Solvency II

A POSITION PAPER OF THE ACTUARIAL ASSOCIATION OF EUROPE

ON THE INDEPENDENT REVIEW OF SOLVENCY II REPORTS

Foreword

The Actuarial Association of Europe ("AAE") believes that independent review of the Solvency and Financial Condition Report ("SFCR") is an important part of the overall governance framework for Solvency II. A series of checks and balances - and associated public disclosures – is needed to give the public confidence in the financial system in Europe, and in particular in insurers within the scope of Solvency II.

This Position Paper is intended to promote a discussion with Solvency II report stakeholders - in the widest sense - to agree on the best possible way to carry out the necessary independent review work.

The AAE notes that the SFCR (and the independent review thereof) is one component - there are also "checks and balances" between key functions (such as risk management, actuarial, compliance and internal audit), which are nevertheless not disclosed, and in the formalised process of model validation (where an approved internal model is used to determine the SCR). The AAE believes it is important that an effective, efficient and proportionate holistic view is taken so that there are no material gaps, overlaps, interference or unnecessary expense within the overall framework.

The AAE is ready to work with stakeholders to establish clear links between the independent review and the actuary who performs such a review.

The AAE is ready to offer its help to draw up further guidelines or standards to set a clear division of responsibilities between the supervisor role and the independent review role.

Michael Renz
Chairperson of the AAE

Content

1. Introduction

Financial reporting and solvency reporting serve different purposes and solvency reporting is not intended to replace the usual financial reports of an insurance undertaking in any way.

With respect to solvency reporting, EIOPA states[1] that public disclosure requirements are one of the cornerstones of Solvency II and convergence should be achieved in order to guarantee a level playing field and assist comparability.

The AAE believes that all publicly disclosed information and the bases of such information, including underlying methodologies, assumptions and expert judgments applied, and the implications of this information for the potential future development of the solvency and capital position of the undertaking, should be independently[2] reviewed[3] and assessed.

As a consequence the independent review should be carried out by persons who have knowledge of actuarial and financial mathematics, commensurate with the nature, scale and complexity of the risks inherent in the business of the insurance or reinsurance undertaking, and who are able to demonstrate their relevant experience with applicable professional and other standards. Fully qualified actuaries[4] who have the required knowledge and experience, and are subject to actuarial standards, are well suited to assess publicly disclosed quantitative information and all associated qualitative information.

The AAE believes, subject to full consideration of costs and benefits, that an independent actuarial review is desirable for the annual SFCR public disclosure. The disclosure should include the basis of the review, by whom it was performed and the opinion of the reviewer in order to assure the public and the supervisor that the methods, assumptions and expert judgments applied in the process are appropriate.

In the context of the balance of the costs and benefits and taking into account the significant differences between the prudential accounts and the statutory accounts, the AAE believes that a targeted independent actuarial review is more appropriate than an extension of the statutory audit of the financial statements.

The AAE believes that the costs involved in the independent review of Solvency II reports should and can be limited as substantial parts of the reports are prepared, at least annually, by professionals - including actuaries – to comply with their professional codes of conduct.

The AAE believes that an independent review will reinforce the underlying principles of Solvency II and will be of great value to all stakeholders and users of financial information.

[1] CEIOPS L2 Advice: Supervisory Reporting and Public Disclosure Requirements, CEIOPS-DOC-50/09

[2] Independent: "Not influenced by others in one's opinion or conduct; thinking or acting for oneself", Shorter Oxford English Dictionnary Sixth Edition, Oxford University Press 2002, 2007.

[3] A review to "appraise the quality of the work performed and conclusions reached by others".

[4] A special class of membership of all full member associations of the AAE.
Fully qualified actuaries are subject to the highest educational requirements.

2. Solvency II framework

The Solvency II legislation introduces a new assessment framework which will apply to most (re)insurers in Europe as of 1 January 2016. The most important objective of Solvency II is to provide better protection of policyholders, and to provide a stimulus and a reward for effective risk management in the insurance industry, linked to specific capital requirements. It is envisaged that this objective will be achieved through supervisory assessment and public disclosure.

