



Banc Ceannais na hÉireann
Central Bank of Ireland

Eurosystem

8th December 2017

Re: Feedback on Actuarial Opinions on Technical Provisions and Actuarial Reports on Technical Provisions following Central Bank of Ireland's thematic review

Dear Head of Actuarial Function,

The Domestic Actuarial Regime and Related Governance Requirements under Solvency II (Domestic Actuarial Regime) were introduced as conditions to which (re)insurance undertakings are subject pursuant to Regulation 26 of the European Union (Insurance and Reinsurance) Regulations 2015 (S.I. No. 485 of 2015). The Central Bank of Ireland (Central Bank) recently conducted a review of Actuarial Opinions on Technical Provisions (AOTPs) and Actuarial Reports on Technical Provisions (ARTPs), both of which are requirements under the Domestic Actuarial Regime. The review incorporated the AOTPs and ARTPs of a sample of 26 insurance companies. The primary objectives of this review were:

- To assess whether Heads of Actuarial Functions (HoAF) had complied with the regulations in the Domestic Actuarial Regime; and
- To provide feedback which might contribute to the improvement of future AOTPs and ARTPs.

In general, the review found that the ARTPs were of a high standard and complied with the Domestic Actuarial Regime. This letter sets out areas of non-compliance that were found and feedback that can be used to enhance the usefulness of AOTPs and ARTPs.

In preparing the AOTP and ARTP, it is important that the HoAF provides the board with transparency around methodologies; assumptions and expert judgement, simplifications; limitations; uncertainties and any other areas the HoAF believes to be material to the calculation of technical provisions (TPs)



While we recognise progress made in relation to the level of discussion around key assumptions and methodologies, the review identified areas where improvements are required. Particular areas of concern highlighted by this review include:

1. Inconsistencies between the AOTP and ARTP when reporting reliances placed on others in the calculation of TPs;
2. Where material concerns, limitations and recommended improvements were set out in the ARTP, they were not always reflected in the AOTP;
3. Inadequate documentation of methods employed by the HoAF to assess the completeness, accuracy and appropriateness of data used; and
4. Material gaps in reporting of methodologies, assumptions and experience analysis, including a lack of detail around simplifications, expert judgement and materiality.

In relation to point 1 and 2 above, where a HoAF wishes to add comments to the AOTP, in order to add context to their opinion, the AOTP template may be amended to incorporate these, without the need for qualifying the opinion.

The appendix to this letter outlines a number of observations from our review, which we encourage HoAFs to consider when preparing AOTPs and ARTPs in the future.

Please approach your normal supervision contact if you would like to discuss any of the points raised in this letter.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Graham Cherry', written over a horizontal line.

Graham Cherry

Head of Function - Actuarial Services



Appendix 1: Findings from Central Bank’s review of year end 2016 AOTP and ARTP submissions

- **Consistency between AOTP and ARTP when reporting reliances placed on third parties**

Section 2.2.3 of the Domestic Actuarial Regime sets out that the AOTP shall “include any material limitations or reliances that were made in providing the opinion on TPs”. Section 2.3.2.j states that the ARTP should include “a discussion on the nature and extent of any reliances placed or not placed on information or reports received, from within the undertaking, or any other source, in forming their opinion on TPs.”

The Central Bank observed instances of the HoAF reporting in the AOTP that they had not materially relied on the work, opinion or assurances of others or set out any limitations associated with the calculation of the Technical Provisions, yet the corresponding ARTP discussed numerous areas where reliances were placed on third parties and/or limitations were set out.

The Central Bank expects consistent reporting and discussion between the AOTP and ARTP. If there are areas referred to in the ARTP where the HoAF has materially relied on the work, opinion or assurances of others or there are material limitations associated with the calculation of the Technical Provisions, this should also be clear from a reading of the AOTP.

- **Documentation of Simplifications, Expert Judgement & Materiality**

Throughout the ARTPs, HoAFs make judgements around simplifications, assumptions and methodologies based on materiality. However, materiality thresholds are rarely defined in the ARTP. This could lead to inconsistencies being employed within the ARTP and/or across years. Where thresholds are not defined, it is not clear how the HoAF validated assumptions around materiality. The Central Bank would expect board discussion on materiality thresholds around which decisions are made, in order for the company’s systems of governance to comply with requirements set out in S.I. No. 485 of 2015. In particular, we note the requirements of paragraph 46, for companies to establish and maintain reporting procedures necessary to identify, measure, monitor, manage and report, on a continuous basis, the risks, on an individual and aggregated level, to which the undertaking is or could be exposed.



Where simplified modelling techniques are used, the Central Bank would expect the ARTP to include an estimate of the impact of this simplification. Few companies that used simplifications provided this information. Similarly, the impact/materiality of expert judgements, some of which are significant, are often not detailed or quantified. To improve transparency and help the board understand the uncertainty around simplifications and expert judgement, the Central Bank recommends that HoAFs detail all material simplifications and expert judgements, along with estimates of their impacts and uncertainties.

