Alignment of Operational Risk and Insurance
The practitioner’s perspective

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30th April 2018
Introduction

• Practitioner’s observations

• 2015 IMIF paper “Operational risk modelling: common practices and future development”
  - The objective is to produce a useful business tool rather than just a means of calculating regulatory capital
  - Holding capital is rarely seen as the best mitigant for operational risk

• Experience: Gaining traction for operational risk capital assessment can be difficult
  - More knowledge from participants can sometimes be a bad thing
  - Focus attention on the benefits which are not primarily the capital inputs

• 2018 IMIF paper “Aligning Operational Risk and Insurance”
  - The alignment of Operational Risk and Insurance enhances the value from the operational risk modelling process
Aligning Operational Risk and Insurance

Enhancing value in operational risk capital assessment

• **Practitioner’s case study**

  • Incorporating scenario and loss data analysis with economic risk transfer
    - Enhances scenario details captured to enable testing of the insurance programme
    - Adds credibility to a process that relies heavily on expert judgement
    - Translates into something senior management team better understand (awareness)

  • Testing the existing insurance programme against operational scenario exercises
    - Does the insurance react in the way we would expect (different severities)?
    - Is the programme appropriate and consistent (central versus local purchase)?
    - Consistency with defined operational risk appetite and control testing

  • Greater confidence in capital inputs and better justification for quantum / movements
    - but still expert judgement (other risk dependencies)
• Practitioner’s opinion on conclusion

The benefits for firms from aligning operational risk and insurance ... include determining an optimal risk transfer strategy, demonstrating “use” of risk management processes and models, and taking insurance into account when estimating capital requirements for operational risk.