

**Comments Template on
Consultation Paper on Proposal for Guidelines on Pre-application for Internal
Models**

**Deadline
19 June 2013
12:00 CET**

Name of Company:	Deloitte	
Disclosure comments:	of Please indicate if your comments should be treated as confidential:	Public
<p>Please follow the following instructions for filling in the template:</p> <ul style="list-style-type: none"> ⇒ <u>Do not change the numbering</u> in the column "reference"; if you change numbering, your comment cannot be processed by our IT tool ⇒ Leave the last column <u>empty</u>. ⇒ Please fill in your comment in the relevant row. If you have <u>no comment</u> on a paragraph or a cell, keep the row <u>empty</u>. ⇒ Our IT tool does not allow processing of comments which do not refer to the specific numbers below. <p>Please send the completed template, in Word Format, to CP-13-011@eiopa.europa.eu. Our IT tool does not allow processing of any other formats.</p>		
Reference	Comment	Resolution
General Comment	<p>We welcome the preparatory guidelines as ensuring convergence of practices across Europe ahead of Solvency II's implementation is critical.</p> <p>To improve the contribution of these guidelines to Solvency II preparedness, we believe that they should be cross-referenced with the envisioned Level 2 and Level 3 measures. This would ensure that the preparatory guidelines are actually seen as a "stepping stone" to the full Solvency II requirements and not a separate set of rules, requiring additional work from undertakings already dealing with much change. We feel that if these preparatory guidelines were an additional burden, not a stepping stone to full Solvency II reporting, this would not serve the purpose which EIOPA aim for but, rather, would distract undertakings from their core implementation activities and have a detrimental effect on their work towards compliance.</p>	

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Introduction. General Comment		
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Section I. General Comments		
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1.20.	<p>We believe yearly reports by February may not be frequent enough if the goal is a “checkpoint” to assess progress on the application of the guidelines. This is in particular true if Solvency II is implemented in 2016 (only one “checkpoint” in 2015 will be considered) or 2017 (only two “checkpoints”). We suggest EIOPA request a summary report by July of each year, in order to better assess the progress of harmonization and discuss any issue with NCAs (such as varying pace of implementation, divergence in the application of the guidelines, etc.).</p> <p>We also suggest that EIOPA gives a high-level content for the progress report. A simple option being the organization of the report along each guideline.</p>	
Section II. General Comments		
Chapter 1. General Comments		
1.21.		
1.22.	<p>The guidelines puts the emphasis on the NCA’s “forming a view” on the compliance of undertakings and groups with regards to the requirements for the approval of an internal model. Further to “provide feedback”, the guidelines should also clarify the level of justification and improvement actions expected from the insurer to meet the requirements.</p> <p>It is proposed to complement the wording as “(...) NCAs should form a view on (...). They should communicate their view to the undertakings, with the facts and findings on which such view is based so that undertakings can identify and agree with the NCAs the steps to take to meet the requirements.”</p>	
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Chapter 2. General Comments		

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1.28.	<p>The guidelines reads: “Whilst the quantitative impact of a model change on the Solvency Capital Requirement or on individual components of the Solvency Capital Requirement may be one of the indicators an insurance or reinsurance undertaking plans to use to identify major changes,...”</p> <p>Is there a specific reason why the words “may be” are used? Based upon other paragraphs (e.g. 1.27 and 1.30) one could expect the use of words like “should be”.</p>	
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1.31.	<p>In 1.30, the guidelines states that the effect of “all changes” should be evaluated in combination. In 1.31 it refers to « the combined impact of multiple changes ». We suggest to reword the guideline and refer to “all minor changes taken together” changes instead of “multiple changes”.</p> <p>We also suggest that EIOPA clarify the scope of the word “all”, in terms of timeline: since the inception of the model, the last validation, last calculation, etc. We suggest to define it as “since the last validation“</p>	
1.32.	<p>The guideline says that the “national competent authorities involved“ should form a view on the Model Change policy of the group. This could mean that each related undertakings would have to discuss the group Model Change policy with the local authority, leading to an increased burden of coordination on both sides : undertaking and on the authorities.</p> <p>We suggest rewording as: “the national competent authority of the group should form a view...” (i.e. the “group supervisor”). “The group supervisor should discuss this view with the national competent authorities involved as appropriate”.</p>	
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Chapter 3. General Comments		

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1.39.	The guideline should outline the level of understanding it expects from different staff groups. For example it should not be expected that the Board of a company should have a detailed understanding of copulas or distributions used in the internal model, but are aware of how the results of the internal model can be used and its weakness.	
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Chapter 4. General Comments		
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Chapter 5. General		

