

COVID-19: impact on risk management

The impacts of Coronavirus will be long and enduring. Already there is an expectation of a global depression that will impact on the global trading environment. Specifically for insurance, the pandemic is presenting concerns over how the insurance industry will manage COVID-19 related claims: it is a fine line to tread defending against an onslaught of claims that could lead to shareholder suits on the one hand and reputational damage or bad faith action if perceived as not honouring contractual obligations.

Aside from the pessimistic outlook, there is some optimism to be had. With new technologies and innovation emerging as a result of the operating model, and remote working, change taking place as a consequence of the crisis.

It is fundamental that the enterprise risk management framework tunes in with the pace of change and volatilities. Risk management needs to be agile, fast-responding, focused and forward thinking.

The Commercial Insurer's Solvency Self-Assessment (CISSA) process should be live and supportive to business assessment of the risks relating to environmental changes, and how the business is evolving strategy in light of COVID-19 developments.

We set out, on the following pages, some key areas for insurers and those in risk management functions to consider when assessing their response to managing the risks of COVID-19, and also in how they are ensuring the CISSA process and report appropriately adapts to the prevailing environment.

Many factors are impacting insurer's risk management frameworks, such as:



Increased agility and adaptability in the face of the evolving phases of the pandemic and its impact;

A deep and long-term test of business **resilience and continuity management;**



Continual monitoring of the impact on current **performance** and **risks** from the pandemic and its economic, **social and political impact**, on both insurers and insureds; and

Alertness to the **changes required, in the medium and longer term**, to deal with changes in the types of insurance business written and the supporting business operating model.



CISSA reporting to the Bermuda Monetary Authority contains a clear articulation of:



How an insurer is managing its own risk assessments across all risk categories and the uncertainties in its assessment of these risks;



How the business is currently strategically positioned in, and the future strategy for, the 'COVID-world';



The risk appetite set by the Board and any changes in this arising from COVID-19; and



Capital implications of these risk assessments, both now and in the future.

Impacts on CISSA



Risk

Reserving risk

- Locked up capital attributable to longer tail COVID-19 claims
- Reflection, in loss reserves, of potential legal disputes from COVID-19
- Challenges of identifying and measuring capital implications of binary events. E.g. widespread legislative reform
- COVID-19 catastrophe modelling accuracy dependant on cedants' ability to handle underlying claims in a timely and appropriate manner

Underwriting risk

- Impact on premium rates for 2020; together with potential reduction in demand (from economic downturn reducing commercial insurance market) brings significant uncertainty to premium estimation
- Changing social behavior impacting on underlying personal insurance products and purchases (eg transition to use-based insurance/ telematic products)
- Consideration of impact on policy T&Cs and corresponding pricing risk
- Optimising underwriting profitability in an unprecedented hard market, which many underwriters have never experienced before

Operational risk

- Market-wide growth in cyber attacks
- People risk management through the pandemic and its aftermath
- Technology innovation and move to remote working
- Ongoing business continuity management
- Rapid pace of change in global business environment and operating environment. Impact on supply chain



Risk management response

- Potential loss portfolio transfer or risk mitigation strategies
- Enhanced benchmarking, and comparison across peer group, of reserve stance
- Enhanced reserving governance
- Increased agility and frequency of reserve projections in light of claims trends
- Enhanced cedant claims controls, including additional management information, monitoring and assurance
- Enhanced monitoring of third party/ external data on COVID-19 related claims trends. Identification of leading indicators of potential reserve threats

- Increased controllership, governance and oversight on premium forecasting and estimation process for 2021, focusing on both rate and volume
- Benchmarking of premium forecasts to wider market data
- Engagement with underlying insurers, brokers and distribution channels on impact of underlying insurance trends
- Increased agility in board and executive governance, strategic assessment, business performance monitoring and oversight
- Review of risk appetite statements and tolerances for underwriting risk

- Increased focus on strategic refresh and revision process and governance
- Focus on the managing risks associated with new technologies and rapid, large scale expansion of such technologies
- Effective change risk management
- Robust information security risk management framework
- Sustainable operational resilience
- Review of operational risk appetite statements and tolerances



