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Dear Tracey

### **CP9/13 PRA draft supervisory statement on Solvency II: applying EIOPA's preparatory guidelines to PRA-authorised firms**

I am responding on behalf of the Financial Reporting Council (FRC)<sup>1</sup> with the benefit of input from our advisory Actuarial Council. Our regulatory activities in relation to actuaries and actuarial work contribute to the PRA's objective of ensuring the safety and soundness of PRA-regulated insurers and to securing the appropriate degree of protection for policyholders. The current PRA Handbook recognises this by effectively requiring compliance with our technical standards by life insurers when setting technical provisions<sup>2</sup>.

We understand and generally welcome the PRA's approach and its emphasis on outcomes and judgement, and the responsibility of PRA-authorised insurers to make preparations for implementation of Solvency II by following the EIOPA preparatory guidelines.

Nevertheless the draft statement's flexibility creates some challenges. There is a risk that the current underpin of our technical actuarial standards (TASs) will be in doubt. In turn this creates uncertainties for the professional regulation of actuaries by the Institute and Faculty of Actuaries (IFoA) which we oversee and in respect of which we handle disciplinary cases in the public interest. A variable approach to the supervision of different insurers creates inconsistencies that might threaten actuarial quality and could undermine our ability to oversee the IFoA appropriately and/or take disciplinary action.

#### **Compliance with technical actuarial standards (TASs)**

The Insurance TAS (at C.1.7) provides that our TASs apply to:

*"actuarial work concerning insurance business performed to enable an insurer or its parent undertakings to fulfil their obligations to their regulators ..."*

The difficulty that arises with the draft statement is that it creates a potential ambiguity as to whether the PRA's supervisory expectations can be treated as "obligations" on insurers, and therefore whether actuarial work to support compliance with the EIOPA preparatory guidelines is expected to comply with the TASs.

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<sup>1</sup> The FRC is the independent UK regulator responsible for promoting high quality corporate governance and reporting to foster investment. The FRC sets UK accounting, auditing and technical actuarial standards, maintains the UK Corporate Governance Code and Stewardship Code, and oversees the professional regulation of auditors, accountants and actuaries in the UK.

<sup>2</sup> INSPRU 1.1.6 – 1.1.7

We do not wish to anticipate the full implementation of Solvency II by amending the TASs at this stage. However, we suggest the PRA make clear to insurers that it will expect actuarial work performed in accordance with the EIOPA preparatory guidelines – whether in support of the actuarial function or the risk management function - to comply with the TASs. Compliance with TASs will provide assurance for insurers of the quality of actuarial work in the preparatory period which in turn will contribute to the safety and soundness of PRA-regulated insurers. Additionally, it is consistent with the current regulatory requirement on life insurers when setting insurance technical provisions.

We recognise that the actuarial work required by Solvency II need not be carried out by a member of an actuarial professional body although we expect that much of it will be. However, TASs apply to actuarial work rather than to the person carrying it out which makes their application pertinent to all actuarial work required in preparing for Solvency II.

### **Professional regulation of actuaries**

#### *Actuarial function*

The challenge with the actuarial function particularly in non-life insurance is to facilitate preparations by insurers to make suitable appointments which comply with Article 48(2) of the directive which requires that:

*“The actuarial function shall be carried out by persons who have knowledge of actuarial and financial mathematics, commensurate with the nature, scale and complexity of the risks inherent in the business of the insurance or reinsurance undertaking, and who are able to demonstrate their relevant experience with applicable professional and other standards”.*

Guideline 13 in the Guidelines on Systems of Governance requires that insurers have a policy on the fit and proper requirements which includes a description of the procedure for assessing the fitness and propriety of the persons who hold key functions. As the Morris Review of the Actuarial Profession found in 2005, there is a problem of information asymmetry between actuaries and their clients and employers. One possible consequence is that it may be difficult, particularly for smaller insurers, to make the necessary fitness assessment for the actuarial function and in particular satisfy themselves that Article 48(2) will be met.

The PRA addresses this difficulty in life insurance by itself approving appointments, and this is matched by the IFoA which requires its members to hold a practising certificate confirming that they have relevant experience. However, in the absence of formal PRA requirements for the actuarial function in non-life insurers outside the Lloyd’s market, the IFoA has not to date imposed corresponding requirements on its members.

The IFoA has developed a practising certificates regime for actuaries at Lloyd’s, but this is restricted to members with experience of the Lloyd’s market. As a result, there is a risk of an uneven playing field being created between those with and without a Lloyd’s certificate, or of insurers being expected to rely on an actuary’s professional standing without any objective corroboration of his or her current competence for the role.

We understand that the IFoA is considering an extension of its practising certificate regime to include actuaries wanting to take on the actuarial function role in non-life insurers as part of proposed changes to reflect Solvency II. We welcome this initiative, and we would invite the PRA to support its early development and implementation during the preparatory period. The PRA might for example indicate, without excluding other methods of demonstrating relevant experience, that in reviewing insurers’ procedure for assessing fitness and the

preparatory appointments made, it will recognise practising certificates as tending to demonstrate that members of the IFoA have relevant experience.

#### *Risk management function*

Similar issues arise for Boards in assessing the fitness of the risk management function.

Actuarial qualifications and experience are not essential to carry out this role effectively. However, we are aware that the IFoA has developed with other actuarial associations a qualification, the Chartered Enterprise Risk Actuary (CERA), which aims to equip actuaries to fill the risk management function role in insurers.

We are encouraging the IFoA to consider developing this and other ways of providing assurance to Boards about the current competence of its members seeking to take on the risk management function. We would invite the PRA to support such a development, without of course disadvantaging other competent individuals including non-actuaries.

#### **Monitoring the quality of actuarial work**

Our concern here is that a variable approach to the supervision of insurers' preparations for Solvency II, without sufficient disclosure and transparency, might create inconsistencies in the quality of actuarial work which may lead to a reduction in the safety and soundness of individual insurers. However, we support the PRA's emphasis on outcomes and the exercise of professional judgement which is consistent with our own standards. We will continue to work with the PRA and the IFoA to coordinate our respective monitoring activities in line with our Memorandum of Understanding and our shared commitment to the principle of transparency.

We would welcome the opportunity to discuss the issues we have raised.

Yours sincerely



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