
Report to the Executive and Professionalism Committees

Prepared by the Actuarial Standards Committee

3 July 2014
Submission

The Actuarial Standards Committee (ASC) is pleased to submit this report to the Executive Committee and the Professionalism Committee. It summarizes the analysis conducted by the ASC based on comments received on the Draft Statements of Intent for ISAPs [5] and [6] – Enterprise Risk Management.

We would like to record our thanks to associations and individuals commenting on the draft SOI, and to the members of the ERM Task Force of the ASC who contributed to the preparation of the draft SOI and analysis of comments.

Exposure of Draft SOIs

Draft SOIs were exposed for comment on 11 April 2014 with a comment deadline of 13 June 2014. We received comments from 10 member associations and five other organizations. All respondents are listed in the Appendix.

A comment template was provided to facilitate content submission and was used by 13 of the 15 respondents. The survey asked four questions:

• Do you agree an ISAP is needed on actuarial services in relation to insurer ERM models?

• Do you agree an ISAP is needed on actuarial services in relation to insurer ERM programs envisaged by the IAIS’s ICPs (particularly 8 and 16)?

• Are any of the proposed topics inappropriate for inclusion in these ISAPs? If so, please explain why the particular topic should not be included.

• What other topics should be included in these ISAPs? Please cover why you wish guidance in this area and if appropriate provide an example to illustrate the issue. Also please indicate in which of these two ISAPs such guidance should be placed.

It also provided a space for additional comments. The full text of all comments is compiled in the report Summary of Responses to Consultation.

Broad support for developing model ISAPs

There were 15 comments submitted with a clear majority of respondents supporting the development of model ISAPs on both topics: actuarial services in relation to insurer ERM models (ISAP [5]) and actuarial services in relation to insurer ERM programs envisaged by the IAIS’s ICPs (ISAP [6]):

• 10 respondents were in favor of developing both standards.

• One respondent could not come to a decision. They did not reach consensus on the “necessity” of these standards but would agree that these standards are “desirable” and that there would be a benefit to having ISAPs on ERM.
• One respondent favored the development of a standard on actuarial services in relation to insurer ERM models (ISAP [5]). However that same respondent was concerned that the proposed scope of ISAP [6] was too broad and would not be the most effective means to facilitate widely accepted convergence of practices within and across jurisdictions.

• Three respondents did not feel that these ISAPs were necessary at this time:
  - One association member believes that “general principles about actuarial practice are sufficient.”
  - One association member supports the development of an IAN (International Actuarial Note) to promote good practice while allowing the subject to develop before standards are created.
  - A third respondent, an organization of risk managers from the insurance industry, states that “local (European) standards are already available and therefore, there is no need to have an additional set of global standards.”

Common Themes

Respondents provided a variety of suggestions on the content of the model ISAPs, with generally broad consensus on the following:

• The model ISAPs should be principles based.

• The model ISAPs should not repeat guidance already provided within other ISAPs.

• The model ISAPs should reflect the principle of proportionality whereby the work required should be proportionate to the nature, scale and complexity of the business being modelled.

• The model ISAPs should not contain educational material; such material is better provided in an International Actuarial Note (IAN).

• The model ISAPs should not place undue burden on actuaries vs others providing the same or similar services.

The ASC recognizes the importance of all these issues and will direct the ERM Task Force to incorporate them into the development of the actual ISAPs.

Other Issues

Individual respondents noted a number of other issues which the ASC considered:

“For both ISAP 5 and ISAP 6, we suggest the inclusion of language regarding how actuaries should collaborate with others, actuaries and non-actuaries alike, for the benefit of the Insurer Enterprise Risk Models and the ERM Programs for the company.” - The ASC intends to highlight the importance of collaboration in the ISAP but believes that the discussion of how actuaries should collaborate with other actuaries and non-actuaries is more appropriately addressed in an IAN.
“For both ISAP 5 and ISAP 6, reinforce the consistency with the emerging or existing regulation and actuarial guidance (e.g. ICP 8, 16 and 17, Basic Capital Requirement or BCR, High Loss Absorbency requirements or HLA, and Insurance Capital Standard or ICS for Global Systemically Important Insurers or G-SIIs, Solvency II, Actuarial Standards of Practice in the USA, the CERA designation, guidance E-19 in Canada, etc.).” – The ASC recognizes the importance of the consistency referenced above and will review any proposed standards in that light. In addition, the development of any ERM standards will also incorporate review of a Note on The Use of Internal Models for Risk and Capital Management Purposes by Insurers produced by the Solvency Subcommittee of the Insurance Regulation Committee (http://www.actuaries.org/CTTEES_SOLV/Documents/Internal_Models_EN.pdf) and any IANs produced by The Enterprise and Financial Risk Committee.

