The ORSA Process In Action

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Solvency II in Europe – fast version

- Solvency II is expected to be implemented by January 2016 ..maybe
- Partial implementation country by country – focusing on the ORSA process and models
- Convergence at a later stage
- Capital models are being refined but still debated and presumably changed

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What is the ORSA Process ?

- The insurance company is required to perform an ORSA process
  - The ORSA process is crucial, and represents a large part of the companys overall risk management.
  - ORSA is laid down in article 44 within the directive.
  - ORSA =**O**wn **R**isk & **S**olvency **A**ssessment.
  - ORSA is a detailed analysis of the of companys current risks, future risk, and their consequences.

ORSA Process - Deliverables

- The purpose of ORSA is for the management to understand:
  - Business model
    - Life, Non-life, reinsurance, lines of business, etc.
  - The risk universe
    - (”lists of expected risks”)

ORSA Process - Deliverables

– Risk profile
  - A description of the risks, as well as a quantified assessment of the risks
  - Should cover the current risks and future risks, and their potential consequences.

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ORSA Process- deliverables

– Strategy

– Financials /budget

– The process needs to show that the board and management have identified and analysed all relevant risks

– Two reports:
  - One to be included in annual report
  - One for local supervisory authorities

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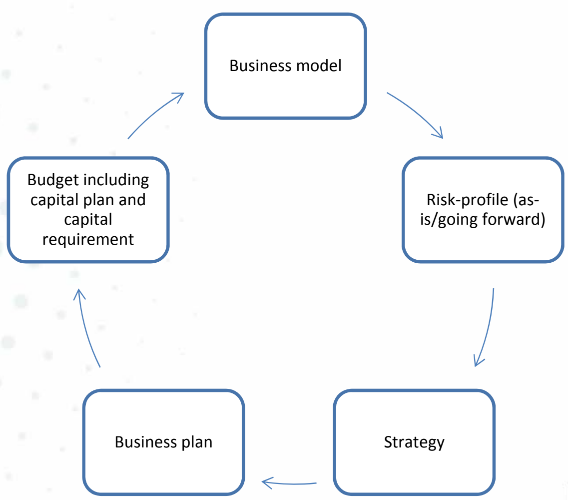
The ORSA Process Report

- The report should include:
  - The process (flow charts), including the staff involved.
  - What kind of information/data was available ?
  - The risk profile
  - Does the company have adequate resources or to many resources, in terms of:
    - Capital
    - Staff
    - IT
    - Other
  - How is ORSA integrated with strategy formulation and does the company need to change its strategy ?

Risk Process



Changes of the actuarial role

- From appointed actuary to cheif risk officer
- Risk advisor
  - Reserve calculation (find the trends, changes of exposure) – how might this impact our tariff, say ?
  - Uncertainty – what is the impact relating to the capital situation ?

Opportunities but also requirements …

- The Chief risk officer/risk advisor should be able to :
  - Communicate with (top)management and the board
  - Be able to communicate and collaborate with underwriters, claims handlers, finance, HR etc.
- A win-win situation : Both ”parties” can learn a lot from each other

Risk Profile

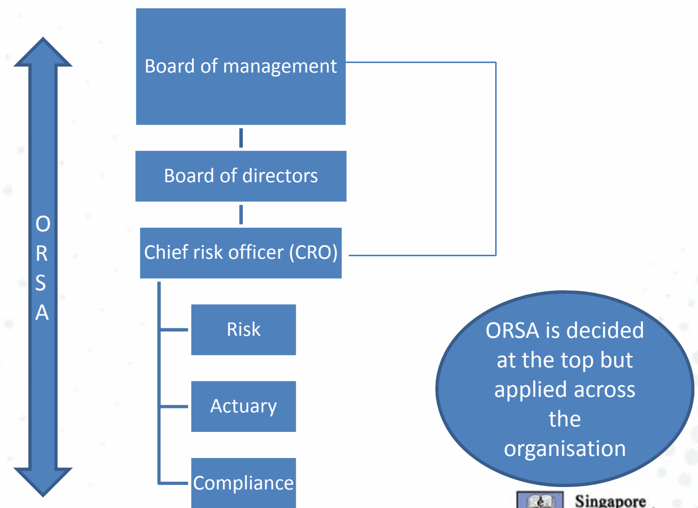
- Underwriting
  - Products/segments
  - Customers
  - Concentration of risks
- Market risks
  - Investments
- Operational risks
  - IT-systems, processes, image, other.

Takes a lot of work !

How to Measure Risks ?

