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Solvency II ORSA

ORSA for Solvency II Standard Formula firms

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Objective

Delegates should understand:

- **The key regulatory developments on ORSA**
- **The quantitative and qualitative assessments that can be used to justify using the Standard Formula**
- **How the development in their ORSA plays an important role in that justification**
- **Key challenges in implementing the ORSA and the current state of UK preparations in ORSA**



Agenda

- Refresh on what an ORSA is
- Update on regulatory developments
- Appropriateness of Standard Formula using ORSA
- Current state of UK preparations
- Conclusion
- Questions & Comments





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Refresh on what an ORSA is

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What is an “ORSA”?

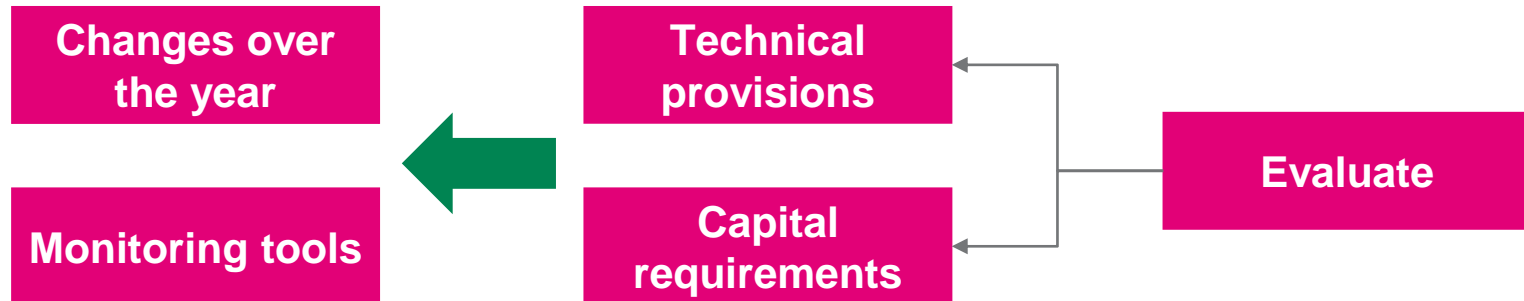
- **ORSA** = Own Risk and Solvency Assessment
- **Purpose:** allows insurers to have a complete and holistic understanding of its business risk profiles to best inform decision making on business strategy and capital planning

“It is an essential risk management and system tool to enable firms to express their overall solvency needs in both quantitative and qualitative terms”

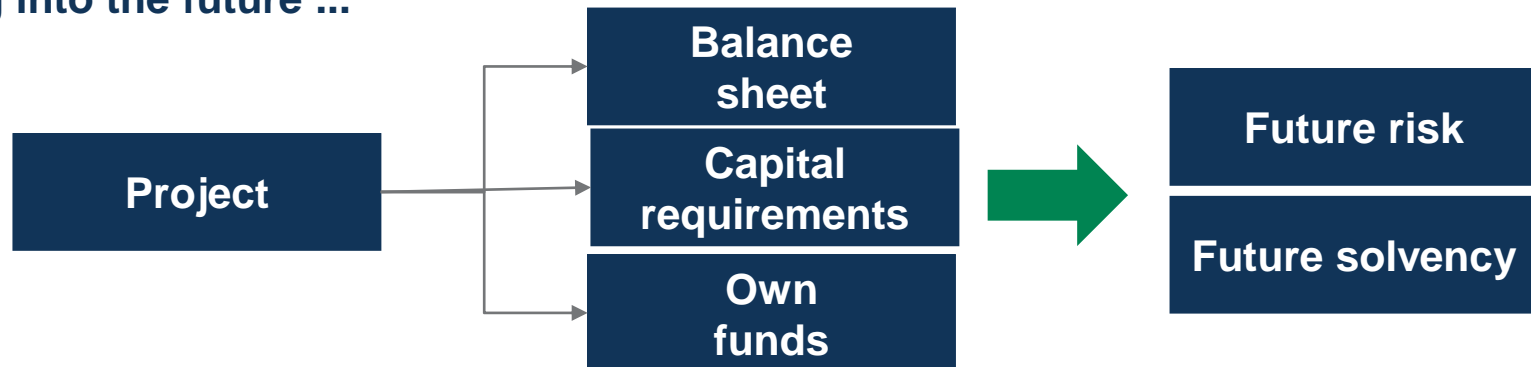


ORSA perspectives

Looking into the past and current monitoring ...



