Solvency II

Own Risk and Solvency Assessment (ORSA) Feedback Document

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Gibraltar Financial Services Commission

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1. Introduction

We consider the Own Risk and Solvency Assessment ("ORSA") to be a key aspect of Solvency II ("SII"). The ORSA report is an important document allowing the communication of key business and risk features to the Board and the regulator. The ORSA process and report should demonstrate and evidence the Board's engagement in business planning, economic capital considerations and capital planning, risk management and risk appetite, stress testing, governance, and the overall review of a firm's business.

In 2015 we required that firms submit a report utilising the preparatory ORSA guidelines, under the title the Forward Looking Assessment of Own Risk ("FLAOR"). These reports were required to be completed and submitted to us for 31 December 2015, and we have collated this feedback document following their review. This document has been written to advance two objectives:

1. To communicate to the industry the minimum requirements and expectations of the ORSA process and reporting, in adherence to the requirements and guidelines of the SII Directive.

2. To give examples of good practice observed to date. These examples do not aim to be exhaustive, but may be used by firms as illustrative ways that can improve the ORSA process.

As we noted in our March 2016 Dear CEO letter ('Plan of supervisory engagement for 2016 under the Solvency II Directive', available on the SII section of the GFSC website), we will be using the ORSA process to facilitate our supervisory approach. We note that as part of our supervisory approach, each licensee receives a level of supervision that will include regular review of their business model, financial situation, and their risks. We expect that the ORSA process will develop to capture sufficient detail in these areas. It is also our expectation that the ORSA process will communicate sufficient granularity of information surrounding business planning. We include some greater detail of clarification of these areas within this document.

Over the course of 2016 we expect to see firms ORSA processes evolve further. Firms are expected to be implementing EIOPA's Final ORSA Guidelines, which are now in force and further reaching than the preparatory phase FLAOR Guidelines. We remind firms that all sets of Guidelines are now in force and available on the EIOPA website. For expediency, we use only the ORSA acronym in the rest of this report. For ease of reference we have included the ORSA Guidelines in Annex 1, and we refer to them in the main body of this report by Guideline (GL).

We remind firms that ORSA's are required to be produced at least annually and therefore the next ORSAs are required to be submitted to us by 31 December 2016. We encourage firms, however, to consider their internal timings of the ORSA process and would recommend that this coincides with the annual business planning process. We request that firms advise us of their proposed submission dates. Please see section 4.4 for further details.

2. Executive Summary of Feedback

We highlight the following areas of key feedback, which we consider relevant to all firms:

- **Demonstration of Board oversight and challenge** (Section 4.2)

  The majority of ORSA submissions did not sufficiently demonstrate or evidence Board involvement and oversight. We expect this evidence to be included as part of the ORSA.

- **Business Planning and its link to the Forward Looking Assessment** (Section 6)

  A good ORSA framework begins with the business plan, and it is the base projections of the business plan that underpin the forward looking assessment of solvency. Almost all firms could improve the level of business plan detail included within the ORSA. The assumptions of the business plan should be included at a level of detail to allow the future drivers of capital projections to be understood. These assumptions should be on a best estimate basis, with any stretch or target elements removed. We include some expectations on the level of detail needed for an informative business plan in section 6.1.

- **Breadth of risks considered** (Primarily Assessment of Overall Solvency Needs, Section 5)

  The assessment of risk should cover all business functions and all material income streams of the firm and where relevant the group. All material risks should be included, and not only those that are deemed to be quantifiable. In the majority of submissions we observed a focus on risks explicitly captured in the standard formula (underwriting, investment, and counterparty risks) at the omission of risks arising from operational aspects, outsourcing arrangements, other group activities (where relevant), liquidity, and conduct behaviour. We expect risks to be identified across all areas of the organisation, typically utilising the risk register, with the most material risks then assessed and stress tested in greater detail.

- **Clarity of Stress and Scenario Testing** (Section 5.4 and Reverse Stress Testing in 5.5)

  All firms could improve in this area. Some stress tests appeared to be arbitrarily derived and of insufficient severity to allow a robust assessment of solvency needs. We expect stress and scenario tests to be derived with clear reference to the specific characteristics of a firm's most material risks. They should allow an evaluation of a firm's position under a range of severe scenarios that are at the edge of plausibility, allowing an assessment at the 1-in-200 one-year time horizon of the SCR (or alternative economic capital risk measure). The details of the assumptions behind stress and scenario tests and the quantification of the result should be clearly set out.

- **Standard Formula Appropriateness** (Section 8)

  There was a limited level of detail of the assessment of deviations from the underlying assumptions of the SCR in the majority of submissions. We expect to see a qualitative assessment of the SCR on a risk by risk basis, and not only at an overall level. Where there are any significant deviations (due to over or under-calibration) these should then be quantified. Any material risks not included within the SCR should also be considered.

We also remind firms of our previous ORSA feedback, included as part of our Solvency II Self-Assessment Feedback paper of 6 May 2015 (see pages 12 to 13).

