



Society of Actuaries in Ireland

ORSA – An International Development

25.02.14



Agenda

What is an ORSA?

Global reach

**Comparison
of
requirements**

**Common
challenges**

**Potential
solutions**



Origin of ORSA

FSA ICAS

Solvency II

IAIS ICP16



What is an ORSA?

- Insurer's own assessment of:
 - A. its risks
 - B. capital needed to protect against those risks
- Documentation of assessment



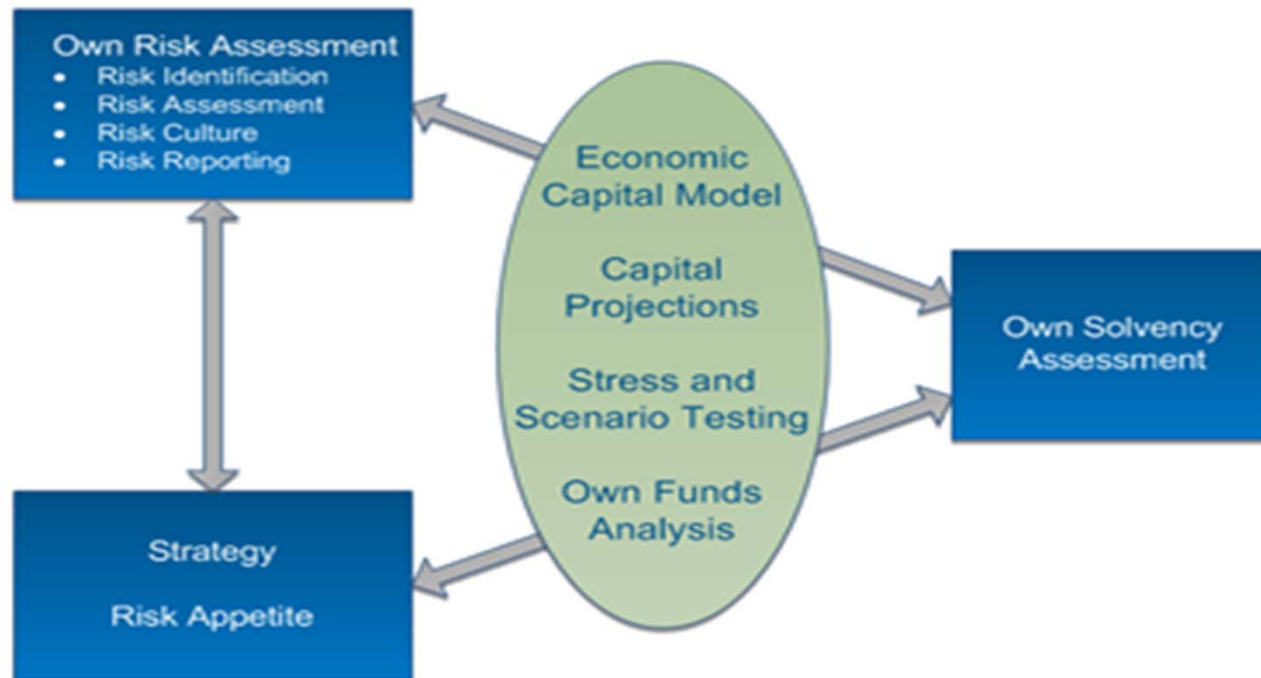
ORSA – a key management tool





ORSA – how the pieces fit together

Own Risk and Solvency Assessment





Objectives of the ORSA

- Board responsibility
- Own risk assessment
- Own solvency assessment
- Forward-looking
- Management information
- Enhance understanding
- Group-wide
- Continuous process
- Adequate documentation



Challenges in achieving objectives

- Risk that ORSA becomes a compliance exercise
- Challenges in
 - Planning and organisation
 - Training
 - Communication
 - Culture
- Need leadership and need to achieve buy-in



