



ACTUARIAL ASSOCIATION OF EUROPE

AAE's standard on ORSA – what does it contain and how is it expected to play a role?

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What I promised to cover

David will speak about the development of ESAP3.

He will explain the principles followed in deciding what to include in the standard and what to leave out, and discuss some of the key decisions taken in its development.

David will finish by giving a flavour of the impact it is hoped the standard will have, both for actuaries and for other professionals involved in the ORSA process.

How I am going to do that

- Background on ESAPs:
 - Principal purposes
 - Criteria to be met
 - Current suite of ESAPs
- Application to ESAP 3
- Key aspects of ESAP 3:
 - Scope
 - Breadth
 - Detail
 - Prescription
 - Enforcement
- Hoped for impact of ESAP 3

Background on ESAPs

The AAE's "Purpose for Standards and Criteria to be met" (2011) states that:

- *"The overriding purpose should be to serve the public interest by ensuring that the users of actuarial services benefit from a high quality of actuarial work."*

It goes on to state:

- principal purposes of AAE actuarial standards
- criteria to be met by a proposed standard

and these are helpful in understanding where ESAP3 fits in and why it covers what it does.

Principal purposes for AAE standards

The principal purposes of AAE actuarial standards should be:

- *To enhance the quality of delivery of professional services by actuaries*
- *To help to ensure that the actuarial work product meets the needs to users of actuarial services*
- *To enable actuaries to play an enhanced role in the protection of policyholders and beneficiaries through the quality of the advice given*
- *To contribute towards the development of consistency of actuarial practices across the EU*
- *To provide guidance to actuaries on good practice.*

Criteria to be met by a proposed ESAP

1. *The proposed standard relates to actuarial work which has common characteristics across the EU ...*
2. *There is no conflict or overlap with an IAA standard ...*
3. *The proposed standard does not conflict with legal or regulatory standards or guidelines ...*
4. *The proposed standard would serve as a significant point of reference for the actuarial profession ...*
5. *Key stakeholders are expecting ...*
6. *There is a lack of clarity in the legal provisions or regulatory requirements ...*

Current suite of ESAPs

1. ESAP 1: General Actuarial Practice (2014)
2. ESAP 2: Actuarial Function Report under Solvency II (2016)
3. ESAP 3: Actuarial practice in relation to the ORSA process under SII (2017)

ESAPs are **model** standards of actuarial practice and, as such, are not binding on any actuary.

The AAE encourages its member associations and other actuarial standard-setters to have in place standards of practice that are **substantially consistent** with the ESAPs.

What this meant for ESAP3 Task Force

Our aims for the standard were:

1. To strengthen the confidence of users of actuarial services (in relation to ORSA) that actuaries subject to ESAPs will deliver high quality services
2. To help actuaries in their work
3. To promote the actuarial profession
4. To support a consistent approach to quality actuarial input across Europe

Key challenges for the ESAP3 Task Force

1. Whose work should the standard apply to?
 - particularly in the context of multi-disciplinary teams
2. What aspects of the ORSA should be covered?
 - just ‘core’ actuarial work?
3. How detailed should the standard be?
 - helpful, but not unduly burdensome
4. How prescriptive should the standard be?
 - particularly in the context of ESAP1 vocabulary
5. How enforceable should the standard be?
 - and should it add requirements beyond regulation?

Whose work should the standard apply to?

See section 1.2 (Scope)

- aimed at ‘the top actuary’ (my words, not ESAP3!)
 - “... *actuary has a material involvement in or responsibility for ...*”
- limited to what they are actually accountable for
 - “... *to the extent relevant to the actuary’s involvement and responsibilities*”
- Wider adoption encouraged:
 - amongst supporting actuaries
 - amongst other professionals involved in ORSA-related work

What aspects of the ORSA should be covered?

Key definitions:

- ORSA process
 - *The framework of activities an entity has put in place in order to satisfy the requirements of Art 45*
- ORSA cycle
 - *The entirety of tasks to be performed regularly for the ORSA process*
- ORSA run
 - *Those parts of the ORSA cycle that consist of making the risk assessment, setting the assumptions, running the models and drawing conclusions from the results*

What aspects of the ORSA should be covered?

Design of the ORSA process:

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

Performance of the ORSA process:

- *Quantitative risk assessment and financial projections*
- *Qualitative risk assessment*

How detailed should the standard be?

- Aim was for a principles-based standard
- Educational material and ‘helpful chat’ removed from ED
 - Intended to be presented in a subsequent AAE EAN
- No repetition of relevant regulations etc
- No repetition of ESAP 1 material
 - ESAP 3 focus is on ORSA aspects that are felt to warrant additional requirements or “*guidance*”
- Lists of matters to consider are kept as short as possible
 - Use of “*including*” to signal where list may not be exhaustive
 - Use of the phrase “*must take reasonable steps to ...*” in order to avoid unduly burdensome requirements

How prescriptive should the standard be?

- Purpose of ESAP is to provide “*guidance*” (see 1.1), but not for the purposes of education
- Language is consistent with ESAP 1:
 - “**must**” means that the indicated action is mandatory
 - “**should**” means that, under normal circumstances, the actuary is expected to follow the indicated action, unless ... (i.e. ‘comply or explain’)
 - “**may**” means that the indicated action is not required, nor even necessarily expected, but in certain circumstances is an appropriate activity, possibly among other alternatives (i.e. indicates ways to satisfy “should” or “must” – TF interpretation)

How prescriptive should the standard be?

- ESAP3 “*Appropriate Practices*” use “*must*” and “*should*”
 - “*may*” only used in ‘natural’ sense of uncertainty (e.g. “*how the latter may change over the time period*”)
- Typically, sub-sections follow the pattern of:
 - A “***must***” statement in bold, followed by
 - “*In considering ... the actuary should consider ...*”
- “*Must*” statements are carefully phrased to avoid too great a burden:
 - “*actuary must take reasonable steps to ensure that*”
- Similarly for documentation requirements:
 - “*actuary must be in a position to explain and justify the approach ... if reasonably requested to do so*”

How prescriptive should the standard be?

- In some situations, onward communication requirements are included – as “*must*” statements – for example:
 - “*Where the actuary has reasonable grounds for believing that there is a material shortcoming ... that renders the ORSA unsuitable for its purpose, then the actuary must ensure that such shortcoming is appropriately communicated.*”
 - “*The actuary must take reasonable steps to ensure that any such deviation and its implications are communicated appropriately to those ...*”
- It is hard to see why the actuary should not do that!
- A benefit of using an appropriately-qualified professional.

How enforceable should the standard be?

- Balance to be struck: education v enforceability
- Also, the bigger the burden, the more expensive the actuarial work, so could be counter-productive.
- However, a professional standard that cannot be enforced may lack credibility
- Solution:
 - ESAP 3 requirements are short – only 3 pages
 - Principles-based
 - Careful wording of “*must*” statements
 - “... *take reasonable steps* ...”
 - “... *communicated appropriately* ...”
 - Only go beyond regulations when obviously appropriate

Hoped for impact of ESAP3

- Achieve the aims set by the Task Force:
 1. To strengthen the confidence of users of actuarial services (in relation to ORSA) that actuaries subject to ESAPs will deliver high quality services
 2. To help actuaries in their work
 3. To promote the actuarial profession
 4. To support a consistent approach to quality actuarial input across Europe
- Welcomed by those actuaries whose work is within scope
- Adopted more widely by both actuaries and other professionals
- Enhanced risk management, serving the public interest

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Time for questions ...