



ACTUARIAL ASSOCIATION OF EUROPE

RISK MITIGATION TECHNIQUES

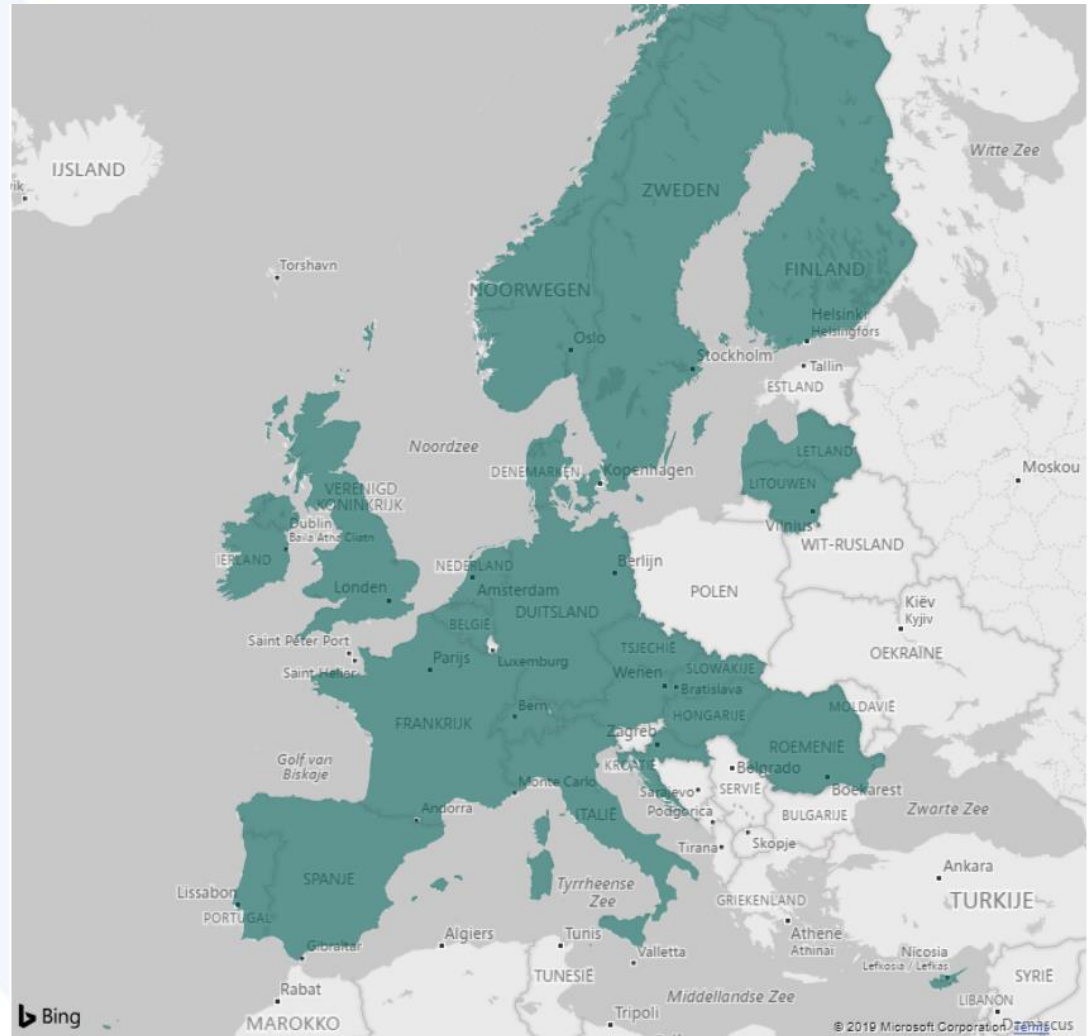
Webinar Update on Insurance Topics

17th September 2019

Matthias Pillaudin (Chairperson AAE Non-Life Working Group)

Participation in the Survey

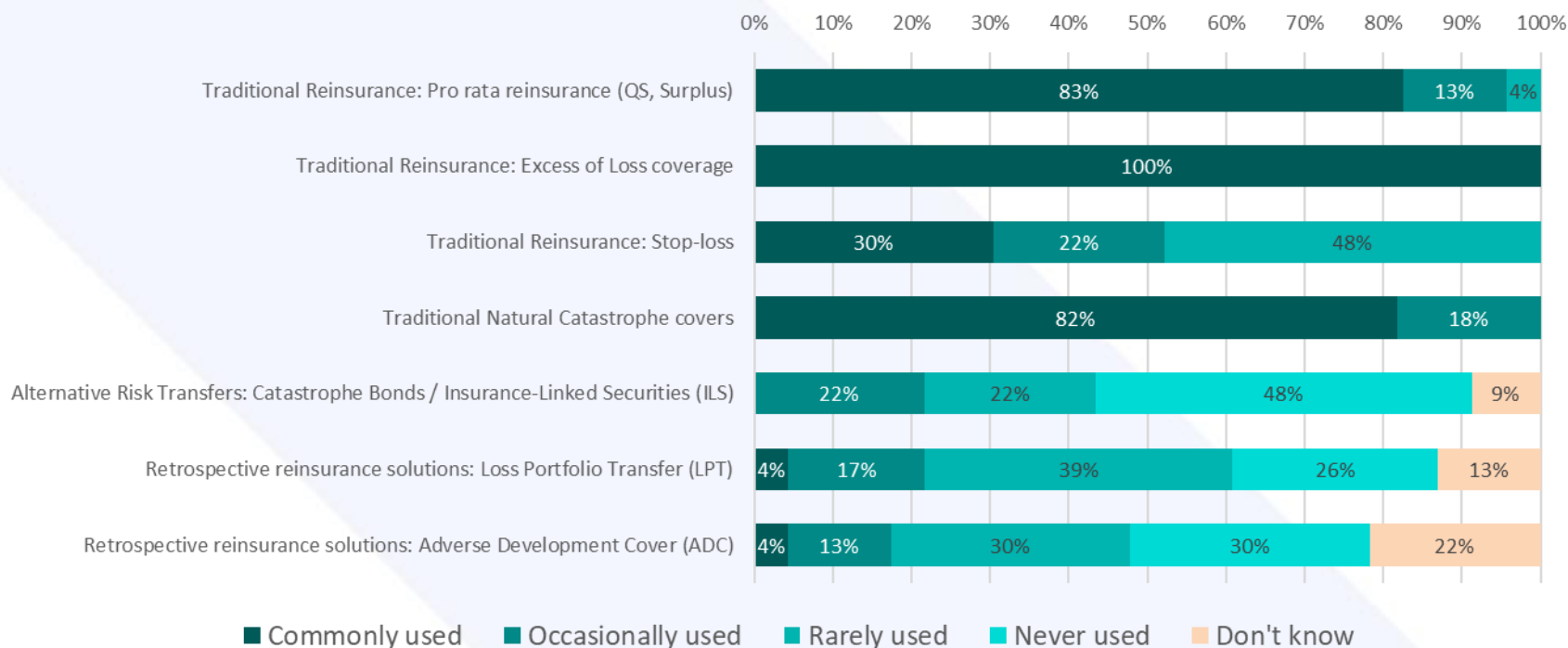
- Survey on application of Risk Mitigating Techniques (RMTs)
- Aim to assess more deeply the effectiveness of RMTs in the context of Solvency II capital requirements for Non-Life underwriting risks.
- 23 member states participated in the RMT Survey.
- Providing a good coverage of the members within the AAE.
- Recognize of limitations of the survey. Insights presented by country should be interpreted with sufficient care.



