NAIC National Association of Insurance Commissioners

Date: 8/25/20

*Joint Conference Call*

**RISK-FOCUSED SURVEILLANCE (E) WORKING GROUP and**
**ORSA IMPLEMENTATION (E) SUBGROUP**
**Tuesday, September 1, 2020**
**1:00 p.m. – 2:00 p.m. Central Time**

**ROLL CALL**

**Risk-Focused Surveillance Working Group:**

| | | | |
|---|---|---|---|
| Justin Schrader, Chair | Nebraska | John Sirovetz | New Jersey |
| Amy Malm, Vice Chair | Wisconsin | Mark McLeod | New York |
| Richard Ford | Alabama | Jackie Obusek/Monique Smith | North Carolina |
| Susan Bernard | California | Dwight Radel/Tracy Snow | Ohio |
| William Arfanis/Kathy Belfi | Connecticut | Eli Snowbarger | Oklahoma |
| Carolyn Morgan/Virginia Christy | Florida | Ryan Keeling | Oregon |
| Cindy Andersen/Eric Moser | Illinois | Joe DiMemmo | Pennsylvania |
| Roy Eft | Indiana | Jack Broccoli | Rhode Island |
| Daniel Mathis | Iowa | Johanna Nickelson | South Dakota |
| Stewart Guerin | Louisiana | Amy Garcia | Texas |
| Vanessa Sullivan | Maine | Jake Garn | Utah |
| Dmitriy Valekha | Maryland | Dan Petterson | Vermont |
| Judy Weaver | Michigan | David Smith | Virginia |
| Debbie Doggett/Shannon Schmoeger | Missouri | Steve Drutz | Washington |
| Patricia Gosselin | New Hampshire | | |

NAIC Support Staff: Bruce Jenson/Jane Koenigsman

**ORSA Implementation Subgroup:**

| | | | |
|---|---|---|---|
| Kathy Belfi, Co-Chair | Connecticut | Doug Bartlett/Pat Gosselin | New Hampshire |
| Mike Yanacheak, Co-Chair | Iowa | Victor Agbu/Edward Kiffel | New York |
| Susan Bernard | California | David Cook/Jeff Lehr | Ohio |
| Robert Ridenour | Florida | Kim Rankin | Pennsylvania |
| Cindy Andersen/Eric Moser | Illinois | Mike Arendall | Texas |
| Debbie Doggett | Missouri | Amy Malm | Wisconsin |
| Justin Schrader/Rhonda Ahrens | Nebraska | | |

NAIC Support Staff: Bruce Jenson/Eli Russo

**AGENDA**

1. Discuss Proposed Revisions to Update ORSA Review Guidance—*Justin Schrader (NE)*
   - Overview of Proposed Changes — Attachment A
   - Proposed Financial Analysis Handbook Revisions — Attachment B
   - Proposed Financial Condition Examiners Handbook Revisions — Attachment C

2. Discuss Any Other Matters Brought Before the Working Group—*Justin Schrader (NE)*

3. Adjournment

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# Attachment A

## *Overview of Proposed Changes*

# Overview of ORSA Review Guidance Revisions

Joint RFSWG/ORSA Subgroup Call

Sep. 1, 2020

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# Project Background – Peer Review Results

- Level of documentation varied depending on which review template was used (Handbook vs. Supplemental)
- Resulting documentation was, at times, very lengthy and not always effective in sharing across states
- Reviews did not always provide clear documentation of conclusions and feedback to company
- ORSA review findings and company key risks not always fully incorporated into ongoing analysis work
- Ambiguity in how review should be used in the financial exam and how results should be communicated back

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## ORSA Template Revisions - Overall

- Moving supplemental guidance into Handbook and simplifying process to coalesce around one standard review template
- Removing Risk Maturity Model guidance and ratings from review template and encouraging more narrative assessment
  - RMM guidance will remain in Exam Handbook as part of overall ERM assessment, but not incorporated into annual review
- Adding appendices in order to provide clearer communication to the company and the exam function

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## ORSA Template Revisions - By Section

| Background | Section I | Section II | Section III | Appendixes |
|---|---|---|---|---|
| • Outlines background information important to understanding and assessing each ORSA filing | • Removes quantitative maturity rating from individual principles<br>• Replaces with key considerations | • Clarified focus on relevant key risks<br>• No longer organized by BR classification<br>• Creates more clear linkage to FA work | • Documentation broken out to discuss key elements of group risk capital | • App. A - Summarize feedback to company<br>• App. B - Suggested follow-up procedures for exam function |

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# Analysis Handbook Updates

- Includes detailed instructions for completing the review template
  - Step by step guidance and considerations for completing review
- Outlines key considerations for understanding and assessing each section of the report
  - Key considerations replace Risk Maturity Model ratings and supporting guidance
- Creates clearer linkage to ongoing financial analysis work
  - Documents how key risks from ORSA are incorporated into Holding Company and/or legal entity analysis documentation

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# Exam Handbook Updates

- Review template removed from FCEH as exam team not expected to utilize template for documentation
  - Results from examination testing and validation to be incorporated into existing reporting mechanism (SRM)
- Guidance focuses on how the Lead State's review can influence examination procedures
- Incorporated additional concepts from ORSA Guidance Manual and supplemental guidance
- Clearer expectation to perform validation and testing procedures and document results via the SRM

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# Attachment B

## *Proposed Financial Analysis Handbook Revisions*

# ORSA Review Template

**Group/Insurer:** ____________________________
**Group Code/Cocode:** ____________________________
**Valuation Date:** ____________________________
**Submission Date:** ____________________________

**General Instructions:**

This template is intended to be used to document a review and assessment of the ORSA Summary Report by the lead/domestic state. Regulators should document the results of their annual review of the ORSA and utilize the appendixes to track and communicate feedback to the company and procedures for regulatory follow-up. See VI.E. Group-Wide Supervision – Enterprise Risk Management Process Risks Guidance for additional guidance in completing this template.

| Prepared/Reviewed By: | Date: |
|---|---|
| | |
| | |
| | |

| | |
|---|---|
| **Date of Last Exam:** | |
| **Date of Next Exam:** | |

 

# Background Information

Summarize and assess background information provided in the report, where available. Key documentation elements are presented below.

1. **Attestation**:

2. **Entities in Scope:**

3. **Accounting Basis:**

4. **Key Business Goals:**

5. **Changes from Prior Filing(s):**

6. **Planned ERM Enhancements:**

# Section I – Description of the Insurer's ERM Framework

Summarize and assess key information from Section I of the ORSA Summary Report for each of the five principles of a risk management framework.

1. **Risk Culture and Governance:**

2. **Risk Identification and Prioritization:**

3. **Risk Appetite, Tolerances and Limits:**

4. **Risk Management and Controls:**

5. **Risk Reporting and Communication:**

**Overall Section 1 Assessment**—After reviewing and considering each principle individually, develop an overall assessment of the group's/insurer's risk management framework including any concerns or areas requiring follow-up investigation or communication:

 

## Section II – Insurer Assessment of Risk Exposures

Prepare documentation summarizing a review and assessment of information provided on the reasonably foreseeable and relevant material risks of the insurer/group.

**THE FOLLOWING TABLE SHOULD BE COMPLETED FOR EACH KEY RISK**

| | |
|---|---|
| **Risk Title/Description** | |
| **Branded Risk(s)** | |
| **Controls/Mitigation** | |
| **Risk Limits** | |
| **Assessment (QT/QL)** | |
| **Normal Exposure** | |
| **Stress Scenario(s)** | |
| **Stressed Exposure** | |
| **Inclusion on GPS/IPS** | |
| **Regulator Review & Assessment:** | |
| | |

**Overall Section 2 Assessment**—After reviewing and considering each key risk individually, develop an overall conclusion regarding the group's/insurer's process to assess key risk exposures including any concerns or areas requiring follow-up investigation or communication:

# Section III – Assessment of Risk Capital and Prospective Solvency

Prepare documentation summarizing a review and assessment of key elements of the risk capital and prospective solvency process as follows.

1. **Discussion of Capital Metric(s) Used:**

2. **Group Risk Capital (GRC) – By Risk and In Aggregate:**

3. **Impact of Diversification Benefit:**

4. **Available Capital:**

5. **Excess Capital:**

6. **Impact of Stresses on GRC:**

7. **Governance and Validation:**

8. **Prospective Solvency Assessment:**

**Overall Section III Assessment**—After reviewing and considering each of the key elements individually, develop an overall assessment of the risk capital and prospective solvency of the insurer/group including any concerns or areas requiring follow-up investigation or communication:

## Appendix A – Feedback to Insurer

Feedback to the insurer on the ORSA Summary Report is critical for the compliance and effectiveness of future filings. The purpose of this form is to help the lead/domestic state gather and provide constructive and practical feedback to the insurer.

**Positive Attributes:**
1.
2.
3.

**Constructive Feedback:**
1.
2.
3.

**Requests for Additional Information:**
1.
2.
3.

 

## Appendix B – Recommended Exam Procedures/Areas for Follow-up Investigation

In completing a review of the ORSA Summary Report, the lead state/domestic regulator should consider whether certain elements could benefit from verification/testing in an examination or additional monitoring and follow-up investigation by the financial analyst. Such procedures and issues can be accumulated here for communication and tracking.

**Background Information**
1.
2.
3.

**Section I - ERM Framework**
1.
2.
3.

**Section II - Risk Assessment**
1.
2.
3.

**Section III - Risk Capital and Prospective Solvency**
1.
2.
3.

 

## Introduction

The process for assessing enterprise risk management (ERM) within the group will vary depending upon its structure and scale. Approximately 90 percent of the U.S. premium is subject to reporting an annual Own Risk Solvency ~~assessment~~ Assessment (ORSA) Summary Report. However, all insurers are subject to an assessment of risk management during the risk-focused analysis and examination, and this review is a responsibility of the lead state. In addition, all groups are required to submit the Form F - Enterprise Risk Report under the requirements of the NAIC *Insurance Holding Company System Regulatory* Act (#440). In addition, both the ORSA Summary Report and the Form F are subject to the supervisory review process, which contemplates both off-site and on-site examination of such information proportionate to the nature, scale and complexity of the insurer/group's risks. Those procedures are discussed in the following two sections. In addition, any risks identified throughout the entire supervisory review process are subject to further review by the lead state in either the periodic meeting with the insurer/group and/or any targeted examination work. When reviewing the ORSA and Form F, the lead state analyst should consider consistency between the documents, as well as information provided in the Corporate Governance Annual Disclosure.

## ORSA Summary Report

The NAIC *Risk Management and Own Risk and Solvency Assessment Model Act* (#505) requires insurers above a specified premium threshold, and subject to further discretion, to submit a confidential annual ORSA Summary Report. Model #505 gives the individual insurer and the insurance group discretion as to whether the report is submitted by each individual insurer within the group or by the insuranc~~er~~e group as a whole (See the NAIC *Own Risk Solvency Assessment Guidance Manual* for further discussion).

- **Lead State:** In the case where the insurance group chooses to submit one ORSA Summary Report for the group, it must be reviewed by the lead state. The lead state is to perform a detailed and thorough review of the information and initiate any communications about the ORSA with the group. The suggestions below set forth some possible considerations for such a review. At the completion of this review, the lead state should prepare a thorough summary of its review, which would include an initial assessment of each of the three sections. The lead state should also consider and include key information to share with other domestic states that are expected to place significant reliance on the lead state's review. The lead state should share the analysis of ORSA with other states that have domestic insurers in the group. The group ORSA review and sharing with other domestic states should occur within 120 days of receipt of the ORSA filing.

- **Non-Lead State:** Non-lead states are not expected to perform an in-depth review of the ORSA, but instead rely on the review completed by the lead state. The non-lead states' review of ~~an~~the lead state's ORSA review should be performed only for the purpose of having a general understanding of the work performed by the lead state, and to understand the risks identified and monitored at the group-level so the non-lead state may better monitor and communicate to the lead state when its legal entity could affect the group. Any concerns or questions related to information in the ORSA or group risks should be directed to the lead state.

- **Single Insurer ORSA:** In the case where there is only one insurer within the insurance group, or the group decides to submit separate ORSA Summary Reports for each legal entity, the domestic state is to perform a detailed and thorough review of the information, which would include an initial assessment of each of the three sections and initiate any communications about the ORSA directly with the legal entity. Such a review should also be shared with the lead state (if applicable) so it can develop an understanding of the risks within the entire insurance group. Single insurer ORSA reviews should be completed within 180 days of receipt of the ORSA filing.

 

*Throughout a significant portion of the remainder of this document, the term "insurer" is used to refer to both a single insurer for those situations where the report is prepared by the legal entity, as well as to refer to an insurance group. However, in some cases, the term group is used to reinforce the importance of the group-wide view. Similarly, throughout the remainder of this document, the term "lead state" is used before the term "analyst" with the understanding that in most situations, the ORSA Summary Report will be prepared on a group basis and, therefore reviewed by the lead state.*

## Background Information

To understand the appropriate steps for reviewing the ORSA Summary Report, regulators must first understand the purpose of the ORSA. As noted in the *ORSA Guidance Manual*, the ORSA has two primary goals:

1. To foster an effective level of (ERM) at all insurers, through which each insurer identifies, assesses, monitors, prioritizes and reports on its material and relevant risks identified by the insurer, using techniques that are appropriate to the nature, scale and complexity of the insurer's risks, in a manner that is adequate to support risk and capital decisions
2. To provide a group-level perspective on risk and capital, as a supplement to the existing legal entity view.

In addition, separately, the *ORSA Guidance Manual* discusses the regulator obtaining a high-level understanding of the insurer's ORSA~~,~~ and discusses how the ORSA Summary Report may assist the commissioner in determining the scope, depth and minimum timing of risk-focused analysis and examination procedures.

There is no expectation with respect to specific information or specific action that the lead state regulator is to take as a result of reviewing the ORSA Summary Report. Rather, each situation is expected to result in a unique ongoing dialogue between the insurer and the lead state regulator focused on the key risks of the group. For this reason, as well as others, the lead state analyst may want to consider ~~including in its initial~~additional support in the form of a broader review team as necessary in reviewing ~~of~~ the ORSA Summary Report, subject to the confidentiality requirements outlined in statute. In reviewing the final ORSA filing prior to the next scheduled financial examination, the analyst should consider inviting the lead state examiner ~~or any other individual acting under the authority of the commissioner or designated by the commissioner with special skills and subject to confidentiality~~to participate on the review team. Regardless of which individuals are involved on a review team, the 120-day or 180-day timeliness standards are applicable to the review. Additionally, the lead state analyst and examiner may want to include ~~them~~ the review team in ~~possible~~ ongoing dialogues with the insurer since the same team will be part of the ongoing monitoring of the insurer and an ORSA Summary Report is expected to be at the center of the regulatory processes. ~~A joint review such as this prior to the lead state analyst documenting its summary of the ORSA Summary Report may be appropriate.~~

These determinations can be documented as part of each insurer's ongoing supervisory plan. However, the *ORSA Guidance Manual* also states that each insurer's ORSA will be unique, reflecting the insurer's business model, strategic planning and overall approach to ERM. As regulators review ORSA Summary Reports, they should understand that the level of sophistication for each group's ERM program will vary depending upon size, scope and nature of business operations. Understandably, less complex organizations may not require intricate processes to possess a sound ERM program. Therefore, regulators should use caution before using the results of an ORSA review to modify ongoing supervisory plans, as a variety of practices may be appropriate depending upon the nature, scale and complexity of each insurer.

~~Collectively, the goals above are the basis upon which the guidance is established. However, the ORSA Summary Report will not serve this function or have this direct impact until the lead state becomes fairly familiar and comfortable with evaluating each insurer's report and its processes. This could take more than a couple of years to occur in practice, since the lead state would likely need to review at least one or two ORSA Summary Reports to fully understand certain aspects of the processes used to develop the report.~~

## General Summary of Guidance for Each Section

The guidance that follows is designed to assist the lead state analyst in the review of the ORSA and to allow for effective communication of analysis results with the non-lead states. It is worth noting that this guidance is expected to evolve over the years, with the first couple of years focused on developing a general understanding of ORSA and ERM. It should be noted that each of the sections can be informative to the other sections. As an example, Section II affords an insurer the opportunity to demonstrate the robustness of its process through its assessment of risk exposure. In some cases, it's possible the lead state analyst may conclude the insurer did not summarize and include information about its framework and risk management tools in Section I in a way that allowed the lead state analyst to conclude ~~it was at Level 5 (defined below)~~on effectiveness, but in practice by review of Section II, ~~it appears to meet the level~~such a conclusion was able to be reached. Likewise, the lead state analyst may assess Section II as ~~Level 5~~effective but may be unable to see through Section III how the totality of the insurer's system is ~~Level 5~~effective because of a lack of demonstrated rigor documented in Section III. Therefore, the assessment of each section requires the lead state analyst to consider other aspects of the ORSA Summary Report. This is particularly true of Section I, because as discussed in the following ~~page (or~~ paragraphs~~)~~, the other two sections have very distinct objectives, whereas the assessment of Section I is broader.

**Background Information** procedures are provided to assist the regulator in gaining an overall understanding of the ORSA Summary Report and assessing compliance with reporting requirements in several critical areas.

**Section I** procedures are focused on assessing the insurer's ~~maturity level with respect to its~~ overall risk management framework. The procedures are presented as considerations to be taken into account when reviewing and assessing an insurer's implementation of each of the risk management principles highlighted in the NAIC's *ORSA Guidance Manual*. ~~The maturity level may be assessed through a number of ways, one of which is through the incorporation of concepts developed within the Risk and Insurance Management Society's (RIMS) Risk Maturity Model (RMM). While insurers or insurance groups may utilize various frameworks in developing, implementing and reporting on their ORSA processes (e.g., COSO Integrated Framework, ISO 31000, IAIS ICP 16, other regulatory frameworks, etc.), elements of the RMM have been incorporated into this guidance to provide a framework for use in reviewing and assessing ERM/ORSA practices. However, as various frameworks may be utilized to support effective ERM/ORSA practices, lead state regulators should be mindful of differences in frameworks and allow flexibility in assessing maturity levels. The RMM, which is only one of a number of processes that may be used to determine maturity levels, provides a scale of six maturity levels upon which an insurer can be assessed. The six maturity levels can generally be defined as follows:~~

~~Level 5: Risk management is embedded in strategic planning, capital allocation and other business processes and is used in daily decision-making. Risk limits and early warning systems are in place to identify breaches and require corrective action from the board of directors or the appropriate committee thereof (hereafter referred to as the "board" for this chapter) and management.~~

- ~~Level 4: Risk management activities are coordinated across business areas and tools and processes are actively utilized. Enterprise-wide risk identification, monitoring, measurement and reporting are in place.~~
- ~~Level 3: The insurer has risk management processes in place designed and operated in a timely, consistent and sustained way. The insurer takes action to address issues related to high-priority risks.~~
- ~~Level 2: The insurer has implemented risk management processes, but the processes may not be operating consistently and effectively. Certain risks are defined and managed in silos, rather than consistently throughout the organization.~~
- ~~Level 1: The insurer has not developed or documented standardized risk management processes and is relying on the individual efforts of staff to identify, monitor and manage risks.~~
- ~~Level 0: The insurer has not recognized a need for risk management, and risks are not directly identified, monitored or managed.~~

~~The guidance developed for use in this Handbook integrates the concepts of RIMS maturity level scale of the RMM with the general principles and elements outlined in Section I of the *ORSA Guidance Manual* to assist lead state regulators in reaching an overall assessment of the maturity of an insurer's risk management framework.~~ In assessing implementation, regulators should consider whether ~~T~~the design of ERM/ORSA practices ~~should~~ appropriately reflect the nature, scale and complexity of the insurer. ~~Lead state regulators should understand the level of maturity that is appropriate for the company based on its unique characteristics. Attainment of "Level 5" level maturity for ERM/ORSA practices is not appropriate, nor should be expected, for all insurers or for all components of the framework.~~

**Section II** takes a much different approach. It provides guidance to allow the lead state analyst to better understand the range of practices they may see in ORSA Summary Reports. However, such practices are not intended to be requirements, as that would eliminate the "Own" aspect of the ORSA and defeat its purpose. As such, analysts should not expect or require insurers to organize or present their risks in a particular manner (i.e. by branded risk classification). Rather, the guidance can be used in a way to allow the lead state analyst to better understand the information in this section. Section II guidance has been developed around reviewing key risks assessed by the ~~company~~insurer, evaluating information provided on the assessment and mitigation of those risks and classifying them within the nine branded risk classifications ~~contained elsewhere in this~~outlined in the Handbook, which are used as a common language in the risk-focused surveillance process for ongoing tracking and communication. As such, the analyst should attempt to classify each key risk assessed by the insurer into a branded risk classification(s) for incorporation into general analysis documentation (IPS or GPS) as appropriate. The branded risk classifications are intentionally broad in order to allow almost any risk of a company to be tracked within one or more categories, but the analyst may also use an "Other" classification as necessary to track exposures.~~The primary reason for utilizing this approach is that it is not uncommon for insurer's to identify within their ORSA Summary Reports, many of the same types of risks, therefore the lead state analyst can leverage this information in their analysis of the insurer. However, lead state regulators should not restrict their focus to only the nine branded risk classifications; as such an approach may not encourage independent judgment in understanding the risk profile of the insurer. Therefore, the reference to the nine branded risk classifications provides a framework to organize the lead state's summary, but it should not discourage regulators from documenting other risks or excluding branded risk categories that are not relevant. From this standpoint, Section II will also provide regulators with information to better understand current insurance market risks and changes in those risks as well as macroeconomic changes and the impact they have on insurers risk identification and risk management processes.~~

**Section III** is also unique in that it provides a specific means for assisting the lead state analyst in evaluating the insurer's determinations of the reasonableness of its group capital and its prospective solvency position on an ongoing basis. Section III of the ORSA Summary Report is intended to be more informative regarding capital than other traditional methods of capital assessment since it~~s~~ sets forth the amount of capital the group determines is reasonable to sustain its current business model rather than setting a minimum floor to meet regulatory or rating agency capital requirements.

