

# **Guidelines on system of governance**

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### **1. Introduction**

- 1.1. According to Article 16 of Regulation (EU) 1094/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (hereinafter "EIOPA Regulation")<sup>1</sup>, EIOPA issues these Guidelines addressed to the supervisory authorities on how to proceed with the application of Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance (hereinafter "Solvency II")<sup>2</sup>.
- 1.2. These Guidelines are based on Articles 40 to 49, Article 93, Article 132 and Article 246 of Solvency II and on Articles 258 to Article 275 of Commission Delegated Regulation (EU) 2015/35 of 10 October 2014 supplementing Directive 2009/138/EC ("Commission Delegated Regulation 2015/35")<sup>3</sup>.
- 1.3. The requirements on the system of governance are aimed at providing for sound and prudent management of the business of undertakings without unduly restricting them in choosing their own organisational structure, as long as they establish an appropriate segregation of duties.
- 1.4. At least the four functions included in the system of governance, namely the risk management, the compliance, the actuarial and the internal audit function, are considered to be key functions and consequently also important or critical functions. Furthermore, persons are considered to be persons having key functions if they perform functions of specific importance for the undertaking in view of its business and organisation. These additional key functions, if any, are identified by the undertaking, but the determination of whether such functions should be considered key or not may be challenged by the supervisory authority.
- 1.5. These Guidelines provide further details on a number of issues regarding remuneration policy, including the composition of the remuneration committee.
- 1.6. The fit and proper requirements apply to all persons who effectively run the undertaking or have other key functions in order to ensure that all the persons having relevant functions in the undertaking are appropriately qualified. The scope of the requirements aims to avoid gaps where important persons for the undertaking are not covered, accepting at the same time that there may well be considerable overlap between persons from senior management who are considered to effectively run the undertaking and other key function holders.
- 1.7. The notification requirements only apply to persons who effectively run the undertaking or are key function holders as opposed to persons who have or perform a key function. In case of outsourcing of a key function or of

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<sup>1</sup> OJ L 331, 15.12.2010, p. 48.

<sup>2</sup> OJ L 335, 17.12.2009, p. 1.

<sup>3</sup> OJ L 12, 17.01.2015, p. 1.

outsourcing of a part of a function where this part is regarded as key, the person responsible is considered to be the one who has the oversight over the outsourcing at the undertaking.

- 1.8. The Guidelines on risk management take as a starting point that an adequate risk management system requires an effective and efficient set of integrated measures which must fit into the organisation and operational activity of the undertaking. There is no single risk management system that is appropriate to all undertakings; the system must be tailored to the individual undertaking.
- 1.9. Although the own risk and solvency assessment (hereinafter "ORSA") is part of the risk management system, the corresponding Guidelines are set out separately.
- 1.10. While internal models are mentioned in connection with the responsibilities of the risk management function, on the whole, the Guidelines on the system of governance do not address specific internal model related issues.
- 1.11. Article 132 of Solvency II introduces the 'prudent person principle' which includes provisions on how undertakings should invest their assets. The absence of regulatory limits on investments does not mean that undertakings can take investment decisions without any regard to prudence and to the interests of policyholders. The requirements of Solvency II and of the Commission Delegated Regulation 2015/35 cover extensively some of the main aspects of the prudent person principle, such as asset-liability management, investment in derivatives, liquidity risk management and concentration risk management. Therefore, the intention of these Guidelines is not to further develop these aspects, but to focus on the remaining aspects of the prudent person principle.
- 1.12. With respect to the actuarial function, these Guidelines focus on what should be done by the actuarial function, rather than how it should be performed. As the purpose of having the actuarial function is to provide a measure of quality assurance through expert technical actuarial advice, it is especially important to establish specific technical guidance on the tasks, responsibilities and other aspects of the actuarial function.
- 1.13. Currently, the institution of the "responsible/appointed actuary" exists in some Member States. As the "responsible/appointed actuary" is not foreseen by Solvency II, it is up to the supervisory authorities concerned to decide on whether to keep the "responsible/appointed actuary" or not, and how it relates to the actuarial function. However, this issue is not addressed under these Guidelines.
- 1.14. The Guidelines on outsourcing are based on the principle that an undertaking has to ensure that it remains fully responsible for discharging all its obligations when outsourcing any function or activities. In particular, there are strict and rigorous measures an undertaking must meet if it outsources a critical or important function or activity. In particular, an undertaking has to give proper consideration to the content of the written agreement with the service provider.