3. Structure and presentation of the ORSA report

A good structure and presentation of the ORSA report is vital to ensure that key risks and key messages are clearly articulated to the Board. We have observed the following examples of good practice:

- Key risks and main messages are clearly identified near the front of the report.
- Risks, tolerances and metrics, specific aspects of mitigation, and a classification of risk materiality are included in the form of a table (or other suitably succinct forms).
- Any future actions following the ORSA process are clearly stated (e.g. actions of strategic change or further analysis).
- Commentary is included alongside figures to ensure that the “so-what” element is always explained.
- Generic statements are not included in the report.
- Group and organisational structures (including the use of outsourcing) are clearly and succinctly set out, with the aid of diagrams, to give greater context to the process of risk identification and assessment.
- Business strategy is explained, and business plan detail is set out with figures and supporting charts.
- The balance sheet is set out with a detailed breakdown of invested assets, technical liabilities, and any other material items.
- Reinsurance strategy and details of the programme are clearly articulated.
- The SCR is presented by risk category, with supporting commentary on the key assumptions used.
- Related documents that add context to the ORSA (e.g. risk register, business plan documents, committee structures and policies) were submitted at the same time or included within appendices. Such documents were clearly sign-posted from the ORSA report. The movement of such information away from the main body of the report reduces its length, improving clarity.
- Where reports used acronyms, firm specific terms or technical terminology, a glossary was included.

We expand on some of these examples in the following sections of this report.

The remainder of this report follows a set of structured headings. Firms do not have to strictly follow this structure when producing their own reports, but they do have to ensure that all EIOPA GLs are adhered to.

4. ORSA Process

The ORSA is an ongoing process which should be actively driven by Board input, oversight, and challenge (see GL 2). We would like to see more evidence of the full ORSA cycle and evidence that the process is more than an isolated report for regulatory compliance. It is a process of risk identification, risk management, and capital assessment.

4.1. ORSA Policy

We expect the ORSA Policy document to be submitted to us alongside the ORSA report. We expect the Policy to give full details of the processes, procedures, and techniques utilised and the individuals (or committees, including their membership) involved. GL 4 sets out the minimum areas of inclusion for this Policy. We also expect to see evidence that the ORSA Policy has been approved by the Board.

There should be clear triggers setting out when an updated ORSA report is required to be produced. An ORSA report is required at least annually, but there should also be a policy of re-performing the ORSA on a more frequent basis in the event that there are significant changes in the risk profile or business plans[1]. Good policies have clearly set out what is considered a significant change and have defined a number of triggers using quantitative and qualitative metrics. This might include:

- Results deviating from business plan (e.g. volumes or loss ratios) by a certain percentage.
- A change of business plan, e.g. entering or exiting a material line of business.
- The SCR increasing or decreasing by a certain percentage.
- The SCR solvency cover falling below a pre-defined threshold.
- A large loss or series of large losses of a significant pre-defined size.

4.2. Documentation and evidence of the ORSA process

We expect that an 'ORSA record' (see GL 3 and 5) should be produced that evidences details of Board discussion and aspects of oversight and challenge. The ORSA record may be helpfully supported by minutes of these meetings. The majority of ORSA submissions reviewed did not contain adequate evidence.

In our May 2015 webinar to Non-Executive Directives (NEDs) (available on the Solvency II – Our Approach section of the GFSC website) it was stated that Boards and NEDs should see the ORSA as a top priority, ensuring oversight and input into aspects of risk and capital management and strategic planning. The importance of NED challenge was also emphasised, to the ORSA Policy, which determines how the ORSA is developed and implemented, and to the analysis and outputs of the process. This oversight and challenge has not been well evidenced to date.

ORSA reports reviewed often included an explanation of work carried out in the business across the Systems of Governance. These explanations, however, did not always indicate how the ORSA process and report had been utilised. We would expect the ORSA record to evidence how the ORSA process and results supports decision making across the business.

[1] Section 21(7) of the Financial Services (Insurance Companies) (Solvency II Directive) Act 2015 [Article 45(5) of the Solvency II Directive 2009/138/EC] requires that the ORSA report should be re-performed without delay following any significant change in risk profile.

The ORSA record should also evidence GL 6 (communication to all relevant staff of results and conclusions of the ORSA) and GL 13 (results and insights of the ORSA taking into account during the process of capital management, business planning, and product development). We expect these GLs to be fulfilled by presentation to and discussion at the Board and relevant committees.

4.3. Wider Systems of Governance

Good reports included clear summaries of the wider structure and processes of the SII Systems of Governance. This helps to fulfil GL 1, indicating how the ORSA process is tailored to fit into the organisational structure and risk-management system of the firm.

Explanations were helpfully supported by details of committee structures and their terms of references. This detail was better included in an Appendix to the main report and supported by the attachments of any relevant documents.

4.4. Timing of Submission

We required submission of reports by 31 December 2015. The next iteration is therefore required to be submitted no later than 31 December 2016 (GL 14 states that the ORSA shall be performed at least annually).

Some firms have noted the challenges of producing an ORSA report to this date, due to their year-end date or the timing of their internal processes. We will be accepting of a change in submission date where a firm is able to demonstrate that this fits better within their annual process. Firms should initially talk to their regulatory officer if they would like to change their submission date, and any change of date should be advised to us in writing. We note that a change in submission date will not waive the requirement for a report to be submitted at least annually.

Some ORSAs submitted at 31 December 2015 were based on 31 December 2014 figures. We found this to result in an overly retrospective view of the risk profile and solvency needs, particularly where it was not justified that the risk profile and SCR had remained constant over the intervening months. To ensure a more current view of risks, firms may consider a valuation date for the ORSA report which is different to the year-end date.

5. Assessment of overall solvency needs

The assessment of overall solvency needs is expected to be in-line with the business structure and strategy, and to follow from the identification of risks. Such an assessment should capture all business functions and note all material income streams of the group. It should also address the strategic decisions around outsourcing arrangements and the use of reinsurance.