The Solvency II framework aims at greater levels of transparency for supervisors and for the public. Supervisors will be served with reports of a more confidential nature (as these include the company's strategy) and the public will get its information from the Solvency and Financial Condition Report ("SFCR"). The latter will increase the level of public disclosure required by undertakings. The SFCR will contain key quantitative and qualitative information on risks to which the undertaking is exposed.

Most importantly, the report will contain the undertaking's view of the future. On the basis of that information the general public and the financial markets in general can gain an understanding of the risk profile and risk assessment of the undertaking and the expected development of its capital position.

Based on the available information of all insurance undertakings subject to Solvency II and comparing these, the general public and, indeed, the market as a whole, may draw conclusions on the financial position of such undertakings. And as we know that is one of the main goals of Solvency II.

3. Financial Reporting and Solvency Reporting

Financial reporting and solvency reporting serve different purposes and solvency reporting is not intended to replace the usual financial reports of an insurance undertaking in any way.

Financial Reporting

A financial report is a formal record of the financial activities of a business, person, or other entity assessed on the basis of a consistent accounting framework (such as the IFRSs, or some of the national GAAPs). Relevant financial information is presented in a structured manner and in a form easy to understand.

They typically include basic financial statements, accompanied by a management report and analysis and include::

1. **Statement of financial position**: also referred to as a balance sheet, reports on a company's assets, liabilities, and ownership equity at a given point in time.
2. **Statement of comprehensive income**: reports on a company's income, expenses, and profits over a period of time. A profit and loss statement provides information on the operation of the enterprise. These include sales and expenses incurred during the processing state.
3. **Statement of cash flows**: reports on a company's cash flow activities, particularly its operating, investing and financing activities.

Financial reporting typically serves financial stakeholders like shareholders, investors and rating agencies, informing them about the profitability and clarifying the financial condition on an on-going basis.

It is important to note that financial reporting gives information at a given point in time and over a period of time[5]. Its purpose is not to supply any forward looking solvency assessment.

It is also worth noting that in so far as an item in a financial reporting framework is subject to risk or uncertainty then the primary purpose of that financial reporting framework is to determine the expected (mean) value (or a value close to the expected value) of that item.

Solvency Reporting

It is important to note that, in contrast to financial reporting, solvency reporting gives to a larger extent forward looking information, based on prospective information and projections. As a result solvency reporting will serve a purpose which is different from, and complementary to, regular financial reporting. Furthermore, solvency assessments are concerned with information on solvability (i.e. ways of avoiding ruin) and hence they focus on special parts of the probability distribution forecast[6] and not the expected (mean) value of items that are exposed to risk or uncertainty. Assessment of these parts of the expected probability distribution needs a deeper analysis and more complex methods, including use of expert judgment, than those used to determine the expected value.

[5] 2013 IAASB Handbook: Financial statements—A structured representation of historical financial information, including related notes, intended to communicate an entity's economic resources or obligations at a point in time or the changes therein for a period of time in accordance with a financial reporting framework.

[6] Article 13 (38) of the Solvency II Directive: 'probability distribution forecast' means a mathematical function that assigns to an exhaustive set of mutually exclusive future events a probability of realisation.

Solvency II Public Reports

According to the Solvency II Directive the Solvency and Financial Condition Report[7] ("SFCR") shall contain the following, publicly disclosed, information:

a) A description of the business and performance of the undertaking;

b) A description of the system of governance and an assessment of its adequacy for the risk profile of the undertaking;

c) A description, separately for each category of risk, of the risk exposure, concentration, mitigation and sensitivity;

d) A description, separately for assets, technical provisions, and other liabilities, of the bases and methods used for their valuation, together with an explanation of any major differences in the bases and the methods used for their valuation in financial statements;

e) A description of the capital management, including at least the following:

- I) the structure and the amount of own funds, and their quality;
- II) the amounts of the Solvency Capital Requirement and of the Minimum Capital Requirement;
- III) the option set out in Article 304[8] used for the calculation of the Solvency Capital Requirement;
- IV) information allowing a proper understanding of the main differences between the underlying assumptions of the standard formula and those of any internal model used by the undertaking for the calculation of its Solvency Capital Requirement;
- V) the amount of any non-compliance with the Minimum Capital Requirement during the reporting period, even if subsequently resolved, with an explanation of its origin and consequences as well as any remedial measures taken.