- The risks are measured by the uncertainty from the expected costs.
- The ”uncertainty” is in most cases based on a rare event – say a 200 year event (which is also being used within the QIS 5/LTGA model).
  - See https://eiopa.europa.eu/ to find the XL-standardmodel

Risk organisation and ORSA



Risk Assessment and Priorities

Risk Evaluation

- Maybe based on a 200 year event.
- Diversification.

Priority of Risks

Insurance Risks /Data

- This Includes:
  - Reserves
  - Underwriting
  - Catastrophe risks
- Reserves
  - Process, models et cetera shall be presented to supervisory authorities.
- Underwriting
  - Claims history – could be based on segments.
  - Analysis of claims – including big claims
  - Maybe concentration risks
  - Terms and conditions
  - Forecasts/budgets

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Insurance Risks - continued

- Catastrophe Risks
  - Standard scenarios maybe from QIS 5/LTGA
  - Catastrophic scenarios that are not being captured by QIS 5/LTGA
- In relation to this the companys reinsurance-program should be assessed and evaluated.
- Decisions on reinsurance, should be supplemented with a cost/benefit analysis of the capital requirement.

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Market Risks

- Securities need to be assessed, with respect to:
  - Equity risks
  - Bond risks
  - Structured products
  - Properties
  - Currencies
  - Concentration
  - Counterparties(credit risk)
- The analysis should be performed in QIS 5/LTGA
  - Including Asset/Liability considerations.

Operational Risks

- The standard model is simple.
- Should be assessed in relation to:
  - The undertakings processes
  - IT-systems
  - Fraud
  - Competences
  - Key employees
  - Communication
  - Infrastructure

Risk Assessment

- The processes behind the assessment of all key risk areas, need to be described in detail.
- Substance over form – not the other way around

Risk Appetite

- The company needs to determine risk appetite for all key areas.
- If the risk appetite changes, so does the risk profile.
- Holistic assessment, not marginal.

Strategy and Budget

- The strategy should be formulated in conjunction with the risk appetite.
- Then a plan for the undertaking should be produced, with a budget.

Capital Plan and Capital Contingency Plan

- The capital plan is the undertakings assessment of the derived capital requirement, adhering to the budget and undertaking plan, on a 3-5 years time horisont. Remember stress-testing.
- Capital contingency plan – short term activities to counter an ”economic catastrophe”, that erodes the companys equity.

Implementation of ORSA

- To initiate the implementation of Solvency II, we begin with the ORSA process
- Start with a pilot project
  – One product or something else
- Collect all risk information relating to this pilot project:
  – Claims, reserver, policies, process information etc

Implementation of Solvency II

- One way to do it : Involve the board and management in the implementation process in order to stay focused
- Present risk information and state what is missing/needs to be improved and why it is important
- Try to do an ORSA – only covering one area
- Project planning can be begin and results from the implementation of Solvency II can used ”immediately”

ORSA in Action – Growth scenario

Questions that can initiate the ORSA-process :

- What is the rationale behind obtaining a market share of XX% ? **(strategy)**
- When shall a market share of XX % be obtained ? **(strategy /budget/capital)**
- Is there a timeframe for when the goals should be achieved ? **(budget and implementation)**
- Shall the growth be profitable in the whole period ? **(budget)**
- Growth based on unchanged lines of business? **(risk profile and risk appetite)**
- Growth based on an unchanged tariff ? **(strategy and budget)**
- Shall growth be organic ? **(strategy)**
- Compete on price, coverage or … ? **(strategy)**
- Indifference to which products that should deliver growth ? **(strategy)**
- Which countries should growth come from ? **(strategy)**
- How shall growth be distributed on respective distribtion channels and products ?**(strategy)**
- How large a provision expense should deliver growth ? **(budget)**
- Is the risk profile changed by growth ? **(risk profile)**
- Have preconditions for decisions and budgets, been stress tested ? **(Stresstest)**
- How does growth encumber SCR ? **(capital assessment)**
- Can the growth be absorbed in the current capital plan or is a revision required? **(capital plan)**
- How will competitors react and will this hurt the company ? **(strategi)**
- Does growth require more employees ? **(budget)**
- Are the current premises adequate ? **(budget)**
- Can existing administrative systems handle growth ? **(budget)**
- Are there existing alternatives where the company with certainty can make the same amount that the growth is expected to provide, or that implies a lower capital requirement? **(strategy)**

ORSA – In Conclusion

- As a matter of fact, ORSA is a systematic way to assess the undertaking, or to make decisions, based on a risk based approach.

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