

Issues Paper

Own Risk and Solvency Assessment (ORSA)

CEIOPS publishes the following Issues Paper to invite stakeholders' comments on CEIOPS' views on the Own Risk and Solvency Assessment under the Solvency II Framework Directive Proposal. CEIOPS will not provide direct feedback to comments, but will take them into account in its future work.

Please send any comments to CEIOPS by email (Secretariat@ceiops.eu) by 27 August 2008, indicating the reference "CEIOPS-IGSRR-09/08".

CEIOPS will make all comments available on its website, except where respondents specifically request that their comments remain confidential.

Style convention

The following has been adopted for this document:

Text marked in grey is a direct quote from the current version of the amended Proposal for a Directive of the European Parliament and of the Council on the taking up and pursuit of the business of Insurance and Reinsurance (“Solvency II”), dated 26 February 2008, COM (2008)119 (“Framework Directive Proposal”).

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Introduction

Background

1. In Article 44 the Framework Directive Proposal prescribes an own risk and solvency assessment (ORSA) as part of the risk management system of every (re)insurance undertaking. This assessment requires (re)insurance undertakings to properly determine their overall solvency needs. ORSA information will also be reported to solo and group supervisory authorities and be used in the Supervisory Review Process (SRP).
2. The ORSA is a new concept and therefore it might not be familiar for (re)insurance undertakings. Consequently this matter calls for more details and explanations. The Framework Directive Proposal does not – and as a Level 1 legal text to some extent cannot – provide all the necessary answers. While the Framework Directive Proposal text covers the most important elements to be assessed as part of the ORSA, the enumeration of the results to be produced is not exhaustive. Also, there is a perception that undertakings may view the ORSA as requirements for a process with a degree of complexity and sophistication far in excess of what the European Commission and CEIOPS actually envisage. All this has created a certain amount of uncertainty for the market as to what to expect from this new requirement.
3. The uncertainty about what will be expected of (re)insurance undertakings in the performance of the ORSA raises concerns, especially for small and medium-sized undertakings, of very demanding requirements. Aware of these concerns, also the European Commission has sought to address the main doubts and has stated, in the Explanatory Memorandum to its Framework Directive Proposal, that the ORSA:
 - a) does not require an undertaking to develop an internal model;
 - b) is not a capital requirement different from the SCR and the MCR;
 - c) should not be too burdensome.
4. When working on the advice to Level 1, CEIOPS discussed in some detail the scope of the ORSA. Some considerations regarding “the purpose of the IRCA¹ and inter-linkage to the SCR and capital add-on” can be found in “CEIOPS Advice to the European Commission in the Framework of the Solvency II project on Pillar II capital add-ons for solo and group undertakings” (CEIOPS-DOC-05/07).²
5. The Framework Directive Proposal does not stipulate any Level 2 implementing measures regarding the ORSA, but there will be development

¹ IRCA means Internal Risk and Capital Assessment; it is the term formerly used to refer to what is now named ORSA.

² 20 March 2007, see Website-Publications.

of the principles relating to the ORSA in Level 3 guidance to be issued by CEIOPS. With no Level 2 advice to prepare, CEIOPS would normally only develop such guidance at a later stage. However, for the sake of transparency, CEIOPS has decided to advance its discussion of ORSA issues and publish its views early on in order to clarify for the market what the ORSA is meant to achieve.

6. In this paper CEIOPS explains its preliminary views on the definition and importance of the ORSA as a management tool, the purpose of the ORSA, some requirements building on the Directive Proposal and some principles and guidance on the ORSA process. The guidance as set out in this document may yet be modified or amended before the introduction of the Solvency II framework, as the framework is being further developed. The present paper only considers the ORSA as a requirement on undertakings; issues related to how supervisors review the ORSA, the requirements on supervisory reporting and how supervisors may use the output from the ORSA will be covered by other Issues Papers which CEIOPS plans to publish.
7. At a later stage, it is likely that CEIOPS will develop additional guidance on the group ORSA requirements provided for in Article 250 of the Framework Directive Proposal. This may, amongst other things, include consideration of the implications of a single ORSA covering multiple entities and the specific conditions established by the group support regime.

