

Guidelines on ancillary own funds

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 ancillary own funds.
- 1.2. The Guidelines relate to Articles 89, 90, 93 to 96, 226 and 235 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 and to Articles 62 to 67, 74, 75, 78 and 79 of Commission Delegated Regulation (EU) 2015/35 of 10 October 2014 supplementing Directive 2009/138/EC (hereinafter "Commission Delegated Regulation 2015/35")³.
- 1.3. These Guidelines are addressed to supervisory authorities under Solvency II.
- 1.4. Ancillary own funds are contingent in that they have not been paid in, and are not recognised on the balance sheet. The need for supervisory approval of such items recognises this contingent nature. If, at some undetermined point in the future, the ancillary own funds are called up, then they cease to be contingent and become basic own-fund items represented by assets on the balance sheet.
- 1.5. Article 89 of Solvency II states that ancillary own funds may comprise any legally binding commitment received by undertakings. This might encompass many arrangements that do not fall within the categories of specific ancillary own-fund items referred to in Solvency II as long as they can be called upon to absorb losses.
- 1.6. These Guidelines describe considerations relating to the supervisory authority approval process for ancillary own-fund items, classification of ancillary own-fund items and ongoing satisfaction of criteria for approval.
- 1.7. The ancillary own funds approval process envisages ongoing communication between supervisory authorities and undertakings, including before an undertaking submits a formal application for approval of an ancillary own-fund item. Where the ancillary own-fund item on call would become an Item not on the lists, and therefore two supervisory approvals are needed, such communication should include the procedural approach to be followed regarding this need for two approvals.
- 1.8. Article 226 of Solvency II permits a group to apply for approval of an ancillary own-fund item in respect of an intermediate insurance holding company or an intermediate mixed financial holding company. In such cases these Guidelines apply as though the intermediate insurance holding company or the intermediate mixed financial holding company were an insurance or reinsurance

¹ OJ L 331, 15.12.2010, p. 48–83

² OJ L 335, 17.12.2009, p. 1-155

³ OJ L 12, 17.01.2015, p. 1-797

undertaking. This also applies where a group is headed by an insurance holding company or a mixed financial holding company in accordance with Article 235 of Solvency II.

1.9. For the purpose of these Guidelines, the following definitions have been developed:

- (a) 'Capital instrument' means an instrument which if called up will generate an asset, often in the form of cash, while simultaneously creating corresponding interests in the insurance or reinsurance undertaking in the case of shares, or corresponding subordinated liabilities of the undertaking;
- (b) 'Item not on the lists' means an own-fund item not included in the lists set out in Articles 69, 72 and 76 of Commission Delegated Regulation 2015/35.

1.10. If not defined in these Guidelines, the terms have the meaning defined in the legal acts referred to in the introduction.

1.11. The Guidelines shall apply from 1 April 2015.

Guideline 1 - Approval of ancillary own-fund items which, once called, take the form of an Item not on the lists

1.12. If an ancillary own-fund item once called up would take the form of an Item not on the lists, undertakings should seek approval of the classification of that item, as provided for in Article 79 of Commission Delegated Regulation 2015/35 prior to submitting an application for approval of the ancillary own-fund item.

Guideline 2 - Entering into the contract for an ancillary own-fund item

1.13. Where supervisory approval has been granted on the condition that the contract is entered into, in accordance with Article 7(3) of the EIOPA Draft Implementing Technical Standard with regard to the procedures to be used for granting supervisory approval for the use of ancillary own-fund items⁴, the undertaking should formally conclude the contract no later than 15 working days after the approval has been granted, unless the undertaking has agreed a longer time period in advance in writing with the supervisory authority.