We found the better ORSA documents to begin by setting out the structure and arrangements of the business, before a risk assessment that covered risks across all aspects of the organisation. For the material risks, mitigation was clearly stated, and those that are quantifiable in nature were stress tested. This analysis then informed a quantification of capital needs. We consider all these aspects as areas of minimum inclusion to address the GLs and refer to each one in turn in the following sub-sections.

5.1 Business / Group Structure

The inclusion of the business structure gives clear context for the assessment of overall solvency needs and is an important way for a user of the ORSA report to assess whether the risk assessment covers all aspects of the business. By a business structure we refer to the group structure with the addition of any key outsourcing arrangements, whether these are to entities inside or outside of the group.

We found the business structure to be most helpfully represented by way of a structure chart of group entities, with the addition of those further outsourced entities, and some supporting commentary to explain the nature of each entity and the relationships between them.

5.2. Risk Identification

Better reports clearly utilised the framework of the risk register. GL 7 states that all material risks should be addressed within the ORSA, and we understand the risk register to be the starting point for the identification of risks in the organisation.

We expect to see clear explanations of material risks and clear description of the mitigation in place. This mitigation will include qualitative aspects for all material risks (e.g. controls and further investigations) and it will include aspects of capital needs where the risk can be quantified. Where the risk is quantifiable the assessment may be supported by stress and scenario testing, which is discussed in section 5.4. We expect reports to articulate considerations around the choice of risks to stress test.

The risk register is an item that we expect to be updated at regular intervals, and so this should also ensure that emerging risks are captured within the ORSA process. In a number of instances, we found limited or no reference to emerging risks to the business, which we expect to improve in the next iteration of the ORSA report.

The ORSA report does not necessarily need to replicate the risk register or include all risks from the risk register. The focus should be on addressing the key/material risks. Where the risk register is not included in its entirety in the ORSA report we would expect it to be submitted as an attachment to the report.

In some cases, where the risk register was included, we identified anomalies in the risk assessment process. For example, key risks were included in the main report which were absent from the risk

register. In other cases some of the risks that were stress tested also did not appear in the risk register. We interpreted this to be evidence of poor processes and of a lack of ORSA use within the business.

We found some risk registers to be very generic in nature. We expect the risk register to specifically reference the key aspects of a firm's own business and risk profile. For example: for underwriting risk, the lines of business and aspects of pricing that are deemed to be most uncertain; and for market risk, the assets which may be subject to the most material fluctuations in market value.

5.3. Risk Appetite and Risk Exposure

Good ORSA reports extended their risk register to include statements on risk appetite and risk exposure, which were supported by qualitative considerations and quantitative metrics. The assessment of risk appetite and risk exposure enhances the assessment of the risk profile and informs the assessment of material risks. The risk appetite should be supported by risk tolerance metrics. For example, risk tolerance metrics might be linked to: the premium volumes written for specific risks, the exposure to an asset class or single reinsurer, the credit rating of invested assets and counterparties, the terms of agreement with key outsourcing partners, or the number of instances of specific operational risks occurring.

Better reports also gave consideration to the granularity of the risk appetite. For instance, insurance risk is often the largest risk, but business might be written across a range of products and distribution channels. In this instance one single broad risk appetite statement and exposure measure encompassing all of insurance risk is unlikely to facilitate a useful level of information for Board discussion and strategic decision making. There may instead be separate risk appetite statements and tolerance and exposure metrics for different products or distribution channels.

5.4. Stress and Scenario Testing

We expect to see improvements in stress and scenario testing through: the selection and breadth of risks tested, the severity and relevance of stress assumptions, and the presentation of results and findings. GL 7 states that, where appropriate, the identified material risks should be subject to a sufficiently wide range of stress tests or scenario analyses in order to provide an adequate basis for the assessment of the overall solvency needs. We observed that many firms did not include scenario testing within their ORSA report, which we expect to improve in the next iteration. We discuss scenario testing as a distinct form of stress testing below.

We considered there to be two broad forms of stress testing exhibited in reports:

1. Sensitivity testing of business plan assumptions (e.g. deviations in loss ratio or investment return). These aid an assessment of the viability and robustness of the business plan.
2. Stresses independently derived. These tended to be more severe stresses that offered an independent check (to the standard formula calibration) of the SCR.

There was a tendency for a number of firms to predominantly consider the first type. This is a useful exercise to inform strategic decisions around solvency cover and future solvency needs, and we would encourage insurers to continue including such stresses within their ORSA process, particularly within the forward looking assessment sections of the ORSA report. We did not always consider,

however, these types of stresses to allow a full consideration of solvency needs at the level of regulatory capital required by Solvency II. Furthermore, it often appeared that these stresses were arbitrarily derived. For example, loss ratios were stressed by 5% but there was no justification given as to why a 5% deviation was selected and most informative. We expect there to be justification for the severity of any stress considered.

We expect there to be an improvement in the use of the second type of stress tests. The Bank of International Settlements describes a stress test as the evaluation of a firm's position under a severe but plausible scenario[2]. In our May 2015 NED webinar these were defined as scenarios at the edge of plausibility. Events that were not likely to happen, but could. Solvency II requires that an insurer considers the range of possible outcomes at least up to the severity of a 1-in-200 event over a one-year time horizon. We did not always consider stress testing severe enough to meet this objective. We would ask that firms do more to consider and document stresses that meet their own internal view of a 1-in-200 event. Such considerations were absent from the majority of reports.