Definition and aim of the ORSA

8. The Framework Directive Proposal, in Article 44, describes the own risk and solvency assessment as a tool of the risk management system that requires (re)insurance undertakings to properly assess their own short and long term risks and the amount of own funds necessary to cover them. At the same time the ORSA represents an important source of information for the supervisory authorities, and the undertakings are obliged to describe the process they have undertaken to satisfy the ORSA requirements through the regulatory reporting requirements.
9. Consequently, the ORSA can be defined as the entirety of the processes and procedures employed to identify, assess, monitor, manage, and report the short and long term risks a (re)insurance undertaking faces or may face and to determine the own funds necessary to ensure that the undertaking's overall solvency needs³ are met at all times.
10. The ORSA aims at enhancing awareness of the interrelationships between the risks an undertaking is currently exposed to, or may face in the long term, and the internal capital needs that follow from this risk exposure, whether an undertaking uses the standard formula or an internal model to calculate the SCR. The administrative or management body should understand and assess the risks which the undertaking is exposed to and determine the level of own funds appropriate to its risk and internal control environment.

³ The term "overall solvency needs" includes the assets necessary to cover the liabilities, including technical provisions, the regulatory capital requirements – SCR and MCR – as well as the internal capital needs.

Why is the ORSA important?

11. The assessment by the undertaking of its own position in terms of risk and solvency is crucial for the implementation of a risk-based regime such as Solvency II. The risk-based approach requires, amongst other things, that undertakings hold an amount of own funds commensurate with the risks which they are or may be exposed to. The ORSA represents first of all the undertaking's opinion and understanding of its risks, overall solvency needs and own funds held.
12. The standard formula to calculate the SCR introduces a capital requirement that aims to take into account all quantifiable risks for the average undertaking. It may however not cover all material risks a specific undertaking is actually exposed to. A standard formula is, by its very nature, a standardised calculation method, and is not tailored to the individual risk situation of a specific undertaking. For this reason, in some cases, the standard formula will not reflect the risk profile of a specific undertaking and consequently its overall solvency needs. Therefore, the use of the standard formula does not exempt the undertaking from assessing the own funds it needs considering the risks it faces or may face. In addition to having sufficient eligible own funds to cover the regulatory capital requirements, the undertaking must assess the adequacy of this regulatory capital requirement to its individual risk position.
13. The matching of the own funds to the risk profile should help promote a strong culture of risk management, which in turn is a key underlying feature of the ORSA process and, more widely, in soundly running the business.
14. Moreover it is important to have a forward-looking perspective. With changes in the risk profile of the undertaking translating into changes of overall solvency needs, it is imperative that undertakings analyse how their risk situation may change according to external factors or their own business plans in the longer term, in order to be able to ensure that increased overall solvency needs can be satisfied if and when they arise. To this end, undertakings need to establish how to properly monitor and measure prospective changes in the risk situation. They also need to consider how these changes affect their capital position and how they have access to additional own funds, if necessary.
15. Through its requirement for an integrated management of risks and capital, the ORSA helps undertakings to ensure that they continuously meet the regulatory capital requirements, as well as the internal capital targets they set themselves.
16. The ORSA process is as important for the undertaking as the final outcome itself. Performing the ORSA helps the undertaking to obtain a real and practical understanding of the risks it is assuming.
17. It is of crucial importance that an undertaking, through the ORSA process, identifies the major issues affecting its overall solvency needs. If the supervisory authority discovers issues that should have been determined in the ORSA, not only must the supervisor take action according to the deficiencies but it also has to assess the reason why the issues were not

identified by the undertaking itself. The non-identification of issues in the ORSA may prove to be of just as much concern to supervisors as the issues themselves.

Proportionality

18. The ORSA may take different levels of sophistication according to the nature, complexity and scale of the risks inherent in the business, ranging from simple stress test calculations on the material risks to the use of more advanced methodologies similar to the ones used in partial or full internal models. While there may be undertakings using the SCR standard formula for which, owing to their size and complexity, the ORSA process necessitates a design not far removed in sophistication from an internal model, this will not apply to all undertakings. Standard formula users with less complex risk profiles may use less sophisticated tools to implement the ORSA.
19. However, it should be recognised that the ORSA exercise could promote the use of more sophisticated methods, since it requires undertakings to become more cognizant of the interrelationships between the risks within their business and their overall solvency needs. It can be expected that, with this increased insight, undertakings will seek to improve their ability to assess and manage their risks and control their overall solvency needs and thus enhance their efficiency by introducing more advanced processes, methods and techniques.