Use of RMTs for Non-Life Insurance U/W risks

Most commonly used RMTs are traditional reinsurance covers (Pro rata and Excess of Loss) and traditional covers for catastrophe risks

To what extent are the following RMTs used for Non-Life insurance underwriting risks (Premium & Reserve risk, CAT risks) in your market / country?

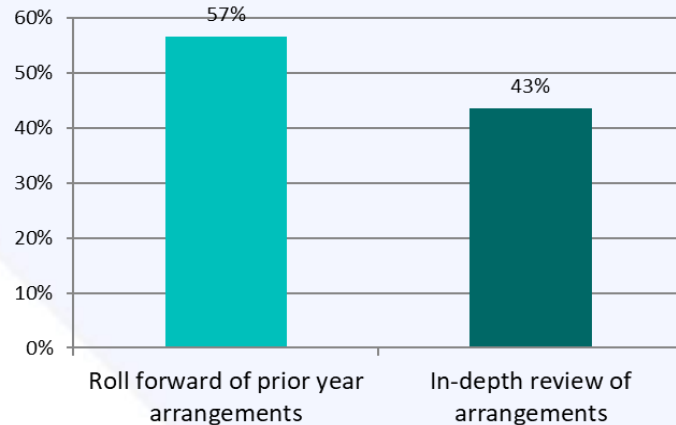


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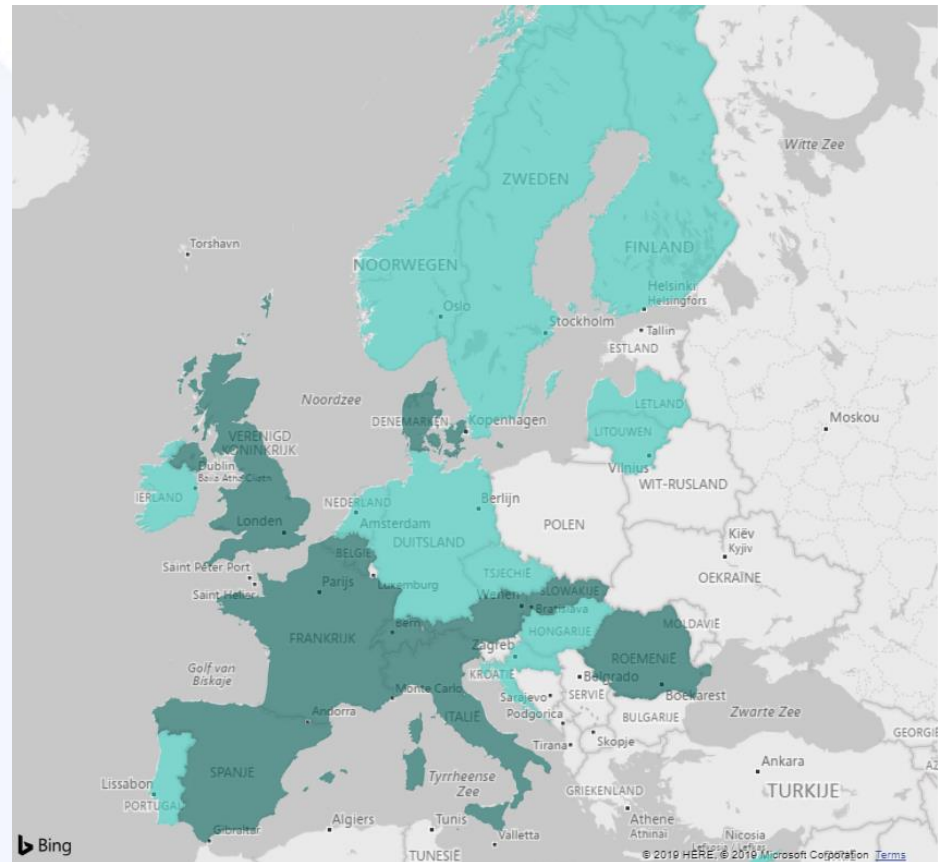
Approach on risk mitigation decisions

In 57% of participating member states typically a roll forward of prior year arrangements is taken, although remarks are made it is often a combination of roll forward and in-depth review

How are risk mitigation decisions typically made?



