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COMPLIANCE & ETHICS FORUM FOR LIFE INSURERS

CEFLI ERM-ORSA Panel CEFLI Compliance & Ethics Symposium

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Agenda

- Emergence of ORSA
- Overview of the NAIC ORSA
- Potential implications for U.S. companies
- Implementing the ORSA



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Emergence of ORSA

Risk management and regulatory supervision are converging

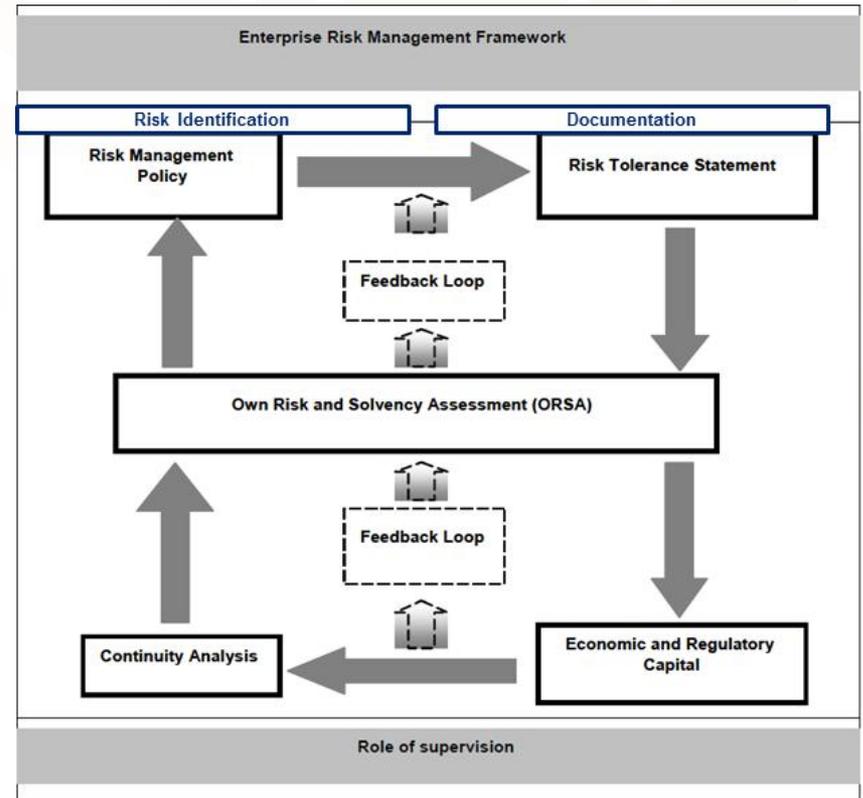
- While the insurance industry weathered the financial crisis relatively well, globally there is increased focus on ERM effectiveness
- Across the globe, effective risk management is becoming a cornerstone of current and emerging supervisory frameworks
- The Own Risk and Solvency Assessment (“ORSA”) is a defined process whereby an insurer will conduct its own formal evaluation of capital requirements based on the business risks being taken

Many factors are shaping risk management practices

- **Insurance Core Principles (ICP) of the International Association of Insurance Supervisors (IAIS)**
 - Provide a globally accepted framework for the supervision of the insurance sector
- **Supervisory requirements**
 - Evolving regimes requiring Own Risk Solvency Assessment (ORSA), capital management and risk based capital charges
- **Supervisory review process**
 - Risk based supervisory review process based on sound and prudent management of the business and assessment of risk management programs and system of governance
- **Rating agencies criteria**
 - ERM is one of the factors that many rating agencies take into consideration within the rating process

The ORSA is seen as central to a risk management framework

- **Insurance Core Principles of the International Association of Insurance Supervisors**
 - The Insurance Core Principles (ICPs) provide a globally accepted framework for the supervision of the insurance sector
- **ICP 16 Enterprise Risk Management**
 - **Statement:** “The supervisory regime establishes enterprise risk management requirements for solvency purposes that require insurers to address all relevant and material risks”
 - **Application:** This ICP applies to insurance legal entities and insurance Groups, including the risks that noninsurance entities pose to the first entities
 - **Enforceability:** This ICP does not prescribe a specific aspect of a solvency regime which is to be applied compulsorily by IAIS members
- **Nevertheless, the IAIS believes that good risk management practices and procedures need to be in place for a solvency regime to be effective**



