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Actuarial Services

Hot topic

CP92 Feedback Statement: Actuarial Regime and Governance Requirements place significant new demands on insurance companies

Highlights

The CBI has published its feedback statement following consultation on CP92 relating to the Actuarial Function framework which will operate for all locally regulated (re)insurance entities from 2016 onwards. The feedback and revised Requirements include information on the new Head of Actuarial Function role as well as on deliverables, both internal to firms and external, that will have to be prepared from 2016 onwards. Companies will need to incorporate these new requirements into their Solvency II planning with immediate effect.

The Central Bank of Ireland (CBI) has published its feedback statement and revised Requirements following consultation on CP92 ('Domestic Actuarial Regime and Related Governance Requirements Under Solvency II'). These Requirements will apply from 1 January 2016 and will form an important part of the local regulatory regime for life and non-life insurance and reinsurance entities in Ireland from 2016 onwards. The final Requirements will be issued by the CBI following transposition of the Solvency II (SII) Directive into Irish law.

Under the new regime, the role of the Head of Actuarial Function (HoAF) will replace the Appointed Actuary and Signing Actuary roles which operate in the current domestic regulatory framework.

The HoAF will be responsible for producing an annual Actuarial Opinion on Technical Provisions (AO TPs) to be delivered to the CBI along with the SII annual quantitative reporting templates (QRTs). In addition, the HoAF must present an Actuarial Report on Technical Provisons (ARTPs) to the Board. The Requirements incorporate a further actuarial opinion to be provided by the HoAF on the ORSA process which includes an assessment of the range of risks considered and the adequacy of the scenarios developed as part of the ORSA process.

Firms must also appoint a Reviewing Actuary (RA) periodically to review their TPs and related AO TPs and the ARTPs. The frequency of review is dictated by each firm's PRISM rating. High Impact firms will be subject to a review at least every 2 years (every 3 and 5 years respectively for Medium High and Medium Low firms) .

Firms' readiness to meet the Requirements will depend primarily on the strength of the governance and controls over the production of SII results as well as the capacity of SII systems to produce all relevant information for the ARTPs on a timely basis. We consider the actions which firms should take now to prepare to meet the Requirements, conscious of the need not to place undue added pressure on internal teams as they continue their preparations in the run up to the SII 'go live' date.

Head of Actuarial Function

This function must be held by one individual who will have to be pre-approved by the CBI through its Fitness and Probity (F&P) regime. The Society of Actuaries in Ireland plans to introduce a voluntary practising certificate regime which can be expected to facilitate actuaries and Boards in demonstrating compliance with F&P requirements.

The HoAF will be responsible for:
- The AO TPs to be submitted to the CBI annually along with the annual QRTs;
- The related ARTPs to be provided to the Board; and
- An actuarial opinion, also provided to the Board, in respect of each ORSA process performed including 'ad-hoc' ORSAs.

We expect the CBI to issue further guidance in relation to actuarial function (AF) responsibilities after transposition of the Solvency II Directive.

Outsourcing of the HoAF role is permitted except for High Impact firms. Applications by composite reinsurers to appoint a single HoAF will be considered by the CBI on a case by case basis.

There will be no 'grandfathering' of the existing Chief Actuary or Signing Actuary roles into the HoAF, though there remains some uncertainty as to how the transition will happen in practice. Firms should not assume that those performing these existing roles will automatically transition to the HoAF. Requirements of the HoAF role mean that this will represent more than just a change in job title.

Further clarity in relation to role transition will be provided when the CBI issues final Requirements and guidance regarding F&P changes under Solvency II.

One of the notable differences between the HoAF regime and the current Appointed Actuary / Signing Actuary roles is that there is no explicit requirement for the HoAF to be a qualified actuary. The Requirements do specify that the HoAF must be a member of a recognised actuarial association and appropriately experienced to fulfil the role. As the role is a Pre-Approval Controlled Function (PCF) position we think it is very likely that it will need to be fulfilled by a suitably experienced and qualified actuary in order to pass the fitness tests.

In the current regime actuaries frequently occupy roles within the first and second line of defence and in a small number of cases occupy both, e.g. fulfilling both Chief Actuary and CRO roles. While the Requirements do not impose restrictions on the HoAF fulfilling the role of CRO, firms now have an opportunity to clearly define duties and responsibilities of the respective roles.