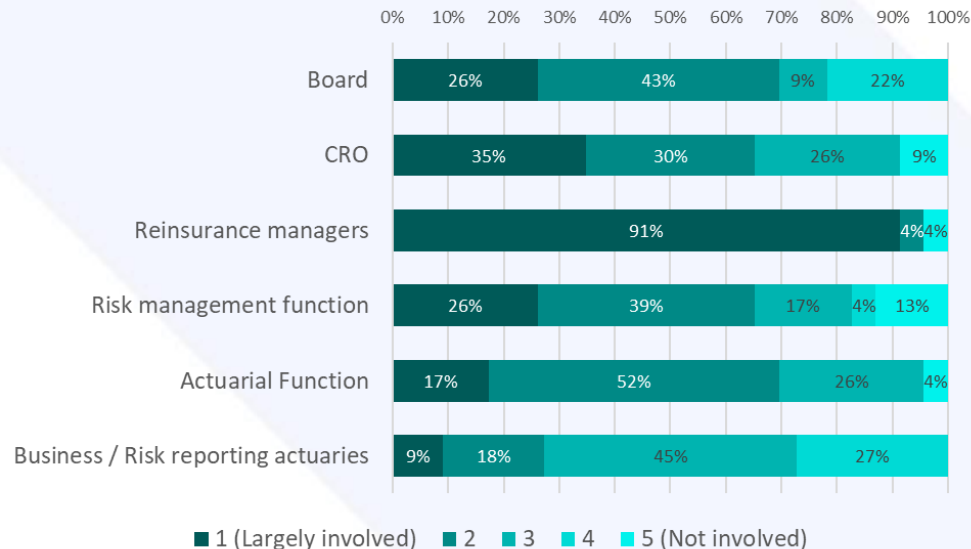
- In-depth review of the arrangements mainly centred on southern/western Europe.
- Those responding with roll forward have mentioned multiple times that it is mainly a mix of both in their member states.
- In addition a combination of roll forward and in-depth review could be the case where in-depth reviews are performed for some specific risks/arrangements and/or performed on a multi annual base.



Involvement of staff in RMT decisions

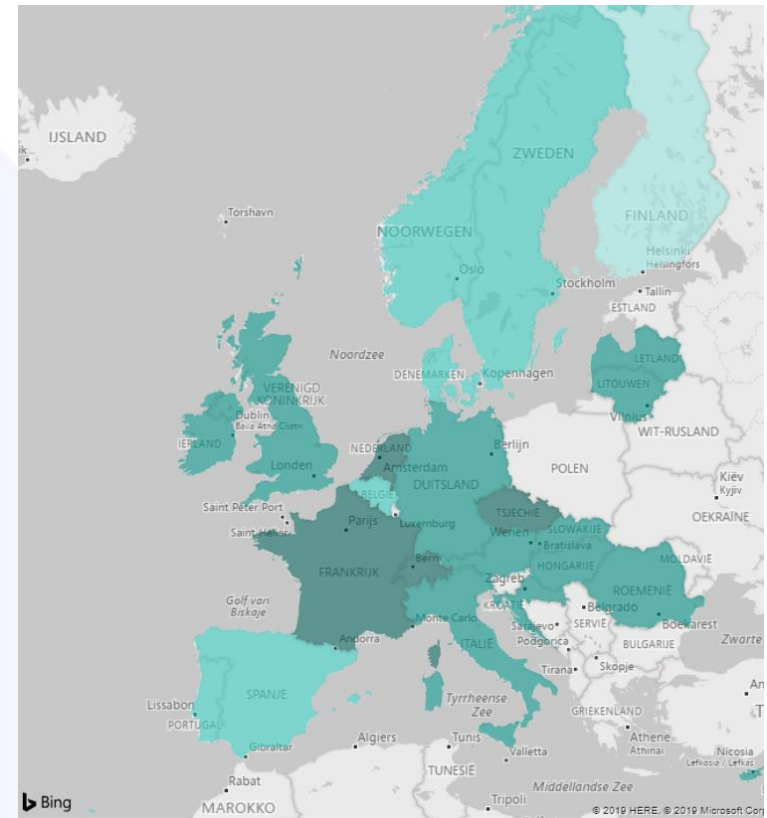
Risk mitigation decisions are primarily taken by the reinsurance managers.

What is the typical level of involvement of the following in risk mitigation decisions?



- A limited number of member states indicate that the actuarial and risk management functions are largely involved.