Looking into the future ...



Key components of the ORSA

ORSA policy

The ORSA policy defines what the business should do to perform the ORSA process. This will be used by the business to provide guidelines to perform the process.

ORSA process

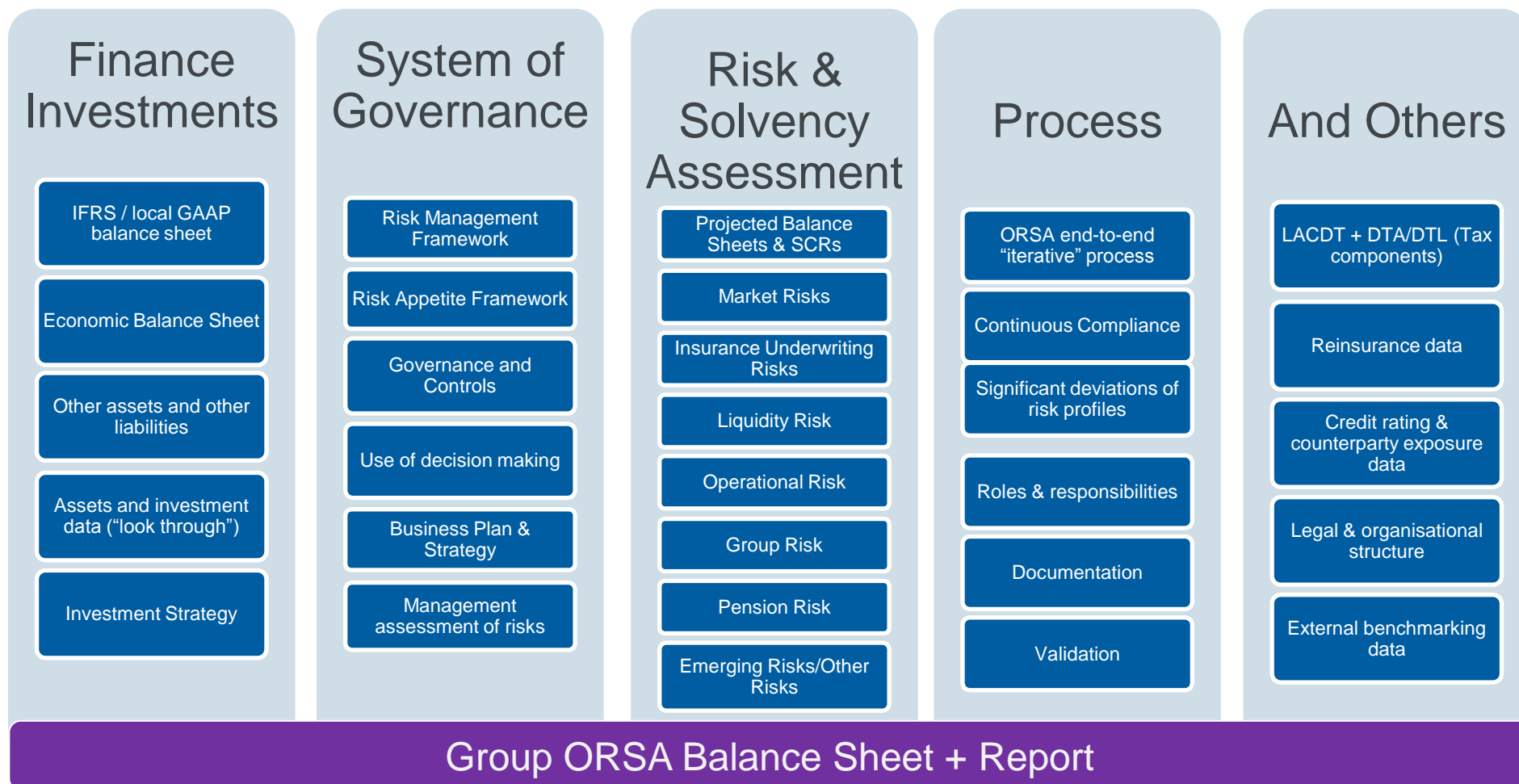
The ORSA process assesses capital requirements and demonstrates how these are linked to the risk assessment and decision making processes.

