

Guidelines on treatment of related undertakings, including participations

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 treatment of related undertakings, including participations.
- 1.2. The Guidelines relate to Articles 92(1)(b) and 111(1)(m) 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 as well as to Articles 68, 168 and 171, without prejudice to Article 84 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. The purpose of these Guidelines is to provide guidance on the identification and the treatment of related undertakings and participations to ensure a consistent approach across Member States.
- 1.5. For the purpose of these Guidelines the participating undertaking is the undertaking which is calculating its solvency position. The term related undertaking refers to any related undertaking of that participating undertaking. The term participation is used to denote one type of related undertaking. Appendix A of the Final Report provides an overview of the different terms used in Solvency II when speaking about the relationship between two or more undertakings.
- 1.6. These Guidelines cover the treatment of all related undertakings in the calculation of the Solvency Capital Requirement (hereinafter "SCR") and include guidance on the determination of own funds in the case of participations in financial and credit institutions. The meaning of financial and credit institutions is explained in Appendix B of the Final Report.
- 1.7. The Guidelines follow a holistic approach. They describe first the identification of different types of related undertakings, including participations. They then cover the treatment of the different types of related undertakings, specifically participations in financial and credit institutions and strategic participations. Finally, they include guidance on the treatment of related undertakings in the standard formula and in internal models to calculate the SCR.
- 1.8. Where these Guidelines refer to the valuation or value of a related undertaking, reference should be made to Article 13 of Commission Delegated Regulation 2015/35.

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

- 1.9. The Guidelines concern the treatment of related undertakings including participations on a solo basis. In most cases the identification of a related undertaking will be the same both from the perspective of the participating undertaking as an individual entity and for group purposes. However, in certain situations there will be differences: The business of the related undertaking may be such that the participating undertaking and related undertaking are not subject to group supervision according to Article 213 of Solvency II. In addition, there may be the case where a number of entities within a group hold voting rights or capital in an undertaking that when combined together, amount to 20% or more of the undertaking's voting rights or capital. Consequently, such an undertaking would be identified as a related undertaking at group level. However, if the holding of each individual entity within the group is lower than 20%, the undertaking would not be identified as a related undertaking by any of those entities within the group at individual entity level.
- 1.10. In certain circumstances the individual entity provisions for related undertakings are used to calculate the contribution of those undertakings to the group SCR. These circumstances are set out in Commission Delegated Regulation 2015/35 and EIOPA's Guidelines on group solvency calculation.
- 1.11. Appendix C of the Final Report provides, in the form of a decision tree, a methodology for the treatment of all types of related undertakings. Additional analysis and calculations will be necessary for financial and credit participations held indirectly as set out in Guideline 4 and Guideline 7. In some cases, the treatment of holdings is identical to the treatment that would result from applying the standard formula where no participation exists.
- 1.12. If not defined in these Guidelines the terms have the meaning defined in the legal acts referred to in the introduction.
- 1.13. The Guidelines shall apply from 1 April 2015.

Guideline 1 - Identification

- 1.14. Participating undertakings should identify their related undertakings and participations based on an assessment from their perspective as an individual entity.
- 1.15. When identifying a related undertaking based on share ownership, directly or by way of control, participating undertakings should determine:
 - (a) their holding of voting rights as a percentage of an undertaking's voting rights;
 - (b) their holding of all classes of share capital issued by an undertaking as a percentage of that undertaking's issued share capital, regardless of voting rights.

Where (a) or (b) are 20% or higher, participating undertakings should treat their investment in the undertaking as a participation.

Where the participation is in an insurance or reinsurance undertaking subject to Solvency II, the assessments under (a) will generally relate to paid-in ordinary

share capital referred to in Article 69(a)(i) of Commission Delegated Regulation 2015/35, and under (b) to paid-in ordinary share capital and paid-in preference shares referred to in Article 69(a)(v) of Commission Delegated Regulation 2015/35.

