

Guidelines on look-through approach

Introduction

- 1.1 According to Article 16 of Regulation (EU) No 1094/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (hereinafter "EIOPA Regulation")¹ EIOPA is drafting Guidelines on the look-through approach.
- 1.2 The Guidelines relate to Article 104 and 105 of 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 (hereinafter "Solvency II")².
- 1.3 These Guidelines are addressed to supervisory authorities under Solvency II.
- 1.4 These Guidelines aim at increasing consistency and convergence of professional practice in the application of the look-through approach for all types and sizes of solo undertakings using the standard formula across Member States.
- 1.5 These Guidelines aim at supporting undertakings in calculating their market risk related Solvency Capital Requirements under Solvency II.
- 1.6 Only cases that do not already qualify as risk-mitigation techniques are considered for potential application of the look-through approach. Where insurance or reinsurance undertakings use risk-mitigation techniques the assumption is that the underlying risks are understood and have already been looked-through.
- 1.7 If not defined in these Guidelines the terms have the meaning defined in the legal acts referred to in the introduction.
- 1.8 The Guidelines shall apply from 1 April 2015.

Guideline 1 – Money market funds

- 1.9 Undertakings should apply the look-through approach to money market funds.

Guideline 2 – Number of iterations

- 1.10 Undertakings should perform a sufficient number of iterations of the look-through approach, where appropriate (e.g. where a fund is invested in other funds) to capture all material risk.

Guideline 3 – Investments in real estate

- 1.11 Undertakings should cover the following investments in the property risk sub-module:
 - (a) land, buildings and immovable property rights;

¹ OJ L 331, 15.12.2010, p. 48–83

² OJ L 335, 17.12.2009, p. 1–155

- (b) property investment held for the own use of the undertaking.
- 1.12 For equity investments in a company exclusively engaged in facility management, real estate administration, real estate project development or similar activities, undertakings should apply the equity risk sub-module.
- 1.13 Where undertakings invest in real estate through collective investment undertakings or other investments packaged as funds, they should apply the look-through approach.

Guideline 4 – Data groupings

- 1.14 With reference to the groupings referred to in Article 84 (3) of Commission Delegated Regulation (EU) 2015/35 of 10 October 2014 supplementing Directive 2009/138/EC (hereinafter "Commission Delegated Regulation 2015/35")³, where assets covered in the spread and interest rate risk sub-modules are grouped according to duration bands, undertakings should ensure that the durations assigned to the bands are demonstrably prudent.
- 1.15 Where groupings across different credit quality steps are used, undertakings should ensure that the credit quality steps assigned to the groups are demonstrably prudent.

Guideline 5 – Data groupings and concentration risk

- 1.16 Where in accordance with Article 84 (3) of Commission Delegated Regulation 2015/35, any grouping is applied to the single name exposures of the underlying assets of collective funds for calculating the market risk concentration charge and it cannot be demonstrated that the groups into which the fund is split do not contain any of the same single name exposures, undertakings should assume that all assets for which the actual single name exposure is not identified belong to the same single name exposure.
- 1.17 The above paragraph is not applicable where exposure limits to single name exposures exists according to which the fund is managed.
- 1.18 Undertakings should aggregate exposures to groups referred to in paragraph 1.16 across all collective funds in which they are invested and reconcile the exposures to each group with the exposures of the known single names in their asset portfolio.

Guideline 6 – Indirect exposure to catastrophe risk

- 1.19 When calculating the Solvency Capital Requirement in respect of indirect exposures to catastrophe risks, such as investments in bonds for which repayment is contingent on the non-occurrence of a given catastrophe event, undertakings should take into account any credit and catastrophe exposures.

³ OJ L 12, 17.01.2015, p. 1-797

- 1.20 Catastrophe exposures should be treated in the relevant catastrophe sub-modules as though the underlying catastrophe exposure is directly held by the undertaking.

Guideline 7 – Catastrophe bonds issued by the undertaking

- 1.21 Where an undertaking issues catastrophe bonds which do not meet the requirements for risk-mitigation techniques set out in Articles 208 to 215 of Commission Delegated Regulation 2015/35, their treatment in the standard formula should not result in a capital relief in respect of the catastrophe features of these bonds.
- 1.22 Undertakings should treat these catastrophe bonds in the calculation of the Solvency Capital Requirement as though the repayment schedule was not contingent on the non-occurrence of a catastrophe event.

Guideline 8 – Longevity bonds

- 1.23 Where undertakings buy longevity bonds which do not meet the requirements for risk-mitigation techniques set out in Articles 208 to 215 of Commission Delegated Regulation 2015/35, they should calculate the capital charge in respect of mortality and spread risk as set out in paragraphs 1.24 to 1.28.
- 1.24 The capital charge of the standard formula mortality sub-module should be based on a notional portfolio of term assurance contracts:
 - (a) paying out the given sum on death;
 - (b) based on a representative sample of the reference population underlying the longevity index;
 - (c) where the term of each term assurance contract is equal to the term of the coupon payment.
- 1.25 The notional portfolio should be constructed by undertakings in such a way that under best estimate assumptions the total benefit payments sum to the coupon payable.
- 1.26 The capital charge of the spread risk sub-module should be based on a bond or a loan with the same market value, duration and credit quality step as the longevity instrument.
- 1.27 Where undertakings sell longevity bonds they should calculate the capital charge in respect of the longevity sub-module as though the notional portfolio consists of endowment contracts, paying out the required sum at survival to a given age, which collectively produce cash-flows equivalent to those of the bond.
- 1.28 Undertakings should not consider longevity bonds which do not meet the requirements for risk-mitigation techniques set out in Articles 208 to 215 of Commission Delegated Regulation 2015/35 to increase in value when the stresses in the life underwriting risk module are applied.

Compliance and Reporting Rules

- 1.29 This document contains Guidelines issued under Article 16 of the EIOPA Regulation. In accordance with Article 16(3) of the EIOPA Regulation, Competent Authorities and financial institutions shall make every effort to comply with guidelines and recommendations.
- 1.30 Competent authorities that comply or intend to comply with these Guidelines should incorporate them into their regulatory or supervisory framework in an appropriate manner.
- 1.31 Competent authorities shall confirm to EIOPA whether they comply or intend to comply with these Guidelines, with reasons for non-compliance, within two months after the issuance of the translated versions.
- 1.32 In the absence of a response by this deadline, competent authorities will be considered as non-compliant to the reporting and reported as such.

Final Provision on Reviews

- 1.33 The present Guidelines shall be subject to a review by EIOPA.