



FINANCIAL REGULATOR
Rialtóir Airgeadais

Pre-application Readiness Assessment Process

April 2010

Insurance Supervision Department

Company Details

| | |
|------------------------------|--|
| Company Name: | |
| Contact Name: | |
| Contact Number/Email: | |

Contents

| | |
|--|----|
| Introduction..... | 2 |
| Section 1 - General Information..... | 4 |
| Section 2 - Overview..... | 4 |
| Section 3 - Planning..... | 5 |
| Section 4 - Scope and Design..... | 6 |
| Section 5 - Governance and the Use Test..... | 7 |
| Section 6 - Statistical Quality Standards..... | 8 |
| Section 7 - Calibration Standards..... | 10 |
| Section 8 - Profit and Loss Attribution..... | 10 |
| Section 9 - Validation Standards..... | 11 |
| Section 10 - Documentation Standards..... | 12 |
| Sign-off..... | 13 |
| Reference Material..... | 14 |

Introduction

As you have returned two questionnaires indicating your intention to participate in the Solvency II internal model pre-application process, we now request that you complete this template as the first step in the pre-application process. We will then conduct an assessment of your undertaking's response and we will allocate resources to your pre-application accordingly. As this is an iterative process we will provide feedback on your undertaking's progress through pre-application and we will communicate with you on its preparedness for an internal model application. Please also note that we may request further information and interaction with your undertaking in order to make this assessment. This interaction may include on-site visits to examine issues relating to the internal model on a practical basis.

Process

An assessment team will be assigned to your pre-application. This team will include your usual contact in the Insurance Supervision Department, with input from our Actuarial team and from our Solvency II project team. The assessment team will review the responses to the questions below, which are based on CEIOPS' recommendations in Consultation Paper 80. Aspects of the model to be examined include the risk management framework, documentation, compliance with standards in the Directive and management involvement. Essentially, pre-application assessment looks at the scope, coverage, design, build, integrity and application of the undertaking's internal model.

At the end of the pre-application process we will come to a view and provide feedback on how prepared your undertaking is to apply for internal model approval. Please bear in mind that the process for approval to use an internal model to determine the Solvency Capital Requirement (SCR) under Solvency II involves two distinct stages. The first stage is pre-application culminating in an opinion on your firm's readiness to

apply, and the second stage involves application, assessment and approval or refusal. We wish to stress that participation in the pre-application process does not guarantee approval after the formal application is submitted; hence pre-application process is not a pre-approval process. The process will allow us to become familiar with your firm's preparations for internal model approval and it will help your firm understand the standards required and the process for obtaining that approval.

Level of detail

This pre-application readiness assessment template consists of fifty-three questions designed to help us determine the progress of your internal model development. The template is divided into categories including project planning, scope and design of the model and compliance with the standards outlined in the Directive. We ask that you create a separate document as a response to this template. In the response document please create corresponding categories and include your responses to each question, labelling your responses clearly. Please confine the length of your answers to the limits indicated for each section.

We are aware that some firms are currently developing their internal models and therefore that preparations for adherence to the requirements of the Directive are at varying stages of advancement. The quality of the responses will depend on the company's stage of development and will be considered in that context. If you wish to provide some context on this point, please do so in response to Question 10 below.

If we require further information on a particular aspect of the model or model planning we will contact you. Insofar as possible, your answers should cover the internal model on a legal-entity basis (and subsidiaries of an Irish-based parent group if applicable).

Timing

We request that you submit your responses by 31st May 2010. If you are unable to meet this deadline, please inform us when you expect to reply.

Section 1 – General Information

(Please limit your response to 1 page)

1. Please indicate who is responsible for the preparation of the responses to this document and what their role is within the firm.
2. Please indicate which other departments within the firm have been involved in the preparation of the responses.

Section 2 – Overview

(5 pages)

3. Please describe the self assessment (if any) that your firm has carried out in relation to its requirements and readiness for internal model approval.
4. Please describe why your firm has chosen to use an internal model rather than the standard formula.
5. Please explain how the internal model will provide an appropriate fit for the business model.
6. If the firm is a subsidiary within a Group, and it intends using the Group's model, please indicate where the firm fits within the overall Group Ownership structure.
7. If the firm is a subsidiary within a Group and it intends using a model separate/distinct from the Group's, please indicate the extent (if any) of Group's involvement in the model design, and the intentions around the Group's involvement in meeting the requirements for model approval.