With respect to solvency reporting, EIOPA states[9] that public disclosure requirements are one of the cornerstones of Solvency II and convergence should be achieved in order to guarantee a level playing field and assist comparability. EIOPA believes the information included in SFCR should provide sufficient information to enable the disclosure audience[10] to understand the main characteristics of the business, the performance and risk profile of the undertaking, the processes to ensure the governance requirements are met, the valuation techniques and assumptions for different items of the balance sheet, the SCR and the MCR, and the amount and structure of own funds.

It is important to note that, in contrast to financial reporting, solvency reporting gives to a larger extent forward looking or prospective information. As a result solvency reporting will serve a different and additional purpose than regular financial reporting.

In our opinion the information disclosed as foreseen in the SFCR will be key to financial markets, policyholders and other interested parties. To develop and maintain the required level of quality, consistency and comparability, the AAE is of the opinion that the SFCR should be subject to an independent review of high quality so that such stakeholders have confidence in the appropriateness of the information disclosed, stating the basis of the independent review and by whom it has been performed.

[7] Solvency II Directive Article 51.1

[8] Solvency II Directive Article 304: Duration-based equity risk sub-module

[9] CEIOPS L2 Advice: Supervisory Reporting and Public Disclosure Requirements, CEIOPS-DOC-50/09

[10] EIOPA: "Potential readers could include other insurance and reinsurance undertakings, intermediaries, trade associations, financial analysts, professional advisors, rating agencies, investors, shareholders, and policyholders, alongside of course supervisory authorities."

Consequently the AAE welcomes any initiative to ensure a harmonized independent review of the SFCR.

The Solvency II reports supplement existing mandatory financial reporting and supplement the embedded value (EEV or MCEV[11]) reports which are currently drawn up by many life insurers on a voluntary basis. The importance of reviews has already been acknowledged by the industry. As an example, the MCEV Principles developed by the CFO Forum require MCEV reports disclosed to an external review[12]. The market will require certainty in some or other form in relation to public solvency reports, certainly at the outset, but also on a continuous and structural basis. We are convinced that this will result in insurers commissioning experts to carry out objective reviews of their public reports. In order to achieve an adequate level of transparency and consistency the AAE is willing to develop and propose principles or guidelines.

[11] EEV (European Embedded Value) and MCEV (Market-Consistent Embedded Value) are valuation methods used to value insurance portfolios. MCEV refers to the Market Consistent Embedded Value Principles as developed by the European Insurance CFO forum (Copyright© Stichting CFO Forum Foundation 2008).

[12] CFO Forum, Market Consistent Embedded Value Principles G1.5: "A statement should be included to confirm that the methodology, assumptions and results have been subject to external review, stating the basis of the external review and by whom it has been performed."

Solvency II non-public reports

In addition to the SFCR a number of other reports are required under the Solvency II Directive. These other reports also require complex and usually prospective quantitative analyses based on projections.

REGULAR SUPERVISORY REPORTING ("RSR")

The objective of the RSR is to facilitate adequate supervision. The RSR is a separate report containing not only data which relate to the insurer's strategy or legal and legislative issues, but also prospective information on the basis of projections of solvency requirements and expected risks. In this regard, the insurer must also offer insight into the (underlying) process of the calculations and must demonstrate on the basis of quantitative analyses that the outcomes of the projections used are in line with expectations.

OWN RISK AND SOLVENCY ASSESSMENT (ORSA)

The ORSA provides an insight into the future development of the company's solvency and financial condition within a broad framework. The ORSA encompasses the consistency between the desired risk profile and the actual risk profile, the strategy of the institution, compliance on a continuous basis, the consistency between the strategy and the underlying processes, and the adequacy of the way in which the company's policy is reflected in (internal/standard) models. The ORSA stimulates the insurer to consider future risk positions, to provide estimates of the changes in risk positions, to determine how these can be measured adequately and how these can be anticipated to achieve the desired capital positions. The ORSA must be carried out at least annually. In this regard, it is the insurer's responsibility to demonstrate that this is sufficiently frequent. The ORSA must in any event include:

- a description of the integration of the ORSA into the management process;
- a description of the frequency with which the ORSA is reviewed by the management of the insurance company;
- a description of the way in which the solvency requirement is determined in the light of the risk profile;
- a guarantee that the ORSA process is well anchored in decision-making and is adequately documented.

