| Comments Template on<br>CP8 -Draft proposal for Guidelines on ORSA | | Deadline<br>20 January 2012<br>12:00 CET |
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| Name of Company: | KPMG ELLP | |
| Disclosure of comments: | Please indicate if your comments should be treated as confidential: | Public |
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| **Reference** | **Comment** | |
| General Comment | We strongly welcome the publication of this consultation paper (CP) in advance of finalisation of Omnibus 2 and Level 2. The ORSA is a very important component on the Solvency II regime, so any guidance that helps firms and groups better understand their needs in this area is very helpful.<br>Overall we support the direction that EIOPA have looked to taken, but believe the paper could be improved greater consistency between the Group guidelines and the rest of the CP.<br>Given international developments, it may be helpful to explain how Recovery and Resolution Plans (RRPs), could be included as part of the ORSA analysis. Although RRPs are currently being discussed for significant international financial institutions (SIFI) only, some insurance groups will need to develop both ORSA and RRPs. For | |

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| | other groups, resolution plans could have a direct link with the ORSA. | |
| 3.1. | | |
| 3.2. | | |
| 3.3. | More clarity could be provided relating to the scope of the ORSA for international groups. This is especially relevant to third country groups where section 260 has been applied by adopting other methods of group supervision. Another area related to national level sub-group supervision – what level of ORSA is required in relation to such groups, or is the sub-group supervision limited to the solvency calculation? | |
| 3.4. | | |
| 3.5. | An area where additional information would be helpful relates to the Supervisory Review Process (SRP) in relation to the ORSA. Given the high-level nature of the material within this ORSA paper (which we welcome) clarity around the supervisory review of the ORSA, the approach to reviewing the ORSA and the supervisory areas of focus would be useful to understand and we welcome EIOPA's comment that this will be covered in guidelines on the SRP. | |
| 3.6. | We are strong believers that information needs to be appropriate to the audience and the risk of information overload should be avoided.<br><br>We therefore believe that the AMSB should be aware of all material risks, rather than all risks, which could be a very long list, especially for large international groups. The proportionality principle should apply. In addition there is a risk that too much information could result in the AMSB's attention becoming focused in the wrong areas from a risk and business perspective. We believe that all risks should be assessed by the risk management function, who would be responsible for ensuring that all material risks are reported to the AMSB. | |
| 3.7. | | |
| 3.8. | Given the proposals to report the ORSA separately from the year end reporting requirements, some clarity regarding the extent of disclosure in relation to differences from the SCR calculation would be helpful. In particular, if the ORSA report and SCR reporting are at different dates, then a numerical comparison may not be helpful. For example, it could be made clear that this does not necessarily need to be a comparison against the annual SCR, but could instead be a comparison | |

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| | against the estimated SCR as reported in the latest quarterly QRT. | |
| 3.9. | | |
| 3.10. | | |
| 3.11. | See 3.3. | |
| 3.12. | | |
| 3.13. | | |
| 3.14. | Consideration needs to be given to the definitions included here. Where a group is located outside the EEA, then the need for a group ORSA will depend on the basis of group supervision determined in accordance with article 260. In addition, some groups will be subject to equivalent group supervision elsewhere. Acknowledgment needs to be given to the fact that such groups will not be required to complete a Solvency II group ORSA> | |
| 3.15. | | |
| 3.16. | Although potentially challenging, regulators may need to consider the behaviours or ethics of a company/group in order to properly review the ORSA Report. Typically, a firm's culture has not been the remit of regulation, but it is hard to argue that behavioural issues were not deeply rooted in many of the causes of the economic crisis.<br><br>A company's culture affects leadership and strategy of the firm, and ultimately shapes decision making. Excessive compensation can incentivise risk taking, so remuneration also needs to be considered. Examining ways to capture such information within the ORSA processes may be worthwhile. | |
| 3.17. | d) ORSA Supervisory Report: We understand that the supervisory reporting regarding the ORSA may no longer be linked to the annual reporting cycle.<br><br>If this is the final position when the rules become effective, then consideration needs to be given to the timing of ORSA reporting. Linking the reporting to supervisors to the timing of internal ORSA reporting is not helpful in our view, as firms have discretion on when to produce their internal report. It should also be recognised that since the ORSA is predominantly about systemns and processes, these are on-going and do not occur at discrete points of time. | |