ORSA report

The ORSA report 'tells the story' of the undertaking's current risk and capital management practices. It demonstrates to the regulators that the undertaking has the necessary available level of capital to sustain significant negative impacts now and in the future.



Key data and model components of the ORSA



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Regulatory updates

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Update on regulatory development

“The ORSA implementation progress is less affected by Solvency II delays”

- **ICAS+** – The PRA’s push is towards insurers incorporating elements of Solvency II development into their ICA models
- **EIOPA Consultations** – EIOPA have released four consultation papers including one on ORSA on 27 March 2013
 - Proposal for Guidelines on System of Governance
 - Proposal for Guidelines on Forward Looking assessment of the undertaking’s own risks (Based on the ORSA principles)
 - Proposal for Guidelines on submission of information to national competent authorities (NCAs)
 - Proposal for Guidelines on Pre-Application of Internal Models



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EIOPA's Guidelines proposal on ORSA

- The Guidelines proposed in this consultation on the forward looking assessment of the undertaking's own risks covers three main aspects:
 - Assessment of overall solvency needs;
 - Assessment of whether the undertaking would comply on a continuous basis with the Solvency II regulatory capital requirements and the requirements regarding the calculation of technical provisions; and
 - Assessment of deviations from the assumptions underlying the solvency capital requirement calculation.



PRA's key messages on ORSA

(PRA's industry briefing on 8/9 April)

- *A full ORSA is not necessarily expected of all firms in 2014. But firms are expected to **develop their ORSA starting in 2014**.*
- *Interim ORSA builds on principles underlying ICAS and other prudential requirements in the PRA Handbook, however, firms should extend their preparations on the following:*
 - Own Solvency needs assessments (OSN)
 - Continuous compliance with the regulatory solvency requirements (SCR)
 - Deviations between risk profile and assumptions underlying SCR calcs
 - Compliance with SII Technical Provision requirements



ORSA – expected regulatory timeframe

- **Timeframes**

- Preparation for ORSA commence from January 2014;
- A plan must be prepared to show how the ORSA process will be fully embedded by January 2016
 - Conduct an ORSA gap analysis during 2013 and carry out an ORSA “Lite” to understand those gaps;
 - Plan for dry runs in 2014 with a near final dry run in 2015

“Scrutiny and prominence of ORSA is increasing. Regulators are expecting to see firms use the ORSA as a key decision making tool”





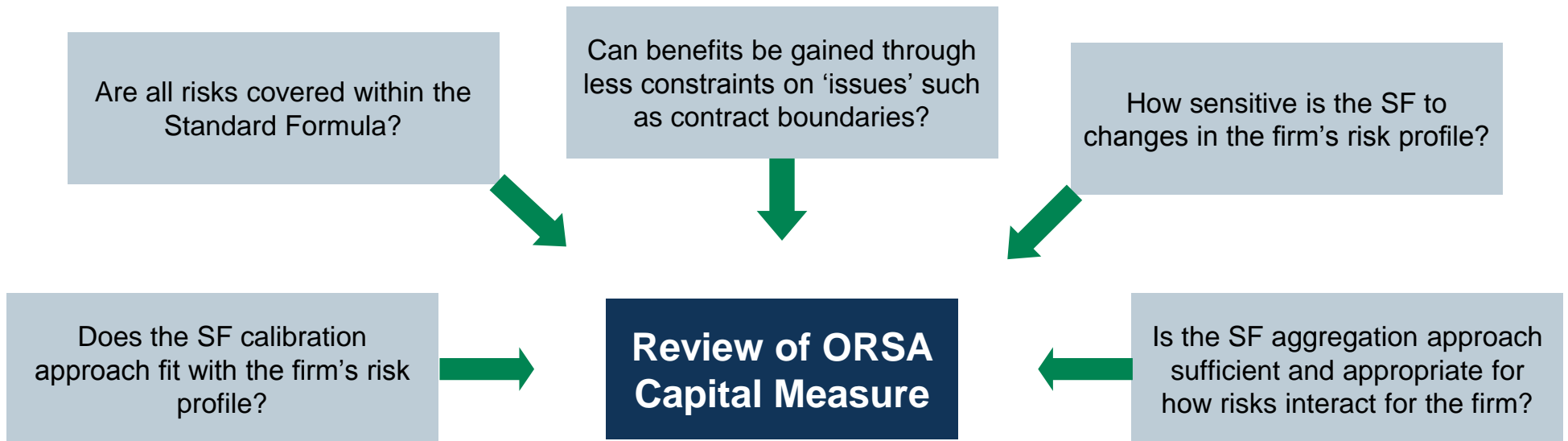
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Quantitative & qualitative assessments of risks in ORSA