- 1.16. Participating undertakings should ensure that they are able to identify the effect of changes in the share capital of related undertakings on the assessment described in the preceding paragraph each time the participating undertaking calculates its SCR in accordance with Article 102 of Solvency II.
- 1.17. When identifying a related undertaking pursuant to Article 212(2) of Solvency II on the basis that the participating undertaking can exert a dominant or significant influence over another undertaking, supervisory authorities should consider:
 - (a) current shareholdings of the participating undertaking in the undertaking and potential increases due to the holding of options, warrants or similar instruments;
 - (b) membership rights of the participating undertaking in a mutual or mutual-type undertaking and potential increases in such rights;
 - (c) representation from the participating undertaking on the administrative, management or supervisory body of the undertaking;
 - (d) involvement of the participating undertaking in policy-making processes of the undertaking, including decision-making about dividends or other distributions;
 - (e) material transactions between the participating undertaking and the undertaking;
 - (f) interchange of persons effectively running the participating undertaking and the undertaking;
 - (g) provision of essential technical information to the undertaking;
 - (h) management of the participating undertaking and undertaking on a unified basis.

Supervisory authorities should consider any initial assessment by the participating undertaking in accordance with points (a) to (h) of this paragraph.

Guideline 2 - Identification of participations in financial and credit institutions

- 1.18. Participating undertakings should treat a related undertaking as a financial or credit institution, where it is an institution listed or described in accordance with Article 4(1) and (5) of Directive 2013/36/EU or with Article 4(1) of Directive 2004/39/EC. These descriptions cover any institution which performs the functions or carries out the business described pursuant to those Articles, notwithstanding that the institution may not be subject to those Directives.
- 1.19. Participating undertakings should ensure that any participation in a financial or credit institution where voting rights or capital are held indirectly is treated in

the same way as a participation in a financial or credit institution where voting rights or capital are held directly.

Guideline 3 - Identification of a strategic participation

1.20. Participating undertakings should identify strategic participations in accordance with Article 171 of Commission Delegated Regulation 2015/35 as follows:

- (a) participating undertakings using the standard formula to calculate their SCR should identify strategic participations regardless of whether their participation is in an insurance or reinsurance undertaking, in a financial or credit institution or in any other related undertaking;
- (b) participating undertakings using an internal model to calculate their SCR need to identify strategic participations in financial and credit institutions only for the purpose of assessing whether Article 68(3) of Commission Delegated Regulation 2015/35 applies.

1.21. For the purpose of demonstrating their compliance with the requirements of Article 171 of Commission Delegated Regulation 2015/35, participating undertakings should not divide a participation into different parts, treating some parts as strategic and others not. Where a particular participation has been identified as strategic:

- (a) in the case of a participation in a financial or credit institution, all investments in its own funds are strategic;
- (b) in the case of any other related undertaking, all equity investments in the participation are strategic.

1.22. In demonstrating that the value of the equity investment is likely to be materially less volatile, in accordance with Article 171(a) of Commission Delegated Regulation 2015/35, participating undertakings should ensure that:

- (a) consistent and appropriate valuations are applied over time both to the participation and to the other equities selected as a basis of comparison;
- (b) they consider the impact of their influence on the participation's value.

1.23. In demonstrating that the nature of the investment is strategic, in accordance with Article 171(b)(i) to (iii) of Commission Delegated Regulation 2015/35, participating undertakings should:

- (a) indicate the period for which the strategy of holding the participation is intended to apply;
- (b) consider the impact of market conditions on the main policies;
- (c) identify any significant factors affecting, or constraints on, the participating undertaking's ability to maintain its strategy and how these could or would be mitigated.