IAIS – ICP16

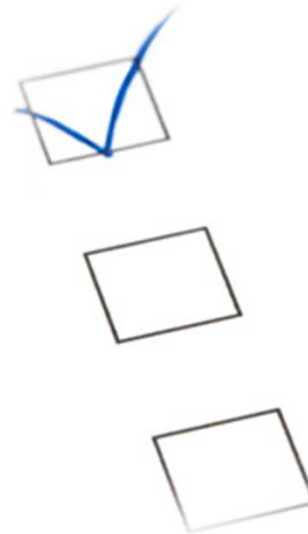


- Assess overall solvency needs
- Continuity analysis (forward looking assessment)
- Responsibility with Board and senior management
- Perform regularly and following significant change
- Group ORSA required
- Supervisor should review output of ORSA
- Document rationale, calculations, actions arising
- Proportionality recognised
- Independent review where proportionate



Comparison criteria

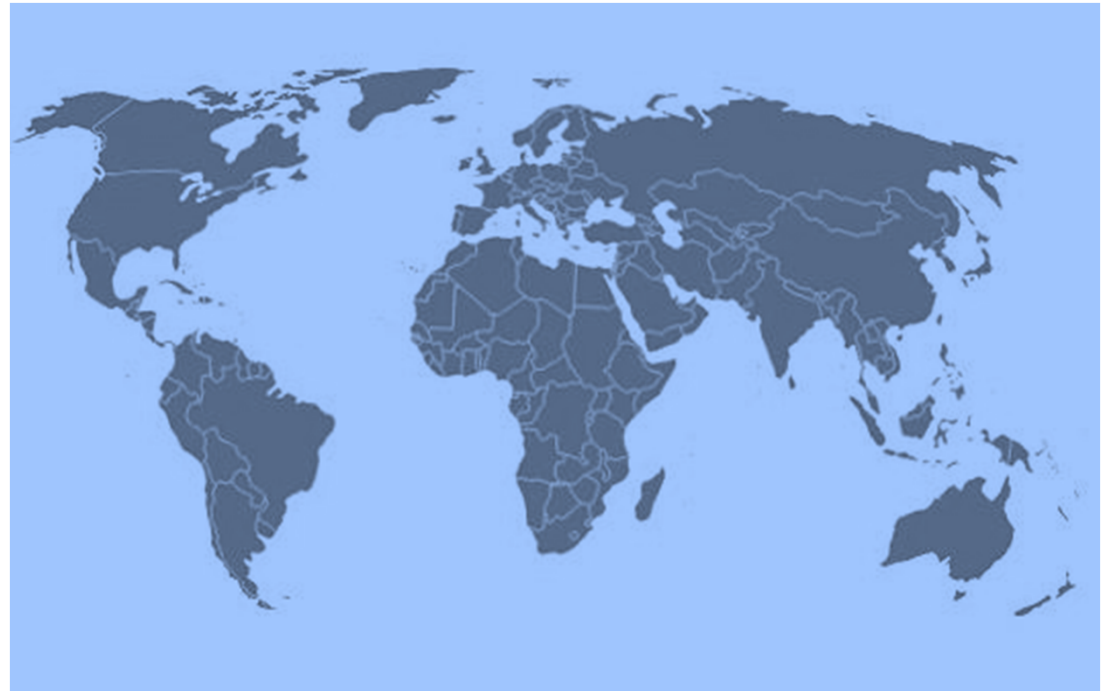
- ✓ Quantitative assessment
- ✓ Qualitative assessment
- ✓ Forward looking
- ✓ Continuous compliance
- ✓ Deviation from assumptions
- ✓ Role of board
- ✓ Use of ORSA
- ✓ Frequency
- ✓ Group assessment
- ✓ First submission
- ✓ Exemption
- ✓ Proportionality
- ✓ Required documentation
- ✓ Independent review





Territories covered include

- ✓ **IAIS (International)**
- ✓ **European Union**
- ✓ **United States**
- ✓ **Australia**
- ✓ **Canada**
- ✓ **Switzerland**
- ✓ **Singapore**
- ✓ **Malaysia**
- ✓ **Bermuda**





Common Requirements



- Large degree of consistency in requirements
- Quantitative assessment
 - stress tests, reverse stress tests, sensitivities and scenario analyses
- Qualitative assessment
- Forward looking perspective
- Performed on regular basis
- Proportionality recognised



