



EIOPA-IRSG-12-03
08 February 2012

**OPINION of the EIOPA Insurance and
Reinsurance Stakeholder Group
regarding EIOPA Consultation on Own
Risk and Solvency Assessment**

(EIOPA-CP-11/008, 7 November 2011)

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Introduction and legal basis:

In November 2011, EIOPA initiated the public consultation on the guidelines on Own Risk and Solvency Assessment.

ORSA is an important element to improve the risk management of EU (re)insurers, to promote a better understanding of the company's overall solvency needs and capital allocation as well as the interrelation between risk and capital management. As a consequence ORSA should ensure better policyholder protection. Moreover, the presented requirements should guarantee that sufficient and clear information on a company's risk profile and capital position is provided to the administrative, management or supervisory body (AMSB) and is not misleading.

ORSA enhances the responsibility of the company's Board not to take on more risks than the capital base is allowing.

ORSA is a valuable tool for management purposes and therefore mixing it with regulatory requirements will dilute the value and overall effectiveness of ORSA to manage business planning against long term solvency needs. Any guidelines on the ORSA should therefore be principles based and avoid unnecessary prescription. The proportionality principle should be applied in the ORSA process to enable undertakings to properly identify and assess the risks they face in the short and long term and to which they are or could be exposed.

The Consultation Paper presents the draft Guidelines and Recommendations, explanatory text, and the analysis of the expected impact from the proposed policy is covered under the 'Impact Assessment' and includes the chronology and results of previous consultations.

This consultation follows the delivery of EIOPA's final advice for the implementing measures to the Commission in June 2010 and the fifth QIS exercise in March 2011. Since then, EIOPA has been preparing the final steps of the implementation of Solvency II in Europe. Under the Regulation establishing EIOPA, EIOPA has the power to issue guidelines and recommendations. The guidelines and recommendations are non-binding tools which should ensure the consistent, efficient and effective supervisory practices within the European System of Financial Supervisors as well as the common, uniform and consistent application of Union Law.

The EIOPA Insurance and Reinsurance Stakeholder Group competence to deliver an opinion towards EIOPA consultation on the guidelines on Own Risk and Solvency Assessment is based on Article 37 of EIOPA Regulation (1094/2010/EC).

General observations regarding EIOPA consultation on Own Risk and Solvency Assessment:

1. ORSA adds value to the transversal awareness on risks

We consider ORSA as an opportunity to reinforce the debate on risks across the company. For us it means non-quantifiable risks as well as quantifiable risks (4.28). At each level, from the insurance intermediary to top management, everyone has to be involved in enhancing a risk culture, while taking care of proportionality.

ORSA has to be set up so as to fit as closely as possible the characteristics of the respective undertaking. It means that the content of the ORSA in terms of qualitative and quantitative information must have a common basis which cannot be a one-size-fits-all process to reach them. In other terms, the company has to justify the method chosen to apply ORSA to the supervisor as well as to the internal stakeholders, even if, internally, ORSA is directed to the board. Given the importance of the relationship of ORSA and SCR, it would be helpful to clarify more the relationship and order of priority of qualitative requirements (which must be core for ORSA) and quantitative requirements (eg 3.23, 3.28, 4.19 - 4.21). However it's important to remark that ORSA is an undertaking driven initiative for management purposes, it is not a supervisory tool and should not be altered for supervisory purposes.

The SCR is calculated over a one year time horizon whereas ORSA will also look into the longer term business planning time horizon and therefore the longer term view of the ORSA should not serve to calculate a regulatory capital requirement and impose capital add-ons

The guidelines on ORSA should state clearly that the MCR is the only requirement to be met "at all times".

What is crucial in ORSA, is the explanation on the way it had been internally proceeded to get to the goal pursued (as is already embedded in articles 3.17 a & b). An undertaking's business strategy will feed into the ORSA in terms of establishing the parameters for assessment. As such, the results will help the board to fulfil this strategy while balancing the risk profile and risk appetite of the undertaking.

We support that this analysis and this process in themselves have to be broadly shared, explained and disclosed among the stakeholders inside the company as well as for the benefit of the supervisor.

In terms of ORSA reporting, however, we believe that the ORSA report should capture an undertaking's underlying management processes and should not be overly engineered. ORSA reports are prepared for the AMSB, and subsequently shared with the supervisor.