QUANTITATIVE REPORTING TEMPLATES (QRT)

In addition to the above-mentioned reports, the supervisor also requires insurers to submit QRT reports. QRT reports are drawn up in order to provide timely signals of developments in the insurer's financial situation, solvency and results. The QRT reports are drawn up in a prescribed fixed format so that the quantitative data provided by the insurers can be compared easily. Under exceptional circumstances and if the (national) situation requires this, the supervisors are allowed to develop specific national templates. The QRT reports must be submitted on a quarterly basis to ensure that the information is up-to-date.

RISK MODELS

Solvency II requires more attention to the creation of risk models. A risk model is specific to an insurer and therefore provides the individual insurer with a better insight into its risks. Solvency II promotes the development of risk models. An important aspect of the introduction of risk models is the requirement that they be embedded well in the organisation. In other words, it is explicitly assumed that the AMSB[13] of the organisation is familiar with the (operation of the) risk models. The use of risk models must be integrated in the company's operations. Reports on the use of risk models must, in any event, contain the following information:

- the way in which and the level at which the management is aware of the operation of internal models, including their structure, logic, dynamics, limitations, diversification and scope;

- the way in which the risk model contributes to decision-making within the insurance company;

- an explanation of the techniques used in calculating parameters and models;

- the way in which the risk models are validated;

- the way in which the theory, assumptions and substantiation of the model is documented;

- the way in which the model outcomes are consistent with the further requirements of Solvency II.

Already during the preparations for Solvency II there has been an increasing need for actuarial expertise and actuaries have been frequently involved in:

- the various QISs[14] carried out to value the technical provisions, the drawing up of market consistent balance sheets, the quantification of risks and calculations of the Solvency Capital Requirement (SCR) and Minimum Capital Requirement (MCR) ;

- the development of economic capital models for the purpose of the ORSA and regulatory capital models in the pre-application process in relation to the application for an internal model under Solvency II;

- the advice to the management on the impact of the models on the business and the translation of this into policy.

Under Solvency II, actuaries employed by an insurer will be involved in the structuring of internal actuarial and risk management functions. In this regard, a distinction may be made between actuaries in operational, policy-making and reviewing roles. In addition, actuaries (both internal and external) will be required to provide objective assessments (or reviews) of models, the results of calculations and reports. This assessment involves the exercise of key expert judgments. These expert judgments require skills such as those described by Article 48 (2) of the Solvency II Directive[15].

The formal Solvency II reports do not form part of the financial annual reports and therefore do not qualify as subject to regular statutory auditing of financial statements. The desired level of assurance on the quality in relation to the Solvency II reports cannot therefore be derived from the assessment of the statutory auditor.

[13] Administrative, Management or Supervisory Body

[14] Quantitative Impact Study

[15] Solvency II Directive Art. 48: "The actuarial function shall be carried out by persons who have knowledge of actuarial and financial mathematics, commensurate with the nature, scale and complexity of the risks inherent in the business of the insurance or reinsurance undertaking, and who are able to demonstrate their relevant experience with applicable professional and other standards."

In Solvency II legislation at the European level, an independent certifying role which applies at present in some Member States is not prescribed as a legal obligation. This does not detract from the fact that it is very likely that there will be a continuing need for an independent review of the technical insurance provisions as included in the annual financial statements.

The direct involvement of actuarial expertise in determining the technical provisions under Solvency II is required by Article 48 of the Solvency II Directive.

4. Solvency II independent review

Scope

To ensure consistency, the scope of the independent review should include all items mentioned in Article 51.1 of the Directive. In particular:

- Article 51.1.e. requires important information about the solvency and financial condition of an (re)insurance undertaking.

- A similar importance should be given to Article 51 2: "The description referred to in point (e)(i) of paragraph 1 shall include an analysis of any significant changes as compared to the previous reporting period and an explanation of any major differences in relation to the value of such elements in financial statements, and a brief description of the capital transferability."

