

Integrating ORSA Requirements between Europe and the US

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2012 ERM Symposium
April 18-20, Washington D.C.

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NAIC ORSA Overview

- Governed by ORSA model act, currently released for public comment (until 5/11/12)
- Target date 1/1/2014
- Key part of NAIC Solvency Modernization Initiative
- Requires an annual ORSA for insurance companies and groups with premium in excess of \$ 500MM or \$ 1B respectively, or if unique circumstances exist
- An ORSA summary report has to be filed upon request

Building blocks of the ORSA summary report

Three major sections

- 1) Description of Risk Management Policy
 - Risk Governance (who is accountable?)
 - Risk Identification (what is being done to make sure risks are understood?)
 - Risk Appetite (what is the tolerance for taking risk?)
 - Risk Management and Controls (how does the company ensure that risk tolerances are not exceeded?)
 - Risk Reporting (how is risk information shared?)

- 2) Quantitative Assessment of risk exposures
 - Models used and governance thereof
 - Results in base and stresses environments

- 3) Group Economic Capital and prospective assessment
 - Economic capital for the Group
 - Assessment of capitalization to support strategic plan

NAIC ORSA – Key Observations

- No prescription of quantitative methods, standardized shocks, etc.
- Gives the Regulator the opportunity to see how companies approach risk differently. No one size fits all expectation.
- Provides insight from comparing and contrasting companies' approaches
- Provides transparency but does not strive for model consistency
 - Avoiding mass behavior through allowing a multitude of models
- Key step towards obtaining Solvency II equivalence for the US

Combining ORSA requirements for US and EU

- For a US sub, need to provide Solvency II ORSA to Group to satisfy Pillar 2 requirements
- At the same time US sub needs to fulfill NAIC ORSA requirements
- Should not produce two different ORSAs
 - Defeats the purpose of the ORSA
 - ORSA discloses how risk is managed in practice. This is independent of the audience
- BUT: This requires good coordination among regulators and open mindedness on methods used
 - Need to understand differences, advantages and limitations of different models
 - Important role of IAIS and college of supervisors
 - NAIC has shown it is sensitive to this issue

Some initial experiences

- Similarities between US and EU requirements for an ORSA provide a good starting point for a common ORSA
- Different models are used to evaluate risk and capitalization. This is already a reality for risk management teams that need to balance different indications out of different models. But it increases the complexity of a common ORSA.
- EU insurers that apply for internal model approval need to balance the requirements of the use test against the complexity of dealing with different models outside of Solvency II
 - Initial Group expectations on ORSA highly focused on internal model
 - Internal model, RBC, Rating agency and GAAP models all play a role in decision making

The role of an internal model in the different regulatory frameworks

US

- Insurance Group should have an internal model that provides an economic view on its businesses to manage its risks
- Internal model exists in addition to regulatory model(s)
- Should reflect the company's views on risk



Transparency Focus

**Can they still
be the same?**

EU

- Internal model is also used for regulatory purposes (if approved)
- Thus it will be a hybrid between the company's view on risk and regulatory requirements.
- Solvency II requirements lead to non-economic elements and conformity of models between different companies
- Use Test



Consistency Focus

Other questions and concerns

- Will the EU-headquartered Group be required to file the entire Group ORSA report with the US state commissioners?
 - Holding Company Model act provides legal basis
 - Any footprint in the US brings the entire Group into reach of US insurance supervision
 - Goes well beyond the concept of Group Supervision within Solvency II
 - Submitting a combined Group report may not give the US regulator a good picture of the US insurance operations
- How does ORSA report relate to Holding Company Model act Enterprise Risk report?
- Filing with multiple states? Individual ORSA reports by legal entity? Are US Subgroups possible?
- Confidentiality of information delivered in ORSA report
 - ORSA report provides key insights in risk management practices and business strategies

How will this information be used?

- **Regulator Complies Across Organizations:**
 - Identified Risks
 - Risk Measurement Tools
 - Corporate Risk Budgets and Corporate track record of deviating from them
 - Focus/method for creating value
- How will regulators decide how to spend their time based on this information?
- What will trigger regulatory action?