Source: IAIS, adapted

Therefore, ORSA is becoming an international requirement



- The ORSA is a key element of the Solvency II framework currently being implemented in Europe
- Insurance Core Principle (ICP) 16 published by the International Association of Insurance Supervisors (IAIS) introduces the ORSA as part of the ERM framework
- Bermuda, Australia and Europe have all adopted ICP 16 and other ICPs (e.g., ICP 9 on supervisory review and reporting)
- Canada's OSFI Draft Guideline E19 proposes a Jan. 1, 2014 effective date for the Canadian ORSA, final version due Fall 2013

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Overview of NAIC ORSA

NAIC ORSA requirements in summary

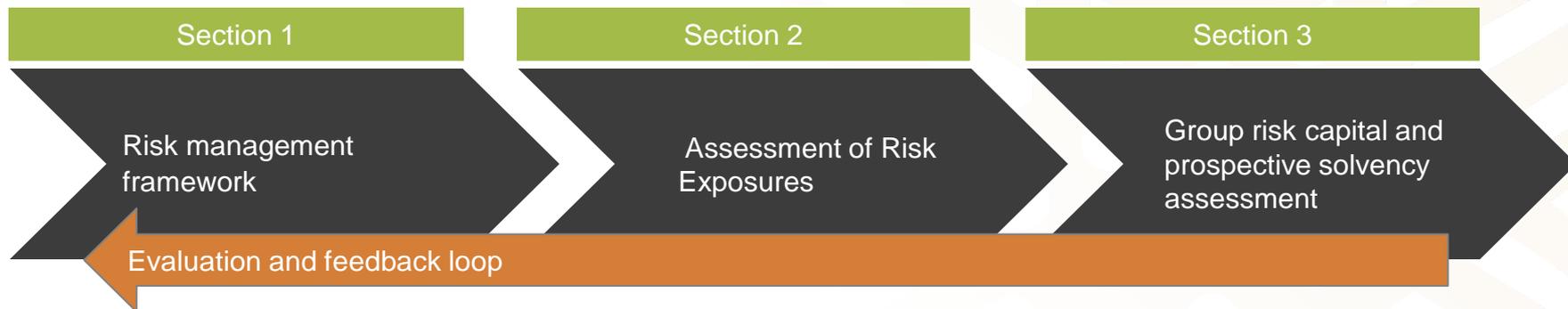
Definition of the ORSA	<ul style="list-style-type: none">• A confidential internal assessment of the significant and relevant risks:<ul style="list-style-type: none">- associated with the insurer's current business plan, and- the sufficiency of capital resources to support those risks• The assessment should be conducted by the insurer itself and should be appropriate to its nature, scale and complexity
Entities in scope	<ul style="list-style-type: none">• Individual insurers with annual direct written premium (plus unaffiliated assumed premium) more than \$500,000,000• Insurance groups with annual direct written premium (plus unaffiliated assumed premium) more than \$1,000,000,000
Requirements	<ul style="list-style-type: none">• Maintain a risk management framework• Regularly conduct an ORSA to assess the adequacy of its risk management and current, and likely future, solvency position• Internally document the process and results• Provide a high-level summary report upon the Commissioner's request no more than once each year• The date of filing will depend on the timing of the internal strategic planning process• This report shall include a signature of the insurer group CRO or other executive having responsibility for the oversight of the enterprise risk management (ERM) process
Effective date	<ul style="list-style-type: none">• Proposed effective date: January 1, 2015