Specific Points to Note Solvency II



- Additional requirements
 - Demonstrate compliance on continuous basis with:
 - Capital requirements
 - Technical provision requirements
 - Assess deviation of risk profile from assumptions of SCR
- Extensive documentation
- No explicit requirement for independent review
- 2014 Implementation through FLAOR



Specific Points to Note NAIC



- Less emphasis on the Role of the Board
 - No explicit requirements to steer/challenge the process
 - Copy of summary report provided to the Board
- Report must be signed
 - By individual responsible for oversight of ERM process
- Less emphasis on Use of the ORSA
- Flexibility on risk capital measure
 - Economic, rating agency and/or regulatory frameworks



Specific Points to Note NAIC



- Group emphasis
 - Performed consistent with the way the business is managed
 - Whether group, legal entity or other basis
 - Not necessarily required for every legal entity

- More focused on ERM?

- Thresholds
 - Annual direct written premium of less than \$500 million; or
 - Part of group with annual direct written premium of less than \$1 billion



Specific Points to Note NAIC



- Preparedness - Milliman survey March 2013
 - 80% of participants don't currently prepare such a report
 - 33% with no risk appetite statement
 - Strategic, reputational and operational risks hardest to assess
 - Marginal beneficial effect expected
- 2015 Implementation



Specific Points to Note APRA



- Internal Capital Adequacy Assessment Process
 - 2013 Implementation
- Capital triggers required
 - Provide time to rectify problems and restore capital
- Risk Appetite address all material sources of risk
 - Doesn't matter if they can't be quantified
- Independent review required
- Target levels of capital and strategy for maintaining target



Specific Points to Note APRA



- Initial feedback from APRA on Summary Statements
 - Significant room for improvement
 - Quality not related to Insurer size
 - Problem areas included:
 - Independent review
 - Stress testing
 - Risk appetite
 - Risk assessment
 - Internal controls



ORSA – an international development

Practical challenges in implementing an ORSA



Questions the ORSA should help answer

- Understanding of risk profile of the company?
- Does company have sufficient capital to support business plan?
- Will company stay within risk appetite going forward?
- What risks are not covered by regulatory capital?
- What risks should be monitored more frequently?
- What scenarios could cause solvency issues?
- What mitigation options are available in these scenarios?
- Key sensitivities to capital & profits?
- Material changes to risk profile over recent period?
- What would cause company to re-run ORSA?

