JOINT RISK MANAGEMENT SECTION

Canadian Institute of Actuaries
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HOW TO REVIEW AN ORSA

Co-Sponsoring Organizations:

Reviewing a Summary ORSA Report: The Score Card Approach

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Introduction

This paper is in response to a call for papers on ORSA reporting review by the Joint (SOA/CAS/CIA) Risk Management section. The objective is to present an approach that allows regulators and other interested parties to compare ORSA summary reports across various insurance companies. ORSA has a broader scope than traditional risk management. It is both qualitative and quantitative in its mandate making it difficult to compare across organizations. It encompasses more than Solvency measures, Stress Testing and Risk Based capital adequacy. This paper focuses on development of a Score Card that will allow regulators, and other interested readers to benchmark and compare different insurers on a common platform.

Questions to be Asked

Any review of an ORSA summary report must begin with a series of questions. Starting with high level questions and then drilling down into more specific questions will provide a deeper understanding of the risk profile of the organization. Where answers are less than adequate, areas for improvement may be highlighted. In time expert judgment will allow more direct comparison across companies with similar and dissimilar profiles.

Does the Report Address all Risks

At the highest level, does the summary report address all current and potential risks faced by the organization? This is the primary question to be asked. All subsequent questions fall out of this basic consideration. The complexity of the organization including product lines, organizational structure and geographical locations will all drive the level of questioning that follows.

Risk Mitigation

How is the company addressing its' risk mitigation activities? Is it using reinsurance to reduce risk and need for capital? Is it addressing only current risks or future potential risks as well? Is it mono-line? Or multi-national? And is it reporting on just its' local domestic risk or across the board? Have some subsidiaries been excluded in the ORSA risk profile and summary report?

Does the company have access to adequate sources of capital should capital infusion be necessary if the risk profile changes?

Product Lines

What exposure does the company have to various product lines? Are some lines more risky than others? Is the mix of business changing over time? Is the company chasing more risky business? If so, is it seeing a commensurate increase in profits relative to other organizations with similar risk profiles? Does the company have plans for acquisition or divesture of certain product lines?

Stress-Testing

What are the results of the latest stress tests and have they been included in the summary report? Are there areas of weakness in the stress tests that still need to be addressed by management? How will the stress tests change going forward?

Determination of whether the stress tests are comprehensive enough may focus on backward-engineered scenarios and how the scenarios chosen score relative to other insurers or past scenario testing of the insurer.

Subjective Risk

Some risks by their very nature are hard to quantify and assess. Risks like reputation, market, foreign exchange and liquidity can be more open to subjectivity or simply ignored in the risk management process. How have the subjective and hard to quantify risks been addressed? Has the insurer provided written policies to address these risks? Or have they simply ignored them?

The Score Card

This paper proposes that a Score Card approach be used to assess the ORSA summary reports of various insurers. Underwriters assess an applicant for life or health insurance (ObamaCare aside) using a series of debits and credits to determine the risk of the applicant for insurance. A Score Card would take the same approach in providing a consistent and fair way to benchmark insurance company risk. By setting a pass target, a tally of the score at the end of the review tells whether the insurer has passed the threshold or not for the given reporting period.

The Score Card addresses the regulatory proclivity for comparability while still leaving the ownership of the risk process in the hands of the company. However, companies realizing they are being judged on a level benchmark across the industry will find motivation to score as high as possible in each of the sections. While a Score Card is not a new concept in risk assessment, applying it to ORSA summary reports provides a level benchmark for judging similar organizations.

The tasks apart from reading the summary report will be to score each section of the Score Card and thus paint a picture of the completeness of the ORSA report. It will also allow highlighting of any missing or under-represented risk profiles.

The Score Card becomes the criteria the reviewer uses to evaluate the amount of attention to devote to the exercise. Attention would also be given to areas where the Score Card points out weaknesses that need to be addressed.

The Score Card is the chassis that determines whether the ORSA report provides adequate insight into an insurer's ERM process and risk profile. The insurer would be expected to identify all key material risks and management's viewpoint in the report. Marks would be awarded for completeness compared to other similar insurers (mono-line/multi-line/international/Life/Health/Casualty). By scoring the summary report, it creates a framework for review and determination of what's missing. Reviewers would then be charged with the responsibility of alerting management to what's missing in the report so that future reports may be improved upon.

Regulatory reviewers would take the approach of scoring the ORSA summary report and providing recommendations on ways to improve scores or address risk concerns.

While the Score Card approach requires some amount of judgment, after a few years, the experience and ability of regulators and others to score items consistently should be improved. Also, regulators will be able to examine how the risk culture of the organization is changing over time. This may allow them to sound alarm bells when necessary. The Score Card and review will be a work in progress that will change and be refined over time.

The ASSESSED SCORE is the reviewer's own expert opinion on how the organization has addressed an individual risk. The MAXIMUM SCORE is the reviewer's estimate of how much weighting to provide to each category of risk. The Total line at the bottom adds each of the individual risks in each column. Individual reviewers may set their own acceptable pass rates on the quality and completeness of the summary report. There are too many potential risks to include them all in the table. The Allocated Capital if available, quantifies how much capital the organization has dedicated to each of the individual risks. If available, it allows the reviewer to compare to previous reports for trending from year to year. It also allows the reviewer to benchmark against other similar organizations. Finally, the COMMENTS/CONCERNS section provides discussion on areas of further review and exploration.

Example Score Card

The table below shows an example of what a Score Card may look like:

RISK	ASSESSED SCORE	MAXIMUM SCORE	ALLOCATED CAPITAL	COMMENTS CONCERNS
Business Risk	3	4	$10 million	PASS
Market Risk	7	9	$5 million	PASS
Geographical Risk	1	1	$2 million	PASS
Interest Rate	6	8	$20 million	FAIL
Risk Culture	4	4	$2 million	PASS
Ownership Risk	2	3	$2 million	PASS
Organizational	5	5	$3 million	PASS
Mono-line	N/A	N/A	N/A	N/A
Multi-Line	8	9	$20 million	PASS
Product Lines	10	12	$30 million	PASS
ORSA and ERM	2	2	$1 million	PASS
Risk Policies	5	5	$2 million	PASS
Underwriting	6	8	$6 million	PASS
Investment	3	4	$7 million	PASS
Claims	8	10	$12 million	FAIL
ALM	2	3	$15 million	PASS
Operations	4	5	$22 million	PASS
Reinsurance Counterparty	4	4	$4 million	PASS
Governance	1	1	$2 million	PASS
Risk Reporting	1	1	$1 million	PASS
Risk Compliance	1	1	$1 million	PASS
Risk Controls	2	3	$1 million	PASS
Foreign Jurisdiction	N/A	N/A	N/A	N/A
Credit Risk	1	1	$9 million	PASS
Liquidity Risk	2	3	$2 million	PASS
Assessment Methods	0	1	$1 million	Needs Improvement
Model Validation	1	1	$1 million	PASS
Model Calibration	1	1	$1 million	PASS
Double Gearing Capital	0	1	$1 million	Further Discussion
V-A-R, Tail VAR	7	7	$20 million	PASS
Probability of Ruin	6	7	$20 million	PASS
Stress Test Results	4	5	$20 million	PASS
Total	108	129	$243 million	PASS

Conclusion

This paper has proposed a potential approach to ORSA review and benchmarking. The paper cannot possibly cover every question a regulator or Board of Directors may want to ask about an organization's ORSA risk profile. Over time as the art of Score Carding improves, the science surrounding it may become more robust.

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