# Solvency II Audit

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# Solvency II audits

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# External audit of Solvency II

The Central Bank of Ireland ("CBI") has finalised its requirements for the external audit of Solvency II regulatory returns / public disclosures, which were originally outlined in Consultation Paper CP 104. The requirements address the external audit of relevant elements of the Solvency and Financial Condition Report ("SFCR").

## Scope and requirements

- The requirements apply to all insurance and reinsurance undertakings regulated by the Central Bank of Ireland;
- The requirements specify a reasonable assurance opinion on the relevant elements of the SFCR;
- The relevant elements of the SFCR in relation to solo undertakings are set out on page [2];
- The relevant elements of the SFCR in relation to Solvency II groups for which the CBI is the group supervisor are set out on page [3];
- It is expected that the auditor will perform some audit procedures in relation to the opening Solvency II balances as required.

## Full and partial internal models

- For undertakings using approved full and partial internal models, the requirements exclude the Solvency Capital Requirement ("SCR") and the Minimum Capital Requirement ("MCR") templates from external audit.

## Commencement and timing

- The requirements apply to the SFCR for financial years ending on or after 31 December 2016 on an annual basis;
- The requirements note that the deadline for submission of the audit report for the year ending 31 December 2016 is **20 May 2017**;
- The deadline will decrease by two weeks every year thereafter, until it reaches 14 weeks after the year end. For example, for the year ending 31 December 2019, the deadline will be 8 April 2020;
- If the SFCR is republished and resubmitted to the CBI, it will need to be re-audited.

# External audit of Solvency II

**Solo undertakings**

The proposed elements of the SFCR to be included in scope of external audit are set out in Appendix 2 of CP104.

CP104 also requires the auditor to assess the information disclosed in the SFCR which is outside the scope of the audit engagement for consistency.

For non-life undertakings, there is a 10 year ‘look back’ period in respect of template S.19.01.21 (non-life insurance claims in the format of development tables). This ‘look back’ period is limited to two years in the first year of audit. Therefore, the first period subject to audit for an undertaking with a 31 December year end would be 31 December 2014.

| SFCR | Template: | Information on: | |
|---|---|---|---|
| Valuation for solvency purposes | • S.02.01.02 | Balance sheet | ✓ |
| | • S.12.01.02 | Life and health technical provisions | ✓ |
| | • S.17.01.02 | Non-life technical provisions | ✓ |
| | • S.19.01.21 | Non-life insurance claims in format of development triangles | ✓ |
| Capital management: Own funds | • S.23.01.01 | Own funds including basic and ancillary own funds | ✓ |
| Capital management: SCR | • S.25.01.21 | Solvency capital requirement using the standard formula | ✓ |
| Capital management: MCR | • S.28.01.01 | Minimum capital requirement for insurance and reinsurance undertakings that pursue only life or non-life activity | ✓ |
| | • S.28.02.01 | Minimum capital requirement for insurance and reinsurance undertakings that pursue both life and non-life activity | ✓ |

# External audit of Solvency II

**Solvency II groups for which CBI is group supervisor**

The proposed elements of the SFCR to be included in scope of external audit are set out in Appendix 3 of CP104.

CP104 also requires the auditor to assess the information disclosed in the SFCR which is outside the scope of the audit engagement for consistency.

| SFCR | Template: | Information on: | |
|---|---|---|---|
| **Capital management: Own funds** | • S.23.01.22 | Own funds including basic and ancillary own funds | ✓ |
| **Capital management: SCR** | • S.25.01.22 | Solvency capital requirement using the standard formula | ✓ |

# Likely areas of particular focus

## *All business*

- Reconciliations of Solvency II with Solvency I / other financial statements
- Data
- Contract boundaries
- Treatment of deferred tax including loss absorbency in stress scenarios
- Allowance for pension scheme risk in the calculation of the SCR
- Model and governance

## *Life*

- **Asset look through**
- **Value of in force**
- **Ring fenced funds**
- **Management actions**
- **Risk mitigants**
- **Best estimate assumptions**
- **Model application of stresses**
- **Italian pre-payment tax-asset**