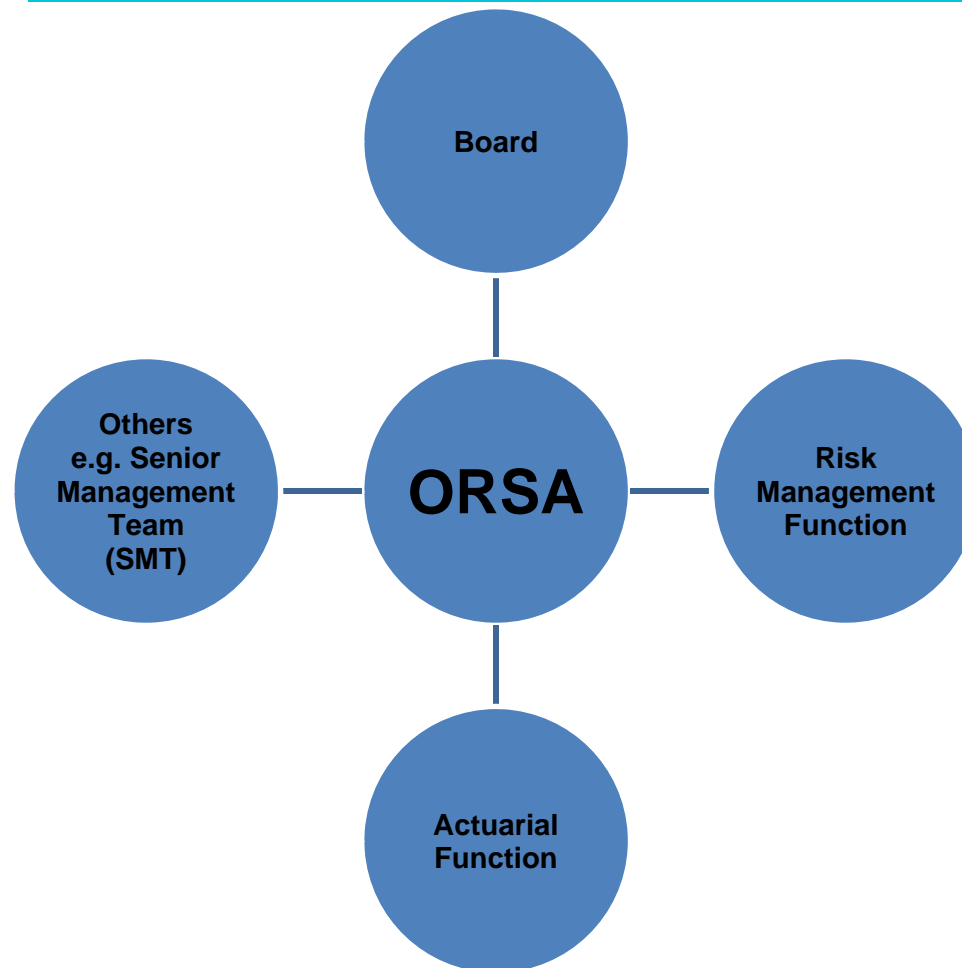


Some challenges and potential solutions

1. Getting the relevant people involved



Who is involved in the ORSA process?





Role of the Board

- Board expected to steer how ORSA is performed and challenge results
 - Involved in the process and users of the outputs
 - Important that this happens and is evidenced
- Board involvement at start of the process
 - Approve ORSA policy
 - Input into stresses and scenarios
- Board involvement at end of the process
 - Challenge outputs
 - Evidence that Board take the output of ORSA into account in
 - Business planning and strategy
 - Setting risk appetite
 - Capital management & dividend policy
 - Product development



