

ORSA/ERM Considerations for Insurers in a COVID-19 Environment

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Speakers:

Ellen M. Dunn, Co-Leader of Insurance Litigation Practice, Sidley

Michael P. Goldman, Co-Leader of Insurance and Financial Services Practice, Sidley

Moderated by:

Andrew R. Holland, Leader of U.S. Insurance Regulatory Practice, Sidley

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Today's Presenters



Ellen M. Dunn

*Co-Leader of Insurance
Litigation Practice*

Sidley



Michael P. Goldman

*Co-Leader of Insurance &
Financial Services Practice*

Sidley



Andrew R. Holland

*Leader of U.S. Insurance
Regulatory Practice*

Sidley

COVID-19 – New Challenges for the Insurance Industry

- **The scope and impact of the COVID-19 pandemic on the insurance industry will be more pervasive than that of past events**
 - Broader geographic reach
 - Affecting insurers both operationally and financially
 - Affecting all lines of business
 - Affecting all insured segments of our society/economy: businesses across a variety of industries, as well as individuals

State Insurance Department Oversight and Reporting

- **State regulators are already requesting ad hoc reports to assess insurers' response to COVID-19**
 - NAIC Reporting Template
 - New York DFS Requests
- **Insurers should ensure that their Form F (ERM) and ORSA reports are consistent with these ad hoc reports and appropriately disclose the impact of COVID-19 on their operations and financial condition**

Enterprise Risk Report (Form F)

- Developed primarily as a result of the 2008 financial crisis
 - Ultimate controlling person (UCP) required to report on ***material risks within the insurance holding company system*** that could pose ***enterprise risk*** to the insurer
 - “***Enterprise risk***” means ***any activity, circumstance, event or series of events involving one or more affiliates of an insurer*** that, if not remedied promptly, is ***likely to have a material adverse effect*** upon the financial condition or liquidity of the insurer or its insurance holding company system as a whole
 - Form F expressly includes a discussion of impacts of risks of non-insurer affiliates that could adversely impact insurers
 - Annual filing; generally due with the Form B Registration Statement

Own Risk and Solvency Assessment (ORSA)

- **Developed as part of the NAIC's Solvency Modernization Initiative**
 - A ***confidential*** internal assessment, appropriate to the nature, scale and complexity of an insurer (or insurance group), to provide a perspective on risk and capital
 - Should cover all reasonably foreseeable and relevant material risks associated with an insurer's current business plan and the sufficiency of capital resources to support those risks
 - ***Links risk identification, assessment, monitoring, prioritization and reporting processes with capital management and strategic planning*** – including the insurer's ability to withstand financial stress
 - Must be ***conducted no less than annually***, but also at ***any time when there are significant changes to the risk profile*** of the insurer (or the insurance group)
 - ORSA summary report must be filed at least annually (no specified due date)

Confidentiality - ORSA

- A. Documents, materials or other information, including the ORSA Summary Report, in the possession of or control of the Department of Insurance that are obtained by, created by or disclosed to the commissioner or any other person under this Act, ***is recognized by this state as being proprietary and to contain trade secrets***. All such documents, materials or other information shall be confidential by law and privileged, ***shall not be subject to [open records, freedom of information, or sunshine laws], shall not be subject to subpoena, and shall not be subject to discovery or admissible in evidence in any private civil action***. However, the commissioner is authorized to use the documents, materials or other information in the furtherance of any regulatory or legal action brought as a part of the commissioner's official duties. The commissioner shall not otherwise make the documents, materials or other information public without the prior written consent of the insurer.
- B. Neither the commissioner nor any person who received documents, materials or other ORSA-related information, through examination or otherwise, while acting under the authority of the commissioner or with whom such documents, materials or other information are shared pursuant to this Act ***shall be permitted or required to testify in any private civil action*** concerning any confidential documents, materials, or information subject to subsection A.

COVID-19 Related Operational Risks

Examples:

- Shelter-in-place orders
- Remote work and related cyber/technology exposure
- Reduced workforce due to illness / quarantine requirements
- Impact on outsourced functions / third-party vendors
- Changing and conflicting state insurance department guidance
- Barriers to typical communication channels
- Disruption to usual management oversight and communication with board of directors
- Return to work and related safe environment protocols

COVID-19 Related Financial Risks

Examples:

- Impact on new business and underwriting capabilities
- Timeliness / collectability of premium payments
- Operational implementation of cancellation and non-renewal moratoriums
- Policyholder requests and regulatory orders requiring policy re-rating or refunds
- Investment performance
 - Market volatility and fluctuations in interest rates
 - Credit deterioration and resulting RBC ratio effects
- Impact of social inflation and coverage mandates
 - Broad scope of affected lines of business (e.g., expanded business interruption coverage)
 - Related actuarial challenges
- Counterparty credit exposure
- Effect on reinsurance and reinsurers
- Liquidity and access to capital markets
- Potential impact of ratings downgrade

