

SUPERVISORY STATEMENT ON ORSA IN THE CONTEXT OF COVID-19

EIOPA-BoS-21/323
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European Insurance and
Occupational Pensions Authority

1. Legal basis

- 1.1. The European Insurance and Occupational Pensions Authority (EIOPA) provides this Supervisory Statement on the basis Article 29(2) of Regulation (EU) No 1094/2010¹. This Article mandates EIOPA to play an active role in building a common Union supervisory culture and consistent supervisory practices, as well as in ensuring uniform procedures and consistent approaches throughout the Union.
- 1.2. EIOPA delivers this Supervisory Statement on the basis of Directive 2009/138/EC (Solvency II).
- 1.3. This Supervisory Statement is addressed to the competent authorities², as defined in Article 4(2) of Regulation (EU) No 1094/2010.
- 1.4. The Board of Supervisors has adopted this Supervisory Statement in accordance with Article 2(7) of its Rules of Procedure³.

2. Context and objective

- 2.1. The COVID-19 pandemic has been affecting economies and societies leading to state and central banking measures being taken to combat its impact. This situation has resulted in a social and economic crisis, the effects of which are being felt throughout the world's and the EU's economy. The financial stress caused, the consequences of which are expected to extend much further in time, has underlined the need for insurance and reinsurance undertakings (collectively "undertakings") to assess the impact of the pandemic on their business from a forward looking perspective. The current pandemic's impact on existing risks should be assessed together with identification of any additional risks that undertakings may have become exposed to.
- 2.2. The Own Risk and Solvency Assessment (ORSA) was designed and considered as an important and effective tool for risk management. The performance of an ORSA under the current circumstances is to give insight into the potential impact of the COVID-19 pandemic on the undertaking's risk profile to support the decision making by their administrative, management or supervisory body (AMSB). In addition, it promotes the identification and effective management of the undertakings' risks to ensure they have sufficient capital to absorb possible losses and help steer their business through periods of adversity.

¹ Regulation (EU) No 1094/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Insurance and Occupational Pensions Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/79/EC (OJ L 331, 15.12.2010, p. 48).

² Notwithstanding the fact that specific points of this Supervisory Statement describe supervisory expectations for insurance and reinsurance undertakings, they are required to comply with the regulatory and supervisory framework applied by their competent authority based on Union or national law.

³ Decision adopting the Rules of Procedure of EIOPA's Board of Supervisors, available at: https://www.eiopa.europa.eu/sites/default/files/publications/administrative/bos-rules_of_procedure.pdf

- 2.3. The aim of this Supervisory Statement is to promote supervisory convergence, focusing on the supervision of the internal processes of undertakings necessary for a good quality ORSA, and guiding undertakings through supervisory expectations under the current situation triggered by the COVID-19 pandemic, taking into account that the impact on each individual undertaking can differ depending on its specific risk profile⁴.
- 2.4. This Statement addresses specifically the situation at the time of its publication, however the recommendations are applicable at any similar situation with the necessary adaptations.

3. Content of the supervisory statement

ORSA as a management tool

- 3.1. The ORSA process and outcomes should be used by the AMSB in any strategic discussion, in particular where developments are expected to materially impact the undertaking. The ORSA outcomes can influence strategic decisions on changes for instance to underwriting and pricing practices, to risk mitigation techniques, to investments strategy, to capital management or on improvements of operational and cyber resilience. In the current context undertakings should especially assess the need for a review of the insurance contracts' terms and conditions including the need for clarifications of coverage or exclusion clauses and further consider increasing/improving the communication with policyholders, in case of risks identified with contract coverage within the ORSA.

Timing of the regular ORSA and/or ad-hoc ORSA

- 3.2. EIOPA acknowledges that the regular ORSA is being submitted on an annual basis with different timings across Europe. In accordance with Article 45 of Solvency II, undertakings should plan their ORSA process in a manner that allows the ORSA outcomes to be embedded in the strategic planning and/or other strategic decisions. This planning should however take into account any ad-hoc strategic planning and/or other strategic decisions being taken as a result of the pandemic situation. This will allow undertakings to define the necessary changes to the business model or risk profile.
- 3.3. Navigating through the pandemic situation requires undertakings to assess on an on-going basis if an ad-hoc/non-regular ORSA is needed based on the analysis of any material changes to the risk profile. Material changes to the undertaking's risk profile can be observed, for example, due to:
 - a) material changes in the undertaking's market or credit risk exposure (including downgrade and/or default scenario);
 - b) material changes in underwriting results in lines of business which are more affected by the pandemic;
 - c) major amendments to business models, products offered, plans and strategies.

⁴ Considering the application of the principle of proportionality in accordance with Solvency II.