- 1.15. Intra-group outsourcing is not necessarily different from external outsourcing. It may allow for a more flexible selection process, but it should not to be seen as automatically requiring less care and oversight than external outsourcing.
- 1.16. The Guidelines apply to both individual undertakings and mutatis mutandis at group level. Additionally, for groups the group specific Guidelines apply.
- 1.17. The implementation of governance requirements at group level should be understood as having in place a robust governance system applied to one coherent economic entity (holistic view) comprising all entities that are part of the group.
- 1.18. Solvency II requires that all the insurance and reinsurance undertakings in a group have in place a risk management system and an internal control system and that this requirement is applied in a consistent manner in the group. However, from a group risk management and governance perspective, the group and the group supervisor have also to take into account the risks arising from other entities that are part of the group.
- 1.19. When the Guidelines refer to entities that are part of the group, in general, they refer to insurance and reinsurance undertakings, but also to all the other entities that are part of the group.
- 1.20. The governance requirements at group level take into account the corporate governance responsibilities of both, the administrative, management or supervisory body at group level, that is, the administrative, management or supervisory body of the participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company, and the administrative, management or supervisory body of legal entities that are part of the group.
- 1.21. For the purpose of these Guidelines, the following definitions have been developed:
  - 'persons who effectively run the undertaking' cover members of the administrative, management or supervisory body taking into account national law, as well as members of the senior management. The latter includes persons employed by the undertaking who are responsible for high level decision making and for implementing the strategies devised and the policies approved by the administrative, management or supervisory body;
  - 'persons having other key functions' include all persons performing tasks related to a key function;
  - 'key function holders' are the persons responsible for a key function as opposed to persons having, carrying out or performing a key function.
- 1.22. If not defined in these Guidelines the terms have the meaning defined in the legal acts referred to in the introduction.
- 1.23. The Guidelines shall apply from 1 January 2016.

### **Guideline 1 - The administrative, management or supervisory body**

- 1.24. The administrative, management or supervisory body (hereinafter "AMSB") should have appropriate interaction with any committee it establishes as well as with senior management and with persons having other key functions in the undertaking, proactively requesting relevant information from them and challenging that information when necessary.
- 1.25. At group level the AMSB of the participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should have an appropriate interaction with the AMSB of all entities within the group that have a material impact on the risk profile of the group, requesting information proactively and challenging the decisions in the matters that may affect the group.

### **Guideline 2 – Organisational and operational structure**

- 1.26. The undertaking should have organisational and operational structures aimed at supporting the strategic objectives and operations of the undertaking. Such structures should be adapted to changes in the strategic objectives, operations or in the business environment of the undertaking within an appropriate period of time.
- 1.27. At group level, the AMSB of the participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should assess how changes to the group's structure impact the financial position of the affected undertakings of the group and make the necessary adjustments in a timely manner.
- 1.28. The AMSB of the participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should, in order to take appropriate measures, have an appropriate knowledge of the corporate organisation of the group, the business model of its different entities and the links and relationships between them and the risks arising from the group's structure.

### **Guideline 3 – Significant decisions**

- 1.29. The undertaking should ensure that any significant decision of the undertaking involves at least two persons who effectively run the undertaking before the decision is being implemented.

### **Guideline 4 - Documentation of decisions taken at the level of the AMSB**

- 1.30. The undertaking should appropriately document the decisions taken at the level of the AMSB of the undertaking and how information from the risk management system has been taken into account.

## **Guideline 5 - Allocation and segregation of duties and responsibilities**

- 1.31. The undertaking should ensure that the duties and responsibilities are allocated, segregated and coordinated in line with the undertaking's policies and reflected in descriptions of tasks and responsibilities. The undertaking should ensure that all the important duties are covered and that unnecessary overlaps are avoided. Effective cooperation between personnel should be fostered.

## **Guideline 6 - Internal review of the system of governance**

- 1.32. The AMSB of the undertaking should determine the scope and frequency of the internal reviews of the system of governance, taking into account the nature, scale and complexity of the business both at individual and at group level, as well as the structure of the group.
- 1.33. The undertaking should ensure that the scope, findings and conclusions of the review are properly documented and reported to its AMSB. Suitable feedback loops are necessary to ensure follow-up actions are undertaken and recorded.

## **Guideline 7 – Policies**

- 1.34. The undertaking should align all policies required as part of the system of governance with each other and with its business strategy. Each policy should clearly set out at least:
- a) the goals pursued by the policy;
  - b) the tasks to be performed and the person or role responsible for them;
  - c) the processes and reporting procedures to be applied;
  - d) the obligation of the relevant organisational units to inform the risk management, internal audit, compliance and actuarial functions of any facts relevant for the performance of their duties.
- 1.35. In the policies that cover the key functions, the undertaking should also address the position of these functions within the undertaking, their rights and powers.
- 1.36. The participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should ensure that the policies are implemented consistently across the group. In addition, it ensures that the policies of the entities of the group are consistent with the group policies.

## **Guideline 8 - Contingency plans**

- 1.37. The undertaking should identify material risks to be addressed by contingency plans covering the areas where it considers itself to be vulnerable, and it should review, update and test these contingency plans on a regular basis.

## **Section 2: Remuneration**

### **Guideline 9 - Scope of the remuneration policy**

- 1.38. In its remuneration policy the undertaking should at least ensure that:
- a) remuneration awards do not threaten the undertaking's ability to maintain an adequate capital base;
  - b) remuneration arrangements with service providers do not encourage risk-taking that is excessive in view of the undertaking's risk management strategy.
- 1.39. The participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should adopt and implement a remuneration policy for the whole group. This should take into account the complexity and structures of the group in order to establish, develop and implement a consistent policy for the whole group that is in line with the group's risk management strategies. The policy should be applied to all relevant persons at group and individual entity level.
- 1.40. The participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should ensure:
- a) an overall consistency of the group's remuneration policies by ensuring that they comply with the legal requirements of undertakings which are part of the group and by verifying their correct application;
  - b) that all undertakings that belong to the group comply with the remuneration requirements;
  - c) that material risks at group level linked to remuneration issues in the group entities are managed.