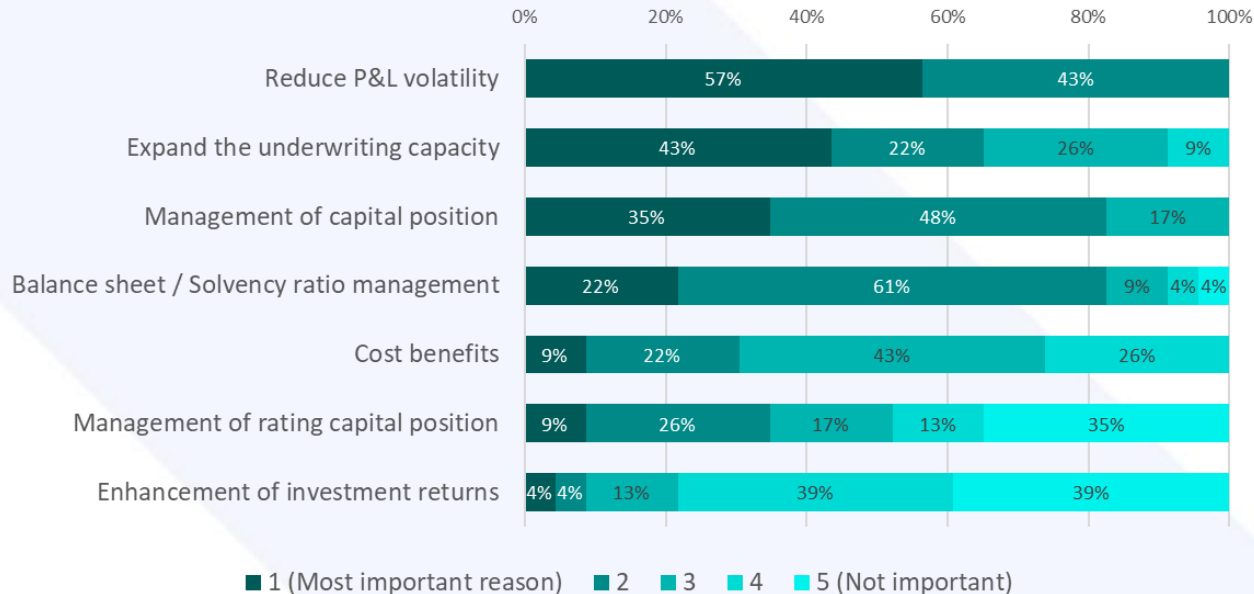
Involvement of Actuarial Function throughout Europe



Main reasons to use RMTs

Reducing P&L volatility is the most important reason for insurers around Europe to use RMTs

What are the main reasons insurers use Risk Mitigation Techniques?

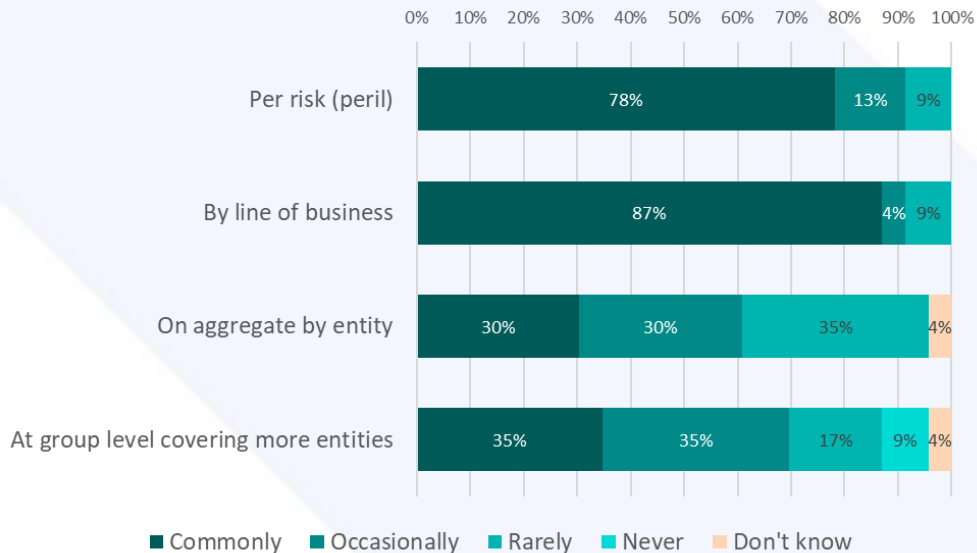


- Besides the reduction of P&L volatility and expansion of underwriting capacity the survey shows that RMTs are also largely used for management of the capital position and the solvency ratio.
- Cost benefits, rating capital position and enhancement of investment returns are less important reasons to use RMTs.

Level of structuring RMTs

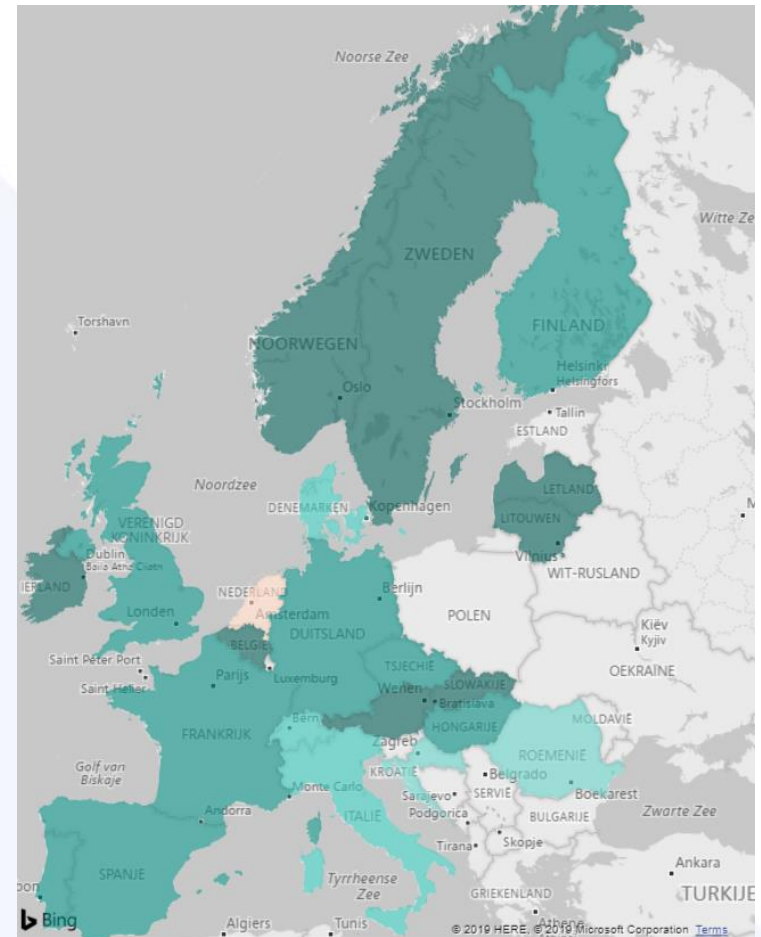
Risk mitigating techniques are most commonly structured per risk (peril) and by line of business

How frequently are RMTs structured on the following bases by insurers in your country?



