

## **Review of pension funds' assets and insurance undertakings' balance sheets in Bulgaria: Follow up actions**

### **I) Background**

The Terms of Reference for the Bulgarian Balance Sheet Review (BSR) in the insurance sector and Asset Review (AR) in the Pension Funds Sector states that the Steering Committee (SC) will approve by 31 January 2016 a proposal and submit it to the Financial Supervision Commission (FSC) Board on:

#### *Insurance's sector*

- the conditions and criteria based on which the results of the BSR for insurance's sector will raise supervisory actions including in terms of capital adequacy in regards to the insurance undertakings;
- the expected deadlines for the undertakings to comply with the required actions;
- the follow-up on the undertakings' compliance with the required actions.

#### *Pension Funds' sector*

- the conditions and criteria based on which the results of the review for the pension funds sector will raise supervisory actions;
- the expected deadlines for the companies to comply with the required actions;
- the follow-up on the companies' compliance with the required actions.

Based on the proposal of the SC, the FSC Board will make a decision on the above conditions, criteria and required actions and make them public by February 15, 2016. Additional supervisory actions can be applied in line with the local legal and regulatory framework.

### **II) Rationale for follow up actions**

In the framework of the enhanced economic policies coordination in the European Union (EU), the Council of Ministers adopted in May 2015 the Update of the National Reform Program (NRP) which presents the Government's policy commitments including on the non-banking financial sector. In addition on August 14, 2015 in State Gazette 62 was promulgated the Law on Recovery and Resolution of Credit Institutions and Investment Firms (LRRCIF). Paragraph 10 of the Transitional and Final provisions of the said Law provides for the tasks which the FSC must accomplish in cooperation with the European Supervisory Authorities.

Accordingly, the FSC will take actions towards strengthening the supervision and legislation of the pension funds and insurance sectors (section 2.2 of the NRP).

The reviews will provide clarity on the real situation of the assets of the participating pension funds and balance sheets of the participating insurance undertakings and their risks.

Where needed, the participating entities need to take action to restore or improve the financial position in a timely manner and improve their risk management. This ensures the stability of the system and confidence of all participants including policy holders.

### **III) Follow up supervisory actions based on the results of the Balance sheet review for the Insurance sector**

Based on the results of the BSR and the recalculation/analyze of prudential indicators, which include reconsideration of an appropriate level of technical provisions as well as assets, the participating insurance and reinsurance undertakings (hereinafter insurance undertakings) as well as insurance groups and sub-groups (hereinafter groups) will be grouped and will be subject to differentiated remedial follow up actions. The remedial actions required by FSC to be implemented by the participant insurance undertakings and insurance groups depend on the magnitude of the capital shortfall revealed by the BSR without prejudice of any adjustment following measures taken after the cut-off date.

#### **1. Grouping of insurance undertakings and groups**

Insurance undertakings and groups will be grouped as follows:

##### **A. Individual level assessment**

- 1) **Group A.1 insurance undertakings:** insurance undertakings that based on the outcome of the BSR do not hold sufficient eligible basic own funds to cover the Minimum Capital Requirement (MCR) and do not comply with the required solvency margin<sup>1</sup> on 31 December 2015 (or, if referring to undertakings exempt from the scope of Solvency II under article 4 of the Solvency II Directive, insurance undertakings breaching the prudential guarantee fund<sup>2</sup>);
- 2) **Group A.2 insurance undertakings:** insurance undertakings that based on the outcome of the BSR do not hold sufficient eligible basic own funds to cover the MCR but comply with the required solvency margin<sup>1</sup> on 31 December 2015;
- 3) **Group A.3 insurance undertakings:** insurance undertakings that based on the outcome of the BSR do not hold sufficient eligible own funds to cover the Solvency Capital Requirement (SCR) and do not comply with the required solvency margin<sup>3</sup> on 31 December 2015 (or, if referring to undertakings exempt from the scope of Solvency II under article 4 of the Solvency II Directive, insurance undertakings breaching the solvency margin and/or not complying with the rules applicable to the coverage of technical provisions by admissible assets);
- 4) **Group A.4 insurance undertakings:** insurance undertakings that based on the outcome of the BSR do not hold sufficient eligible own funds to cover the SCR but comply with the required solvency margin<sup>2</sup> on 31 December 2015.

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<sup>1</sup> Referred to in Article 28 of Directive 2002/83/EC, Article 16a of Directive 73/239/EEC or Article 37, 38 or 39 of Directive 2005/68/EC.

