DIMA

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Dear Sir/Madam

DIMA welcomes the opportunity to respond to the Central Bank of Ireland's consultation paper 104 on "External Audit of Solvency II Regulatory Returns / Public Disclosures". Certain sectors of the re/insurance industry will be subject to these types of provisions for the first time when the new requirements are finalised, and to that end it is important that companies facing these changes particularly in the "peak load" year of Solvency II are given sufficient time to properly establish systems and processes, and that those systems and processes are appropriate for the types of organisations to which they will be applied.

General comments

There are significant time pressures related to the current implementation date as proposed by the CBI, details of which are referred to within the specific responses section of this paper. We propose that the CBI extends the implementation date to ensure that there is sufficient time and resource for a proper and efficient implementation of the requirements. We suggest that the proposals are deferred for implementation until year end 2017.

The proposals do not apply proportionality, and as such do not reflect the regulatory ethos behind Solvency II. For regulated entities which are designated low risk under the CBI's PRISM system, there is no evidence that the full application of the external audit requirements will provide any tangible benefit for any stakeholders and instead put an unnecessary and significant burden on resource and activity. We propose that the CBI does not apply the full proposals to regulated entities in the low risk category under the PRISM model and instead refer to the audited IFRS or Irish GAAP financial statements.

We welcome the clarification that elements calculated using an approved internal model are out of scope for the purposes of the audit. We infer that all elements calculated or derived from an approved internal model are out of scope.

Certain aspects considered in more detail further in this response to the consultation include the removal of loss development tables from the scope of external audit, and that there is a "limited assurance" audit opinion.

Specific responses:

1.2 *"The proposals apply to all undertakings in the scope of Solvency II. It is proposed that the Central Bank will impose the external audit requirement for financial years ending on or after 31 December 2016."*

The CBI has a well-developed and unified systemic risk-based regulatory framework in the form of PRISM. Enhancements to the PRISM framework enacted early this year mirror the risk categories under Solvency II, and reflect the appropriate levels of regulatory interaction and intervention for the diverse entities within the international re/insurance industry in Ireland. External audit requirements are a new phenomenon for certain types of entities and the value of these requirements does not give any greater regulatory advantage; in fact, the pressure on resource from a Solvency II external audit for a low rated entity could arguably been seen to outweigh any possible benefits. Therefore we propose that low rated entities be descoped from the external audit requirements.

1.3 *"Under Solvency II, undertakings are required to prepare a Solvency and Financial Conditions Report ("SFCR") on an annual basis. This report forms part of a suite of regulatory returns and is also publicly disclosed by undertakings. Regulation 37 of S.I. No. 485 of 2015 (regarding the Auditor's Report) ("Regulation 37") enables the Central Bank, by notice in writing, to require that elements of the quantitative information submitted by insurance and reinsurance undertakings be audited, and that the audit report should include a reasonable assurance opinion on the elements of the SFCR relevant to the balance sheet, own funds and capital requirements ("the relevant elements") as described in Regulation 52 of that S.I. ("Regulation 52"). In accordance with Regulation 37, the audit report shall be made to the Central Bank and, as such, it will not be publicly available."*

It is appropriate that the board of directors/company be a co-addressee on the audit report.

2.2 *"To assist insurance and reinsurance undertakings and auditors in planning audit work associated with the financial year end 31 December 2016 the Central Bank is aiming to determine the final policy position by end September 2016. In order that stakeholder feedback can inform that decision, the Consultation Paper will be subject to an abridged comment period of eight weeks, in accordance with the Central Bank's Stakeholder Consultation Protocol."*

The Solvency II implementation project continues to provide stresses on resource and foreshortened timelines add to the pressure being exerted on regulated entities. Many EU jurisdictions have indicated that they will either defer or not require external audit reports. To this end, it is proposed that the CBI defer its audit requirement while a more standardised pan-European approach is being developed. This applies equally to point 4.4 (further in this response), where external guidance is expected to be developed subsequent to the final policy position at the end of September. This timeline is insufficient for industry/audit committees and the audit profession to be properly prepared for the year ended December 2016; deferring implementation for one year or more would give the various stakeholders sufficient time to prepare appropriately.