Guideline 3 - Callable on demand

1.14. For the items described in points (a), (b), (c), (d), (f) and (i) of Article 74 of Commission Delegated Regulation 2015/35 to be callable on demand, undertakings should ensure that the call is not:

- (a) contingent on the occurrence of an event or criteria being met;
- (b) subject to the agreement of the counterparty or any third party;

⁴ <https://eiopa.europa.eu/Pages/Supervision/Insurance/draft-implementing-technical-standards-on-the-supervisory-approval-processes-for-solvency-ii.aspx>

- (c) subject to any agreement, arrangement or incentive that means that the undertaking is not permitted or is not likely to call up the item; or
 - (d) subject to any other arrangement or combination of arrangements which has the same effect as points (a) to (c).
- 1.15. With regard to the assessment of future claims by a mutual or mutual-type association with variable contributions for the purposes of Article 90 of Solvency II, supervisory authorities should consider whether there are any impediments to the claims being used to cover losses when they arise, and to the amounts being recovered in a timely manner.

Guideline 4 - Classification of ancillary own-fund items

- 1.16. The supervisory authority should not determine the classification of an ancillary own-fund item based only on the form in which the item is presented or described. The supervisory authority's assessment and the classification of the ancillary own-fund item should depend upon the item's economic substance and the extent to which it would satisfy the characteristics and features set out in Articles 93 to 96 of Solvency II and Articles 74, 75, and 78 of Commission Delegated Regulation 2015/35.
- 1.17. Where ancillary own-fund items become Capital instruments on call, undertakings should classify the ancillary own-fund item by assessing the features of that Capital instrument and determine to which tier the Capital instrument would belong if called up.
- 1.18. Undertakings should ensure that where an ancillary own-fund item on being called results in the receipt of cash or other assets, that basic own-fund item is only treated as a contribution where it does not give rise to a corresponding Capital instrument or liability, whether contingent or not, of the undertaking.
- 1.19. Undertakings should treat items as contributions:
- (a) when they are in the form of an unconditional gift, or donation of own funds;
 - (b) whether they are from a parent undertaking, or any other party, or in the form of supplementary contributions from members of mutual or mutual-type undertakings;
 - (c) regardless of the treatment of the item for accounting purposes, as contributing to profit or loss or contributing directly to reserves.
- 1.20. Since the balance sheet treatment of contributions which satisfy the necessary features and characteristics used to classify own funds into tiers, is an increase in the undertaking's assets with a corresponding increase in the reconciliation reserve, and since the contribution does not give rise to any Capital instrument or liability or any other basic own-fund item, undertakings should classify the item as Tier 2 ancillary own funds.
- 1.21. Undertakings should classify contractual arrangements which when called up meet the undertaking's liabilities by indemnifying third-parties, in the same manner as contributions if they:

- (a) generate an asset for a third-party creditor of the undertaking;
 - (b) do not create corresponding liabilities for the undertaking.
- 1.22. Undertakings should treat contracts of indemnity, which oblige a third-party indemnifier to pay sums to the undertaking's creditor without obliging the undertaking to repay such sums to the indemnifier, as ancillary own-fund items, subject to approval by the supervisory authority.
- 1.23. Supervisory authorities should classify ancillary own-fund items which on call do not become Capital instruments, contributions or arrangements, but which meet an undertaking's liabilities, by considering the features of whatever the ancillary own-fund item delivers on call.

Guideline 5 - Ongoing satisfaction of the criteria

- 1.24. Undertakings should discuss with the supervisory authority as early as possible, if they have reason to believe that a material change in the loss-absorbency of an ancillary own-fund item is imminent or likely.

Guideline 6 - Assessment of the ongoing satisfaction of the criteria

- 1.25. When considering whether the amount ascribed to an ancillary own-fund item continues to reflect its loss-absorbency, supervisory authorities should consider using information obtained from other sources in addition to the information received from undertakings in accordance with Article 62(1)(d) of Commission Delegated Regulation 2015/35, including but not limited to:
- (a) information obtained through on-site inspections;
 - (b) ad-hoc information received or obtained as part of the supervisory review process;
 - (c) information provided by other supervisory authorities within the college of supervisors, where applicable.

Compliance and Reporting Rules

- 1.26. 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.
- 1.27. Competent authorities that comply or intend to comply with these Guidelines should incorporate them into their regulatory or supervisory framework in an appropriate manner.
- 1.28. 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.
- 1.29. 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

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