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The quantitative work required in the ORSA

Firms using the Standard Formula for Pillar 1 will need to assess whether this is a suitable measure for use within the ORSA



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Assessment of deviations from Standard Formula

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Assessment of deviations

Key components of an analysis of the difference between an undertaking's risk profile and the assumptions underlying the Standard Formula SCR calculation:

- An analysis of the risk profile and an assessment of the reasons why the standard formula is appropriate, including a ranking of risks;
- An analysis of the sensitivity of the standard formula to changes in the risk profile, including the influence of reinsurance arrangements, diversification effects and the effects of other risk mitigation techniques;
- An assessment of the sensitivities of the SCR to the main parameters, including undertaking-specific parameters;
- An elaboration on the appropriateness of the parameters of the standard formula or of undertaking-specific parameters;
- An explanation why the nature, scale and complexity of the risks justify any simplifications used; and
- An analysis of how the results of the standard formula are used in the decision making process.

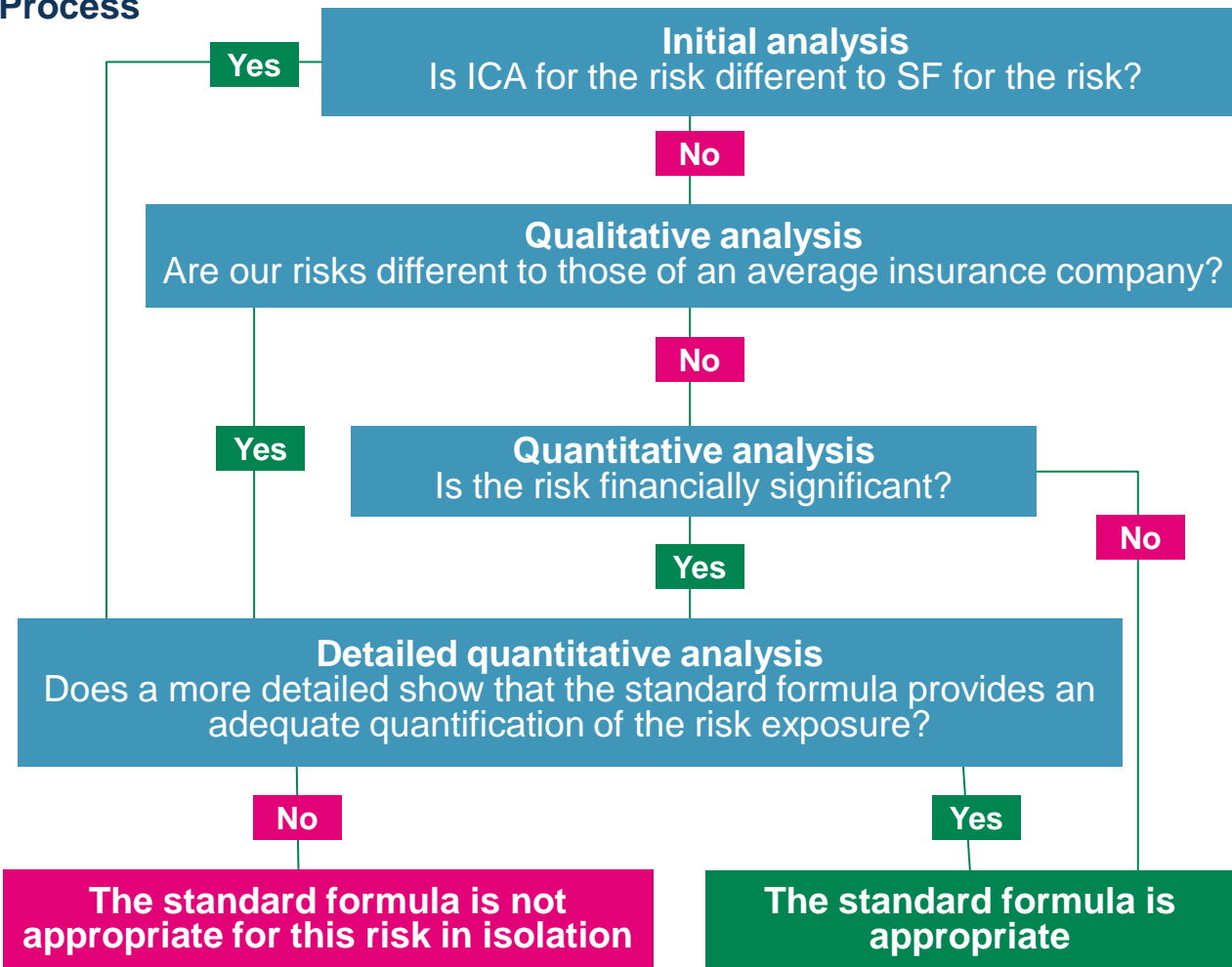
Source: EIOPA Final Report on Public Consultation No. 11/008 On the Proposal for Guidelines On Own Risk and Solvency Assessment - Explanatory Text (July 2012)



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Outline of an approach

Possible Process



Comparison between ICA and Solvency II SCR will give a good feel for the other tests

Typical qualitative questions include:

- What products do we have?
- What investment strategy do we follow?
- What is our customer base?

“Choosing to use the standard formula is an active choice”

Slavko Gvero (FSA Solvency II Implementation Manager)

Stated at speech to firms attending implementation seminars held by the Association of British Insurers, 25 May 2012



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ORSA: Deviations from assumptions underlying the SCR calculation

Proposal for Guidelines on Forward Looking assessment of the undertaking's own risks (based on ORSA principles), March 2013