- 1.24. In demonstrating the existence of a durable link, in accordance with Article 171(b)(iv) of Commission Delegated Regulation 2015/35, participating undertakings should consider the following criteria:
- (a) whether a stable relationship between the two undertakings exists over time;
 - (b) whether that stable relationship results in a close economic bond, the sharing of risks and benefits between the undertakings or exposure to risks from one to the other;
 - (c) the form of the relationship between the two undertakings, which may include ownership, joint products or distribution lines, cross-selling, the creation of joint ventures or other long term operational or financial links.
- 1.25. In accordance with Article 171(b)(v) of Commission Delegated Regulation 2015/35, a participating undertaking that is part of a group should regard the main policies guiding or limiting the actions of the group as those defined by the ultimate parent undertaking or, if different, by the undertaking which sets the main policies for the group as a whole.
- 1.26. Participating undertakings should document their consideration of the matters set out in Article 171 of Commission Delegated Regulation 2015/35 and paragraphs 1.21 to 1.25, including any other relevant factors, together with relevant supporting material.

Guideline 4 - Scope of calculations for Article 68 of Commission Delegated Regulation 2015/35

- 1.27. When determining the value of participations in financial and credit institutions for the purposes of Article 68 of Commission Delegated Regulation 2015/35, participating undertakings should include holdings of equity and any other own-fund items, whether held directly or indirectly.
- 1.28. Participating undertakings should apply the following approaches:
- (a) for direct holdings, the value of participations in financial and credit institutions, as determined by the participating undertaking in accordance with Solvency II valuation principles, should be used for the purposes of Article 68 of Commission Delegated Regulation 2015/35 as set out in Guideline 5;
 - (b) participations in financial and credit institutions, held indirectly via another participation in a financial or credit institution should not be considered under Article 68 of Commission Delegated Regulation 2015/35, as their value should already have been included in the value of the directly-held participation in a financial or credit institution in accordance with point (a);
 - (c) a deduction for a participation in a financial or credit institution held indirectly should only arise where related undertakings between the

participating undertaking and the financial and credit participation are other than financial and credit participations;

- (d) for other indirect holdings in a financial or credit institution the value of the participation as determined by the related undertaking in accordance with Article 13 of Commission Delegated Regulation 2015/35 should be used for the purposes of Article 68 of Commission Delegated Regulation 2015/35;
- (e) the values used for Article 68 of Commission Delegated Regulation 2015/35 purposes should represent the participating undertaking's proportional ownership, held directly and indirectly, of the participation in the financial or credit institution.

Guideline 5 - Calculations for the purpose of Article 68 of Commission Delegated Regulation 2015/35

- 1.29. In calculating 10% of the items included in Article 69(a)(i), (ii), (iv) and (vi) of Commission Delegated Regulation 2015/35 for the purposes of Article 68 of Commission Delegated Regulation 2015/35, participating undertakings should use the amount of basic own-fund items before any deduction pursuant to Article 68 of Commission Delegated Regulation 2015/35 in respect of participations in financial and credit institutions.
- 1.30. Where the value of all participations in financial and credit institutions, other than participations referred to in Article 68(1) of Commission Delegated Regulation 2015/35, does not exceed 10% of items included in Article 69(a)(i), (ii), (iv) and (vi) of Commission Delegated Regulation 2015/35 for the purposes of Article 68(2) of Commission Delegated Regulation 2015/35, then no deduction takes place and Guideline 8 or 9 apply.
- 1.31. Participating undertakings should only apply Article 68(3) of Commission Delegated Regulation 2015/35 in the cases where:
 - (a) they have demonstrated in accordance with Guideline 3 that the participation meets the criteria for a strategic participation;
 - (b) the participating undertaking and the participation are included in calculations on the basis of method 1 in accordance with Directive 2002/87/EC for the financial conglomerate to which they belong or on the basis of method 1 under Solvency II.