- Structuring of risk mitigating techniques appears to be structured mainly per risk and by line of business.
- Structuring at entity or group level is used rarely to none in around 25 to 35% of member states.

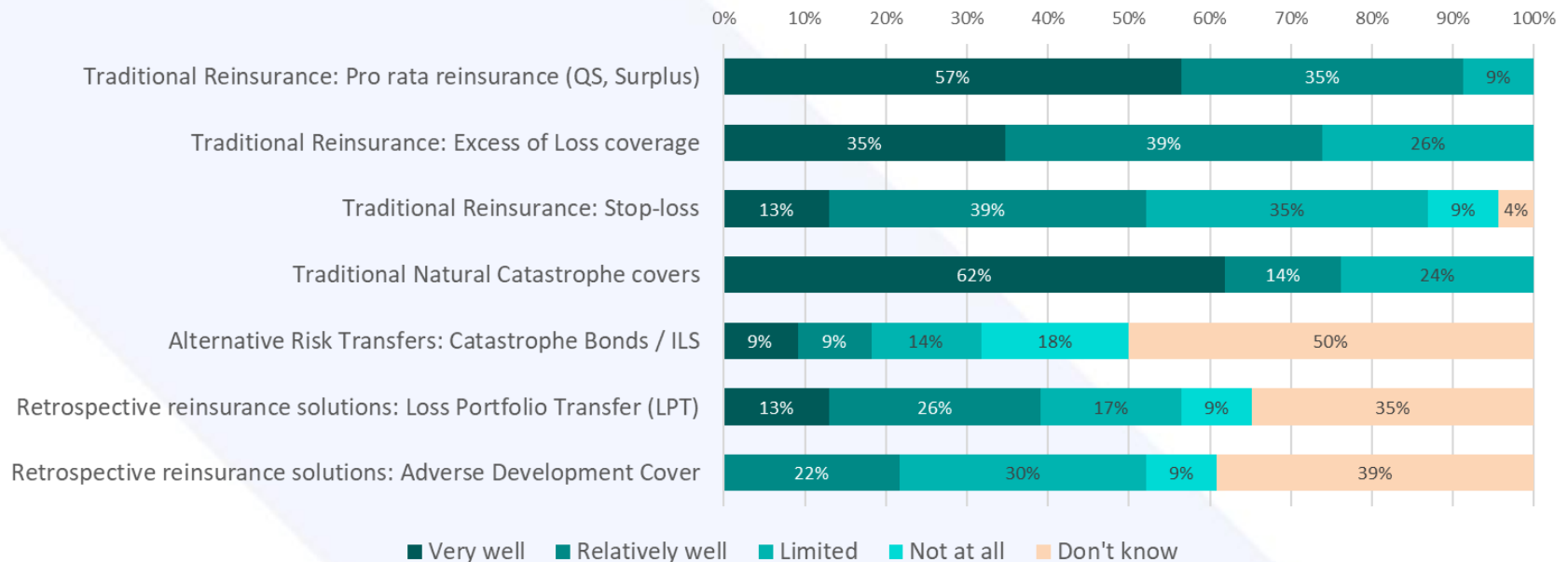
Structuring RMTs at Group Level throughout Europe



Effectiveness of RMTs to reduce SCR

Mainly the traditional RMTs on pro-rata basis and for natural catastrophe covers are most effective to reduce SCR.

To what extent are the following RMTs effective to reduce the SCR within the SII Standard Formula framework?

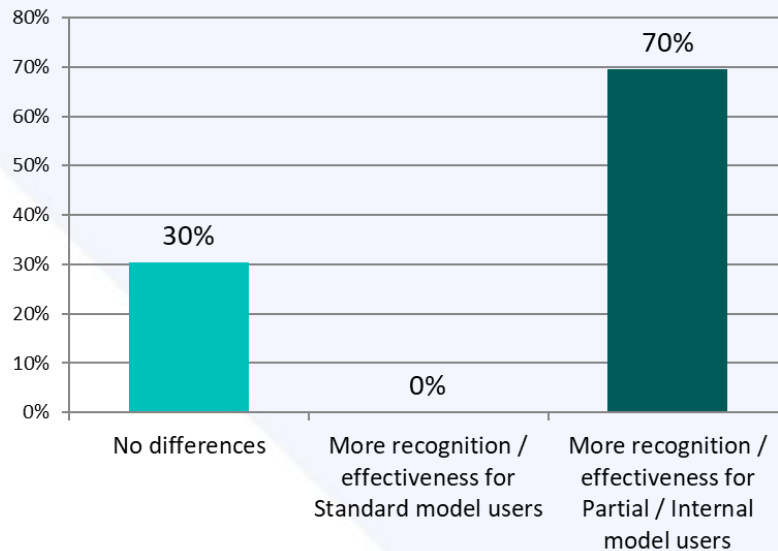


- The traditional RMTs on pro-rata basis and for natural catastrophe covers are most effective to reduce SCR.
- Excess of loss as well as stop-loss covers are acknowledged to be less effective.
- The impact of alternative risk transfers and retrospective reinsurance solutions is less known.