### **Guideline 10 - Remuneration committee**

- 1.41. The undertaking should ensure that the composition of the remuneration committee enables it to exercise a competent and independent judgment on the remuneration policy and its oversight. If no remuneration committee is established, the AMSB should assume the tasks that would otherwise have been assigned to a remuneration committee in a way that avoids conflicts of interest.

## **Section 3: Fit and proper**

### **Guideline 11 – Fit requirements**

- 1.42. The undertaking should ensure that persons who effectively run the undertaking or have other key functions are 'fit' and take account of the respective duties allocated to individual persons to ensure appropriate diversity of qualifications, knowledge and relevant experience so that the undertaking is managed and overseen in a professional manner.

- 1.43. The AMSB should collectively possess appropriate qualification, experience and knowledge about at least:
- a) insurance and financial markets;
  - b) business strategy and business model;
  - c) system of governance;
  - d) financial and actuarial analysis;
  - e) regulatory framework and requirements.

#### **Guideline 12 - Proper requirements**

- 1.44. When assessing whether a person is 'proper', the undertaking should consider that the period of limitation of the relevant criminal or any other offence is lapsed based on national law.

#### **Guideline 13 - Fit and proper policies and procedures**

- 1.45. The undertaking should have a policy on the fit and proper requirements, which includes at least:
- a) a description of the procedure for identifying the positions for which notifying is required and for the notification to the supervisory authority;
  - b) a description of the procedure for assessing the fitness and propriety of the persons who effectively run the undertaking or have other key functions, both when being considered for the specific position and on an on-going basis;
  - c) a description of the situations that give rise to a re-assessment of the fit and proper requirements;
  - d) a description of the procedure for assessing the skills, knowledge, expertise and personal integrity of other relevant personnel not subject to the requirements of Article 42 of Solvency II according to internal standards, both when being considered for the specific position and on an on-going basis.

#### **Guideline 14 - Outsourcing of key functions**

- 1.46. The undertaking should apply the fit and proper procedures in assessing persons employed by the service provider or sub service provider to perform an outsourced key function.
- 1.47. The undertaking should designate a person within the undertaking with overall responsibility for the outsourced key function who is fit and proper and possesses sufficient knowledge and experience regarding the outsourced key function to be able to challenge the performance and results of the service provider. This designated person should be considered as the person responsible for the key function according to Article 42 (2) of Solvency II that needs to be notified to the supervisory authority.



## **Guideline 15 - Notification**

1.48. The supervisory authority should require as a minimum from the undertaking the information included in the Technical Annex<sup>4</sup> to be submitted by means of a notification.

## **Guideline 16 - Assessment of the fit and proper requirements by the supervisory authority**

1.49. The supervisory authority should assess the fit and proper requirements of the persons subject to notification requirements and give feedback on this to the undertaking concerned within an appropriate timeframe from the receipt of a complete notification.

## **Section 4: Risk management**

### **Guideline 17 - Role of the AMSB in the risk management system**

1.50. The AMSB should be ultimately responsible for ensuring the effectiveness of the risk management system, setting the undertaking's risk appetite and overall risk tolerance limits, as well as approving the main risk management strategies and policies.

1.51. The AMSB of the participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should ensure that the risk management system of the whole group is effective. This risk management system of the group should include at least:

- a) the strategic decisions and policies on risk management at group level;
- b) the definition of group's risk appetite and overall risk tolerance limits;
- c) the identification, measurement, management, monitoring and reporting of risks at group level.

1.52. The AMSB of the participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should ensure that such strategic decisions and policies are consistent with the group's structure, size and the specificities of the entities that are part of the group.

### **Guideline 18 - Risk management policy**

1.53. The undertaking should establish a risk management policy which at least:

- a) defines the risk categories and the methods to measure the risks;
- b) outlines how the undertaking manages each relevant category, area of risks and any potential aggregation of risks;

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<sup>4</sup> Technical Annex is available in EIOPA's webpage Publications/EIOPA\_Guidelines

- c) describes 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) specifies risk tolerance limits within all relevant risk categories in line with the undertaking's risk appetite;
- e) describes the frequency and content of regular stress tests and the situations that would warrant ad-hoc stress tests.

#### **Guideline 19 - Risk management function: tasks**

1.54. The undertaking should require the risk management function to report to the AMSB on risks that have been identified as potentially material. The risk management function should also report on other specific areas of risks both on its own initiative and following requests from the AMSB.

#### **Guideline 20 - Underwriting and reserving risk management policy**

1.55. In its risk management policy, the undertaking should cover at least the following with regard to underwriting and reserve risk:

- a) the types and characteristics of the insurance business, such as the type of insurance risk the undertaking is willing to accept;
- b) how the sufficiency 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 its products;
- d) how, in the process of designing a new insurance product and the premium calculation, the undertaking takes account of the constraints related to investments;
- e) how, in the process of designing a new insurance product and the premium calculation, the undertaking takes account of reinsurance or other risk mitigation techniques.

#### **Guideline 21 - Operational risk management policy**

1.56. In the risk management policy, the undertaking should cover at least the following with regard to operational risk:

- a) identification of the operational risks it is or might be exposed to and assessment of the way to mitigate them;
- b) activities and internal processes for managing operational risks, including the IT system supporting them;
- c) risk tolerance limits with respect to the undertaking's main operational risk areas.

