



## Solvency II

# QIS5:

## How PricewaterhouseCoopers can help you

### Overview of QIS5

- The QIS5 exercise will run from **August to November 2010** with submission deadlines of end October for solo entities and mid November for groups. The final technical specification was issued on 6 July and the latest indication is that the QIS5 submission spreadsheets will be available from the end of the first week of August.
- Even firms planning to use their **own internal models should be aware of the changes to the standard formula**; they will need to use it if they do not obtain full model approval and may initially need to use it in parallel with their own model. Further, participation in QIS5 constitutes one of the qualification criteria for firms wishing to join the FSA's internal model pre-application process.
- Firms should be aware that QIS5 looks at the Solvency II **balance sheet** as well as the **capital requirements**. In particular, QIS5 requires firms to calculate technical provisions, comprising a best estimate and risk margin, on a Solvency II valuation basis.
- The **FSA is strongly encouraging firms** to move away from the "best efforts" basis adopted for QIS4 and to carry out the QIS5 exercise **"for real"**. This applies to both the capital and balance sheet calculations and means that the QIS5 exercise will take longer to complete than QIS4.

### Key points under QIS5

- The base risk-free rate is defined as the swap curve less 10 b.p.
- Three risk-free curves are specified with different allowances for illiquidity. Annuities use 100% of the prescribed illiquidity premium, participating contracts 75% and all other contracts 50%. An illiquidity premium stress test (65% fall in illiquidity premiums) has been introduced in the final specification.
- For Life firms, the calibration of the QIS5 standard formula is expected to increase capital requirements compared to QIS4.
- The QIS5 calibration for non-life risk is lower than the Level 2 advice issued by CEIOPS in 2009 but higher than QIS4.
- The approach to premium risk for non-life has been refined to capture better the risk-mitigating effects of non-proportional reinsurance.
- Geographical diversification has been reintroduced after being removed from the Level 2 advice. The geographical split better reflects UK firms' diversification benefits compared to QIS4.
- Full allowance for diversification between lines of business is permitted when calculating the capital to be used in the risk margin calculation. However, diversification between entities is not permitted for the group risk margin calculation. Previously no allowance for diversification was allowed.
- Standardised catastrophe scenarios are to be used for exposures within the EEA. If the standardised scenarios are not suitable for a firm's business or there are exposures outside the EEA, firms will likely need to seek partial model approval for this area.

### What a QIS5 exercise will provide

- Solvency II capital requirement (the MCR and SCR) based on the European Commission's latest iteration of the standard formula.
- Balance sheet (and available capital) on a Solvency II valuation basis including best-estimate liability and the risk margin.
- Responses to questions in the QIS5 questionnaire.
- Insights in the following areas:
  - Capital required should the firm's internal model not gain approval ('impact assessment');
  - Standard formula data requirements including the required quality and granularity of data;
  - Processes required to calculate capital requirement using the standard formula approach;
  - Strengths/weaknesses in the firm's current processes ('gap analysis');
  - Key drivers of capital under the standard formula approach; and
  - How the standard formula reconciles to the assumptions and outputs from the internal model.

Full and robust participation is an essential step in the preparation for Solvency II. However this comes at a time when resources are heavily constrained with ICA submissions, the pre-application process and interim reporting. Nonetheless, it is a key milestone as a dry-run test of firms' processes. Equally, if not of greater importance, it will cause many firms to reconsider the strategic implications of Solvency II.

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### How can we help

For each area where PwC can support you, the level of our involvement and work can be varied. The cost will depend on the level of support required and the size of the firm, complexity of the **business and the efficiency of existing processes**.

Support	Examples of how we can help
Training	One or two-hour training sessions for the Board, Senior Management or delivery teams giving an overview of QIS5 and potential implications for the firm.
	Half-day workshops for the Board, Senior Management or teams going into more detail on the completion of QIS5. This would include a walkthrough of the QIS5 spreadsheets, facilitation of the discussion on data requirements and identifying efficient ways to meet the QIS5 requirements.
Review	Review of approaches used to estimate the technical provisions, both best-estimate liabilities and risk margins, and to derive the capital requirements.
	Review of inputs to the QIS5 spreadsheet to calculate the Solvency Capital Requirement.
	Full review and challenge of the QIS5 submission against specifications by our experts.
	Reasonableness of the tax assumptions included in QIS5 and allowance for tax in stress scenarios.
Output	<b>Impact assessment:</b> High-level assessment of key impacts of QIS5 on technical provisions and capital requirements. Comparison of QIS5, Level 2, QIS4 and ICA requirements.
	<b>Gap analysis:</b> Analysis of gaps between existing processes and what will be required both for QIS5 in the short term and for your longer term vision for Solvency II.
	<b>Peer comparison:</b> Benchmarking of QIS5 approach against industry best practice and peers.
	<b>Presentation of results:</b> Workshop for the Board, Senior Management and other key stakeholders presenting the QIS5 results and highlighting key learning points from and implications of the QIS5 exercise.
Calculation support	Targeted advice to maximise the efficiency of in-house teams, e.g. scoping, planning, resourcing, Q&A.
	Provision of resources to assist with calculations and/or submission.
	Backfilling 'Business As Usual' roles to free up resources to work on QIS5.

### Our Credentials

- We supported over 30 QIS4 exercises and have advised numerous clients on the implications of the Level 2 advice and QIS5 draft technical specification. We are already working with a number of clients on their QIS5 exercise.
- These QIS exercises have been completed with minimal impact on business as usual, by getting the team started quickly and efficiently on the QIS spreadsheet and underlying analysis. Our approach is to not only to deliver the QIS submission but to prompt our clients to re-examine their strategy for Solvency II by giving management insights into the likely capital impacts.
- We have participated actively in the industry debate following QIS4 and during the Level 2 consultation process. This has included providing detailed feedback to CEIOPS on its standard formula Level 2 consultation papers, contributing to the shaping of the standard formula.
- We have a team of trained and dedicated QIS5 resources that are ready to be deployed to assist you in your QIS5 project in anticipation of the greater participation and demands on time. This includes not just actuarial, but also finance process, data & IT, tax and reporting experts.

We have a large team of experts across the UK and Europe ready to help you.

**If you would like to discuss any aspect of QIS5, please contact one of our team:**



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