Back a winning ORSA
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Objectives for today

• Learn something new
• Do something different
• Insight into market practice
• Audience participation
Agenda

Introduction and market update

Part 1
Risk and capital – example ORSA outputs

Part 2
Emerging risk

Part 3
ORSA reporting

Part 4
Forward looking assessment

Questions

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Institute and Faculty of Actuaries

Introduction and market update
From the ORSA's mouth (LCP ORSA Survey 2014)

46 Firms participated
30 Face-to-face
16 Online questionnaire

Key messages

- Time and resource is the largest non-technical challenge
- Is it a report or is it a process?
- Would organisations benefit from an ORSA process timetable?
So what?

Which of the following do you think adds most value?

1. Emerging risks
2. Risk appetite
3. Scenario analysis and reverse stress testing
4. Forward looking assessment
5. Continuous solvency assessment
Which of the following do you think adds least value?

1. Emerging risks
2. Risk appetite
3. Scenario analysis and reverse stress testing
4. Forward looking assessment
5. Continuous solvency assessment

It's a one ORSA firm
Risk and capital

Don’t put the cart before the ORSA

Risk Appetite  Aggregate level risk willing to accept in order to achieve business objectives
Risk Tolerance  Early warning indicators to ensure risk appetite is not breached
Risk Limit  Operating limits

Capital impairment  Earnings targets  Investments or liquidity  Operations

Set and measured by risk module
Operating limits
Don’t put the cart before the ORSA

Capital Impairment (loss as a % of capital)

<table>
<thead>
<tr>
<th>Return Period</th>
<th>% of capital impaired</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 in 4</td>
<td>10%</td>
</tr>
<tr>
<td>1 in 10</td>
<td>25%</td>
</tr>
<tr>
<td>1 in 50</td>
<td>55%</td>
</tr>
</tbody>
</table>

Does this style of risk appetite work?

1. Effective way to start a debate on risk appetite
2. Has potential, I could see some uses for it
3. Not convinced, but may consider further
4. Don’t really see the point
Don’t look a gift ORSA in the mouth


<table>
<thead>
<tr>
<th>Year</th>
<th>TP at 31/12/2012</th>
<th>TP at 31/12/2013</th>
<th>TP at 31/12/2014</th>
</tr>
</thead>
<tbody>
<tr>
<td>2012</td>
<td>£16.4m (best estimate)</td>
<td>Around 1 in 4 bad year relative to 2012 SCR calculations</td>
<td>£14.4m. Around 1 in 6 good year relative to 2012 SCR calculations and 1 in 300 good year relative to 2013</td>
</tr>
</tbody>
</table>

Can you see uses for this style of information?

1. Plenty of possible uses
2. Limited uses, depending on what model output is easily available
3. More of a validation tool than anything else
4. Don’t really see the point
Don’t get saddled with uninformative scenarios

Consultation Paper on the proposal for Guidelines on system of governance and own risks and solvency assessment

“…a sufficiently wide range of stress test or scenario analyses…”

“…carry out stress tests and scenario analyses to assess the resilience of the business.”

Don’t get saddled with uninformative scenarios

Compare scenarios side-by-side

<table>
<thead>
<tr>
<th>Write 25% more business</th>
<th>Impact at mean</th>
<th>Impact at 99.5th</th>
</tr>
</thead>
<tbody>
<tr>
<td>- Across all LoBs evenly</td>
<td></td>
<td>Insert in £</td>
</tr>
<tr>
<td>- Within specifics LoBs</td>
<td></td>
<td>Insert in %</td>
</tr>
</tbody>
</table>

Consider more than just numbers

<table>
<thead>
<tr>
<th>Overview of scenario</th>
<th>Describe scenario</th>
</tr>
</thead>
<tbody>
<tr>
<td>Scenario impact</td>
<td>Financial, reputational, operational issues etc</td>
</tr>
<tr>
<td>External factors</td>
<td></td>
</tr>
<tr>
<td>- reducing / increasing scenario likelihood or impact</td>
<td></td>
</tr>
<tr>
<td>Key controls</td>
<td></td>
</tr>
<tr>
<td>Agreed management actions</td>
<td></td>
</tr>
</tbody>
</table>
Emerging risks

The dark ORSA

- Environmental
  - Nanotechnology
  - Solar Storms
  - Methane Hydrate
  - Middle East crisis (including Iraq and Gaza)
  - Ebola

- Social / Economic / Political
  - UK Leaving EU
  - North Korea
  - Ukraine crisis
  - Reform of insurance contract law
  - Bitcoin
  - Fracking

- Legal / Regulatory
  - Lloyd's control framework
  - IFRS regulation
  - ConFrame
  - FSA Recovery & Resolution

- Technological
  - Cyber

Timeframe
- 0-3 years
- 3-5 years
- 5+ years
- Current

22/09/2014
Can analysis of emerging risks actually be useful?