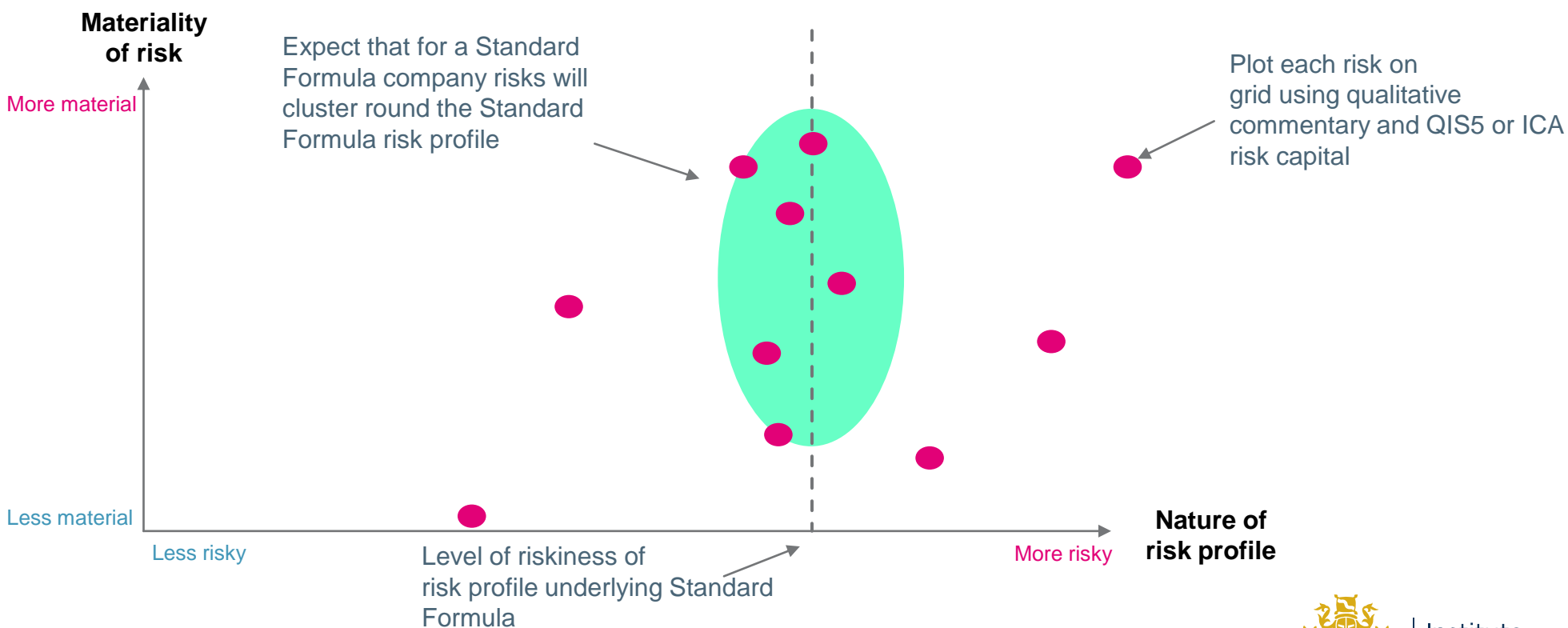
...national competent authorities should ensure that the undertaking assesses whether its risk profile deviates from the assumptions underlying the Solvency II Solvency Capital Requirement calculation and whether these deviations are material.

If the outcome of this qualitative and quantitative assessment is that there are significant deviations between the risk profile of the undertaking and the SCR calculation, the undertaking would be expected to consider during the preparatory period how this could be addressed. It could decide to align its risk profile with the standard formula, to apply for undertaking-specific parameters, where this is allowed, or to develop a (partial) internal model. Alternatively, the undertaking could decide to de-risk.

