



The Solvency II ORSA Process

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Agenda

- Purpose of Session
- What is ORSA?
- ORSA and the Internal Model/Standard Formula
- Entity Specific Considerations
- Role of the Actuary
- Outline Contents of Process
- Conclusion



Purpose of Session

Terms of Reference:

- *To produce and present a paper for the members of the Society of Actuaries in Ireland which:*
 - *Reviews the existing literature on the ORSA process.*
 - *Explains the ORSA process and its place in the Solvency II regime.*
 - *Discusses the role of the actuary in the ORSA, covering both Life and Non-Life practice areas.*
 - *Outlines the potential contents of the ORSA process.*



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What is ORSA? - CEIOPS

“the ORSA can be defined as the entirety of the processes and procedures employed to identify, assess, monitor, manage, and report the short and long term risks a (re)insurance undertaking faces or may face and to determine the own funds necessary to ensure that the undertaking’s overall solvency needs are met at all times.”

Source: CEIOPS ORSA Issues Paper (May 2008)]



What is ORSA? - Directive

- ORSA is set out in Article 45 of the Solvency II directive (paraphrased below)
- ORSA must include at least:
 - Assessment of the overall solvency needs of the undertaking allowing for risk profile and business strategy.
 - compliance, on a continuous basis, with the SII capital requirements.
 - Assessment of risk profile versus the assumptions underlying the SCR calculation.



What is ORSA? - Directive

- ORSA processes should be proportionate to the nature, scale and complexity of the risks inherent in its business.
- ORSA should be an integral part of the business strategy and should be performed regularly, and without any delay following any significant change in their risk profile.



What is ORSA? - Directive

- ORSA is documented and reported to the regulator.

“The non-identification of issues in the ORSA may prove to be of just as much concern to supervisors as the issues themselves”

Source: CEIOPS ORSA Issues Paper (May 2008)]

- ORSA does not of itself create an additional capital requirement.



What is ORSA?

- ORSA is a fundamental part of the risk management system for an insurance undertaking.
- ORSA is not a one-off exercise or a single report.
- Think of ORSA more as a documented process.
- There will be a central report drawing together the various elements of the process.



What is ORSA? - Responsibility

- ORSA sits in the Risk Management Function.
- However, article 48 sees a clear role for the Actuarial Function in supporting the ORSA.
- While the execution of the ORSA can be outsourced, the administrative or management body remains responsible.



What is ORSA? – Life/Non-Life

- Principles of ORSA are common to Life and Non-Life.
- Focus will differ due to different risk profiles.
- Current Life FCR may be a useful starting point for the Capital Plan element of ORSA.



What is ORSA - Literature

- Main sources
 - The Directive
 - CEIOPS Issues Paper 2008
 - Groupe Consultatif response to Issues Paper.
- No “Level 2” implementing measures.
- Level 3 material expected early 2011.



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ORSA and the Internal Model/Standard Formula

ORSA view of Capital:

- “Economic Capital” v “Regulatory Capital”
- Economic Capital may allow for
 - Different time horizon/risk measure
 - Business plans
 - Risks not captured in the SCR
 - Future sources of capital
- NB – ORSA does not create an additional regulatory capital requirement.



ORSA and the Standard Formula

- Evaluate appropriateness of Standard Formula:
 - describe the risk profile of the company.
 - Consider SCR module by modules.
 - Test sensitivity of the standard formula to changes in the risk profile.
- Justify, analyse and explain the impact of USP's.
- Justify any simplifications applied to the standard formula.



ORSA and the Internal Model

- Model Governance.
- Model Scope
 - Risk identification and assessment .
 - Which risks are to be modelled?
- Model Calibration, Data, Statistical Quality.
- Reconcile Internal Calibration to SII Calibration.
- Analyse and explain the differences between
 - the Model SCR, and
 - the SCR calculated using the Standard formula.



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Entity Specific Issues - Proportionality

- ORSA principles are the same for all companies.
- ORSA process will reflect Nature, Scale and Complexity of risks.



Entity Specific Issues - Proportionality

“Uncertainty about what will be expected of undertakings in the performance of the ORSA raises concerns, especially for small and medium-sized undertakings, of very demanding requirements. Aware of these concerns, the EC has ... stated ... that the ORSA:

- Does not require an undertaking to develop an internal model.*
- Is not a capital requirement different from the SCR and the MCR.*
- Should not be too burdensome.”*

Source: CEIOPS ORSA Issues Paper (May 2008)]



Entity Specific Issues - Proportionality

“the ORSA may take different levels of sophistication according to the nature, complexity and scale of the risks inherent in the business, ranging from simple stress test calculations on the material risks to the use of more advanced methodologies similar to the ones used in partial or full internal models”.

Source: CEIOPS ORSA Issues Paper (May 2008)]



Entity Specific Issues – Group ORSA's

- Solvency II allows for “Centralised Risk Management” (CRM)
- Irrespective of CRM, each regulated entity will still have its own ORSA
- Independent of CRM, groups can apply for a centralised ORSA process.