The determination of materiality is a matter of the HoAF's professional judgement. The Central Bank is not recommending any specific measure of materiality.

- **Documentation of methods used by the HoAF to assess sufficiency and quality of the data used in the calculation of Technical Provisions**

In accordance with Section 2.3.2.b of the Domestic Actuarial Regime, the HoAF should include in the ARTP, a description of how they have assessed the sufficiency and quality of data used in the calculation of technical provisions. The HoAF is not expected to duplicate the work of others¹. However, they are expected to make appropriate enquiries in order to provide informed opinions to the board. In certifying the data to be appropriate, complete and accurate, the HoAF should provide detail on the extent of any reliance on others, and on the work they did themselves to get comfortable with the data. The Central Bank would expect the HoAF to comment on whether the checks conducted are accurate and appropriate and to include reference to both the breadth and robustness of tests carried out.

ARTPs that met Central Bank expectations in this area included commentary from the HoAF on the appropriateness of tests carried out, the need for additional tests if applicable, and spot checks carried out by the HoAF on these third party data checks.

¹ See section 2 of the Central Bank's Guidance for (Re)Insurance Undertakings on the Head of Actuarial Function Role



- **HoAF recommendations for improvement**

Section 2.2.3 of the Domestic Actuarial Regime sets out that the AOTP shall “convey recommendations on improvements to be made, where appropriate”. Whilst most ARTPs included a ‘recommended improvements’ section, only three HoAFs went as far as including a ‘recommended improvements’ section in their AOTP statement. Whilst ARTPs have been comprehensive in setting out recommended improvements, we expect material recommendations to be clearly visible for the board.

By setting out the most material recommended improvements in the AOTP, HoAFs are providing the level of transparency for board members and senior management expected by the Central Bank.

- **Transparency of link between experience analysis and assumption setting**

The quality of the analysis of experience varied widely across companies. Some ARTPs included a comprehensive analysis of experience and detailed how this analysis informed the assumption setting process. The weaker ARTPs restricted their analysis to a small subset of assumptions, often failing to describe the link between this analysis and the assumption setting process. The Central Bank expects analysis of experience in the ARTP to address all assumptions, financial and non-financial, that materially impact on the calculation of the TPs. This analysis should also be at an appropriate degree of granularity, whether by product type or demographic.

Furthermore, Section 2.3.2.k of the Domestic Actuarial Regime states that ARTPs should distinguish between deviations which are judged to arise from volatility of the underlying experience and those which are viewed as impacting on the appropriateness of the data, methodologies or assumptions used.

The better examples of this analysis broke the variation in experience down into trend and volatility components and noted the impact on assumption setting. Few ARTPs reviewed met the Central Bank’s expectations in this regard.



Where this analysis has been completed outside the ARTP, the HoAF is not expected to duplicate this work but would be expected to include an overview of the results with details for the board on where specifics of the review can be found.

- **Transparency in relation to methodology & assumption setting**

The review highlighted a number of weaknesses in discussion around methodologies and assumptions. Common issues noted were:

- Insufficient detail provided on the choice of assumptions used and the rationale behind selecting methodologies in the technical provisions calculation;
- Reporting of uncertainties was generally weak with uncertainties not being appropriately communicated to boards;
- Insufficient details on the approach to segmentation used;
- Events Not In Data (ENIDs) are often assigned 100% to the provision for claims outstanding. Further consideration should be given to calculating/allocating ENIDs to the premium provision;
- Insufficient justification for the choice of methodology used to calculate the risk margin. Where the risk driver approach is used, insufficient justification of the specific risk drivers used; and
- Where the HoAF has relied on the input of others in calculating the risk margin, insufficient detail was provided as to how they gained comfort with the risk margin calculation.

- **Linking TPs with the firm's background, strategy, experience and operating environment throughout the year**

Section 2.3.2.f of the Domestic Actuarial Regime requires HoAFs to provide a description of the undertaking's background and its strategy, including experience and operating environment, throughout the year, in the context of calculating technical provisions.

Many HoAFs failed to link the undertakings' background, strategy, experience and operating environment to the calculation of TPs. In providing background information on the company, ARTPs often set out details of the external environment the company operates in at a high level. There was



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a lack of focus on how the experience and environment could affect technical provisions during the year. In addition some key trends specific to the company (e.g. a material deterioration in claims experience, material deviations in new business volumes) were not covered in sufficient detail.

The Central Bank would also expect the HoAF to consider whether any post balance sheet events, occurring prior to the finalising of the AOTP and ARTP, are sufficiently material to warrant inclusion.

The Central Bank expects HoAFs to consider the sufficiency and relevance of information provided in this section. In weaker ARTPs, this section consisted of pages of information on the company history, little of which were pertinent to the calculation of technical provisions. The ARTPs that met our expectations in this regard focused on specific issues, inside and outside the company's control that could affect directly on their technical provisions, including, but not limited to, areas such as emerging risks, potential legislative changes, changes to Long Term Guarantee Measures and reinsurance strategies.