Difference in effectiveness RMTs between SF / PIM

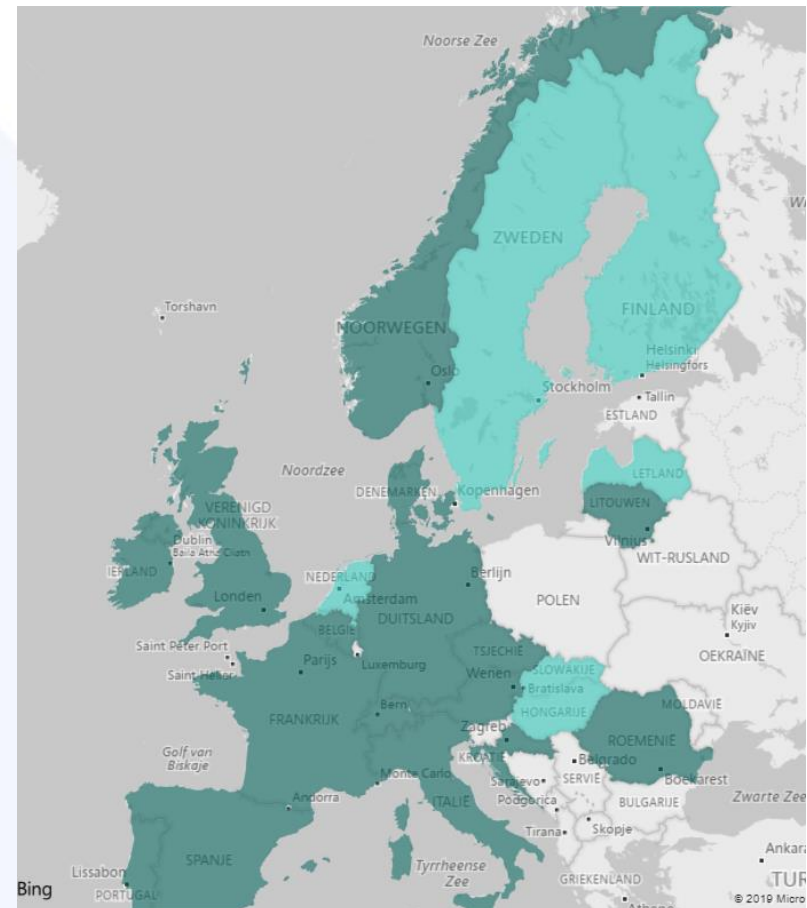
70% of the member states indicate that the use of a (partial) internal model results in more recognition / effectiveness of RMTs to reduce SCR

To what extent are there differences in effectiveness in reducing the SCR within the SII Standard Formula framework or for partial/internal models?



- The use of RMTs in partial / internal models is recognized to be more effective to reduce the SCR compared to the Standard Formula by 70% of the member states.

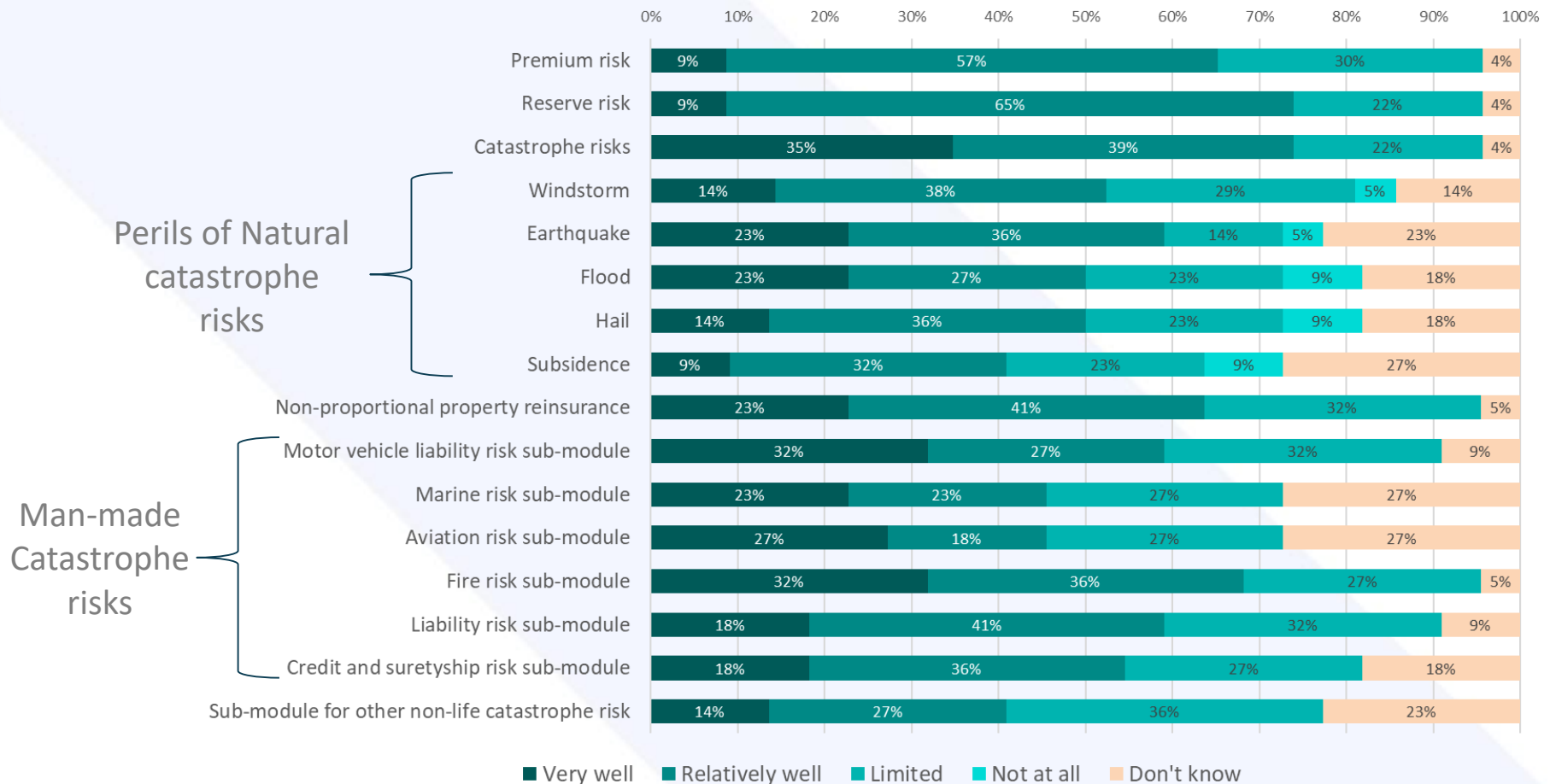
Differences in effectiveness use (partial) internal model throughout Europe