At this stage firms should already have commenced engagement with their prospective HoAF to ensure that the PCF application and certification is in place before 1 January 2016.

Actuarial Opinion on Technical Provisions

The purpose of the AO TPs is for the HoAF to opine on the reliability and adequacy of each component part of the TPs calculation. This includes the data, assumptions, methodology and models that underpin the TPs calculation along with identification of and commentary on any known material limitations and recommendations. The form of the AO TPs will be issued with the final Requirements.

The opinion must consider separately the best estimate liabilities (BEL), the risk margin and recoverables from reinsurance treaties and SPVs.

The scope of the opinion includes all classes of business written and reported in the annual QRTs and is required at the SII lines of business level. This represents a change in focus compared to the existing regime for reinsurers and non-life insurers where the Signing Actuary is concerned with a comparison of 'aggregate' best estimate against a 'booked' reserve.

The HoAF must submit the AO TPs to the CBI at the same time as the annual QRTs. In order to meet these requirements we would expect firms to be able to rely, for the most part, on the work done to express a conclusion on the adequacy and reliability of the TPs which is to be included in the actuarial function report (AFR) (Article 272 of the Delegated Acts).

The Requirements set a high bar for the opinion to be provided by the HoAF, requiring it to consider compliance against all relevant SII requirements. Firms' readiness will be determined by the robustness of the control framework that has been established for the TPs calculation process. While some of the control framework that operates around the calculation of Solvency I and/or statutory reserves is likely to remain in place for the SII BEL, it is likely that this will not, for example, cover the risk margin calculation. The quality of documentation developed in areas such as expert judgement and known limitations across data, methodology and assumptions will also be a determinant of how onerous the provision of the opinion will be.

Firms will have to produce the AO TPs based on their first set of full year results under SII. The majority of firms operate a 31 December year-end and therefore will produce their first AO TPs in 2017 based on their year-end 2016 SII results.

Actuarial Report on Technical Provisions

The ARTPs is an annual requirement and must be presented to the Board in full within 2 months of submission of the AO TPs; and at least in summary form at the same time as the AO TPs.

The ARTPs sets the foundation for the AO TPs in that it describes the steps undertaken by the HoAF in reaching the opinion. The Requirements allow for the

ARTPs to be combined with the (at least) annual AFR. Given the nature and extent of overlap of content across the AO TPs, ARTPs and AFR, firms will be aiming to harmonise their reporting as much as possible so as to minimise duplication of effort.

The information required for the ARTPs includes:

Technical information: This includes, for example, the appropriateness of segmentation and risk margin calculation methodologies. The use and impact of the matching or volatility adjustment along with transitional measures, where relevant, must also be addressed.

Governance: The ARTPs must describe how the reliability and adequacy of the TPs has been assessed. It must also describe the reasons and rationale for reaching the opinion on the TPs as stated in the AO TPs.

Commercial: The firm's current strategy and operating environment, as they pertain to the TPs calculation, including discussion of any material emerging market trends.

Assumptions: The appropriateness of key assumptions including material areas of expert judgement, approximations and simplifications, and the approach to large claims.

Data: The ARTPs is required to describe any material unresolved data issues and limitations and their impact on the calculation of the TPs. The nature and extent of reliances placed, or not placed, on information received from sources both internal and external to the firm must be disclosed.

Risks and Uncertainties: The key risks and uncertainties associated with the TPs must be described with reference to the firm's reserving policy, risk appetite and SII rules.

The ARTPs requirements will allow Boards to be provided with relevant and timely information to achieve an adequate understanding of their TPs. This will facilitate challenge and decision making. The CBI feedback on 2014 FLAOR submissions published in May sets high expectations regarding Board ownership of technical issues. We expect the CBI to have similarly high expectations regarding Board review of the ARTPs. We think that it is important that insurers consider the needs of the Board in this process when designing their AO TPs and ARTPs processes.

With firms already under heavy pressure to be fully prepared for SII, it is important that further impact on internal teams tasked with implementing the Requirements is kept to a minimum. Management information currently produced for the Board along with the contents of the RSR, ORSA and AFR can be leveraged to populate much of the ARTPs. Consideration should be given to when in the reporting cycle this information will be available and how this aligns with the deadlines for the summary and full ARTPs.