ORSA Requirements

20. This part of the paper aims at broadly explaining CEIOPS' views on the ORSA requirements according to the Framework Directive Proposal.
21. It is up to an undertaking to decide how it designs its ORSA process, but it has to ensure that the process meets the requirements set out in Article 44 of the Framework Directive Proposal, and is also proportionate to the nature, scale and complexity of its risks.
22. Although the execution of the ORSA as such can be outsourced, the administrative or management body remains responsible for the compliance with the requirements of the ORSA and with Article 48 of the Framework Directive Proposal, as well as for the management decisions required as part of the risk and capital management to which the ORSA relates.

23. Article 44 (1) of the Framework Directive Proposal identifies what an undertaking is required to determine in the ORSA process:

"1. As part of its risk management system every insurance or reinsurance undertaking shall conduct its own risk and solvency assessment.

That assessment shall include at least the following:

(a) the overall solvency needs taking into account the specific risk profile, approved risk tolerance limits and the business strategy of the undertaking;

(b) the compliance, on a continuous basis, with the capital requirements, as laid down in Chapters VI, Sections 4 and 5 and with the requirements regarding technical provisions, as laid down in Chapter VI, Section 2.

(c) the extent to which the risk profile of the undertaking concerned deviates significantly from the assumptions underlying the Solvency Capital Requirement as laid down in Article 101 (3), calculated with the standard formula in accordance with Chapter VI, Section 4, Subsection 2 or with its partial or full internal model in accordance with Chapter VI, Section 4, Subsection 3.

24. The purpose of the ORSA is to ensure that undertakings have robust processes for assessing and monitoring their overall solvency needs, not to duplicate, validate or analyse in detail the parameterisation of the SCR calculation.

25. The ORSA is part of the risk management system. The written policy on risk management as referred to in Article 41 (3) of the Framework Directive Proposal should include a policy concerning the ORSA process.

26. The following sections include certain aspects that should be taken into account in the ORSA, but are not meant to be an exhaustive list.

The overall solvency needs

27. As mentioned before, the term "overall solvency needs" includes the assets necessary to cover the liabilities including technical provisions, the regulatory capital requirements – SCR and MCR – as well as the internal capital needs. Whereas the regulatory capital requirements can only be covered by eligible own funds, other elements of capital may be taken into account to cover an undertaking's internal capital needs.

28. Furthermore, Article 44 (2) of the Framework Directive Proposal states that:

2. For the purposes of point (a) of paragraph 1, the undertaking concerned shall have in place processes which enable it to properly identify and measure the risks it faces in the short and the long term and also to identify possible events or future changes in economic conditions that could have unfavourable effects on its overall financial standing. The

undertaking shall demonstrate the methods used to determine its overall solvency needs.

29. An undertaking should not only assess its current risks but also the risks it faces in the long term. That means that long term projections of the business which are a key part of any undertaking's financial planning, such as projections of business plans, economic balance sheet and profit and loss account, are required. These projections should feed into the ORSA in order to enable the undertaking to form an opinion on the future overall solvency needs and own funds. Suitable capital planning should include projections of capital requirement and own funds (e.g. raising new own funds). It is up to the undertakings to decide on reasonable assumptions, parameters, correlations or levels of confidence to be used in the projections. However, Level 3 may provide some guidance on the minimum contents supervisors should expect from the ORSA in this respect.
30. An undertaking should also identify and take into account external factors that could have an adverse effect on its overall solvency needs or its own funds. These external factors can be: changes in the economic conditions, changes in the legal environment, changes in the insurance market, technical developments that have an impact on the underwriting risk or any other event the crystallisation of which is sufficiently probable that it be considered by a prudent person.
31. When assessing its overall solvency needs, an undertaking should also take into account management actions that may be adopted by the undertaking in unfavourable economic conditions. Particular consideration should be given to whether these management actions will operate as planned under such unfavourable economic conditions.
32. In the SRP, supervisors may also challenge the bases for the projections and an undertaking should be prepared to explain the rationale for selecting them and demonstrate that its methods and practices are appropriate.