Recognition effects of RMTs to reduce SCR

The effects of RMTs on premium and reserve risk appear to be recognized relatively well to very well by around 75% of respondents

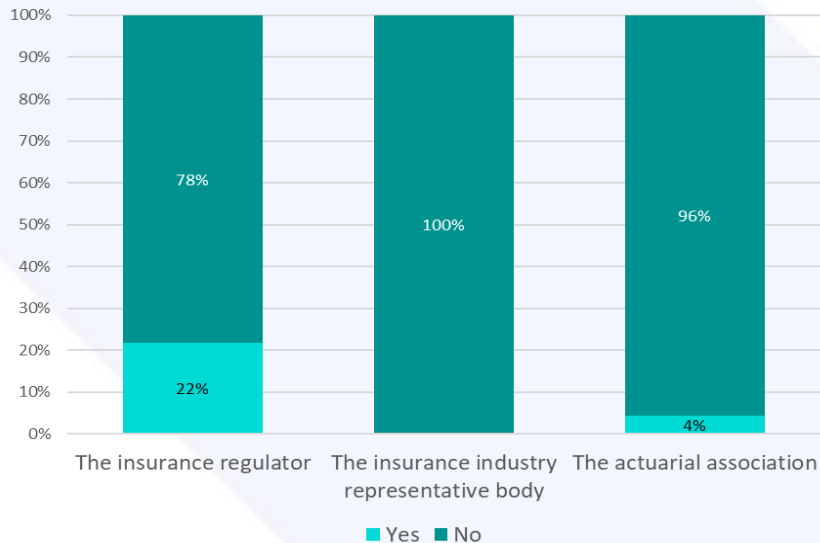
Are the effects of RMTs sufficiently recognized in the different components of the standard formula?



Guidance to use RMTs

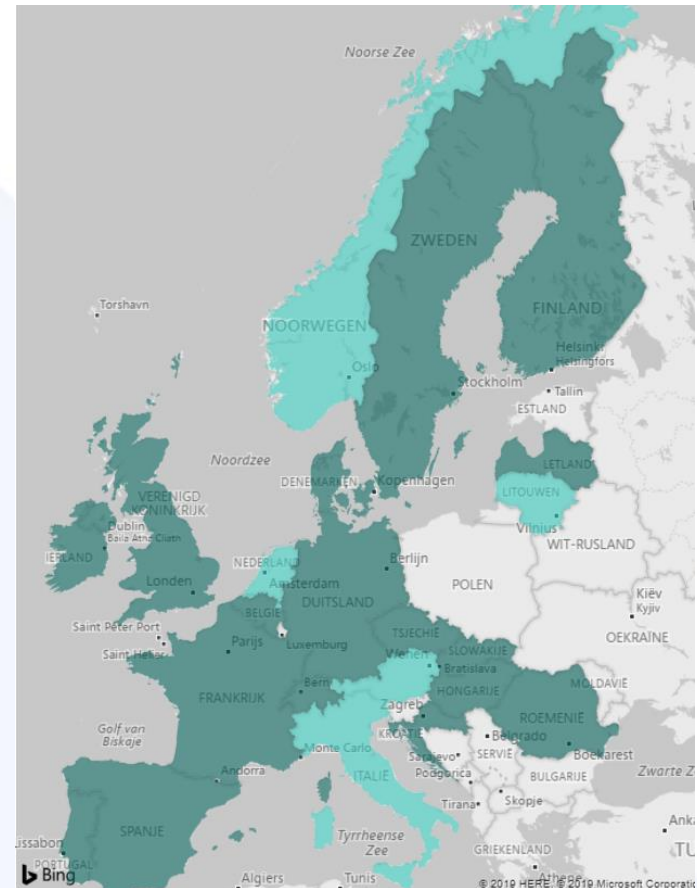
Limited guidance in the use of risk mitigation techniques has been provided throughout the European market

Are specific guidelines on the application of risk mitigation measures/techniques in the SCR provided in your country by the following bodies?



- In a limited number of member states the insurance regulator has provided guidance on the application of RMTs in the SCR.
- The actuarial association has provided guidance in one member state (the UK).
- In the comments with the survey several respondents refer to the use of EIOPA Guidance.

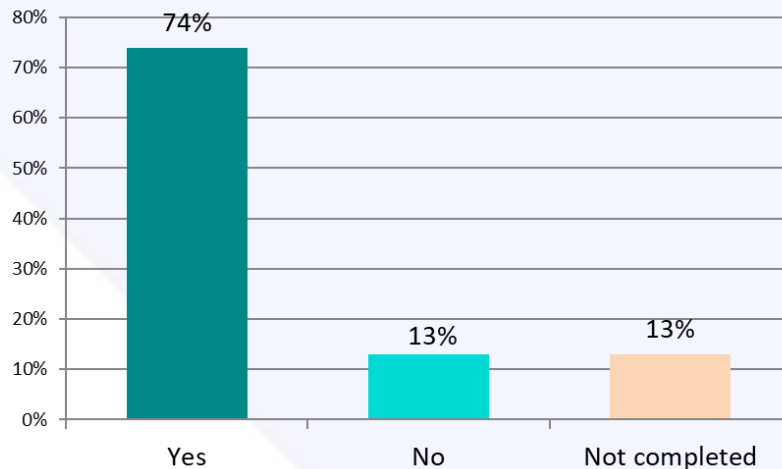
Guidance from insurance regulator throughout Europe