- 1.57. The undertaking should have processes to identify, analyse and report on operational risk events. For this purpose, it should establish a process for collecting and monitoring operational risk events.
- 1.58. For the purposes of operational risk management, the undertaking should develop and analyse an appropriate set of operational risk scenarios based on at least the following approaches:
- a) the failure of a key process, personnel or system;
  - b) the occurrence of external events.

**Guideline 22 - Reinsurance and other risk-mitigation techniques – risk management policy**

- 1.59. In the risk management policy the undertaking should cover 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 tolerance limits and which kind of reinsurance arrangements are most appropriate considering the undertaking's risk profile;
  - b) principles for the selection of such risk mitigation counterparties and procedures for assessing and monitoring the creditworthiness and diversification of reinsurance counterparties;
  - c) procedures for assessing the effective risk transfer and consideration of basis risk;
  - d) liquidity management procedures to deal with any timing mismatch between claims' payments and reinsurance recoverable.

**Guideline 23 - Strategic and reputational risk**

- 1.60. The undertaking should manage, monitor and report the following situations:
- a) actual or potential exposure to reputational and strategic risks and the interrelationship between these risks and other material risks;
  - b) key issues affecting its reputation, considering the expectations of stakeholders and the sensitivity of the market.

**Guideline 24 - Asset-liability management policy**

- 1.61. In its risk management policy the undertaking should cover at least the following information with regard to asset-liability management:
- a) 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) a description of mitigation techniques to be used and the expected effect of relevant risk-mitigating techniques on asset-liability management;
  - c) a description of deliberate mismatches permitted;

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

### **Guideline 25 - Investment risk management policy**

- 1.62. In its risk management policy the undertaking should cover at least the following information with regard to investments:
- a) the level of security, quality, liquidity and profitability the undertaking is aiming for with regard to the whole portfolio of assets and how it plans to achieve this;
  - b) its quantitative limits on assets and exposures, including off-balance sheet exposures, that are to be established to help to ensure the undertaking achieves its desired level of security, quality, liquidity, profitability and availability for the portfolio;
  - c) the level of availability the undertaking is aiming for with regard to the whole portfolio of assets and how it plans to achieve this
  - d) consideration of the financial market environment;
  - e) the conditions under which the undertaking can pledge or lend assets;
  - f) the link between market risk and other risks in adverse scenarios;
  - g) the procedure for appropriately valuing and verifying the investment assets;
  - h) the procedures to monitor the performance of the investments and review the policy when necessary;
  - i) how the assets are to be selected in the best interest of policyholders and beneficiaries.

### **Guideline 26 - Liquidity risk management policy**

- 1.63. In its risk management policy the undertaking should cover at least the following information 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) consideration of total liquidity needs in the short and medium term, including an appropriate liquidity buffer to guard against a liquidity shortfall;
  - c) consideration of the level and monitoring of liquid assets, including a quantification of potential costs or financial losses arising from an enforced realisation;
  - d) identification and costs of alternative financing tools;
  - e) consideration of the effect on the liquidity situation of expected new business.

## **Section 5: The prudent person principle and the system of governance**

### **Guideline 27 - Investment risk management**

- 1.64. The undertaking should not solely depend on the information provided by third parties, such as financial institutions, asset managers and rating agencies. In particular, the undertaking should develop its own set of key risk indicators in line with its investment risk management policy and business strategy.
- 1.65. When making its investment decisions, the undertaking should take into account the risks associated with the investments without relying only on the risk being adequately captured by the capital requirements.

### **Guideline 28 – Assessment of non-routine investment activities**

- 1.66. Before performing any investment or investment activity of a non-routine nature the undertaking should carry out an assessment of at least:
- a) its ability to perform and manage the investment or the investment activity;
  - b) the risks specifically related to the investment or the investment activity and the impact of the investment or the investment activity on the undertaking's risk profile;
  - c) the consistency of the investment or investment activity with the beneficiaries' and policyholders' interest, liability constraints set by the undertaking and efficient portfolio management;
  - d) the impact of this investment or investment activity on the quality, security, liquidity, profitability and availability of the whole portfolio.
- 1.67. The undertaking should have procedures that require that where such investment or investment activity entails a significant risk or change in the risk profile, the undertaking's risk management function communicates such a risk or change in the risk profile to the AMSB of the undertaking.

### **Guideline 29 – Security, quality, liquidity and profitability of the investment portfolios**

- 1.68. The undertaking should regularly review and monitor the security, quality, liquidity and profitability of the portfolio as a whole by considering at least:
- a) any liability constraint, including policyholders' guarantees, and any disclosed policy on future discretionary benefits and, where relevant, reasonable policyholders' expectations;
  - b) the level and nature of risks that an undertaking is willing to accept;
  - c) the level of diversification of the portfolio as a whole;
  - d) the characteristics of the assets including:
    - (i) credit quality of counterparties;
    - (ii) liquidity;

- (iii) tangibility;
  - (iv) sustainability;
  - (v) existence and quality of collateral or other assets backing the assets;
  - (vi) gearing or encumbrances;
  - (vii) tranches;
- e) events that could potentially change the characteristics of the investments, including any guarantees, or affect the value of the assets;
- f) issues relating to the localisation and availability of the assets including:
- (i) non-transferability;
  - (ii) legal issues in other countries;
  - (iii) currency measures;
  - (iv) custodian risk;
  - (v) over-collateralisation and lending.