## *Non-Life*

- Exposure information for catastrophe module
- Risk mitigation information for catastrophe module
- Calculation of premium provision: including appropriateness of loss ratios used to calculate profit in unexpired risks/ future premium
- Classification of counterparties
- Lapse risk sub-module

# Elements to plan with your auditor

- **Timeliness (as much as possible before period end)**
  **- assumptions**
  **- methodologies**
  **- data, models, systems and controls**
- **Resource availability (actuarial and auditors)**
- **Actuarial involvement and interaction with Reviewing Actuary**
- **Scope and scale of activity, including synergies arising from**
  **- Reviewing Actuary work**
  **- Head of Actuarial Function work**
  **- any previous assurance work on Solvency II implementation**
- **Interaction with financial statements audit**
- **Means for consideration/resolution of issues arising**

# Use of Experts

- **CBI expects the auditor to decide whether they should use the work of an expert e.g. an actuarial expert, in accordance with applicable auditing standards and technical guidance**
- **HoAF: Outsourcing v insourcing**
- **Reliance on Peer Review:**
  - was a peer review performed?
  - what is the timing and availability of peer review report?
- **Chartered Accountants Ireland to develop technical guidance**

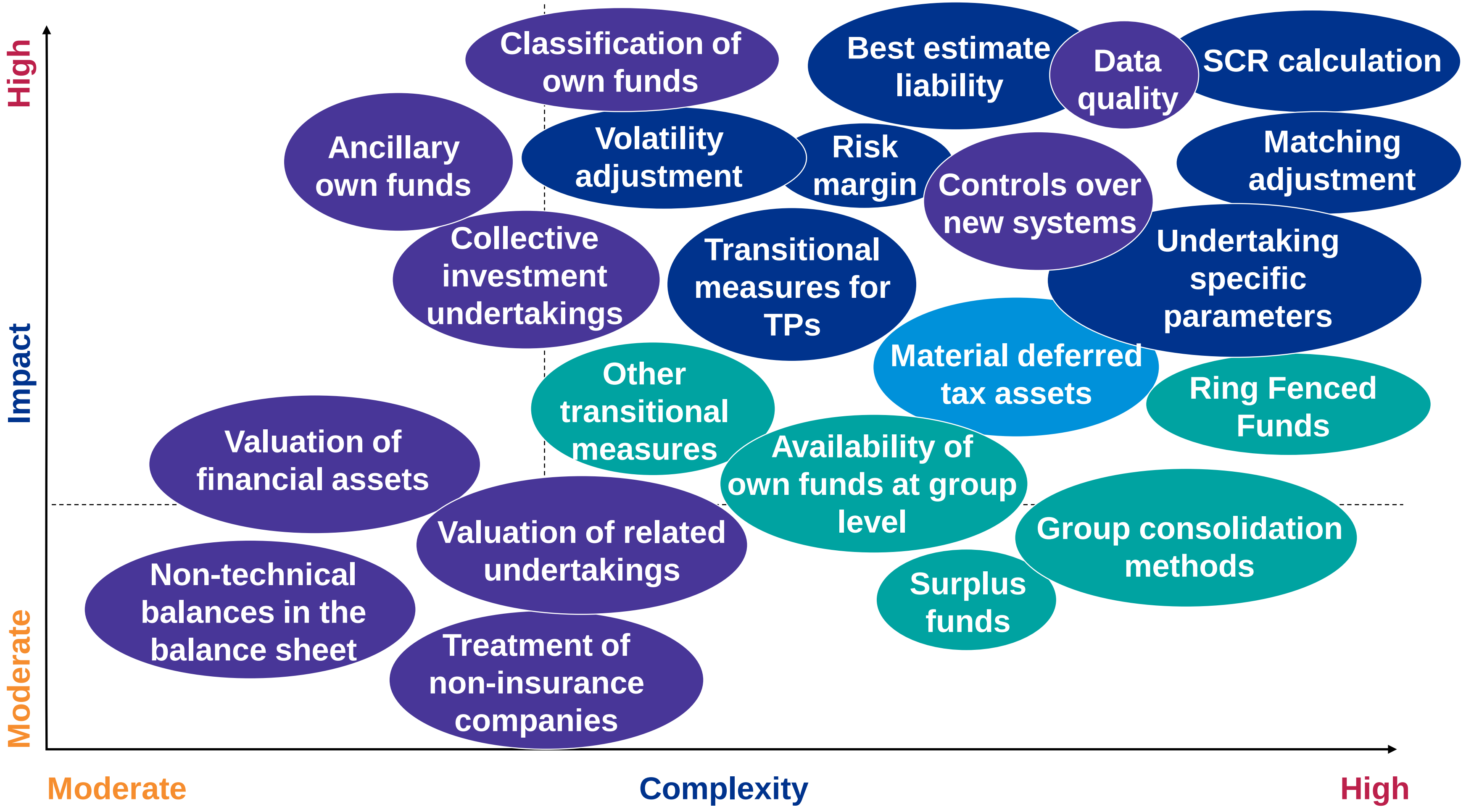
# Materiality

The information to be disclosed in the solvency and financial condition report shall be considered as material if its omission or misstatement could influence the decision–making or the judgement of the users of that document, including the supervisory authorities.

- Consideration of users
- Consider level of solvency coverage
- Appropriateness of benchmark metrics
- Materiality potentially different from financial statements audit
- Responding to misstatements identified at lower levels of materiality

- Client materiality policy
- Materiality for individual disclosures

# Illustrative risks and complexities



# Management and board responsibility

## How has the board obtained comfort that the SFCR has been properly prepared in accordance with the rules?

| | | |
|---|---|---|
| What procedures does the firm have in place to ensure ongoing compliance? | Who reviews the evidence? Entire board? Does the board delegate responsibilities to other individuals in the firm to review the submission? | Is there effective challenge of management by the Board? Is the review and challenge adequately evidenced, documented and validated? |
| What formal procedures are in place to address errors in the regulatory reporting? How does that impact other public reporting? | Are the reporting systems and structures fit for purpose? What oversight? | Are governance arrangements appropriate given nature, scale and complexity of the business? |
