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CLIENT BRIEFING

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GETTING READY FOR ORSA

HEALTH INSURERS FACE NEW REGULATORY REQUIREMENTS ON RISK. OUR ADVICE: DON'T TREAT THEM LIKE REGULATORY REQUIREMENTS

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Last fall, the National Association of Insurance Commissioners (NAIC) Risk Management adopted the Own Risk Solvency Assessment (ORSA) Model Act, which will require institutions to be more transparent in reporting their approaches to their risk exposures, their risk management practices, and their capital management policies. Though the legislatures of individual states need to prepare and pass their own versions of the legislation, we are advising clients to work on the assumption that they need to be ready for a full launch in 2015.

In practice, that is a very tight schedule, especially for institutions – a substantial percentage of them in our experience – that lack a well-functioning Enterprise Risk Management (ERM) framework or that do not already have a well-defined and enforced risk appetite. ORSA is not simply a matter of defining exposures or reporting financial results or the output of current point-in-time stress testing. The ORSA's intention is to drive the adoption of integrated, robust approaches to risk measurement, management, and governance across the entire enterprise. The model law describes a process that will require institutions to demonstrate that they have a comprehensive, appropriately quantitative ERM program at the enterprise level, that it is delivering risk insight, and that they are using it in making business decisions.

Though the guidelines allow for companies to define the specificity in strategy and risk appetite, they require institutions to demonstrate that they have sufficient financial resources to back their current business and their strategic ambitions. For many, this will require development of more sophisticated financial projection capabilities and an ability to "bring it all together" under a common assessment umbrella. At a minimum, this will require multi-scenario testing and significant qualitative commentary that also considers the macro and competitive environments.

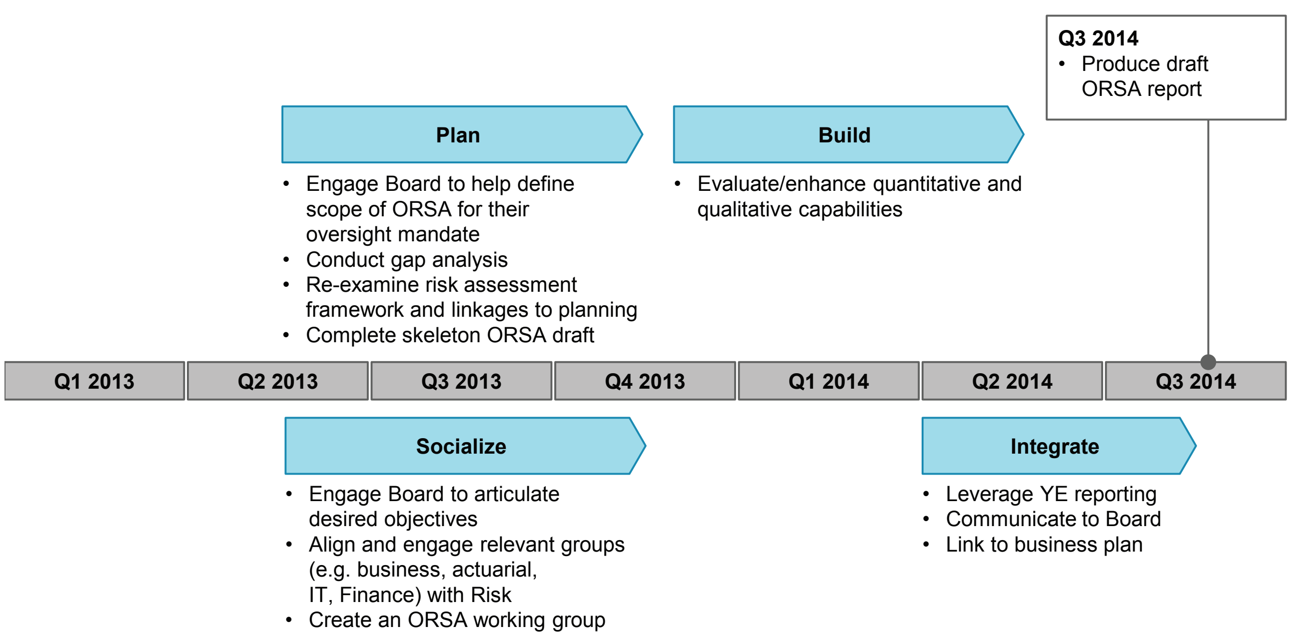
DO IT THE HARD WAY

As in so many things, there's an easy way to get ready for ORSA, and a hard way. In this case, we strongly recommend the hard way. Or to put it another way, many companies will be tempted to treat ORSA primarily as a regulatory hurdle and invest limited time and attention in it. In a few years, that might be acceptable. We think that is a bad idea. The ORSA process invites carriers to get a much stronger understanding of the risks they face, at an enterprise level, and how various contingencies might affect their solvency, capital needs, and business plans. That's an invitation you should accept.

WHY? FOR SEVERAL REASONS:

- The ORSA guidelines are not just about a new way to report data or results or a knee-jerk reaction to the financial crisis; they're about a new way to do business. And the sooner you fully adopt an integrated, robust approach to risk identification, measurement, management, monitoring, reporting, and governance, the better off you will be.
- The healthcare marketplace is undergoing a revolutionary change; new business models are replacing old among providers, and the whole industry is shifting in the direction of retail. All of this will affect the strategies and risk exposure of insurers in ways that are still not completely understood.
- The Affordable Care Act will bring a flood of new customers into the healthcare market, but also will challenge health plans to adapt to new demands and new competitive challenges.

EXHIBIT 1: ORSA – COUNTDOWN TO 2015



Source: Oliver Wyman anaylsis

- Healthcare organizations are becoming increasingly complex, as they enter new businesses and new partnership arrangements with different economics and risk profiles.
- The market presents an unusually large number of unanswered questions: Will employers continue to offer traditional health insurance, or will they shift to defined contribution plans? Will the growth of medical costs slow, or will it continue to beat inflation? Will healthcare reform continue to focus on access, or will the focus shift to costs? How will the balance shift between the fully insured business and ASO? Major uncertainties like these add to the complexity of risk analysis.

Your experience with risk, your hard-won intuitions, and even many of the systems and procedures you have already put into place to assess and manage risk have not yet caught up with a changing marketplace, but they do provide a foundation. The ORSA process is an ideal launch pad to rocket ahead.

COUNTDOWN TO 2015

As Exhibit 1 shows, there are several key efforts to prepare for ORSA. For 2013, focus on the early steps:

- Prepare for ORSA and build convergence around your vision for ERM. Create an agreed work plan, first understanding the ERM gaps. Build essential capabilities (e.g. Risk Appetite Statement and supporting quantitative tools). Also, attempt to complete a draft skeleton of an ORSA report. This will expose gaps and force answers about exactly what level of detail to disclose.
- Start, or continue to implement, your best-in-class ERM framework, which also means adopting all the components of ORSA across risk appetite, culture, assessment, management, communication, etc. in proportion to the size, complexity, and materiality of the businesses and the risks to which they are exposed.

Whether your ERM framework is new or developing, or seasoned but not battled-tested, we see a lot of immediate value from a critical self-examination of your risk appetite statement and your business planning cycle. Do these tie together? Do they reflect your aspirations of the company, the market, and competitors while realistically stressing the company's ability to manage risk in the near term? Even without an ORSA requirement, this is ORSA.

ABOUT THE AUTHOR

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ABOUT OLIVER WYMAN

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