ORSA – Bigger Picture Thinking
Niamh Hensey

Introduction to the ORSA
The Basics – What is an ORSA?

- The ORSA is a Pillar 2 requirement defined in Article 45 of the Directive.

- Company’s own risk profile and tolerance limits
- Continuous compliance
- Short and long term risks
- Proportionate to risks inherent in the business
- Integral part of business strategy
- Deviation from assumptions underlying SCR calculation
- Taken into account in strategic decisions
Other key points on ORSA requirements

- Performed at least annually
- Disclosed privately to the regulator in the *Report to Supervisors*
- Summary of ORSA process in *Solvency and Financial Condition Report*
- Documentation
  - *ORSA policy*
  - *ORSA process*
  - *ORSA report*
- Management body of the organisation needs to take an active role in the ORSA process and sign-off the results
Existing and expected future expected guidance on ORSA

CEIOPS 5 Principles (May ‘08)

1. Responsibility of the undertaking
2. Encompass all material risks
3. Adequate measurement/assessment processes and embedded in the decision making
4. Forward-looking
5. Appropriately evidenced/document and independently assessed

Level 3 guidance
(pre-consultation paper December 10)

1. Capturing all risks
2. Forward looking perspective
3. Ownership / role of governing body
4. Communications
5. Processes versus the report
6. ORSA linked to business strategy
Other reference points – Emerging regional and national standards

<table>
<thead>
<tr>
<th>Territory/Domicile</th>
<th>Regulatory/Supervisory Authority</th>
<th>Risk and Solvency Assessment</th>
<th>Status/Comment</th>
</tr>
</thead>
<tbody>
<tr>
<td>EU</td>
<td>European Insurance and Occupational Pensions Authority (EIOPA)</td>
<td>Own Risk and Solvency Assessment (ORSA)</td>
<td>Expected to come into force on 1 January 2013</td>
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<tr>
<td>US</td>
<td>US National Association of Insurance Commissioners (NAIC)</td>
<td>Own Risk and Solvency Assessment (ORSA) for the Solvency Modernization Initiative</td>
<td>Proposals currently being discussed by the Group Solvency Issues Working Group</td>
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<tr>
<td>Bermuda</td>
<td>Bermuda Monetary Authority (BMA)</td>
<td>Commercial Insurer’s Solvency Self Assessment (CISSA)</td>
<td>Expected to become effective in 2011, CISSA combines ERM and ORSA requirements</td>
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<tr>
<td>Switzerland</td>
<td>Swiss Financial Market Supervisory Authority (FINMA)</td>
<td>Risk Management/Internal Control System Tool (RM/ICS Tool)</td>
<td>Developed in 2007 by FINMA as part of the Swiss Quality Assurance (SQA)</td>
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<tr>
<td>Australia</td>
<td>Australian Prudential Regulation Authority (APRA)</td>
<td>Internal Capital Adequacy Assessment Process (ICAAP)</td>
<td>Capital standards under review following 2010 consultation — final standard expected to be implemented in 1 January 2013</td>
</tr>
<tr>
<td>Canada</td>
<td>Superintendent of Financial Institutions Canada (OSFI)</td>
<td>Dynamic Capital Adequacy Testing (DCAT)</td>
<td>In 2009, OSFI published guidance on stress, scenario, and sensitivity testing to extend the use of testing beyond DCAT</td>
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</table>
ORSA is as much about the process as the numbers…

- Product of an ORSA is a solvency assessment
- BUT a great deal more focus on risk management process
- Qualitative - Regulator likely to be as concerned with whether the process works than on the quantum of the numbers
- Forward looking - what may cause risk position to change
- Process should include continuous monitoring of internal and regulatory minimum solvency
- Integration with business management
- Proportionality
What does the ORSA process look like?