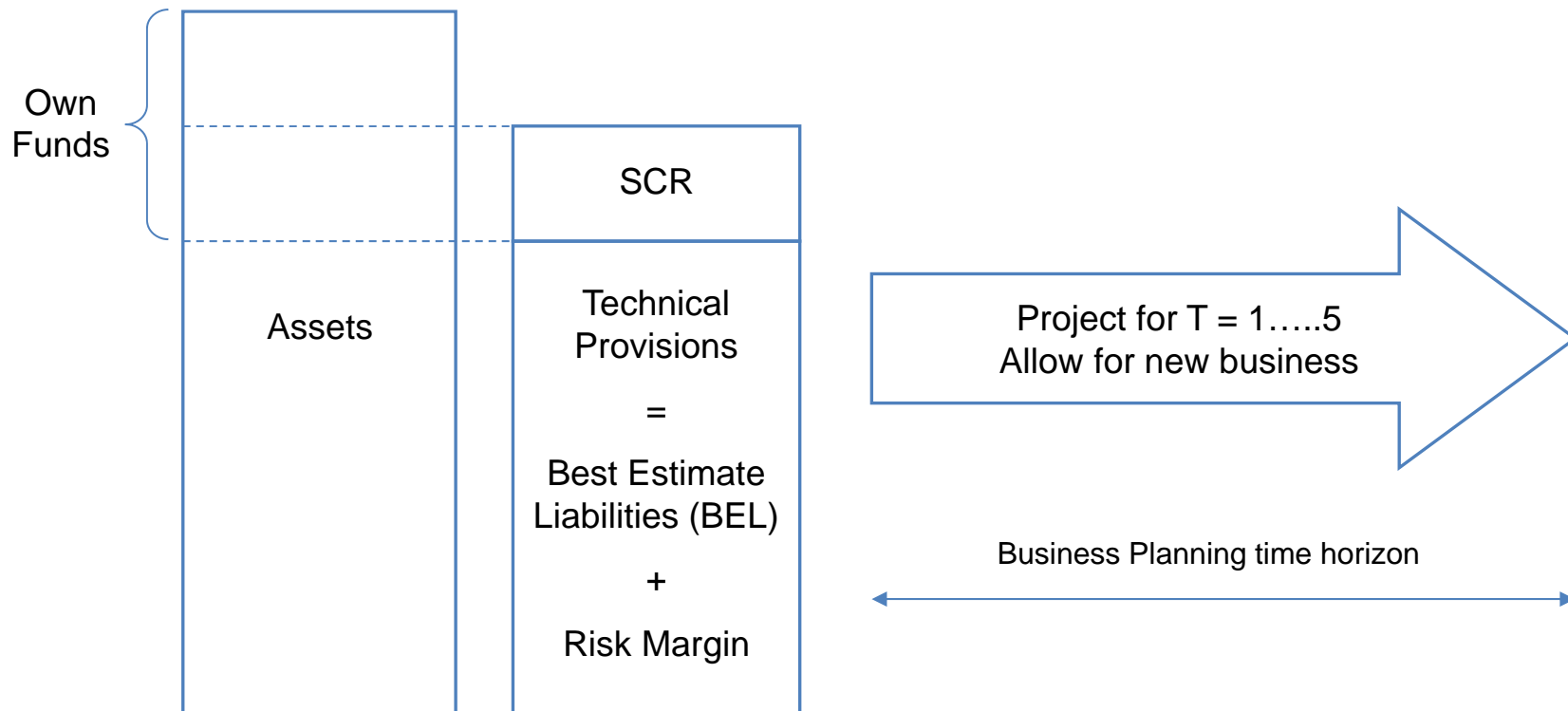
Some challenges and potential solutions

2. Balance Sheet Projections



Balance Sheet Projections

Forward Looking Perspective



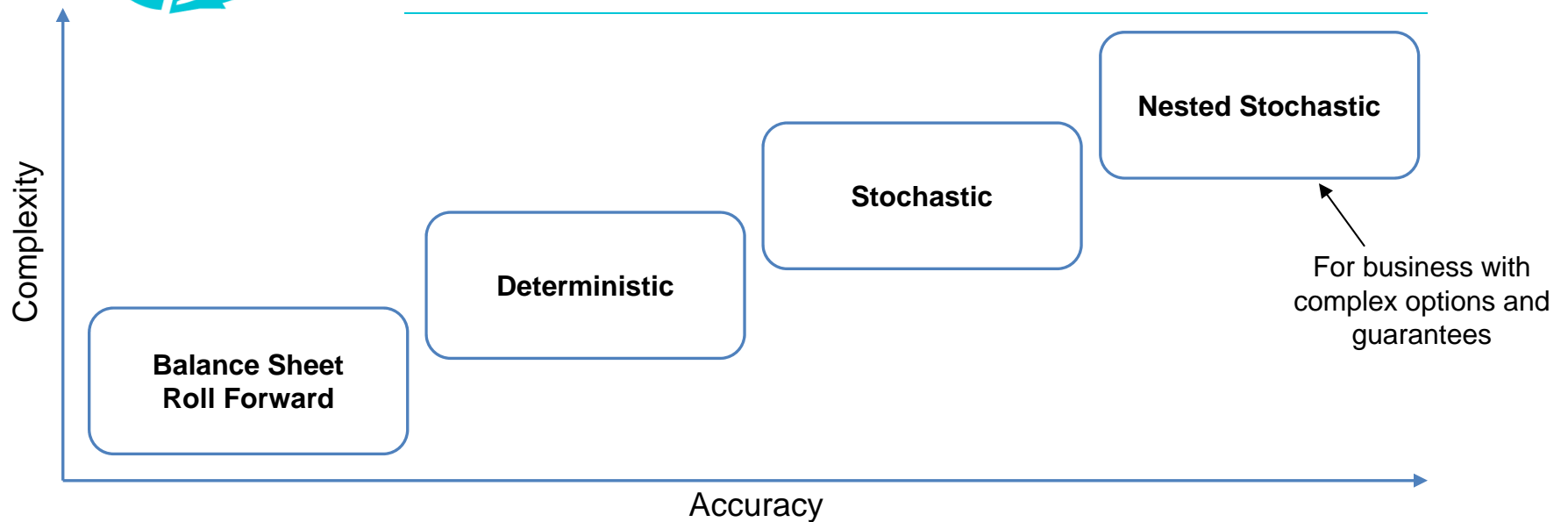


Projections

- Required to project Assets, Liabilities and SCR
 - Not a trivial task!
 - Responsibility of the Actuarial Function
- Existing capital projections models may already be available
 - e.g. Financial Condition Reports
- Approach should be proportionate to the nature scale and complexity of the business
 - Trade off between simplicity and accuracy
 - Need to be able to understand and explain output to Board