2.4 *"While the Central Bank will take full account of all submissions, it can be assumed that a regime broadly aligned to the type proposed in this document is likely to be introduced. With this in mind, undertakings are advised to take account of the likely introduction of such a regime now and begin to adapt their reporting practices in anticipation of its introduction."*

Industry supports the CBI's overall approach and objectives as represented in this consultation. However, the foreshortened timelines associated with this proposed regime are extremely challenging, even taking into account the notice inherent in this paragraph. Therefore, we reiterate that transitional measures and a longer lead-in time are appropriate treatments.

3.1 *"Regulation 37 enables the Central Bank, by notice in writing, to require that elements of the quantitative information submitted by insurance and reinsurance undertakings be audited, and that the audit report should include a reasonable assurance opinion on the elements of the SFCR relevant to the balance sheet, own funds and capital requirements as described in Regulation 52."*

The CBI rightly identifies Regulation 37 as enabling it to require a reasonable assurance opinion. We again propose that the CBI implements this in a transitional way and in line with other EU member states. The CBI's current proposals are similar to that issued by the PRA in the UK, and both are significantly more detailed than any other EU Member State. To all intents and purposes, this therefore leaves Ireland as an outlier in the future EU scenario, rather than directing to the maximum harmonisation elements of Solvency II.

4.4 *"Following the consultation period it is expected that external audit guidance, including the format of the audit report, will be developed by CAI in consultation with the Central Bank."*

The audit report format will need to be reviewed by audit committees and boards in order that are cognisant of the levels of comfort and assurance provided by external auditors. It is vital that industry is key in the CAI's development of the audit report format, again to fully understand the scope and level of the audit work to be performed. The truncated timeline provided in the current proposals in this consultation will not allow for the proper development of these factors, and thus it should be extended, as per our previous comments.

5.1 *"The publication of the SFCR will provide useful information to investors and other stakeholders as much of the information in the SFCR is not otherwise publicly available. For example, the technical provisions calculated for the Solvency II balance sheet may be substantially different from those in the audited International Financial Reporting Standards (IFRS) or Generally Accepted Accounting Practice in Ireland (Irish GAAP) financial statements."*

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It is accepted that for large or more complex undertakings, the Solvency II balance sheet and the audited financial statement may be substantially different. This is not, however, the case for entities rated a low risk within the PRISM framework. Thus we would expect that the audited IFRS or Irish GAAP financial statements will provide sufficient audited information to support any Solvency II returns or SFCRs.

5.3 *"The cost of an external audit of the relevant elements of the SFCR will be impacted by:*

- *The type of business – technical provisions and the asset side of the balance sheet tend to be more complex for life insurers than for non-life insurers;*
- *Whether the undertaking calculates its Solvency Capital Requirements ("SCR") using an approved internal model or the standard formula;*
- *The extent to which the auditor can rely on the systems, controls and processes in place at the undertaking when determining the type and level of evidence required to give an opinion; and*
- *The group structure from a Solvency II perspective."*

The CBI's domestic actuarial regime already requires peer review of the Head of Actuarial Function. This requirement is therefore no longer relevant as the technical provisions are now under the scope of the currently open consultation (CP104) and as such the peer review does not add any additional benefit. If the CBI prefers to retain the Peer Review Regime, consideration should be given to the scope of the audit, such as carving out technical provisions, in order to ensure there is no duplication of effort.