NAIC ORSA proposed implementation timeline



- The NAIC conducted an “ORSA Feedback Pilot Project” for 13 undisclosed groups to voluntarily submit an ORSA Summary Report June 30, 2012, for regulatory review under confidentiality agreement. The NAIC is holding a second pilot this year
- The NAIC will start training the state financial examiners on ORSA in 2013
- Some states have been issuing communications urging insurers to address their ERM framework in preparation for the ORSA (e.g., Insurance Circular Letter No. 14, from December 19, 2011, issued by the New York State Department of Financial Services)
- In the case of companies whose statutory examination is coming up before 2015, they may be asked to answer questions on ERM and to establish whether they will be ORSA compliant by the proposed effective date of January 1, 2015

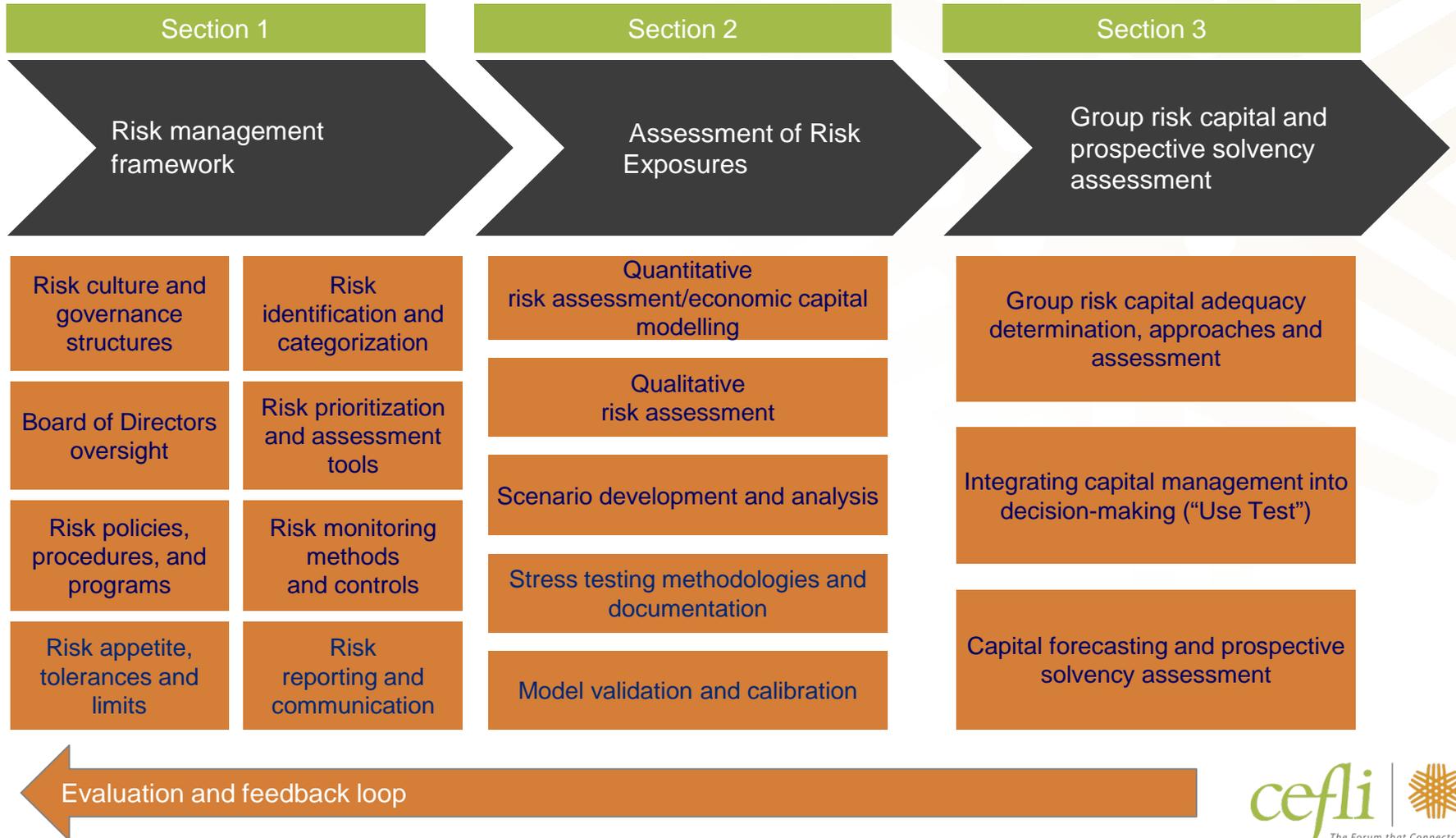
The NAIC ORSA summary report is structured in three sections



