Statement of Intent (SOI) for a Proposed International Standard of Actuarial Practice (ISAP) on Enterprise Risk Management

Submitted by: The Enterprise Risk Management Task Force of the Interim Actuarial Standards Sub-Committee (IASSC)

Background

ERM is an emerging discipline and recent economic events have shown that enhanced ERM practices could contribute significantly in protecting companies from future market turmoil. That need for enhanced risk management has been recognized by the G20 heads of state in their November 2008 Statement\(^1\) and more recently by the International Association of Insurance Supervisors in their November 2011 publication on Insurance Core Principle 16 – Enterprise Risk Management\(^2\).

However, while there currently are a number of standards for company ERM practices, there are none for ERM professionals. The development of a professional standard for ERM practitioners would help raise the degree to which ERM practices can become more consistent and reliable throughout financial services and many other industry sectors, thereby performing a highly desirable public service. It is conceivable that a well-constructed standard could be used to guide the performance of both actuaries and non-actuaries alike.

Professionalism is exhibited by of high quality educational standards in concert with high quality technical standards. The development of this standard, together with the development of the new international CERA\(^3\) educational program, will provide actuaries with an unparalleled foundation of ERM professionalism. Specifically, with regard to the new ICP 16 requirements for an Own Risk and Solvency Assessment (ORSA), professional standards of practice could make actuaries the preferred professionals for the performance of the work that supports the required management opinion on the ERM practices of insurers.


**Purpose**

Given the issues discussed above, it is expected that this standard will:

**Help to increase public confidence in the ERM work of actuaries** - With a robust set of standards, the public (including users of actuarial work products, employers and regulators/supervisors) will recognize that the highest quality ERM work will be produced by actuaries. Given the recent performance of the financial services industry, it is clearly in the public interest to promote enhanced ERM practices to help to avoid future market turmoil and to mitigate the damaging consequences of what market turmoil does occur.

**Help to achieve greater transparency and consistency** – Prior to the financial crisis many firms had ERM processes, but there was little, if any, consistency or comparability. In addition, many ERM practitioners were applying techniques that were often new and untested. Actuaries have a 100+ year history of providing assessments of many types of risk. An ERM standard will support the expansion of our discipline into the areas of contingent losses that are not directly a part of traditional actuarial assessments but which will rely heavily on the time-proven techniques that underlie many traditional analyses of risk.

**Help to give certainty to managers and regulators** - The lack of a coherent set of standards puts all users of ERM work products in the difficult position of evaluating the quality of the work without knowing if it was done in a professional manner. Actuaries who practice within a set of clearly articulated professional standards (including those addressing ERM) will be relied upon more readily by managers and regulators who want to feel more comfortable regarding the quality of the ERM work they are reviewing.

**Help to promote the development of the actuarial profession** – Taking a lead role in the development of professional standards for ERM practice, in conjunction with the CERA educational initiative, will establish the actuarial profession as the thought leader in this area.

**Scope**

The ERM ISAP will apply to all actuarial work in the areas of:

- The evaluation and reporting of risk positions; and
- The treatment of risk within a control cycle.

ERM practice may involve many different functions. It is generally agreed among practitioners and academics that the key functions are:

- The management of risk management systems;
- The integration of risk management information into decision making;
- The evaluation and reporting of risk positions; and
- The treatment of risk within a control cycle.
The first two of these functions are largely management issues and we have determined that they should not be included within actuarial standards of practice.

Specifically, this ISAP will address the following topics:

- The identification, evaluation and reporting of risk positions to company management and boards, as well as to regulators/supervisors, through risk dashboards and other methodologies;
- Economic capital modeling and methodologies for capital allocation;
- Stress testing;
- Determination of insurance risk metrics;
- Determination of other risk metrics (such as duration, convexity, delta);
- Development of risk tolerances, appetites and limits;
- Asset/Liability management; and
- Risk mitigation techniques including pooling, hedging, and reinsurance program design and technical selection.

Principle of Subsidiarity

As with all standards promulgated by the IAA, this ISAP is a model standard and imposes no responsibility on any FMA or its members. As such, it is compliant with the Principle of Subsidiarity.