

## **ESAP3 – responses to 2<sup>nd</sup> ED Formal Consultation process – 28 April 2017**

### **Introduction:**

The formal consultation on the second Exposure Draft of ESAP3 (ED2) took place during December 2016 to March 2017. We received 7 responses – from 6 member associations and the UK's Financial Reporting Council (FRC).

One member association (Deutsche Aktuarvereinigung e. V.) responded, following the deadline extension email from Monique, to say that they were not going to respond. They have not been included in the count of responses stated above. (The DAV had responded to the informal consultation with a “no comment” response.)

The 6 member associations that responded to the formal consultation on ED2 were:

- Česká společnost aktuárů (Czech society of actuaries)
- Hungarian Actuarial Society
- Institute and Faculty of Actuaries
- Instituto dos Atuários Portugueses
- Royal Dutch Actuarial Association
- Society of Actuaries in Ireland

Apart from the comments from the Royal Dutch Actuarial Association, the responses have generally been supportive of the changes we have made, with only a couple of points being raised that warrant a bit of thought. The response from our Dutch colleagues raises fundamental questions over the direction we have taken the ESAP and would seem to favour something much more like the first ED (that received so much push back from other respondents). The Dutch comments are in line with what they said in their informal consultation response, and so Gabor Hanak and two member of the ESAP 3 Task Force (David Hare and Dieter Köhnlein) held a discussion with representatives of the Dutch association (John Oost and Ernst Visser) to understand their concerns better and see if there is some middle ground that could work for all member associations. The representatives of the Dutch association expressed their view that there should be more guidance in the ESAP (e.g. on the triggering events or on the assessment of the appropriateness of the Standard Formula). However, while they would be happier if those changes were made (as it would simplify the adoption/adaption process for the Dutch association), they would accept the ESAP without fundamental changes – keeping in mind that the ESAP will be a model standard that can be customized by any member association of the AAE. The discussion took place on 22<sup>nd</sup> April. It is possible that some further suggestions of additional

material to include in the ESAP will come from our Dutch colleagues over the next week or two, in which case, an updated version of this note will be produced, but it is not envisaged that any of those suggestions will be fundamental in nature.

The purpose of this note is to present the other 6 responses, discuss the comments and suggestions they included, and record how the TF agreed to respond to them.

### **Background to the consultation:**

The 2<sup>nd</sup> ED issued for the formal consultation starting on 5<sup>th</sup> December 2016 was very similar to the version issued, a month before, for the October 2016 informal consultation. We had chosen this two-stage approach in order to reduce the risk of material new points emerging in the formal consultation.

The formal consultation was issued to all the AAE member associations, along with a list of other relevant bodies and stakeholders. We invited respondents to complete a comment template that asked the following 4 questions:

1. Do you think that the 2<sup>nd</sup> ED achieves the following goals:
  - a. Making the scope of the ESAP clear Y/N
  - b. Achieving an appropriate level of balance between core and non-core material for actuarial work Y/N
  - c. Appropriately principles-based guidance Y/N
  - d. Including only guidance that either must be followed or is on a comply or explain basis Y/N
  - e. If not then please indicate your concerns:
2. Is any of the proposed guidance inappropriate for inclusion in ESAP3? If so, please indicate which one(s) and explain why the particular topic(s) should not be included.
3. What other topics should be included in ESAP3? Please indicate which one(s) and explain why you wish guidance in the area(s).
4. Any additional comments

The consultation ran from 5<sup>th</sup> December 2016 to 5<sup>th</sup> March 2017. The AAE extended the deadline for comments until 10<sup>th</sup> March, and we received a couple more responses that week.

### **“No suggestion” responses:**

Two of the member associations responded by email to indicate their support for the ED:

- Instituto dos Atuários Portugueses: “We approve ESAP3”
- Society of Actuaries in Ireland: “The Society of Actuaries in Ireland is happy with the 2nd Exposure Draft of ESAP3.”