Compliance on a continuous basis

33. The undertaking is responsible for having sufficient eligible own funds to cover the MCR and the SCR on a continuous basis. The ORSA should include an assessment as to whether the undertaking holds sufficient eligible own funds determined in accordance with the Directive at any time over the business planning time horizon.
34. CEIOPS' interpretation of "on a continuous basis" in Article 44 (1) (b) of the Framework Directive Proposal is that it refers to compliance and not to the required assessment, i.e. the paragraph does not constitute an obligation to constantly recalculate the SCR and MCR. In order to ensure that the capital requirements are met at all times, the undertaking needs to have processes in place that enable it to estimate the changes in its capital requirements and eligible own funds' level since the last full solvency calculation. How often such a full calculation is to be performed will depend particularly on the volatility of the capital requirements and the own funds, as well as on the level of solvency. The undertaking should be able to justify the adequacy of

the frequency of the calculation taking into account its risk profile. A full calculation is in any case required if the risk profile changes significantly.

35. The assessment of the overall solvency needs should not only focus on the amount of own funds needed going forward, but also on the quality of the own funds, especially those needed to comply with the capital requirements, and the ability to raise more own funds.

Assessment of the risk profile

36. The assessment includes an analysis of the differences, if any, between the amount of own funds which the undertaking considers necessary for its business needs and the capital requirement the SCR generates.
37. There are a number of reasons why differences between internal capital needs and regulatory solvency capital requirement may exist, such as:
 - a) The undertaking may operate at a different confidence level for business purposes compared to the regulatory assumptions on which the SCR calculation is based. For instance, it may choose to hold own funds for rating purposes, which represents a higher confidence level than that used to calibrate the SCR.
 - b) The undertaking's risk profile may differ from the one implicit in the SCR. For instance, the undertaking's assessment of the capital needed to back a particular insurance risk might be different from the assessment on which the parameters of the SCR calculation are based or the undertaking's risk profile may include risks which are not covered by the SCR.
 - c) In the ORSA the undertaking may use a time horizon for its business planning purposes that differs from the time horizon underlying the SCR.
 - d) In the ORSA the undertaking may consider any agreed management actions that could influence the risk profile.
38. Although an undertaking, in performing its ORSA, may for its own business purposes use a confidence level or a time horizon that differs from that of the SCR calculation, it is also required to perform the internal calculation on the basis of a 99.5% confidence level and a one-year time horizon, in order to assess the deviation of its risk profile from the assumptions underlying the SCR calculation, as required by Article 44 (1) (c).
39. Under the ORSA an undertaking should use the parameters that in its opinion best reflect its individual risk situation.⁴

⁴ The Framework Directive Proposal allows undertakings to use entity-specific parameters when calculating the life, non-life and special underwriting risk modules. The use of these specific parameters is subject to supervisory approval.

40. Where the undertaking is using internal models, Article 44 (3) of the Framework Directive Proposal states that:

3. In the case referred to in point (c) of paragraph 1 when an internal model is used, the assessment shall be performed together with the recalibration that transforms the internal risk numbers into the Solvency Capital Requirement risk measure and calibration.

41. An internal model is in itself a tool for the ORSA. For an undertaking using an internal model to calculate the SCR, the ORSA should include a description of the role of the internal model in the integrated management of risk and capital needs. An undertaking should be able to justify the continued adequacy of the model compared with the risk profile of the undertaking.

42. When the internal model is calibrated for a different time horizon and/or a different level of confidence from the SCR standard formula, the ORSA should give information both on the internal capital needs identified for the undertaking's internal purposes and on the regulatory capital requirements.

The outcome of the ORSA

43. If the outcome of the ORSA is that the internal capital needs differ in either direction from the amount resulting from the SCR, the undertaking should explain the reasons and individually identify any impact on the calculation of the solvency capital requirement.

44. If the outcome from the ORSA is that the internal capital needs are higher than the regulatory capital, this does not automatically mean that the undertaking will have a capital add-on imposed by the supervisor. Supervisors will look into the reasons for the differences and discuss their views with the undertaking concerned before taking any decisions. For example, the use of a different time horizon or a different confidence level would not result in an add-on. Any changes the undertaking plans to introduce in order to reduce its risk profile as a consequence of the ORSA process would also be duly considered by supervisors. Before setting a capital add-on, supervisors would moreover not only take into account the ORSA results but also the full results of the SRP. Details on capital add-ons will be covered by a forthcoming CEIOPS Issue Paper.

