

Institute of Risk Management

Solvency II Special Interest Group – Workshop 4

16th February 2010 9.30am-12pm, IRM Conference Room

‘The ORSA’

What does an ORSA look like?

How would an ORSA process operate?

How to gauge the level of detail to include in an ORSA report?

Setting the boundaries between Internal Model and ORSA?

Item	Details discussed and agreed
1	<p>Philip Whittingham took the chair. There were over 50 people in attendance. The speakers were introduced. He made some introductory remarks about the topic and the current lack of firm guidance on the ORSA and therefore the need for risk practitioners to develop best practice.</p>
2	<p>Jonathan Groves presented back the findings of the third SIG survey. 25% of SIG members responded. The key messages are presented on the website but summarised as follows:</p> <ul style="list-style-type: none">- The main application of the ORSA is anticipated around capital assessment and business planning- Other uses refer to risk appetite setting, risk governance process operation, scenario testing, and forward looking statements- The survey respondents were very frank and open. 47% report not having an ORSA or it being at a very early stage.- In fact 15% say they have an ORSA framework in place, and this was brought under question during the meeting- 49% of respondents reported not having a useable / used ORSA process, with 11% having a developed process that is not yet embedded.- The risk identification and assessment process remains an area of work, 33% report that this is undeveloped and 48% have a process that remains to be embedded in the business. <p>Jonathan comment that everyone had less time than anticipated given the lead time to establish and process and evidence it for submissions to regulators ahead of approval in October 2012, the real deadline for having an operational ORSA was nearer October 2011, which made it an agenda item for mid 2010.</p> <p>Jonathan finally encouraged all SIG members to take part in the 4th survey on the Operational Risk which is available for completion until</p>

	<p>15th March 2010 as per email sent to all members.</p> <p>Thanks to Ian Fraser again at the IRM for managing the online survey process.</p>
3.	<p><u>Jim Bichard, Partner, PwC (No Slides)</u></p> <ul style="list-style-type: none"> • There are two camps with clients he sees, <ol style="list-style-type: none"> (a) ‘Tweakers’ – those that fundamentally start from existing processes and adopt these to the needs of Solvency 2 (b) ‘Clean sheeters’ – those that take the opportunity to redesign the process and develop what they would like in the future <p>Both processes are valid, but having clarity of what the ORSA is for and how it will be used is important</p> • ORSA is not just a regulatory document but a tool to add value to business strategy on capital management. The ORSA is about a business process, not a document. • It should not be seen as a monitoring tool but rather an active management tool • Define who owns the ORSA – there is a preference to make it the CRO current but is this right? <ol style="list-style-type: none"> (a) CRO to own the process and have accountability for oversight and challenge (b) Entity Management to embrace the process and own / sign-off content – this would need a significant change in many organisations but is keep to the ‘use test’. • Questions to consider in setting up the ORSA Process <ol style="list-style-type: none"> 1. Frequency 2. Inputs 3. Is it aligned to the corporate calendar? 4. What is going to be in it? 5. How does output add value to decision making 6. What assumptions need to be considered in the ORSA 7. Consider the audience and Visibility – Internal and External <p>Answering these questions will make the process more real and will clarify the ORSA’s purpose and how it will be used.</p> • Key questions remain – how to project forward 3-5 years? • What will we do better as a result of an ORSA? Better discussion risk • ORSA needs to be useable in the context of generating a debate within senior management forums.
4.	<p><u>Rick Lester, Partner, Deloitte (No Slides)</u></p> <ul style="list-style-type: none"> • Rick expressed surprise that from the survey anyone had an ORSA framework developed at this stage.