A third, the Hungarian Actuarial Society, completed the comment template we had issued, answering yes to the four goals in Q1, confirming that they felt that “All of the proposed guidance are appropriate” and “we do not propose any additional topic”, and had no additional comments to make.

**“Minor comment” response:**

The response from the IFoA answered yes to the four goals in Q1 and no to Qs 2 and 3 (i.e. no suggestions for material to take out or to add). However, they did make one drafting suggestion, similar to what they had said in response to the informal consultation, namely:

*“The ESAP states in the purpose section that it “provides guidance to actuaries...” (our emphasis added). There is a risk that using the term ‘guidance’ may cause confusion about the nature of the requirements within the ESAP. Therefore it may be helpful to use different terminology that makes it clear the provisions are intended to be mandatory (once implemented by Member Associations) rather than non-mandatory ‘guidance’”*

Response from TF:

The text the IFoA are quoting is from section 1.1 of the 2<sup>nd</sup> ED, which states “Purpose – This ESAP provides guidance to actuaries ....” This form of words mirrors the equivalent section of ESAP 1 which says, in section 1.1, “Purpose – This ESAP provides guidance to actuaries when performing actuarial services ...” Thus, this is a standard form of words for ESAPs and our previous steer from Gabor, as the chair of SPT, is to keep consistent with ESAP1 (and the contents of the ISAPs promulgated by the IAA using a similar language). We therefore propose writing to the IFoA to explain why we are not taking up their suggested change of wording.

By way of background, here are the comments that Gabor gave us when the FRC made a similar point in their response to the informal consultation last October:

**1.1. “Guidance” vs “requirements”**

The matter is about what we understand as “guidance”. Consistently with all ISAPs/ESAPs promulgated, the purpose talks about guidance in the sense of stipulations to be followed; i.e. the guidance is either a “must” or a “should”. E.g. ISAP1/ESAP1 states in 1.1: “This ISAP provides **guidance** to actuaries when performing actuarial services to give intended users confidence that”. All other ISAPs/ESAPs promulgated so far has the similar purpose (i.e. starting with “This ISAP provides **guidance** to actuaries”). This notion might be looked at in the UK differently. However, having in mind the intent and the meaning of the “guidance” in the sense of ISAPs/ESAPs, nothing prevents the FRC or any other local standard setter in the UK to amend the ISAPs/ESAPs and promulgate locally binding standards using different wording (e.g. using “requirements” instead of “guidance”) but keeping substantial consistency with those ISAPs/ESAPs.

I think consistency between existing ISAPs/ESAPs and ISAPs/ESAPs being developed is key.

**Responses raising more substantial/contentious issues:**

The remaining three responses, from:

- Česká společnost aktuárů (Czech society of actuaries)
- Financial Reporting Council
- Royal Dutch Actuarial Association

raise more challenge.

As stated earlier, the Dutch response was the subject of joint discussions on 22<sup>nd</sup> April. Their completed template is attached as an appendix to this document for information and comment, but no changes to the ESAP in response are proposed at this stage, other than the replacement of the word “assessing” with “considering”, in order to avoid an unintended reading of the former term.

The discussions on 22<sup>nd</sup> April provided a helpful opportunity to explore the principles-based approach of the ESAP in the context of an association that wished to produce material to help its members apply the requirements in practice. It was recognised that adopting the model standard, ESAP 3, for any association, would not stop that association also producing additional, even educational, material to help members comply with it. Indeed, the AAE is developing an educational note (its first EAN, European Actuarial Note) to help all member associations in applying ESAP 3.

The 22<sup>nd</sup> April discussions covered the criteria that had influenced what material was proposed for the ESAP and what was felt not necessary to cover (e.g. either because it was sufficiently covered by ESAP 1 or because it was a matter of law or covered sufficiently in regulatory text, with no particular actuarial consideration to add). The AAE representatives stressed their openness to considering further proposals for material to be included in the ESAP which met these criteria and the Dutch representatives have agreed to consider whether they wish to bring forward such proposals between now and early May. In the meantime, no further changes are proposed to the ESAP apart from those noted in this document.

