MFSA

MALTA FINANCIAL SERVICES AUTHORITY

The System of Governance

18 January 2012

Table of Contents

1. Introduction 1
2. The Board of Directors 2
3. Board Committees 2
4. Business Strategy and Board Policies 3
5. Board Policies 4
6. Remuneration 4
7. Organizational Structure 5
8. Key functions 6
9. Internal Control System 8
10. Compliance function 9
11. Internal Audit function 10
12. Actuarial Function 11
    12.1 Coordination of the calculation of technical provisions 11
    12.2 Providing opinion on the underwriting and reinsurance arrangements 12
    12.3 Contributing to the effective implementation of the risk-management system 13
    12.4 Contributing to the design of an Internal Model 14
    12.5 Annual internal report to the BOD 14
    12.6 Fitness and Propriety of the Actuarial Function 15
13. Outsourcing 15
    13.1 Outsourcing of the underwriting function 16
    13.2 Intra-group Outsourcing 16
14. Fitness and Properness 17
15. Fitness and Properness of service providers 19
16. Notifications 19
17. Records of the Undertaking 20
18. Contingency Planning 20
19. Internal review of the system of governance 21
Annex 22
System of Governance Questionnaire 30

1. Introduction

On the 22 April 2010 the Malta Financial Services Authority (MFSA) issued a guidance paper on the System of Governance requirements under the Solvency II regime. This guidance paper is a follow-up to that paper and is being issued to provide further details on a number of issues and to continue to assist insurance and reinsurance undertakings in their preparations for the Solvency II implementation. As you are aware, the Solvency II requirements are grouped using a three pillar approach. This paper addresses the **Pillar 2** requirements. Although these requirements will become effective after the Solvency II framework comes into force, it is strongly advised that undertakings consider the implications of these requirements and start working towards their implementation. Moreover, most requirements in relation to the System of Governance equally apply under the current regime as they are considered to be principles of best practice and fall within the scope of existing Rules.

The principle of proportionality [1] should be kept in mind when considering the various aspects addressed in this paper as it allows undertakings to design their system of governance in a manner that reflects their operations but still satisfies the regulatory requirements. The individual risk profile of the undertaking should serve as the primary guide in assessing the need to apply the proportionality principle. The undertaking will be required to provide the supervisory authority with the assessment performed, explaining the criteria used in applying the proportionality principle.

The risk management function is an important element of the system of governance but is not addressed in this paper as it will be the subject of another paper to be issued by the MFSA. Similarly, this paper does not include detail on the Own Risk and Solvency Assessment (ORSA) as this was addressed in the Consultation paper issued by EIOPA on the 7th November 2011. Further details on this consultation paper were notified by the MFSA on the same date and are available on the MFSA web-site. This consultation is open until 20 January 2012.

Annexed to this paper is a questionnaire which seeks to determine which systems, processes and procedures insurance undertakings have already implemented, or plan to implement, in preparation for Solvency II with respect to the system of governance. Undertakings are required to respond to the questionnaire by **31 March 2012**. It is being requested that answers to the

[1] Article 41(2) of the Solvency II Directive – "The system of governance shall be proportionate to the nature, scale and complexity of the operations of the insurance or reinsurance undertaking." A consultation paper had been issued by CEIOPS in May 2008 - CEIOPS-DOC-24/08 – Advice to the European Commission on the Principle of Proportionality in the Solvency II Framework Directive Proposal

questions are given as objectively as possible and that the directors review the questionnaire before submission to the MFSA.

It should be noted that although drafting of the Level 3 Guidelines and Recommendations on the System of Governance is at an advanced stage, they are still being developed by EIOPA at the time of publication of this guidance paper and therefore changes may be effected.

2. The Board of Directors

As indicated in the first guidance paper on the System of Governance the term "administrative, management or supervisory body" which is used throughout the Solvency II Directive refers to the board of directors in the case of a one tier system as is the case in Malta. In this guidance paper this term will be shortened to "BOD".

The BOD is the mainstay of the system of governance and is collectively responsible for compliance with the requirements of the Solvency II Directive.

One of the BOD's highest priorities is setting the 'tone at the top' to establish the corporate culture and the values by which executives throughout the undertaking will behave. To this end, the BOD should set a Code of Conduct for itself, senior management and staff. This supports the goal of achieving sound and prudent management. Moreover, the BOD should have regular interaction with committees it establishes, senior management and persons performing tasks related to key functions (See Section 7 of this paper). It is important that the BOD does not passively accept information provided but should actively request any additional information required to make effective decisions and should raise challenge whenever necessary. Sound and prudent management also entails an effective risk management function and the implementation of adequate internal control practices in a consistent manner throughout the organizational structure.***(Article 41(1) of the Solvency II Directive)***

The BOD must also ensure that any significant decision of the undertaking should have the support of at least two persons who are legally responsible for the running of the undertaking or have the necessary decision-making power. Persons effectively running the undertaking are the BOD as well as senior management, who include persons who are responsible for the implementation of strategies and policies established by the BOD and are authorised to take high level decisions. ***(Article 41(1) of the Solvency II Directive)***

3. Board Committees

The BOD may appoint committees to assist it in the governance role but still retains the ultimate responsibility for those functions that are delegated to these committees. The committees should have clear terms of reference and reporting lines. An important element of effective governance is ongoing interaction of the BOD with its committees and regular scrutiny by the BOD, ensuring it requests the information required and raises challenge to its committees, when necessary. ***(Article 41(1) of the Solvency II Directive)***

4. Business Strategy and Board Policies

The BOD is responsible for the development of the overall business strategy which should be supported by written policies that ensure the proper implementation of the strategy. Written policies should be in place in relation to *at least* risk management, internal control, compliance, internal audit and outsourcing, if applicable. It should be noted that the risk management policy should comprise policies for each risk area as set out in Article 44 (2) of the Solvency II Directive (See Para. 3 of Annex to this Guidance Paper). The undertaking should ensure that sufficient policies are developed so as to encompass all the undertaking's processes. Other policies that are referred to in the Solvency II Directive and Implementing Measures are the Remuneration policy, Fit & Proper policy, ORSA policy, Solvency and Financial Condition Report (SFCR) policy and Model change policy, as indicated later on in this paper.

Policies specifically referred to in the Solvency II Directive or Implementing Measures need not be separate but may be combined to align them with the undertaking's organizational business structure and should, in relation to the function or process to which they relate, clearly set out:

a) the goals pursued with the policy;
b) the tasks to be performed and who is responsible for them;
c) the processes and reporting procedures to be applied; and
d) the obligation of the relevant organisational units to inform the risk management, internal audit, compliance and actuarial functions of facts relevant for the discharge of their duties.

The policies that cover the key functions should also address the standing of these functions within the undertaking, their rights and powers.

These written policies and any subsequent amendments thereto are subject to the approval of the BOD and should be reviewed at least annually and when there are material changes to the business structure. This review is to be appropriately documented identifying the reviewer, recommendations made and the BOD's consideration of these recommendations.

The undertaking must ensure effective communication of the written policies and any changes thereto, to staff so that they are familiar with and observe the policies relative to their area of work. To ensure an effective process throughout all levels of the organisation there should be a hierarchy for policy documentation whereby the BOD establishes an overall business strategy which is then supported by a number of underlying strategies each covering specific areas, which would then be detailed in a number of underlying policies and then each policy is translated into a number of processes and procedures, as necessary. The complexity of the structure would be proportionate to the complexity of the undertaking's operations. If a function is outsourced, the outsourcing agreement should then tie in with the established policy for that particular function. ***(Article 41(1)& 41(3) of the Solvency II Directive)***

5. Board Policies

The Solvency II Directive and Implementing Measures refer to a number of written policies that should be developed by the BOD. However, an undertaking may require other policies corresponding to its particular business profile. All policies should comply with the general guidelines specified under *Business Strategy and Board Policies* above (Section 3) and additionally include specificities for the particular policy. The Annex to this paper provides guidelines on the specific policies.