45. Supervisors are not empowered to allow a reduction of the SCR as calculated in accordance with the standard formula if an undertaking demonstrates in its ORSA that the SCR calculation overestimates its risks. If the outcome from the ORSA is that the internal capital needs are considerably lower than the SCR, the undertaking may wish to consider whether it is appropriate to develop a partial or a full internal model and seek supervisory approval for its use in the calculation of the SCR.

Integration of the ORSA

46. Article 44 (4) of the Framework Directive Proposal states that:

4. The own risk and solvency assessment shall be an integral part of the business strategy and shall be taken into account on an ongoing basis in the strategic decisions of the undertaking.

47. As an integral part of the overall business strategy, an undertaking is required to have in place its own strategies for internal capital needs and all material risks to which it is exposed (such as underwriting, credit, market, liquidity, concentration and operational risks), as well as an appropriate policy for the use of risk mitigation and transfer arrangements (e.g. reinsurance and derivatives) that together manage and address overall solvency needs. The ORSA and the business strategy affect each other. When performing the ORSA, the undertaking should take into account the business strategy and any strategic decisions influencing the risk and overall solvency needs. In reverse, the administrative or management body needs to be aware of the implications strategic decisions have on the risk and overall solvency needs of the undertaking and to consider whether these effects are desirable and affordable. Any strategic decision that may affect the risk and/or own funds' position of the undertaking should be considered through the ORSA process before such a decision is taken.

Frequency of the ORSA

48. Article 44 (5) of the Framework Directive Proposal states that:

5. Insurance and reinsurance undertakings shall perform the assessment referred to in paragraph 1 regularly and without any delay following any significant change in their risk profile.

49. CEIOPS interprets the word "regularly" to mean at least annually in this context. The ORSA would also need to be performed within that period if an undertaking experiences a change in the risk and solvency profile that may impact the ORSA result in a way that the undertaking should be aware of. The undertaking should establish its own frequency of the assessment taking into account its own risk profile. It should be able to justify the adequacy of the frequency of the assessment.

Information on the result of the ORSA to supervisory authorities

50. Article 44 (6) of the Framework Directive Proposal states that:

6. The insurance and reinsurance undertakings shall inform the supervisory authorities of the results of each own risk and solvency assessment as part of the information reported under Article 35.

51. Information about the ORSA process and the outcome of the ORSA is also a supervisory tool that will be used, together with other items of the supervisory reporting, as part of the SRP, to enable supervisors to:
- a) Assess the ability of the undertaking to assess its overall solvency needs; and
 - b) To better understand the risks to which the undertaking is or may be exposed.
52. CEIOPS will give information on how it envisages supervisory reporting on the ORSA in its Level 2 advice/Level 3 measures on supervisory reporting which it will publish in a forthcoming Issues Paper.

ORSA – Principles and guidance for undertakings

53. This paper includes tentative ORSA principles and guidance addressed both to solo undertakings and to groups.
54. The principles should be applied in a proportionate manner having due regard to the nature, scale and complexity of the activities of the undertaking concerned.

Principles

55. The undertaking should have regard to the following principles when conducting its ORSA:

- A. The ORSA is the responsibility of the undertaking and should be regularly reviewed and approved by the undertaking's administrative or management body.
- B. The ORSA should encompass all material risks that may have an impact on the undertaking's ability to meet its obligations under insurance contracts.
- C. The ORSA should be based on adequate measurement and assessment processes and form an integral part of the management process and decision making framework of the undertaking.
- D. The ORSA should be forward-looking, taking into account the undertaking's business plans and projections.
- E. The ORSA process and outcome should be appropriately evidenced and internally documented as well as independently assessed.

Guidance

56. Further explanations and guidance regarding the principles defined above are set out below. These should not be read as mandatory requirements, but undertakings should nevertheless carefully consider the extent to which all or some of them are applicable to their specific situation.

A. The ORSA is the responsibility of the undertaking and should be regularly reviewed and approved by the undertaking's administrative or management body.