Form F Disclosure

- Responses to the following prompts, which are contained in the Form F, may be affected due to the previously discussed operational and financial risks.
 - Any material developments regarding **strategy**, internal audit findings, **compliance or risk management** affecting the insurance holding company system
 - **Business plan** of the insurance holding company system and **summarized strategies for the next 12 months**
 - Identification of insurance holding company system **capital resources and material distribution patterns**
 - Identification of any **negative movement, or discussions with rating agencies** which may have caused, or may cause, potential negative movement in the credit ratings and individual insurer financial strength ratings assessment of the insurance holding company system (including both the rating score and outlook)
 - Information on **corporate or parental guarantees** throughout the holding company and the **expected source of liquidity** should such guarantees be called upon
 - Identification of **any material activity or development** of the insurance holding company system that, in the opinion of senior management, could adversely affect the insurance holding company system

ORSA Report

- The following components of the ORSA may need to be reviewed in view of the effects of COVID-19.
 - **Description of insurer/insurance group's ERM Framework**
 - Identified shortcomings in the insurer's business continuity plans and ERM framework
 - **Insurer/insurance group's assessment of risk exposures:**
 - Normal and stressed environments
 - Relationships between risk categories
 - **Group Assessment of Risk Capital and Prospective Solvency Assessment**
 - Fungibility of capital within holding company system
 - Impact of stacked capital
 - Potential restrictions on previously planned dividends
 - Servicing of holding company debt or insurer surplus notes

Consistency with Other Disclosure

- **Content of the reports should be consistent with:**
 - **Ad hoc reporting to state insurance departments**
 - **Other public disclosure by the company or members of its holding company group**
 - Coordination with SEC reporting team, marketing/public relations, government/regulatory affairs, etc.

Potential for Enforcement Actions

- **Market conduct examinations and compliance with state insurance department directives**
- **Likelihood of increased consumer complaints**
- **Potential for conflict between anti-rebating / inducement prohibitions and consumer friendly actions**
- **Need to avoid unfair discrimination**

Potential for Coverage Litigation Consumer/Investor and Other Class Actions

- **Business interruption coverage, pandemic/virus exclusions and requirements for physical damage to property to trigger coverage**
- **Public Company Disclosure and D&O Coverage Issues**
- **Workforce-related claims (i.e., disproportionate furlough/layoff policy, unsafe environment claims, etc.)**

Potential for Legislative Action

- **Retroactive grant of coverage with respect to individuals, small businesses or all policyholders**
- **Federal solution, such as TRIA expansion, to cover pandemic losses**

Questions?

Please e-mail: chevents@sidley.com.

Lawyer Bios



Ellen M. Dunn

Partner
Sidley
edunn@sidley.com
New York +1 212 839 8540

ELLEN M. DUNN is co-leader of the firm's Insurance Litigation group and has 25 years of experience representing life, health and property casualty insurers in litigation, regulatory investigations, administrative hearings and compliance matters, including privacy and data security. She has extensive experience with internal investigations, policyholder and shareholder class actions, insurance insolvencies, complex contractual disputes and commercial arbitrations.

Ellen regularly represents insurers before state insurance departments and in investigations and inquiries by state attorneys general, particularly in connection with market conduct and other compliance issues.

Formerly co-head of another global law firm's U.S. Litigation practice, Ellen also served as a Special Assistant United States Attorney in the Banca Nazionale Del Lavoro (Iraqgate) investigation for the U.S. Department of Justice.

Ellen has been recognized by Best Lawyers in America for her work in Insurance Law since 2018.



Michael P. Goldman

Partner
Sidley
mgoldman@sidley.com
Chicago +1 312 853 4665

MIKE GOLDMAN is co-leader of the firm's global Insurance and Financial Services group and a member of Sidley's Executive Committee.

Mike advises insurance industry clients in connection with acquisitions, divestitures and corporate reorganizations (including demutualization and mutual holding company conversions); the formation, capitalization and corporate financing of insurance companies and related ventures; the regulation of insurance holding company systems; the regulation of insurance company investment practices, including the use of derivative instruments and strategies; the structure and regulation of alternative risk financing mechanisms and complex reinsurance arrangements, including insurance securitization and derivatives, loss portfolio transfers and commutations and the placement of insurance-linked securities; the structure of unique marketing and insurance distribution systems; and captive insurance companies, risk retention groups and other alternative market mechanisms.

Mike also represents investment banks, commercial banks, private equity funds, investment advisers, derivatives dealers and other sectors of the financial services industry, with respect to insurance company relationships and transactions.



Andrew R. Holland

Partner
Sidley
aholland@sidley.com
New York +1 212 839 5882

ANDREW HOLLAND leads the U.S. insurance regulatory practice within Sidley's Insurance and Financial Services group. His practice is concentrated in the representation of insurance companies, insurance intermediaries and institutional investors with respect to insurance regulatory and corporate matters. He also serves on the firm's COVID-19 Task Force.

He has a broad range of experience, including corporate transactions, enforcement matters, corporate governance, licensing of insurers, insurance holding company act issues, financial examinations and statutory accounting matters, producer compensation and non-admitted insurance, and has also advised numerous insurtech startups and sharing economy companies with respect to insurance regulatory matters.

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