- Article 51.1.c requires the undertaking to disclose "a description, separately for each category of risk, of the risk exposure, concentration, mitigation and sensitivity".

- Article 295 (6) of the draft Level 2 regulation[16] states that "With regard to risk sensitivity the solvency and financial condition report shall include a description of the methods used, the assumptions made and the outcome of stress testing and sensitivity analysis for material risks and events."

- That implies that Article 51.1.b (risk profile should also be covered as the risk profile is central to a risk based prudential regulatory framework.

The AAE believes that all quantitative information, including underlying methodologies, assumptions and in any case the implications of this quantitative information for the potential future development of the solvency and capital position of the undertaking under review should be reviewed and assessed. This review will be specific to each undertaking and will rely on a combination of analysis of past experience and judgment of future trends, including various potential economic and entity specific scenarios that could influence the solvency and capital position of the undertaking. As a consequence the review should be carried out by persons who have knowledge of actuarial and financial mathematics, commensurate with the nature, scale and complexity of the risks inherent in the business of the insurance or reinsurance undertaking, and who are able to demonstrate their relevant experience with applicable professional and other standards.

The AAE believes, subject to full consideration of costs and benefits, that an independent actuarial review is desirable for the annual SFCR public disclosure. The disclosure should include the basis of the independent review, by whom it was performed and the opinion of the reviewer.

The AAE is of the opinion that fully qualified actuaries are best qualified to carry out such a review. As a logical consequence the review role should not be reserved for statutory auditors whose professional background is primarily in accounting or auditing. Balancing the costs and benefits and taking into account the fact that prudential accounts are based on an entirely different framework from the statutory accounts, the AAE believes that a targeted independent actuarial review is more appropriate than an extension of the statutory audit process of the financial statements.

The AAE is concerned about the potential lack of convergence between the national practices related to external scrutiny and review process for the purposes of the Solvency II.

[16] Version of 28 July 2014

Independent Review

This leads to three main questions that the AAE has considered:

1. **What should be the aim of the independent review?**
2. **What should be the scope of the independent review to achieve this aim?**
3. **Who should be playing a role in this independent review?**

Aim of the independent review

The AAE believes that the aim is to give the public confidence in the insurance undertaking's SFCR disclosure.

The report of the independent actuarial review should be disclosed on the website of the undertaking in the same way as the SFCR is published[17].

Scope of the independent review

The AAE has considered whether a limited scope to check arithmetical accuracy and processes or a fuller scope will serve the aim of the independent review. The AAE supports broadening the scope of the review to encompass all aspects of the SFCR, regardless of whether or not it is compulsory.

The AAE believes that one of the most important tasks in the independent review is the assessment of the expert judgments made in the process of selecting methodology and setting assumptions in relation to relevant future outcomes.

However, if the scope of the review is restricted to certain specific elements of the SFCR, there is a danger that the public could believe, wrongly, that all or at least all quantitative information in the SFCR has been subject to independent review.

Thus either the independent review should address all information in the SFCR or - as a minimum - a robust and transparent mechanism needs to be applied in the SFCR so that the public is properly informed about the scope of the independent review.

Actors in the independent review

THE RIGHT EXPERTISE

The AAE believes it is essential that the review is conducted with the right expertise. In particular, Article 48 (2) of the Solvency II Directive sets necessary competencies for the actuarial function which the AAE thinks should also apply to the independent actuarial reviewer. The review needs to be carried out "by persons who have knowledge of actuarial and financial mathematics, commensurate with the nature, scale and complexity of the risks inherent in the business of the insurance or reinsurance undertaking, and who are able to demonstrate their relevant experience with applicable professional and other standards".

[17] Art. 301 (1) of draft Level 2 regulation.

EXPERT JUDGMENT

Since the internal expert judgments need actuarial expertise, an independent actuary's opinion should be required to perform any independent review in order to assure the public and the supervisor that the expert judgments applied in the process are appropriate. As a means of giving independent confidence to the public, the opinion of the independent actuary should be disclosed. This disclosure should include the basis of the independent actuarial review, by which actuary it was performed and the opinion of that actuary.

The actuarial review needs to include the expert judgments made for the calculation of the technical provisions[18] and of the SCR and MCR[19].

