MAS consults on Enterprise Risk Management ("ERM") for insurers

4 February 2013

Key messages at a glance

- First reporting for Tier 1 insurers by 30 April 2014 and Tier 2 insurers by 30 April 2015
- Requirements are close to ORSA requirements under Solvency 2
- ORSA was a challenging area for Solvency 2 – see page 2 for some of the main challenges

Following the MAS' consultation paper on RBC 2 in August 2012, the expected consultation paper on ERM has now been published and will close for comments on 28 February 2013.

The requirements published are not in the form of detailed rules, but rather principles close to the Own Risk and Solvency Assessment ("ORSA") Requirements under Solvency 2. The principle-based approach by MAS gives insurers the ability to tailor and enhance their risk management framework in line with the nature and complexity of their business.

When must the requirements be implemented?

The proposed date for implementation is 1 January 2014.

Tier 1 insurers are expected to submit a first ORSA report to MAS by 30 April 2014, Tier 2 insurers by 30 April 2015.

ORSA is required to be performed at least annually. Tier 1 insurers are to submit an ORSA report every year, and Tier 2 insurers every three years.

Members of groups are allowed to rely on their group ERM framework provided that it is relevant and appropriate and this can be evidenced at the local level.

What is expected by the MAS?

MAS expects each insurer to enhance its risk management (enterprise-wide) practices in identifying, assessing, measuring, monitoring, controlling and mitigating risks, in terms of:

- having a holistic view of risks that impact the business;
- putting in place risk management policies and practices that ensure long term business viability and which correspond with the company's goals, strategy and capital resources;
- identifying and managing interdependencies between risks;
- embedding risk management into strategic management actions and capital planning;
- determining financial resources considering risk tolerance and business strategy, and assessing the quality of its capital resources; and
- performing a regular continuity analysis over the business planning period (3 to 5 years), and linking the current solvency position to the future business plan.

MAS articulates that ERM involves regular self-assessment of all reasonably foreseeable and material risks and that the ERM framework should be consistent with the nature, scale and complexity of the business and the risks of the organisation. Attention must be dedicated to linking risk management and the management of capital adequacy and solvency.

Key Challenges

Some of the main challenges for ORSA implementation experienced by our clients are:

- embedding risk management in strategic decisions and operational processes;
- assessing the own risk and solvency position;
- implementing forward looking aspects such as continuity analysis and reverse stress testing; and
- setting up comprehensive, but effective risk management reporting.

Next steps to take

Akin to the Solvency 2 ORSA requirements, the implementation for ERM is also very company-specific and the majority of companies already have risk management processes in place. The challenge is for the insurers to translate these ERM principles into a suitable tailored framework, where possible through enhancing existing processes.

Typically, insurers should start by assessing existing processes and identifying gaps to develop a company specific project plan and allocate resources needed.

Contact us

If you would like further information in relation to the issues outlined above, please call your usual PwC contact or any of the individuals listed below:

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Key challenges

- Develop a robust, comprehensive and relevant ERM framework
- Integrate ERM in daily operational and decision taking processes
- Develop company specific assessment of current and future risk and solvency situation, including appropriate modelling and quantification
- Efficient implementation of requirements in the company by making good use of existing policies and procedures

How can we help?

- Local and regional PwC teams with extensive experience supporting insurance firms and other financial institutions with changes in solvency and risk management requirements (including Solvency 2 ORSA). For instance:
- Conducting gap analysis and assisting in translating the results into a company specific action plan
- Board and management training on ERM
- Developing the ORSA report, assisting with risk appetite, modelling and Management Information
- Assisting with appropriate and tailored solutions

Appendix

Proposals by the MAS

1 MAS proposes to apply the ERM requirements to all registered insurers, except captive insurers and marine mutual insurers.

2 For an insurer which is part of a group that maintains a group-wide ERM framework, MAS proposes to allow the insurer to rely on its group's ERM framework to meet the ERM requirements, subject to the insurer's own assessment of the relevance of the risks identified and the appropriateness and adequacy of techniques employed to measure the risks.

3 MAS proposes to require each insurer to establish an ERM framework which provides for the identification and quantification of risks under a sufficiently wide range of outcomes, using techniques which are appropriate to the nature, scale and complexity of the risks the insurer bears and are adequate for risk and capital management, and for solvency purposes.