### **Guideline 30 - Profitability**

1.69. The undertaking should establish targets for the returns it seeks from its investments taking into account the need to obtain a sustainable yield on the asset portfolios to meet reasonable policyholders' expectations.

### **Guideline 31- Conflicts of interests**

1.70. The undertaking should describe in its investment policy how it identifies and manages any conflict of interest that arises regarding investments, irrespective of whether they arise in the undertaking or in the entity which manages the asset portfolio. It should also document the actions taken to manage such conflicts.

### **Guideline 32 - Unit-linked and index-linked contracts**

1.71. The undertaking should ensure that its investments of unit-linked and index-linked contracts are selected in the best interest of policyholders and beneficiaries taking into account any disclosed policy objectives.

1.72. In the case of unit-linked business the undertaking should take into account and manage the constraints related to unit-linked contracts, in particular liquidity or any contractual or legal transferability constraints.

### **Guideline 33 - Assets not admitted for trading on a regulated financial market**

1.73. The undertaking should implement, manage, monitor and control procedures in relation to investments that are not admitted to trading on a regulated financial market or to complex products, which are difficult to value.

1.74. The undertaking should treat assets admitted to trading, but not traded or traded on a non-regular basis, similarly to those assets not admitted to trading on a regulated financial market.

#### **Guideline 34 - Derivatives**

1.75. When using derivatives, the undertaking should implement the procedures in line with its investment risk management policy to monitor the performance of these derivatives.

1.76. The undertaking should demonstrate how the quality, security, liquidity or profitability of the portfolio is improved without significant impairment of any of these features where derivatives are used to facilitate efficient portfolio management.

1.77. The undertaking should document the rationale and demonstrate the effective risk transfer obtained by the use of the derivatives where derivatives are used to contribute to a reduction of risks or as a risk mitigation technique.

#### **Guideline 35 - Securitised instruments**

1.78. Where the undertaking invests in securitised instruments, it should ensure that its interests and the interests of the originator or sponsor concerning the securitised assets are well understood and aligned.

### **Section 6: Own fund requirements and the system of governance**

#### **Guideline 36 – Capital management policy**

1.79. The undertaking should develop a capital management policy which includes a description of the procedures to:

- a) ensure that own-fund items, both at issue and subsequently, are classified according to the features in Articles 71, 73, 75 and 77 of Commission Delegated Regulation 2015/35;
- b) monitor tier by tier the issuance of own fund items according to the medium-term capital management plan, and ensure before issuance of any own fund items that it can satisfy the criteria for the appropriate tier on a continuous basis;
- c) monitor that own-funds items are not encumbered by the existence of any agreements or connected transactions, or as a consequence of a group structure, which would undermine their efficacy as capital;
- d) ensure that the actions required or permitted under the contractual, statutory or legal provisions governing an own-fund item are initiated and completed in a timely manner;
- e) ensure that ancillary own-fund items can be, and are, called in a timely manner when necessary;

- f) identify and document any arrangements, legislation or products that give rise to ring-fenced funds, and ensure that appropriate calculations and adjustments in the determination of the solvency capital requirement and own funds are made;
- g) ensure that the contractual terms governing own-fund item items are clear and unambiguous in relation to the criteria for classification into tiers;
- h) ensure that any policy or statement in respect of ordinary share dividends is fully taken into account in consideration of the capital position and the assessment of the foreseeable dividends;
- i) identify and document the instances in which distributions on tier 1 own-fund items might be cancelled on a discretionary basis;
- j) identify, document and enforce the instances in which distributions on an own-funds item need to be deferred or cancelled in accordance with Articles 71(1)(l) and 73(1)(g) of Commission Delegated Regulation 2015/35;
- k) identify the extent to which the undertaking relies on own-fund items subject to transitional measures;
- l) ensure that the manner in which items included in own funds under the transitional measures operate in times of stress, and in particular how the items absorb losses is assessed and, if necessary, taken into account in the ORSA.

### **Guideline 37 – Medium-term capital management plan**

- 1.80. The undertaking should develop a medium-term capital management plan which is monitored by the AMSB, and which includes at least considerations of:
- a) any planned capital issuance;
  - b) the maturity of own-fund items, incorporating both the contractual maturity and any earlier opportunity to repay or redeem, relating to the undertaking's own fund items;
  - c) the result of the projections made in the ORSA;
  - d) how any issuance, redemption or repayment, or other variation in the valuation of own-funds items affects the application of the limits on tiers;
  - e) how applying the distribution policy will affect own funds; and
  - f) the impact of the end of the transitional period.

## **Section 7: Internal controls**

### **Guideline 38 – Internal control environment**

- 1.81. The undertaking should promote the importance of performing appropriate internal controls by ensuring that all personnel are aware of their role in the internal control system. The control activities should be commensurate to the risks arising from the activities and processes to be controlled.



1.82. The participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should ensure a consistent implementation of the internal control systems across the group.

### **Guideline 39 – Monitoring and reporting**

1.83. The undertaking should establish monitoring and reporting mechanisms within the internal control system which provide the AMSB with the relevant information for the decision-making processes.