A gap analysis may be useful in identifying any additional information that needs to be produced to satisfy the new requirements.

Peer Review

Role of the Reviewing Actuary (RA)
Under the Requirements all firms rated as High, Medium High and Medium Low Impact must engage an external RA to conduct a peer review of the TPs. High Impact SII firms must conduct a peer review at least every 2 years. Medium High and Medium Low Impact firms will be subject to review at least every 3 and 5 years respectively.

The Requirements place restrictions on who may perform the RA role. The RA can neither be an employee of the firm nor an employee of a firm to which the HoAF or calculation of the TPs has been outsourced. The RA may be from the same firm as the external auditor. The RA is not a PCF and is not therefore subject to CBI F&P requirements.

While the RA for Medium High and Medium Low firms can be from the same group, we expect the industry norm to be that the RA would be external to the group. This will make it easier for Boards to demonstrate independence while also providing access to information on best practice and benchmarking across the market.

Contents of the Peer Review Report
The prescribed contents of the Peer Review Report have some similarities with those specified under existing non-life reserving requirements with commentary required around the assumptions, methodologies and uncertainties inherent in the calculation of TPs. The RA will be required to assess the reasonableness of the HoAF's conclusions in respect of TPs.

There are additional peer review requirements for High and Medium High Impact firms, including a review of all lines of business which are deemed to have a significant impact on the firm's TPs.

Other Requirements

Firms must establish a written reserving policy which includes detail on their approach to calculating TPs. This document must also provide an overview of the reserving process including information on key roles, responsibilities and controls within the process. Firms may wish to use existing SII methodology papers as an initial starting point for their reserving policy.

There is an additional requirement for High Impact non-life insurers and reinsurers to establish a reserving committee. The committee, which must meet at least quarterly, is required to include all senior staff with input into the reserving process and, in addition, at least one independent Non-Executive Director, the member of the executive committee responsible for claims, the HoAF, the Head of Underwriting and the Head of Finance.

This committee's responsibilities must include overseeing the governance of the setting of TPs and the firm's compliance with the reserving policy. This will include responsibility for ensuring that any changes to claims handling practices are documented and communicated to the Actuarial Function.

Future changes to the criteria used by the CBI to designate firms' PRISM ratings could have an impact on which firms this additional requirement applies to. It may, therefore, be sensible for firms to consider their current rating and whether they are exposed to a potential switch to a PRISM rating that would expose them to this additional requirement.

The Requirements do not address AF responsibilities in respect of underwriting and reinsurance.

What do I need to do now to meet these Requirements?

The CBI's new requirements come into force on 1 January 2016 and firms will be under pressure to finalise their preparations to meet all aspects, on top of ongoing SII preparations. With the squeeze on resources unlikely to reduce in 2016 as teams 'turn the handle' on SII for the first time, it is vital that firms seek to minimise the impact of the CBI's new requirements.

Appoint a Head of Actuarial Function
The Appointed Actuary and Signing Actuary roles which operate in the current domestic regulatory framework will cease to apply from 1 January 2016. With less than 3 months to go until the SII 'go-live' date preparations should be underway for getting a HoAF certified and in place.

Establish Reserving Policy and, where required, Reserving Committee
All firms will need to prepare and agree their reserving policy for TPs. Additional requirements apply for High Impact non-life firms where a reserving committee must be established with appropriate membership and terms of reference in place, although we expect that much of this is already in place for those firms.

Appoint Reviewing Actuary
There are a number of factors that insurers must consider when choosing their Reviewing Actuary. It is likely that appointing a party that has provided assurance services in the past on aspects of reserving and/or the SII programme can realise significant cost/time synergies.

Plan for Actuarial Opinion & Actuarial Report on Technical Provisions
Firms must review their current reporting processes to ensure that additional information and resources required to complete the AO TPs and ARTPs are available to ensure timely delivery. Some Board training may be required as part of this preparation.

Involve Actuarial Function in required elements of ORSA process
The Actuarial Function must be in a position to provide an opinion on the range of risks and adequacy of scenarios considered as part of the ORSA process.

Consider potential changes in your status
Being aware of any changes to the criteria used to set firms' PRISM ratings and their implications will be crucial as this may trigger additional and more onerous requirements or serve to unwind the usefulness of prior investment.

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