Following the information principles, as set out in Article 35 (4) of the Solvency II Directive, "(a) [the information] must reflect the nature, scale and complexity of the business of the undertaking concerned, and in particular the risks inherent in that business; (b) it must be accessible, complete in all material respects, comparable and consistent over time; and (c) it must be relevant, reliable and comprehensible."

The AAE would welcome attempts to establish common EU approaches to independent review. However the AAE recognises that a member state may find it difficult to accept such guidelines if they prescribe a narrower scope than the member state's current regime of scrutiny and review.

EMERGING RISKS AND CHANGES IN RISK

A key component missing from this information is an expert view on elements such as emerging risks or market trends (or other potential changes in risk in the future) that might threaten the company's solvency position in the near or longer term.

The independent actuarial reviewer should receive information demonstrating that the standard formula SCR appropriately reflects the specific risk profile of the undertaking or that a (partial) internal model or undertaking-specific parameter is necessary.

The independent actuarial reviewer should also check (in conjunction with the Actuarial and the Risk Management Functions) that the risk profile has not evolved in a such way that the standard formula no longer reflects the specific risks of the undertaking or that the deviation between them should trigger the development of a (partial) internal model. In our view the appropriate reflection of the evolution of the risk profile within the standard formula calculations as at year end should be part of an independent actuarial opinion.

[18] Solvency II Directive Art. 77 and Art. 121

[19] Even if the Standard Formula is used to calculate the SCR, expert judgment may be necessary in the process of selecting and deriving undertaking specific parameters or in the process of applying simplifications.

OPINION

The form of the independent review opinion should be set by the regulation and should be clear for the public according to the extent of the review. Adapting "Forms of Opinion" (ISA[20] 805[21] - A8[22]), the independent reviewer may be expected to provide an unmodified opinion when the reviewer concludes that the prudential balance sheet and the MCR / SCR are presented fairly, in all material respects, in accordance with the Solvency II framework.

The independent review opinion should assure that results are free from material mistakes and prepared, in all material aspects, in accordance with the Solvency II regulatory framework. In addition, it should cover elements such as emerging internal and external risks and market trends which might not sufficiently be captured in the underlying models and processes.

The AAE considers it most important that such a forward looking view of an independent expert should be included. The Solvency II independent review report should be disclosed.

The AAE is ready to provide proposals in the development of this process.

[20] ISA: International Standard of Auditing

[21] ISA 805: Audits of single financial statements and specific elements, accounts or items of a financial statement.

[22] A8 of ISA 805: Form of Opinion

Other aspects of an independent review

Risk profile

Statements on the actual risk profile of the company (Article 51.1.b) should also be subject to independent review. Guidelines should be specified for this review. As sensitivities and stress testing are part of the SFCR (Article 295 of the draft Level 2 regulation), the AAE proposes to help draft such guidelines. This review will rely on the forward looking view on the individual company risk profile, supported by the quantitative assessment and results of the ORSA process, not to disclose them but to check whether the summary presented in Article 51.1.b correctly presents the risk profile of the undertaking. Such opinion can best be expressed by a fully qualified actuary. It is important for the public to be assured of the risk profile of the undertaking which will underwrite insurance.

Technical provisions

VALIDATION

The AAE notes that the Solvency II Directive does not require independent validation/assurance of Technical Provisions. This is despite the fact that Technical Provisions will often be the most significant item on an insurer's balance sheet that requires expert judgment. If independent assurance is to serve its stated purpose it needs to encompass comprehensive reassurance on the value of Technical Provisions.

Current practice in some member states requires either independent or professional review of the Technical Provisions calculated by insurers. These member states are unlikely to want to dilute the level of policyholder protection afforded by their current regime, so harmonisation of assurance on Technical Provisions would seem to point to an extension of independent or professional review to all member states.

The AAE is of the view that due to the inherent complexity of technical provisions and due to the fact that these are falling under the domain of the Actuarial Function, to be approved by the AMSB of the undertaking, it would be desirable to have the technical provisions reviewed by an independent fully qualified actuary conforming to professional and ethical standards as required for that function.