57. The undertaking's administrative or management body should approve and regularly review the assumptions, including any management actions, and parameters used in the ORSA and should also sign-off the results as it has the ultimate responsibility for the adequacy of the ORSA.

58. As the ORSA should form an integral part of the business strategy and be taken into account on an ongoing basis in the strategic decisions of the undertaking, it is imperative that the administrative or management body is actively involved in the review and challenge of the ORSA.

59. When relying on prospective management actions, an undertaking should understand the implications of taking such actions, including the financial effect, and take into consideration any preconditions that might affect the value of management actions as risk mitigants. The assessment should also address how any management actions would be enacted in times of financial stress.

60. The ORSA should set out details of any management actions assumed in the assessment and should not only explain and justify these actions but also provide an impact assessment of them, i.e. sensitivity testing of the key management actions.

61. The ORSA should take into account the risk appetite or level of confidence that the undertaking uses for internal purposes as regards the certainty with which its liabilities to policyholders will be met. This level of confidence may be different to the required regulatory level of confidence for the SCR.

B. The ORSA should encompass all material risks that may have an impact on the undertaking's ability to meet its obligations under insurance contracts.

62. The undertaking's ORSA should consider all risks that may lead to a material reduction in the current level of own funds or the protection offered to policyholders. The undertaking needs to give due consideration to the risks included in the calculation of the SCR, as well as the risks which are not or not fully captured in the SCR calculation. Areas considered should at least cover: underwriting, market, credit and operational risks, as well as any other material risks. Consideration should also be given to the impact of risk mitigation techniques, including reinsurance, any diversification effect

between risks (correlations), and to the actual loss-absorbing capacity of technical provisions and deferred taxes.

63. The undertaking's ORSA should include an assessment of the adequacy of the undertaking's governance system and take into consideration any risks that may arise from any inadequacy or deficiency.
64. The undertaking should, on an ongoing basis, gather information about current and future risks across all hierarchy levels, operational processes and functional areas. Systematic identification of risks includes an early and regular recognition, as well as a structured recording of any disruptive factors that may have an effect on the overall risk profile of an undertaking and the collection of important information on possible risk connections and dependent risk factors.
65. The ORSA should set out the assumptions used by the undertaking in assessing and aggregating risks. Where assumptions are different from those used in the SCR calculation, the differences and reasons for them should be clearly identified.
66. As a result of the measuring of the risks, any risks that do not correspond to the assumptions underlying the SCR as laid down in Article 101 of the Framework Directive Proposal or in accordance with its approved internal model, should be identified separately.
67. There are two main areas from where differences between the SCR and the undertaking's actual risk profile might arise: risks not considered in the standard formula and risks not adequately captured by the standard formula. The ORSA should address both areas.
68. The following risks are examples of risks not considered in the standard formula, but which should be considered in the ORSA, if they are material for the undertaking:
 - a) Liquidity risk;
 - b) Reputational risk;
 - c) Strategic risk.
69. The areas referred to in the following paragraphs should be considered as being amongst those where differences between the SCR and the undertaking's actual risk profile might arise, and therefore should be addressed in the ORSA by explanation of how they are taken into account, or why they are not relevant. This list is not exhaustive and an undertaking should identify all relevant areas in its ORSA.
70. The undertaking has specific risk characteristics of assets and liabilities; e.g., in the context of the standard formula, the factor-based approach to premium and reserve risk in non-life insurance only partially reflects the undertaking-specific profile of its non-life business (which is impacted e.g. by the specific type of products sold, or the sales policy of the undertaking).
71. Another example of inadequacy of the standard formula would be an insurance portfolio with a higher than average level of concentration in one or more risk factors (e.g. property policies in the same region or death

protection sold to a high number of impaired lives, for instance due to poor underwriting or adverse selection). Also, a niche player is likely to have a materially different risk exposure than the one reflected in the calibration of the standard formula. These cases could, of course, be mitigated by the use of undertaking-specific parameters (Article 104 (7) of the Framework Directive Proposal).