## Background Information

The *ORSA Guidance Manual* encourages discussion and disclosure of key pieces of information to assist regulators in reviewing and understanding the ORSA Summary Report. As such, the following considerations are provided to assist the regulator in reviewing and assessing the information provided in these areas.

- **Attestation** – The report includes an attestation signed by the Chief Risk Officer (or other executive responsible for ERM oversight) indicating that the information presented is accurate and consistent with ERM reporting shared with the Board of Directors (or committee thereof).
- **Entities in Scope** – The scope of the report is clearly explained and identifies all insurers covered. The scope of a group report also indicates whether material non-insurance operations have been covered. The lead state analyst should utilize Schedule Y and other related tools/filings to verify that all appropriate entities are accounted for.
- **Accounting Basis** – The report clearly indicates the accounting basis used to present financial information in the report, as well as the primary valuation date(s).

- **Key Business Goals** – The report provides an overview of the insurer's/group's key business goals in order to demonstrate alignment with the relevant and material risks presented within the report.
- **Changes from Prior Filing(s)** – The report clearly discusses significant changes from the prior year filing(s) to highlight areas of focus in the current year review including significant changes to the ERM framework, risks assessed, stress scenarios, overall capital position, modeling assumptions, etc.
- **Planned ERM Enhancements** – The report provides information on planned enhancements for improving the effectiveness of the insurer's/group's ERM practices to demonstrate ongoing development and a functioning feedback loop.

## Review of Section I - Description of the Insurer's Risk Management Framework

The *ORSA Guidance Manual* requires the insurer to discuss the key principles below in Section I of the ORSA Summary Report. For purposes of evaluating the ORSA Summary Report, and moreover, the lead state analyst's responsibility to assess the insurer's risk management framework, the lead state analyst should review the ORSA Summary Report to ascertain if the framework meets the principles. Additional guidance is included to provide further information on what may be contemplated ~~when considering~~in assessing such principles~~ as well as examples of attributes that may indicate the insurer is more or less mature in its handling of key risk management principles. These attributes are meant to assist the lead state analyst in reaching an initial high-level assessment of the insurer's maturity level for each key principle as "Level 5" through "Level 0"~~.

Key Principles:

A. Risk Culture and Governance

B. Risk Identification and Prioritization

C. Risk Appetite, Tolerances and Limits

D. Risk Management and Controls

E. Risk Reporting and Communication

### Documentation for Section I

~~Consideration When Reviewing for Key Principles:~~

When reviewing the ORSA Summary Report, the lead state analyst should consider the extent to which ~~of~~ the above principles are present within the organization. In reviewing these principles, examples of various ~~attributes/traits associated with various maturity levels (e.g., "Level 5" practices)~~considerations are provided for each principle in the following sections. The intent in providing these ~~attributes or traits~~considerations is to assist the lead state analyst in assessing the risk management framework. However, these ~~attributes~~ considerations only ~~demonstrate common practices associated with each of the various maturity levels~~highlight certain elements associated with the key principles and practices of individual insurers that may vary significantly~~ from the examples provided~~. The lead state analyst should document a summary of the review of Section I by outlining key information and developing an assessment of each of the five principles set forth in the *ORSA Guidance Manual* using the template located in the next section of this Handbook.

### A. Risk Culture and Governance

It is important to note some insurers view risk culture and governance as the cornerstone to managing risk. The *ORSA Guidance Manual* defines this item to include a structure that clearly defines and articulates roles, responsibilities and accountabilities, as well as a risk culture that supports accountability in risk-based decision making. Therefore, the objective is to have a structure in place within the insurer that manages reasonably foreseeable and relevant material risk in a way that is continuously improved. Key considerations in reviewing and assessing risk culture and governance might include, but aren't limited to:

- **Roles and Responsibilities** - Roles and responsibilities of key stakeholders in risk and capital management are clearly defined and documented in writing, including members of the board (or committee thereof), officers and senior executives, risk owners, etc.

- **Board or Committee Involvement** – The Board of Directors or appropriate committee thereof demonstrates active involvement in and oversight of ERM activities through regular monitoring, reporting and recommendations.
- **Strategic Decisions** – Directors, officers and other members of senior management utilize information generated through ERM processes in making strategic decisions.
- **Staff Availability and Education** – The insurer maintains suitable staffing (e.g. sufficient number, educational background, and experience) to support its ERM framework and deliver o~~f~~n its risk strategy. Staff is kept current in its risk education in accordance with changes to the risk profile of the insurer.
- **Leadership** – The Chief Risk Officer (CRO), ~~(~~or equivalent position,~~)~~ possesses an appropriate level of knowledge and experience related to ERM and receives an appropriate level of authority to effectively fulfill responsibilities. This includes clear and direct communication channels between the CRO and the BOD or appropriate committee thereof.
- **Compensation** – The insurer demonstrates that incentives, compensation and performance management criteria have been appropriately aligned with ERM processes and do not encourage excessive risk taking given the capital position of the insurer.
- **Integration** – The insurer integrates and coordinates ERM processes across functional areas of the organization including human resources, information technology, internal audit, compliance, business units, etc.
- **Assessment** – The insurer's ERM framework is subject to regular review and assessment, with updates made to the framework as deemed necessary.

- ~~Level 5~~

  ~~Risk culture is analyzed and reported as a systematic view of evaluating risk. Executive sponsorship is strong, and the tone from the top has sewn an ERM framework into the corporate culture. Management establishes the framework, and the risk culture and the board reviews the risk appetite statement in collaboration with the chief executive officer (CEO), chief risk officer (CRO) where applicable, and chief financial officer (CFO). Those officers translate the expectations into targets through various practices embedded throughout the insurer. Risk management is embedded in each material business function. Internal audit, information technology, compliance, controls and risk management processes are integrated and coordinate and report risk issues. Material business functions use risk-based best practices. The risk management lifecycle for business process areas are routinely evaluated and improved (when necessary).~~

- ~~Level 4~~

  ~~The insurer's ERM processes are self-governed with shared ethics and trust. Management is held accountable. Risk management issues are understood and risk plans are conducted in material business process areas. The board, CEO, CRO (if applicable) and CFO expect a risk management plan to include a qualitative risk assessment for reasonably foreseeable and relevant material risks with reporting to management or the board on priorities, as appropriate. Relevant areas use the ERM framework to enhance their functions, communicating on risk issues as appropriate. Process owners incorporate managing their risks and opportunities within regular planning cycles. The insurer creates and evaluates scenarios consistent with its planning horizon and product timelines, and follow-up activities occur accordingly.~~

- ~~Level 3~~

  ~~ERM risk plans are understood by management. Senior management expects that a risk management plan captures reasonably foreseeable and relevant material risks in a qualitative manner. Most areas use the ERM framework and report on risk issues. Process owners take responsibility for managing their risks and opportunities. Risk management creates and evaluates scenarios consistent with the business planning horizon.~~

- ~~Level 2~~

  ~~Risk culture is enforced by policies interpreted primarily as compliance in nature. An executive champions ERM management to develop an ERM framework. One area has used the ERM framework, as shown by the department head and documented team activities. Business processes are identified, and ownership is defined. Risk management is used to consider risks in line with the insurer's business planning horizon.~~

- ~~Level 1~~
  ~~Corporate culture has little risk management accountability. Risk management is not interpreted consistently. Policies and activities are improvised. Programs for compliance, internal audit, process improvement and IT operate independently and have no common framework, causing overlapping risk assessment activities and inconsistencies. Controls are based on departments and finances. Business processes and process owners are not well-defined or communicated. Risk management focuses on past events. Qualitative risk assessments are unused or informal. Risk management is considered a quantitative analysis exercise.~~

- ~~Level 0~~
  ~~There is no recognized need for an ERM process and no formal responsibility for ERM. Internal audit, risk management, compliance and financial activities might exist but are not integrated. Business processes and risk ownership are not well-defined.~~

## B. Risk Identification and Prioritization

The *ORSA Guidance Manual* defines this as key to the insurer. Responsibility for this activity should be clear, and the risk management function is responsible for ensuring the processes are appropriate and functioning properly. Therefore, an approach for risk identification and prioritization may be to have a process in place that identifies risk and prioritizes such risks in a way that potential reasonably foreseeable and relevant material risks are addressed in the framework. Key considerations in reviewing and assessing risk identification and prioritization might include, but aren't limited to:

- **Resources** – The insurer utilizes appropriate resources and tools (e.g. questionnaires, external risk listings, brainstorming meetings, regular calls, etc.) to assist in the risk identification process that are appropriate for its nature, size and structure.
- **Stakeholder Involvement** – All key stakeholders (i.e. directors, officers, senior management, business unit leaders, risk owners, etc.) are involved in risk identification and prioritization at an appropriate level.
- **Prioritization Factors** – Appropriate factors and considerations are utilized to assess and prioritize risks (e.g. likelihood of occurrence, magnitude of impact, controllability, speed of onset, etc.).
- **Process Output** – Risk registers, key risk listings and risk ratings are maintained, reviewed and updated on a regular basis.
- **Emerging Risks** – The insurer has developed and maintained a formalized process for the identification and tracking of emerging risks.

- ~~Level 5~~
  ~~Information from internal and external sources on reasonably foreseeable and relevant material risks, including relevant business units and functions, is systematically gathered and maintained. A routine, timely reporting structure directs risks and opportunities to senior management. The ERM framework promotes frontline employees' participation and documents risk issues or opportunities' significance. Process owners periodically review and recommend risk indicators that best measure their areas' risks. The results of internal adverse event planning are considered a strategic opportunity.~~

- ~~Level 4~~
  ~~Process owners manage an evolving list of reasonably foreseeable and relevant material risks locally to create context for risk assessment activities as a foundation of the ERM framework. Risk indicators deemed critical to their areas are regularly reviewed in collaboration with the ERM team. Measures ensure downside and upside outcomes of risks and opportunities are managed. Standardized evaluation criteria of impact, likelihood and controls' effectiveness are used to prioritize risk for follow-up activity. Risk mitigation is integrated with assessments to monitor effective use.~~

- ~~Level 3~~
  ~~An ERM team manages an evolving list of reasonably foreseeable and relevant material risks, creating context~~

~~for risk assessment as a foundation of the ERM framework. Risk indicator lists are collected by most process owners. Upside and downside outcomes of risk are understood and managed. Standardized evaluation criteria of impact, likelihood and controls' effectiveness are used, prioritizing risk for follow-ups. Enterprise level information on risks and opportunities are shared. Risk mitigation is integrated with assessments to monitor effective use.~~

- ~~Level 2~~
  ~~Formal lists of reasonably foreseeable and relevant material risks exist for each relevant business unit or function, and discussions of risk are part of the ERM process. Corporate risk indicators are collected centrally, based on past events. Relevant business units or functions might maintain their own informal risk checklists that affect their areas, leading to potential inconsistency, inapplicability and lack of sharing or under-reporting.~~
- ~~Level 1~~
  ~~Risk is owned by specialists, centrally or within a business unit or function. Risk information provided to risk managers is probably incomplete, dated or circumstantial, so there is a high risk of misinformed decisions, with potentially severe consequences. Further mitigation, supposedly completed, is probably inadequate or invalid.~~
- ~~Level 0~~
  ~~There might be a belief that reasonably foreseeable and relevant material risks are known, although there is probably little documentation.~~

## C. Risk Appetite, Tolerances and Limits

The *ORSA Guidance Manual* states that a formal risk appetite statement, and associated risk tolerances and limits are foundational elements of a risk management framework for an insurer. While risk appetites, tolerances and limits can be defined and used in different ways across different organizations, this guidance is provided to assist the regulator in understanding and evaluating the insurer's practices in this area.

Risk appetite can be defined as the amount of specific and aggregate risk that an organization chooses to take during a defined time period in pursuit of its business objectives. ~~Understanding~~ Articulation of the risk appetite statement ensures alignment ~~with~~ of the risk strategy with the business strategy set by senior management and reviewed and evaluated by the board. Not included in the Manual, but widely considered, is that risk appetite statements should be easy to communicate, be understood, and be closely tied to the insurer's strategy.

After the overall risk appetite for the insurer is determined, the underlying risk tolerances and limits can be selected and applied to business units and specific key risks identified ~~areas as deemed appropriate~~ by the ~~company~~insurer. Risk tolerance can be defined as the aggregate risk-taking capacity of an organization. Risk limits can be defined as thresholds used to monitor the actual exposure of a specific risk or activity unit of the organization to ensure that the level of actual risk remains within the risk tolerance. The ~~company~~insurer may apply appropriate quantitative limits and qualitative statements to help establish boundaries and expectations for risks that are hard to measure. These boundaries may be expressed in terms of earnings, capital, or other metrics (growth, volatility, etc.). The risk tolerances/limits provide direction outlining the insurer's tolerance for taking on certain risks, which may be established and communicated in the form of the maximum amount of such risk the entity is willing to take. However, in many cases these will be coupled with more specific and detailed limits or guidelines the insurer uses.

Due to the varying level of detail and specificity that different insurers incorporate into their risk appetites, tolerances and limits, lead state regulators should consider these elements collectively to reach an overall assessment in this area and should seek to understand the insurer's approach through follow-up discussions and dialogue. Key considerations in reviewing and assessing risk appetites, tolerances and limits might include, but aren't limited to:

- **Risk Appetite Statement** – The insurer has adopted an overall risk appetite statement consistent with its business plans and operations that is updated on a regular basis and approved by the board of directors (or committee thereof).

- **Risk Tolerances/Limits** – Tolerances and limits are developed for key risks in accordance with the overall risk appetite statement.
- **Risk Owners** – Key risks are assigned to risk owners with responsibility for monitoring and reporting on risk tolerances and limits, including actions to address any breaches.

- ~~Level 5~~
  ~~A risk appetite statement has been developed to establish clear boundaries and expectations for the insurer to follow. A process for delegating authority to accept risk levels in accordance with the risk appetite statements is communicated throughout the insurer. The management team and risk management committee, if applicable, may define tolerance levels and limits on a quantitative and/or qualitative basis for relevant business units and functions in accordance with the defined risk appetite. As part of its risk management framework, the insurer may compare and report actual assessed risk versus risk tolerances/limits. Management prioritizes resource allocation based on the gap between risk appetite and assessed risk and opportunity. The established risk appetite is examined periodically.~~

- ~~Level 4~~
  ~~Risk appetite is considered throughout the ERM framework. Resource allocation decisions consider the evaluation criteria of business areas. The insurer forecasts planned mitigation's potential effects versus risk tolerance as part of the ERM framework. The insurer's risk appetite is updated as appropriate, and risk tolerances are evaluated from various perspectives as appropriate. Risk is managed by process owners. Risk tolerance is evaluated as a decision to increase performance and measure results. Risk-reward tradeoffs within the business are understood and guide actions.~~

- ~~Level 3~~
  ~~Risk assumptions within management decisions are clearly communicated. There is a structure for evaluating risk and gauging risk tolerance on an enterprise-wide basis. Risks and opportunities are routinely identified, evaluated and executed in alignment with risk tolerances. The ERM framework quantifies gaps between actual and target tolerances. The insurer's risk appetite is periodically reviewed and updated as deemed appropriate by the insurer, and risk tolerances are evaluated from various perspectives as appropriate.~~

- ~~Level 2~~
  ~~Risk assumptions are only implied within management decisions and are not understood outside senior leadership with direct responsibility. There is no ERM framework for resource allocation. Defining different views of business units or functions from a risk perspective cannot be easily created and compared.~~

- ~~Level 1~~
  ~~Risk management might lack a portfolio view of risk. Risk management might be viewed as risk avoidance and meeting compliance requirements or transferring risk through insurance. Risk management might be a quantitative approach focused on the analysis of high-volume and mission-critical areas.~~

- ~~Level 0~~
  ~~The need for formalizing risk tolerance and appetite is not understood.~~

## D. Risk Management and Controls

The *ORSA Guidance Manual* stresses managing risk as an ongoing ERM activity, operating at many levels within the insurer. This principle is discussed within the governance section above from the standpoint that a key aspect of managing and controlling the reasonably foreseeable and relevant material risks of the insurer is the risk governance process put in place. For many companies, the day-to-day governance starts with the relevant business units. Those units put mechanisms in place to identify, quantify and monitor risks, which are reported up to the next level based upon the risk reporting triggers and risk limits put in place. In addition, controls are also put in place on the backend, by either the ERM function or the internal audit team, ~~or some independent consultant,~~ which are designed to ensure compliance and a continual enhancement approach. Therefore, one approach may be to put controls in place to ensure the insurer is abiding by its limits. Key considerations in reviewing and assessing risk management and controls might include, but aren't limited to:

- **Lines of Defense** – Multiple lines of defense (i.e. business unit or risk owners, ERM function, internal audit) are put in place to ensure that control processes are effectively implemented and maintained.
- **Control Processes** – Specific control activities and processes are put in place to manage, mitigate and monitor all key risks.
- **Implementation of Tolerances/Limits** – Risk tolerances and limits are translated into operational guidance and policies around key risks through all levels of the organization.
- **Indicators/Metrics** – Key risk indicators or performance metrics are put in place to monitor exposures, provide early warnings and measure adherence to risk tolerances/limits.

- ~~Level 5~~
  ~~ERM, as a management tool, is embedded in material business processes and strategies. Roles and responsibilities are process driven with teams collaborating across material central and field positions. Risk and performance assumptions within qualitative assessments are routinely revisited and updated. The insurer uses an ERM process of sequential steps that strive to improve decision-making and performance. A collaborative, enterprise-wide approach is in place to establish a risk management committee staffed by qualified management. Accountability for risk management is woven into material processes, support functions, business lines and geographies as a way to achieve goals. To evaluate and review the effectiveness of ERM efforts and related controls, the insurer has implemented a "Three Lines of Defense" model or similar system of checks and balances that is effective and integrated into the insurer's material business processes. The first line of defense may consist of business unit owners and other front line employees applying internal controls and risk responses in their areas of responsibility. The second line of defense may consist of risk management, compliance and legal staff providing oversight to the first line of defense and establishing framework requirements to ensure reasonably foreseeable and relevant material risks are actively and appropriately managed. The third line of defense may consist of auditors performing independent reviews of the efforts of the first two lines of defense to report back independently to senior management or the board.~~

- ~~Level 4~~
  ~~Risk management is clearly defined and enforced at relevant levels. A risk management framework articulates management's responsibility for risk management, according to established risk management processes. Management develops and reviews risk plans through involvement of relevant stakeholders. The ERM framework is coordinated with managers' active participation. Opportunities associated with reasonably foreseeable and relevant material risks are part of the risk plans' expected outcome. Authentication, audit trail, integrity and accessibility promote roll- up information and information sharing. Periodic reports measure ERM progress on reasonably foreseeable and relevant material risks for stakeholders, including senior management or the board. The insurer has implemented a "Three Lines of Defense" model to review and assess its control effectiveness, but those processes may not yet be fully integrated or optimized.~~

- ~~Level 3~~
  ~~The ERM framework supports material business units' and functions' needs. ERM is a process of steps to identify, assess, evaluate, mitigate and monitor reasonably foreseeable and relevant material risks. ERM frameworks include the management of opportunities. Senior management actively reviews risk plans. The ERM process is collaborative and directs important issues to senior management. The "Three Lines of Defense" are generally in place, but are not yet performing at an effective level.~~

- ~~Level 2~~
  ~~Management recognizes a need for an ERM framework. Agreement exists on a framework, which describes roles and responsibilities. Evaluation criteria are accepted. Risk mitigation activities are sometimes identified~~

~~but not often executed. Qualitative assessment methods are used first in material risk areas and inform what needs deeper quantitative methods, analysis, tools and models. The "Three Lines of Defense" are not yet fully established, although some efforts have been made to put these processes in place.~~

- ~~Level 1~~
  ~~Management is reactive and ERM might not yet be seen as a process and management tool. Few processes and controls are standardized and are instead improvised. There are no standard risk assessment criteria. Risk management is involved in business initiatives only in later stages or centrally. Risk roles and responsibilities are informal. Risk assessment is improvised. Standard collection and assessment processes are not identified.~~

- ~~Level 0~~
  ~~There is little recognition of the ERM framework's importance or controls in place to ensure its effectiveness.~~

## E. Risk Reporting and Communication

The *ORSA Guidance Manual* indicates risk reporting and communication provides key constituents with transparency into the risk-management processes as well as facilitates active, informal decisions on risk-taking and management. The transparency is generally available because of reporting that can be made available to management, the board, or compliance departments, as appropriate. However, most important is how the reports are being utilized to identify and manage reasonably foreseeable and relevant material risks at either the group, business unit or other level within the insurer where decisions are made. Therefore, one approach may be to have reporting in place that allows decisions to be made throughout the insurer by appropriately authorized people, with ultimate ownership by senior management or the board. Key considerations in reviewing and assessing risk reporting and communication might include, but aren't limited to:

- **Training** – The importance of ERM processes and changes to the risk strategy are clearly communicated to all impacted areas and business units through ongoing training.
- **Key Risk Indicator Reporting** – Summary reports on risk exposures (i.e. key risk indicators) and compliance with tolerances/limits are maintained and updated on a regular basis.
- **Oversight** – Summary reports are reviewed and discussed by directors, officers and other members of senior management on a regular basis.
- **Breach Management** – Breaches of limits and dashboard warning indicators are addressed in a timely manner through required action by directors and officers.
- **Feedback** – A feedback loop is embedded into ERM processes to ensure that results of monitoring and review discussions on key risks by senior management and the board are incorporated by business unit leaders and risk owners into ongoing risk-taking activities and risk management processes.