For most firms we expect improvement in the number and range of stress tests considered. We do not define the number of stresses that should be developed in detail. The number of stress tests should follow on from the number of risks that a firm classifies as material. We would, however, expect that more than the top 3 risks are used to formulate the stress tests.

Reports often included a number of stresses from the risk areas well defined within the standard formula (e.g. across insurance risk, market risk, and counterparty risk). Better reports also considered those risks less clearly defined in the standard formula (e.g. operational aspects, outsourcing arrangements, other group activities, ancillary income streams, and conduct behaviour). These stresses were often derived from using the risk register as a starting point. We would expect the most material risks to flow through into the stress testing exercise of the ORSA.

Stresses might be considered in isolation, or in combination through scenario testing. Some stresses may naturally be more correlated, for instance insurance risk and expected reinsurance recoveries, or market risk events from downturns across different asset classes. Severe scenario testing should also consider a combination of severe stresses that might be assumed to be relatively uncorrelated in normal circumstances.

The details of the assumptions behind stresses and scenarios and their detailed quantification were not always given. Better reports included a complete explanation of any assumptions and assumed management actions within the explanation of individual stress and scenario tests, enabling the reading to clearly understand how the output was derived. These details are a necessary inclusion to allow users of the ORSA report to fully understand the tests and to be able to challenge their findings.

Some reports included the quantification of stress and scenarios before and after management action. We found this a helpful exercise, as it gave an indication of a firm's ability to respond in given scenarios.

We note that stress tests might be considered at different return periods (e.g. 1-in-10 or 1-in-200 year event). Better reports stated return periods of each stress, which we found to be a useful way to give greater context to the stress tests considered.

[2] From the BIS publication 'Principles for sound stress testing practices and supervision' of May 2009

Table 1 includes examples of stresses observed, across standard formula and non-standard formula areas. This is not an exhaustive list, and not all stresses will be applicable to every firm. We have included these examples to give further indication of the level of detail that might be needed to ensure stresses are relevant to a firm's specific risk profile.

Table 1 - Stress testing examples

Risk Area	Stress	Commentary
Insurance risk	Underwriting performance	Assumptions around severity of deteriorations in performance linked to the risk characteristics of underlying lines of business.
Insurance risk	Reserve deteriorations	Assumptions of deteriorations linked to specific characteristics of lines of business, claims inflationary effects, or changes and uncertainty in claims processes.
Insurance risk	Periodical Payment Orders (PPOs)	PPO claims may be impacted by propensity changes, legal changes, and uncertainty around longevity and the economic environment. See section 8.1 for further details. Where risk is largely ceded to reinsurers, impact on reinsurance risk should be considered.
Insurance risk	Lapse rate increase	An increase in lapses may reduce expected premiums receivables with adverse impact to the balance sheet. Of particular relevance to firms where material amounts of premium are received in instalments.
Reinsurance risk	Reinsurance failure	A failure of or dispute with a large reinsurance counterparty causing a material reduction in expected reinsurance recoverables from the counterparty.
Reinsurance risk	Sliding scale and profit commissions	A deterioration in underwriting performance causing deteriorations in expected commission. Usefully combined with a scenario test covering insurance risk.
Reinsurance risk	Loss of capacity	Inability to continue reinsurance arrangements, resulting in loss of reinsurance capacity.
Market risk	Investment losses	Investment losses in key assets classes, with size of loss related to the market value characteristics of the investment class.
Market risk	Risk-free rate shock	The SII balance sheet is discounted using the risk-free rate. A shock to the risk-free rate could be due to changes in interest rates or other economic effects, with a consequent shock to liability valuation.
Liquidity risk	Asset liability matching of short term liabilities with	For a shock in short term liabilities (due to insurance or operational event), assessment of

	liquidity assets	whether payments can be covered by cash and available liquid assets.
Operational risk	IT and systems	Systems failure resulting in continuity risks or the need for an alternative system.
Operational risk	Cyber risk	Breach of systems, possible detriment to customer records, and risk of breach of data protection requirements.
Operational risk	People	Loss of key staff resulting in challenges to maintain company strategy or to ensure adherence to internal policies.
Outsourcing risk	Failure of key outsourced provider	Failure in key distribution partner or claims handling provider.
Group risk	Operational or Financial Contagion	Major risks materialising in other entities in the group result in operational or financial impacts to the insurance company.
Group risk	Funding structure	Events result in pressure to the group's funding structure and that of the insurance company.
Conduct risk	Reputation	Regulatory event or negative coverage resulting in reputational damage. Complaints monitoring may be used to support assessment of risk.
Conduct risk	Customer Redress	As above, with additionally quantifiable impact.

5.5. Reverse stress tests

The majority of firms struggled with the concept of reverse stress testing. (GL 4 indicates that reverse stress testing should be included within the ORSA process). A reverse stress test starts with the outcome of business failure and identifies circumstances where this might occur. Often firms stated that they were not able to envisage such a scenario, or that the standard formula offered a suitable measure.

The majority of firms considered business failure as the exhaustion of all capital. A small number of firms, however, gave more detailed consideration to when ongoing business plans might reach the point of failure. For instance, following a certain shortfall in capital it might be envisaged that the business is put into run-off or put up for sale. Such a failure point might be where the market loses confidence in the firm, resulting in difficulties in finding new capital providers and an unwillingness for current counterparties to continue their involvement. This point could be reached before a firm's regulatory capital is exhausted. In deciding upon the definition of failure a firm might consider the preferences of their shareholders, the nature of their main counterparty agreements, or the reliance on any key service partners.