6. Remuneration

The business strategy should incorporate the inherent quality of providing incentives to attract and retain human resources that possess the necessary competence, skills and experience. The remuneration policy is a key element of this aspect but should also ensure that the personnel selected adhere to the risk management strategy and business objectives of the undertaking by providing the correct incentives for staff to make decisions and take risks in line with such strategy as established by the BOD. Where remuneration is related to performance, the undertaking, in performing its assessment, could make use of indicators in relation to the individual's adherence to risk management and compliance. Remuneration awards should never threaten the undertaking's ability to maintain an adequate capital base[2].

Any termination payments should be structured so as to reflect the principles and performance criteria used for the compensation of the individual over the whole period of employment at the undertaking. In this way they will be better aligned with the objectives and implementation of other aspects of the remuneration policy, and avoid rewarding failure.

The remuneration policy should also extend to arrangements of the undertaking with various service providers such as asset managers or investment managers or with intermediaries such as agents, brokers or tied insurance intermediaries involved in marketing and distribution of the undertaking's products. The interests of these service providers and intermediaries may not always be well-aligned with those of the undertaking and remuneration arrangements may

[2] CEIOPS-DOC-51/09- CEIOPS Advice for Level 2 Implementing Measures on Solvency II : Remuneration Issues issued in October 2009 – former Consultation Paper no. 59

incentivize excessive risk-taking behaviour. The undertaking should consider how adjustments to such remuneration arrangements may mitigate such risks.
Therefore the following aspects should be considered with regard to the overall design of the remuneration policy. An undertaking's

a) overall business strategy;
b) risk policy and risk tolerance limits;
c) risk control and governance mechanisms, including those to manage conflicts of interest that may arise
    i) for the individuals establishing the remuneration policy and approving and reviewing the remuneration policy and remuneration contracts;
    ii) for those remunerated for selling or underwriting significant new business that may affect the risk profile of the undertaking;
    iii) for asset managers and the undertaking; and
d) methodology for identifying staff that may have a material impact on the undertaking's risk profile.

Best practice encourages a regular, independent review of the remuneration policy. This would include an assessment of the adequacy of the remuneration levels and that all current and future risks, the solvency position, risk profile and long term objectives of the undertaking are being addressed by the remuneration policy.

An undertaking may decide to establish a remuneration committee. This decision should be guided by the proportionality principle and therefore should consider the size, nature and scope of the business, the complexity of the organisational structure and the corresponding complexity of the remuneration policy and its alignment to the risk profile.

The remuneration committee should be able to exercise competent and independent judgment on the remuneration policy and its oversight. If no remuneration committee is established, the BOD should designate a non-executive director to assume such a role. The committee or designated person should have access to all the data necessary to offer advice and support to the BOD on the development and maintenance of the remuneration policy. The role will also be responsible for regular review of the remuneration policy to ensure it remains appropriate as the undertaking's profile changes and to report to the BOD on the performance of the remuneration policy.

7. Organizational Structure

The effectiveness of governance is reflected in the practical operation of an undertaking and is supported by well-defined organizational and operational structures that are aimed at achieving the established business strategy. Clear reporting lines that reflect information flows and well-defined duties and responsibilities are key factors in the organizational structure of an undertaking. This structure should be documented and kept up-to-date.

It should be ensured that there is sufficient segregation of duties to ensure that the persons performing tasks are not also responsible for monitoring and controlling the adequacy of this performance.

The undertaking should identify any functions which, when performed by the same person, could give rise to conflicts of interest and ensure that these are allocated to different persons. This applies to all levels of the undertaking, including the BOD. Where it is not possible or disproportionate to eliminate the conflicts of interest, then the undertaking has to manage them appropriately to safeguard proper decision-taking or execution of tasks. The periodic rotation of staff assignments is a measure that helps to mitigate the risk of any conflicts of interest.

Key functions should have an appropriate standing within the organisational structure. It is important that such key functionaries have clearly defined responsibilities and adequate authority to assume such responsibilities.

The structure of an organization must also establish well defined communication and reporting procedures so that it is clear what information should be shared, by whom and when. Information should flow up and down the hierarchy levels and horizontally between different departments or business units. ***(Article 41(1) of the Solvency II Directive)***

8. Key functions

The Solvency II Directive refers to four key functions which are **Risk Management, Compliance, Actuarial and Internal Audit**. However, undertakings may have other functions which are of specific importance to the undertaking in view of its business and organization. The undertaking will be required to identify such critical or important functions but may be challenged by the supervisory authority in the determination or non-determination of such functions. Such critical or important operational functions will vary from one undertaking to another. However, it is expected that 'critical' functions will also be 'important'. An important indicator in establishing the importance of a function is the resultant impact on the undertaking should that function be outsourced.

Examples of critical or important functions or activities include:

a) the design and pricing of insurance products;
b) the investment of assets or portfolio management;
c) claims handling;

d) provision of regular or constant compliance, internal audit, accounting, risk management or actuarial support;
e) provision of data storage;
f) provision of ongoing, day-to-day systems maintenance or support; and
g) the ORSA process.

In establishing its organizational structure the undertaking must ensure that:

- The Internal Audit function is ***fully independent*** from all other functions. Therefore, unless it is outsourced, this function must be performed by a separate unit or by an individual who has no other duties within the undertaking ; and

- The structure should achieve ***operational independence*** for the other key functions. This means that the key function is performed without any undue influence, control or constraint by another operational or key function, senior management or the BOD. The key functions have to retain the responsibility for taking the decisions necessary for the proper performance of their duties without interference from others. The BOD is ultimately responsible to review the performance of the key functions and consider any recommendations made by these functions. The decisions or actions taken by the BOD may differ from the opinion of the key function. However, the BOD may not exert influence on the key function so as to alter its recommendations to bring them in line with the BOD's actions.

An undertaking may not want to separate certain key functions such that a person may perform more than one key function. Such undertakings would have to demonstrate that the structure proposed is proportionate with their risk profile and would be required to notify details of the processes and procedures in place to ensure that operational independence will not be compromised.

Operational independence may sometimes be encroached upon even though key functions are performed by different persons. The undertaking must ensure that effective measures are implemented to keep the performance of the key functions free from interference.

In order to achieve operational independence, the key functions should be able to report directly to the BOD without restrictions being imposed by any other person. However, this does not preclude a process whereby such reports would be reviewed for comment by other relevant functions before being passed on to the BOD.

It is important that there is effective interaction between the key functions so that information is shared in a timely and efficient manner by the persons who need it. ***(Article 41(1) & 49 of the Solvency II Directive)***

The following functions should **not** be considered to be critical or key functions:

- Advisory services that do not form part of the undertaking's insurance/reinsurance activities, such as legal advice, the training of personnel, billing services and the security of premises and personnel;
- the purchase of standardised services, including market information services and the provision of price feeds;
- the provision of logistical support, for example, cleaning or catering; and
- the provision of elements of human resources support, such as sourcing temporary employees and processing of payroll.