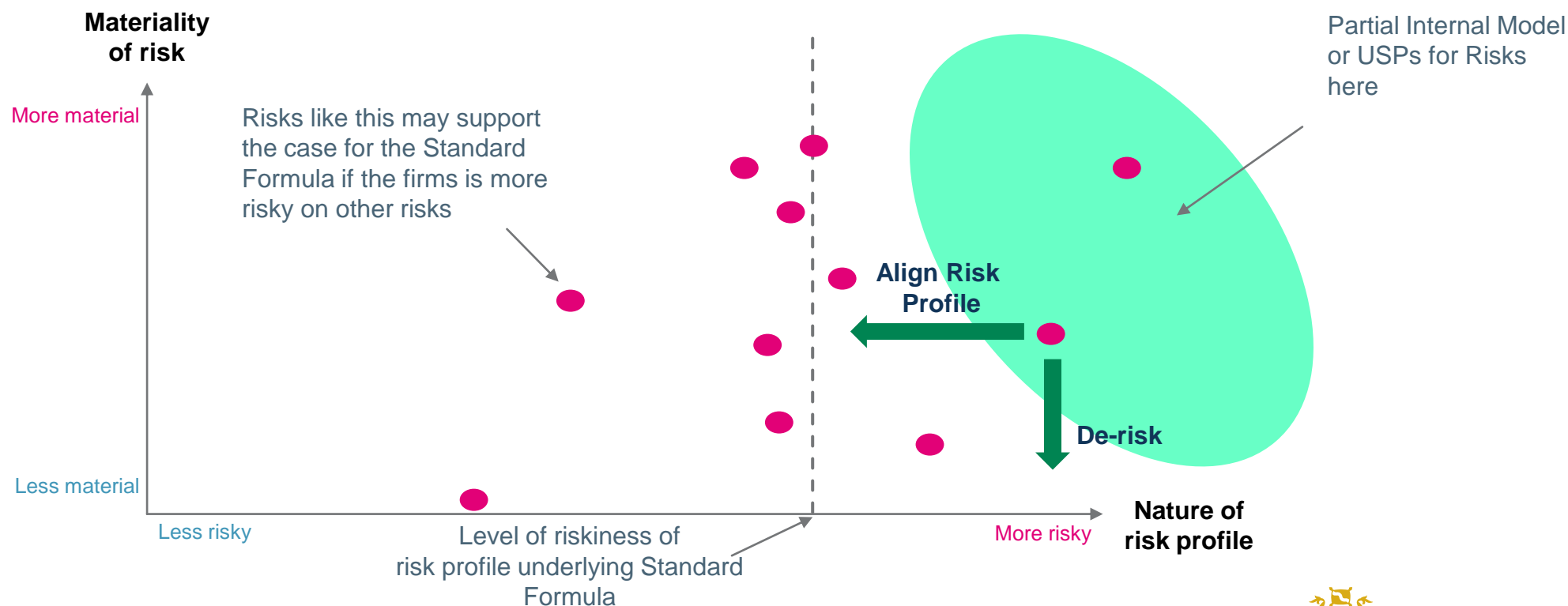


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ORSA: Deviations from assumptions underlying the SCR calculation



ORSA: Deviations from assumptions underlying the SCR calculation





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Current state of UK preparations

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Latest ORSA developments

Current state of UK preparations

Progress to date

- **Training** – Board and Senior Management awareness raised to the ORSA and its component parts. The Board must be fully engaged in the process and help to drive the assessment and provide challenge.
- **Framework Development** – Firms have prepared policies, standards and report templates to help steer the ORSA

Areas for development

- **Board Challenge** – Few reports demonstrate an appropriate level of Board challenge and interaction on the results of the ORSA process. There was very limited information in reports explaining to the Board what the material weaknesses and strengths were
- **Testing and embedding** – Demonstrate the ORSA is being used as a decision making tool and is aligned to the strategic plan for the business



Latest ORSA developments

Current state of UK preparations

Progress to date

- **Report Production** – Populated ORSA reports based on readily available information. Some firms doing phased implementation – Each dry-run building on the last. The contents of the report are now clearer and this must be submitted within 2 weeks of the conclusion of the assessment. Although not specified, this could be considered as the point at which the report is agreed and signed-off by the Board.
- **Report Content** – reports are good at reflecting the end position of the capital positioning

Areas for development