We consider it an important exercise to give better consideration, in workshop and Board discussion, to the reserve stress concept and the point of failure, as it helps to identify the key vulnerabilities of the business and how they might be better mitigated.

We further note it might be a combination of stresses (a scenario) that leads to this failure. Even where this is deemed to be unlikely, it does not eliminate the requirement to carry out the exercise.

5.6. Presentation of the SCR

Good ORSAs included a breakdown of the SCR result by risk category. For the standard formula, results for each sub-module were presented. Commentary was also given by risk category to explain the key assumptions and any key aspects of judgment that affect the SCR.

Some firms included greater detail in an Appendix or separate documentation to comprehensively document how the balance sheet and business plan translates to the SCR result.

5.7. Capital Needs

The assessment of overall capital needs is expected to be informed by the above assessment of material risks. It should be clear how the risks faced translate into solvency requirements or other risk management techniques and mitigations. Reports often set out a target level or target range of solvency coverage as a percentage of SCR, expressing capital needs as a metric that has been approved by the Board. Better ORSA reports gave clear justification for the chosen level of capital needs.

Examples of these included:

- having sufficient capital to mitigate the key risks faced by the business;
- having additional levels of capital to give quantitative mitigation to risks not covered in the standard formula (discussed further in section 8);
- being able to absorb the future capital requirements of strategic plans;
- being able to maintain SCR compliance with the capital volatility expected in the ordinary course of running a business; and
- the choice of risk measure for capital needs, which may differ from the 99.5% one-year Value-at-Risk of the SCR.

Where a firm has strategic mitigation in place to reduce volatility then we would expect explicit reference to this within this section of the report. For example, quota share reinsurance might have been utilised for reasons of capital capacity and XL reinsurance to reduce the volatility of large losses. Firms should, however, remain mindful of any residual risk from these strategies. For example, with reinsurance there is the risk of reinsurer default or deviations from expected performance commissions. Such considerations were often absent.

6. Forward looking assessment

The majority of firms could improve the level of business planning detail that underlies this assessment. Many firms did, however, make clear progress from last year in the level of detail of the forward looking assessment of solvency.

The better forward looking assessments included a clear link to the business plan, setting out the base projection and its assumptions at an equivalent level of detail. From the perspective of the user of an ORSA report, we found this detail to be a necessary inclusion to ensure that the future drivers of the capital projections could be understood. Because business planning is also an explicit part of the ORSA process we include headings below on both business planning and the forward looking assessment of solvency.

ORSA reports have now gone through at least one or two iterations over the preparatory period of SII. Only a few firms, however, benefited from this history through the inclusion of a comparison to previous forecasts. We found this inclusion to offer a useful feedback loop to the credibility of prior years' business planning and capital projections. Observing prior deviations against expectation also gives useful insights to the formation of stress testing and to the assessment of capital needs on a current and forward looking basis.

6.1. Business Planning

Business planning is a natural part of the ORSA process as it underlies the forward looking assessment of solvency needs. In the reports submitted, however, business planning detail was often absent. In future ORSAs firms need to include the business plan, with key assumptions set out with sufficient clarity to understand how it underlies the solvency calculation for future years. For example: premium and reserve volumes set out by line of business, any changes in reinsurance and distribution strategy that impact counterparty risk, and clear asset allocations. GL 13 states that undertakings should take into account the ORSA results and process when carrying out its business planning.

A number of firms referred to separate business plan reports separately submitted to the GFSC, but often these reports also lacked the necessary detail, granularity, and explanation to be used alongside the ORSA report.

There were some instances where we have observed actual results to deviate materially from a business firm or budget submitted to us. As stated in section 4.1 we expect thresholds of material deviation that would require a re-submission to be clearly set out. When we observed these instances, it suggested a lack of integration of ORSA process and governance.

In respect of the level of detail of an informative business plan, we expect to see the following:

- A document that is more than a purely quantitative exercise. The use of a narrative alongside the figures to explain the business plan within the strategic context of the firm's objectives.
- Business planning assumptions are clearly stated, alongside the justification for these assumptions.
- Assumptions are on a credible best estimate basis, with any stretch or target elements removed.

- The business plan has a level of granularity that identifies separate jurisdictions, products, and distribution channels.
- Details of the reinsurance plan in place, including the reinsurers, terms of cover, any commission structures. Assumed loss ratios and reinsurance recoveries split out by reinsurer and year of cover.
- Investments allocation by asset category, alongside expected rates of return.
- A clear breakdown of expenses.
- Material cash-flows from and to non-insurance entities set out by separate entity.
- A prior year budget included with a comparison against the latest actual position.

We expect the business plan to cover the same period as the forward looking assessment of solvency.

We note that the full business planning exercise may be recorded in a separate document, particularly where the timing of business planning is different to the timing of the approval and submission of the ORSA report. Where business planning is separate, however, we consider the need for the ORSA report to include a clear summary of the key business plan figures and assumptions to allow the forward looking capital calculations to be understood. We also request than any separate business planning document is submitted to us as an attachment to the ORSA report.

6.2 Forward-Looking Assessment of Solvency

While all firms included a projection of the SCR within their ORSA report, only a small number of firms gave any commentary or wider consideration to the projected solvency and capital needs, and as to how this differed to the SCR figure. We expect the key risks and assessment of overall solvency and capital needs to be discussed on a forward looking basis as relevant. GL 8 requires a medium or long term view, which we would generally consider to be 3-5 years.

