

Board perspective

PRESENTATION TO IFOA CAPITAL MODELLING SEMINAR
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AGENDA

- Putting the Board's role in perspective
- The role of the Board in capital modelling
- 10 questions Boards might ask about your model
- How to help your Boards provide oversight and challenge to the capital modelling process

Putting the Board's role in perspective

- Performance and Strategy
- UK Corporate Governance Code
- FRC guidance on risk management
- Senior Insurance Managers Regime
- Governance models vary – Risk Committee example
- NEDs role: Support and Oversight

Role of Boards in Capital Modelling

- Ultimately accountable for quality of model
- Oversight and Challenge
- Key issue is how can Boards challenge effectively
- Complexity of model distilled by Executive
- Help Board members to understand overall model design and key assumptions, judgements, sensitivities and limitations.
- Enables Board to understand:
 - Where the model works well/where it does not
 - Whether output is credible
 - If assumptions/judgements are reasonable
- Executive need to provide MI to enable Board to carry out this role
- Detail will depend on company and committee structure

PRA's Questions to NEDs

- Outlined in PRA seminar for NEDs earlier this year
- Gives good insight into PRA's expectations of Boards regarding their understanding of capital models
- Over 40 questions that NEDs might be expected to answer
- Grouped under Model Scope, Key Features and Use of Model, ORSA, System of Governance etc.
- Example (challenging?) questions:
 - Has the Board been involved in agreeing the design of the validation work?
 - What are the key assumptions that underlie the model? How has the Board been involved in assessing these?
 - Is the Board tracking actively how key validation issues are being addressed?
 - Have you seen any of the regulatory reporting data and has this been explained to you by the executives?
 - What contingency plans exist if model approval is not granted? Can the firm survive on the Standard Formula or would it need to take other mitigating actions?

10 questions to answer about your capital model

1. Does the model capture all risks on our Risk Register?
2. Which areas of the business are the most challenging from a model use perspective?
3. Which risk categories do you need to rely most on judgement for calibrating the model parameters?
4. How will I know if the model results are reasonable?
5. What feedback have we had from the regulator and how have we responded to it?
6. What benchmarking has been done on the areas of key judgement?
7. Do the results look credible at lower return periods?
8. How does the CRO get comfortable with the results?
9. What would you change about the model, if time and budget were no constraint?
10. What is a t-copula?

Making it real for the Board

- KPIs using model: E.g Chance of loss ratios exceeding XXX%
- Sensitivity of SCR to changes in key assumptions: Frequency/Severity of cat's up 25%
- Comparison of multiple event impact and SCR
- Executive Summary: E.g. Charts showing erosion of SCR by stress and scenario tests
- Show decisions with and without use of model
- Likelihood approach better than probabilistic?

Some ideas to assist with challenge and oversight

- Training: Bespoke, not general
- Demonstrate the working model
- Learn from senior Executives/technical NEDs
- Answer the 40 NED questions from PRA
-and draft your own Q&A
- Be open about limitations
- Make validation meaningful for Board
- Provide feedback to Board