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Comments		
1.73.		
1.74.	<p>Section (a): Could EIOPA clarify the difference between “the valuation of assets and liabilities for solvency purposes” and “the internal model for the purpose of Solvency Capital Requirements calculations”. Does the first part relate to the economic balance sheet and the second to the SCR?</p> <p>Section (b) talks about “valuation of assets and liabilities for solvency purposes” whereas other sections in this paragraph talk only about “valuation of assets and liabilities” without mentioning solvency. Could EIOPA clarify whether it is referred to the valuation of assets and liabilities for internal model purposes or for the purpose of calculation of technical provisions?</p> <p>Section (b) – Could EIOPA clarify the difference between “initial valuation of assets and liabilities in the internal model at the valuation date” and “the original valuation of assets and liabilities for solvency purposes”.</p>	
1.75.	In our opinion, consistency between marginal risk distributions and aggregation model should also be considered. We suggest adding this point to the guideline: “(d) the consistency of the probability distributions used for calculating solvency capital requirements for individual risks and the overall solvency capital requirement.”	
1.76.	The Consistency Assessment included in these guidelines has not been included in previous drafts. Clarification is needed around its potential inclusion in the validation tools. If it is to be included in the validation tools, guidance around its importance relative to the other validation tools needs to be provided.	
1.77.		
1.78.	We interpret from this guideline (and also paragraph 1.80) that the Consultation Paper distinguishes between “deviations” and “inconsistencies”. We suggest clarifying what is meant by “deviations” as this can be interpreted in several ways.	
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1.80.	We agree that any inconsistencies should be justified. However additional guidance on how undertakings should justify inconsistencies should be provided.	

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	As the question is whether the correct SCR is calculated, inconsistencies might be acceptable as long as results are not materially misstated. We suggest adding at the end of this paragraph: "... that will lead to material misstatements of the final results".	
Chapter 6. General Comments	The main concept in this chapter is the richness of the Probability Distribution Forecast, which has limited emphasis in the Statistical Quality standards outlined in Article 121 of the Solvency II directive and previous Consultation Papers. This appears to be a shift in focus relative to the Guidelines on other areas of Statistical Quality standards. An explicit definition of "richness" should be given, in a more detailed way than in paragraph 1.15, so as to avoid different interpretations.	
1.81.	We disagree with the word "exhaustive". It would not be possible to ensure exhaustiveness in principle. The use of the word "exhaustive" in this paragraph differs from the materiality approach outlined in article 121 paragraph 4 of the Solvency II directive. Additionally the ORSA should have a qualitative description of risks not covered in the SCR, which conflicts with the word "exhaustive". We suggest to reformulate the requirement and to state that the set of events of the probability distribution forecast should be fit for the identified risk profile. A proposed wording would be: "... ensures that the set of events of the probability distribution forecast underlying the internal model is material and significant ".	
1.82.		
1.83.	We would welcome clarification on the difference between "risk factors" and "variable underlying probability distribution". We suggest adding the requirement that all identified risk drivers that have material impact on the calculation should be properly reflected. The proposed wording would be: "In particular, national competent authorities should form a view on how the insurance or reinsurance undertaking aims to maintain the knowledge of all risk drivers and other factors that have material impact on the behavior of the probability distribution forecast, so that the probability distribution can reflect all relevant characteristics of its risk profile."	
1.84.	Could EIOPA clarify the following statement: "and on how it considers the capability of the techniques to process the knowledge of the risk profile as an important criterion"?	
1.85.	We suggest that the formulation of this paragraph and paragraph 1.81 to be aligned in defining richness or exhaustiveness / materiality of the forecast.	