It was also noted at the 22<sup>nd</sup> April discussions that 1.3.3 of ESAP3 is intended to use the most recent thinking of the Actuarial Standards Committee (ASC) of the IAA on that subject. The ASC is considering potential changes to ISAP 1 (in connection to the proposed merging of ISAP 1A into ISAP 1) and the current proposed text in ESAP3 reflects the expected outcome of the change to ISAP 1.

The other two responses are now discussed in turn.

#### **Response from Česká společnost aktuárů (Czech society of actuaries)**

The Czech society answered yes to the four goals in Q1, but also suggested three areas where they would like to see changes to the text. They answered no to Q2 (re material to take out of the ESAP), but, under Q3, suggested adding a new sub-section between 3.1.3 and 3.1.4. They also made 6 proposals re small “tweaks” to existing ED2 text.

#### **Q1 – suggestion 1**

The suggestion from the Czech Society is:

*“As Just a small note to article 1.2 and its second paragraph. We don’t think there is such an important difference between the two approaches in designing and effecting ORSA process as suggested by this paragraph. Either ORSA process is completely new or it comes from connecting and possibly extending existing management procedures, but one way or another at the end there is defined ORSA process which must comply with SII requirements and should be covered by ESAP3.*

*We agree both ways to the ORSA process can be acknowledged in the standard, but we would maybe write that the standard is equivalently relevant to both. Also many management processes are newly built or extended based on the SII requirements in other areas and connecting and utilizing them also for ORSA is a good way to efficient SII implementation. It also limits the risk of inconsistency between the risk management approaches presented in ORSA and those used in real risk management as discussed in article 3.1.4. We therefore see the implicit preference of the specific ORSA process in the standard as a bit unfortunate.*

*We also believe that, based on what we see, the approach of connecting and extending existing procedures to form ORSA process is more common than creating new specific ORSA process.*

*We would actually suggest that effective utilisation of existing processes and documentation should be exercised by an actuary working on ORSA. We propose to consider inclusion of an article regarding this to the standard as suggested in section 3 below.”*

TF response:

The Czech Society would seem to have read the wording in a different way to what we intended. The text was meant to recognise that a "virtual ORSA" rather than an explicit, identifiable, ORSA process could satisfy the regulations. However, they seem to have put weight on the "specifically developed" text and read it as not including re-using existing processes and reports within the explicit ORSA process. The TF **propose that, rather than re-write 1.2, we add "or amended" after "specifically developed" and then add some commentary to the EAN.**

#### Q1 – suggestion 2

The suggestion from the Czech Society is:

*"We also see some problem in the introduction to Section 3.1 which says it should relate to the actuary's role in designing the ORSA process, but in individual subsections it is sometimes difficult to say whether they relate to the actuary responsible only for the design of that part of the process or also its execution. Maybe the section 3.1 could be named "Quality of ORSA process" and the initial sentence/paragraph could be without words "the design of" leaving just "... material involvement in, or responsibility for, the ORSA process ..."*

TF response:

This would seem to be a mis-reading of the text. 3.1 is about assessing whether or not the process covers the necessary areas BY DESIGN. It is not about carrying out the different aspects. The TF believe we should keep the distinction between design and performance. Thus, **no change is proposed by the TF.** We can make reference, though, to the comments received in the EAN.

#### Q1 – suggestion 3

The suggestion from the Czech Society is:

*"Last point relates also to the section 3.1, where it is said that "... it is envisaged that the scope of his or her work will cover each of the sub-sections within 3.1" We would probably prefer not to envisage any specific scope of the actuary's ORSA related work in the standard but instead say something like "... he or she must, in proportion to the responsibility assigned to him or her, ensure that the ORSA process covers appropriately each of the subsections within 3.1." We believe the sub-sections of section 3.1 are good selection and undertaking having actuary working on ORSA process and obeying ESAP3 should have additional benefit in those areas.*

TF response:

This is a similar point to a concern raised by the FRC. The ED currently envisages that, if an actuary "has material involvement in, or responsibility for, the design of the ORSA process", then their work will encompass all 4 sub-sections of 3.1 – i.e. it will cover all of:

- Establishing a structured approach to uncertainty
- Derivation from Solvency II balance sheet approach and methodology
- The ORSA consideration period
- Inconsistency with the undertaking's risk management approach

and also every bullet in the list in 3.1.1. We took this approach, because we didn't want to have the ESAP applying to every actuary involved in any way with the ORSA work. However, maybe we have gone too far in the other direction. In particular, we do not allow for the situation where an actuary has material involvement in, or responsibility for, PART of the design of the ORSA process – for example, say, the stress and scenario testing to be carried out, and the projections work. In such a case, the 2<sup>nd</sup> ED would require the actuary to “take reasonable steps to ensure that the [whole of – my emphasis] the ORSA process follows an appropriately structured approach to uncertainty” unless the actuary could argue that the ESAP did not apply to their work at all since it was not sufficiently significant for the actuary to be considered to have “material involvement in, or responsibility for, the design of the ORSA process”.

The FRC made a similar point (see below), that the ESAP should only give guidance to actuaries “to the extent relevant to the actuary's involvement and responsibilities” and suggested adding text to this effect in the Purpose section (1.1).

One could perhaps argue that “take reasonable steps” could be interpreted to mean something less onerous with regards to areas outwith the actuary's responsibility, in which case we would not need to amend 3.1 in light of the Czech comments. However, we would prefer a more direct approach to this issue, and so **the TF propose adding new text in 3.1**, based on the preamble text at the start of section 3, as follows:

“Where the actuary has material involvement in, or responsibility for, the design of the ORSA process, it is envisaged that the scope of his or her work will cover each of the sub-sections within 3.1. Where the actuary has material involvement in, or responsibility for, the design of parts of the ORSA process, but not all of it, the actuary should confirm with his or her principal (ideally as early in the process as possible or practical) the extent to which the scope of his or her work includes the topics addressed within the sub-sections within this Section and, in the case of sub-section 3.1.1, which of the areas mentioned in the bullet points fall within the scope of their work.”

The TF also propose, therefore, removing the preamble text to Section 3 (i.e. the text that currently appears before the table of Appropriate Practices).

A third proposal from the TF is to add the words “to the extent relevant to the actuary's involvement and responsibilities” to the bold text in 3.1.1, as follows:

“**The actuary must take reasonable steps, to the extent relevant to his or her involvement and responsibilities, to ensure that the ORSA process follows an appropriately structured approach to uncertainty.**”

The TF wondered whether or not to add the same text to the first sentence after it, as follows:

In considering whether the ORSA process follows an appropriately structured approach to uncertainty, the actuary should take into account, to the extent relevant to his or her involvement and responsibilities, whether it: ...”

but we felt that this would be too much duplication. Thus, we are not proposing this final change.

### **Q3 – suggested new sub-section**

The suggestion from the Czech Society is:

*“We propose to consider insertion of a new article between current articles 3.1.3 and 3.1.4 which would deal with building on existing processes and documentation. Mostly for the reasons given above. We also believe that for example Actuarial Function Report should form critical input for the ORSA process. The article may go along following lines:*

*Building on existing processes and documentation*

*To foster efficient embedding of the risk management and ORSA into business as usual the actuary must consider and utilize existing processes and documentation produced within the undertaking in the areas relevant for his/her part in ORSA process if those are of sufficient quality.*

*In cases where those existing processes and documentation are insufficient the actuary should propose necessary adjustments or extensions.*

*The documentation and processes likely relevant for the ORSA process which should be utilized include but are not confined to:*

- *Actuarial Function Report*
- *Internal audit reports”*

**TF response:**

We think this is going to a level of detail too great for a principles-based standard. The “re-use existing material” point already mentioned has been addressed with the proposed revision to 1.2. **The TF propose not to add the new section suggested.**

#### **Q4 – drafting suggestion 1 of 6**

The suggestion from the Czech Society is:

*“In article 3.1.2 in the first sentence we would suggest limiting actuary’s responsibility just to the areas where he/she is involved as we see that “any aspect of balance sheet” as bit too wide.*