8. If the firm is the parent undertaking of a Group, please provide an organisation chart of the Group, noting the names of all the companies within the Group and their supervisors. Please indicate which firms are within the scope of the model.
9. Please provide the current organisational structure (staffing) for the firm and indicate which functions you expect will use output from the model.

Section 3 – Planning

(10 pages)

10. Please describe your internal model implementation plan including:
 - (a) A detailed timetable of tasks;
 - (b) Documentation surrounding the project plan;
 - (c) Interdependencies and assumptions;
 - (d) Risk factors and risk mitigation plans, and
 - (e) Resources allocated to the internal model project and overall budget for Solvency II implementation.
11. Did the firm complete a QIS4 spreadsheet on behalf of the local entity?
12. Describe how you are planning to complete QIS5 including:
 - (a) Time expected to complete;
 - (b) Resources required, and
 - (c) Potential risks that would prevent completion.
13. Please provide details of the governance structure of your internal model implementation plan including:
 - (a) Key personnel involved in the internal model development and implementation;

- (b) Co-ordination with group parent (if applicable);
- (c) Details on reporting, and
- (d) Senior management involvement and level at which the implementation plan and budget has been signed off.

Section 4 – Scope and Design (Art. 112)

(5 pages)

14. Please provide an overview of the model (including a diagram) to include:

- (a) The process that will be used to calculate the SCR;
- (b) The inputs to the model;
- (c) The calculation kernel(s) for calculating the SCR for each of the risk modules, risks, and adjustments as set out in Arts 104-108 of the Directive, and
- (d) A description of the information technology used in the internal model.

15. Please provide details of any internal model currently being used to determine capital requirements.

16. Please explain why your risk profile is better captured by the planned internal model than by the standard formula.

17. What risks (if any) are taken account of in the standard formula but are not captured by the internal model?

18. If using a partial internal model, what are the justifications for the limited scope of the model?

19. What are the key internal model risks that have been identified?
Please consider areas such as documentation, IT, model governance and security in your response.

Section 5 – Governance and the Use Test (Art. 120)

(5 pages)

20. Do Senior Management and the Board (including Non-executive Directors) understand the model?¹ Please support your answer with an explanation as to how this understanding has been achieved.

21. How are Senior Management and Directors expected to use the model?

22. Have clear reporting lines been established relating to the use of the internal model?

23. Describe the reporting lines that have been/will be established for the running and maintenance of the model.

24. Will the outputs of the internal model be included in regular reporting for:

(a) The Board of Directors:

(b) Senior Management, and

(c) Other personnel responsible for key functions.

Please explain your responses with the aid of examples.

25. Outline how the internal model is or will be used in:²

¹ If not, please provide a plan as to how this understanding will be achieved.

² This does not imply that use in all of the areas listed is required to satisfy the use test.

- a) Risk limit setting
- b) Risk Strategy
- c) Capital allocation
- d) Strategic business decisions
- e) Budgeting
- f) Product development
- g) Pricing
- h) Performance analysis
- i) Asset Liability Modelling
- j) Reinsurance
- k) Bonus setting
- l) Investment policy
- m) Dividend payments
- n) Market consistent technical provision
- o) Cost of Capital risk margin
- p) Assessment of uncertainty in technical provisions
- q) Asset allocation
- r) Management compensation
- s) Other

26. Are future management actions taken into account (yes / partly / no)?

27. If yes or partly, please summarise how the internal model allows for future management actions, e.g.

- Changes in future bonus rates
- Reductions in surrender values
- Changes in asset dispositions
- Changes in expense charges
- Changes in risk premium charges

- Changes in or use of dynamic option and guarantee charge mechanisms
- Restrictions in the ability to surrender
- Other – please specify.

28. Give examples of how the internal model is incorporated in the risk-management system and decision making process in such a way that there are continuous incentives to improve the quality of the model.