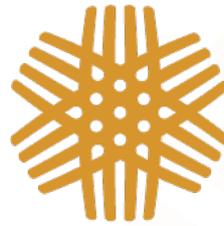
- Many insurers will already have implemented part of the elements that together comprise the ORSA, in varying degree of maturity
- The challenge posed by the ORSA is to improve each sub-process to the required maturity, and to bind the elements together into an overall process
 - Integrating into the decision-making process
 - Providing a common view of risk and capital management across the enterprise
 - Contributing to a continuous improvement of the risk management framework
- The requirements for each section can be segmented into distinct building blocks
 - across the different sections
 - including a feedback loop to use the ORSA results in improving the risk management framework

A “Building Block” view of ORSA components

- NAIC ORSA can be structured around segmented building blocks, each with its own principles.



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**Potential implications for
U.S. companies**

Key areas that could be affected by the ORSA process

Capital management	<ul style="list-style-type: none">• Determining approach for economic capital calculation and projection finding the proper balance between feasibility and accuracy• Group view on capital and solvency
ERM framework	<ul style="list-style-type: none">• Integrating several existing risk management processes into one consistent ORSA process, based on a common planning, maturity level, valuation basis, and assumption set• Strengthen Group and subsidiaries ERM and governance framework• Establishing a relevant link between the risk tolerance of subsidiaries' and Group
Strategy	<ul style="list-style-type: none">• Embedding the ORSA process into the strategic process• Aligning granularity, risk indicators and model parameters between strategic planning and risk modeling, to increase the relevance of the ORSA for decision making
Resources	<ul style="list-style-type: none">• Changing skill set for finance, actuarial and risk management• Having in place adequate processes, controls and risk quantification tools
Risk culture	<ul style="list-style-type: none">• Board ownership of the ORSA process, to prevent a 'silo-based' approach across entities and risk categories• Improve communication between different capabilities within the insurer• Managing business in accordance with risk appetite and risk tolerance levels
Technology	<ul style="list-style-type: none">• Developing robust systems and data environment to perform and analyze risk metrics in tight time frames

Discussions with insurers point to some challenges

Operationalizing the risk appetite	<ul style="list-style-type: none">• Linkage to strategic planning, tolerances and limits and monitoring
Scope of the ORSA	<ul style="list-style-type: none">• Legal entity versus Group ORSA• Overlap and alignment with various jurisdictions
Governance and the Role of the Board	<ul style="list-style-type: none">• The Board's ORSA awareness and ownership• Silo approach relying on inconsistent assumptions and underestimating the interactions between the different risks, within each entity and within the Group
Linking risk management/ORSA with strategic decision making	<ul style="list-style-type: none">• Taking the ORSA into account on an ongoing basis in strategic decisions
Creating a positive risk culture	<ul style="list-style-type: none">• Management objectives linked to risk management objectives
Modeling, Projections and Forward Looking Risk Management	<ul style="list-style-type: none">• Integrating the risk and strategic planning processes with forward looking projections and designing indicators so that management can take action• Having methods/models that comply with minimum quality requirements (e.g. validation standards)• Data quality and appropriate supporting infrastructure• Emerging risks and forward looking risk management and thinking

