

ICAS Making the most of your FSA feedback Workshop C05

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Agenda

- Introductions
- Update on ICA progress
- Improving governance and demonstrating Board ownership
- Acting on FSA feedback
- Operational risk considerations
- Developments in scenario testing
- Analysis of change and key messages for analysts
- Future challenges
- Questions

Update on ICA progress

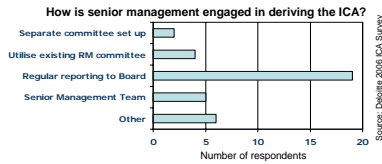
- FSA has received ICA submissions from over 50 firms
- Gap between ICG and ICA has been reducing
- Underlying methods largely unchanged
- Greater use of hedging, reinsurance or financial engineering to manage risk
- More robust approaches to operational risk are being planned and adopted
- Embedding the ICA and scenario testing are still the greatest challenges
- Greater information available to help

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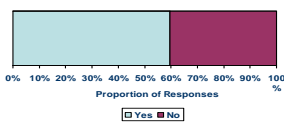
Improving governance and demonstrating Board ownership

- The FSA investigates the use of the ICA in risk management by asking;
 - How is senior management engaged with the process and what data sources are used?
 - How are ICAS principles and models used for day to day management?
 - How is ICAS used to influence risk management strategy?

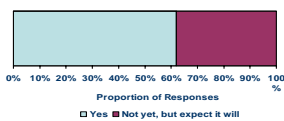


Improving governance and demonstrating Board ownership

Are ICAS principles used for day to day management purposes?



Are the ICA results used to prioritise risk management activities within the business?



Improving governance and demonstrating Board ownership

- The ICAS regime is more than just calculating a number for the regulator
- ICA provides a framework to investigate, quantify and manage risks and their interactions
- This can feed into an integrated approach to risk management including,
 - Defining internal risk appetite
 - Refining process and controls, including risk identification and monitoring
 - Pricing
 - Business planning
- Governance could include external review

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Acting on FSA feedback

- Common areas for capital add ons include
 - Operational risk
 - Management actions
 - Capital resources
 - Mortality catastrophe
 - Correlation assumptions
 - Non linearity
 - Quality of risk management
- These represent future areas of development for many companies
- Feedback only given in significant areas of concern

Acting on FSA feedback

- But ICG is not just about capital add ons – it also includes qualitative feedback points
 - Indicating areas where firms have done a good job!
 - Highlighting areas where the FSA is requesting or recommending further work
 - Where capital may not be the best mitigant
- Feedback items may be more likely to lead to additional work than capital add ons
- Actions taken must not conflict with other areas, eg TCF

Acting on FSA feedback

- Some common items for qualitative feedback include
 - Improved identification and quantification of individual risks
 - More robust methodologies
 - Further consideration of aggregation and scenario testing
 - Derivation of internal risk appetite
 - Identification of ICA trigger points
 - Analysis of change
 - Evidence that ICA is being embedded into the business

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Operational risk considerations

- Good operational risk assessment in the ICA relies on;
 - Links to the Risk Management Framework
 - A robust methodology to produce a capital number
- Risk Management Framework
 - Difficult to mitigate all types of operational risk
 - Near misses
 - Actuarial operational risk!
 - One of the few risk areas that can affect all employees... harder to embed but everyone can get involved

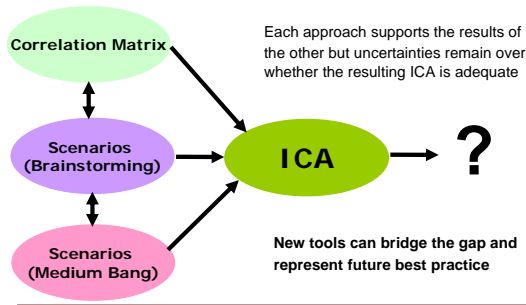
Operational risk considerations

- Robust methodology
 - Top down vs bottom up
 - Diversification between operational risks and other major risk categories
 - Sensitivity testing important
 - Limited historic data available so requires senior management judgement
 - Senior management challenge to the results
- A challenging area!
- One of the least developed major risk categories for most companies
- Hard to convince the FSA you've done a good job as it's relatively subjective
- Lots of companies are still improving their OR assessments

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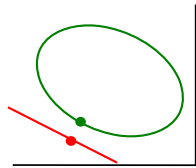
Developments in scenario testing



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Developments in scenario testing

- Many companies are now developing "smarter" scenario testing
 - Targets the most onerous scenario at given confidence level
 - Retains the simplicity of the stress test and correlation approach
 - The ease of communication of a scenario test
 - Implicit allowance for non-linearity
- Identifying adverse scenarios helps risk management and consideration of risk mitigation
- Allows impact of potential management actions to be explored and evaluated



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Analysis of change and key messages for analysts

- AOC increasingly important now that ICA is BAU
- Important for the next round of ICA reviews by the FSA
 - Arrow and ICA review more likely to be integrated
 - FSA may require AOC between current ICA and that seen previously
- An important risk control
- Information for analysts
 - demonstration of reliable numbers
 - strong internal risk controls
 - governance and risk management framework
- ICG is currently private, Solvency 2 may be public

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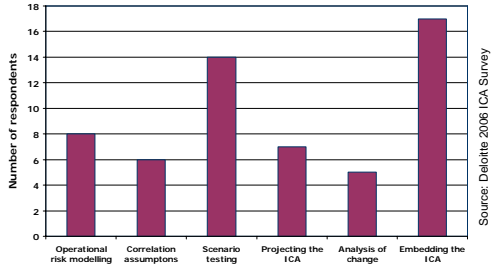
Will ICG ever equal ICA?

- This time last year, ICG was between 110% and 170% of ICA
- Since then the average capital add on as a percentage of ICA has reduced
 - Fewer companies missing obvious items of risk
 - FSA will now consider material areas of prudence
 - Some companies have restated elements of the ICA during the review process
- Industry knowledge and best practice will continue to evolve
- It is expected the gap between ICA and ICG will continue to reduce

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Future challenges for life insurers

What do you see as the main unresolved challenges as part of the ICA requirements?



Source: Deloitte 2006 ICA Survey

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Future challenges for life insurers

- Focus moving from calculating numbers to risk management
- Many firms planning further developments
- The FSA has repeated their 2003 exercise to assess risk management practices and the extent to which ICAS is integrated
- The FSA is now reviewing smaller companies' ICAs
- Group capital requirements are becoming a major consideration
- Solvency 2 – likely to have much in common with the ICA regime, while bringing further challenges of its own.

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Questions



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