- ~~Level 5~~
  ~~The ERM framework is an important element in strategy and planning. Evaluation and measurement of performance improvement is part of the risk culture. Measures for risk management include process and efficiency improvement. The insurer measures the effectiveness of managing uncertainties and seizing risky opportunities. Deviations from plans or expectations are also measured against goals. A clear, concise and effective approach to monitor progress toward strategic goals is communicated regularly with relevant business units or functional areas. Individual, management, departmental, divisional and corporate strategic goals are linked with standard measurements. The results of key measurements and indicators are reviewed and discussed by senior management or the board, on a regular basis and as frequently as necessary to address breaches in risk tolerances or limits in a timely manner.~~

- ~~Level 4~~
  ~~The ERM framework is an integrated part of strategy and planning. Risks are considered as part of strategic planning. Risk management is a formal part of strategic goal setting and achievement. Investment decisions for resource allocation examine the criteria for evaluating opportunity impact, timing and assurance. The insurer forecasts planned mitigation's potential effect on performance impact, timing and assurance prior to~~

~~use. Employees at relevant levels use a risk-based approach to achieve strategic goals. The results of key measurements and indicators are shared with senior management or the board on a regular basis.~~

- ~~Level 3~~
  ~~The ERM framework contributes to strategy and planning. Strategic goals have performance measures. While compliance might trigger reviews, other factors are integrated, including process improvement and efficiency. The insurer indexes opportunities qualitatively and quantitatively, with consistent criteria. Employees understand how a risk-based approach helps them achieve goals. Accountability toward goals and risk's implications are understood and are articulated in ways frontline personnel understand. The results of key measurements and indicators are shared with senior management or the board.~~

- ~~Level 2~~
  ~~The ERM framework is separate from strategy and planning. A need for an effective process to collect information on opportunities and provide strategic direction is recognized. Motivation for management to adopt a risk-based approach is lacking.~~

- ~~Level 1~~
  ~~Not all strategic goals have measures. Strategic goals are not articulated in terms the frontline management understands. Compliance focuses on policy and is geared toward satisfying external oversight bodies. Process improvements are separate from compliance activities. Decisions to act on risks might not be systematically tracked and monitored. Monitoring is done, and metrics are chosen individually. Monitoring is reactive.~~

- ~~Level 0~~
  ~~No formal framework of indicators and measures for reporting on achievement of strategic goals exists.~~

## Overall Section 1 Assessment

**~~Documentation for Section I~~**

~~The lead state analyst should prepare a summary of Section I by developing an assessment of each of the five principles set forth in the *ORSA Guidance Manual* using the template at the end of these procedures.~~ After summarizing the information reviewed for each of the key principles individually, the lead state analyst should provide an overall assessment of the insurer's ERM framework, including any concerns or areas requiring follow-up investigation or communication. In preparing the assessment, ~~T~~the lead state analyst should understand that ORSA summary reports may not always align with each of these specific principles. Therefore, the lead state analyst must use judgment and critical thinking in accumulating information to support their evaluation of each of these principles. The overall evaluation should focus on critical concerns associated with any of the individual principles and should also address any other ERM framework concerns that may not be captured within these principles.

The lead state analyst should also be aware that the lead state examiner is tasked ~~to update the assessment by~~with supplementing the lead state analyst's assessment with additional onsite verification and testing. The lead state analyst should direct the lead state examiner to those areas where such additional verification and testing is appropriate and could not be performed by the lead state analyst. Where available from prior full scope or targeted examinations, ~~the assessment~~information from the lead state examiner should be used as a starting point for the lead state analyst to update. Consequently, on an ongoing basis, the lead state analyst's update may focus ~~as much~~ on changes to ERM processes and the ORSA Summary Report ~~(positive or negative)~~ since the ~~insurer was previously examined; and, similar to an initial assessment by the lead state analyst, they may want to~~prior exam in directing targeted onsite verification and testing ~~for changes that have occurred since the last examination~~.

The lead state analyst, after completing a summary of Section I, should consider if the overall assessment, or any specific conclusions, should be used to update either the ERM section of the Group Profile Summary (GPS) (if the ORSA Summary Report is prepared on a group basis) or information in the Insurer Profile Summary (IPS) (if the

ORSA Summary Report is prepared on a legal entity basis). In addition, key information from the review should be incorporated into the Risk Assessment Worksheet (RAW) during the next full analysis (quarterly or annual) of the insurer ~~if~~where relevant.

## Review of Section II - Insurer's Assessment of Risk Exposure

Section II of the ORSA Summary Report is required to provide a high-level summary of the quantitative and/or qualitative assessments of risk exposure in both normal and stressed environments. The *ORSA Guidance Manual* does not require the insurer to ~~include~~ address specifi~~e~~ed~~c~~ risks, but does ~~give possible~~provide examples of reasonably foreseeable and relevant material risk categories (e.g. credit, market, liquidity, underwriting, and operational risks). In reviewing the information provided in this section of the ORSA, lead state analysts may need to pay particular attention to risks and exposures that may be emerging or significantly increasing over time. To assist in identifying and understanding the changes in risk exposures, the lead state analyst may consider comparing the insurer's risk exposures and/or results of stress scenarios to those provided in prior years.

Section II provides risk information on the entire insurance group, which may be grouped in categories similar to the NAIC's nine branded risk classifications. However, this is not to suggest the lead state analyst or lead state examiner should expect the insurer to address each of the nine branded risk classifications. In fact, in most cases, they will not align, but it is not uncommon to see some similarities for credit, market, liquidity, underwriting and operational risks. A fair number of insurer risks may not be easily quantified or are grouped differently than these nine classifications. Therefore, it is possible the insurer does not view them as significant or relevant. The important point is not the format, but for the lead state analyst or lead state examiner to understand how the insurer categorizes its own risks and contemplate whether there may be material gaps in identified risks or categories of risks.

### Documentation for Section II

Prepare a summary and assessment of Section II by identifying and outlining key information associated with the significant reasonably foreseeable and material relevant (key) risks of the insurer per the ORSA Summary Report~~, including those that correspond to the nine branded risk classifications, if applicable~~. Following the documentation on each ~~of the significant reasonably foreseeable and material relevant risks~~key risk per the report, the lead state analysts should include an analysis of such risk. In developing such analysis, the lead state analyst is encouraged to use judgment and critical thinking in evaluating if the risks and quantification of such risks under normal and stressed conditions are reasonable and generally consistent with expectations. The lead state analyst should be aware that the lead state examiner is tasked to update the assessment by supplementing the lead state analyst's assessment with additional on-site verification and testing. The lead state analyst should direct the lead state examiner to those areas where such additional verification and testing is appropriate and could not be performed by the lead state analyst. Suggested information to be documented on each key risk, including supporting considerations, is outlined below:

- **Risk Title and Description** – Provide the title for each key risk as identified/labeled by the insurer as well as a basic description.
- **Branded Risk** – Provide information on the primary branded risk classification(s) that apply to the key risk and briefly discuss how they apply/relate.
- **Controls/Mitigation** – Summarize information known about the controls and mitigation strategies put in place by the insurer to address the key risk.
- **Risk Limits** – Provide information on any specific risk tolerances or limits associated with the key risk and how they are monitored and enforced.
- **Assessment** – Discuss how the key risk is assessed by the insurer, including whether the assessment is performed on a quantitative (QT) or qualitative (QL) basis. Describe the methodology used, the key underlying assumptions and the process utilized to set these assumptions.
- **Normal Exposure** – Summarize the insurer's normal exposure to this key risk based on budget information or historical experience.

- **Stress Scenario(s)** – Discuss the stress scenario(s) identified and applied to the key risk and how they were determined and validated by the insurer.
- **Stressed Exposure** – Provide information on the impact of the stress scenario(s) on the key risk and potential impact on the insurer's surplus position and business strategy/operations.
- **Inclusion on IPS/GPS** – Discuss whether the key risk will be recognized on the IPS/GPS of the insurer, including the risk component it will be incorporated into.
- **Regulator Review & Assessment** – Assess the adequacy of the risk assessment performed by the insurer on each key risk (including the appropriateness of controls/limits and reasonableness of methodology, assumptions and stress scenarios used) and whether any specific issues or concerns are identified that would require further investigation or follow-up communication

After completing a summary and assessment for each key risk addressed in~~of~~ Section II, the lead state analyst should use the information to update the risk assessment in either the GPS (if the ORSA is prepared on a group basis) or the IPS (if the ORSA is prepared on a legal entity basis) and supporting documentation if deemed necessary. In addition, key information from the review should be incorporated into the RAW during the next full analysis (quarterly or annual) of the insurer ~~if~~where relevant.

**Overall ~~Risk Assessment Summary~~Section 2 Assessment**

~~In addition, t~~The lead state analyst should complete an overall assessment of the information provided in Section II, including an evaluation of the insurer's risk assessment processes and whether all material and relevant risks were assessed and presented at an appropriate level of detail. This should include consideration of whether there is consistency between the insurer's Risk Identification and Prioritization process discussed in Section I and risks that are assessed and reported on in Section II (i.e. have all key risks been addressed). In addition, this should focus on critical concerns associated with the assessment of individual key risks as well as whether the insurer's overall assessment process (i.e. methodology, assumptions and stress scenarios) is adequate and well-supported.~~After considering the various risks identified by the insurer through Section II, develop an overall risk assessment summary of possible concerns that may exist.~~

## Review of Section III - Group Assessment of Risk Capital

~~Section III of the ORSA is unique in that it is required to be completed at the insurance group level as opposed to the other sections which may be completed at a legal entity level. However, in many cases, insurers will choose to also complete Section I and Section II at the group level. This requirement is important because it provides the means for lead state regulators to assess the reasonableness of capital of the entire insurance group based upon its existing business plan.~~

In reviewing Section III of the ORSA Summary Report, the lead state analyst should recognize this section is generally presented in a summarized form. Although this section requires disclosure of aggregate available capital compared against the enterprise's risk capital (i.e. the amount deemed necessary to withstand unexpected losses arising from key risks), the report may not provide sufficient detail to fully evaluate the group capital position. As such, the lead state analyst may need to request the assistance of staff actuaries when available in evaluating the reasonableness and adequacy of the stress tests selected, request additional detail from the insurer in order to understand and evaluate the group capital position and/or refer additional investigation to the financial examination function.

The *ORSA Guidance Manual* (Manual) requires the insurer to estimate its prospective solvency under stressed conditions by identifying stress scenarios that would give ris~~k~~e to significant losses that have not been accounted for in reserves. Furthermore, the Manual requires the insurer to estimate its prospective solvency in Section III by projecting the aggregate capital available and comparing it against the enterprise's risk capital. Insurers may include information in the ORSA Summary Report developed as part of their strategic planning and may include pro forma financial information that displays anticipated changes to key risks as well as projected capital adequacy in those future periods based on the insurer's defined capital adequacy standard. In reviewing information on prospective solvency, the lead state analyst should carefully consider projected changes to the group capital position as well as significant shifts in the amount of capital allocated to different risks, which could signal changes in business strategy and risk exposures.

~~Section III will be directly used as part of the lead state's insurance holding company analysis evaluation of group capital.~~

### Documentation for Section III

Insurance groups will use different means to ~~measure risk (i.e., required)~~manage capital and they will use different accounting and valuation frameworks. For example, they may determine the amount of capital they need to fulfil regulatory and rating agencies' requirements, but also determine the amount of capital (risk capital) they need to absorb unexpected losses that are not accounted for in the reserves. The lead state analyst may need to request management to discuss their overall approach to ~~both of these items~~capital management and the reasons and details for each approach so that they can be considered in the evaluation of estimated risk capital.

Many insurers use internally developed capital models to quantify the risk capital. In these cases, ~~T~~the ORSA Summary Report should summarize the insurer's process for model validation to support the quantification methodology and assumptions chosen to determine risk capital~~, including factors considered and model calibration~~. The lead state analyst should use the model validation information to assess the reasonableness of the quantification methodology and assumptions used. If the ORSA Summary Report does not provide a summary of the model validation process, the lead state analyst should request copy of the validation report prepared by the insurer. With regard to the determination of the risk capital under stressed conditions, ~~B~~because the risk profile of each insurer is unique, there is no standard set of stress conditions that each insurer should run.~~;~~ ~~h~~However, the lead state regulator should be prepared to dialogue with management about the selected stress scenarios if there is concern with the rigor of the scenario. In discussions with management, the lead state analyst should gain an understanding of the modeling methods used to project available and risk capital over the duration of the insurer's business plan as well as the potential changes to the risk profile of the insurer over this time horizon (i.e. changes to the list of key risks) based on the business plan~~(e.g., stochastic vs. deterministic) and be prepared to dialogue about and understand the material assumptions that affected the model output, such as prospective views on risks~~. The aforementioned dialogue may occur during either the financial analysis process and/or the financial examination process.

The lead state analyst, after completing a summary of Section III, should assess the overall reasonableness of the capital position compared to the group's estimated risk capital. Additionally, the lead state analyst should also consider if any of the information, or any specific conclusions, should be used to update either the GPS or IPS.

~~Support the~~An assessment of the reasonableness of group risk capital and the process to measure it should be provided by developing a narrative that ~~considers~~ provides the following for each individual element of the insurer's assessment of risk capital:

- **Discussion of Capital Metric(s) Used** – Discuss the method(s) used by the group in assessing group risk capital and their basis for such a decision. Identify the capital metric(s) used to estimate group risk capital, as well as the level of calibration selected. Consider whether the capital metric(s) utilized to assess the group's overall capital target are clearly presented and described. Metrics may consist of internally developed economic capital models (deterministic or stochastic) and/or externally developed models, such as regulatory capital requirements (RBC) or A.M. Best's Capital Adequacy Ratio (BCAR). In discussing calibration, consider both the method used (e.g. Value at Risk, Tail Value at Risk) and its level (e.g. 99.5%) to evaluate whether the results are calibrated to an appropriate confidence level. Discuss whether the capital metric(s) selected address all key risks of the group. Of particular importance is considering whether the metric used fits the approach used to determine the group's risk appetite. Document the extent to which the lead state analyst believes the approach used by the insurer is reasonable for the nature, scale and complexity of the group and if this has any impact on the lead state analyst's assessment of the insurer's overall risk management.
- **Group Risk Capital - By Risk and in Aggregate** – Provide information on the amount of risk capital determined

for each individual key risk and in aggregate. In reviewing the results for each individual risk, evaluate whether all key risks are adequately accounted for in the metric by assessing the amount of capital allocated to each risk. Consider significant changes in group risk capital from the prior filing, the drivers of such change, and any decisions made as a result of such movement.

- **Impact of Diversification Benefit** – Discuss the impact of any diversification benefit calculated by the group in aggregating its group risk capital. Diversification benefit is typically calculated by aggregating individually modeled risk capital and then accounting for potential dependencies among those risks to allow for an offset or reduction in the total amount of required capital (group risk capital). In evaluating the group's diversification benefit, consider whether the benefit is calculated based on dependencies/correlations in key risk components that are reasonable/appropriate.
- **Available Capital** – Provide information on and discuss the amount of capital available to the group. Evaluate the quality of available capital from the standpoint of whether that capital is freely available to meet policyholder obligations. Determine if there is any double counting of capital through the stacking of legal entities or challenges in accessing group capital due to fungibility issues (i.e. capital trapped within various legal entities).
- **Excess Capital** – Discuss the extent to which the group available capital amount exceeds the group risk capital amount per the ORSA Summary Report. In evaluating the overall adequacy of excess capital, consider any concerns outlined above relating to the capital metric(s), group risk capital, impact of diversification and available capital. If the level of excess capital or its availability/liquidity is of concern, evaluate the group's ability to remediate capital deficiencies by obtaining additional capital or reducing risk where required. If further concerns exist, contact the group to discuss and communicate with department senior management to determine whether additional investigation or regulatory action is necessary.
- **Impact of Stresses on Group Risk Capital** – Discuss whether additional stress scenarios have been applied to the model results to demonstrate the group's resiliency to absorb extreme unexpected losses. This step is particularly important when reviewing the use of external capital models that may not be tailored to address the enterprise's specific exposures. Evaluate the range and adequacy of any stress scenarios applied and the resulting impact on the group's ability to accomplish its business strategy, provide sufficient liquidity and meet the capital expectations of rating agencies and regulators.
- **Governance and Validation** – Discuss and evaluate the group's model governance process and the means by which changes to models are overseen and approved. Consider whether the board of directors (or committee thereof) and members of senior management are adequately involved. Discuss the extent to which the group uses model validation (including validation of data inputs) and independent review to provide additional controls over the estimation of group capital.
- **Prospective Solvency Assessment** – Discuss the information provided by the group on its prospective solvency position, including any capital projections. Consider whether the business goals of the ~~company~~insurer and its strategic direction are adequately discussed and incorporated into the prospective solvency assessment. For example, are expected changes in risk profile presented and discussed? Also consider whether prospective solvency is projected across the duration of the current business plan. To the extent the prospective assessment suggests that the group capital position will weaken, or recent trends may result in certain internal limits being breached, the lead state analyst should understand and discuss what actions the insurer expects to take as a result of such an assessment (e.g., reduce certain risk exposure, raise additional capital, etc.).

**Overall Section 3 Assessment**

In addition, after summarizing the assessment of each individual element above, the lead state analyst should provide an overall assessment of the insurer's risk capital assessment process, including any concerns or areas requiring follow-up investigation or communication. The overall evaluation should focus on critical concerns associated with any of the individual elements noted above and should also address any other risk capital assessment concerns that may not be captured within these principles.

The lead state analyst, after completing a summary of Section 3, should consider if the overall assessment, or any specific conclusions, should be used to update either the ERM section of the GPS~~)~~ (if the ORSA Summary Report is prepared on a group basis) or information in the IPS (if the ORSA Summary Report is prepared on a legal entity basis). In addition, key information from the review should be incorporated into the RAW during the next full analysis (quarterly or annual) of the insurer if relevant.

- ~~Actual Capital Amount–Discuss the extent to which the group available capital amount exceeds the group risk capital amount per the ORSA Summary Report. In the rare situation where the calculation revealed group capital was not sufficient compared to internal/rating agency/regulatory capital, immediately contact the group to determine what steps it is taking to address the issue. Consider in that discussion, the section below, which requires the lead state analyst to consider the controls the group has in place relative to this issue. For all other groups, when considering if group capital is either well in excess of internal/rating capital or currently sufficient, consider all of the following considerations, but paying particular attention to the cushion based upon the use of economic capital scenarios and/or stress testing.~~

- ~~Cushion Based Upon Use of Economic Capital Scenarios and/or Stress Perhaps the most subjective determination when considering group capital is determining the sufficiency of such amount compared to a predefined minimum. That minimum, be it regulatory, rating agency, or economic, uses certain assumptions, including assumptions that may already provide a cushion. The lead state analyst shall bear in mind the "Own" in ORSA, noting that each insurer's methodology and stress testing will vary. However, the lead state analyst should be able to develop and document the general methodology applied and how outputs from the prospective solvency calculations compare with recent trends for the group and, in general, be able to determine the sufficiency of capital.~~

- ~~Method of Capital Measurement~~
  ~~Discuss the method used (e.g., internal, rating agency) by the insurer in assessing group capital and their basis for such decision. If no information on this issue exists within the ORSA Summary Report, consider asking the insurer the question. Document the extent to which the lead state analyst believes the approach used by the insurer is reasonable for the nature, scale and complexity of the group and if this has any impact on the lead state analyst's assessment of the insurer's overall risk management.~~

- ~~Quality of Capital~~
  ~~If the insurer uses an internal capital model, evaluate the quality of available capital included in the report from the standpoint of whether that capital is freely available to meet policyholder obligations. In addition, determine if there is any double counting of capital through the stacking of legal entities. If the insurer used rating agency capital, verify if capital used internally in the ORSA Summary Report meets such firm's requirements. If no information on this issue exists within the ORSA Summary Report, the lead state analyst should consider asking the insurer the question.~~

- ~~Prior Year Considerations~~
  ~~Some insurers will provide qualitative information in the ORSA Summary Report that describes their movement of required capital from one period to the next, the drivers of such change, and any decisions made as a result of such movement. If no information on this issue exists within the ORSA Summary Report, consider asking the insurer questions, particularly if there have been material changes in the group capital position year over year or material changes to business plans, operations or market conditions, without a corresponding change in group capital position. This information, as well as the lead state analyst's existing knowledge of the group, and its financial results, should be used to determine the overall reasonableness of the change in group capital and should be an input into evaluating the group capital calculation.~~

- ~~Quantification of Reasonably Foreseeable and Relevant Material Risks~~
  ~~Discuss and document if the group capital fails to recognize any reasonably foreseeable and relevant material risks the lead state analyst is aware of.~~

- ~~Controls over Capital~~
  ~~Discuss the extent to which the ORSA Summary Report demonstrates the group has a strategy, including senior management or the board oversight, for ensuring adequate group capital is maintained over time. This includes~~

~~plans for obtaining additional capital or for reducing risk where required. If no information on this issue exists within the ORSA Summary Report, consider asking the insurer the question.~~

- ~~Controls over Model Validation and or Independent Reviews~~
~~If the insurer uses an internal capital model, discuss the extent to which the group uses model validation and independent review to provide additional controls over the estimation of group capital. If no information on this issue exists within the ORSA Summary Report, consider asking the insurer the question. Lead state analysts and lead state examiners are encouraged to: 1) look to the insurer's own process by which they assess the accuracy and robustness of its models; look how the insurer governs model changes and parameter or assumption setting; and 3) limit lead state examiner-lead validation of model output to more targeted instances where conditions warrant additional analysis.~~

~~**Review of Section III – Prospective Solvency Assessment**~~
~~The *ORSA Guidance Manual* requires the insurer to estimate its prospective solvency. Insurers may include in the ORSA Summary Report information developed as part of their strategic planning and may include pro forma financial information that displays possible outcomes as well as projected capital adequacy in those future periods based on the insurer's defined capital adequacy standard. The lead state analyst should understand the impact such an exercise has on the ongoing business plans of the insurer. For example, to the extent such an exercise suggests that at the insurer's particular capital adequacy under expected outcomes the group capital position will weaken, or recent trends may result in certain internal limits being breached, the lead state analyst should understand what actions the insurer expects to take as a result of such an assessment (e.g., reduce certain risk exposure, raise additional capital, etc.). It should be kept in mind, however, that a mere "weakening" of a group capital position, or even trends, are less relevant than whether group available capital exceeds the group's risk capital over the forecast period. The lead state analyst should document its findings/review of this section.~~

## Feedback to the Insurer

After completing a review of the ORSA Summary Report, the lead state should provide practical and constructive feedback to the insurer related to the review. Feedback plays a critical role in ensuring the compliance and effectiveness of future filings. Feedback also provides a means for asking follow-up questions or requesting additional information to facilitate the review and incorporation of ORSA information into ongoing solvency monitoring processes.