Few reports set out the Board's approach to future dividends. Due to the impact on the future solvency coverage we expect firms to describe their dividend policy in this section.

As noted in section 5.4 the results from any stress and scenario/sensitivity testing of the business plan should support the forward looking assessment of solvency.

7. Continuous compliance with regulatory capital requirements and technical provisions (TPs)

These sections were largely absent from the submissions received. We would expect them to be included in the next iteration of ORSA reports as all firms seek to comply with the ORSA Guidelines.

7.1. Compliance with regulatory capital requirements

This section should constitute an assessment of the own funds and how it might change over the period of the forward-looking assessment of solvency. GL 10 states that it should include at least: a) potential material changes in risk profile; b) quantity and quality of own funds over the business planning period; and c) the composition of own funds across tiers.

We expect this assessment to set out the own funds items and whether there are any risks to changes in the quantity of the item or to the characteristics that satisfy the classification features of the Commission Delegated Regulations Chapter IV. The assessment should also cover whether there are expected or potential impacts to eligibility limits from changes in the SCR or MCR.

Good ORSAs also described contingency plans for increasing the own funds position in the event that the solvency coverage falls below target levels.

7.2. Compliance with TPs

We expect that the ORSA report summarises the results of the Actuarial Function's assessment of: a) input as to whether there would be continuous compliance with technical provision requirements; and b) identification of potential risks arising from the uncertainties connected to this calculation. This is in accordance with GL 11. These should state the key assumptions of the technical provisions calculation and the uncertainty of these assumptions. Any risks around the process of calculating the technical provisions should also be highlighted.

We understand that the tasks set out in (a) and (b) above are also general requirements of the Actuarial Function, which should be covered in the written report of the Actuarial Function that is produced at least annually for the Board[3].

[3] Article 272 of Commission Implementing Regulation (EU) 2015/35 sets out the tasks of the actuarial function.

8. Deviations from assumptions underlying the standard formula and the SCR

There was a limited level of detail of this assessment, and note that it is an area of improvement for all firms.

Many ORSA reports only considered a brief assessment of the standard formula and purely on a qualitative basis. GL 12 states that as a first step a qualitative analysis of standard formula appropriateness may be performed, and if that indicates the deviation is not significant, a quantitative assessment is not required. We consider, however, that this qualitative analysis of significant deviations should take place on a risk by risk basis, and not simply at an overall level. An assessment may indicate that some aspects of the risk profile are over-calibrated (i.e. the standard formula calibration results in a view of a risk that is higher than a firm's own risk) while others are under-calibrated or not captured at all. Overall, a firm may consider the standard formula to be appropriate, but where any individual risk deviations are significant we expect that quantitative analyses are carried out. We include examples of potential risk deviations in section 8.1.

For most firms, the SCR is generated by the standard formula. Non-standard formula firms are discussed in section 8.2.

8.1. Standard Formula Appropriateness

To aid this assessment EIOPA have produced a documented entitled 'The underlying assumptions in the standard formula for the Solvency Capital Requirement calculation'. The document outlines the assumptions and the calibration of each standard formula sub-module.

Following our review of submissions and the risk profile of firms we note some key areas of standard formula appropriateness considerations as follows:

- Whether premium and reserve risk parameters capture the specific nature of a firm's business.
- The specific nature of reinsurance arrangements.
- Periodical Payment Orders (PPOs).
- Volatility around ancillary income streams not captured in the standard formula.
- Contagion risk from other group / related party entities and activities.
- Aspects of investment portfolio that differ from main financial indices.

We cover each of these in turn in the following paragraphs. This is a non-exhaustive list and we expect each firm to carry out their own assessment based on the specifics of their risk profile.

The premium and reserve risk parameters have been calibrated to be reflective of the average size and performance of portfolios of insures in the European market. A firm may have product specificities that means that risk deviates from these parameters. Further, for reasons of immaturity or other drivers of uncertainty, the risk may also deviate.

Reinsurance contracts can have terms, conditions, limits, loss ratio caps, commutation clauses, and commission structures that are not well reflected in the standard formula. In particular, it might be that the percentage of reinsurance recoveries to gross technical provisions varies quite considerably depending on the loss ratio. An example of good practice to highlight this potential risk has been to present the range of balance sheet impacts or net loss ratios (incorporating commissions) following

the application of a reinsurance contract or contracts, which varies by the ultimate gross loss ratio. This might be presented in a table form, such as in table 2, or graphically.

Table 2 – Example scenario: underwriting profit/loss to insurer, gross and net of reinsurance

Loss Ratio on book of business	**Gross underwriting profit/loss**	**Net underwriting profit/loss**
60.00%	xx	xx
70.00%	xx	xx
...	...	...
120.00%	xx	xx

In our Solvency II FAQ we state that PPOs are to be treated as a non-life annuity when they are settled, but otherwise as a motor liability risk. The motor liability premium and reserve risk factors have not been calibrated on the basis of there being a material number of potential PPOs. Further, the elements of life risk for non-life annuities are calibrated on the basis of an ordinary life insurance portfolio and do not well capture the greater uncertainty around the impaired life longevity and inflation rate on periodic payments (linked to ASHE in the UK) faced by PPOs. There is also uncertainty on the propensity for large claims to become PPOs, which is subject to the legal and social environment. Where PPO risk is material we consider scenario testing to be the minimum level of quantitative assessment. This may therefore be considered via the stress and scenario testing discussed in section 5.4.