9. Internal Control System

The BOD should establish policies and procedures that instill a strong internal control system and encourage a high level of integrity. All members of staff should be aware of the internal control system and should understand their role within it such that the system is embedded in the overall culture of the undertaking. ***(Article 46(1) of the Solvency II Directive)***

Internal control combines the following aspects:

a) control environment
b) control activities
c) communication
d) monitoring

An effective internal control system should apply at the various levels of the organizational structure and its time horizons should be relevant to the internal processes and should include sufficient detail, as required by the risk profile of the undertaking. A few examples of possible control activities are authorizations, approvals, reconciliations, reviews of processes and/or results, checks on adherence to compliance requirements and access to hardware, software systems and data. Internal controls should also identify and manage possible conflicts of interest.

The undertaking should also ensure that internal controls facilitate effective and timely communication to ensure that accurate and timely reports are produced. The internal control system should empower management to monitor systems and identify any weaknesses.

Moreover, the undertaking should encourage suggestions for improvements and allow reporting lines to be sidelined if a serious situation renders such action necessary so as to enable negative information to flow upwards and prevent it being suppressed.

The internal control system itself should be monitored continuously to ensure that any necessary improvements are implemented. The internal audit function plays an important role in auditing the internal control system. ***(Article 46(1) of the Solvency II Directive)***

10. Compliance function

The Compliance function is a key function that should identify all areas of business activity of the undertaking that are susceptible to compliance risk and implement the necessary controls to ensure that the undertaking complies with the applicable laws and regulatory requirements. This encompasses - but is not restricted to - licensing requirements, disclosure requirements during the selling of products, proper monitoring of all distribution channels and third party service providers used by the undertaking, advertising requirements, reporting and public disclosure requirements and compliance with general good provisions imposed by host jurisdictions when an undertaking carries out activities under freedom of establishment or the freedom of services provisions. The role demands a sound knowledge of the applicable laws and regulatory requirements and is responsible for creating an awareness among staff of the undertaking and providing the necessary training to enable them to identify compliance risks or report breaches as necessary.
The undertaking should develop a compliance plan that details the work to be undertaken during the forthcoming business year and ensuring that all areas of business activity that are susceptible to compliance risk are addressed. Some examples of compliance activities are:

a) drawing up guidelines and procedures for the staff relating to compliance matters;
b) enhancing staff awareness and ensuring continuous training of staff on compliance matters;
c) recording any incident that must be reported and ensure that the undertaking fulfils the obligations as regards notification to third parties;
d) investigating and following up violations of the laws and regulations;
e) advising on new products, services and markets from a compliance point of view;
f) monitor projected revisions of legislation and plans to introduce new regulation and assess their potential impact on the undertaking and monitor the relevant court decisions; and
g) regular reporting, at least annually, to the BOD on compliance issues.

(Article 46(2) of the Solvency II Directive)

11. Internal Audit function

The internal audit function is an independent function that is established within the structure of the undertaking to examine and appraise the system of governance of the undertaking, in particular the effectiveness of the internal control environment. It is therefore an important role that assists the BOD in fulfilling its responsibilities by reviewing various processes and activities and reporting to the BOD with recommendations, as necessary. However, the internal audit function must be completely independent from any interference in performing its work and must not be under instruction from the BOD, to ensure impartiality. The internal audit function must also be allowed to express its findings without reserve. To this end, the internal audit function must have appropriate standing and authority within the organizational structure.

The person/s involved in internal audit cannot be involved in any operational activities of the undertaking or in developing or introducing internal controls. Moreover, internally recruited auditors should not audit activities or functions which they performed in the recent past. This will ensure that the internal audit function is performed in an objective manner. However, the internal audit function also has a secondary consultative function and may therefore be consulted for an opinion on specific matters related to achieving compliance with the internal control principles without impinging on the independence of the basic function.

The scope of the internal audit function is very wide in that it encompasses all the activities of the undertaking and all elements of the system of governance. The function includes, amongst others, a review of all the processes and relevant controls at various levels of the operation; verification of compliance with established policies, in particular risk tolerance limits; and assessments of electronic information systems used together with the quality of records and data available both for internal and external reporting.

Although an undertaking may have established a separate function to monitor a specific activity as part of the internal control system, the internal audit function would still be required to audit that specific activity. However, in so doing, the internal audit function may make use of information provided by the control functions. Nonetheless, the internal audit function remains responsible for its appraisal.

An annual audit plan should be developed and the audit cycle should result in a review of all the significant activities of the undertaking within a reasonable period of time. The audit plan should clearly establish the objectives of the planned reviews and clearly define the methodology to be applied for the scrutiny. It is expected that the internal audit function is well documented in working papers that reflect the work done and support the findings. Such working papers should permit a review of the effectiveness of the internal audit function, such that the methodology and results achieved are retraceable. The findings should be presented to the BOD in a written report without delay. Any shortcomings should be identified and recommendations made with the relevant timelines to address the shortcomings and identifying the person responsible for the corrective action. Such recommendations should be monitored by the internal audit function to ensure proper and timely implementation.

The BOD should regularly assess the internal audit function to ensure it has adequate resources and powers to perform its function effectively and should review the audit plan and receive an internal audit report, at least annually, which report should identify the level of execution of the audit plan and the extent of implementation of recommendations arising from the reviews performed. ***(Article 47 of the Solvency II Directive)***

12. Actuarial Function

The actuarial function required under the Solvency II regime acts as a safeguard that certain control tasks of an undertaking are based on expert technical actuarial advice. It is a coordinating function that reviews and assesses the assumptions made and the methodologies adopted by the undertaking in evaluating its technical provisions; reviews the underwriting policy and the reinsurance policy of the undertaking and their impact on the technical provisions; assesses the quality of internal data and any external data that is integrated into the calculation of the technical provisions and contributes towards an effective implementation of the risk management system. Therefore there must be effective communication between the actuarial function and the risk management function to integrate the actuarial perspective into the risk management function.

The actuarial function should be carried out by persons who have knowledge of actuarial and financial mathematics, commensurate with the proportionality principle. Persons performing this role should demonstrate their relevant experience with applicable professional and other standards.

12.1 Coordination of the calculation of technical provisions

One of the tasks of the actuarial function is the coordination of the calculation of technical provisions. Whilst this does not explicitly include the actual calculations of the technical provisions, the actuarial function is responsible for ensuring the appropriateness of methodologies and assumptions used in these calculations, as well as carrying out an assessment of the quality of data used in such calculations.

The methodologies used to calculate technical provisions should be validated by the actuarial function and this includes back-testing such methodologies against past experience. Moreover the actuarial function should also ensure that the assumptions and methodologies underlying the calculation of technical provisions appropriately reflect all risks.

Where there are material deviations among the estimates of technical provisions for different years the actuarial function should interpret these differences and provide an explanation in terms of their sources and propose appropriate changes to address such differences. The results of such reviews should be reported to the BOD to assist in the understanding of the calculations and to empower the BOD to make decisions regarding the issue.

It is up to the undertaking to decide who should perform the calculation of technical provisions as long as conflicts of interest are well managed if multiple roles are performed by one individual. However it is important to note that, like the actuarial function, the persons performing the calculation of technical provisions are subject to the requirement of knowledge of actuarial and financial mathematics, commensurate with the nature, scale and complexity of the risks accepted by the undertaking. Such expertise should be demonstrated with applicable professional and other standards.