Projection methodologies



- Issues to consider:
 - IT resources and run times
 - Spurious accuracy
- **IMPORTANT:** Output must be understood and used by the business

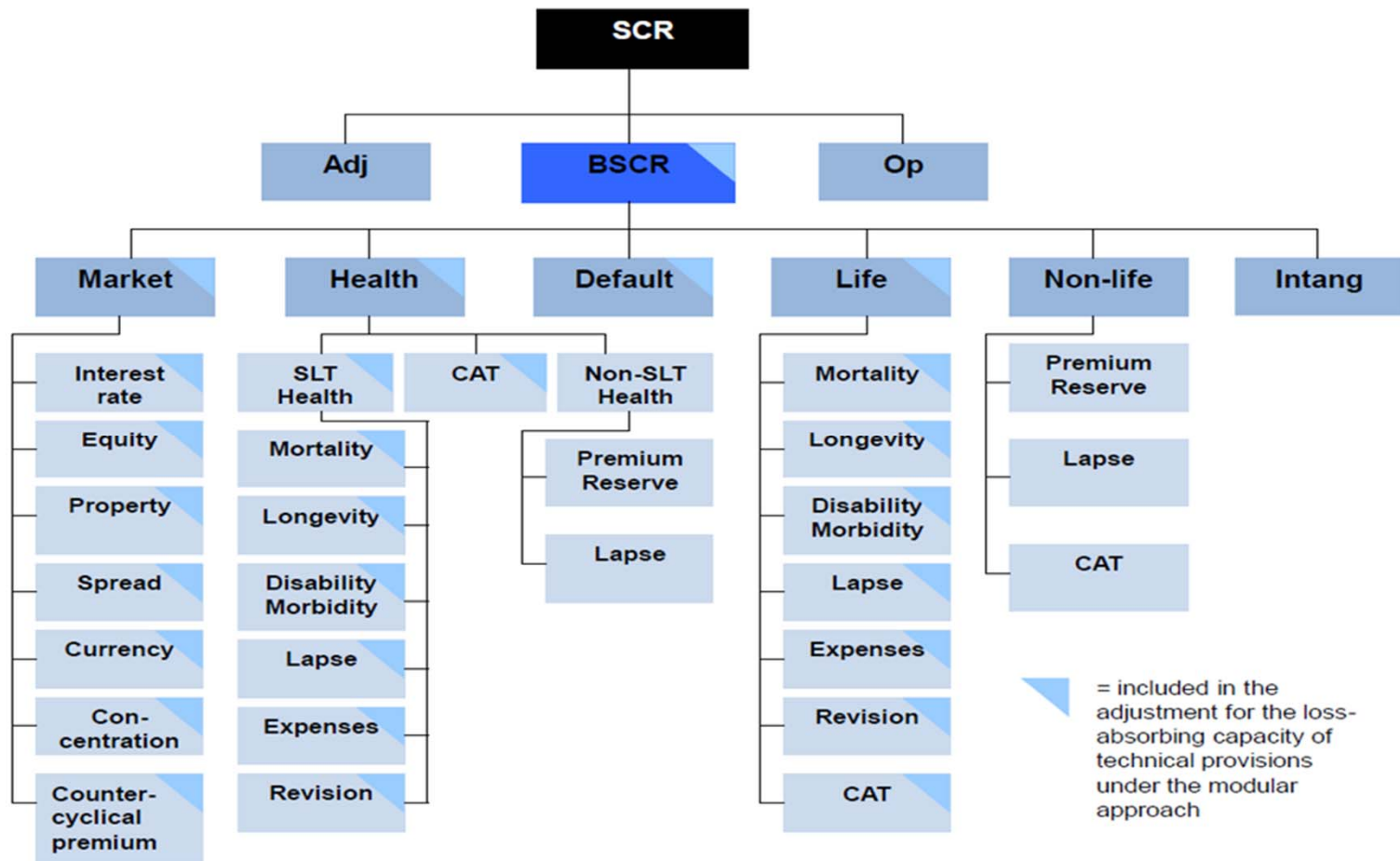


Projecting Assets & Liabilities

- Deterministic approach may be appropriate for many lines of business
- Liabilities
 - Run-off of Existing BEL and Risk Margin in line with best estimate assumptions
 - Build model points for future new business
- Assets – issues to consider
 - Granular data available on asset holdings?
 - What is the company's ALM strategy?
 - Reinvestment policy for existing assets?
 - What assets are assumed to back new business?
 - What is the company's capital and dividend policy?
 - Rebalancing of portfolio in particular scenarios?



SCR – Standard Formula





Projecting SCR

- Full recalculation for each future year very onerous
 - Significant number of market consistent valuations to calculate opening SCR
 - Projecting forward, total number of calculations mounts up very quickly
- Key risk drivers, e.g.
 - Sums at risk for insurance risks
 - Growth in equity / property / bonds for market risks
 - Funds under management for future AMCs
- Other options available
 - Trade off between accuracy and practicality



Some challenges and potential solutions

3. Stress and Scenario Testing



Stress and Scenario Testing - Options

- Stress tests
 - Sensitivity of capital position to particular risks (e.g. an equity shock)
 - Consider risks not covered by regulatory capital (e.g. sovereign)
- Scenario analysis
 - Combinations of stresses
 - “What if” scenarios
- Reverse stress tests
 - Determine outcome e.g. own funds falls below SCR / MCR
 - Solve for stress level