During the review, topics for feedback communication to the insurer can be accumulated on **Appendix A** of the template. The appendix encourages the lead state to accumulate positive attributes to reinforce the effectiveness of certain practices and information in the summary report. In addition, the appendix encourages the lead state to identify areas for constructive feedback to encourage the insurer to provide additional information or clarify the presentation of certain items in future filings. Finally, the appendix encourages the lead state to list requests for additional information that may be necessary to complete a review and evaluation of the insurer's ORSA/ERM processes.

## Suggested Follow-up by the Examination Team

~~As noted at the end of each section~~After completing a review of the ORSA Summary Report, the lead state analyst should direct the lead state examiner to those areas where such additional verification and testing is appropriate and could not be performed by the lead state analyst. These items can be accumulated on **Appendix B** of the template for follow-up and communication. If there are specific reports, information and/or control processes addressed in the ORSA Summary Report that the lead state analyst feels should be subject to additional review and verification by the examination team, the lead state analyst is expected to provide direction as to its findings of specific items and/or recommended testing and such amounts should be listed in the template by the lead state analyst. During planning for a financial examination, the lead state examiner and lead state analyst should work together to develop a plan for additional testing and follow-up where necessary. The plan should consider that the lead state examiner may need to expand work to address areas of inquiry that may not be identifiable by the lead state analyst.

In addition to this specific expectation, during each coordinated financial condition examination, the exam team as directed by the lead state examiner and with input from the lead state analyst will be expected to review and assess the insurer's risk management function through utilization of the most current ORSA Summary Report received from the insurer. The lead state will direct the examination team to take steps to verify information included in the report and test the operating effectiveness of various risk management processes on a sample basis (e.g., reviewing certain supporting documentation from Section I; testing the reasonableness of certain inputs into stress testing from Section II; and reviewing certain inputs, assumptions and outputs from internal capital models).

**Detail Eliminated to Conserve Space**

# Attachment C

***Proposed Financial Condition Examiners Handbook Revisions***

# XI. REVIEWING AND UTILIZING THE RESULTS OF AN OWN RISK AND SOLVENCY ASSESSMENT

This section of the Handbook provides general guidance for use in reviewing, assessing and utilizing the results of an insurer's confidential Own Risk and Solvency Assessment (ORSA) in conducting risk-focused examinations. Therefore, this guidance may be used in support of the risk management assessments outlined in other sections of the Handbook (e.g., Phase 1, Part Two: Understanding the Corporate Governance Structure, Exhibit M – Understanding the Corporate Governance Structure) at the discretion of Lead State examiners.



## A. Background Information

The NAIC's *Risk Management and Own Risk and Solvency Assessment Model Act* (#505) requires insurers above a specified premium threshold, and subject to further discretion, to submit a confidential annual ORSA Summary Report. The model gives the insurer and insurance group (hereinafter referred to as "insurer" or "insurers" throughout the remainder of this guidance) discretion as to whether the report is submitted by each individual insurer within the group or by the insurer group as a whole. (See the *NAIC ORSA Guidance Manual* for further discussion.)

There is no expectation with respect to specific information or specific action that the Lead State regulator is to take as a result of reviewing the ORSA Summary Report. Rather, each situation is expected to result in a unique ongoing dialogue between the insurer and the Lead State regulator focused on the key risks of the group. For this reason, as well as others, the Lead State analyst may want to consider including the Lead State examiner or any other individual acting under the authority of the commissioner or designated by the commissioner with special skills and subject to confidentiality that may be of assistance in their initial review of the ORSA Summary Report in possible dialogue with the insurer since the same team will be part of the ongoing monitoring of the insurer and an ORSA Summary Report is expected to be at the center of the regulatory processes. A joint review such as this prior to the Lead State analyst documenting his or her summary of the ORSA report may be appropriate.

After participating in the initial review of information provided in the ORSA Summary Report, the Lead State examiner is expected to incorporate a review of ORSA information into ongoing on-site examination activities. Examiners are reminded that ORSA information is highly sensitive, proprietary and confidential, and examiners should exercise caution to ensure that no ORSA or ORSA-related materials are inadvertently made public in any way, including in any Exam Report. Depending upon the examination schedule or cycle, the Lead State examiner may consider performing a limited-scope exam to conduct on-site examination activities related to ORSA information on a timely basis. In incorporating a review of ERM/ORSA information into financial exam activities, the Lead State examiner should seek to utilize existing resources to avoid duplication of efforts and provide exam efficiencies.

In cases where one insurer provides an ORSA Summary Report, the domestic state is responsible for verifying, assessing and utilizing the information received to facilitate and gain efficiencies in conducting on-site examinations. In cases where a group of insurers provides an ORSA Summary Report (or multiple legal entities within an insurance group provide separate ORSA Summary Reports), the Lead State is expected to coordinate the review, assessment and utilization of the information received to facilitate and gain efficiencies in conducting coordinated examinations in accordance with Section 1, Part I of the Handbook. To the extent that an insurance group is organized into subgroups for examination purposes, the review, assessment and utilization of various aspects of the insurance group's ORSA Summary Report may require delegation of responsibilities to an Exam Facilitator. However, in all cases, examination teams should seek to avoid duplication and utilize existing work in reviewing, assessing and utilizing the ORSA Summary Report to conduct examinations of entities that are part of an insurance group. Throughout the remainder of this document, the term "Lead State" is used before the term "examiner" or "regulator" with the understanding that in most situations, the ORSA Summary Report will be prepared on a group basis, and, therefore, primarily reviewed by the Lead State. However, this does not remove the requirement for the domestic state to perform these responsibilities in the event of a single-entity ORSA Summary Report.

For additional guidance for sharing the ORSA Summary Report and/or the Lead State's analysis of the ORSA Summary Report with other regulators and/or other third parties, refer to the ORSA Information Sharing Best Practices found on the ORSA Implementation (E) Subgroup webpage.

As stated in the *NAIC ORSA Guidance Manual* (Guidance Manual), the ORSA has two primary goals:

1. To foster an effective level of ERM for all insurers, through which each insurer identifies, assesses, monitors, prioritizes and reports on its material and relevant risks identified by the insurer, using techniques appropriate to the nature, scale and complexity of the insurer's risks, in a manner adequate to support risk and capital decisions.

2. To provide a group-level perspective on risk and capital, as a supplement to the existing legal entity view.

The Guidance Manual states that regulators should obtain a high-level understanding of the insurer's ORSA framework, and discusses how the ORSA Summary Report may assist in determining the scope, depth and minimum timing of risk-focused analysis and examination procedures.

These determinations can be documented as part of each insurer's ongoing supervisory plan. However, the Guidance Manual also states that each insurer's ORSA will be unique, reflecting the insurer's business model, strategic planning and overall approach to ERM. As regulators review ORSA Summary Reports, they should understand that the level of sophistication for each group's ERM program will vary depending upon size, scope and nature of business operations. Understandably, less complex organizations may not require intricate processes to possess a sound ERM program. Therefore, regulators should use caution before using the results of an ORSA review to modify ongoing supervisory plans, as a variety of practices may be appropriate depending upon the nature, scale and complexity of each insurer.

Collectively, the goals above are the basis upon which the guidance is established. However, the ORSA Summary Report will not serve this function or have this direct impact until the Lead State becomes fairly familiar with and comfortable with evaluating each insurer's report and its processes. This could take more than a couple of years to occur in practice since the Lead State would likely need to review at least one or two ORSA Summary Reports to fully understand certain aspects of the processes used to develop the report.

**B. General Summary of Guidance for Each Section**

This section is designed to assist the examiner through general guidance regarding how each section of the ORSA Summary Report is expected to be reviewed and assessed during a financial examination. This guidance is expected to evolve over the years, with the first couple of years focused on developing a general understanding of ORSA and ERM. Each of the sections of the ORSA Summary Report requires distinct consideration to be adequately understood and assessed. However, each of the sections can supplement the understanding and assessment of the other sections. For example, Section II provides an insurer the opportunity to demonstrate the robustness of its process by including a detailed description of the reasonably foreseeable and relevant material risks it faces and their potential impact to the insurer. This can allow the Lead State regulator to gain a better understanding and increased appreciation for the insurer's processes to identify and prioritize reasonably foreseeable and relevant material risks described in Section I. Alternately, the Lead State regulator may assess stresses applied to individual risks in Section II as appropriate, but may not feel stresses are appropriately aggregated to determine an adequate group capital assessment in Section III. Therefore, the review and assessment of each section requires a full understanding of each of the other sections, and the Lead State regulator should exercise caution in the allocation of review responsibilities in this area.

Further, regulators do not believe there is a standard set of stress conditions each insurer should test. The Lead State examiner should never specify the stresses to be performed, nor what should be included in the insurer's ORSA Summary Report, as this would eliminate the "Own" aspect of the ORSA and defeat its purpose, which is to permit the Lead State regulator to better understand the risk from the perspective of the insurer. This is not to suggest that the Lead State examiner should not consider asking questions about the extent to which the insurer considers particular risks, as these questions may provide the insurer an opportunity to discuss the robustness of its processes and considerations, either in specifically identified stresses or the inclusion of similar risks within a stochastic economic capital model for a particular risk.

Background Information

Procedures are provided to assist the regulator in gaining an overall understanding of the ORSA Summary Report and assessing compliance with reporting requirements in several critical areas.

Section I

The guidance in Section I is designed to assist the Lead State examiner in performing procedures to verify and validate relevant information and assess~~reaching an assessment of~~ the risk management framework of the insurer. The Lead State examiner's assessment should utilize existing assessments of the insurer's risk management framework performed by the Lead State financial analyst through a review of the ORSA Summary Report, but should supplement the Lead State analyst's assessment with additional on-site verification and testing to reach a final conclusion.

The Section I procedures are focused on ~~determining the insurer's maturity level in regards to its~~the overall risk management framework of the insurer/group. . The procedures are presented as considerations to be taken into account when reviewing and assessing an insurer's implementation of each of the risk management principles highlighted in the NAIC's ORSA Guidance Manual. ~~The maturity level may be assessed through several ways, one of which is the incorporation of concepts developed within the Risk and Insurance Management Society's (RIMS) Risk Maturity Model (RMM). While insurers or insurance groups may utilize various frameworks in developing, implementing and reporting on their ORSA processes (e.g. COSO Integrated Framework, ISO 31000, IAIS ICP 16, other regulatory frameworks, etc.), elements of the RMM have been incorporated into this guidance to provide a framework for use in reviewing and assessing ERM/ORSA practices. However, as various frameworks may be utilized to support effective ERM/ORSA practices, Lead State regulators should be mindful of differences in frameworks and allow flexibility in assessing maturity levels. The RMM, which is only one of several processes that may be used to determine maturity levels, provides a scale of six maturity levels upon which an insurer can be assessed. The six maturity levels can generally be defined as follows:~~

~~Level 5: Risk management is embedded in strategic planning, capital allocation and other business processes, and is used in daily decision-making. Risk limits and early warning systems are in place to identify breaches and require corrective action from the board of directors or committee thereof (hereafter referred to as "board") and management.~~

~~Level 4: Risk management activities are coordinated across business areas, and tools and processes are actively utilized. Enterprise-wide risk identification, monitoring, measurement and reporting are in place.~~

~~Level 3: The insurer has risk management processes in place designed and operated in a timely, consistent and sustained way. The insurer takes action to address issues related to high priority risks.~~

~~Level 2: The insurer has implemented risk management processes, but the processes may not be operating consistently and effectively. Certain risks are defined and managed in silos, rather than consistently throughout the organization.~~

~~Level 1: The insurer has not developed or documented standardized risk management processes and is relying on the individual efforts of staff to identify, monitor and manage risks.~~

~~Level 0: The insurer has not recognized a need for risk management, and risks are not directly identified, monitored or managed.~~

~~The guidance developed for use in this Handbook integrates the concepts of the RMM with the general principles and elements outlined in Section I of the Guidance Manual to assist Lead State regulators in reaching an overall assessment of~~

~~the maturity of an insurer's risk management framework.~~ In assessing implementation, regulators should consider whether ~~T~~the design of ERM/ORSA practices should appropriately reflect the nature, scale and complexity of the company. ~~Lead State regulators should understand the level of maturity that is appropriate for the company based on its unique characteristics. Attainment of Level 5 maturity for ERM/ORSA practices is not appropriate, nor should be expected, for all companies or for all components of the framework.~~

Section II

The guidance for use in reviewing Section II is primarily focused on assisting the Lead State examiner in gaining an understanding of management's assessment of its reasonably foreseeable and relevant material risks. In addition, the guidance assists the Lead State examiner in understanding the potential impact of reasonably foreseeable and relevant material risks by considering the stress scenarios and stress testing presented by the insurer. Finally, information in Section II can inform or support the assessment of key principles reached during a review of Section I.

In order for the Lead State examiner to understand and utilize the information on reasonably foreseeable and relevant material risks provided in Section II, the Lead State examiner must obtain a minimum level of confidence regarding the reasonability of the information presented. ~~Much of the~~ Section II guidance has been developed around reviewing key risks assessed by the company and classifying them within the nine branded risk classifications outlined in Exhibit L of this Handbook, which are used as a common language in the risk-focused surveillance process. ~~The primary reason for this approach is that insurers may utilize similar risk classifications in their ORSA Summary Reports. However, Lead State regulators should not restrict their focus to only the nine branded risk classifications as such an approach may not encourage independent judgment in understanding the risk profile of the insurer. Therefore, the use of the nine branded risk classifications provides a framework to organize the Lead State's summary, but should not discourage regulators from documenting other risks or excluding branded risk categories that aren't relevant. From this standpoint, Section II will also provide regulators with information to better understand current insurance market risks, changes in those risks as well as macroeconomic changes, and the impact they have on insurers' risk identification and risk management processes.~~

As part of evaluating the information presented on reasonably foreseeable and relevant material risks, the Lead State examiner may document how the insurer determines the appropriateness of its stress scenarios identified and stress testing performed by the insurer. However, regulators do not believe there is a standard set of stress conditions each insurer should test. Consistent with the language in the Guidance Manual, the Lead State examiner should not specify the stresses to be performed (other than in rare situations deemed necessary by the commissioner), nor what should be included in the company's ORSA Summary Report beyond the basic framework necessary to understand the work performed. Therefore, guidance has been provided to assist the Lead State examiner in considering the reasonableness of the assumptions and methodologies used in conducting stress scenarios/testing and to facilitate discussion with the insurer.

Section III

The guidance for reviewing Section III of the ORSA Summary Report is intended to assist the Lead State examiner in understanding and assessing the estimated amount of capital the insurer determines is ~~reasonable~~ needed to sustain its current ~~business model~~risk profile, as well as its prospective solvency position on an ongoing basis. This determination typically utilizes internally developed capital models that estimate the distribution of potential losses and associated probabilities. Other insurers might base their determination on rating agency or regulatory capital models to determine the amount of capital needed to support a particular rating or to quantify the amount of capital at risk in case of extreme shocks. ~~and/or aggregates the outputs of Section II (i.e., stress testing) to calculate the amount of capital required to support ongoing business operations for a wide range of potential outcomes.~~ All of these approaches require the insurer to establish a capital quantification methodology and select supporting assumptions. Therefore, much of the guidance in this section relates back to how the insurer determines the reasonableness of the ~~assumptions and~~capital quantification methodolog~~ies~~y and assumptions, as well as the process undertaken by the insurer to validate the inputs, calculations and outputs.~~utilized to calculate and allocate capital to the reasonably foreseeable and relevant material risks it faces. Often, this calculation may be wholly or partially based on internal models developed by the insurer for this purpose. Therefore, the guidance also directs the Lead State examiner to consider and evaluate the insurer's processes to validate the suitability, reasonability and reliability of its internal models.~~

**C. Review of Background Information**

The ORSA Guidance Manual encourages discussion and disclosure of key pieces of information to assist regulators in reviewing and understanding the ORSA Summary Report. As such, the following considerations are provided to assist the Lead State examiner in reviewing and assessing the information provided in these areas.

| Consideration | Description | Possible Test Procedure(s) |
|---|---|---|
| Attestation | The report includes an attestation signed by the Chief Risk Officer (or other executive responsible for ERM) indicating that the information presented is accurate and consistent with ERM reporting shared with the Board of Directors (or committee thereof). | • Consider the results of review/test procedures performed in Sections I - III to evaluate the accuracy of information in the ORSA Summary Report to verify this attestation<br>• Obtain and review BOD (or appropriate committee) minutes or packets to verify that ORSA Summary Report (or similar ERM documentation) is subject to an appropriate level of review and oversight |
| Entities in Scope | The scope of the report is clearly explained and identifies all insurers covered. The scope of a group report also indicates whether material non-insurance operations have been covered. | • Compare insurance entities covered in ORSA report to Schedule Y and holding company filings to identify any missing entities<br>• Obtain and review information provided in Form F to get an understanding of whether non-insurance entities pose a risk to the insurance entities<br>• If necessary, obtain and review the non-U.S. ORSA report(s) to get a full understanding of the group's risk capital<br>   o Review the home jurisdiction's ORSA requirements and compare against the NAIC ORSA Guidance Manual to understand differences |
| Accounting Basis | The report clearly indicates the accounting basis used to present financial information in the report, as well as the primary valuation date(s). | • Compare valuation date and accounting basis utilized across various sections of the report to ensure consistency<br>• If multiple accounting bases are used, gain an understanding of which basis is used to manage capital |
| Key Business Goals | The report provides an overview of the insurer's/group's key business goals in order to demonstrate alignment with the relevant and material risks presented within the report. | • Compare the key business goals summarized in the report against other company filings and documents (e.g., MD&A, Holding Company Filings, submitted business plans, etc.) other regulatory documents (i.e. IPS/GPS) and the regulator's understanding of the insurer<br>   o If inconsistencies are noted, discuss with the company to determine if any key risks are excluded from assessment within the ORSA |
| Changes from Prior Filing(s) | The report clearly discusses significant changes from the prior year filing(s) to highlight areas of focus in the current year review including changes to the ERM framework, risks assessed, stress scenarios, overall capital position, modeling assumptions, etc. | • Focus test procedures in Section I, II and III on significant changes from prior filings<br>• Verify appropriate governance over changes by requesting supporting documentation and approvals for a sample of changes made<br>• After completing a review of other sections of the ORSA, consider whether all significant changes from the PY filing were appropriately summarized and disclosed |
| Planned ERM Enhancements | The report provides information on planned enhancements for improving the effectiveness of the insurer's/group's ERM practices to demonstrate ongoing development and a functioning feedback loop. | • Perform procedures to understand and evaluate the current status of planned enhancements to verify information reported and assess the adequacy of governance over planned enhancements |

**D. Review of Section I - Description of the Insurer's Risk Management Framework**

The Guidance Manual requires the insurer to discuss five key principles of an effective risk management framework in Section I of the ORSA Summary Report. Therefore, the Lead State examiner is required to review and assess the insurer's risk management framework by considering and evaluating each of the key principles. Upon receipt of the ORSA Summary Report, the Lead State financial analyst should perform an initial, high-level assessment of each of the key principles. During an on-site examination, the Lead State examiner is expected to supplement this initial assessment with additional procedures to verify the reported information and test the operating effectiveness of the insurer's risk management processes and practices. Upon conclusion of these procedures, the Lead State examiner should reach his or her own assessment regarding each of the five principles. This should be utilized to adjust the scope of the risk-focused examination and communicated back to the Lead State financial analyst for ongoing monitoring and adjustment of the supervisory plan.