## **Section 8: Internal audit function**

### **Guideline 40 – Independence of the internal audit function**

1.84. The undertaking should ensure that the internal audit function does not perform any operational functions and is free from undue influence by any other functions including key functions.

1.85. When performing an audit and when evaluating and reporting the audit results, the undertaking should ensure that the internal audit function is not subject to influence from the AMSB that can impair its operational independence and impartiality.

### **Guideline 41 – Conflicts of interest within the internal audit function**

1.86. The undertaking should take adequate measures in order to mitigate the risk of any conflict of interest.

1.87. The undertaking should therefore ensure that internally recruited auditors do not audit activities or functions they previously performed during the timeframe covered by the audit.

### **Guideline 42 - Internal audit policy**

1.88. The undertaking should have an internal audit policy which covers at least the following areas:

- 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) if relevant, internal rules setting out the procedures the person responsible for the internal audit function needs to follow before informing the supervisory authority;
- c) where appropriate, the criteria for the rotation of staff assignments.

1.89. The participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should ensure that the internal audit policy at group level describes how the internal audit function:

- a) coordinates the internal audit activity across the group;
- b) ensures compliance with the internal audit requirements at group level.

### **Guideline 43 – Internal audit plan**

- 1.90. The undertaking should ensure that the internal audit plan:
- a) is based on a methodical risk analysis, taking into account all the activities and the complete system of governance, as well as expected developments of activities and innovations;
  - b) covers all significant activities that are to be reviewed within a reasonable period of time.

### **Guideline 44 - Internal audit documentation**

- 1.91. The undertaking should keep a record of its work in order to allow for an assessment of the effectiveness of the work of the internal audit function, and to document the audits in a way that allows for retracing the audits undertaken and the findings they produced.

### **Guideline 45 – Internal audit function tasks**

- 1.92. The undertaking should require that the internal audit function, in the report to the AMSB, includes the envisaged period of time to remedy the shortcomings, and information on the achievement of previous audit recommendations.

## **Section 9: Actuarial function**

### **Guideline 46 - Tasks of the actuarial function**

- 1.93. The undertaking should take appropriate measures to address the potential conflicts of interests, if the undertaking decides to add additional tasks or activities to the tasks and activities of the actuarial function.
- 1.94. The participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should require that the actuarial function gives an opinion on the reinsurance policy and the reinsurance program for the group as a whole.

### **Guideline 47 - Coordination of the calculation of technical provisions**

- 1.95. The undertaking should require the actuarial function to identify any inconsistency with the requirements set out in Articles 76 to Article 83 of Solvency II for the calculation of technical provisions and propose corrections as appropriate.
- 1.96. The undertaking should require the actuarial function to explain any material effect of changes in data, methodologies or assumptions between valuation dates on the amount of technical provisions.

### **Guideline 48 – Data quality**

- 1.97. The undertaking should require the actuarial function to assess the consistency of the internal and external data used in the calculation of technical provisions

against the data quality standards as set in Solvency II. Where relevant, the actuarial function should provide recommendations on internal procedures to improve data quality so as to ensure that the undertaking is in a position to comply with the Solvency II framework.

#### **Guideline 49 – Testing against experience**

1.98. The undertaking should ensure that the actuarial function reports any material deviations from actual experience to the best estimate to the AMSB. The report should investigate the causes of the deviations and, where applicable, propose changes in the assumptions and modifications to the valuation model in order to improve the best estimate calculation.

#### **Guideline 50 – Underwriting policy and reinsurance arrangements**

1.99. The undertaking should require the actuarial function, when providing its opinion on the underwriting policy and the reinsurance arrangements, to take into consideration the interrelations between these and the technical provisions.

#### **Guideline 51 – The actuarial function of an undertaking using an internal model**

1.100. The undertaking should require the actuarial function to contribute to specify which risks within their domain of expertise are covered by the internal model. The actuarial function should also contribute to how dependencies between these risks and dependencies between these risks and other risks are derived. This contribution should be based on a technical analysis and should reflect the experience and expertise of the function.

### **Section 10: Valuation of assets and liabilities other than technical provisions**

#### **Guideline 52 - Valuation of assets and liabilities other than technical provisions**

1.101. In its policy and procedures for valuation of assets and liabilities the undertaking should cover at least the following:

- a) the methodology and criteria to be used for the assessment of active and non-active markets;
- b) the requirements to ensure adequate documentation of the valuation process and of the accompanying controls, including those for data quality;
- c) the requirements on the documentation of the valuation approaches used regarding:
  - (i) their designs and the way they are implemented;
  - (ii) the adequacy of data, parameters and assumptions;

- d) the process for the independent review and verification of the valuation approaches;
- e) the requirements for the regular reporting to the AMSB for matters that are relevant for its governance on valuation.

### **Guideline 53 – Data quality control procedures**

1.102. The undertaking should implement data quality control procedures to identify deficiencies and to measure, monitor, manage and document their data quality. These procedures should include:

- a) completeness of data;
- b) appropriateness of data, both from internal and external sources;
- c) independent review and verification of data quality.

1.103. The policies and procedures implemented by the undertaking should address the need to periodically review market data and inputs against alternative sources and experience.