<sup>2</sup> Guarantee Fund as foreseen in article 29 of Directive 2002/83/EC of the European Parliament and of the Council of 5 November 2002 (recast Life Directive) and in article 17 of the First Council Directive 73/239/EEC, of 24 July 1973 (Non-Life Directive), implemented in national regulation.

<sup>3</sup> Referred to in Article 16a of Directive 73/239/EEC, Article 28 of Directive 2002/83/EC, or Article 37, 38 or 39 of Directive 2005/68/EC.

## **B. Group level assessment**

- 1) **Group B.1 insurance undertakings:** groups that based on the outcome of the BSR do not hold sufficient eligible basic own funds to cover the Minimum Capital Requirement at group level (hereinafter group SCR floor)<sup>4</sup>;
- 2) **Group B.2 insurance undertakings:** groups that based on the outcome of the BSR do not hold sufficient eligible own funds to cover the group Solvency Capital Requirement (group SCR) and do not comply with the Adjusted Solvency<sup>5</sup> on 31 December 2015;
- 3) **Group B.3 insurance undertakings:** groups that based on the outcome of the BSR do not hold sufficient eligible own funds to cover the group SCR but comply with the Adjusted Solvency<sup>3</sup> on 31 December 2015.

**Group C. insurance undertakings:** insurance undertakings and groups that based on the outcome of the BSR achieve the MCR, SCR, group SCR floor and group SCR (or, if referring to undertakings exempt from the scope of Solvency II under article 4 of the Solvency II Directive, insurance undertakings complying with the Solvency I prudential indicators).

### **2. Deadlines for the submission of realistic short-term finance schemes and recovery plans and for their approval**

**Groups A. 1, A. 2 and B. 1. insurance undertakings:** FSC shall require the undertaking to submit a short-term realistic finance scheme for the implementation of remedial actions within 30 calendar days following the publication of the results of the BSR on FSC's website.

**Groups A. 3, A. 4, B. 2 and B.3 insurance undertakings:** FSC shall require the undertaking to submit a realistic recovery plan for the implementation of remedial actions within 60 calendar days following the publication of the results of the BSR on FSC's website.

**All undertakings (Groups A. and B.)** should further explain how they will address the risks identified by the BSR and how this impacts the risk management.

FSC will analyze the plans received within 30 calendar days from the plan's submission date, where adequate propose changes, and approve it.

In case the participating undertakings are already in the process of implementing approved action/financial recovery plan submitted to FSC before the date of publication of the results of the BSR and those results indicate the need for additional own funds, the undertaking must assess the sufficiency of the actions/financial recovery plan and update it where insufficient. The respective undertakings will have 30 calendar days following the publication of the results of the BSR to report to FSC the plan's update to be approved by FSC within the above referred deadline.

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<sup>4</sup>Foreseen in article 230 (2) of Directive 2009/138/EC of 25 November 2009 (hereinafter Solvency II Directive).

<sup>5</sup>Referred to in Article 9 of Directive 98/78/EC.

### **3. Deadlines for progress reports and for restoring compliance with prudential indicators/correct deficiencies**

**Groups A.1 and B.1 insurance undertakings** will be requested to submit monthly, within 3 weeks after the end of the reference month, until the financial situation is restored, a progress report to FSC setting out the measures taken and the progress made to ensure compliance with the MCR and group SCR floor levels, (or, if referring to undertakings exempt from the scope of Solvency II under article 4 of the Solvency II Directive, the progress made to ensure compliance with the prudential guarantee fund) in 3 months following the publication of the results of the BSR on FSC's website.

**Group A. 2 insurance undertakings** will be requested to submit monthly, within 3 weeks after the end of the reference month, until the financial situation is restored, a progress report to FSC setting out the measures taken and the progress made to ensure compliance with the MCR the latest by end December 2016.

**Groups A.3 and B.2 insurance undertakings** will be requested to submit every 3 months, within 3 weeks after the end of the reference month, until the financial situation is restored, a progress report to FSC setting out the measures taken and the progress made to ensure compliance with the SCR and group SCR levels (or, if referring to undertakings exempt from the scope of Solvency II under article 4 of the Solvency II Directive, the measures taken and the progress made to ensure compliance the solvency margin and/or the rules applicable to the coverage of technical provisions by admissible assets) in 6 months following the publication of the results of the BSR on FSC's website.

**Groups A.4 and B.3 insurance undertakings** will be requested to submit every 3 months, within 3 weeks after the end of the reference month, until the financial situation is restored, a progress report to FSC setting out the measures taken and the progress made to ensure compliance with the SCR and group SCR levels the latest by end December 2017.