The undertaking must ensure that where personnel or business units perform multiple tasks, conflicts of interest are adequately managed to ensure that the function is performed in a sound, honest and objective manner. Separate reporting lines strengthens segregation of duties but where full segregation is considered to be unreasonable and disproportionate, the undertaking may implement other arrangements to ensure that the conflicts of interest which result are managed in an appropriate way. Essentially, the person performing a task should not assess or control the same task. This equally applies to the person who calculates technical provisions and the person who provides an opinion on the calculations. Similarly, the actuarial function cannot provide an independent opinion on the underwriting policy and reinsurance arrangements of the undertaking if the actuarial function is the main driver in establishing those policies. ***(Article 48 of the Solvency II Directive)***

12.2 Providing opinion on the underwriting and reinsurance arrangements

Persons carrying out the actuarial function can provide a different perspective from underwriters and reinsurance teams due to differing skills and experience and their assessment of the underwriting policy and reinsurance arrangements of the undertaking will therefore provide the BOD with a fuller understanding. The actuarial opinion should, if necessary, include recommendations regarding the most appropriate strategies to be adopted by the undertaking in this respect.

The actuarial function should identify the interrelationships between an undertaking's reinsurance arrangements, underwriting policy and technical provisions.

The opinion on the overall underwriting policy should include the following issues:

- Ensuring consistency with product pricing;

- Identifying principal risk factors that influence profitability of business to be written in the following year such as inflation, legal risk and changes in the market environment;
- The likely financial impact of any material changes in the terms and conditions of products; and
- The degree of variability surrounding the estimate of expected profit and whether this extent of variability is consistent with the undertaking's risk appetite.

The opinion on the adequacy of reinsurance arrangements should include the following issues:

- Consistency of the undertaking's reinsurance arrangements with the undertaking's risk appetite;
- The effect of reinsurance on the estimation of net technical provisions and on the volatility of the undertaking's financial strength; and
- The performance of the reinsurance arrangements under different stress scenarios.

The requirement on the actuarial function to express an opinion on the overall underwriting and reinsurance policies does not imply that the actuarial function may not be involved in the original decisions on these issues. However, in such instances, the actuarial review should include more detail and include an assessment of possible alternatives. ***(Article 48 of the Solvency II Directive)***

12.3 Contributing to the effective implementation of the risk-management system

There are strong links between the tasks to be performed by the risk management function and the actuarial function and the two functions should support each other. The two functions may be partially or fully integrated but conflicts of interest must be managed appropriately.

The actuarial function is particularly involved in the risk assessment that underlies the calculation of the solvency capital requirement (SCR) and minimum capital requirement (MCR) as this will, to varying degrees of complexity, require a sound understanding of the probabilities of insurance risks, such as mortality, morbidity, claims frequencies and severities, risk mitigation techniques, volatility and deviations. The calculation of SCR and MCR is subject to review and the undertaking must therefore avoid any conflict of interests if it decides to appoint the actuarial function to be involved in the calculation and also carry out the review.

The actuarial function is also involved in the ORSA process as it assesses the compliance of technical provisions with the relevant requirements and analyses deviations of the risk profile of the undertaking from the assumptions underlying the calculation of the SCR, whether by using the standard formula or with a partial or full internal model.

Companies with an internal model should view the model as a widely-understood risk management tool and not purely a mathematical model. The risk management function is responsible for a number of areas of the internal model but it is expected that the actuarial function should assist in the design, implementation, testing and validation of the internal model. The actuarial function could also be a user of the model, as the output of the internal model can be used to support the analyses carried out by the function. Additionally, the communication loop between the actuarial function and the risk management function should allow sharing of insights on the model which could lead to the detection of shortcomings and proposals of improvement of the model. ***(Article 48 of the Solvency II Directive)***

12.4 Contributing to the design of an Internal Model

When an undertaking develops an internal model, the actuarial function contributes towards the design of the internal model by providing an opinion as to the scope of the internal model i.e. which risks should be covered by the internal model and how dependencies between risks should be derived. In providing this opinion, the actuarial function must perform a technical analysis which reflects the experience and expert judgement of the function.

The technical analysis will necessitate consideration of the level of data quality required for the model. Since the actuarial function is responsible for analysing the sufficiency and quality of internal and external data used to calculate technical provisions, it is in a position to provide such an opinion regarding any limitations of data quality. Similarly, the actuarial function assesses the assumptions underlying the calculation of technical provisions. Such assumptions should be consistent with the assumptions applied to the calculation of the SCR and are therefore an important factor in developing the modelling of underwriting risks. Therefore the input of the actuarial function is essential. The actuarial function may also be involved in the validation tasks which include the collection and analysis of data related to actual against expected experience.

12.5 Annual internal report to the BOD

On an annual basis the actuarial function needs to report to the BOD on at least the following:

(a) a description of the methodologies applied to assess the sufficiency of technical provisions and an explanation on why such methodologies were chosen (paragraph 1b[3]);

(b) a description of the relevant underlying assumptions inherent to the application of the methodologies to calculate technical provisions and to assess its sufficiency, including an analysis of the level of uncertainty if applicable (paragraph 1b + 1f[3]);

(c) a general description of the review made to data used to perform the calculation of technical provisions (paragraph 1c + 1f[3]);

[3] The paragraphs being referred to are the respective paragraphs of Article 48 of the Solvency II Directive.

(d) a description and justification of the differences identified among the estimates of different years, if material (paragraph1d + 1f[3]);

(e) the conclusions of the process of comparison of best estimates against experience. The results should be commented and in particular any sources of deviation expressed in the output of the analysis should be explained (paragraph 1d[3]);

(f) an opinion on the overall underwriting policy (paragraph 1g[3]);

(g) an opinion on the overall reinsurance policy (paragraph 1g[3]); and

(h) a description of the contribution to the risk modelling underlying the calculation of the capital requirements (paragraph 1i[3]).

The actuarial function should also present to the BOD any shortcomings that it identifies together with recommendations as to how these can be overcome. Such shortcomings may relate to data, technical procedures, methodologies and/or knowledge. The undertaking should have adequate follow-up procedures to monitor the implementation of corrective action to address the shortcomings that are identified. ***(Article 48 of the Solvency II Directive)***

12.6 Fitness and Propriety of the Actuarial Function

The assessment of the fitness and propriety of the actuarial function is aligned to the requirements as specified in the relevant section of this paper. Whilst no additional standards for the function are expected from a Solvency II perspective, other than those indicated in Article 48 (2) of the Solvency II Directive and in the actuarial guidelines that are expected to be issued by EIOPA in the near future, undertakings may wish to consult or refer to actuarial or other professional standards or guidance issued by actuarial or other professional bodies as an additional benchmark. ***(Article 42 of the Solvency II Directive)***

13. Outsourcing

Any outsourcing arrangements other than those relating to activities ***which are not*** critical or important/key operational activities (see section 7 above) must be notified to and approved by the supervisory authority prior to the outsourcing. Such arrangements must also be supported by a written agreement. Although an undertaking may decide to outsource certain functions the BOD remains fully responsible for those functions and must therefore manage the risk generated by the outsourcing. The undertaking should have sufficient competence and established procedures to monitor and review the service provider on an on-going basis and ensure the function is performed in accordance with the agreed terms. Provisions should be made for circumstances where the service provider fails to deliver the expected level of service. Care should also be exercised when a service provider is outside the EU to ensure that there are no local laws or regulations that limit access to the premises of or data held by the service provider both by the undertaking and its home regulator.

Before outsourcing any function, the undertaking should carry out a due diligence process on the service provider, irrespective of whether it is a supervised entity or an entity within the same group[4]. The due diligence process should assess:

i) the technical and financial ability of the service provider and its capacity to perform the outsourced function and

ii) the internal control system of the service provider

The results of the due diligence should enable the undertaking to assess the level of risk it is facing as a result of the outsourcing.