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| | We therefore believe it would be helpful to provide an indication fo where within a firm's annual business cycle (from initial business planning to annual reporting), supervisors would most like to receive the ORSA report. | |
| 3.18. | The contents of the ORSA policy as outlined overlaps with other required written policies. It would therefore be helpful to clarify that existing documents can be used to meet these requirements to avoid duplication. | |
| 3.19. | | |
| 3.20. | | |
| 3.21. | There are concerns that some of the outstanding pillar 1 issues may be resolved in a manner that many believe is not a true economic approach. In that case, such firms may continue to use their own economic capital basis internally to run their business and in the ORSA. In this situation, how much explanation would be required on the differences in recognition and valuation bases ?<br><br>Formalising links between insurers' strategic objectives and options with risk appetite, and establishing formal reporting mechanisms is a practical policy option available to supervisors. Extending such arrangements, such as to instances of acquisitions and mergers, may also assist regulators to better assess the systemic relevance of firms, as well as enabling insurers to articulate impacts to the business model of such changes. These requirements could usefully form part of the ORSA set of requirements expected of insurers. | |
| 3.22. | | |
| 3.23. | | |
| 3.24. | Would EIOPA consider for the ORSA that it would be sufficient for the firm to leverage off the stress/scenario analyses undertaken for their internal model ? | |
| 3.25. | | |
| 3.26. | | |
| 3.27. | The actuarial function is the only function mentioned in this paper. Guidance would be helpful setting out the role and responsibilities expected of the other functions (especially risk management and internal audit). | |
| 3.28. | How does this guideline apply to firms with an approved internal model? | |

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| | A separate section on the expectations for firms not having a full approved internal model would be useful. | |
| 3.29. | The ORSA should include several feedback loops to ensure information remains up to date and relevant. Projected solvency positions also need to be consistent with the risk strategy and business plans. | |
| 3.30. | | |
| 3.31. | We agree that all entities should be in the scope of the group ORSA. However, the entities covered here only relate to the insurance part of a group. Insurance groups are likely to contain in addition companies outside the insurance sector.<br><br>One of the areas groups are grappling with is in understanding how the group ORSA requirements interact with the non-insurance parts of their business. In particular, the extent to which group ORSA needs to drive down into the decisions taken within this part of the group.<br><br>In order to properly understand group risks, all such entities should be included within the ORSA, which is what this section suggests (given the link to the scope of group supervision). It would therefore be very helpful if specific consideration of the interaction of the group ORSA with these businesses could be included within this paper. | |
| 3.32. | | |
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| 3.35. | | |
| 3.36. | This suggests there will be no requirement to harmonise business planning periods throughout the group. This may be helpful for groups which has subsidiaries with non-coterminous year ends, but this could result in a mix of ‘real’ and ‘projected’ information being used.<br><br>It would therefore be helpful to understand the intention behind this guideline. | |
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| 3.39. | | |
| 3.40. | As with our comment in 3.31, this only refers to insurance businesses and not to other group operations.<br><br>Read cold (ie without the additional material in 4.99), it is unclear what the reference to deduction and aggregation means.<br><br>See also our comments at 4.99 | |
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| 4.1. | | |
| 4.2. | This seems to indicate that management need a risk methodology setting out how risks are managed on an individual level within the business (i.e. capital as a mitigant if quantifiable and in the internal model, managed by monitoring actions and controls so not in internal model, or both). Is this the expectation? | |
| 4.3. | | |
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| 4.7. | Although Article 45 only refers to the assessment being performed 'regularly', we had understood that the minimum frequency was annual. This suggests that if the firm has a has higher risk profile the minimum frequency should be more frequent than this.<br><br>If the reporting to supervisors is linked to the internal reporting timetable, then this could result in ORSA supervisory reports on a more frequent basis than annually.  Is this the intention?  This would not have been the case when the ORSA was required to be reported as part of the RSR | |