- **Further dry run activities** – Further development of underlying components supporting the ORSA, e.g. projections and link to risk appetite. Also we have seen less progress on the links between components to create a holistic picture of the business
- **Reports should reflect the process** – no clear description of the ORSA process or area where decisions have been made or other ‘use’

Firms need to make sure dry-runs are driving developments rather than just making the process smoother



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Beyond UK and Europe...

Other Regulatory Jurisdictions – Beyond Europe there has been notable interest in implementing an requirements similar to ORSA

North
America

Asia

South
Africa

“Scrutiny and prominence of ORSA is increasing. Regulators are expecting to see firms use the ORSA as a key decision making tool”



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Conclusion

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Key things to consider

- Key role the ORSA plays in justifying your SF approach
- State of your ORSA preparedness
- Status of development plan
- Your company's response to EIOPA's Consultation Paper / PRA messages



Next steps

- Understand where your ORSA is by having a holistic overview of key components and carrying out “gap analysis”
- Impact assessments based on EIOPA’s Guidelines Proposal (link: <https://eiopa.europa.eu/consultations/consultation-papers/index.html>)
- Quantitative and qualitative assessments on deviations from SF basis
- Document your assessments
- Understand key challenges of implementing Standard Formula



Questions

Comments

Expressions of individual views by members of the Institute and Faculty of Actuaries and its staff are encouraged.

The views expressed in this presentation are those of the presenter.



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Thank you!