Solvency II leading to changes in the use of RMTs

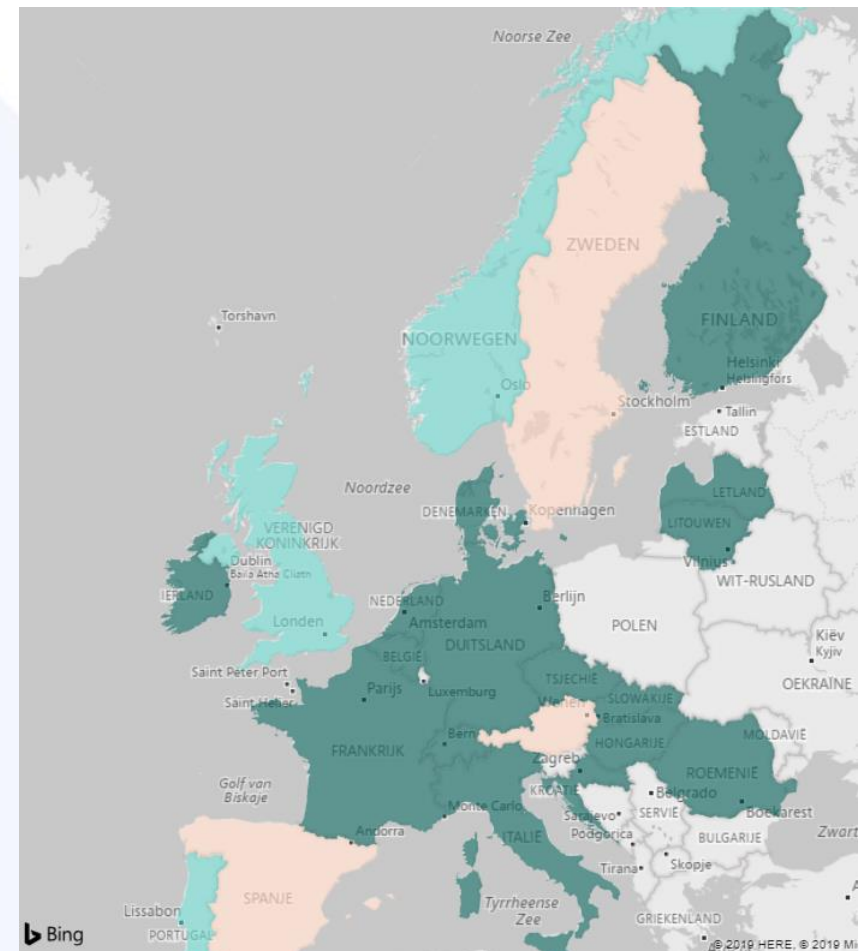
74% of all member states respondents mention that Solvency II has lead to changes in the use of risk mitigation techniques

Has Solvency II led to changes in the use of risk mitigation measures/techniques in your market?



- Solvency II has largely changed the use of risk mitigation techniques by insurers throughout Europe.
- Some member states mention that Solvency II has lead to buying more reinsurance.

Changes in use of RMTs due to Solvency II throughout Europe



Key conclusions / messages (1/2)

- This survey assessed the use of Risk mitigating techniques (RMTs) in different AAE member states:
 - RMTs based on traditional reinsurance structures are broadly used;
 - there is a limited use of alternative risk transfer and retrospective reinsurance.
- Main reasons to use RMTs are to reduce P&L volatility and increase underwriting capacity but also for capital and balance sheet / solvency II ratio management. The latter driven by the direct link between risk and capital under the Solvency II framework.
- Most participants indicate the decision on RMTs are mostly taken by the reinsurance managers. Only a few participants indicate a large involvement of the actuarial and risk management function. From the survey there appears to be a dependency between the use of RMTs for balance sheet / SII ratio management and the involvement of the actuarial and risk management functions.
- Structuring RMTs is mostly done by peril/risk or line of business. Around 40% of the participants indicate that structuring RMTs is rarely to never done on an entity or group level. Particularly under Solvency II an integrated approach on entity or group level could be beneficial from a risk and capital perspective.
- Mainly the traditional RMTs on pro-rata basis and for natural catastrophe covers are indicated to be most effective to reduce SCR. Alternative risk transfers and retrospective reinsurance are presumed much less effective to reduce SCR. There is currently no easy fit for these RMTs in the standard formula.

Key conclusions / messages (2/2)

- Around 75% of respondents mention that Solvency II has led to changes in the use of RMTs.
- Participants indicate that RMTs are in general relatively well recognized in the SF for the premium and reserve risk. For the different components of the catastrophe risk RMTs it is interesting to note that results are more diverse; rather mentioning the RMTs are recognized very well or limited to not at all. This could potentially be driven by differences in interpretation or the actual reinsurance structures.
- It is broadly recognized that the SF is less effective in capturing the RMTs. Although this makes perfect sense, this could lead to less optimal reinsurance solutions for SF users as the choice of RMT might be driven by its effects on the SCR rather than the actual risk that it mitigates. Rather than less optimal RMTs under the SF this ideally should lead to improvements in the allowance of RMTs in the SF or insurers moving to (partial) internal models.
- So far limited guidance in the use of risk mitigation techniques has been provided throughout Europe. Guidance used appears to be limited to EIOPA and local regulators.
- The results of the survey show differences in use and effectiveness of RMTs in the SF throughout Europe. To the view of the AAE Non-Life working group the results of this survey could be used as starting point to further discuss these differences with the aim of further harmonization and improved applicability of RMTs throughout Europe.