72. Complex relationships between different risks may also give rise to dependencies in the risk profile. The most obvious of these is the relationship between non-life underwriting risk and contingent credit risk. The circumstances that cause increased insurance losses, and therefore an increase in reinsurance recoveries, may in turn have a negative effect on the creditworthiness of the reinsurer.
73. Another example concerns the relationship between underwriting risk and market risk – an inappropriate investment policy may expose certain types of undertakings to increased investment losses (from holdings in bonds or equities) at a time of increased claims, if the causes of the claims affect the value of the investments.
74. Where the undertaking is relying on systems and controls in order to mitigate risks, it should consider the effectiveness of those systems and controls in a stress situation.

C. The ORSA should be based on adequate measurement and assessment processes and form an integral part of the management process and decision making framework of the undertaking.

75. The ORSA should be proportionate in its sophistication and depth to the nature, scale and complexity of the undertaking's business.
76. The ORSA should:
 - a) Reflect all assets and liabilities, including intra-group arrangements;
 - b) Take into consideration off-balance sheet items, for instance ancillary own funds;
 - c) Reflect the undertaking's management practices, systems and controls;
 - d) Use a valuation basis that is consistent throughout the assessment.
77. An undertaking should be able to explain and justify:
 - a) The methodology and key assumptions used in the assessment of each category of risk;
 - b) The results of the assessment, including the sensitivity of the results to any assumptions made;
 - c) The appropriateness of the assessment or modelling approach adopted, including how it captures all risks material to its business;
 - d) The sources of data it has used in its ORSA and the systems and controls around it;

- e) The approach to dealing with parameter uncertainty and fluctuations.
78. The ORSA should include an assessment, both quantitative and qualitative, of the own funds held by the undertaking, including the changes expected in financial stress situations.
 79. An undertaking's own funds should normally be restricted to its own resources. Where the undertaking is relying on resources outside its direct control these should only be included to the extent that it has a right to call on those resources and the provider has an irrevocable obligation to provide those resources.
 80. Although it would be practical that the valuation bases used are consistent with Solvency II principles, it would be for the undertaking to determine the valuation bases to be used in its ORSA. These may therefore differ from those required to be used for the purposes of the SCR calculation.
 81. Undertakings should carry out a broad reconciliation of key parts of any balance sheet items used in the ORSA with the corresponding entries from financial statements.
 82. Undertakings should also provide an explanation within the ORSA of any differences between accounting and economic capital measures.
 83. The results of the ORSA and the insights gained in the process should be taken into account in the strategy formulation, own funds' allocation, product development, governance, and decision making of the undertaking.

D. The ORSA should be forward-looking, taking into account the undertaking's business plans and projections.

84. The assessment should reflect both the undertaking's desire to fulfil its business objectives and its responsibility to meet liabilities to policyholders. This means that the ORSA should demonstrate that the undertaking holds sufficient financial resources to be able to make planned investments and take on new business (within an appropriate planning horizon).
85. The undertaking should take into account any risks that it considers it may be exposed to in the future with a reasonable degree of probability, either through internal factors, such as a change in business plan, or through external factors, such as certain possible events with negative effects or a deterioration of economic conditions.

E. The ORSA process and outcome should be appropriately evidenced and internally documented as well as independently assessed.

86. The undertaking should describe how the ORSA is used in the management of the business. In particular, the undertaking should comment on the extent

to which it has embedded the ORSA within its strategic, operational and risk management processes.

87. Documentation should at a minimum include:

- a) A description of the areas that are included in the ORSA;
- b) A description of the process of conducting the ORSA and the responsibilities of key personnel involved in the process;
- c) Stress tests used and their results;
- d) The amount of overall solvency needs and the financial condition of the undertaking, signed-off by the administrative or management body;
- e) Any strategies for raising additional own funds where necessary;
- f) A description of the independent assessment and the results of the last assessment;
- g) Frequency and contents of the internal reporting.

88. The undertaking should ensure that the ORSA can be easily reviewed by the supervisory authority as part of the SRP. Documentation should be compiled in a way that can easily be shared with the supervisory authority. The reporting requirements to supervisors will be developed in another paper which CEIOPS intends to publish soon.

89. The administrative or management body shall ensure that a regular assessment of the ORSA process is performed by persons that have not been responsible for the part of the ORSA process they review and who are thus independent in their assessment. The assessment may be conducted by an internal or external auditor or any other skilled internal or external function, as long as they are independent in their assessment task. The conclusions drawn from the independent assessment should be reported to the administrative or management body in order to enable it to act on this information if necessary.