality's accounting and treasury.

In articles 172-173 of the Provincial Decree, similar provisions are laid down with respect to the multiannual plan and the budget of the provinces. The Flemish Government supervises the Flemish provinces, and can suspend or modify their multiannual plan or budget. Similar provisions for the municipalities and provinces in Wallonia are laid down in articles 16, 17, 22bis and 22ter of the Decree organising the supervision on muncipalties, provinces and intermunicipal companies of Wallonia and its subsequent modifications.

It thus appears from the legal reference above, that the budget of Belgian municipalities and provinces is indeed supervised by other authorities which are considered of the same risk as the central government.

Conclusion
Belgian municipalities and provinces have revenue-raising powers and are subject to institutional arrangements which reduce their risk of default. In accordance with article 109a.2(a) of the Solvency II Directive and article 85 of the Delegated Regulation, Belgian municipalities and provinces should remain in the list of RGLA. We agree with the prior decision to include municipalities and provinces in the ITS 2015/2011 and thus believe that no changes to the list of RGLA seem necessary for Belgium. | |
| 4.4.4 | **Partial guarantees and guarantees under the type 2 counterparty default sub-module**

In the consultation paper, the following formula is proposed in order to allow for (partial) guarantees under the type 2 counterparty default sub-module: | |

LGD=max(loan-max(80%*Mortgage;guarantee);0)

Although we fully support the intention to allow capital charge reductions for (partially) guaranteed mortgages, we would like to point out the following remarks with respect to the formula for LGD proposed in the consultation paper:

Applicability to the NHG

As stated in paragraph 193 of the consultation paper, most of the type 2 exposures which have guarantees by Member States' central governments are the Dutch residential mortgages loans ("Nationale Hypotheekgarantie" or NHG). It is however very unlikely that the formula for LGD, proposed in the consultation paper, will lead to any change to the capital requirements for mortgage loans guaranteed by the NHG. Indeed, the NHG shows the following main features:

- The amount paid out in case of default is at most the difference between the nominal value and the value of the collateral, as stated in article A1.1 of the NHG general conditions.
- For loans concluded as of 1/1/2017, the guarantee is set at 90 percent of the remaining notional at default, as stated in article B13.2 of the NHG general conditions.

These features entail that the guarantee will inevitable be lower compared to the value of 80% of the collateral. Even though the NHG guarantee clearly reduces the risk for insurance undertakings, the capital charge remains unchanged when the LGD formula proposed in the consultation paper is applied.

Differences between Solvency II and the CRR

EIOPA has concluded that the differences in recognition of partial guarantees under Solvency II and the banking framework are not justified for mortgage loans (paragraph 200 of the consultation paper). We fully support this conclusion. However, the formula for LGD proposed in the consultation paper will lead to very different results compared to the approach for partial guarantees currently applied under the CRR.

Under the CRR, partial guarantees for mortgages are effectively recognized and lead to a

reduction in capital requirements. Indeed, under article 235 of the CRR, the risk-weighted exposure is calculated as:

max {exposure – guarantee}*(risk weight obligor)+guarantee*(risk weight guarantor)

For mortgage loans which are sufficiently covered by collateral, the risk weight of the obligor is reduced to 35% (article 125 of the CRR). As such, under the CRR, the risk-mitigating effect of the partial guarantee (article 235) and the risk-mitigating effect of collateral (35% risk weight, article 125) are recognised cumulatively.

The formula for LGD proposed in the consultation paper differs heavily from the approach of the CRR. Indeed, in the proposed formula for LGD, the effect of collateral (80%*Mortgage) and the effect of the partial guarantee are mutually exclusive:

max(80%*Mortgage;guarantee)

In the case of the NHG, it is very likely that the risk-mitigating effect of the guarantee will be disregarded in the formula above. As such, a significant difference between Solvency II and the CRR will remain.

Proposed alternative

As an alternative to the formula for LGD mentioned in the consultation paper, the following formula for LGD is proposed:

LGD = max(Loan – (80%*mortgage + guarantee);0)

This alternative formula effectively recognises the risk-mitigating effect of the NHG and will lead to a better alignment with article 235 of the CRR.

Conditions applicable to partial guarantees

In article 215(f) of the Delegated Regulation, the following condition for guarantees is imposed:

"(f) the guarantee fully covers all types of regular payments the obligor is expected to make in respect of the claim."

In the consultation paper, it is proposed that the guarantee should be recognised provided it complies with the requirements of Articles 209 to 215, except for the requirement that it "fully covers …"

Under a strict reading of this proposal, the NHG guarantee scheme may still be disqualified.

