KPMG

SII - Validation of Technical Provisions

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Formal validation of technical provisions has been a key area of focus for the Actuarial Function of many life (re)insurers. This is not surprising given the explicit requirements set out in Articles 264 and 265 of the Solvency II Delegated Regulation, along with increasing scrutiny from Regulators, External and Internal Auditors, Reviewing Actuary, External Heads of Actuarial Functions and a myriad of other interested parties.

The bar continues to be raised, with the view that if the validation is not evidenced, then it has not been completed. We have benchmarked approaches across the industry through our work in many of the roles outlined above. Our key observations include:

1. **Transparency** of validation processes and controls makes for more efficient engagement with external stakeholders. This can be supported by documenting formal validation policies and producing checklists against regulatory requirements, which can have the added benefit of providing an internal check that all validation requirements have been completed before writing up the Actuarial Report on Technical Provisions ("ARTP"), as required under the Central Bank of Ireland's Domestic Actuarial Regime.

2. **Formal documented attestations** are increasingly seen as a key element in support of data completeness, accuracy and reliability. Insurers with more advanced validation frameworks have defined processes around formalised interactions with key data owners throughout the year so there are no surprises at year end.

3. **Reporting** is emerging as an area of focus, with documentation prepared by the Actuarial Function (e.g. Head of Reserving) for handover to an internal or external Head of Actuarial Function to demonstrate the validation carried out on data, models and results. For many, there is scope to formalise the reporting further and use these as evidence of the key processes and controls around the coordination and calculation of the technical provisions (relates to the point above on "transparency").

4. Article 264 of the Delegated Regulation specifically indicates that an **analysis of movement** is a key validation tool (noting that it has, generally, been a key tool for life (re)insurers for many years). Key enhancements we have observed to this validation process include formally evidenced checks for each of the movement items, with further detail being provided than is required by Solvency II Quantitative Reporting Templates. Audit trails to other relevant sources, such as documentation outlining the impact of any proposed assumption changes or model changes made during the period, also support the validation process. Finally, companies with more advanced validation frameworks have governance and controls in place around the level of "unexplained" items within the analysis of movement, which typically specify maximum acceptable thresholds.

5. There is increasing focus on **formal data validation**[1] within companies, with the aim being to have a proactive data validation program in place, rather than reacting to issues as they arise. Examples of good practice include data quality assessment programs which compare data administration systems against source information. Another key area is the data used for assumption setting, where insurers with more advanced frameworks demonstrate the completeness, reliability and accuracy of this information by formally demonstrating data validation in experience study documentation.

6. There are improvements being observed in **model governance**[2] for the actuarial models used to calculate technical provisions. We are seeing a move towards a regular validation program, where material products and features are being tested on a rolling basis. Furthermore, there is an increasing focus on "out-of-model" elements, with reviews undertaken to assess whether these can be implemented within core models. Where such changes cannot be facilitated, we see undertakings implementing enhancements to the processes and controls around such "out-of-model" items.

7. Assessment and validation of simplified methods, approximations and expert judgment can often be down the list when it comes to validation of technical provisions. More advanced companies have **formal logs** and carry out validation exercises on a **regular basis** ahead of the year-end process. We have found that it is also helpful to list the impact of simplifications, approximations and expert judgement against materiality as part of the overall assessment.

8. Validation is not just a consideration for the Actuarial Function. We have seen, for some companies, that there is wider involvement to support the validation of technical provisions, with Risk Management and Internal Audit carrying out model validation, or the scope of external audits being widened to include this.

The examples listed above can be looked on as a useful touch point as you continue to develop your validation processes.

[1] https://assets.kpmg/content/dam/kpmg/ie/pdf/2020/10/ie-data-governance-in-the-insurance-industry.pdf

[2] https://assets.kpmg/content/dam/kpmg/ie/pdf/2020/11/ie-model-risk-management.pdf

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