Risk Management Framework

- Risk Appetite
- Stress & Scenario Testing
- Identify & Assess Risks
- Monitoring & Reporting
- Link to Business Strategy
- Risk Culture
Compare ORSA with existing ICA calculations currently forming UK Pillar 2 requirements

<table>
<thead>
<tr>
<th>AREA</th>
<th>ICA</th>
<th>ORSA</th>
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</thead>
<tbody>
<tr>
<td>Calculation frequency</td>
<td>At least annual</td>
<td>At least annual</td>
</tr>
<tr>
<td>Calculation Time horizon</td>
<td>1 Year (few perform run-off ICAs)</td>
<td>Business planning period</td>
</tr>
<tr>
<td>Confidence level</td>
<td>1 in 200 over 1 year</td>
<td>Company specific</td>
</tr>
<tr>
<td>Allowance for new business</td>
<td>1 year / allowance for closure</td>
<td>Full</td>
</tr>
<tr>
<td>Links to business plan</td>
<td>Some consideration</td>
<td>Stronger links</td>
</tr>
<tr>
<td>Scenario testing</td>
<td>Some short term</td>
<td>Longer term including consideration of changing business plans</td>
</tr>
<tr>
<td>Capital planning</td>
<td>More of a snapshot</td>
<td>Explicit requirement to consider ability to raise own funds in future</td>
</tr>
<tr>
<td>Disclosure</td>
<td>Supervisor only</td>
<td>Supervisor only</td>
</tr>
<tr>
<td>How are deficiencies addressed by regulator</td>
<td>Mainly capital add-ons</td>
<td>Capital add-ons possible / More focus on fixing the process</td>
</tr>
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</table>
ORSA reconciled to Solvency II Pillar 1 - SCR

- Potential differences to standard model SCR
  - Additional risks
  - Methodology differences
  - Different assumptions

- Potential differences to internal model SCR
  - Different metrics
  - Time horizon
  - Confidence level
## Responsibilities of company stakeholders

<table>
<thead>
<tr>
<th>Role</th>
<th>Responsibilities</th>
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<tbody>
<tr>
<td><strong>Board / executive</strong></td>
<td>Setting overall business strategy and risk appetite</td>
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<tr>
<td></td>
<td>Engaging with stress tests</td>
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<td></td>
<td>Sign-off of ORSA deliverables</td>
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<tr>
<td><strong>Risk management function</strong></td>
<td>Producing ORSA report</td>
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<tr>
<td></td>
<td>Developing risk reporting templates (with others)</td>
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<tr>
<td></td>
<td>Managing scenario testing and reverse stress testing</td>
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<tr>
<td><strong>Actuarial function / Finance</strong></td>
<td>Developing risk measurement tools</td>
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<td></td>
<td>Investigating risk-reward optimisation</td>
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<td></td>
<td>Stress &amp; scenario analysis / financial projections</td>
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<tr>
<td><strong>Strategy / Treasury function</strong></td>
<td>Business planning</td>
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<tr>
<td></td>
<td>Capital structure</td>
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<td></td>
<td>Input on strategic direction</td>
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<tr>
<td><strong>External organisations / Internal Audit</strong></td>
<td>Challenge, benchmarking and independent review</td>
</tr>
<tr>
<td></td>
<td>Ensuring appropriate control framework</td>
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<td></td>
<td>Quality assurance</td>
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How could this process fit into an annual timeframe?

Q1:
- Review Risk Appetite
- Annual SCR Calculation
- Capital management planning
- Measure risk culture
- Review and Update ORSA Policy and Process
- Monthly Risk Committee Meeting

Q2:
- Annual risk review
- Business Planning Period
- Review Hedging & Reinsurance Strategy

Q3:
- Capital management planning
- Stress and Scenario Testing of base position and Business Plans

Q4:
- Model Updates and Improvements
- Quarterly SCR update
- Quarterly SCR update
- Quarterly SCR update
- Produce Annual ORSA Report
The ORSA is a way to realise benefits of Solvency II!

• Better risk awareness and foresight
  – More insightful decision making
  – Forward looking and proactive risk management

• Focusing management attention on risks that matter
  – Focus on regular, current and relevant information

• Increased alignment of risk appetite and business strategy
  – ORSA pulls together existing ERM components

• Improve capital efficiency
  – Reduce cost of capital through better management of volatility
  – Uncover natural hedges

• An internal model, without the formal approval process!
Questions or comments?

Expressions of individual views by members of The Actuarial Profession and its staff are encouraged.

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