Impact on CISSA

- ✓ Consideration of external review and benchmarking of aspects of loss reserves, CISSA assumptions and capital forecasts as set out in the CISSA
- ✓ Increased Board engagement and reporting on the CISSA
- ✓ Increased agility and frequency of CISSA process to align to any increased frequency in claims reserving process
- ✓ Consideration of key measures communicated through the CISSA report

- ✓ Increased governance over premium estimates included in CISSA
- ✓ Additional disclosure of the assumptions supporting premium forecasts underpinning capital needs projections
- ✓ Increased focus and consideration, by the Board, on the medium/ long-term strategic outlook as communicated in the CISSA report
- ✓ Ensure appropriate and accurate portrayal of risk appetite and tolerances in business plan and CISSA

- ✓ Increased agility in CISSA process
- ✓ Frequent review and refresh of environmental factors, and internal performance metrics, that would trigger a CISSA review/ refresh
- ✓ Enhanced Board and executive-wide engagement and communication in relation to CISSA process and its outcomes/ reporting
- ✓ Enhanced documentation, in the CISSA report, of operational resilience and risk management, specifically new technologies, security and change
- ✓ Ensure appropriate and accurate portrayal of risk appetite and tolerances in business plan and CISSA

Impacts on CISSA



Risk

Strategic risk

- Failure to flex strategy in line with changing global landscape and/ or falling behind in adapting technology and business model changes
- Inappropriate corporate position resulting in adverse reputation and brand damage (e.g. disputing COVID- related claims; positioning with employees)

Market risk

- Stock market uncertainties reducing investment valuation and returns in 2020, amidst threat of a global depression
- Increased political risk from nationalistic tendencies globally, post-pandemic and risk of wider socio-economic disruption through bank and capital market failure

Credit risk

- Credit control from underlying insureds impaired cash flow and potential corporate failures/ restructuring activity
- Credit worthiness of reinsurers
- Economic downturn resulting in corporate failures and fall in investment returns/ valuations
- Processes and KPIs poorly manage premium collections

Liquidity risk

- Cash flow impaired by increased claims
- Increased claims place pressure on collateral arrangements



Risk management response

- Continual monitoring of environmental analysis within which strategy is set
- More frequent and deeper periodic review/ refresh of strategy and risk appetite statements by executive and Board
- Enhanced processes and controls to identify, collate and monitor claims attributable to COVID-19

- Review of variance at risk in investment portfolio
- Increased frequency and depth to investment portfolio review and analysis, especially for illiquid/ low-grade and long-term investments
- Enhanced assessment of geographic reach and risk of the investment portfolio and insurance business, integrating political risk into these assessments
- Regular and routine assessment of structural review of the investment portfolio and underlying risk

- Enhanced focus and controllership within credit control
- Amendment to credit terms and assessment of T&C to cancel underlying risk if premium defaults
- Increased focus on premium default risk factors underlying premium forecasts

- Increased and real time monitoring of claims payment trends
- Introduction of AI/ predictive tools, to assess cash flow needs given COVID-19 claims
- Enhanced frequency and depth of governance and oversight of collateral arrangements to ensure all remain fit for purpose



Impact on CISSA

- ✓ Enhanced governance, oversight and reporting in CISSA, of any COVID-19 claims that are currently disputed/ rejected, where legal action or reputational damage may impact on claims treatment
- ✓ Clarity on triggers (from environmental factors) that would require a formal/ partial strategic re-assessment and/ or re-run of the CISSA process

- ✓ Increased reporting on underlying market risk within the investment portfolio and geographical/ political risk within the CISSA report
- ✓ Clarity on triggers that would require a re-run of the CISSA process should investment market risk fall below risk tolerances, challenging the underlying investment strategy
- ✓ Enhanced documentation of valuation assumptions underpinning illiquid/ low-grade investment valuations

- ✓ Documentation of assumptions within capital forecasts in relation to credit default factors

- ✓ Increased evidence, within the CISSA, of the process for asset-liability matching

Contact us

Our Bermuda-based team, of risk management, actuarial, technology, governance and assurance professionals, are already supporting a range of clients on COVID-19 implications.



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