Perspectives from first NAIC ORSA Pilot*

- 13 participants
 - 8 provided what the NAIC considered to be complete submissions
 - 3 participants provided actual numerical figures
 - 2 subsidiaries of international groups
 - The length of the reports varied between 10 and 100 pages
- NAIC observed that the following components of the Reports were beneficial to the overall usefulness of the Reports, but these components are not necessarily required.
 - “Comparative view of up to three years of financial data provided in the report
 - Mapping of legal entities to business units described in the Report
 - Glossary of terms and acronyms that are not defined in the body of the Report
 - Detail of what the risk limits actually are to support the assertion that the Company has risk limits
 - Perform combined stress scenarios in addition to single stress scenarios
 - When using tables and graphs, provide an explanation of the table or graph for better understanding

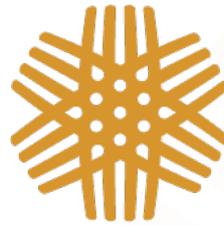
*Source: NAIC Summer National Meeting, Atlanta, GA, August 2012 & 2012 ORSA Feedback Pilot Project Observations of the ORSA (E) Subgroup

Perspectives from first NAIC ORSA Pilot* (cont.)

- Provide an explanation of how capital models are calculated and discuss the group capital analysis performed by the insurer/group
- If the insurer/group is international, the ORSA should include overall group capital in Section 3
- List of risk owners (i.e. department accountable for the risk)
- Explanation of how compensation and incentives are tied to risk management
- Include Heat Maps
- When using multiple capital models, create a graphical illustration to compare the different model results
- If the ORSA references other documents, make those documents available upon request
- Provide more stress testing on liquidity, especially for life insurance business, rather than a single focus on capital
- Provide an executive summary for large, complex ORSA reports
- Discuss emerging risks in the prospective risk section of the ORSA
- Identify risks associated with intercompany dependencies
- Include a discussion of information technology risk”

*Source: NAIC Summer National Meeting, Atlanta, GA, August 2012 & 2012 ORSA Feedback Pilot Project Observations of the ORSA (E) Subgroup

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Implementing the ORSA

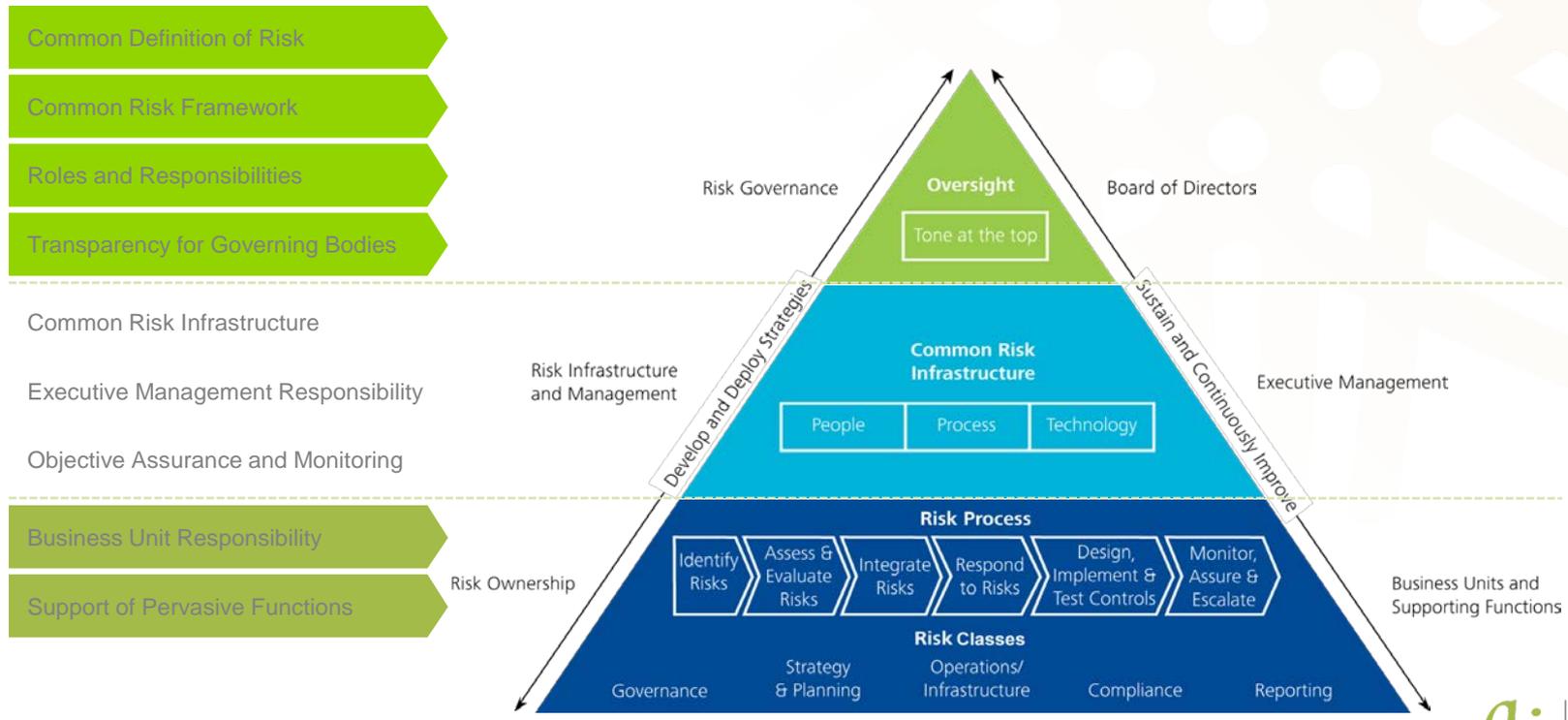
Getting started: Process for ORSA implementation



