



10 June 2009

Mr. Carlos Montalvo Rebuelta
Secretary General
CEIOPS
Westhafen Tower
Westhafenplatz 1
D-60327 Frankfurt Am Main

Ref.: *CEIOPS-CP-33-09*

Our Ref.: INS/HvD/LF/SR

Dear Mr. Montalvo Rebuelta,

Re: FEE Comments to CEIOPS on Consultation Paper No. 33 Draft CEIOPS' Advice for Level 2 Implementing Measures on Solvency II: System of Governance

- (1) FEE (the Federation of European Accountants) is pleased to provide you below with its comments on the CEIOPS Consultation Paper No. 33 Draft CEIOPS' Advice for Level 2 Implementing Measures on Solvency II: System of Governance ("the Paper").

General comments

- (2) Overall, the paper provides a sensible level of guidance on key governance issues and is largely uncontroversial. There are a number of areas we have identified where some additional guidance would be welcome, perhaps in the form of practical examples.
- (3) We reiterate our comment made earlier this year, in our comments on CEIOPS Issues Paper "Implementing Measures on System of Governance", that it would be helpful if Level 2 implementing measures and potential Level 3 guidance could make clear how the terminology used of "administrative or management body and the organisation of internal supervision" relates to unitary as well as two-tier board systems. Much of the Issues Paper appears to be written in the context of a unitary board system. For this reason, we think that further consideration is required as to how well certain aspects would translate to the two-tier system of governance.

Detailed comments

Paragraph 3.6

- (4) The explanatory text states 'Undertakings should adopt an overall remuneration policy that is in line with its business strategy, risk profile and objectives', however, the following draft CEIOPS advice makes no reference to remuneration policy. This is surprising given that the financial crisis has brought renewed focus on remuneration policies. Remuneration policy at both board and executive levels needs to be aligned with the risk appetite of the undertaking, as misalignment can reduce the effectiveness of the governance system.

Paragraph 3.15

- (5) Paragraph 3.15 notes the level 1 text requirement for the internal audit function not to be combined with other operational duties or functions. In practice, many smaller undertakings combine internal audit, risk management and certain compliance functions. We welcome the CEIOPS recognition of the need for proportionality but note that this requirement risks creating a disproportionate need for internal audit. CEIOPS might also address this by looking at the independence of the internal audit function from the operational processes it is assessing, the potential threats to that independence and any safeguards in place against those threats. We consider that the head of internal audit could have certain risk management and compliance responsibilities without compromising their objectivity if, for example, those additional responsibilities did not involve the operation of control processes.

Paragraph 3.51

- (6) This section provides a good framework for the requirements of the risk management function. However, it would be useful, particularly for smaller insurance undertakings, to have some examples of how this might be applied in practice.
- (7) In 3.53(f) the paper refers to ORSA process, but does not provide any further detail of how this might fit into the risk management function. The ORSA and internal models are both new concepts under Solvency 2 which will be among the most challenging for undertakings to implement. These are the areas where practical examples and additional guidance are most needed and would be most useful. We recognise that CEIOPS has issued a previous paper on the ORSA, we would have expected this additional assistance from CEIOPS on their expectations in these areas and wonder whether the level 3 guidance might include some examples of how this might be applied by different types of organisation.

Paragraph 3.192

- (8) Paragraph 3.192 and the associated text in 3.183 assigns responsibility for how the internal model is integrated into the risk management system and to the risk management function. Overall responsibility for this should sit with the board, although it is sensible for the day to day responsibility for this to be assigned to the risk management function. However, we note that many different functions of the organisations have input into the internal model. Separating responsibilities for the model too strongly from the operational areas of the business might adversely impact on its effectiveness as a risk management tool.
- (9) As noted in our comments in respect of paragraph 3.51 above, this is an area where additional practical examples would be useful. It is not, for example, clear how the internal model is expected to interact with the ORSA process. There is a risk that, without practical examples, firms may apply the ORSA and internal model as additional layers on top of their existing governance structures, rather than fully embedding them, which we believe to be the intention of CEIOPS.
- (10) By assigning responsibility for the risk model to the risk management function, there is a danger, during the transitional phase, that the resources of the risk management function will be diverted towards applying this new responsibility, risking insufficient attention being paid to other areas of risk management. This may create short term resourcing challenges until undertakings have had time to assess their long term staffing needs for their increased responsibilities. Practical examples may make it easier for firms to assess their resource needs.

Paragraph 3.295

- (11) We agree that option 3 under paragraph 3.253 is most appropriate as it provides the opportunity for input from all stakeholders, although note that this will create practical challenges given the tight implementation timetable.
- (12) We agree that option 2 under paragraph 3.262 is most appropriate as some degree of additional prescription would provide useful guidance to firms. However, this guidance should not be overly prescriptive and should not prevent firms from designing the scope of their actuarial function so that it is appropriate and proportionate to the needs of their business and its risks.
- (13) We agree that option 2 under paragraph 3.283 is most appropriate as it is most likely to result in more relevant reporting, appropriate to the risks of the business.

Paragraph 3.309

- (14) Paragraph 3.309 requires the actuarial function to report annually to the administrative or management body. This is an area where greater clarity is needed on the differences between the unitary and two-tier board systems, as noted in our general comments. In this case, we would expect such reporting to be to the supervisory board.

For further information on this letter, please contact Ms. Saskia Slomp from the FEE Secretariat.

Yours sincerely,

A handwritten signature in black ink, appearing to be 'Hans van Damme', written over a horizontal line.

Hans van Damme
President