The ERM framework shall also identify and address all reasonably foreseeable and material risks to which the insurer is, or is likely to become, exposed. Such risks shall include, at a minimum:

a) insurance risk
b) market risk
c) credit risk
d) operational risk
e) liquidity risk; and
f) additional risks arising due to membership of a group (if applicable).

The ERM framework shall also be supported by accurate documentation, providing detailed descriptions and explanations of the risks covered, the measurement approaches used and the key assumptions made.

4 MAS proposes to require each insurer to establish and maintain a risk tolerance statement which sets out its overall quantitative and qualitative risk tolerance limits, taking into account its financial strength and long term business goals.

5 MAS proposes to require each insurer to have a risk management policy which, at a minimum encompasses the following areas:

a) the insurer's policy for managing the risks to which it is exposed, including underwriting and investment risks;
b) the insurer's policies towards risk retention, risk management strategies including reinsurance and the use of derivatives, diversification and asset-liability management. For insurance risks, particular attention should be paid to risk retention and risk transfer, as well as take into account of the effectiveness of risk transfer under scenarios of financial distress;
c) the insurer's policy regarding the processes and methods for monitoring risk; and
d) the relationship between its risk management policy, of the insurer's risk tolerance limits, its management of capital, and its corporate objective and strategy (which takes into account current circumstances).

6 MAS proposes to require each insurer to ensure that its ERM framework is responsive to changes in its risk profile, and include mechanisms to incorporate new risks and new information on a regular basis. A review of the ERM framework to ensure this should be carried out at least every quarter.

In addition, there should be in place a feedback loop to enable the insurer to monitor and respond in a timely manner to changes in its risk profile.

7 MAS proposes to require each insurer to perform its ORSA, at least annually, to assess the adequacy of its risk management, as well as its current, and projected future, solvency position. When undertaking its ORSA, each insurer will be required to document the rationale of the decisions, considerations and assumptions made; calculations related to its decisions, considerations and assumptions; and action plans arising from its ORSA.

The ORSA shall encompass all reasonably foreseeable and relevant material risks including, at a minimum:

a) insurance risk
b) credit risk
c) market risk
d) operational risk
e) liquidity risk
f) additional risks arising due to membership of a group, if applicable.

The ORSA shall also identify the relationship between risk management and the level and quality of financial resources that is needed and available.

8 MAS proposes to require each insurer, as part of its ORSA, to:

a) determine the overall financial resources it needs to manage its business given its own risk tolerance and business plans, and to demonstrate that regulatory requirements are met;
b) base its risk management actions on consideration of its economic capital, regulatory capital requirements and financial resources; and
c) assess the quality and adequacy of its capital resources to meet regulatory and economic capital requirements.

9 MAS proposes to allow insurers to adopt a simplified approach to economic capital calculations if based on the nature, scale and complexity of their business and risks, the insurer deems this to be appropriate. The reasons should be clearly articulated and justified in the ORSA.

10 MAS proposes to require an insurer, as part of the continuity analysis, to identify likely causes that may result in its business failure through the use of reverse stress testing and take the necessary actions to manage this risk. "Business failure" is defined as:

a) the insurer's solvency position falling below any regulatory capital requirement;
b) the insurer's capital position falling below any internal target; or
c) the insurer being wound up.

As part of the insurer's identification of causes for business failure, it shall maintain contingency plans and procedures for use in a going concern or winding-up situation, to identify precautionary, countervailing and off-setting measures that could be taken.

11 MAS proposes to require a Tier 1 insurer to submit its latest ORSA report, together with the minutes of the Board's deliberation and approval of the report, on an annual basis. The first report is to be submitted by 30 April 2014 and annually thereafter. For a Tier 2 insurer, the first report is to be submitted by 30 April 2015 and by 30 April of every third year thereafter (i.e. the next report is to be submitted by 30 April 2018).

12 MAS proposes to extend the ERM requirements laid out in proposals 2 to 11 to all insurance groups. Each of these entities' group ERM framework must take into account risks arising from all parts of the group, including non-insurance entities (regulated or unregulated) and partly-owned entities.

MAS also proposes to require such insurance groups to submit a Group ORSA on an annual basis, in addition to the ORSA report submitted by the local registered insurer. The Group ORSA report shall include identification of material risks, economic and regulatory capital calculations and continuity analysis from a group-wide perspective, whereas the registered insurer's ORSA report comes from a solo perspective.

Deliberation of the Group ORSA report is required by the Board in control of the insurance group.

13 MAS proposes to issue a new Notice on ERM and implement the requirements from 1 January 2014.