An effective ORSA is based on sound risk management fundamentals

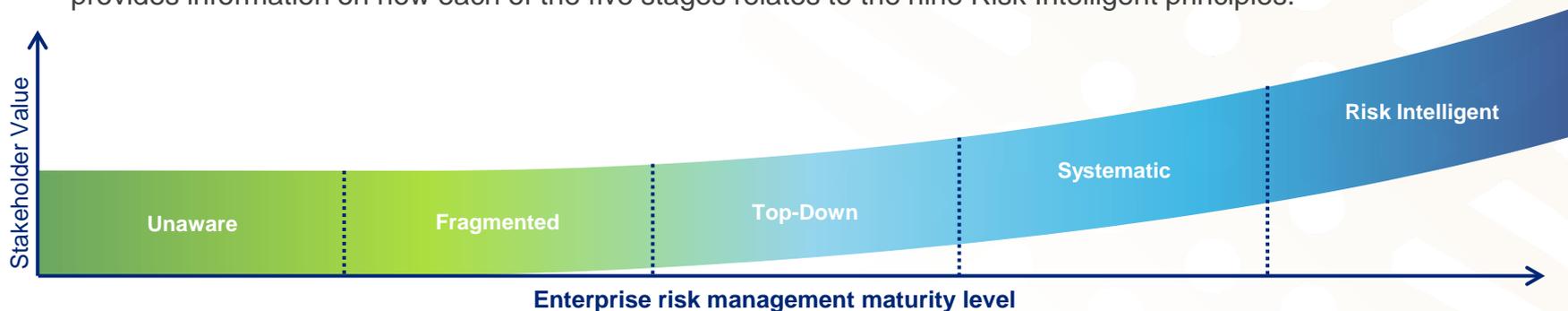
- Risk Intelligence(RI) is Deloitte’s risk management philosophy that is focused on maintaining the right balance between risk and reward. Simply put, organizations create value by taking risks and lose value by failing to manage them. An effective risk management program focuses simultaneously on value protection and value creation.

“Risk Intelligent Enterprise™:” Organizations with an advanced state of risk management capability, balancing value preservation with value creation



Today, Insurers are at various points in risk management maturity

- The Risk Intelligence Maturity Model can help companies identify where existing risk management capabilities may lie on a maturity continuum and determine how they can chart a roadmap to achieve a certain level of maturity. The model provides information on how each of the five stages relates to the nine Risk Intelligent principles.