**TF response:**

We disagree that the wording is too wide in this context. What we are asking for here is that, where the actuary has material involvement with, or responsibility for, the choice of measurement bases used for assets and liabilities in the ORSA projections that he or she is aware of how they differ from what is used for S2 solvency reporting. We do not think we should water that down to only parts of the balance sheet. **The TF propose to leave the current ED text unchanged.**

#### **Q4 – drafting suggestion 2 of 6**

The suggestion from the Czech Society is:

*“In article 3.1.3 we would like to specify bit more what is meant by expected and unexpected changes in the economic environment as those things quite often raise misunderstanding about usefulness of considered scenarios. We suggest to extend last two bullets in a following way:*

- *Expected changes in the economic environment, i.e. those which are considered very likely to happen.*
- *Unexpected changes in the economic environment, i.e. those which are considered possible and plausible, but currently not considered likely.”*



TF response:

We felt this was a helpful suggestion. However, we felt that an alternative form of the proposed revision would be better, in order to avoid using words that then needed to be defined. Thus, **the TF propose that we change the two bullets in 3.1.3 as follows:**

**“changes in the economic environment which are considered likely to happen; and**

**changes in the economic environment which are considered possible and plausible, but currently not considered likely.”**

#### **Q4 – drafting suggestion 3 of 6**

The suggestion from the Czech Society is:

*“In article 3.1.4 we agree with the purpose of the article we would however prefer bit more constructive formulation requiring actuary to, besides communicating the situation, make some efforts to remedy the situation or at least to propose how the situation could be rectified. Also this probably links back to the approach to ORSA process discussed in article 1.2 and above. Inconsistency as in article 3.1.4 is more likely to emerge when ORSA is designed as a specific standalone process than when ORSA is built on connecting and extending other running processes in which case the room for inconsistency is largely reduced.”*

TF response:

All the current text in the ED requires is that “Where the actuary has reasonable grounds for believing that there is a material shortcoming in the projections that render the ORSA unsuitable for its purpose, then the actuary must ensure that such shortcoming is appropriately communicated.” This does not preclude what the Czech Society are suggesting. However, we don’t think we should add a requirement to do this, particularly not using the verb “must”, if the actuary’s role profile in the undertaking does not already require that. Thus, **the TF propose to leave the current ED text unchanged.**

#### **Q4 – drafting suggestion 4 of 6**

The suggestion from the Czech Society is:

*“In article 3.2.1 we would suggest to extend the title to explicitly cover also quantitative risk assessment, e.g. “Quantitative risk assessment and financial projections” and change the first sentence to “...to ensure that the risk quantifications and financial projections used ...”. The reason is to make the section 3.2 in certain sense complete as we have there “Financial projections” and “Qualitative risk assessment” which makes quantitative risk assessment to look missing.”*

TF response:

Another helpful suggestion. **The TF propose that the text suggested is added to 3.2.1.**

#### **Q4 – drafting suggestion 5 of 6**

The suggestion from the Czech Society is:



*“We would also stress the role of other calculations used in ORSA not necessarily only projections. We would change the sentence opening the bullet list to “In assessing whether calculations and projections are...”, we would change the first bullet to “... significance of a material risk drivers or risks;” and we would change the last bullet to “... significance of a material risk drivers or risks.”. We would also add one more bullet to the end of the list reading “The projections and calculations uncertainty increases for the periods further in the future.””*

TF response:

We think it is helpful to distinguish between “risk drivers” and “risks” themselves. However, we are less convinced that we need to add the suggested extra bullet point, regarding uncertainty increasing with future time periods. We would have thought such considerations are already covered by what we have written in the ED. Thus, **the TF propose to make the first change suggested to 3.2.1, but not to add the proposed new final bullet.**

#### **Q4 – drafting suggestion 6 of 6**

The suggestion from the Czech Society is:

*“In article 3.2.2 we would suggest to limit the scope for ensuring the appropriateness of the qualitative risk assessments just to the area of actuary’s responsibility. There may be many risks assessed qualitatively many of which might be quite correctly well outside of actuary’s sight. We would change the initial sentence of sub-section 3.2.2 to “... qualitative risk assessments within his area of responsibility used in ORSA process are ...”.*

TF response:

Agreed. This links in with the earlier point that the FRC also raised. **The TF propose to add appropriate text to 3.2.2.**

#### **Response from the Financial Reporting Council**

The FRC answered yes to two of the four goals in Q1, regarding “appropriately principles-based guidance” and “including only guidance that either must be followed or is on a comply or explain basis”. Indeed, they were very complimentary of the ED, saying *“We consider that the changes made to the 2nd ED draft for ESAP3 move significantly towards achieving the goals described above. In particular, we consider that the 2nd ED is appropriately principle based.”* The TF thinks this is “high praise indeed”!

However, the FRC answered no to the first two goals in Q1, regarding “making the scope of the ESAP clear” and “Achieving an appropriate level of balance between core and non-core material for actuarial work”, and made a suggestion in respect of each of these goals.

Under Q2, the FRC again took the opportunity to praise the ED, saying: *“We consider the changes to ESAP 3 to simplify the guidance and remove duplication of the Solvency II requirements are appropriate.”* They also raised two points under Q2 where they suggested small changes to the draft text. They also made one suggestion, under Q3, regarding an additional requirement to add to the ED.

The chair of the TF phoned the Director of Actuarial Policy at the FRC (Ann Muldoon, who was the signatory of their response) and discussed their comments, the outcome of which has influenced the proposals set out below.

### Q1 – suggestion 1 (re scope)

The suggestion from the FRC is:

*“The further clarity provided on the scope is welcomed. However, we feel that actuaries working on key individual components of the ORSA may be unclear whether ESAP 3 applies or not and the extent to which it applies.*

*We suggest that the scope of ESAP 3 could be changed to provide additional clarity and suggest the following “This ESAP provides guidance to actuaries who have an involvement in or responsibility for the design or performance of the ORSA process to the extent relevant to the actuary’s involvement and responsibilities.” “*

TF response:

As noted above, this is similar to a point made by the Czech Society, and is a good one. **The TF propose adding this clarification to the ED text in 1.2, 3.1, 3.1.1, and 3.2.2.**

### Q1 – suggestion 2 (re balance between Core and Non-core actuarial work)

The suggestion from the FRC is:

*“We consider that the ESAP appropriately considers core and non-core actuarial work. However, a key component of the ORSA is bringing together risk and capital management considerations across an insurer’s business, which may require actuaries to engage more extensively with non-actuaries in relation to non-core actuarial work. The different perspectives of different teams can lead to different communication of risks and the risk profile and the actuary is well placed to understand such differences.*

*We suggest that the following is added to paragraph 3.1.4 or as a separate 3.1.5, “Where information provided by the actuary in the ORSA process is inconsistent with or may be interpreted in a different way to information provided by other functions in the ORSA process, the actuary should seek to understand any such differences and ensure any such inconsistency or potentially different interpretation of the assessments provided is communicated and explained clearly.” “*

TF response:

We don’t think we should be adding responsibilities to actuaries which are not already in their role profile. Ann Muldoon accepted that point too.

Also, 3.1.4 already requires the actuary, to ensure that any material inconsistencies are appropriately communicated. Thus, one could argue that the 2<sup>nd</sup> ED as drafted does not stop the actuary doing what the FRC has proposed. Thus, **the TF propose to leave the current ED text unchanged.**

### Q2 – suggestion 1 (re inconsistency with ESAP1)

The suggestion from the FRC is:

*“In paragraph 1.3 we suggest changing the first sentence after the brackets to say: “An actuary may depart from the requirements of this ESAP but still comply with it ...”*

*This wording would be consistent with the similar paragraph in ESAP1.”*

TF response:

The text we have used in the 2<sup>nd</sup> ED is the latest version of the equivalent section from IAA standards. Gabor informed us, on our 7th April call, that it is very likely that ISAP1 will be brought into line with this new form of words when ISAP1 is amended and ISAP1A merged into it. Thus, in the interests of

maintaining consistency with ISAP 1, **the TF propose not to change the current text of 1.3 in the ED, apart from some refinements to 1.3.3 in order to reflect the latest thinking from the IAA.**

## **Q2 – suggestion 2 (re inclusion of regulatory requirements)**

The suggestion from the FRC is:

*“Paragraph 3.1.2 appears to repeat an element of the EIOPA guidelines (Guideline 9) which may lead to inconsistent interpretation between ESAP 3 and the EIOPA guidelines.*

*We suggest that ESAP 3.1.2 is replaced with a high level principle that “The actuary must ensure that information in the ORSA process clearly communicates on what basis risk and capital assessments have been prepared and that, in aggregate, the documented communication is transparent with regard to material differences between different risk and capital assessment bases and the reasons for those differences.” “*

*TF response:*

The proposed text from the FRC has its merits. However, in drafting 3.1.2, we had been very clear that we wanted to imply that the S2 balance sheet was the one to use unless there were good reasons to use something else. This led us to the strong requirement (using “must”) to document any material deviations from S2 balance sheet measurements.

Ann Muldoon accepted this point. Thus, **the TF propose to leave the current ED text unchanged.**

## **Q3 – suggested additional requirement**

The suggestion from the FRC is:

*“We suggest that the last sentence in each of sections 3.2.1 and 3.2.2 is extended to include “...and escalated in line with the undertaking’s risk governance processes”. “*

*TF response:*

At the moment, the 2<sup>nd</sup> ED just requires that “such shortcoming is appropriately communicated”. One could argue that this is consistent with the FRC’s suggestion, and certainly does not preclude it. However, we have been careful not to add responsibilities to actuaries (particularly using the verb “must”). Thus, where escalation in line with the undertaking’s risk governance processes is not within the actuary’s responsibilities within the undertaking, it would not be appropriate for the ESAP to add this as a requirement.

Thus, **the TF propose to leave the current ED text unchanged.**

**David Hare, Chair of ESAP 3 Task Force**

**26 April 2017**

## APPENDIX 1 – Response from the Royal Dutch Actuarial Association

### Comment Template

#### 2<sup>nd</sup> Exposure Draft of ESAP3 – Actuarial practice in relation to the ORSA process under Solvency II

1. Do you think that the 2<sup>nd</sup> ED achieves the following goals?

Goal	YES	NO
Making the scope of the ESAP clear		x
Achieving an appropriate level of balance between core and non-core material for actuarial work	-	-
Appropriately principles-based guidance		x
Including only guidance that either must be followed or is on a comply or explain basis		x

If not then please indicate your concerns:

With respect to scope:

- Our main comment is that the scope is not clear to us. Two roles are mentioned: 1. design and 2. performance. It is not directly clear what is meant by these two roles. Design suggests the setting up and the implementation of the ORSA policy, but the practices use the wording ‘assess’ which indicates a review role. Performance suggests a role in the execution of the ORSA process but also here the wording ‘assess’ is used which again suggests the review role. We have the following recommendations:
  - To make clear which roles the actuary could have in the ORSA process including development, execution, reporting and review and to properly define them. Next, a choice has to be made on the scope of the standard, taking into account that guidance on (parts of) the ORSA process can also be covered or will be covered in other standards, see the next bullet.
  - Many elements of ORSA are or should be integrated in the risk management system of the undertaking. As many elements are part of a wider risk management system these elements could be also part of existing and future standards, such as capital modelling and stress testing and scenario testing. It would be beneficial if this relationship is acknowledged and mentioned in the standard.
- We (still) notice that the general section is formulated in another way than ESAP1 such as the compliance and language section and we don’t understand the reasons for this.
- Section 1.1: The term “material involvement” is rather vague and in our opinion not necessary. This kind of wording is also not used in other standards. Each section in the standard could start with: “When ..” or “When the actuary is involved in ...” Furthermore, it could be considered to add a section on proportionality as done in the IAA standards.
- Section 1.2: We don’t understand the added value of the paragraph on the variety of approaches in section 1.2.