6 *"Regulation 37 is prescriptive in relation to the scope of the review stating that a reasonable assurance audit opinion shall be sought, in a report made to the Central Bank, on "the elements of the report on the solvency and financial condition of the undertaking as referred to in Regulation 52 relevant to the balance sheet, own funds and capital requirements". On that basis the Central Bank's proposal is set out below."*

Again the current timelines and multiple Solvency II reporting requirements are posing a serious challenge to industry. Taking into account the stated decisions of other EU Member States that they are deferring implementation or not intending to require an audit opinion at all, the CBI should defer the implementation date of the audit requirement in Ireland and ensure that the regulatory developments in Ireland are in step with those of other European Member States, to reflect the maximum harmonisation aspects of the Solvency II regime.

Entities included in scope

1. *"As per Regulation 37 certain information to be submitted to the Central Bank by insurance and reinsurance undertakings shall be in scope for this engagement. It is proposed that all insurance and reinsurance undertakings regulated by the Central Bank will be in scope given the value of an audit opinion to supervisors, investors and other stakeholders. This is a new requirement for reinsurers whose regulatory returns were not subject to review by auditors under the pre-Solvency II regime."*

The CBI recognises the different nature, scale and complexity of regulated entities through its PRISM process. The principle of proportionality embodied in the Solvency II

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Directive is reflected in the amended PRISM system, and we refer once again to the proposal that low-rated entities in Ireland should not be brought within the scope of these requirements, but instead that audited IFRS/Irish GAAP financial statements will provide sufficient audited information to support any Solvency II returns of SFCRs for entities within this designation.

3. *"It is proposed that the capital requirements templates, comprising the SCR and the Minimum Capital Requirements ("MCR"), of undertakings using approved full internal models will be excluded from this proposal, given the complexity of models, the high cost of audit, the limited additional value and that the internal model is already subject to an undertaking's internal validation and the Central Bank's approval. This proposal is consistent with the approach of a number of other EU national regulatory authorities."*

There is a developing approach in other EU Member States that information derived from the internal model is out of scope, and therefore information derived from the SCR including the risk margin is also out of scope. Clarification is sought from the CBI to confirm that this is also the regulatory approach in Ireland.

Opening balance

5. *"As part of their procedures to support a reasonable assurance opinion on the relevant elements of the SFCR, it is expected that the auditors will perform certain audit procedures in respect of opening balances under Solvency II as required. A separate audit report will not be required in this regard."*

Industry welcomes the confirmation that opening balances are not in scope of the audit report but are of the view that any procedures in respect of opening balances should form part of the audit plan agreed between the auditor and firm and not be referenced in the CBI guidance.

Who shall undertake the review

6. *"In accordance with Regulation 37, elements of the quantitative information to be submitted to the Central Bank by insurance and reinsurance undertakings under financial services legislation and other laws applicable in the State shall be audited by a person duly qualified under the Companies Act of 2014 ("the Companies Act")."*

As noted previously, the CBI already requires that a periodic peer review is carried out on the Technical Provisions including Actuarial Opinion on the Technical Provisions and the Actuarial Report on the Technical Provisions. This proposal therefore would effectively create a duplication of activity, with additional burden on resources with no related benefit. We propose that the CBI reconsiders the need for a peer review of the Technical Provisions under the Domestic Actuarial Regime or provide for a joint sign-off from the Peer Review actuary and the auditing firm under the external audit of Solvency II reporting.

10. *"As part of their audit, auditors shall determine whether they should use the work of an auditor's expert, for example an actuarial expert. In these instances the Central Bank understands that the work of the auditor's expert may be relied on in accordance with the*

requirements of the Insurance Standards on Auditing (UK and Ireland) and the audit firm's own due diligence procedures. The Central Bank expects that auditors will obtain and pay due regard to advice from an independent actuarial expert as they deem necessary."

Industry welcomes the clarification that auditors may rely on the use of an actuarial expert and requests that the CBI allow the independent actuarial expert to provide an opinion on technical provisions and relevant SCR calculations directly to the CBI, in conjunction with the audit firms' opinion for the other areas in scope. This should be at the discretion of each company and will reduce duplicate work with the peer review process should it be required and increase efficiency within the system.