- Purpose – Communicating Risk/Capital & Solvency both now and in the future. Everyone needs to focus more on the ‘Communication’ element and less on documentation.
- Communication is will all stakeholders, not just internal management, but also externally – regulators, rating agencies, analysts. A good ORSA gives competitive advantage by making the organisation more able and confident to communicate its approach to risk and capital. When defining the detail (content) , consider Internal and External audience,
- Responsibility of its content is with the Board (It should consider all risks to the business)
- The ORSA must be well documented. Two stages – the process and the output
- The ORSA needs to be approved internally but also independently validated (by internal audit or external advisers/auditors).
- The ORSA needs to be used on a continuous basis – this means it needs to be able to be repeated as a process and embedded into management reporting
- The output should answer three Key Questions:
 - Is our Current Capitalisation adequate?
 - Is our Future capitalisation adequate?, and
 - Risk Appetite: Compare actual risk against risk appetite to give assurance that working within appetite(s)
- elements of capital modelling to consider are:
 - Balance Sheet → Representation of assets and Liabilities
 - P&L → Economic Profit vs. Expected profits, explain reason for variance.
 - Capital at risk
 - Cash Flow → Projections vs. risk appetite
 - Evidence of Scenario Analysis testing extreme events on balance sheet
 - Classify Risk Capital → Consider pre, post and projected capital valuations
- Include the organisational context
- Think about the “use test” process and RMF and use those expected objectives as inputs into developing the ORSA.
- Define Roles and Responsibilities of the ORSA process and content
 - ORSA needs to be in place at entity level (and potentially at Group. Hence needs to be embedded and owned at entity level.
 - Define who owns the ORSA (CRO or CEO?)
 - Ownership may change between the implementation phase and ‘Business as Usual’ to demonstrate use and embedding.
 - Consider the dependencies of the ORSA content from other departments – the data feeds are complex and will take time to establish
 - Some business processes only happen once per year, so if

	<p>you want to make the links you might need to do it during 2010</p> <ul style="list-style-type: none"> • Implications of where MCR + SCR + Internal Model is used. • For each ORSA build a robust review and signoff. <ul style="list-style-type: none"> ○ Data quality is an issue for sign off and confirming accuracy ○ What about back testing of data and assumptions? ○ Don't under-estimate the systems and technology implications ○ Self-certification may be needed, how will this work? ○ Where does independent validation fit in to the approval and review process? • Think of how the Validation process of the ORSA will be applied → internal Audit → Data integrity • Embedding means communication, awareness and training. This takes time and commitment. Start early.
5.	<p>Michael Crawford, Associate Partner, Financial Risk Management, KPMG (No Slides)</p> <ul style="list-style-type: none"> • Define the business requirements on what the business want in the ORSA rather than just the regulation requirements • Clearly articulate the VALUE PROPOSITION – what does the ORSA do for management – How it will it be used and what Benefits will it provide. • Consider: <ul style="list-style-type: none"> ○ The transparency of this info to the markets, ○ its impact on share price and market confidence during market downturns. The ORSA might be 'value sustaining' tool for communication with stakeholders. ○ How will the ORSA add value during periods of shock. What shock management information is required? Reflect on 2005 cat loss season. Those companies who could clearly and quickly express their exposures were rewarded in terms of share price and sentiment. • Group vs. Entity considerations <ul style="list-style-type: none"> ○ One ORSA or 6 – will the entity ORSAs aggregate in the Group ORSA or will group have a solo ORSA? (EU companies plan to have one ORSA at Group level) • Don't focus on manipulating the ICAP and ICA reports to make the ORSA but rather focus on what the Business want to see in the ORSA to make it meaningful to business control and planning – start with the 'end state' of where you want to be first. • Be clear on the primary purpose of the ORSA in your organisation: <ul style="list-style-type: none"> ○ Performance Management? ○ Monitoring? ○ Reporting? ○ Is it just good strategic planning?