With respect to achieving an appropriate level of balance between core and non-core material for actuarial work scope:

- We don’t fully understand what is meant by this question. If this questions deals with the proper amount of ORSA topics, we believe that several topics are missing depending on the chosen scope of the standard, see also question 3.

With respect to “appropriately principles-based guidance”:

- In general we believe that the standard could be improved by adding more detail so that in practice it is clear what exactly is required. We acknowledge that this comment is closely related to the former comment that the scope of the standard is unclear and that the standard should be extended on several topics, see question 3. We believe that a good example of the proper amount of detail is section 3.1.3 which addresses a specific element of ORSA and contains the sufficient amount of guidance.
- Some specific examples of guidance which are difficult to understand are:
  - Section 3.1.2: it not clear when the actuary should make this consideration.
  - Section 3.1.2: more explanation should be added on deviation from SII balance sheet approach and methodology, e.g. is appropriateness testing of SF and IM SCR involved here.
  - Section 3.1.3: it is not clear what is required by: “The actuary must be in a position to explain and justify the selection of the time period ....” What kind of position?
  - Section 3.1.4: more explanation on what is meant with material inconsistency between ORSA and the risk management approach. In our thinking ORSA should be part of an effective good risk management system. What probably is meant here is that the regulatory ORSA process / reporting deviates from internal risk management practices, but this is also (partly) covered by section 3.1.2.

With respect to “including only guidance that either must be followed or is on a comply or explain basis”:

- This item relates probably to the use of the wordings ‘must’ and ‘should’. The sentences on “reasonable steps” in each section could be removed in our opinion as the reasonable steps are more or less explained in the same section and the sentence therefore only causes confusion on must and should.
2. Is any of the proposed guidance inappropriate for inclusion in ESAP3? If so, please indicate which one(s) and explain why the particular topic(s) should not be included.
- As mentioned before section 3.1.1 is written very general and it is not clear when the actuary has to perform these tasks and what the actuary should do. We recommend to start the standard with a general section such as section 2.1 of ISAP1A which gives an overview of all key elements of the ORSA where it is required that “An actuary which is involved in ORSA should be satisfied that ...”.
3. What other topics should be included in ESAP3? Please indicate which one(s) and explain why you wish guidance in the area(s).
- Depending on the scope chosen we miss guidance on some typical ORSA elements and/or believe that elements should be mentioned more explicitly such as:
    - risk identification
    - documentation of the ORSA including the policy for the ORSA
    - quantification of capital needs
    - appropriateness assessment
    - risk appetite testing
    - ORSA tooling
    - ORSA reporting
    - The role of the key functions, e.g. the link with the CRO assessment but also the independent AFH assessment of the ORSA, taking notice of the input of Internal Audit w.r.t. a review of the ORSA process and the compliance function w.r.t. risks related to consumer conduct.

As mentioned the question if additional guidance should added depends on the scope which should clearer describe the different roles of the actuary in ORSA and the focus of this standard with respect to these roles.

4. Any additional comments

- In general we wonder why this standard is written differently from the other international standards, for example with respect to the preface and the use of the bold text for text involving the verb ‘must’.
- As mentioned before we believe that the standard should be extended on the different roles of the actuary in the ORSA process, the amount of ORSA topics and the level of detail.
- We prefer to use document instead of communication. Communication is in our opinion too general and will not work in practice. As in other standards we prefer to add a separate section on this instead of mentioning this in each section.

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**IMPORTANT:**

Please check if the relevant cells are ticked appropriately and save the file renamed with the name of your association (i.e. ESAP3(ORSA)\_2ndED\_CommentTemplate\_[ name of your association].Doc). E-mail the file as an attachment to [moniques@actuary.eu](mailto:moniques@actuary.eu), with “Comments to the 2<sup>nd</sup> ED of ESAP3 by [name of your association]” in the e-mail subject.

**APPENDIX 2 – Revised ED in light of responses received to formal consultation  
(currently in a separate file)**