### **Guideline 54 – Documentation when using alternative valuation methods**

1.104. Where alternative methods for valuation are used, the undertaking should document:

- a) a description of the method, purpose, key assumptions, limitations and output;
- b) the circumstances under which the method would not work effectively;
- c) description and analysis of the valuation process, and the controls linked with the method;
- d) an analysis of valuation uncertainty linked with the method;
- e) a description of back-testing procedures performed on the results and, where possible, a comparison against comparable models or other benchmarks, which should be carried out when the valuation method is first introduced and regularly thereafter;
- f) a description of the tools or programs used.

### **Guideline 55 - Independent review and verification of valuation methods**

1.105. The undertaking should ensure that an independent review of the valuation method, following Article 267 (4)(b) of Commission Delegated Regulation 2015/35 takes place before the implementation of a new method or a major change, and on a regular basis thereafter.

1.106. The undertaking should determine the frequency of the review in line with the significance of the method for the decision-making and risk management processes.

1.107. The undertaking should apply the same principles for the independent review and verification of both internally developed valuation methods or models and for vendor provided valuation methods or models.

1.108. The undertaking should have processes in place to report the results of the independent review and verification, as well as the recommendations for remedial actions to the appropriate management level of the undertaking.

**Guideline 56 - Oversight by the AMSB and other persons who effectively run the undertaking**

1.109. The AMSB and other persons who effectively run the undertaking should be able to demonstrate an overall understanding of the valuation approaches and the uncertainties involved in the valuation process to allow a proper oversight of the risk management process concerning valuation.

**Guideline 57 – Request to the undertaking by the supervisory authority, for an external independent valuation or verification**

1.110. The supervisory authority should consider requesting an independent valuation or verification from the undertaking at least when there is a risk of misstatements in the valuation of material assets or liabilities, with possible material consequences for the undertaking's solvency situation.

**Guideline 58 – Independence of the external expert**

1.111. The undertaking should be able to demonstrate to the supervisory authority that the external valuation or verification has been performed by independent experts with the relevant professional competence, due care and relevant experience.

**Guideline 59 – Information to be provided to the supervisory authority on the external valuation or verification**

1.112. The undertaking should provide the supervisory authority with all relevant information requested on external valuation or verification. The undertaking should include in this information, at least, the experts' written opinion on the valuation of the relevant asset or liability.

**Section 11: Outsourcing**

**Guideline 60 - Critical or important operational functions and activities**

1.113. The undertaking should determine and document whether the outsourced function or activity is a critical or important function or activity on the basis of whether this function or activity is essential to the operation of the undertaking as it would be unable to deliver its services to policyholders without the function or activity.

### **Guideline 61 - Underwriting**

1.114. When an insurance intermediary, who is not an employee of the undertaking, is given authority to underwrite business or settle claims in the name and on account of an undertaking, the undertaking should ensure that the activity of this intermediary is subject to the outsourcing requirements.

### **Guideline 62 - Intra-group outsourcing**

1.115. If critical or important functions or activities are outsourced within the group, the participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should document which functions relate to which legal entity and ensure that the performance of the critical or important functions or activities concerned at the level of the undertaking is not impaired by such arrangements.

### **Guideline 63 - Outsourcing written policy**

1.116. The undertaking that outsources or considers outsourcing should cover in its policy the undertaking's approach and processes for outsourcing from the inception to the end of the contract. This in particular should include:

- a) the process for determining whether a function or activity is critical or important;
- b) how a service provider of suitable quality is selected and how and how often its performance and results are assessed;
- c) the details to be included in the written agreement with the service provider taking into consideration the requirements laid down in Commission Delegated Regulation 2015/35;
- d) business contingency plans, including exit strategies for outsourced critical or important functions or activities.

### **Guideline 64 - Written notification to the supervisory authority**

1.117. In its written notification to the supervisory authority of any outsourcing of critical or important functions or activities the undertaking should include a description of the scope and the rationale for the outsourcing and the service provider's name. When outsourcing concerns a key function, the information should also include the name of the person in charge of the outsourced function or activities at the service provider.

## **Chapter II: Group governance specific requirements**

### **Guideline 65 – Responsibilities for setting internal governance requirements**

1.118. The participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should set adequate internal governance requirements across the group appropriate to the structure, business model and risks of the group and of its related entities, and should consider the appropriate structure and organization for risk management at group level, setting a clear allocation of responsibilities at all entities that are part of the group.

1.119. The participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should not impair the responsibilities of the AMSB of each entity in the group when setting up its own system of governance.

### **Guideline 66 – System of governance at group level**

1.120. The participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should:

- a) have in place appropriate and effective tools, procedures and lines of responsibility and accountability enabling it to oversee and steer the functioning of the risk management and internal control systems at individual level;
- b) have in place reporting lines within the group and effective systems for ensuring information flows in the group bottom up and top-down;
- c) document and inform all the entities that are part of the group about the tools used to identify, measure, monitor, manage and report all risks to which the group is exposed;
- d) take into account the interests of all the entities belonging to the group and how these interests contribute to the common purpose of the group as a whole over the long term.