Furthermore in the course of the evaluation of the need to perform an ad-hoc ORSA, undertakings might engage in a supervisory dialogue with their supervisory authority.

- 3.4. If the undertaking has taken the decision to develop an ad-hoc ORSA, the undertaking should assess whether the full ORSA is necessary or if the process will focus only on specific areas of the risk profile and its impact, for example on the ongoing compliance with the Solvency Capital Requirement.

Scenarios used in the ORSA⁵

- 3.5. One component of the ORSA process is the forward-looking stress tests (including reverse stressing) and scenario analysis, taking into account the principle of proportionality. The development of the ORSA reflecting the impact of the COVID-19 pandemic, either ad-hoc or regular, should:
 - a) consider the conditions observed at a given moment and any expected stresses for example on capital markets, claims development for both non-life business (e.g. business interruption, travel, event cancellation, medical malpractice) and life-business (e.g. claims arising from higher mortality, sickness rates), and the impact on operational risks (e.g. digital resilience, business continuity);
 - b) include an assessment of the soundness and sustainability of the business model from a forward-looking perspective⁶.
- 3.6. As part of the assessment of the overall solvency needs (Article 45 (1)(a) of Solvency II) undertakings should consider the future impact of the pandemic, including potential litigation with regard to the coverage provided by insurance policies, the limited and comparable statistical data, the role of state support and other public backstops, any limitation of dividends distribution and other capital support in a group structure including financial conglomerates. Undertakings should use the latest available information from reliable sources in the different areas to be considered.
- 3.7. Given the unprecedented nature and consequences of the current pandemic, a number of major uncertainties still remain that are decisive for the future. The degree of uncertainty should be assessed for all relevant aspects, including, but not limited to, the volume of premiums, the development of claims, liquidity aspects and investment income. The identification of the sources and levels of uncertainty considered material for the undertaking should be documented.
- 3.8. Where the undertaking concludes, based on the analysis of its current risk exposure, that it is or could be materially exposed to risks revealed by the pandemic, this should be reflected in the decision and in the design of scenarios used and documented in the ORSA process. The undertaking should take into account the uncertainty in the duration and (macroeconomic) impact of the pandemic in its ORSA and, if relevant for its risk profile, consider multiple scenarios to capture this uncertainty in an appropriate manner. In this case the scenarios are expected to

⁵ All conditions and impacts are to be considered to the extent that they are relevant for the overall solvency needs taking into account the undertaking specific risk profile.

⁶ Relevant in the context where Covid-19 or future similar events are expected to jeopardize the business model and this has/will have implications for the undertaking's assessment of the overall solvency needs.

include several degrees of severity for the pandemic's impact on the undertaking's solvency and capital needs taking into account its individual situation.

- 3.9. The ORSA process includes an assessment of the undertaking's business exposures related to the risk coverages or guarantees of its insurance products. When performing this analysis, undertakings should include the assessment of possible material policyholder actions such as lapses, cancellations, claims and potential litigation over compensation disputes. In case the undertaking anticipates launching new products and/or stopping or substantially changing products, for example regarding their pricing or availability or application procedure, the ORSA should also consider the material impact of this new or amended product portfolio on the overall solvency needs as well as on the regulatory solvency.
- 3.10. In order to ensure adequate risk management, undertakings should carry out scenario analysis covering the short and long term. Undertakings should examine the effects of the COVID-19 pandemic on their solvency over a period that reflects the undertaking's risk exposure and take into account second-order effects that may occur in the longer term. EIOPA expects an analysis over a three-year period as a minimum time horizon for the majority of the insurance undertakings.
- 3.11. Taking into consideration proportionality principle and the materiality of the outcomes resulting from the assessments performed, the solvency capital requirements and eligible own funds should be recalculated according to each stressed scenario and to the valuation of assets and technical provisions. If the scenario analysis reveals that the solvency ratio may be at risk of non-compliance in the following three months, may come under pressure or fall below the solvency target self-imposed by undertakings, it is important to formulate risk mitigating measures and/or management actions that can improve the solvency position, while taking into consideration the possible limited availability of those measures and/or management actions under a stressed situation. In this context, undertakings should also assess whether their own internal metrics set for risk management are adequate and sufficient taking into account the applied stresses of the COVID-19 pandemic. The analysis should reflect upon:
 - a) risk appetite;
 - b) quantitative or qualitative indicators/measures;
 - c) overall risk tolerance limits;
 - d) metrics used within the risk management system to measure risks;
 - e) stress test framework;
 - f) monitoring process.

Done at Frankfurt am Main, on 16 June 2021.

[signed]

For the Board of Supervisors

[name]

Chairperson

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