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December 9<sup>th</sup> 2016

## Re: Review of the standard formula Solvency Capital Requirement

Dear Title Surname,

The Central Bank of Ireland ("Central Bank") has recently carried out a review of the solvency capital requirement ("SCR") calculations for a number of life insurance companies. This has highlighted some key control issues relating to these calculations. The purpose of this letter is to bring these issues to your attention so that you can ensure that they or similar issues are not present within your own firm. The general findings were as follows:

**Inadequate controls:** Our review has evidenced inadequate controls and testing around manual spreadsheets used in the SCR calculations. Additionally, the Central Bank has evidenced a large number of instances where the model parameters have been updated incorrectly. There have also been examples of wrong currencies being assumed for funds which understated the SCR results.

**Not meeting Solvency II regulations:** There were a number of instances where the Solvency II regulations were not applied correctly. Firms should have a robust process in place within their governance structures to review and challenge the application of Solvency II regulations guided by the principle of proportionality. Some examples of where the regulations were not applied correctly include contract boundary conditions not meeting the criteria set out in Article 18 of Commission Delegated Regulation (EU) 2015/35 of 10 October 2014; certain expense items excluded from expenses stresses and ring-fenced funds were not subject to stresses consistent with those applied to the firm as a whole.

**Management actions not approved:** Future management actions assumed in the technical provision and SCR calculations, which reduced a firm's expenses, were not supported by a Board approved management action plan. Such a plan is required under Article 23 of Commission Delegated Regulation (EU) 2015/35 of 10 October 2014. The Central Bank requires that future management actions are approved by the Board before inclusion within the technical provision and SCR calculations. The Central Bank also requires that future management actions related to expenses in the SCR calculations are subject to the full expense stresses detailed in Article 140 of Commission Delegated Regulation (EU) 2015/35 of 10 October 2014.



**Employee defined benefit scheme not treated as ring-fenced fund:** When performing the SCR calculations, some standard formula calculations have allowed for diversification of the pension scheme with the firm's other business when calculating the market risk SCR. The Central Bank expects firms using the standard formula to treat employee defined benefit pension schemes as ring-fenced funds with no diversification benefits across other ring-fenced funds and/ or other funds of the company.

Whilst the above issues have been driven by control issues seen in reviewing SCR calculation, they are correlated with wider issues that the Central Bank has seen in the broader Solvency II reporting. Although these have mainly been addressed in the submission of Quarterly Reporting Templates ("QRTs"), the annual reporting represents a step-change in the complexity and breadth of Solvency II reporting requirements. Firms should ensure that their own governance frameworks have the capability and capacity to review, challenge and remediate inaccuracies relating to broader data reporting standards so that the returns clearly represent their business as a whole, and not take false comfort from checks purely relating to the internal consistency of the forms.

Please approach your normal supervision contact if you would like to discuss any of the points raised in this letter.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Sylvia Cronin', written in a cursive style.

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Sylvia Cronin  
Director of Insurance