	<ul style="list-style-type: none"> • Define a scope of sophistication (Don't over complicate it – think of the granularity that different elements of the business need from the ORSA) • Understand the Use Test and that will give guidance in what should be included in the ORSA • Consider timings of the ORSA process against the business plan – monthly, qtrly, Hlf year, annually and regulator deadlines • Don't create a large complicated process – what is needed? • Keep it practical • Look to systemise the current process so that is easier to embed.
6.	<p>Questions & Answers:</p> <ul style="list-style-type: none"> • There is no clear definition of how far in the future the ORSA should project the solvency of the business. – Businesses should set their own timelines for now. Nothing is prescriptive around 3 or 5 years, but what is reasonable? <ol style="list-style-type: none"> 1. Recognise it is not possible to evaluate impact of all variable over a prolonged period 2. Focus on the major issues 3. This will overlap with strategic planning 4. This is what the rating agencies do – so help them get the right messages by being proactive. • The output from internal models will be vital to the input of the ORSA so its worth making sure the internal model is well documented and understanding how it works is vital to understand the meaning of its output. • Sign off and communication to stakeholders: need to create summaries that CEOs and Boards can engage with and challenge. So needs to be simple, agile and summarised. But also enable drill down and challenge, <ul style="list-style-type: none"> ○ Work from what executives want to see, but shaping a strawman ○ Embed in normal MI reporting ○ Needs to be forward looking ○ Recognise this will take time and need to start consultation and building strawman soon • Use Test Validation expectations <ul style="list-style-type: none"> ○ Audit expects to see typical behavioural aspects in day to day activities, not just evidence that a process has been implemented (compare Goldman Sachs to Morgan Stanley – one is focus on behaviours, the other on process). Process alone will never lead to embedding. ○ To start, focus on the strategic decisions if time is short to role out across the business • MI needs to be forward looking and not just reporting on historic events • Captives (a grey area) <ul style="list-style-type: none"> ○ Many captive owners are trying to ignore the problem

	<p>currently</p> <ul style="list-style-type: none"> ○ The proportionality argument can be used here ○ It is predicted that a lot of captives will use the SCR ○ Captives are generally well capitalised so this may not be a problem ○ There may be some re-domiciliation to outside the EU <ul style="list-style-type: none"> ● Documentation - Don't over document the process and its content. If the process is in place, the evidence will speak for itself <ul style="list-style-type: none"> ○ Less is more often ○ If there is confidence in underlying processes, documentation can be cut back ● M&A: The ORSA process and its content should consider the implications of M&A <p>Analysts and Markets</p> <ul style="list-style-type: none"> ● Sell-side analysts are putting out negative messaging on Solvency 2 across the insurance sector. This could depress investment and share prices. Companies are not communicating enough and selling their strategy for Solvency 2. ● This is ironic – as Solvency 2 is clearly the type of regulatory 3-year forward looking risk that an ORSA should be picking up and addressing! ● If you have a good story, then tell people ● ORSA's may help inform strategic decisions about diversification of business portfolios and creation of nature hedges. Explaining this to analysts would be a valuable disclosure and communication process. ● This is important – if you have a large cat loss, where do you expect to re-capitalise from and do the analysts and investors support you and believe you are credible? ● It seems analysts are already doing these calculations in the city to gauge insurers impact. Is it worth reading such reports to gauge their approach?
7.	Phil Whittingham thanked the speakers for their contribution and the audience for their participation in a very instructive discussion.
8.	Alex Hindson reiterated that non-members of the SIG who had attended 2 meetings would be actively approached to join and we encouraged them to do so. Please pass on information about the SIG to colleagues and contacts.
9..	Next meeting – 17 th February 2010, 9.30am to 12noon at IRM Offices. A dial in facility will be provided as before Book early to attend as spaces are limited to about 60 (The IRM has acquired more chairs) but there are already about 50 signed up.

	Please complete the survey questionnaire developed on Operational Risk and available on the webpage.
10.	<p>Future meetings</p> <p>April (at the Forum) – Can actuaries and risk professionals learn to love each other? YOU NEED TO BOOK A PLACE AT THE FORUM (FOR AT LEAST 1 DAY) TO ATTEND, Please contact Catherine Tasker at IRM or register online.</p> <p>May – Talent and Solvency 2</p> <p>June – Risk Appetite</p> <p>July – Date and speakers to be confirmed – “Stress Testing and Reverse Stress Testing – how to take the stress out of the process”.</p> <p>If you have any topics you want covered or speakers you would recommend please contact Phil Whittingham or Alex Hindson with your recommendations.</p> <p>Please book early by contacting Alex Hindson, as places under demand</p>

Minutes taken by Alex Hindson
With grateful help from Richard Hawkins
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