Guidance is provided to assist the Lead State examiner in ~~developing review procedures and to give examples of attributes that may indicate the insurer is more or less mature in its handling of the individual~~assessing the effectiveness of the insurer's key risk management principles.~~ These attributes are meant to assist the Lead State examiner in reaching an assessment of the insurer's maturity level for each key principle.~~

Key Principles

1. Risk Culture and Governance
2. Risk Identification and Prioritization
3. Risk Appetite, Tolerances and Limits
4. Risk Management and Controls
5. Risk Reporting and Communication

Considerations When Reviewing and Testing Key Principles

When reviewing processes described in the ORSA Summary Report, the Lead State examiner should consider the extent to which the above principles are integrated into the organization. To do so, the Lead State examiner may need to review processes and practices beyond those documented within the ORSA Summary Report. In addition, the Lead State examiner may need to review and consider changes made to risk management processes since the filing of the last ORSA Summary Report. ~~In so doing, the Lead State examiner may consider information beyond what is included in the ORSA Summary Report to reach an assessment of the insurer's maturity level for each key principle.~~

In reviewing these key principles, examples of various ~~attributes/traits associated with various maturity levels~~considerations and possible test procedures for each key principle are provided. However, these ~~attributes~~ considerations and procedures only ~~demonstrate common currently known practices associated with each of the various maturity levels,~~ address certain elements associated with the key principles and practices of individual insurers may vary significantly.~~ from the examples provided. It is possible that the insurer has mature practices in place, even if those practices differ from the example attributes provided.~~ Therefore, the Lead State examiner should exercise professional judgment in determining the appropriate ~~maturity level to select~~consideratios and procedures to be performed when assessing each of the key risk management principles.

~~The following table provides example test procedures that may be performed by the Lead State examiner to verify information on risk management processes included in the ORSA Summary Report or to test the operating effectiveness of such practices.~~ Several of these procedures may be performed in conjunction with other risk-focused examination processes, and Lead State examiners should attempt to gain efficiencies by coordinating testing and review efforts wherever possible. Lead State examiners should use professional judgment in selecting or tailoring procedures to assist in the assessment of each of the five risk management principles for the insurer. In addition, the Lead State examiner should incorporate any specific verification or testing recommendations made by the Lead State financial analyst into the planned examination procedures for Section I and consider the extent to which additional procedures should be utilized to test the changes that have been made to the insurer's ERM framework since the last on-site examination.

1. **Risk Culture and Governance**

It's important to note some organizations view risk culture and governance as the cornerstone to managing risk. The Guidance Manual defines this item to include a structure that clearly defines and articulates roles, responsibilities and accountabilities, as well as a risk culture that supports accountability in risk-based decision making. Therefore, the objective is to have a structure in place within the organization that manages reasonably foreseeable and relevant material risk in a way that is continuously improved. Key considerations and possible test procedures for use in reviewing and assessing risk culture and governance might include, but aren't limited to:

| Consideration | Description | Possible Test Procedure(s) |
|---|---|---|
| Roles & Responsibilities | Roles and responsibilities of key stakeholders in ERM are clearly defined and documented, including members of the board (or committee thereof), officers and senior executives, risk owners, etc. | • Review documentation to determine whether key stakeholders are identified and roles are clearly defined within the ERM framework<br>• Consider the results of review/test procedures performed across Sections I-III to determine whether roles are effectively implemented |
| Board or Committee Involvement | The Board of Directors or appropriate committee thereof demonstrates active involvement in and oversight of ERM activities through regular monitoring, reporting and recommendations | • Obtain and review management, board or committee minutes/packets for the director group responsible for ERM oversight and evaluate the level of oversight provided<br>• Interview board member(s) with responsibilities for risk management oversight to determine level of knowledge and involvement of directors in risk oversight activities |
| Strategic Decisions | Directors, officers and other members of senior management utilize information generated through ERM processes in making strategic decisions | • Interview management or board member(s) to determine how risk management processes and results are utilized in strategic decision making<br>• Evaluate the consistency between the insurer's business strategy and its risk management processes<br>• Evaluate whether the insurer utilizes ERM to identify strategic opportunities, as opposed to focusing only on limiting exposures |
| Staff Availability & Education | The insurer/group maintains suitable staffing (e.g. sufficient number, educational background, experience) to support its ERM framework and deliver on its risk strategy | • Obtain and review information on the staffing and activity of key ERM functions (e.g. ERM group, Internal Audit, etc.) to evaluate their level of activity and involvement<br>• Select a sample of key individuals to review job descriptions and biographical information for appropriateness and suitability<br>• Interview a sample of key individuals to assess their suitability and verify their involvement in the operation of the ERM framework<br>• Obtain and review evidence of formalized risk training programs for staff and consider whether the training matches the risk profile of the insurer/group |
| Leadership | The Chief Risk Officer (or equivalent position) possesses an appropriate level of knowledge and experience related to ERM and receives an appropriate level of authority to effectively fulfill responsibilities | • Obtain and review information necessary (i.e. biographical affidavit or equivalent) to evaluate the suitability of the Chief Risk Officer (or equivalent position)<br>• Obtain and review information necessary to evaluate the authority and resources provided to the CRO to fulfill responsibilities<br>• Review BOD/committee minutes to verify CRO access and reporting to the BOD/committee on a regular basis and assess the CRO's response to BOD recommendations |
| Compensation | The insurer/group demonstrates that incentives, compensation and performance management criteria have been appropriately aligned with ERM processes and do not encourage excessive risk taking given the capital position of the insurer/group | • Obtain and review information on the insurer's compensation plans to determine that risk management decision-making is not undermined by compensation structure<br>• Obtain and review job descriptions or performance review criteria for select management positions to determine whether risk management elements are incorporated<br>• Interview a member(s) of the BOD (or appropriate committee thereof) to discuss oversight of compensation and understand if there are concerns about excessive risk taking |
| Integration | The insurer/group integrates and coordinates ERM processes across functional areas of the organization | • Interview selected executives from different functional areas to get a feel for the "tone at the top" of the organization and the level of consistency in applying risk management processes across departments |

| | | |
|---|---|---|
| | including HR, IT, internal audit, compliance, business units, etc. | |
| Assessment | The insurer's ERM framework is subject to regular review and assessment, with updates made to the framework as deemed necessary | • Gain an understanding of the insurer's process to review and update its ERM framework to ensure involvement of appropriate stakeholders<br>• Perform procedures to verify the insurer is reviewing and updating its framework on a regular basis |

~~Level 5~~

~~Risk culture is analyzed and reported as a systematic view of evaluating risk. Executive sponsorship is strong, and the tone from the top has sewn an ERM framework into the corporate culture. Management establishes the framework and the risk culture, and the board reviews the risk appetite statement in collaboration with the chief executive officer (CEO), chief risk officer (CRO) where applicable and chief financial officer (CFO). Those officers translate the expectations into targets through various practices embedded throughout the organization. Risk management is embedded in each material business function. Internal audit, information technology, compliance, controls and risk management processes are integrated, and coordinate and report risk issues. Material business functions use risk-based best practices. The risk management life cycle for business process areas are routinely evaluated and improved (when necessary).~~

~~Level 4~~

~~The insurer's ERM processes are self-governed with shared ethics and trust. Management is held accountable. Risk management issues are understood and risk plans are conducted in material business process areas. The board, CEO, CRO (if applicable) and CFO expect a risk management plan to include a qualitative risk assessment for reasonably foreseeable and relevant material risks with reporting to management or the board on priorities, as appropriate. Relevant areas use the ERM framework to enhance their functions, communicating on risk issues as appropriate. Process owners incorporate managing their risks and opportunities within regular planning cycles. The insurer creates and evaluates scenarios consistent with its planning horizon and product timelines, and follow-up activities occur accordingly.~~

~~Level 3~~

~~ERM risk plans are understood by management. Senior management expects that a risk management plan captures reasonably foreseeable and relevant material risks in a qualitative manner. Most areas use the ERM framework and report on risk issues. Process owners take responsibility for managing their risks and opportunities. Risk management creates and evaluates scenarios consistent with the business planning horizon.~~

~~Level 2~~

~~Risk culture is enforced by policies interpreted primarily as compliance in nature. An executive champions ERM management to develop an ERM framework. One area has used the ERM framework, as shown by the department head and documented team activities. Business processes are identified, and ownership is defined. Risk management is used to consider risks in line with the insurer's business planning horizon.~~

~~Level 1~~

~~Corporate culture has little risk management accountability. Risk management is not interpreted consistently. Policies and activities are improvised. Programs for compliance, internal audit, process improvement and IT operate independently and have no common framework, causing overlapping risk assessment activities and inconsistencies. Controls are based on departments and finances. Business processes and process owners are not well defined or communicated. Risk management focuses on past events. Qualitative risk assessments are unused or informal. Risk management is considered a quantitative analysis exercise.~~

~~Level 0~~

~~There is no recognized need for an ERM process and no formal responsibility for ERM. Internal audit, risk management, compliance and financial activities might exist, but they aren't integrated. Business processes and risk ownership are not well defined.~~

2. **Risk Identification and Prioritization**

The Guidance Manual defines this as key to the organization, and responsibility for this activity should be clear. The risk management function is responsible for ensuring the processes are appropriate and functioning properly. Therefore, an approach for risk identification and prioritization may be to have a process in place that identifies risk and prioritizes such risks in a way that potential reasonably foreseeable and relevant material risks are addressed in the framework. Key considerations and possible test procedures for use in reviewing and assessing risk identification and prioritization might include, but aren't limited to:

| **Consideration** | **Description** | **Possible Test Procedure(s)** |
| --- | --- | --- |
| Resources | The insurer/group utilizes appropriate resources and tools (e.g. questionnaires, external risk listings, brainstorming meetings, regular calls, etc.) to assist in the risk identification process that are appropriate for its nature, size and structure | • Obtain and review information and tools associated with the risk identification and prioritization process for appropriateness<br>• Determine whether appropriate external sources have been used to assist in risk identification (e.g. rating agency information, emerging risk listings, competitor 10K filings, etc.) where applicable<br>• Obtain and review lists of key risks (or risk register) at different dates to identify which risks have been added/removed to understand and assess the process |
| Stakeholder Involvement | All key stakeholders (i.e. directors, officers, senior management, business unit leaders, risk owners, etc.) are involved in risk identification and prioritization at an appropriate level | • Interview select process owners/business unit leaders to verify their role in risk identification and prioritization<br>• Interview risk management staff to understand and evaluate how risks are identified and aggregated across the organization |
| Prioritization Factors | Appropriate factors and considerations are utilized to assess and prioritize risks (e.g. likelihood of occurrence, magnitude of impact, controllability, speed of onset, etc.) | • Assess the insurer's process and scale by which it prioritizes the key risks identified<br>• Review the approach for, and results of, the insurer's likelihood, severity and speed of onset risk assessments, if applicable |
| Process Output | Risk registers, key risk listings and risk ratings are maintained, reviewed and updated on a regular basis | • Obtain and review a current copy of the organization's risk register<br>• Verify that the organization's risk register is updated/reviewed on a regular basis by requesting copies at various dates |
| Emerging Risks | The company has developed and maintained a formalized process for the identification and tracking of emerging risks | • Obtain and review tools and reports utilized to identify and evaluate emerging risks to determine whether appropriate stakeholders and resources are utilized in this process |

~~Level 5~~

~~Information from internal and external sources on reasonably foreseeable and relevant material risks, including relevant business units and functions, is systematically gathered and maintained. A routine, timely reporting structure directs risks and opportunities to senior management. The ERM framework promotes frontline employees' participation and documents risk issues' or opportunities' significance. Process owners periodically review and recommend risk indicators that best measure their areas' risks. The results of internal adverse event planning are considered a strategic opportunity.~~

~~Level 4~~

~~Process owners manage an evolving list of reasonably foreseeable and relevant material risks locally to create context for risk assessment activities as a foundation of the ERM framework. Risk indicators deemed critical to their areas are regularly reviewed in collaboration with the ERM team. Measures ensure downside and upside outcomes of risks and opportunities are managed. Standardized evaluation criteria of impact, likelihood and controls' effectiveness are used to prioritize risk for follow-up activity. Risk mitigation is integrated with assessments to monitor effective use.~~

~~Level 3~~
~~An ERM team manages an evolving list of reasonably foreseeable and relevant material risks, creating context for risk assessment as a foundation of the ERM framework. Risk indicator lists are collected by most process owners. Upside and downside outcomes of risk are understood and managed. Standardized evaluation criteria of impact, likelihood and controls' effectiveness are used, prioritizing risk for follow-ups. Enterprise-level information on risks and opportunities are shared. Risk mitigation is integrated with assessments to monitor effective use.~~

~~Level 2~~
~~Formal lists of reasonably foreseeable and relevant material risks exist for each relevant business unit or function, and discussions of risk are part of the ERM process. Corporate risk indicators are collected centrally, based on past events. Relevant business units or functions might maintain their own informal risk checklists that affect their areas, leading to potential inconsistency, inapplicability and lack of sharing or under-reporting.~~

~~Level 1~~
~~Risk is owned by specialists, centrally or within a business unit or function. Risk information provided to risk managers is probably incomplete, dated or circumstantial, so there is a high risk of misinformed decisions, with potentially severe consequences. Further mitigation, supposedly completed, is probably inadequate or invalid.~~

~~Level 0~~
~~There might be a belief that reasonably foreseeable and relevant material risks are known, although there is probably little documentation.~~

3. **Risk Appetite, Tolerances and Limits**

The Guidance Manual states that a formal risk appetite statement, and associated risk tolerances and limits, are foundational elements of a risk management framework for an insurer. While risk appetites, tolerances and limits can be defined and used in different ways across different organizations, this guidance is provided to assist the regulator in understanding and evaluating the insurer's practices in this area. Risk appetite can be defined as the amount of specific and aggregate risk that an organization chooses to take during a defined time period in pursuit of its business objectives. ~~Understanding~~ Articulation of the risk appetite statement ensures alignment ~~with~~ of the risk strategy with the business strategy set by senior management and reviewed and evaluated by the board. Not included in the Guidance Manual, but widely considered, is that risk appetite statements should be easy to communicate, understood and closely tied to the organization's strategy.

After the overall risk appetite for the organization is determined, the underlying risk tolerances and limits can be selected and applied to business units and specific key risks identified by ~~areas as~~ the company ~~deems appropriate~~. Risk tolerance can be defined as the aggregate risk-taking capacity of an organization. Risk limits can be defined as thresholds used to monitor the actual exposure of a specific risk or activity unit of the organization to ensure that the level of actual risk remains within the risk tolerance. The company may apply appropriate quantitative limits and qualitative statements to help establish boundaries and expectations for risks that are hard to measure. These boundaries may be expressed in terms of earnings, capital or other metrics, such as growth and volatility. The risk tolerances/limits provide direction outlining the insurer's tolerance for taking on certain risks, which may be established and communicated in the form of the maximum amount of such risk the entity is willing to take. However, in many cases, these will be coupled with more specific and detailed limits or guidelines the insurer uses.

Due to the varying level of detail and specificity different organizations incorporate into their risk appetites, tolerances and limits, Lead State regulators should consider these elements collectively to reach an overall assessment in this area and should seek to understand the insurer's approach through follow-up discussions and dialogue. Key considerations and possible test procedures for use in reviewing and assessing risk appetite, tolerance and limits might include, but aren't limited to:

| Consideration | Description | Possible Test Procedure(s) |
|---|---|---|
| Risk Appetite Statement | The insurer/group has adopted an overall risk appetite statement consistent with its business plans and operations that is updated on a regular basis and approved by | • Determine whether the insurer considers legal entity regulations and capital requirements in setting its overall risk appetite (if applicable) |

| | | |
|---|---|---|
| | the board of directors (or committee thereof) | • Consider whether the insurer appropriately considers both qualitative and quantitave measures of risk appetite<br>• Evaluate the appropriateness of the risk appetite statement and its consistency with the insurer's business strategy<br>• Review board/committee minutes or supporting materials to verify that the organization's risk appetite is reviewed, updated and approved as appropriate |
| Risk Tolerances/Limits | Tolerances and limits are developed for key risks in accordance with the overall risk appetite statement | • Select a sample of key risks to verify that specific tolerances and limits have been put in place<br>• Gain an understanding of the checks and balances (i.e. supervisory review) in place to ensure that tolerances and limits are in accordance with the risk appetite<br>• Review and evaluate the consistency between the insurer's risk appetite, tolerances and limits, as well as their appropriateness in light of the business strategy |
| Risk Owners | Key risks are assigned to risk owners with responsibility for monitoring and reporting on risk tolerances and limits, including actions to address any breaches | • Verify, as applicable, that all key risks are assigned appropriate risk owners<br>• Interview select risk owners to get an understanding of and assess their roles and responsibilities in setting/updating tolerances and limits |

~~Level 5~~
~~A risk appetite statement has been developed to establish clear boundaries and expectations for the organization to follow. A process for delegating authority to accept risk levels in accordance with the risk appetite statements is communicated throughout the organization. The management team and risk management committee, if applicable, may define tolerance levels and limits on a quantitative and/or qualitative basis for relevant business units and functions in accordance with the defined risk appetite. As part of its risk management framework, the company may compare and report actual assessed risk versus risk tolerances/limits. Management prioritizes resource allocation based on the gap between risk appetite and assessed risk and opportunity. The established risk appetite is examined periodically.~~

~~Level 4~~
~~Risk appetite is considered throughout the ERM framework. Resource allocation decisions consider the evaluation criteria of business areas. The organization forecasts planned mitigation's potential effects versus risk tolerance as part of the ERM framework. The insurer's risk appetite is updated as appropriate and risk tolerances are evaluated from various perspectives as appropriate. Risk is managed by process owners. Risk tolerance is evaluated as a decision to increase performance and measure results. Risk-reward tradeoffs within the business are understood and guide actions.~~

~~Level 3~~
~~Risk assumptions within management decisions are clearly communicated. There's a structure for evaluating risk on an enterprise-wide basis and for gauging risk tolerance. Risks and opportunities are routinely identified, evaluated and executed in alignment with risk tolerances. The ERM framework quantifies gaps between actual and target tolerances. The insurer's risk appetite is periodically reviewed and updated as deemed appropriate by the company, and risk tolerances are evaluated from various perspectives as appropriate.~~

~~Level 2~~
~~Risk assumptions are only implied within management decisions and are not understood outside senior leadership with direct responsibility. There is no ERM framework for resource allocation. Defining different views of business units or functions from a risk perspective cannot be easily created and compared.~~

~~Level 1~~
~~Risk management might lack a portfolio view of risk. Risk management might be viewed as risk avoidance and meeting compliance requirements or transferring risk through insurance. Risk management might be a quantitative approach focused on the analysis of high-volume and mission-critical areas.~~

~~Level 0~~
~~The need for formalizing risk tolerance and appetite is not understood.~~

4. **Risk Management and Controls**

The Guidance Manual stresses managing risk is an ongoing ERM activity, operating at many levels within the organization. This principle is discussed within the governance section above from the standpoint that a key aspect of managing and controlling the reasonably foreseeable and relevant material risks of the organization is the risk governance process put in place. For many companies, the day-to-day governance starts with the relevant business units. Those units put mechanisms in place to identify, quantify and monitor risks, which are reported up to the next level based upon the risk reporting triggers and risk limits put in place. In addition, controls are also put in place on the back end, by either the ERM function or the internal audit team~~ or an independent consultant~~, which are designed to ensure compliance and a continual enhancement approach. Therefore, one approach may be to put controls in place to ensure the organization is abiding by its limits. Key considerations and possible test procedures for use in reviewing and assessing risk management and controls might include, but aren't limited to:

| Consideration | Description | Possible Test Procedure(s) |
|---|---|---|
| Lines of Defense | Multiple lines of defense (i.e. business unit or risk owners, ERM function, internal audit) are put in place to ensure that control processes are effectively implemented and maintained | • Gain an understanding of business unit involvement in risk management and control processes to assess appropriateness<br>• Review, verify and evaluate the role of ERM staff in setting and enforcing risk management processes and controls<br>• Obtain a listing of internal audit reports to determine whether risk management processes are subject to periodic review.<br>• Perform procedures to verify and evaluate segregation of duties between business units, ERM staff and the internal audit department in carrying out risk management responsibilities. |
| Control Processes | Specific control activities and processes are put in place to manage, mitigate and monitor all key risks | • Obtain minutes of internal risk management committee (or equivalent management group) meetings to review frequency and extent of oversight activities.<br>• Review and evaluate how specific controls are mapped to legal entities (as appropriate if mapping is relevant to understanding of control).<br>• Select a sample of key risks to verify that risk controls and mitigation activities are identified and implemented |
| Implementation of Tolerances /Limits | Risk tolerances and limits are translated into operational guidance and policies around key risks through all levels of the organization | • Select a sample of key risks to verify that operational guidance and policies at mutliple levels/areas of the organization are in place and consistent with risk limits identified through ORSA process<br>• Identify and test the operating effectiveness of preventive controls in select areas to determine how risk tolerances/limits are enforced. |
| Indicators/Metrics | Key risk indicators or performance metrics are put in place to monitor exposures, provide early warnings and measure adherence to risk tolerances/limits | • Select a sample of key risks to verify that risk metrics have been identified to monitor exposures, provide early warnings and measure adherence to tolerances/limits<br>• Perform procedures to verify that risk metrics are measured and monitored accurately and on a regular basis<br>• Review and evaluate escalation process and remediation efforts when limits on key risks are breached |

~~Level 5~~
~~ERM, as a management tool, is embedded in material business processes and strategies. Roles and responsibilities are process-driven, with teams collaborating across material central and field positions. Risk and performance~~

~~assumptions within qualitative assessments are routinely revisited and updated. The organization uses an ERM process of sequential steps that strive to improve decision-making and performance. A collaborative, enterprise-wide approach is in place to establish a risk management committee staffed by qualified management. Accountability for risk management is woven into all material processes, support functions, business lines and geographies as a way to achieve goals. To evaluate and review the effectiveness of ERM efforts and related controls, the organization has implemented a "Three Lines of Defense" model or similar system of checks and balances that is effective and integrated into the insurer's material business processes. The first line of defense may consist of business unit owners and other front-line employees applying internal controls and risk responses in their areas of responsibility. The second line of defense may consist of risk management, compliance and legal staff providing oversight to the first line of defense and establishing framework requirements to ensure reasonably foreseeable and relevant material risks are actively and appropriately managed. The third line of defense may consist of auditors performing independent reviews of the efforts of the first two lines of defense to report back independently to senior management or the board, as appropriate.~~

~~Level 4~~
~~Risk management is clearly defined and enforced at relevant levels. A risk management framework articulates management's responsibility for risk management, according to established risk management processes. Management develops and reviews risk plans through involvement of relevant stakeholders. The ERM framework is coordinated with managers' active participation. Opportunities associated with reasonably foreseeable and relevant material risks are part of the risk plans' expected outcome. Authentication, audit trail, integrity and accessibility promote roll-up information and information sharing. Periodic reports measure ERM progress on all reasonably foreseeable and relevant material risks for stakeholders, including senior management or the board, as appropriate. The organization has implemented a "Three Lines of Defense" model to review and assess its control effectiveness, but those processes may not yet be fully integrated or optimized.~~

~~Level 3~~
~~The ERM framework supports material business units' and functions' needs. ERM is a process of steps to identify, assess, evaluate, mitigate and monitor reasonably foreseeable and relevant material risks. ERM frameworks include the management of opportunities. Senior management actively reviews risk plans. The ERM process is collaborative and directs important issues to senior management. The "Three Lines of Defense" are generally in place but are not yet performing at an effective level.~~

~~Level 2~~
~~Management recognizes a need for an ERM framework. Agreement exists on a framework, which describes roles and responsibilities. Evaluation criteria are accepted. Risk mitigation activities are sometimes identified but not often executed. Qualitative assessment methods are used first in all material risk areas and inform what needs deeper quantitative methods, analysis, tools and models. The "Three Lines of Defense" are not yet fully established, although some efforts have been made to put these processes in place.~~

~~Level 1~~
~~Management is reactive, and ERM might not yet be seen as a process and management tool. Few processes and controls are standardized and are instead improvised. There are no standard risk assessment criteria. Risk management is involved in business initiatives only in later stages or centrally. Risk roles and responsibilities are informal. Risk assessment is improvised. Standard collection and assessment processes are not identified.~~

~~Level 0~~
~~There is little recognition of the ERM framework's importance or controls in place to ensure its effectiveness.~~

## 5. Risk Reporting and Communication

The Guidance Manual indicates risk reporting and communication provides key constituents with transparency into the risk-management processes and facilitates active, informal decisions on risk-taking and management. The transparency is generally available because of reporting that can be made available to management, the board or compliance departments, as appropriate. However, most important is how the reports are being utilized to identify and manage reasonably foreseeable and relevant material risks at either the group, business unit or other level within the organization where decisions are made.