Care should be taken to avoid any conflicts of interest that may exist between the undertaking and the service provider or arrangements with competitors. The due diligence exercise performed by the undertaking and its outcome should be documented to enable subsequent review at any time. Upon notification of the outsourcing of a key function as described under section 16 of this guidance paper, the supervisory authority may request the service provider to submit evidence that it satisfies the fitness and properness requirements and may ask the service provider to provide the supporting documentation necessary to assess the fitness and properness (See section 14 below).

13.1 Outsourcing of the underwriting function

Where an undertaking grants underwriting and/or claims settlement authority to an insurance intermediary, this is considered to be an outsourcing of a critical or important function and is subject to the requirements of Article 49 of the Solvency II Directive and relevant Level III Guidelines that will be issued.

Other typical intermediary activities as described under Article 2(3) of the Insurance Mediation Directive - such as introducing, performing preparatory work leading to conclusion of the contracts of insurance and assistance in administering or performing the contracts of insurance, particularly in the event of a claim - are not subject to the Solvency II outsourcing requirements.

13.2 Intra-group Outsourcing

Where the appointed service provider is a legal entity within the same group a written outsourcing agreement is still required but may take the form of a service level agreement as intra-group negotiations may be less formal. However, the undertaking should still assess the service provider, albeit in a less detailed manner, on the understanding that the management of the undertaking is familiar with the group processes and controls and personnel of the service

[4] Article 42(1) of the Solvency II Directive – Insurance and reinsurance undertakings shall ensure that all persons who effectively run the undertaking or have other key functions at all times fulfil the following requirements: (a) their professional qualifications, knowledge and experience are adequate to enable sound and prudent management (fit); and (b) they are of good repute and integrity (proper).

provider. The undertaking should take into consideration the level of control it may exercise on the service provider and the power it has to influence the actions of the service provider in relation to its outsourced activity. ***(Article 49 of the Solvency II Directive)***

14. Fitness and Properness

All persons effectively running the undertaking and all persons working within a key function must be 'fit and proper'. The undertaking must itself assess the fitness and propriety of all persons effectively running the undertaking as well as all persons *working within* (as opposed to being responsible for) a key function..

Moreover, the undertaking must formally notify the supervisory authority of the appointment of persons to be responsible for a key function or persons who effectively run the undertaking and submit the information necessary to assess whether the individual concerned is fit and proper.

The fit and proper requirements demand qualities in relation to the integrity demonstrated in personal behaviour and business conduct, soundness of judgement and a sufficient degree of knowledge, experience and professional qualifications. The qualifications and experience of other employees within the undertaking may be taken into consideration when assessing the level of competence and experience required for a particular role.

An undertaking should not only have procedures in place to perform the fitness and properness assessment of personnel at the time of employment but should incorporate ongoing assessment of professional training requirements to ensure that personnel are kept abreast with the changing or increasing demands of their role.

To satisfy the 'fitness' criteria, the collective knowledge, competence and experience of the BOD should at a minimum include:

a) Market knowledge - the awareness and understanding of the wider business, economic and market environment in which the undertaking operates and the knowledge and needs of policyholders;
b) Business strategy and Business model - an appropriately detailed understanding of the undertaking's business strategy and model;
c) System of governance - this includes risk management and control, which means the awareness and understanding of the risks the undertaking is facing and the capability of managing them. Furthermore the ability to assess the effectiveness of the undertaking's arrangements to deliver effective governance, oversight and controls in the business and, if necessary, oversee changes in these areas;

d) Financial and actuarial analysis - the ability to interpret the undertaking's financial and actuarial information, identify key issues, put in place appropriate controls and take necessary measures based on this information;
e) Regulatory framework and requirements - awareness and understanding of the regulatory framework in which the undertaking operates, and the regulatory requirements and expectations relevant to it and the capacity to adapt to changes which stem from the regulatory framework without delay.

The individual directors are not each expected to possess expert knowledge, competence and experience on all areas of the undertaking. However, the collective knowledge, competence and experience of the BOD as a whole has to provide for a sound and prudent management of the undertaking. This collective knowledge must be maintained at all times so that any change in the members of the BOD will also be considered from this perspective. The undertaking will be required to demonstrate that such collective knowledge is maintained. ***(Article 42 (1a) of the Solvency II Directive)***

Propriety

The assessment of the propriety of a person will take into consideration the reputation and integrity of a person. Honesty is one of the qualities to be considered and in this respect the financial soundness of a person may have an impact on his behaviour. Similarly, conflicts of interest may influence a person's behaviour and should be avoided as best possible. The assessment will also consider :

- any conviction for criminal offences, in particular under the laws governing banking, financial, securities or insurance activity or concerning securities markets, securities or payment instruments and include laws on money laundering, market manipulation or insider dealing and usury as well as any offences of dishonesty such as fraud or financial crime. It will also consider any other offences under legislation relating to companies, bankruptcy, insolvency, or consumer protection;
- other criminal offences currently being tried or that were tried in the past may also be relevant as they may cast doubt on the integrity of the person;
- disciplinary or administrative offences made under a financial sector activity, including offences under legislation relating to companies, bankruptcy, insolvency or consumer protection;
- current investigations or enforcement actions or administrative sanctions for non-compliance with provisions governing banking, financial, securities or insurance activity, securities markets, securities or payment instruments or any financial services legislation;

- current investigations or enforcement actions by any relevant regulatory or professional body for non-compliance with any relevant provisions;

The required level of propriety is not affected in any way by the proportionality principle in that the same standards apply irrespective of the nature, scale and complexity of the risks inherent to the business or of the undertaking's risk profile.

Propriety considerations are relevant for all employees of an undertaking, However, any assessment should take into account their level of responsibility within the undertaking and will differ proportionately, according to whether or not, for example, they are persons effectively running the undertaking or holding a key function. ***(Article 42 (1b) of the Solvency II Directive)***

15. Fitness and Properness of service providers

When an undertaking outsources a key function, it must ascertain that the service provider had performed a fitness and propriety assessment of all the employees who will carry out the outsourced function for the undertaking. In addition, a person within the undertaking should have overall responsibility for oversight of that outsourced function and should also be assessed to be fit and proper for that role. This person within the undertaking may not have deep technical knowledge or expertise to the extent required of the persons within the service provider performing the function. However, the person within the undertaking remains responsible for the outsourced function and should be able to challenge the performance and results of the service provider. On the other hand, the service provider should possess a sufficient level of knowledge, experience and professional qualifications to perform the function. ***(Article 42 of the Solvency II Directive)***

16. Notifications

Undertakings must identify the positions within their organizational structure which effectively run the undertaking and those which are considered to be key functions. The supervisory authority must be notified of these management positions and key functions, together with the reasons why those positions or functions were selected and the names of the individuals performing the roles identified. Any new appointments in such roles, or terminations or changes must also be notified to the supervisory authority, together with the supporting criteria for the action taken.

When an undertaking outsources a critical or important function (sections 8 and 13 above refer), the supervisory authority must also be notified accordingly. The notification should include a description of the outsourced activity/function and the service provider selected to perform this function. Where this function is also a key function, the notification must include the identity of the person within the service provider who will be responsible for the function and the person within the undertaking who is responsible for oversight of that outsourced key function. The draft outsourcing agreement should also be submitted. Further notification requirements may result if concerns arise over time in relation to the services provided that necessitate a re-assessment of the outsourcing arrangements. ***(Article 42 and 49 of the Solvency II Directive)***

17. Records of the Undertaking

Undertakings must ensure that the information systems used provide sufficient, reliable, consistent and timely data for all the activities undertaken and to record the risks borne by the undertaking. This information system should be managed effectively, restricting access to particular areas to the persons who need it and limiting such access to 'passive' access where necessary. At the same time, it should be ensured that personnel have the necessary data to discharge their duties.