“The goal/value proposition of the ISAP should go beyond capital adequacy. Instead, the focus of the ISAP should be providing guidance to companies to set up the right infrastructure for risk taking activities to enable long term sustainability in the business.” – The ASC believes that this scope would go far beyond what our members would support.

“…as local (European) standards are already available, we do not see the need to have an additional set of global standards.” – The ASC believes that, as the survey has shown, IAA members do not feel that there are sufficient standards currently in existence.

“ISAP [6] should focus on qualitative aspects of ERM and omit quantitative aspects.” – The ASC believes that, while much of ERM actuarial work is qualitative in nature, the quantitative aspects can be equally important.

“The scope of these proposed ISAPs should be considerably narrowed and, in the first instance, limited to areas where the actuary has a relevant statutory obligation or the work is performed for the purposes of, for example, ICP 8 (Risk Management and Internal Controls) and ICP 16 (Enterprise Risk Management for Solvency Purposes) issued by the International Association of Insurance Supervisors.” – The ASC has been very careful in defining the already narrowed scope of the current SOIs and the large majority of the survey responses support that decision.

“Some additional guidance on specific risk categories may be useful (e.g., operational risk, liquidity risk, group risk).” – The ASC agrees that a discussion of these topics has some educational value and has recommended that it be included in IAN material.

“To be included in ISAP 6: Reporting of risk management information, Emerging risks, Risk culture, Governance of the risk processes, Interactions between Risk management and Actuarial functions - IAN could be considered for some of these topics.” and “To be considered in ISAP 5: Use of proxies (including roll forward), Basis risk assessment, Frequency of calculations, Reverse stress testing - IAN could be considered for some of these topics.” – The ASC acknowledged the value of incorporating these topics and has modified the SOI accordingly.

“The scope of ISAP [6] should also include risk governance and risk culture” and “the scope of ISAP [6] should also cover risk appetite framework and how risk appetite can be cascaded to risk tolerance and limits.” – The ASC recognizes that these topics are key pieces of ICP 16 and will certainly address them in the ISAP.
Changes to the Draft SOIs

The attached SOIs reflect the changes discussed above. Based upon the largely supportive feedback from the responses, these changes consist of:

1. Clarifications concerning the topics to be included; and,

2. Additional material suggested by the respondents that the ASC will include in its recommendation to the The Enterprise and Financial Risk Committee to develop an IAN on Enterprise Risk Management.

As noted in the proposed SOIs, the ASC believes that the following topics are better addressed in one or more International Actuarial Notes rather than in an ISAP:

- Detailed considerations for Risk and Control Self-Assessment;
- Risk Governance and Risk Culture;
- Detailed considerations for Risk Appetite, Tolerance and Limits;
- Infrastructure for risk taking;
- Guidance on specific risk categories;
- Detailed considerations for techniques for quantification of various types of risk;
- Detailed considerations for determination of risk interdependencies and aggregation of risks;
- Detailed considerations for implications of the differences between economic and regulatory capital adequacy;
- Reporting of risk management information;
- Emerging risks;
- Interactions between Risk management and Actuarial functions;
- Detailed model validation procedures;
- Detail of establishing probability distributions and testing of statistical quality;
- Specific requirements appropriate to the use of partial models (i.e. a model that combines elements of an insurer’s own model and a model prescribed by regulation);
- Methods for verification of the accuracy and completeness of data;
- Detailed procedures for assessment of dependency and diversification of risks; Limitations of ERM-Models; and
- “Governance Considerations” concerning ERM-Models.

Recommendation

Given the broad support for developing model ISAPs, the ASC asks the Executive Committee to approve SOIs for Proposed ISAPs on both topics: actuarial services in relation to insurer ERM models (ISAP [5]) and actuarial services in relation to insurer ERM programs envisaged by the IAIS’s ICPs (ISAP [6]) thereby authorising the ASC to develop the appropriate ISAPs.
Appendix – Respondents to the Draft SOI

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<thead>
<tr>
<th>Letter Number</th>
<th>Submitted By</th>
<th>Date Received</th>
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<td>1</td>
<td>DAV – Deutsche Aktuarvereinigung e.V.</td>
<td>26 May 2014</td>
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<tr>
<td>2</td>
<td>Office of the Superintendent of Financial Institutions Canada</td>
<td>4 June 2014</td>
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<td>3</td>
<td>Institute of Actuaries of Australia</td>
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<td>5</td>
<td>Canadian Institute of Actuaries</td>
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<td>6</td>
<td>Dutch Actuarial Association</td>
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<td>7</td>
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