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1.86.		
1.87.	We suggest replacing the word "rich" with the phrase "sufficiently rich as specified in 1.85".	
1.88.	<p>Section (c): in order to assess the level of probability distribution forecast richness, this section makes a reference to a broad set of requirements for an internal model. However, for example, it is not clear to what extent documentation standards (Article 125) have a direct impact on the level of probability distribution forecast richness. We suggest making this requirement more specific.</p> <p>Section (d): we understand that this section aims at the effect of risk aggregation on the richness of the probability distribution forecast. We suggest reformulating this section to make it more explicit. The proposed wording would be: "...the consistency of the probability distribution forecasts for all the risks in the scope of the internal model and the aggregation method as regards the level of the richness of the probability distribution forecast".</p> <p>Section (e) is a general statement that should apply to all formulated guidelines. This section can be specified once in the general section and be left out here in this specific Chapter.</p>	
1.89.		
1.90.	<p>There is a typo in the word "judgment" in the last line of this paragraph.</p> <p>Although almost all the tests and standards for internal model validation (CEIOPS Former CP 56) are mentioned in the CP-13/011 in specific corresponding chapters, the Statistical Quality Standard is only mentioned as a part of the Chapter on Probability Distribution Forecast. Is this an explicit decision to highlight the importance of the Probability Distribution Forecast?</p>	
Chapter 7. General Comments		
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1.94.	We think this guideline is ambiguous. The text does not follow the heading "Reference risk measure as an intermediate result" so either the heading should be changed or the paragraph should be reworded.	
1.95.	The following statement is included in this paragraph "until t =1", we would suggest that this is reworded to "up to and including t = 1". We also suggest rewording "in any foreseeable situation" as the initial wording "any situation" is not practical and feasible. Section (b) states "there should be no significant variation of this material difference". Additional clarification needs to be given in relation to what a "significant variation" is and if the variation is based on an absolute amount or a percentage amount.	
1.96.	The following statement is included in this paragraph "until t =1", we would suggest that this is reworded to "up to and including t = 1". We also suggest rewording "in any foreseeable situation" as the initial wording "any situation" is not practical and feasible.	
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Chapter 8. General Comments		
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1.103.	Could EIOPA please clarify what is meant by this paragraph? This requirement is unclear.	
1.104.	We suggest adding "attribution" at the end of the sentence: "... uses this variable for the purposes of profit and loss attribution. "	

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1.105.		
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1.107.	We suggest adding a definition for the expression "regular basis". We propose it be defined as "at a minimum annually or more frequently if required". Should this expression be used in several paragraphs in the final version of the guidelines, we suggest to add the definition in paragraph 1.15	
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Chapter 9. General Comments		
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1.138.	<p>We suggest that EIOPA does not single out "stress tests and scenario analysis". Other validation tools could also be considered by national authorities, such as: benchmarking, back-testing...?</p> <p>We suggest at least rewording the paragraph as: "...undertaking uses at least stress tests and scenario analysis as part of..."</p>	
1.139.	Same as in 1.138.	
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Chapter 10. General Comments		
1.142.	We suggest to reword "...regularly reviewed" as "...regularly reviewed and at least yearly".	
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1.146.	The guideline says that the documentation shall include "if available, the history of the development of the methodology, as well as any other methodologies which were considered but not subsequently used..." We believe this requirement will considerably expand the documentation, and would not add much valuable information to the understanding of an undertaking's chosen methodology. Since we expect that the discussion of "any other methodology" will be part of the validation anyway, we believe it is more effective to motivate the methodology used and not put the whole discussion process for a new methodology as part of the documentation.	
1.147.	Section (f) refers to "limitations of information technology used in the internal model". It is unclear whether "information technology" is referring to hardware and/or software. We suggest rewording as: "hardware or software".	
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Chapter 11. General Comments		
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1.155.	Section d): "develops processes to run timely consistency checks including comparisons with other relevant sources". This should be expanded to reflect what other relevant sources EIOPA expect undertakings to use. For example, the following wording could be added: "internal if available or external otherwise" as other sources may be difficult to locate or obtain, such as for asset holding data.	
1.156.		
1.157.	By tying the attention an undertaking should pay to their known risk profile, there is a risk of them missing out on secondary factors that may become material during the period under concern. A more comprehensive view should also be formed. We suggest the rewording : "...and sensitivity testing to ensure that the external model continues to be the correct option" (as opposed to alternative models - internal or external)	
1.158.		
1.159.	The guideline says "...undertaking is not overly reliant on one provider". We believe most undertakings are going to be heavily reliant on one model if they use it. The explanatory text point 3.437 says that "the undertaking may decide on the use of multiple models, as a way to mitigate the risk of over reliance on a particular model". This could result in an inefficient use of resources. It would be useful if EIOPA could give examples (as they do for some of the other guidelines in this chapter) where they think this might happen.	
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1.171.	NCA's should harmonize their expectation (e.g. in the college of supervisors) regarding the specific information for the assessment of an external model. External model providers may be based in different jurisdictions from the undertaking. The information provided may be sufficient for an NCA while not being sufficient by another NCA involved / concerned. The provider may not be willing to provide some information under existing contractual terms and may try to align on the least demanding NCA ; this would be detrimental to insurers overseen by more demanding NCA's	
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Chapter 12. General Comments		
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1.197.	This paragraph could include a stronger statement in relation to sharing tools and techniques. We propose that instead of using "NCAs involved should consider sharing the tools and techniques" the guidelines should state "NCAs involved should share the tools and techniques".	
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Compliance and Reporting Rules		
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