There may be income streams into the business related to the insurance business written or from related party arrangements, such as ancillary income streams. As stated in section 6.1 we expect that the business plan sets out whether any of these income streams are material to the business, facilitating any standard formula appropriateness considerations. These income streams may be related to volumes written or to loss ratios in a way that is not well captured by the standard formula. Considerations should indicate whether or not volatility in these income streams is captured by the standard formula calibration, and whether the resulting calibration of the risk is deemed appropriate.

The standard formula does not directly capture group risks, which might arise due to the contagion effect from the non-insurance entities in the group. As noted in section 5.1 and 6.1 we expect the ORSA report to identify the group structure and material cash-flows to other group entities. Risk events occurring at these other entities, or the failure of an entity, may result in an adverse capital impact to the insurer, particularly if a key outsourcing relationship is impacted. We note that where there are key outsourcing relationships with entities outside of the group structure, but which are under common ownership, then we expect similar considerations to apply.

Group risk might also arise due to the funding structure of the group.

The market risk sub-modules of standard formula have largely been calibrated to global indices. Where a firm has a concentration of investments to a specific sector then then this may result in a decrease in investment diversification and a level of risk that is higher than the standard formula calibration. Certain investments might also have characteristics that differ from the nature of those

underlying global indices. We note that firms are required to adhere to the Prudent Person Principle[4], which should be considered as part of the ORSA process.

8.2. Undertaking Specific Paramater and (Partial) Internal Model firms

Where firms have been approved to use USPs or a partial or full internal model, we expect that standard formula SCR results are still included to support the assessment of own assumptions.

For a USP firm, the SCR deviates from the standard formula only in respect of a select number of insurance risk parameters. For all other aspects of the SCR the assessment will be the same as section 8.1.

Where a firm has an approved partial of full internal model, this section should address the ongoing appropriateness of the model. It should also denote the risks that are not explicitly captured by the internal model and justify why this does not result in a material misstatement of the SCR. The ORSA report may sign-post to other internal model documentation, where relevant, for greater detail.

Where a firm has in-development a partial or full internal model, the ORSA process should contain evidence of its use. The ORSA report should state and analyse the key areas where the model deviates from the standard formula.

[4] Schedule 1 Section 58 of the Financial Services (Insurance Companies) (Solvency II Directive) Act 2015 [Article 132 of the Solvency II Directive 2009/138/EC] requires that the ORSA report should be re-performed without delay following any significant change in risk profile.

9. Group ORSA

Not all relevant Solvency II groups produced a group report. Those firms that have been classified as belonging to an EEA group or sub-group with an insurance holding company or mixed financial holding company are required to submit a Group ORSA5. These firms are reminded that this report is required to be submitted by 31 December 2016.

Groups with a mixed-activity holding company do not have a requirement to complete a Group ORSA, but we expect elements of wider group strategy and risk to be incorporated into the solo ORSA in-line with our comments in the above sections.

Where a group ORSA is required, it is expected to reflect the nature of the group structure and risk profile, and covering all material risks arising from all entities that are part of the group (per GL 15). Our comments from early sections of the report are equally applicable on this group basis.

The group ORSA may be produced as a separate report or a group may apply to the GFSC to produce a single ORSA covering both the group and subsidiaries of the group. Of the two approaches the latter has resulted in reduced duplication of information. The GFSC is minded to approve any application for a single ORSA providing the group can commit to including the same level of detail on solo insurers within the reports as would exist in stand-alone solo ORSAs. GL 19 sets out the minimum specific requirements for a single group ORSA document, including a description of how governance requirements are met at the level of each entity subject to SII.

GL 17 and 18 set out Group ORSA specificities regarding overall solvency needs and the continuous compliance with regulatory capital requirements. This includes considerations on the availability, transferability, and fungibility of own funds across the group entities and references to any envisaged transfers of capital within the group (e.g. dividends to the holding company).

[5] In accordance with Section 102 and 132 of the Financial Services (Insurance Companies) (Solvency II Directive) Act 2015 [Article 213 and 246 of the Solvency II Directive 2009/138/EC] requires that the ORSA report should be re-performed without delay following any significant change in risk profile.

Annex 1 – EIOPA Guidelines

The EIOPA Guidelines on Own Risk and Solvency Assessment are displayed in the following table for ease of reference.

GL	Title	Text
1	General Approach	The undertaking should develop for the ORSA its own processes with appropriate and adequate techniques, tailored to fit into its organisational structure and risk-management system and taking into consideration the nature, scale and complexity of the risks inherent to the business.
2	Role of the AMSB [the Board]: top down approach	The AMSB should take an active part in the ORSA, including steering, how the assessment is to be performed and challenging the results.
3	Documentation	The undertaking should have at least the following documentation on the ORSA: a) the policy for the ORSA; b) record of each ORSA; c) an internal report on each ORSA; d) a supervisory report of the ORSA.
4	Policy for the ORSA	The AMSB of the undertaking should approve the policy for the ORSA. This policy should include at least a description of: a) the processes and procedures in place to conduct the ORSA; b) the link between the risk profile, the approved risk tolerance limits and the overall solvency needs; c) the methods and methodologies including information on: (i) how and how often stress tests, sensitivity analyses, reverse stress tests or other relevant analyses are to be performed; (ii) data quality standards; (iii) the frequency of the assessment itself and the justification of its adequacy particularly taking into account the undertaking's risk profile and the volatility of its overall solvency needs relative to its capital position; (iv) the timing for the performance of the ORSA and the circumstances which would trigger the need for an ORSA outside of the regular time-scales.
5	Record of each ORSA	The undertaking should evidence and document each ORSA and its outcome.
6	Internal reporting on the ORSA	The undertaking should communicate to all relevant staff at least the results and conclusions of the ORSA, once the process and the results have been approved by the AMSB.