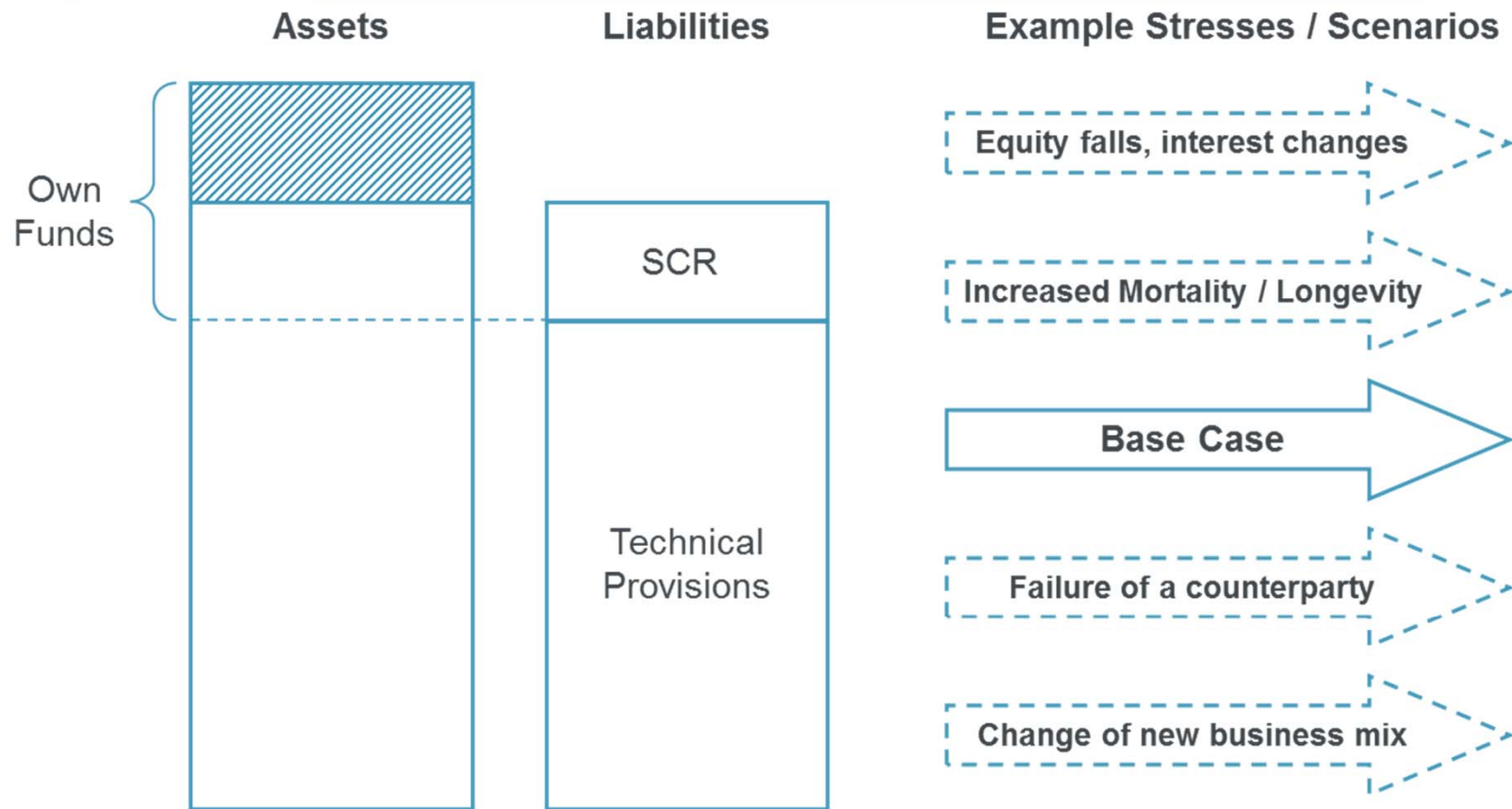


Selecting stresses and scenarios

- Selection of business scenarios should involve
 - Board and SMT
 - Risk Management
 - Actuarial Function
 - Others (e.g. sales)
- Consider wide range of scenarios
 - Macro-economic scenarios (e.g. multiple dependant market shocks)
 - Insurance risk scenarios (e.g. pandemics, lapse events)
 - Company specific scenarios
 - Historical events that have been encountered
 - Events that are difficult to quantify (e.g. operational errors)
- Additional considerations
 - Dependencies / Correlations
 - Timing
 - Mitigations



Scenarios – Overall Solvency Needs



Overall solvency needs = level of buffer required to withstand stresses



Some challenges and potential solutions

4. Linking to business plan and strategy



Linking to business plan and strategy





Some challenges and potential solutions

5. Documentation



Documentation

- Required:
 - ORSA policy
 - Record of each ORSA process
 - Internal Report
 - Supervisory Report
- Challenge to produce a comprehensive report that covers all the requirements and also meets the needs of all stakeholders
 - Good overview and executive summary
 - Core of report concise - focus on key issues
 - Detail in the appendices for interested parties
 - “Courage to omit”



Possible outline of report

- Company overview
 - Business written, market information
 - Strategic Plan, Risk appetite, Capital strategy etc.
- Current and future solvency position
 - Base case projection on current business plan
 - Identification of key risks and results of stress testing
 - Risk mitigation strategies and management actions
- Challenge and conclusions
 - Board and SMT review and challenge
 - Conclusions with respect to capital required to run business
 - Evidence of link between ORSA and strategy
- Appendices



Risk Management versus Compliance

- The ORSA **is** about:
 - ✓ Better risk awareness
 - ✓ Understanding the overall solvency needs of the company
 - ✓ Increased alignment between risk appetite and strategy
 - ✓ More insightful decision making
 - ✓ Improved capital efficiency
- The ORSA **is not** about:
 - ✗ Just addressing the guidelines (ticking the boxes)
 - ✗ Creating a very complex process - output not understood by Board
 - ✗ Designing a complex mathematical model
 - ✗ Creating a huge report - key messages not clear



Summary

- ORSA is now an international requirement
 - Significant consistency in requirements across territories
 - Provides similar challenges for companies globally
- Focus on what ORSA is trying to achieve and develop approach that works for the Company
 - No perfect model, will improve over time
- There are many benefits to the ORSA **if done well!**