

SUMMARY
OF NÁRODNÁ BANKA SLOVENSKA'S MOST FREQUENT RECOMMENDATIONS
TO IMPROVE THE QUALITY
OF OWN RISK AND SOLVENCY ASSESSMENT (ORSA) REPORTS,
MADE AFTER ASSESSING THE ORSA REPORTS
SUBMITTED BY INSURANCE UNDERTAKINGS IN 2016

Foreword

As part of its risk management system, every insurance undertaking subject to NBS supervision ("supervised entity") is required to conduct an own risk and solvency assessment (ORSA) in accordance with Article 26 of Act No 39/2015 Coll. on insurance, as amended ("the Insurance Act"). The results of each ORSA must be reported by the supervised entity to NBS as part of the information to be provided for supervisory purposes. Supervised entities are required to conduct an ORSA regularly, at least once a year, and without any delay following any significant change in their risk profile.

Supervised entities must submit a supervisory report on each of their ORSAs ("an ORSA report") to NBS in accordance with Article 304 of Commission Delegated Regulation (EU) 2015/35 of 10 October 2014 supplementing Directive 2009/138/EC of the European Parliament and of the Council on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II) ("Delegated Regulation 2015/35").

Following the provisions of Articles 23, 25 and 26 of the Insurance Act and Articles 262 and 306 of Delegated Regulation 2015/35, NBS issued Recommendation No 5/2016 of the Financial Market Supervision Unit of Národná banka Slovenska of 17 May 2016 on own risk and solvency assessments for the insurance and reinsurance sector ("FMSU Recommendation No 5/2016").

All the insurance undertakings subject to the Solvency II regulatory regime met the obligation to conduct at least one ORSA in 2016.

During 2016 Národná banka Slovenska acquired detailed information about each insurance undertaking's risk management system and also reviewed all their ORSA reports. At each insurance undertaking, NBS held a day-long meeting with staff members responsible for performing the risk management and actuarial functions.

Based on these meetings, as well as on the review of the ORSA reports, NBS sent each insurance undertaking written recommendations on how to improve the quality of their ORSA report in the next period. The most frequent of these recommendations are listed below.

Summary of NBS's most frequent recommendations to improve the quality of ORSA reports

The own risk and solvency assessment process, its place within the insurance undertaking's organisation, and its integration into the planning process

Under Article 26(1) of the Insurance Act, insurance undertakings are required to conduct an own risk and solvency assessment as part of their risk management system. At the same time, Article 25(2) of the Insurance Act requires the risk management system to be effective and well integrated into the undertaking's organisational structure.

NBS recommended insurance undertakings to give a more detailed account of their system of governance as it relates to the ORSA process, for example by describing the operation of the risk management system and the integration of particular organisational units or committees into the ORSA process.

For the purposes of the ORSA, insurance undertakings are required under Article 26(2) of the Insurance Act to have in place processes which are proportionate to the nature, scale and complexity of the risks inherent in their business.

NBS recommended insurance undertakings to include in their ORSA reports information about the timeframe for the ORSA process and the frequency with which the management reviews the ORSA.

Under Article 26(5) of the Insurance Act, insurance undertakings must make the ORSA an integral part of their business strategy and take it into account on an ongoing basis in their strategic decisions. The business plans of insurance undertakings are based on business strategies and policies and incorporate elements of undertakings' own risk assessments as set out in the ORSA process.

NBS recommended insurance undertakings to include in the description of their planning process a description of the ORSA process so as to demonstrate its integration in the planning process.

Assessment of overall solvency needs taking into account the specific risk profile, approved risk tolerance limits and the business strategy of the undertaking

Under Article 26(1)(a) of the Insurance Act, the ORSA must include the overall solvency needs of the insurance undertaking taking into account, in conjunction with Guideline 4(1)(b) of FMSU Recommendation 5/2016, the interlinkage between the undertaking's risk profile, approved risk tolerance limits and business strategy.

NBS recommended insurance undertakings to include in their ORSA reports, in the context of risk assessment, their risk tolerance limits, risk impact assessments, risk management process and risk mitigation techniques. NBS also recommended insurance undertakings to state the

main source of individual risks. In addition, NBS recommended insurance undertakings to include in their ORSA reports an assessment of the compatibility of their risk appetite and key risk indicators (KRIs) with their business plans, as well as the results of this assessment.

Under Article 306(b) of Delegated Regulation 2015/35, the ORSA report must present the methods and main assumptions used in the ORSA.

NBS deems that the main assumptions referred to in Article 306(b) of Delegated Regulation 2015/35 include key risk indicators and KRI thresholds.