Therefore, one approach may be to have reporting in place that allows decisions to be made throughout the organization by appropriately authorized people, with ultimate ownership by senior management or the board, as appropriate. Key considerations and possible test procedures for use in reviewing and assessing risk reporting and communication might include, but aren't limited to:

| Consideration | Description | Possible Test Procedure(s) |
|---|---|---|
| Training | The importance of ERM processes and changes to the risk strategy are clearly communicated to all impacted areas and business units through ongoing training | • Obtain and review formal ERM training materials provided by the insurer to relevant employees and directors<br>• Review records of recent training sessions to verify sessions are regular and ongoing and attended by all key stakeholders involved in the design, oversight and operation of the ERM framework |
| Key Risk Indicator Reporting | Summary reports on risk exposures (i.e. key risk indicators) and compliance with tolerances/limits are maintained and updated on a regular basis | • Obtain a current copy of the organization's risk dashboard (or equivalent report) to verify that tracking for key risks is appropriate and to obtain a more current view of risks since the last ORSA valuation date<br>• Verify the frequency with which risk information is accumulated and reported by selecting a sample of historical risk dashboards (or equivalent reports) to review<br>• Test the reasonableness of key risk indicator information included on the risk dashboard (or equivalent report) on a sample basis |
| Oversight | Summary reports are reviewed and discussed by directors, officers and other members of senior management on a regular basis | • Review meeting minutes and packets to determine whether risk reporting information is evaluated by the board and used by senior management for strategy and planning purposes<br>• Gain an understanding of and evaluate the BOD's (or committee thereof) role in overseeing, reviewing and approving the ORSA process and resulting Summary Report<br>• Select a sample of ERM information reported to the BOD for comparison against the ORSA Summary Report to validate accuracy and consistency in reporting |
| Breach Management | Breaches of limits and dashboard warning indicators are addressed in a timely manner through required action by directors and officers | • Select a sample of breaches from recent dashboard reports to determine whether Senior Management and/or the BOD take an active role in addressing breaches and/or significant changes in risk exposure<br>• For the sample selected, review and evaluate the timeliness with which breaches in risk limits are reported and communicated to the appropriate authority |
| Feeback Loop | A feedback loop is embedded into ERM processes to ensure that results of monitoring and review discussions on key risks by senior management and the board are incorporated by business unit leaders and risk owners into ongoing risk-taking activities and risk management processes | • Discuss with ERM staff how input and feedback from BOD/committee or Senior Management review of summary reports is incorporated into risk management processes<br>• Review relevant BOD/committee minutes and select a sample of decisions made on ERM to verify that they were appropriately incorporated into ongoing processes |

~~Level 5~~

~~The ERM framework is an important element in strategy and planning. Evaluation and measurement of performance improvement is part of the risk culture. Measures for risk management include process and efficiency improvement. The organization measures the effectiveness of managing uncertainties and seizing risky opportunities. Deviations from plans or expectations are also measured against goals. A clear, concise and effective approach to monitor progress toward strategic goals is communicated regularly with relevant business units or functional areas. Individual, management, departmental, divisional and corporate strategic goals are linked with standard measurements. The results of key measurements and indicators are reviewed and discussed by senior management~~

~~and the board, as appropriate, on a regular basis and as frequently as necessary to address breaches in risk tolerances or limits in a timely manner.~~

~~Level 4~~
~~The ERM framework is an integrated part of strategy and planning. Risks are considered as part of strategic planning. Risk management is a formal part of strategic goal setting and achievement. Investment decisions for resource allocation examine the criteria for evaluating opportunity impact, timing and assurance. The organization forecasts planned mitigation's potential effect on performance impact, timing and assurance prior to use. Employees at all relevant levels use a risk-based approach to achieve strategic goals. The results of key measurements and indicators are shared with senior management and the board, as appropriate, on a regular basis.~~

~~Level 3~~
~~The ERM framework contributes to strategy and planning. Strategic goals have performance measures. While compliance might trigger reviews, other factors are integrated, including process improvement and efficiency. The organization indexes opportunities qualitatively and quantitatively, with consistent criteria. Employees understand how a risk-based approach helps them achieve goals. Accountability toward goals and risk's implications are understood and are articulated in ways frontline personnel understand. The results of key measurements and indicators are shared with senior management and the board, as appropriate.~~

~~Level 2~~
~~The ERM framework is separate from strategy and planning. A need for an effective process to collect information on opportunities and provide strategic direction is recognized. Motivation for management to adopt a risk-based approach is lacking.~~

~~Level 1~~
~~Not all strategic goals have measures. Strategic goals aren't articulated in terms the frontline management understands. Compliance focuses on policy and is geared toward satisfying external oversight bodies. Process improvements are separate from compliance activities. Decisions to act on risks might not be systematically tracked and monitored. Monitoring is done, and metrics are chosen individually. Monitoring is reactive.~~

~~Level 0~~
~~No formal framework of indicators and measures for reporting on achievement of strategic goals exists.~~

**~~Examination Procedures for Section I~~**

~~The following table provides example test procedures that may be performed by the Lead State examiner to verify information on risk management processes included in the ORSA Summary Report or to test the operating effectiveness of such practices. Several of these procedures may be performed in conjunction with other risk-focused examination processes, and Lead State examiners should attempt to gain efficiencies by coordinating testing and review efforts wherever possible. Lead State examiners should use professional judgment in selecting or tailoring procedures to assist in the assessment of each of the five risk management principles for the insurer. In addition, the Lead State examiner should incorporate any specific verification or testing recommendations made by the Lead State financial analyst into the planned examination procedures for Section I and consider the extent to which additional procedures should be utilized to test the changes that have been made to the insurer's ERM framework since the last on-site examination.~~

| ~~Principle~~ | ~~Possible Test Procedures~~ |
| --- | --- |
| ~~Risk Culture and Governance~~ | • ~~Obtain and review management, board or committee minutes/packets for the director group responsible for ERM oversight and evaluate the level of oversight provided.~~<br>• ~~Obtain and review formal ERM training materials provided by the insurer to relevant employees and directors.~~<br>• ~~Interview management or board member(s) with responsibilities for risk management oversight to determine level of knowledge and involvement of management or directors in risk management processes.~~<br>• ~~Interview insurer executives to get a feel for the "tone at the top" of the organization and the level of consistency in applying risk management processes across departments.~~<br>• ~~Obtain and review information on the insurer's compensation plans to determine that risk management decision-making is not undermined by compensation structure.~~<br>• ~~Obtain and review job descriptions or performance review criteria for select management positions to determine whether risk management elements are incorporated.~~ |
| ~~Risk Identification and Prioritization~~ | • ~~Obtain a current copy of the organization's risk listing/universe.~~<br>• ~~Determine whether appropriate external sources have been used to assist in risk identification (e.g. rating agency information, competitor 10K filings, etc.) where applicable.~~<br>• ~~Verify that the organization's risk listing/universe is updated/reviewed on a regular basis by requesting copies at various dates.~~<br>• ~~Assess the insurer's process and scale by which it prioritizes the key risks identified.~~<br>• ~~Review the approach for and results of the insurer's likelihood, severity and speed of onset risk assessments, if applicable.~~<br>• ~~Interview select process owners/business unit leaders to verify their role in risk identification and prioritization.~~<br>• ~~Interview risk management staff to understand and evaluate how risks are identified and aggregated across the organization.~~ |
| ~~Risk Appetite, Tolerances and Limits~~ | • ~~Review the management committee's or board's supporting materials to verify that the organization's risk appetite is reviewed as appropriate.~~<br>• ~~Review and evaluate how risk appetite, tolerances and limits are set for the insurer.~~<br>• ~~Determine whether the insurer considers legal entity regulations and capital requirements in setting its overall risk appetite (if applicable).~~<br>• ~~Review and evaluate steps taken to address breaches in risk limits on a sample basis (if applicable).~~<br>• ~~Verify, as applicable, whether reasonably forseeable material and relevant risks are assigned risk owners to monitor risks and oversee mitigation plans.~~<br>• ~~Interview select risk owners to get an understanding of how risk limits are set and updated.~~<br>• ~~Verify that checks and balances (i.e., supervisory review) are in place to ensure that risk limits are set in accordance with the organization's overall risk appetite.~~ |

| ~~Principle~~ | ~~Possible Test Procedures~~ |
|---|---|
| ~~Risk Management and Controls~~ | • ~~Obtain minutes of internal risk management committee (or equivalent management group) meetings to review frequency and extent of oversight activities.~~<br>• ~~Obtain a listing of internal audit reports to determine whether risk management processes are subject to periodic review.~~<br>• ~~Identify and test the operating effectiveness of preventive controls in select areas to determine how risk limits are enforced.~~<br>• ~~Review and evaluate how specific controls are mapped to legal entities (as appropriate if mapping is relevant to understanding of control).~~ |
| ~~Risk Reporting and Communication~~ | • ~~Obtain a current copy of the organization's risk dashboard (or equivalent report) to verify that tracking for reasonably foreseeable material and relevant risk areas exists.~~<br>• ~~Verify the frequency with which risk information is accumulated and reported by selecting a sample of historical risk dashboards (or equivalent reports) to review.~~<br>• ~~Test the reasonableness of information included on the risk dashboard (or equivalent report) on a sample basis.~~<br>• ~~Determine whether risk reporting information is evaluated by the board and used by senior management for strategy and planning purposes.~~<br>• ~~Review and evaluate the timeliness with which breaches in risk limits are reported and communicated to the appropriate authority.~~ |

~~**Documentation for Section I**~~

~~The Lead State examiner should prepare documentation summarizing the results of the risk management framework assessment by addressing each of the five principles set forth in the Guidance Manual using the template at the end of this section. Each assessment should first provide a summary of the Lead State analyst's initial assessment, followed by a summary of the results of exam procedures, leading to a final exam assessment for each principle. The summary of exam results should provide rationale for any deviation from the Lead State analyst's initial assessment of the principle.~~

**~~D~~E. Review of Section II - Insurer's Assessment of Risk Exposure**

Section II of the ORSA Summary Report is required to provide a high-level summary of the insurer's quantitative and/or qualitative assessments of its exposure to reasonably foreseeable and relevant material risks. There may be a great deal of variation in how this information is displayed from one insurer to the next, but in most cases, insurers tend to organize this information around the reasonably foreseeable and relevant material risks of the insurer. The Guidance Manual does give possible examples of relevant material risk categories (credit, market, liquidity, underwriting, and operational risks). In reviewing the information provided in this section of the ORSA, Lead State regulators may need to pay particular attention to risks and exposures that may be emerging or significantly increasing over time.

Lead State examiners may find the information regarding reasonably foreseeable and relevant material risk exposures the most beneficial aspect of the ORSA Summary Report, as this information may be useful in identifying risks and controls for use in the remaining phases of a risk-focused examination. This may be attributed to the fact that Section II provides risk information on the insurance group that may be grouped in categories similar to the NAIC's nine branded risk classifications (see Exhibit L). However, the grouping of risk information in the report is entirely up to the insurer, and the Lead State examiner should not expect each of the nine branded risk classifications to be directly addressed within Section II.

Stress Testing

In addition to providing background information on reasonably foreseeable and relevant material risks the insurer is facing, Section II anticipates the risk exposures to be analyzed under both normal and stressed environments. Therefore, as part of evaluating the information presented, the Lead State examiner is expected to consider the stress scenarios identified and assessment techniques performed by the insurer to quantify the financial impact of risks. In so doing, the Lead State examiner should note the assumptions and methodologies used by the insurer in conducting stress scenarios/testing. The Lead State examiner should obtain information from the Lead State analyst to determine the extent to which the state has already been provided information on the assumptions and methodologies.

The Lead State examiner should consider the assessment techniques the insurer has utilized to evaluate the impact that reasonably foreseeable and relevant material risks could have on its ongoing operations. In reviewing the insurer's efforts in this area, the Lead State examiner's focus would be on considering if additional information and support for the stress testing of individual risks or groups of risks are available in order to test the effectiveness of such processes. In reviewing the insurer's assessment techniques for ~~each of the nine branded risk classifications (if applicable) and other relevant risks~~its material and relevant (key) risks, the Lead State examiner should consider ~~each of~~ the following elements and possible test procedures:

**Note:** Possible test procedures that could duplicate or overlap with procedures listed in Section I or Section III are marked with an asterisk.

| **Consideration** | **Description** | **Possible Test Procedure(s)** |
|---|---|---|
| Risks Assessed | Key risks assessed are consistent with the insurer's risk identification and prioritization process, its business strategy and the regulator's understanding of exposures | • Evaluate the effectiveness of risk presentation and classification<br>o If necessary, prepare feedback to the financial analyst related to the mapping of the insurer's key risks to branded risk classifications<br>• Compare risks discussed in Section II to the insurer's risk register and prioritization documentation to ensure that all significant risks have been assessed<br>• Consider the completeness of the key risks identified by considering the company's business operations and strategy, as well as information presented in Form F, SEC reports and other filings<br>• Compare risks identified by the insurer to those tracked by regulators on the IPS/GPS and risk-focused examinations<br>• If key risks appear missing, consider discussing/addressing with the insurer |
| Presentation and Design of ERM Controls | Mitigation strategies and controls to address exposures are accurately presented and effectively designed for all key risks | • Verify that mitigation strategies and controls are clearly presented for all key risks identified in the summary report*<br>• Request and review additional information on mitigation strategies/controls that aren't clearly presented in the report<br>• Determine whether relevant metrics are in place to monitor risk exposures on a regular basis by selecting and reviewing a sample of key reports for review*<br>• In conjunction with work performed in Ph. 3 of a risk-focused examination, perform procedures to test the design effectiveness of mitigation strategies/controls for the company's key risks |
| Operating Effectiveness of ERM Controls | Mitigation strategies and controls are operating effectively in addressing the company's key risks | • Determine whether risk measurement metrics are compared against tolerances and risk limits by selecting a sample of key risks for review and testing*<br>• Select a sample of risks that have breached tolerances/limits to review and assess the steps taken by the company to escalate, remediate and address issues*<br>• In conjunction with work performed in Ph. 3 of a risk-focused examination, perform procedures to test the operating effectiveness of mitigation strategies/controls for the company's key risks |
| Rationale for Assessment Techniques | Assessment techniques and underlying assumptions are | • Verify that all significant risks are clearly assessed and presented in Section II of the ORSA Summary Report<br>• Review the descriptions of and rationale for assessment techniques utilized in the ORSA Summary Report for appropriateness |

| Consideration | Description | Possible Test Procedure(s) |
|---|---|---|
| | appropriately described and supported | • Review the process used to select and document rationale for assumptions used in risk assessment and select a sample of risks to verify documented support for the assumptions used<br>• Request and review additional information on assessment techniques not clearly presented in the report |
| Effectiveness of Assessment Tecnniques | Assessment techniques and underlying assumptions appear reasonable and in accordance with insurer standards and industry best practices | • Evaluate whether risks have been subjected to quantitative and qualitative analysis in accordance with their underlying characteristics<br>o For those risks only subject to qualitative assessment, determine why they have not been quantitatively assessed (e.g. lack of data, lack of methodology) and consider its appropriateness<br>• Evaluate the reasonableness of assumptions used and scenario/stress testing used by the insurer to assess risks by comparing to historical results and industry best practices and/or consulting with a specialist<br>• Review scenario analysis and stress testing performed to verify that both capital adequacy and liquidity are addressed for all relevant key risks*<br>• Assess whether the time horizons used to measure key risks are appropriate given their nature |
| Impact of Assessments | Results of assessments indicate that key risks have been effectively mitigated | • Review the results of stress testing and scenario analysis to assess the sufficiency of the insurer's capital/liquidity resources in the event of adverse situations*<br>• If concerns are identified related to scenario results, inquire regarding the insurer's remediation plans and evaluate their adequacy |

- ~~Was each of the most significant solvency risks facing the insurer identified and subjected to assessment techniques?~~
- ~~If scenarios were utilized to evaluate/stress the impact of such risks, were they appropriately described and justified?~~
- ~~Were techniques utilized to assess reasonably forseeable material and relevant risks in accordance with insurer standards and industry best practices?~~
    - ~~Did the time horizon or duration of the risks identified have an impact on the nature and extent of the assessment techniques selected?~~
- ~~Did the results of the assessment techniques indicate that the insurer had appropriately mitigated the impact that the risk might have on the insurer?~~
- ~~Do the assessment techniques utilized address issues from both a capital and liquidity perspective?~~

~~**Documentation for Section II**~~

~~Upon the conclusion of the Lead State examiner's review and testing of the information provided in Section II and related processes, documentation should be prepared to discuss whether the insurer included an appropriate discussion of reasonably foreseeable and relevant material risks. The nine branded risk classifications may be discussed within this summary, as well as any additional risk categories that the Lead State examiner deems relevant. In addition, the Lead State examiner should provide an assessment of the corresponding stress assumptions and test results presented for each of the risk categories discussed, keeping in mind that a company is not required to solely focus on the nine branded risk classifications.~~

**~~E~~F. Review of Section III - Group Assessment of Risk Capital**

~~Section III of the ORSA is unique in that it is required to be completed at the insurance group level, as opposed to the other sections, which may be completed at a legal entity level. However, in many cases, insurers will choose to also complete~~

~~Sections I and II at the group level. The requirement to complete Section III at the group level is important because it provides the means for Lead State insurance regulators to assess the reasonableness of capital of the entire insurance group based upon its existing business plan.~~ The focus of financial analysis in reviewing Section III will be to understand the insurer's assessment of the ~~reasonableness of~~risk capital of the entire group to withstand potential unexpected losses and detrimental events, as well as the prospective outlook of the insurer's solvency position. The focus of the Lead State examiner in reviewing Section III should be on understanding the process the insurer used to ~~accumulate and present the information provided~~determine its capital needs. To perform this review, the Lead State examiner may need to request additional detail supporting the group capital calculations that the insurer performed.

Insurance groups will use different approaches to group capital calculation~~means to measure estimated risk (required) capital,~~ and they will use different accounting and valuation frameworks. For example, they may determine the amount of capital they need to fulfil regulatory and rating agencies' requirements, but also determine the amount of risk capital they need to absorb unexpected losses that are not accounted for in the reserves. While the insurer is free to select whichever approach or combination of approaches are appropriate to meet its needs, the Lead State examiner should consider whether the approach selected is consistent with the nature, size and extent of risks that the group faces.The Lead State examiner, in conjunction with the Lead State analyst, may need to request that management ~~to~~ discuss their overall approach to capital management and the reasons and details of the approach so that they can be considered in evaluating the estimation of group risk capital~~both the accounting and valuation frameworks, as well as the reasons and details for each. A different accounting basis can result in a significant difference in perceived risk exposures and capital needs.~~

The ORSA Summary Report should summarize the insurer's process for model validation to support the quantification methodology and assumptions chosen to determine the risk capital. The Lead State examiner should evaluate the work that the insurer performed to validate the reasonableness of the quantification methodology and assumptions used. If the ORSA Summary Report does not provide a summary of the model validation process, the Lead State examiner should request copy of the validation report prepared by the insurer.