Entity Specific Issues – Group ORSA's

CEIOPS Level 2 Advice on Group Supervision is that:

- Under CRM, the ultimate parent should perform the Group ORSA and the subsidiaries' ORSAs at the same time and produce a single document covering all the assessments.
- In the absence of CRM the ultimate parent should
 - develop an appropriate ORSA process at group level; and
 - undertake at the GROUP ORSA.

It is also possible to have one document covering the assessment on solo and group level.



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Role of the Actuary in ORSA

- Formal roles of the appointed actuary and signing actuary will no longer exist.
- Actuarial Function:
 - Technically no formal requirement for “actuaries” although the term “actuarial” is prominent throughout the directive.
- Clear fit between the role of the actuarial function and the “actuary”.



Role of the Actuary in ORSA

- Article 48 sets out role of the Actuarial Function as
 - Coordinate calculation of Technical Provisions (and associated tasks).
 - express an opinion on the overall underwriting policy.
 - express an opinion on the adequacy of reinsurance arrangements.
 - contribute to the risk-management system, in particular with respect to
 - the calculation of the SCR.
 - the ORSA.



Role of the Actuary in ORSA

Clear technical roles in

- Projections for the Capital Plan.
- Calibration and maintenance of the Internal model.
- Application of the Standard Formula.
- The statistical analysis for
 - Standard Formula USP's; and
 - Internal Model parameters.



Role of the Actuary in ORSA

Wider role in risk management generally, e.g.

- quantitative understanding and communication of risks;
- Reinsurance and risk-mitigation;
- Asset Liability management
 - e.g. with profits business / embedded options.



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ORSA Contents

- Actuaries tend to gravitate towards Pillar I (quantitative aspects) of Solvency II.
- Equally important and a key aspect of ORSA are
 - Pillar II: Supervisory review / Internal Controls
 - Pillar III: Disclosure



ORSA Contents

THEME	MAIN PILLAR
Governance	II
Risk Management	II
Underwriting	I
Investment	II
Technical Provisions	I
Solvency	I
Additional & External Risks	II
Supervision/Reporting	III



ORSA Contents - Governance

System of Governance

- Review system of governance taking into account the company's specific risk profile.
- Update documentation of structure, strategy and objectives.



ORSA Contents – Risk Management

Risk Management Framework and Risk Management Policy

- Independently (internal or external) assess the Risk Management Framework and Policy, including the procedures for the conduct of the ORSA.



ORSA Contents – Risk Management

Risk Identification and Assessment

- Formal process for existing and emerging Risks
- Qualitative and quantitative assessment

Risk Tolerance

- Review risk limits at a risk category level
- Review processes to ensure that the company behaves within the stated risk tolerance
- Review stated risk appetite



ORSA Contents – Underwriting

Underwriting Policy

- Evaluate overall underwriting policy including:
 - Claims Experience
 - Expenses
 - Business Volumes
 - Policy Wordings / Risk Mitigation
 - Consideration of any additional local legislative requirements for Life or Non-Life Insurance contracts [e.g. Life PRE in Ireland].



ORSA Contents – Underwriting

Reinsurance Policy

- Overall Reinsurance Strategy
 - Types of Cover
 - Treaty / Facultative
 - Limits
 - Cost
 - Processes
- Security of Counterparties
- Reinsurance by Line of Business



ORSA Contents – Investment

Investment Policy

- Asset Classes / Limits / Diversification
- Matching
- Derivatives
- Security of Counterparties
- Links with underwriting, reserving and reinsurance risks
- Processes
- Breaches



ORSA Contents – Technical Provisions

Technical Provisions

- Evaluate Reliability and Adequacy of Technical Provisions
 - Data
 - Techniques Applied
 - Simplifications
 - Assumptions



ORSA Contents – Solvency

Solvency

- Current Solvency Position
- Capital Plan
- Continuous Compliance with SCR
- Assess Risk Profile
 - Assess specifics for Internal Model or Standard Model



ORSA Contents – Additional & External Risks

Non-SCR Risks

- Assess “non-SCR” Risks and how they are considered and quantified, e.g. (not exhaustive!)
 - Liquidity risks,
 - Resourcing and skill-base risk,
 - Economic cycles,
 - Reputational risks,
 - Contagion Risks,
 - Legal and Political risks,
 - Social and Technological changes.



ORSA Contents – Supervisory

Supervisory Issues

- Review ORSA Submission Process
- Review Breaches of Process
- Review engagement with supervisors



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Conclusion –

- ORSA is a fundamental part of Solvency II.
 - ORSA is really a codification of risk management best practice for insurers.
- Actuaries have a key role to play in the ORSA.
 - But...ORSA can't just be “left to the actuaries”.



Conclusion – Next steps for you as actuaries

- Get up to speed with what the ORSA is.
- Watch out for level 3 measures and Groupe Consultatif's ideas early next year.
- Understand how your organisation will implement the ORSA.
- Think about how your / your department's role will need to evolve over 2011/12 to be ready for the ORSA when SII goes live.



Discussion

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