NBS recommended insurance undertakings to include in their ORSA reports their key risk indicators, KRI thresholds and risk tolerance limits.

NBS deems that the main assumptions referred to in Article 306(b) of Delegated Regulation 2015/35 also include the undertaking's quantified business and financial objectives for at least the next three years, being the basis of its risk and capital planning.

NBS recommended insurance undertakings to present their business and financial objectives for at least the next three years and an assessment of their business strategy in the light of their overall solvency needs.

NBS deems that the main assumptions referred to in Article 306(b) of Delegated Regulation 2015/35 furthermore include the methods and assumptions used for the projection of the solvency capital requirement (SCR).

NBS recommended insurance undertakings to include in their ORSA reports a description of their SCR projection methods, references to the internal regulations in which these methods are set out, and the SCR projection assumptions.

Appropriateness of the standard formula

Under Article 26(1)(c) of the Insurance Act, insurance undertakings are required to identify the difference between their risk profile and the assumptions underlying the SCR calculated with the standard formula or with its partial or full internal model.

NBS recommended insurance undertakings to include in their ORSA reports information about the appropriateness of the standard formula.

Information about data quality standards

Under Article 26(1)(a) of the Insurance Act, in conjunction with Article 306(b) of Delegated Regulation 2015/35, insurance undertakings are required to conduct an ORSA as part of their risk management system, taking into account, in conjunction with Guideline 4(1)(c) point 2 of FMSU Recommendation 5/2016, information about data quality criteria.

Under Article 20 of Delegated Regulation 2015/35, insurance undertakings are required to document appropriately the limitations of data including a description of whether and how such limitations will be remedied. Under Article 26(7) of the Insurance Act, insurance undertakings are required to inform NBS of the results of each ORSA. On that basis, the results of their review of data quality criteria, including the limitations of data, should be presented in the ORSA report.

NBS recommended insurance undertakings to include in their ORSA reports the results of their review of data quality criteria, including the limitations of data. NBS also recommended insurance undertakings to include in their ORSA reports information about their approval process (in respect of data quality and the review/validation of results) including information about the review and approval process and its results within the internal control system.

Stress testing

Under Article 26(1)(a) and (b) of the Insurance Act, the ORSA must include the overall solvency needs and the compliance, on a continuous basis, with the capital requirements. At the same time, under Guideline 7(2) of FMSU Recommendation 5/2016, insurance undertakings should perform stress tests and scenario analysis with regard to all the relevant risks that they face, and do so to such an extent that allows them to assess their overall solvency needs. Subsequently, in accordance with Guideline 10(1)(a) and (b) of FMSU Recommendation 5/2016, as part of the review of their continuous compliance with capital requirements, insurance undertakings should perform stress tests and scenario analysis on a regular basis in order to estimate potential future material changes in their risk profile and to estimate their future own funds.

Where NBS took the view that an insurance undertaking's stress tests included too few scenarios, it recommended the undertaking to add more scenarios, such as for life or non-life underwriting risk, for insurance technical risks, for market risk, and for other potentially significant risks. NBS also recommended that the ORSA report include an explanation of scenario results in respect of those risks for which the most pronounced changes in level are observed.

In addition, NBS recommended that stress test analyses present the measures taken by the undertaking's management to mitigate the potential outcomes identified in the stress tests.

NBS furthermore recommended insurance undertakings that had performed a reverse stress test to present the results of that test, too.

Clarity and comprehensiveness of ORSA reports

NBS recommended insurance undertakings to edit the structure and content of their ORSA reports so that the reports do not repeat the same information in different places and do not repeat the wording of the ORSA policy. If a certain point needs to be reiterated, it will suffice

to provide a reference to the place in the report, or the ORSA policy, where it was previously stated or a reference to another document or policy in which the information appears.

Type of ORSA report (internal vs supervisory)

Under Guideline 3(c) and (d) of FMSU Recommendation 5/2016, the minimum documentation about each ORSA should include an internal ORSA report and an ORSA supervisory report that is to be provided to the supervisory authority.

NBS takes the view that if an insurance undertaking uses its internal report also as the supervisory report, it should state this fact in that report.

NBS recommended insurance undertakings to state in their ORSA reports whether the supervisory report was the same as the internal report.

Informing relevant staff members about ORSA outcomes

Under Guideline 6 of FMSU Recommendation 5/2016, insurance undertakings should ensure that after the ORSA process and outcomes have been approved by the management board, the relevant staff members are informed at least about the ORSA outcomes.

NBS recommended insurance undertakings to identify in their ORSA reports or ORSA policies which of their staff members are to be informed about the ORSA outcomes after the ORSA process and outcomes have been approved by the management board.