To summarize, we consider ORSA as a sound and fruitful process if it is implemented in order to enhance a self-analysis of the company under the point of view of the risk, and with the involvement of the appropriate persons and functions.

2. Too prescriptive guidelines would raise concerns

In some cases, the guidelines and explanatory text go beyond the objectives of ORSA and provide a lot of details on the processes regarding the way to reach the goal, and appears to be too prescriptive.

The guidelines are a little bit too ambitious in many aspects. Although there is a formal distinction between users of the standard formula and users of an internal model, there is no real difference in practice: for users of internal models, a lot of the aspects specified in the guidelines are mapped in an internal model. For users of the standard formula on the other hand a lot of those things are "unknown territory". A simplified approach should be available for undertakings presenting lower risks.

3. Vocabulary on corporate governance should be clarified and aligned with the corporate governance framework at EU level

ORSA concerns risk management and Governance responsibilities.

ORSA is part of Solvency II and as such part of a regulatory approach, not corporate law.

In parallel, corporate governance and thus administrative, management or supervisory body (AMSB) responsibility as well as risk management and risk governance are discussed under the headings of corporate governance and company law equally at a European level.

Many terms are used in both the regulatory approach as well as the corporate approach. This leads to confusion which needs to be avoided for the users, i.e. the (re)insurers. For example, the term "risk profile", which appears repeatedly in the context of ORSA and Solvency II, is used also in the Green Paper on the EU corporate governance framework (Green Paper 2011) – apart from being referred to also in Basel III/CRD IV as well as other documents concerning financial institutions. Ambiguities and misunderstandings must be avoided.

As a consequence it would be good if we had clear definitions as regards the various terms used in combination with "risk". We could review and suggest addition to the CEA Solvency II Glossary.

With regards to the role of the administrative, management and supervisory body (top-down approach), the undertaking should ensure that its administrative, management or supervisory body takes an active part in the ORSA process by steering how the assessment is to be performed and challenging its results, with the support of the risk management function.

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Specific observations regarding EIOPA draft Advice:

Detailed comments regarding EIOPA draft guidelines on Own Risk and Solvency Assessment are provided in the comment template attached below.

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Adopted by the EIOPA Insurance and Reinsurance Stakeholder Group at Frankfurt am Main, 08 February 2012.

The Chairperson of the EIOPA Insurance and Reinsurance Stakeholder Group
Michaela KOLLER

EIOPA INSURANCE AND REINSURANCE STAKEHOLDER GROUP – OPINION

CONSULTATION – OWN RISK AND SOLVENCY ASSESSMENT – FEBRUARY 2012

Comments Template on CP8 -Draft proposal for Guidelines on ORSA		Deadline 20 January 2012 12:00 CET
Name of Company:		
Disclosure comments:	of Please indicate if your comments should be treated as confidential:	Confidential/Public
<p>Please follow the following instructions for filling in the template:</p> <ul style="list-style-type: none"> ⇒ <u>Do not change the numbering</u> in the column “reference”; if you change numbering, your comment cannot be processed by our IT tool ⇒ Leave the last column <u>empty</u>. ⇒ Please fill in your comment in the relevant row. If you have <u>no comment</u> on a paragraph or a cell, keep the row <u>empty</u>. ⇒ Our IT tool does not allow processing of comments which do not refer to the specific numbers below. <p>Please send the completed template, in Word Format, to cp008@eiopa.europa.eu. Our IT tool does not allow processing of any other formats.</p> <p>The numbering of the paragraphs refers to Consultation Paper 008.</p>		
Reference	Comment	
3.6.	This introductory guideline should precise that the AMSB’s involvement in the ORSA process needs clarification, taking into account the introduction of new Recital 44 a CRD IV by ECON	
3.14.	With the agreement of the local supervisor, it should be possible to perform an ORSA at an intermediate aggregation level when some local entities are not differentiated in terms of management and operate in the same country. Indeed, in such situations, performing the ORSA for each entity seems pointless as the entities are managed at a global level. However, ORSA should provide quantitative and qualitative information for each legal entity (no sub-group view).	