Quantitative Reporting Templates (QRTs)

12. *"In respect of QRT S19.01.21 (Information on non-life insurance claims in the format of development triangles for the total non-life business), the claims paid triangle in the QRT includes a 10 year "look back" period. In recognition of the cost and practicalities associated with obtaining a reasonable assurance opinion on a 10 year "look back" period the Central Bank has decided to limit the "look back" period subject to audit in the first year to 2 years (i.e. the first period audited for the purposes of the claims paid triangle will be the period ended 31 December 2014)."*

    QRT S19.01.21 is not a core part of the EBS, SCR, MCR or Own Funds section of the SFCR and as such should not be included in the audit scope. The EBS in total is already subject to audit and this opinion will provide a reasonable assurance opinion on the non-life reserves. We welcome the 2 year limit to the "look back" period but this still brings the scope back to 2014 for best estimate of non-life technical provisions which is a significant increase in work for a disclosure template and is inconsistent with the rest of the requirements which focus on the 2016 year end.

13. *"In order to enable the auditors to obtain an understanding of the valuation basis used to calculate the relevant quantitative information and assess consistency between the quantitative and qualitative information on the same items, it is expected that the auditors will review relevant qualitative elements of the SFCR. These may include, for example, elements of the SFCR sections relating to valuation for solvency purposes and capital management."*

    Industry anticipates that any extension of these types of elements beyond the guidance given in Appendix 2 will be subject to consultation.

14. *"The external auditor engaged by an undertaking must assess whether the information disclosed by the undertaking in its SFCR which is outside the scope of the audit engagement is consistent with the relevant elements of the SFCR and any other information to which the auditor has had access."*

    We request that the CBI amends the language here from "is consistent" to "is not materially inconsistent" where the item is not a relevant element of the SFCR.

Level of assurance

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16. *“As set out in Regulation 37, a reasonable assurance opinion will be sought on the relevant elements of the SFCR. It is proposed that the QRTs relating to the balance sheet, technical provisions and claims, long term guarantees, own funds, the SCR (with the exception of those elements calculated using an approved internal model) and MCR, as set out in Appendices 2 and 3, shall be included in scope.”*

As previously noted, elements derived from internal models should be excluded from the scope of the audit to ensure that internal models are not indirectly caught within the scope of these requirements.

General application and implementation

17. *“The Central Bank intends to impose the requirement sin respect of SFCRs relating to financial years ending on or after December 2016.”*

The comments made previously in relation to item 6 apply equally in this case, namely: Again the current timelines and multiple Solvency II reporting requirements are posing a serious challenge to industry. Taking into account the stated decisions of other EU Member States that they are deferring implementation or not intending to require an audit opinion at all, the CBI should defer the implementation date of the audit requirement in Ireland and ensure that the regulatory developments in Ireland are in step with those of other European Member States, to reflect the maximum harmonisation aspects of the Solvency II regime.

Appendix 1: Regulation 37 from S.I.485 of 2015 – European Union (Insurance and Reinsurance) Regulations 2015

Auditor’s Report

37. *“(1) Such elements of the quantitative information to be submitted by insurance undertakings and reinsurance undertakings under financial services legislation and other laws applicable in the State adopted pursuant to the Directive as may from time to time be specified by notice in writing by the Bank shall be audited by a person duly qualified under the Act of 2015 who shall make a report to the Bank in a form specified by the Bank from time to time.”*

To date there has been no indication of the proposed wording of the report. We reiterate our position that a delay to the implementation of these requirements is appropriate, which will give all stakeholders sufficient time to understand and implement the final proposals and wordings.

Appendix 2: Proposed elements of the SFCR to be included in scope at solo level

Article 4 (a)-(f)

Please refer to earlier comments on triangulation under Item 12.

DIMA and industry representatives will be happy to meet with the CBI to discuss any of these items in further detail.

Yours faithfully

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