	Indeed, in paragraph 198 of the consultation paper, it is stated that "NHG does not cover all types of regular payments the obligor is expected to make in respect of the claim". This entails that article 215(f) should entirely be disregarded, not only the requirement that it "fully covers …" **Guarantees issued by RGLA** We fully support the introduction of new provisions in Articles 180 and 187 in order the recognize guarantees issued by RGLA. In order to avoid confusion, we also propose to delete the last sentence of recital 42: "When setting up lists of regional governments and local authorities, EIOPA should respect the requirement that there is no difference in risk between exposures to these and exposures to the central government in whose jurisdiction they are established because of the specific revenue raising powers of the former and that specific institutional arrangements exist, the effect of which is to reduce the risk of default. ~~The effect of the implementing act adopted pursuant to Article 109a(2)(a) of Directive 2009/138/EC relating to these lists is that direct exposures to the regional governments and local authorities listed are treated as exposures to the central government of the jurisdiction in which they are established for the purposes of the calculation of the market risk module and the counterparty default risk module of the standard formula.~~"	
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6.4.3	**Look-through of investment related undertakings** We fully support the intention of EIOPA extend the look-through approach to investment related undertakings. In paragraph 375 of the consultation paper, an investment related undertaking is defined as "a related undertaking that meets the following conditions: its purpose is holding assets on behalf of the (parent) insurance undertaking…" A strict reading of this condition may exclude many investment related undertakings, which do not solely *hold* assets, but actively *manage* assets. As an example, investment related undertakings specialized in real estate will not passively hold real estate, but will also construct, lease, refurbish… (i.e. manage) real estate. We therefore propose the following clarification: "its purpose is holding or managing assets on behalf of the (parent) insurance undertaking" We agree that the look-through approach to investment related undertakings should be mandatory and not optional. A mandatory look-through leads to a risk-based view of the underlying investments. The SCR will then better reflect the exposure of the investment related undertaking.	
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8.4.4	**Solvency ratio and LAC DT: paragraphs 492 and 502** In paragraph 492 of the consultation paper, it is stated that "relatively low capitalised undertakings try harder to demonstrate likely utilisation of their LAC DT in order to get a lower SCR and as a consequence a higher SCR ratio." This message is reiterated in paragraph 502 of the consultation paper. These strong statements seem exaggerated. Indeed, correlation coefficients of minus 9.7% and 0.1% are too small to allow EIOPA to conclude a linear relationship between solvency ratio and LAC DT. Similarly, the regression coefficients of -0.9% and -0.6% reported in table 11 may be statistically significant, but are not large enough to be considered economically relevant.	
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8.5.1	**Timing of net DTL: paragraph 510**	

	In paragraph 510 of the consultation paper, the following is stated: "Some NSAs require undertakings to provide evidence that the timing of the net DTL after the shock loss is such that they are available on the right time to utilise the DTA…" Demonstrating the timing of the reversal of net DTL is not proportionate. Instead, it should be assumed that insurance undertakings are able to control the reversal of net DTL on the Solvency II balance sheet. As an example, assume that that an unstressed solvency II balance sheet displays a large amount of net DTL due to declining credit spreads on fixed income assets. Assume that the BSCR of the insurance undertaking is mainly composed of equity shocks. The management of the insurance undertaking has a full discretion on the purchase or sale of assets – this consideration being relevant for jurisdictions that tax on a realised basis. Hence, the management can make sure that the fiscal losses, stemming from the sale of equities at a loss, occur simultaneously with the interest income or gains from the sale of fixed income assets. As such, tax losses resulting from the equity shock do not cause a tax loss carry forward, because the insurance undertaking can steer its asset management such that taxable temporary differences correspond to the tax losses resulting from the equity shock. If the assumption, that insurance undertakings are able to control the reversal of net DTL, was disregarded, undertakings would be required to explicitly demonstrate that the timing of the net DTL corresponds to the utilization of DTA post shock. This would imply that undertakings are required to report hypothetical scenarios in which they will demonstrate that, through the sale or maturity of assets (or the run-off or sale of insurance portfolios), tax losses occur simultaneously with tax profits. Such reportings will be of very little or no added value, because in reality, the management of the insurance undertaking will always be able to steer the occurrence of tax losses and profits through targeted sales or purchases of assets and liabilities.	
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8.5.3.3	**Pull-to-par: paragraph 551** In paragraph 551 of the consultation paper, the following is stated: "Allowing pull-to-par implies that the part of the losses due the credit spread shock does not materialise to the full extent. It would be inconsistent with the credit spread shocks themselves in the calculation of the basic SCR that also do not take account of any pull-to-par." A distinction should be made between the shocks of the BSCR on the one hand and the assumptions used to demonstrate future profitability and the increase in DTA on the other hand. A pull-to-par does not mean that spread shocks do not exist. The assumption of a pull to par could never neutralise the entire spread shock, as the loss-absorbing effect is inevitably capped by the tax rate. Assuming a pull-to-par only means that the spread shock will lead to limited fiscal losses in jurisdictions that tax on a realised basis. The amount of the BSCR is legally fixed by article 207(1) of the Delegated Acts and is not affected by a pull-to-par assumption. Undertakings that use a pull-to-par assumption still recognise that spread shocks affect asset valuations on the Solvency II balance sheet. The essence of a pull-to-par assumption is that these spread shocks, over time, will not lead to fiscal losses. There is indeed ample evidence that spreads are more volatile compared to the actual default experience. It is therefore sound to assume that spread shocks will not fully materialise into fiscal losses.	
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