Many insurers use internally developed capital models to quantify the risk capital. In these cases, ~~T~~the ORSA Summary Report should summarize the insurer's process for model validation to support the quantification methodology and assumptions chosen to determine risk capital.~~, including factors considered and model calibration.~~ The Lead State examiner should evaluate the work that the insurer performed to validate the reasonableness of the quantification methodology and assumptions used. If the ORSA Summary Report does not provide a summary of the model validation process, the Lead State examiner should request copy of the validation report prepared by the insurer. With regard to the determination of the risk capital under stressed conditions, ~~B~~because the risk profile of each insurer is unique, there is no standard set of stress conditions that each insurer should run. However, the Lead State regulator should be prepared to dialogue with management about the selected stress scenarios if there is concern with the rigor of the scenario. In discussions with management, the Lead State regulator should gain an understanding of the modeling methods used to project available and risk capital over the duration of the insurer's business plan as well as the potential changes to the risk profile of the insurer over this time horizon (i.e. changes to the list of key risks) based on the business plan~~(e.g., stochastic vs. deterministic) and be prepared to dialogue about and understand the material assumptions that affected the model output, such as prospective views on risks~~. Th~~e~~is ~~aforementioned~~ dialogue may occur during either the financial analysis process and/or the financial examination process.

~~In focusing on the insurer's process to calculate and assess its group risk capital, the Lead State examiner will need to consider the source of the group's internal capital assessment. Some insurers may develop a group capital assessment based upon external models developed by third-party vendors, regulators or rating agencies, while other insurers may also consider and assess the results of an internal capital model. While the insurer is free to select whichever approach or combination of approaches are appropriate to meet its needs, the Lead State examiner should consider whether the approach selected is consistent with the nature, size and extent of risks that the group faces. In addition, the Lead State examiner should evaluate the work that the insurer performed to validate the approach and model utilized.~~

Internal Capital Models

The Guidance Manual states the analysis of an insurer's group assessment of risk capital requirements and associated capital adequacy description should be accompanied by a description of the approach used in conducting the analysis. This should include model design decisions, key methodologies, assumptions and considerations used in quantifying available capital and risk capital. Examples of information to be provided in Section III describing an insurer's processes in this area are provided in the Guidance Manual, and Lead State examiners should become familiar with these elements in order to assess an insurer's processes in this area.

In some situations, the insurer might purchase or license economic capital modeling software tools developed by third-party vendors that can be customized and tailored to by the insurer to operate as an internal capital model. Regardless of whether the internal capital model is developed in-house or licensed from a third-party vendor~~In reviewing an insurer's use of internal models~~, the Lead State examiner should gain an understanding of the work that the insurer performed to validate its own models, whether completed by internal audit, a third-party consultant or some other party. The importance of reviewing the insurer's self-validation process is not only to gain comfort on the information provided in Section III of the report, but also due to the fact that the insurer may be making business decisions based on the results of its modeling. This is an important step because the Lead State examiner is encouraged to look to the insurer's own process by which it assesses the accuracy and robustness of its models, as well as how it governs model changes and parameter or assumption setting, and limits Lead State examiner validation of reports to more targeted instances where conditions warrant additional analysis.

Depending upon the strength of the insurer's internal model validation processes, Lead State examiners may need to perform some level of independent testing to review and evaluate the controls over internal model(s) utilized by the insurer for its group economic capital calculation. This is largely due to the challenges inherent in developing, implementing and maintaining an effective internal capital model. In instances where independent testing is deemed necessary, this testing may consist of procedures to evaluate the appropriateness of assumptions and methodologies used in stochastic/deterministic modeling scenarios for individual risks or in estimating the amount of diversification benefit realized. In so doing, the Lead State examiner may need to select a sample of individual risks for review and consideration and involve an actuary to assist in the evaluation. When involving an actuary, the primary focus of this review would be on evaluating the reasonableness of the inputs and outputs of the models. An actuary may be able to provide input on the reasonableness of the inputs, while the outputs may be most easily tested by performing a walkthrough in which the inputs are modified, and the Lead State examiner or actuary evaluates and discusses with the insurer the impact that the change has on the outputs. There is no one set of assumptions or methodologies that fits every company. ~~The Lead State examiner may consider asking questions about the modeling approach that the company uses, as such questions may provide the company an opportunity to elaborate on information provided in the ORSA Summary Report and further the Lead State examiner's understanding.~~

External Capital Models

~~For some insurers, the group capital assessment may be based upon~~Many insurers utilize the output of external ~~capital~~ models (e.g., cat models, economic scenario generators) as an input into their internally developed capital models. These models are typically developed by third-party vendors and made available to the insurer through either a licensing or outsourced service agreement. In other instances, the insurer may use an external capital model developed for rating agency or regulatory purposes to assist in quantifying its own capital needs. ~~If an insurer presents its standing in relation to external capital models, the insurer may provide information showing its potential standing after considering the impact of stresses. This information may be beneficial as it can demonstrate what types of events an insurer could withstand before potentially losing its rating or violating regulatory capital requirements. While some of this information may be presented in Section II of the report, the impact of stresses on external capital models, while not required, should be considered in an assessment of Section III. There are several ways this can be demonstrated, including the rigor the insurer applies to its stress scenarios.~~

If an insurer bases its group capital assessment ~~largely~~ on third-party vendor tools, rating agency capital calculations or regulatory capital requirements, the Lead State examiner should consider what validation efforts have been conducted to allow reliance to be placed on external models~~the appropriateness of such reliance based upon the nature, scale and complexity of the insurer's reasonably foreseeable and relevant material risks~~. In addition, the Lead State examiner should consider whether the insurer ~~has applied~~applies a reasonable range of stress scenarios to the outputs of these ~~its available capital to determine its prospective standing in relation to external capital~~ models under a wide range of different scenarios.

Prospective Solvency Assessment

The Guidance Manual requires the insurer to consider the prospective solvency of the group. Many companies will include information developed as part of their strategic planning, including pro forma financial information displaying possible outcomes as well as projected capital adequacy in those future periods based on the insurer's defined capital adequacy standard. However, the Lead State examiner should review the information provided to understand the impact such an exercise has on the ongoing business plans of the group. For example, to the extent such an exercise suggests that at the insurer's particular capital adequacy under expected outcomes, the group capital position will weaken, or recent trends may result in certain internal limits being breached, the Lead State examiner should understand what actions the insurer/group expects to take as a result of such an assessment (e.g., reduce certain risk exposure, raise additional capital, etc.). In addition, the Lead State examiner should consider how any planned changes in risk exposure or strategy may affect both the insurer's short- and long-term solvency positions. Finally, the Lead State examiner should consider whether the assumptions and methodologies used in preparing the prospective solvency assessment are consistent with the insurer's business strategy and should assess whether these assumptions and methodology are reasonable.~~industry best practices~~. However, there is no one set of assumptions or methodologies that fit every insurer. Regulators must use professional judgment to assess the reasonability and plausibility of capital model inputs and outputs. ~~This is not to suggest that the Lead State examiner should not consider asking questions about the modeling approach used by the insurer, as such questions may provide the insurer an opportunity to elaborate on information provided in the ORSA Summary Report and further the Lead State examiner's understanding.~~

In conducting examination procedures to verify and evaluate the insurer's processes for calculating group risk capital and a prospective solvency assessment, the Lead State examiner should consider the following elements and possible test procedures:

| **Topic** | **Considerations** | **Possible Test Procedure(s)** |
|---|---|---|
| Capital Metric(s) Used | The capital metric(s) utilized to assess the group's overall capital target are clearly presented and described. | • Review and validate information presented on capital measurement tools for completeness and accuracy<br>• Gain an understanding of and evaluate the scope and purpose of each of the capital models used by the group (internal and external) |
| | The capital metric(s) selected address all key risks of the group. | • Gain an understanding of the risks assessed through the capital metric(s) used and determine whether all key risks of the group are included in the quantification of risk capital<br>• For external capital metrics, evaluate the appropriateness of their use considering the risk profile of the insurer/group<br>○ If necessary, involve a specialist in this evaluation |
| | Individual risk components are subject to reasonable/appropriate modeling scenarios. | • Gain an understanding and evaluate the use of stochastic/deterministic scenarios in modeling the group's exposure to key risks<br>• If necessary, involve a specialist in evaluating the appropriateness of scenarios, assumptions and methodologies used to calculate and allocate capital to individual risk components<br>• Gain an understanding of and evaluate the insurer's/group's processes for addressing key risks not directly quantified in its capital metrics into the risk capital process |
| | Model results are calibrated to an appropriate security standard | • Gain an understanding of the risk capital metric (e.g. Value at Risk, Tail Value at Risk) and security standard (e.g. 99.5%) used in the capital model and evaluate their appropriateness considering the insurer's risk profile and exposure to tail risk |
| Group Risk Capital (GRC) | Group risk capital is clearly presented and described on both an aggregate and per risk basis. | • Verify that the group risk capital presented in the ORSA Summary Report appropriately reconciles to modeled results and investigate any significant differences<br>• Identify and review significant changes in group risk capital (individual components and in aggregate) from the prior filing |
| Impact of Diversificiation Benefit | Diversification benefit is calculated based on correlations in key risk components that are reasonable/appropriate | • Obtain and review information on the risk aggregation process used by the company (i.e. correlation matrixes or copulas) to address risk correlations and review the process |

| | | |
|---|---|---|
| | | and the overall diversification benefit taken for reasonableness<br>• If necessary, involve a specialist in reviewing and testing the aggregation process and diversification benefit calculation |
| Available Capital | The group's capital is of high quality and sufficient to meet its business needs | • Consider whether the group's capital is freely available to absorb losses and is permanent and fungible (i.e. available to be distributed as needed) in form<br>• Assess the quality of group capital by determining whether it includes items such as double counting/stacking of capital and/or excessive amounts of goodwill, intangible assets or deferred tax assets, etc. |
| Excess Capital | Results of capital metrics demonstrate the group has sufficient capital to meet its obligations over a wide range of expected outcomes | • Compare methods utilized and overall results to those from prior periods to assess consistency and identify/evaluate significant changes.<br>• If concerns are identified over the level of excess capital available, perform procedures to determine whether sufficient additional sources of capital are available to the group and whether there are plans to access these additional sources of capital<br>• Review the results of stress testing and scenario analysis to assess the sufficiency of the insurer's capital/liquidity resources in the event of adverse situations |
| Impact of Stresses on GRC | The results of external capital models are subject to consideration under a wide range of stress scenarios | • Assess how the insurer has determined the number of scenarios to run under a stochastic modeling approach (if utilized)<br>• Assess whether the insurer has applied reasonable unfavorable stress scenarios in determining an appropriate level of risk capital and liquidity through use of a deterministic modeling approach, particularly if relying primarily on external capital metrics<br>    ○ Evaluate whether rating downgrades or regulatory intervention could impact the insurer's ability to achieve its business strategy under certain scenarios |
| Governance and Validation | Capital models and metrics utilized are subject to a sufficient level of governance, oversight and ongoing validation. | • Obtain and review the model governance policy to understand and evaluate the role of the BOD and Senior Management in overseeing internal capital models<br>• Obtain and review the model change authority policy to understand who is authorized to make changes to the capital model<br>• Verify the operating effectiveness of oversight responsibilities by reviewing supporting documentation on a sample basis.<br>• Select a sample of significant changes in the internal capital model to verify appropriate levels of change authority and supervisory review and approval.<br>• Assess the level of oversight in place over the selection and application of the risk capital metric and security standard used in the internal capital model.<br>• Obtain and review the data quality policy (if available) and review work performed by the company to validate data inputs for completeness and accuracy |
| Prospective Solvency Assessment | Prospective solvency is projected and evaluated in accordance with the group's ongoing business strategy/plans | • Evaluate whether the assessment covers an appropriate time horizon, considering the insurer's business plan and strategy.<br>• Evaluate the methodologies to project available and risk capital over the time horizon and whether these methodologies take into account future new business.<br>• Evaluate whether the expected changes in risk profile are consistent with the business strategy and plans presented by |

| | | |
|---|---|---|
| | | the group and how these changes have been incorporated into the capital projections<br>• If concerns are identified through a review of the prospective solvency assessment, discuss with the company and perform additional procedures as necessary. |

~~**Documentation for Section III**~~

~~The Lead State examiner should summarize exam conclusions regarding the insurer's assessment of group risk capital by describing the method used (e.g., internal, external, combination) by the insurer to assess its overall group capital target and its basis for such a decision.~~

~~If internal capital models are utilized in the process to assess group risk capital, a discussion of material assumptions and methodologies utilized in calculating capital allocated to individual risk components should be provided. In addition, material assumptions and methodologies utilized in calculating a diversification credit should be discussed. Finally, controls over model validation and/or results of independent testing performed in this area should be discussed.~~

~~If external capital models are utilized in the process to assess group risk capital, the Lead State examiner should describe the external capital models utilized and their importance to the insurance group. In addition, a discussion of the stress scenarios and testing applied to the external capital model to account for a wide range of potential events should be provided.~~

~~The Lead State examiner should also summarize exam conclusions regarding the prospective solvency assessment provided by the insurance group. This summary should discuss the group's prospective solvency projections and projected changes in risk exposures. For example, the Lead State examiner should discuss the material assumptions and methodologies that the insurer used in performing a prospective solvency assessment and whether the assumptions are consistent with the insurer's overall business plan and strategy. Finally, the Lead State examiner should discuss any material changes in individual risk exposures outlined by the insurer and whether any of the information provided presents concerns to be addressed in the remaining phases of the examination.~~

**Overall Assessment of ORSA/ERM Function**

After conducting procedures to verify, validate and assess the processes and information reported on the insurer's ERM function in each section of the ORSA Summary Report, the Lead State examiner should reach an overall conclusion regarding the maturity and reliability of the function. In so doing, the Lead State examiner should consider both processes covered in the ORSA and verified during the onsite exam, as well as ERM processes that may not have been covered in the ORSA Summary Report but were identified and tested during the exam. In reaching an overall assessment, the Lead State examiner can consider the use of Handbook guidance, examiner judgment and/or the use of third-party tools such as the Risk and Insurance Management Society's (RIMS) Risk Maturity Model (RMM).

Insurers or insurance groups may utilize various frameworks in developing, implementing and reporting on their ORSA processes (e.g. COSO Integrated Framework, ISO 31000, IAIS ICP 16, other regulatory frameworks, etc.). Elements of the RMM have been outlined in this guidance to provide a reference for use in reviewing and assessing ERM/ORSA practices. However, as various frameworks may be utilized to support effective ERM/ORSA practices, Lead State regulators should be mindful of differences in frameworks and allow flexibility in assessing ERM. The RMM provides a scale of five maturity levels upon which an insurer can be assessed. The five maturity levels can generally be defined as follows:

- Leadership: Risk management is embedded in strategic planning, capital allocation and other business processes, and is used in daily decision-making. Risk limits and early warning systems are in place to identify breaches and require corrective action from the board of directors or committee thereof (hereafter referred to as "board") and management.

- Managed: Risk management activities are coordinated across business areas, and tools and processes are actively utilized. Enterprise-wide risk identification, monitoring, measurement and reporting are in place.

- Repeatable: The insurer has risk management processes in place designed and operated in a timely, consistent and sustained way. The insurer takes action to address issues related to high priority risks.

- Initial: The insurer has implemented risk management processes, but the processes may not be operating consistently and effectively. Certain risks are defined and managed in silos, rather than consistently throughout the organization.

- Ad hoc: The insurer has not developed or documented standardized risk management processes and is relying on the individual efforts of staff to identify, monitor and manage risks.

The design of ERM/ORSA practices should appropriately reflect the nature, scale and complexity of the company. In assessing the effectiveness of an insurer's ERM program, Lead State regulators should understand the level of maturity that is appropriate for the company based on its unique characteristics. Attainment of "Leadership" or "Managed" levels of maturity for ERM/ORSA practices may not be appropriate, nor should it be expected, for all companies. Additionally, it would be expected that the level of testing performed in an examination to verify or validate ERM maturity would be commensurate with the level of maturity assessed. For example, ERM programs assessed at a "Leadership" or "Managed" level of maturity would typically be subject to more of the suggested exam procedures highlighted above than those programs assessed at a lower level of maturity.

## ~~F~~G. ORSA Review Documentation ~~Template~~

As outlined above, the Lead State examiner is expected to incorporate a review of ORSA information into ongoing on-site examination activities, including workpaper documentation. This includes documenting the work completed to verify and validate information presented in the three sections of the ORSA Summary Report, as well as assessing the effectiveness and maturity of the insurer's ERM processes. The results of such work can be documented in various areas of the examination file (e.g. Phase 1 documentation, Exhibit M, various risk matri~~x~~ces, etc.), as deemed appropriate.

T~~t~~he Lead State examiner is also expected to summarize the results and key findings/assessments in the Summary Review Memorandum (SRM) for communication to others within the department. See Exhibit AA – Summary Review Memorandum for additional guidance on relevant information to be included in the SRM on the ORSA/ERM function.

~~ORSA Summary Report Examination Results~~
~~Insurer XYZ 12/31/XX Examination~~
~~Using ORSA Summary Reported Dated XX/XX/XXXX~~

~~**Section I**~~

~~Prepare documentation summarizing the results of the risk management framework assessment by addressing each of the five principles set forth in the Guidance Manual. Each assessment should first provide a summary of the Lead State analyst's initial assessment, followed by a summary of the results of Lead State exam procedures, leading to a final exam assessment for each principle. The final Lead State exam assessment should provide adequate rationale for any deviation from the Lead State analyst's initial assessment of the principle.~~

~~A **Risk Culture and Governance** – Governance structure that clearly defines and articulates roles, responsibilities and accountabilities, and a risk culture that supports accountability in risk-based decision making.~~

~~Initial Lead State Analyst Assessment:~~

~~Summary of Lead State Exam Results:~~

~~Final Lead State Exam Assessment:~~

~~☐5 ☐4 ☐3 ☐2 ☐1 ☐0~~

~~B **Risk Identification and Prioritization** – Risk identification and prioritization processes are key to the organization. Responsibility for this activity is clear. The risk management function is responsible for ensuring the process is appropriate and functioning properly.~~

~~Initial Lead State Analyst Assessment:~~

~~Summary of Lead State Exam Results:~~

~~Final Lead State Exam Assessment:~~

~~☐5 ☐4 ☐3 ☐2 ☐1 ☐0~~

~~C **Risk Appetite, Tolerances and Limits** – A formal risk appetite statement, associated risk tolerances and limits are foundational elements of risk management for an insurer. Understanding of the risk appetite statement ensures alignment with risk strategy set by senior management and reviewed and evaluated by the board.~~

~~Initial Lead State Analyst Assessment:~~

~~Summary of Lead State Exam Results:~~

~~Final Lead State Exam Assessment:~~

~~☐5 ☐4 ☐3 ☐2 ☐1 ☐0~~

~~D **Risk Management and Controls** – Managing risk is an ongoing ERM activity, operating at many levels within the organization.~~

~~Initial Lead State Analyst Assessment:~~

~~Summary of Lead State Exam Results:~~

~~Final Lead State Exam Assessment:~~

~~☐5 ☐4 ☐3 ☐2 ☐1 ☐0~~

~~E **Risk Reporting and Communication** – Provides key constituents with transparency into the risk-management processes and facilitates active, informal decisions on risk-taking and management.~~

~~Initial Lead State Analyst Assessment:~~

~~Summary of Lead State Exam Results:~~

~~Final Lead State Exam Assessment:~~

~~☐5 ☐4 ☐3 ☐2 ☐1 ☐0~~

~~**Overall Section I Assessment**~~
~~After considering the assessment of each of the five previously identified principles and taking into account any additional factors that the examiner identified during the review of the ERM framework, develop an overall assessment of the insurer's risk management framework using the same risk maturity model. The assessment, along with findings from Section II and Section III, will assist the examination team in determining the extent of reliance to be placed on the insurer's ORSA/ERM processes throughout the remaining phases of a full-scope examination and through modifications to the ongoing supervisory plan. Results should also be provided to the analyst at the conclusion of the examination.~~

~~Overall Lead State Assessment Rationale:~~

~~☐5 ☐4 ☐3 ☐2 ☐1 ☐0~~

~~**Section II**~~

~~Prepare documentation summarizing a review and assessment of information that the insurer provided on its reasonably foreseeable and relevant material risks, and corresponding stress assumptions and test results.~~

~~A Based on your knowledge of the group, did the insurer include in its ORSA a discussion of risks and related stresses that you consider appropriate for the group? **Note whether the following are applicable or not.**~~

~~A **Credit** – Amounts actually collected or collectible are less than those contractually due or when payments are not remitted on a timely basis.~~

~~Lead State Examiner Summary of Risks and Stress Testing:~~

~~B **Legal** – Nonconformance with laws, rules, regulations, prescribed practices or ethical standards in any jurisdiction in which the entity operates will result in a disruption in business and financial loss.~~

~~Lead State Examiner Summary of Risks and Stress Testing:~~

~~C **Liquidity** – This is the inability to meet contractual obligations as they become due because of an inability to liquidate assets or obtain adequate funding without incurring unacceptable losses.~~

~~Lead State Examiner Summary of Risks and Stress Testing:~~

~~D **Market** – Movement in market rates or prices (such as interest rates, foreign exchange rates or equity prices) adversely affects the reported and/or market value of investments.~~