LOSS ABSORBING CAPACITY

The review should include the loss absorbing capacity of technical provisions and deferred taxes which is subject to an expert judgment; Article 108 of the Solvency II Directive states: "The adjustment referred to in Article 103(c) for the loss-absorbing capacity of technical provisions and deferred taxes shall reflect potential compensation of unexpected losses through a simultaneous decrease in technical provisions or deferred taxes or a combination of the two. That adjustment shall take account of the risk mitigating effect provided by future discretionary benefits of insurance contracts, to the extent insurance and reinsurance undertakings can establish that a reduction in such benefits may be used to cover unexpected losses when they arise. The risk mitigating effect provided by future discretionary benefits shall be no higher than the sum of technical provisions and deferred taxes relating to those future discretionary benefits."

Other additional voluntary disclosures

The independent review report should be clear if any additional voluntarily disclosed information is subject to review. As stated by Article 298 of draft Level 2 regulation, "Where insurance and reinsurance undertakings disclose publicly, in accordance with Article 54(2) of Directive 2009/138/EC, any information or explanation related to their solvency and financial condition whose public disclosure is not required these undertakings shall ensure that such additional information is consistent with any information provided to the supervisory authorities pursuant to Article 35 of that Directive."

SFCR other than the regular annual one

Article 54 of the Solvency II Directive states that "In the event of any major development affecting significantly the relevance of the information disclosed in accordance with Articles 51 and 53, insurance and reinsurance undertakings shall disclose appropriate information on the nature and effects of that major development." A statement from the independent actuarial reviewer should be published alongside this additional SFCR.

Links between the independent review and the statutory audit

For reasons of efficiency duplicating any review that is already covered by traditional statutory audit should be avoided. In particular, the review of the assets and the liabilities, other than technical provisions and reinsurance assets, may be directly driven by the statutory review.

Recovery plan

The SFCR may contain elements regarding periods of non compliance with the SCR. In particular, a recovery plan may be disclosed with forecast data. The AAE believes that actuaries are best placed to review these disclosures.
The AAE is ready to offer its help to draw further guidelines or standards to set a clear division of responsibilities between the supervisor role and the external auditor role.

Internal model

The AAE considers that the (partial) internal model approval does not fall within the scope of the independent actuarial review. This (partial) internal model approval is the subject of a formalized process between the undertaking and the supervisor. It may involve independent actuaries through the process of validation but it has nothing to do with the independent review of the SFCR. The (partial) internal model is evaluated and approved by the supervisory authority.

To avoid any doubt whether the insurance undertaking has ceased to comply with the requirements set out in Articles 120 to 125 during the year, the independent reviewer should receive information from the AMSB confirming that the internal model is still valid and should be given insight in the (independent review of the) internal model including the appropriate reflection of the evolution of the risk profile within that model. If this is not the case the AAE believes that it would diminish the interest of the independent review for the public.

Timelines

As the publication of the independent review may add several weeks to the processes, timelines of the SFCR publication should be adapted to this.

5. Proportionality and Efficiency

Despite the wide acceptance of the Solvency II framework in the (re)insurance industry, there is still a lot of discussion and uncertainty about the potential operational costs. Smaller companies are especially worried about the impact on their organisation and the costs involved.

The starting point should be that the required Solvency II reporting is carried out in an integrated way within the other risk management and financial reporting requirements of the undertaking.

To a large extent this will depend on the organisational ability of the undertaking itself. But at any rate unnecessary activities (calculations, modelling) or duplication of work should be avoided at all times.

The AAE believes that the costs involved in the independent review of Solvency II reports should and can be limited as some or most of the elements and processes necessary to carry out the required reporting activities are checked by professional auditors in the statutory accounts on - at least - an annual basis.

On that occasion, if justified, the auditor gives an (unmodified) opinion and concludes "that the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework".[23]

It can be expected that the underlying information necessary to produce a Solvency II report does not differ from the underlying information ("audit evidence")[24] on which the auditor has based his/her opinion for the most recent (published) financial statements, it may be sufficient that the AMSB issues a statement that the underlying information is still correct. If not, the AMSB can give information where the underlying information differs (from the underlying information ("audit evidence") on which the auditor has based his/her opinion for the most recent (published) financial statements) and limited additional audit work may be carried out.