Undertakings are required to keep orderly and adequate records of their business activities and such records are to be kept for an appropriate time frame, taking into consideration any prescribed record retention periods under legislation. ***(Article 41(1) of the Solvency II Directive)***

18. Contingency Planning

Undertakings are required to have documented contingency or business continuity plans which should aim to achieve a predetermined minimum level of activity after a disruption, whether it is caused by a natural disaster or a man-made event. The contingency plan should consider all the significant activities of the undertaking and should be subject to regular testing and review. The relevant personnel involved in the plan should be provided with the plan and made aware of their role. ***(Article 41(4) of the Solvency II Directive)***

In the case of outsourcing, irrespective of the service provider's governance obligation to establish suitable contingency plans for the function outsourced by the undertaking, the undertaking needs to consider in its own contingency planning how to take the outsourcing away from the current service provider and give it to another service provider, or bring it back in-house, as appropriate.

19. Internal review of the system of governance

The BOD should establish a regular internal review of the system of governance which encompasses all the activities covered in this guidance paper and must determine the scope and frequency of such reviews and who is to perform them. The findings of the internal audit function as regards the system of governance may also serve as input for this review. The review should involve interaction with the key functions and allow feedback. The BOD should then be provided with a report and recommendations, as necessary. Discussions and decisions should be well documented and followed up to ensure implementation. ***(Article 41 (3) of the Solvency II Directive)***

Annex

Board Policies

The following are the policies referred to in the Solvency II Directive and Implementing Measures. However, an undertaking may require other policies corresponding to its particular business profile. **As explained in the guidance paper, all policies should comply with the general guidelines specified under the section *Business Strategy and Board Policies* and additionally include the following specificities:**

1. **Business continuity policy**

Insurance and reinsurance undertakings shall establish, implement and maintain a business continuity policy aimed at ensuring, in the case of an interruption to their systems and procedures, the preservation of essential data and functions and the maintenance of insurance and reinsurance activities, or, where that is not possible, the timely recovery of such data and functions and the timely resumption of their insurance or reinsurance activities.

(Art. 41(1) to (4) of the Solvency II Directive)

2. **Fit and proper policy**

The undertaking's policy on Fit and Proper should include:

(a) a description of the procedure of the notification to the supervisory authority for each of the notification situations as mentioned in the guidance paper under Section 15;

(b) a description of the procedure of assessing fitness and propriety of persons who are effectively running the undertaking or have a key function, both initially at the time of employment and on an on-going basis;

(c) a description of the minimum situations that give rise to a re- assessment of fitness and propriety so as to establish whether a person should no longer continue to be regarded as fit and proper; and

(d) a description of the procedure for assessing the fitness and propriety of other relevant personnel, both initially and on an on-going basis.

(Article 42 of the Solvency II Directive)

3. **Risk management policy**

The risk management policy should:

(a) define the risk categories and the methods applied to measure the risks;

(b) outline how the undertaking manages each relevant category and area of risks;

(c) describe the connection with the overall solvency needs assessment as identified in the ORSA, the regulatory capital requirements and the undertaking's risk tolerance limits;

(d) specify risk tolerance limits within all relevant risk categories in line with the undertaking's overall risk appetite;

(e) set out the frequency and content of regular stress tests , as well as describe the situations that would warrant special stress tests; and

(f) consider all other policies and sub-policies defined by the undertaking.

(Article 44 (2) of the Solvency II Directive)

In the Risk Management policy, the undertaking should consider at least the following sub-policies:

3.1 Underwriting and reserving risk

In the risk management policy, the undertaking should consider at least the following with regards to underwriting and reserving risk:

(a) The classes and characteristics of the insurance business (i.e. the type of insurance risk) the undertaking is willing to accept; Where appropriate, the maximum acceptable exposure to specific risk concentrations; internal underwriting limits for the various products/classes; and considerations regarding reinsurance and other risk mitigation techniques and their effectiveness.

(b) How the adequacy of premium income to cover expected claims and expenses is to be ensured;

(c) The identification of the risks arising from the undertaking's insurance obligations, including embedded options and guaranteed surrender values in the products;

(d) How, in the design of a new insurance product and the premium calculation, the undertaking takes account of the constraints related to investments, for example:
   i) An undertaking planning to sell a new life product with minimum guaranteed rate has to take into account the return available on the market;
   ii) An undertaking planning to sell a new P&C contract has to take into account the liquidity constrains that could be linked to the contract;

(e) How in the design of a new insurance product and the premium calculation, the undertaking takes account of reinsurance or other risk mitigation techniques.

The undertaking should ensure that all policies and procedures established for underwriting are applied by all its distribution channels.

(Article 44 (2) of the Solvency II Directive)

3.2 Operational risk

In the risk management policy, the undertaking should consider at least the following with regards to operational risk:

(a) Identification of the operational risks it is or might be exposed to and the way to mitigate it;

(b) All activities and internal processes in place in the undertaking, including the IT system supporting them; and

(c) Risk tolerance limits with respect to the undertaking's key operational risk areas.

(Articles 44 (2) of the Solvency II Directive)

3.3 Reinsurance and other risk mitigation techniques

In the risk management policy the undertaking should consider at least the following with regard to reinsurance and other risk mitigation techniques:

(a) Identification of the level of risk transfer appropriate to the undertaking's defined risk limits and which kind of reinsurance arrangements are most appropriate considering the undertaking's risk profile;

(b) Principles for the selection of reinsurance counterparties and procedures for assessing and monitoring the creditworthiness and diversification of reinsurance counterparties;

(c) Procedures for assessing the effective risk transfer;

(d) Liquidity management to deal with any timing mismatch between claims' payments and reinsurance recoveries; and

(e) Procedures for ensuring that policyholders continue to receive benefits in line with aims and of objectives originally communicated to them.

(Articles 44 (2) of the Solvency II Directive)

3.4 Asset-Liability Management

In the risk management policy the undertaking should consider at least the following with regard to Asset-Liability Management:

(a) Description of the procedure for identification and assessment of different natures of mismatches between assets and liabilities, at least with regard to terms and currency;

(b) Description of mitigation techniques used;

(c) Description of the mismatches that deliberately will be left uncovered, and the content and frequency of stress-tests to monitor them; and

(d) Description of the underlying methodology and frequency of stress-tests and scenario tests to be carried out.

(Article 44 (2) of the Solvency II Directive)

3.5 Investments

In the risk management policy the undertaking should consider at least the following with regard to investments:

(a) the level of security, quality, liquidity, profitability and availability the undertaking is aiming for with regard to the whole portfolio of assets and how it aims at achieving this;

(b) the internal quantitative limits on assets and exposures, including off-balance sheet exposures, that will help the undertaking achieve its desired level of security, quality, liquidity, profitability and availability for the portfolio;

(c) the financial market environment;

(d) conditions under which the undertaking can pledge or lend assets;

(e) the link between market risk and other risks in highly adverse scenarios;

(f) the procedure of appropriately valuating and verifying the investment assets;

(g) the procedures to monitor the performance and review the policy when necessary; and

(h) how the assets are to be selected in the best interests of policyholders and beneficiaries.

(Article 44 (2) & (3) of the Solvency II Directive)

3.6 Liquidity risk

In the risk management policy the undertaking should consider at least the following with regard to liquidity risk:

(a) the procedure for determining the level of mismatch between the cash inflows and the cash outflows of both assets and liabilities, including expected cash flows of direct insurance and reinsurance such as claims, lapses or surrenders;

(b) the total liquidity needs in the short and medium term including an appropriate buffer for liquidity shortfall;

(c) the level and monitoring of liquid assets, including a quantification of potential costs or financial losses arising from an enforced realisation;

(d) the identification and cost of alternative financing tools; and

(e) the effect on the liquidity situation of expected new business.