29. Are you already disclosing the results of the internal model in the annual accounts?

Section 6 – Statistical Quality Standards (Art. 121)

(5 pages)

30. Describe the process that will be used to derive the assumptions that are input into your internal model.
31. Does your firm have a written Data Policy? What checks will be performed to ensure that the data that will be used to support assumptions is accurate and credible?
32. What sensitivity analysis will you perform on the assumptions input into your internal model?
33. Describe how you will ensure that the assumptions and probability distributions used in the internal model are consistent with the methods used for the valuation of assets and liabilities.
34. How will you ensure that the internal model is consistent with the Company's budget / plan?

35. How are/(will) risk mitigation techniques (be)reflected in the choice of assumptions used in the internal model?
36. What correlation factors are/will be used in the internal model?
37. Which correlation factors is the internal model most sensitive to?
38. Describe the process used to determine the correlation factors.
39. To what extent is there reliance on Expert Judgement in the assumptions and parameterisation of your model? Where Expert Judgement is used, is this justified, documented and validated?

Section 7 – Calibration Standards (Art. 122)

(1 page)

40. Describe how you will derive the SCR from the probability distribution forecast. Can you demonstrate how this will be at least equivalent to the Value-at-Risk of the basic own funds of the firm subject to a confidence level of 99.5% over a one-year period?
41. What time periods, risk measures and probability will you use in the internal model to set the SCR?
42. To what extent do you use approximations to calculate the SCR?

Section 8 – Profit and Loss Attribution (Art. 123)

(2 pages)

43. How will the internal model analyse the SCR in terms of the different risks? Use list below if appropriate:
 - (a) Non-life underwriting risk
 - (b) Life underwriting risk

- (c) Health underwriting risk
- (d) Market risk
- (e) Credit risk
- (f) Operational risk

44. How will you analyse the impact on the profit and losses of the company using the risk drivers modelled?

Section 9 – Validation Standards (Art. 124)

(5 pages)

45. Please describe with the aid of example(s), how the following areas of the internal model are/will be validated?

- Data
- Methods
- Assumptions
- Expert judgement
- Calculation
- Results

(Possible methods include sensitivity & scenario analysis and back testing)

46. How often will the results of the internal model be tested against experience and any other available appropriate data?

47. Is your model validation independent from the model development?

48. Please provide a description of the internal model limitations or shortcomings identified during the validation process and the steps taken to address these (if applicable).
49. Has the internal model been created in-house or has the internal model (or a part of it) been licensed from an external software supplier?
50. Explain the role in your internal model of any parts of the internal model obtained from a third-party (external models) and data used in the internal model obtained from a third-party (external data) and the reasons for preferring external models to internally developed models.

Section 10 – Documentation Standards (Art. 125)

(2 pages)

51. Please explain how your internal model documentation will demonstrate compliance with:
- (a) The use test
 - (b) Statistical quality standards
 - (c) Calibration standards
 - (d) Profit and loss attribution
 - (e) Validation standards.
52. Does the internal model documentation include an outline of the theory, assumptions, and mathematical and empirical bases underlying the internal model?
53. What steps have you taken to ensure that an independent knowledgeable third party, on reviewing this documentation, would

be able to understand the design and operational details of the internal model? Does the documentation clearly explain the outputs of the internal model?

Sign-Off

To demonstrate senior management involvement in your undertaking's internal model development, this document must be signed by the CEO of the undertaking or a board member with specific responsibility for the Solvency II implementation plan. Please be advised that information provided to us in this document may be shared with other EU supervisory authorities for co-ordination purposes. We may request further information and conduct on-site visits to assess the internal model during the pre-application process.

I, the undersigned, confirm that the information contained in this template is accurate to the best of my knowledge and I will be responsible for advising the Financial Regulator should any of this information change during this phase of the pre-application assessment.

Name _____

Signature _____

Date _____

Position _____

Reference Material

The following documents may prove helpful for relevant personnel during the pre-application process:

Level 1 Directive

Articles 110-125 of the directive

CEIOPS Consultation Papers (Level II Implementing Measures)

Consultation Paper 37 (The Procedure to be followed for the Approval of Internal Models)

Consultation Paper 56 (Tests and Standards for Internal Model Approval)

Consultation Paper 65 (Partial Internal Models)

Level 3 Guidance

Consultation Paper 80 (Pre-application Process for Internal Models)



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