7	Assessment of the overall solvency needs	The undertaking should provide a quantification of the capital needs and a description of other means needed to address all material risks irrespective of whether the risks are quantifiable or not. Where appropriate, the undertaking should subject the identified material risks to a sufficiently wide range of stress tests or scenario analyses in order to provide an adequate basis for the assessment of the overall solvency needs.
8	Forward-looking perspective of the overall solvency needs assessment	The undertaking should ensure that its assessment of the overall solvency needs is forward-looking, including a medium term or long term perspective as appropriate.
9	Valuation and recognition bases of the overall solvency needs	The undertaking should, if it uses recognition and valuation bases that are different from the Solvency II bases in the assessment of its overall solvency needs, explain how the use of such different recognition and valuation bases ensures better consideration of the specific risk profile, approved risk tolerance limits and business strategy of the undertaking, while complying with the requirement for a sound and prudent management of the business. The undertaking should quantitatively estimate the impact on the overall solvency needs assessment of the different recognition and valuation bases in those cases where recognition and valuation bases, that are different from the Solvency II bases, have been used in the assessment of its overall solvency needs.
10	Continuous compliance with regulatory capital requirements	The undertaking should analyse whether it complies on a continuous basis with the Solvency II regulatory capital requirements and as part of this assessment it should include at least: a) the potential future material changes in its risk profile; b) the quantity and quality of its own funds over the whole of its business planning period; c) the composition of own funds across tiers and how this composition may change as a result of redemption, repayment and maturity dates during its business planning period.
11	Continuous compliance with technical provisions	The undertaking should require the actuarial function of the undertaking to: a) provide input as to whether the undertaking would comply continuously with the requirements regarding the calculation of technical provisions; b) identify potential risks arising from the uncertainties connected to this calculation.
12	Deviations from assumptions underlying the SCR calculation	The undertaking should assess whether its risk profile deviates from the assumptions underlying the SCR calculation and whether these deviations are significant. The undertaking may as a first step perform a qualitative analysis and if that indicates that the deviation is not significant, a quantitative assessment is not required.
13	Link to the strategic	The undertaking should take into account the results of the ORSA and the insights gained during the process of this assessment in at least:

	management process and decision-making framework	a) its capital management; b) its business planning; c) its product development and design.
14	Frequency	The undertaking should perform the ORSA at least annually.
Group ORSA Guidelines		
15	Scope of group ORSA	The participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should design the group ORSA to reflect the nature of the group structure and its risk profile. They should cover in the group ORSA the material risks arising from all the entities that are part of the group.
16	Reporting to the supervisory authorities	The participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should send to the group supervisor the group supervisory ORSA report. The document sent to the group supervisor with the outcome of the group ORSA should be in the same language as the group Regular Supervisory Reporting. If a single ORSA document has been performed, the participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should ensure that, if requested by a member or a new member of the college, a translation into the official language of that Member State of the part of the ORSA information concerning the related undertaking is provided to the requiring member, in timely manner.
17	Group specificities on overall solvency needs	The participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should adequately assess the impact of all group specific risks and interdependencies within the group and the impact of these risks and interdependencies on the overall solvency needs. They should take into consideration the specificities of the group and the fact that some risks may be scaled up at the level of the group. In accordance with Guideline 5 on the record of each ORSA, the participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should include in the record of the group ORSA at least a description on how the following factors were taken into consideration for the assessment of overall solvency needs: a) the identification of the possible sources of capital within the group and identification of potential needs for additional capital; b) the assessment of availability, transferability or fungibility of capital; c) references to any envisaged transfer of capital within the group, which would have a material impact on any entity of the group, and its consequences; d) alignment of individual strategies with the ones established at the level of the group; e) specific risks the group could be exposed to.
18	Group specificities on	In accordance with Guideline 5 on the record of each ORSA, the participating insurance or reinsurance undertaking, the insurance holding company or the

	the continuous compliance with regulatory capital requirements	mixed financial holding company should include in the record of the group ORSA at least a description on how the following factors were taken into consideration for the assessment of continuous compliance with regulatory requirements: a) the identification of the sources of own funds within the group and if there is a need for additional own funds; b) the assessment of availability, transferability or fungibility of own funds; c) references to any planned transfer of own funds within the group, which would have a material impact on any entity of the group, and its consequences; d) alignment of individual strategies with the ones established at the level of the group; e) specific risks the group could be exposed to.
19	Specific requirements for a single ORSA document	In case of application to undertake the ORSA according to third subparagraph of Article 246(4) of Solvency II , the participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should provide to the group supervisor: a) a list of the undertakings for which the individual assessments required by Article 45 of Solvency II are covered in the single ORSA document including the reason of the choice made; b) a description of how the governance requirements are met at the level of these undertakings and in particular how the AMSBs of the subsidiaries are involved in the assessment process and approval of the outcome; c) a description of how the single ORSA document is organised in order to allow the group supervisor to separate individual assessments for the other supervisors in the college; d) where necessary, a specific indication on required translations, with specific attention to timing and content.
20	Integration of related third-country insurance and re-insurance undertakings	In the assessment of the group overall solvency needs, the participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company, should include the risks of the business in third countries in a consistent manner as it does for European Economic Area-business with special attention to the assessment of transferability and fungibility of capital.