(Article 44 (2) of the Solvency II Directive)

3.7 Derivatives

When an undertaking uses derivatives as an investment strategy, the risk management policy should, in the section of investments, additionally at least consider:

(a) setting internal limits on investment in derivatives recognising the underlying exposure generated by the derivative;

(b) applying appropriate stress and scenario testing, including reverse stress testing; and

(c) a process that provides for the global derivative exposure to be calculated on a regular basis and generally at least daily.

(Article 132 of the Solvency II Directive)

4. Compliance policy

Undertakings need to have a compliance policy in place. The compliance policy should comply with the guidelines specified under the section **Business Strategy and Board Policies** above.

(Article 46 (2) of the Solvency II Directive)

5. **Internal Audit policy**

The undertaking should have in place an audit policy and such policy should include at least:

(a) the terms and conditions according to which the internal audit function can be called upon to give its opinion or assistance or to carry out other special tasks;

(b) internal rules setting out the procedures the person responsible for the internal audit function needs to follow before informing the supervisory authority.

(Article 47 (1) of the Solvency II Directive)

6. **Outsourcing policy**

An undertaking that outsources or considers outsourcing should develop a written policy which complies with the applicable requirements and additionally includes at least the undertaking's processes and strategies for outsourcing from inception to the end of the contract. In particular, it needs to set out:

(a) how a service provider of suitable quality is to be selected;

(b) the details to be included in the written agreement;

(c) how the outsourcing is to be managed and monitored; and

(d) business contingency plans, including exit strategies.

(Article 49 of the Solvency II Directive)

7. **Policy for changing the internal model**

Companies with an internal model shall have in place a policy for changing the model. The policy shall set out, amongst others, the governance requirements in relation to changes to the internal model, including internal approval of changes, internal communication, documentation and validation of changes. The policy for changing the internal model foresees that the internal model is changed, where relevant, to reflect changes in the risk management system.

(Article 115 of the Solvency II Directive)

8. Policy on data used in the internal model

With respect to the data used in the internal model, insurance and reinsurance undertakings shall establish, implement and maintain a written data policy which covers the following areas:

(a) the definition and assessment of the quality of data, including specific qualitative and quantitative standards for different data sets, based on the criteria of accuracy, completeness and appropriateness;

(b) the use and setting of assumptions made in the collection, processing and application of data;

(c) the process for carrying out data updates, including the frequency of regular updates and the circumstances that trigger additional updates and recalculations of the probability distribution forecast.

(Art. 121 of the Solvency II Directive)

9. Validation policy

Insurance and reinsurance undertakings shall establish, implement and maintain a written validation policy which describes the validation processes to be used. The validation policy shall specify at least:

(a) the purpose and the scope of the validation policy;

(b) the processes and methods used to validate the internal model;

(c) for each part of the internal model, the frequency of regular validations and the circumstances which trigger additional validation;

(d) the persons who are responsible for each validation task;

(e) the procedure to be followed in the event that the validation process identifies problems with the reliability of the internal model and the decision-making process to address those concerns;

(f) an assessment by the insurance or reinsurance undertaking of the quality of the validation process;

(g) an assessment of the independence of the validation process taking into account:
  - in relation to the internal validation process, the responsibilities and reporting structure of the persons involved in the process,

- in relation to any external validation process, the remuneration structure of the persons, including where applicable their employees or other persons acting on their behalf, who are involved in the process and any other mandates of these persons relating to the insurance or reinsurance undertaking,

(h) in the case of a partial internal model, the scope of the model, the integration technique to integrate the partial internal model into the standard formula and its appropriateness.

(Art. 124 of the Solvency II Directive)

10. Remuneration policy

In the remuneration policy the undertaking should at least ensure that:

a) the remuneration policy is well-integrated and in line with the business and risk management strategies and system of governance;

b) remuneration arrangements with service providers do not encourage excessive risk-taking; and

c) remuneration awards do not threaten the undertaking’s ability to maintain an adequate capital base.

System of Governance Questionnaire

Please read the Guidance Paper before completing this questionnaire.

Q1(a). Has the undertaking performed a gap analysis relative to Solvency II requirements in relation to the System of Governance?

Please tick the relevant box

Yes ☐

No ☐

Q1(b). What gaps were identified and what are the planned measures to be adopted to address such gaps?

Please attach a summary of the gaps identified and of the planned measures

If the reply to above is negative, are there plans to perform such a gap analysis? ***Please tick the relevant box***

Yes ☐

No ☐

Q2 What is the timeframe anticipated for its completion? ____________

Q3 Board of Directors

a. How many directors are non-executive directors? ☐

Please fill in the relevant number

Please identify them:

____

____

____

____

b. How many of the non-executive directors are also independent ☐

(A director is considered to be independent when he is free from any business, family or other relationship with the company, its controlling shareholder or the management of either – that creates a conflict of interest such as to jeopardise exercise of his free judgement)?

Please fill in the relevant number

Please identify them:

____

____

____

____

c. In what area of competence and/or experience does each director contribute towards the collective knowledge of the Board for sound and prudent management of the undertaking? (Refer to Section 14 of the Guidance Paper (pg 18))
Please tick the relevant box(es). ***More than one box can be ticked for the same director***

Name of Director	**a**	**b**	**c**	**d**	**e**
1. ___________________	☐	☐	☐	☐	☐
2. ___________________	☐	☐	☐	☐	☐
3. ___________________	☐	☐	☐	☐	☐
4. ___________________	☐	☐	☐	☐	☐
5. ___________________	☐	☐	☐	☐	☐
6. ___________________	☐	☐	☐	☐	☐
7. ___________________	☐	☐	☐	☐	☐
8. ___________________	☐	☐	☐	☐	☐
9. ___________________	☐	☐	☐	☐	☐

d. Please provide a brief description of the qualifications/experience of the director relative to each area of competence identified above.

Director 1

____

____

____

Director 2

Director 3

Director 4

Director 5

Director 6

Director 7

Director 8

Director 9

____

____

____

e. Does the board perform self-assessments?
Please tick the relevant box

Yes ☐
No ☐

f. If yes, when was the last one performed?

____

g. Are Directors required to undergo due diligence checks at least on an annual basis?
Please tick the relevant box

Yes ☐
No ☐

If yes, describe the due diligence checks that are generally carried out.

____

____

____

h. Are Directors required to declare any convictions, fines, disciplinary or administrative offences (including offences under legislation relation to companies, bankruptcy, insolvency or consumer protection) or penalties imposed upon them or court cases they may become involved in?
Please tick the relevant box

Yes ☐
No ☐

Q4 Board Strategy/Policies

a. Has the Board developed a formal written overall business strategy?
Please tick the relevant box

Yes ☐
No ☐

b. How often is this strategy reviewed? ____________

c. Have written policies been developed to support this strategy?
Please tick the relevant box

Yes ☐
No ☐

i. If yes, which policies are completed?

____

____

____

____

____

____

____

____

____

ii. If not, what is the anticipated timeline for completion?

____

iii. Is there a written remuneration policy that also covers directors' remuneration?
Please tick the relevant box

Yes ☐
No ☐

d. Has the undertaking developed a Code of Conduct for all its staff including the Board of Directors?
Please tick the relevant box

Yes ☐
No ☐

e. Does this address the manner in which conflicts of interest are to be managed by the Board?
Please tick the relevant box

Yes ☐
No ☐

f. What circumstances or developments give rise to a re-assessment of the fitness & properness of key persons within the undertaking including the directors?