1. Can run scenario analysis, consider mitigation actions and prepare ahead of time in order to make better decisions

2. Can consider the impact for the business, but unlikely to change/influence decisions

3. By the time there is enough information the risk is no longer emerging

4. Don’t really see the point

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ORSA reporting
Key messages

- Challenge to get the right balance between satisfying regulators and the Board
- Making the ORSA available to a wider audience
- Year-round, continuous reporting

ORSA’s for courses...

- Board
- Risk Committee
- Regulator
- Shareholders
- Staff
Did you read your firm’s last ORSA report?

1. Yes – from cover to cover
2. I skimmed through it
3. Just the exec summary
4. No – I don’t get to see it
5. No – I have access but haven’t read it
6. Not applicable

Forward looking assessment
1. Qualitative assessment

Some narrative about likely future capital requirements, eg maintaining “status quo” or reducing risk/capital.

ORSA report

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Future capital

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2. Simple deterministic approach

<table>
<thead>
<tr>
<th>£m</th>
<th>Mean profit</th>
<th>Independent 1 in 200 result</th>
<th>Difference from mean</th>
<th>Allocated capital</th>
</tr>
</thead>
<tbody>
<tr>
<td>Catastrophe risk</td>
<td>5</td>
<td>-95</td>
<td>-100</td>
<td>50</td>
</tr>
<tr>
<td>Premium risk</td>
<td>50</td>
<td>-300</td>
<td>-350</td>
<td>310</td>
</tr>
<tr>
<td>Reserve risk</td>
<td>3</td>
<td>-197</td>
<td>-200</td>
<td>150</td>
</tr>
<tr>
<td>Credit risk</td>
<td>0</td>
<td>-50</td>
<td>-50</td>
<td>15</td>
</tr>
<tr>
<td>Operational risk</td>
<td>-3</td>
<td>-78</td>
<td>-75</td>
<td>25</td>
</tr>
<tr>
<td>Market risk</td>
<td>10</td>
<td>-115</td>
<td>-125</td>
<td>75</td>
</tr>
<tr>
<td>Total (undiversified)</td>
<td>65</td>
<td>-635</td>
<td>-900</td>
<td>625</td>
</tr>
</tbody>
</table>

Scenarios
- Profitability forecast worsens by £20m
- Write 25% more catastrophe business
- Increase reserves by 50%
- Total for all scenarios

Projected capital next year: 770

3. Re-run model with new inputs

| t=1 balance sheet | Assets | Liabilities | Net assets |
| Future assumptions |

| t=2 balance sheet | Assets | Liabilities | Net assets |
| Projected future assumptions |
4. Multi-year stochastic model

Future capital requirements at t=1, t=2, t=3...etc

Future assumptions, including future time dependent assumptions dependencies

$t=0$ balance sheet
Assets
Liabilities
Net assets

$t=0$ BS
$t=1$ BS
$t=2$ BS
$t=3$ BS
$t=4$ BS
$t=5$ BS

Forward looking assessment: which method should you choose?

- What are your plans and scenarios?
- What risks are you trying to model?
- Are you really demonstrating model use?
- Parsimony?
- What are you using the numbers for?
Cracking the whip on continuous compliance

- Shift in understanding following recent EIOPA guidance
- Retrospective?
  - Meeting minutes
  - Signposting reports
  - Capital tracking
- Prospective?
  - FLAOR
  - Policy confirmation statements
  - Audit plans

Are you concerned about continuous compliance?

1. Very concerned
2. Fairly concerned
3. Not really concerned
4. I haven’t thought about it yet
Wrap up

Your best bet is an accumulator…

- Clear communications
- Good engagement
- Compliant with requirements
- Reporting
- Maximise efficiency
- Clear scoping
- Interaction
- Emerging value
- Genuine integration
Your best bet is an accumulator…

Clear communications  Good engagement  Compliant with requirements

Reporting  Maximise efficiency  Clear scoping

Interaction  Emerging value  Genuine integration

How have you found this session?

1. Very useful and I have learnt something
2. Useful and I will use these slides for reference
3. Useful, but greater technical detail would have been beneficial
4. Useful, but too much technical detail for me
5. Not very useful

...Vote