With respect to the Risk Ownership principles and the processes used to support those, the Risk Intelligence Maturity Model describes the five stages as follows:

Unaware	Fragmented	Top-Down	Systematic	Risk Intelligent
<ul style="list-style-type: none"> Minimal participation of business units in ERM No identification of potential risk events Minimal tools, techniques, and capabilities Risk data is not adequately captured Risks are minimally reported Risk controls are poorly designed/ineffective 	<ul style="list-style-type: none"> Limited participation of business units Limited capability to identify potential risk events and establish responses Risk data is captured in silos Risks are reported inconsistently Risk controls are inadequate 	<ul style="list-style-type: none"> Selected business units are held accountable Major potential threats are identified Specific tools and techniques are used Data is captured to respond to risks Risks above established thresholds are reported to management Controls are adequate 	<ul style="list-style-type: none"> Appropriate business units oversee ERM Potential threats to the organization are identified Standardized tools and techniques are used Data is captured to identify, assess, and respond to risks Risks above established thresholds are reported to the board/management 	<ul style="list-style-type: none"> Appropriate business units are actively engaged in ERM Potential threats and opportunities are identified Tools and techniques are applied prospectively Data is captured to manage risk to within tolerances An early warning system is in place

The insights from the readiness assessment can be an accelerator for the next phases: Design and implementation of the ORSA

Phase 1: Readiness assessment

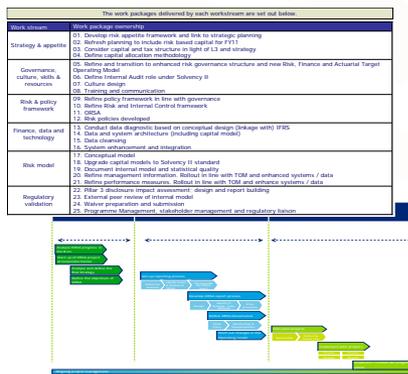
Phase 2: Design

Phase 3: Implementation

Building Block	Scoring	
Risk culture and governance	Orange	Light Blue
Risk prioritization process	Light Blue	Dark Green
Risk appetite statement	Orange	Light Blue
Risk monitoring and controls	Light Blue	Light Blue
Risk reporting and communication	Orange	Light Blue
Detailed risks descriptions	Light Blue	Dark Green
Risk assessment techniques	Dark Red	Light Blue
Risk tolerance statement	Dark Red	Light Blue
Management intervention plan	Orange	Light Blue
Assumptions and scenarios	Orange	Light Blue
Qualitative risk assessment	Orange	Light Blue
Quantitative risk assessment	Dark Red	Light Blue
Stress testing	Orange	Light Blue
Validation and assurance	Dark Red	Light Blue
Group risk capital assessment	Dark Red	Light Blue
Capital projection	Dark Red	Light Blue
Prospective solvency assessment	Dark Red	Light Blue



Action plan



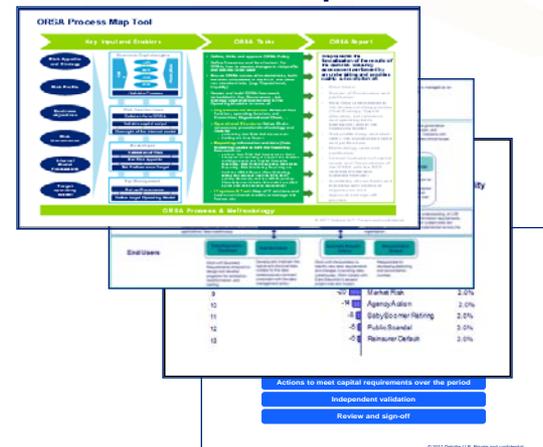
ORSA framework



Risk Management Toolkit:

- Risk intelligence map
- Risk heat map
- Failures Modes and Effects Analysis (FMEA)
- Event tree model
- Stress testing: IntEvaR™
- Risk appetite
- Crisis response strategy
- Risk catalog
- Risk reporting

ORSA templates



Questions and answers

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