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3.16.	We agree that the role of the AMSB is to perform and challenge the results of ORSA, also including the emerging results.	
3.17.	Is it really requested by Article 45 para 2 Solvency II to have an internal report as well as a supervisory report? 4.16 seems to suggest, that only one report is produced covering internal purposes as well as supervisory needs. ORSA is a valuable tool for management purposes and reporting of ORSA results should reflect this. Undertakings should have flexibility to determine whether the internal report would also serve supervisory needs. It is important that the ORSA process is not made too burdensome and costly for smaller undertakings and one report would be a proportionate approach.	
3.18.	We consider that the point c), information on “(ii) data quality requirements” should be suppressed as data quality issues are already adequately dealt in the Solvency II framework	
3.19.	This general rule regarding the documentation does not add any value compared to Guideline 3 and the explanatory text of the Guideline 5 is too prescriptive. Therefore, we suggest to delete Guideline 5.	
3.20.	We agree with this guideline and we consider that the emphasis should be on the implications for business policies.	
3.23.	3.22 and 3.23 highlight quantitative terms. Article 45 para 7 Solvency II states in absolute clear terms that ORSA does not serve to calculate a capital requirement. Accordingly, it would seem appropriate for the guidelines to emphasize that any ORSA figure will not replace the SCR calculation and that there will not be any automatic capital add-ons.	
3.25.	We agree that an insurer should do forward-looking analyses to demonstrate its ability to manage risk over the longer term. To provide a very detailed breakdown per year of the business planning period would be however very burdensome and it should be clear that a simplified forward looking projection, is acceptable. Including for example a qualitative assessment highlighting multi-year tendencies and developments	
3.27.	New wording proposal :	

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	As part of the ORSA process the undertaking should ensure that the actuarial function provides input concerning the capacity continuously to comply with the requirements regarding the calculation of technical provisions	
3.28.	New wording proposal : The undertaking may assess deviations between its risk profile and the profile set underlying the SCR standard formula calculation on a qualitative basis. If this assessment indicates that the undertaking’s risk profile deviates materially from the profile set underlying the SCR calculation the undertaking should quantify the approximate significance of the deviation.	
3.30.	Delete reference to higher frequency review: the possible need for higher frequency is dealt in Guideline 4 on ORSA Policy.	
3.33.	Paragraph 3.32 requires the Group ORSA to be in the same language as the Group RSR. This paragraph elaborates that the group may be required to provide translations into local languages. This may undermine the benefits of performing a group ORSA. Translations should be limited to situations where the group supervisor must work specifically with that local supervisor with regards to the solvency situation of the group.	
3.40.	This guideline should be aligned with the guidance provided on the group SCR. For example, if the deduction & aggregation method is used for parts of the group, several of the assessments are not relevant. If the third country regime is considered to be equivalent there should be no need to state the consequences of applying local capital requirements and technical provisions calculations. Otherwise it could be interpreted that the equivalence decision has been contested. Therefore we would add at the end of the paragraph: "this requirement does not apply to undertakings whose country regime is considered to be equivalent".	

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4.3.	<p>Given the procyclical design of standard formula (for example mass lapse risk), it will be impossible to ensure that the SCR will be met “at all times”, as indicated in this guideline. There’ll always be a stressed scenario where , if it happens, the SCR will be broken. These guidelines should say “ensure with a sufficient probability...”. To improve the awareness of the AMSB, an analysis of scenario breaching the SCR should be provided in ORSA.</p> <p>When analyzing a stress scenario, undertaking should be allowed to take into account EIOPA’s action to allow a countercyclical premium. And the guidelines should recognize that during a major financial crisis, MCR is the only requirement to be met at all times.</p>	
4.5.	The second sentence is unclear and also seems superfluous. Therefore, it should be deleted.	
4.8.	Add: "...with the support of the risk management function..." to be brought in line with EU thinking regarding stepping up the profile of the risk management function and corresponds to practical need.	
4.10.	Second sentence: The AMSB can in some cases not [and need not always] give instructions to management. Better wording: "It also challenges the management on actions..." (instead of “gives instructions”).	
4.14.	e) Solvency II is designed on a one-year-period time frame. A demand for a multi-year-period time frame based on the planning period seems to be very onerous. Guidelines should explicitly give allowance for simplified estimation methods, such as projecting the SCR for future period and the use of scaling factors.	
4.16.	We do not understand this statement as the ORSA report provided to the Supervisor must be consistent with the ORSA internal report approved by the AMSB. It can not be additional to the internal report.	
4.21.	<p>There is no further assessment if the planned risk mitigation techniques are realistic . The explanation of the undertaking must focus more on efficiency, applicability of risk mitigation tools.</p> <p>Furthermore this is already subject to the Supervisory review process and the activities of the</p>	