The additional work relating to prospective information and projections has to be carried out - in principle - every time a report is being issued, as this will be based on actual portfolio data, actual methodology used and the current set of economic and entity specific assumptions.

In this way the work to be carried out for Solvency reports can be limited to some extent, although we have to acknowledge that it will still involves quite some work.

[23] 2013 IAASB Handbook Glossary.

[24] 2013 IAASB Handbook Glossary; "Information used by the auditor in arriving at the conclusions on which the auditor's opinion is based. Audit evidence includes both information contained in the accounting records underlying the financial statements and other information".

6. The Actuarial Profession in Europe

The actuarial profession is governed by high quality standards of qualification, practice, code of conduct and discipline. For further reference see also Annex 2.

Based on the Vision, Value and Mission of the AAE the European actuaries feel responsibility for carrying out actuarial services of the highest quality, including direct services to employers, regulators, auditors and other principals and independent reviews in relation to work product of others. Within the framework of this paper they are especially interested in contributing to the goals of the Solvency II framework.

ANNEX 1 Reference

- SOLVENCY II DIRECTIVE 2009/138/EC
- SOLVENCY II LEVEL 2 REGULATION
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ANNEX 2 Actuarial Association of Europe (AAE)

The AAE was established in 1978 to bring together the actuarial associations in the European Union to represent the actuarial profession in discussion with the European Union institutions on existing and proposed EU legislation which has an impact on the profession. The AAE also now provides a forum for discussion amongst all actuarial associations throughout Europe. The AAE currently has thirty-seven member associations in thirty-five European countries, representing about 20,000 actuaries. Advice and comments provided by the AAE on behalf of the European actuarial profession are totally independent of industry interests.

VISION

The vision of the AAE is for the actuarial profession in Europe to be, and to be recognised as being, the leading quantitative professional business advisers in financial services, in risk management and in the financing of social protection, contributing to the well-being of society, with European institutions recognising the valuable role that the AAE plays as a leading adviser on actuarial issues.

VALUES

The AAE espouses the following values.

- concern for the public interest
- integrity
- independence
- collaboration and respect
- transparency and accountability
- professionalism

MISSION

To enhance the role of the AAE, on behalf of the actuarial profession in Europe, as an objective, independent, professional, leading adviser, contributor and spokesperson to European institutions and stakeholders on all matters of actuarial relevance, widely recognised and respected in this role, in pursuit of the public interest.

To create added value for the actuarial profession in Europe and to provide support by sharing, encouraging, facilitating and resourcing in order.

- to enhance the quality of actuarial work to the benefit of the public and the users of actuarial advice
- to promote professionalism
- to develop model standards and to encourage member associations to adopt
- to encourage advancement of actuarial education, research, science and practice
- to promote the role of the actuarial profession in protecting the consumer
- to promote a holistic role for actuaries as business advisers and influencers as well as technical experts
- to provide opportunities for networking and encourage sharing of best practice across Europe
- to respect the principle of subsidiarity

MEMBERSHIP

The Statutes of the AAE requires that full member associations

- must have a Code of Conduct that reflects at least the requirements of the AAE's Code of Professional Conduct, and comply with minimum education standards as set out in the AAE's Core Syllabus
- have to have a formal disciplinary process in place
- if standards of practice are recommended by the association an appropriate promulgation process must be in place

The Actuarial Association of Europe

The Actuarial Association of Europe (AAE), founded in 1978 under the name of Groupe Consultatif Actuariel Européen, is the Brussels-based umbrella organisation, which brings together the 37 professional associations of actuaries in 35 countries of the EU, together with the countries of the European Economic Area and Switzerland and some EU candidate countries.

The AAE has established and keeps up-to-date a core syllabus of education requirements, a code of conduct and discipline scheme requirements, for all its full member associations. It is also developing model actuarial standards of practice for its members to use and it oversees a mutual recognition agreement, which facilitates actuaries being able to exercise their profession in any of the countries concerned.

The AAE also serves the public interest by providing advice and opinions, independent of industry interests, to the various institutions of the European Union - the Commission, The Council of Ministers, the European Parliament, ECB, EIOPA and their various committees - on actuarial issues in European legislation and regulation.

actuarial association of europe

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