Guideline 6 - Deductions in respect of participations in financial and credit institutions

- 1.32. Where deductions in accordance with Article 68(1) and (2) of Commission Delegated Regulation 2015/35 cannot be made from the corresponding tier as set out in Article 68 (5) of Commission Delegated Regulation 2015/35, undertakings should adopt the following approaches:
 - (a) where the items to be deducted are not classified into the tiers set out in Article 68(5) of Commission Delegated Regulation 2015/35, all

deductions should be made from the amount of items included in Article 69(a)(i), (ii), (iv) and (vi) of Commission Delegated Regulation 2015/35;

- (b) where the amount of the deduction exceeds the amount from which it is required to be deducted in accordance with Article 68(5) of Commission Delegated Regulation 2015/35, the excess should be deducted as follows:
 - (i) holdings of Additional Tier 1 instruments in excess of items included in Article 69(a)(iii), (v) and (b) of Commission Delegated Regulation 2015/35 are deducted from items included in Article 69(a)(i), (ii), (iv) and (vi) of Commission Delegated Regulation 2015/35;
 - (ii) holdings of Tier 2 instruments in excess of basic own funds included in Article 72 of Commission Delegated Regulation 2015/35 are deducted first from items included in Article 69(a)(iii), (v) and (b) of Commission Delegated Regulation 2015/35, and then from items included in Article 69(a)(i), (ii), (iv) and (vi) of Commission Delegated Regulation 2015/35 until the deduction is made in full.

Guideline 7 - Adjustments due to deductions of indirectly-held participations in financial and credit institutions

- 1.33. Where a deduction of the value of a participation in a financial or credit institution held indirectly is required, in full or in part, in accordance with Article 68 of Commission Delegated Regulation 2015/35, participating undertakings should, only for the purposes of calculating the SCR:
- (a) reduce, by the amount of that deduction, the value of the directly-held related undertaking, which is an asset of the participating undertaking, through which the participation in the financial or credit institution is held indirectly;
 - (b) for the adjustment described in point (a), follow the approach set out in Article 68(5) of Commission Delegated Regulation 2015/35 and in Guideline 6.

Guideline 8 - Application of the standard formula to related undertakings

- 1.34. This Guideline applies to participating undertakings using the standard formula to calculate the SCR in respect of the risks arising from related undertakings held directly by the participating undertaking.
- 1.35. Where a participating undertaking holds as assets own-fund items of a related undertaking and their value is not deducted in full, or at all, from the participating undertaking's own funds as a result of applying Article 68 of Commission Delegated Regulation 2015/35, risk charges for the remaining value of those holdings should be calculated in accordance with the standard formula.

- 1.36. The participating undertaking should apply the standard formula as follows:
- (a) holdings in ordinary or preference share capital of the related undertaking should be treated as equities applying the equity risk sub-module as appropriate;
 - (b) holdings in subordinated liabilities issued by the related undertaking should be treated as financial instruments taking account of contractual terms and applying market stresses as appropriate, including the interest rate, spread, currency, concentration and other risk sub-modules as appropriate;
 - (c) any holdings of the above which exhibit both equity and bond features should be dealt with in accordance with Guideline 5 of the Guidelines on the Treatment of market and counterparty risk exposures in the standard formula.

Guideline 9 - Application of internal models to related undertakings

- 1.37. This Guideline applies to participating undertakings using a full or partial internal model to calculate the SCR in respect of the risks arising from related undertakings.
- 1.38. Where a participating undertaking holds as assets own-fund items of a related undertaking and their value is not deducted in full, or at all, from the participating undertaking's own funds as a result of applying Article 68 of Commission Delegated Regulation 2015/35, the risks arising from the remaining value of those holdings should be captured as part of the internal model.
- 1.39. The participating undertaking should cover in the internal model all material quantifiable risks arising from its related undertakings, taking account of exposures to the related undertakings including holdings of equity and subordinated liabilities. Relevant measures of these risks should be reflected in the model.
- 1.40. Where a participating undertaking performs the SCR calculation at individual entity level for a participation or related undertaking in a manner which takes account of risks to the value of the underlying assets and liabilities of that related undertaking, it should ensure this is an appropriate calculation at individual entity level, and should not replace that calculation by a consolidated calculation as though the participating undertaking and its related undertaking were a Solvency II group.

Compliance and Reporting Rules

- 1.41. 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.

- 1.42. Competent authorities that comply or intend to comply with these Guidelines should incorporate them into their regulatory or supervisory framework in an appropriate manner.
- 1.43. 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.
- 1.44. 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

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