~~Lead State Examiner Summary of Risks and Stress Testing:~~

~~E **Operational** – The risk of financial loss resulting from inadequate or failed internal processes, personnel and systems, as well as unforeseen external events.~~

~~Lead State Examiner Summary of Risks and Stress Testing:~~

~~F **Pricing/Underwriting** – Pricing and underwriting practices are inadequate to provide for risks assumed.~~

~~Lead State Examiner Summary of Risks and Stress Testing:~~

~~G **Reputation** – Negative publicity, whether true or not, causes a decline in the customer base, costly litigation and/or revenue reductions.~~

~~Lead State Examiner Summary of Risks and Stress Testing:~~

~~H **Reserving** – Actual losses or other contractual payments reflected in reported reserves or other liabilities will be greater than estimated.~~

~~Lead State Examiner Summary of Risks and Stress Testing:~~

~~I **Strategic** – Inability to implement appropriate business plans, make decisions, allocate resources or adapt to changes in the business environment will adversely affect competitive position and financial condition.~~

~~Lead State Examiner Summary of Risks and Stress Testing:~~

~~J **Other** – Discuss any other reasonably foreseeable and relevant material risks facing the insurer that do not fit into one of the nine branded risk classifications identified above.~~

~~Lead State Examiner Summary of Risks and Stress Testing:~~

~~**Overall Risk Assessment Summary**~~
~~After considering the various risks that the insurer identified, as well as an analysis of such risks, develop an overall risk assessment summary of possible concerns that may exist.~~

~~**Section III**~~

~~Prepare documentation summarizing a review of the group capital assessment and prospective solvency assessment provided by the group as follows:~~

~~A. Summarize exam conclusions regarding the insurer's assessment of group risk capital by addressing each of the following elements:~~

~~1. **Overall Method of Capital Measurement**: Discuss the method(s) (e.g., internal, external, combination) that the insurer used in assessing its overall group capital target and its basis for such a decision.~~

~~Lead State Examiner Summary:~~

~~2. **Internal Capital Models**: If internal capital models are utilized in the process to assess group risk capital, discuss each of the following items:~~

~~1. Material assumptions and methodologies utilized in calculating capital to be allocated to individual risk components.~~

~~Lead State Examiner Summary:~~

~~2. Stress scenarios and testing applied to individual risk components.~~

~~Lead State Examiner Summary:~~

~~3. Material assumptions and methodologies utilized in calculating a diversification credit based on the correlation between risk components.~~

~~Lead State Examiner Summary:~~

~~4. Controls over model validation and/or results of independent testing performed in this area.~~

~~Lead State Examiner Summary:~~

~~3. **External Capital Models**: If external capital models are utilized in the process to assess group risk capital, discuss each of the following items:~~

~~1. External capital models utilized and their importance to the insurance group.~~

~~Lead State Examiner Summary:~~

~~2. Stress scenarios and testing applied to the external capital model to account for a wide range of potential events.~~

~~Lead State Examiner Summary:~~

~~B. Summarize exam conclusions regarding the prospective solvency assessment that the insurance group provided by discussing each of the following elements:~~

~~1. **Prospective Solvency Projections**: Discuss the material assumptions and methodologies that the insurer utilized in performing a prospective solvency assessment. Are assumptions consistent with the insurer's overall business plan and strategy?~~

~~Lead State Examiner Summary:~~

~~2. **Changes in Risk Exposure**: Discuss material changes in individual risk exposures that the insurer outlined. Document whether any of the information provided present concerns to be addressed in the remaining phases of the examination.~~

~~Lead State Examiner Summary:~~

## ~~G~~H. Utilization of ORSA Results in the Remaining Phases of the Examination

The review and assessment of the insurer's ORSA/ERM processes during an on-site examination is meant to provide input and feedback to the Lead State financial analyst for updating the insurer's ongoing supervisory plan and in reaching a final assessment regarding the maturity of the insurer's ERM framework. However, the knowledge that the Lead State examiner gains in performing this review and assessment should also be utilized to gain efficiencies, if appropriate, in the seven-phase risk-focused examination process.

The extent to which the Lead State examination team utilizes information from the insurer's ORSA/ERM processes to create efficiencies should depend upon the overall assessment of the insurer's ERM framework as follows:

| Maturity Level | Resulting Examination Impact |
|---|---|
| ~~5~~ Leadership | The Lead State examination team may place a high degree of reliance on the insurer's general ERM framework and related controls and may utilize ORSA conclusions to substantially reduce and focus the scope of remaining examination activities. For example, in examining insurers with ERM functions at a "Leadership" level, most (if not all) other than financial reporting risks reviewed during the exam would be expected to come from risks assessed within Section II of the ORSA Summary Report, with corresponding mitigation strategies and controls sourced from ERM/ORSA functions. |
| ~~4~~ Managed | The Lead State examination team may place a moderate-high degree of reliance on the insurer's general ERM framework and related controls, while considering additional testing for significant individual controls/strategies. ORSA conclusions may be utilized to reduce and focus the scope of remaining examination activities. For example, in examining insurers with ERM functions at a "Managed" level, many other than financial reporting risks reviewed during the exam would be expected to come from risks assessed within Section II of the ORSA Summary Report, with corresponding mitigation strategies and controls sourced from ERM/ORSA functions. |
| ~~3~~ Repeatable | The Lead State examination team may place a moderate degree of reliance on the insurer's general ERM framework and related controls, but significant individual controls/strategies should be subject to testing. ORSA information should be considered in limiting and focusing the scope of remaining examination activities. For example, in examining insurers with ERM functions at a "Repeatable" level, some other than financial reporting risks reviewed during the exam would be expected to come from risks assessed within Section II of the ORSA Summary Report. |
| ~~2~~ Initial | The Lead State examination team may place a low degree of reliance on the insurer's general ERM framework and related controls. Individual controls/strategies should be subject to examination testing. ORSA information should be considered in focusing the scope of remaining examination activities. |
| ~~1~~ Ad hoc | The Lead State examination team should not place reliance on the insurer's ERM framework and related controls without performing testing on individual controls/processes. ORSA information can be considered in scoping examination activities, but it should be supplemented by additional tools and resources. |

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|---|---|
| ~~0~~ | ~~The Lead State examination team should not place any reliance on nor consider the results of the insurer's ERM/ORSA framework in scoping examination activities.~~ |

While this guidance is developed with ORSA-compliant insurers in mind, the concepts may also be applied to non-ORSA companies that have implemented risk management functions. Therefore, the Lead State examination team should customize the consideration of ERM processes during each examination to meet the needs of the insurer being reviewed.

While the results of the ERM maturity assessment can be broadly utilized in customizing risk-focused examination activities, additional guidance has been prepared to provide examples of specific information obtained through the ERM/ORSA review process that may be utilized to reduce or facilitate the remaining phases of the financial examination. The Lead State examination team may be able to utilize information obtained through a review of ERM/ORSA processes to gain exam efficiencies as outlined in the following table:

| ERM/ORSA Information | Related Examination Process(es) | Explanation |
|---|---|---|
| Section I – Description of the Insurer's Risk Management Framework | Phase 1, Part Two: Understanding the Corporate Governance Structure | The Lead State examiner's work to review and assess the insurer's ERM framework (as reported in the ORSA) may be used to satisfy the requirement to review the insurer's risk management practices as part of the Phase 1 corporate governance review. The overall assessment of ORSA/ERM ~~maturity level assessment~~framework discussed above should be completed during the planning stage of an exam. |
| Section I – Risk Identification & Prioritization; Section II – Insurer's Assessment of Risk Exposure | Phase 1, Part Five: Prospective Risk Assessment; Exhibit V – Overarching Prospective Risk Assessment; Phase 2: Identifying and Assessing Inherent Risks | The risks described, prioritized and quantified through the insurer's ERM/ORSA processes should assist the Lead State examiner in identifying and assessing reasonably foreseeable and relevant material risks to be reviewed during the exam. |
| Section I – Risk Appetites Tolerances and Limits; Section II – Insurer's Assessment of Risk Exposure | Phase 3 – Identify and Evaluate Risk Mitigation Strategies/ Controls; Exhibit V – Overarching Prospective Risk Assessment | Risk tolerances and limits that the insurer set may represent strategies/controls that can be relied upon to mitigate reasonably foreseeable and relevant material risks in Phase 3 of the examination process or to address overarching prospective reasonably foreseeable and relevant material risks. |
| Section II – Insurer's Assessment of Risk Exposure; Section III – Group Assessment of Risk Capital | Phase 5 – Establish/ Conduct Detail Test Procedures | The results of stress testing that the insurer performed, as well as the amount of capital allocated to individual risk components, may assist the Lead State examiner in determining the ultimate impact of unmitigated residual risks on the insurer. To the extent that the insurer accepts certain residual risks and capital is allocated to the risk under a wide range of potential outcomes, the Lead State examiner may choose to document this fact in Phase 5 ~~and~~ to avoid documenting a finding or ongoing concern in this area. However, the documentation should discuss reasonably foreseeable and relevant material risks, capital and liquidity in sufficient detail to address future solvency concerns in these areas. |

| | | |
|---|---|---|
| Section III – Group Assessment of Risk Capital | Exhibit DD – Critical Risk Categories (Capital Management) | The overall results of the group risk capital assessment, as well as the prospective solvency assessment that the insurer performed, should provide evidence of whether the insurer's capital management ~~plans are~~is adequate. This information may be used to address reasonably foreseeable and relevant material risks related to capital management required to be considered by Exhibit DD – Critical Risk Categories. |
| Section III – Prospective Solvency Assessment | Phase 6 – Update Prioritization & Supervisory Plan; Phase 7 – Draft Exam Report & Management Letter | Information provided in the insurer's prospective solvency assessment should address the insurer's ongoing strategy and business outlook. This information may be useful in reaching overall exam conclusions and determining steps for future monitoring efforts required to be documented in Phases 6 and 7 of the examination and communicated to financial analysis through the SRM. |

## EXHIBIT M
## UNDERSTANDING THE CORPORATE GOVERNANCE STRUCTURE

The purpose of this exhibit is to assist the examiner in documenting the understanding and assessment of an insurer's corporate governance policies and practices, including its ERM function. As insurers are expected to demonstrate different corporate governance practices in accordance with the nature and extent of their operations, examiners should not expect the practices of each individual insurer to specifically match the guidance provided in this exhibit. Therefore, the focus of an examination team's considerations in this area should be to determine whether the practices implemented by the insurer are reasonable and effective.

The examination team should first attempt to utilize information obtained through Exhibit B – Examination Planning Questionnaire, Exhibit Y – Examination Interviews and other planning sources (including information provided to the financial analyst and any other information available to the examiner) before requesting any additional information that may be necessary to gain an understanding and perform an assessment of corporate governance. A favorable overall assessment of governance does not, by itself, serve to reduce the scope or extent of examination procedures; rather, specific governance controls need to be assessed for their adequacy of the management of specific risks, in conjunction with other controls designed to manage the same.

In conducting examinations of insurers that are part of a holding company group, the work to gain an understanding and assess corporate governance should focus on the level at which insurance operations are directly overseen (e.g., ultimate parent company level, insurance holding company level, legal entity level, etc.). However, in certain areas, it may be necessary to review governance activities occurring at a level above or below the primary level of focus. Many critical aspects of governance usually occur at the holding company level. The exam team should seek to coordinate the review and assessment of group corporate governance in accordance with the exam coordination framework and lead state approach outlined in Section 1 of this Handbook. Where possible, in a coordinated examination, the lead state's work on the corporate governance assessment should be utilized to prevent duplication of effort and to leverage examination efficiencies. Additionally, the examiner should utilize the Corporate Governance Annual Disclosure (CGAD), which is required to be filed with the Department of Insurance (DOI) annually in accordance with the *Corporate Governance Annual Disclosure Model Act* (#305) and *Corporate Governance Annual Disclosure Model Regulation* (#306). The CGAD provides a narrative description of the insurer's or insurance group's corporate governance framework and structure and may enhance examination efficiencies when leveraged. Examiners should also ensure they understand/leverage the Holding Company Analysis work performed by the lead state's financial analyst, as well as the Lead State's review of the ORSA filing, to understand and assess the company's corporate governance, as well as the filings noted above.

**Detail Eliminated to Conserve Space**

E. REVIEWING THE RISK MANAGEMENT FUNCTION

A review of the entity's risk management function should be conducted through discussions with senior management and the board of directors and through gaining an understanding of the risk management function including inspection of relevant risk management documentation.~~. For companies subject to the Own Risk and Solvency Assessment (ORSA),~~ The ORSA guidance outlined in Section 1, Part X of this Handbook includes procedures which may assist the examiner in conducting a robust review of the company's risk management practices and policies. ~~a review of the ORSA summary report – including completion of the ORSA Documentation Template in Section 1, Part X of this Handbook – may be used in place of completing this section. For companies that do not submit an ORSA summary report, the ORSA guidance contained in this Handbook may still be a helpful tool in assessing the maturity of an insurer's risk-management framework, which should include an assessment of each of five key principles.~~ While each of the key principles can be applicable to all insurers, it is important to consider variations in size and complexity and alter expectations appropriately. As a general guideline, the following areas should be considered in conducting a review of the risk-management function:

1. Risk Culture and Governance

   a. What kind of risk-management culture is demonstrated throughout the organization? What does the culture indicate regarding the importance of risk management to the organization?

2. Risk Identification and Prioritization
   a. How are existing risks identified, monitored, evaluated and responded to? Does risk assessment take probability, potential impact and time duration into account?
   b. How are emerging and/or prospective risks identified, monitored, evaluated and responded to?

3. Risk Appetite, Tolerances and Limits
   a. How are risk tolerances, appetites and limits defined and communicated throughout the organization? Does the insurer maintain appropriate policies outlining specific obligations of employees in dealing with risk?
   b. How does the organization use the risk information it gathers to determine its capital needs?

4. Risk Management and Controls
   a. How are responsibilities for risk-management functions delegated and monitored within the organization?

5. Risk Reporting and Communication
   a. What is the involvement of the board of directors in the risk-management function of the organization?

An effective risk-management function is essential in providing effective corporate governance over financial solvency. During the latter phases of the risk-focused examination, the examiner will document a review of the entity's individual risk-management functions within the system. However, during a review of the entity's corporate governance, the examiner should document the review of the entity's risk-management function as a whole, as well as its place and importance in the entity's corporate governance structure. For ORSA companies, the knowledge gained in performing a review and assessment of enterprise risk management (ERM) may also be utilized to gain efficiencies, if appropriate, in accordance with the insurer's assessed maturity level, in the latter phases of the risk-focused examination as described in Section 1, Part X of this Handbook.

F. DOCUMENTATION

The examination team should document its understanding and assessment of the entity's governance, as well as its assessment on the related impact on the examination. This summary should include a description of any unique examination procedures, including special inquiries that are considered necessary to any significant risks identified as a result of the assessment.

The Risk Assessment Matrix, as the central documentation tool, should be utilized for the identification and assessment of individual solvency risks requiring review through the risk assessment process. However, documentation on the understanding and assessment of corporate governance is at the discretion of the examiner and would not typically be presented in a Risk Assessment Matrix. For most companies, a memorandum and/or corresponding documentation in the electronic workpapers addressing the items presented in this exhibit should provide sufficient documentation. For example, the documentation could summarize the attributes and techniques supporting the examiner's overall evaluation, any resulting examination scope implications, and the approach used to validate the more significant attributes and techniques. For smaller companies, documentation of the examination's consideration of corporate governance may be provided in the appropriate section of Exhibit I – Examination Planning Memorandum.

Specific findings or concerns related to an insurer's corporate governance practices should be accumulated for inclusion in a management letter (or similar document) to provide feedback and recommendations to the insurer. In addition, the examination should utilize Exhibit AA – Summary Review Memorandum (or similar document) to summarize its understanding and assessment of the insurer's overall corporate governance framework, as well as the maturity and reliability of its ERM function, to ensure appropriate communication back to the financial analyst. ~~it may be necessary for the examination to document information on the corporate governance assessment for communication back to the financial analyst through the use of Exhibit AA – Summary Review Memorandum (or similar document).~~

# EXHIBIT AA
# SUMMARY REVIEW MEMORANDUM

The following is an illustration of how a summary review memorandum (SRM) may be set up to assist examiners in documenting the key issues and results of a risk-focused examination that should be shared with the Chief Examiner and the assigned analyst. The illustration also includes a high-level overview of the insurer's holding company structure (if applicable) and how that structure affected exam coordination with other states. Additionally, the SRM includes discussion of the insurer's governance and risk management practices, and a summary, by branded risk classification, of significant exam findings and/or concerns warranting communication. These findings may include overarching solvency concerns, examination adjustments, other examination findings, management letter comments, subsequent events and other residual risks or concerns the examiner may want to communicate to department personnel. The final sections, prioritization level and changes to the supervisory plan, provide discussion of the examiner's overall conclusions regarding ongoing monitoring, including specific follow-up recommended to the analyst .

This exhibit provides an example template, which is not intended to be all-inclusive and should be tailored to each examination. Reference to each branded risk classification is necessary and should be included in the examination's SRM; however, it is not necessary to address each of the supporting areas and points discussed herein. Therefore, the examiner-in-charge should use his or her judgment in determining which sections of this illustration are applicable and document any other relevant information deemed necessary. The purpose of the SRM is to provide interpretative analyses relative to significant examination areas and to provide a basis for communicating examination findings and recommendations to department personnel. In so doing, the SRM will provide input into the Insurer Profile Summary (IPS) and the supervisory plan. In fulfilling this purpose, the SRM should not merely repeat comments made in the examination report or management letter, but instead provide a comprehensive summary of examination conclusions both objective and subjective in nature. Conclusions should provide information necessary for ongoing supervision of the insurer that includes areas of concern as well as areas that support a positive outlook for the insurer.

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**COMPANY NAME:** **EXAMINATION DATE:**

**EXAMINATION BACKGROUND**

The purpose of this section of the memorandum is to document at a high level what, if any, group the insurer belongs to, if the insurer was part of a coordinated exam and how the coordinated exam was conducted. Additional information regarding the timing of the exam, staffing resources utilized—including what specialists were used—or other background information necessary to understand the results presented in the memo should also be included.

**CORPORATE GOVERNANCE ~~AND RISK MANAGEMENT~~**

The purpose of this section of the memorandum is to summarize an understanding and assessment of the ~~an~~ insurer's corporate governance including its board of directors, senior management and organizational structure. ~~, as well as the results of the review of the enterprise risk management (ERM) function of the insurer.~~ This assessment should include information obtained during both the planning and the completion stages of the examination. Therefore, consideration of information gathered during C-level interviews, completion of Exhibit M and review of the insurer's Own Risk and Solvency Assessment (ORSA), if applicable, should be combined with information obtained during detail testwork to reach a concise final assessment that focuses on communicating significant areas of strength or weakness within the overall corporate governance structure ~~and ERM functions~~ of the insurer. When the insurer is part of a holding company, documentation should reference the level at which conclusions are reached. Additional assessment may be necessary at the individual entity level, but the primary focus of the assessment will commonly be at the holding company level in a coordinated examination.

**RISK MANAGEMENT**

The purpose of this section of the memorandum is to summarize an understanding and assessment of the insurer's enterprise risk management (ERM) function of the insurer. This assessment should include information obtained during ~~both~~ the planning, fieldwork, and ~~the~~ completion stages of the examination. ~~Therefore, consideration of information gathered during~~

~~C-level interviews, completion of Exhibit M and review of the insurer's Own Risk and Solvency Assessment (ORSA), if applicable, should be combined with information obtained during detail testwork to reach a concise final assessment.~~In documenting the regulator's assessment, regulators may consider using the maturity terminology established within the Risk Maturity Model (i.e. Leadership, Managed, Repeatable, Initial, and Ad hoc). ~~that focuses on communicating significant areas of strength or weakness within the overall ERM functions of the insurer~~In documenting the key points for the regulator's assessment of the maturity and reliability of the insurer's ~~company's~~ ERM~~'s~~ function~~maturity and reliability~~, consideration should be given to the following areas, if applicable:

- Information on key entity level ERM controls that were validated during the examination
- Summary assessment of significant areas of strength and weaknesses within the ERM framework
- Work performed to review the company's capital modeling processes
- Work performed to review the company's stress testing framework
- Evaluation of the company's key risks, risk appetites, tolerances and limits
- Evaluation of the company's capital and surplus (i.e. quality of capital, availibility of capital, etc.)
- Evaluation of the company's prospective risk assessment and capital position
- Recommendations to be made to the company based on ERM work performed

When the insurer is part of a holding company, documentation should reference the level at which conclusions are reached. Additional assessment may be necessary at the individual entity level, but the primary focus of the assessment will commonly be at the holding company level in a coordinated examination. Documentation should clearly indicate the exam's utilization and reliance on the company's ORSA/ERM processes to assist in the identification of key risks and/or controls.

It may also be appropriate to provide additional risk specific commentary related to ERM/ORSA review within the Branded Risk Assessments. Documentation should provide summary level information for key risks, with reference to examination workpapers for additional detail, when necessary. ~~on~~ Risk specific commentary should include consideration the following areas, if applicable:

- New risks for the analyst to consider in its ongoing financial surveillance
- Risk specific controls/risk mitigation strategies that were validated during the examination
- Evaluation of risk assessment techniques, including appropriateness of stress scenarios and underlying quantification techniques and assumptions
- Risks that may require further ongoing surveillance or recommended follow--up by the Department
- Other sources of information to evaluate key risks  not referenced in the ORSA (e.g. key risk indicators, presentations to the BOD, project plans, etc.)

**Detail Eliminated to Conserve Space**