### **Guideline 67 – Risks with significant impact at group level**

1.121. The participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should consider in its risk management system the risks both at individual and group level and their interdependencies, in particular:

- a) reputational risk and risks arising from intra-group transactions and risk concentrations, including contagion risk, at the group level;
- b) interdependencies between risks stemming from conducting business through different entities and in different jurisdictions;
- c) risks arising from third-country entities;
- d) risks arising from non-regulated entities;

e) risks arising from other regulated entities.

### **Guideline 68 –Risk concentrations at group level**

1.122.The participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should ensure that there are processes and procedures in place to identify, measure, manage, monitor and report risk concentrations.

### **Guideline 69 - Intra-group transactions**

1.123.The participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should ensure that the risk management system of the group and the individual undertakings include processes and reporting procedures for identifying, measuring, monitoring, managing and reporting of intra-group transactions, including significant and very significant intra-group transactions as referred in Solvency II.

### **Guideline 70 – Group risk management**

1.124.The participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should support in its risk management at group level by appropriate processes and procedures to identify, measure, manage, monitor and report the risks that the group and each individual entity are or might be exposed to.

1.125.The participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should ensure that the structure and organization of the group risk management do not impair the undertaking's legal ability to fulfil its legal, regulatory and contractual obligations.

### **Compliance and Reporting Rules**

1.126.This document contains Guidelines issued under Article 16 of the EIOPA Regulation. In accordance with Article 16(3) of the EIOPA Regulation, competent authorities and financial institutions shall make every effort to comply with guidelines and recommendations.

1.127.Competent authorities that comply or intend to comply with these Guidelines should incorporate them into their regulatory or supervisory framework in an appropriate manner.

1.128.Competent authorities shall confirm to EIOPA whether they comply or intend to comply with these Guidelines, with reasons for non-compliance, within two months after the issuance of the translated versions.

1.129.In the absence of a response by this deadline, competent authorities will be considered as non-compliant to the reporting and reported as such.



## **Final Provision on Reviews**

1.130. The present Guidelines shall be subject to a review by EIOPA.

## **Technical Annex: Minimum information to be provided to the supervisory authority concerning the fit & proper assessment**

### **Contact information**

- Name of the undertaking.
- Undertaking's registration number.
- Contact person:
  - a) First name.
  - b) Surname.
  - c) Title.
  - d) Telephone number.
  - e) E-mail address.
  - f) Fax number.

### **Fact being notified**

- First appointment.
- Change in previous information.
- Change of position.

### **Description of the position being notified**

- Name of the position.
- Scope of the responsibilities.
- Date of the appointment.
- Length of appointment, if applicable.
- Executive functions or not.
- Any other information the undertaking deems relevant for the assessment.

### **Information on the person subject to notification**

- First name.
- Surname.
- Any previous names.
- Personal address.
- Telephone number.
- Date of birth.
- Place of birth.
- Nationality.
- Information on any previous assessment/notification process by a supervisory authority of the financial sector within the EEA:
  - a) Name of the supervisory authority.
  - b) Country.
  - c) Date.
- Information on previous employments, qualified assignments or appointments as a member of an administrative, management or supervisory body:

- a) Company name and registration number.
- b) Nature and scope of the operations.
- c) The registered office of the undertaking.
- d) Position.
- Any other positions held:
  - a) Company name and registration number.
  - b) Nature and scope of the operations.
  - c) The registered office of the undertaking.
  - d) Position.
- Description of the level of knowledge, competence and experience of the person to perform the task, including:
  - a) Skills, knowledge (university degree, training or diploma).
  - b) Professional relevant experience.
- Information on potential conflicts of interest with details, if applicable.
- Qualifying ownership or any other form of substantial influence in the undertaking.
- Any other companies in which the notified person has a direct or indirect qualifying ownership:
  - a) Company name and registration number.
  - b) Nature and scope of the operations.
  - c) The registered office of the company.
  - d) Possession in percentage.
- Close relatives with ownership shares in the undertaking that notifies or in any other company which has ownership shares in that company.
- Close relatives with any other financial relations to companies mentioned above.
- Any other commitments that may give rise to conflict of interest with explanations as to the circumstances and a statement how the notified person intends to deal with potential conflicts of interest.
- Conviction in a domestic or foreign court within the last X years [number of years according to national law] with explanation of circumstances, if applicable.
- Pending criminal proceedings.
- Membership in a board of directors in an operating undertaking that has not been granted a release from liability.
- Dismissal from a position in a financial institution, company or from employment as a senior executive or termination of an engagement as a board member or auditor in another operating undertaking.
- Participation in an arbitration board.
- Bankruptcies or the equivalent abroad.
- Rejection of an application, exclusion or limitation in any other way in terms of the right to conduct operations or a profession which requires authorisation, registration or such of the competent authority, organisation or equivalent body.

- Supervisory sanctions against the person notified or a company where the person had a key function.
- Any other information relevant to the assessment by the supervisory authority.

### **Documents to be submitted**

- Extract from the judicial record or an equivalent document issued by a competent judicial or administrative authority.

### **Declarations**

- Declaration signed by the appropriately authorized person [according to national law/practice the management or supervisory body or the person responsible for this in the undertaking with the position of the person(s) in the undertaking given] that the assessment was performed in accordance with the laws, regulations and undertaking's fit and proper policy and the person subject to notification was considered as fit and proper for the job.
- Declaration that the information submitted in the notification is correct and complete: date, name of signatories in block letters, signatures.