____

____

____

____

____

Q5 Board Committees

a. Are there any new board committees other than those notified to the MFSA as at December 2010?
Please tick the relevant box

Yes ☐
No ☐

If yes, please describe the committee's role, identify its members and submit its terms of reference.

____

____

____

____

b. Has the Board appointed a remuneration committee?
Please tick the relevant box

Yes ☐
No ☐

If not, who is the non-executive director responsible for the remuneration policy and its oversight?

____

c. Where there any changes to the board committees notified to the MFSA as at December 2010?
Please tick the relevant box

Yes ☐
No ☐

If yes, please describe relevant changes.

____

____

____

d. Are all board committees operative?
Please tick the relevant box

Yes ☐
No ☐

If not, please advise when the committee(s) will start to function.

____

e. Does the Board review minutes of all its board committees?
Please tick the relevant box

Yes ☐
No ☐

If not, how does it monitor the committees' activities and assess its effectiveness? What form of reporting is adopted? How often?

____

____

____

____

____

Q6 Persons that effectively run the undertaking and Key Functions (***Enclose an updated organisational structure)***

a. Does any significant decision of the undertaking require the support of at least two persons who are legally responsible for the running of the undertaking or have the necessary decision-making power?
Please tick the relevant box

Yes ☐
No ☐

Please identify these persons and position held:

____

____

____

____

b. Name and describe the positions within the organisation that effectively run the undertaking. Give reasons for identifying these positions.

Name of individual ___________________	Name of individual: ___________________
Position: ____________________________	Position: ____________________________
Role: _______________________________	Role: _______________________________
Reason: _____________________________	Reason: _____________________________
Name of individual ___________________	Name of individual: ___________________
Position: ____________________________	Position: ____________________________
Role: _______________________________	Role: _______________________________
Reason: _____________________________	Reason: _____________________________
Name of individual ___________________	Name of individual: ___________________
Position: ____________________________	Position: ____________________________
Role: _______________________________	Role: _______________________________

Reason: ______________________________ Reason: ______________________________

______________________________________ ______________________________________

______________________________________ ______________________________________

______________________________________ ______________________________________

______________________________________ ______________________________________

Name of individual ___________________ Name of individual: ___________________

Position: _____________________________ Position: _____________________________

Role: ________________________________ Role: ________________________________

Reason: ______________________________ Reason: ______________________________

______________________________________ ______________________________________

______________________________________ ______________________________________

______________________________________ ______________________________________

______________________________________ ______________________________________

c. The following functions are considered to be key functions:

- Risk Management
- Compliance
- Internal Audit
- Actuarial

Please identify the persons responsible for each key function.

Key function	**Person responsible**
Risk Management	
Compliance	
Internal Audit	
Actuarial	

List ***other*** functions which the Board considers to be critical or important functions in the undertaking, identifying the person responsible for each function and stating the reasons why such function is considered as critical or important to the undertaking?

Other critical or important function	
Person responsible	
Reason	

Other critical or important function	
Person responsible	
Reason	

Other critical or important function	
Person responsible	
Reason	

d. Are all the key/critical or important functions operationally independent?
Please tick the relevant box

Yes ☐
No ☐

If not operationally independent, please describe processes in place to safeguard proper decision-taking and/or execution of tasks so that the key/critical or important function is not compromised.

____

____

____

____

____

____

____

____

____

e. Do all key/critical or important functions report directly to the Board?
Please tick the relevant box

Yes ☐
No ☐

f. Are persons responsible for and persons performing key/critical or important functions required to undergo due diligence checks at least on an annual basis? ***Please tick the relevant box***

Yes ☐
No ☐

If yes, describe the due diligence checks that are generally carried out.

____

____

____

g. Is the internal audit function completely independent from the operational areas being audited?
Please tick the relevant box

Yes ☐
No ☐

Was the person performing the internal audit function involved in any operative role in the recent past; a role that he/she is now auditing?
Please tick the relevant box

Yes ☐
No ☐

If yes, which role/s?

____

Does the internal audit function extend to all outsourced activities?
Please tick the relevant box

Yes ☐
No ☐

How often is the full cycle of the undertaking's processes reviewed? ____________

h. Who is the director designated for oversight of the Risk Management system?

____

i. Does the Risk Management system provide for stress testing?
Please tick the relevant box

Yes ☐
No ☐

How often? ____________

j. Is the Board informed of the methodologies applied to assess the sufficiency of technical provisions?
Please tick the relevant box

Yes ☐
No ☐

By whom? ____________

k. Is any key function outsourced or will it be?
Please tick the relevant box

Yes ☐
No ☐

If yes, who is the person within the undertaking responsible for oversight of the outsourcing of the function?

Key function outsourced *(delete as applicable)*	**Person responsible for oversight of the outsourcing of the function**
Risk Management	
Compliance	
Internal Audit	
Actuarial	

Q7 Outsourcing

a. Has the undertaking notified the MFSA of all its outsourcing arrangements, whether intra-group outsourcing or to third party service providers?
Please tick the relevant box

Yes ☐
No ☐

If not, please provide details and submit a draft copy of the outsourcing agreement.

b. Are all such arrangements supported by a written agreement/formal appointment?
Please tick the relevant box

Yes ☐
No ☐

If yes, has this agreement/appointment been submitted to the MFSA?
Please tick the relevant box

Yes ☐
No ☐

c. Did the undertaking perform a due diligence exercise on the service provider before entering into the outsourcing agreement?
Please tick the relevant box

Yes ☐
No ☐

If yes, describe the due diligence checks that were carried out.

d. Please identify any delegated underwriting or claims settling authority to an intermediary which has not yet been notified to the MFSA?

____

____

____

____

e. Are any third party service providers/intermediaries of the undertaking located outside the EU?
Please tick the relevant box

Yes ☐
No ☐

If yes, please identify the service provider/intermediary, the outsourced function and the relevant jurisdiction.

Service provider/intermediary	Outsourced function	Jurisdiction

Q8 Information Systems

a. What software systems are in place to support the undertaking's internal processes?

____

____

____

____

b. Are there any concerns regarding data quality?
Please tick the relevant box

Yes ☐
No ☐

c. Are major enhancements necessary to satisfy data requirements under Solvency II?
Please tick the relevant box

Yes ☐
No ☐

d. Are clear records kept of personnel who need access to specific areas of the information system to provide input and/or personnel with passive access to retrieve data for the performance of their duties?
Please tick the relevant box

Yes ☐
No ☐

Q9 General Governance

a. Is the undertaking's system of governance subject to internal review?
Please tick the relevant box

Yes ☐
No ☐

b. Does the Board determine the scope and frequency of such a review?
Please tick the relevant box

Yes ☐
No ☐

c. Who performs these reviews and how often are they performed? _____________
Does the internal audit function provide input to this review?
Please tick the relevant box

Yes ☐
No ☐

d. Does the Board receive a written report on the findings of this review?
Please tick the relevant box

Yes ☐
No ☐

e. Does the undertaking have a Business Continuity Plan?
Please tick the relevant box

Yes ☐
No ☐

How often is it reviewed? ____________________

Signed by : ___________________________________ _______________
Director **Date**

Checklist of documents to be attached to the questionnaire (where applicable):

1. A summary of the gaps identified and of the planned measures – Question 1(b);
2. Terms of reference of new board appointed committees – Question 5 (a)
3. Updated organisational structure setting out the management structure, key functionaries, committees, third party service providers and reporting lines. – Question 6
4. Draft copy of outsourcing agreement/s not yet submitted to the Authority – Question 7(a)