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	actuarial function. This should not be duplicated in this process.	
4.25.	In this section (as well as in many other sections) the impression is that users of the standard formula are confronted with the demand to introduce a "quasi" internal model by the "backdoor" of ORSA guidelines. If Solvency II allows the use of a standard formula for SMEs than there should not be too much effort for SMEs to prove the adequacy of this formula.	
4.28.	Following completion of an ORSA, the undertaking should be able to provide an assessment of, and differentiate between, material and immaterial risks. While we agree that all risks should be covered by ORSA, there are certain risks which are handled more appropriately in a qualitative way. It should be clarified in this paragraph that a “pure qualitative assessment” is also acceptable. Suggested text: “It could be “pure” quantification based on quantitative methodologies or an estimated value, or range of values, based on assumptions or scenarios, or more or less judgemental <u>or purely qualitative</u> . It is however required that the undertaking demonstrates the rationale for the assessment.”	
4.31.	We suggest to precise the point b) to include here insurance frauds and operational risks	
4.34.	It is unclear to us whether the text in this paragraph implies that entities in a winding up situation do not have specific requirements for ORSA. With regards to reconciliation requirements, please refer to paragraph 3.25 for comments on the use of qualitative assessments. We propose to change the last sentence as follows, “these projections, <u>if required</u> , are to feed...”. This provides consistency with the previous sentence, which suggests that the projections “may be required” rather than that they will be required.	
4.35.	Only significant changes and new business plans with a significant impact on the risk profile should need to be reflected (cf. references to Article 102 (1) subparagraph 4 in 4.40, 4.49 and 4.62).	
4.38.	It is unclear what the relationship is between required stress tests, reverse stress test, sensitivity analysis, scenario analysis and the ORSA process (regular / non regular). Undertakings should have flexibility to decide whether stress tests or scenario analyses are	

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	necessary given their risk profile. Suggested text: “<u>undertakings should carry out any of the following...</u>”	
4.39.	This seems to be very onerous for users of the standard formula It is unlikely that smaller undertakings will use internal models and the proportionality principle must be considered.	
4.40.	While reference to Article 102 (1) subparagraph 4 in the last sentence is not wrong, this reference would be more appropriate under Guideline 13 and could be added at the end of 4.49.	
4.49.	Add reference to Article 102 (1) subparagraph 4 at the end by way of shifting the last sentence of 4.40 to this place: "A full calculation is in any case required if the risk profile changes significantly according to Article 102 (1) subparagraph 4."	
4.50.	It seems to be absolutely necessary to support users of the standard formula in carrying out 4.49, as far as it does not imply to justify the use of the standard formula.	
4.51.	A lot of users of the standard formula do not understand the mathematical framework in its whole complexity. They will face very significant challenges to carry out all these estimations.	
4.62.	Add at the end: "A full calculation is in any case required if the risk profile changes significantly according to Article 102 (1) subparagraph 4." – this sentence was taken from 4.40 and added to 4.49 and here.	
4.75.	Does the first sentence intend to make reference to Article 102 (1) subparagraph 4? In any event, the term "non-regular ORSA", if maintained, should be highlighted better as an important definition (e.g. in 3.14).	
4.85.	The translation obligations under Guideline 17 seem overly burdensome. In any event, an English version of the supervisory report should be sufficient; no ORSA report is necessary for subsidiaries outside of EEA – please clarify explicitly. Likewise, non-regulated entities need not provide solo ORSA reports; overall "solo ORSA" and not "single ORSA" unless the difference is explained – applies to all the guidelines.	
4.92.	It will be very challenging to allocate diversification effects at group level to each entity of the group.	

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	<p>It will also be challenging to carry out appropriate sensitivity analyses of diversification effects at group level, and group solvency, with respect to material changes of the group structure. The group ORSA process should focus on a qualitative assessment of these issues. The exact assessment/s should be determined by the undertaking.</p> <p>Suggested text: c) appropriate sensitivity analysis, stress and/or scenario analysis..”</p>	
5.45.	<p>Reference in sentence 2 "at all times" should be clarified, so as not to mean e.g. on a daily basis. Technical correction: "requires<u>s</u>".</p>	