**Group C insurance undertakings:** where are identified by the independent external reviewers vulnerabilities or deficiencies those undertakings will submit, within 30 calendar days following the publication of the results of the BSR on FSC's website, plans aimed at correcting those until end December 2016.

In case undertakings fall in more than one group, FSC may allow the submission of only one plan covering the overall measures to address the different deficiencies.

### **4. Supervisory measures**

Where:

- 1) the short-term finance scheme or recovery plan are not considered realistic or sufficient by FSC within the time limit set above (i.e. 30 calendar days); or
- 2) there is no significant progress showed following FSC's assessment of the monthly and quarterly progress reports in restoring the MCR and/or SCR (or Solvency I prudential indicators if referring to undertakings exempt from the scope of Solvency II under article 4 of the Solvency II Directive); or

- 3) the undertaking or group fails to restore the MCR and/or SCR (or Solvency I prudential indicators if referring to undertakings exempt from the scope of Solvency II under article 4 of the Solvency II Directive) at the end of the established deadlines,

FSC shall within 4 weeks (from the submission date of the short-term finance scheme or recovery plan or the monthly and quarterly progress reports or the established deadline to restore the MCR and/or SCR (or Solvency I prudential indicators if referring to undertakings exempt from the scope of Solvency II under article 4 of the Solvency II Directive)), take all measures necessary to safeguard the interest of policyholders, including, and without prejudice of other measures foreseen in the law that may be applied alongside, the following:

SCR breach (or breach of the solvency margin/covering of technical provisions by admissible assets if referring to undertakings exempt from the scope of Solvency II under article 4 of the Solvency II Directive)

- measures aimed at reducing the risk profile such as requiring the undertaking to refrain from underwriting new risks or to renew pending contracts in certain lines of business, or requiring the undertaking to change its asset portfolio with the aim of reducing the market and credit risk;
- measures aimed at limiting or preventing a reduction of financial resources such as setting limitations on dividend payments and prohibiting the free disposal of assets;
- imposing, together with other measures, additional reporting requirements to enable improved monitoring.

MCR breach (or breach of the prudential guarantee fund if referring to undertakings exempt from the scope of Solvency II under article 4 of the Solvency II Directive)

- restrict free disposal assets;
- withdrawal of authorization.

#### **IV) Follow up supervisory actions based on the results of the asset review for the Pension sector**

Based on the results of the assets review (including the review of the pension funds' risks) the FSC will:

- require the pension companies for which there was an adjustment of the fund assets' value following the AR, to correct the value of one unit and to publish information about the mistake in the calculation in the value of one unit of the pension fund on its website in accordance with the provisions of Art. 21a and Art. 22 of Ordinance No 9 of the FSC;
- to analyse on the basis of the results from the assets review whether there are necessary additional changes in the legal framework and to inform the SC about the outcome of analysis by 15 October 2016;
- to propose additional changes in the legal framework, if necessary, by the end of 2016;
- apply coercive administrative measures and/or administrative penalties in accordance with the legislation in force in case there have been established violations of the legal framework, after conducting, if necessary, additional inspections.

Furthermore, based on the outcome of the review, including the findings about the risks, all pension companies should be required to send to FSC information, within 20 calendar days following the publication of the results of the AR on FSC's website, how the outcome of the review impacts their risk management strategies.

FSC will analyze that information within 30calendar days from the submission date and make comments where appropriate. This analysis should update the FSC supervisory work plan including in regards to the performance of on-site inspections on the pension funds' risk management.

**V) Information to EIOPA, SC observersand other Member States**

1) FSC shall provide EIOPA and SC observers with an overview of the follow-up made following the initial assessments of the short-term finance scheme and recovery plans as well as the progress reports within 2 weeks of the recovery plan/progress report's submission date. Where more severe actions are taken by FSC to safeguard the interest of policyholders those shall be immediately communicated;

2) By the end of 2016 FSC shall provide EIOPA and SC observes with an overview of the measures taken by the Pension companies and the measures imposed by the supervisory authority;

3) FSC shall provide EIOPA and SC observers with an overview on how the outcome of the review impacted the risk management strategies in the Pension Funds' Sector and its effect on the FSC supervisory work plan as soon as that analysis is available;

4) FSC shall inform within 3 days from the measure's datethe relevant Group supervisors and concerned host Members States about the measures taken and any deviations from planned progress.

5) FSC shall provide EIOPA and SC observers 3 months after 2017 year end (2 years after implementation of Solvency II) with a report informing about the overall state of play of the Bulgarian market following the surveillance and actions taken.

The information will be provided by the FSC without violation of Art 24-25 of the Financial Supervision Commission Act regarding the professional secrecy.