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| | reporting process.<br><br>If this is the intention, then who will determine the appropriate frequency – the firm or the supervisor? We believe it should be the firm. | |
| 4.8. | The requirement to have an indepedent assessment has been removed. Is this because it is up to the AMSB to determine how they satisfy themselves the ORSA process operates as designed?<br><br>Also is it expected that internal audit should review the ORSA processes, as they would any other area of the business? If so we would suggest this is added to the document. | |
| 4.9. | | |
| 4.10. | | |
| 4.11. | | |
| 4.12. | Should the policy also cover how the firm plans to address the forward-looking aspects (i.e. Pillar 1 projection methodology, stress tests / scenarios tests / reverse stress tests, risk appetite across the plan)?<br><br>The reverse stress test requirement should be added into guideline 4 to make it consistent with the description under guideline 10. We believe it is absolutely right to have reverse stress tests in the paper as they are part of a coherent stress testing framework and a useful supervisory tool for assessing financial stability. Our experience has shown that those firms who have developed them feel they have learnt about their business as a result.<br><br>The paper includes a guideline on 3 of the 4 documntation requirements so it would be worth including one on the ORSA supervisory report (even if it is in the Pillar 3 CPs) for completeness? | |
| 4.13. | | |
| 4.14. | e) Is a range of ‘own solvency needs’ acceptable or will supervisors require a single answer?<br><br>k) see 3.6. We agree that the feedback and challenge process of AMSB should be documented. | |
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| 4.20. | Will the materiality assessment process need to be explained in the ORSA policy document? | |
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| 4.24. | Material off-balance sheet aspects should also be considered. | |
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| 4.27. | This analysis requires insurers to incorporate detailed market analysis, the focus of which could now incorporate risks posed to the wider economic environment. In some markets, supervisors are already moving to requiring forward assessments of the financial condition of an insurer under a range of scenarios. For example, in the UK, the Individual Capital Adequacy Standards (ICAS) requires extensive testing of capital, insurance, market, credit, liquidity and operational risks, in addition to other relevant risks such as reinsurance, strategic risks, and corporate governance risk.<br><br>Such requirements will ostensibly be extended in Solvency II via the ORSA requirements and for those firms using an internal model, including the capital methodology proposed for calculating capital requirements. A widening of these existing and proposed supervisory tools to take account of potential economic impact considerations would largely complement the analysis performed and in this context, may be a cost effective and proportionate method for the insurance industry. | |
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| 4.31. | a) Solvency II requirements require insurers to invest in assets whose risks it can properly assess and manage, especially concerning the use of more complex and less transparent classes of assets and investment in markets or instruments that are subject to less governance or regulation. This should make solvency needs in relation to these investments easier to determine.<br><br>However, further analysis is likely to be beneficial. For example, consistent requirements relating to special purpose vehicles, hedge funds, derivatives, private equity, structured credit products, insurance linked instruments, hybrid instruments that embed derivatives and dynamic hedging programs all come under the banner of 'inherently risky' financial instruments that are likely to require greater scrutiny by both firms and supervisors. The risks within these investments need to be properly understood to enable solvency needs in relation to them to be determined.<br><br>It may be helpful if firms were required to undertake specific analysis of such instruments within their ORSA assessments with particular regard to whether such assets lead to an increased systemic risk scenario.<br><br>g) The need for consistent valuation basis needs to be expanded, especially as regards the non-EEA, non-insurance parts of an insurance group. | |
| 4.32. | | |
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| 4.34. | Is there an expectation that the emerging risk process should be included in this forward-looking process? If yes, then it would be worth setting out this expectation. | |
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| 4.38. | Is it worth making clear that reverse stress tests are not about capital per se but about what you can learn from the business and the vulnerabilities of your business model. | |
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| 4.53. | It seems unrealistic to force a company to de-risk if it does not have the resources to build an internal model and seek to get that approved. This could fundamentally alter the market and stifle innovation. EIOPA should carefully consider this and other courses of action such as voluntarily holding higher capital levels for the products. | |
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| 4.61. | e) needs clarification - is a quantification of minor model changes part of the ORSA reporting? We would expect it to fall within the RSR rather than the ORSA report. | |
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| 4.82. | The comparison needs to be made clearer. In respect of the predominantly banking/credit business group, the group ORSA would only apply at the small insurance subgroup level, so would exclude this business. | |
| 4.83. | | |
| 4.84. | | |
| 4.85. | The requiments for an ORSA supervisory report whenever a regular or non-regular ORSA is performed could result in several such reports needing to be submitted each year. Is this the intention? | |

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| | Is there scope for a shorter report in relation to ad hoc ORSA? For example, focusing on what has triggered its preparation and what has changed since the last regular ORSA? | |
| 4.86. | | |
| 4.87. | As well as the interrelationships between the risks of the parent and the solo undertakings, significant interrelationships between solo undertakings should be described. | |
| 4.88. | | |
| 4.89. | | |
| 4.90. | (b) Clarification required on what measure should be used for non-EEA insurers. As written, this would require solo SCRs to be calculated for each of these third country insurance entities, which is disproportionate where the accounting consolidation basis is applied. | |
| 4.91. | | |
| 4.92. | (a) – as 4.90 above<br>(b) - what is the intention of this allocation? Given the comment in 4.90 above, this may not be practicable in relation to third country insurers<br>(d) – this suggests that diversification effects are somehow allocated down to individual companies. Again the rationale for this and practicability of this are unclear | |
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| 4.99. | (a) We do not agree with the requirement that where a third country has been deemed equivalent to Solvency II, a group sould still need to assess the overall solvency needs in accordance with Article 45. In order to have been deemed equivalent, the regulations applying in that third country will require its own version of the ORSA, and we believe this should be used within the group ORSA process, rather than requiring it to be reassessed on a Solvency II basis. | |

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| | (b) We do agree that fungibility and transferability remains relevant.<br><br>(c) If the third country concerned does not require such an explanation of differences between capital requirements applied and the required capital requirement, then it is unreasonable to require this to be included within the group ORSA. As reference is equivalence, the capital requirement will have had to be calibrated to a level sufficient to pass the equivalence assessment, so it is unclear what this seeks to achieve. | |
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