| What management information is there to monitor compliance? | Will the firm's approach satisfy the regulator? | How do directors attest / provide sign off? |

# Added complexity

- (Far) more complex than SI returns
- First year of application
- Interpretations and areas of judgment
- Limited benchmarking to date
- Limited supervisory precedents
- Industry focus on TPs and SCR
- Methodology documents may need updating
- New systems
- Limited controls
- Increased use of specialists
- Deadlines and timing
- In accordance with International Auditing Standards
- Scope limitations
- Materiality may differ from financial statements audit
- Post balance sheet events
- Voluminous narrative disclosures
- Regulatory group consolidation differs from IFRS
- Additional work over material group components
- XBRL submissions
- Governance and role of management


Q&A
Feedback

# Appendix

# Reasonable Assurance

**A reasonable assurance opinion under International Standards on Auditing (ISAs)**

**Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists.**

**The objectives of a reasonable assurance opinion are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor’s report that includes an opinion. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.**

**As part of an audit in accordance with ISAs, the auditor exercises professional judgment and maintains professional skepticism throughout the audit.**

# Reasonable Assurance

**The auditor also:**

**Identifies and assesses the risks of material misstatement of the financial statements, whether due to fraud or error, designs and performs audit procedures responsive to those risks, and obtains audit evidence that is sufficient and appropriate to provide a basis for the auditor's opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control;**

**Obtains an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control;**

**Evaluates the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management; and**

# Reasonable Assurance

**Concludes on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If the auditor concludes that a material uncertainty exists, the auditor is required to draw attention in the auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify the opinion. The conclusions are based on the audit evidence obtained up to the date of the auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.**

**The auditor communicates with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that are identified during the audit.**

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