actuarial association of europe

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MESSAGES OF THE AAE

ANTICIPATING EU PARLIAMENTARY ELECTION AND THE NEW COMMISSION

The Actuarial Association of Europe[1] (AAE) is committed to safeguarding the competencies and integrity of fully qualified actuaries around Europe with a sound code of conduct, strict education requirements and mandatory standards of practice which apply to the various areas in which actuaries operate.

Actuaries are professionals with expertise in the quantification, mathematical modelling and management of risks, especially those with longer time horizons. Integrity is the foundation of our profession and the AAE fosters the integrity of the profession in Europe through its strict professional code of conduct.

Actuaries are, among other areas, committed to

- aid in reviews of elements of European regulation (especially Solvency II and Institutions for Occupational Retirement Provision (IORP II)) where actuarial input is valuable,
- help in consumer protection issues, including preparation of the Pan-European Pension Product (PEPP),
- aid in building sound social protection systems covering pensions, health and other benefits,
- contribute to the ever increasing need to strive for a more sustainable future, and
- offer their expertise to provide support in Europe as interest rates could undergo the anticipated reversion to a more normal level, and in dealing with the consequences of Brexit. Both of these outcomes will cause difficulties in a number of sectors of the economy.

Reflecting the general trend, for the benefit our societies, toward more defined and extensive governance requirements we encourage regulators to mandate stronger roles for actuaries in insurance, pensions and social security. Actuaries can contribute optimally if they are given the status they need to effectively exercise their capabilities.

EU institutions will benefit from utilising actuarial expertise in the forthcoming regulatory reviews
During the mandate of the new Commission and the new Parliament, the EU will undertake the so-called 2020 review of the Solvency II directive. Actuaries have played a key role over many years in the development of the current directive and its predecessors (mainly the three life/non-life directives), and stand ready to support the latest review.

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[1] The Actuarial Association of Europe (AAE) was established in 1978 under the name Groupe Consultatif to represent actuarial associations in Europe. Its primary purpose is to provide advice and opinions to the various organisations of the European Union - the Commission, the Council of Ministers, the European Parliament, the European Supervisors and their committees – on actuarial issues in European legislation. The AAE currently has 36 member associations in 35 European countries, representing over 25,000 actuaries. Advice and comments provided by the AAE on behalf of the European actuarial profession are totally independent of industry interests.
The Actuarial Association of Europe is registered in the EU Transparency Register under number 550855911144-54

Over this period there will also be developments connected to pensions (IORP II) and social security. It will be essential that the full extent of risks being run in these areas is understood. As a profession, we have strong insights to the risks involved and are well-positioned to create valuation systems that effectively address relevant risks and are consistent with each other.
All of these areas will be advanced in the continuing uncertainty that started with the financial crisis. This uncertainty is most visible in the continuing era of low interest rates. Possible reversion of interest rates to a more normal level will create challenges, at least during the transition phase. Another challenge is Brexit which has the potential to create instability in financial markets and will require new equivalence rules.

The next regulatory season could also see the finalisation of the global International Capital Standard (ICS). Actuaries are deeply involved in the development of the ICS through the global International Actuarial Association (IAA). The AAE is promoting the virtues of Solvency II with a view to ensuring that the ICS will become truly risk based, and that Solvency II will be acknowledged as a valid implementation of the ICS.

Taking care of systemic risks in insurance and pensions will be one of the topics to be addressed during the next Parliament and Commission. Appropriate measures are important, but we see dangers in an over-simplified approach and advise against the unconsidered application of banking rules to other areas. The risks involved should be carefully analysed and tools devised which are effective in insurance, pensions and, where relevant, in social security. Sums of money involved in these areas are huge but the balance sheet dynamics differ from the dynamics of banking, and regulation must reflect these differences.

The ongoing work on the endorsement of the International Financial Reporting Standard 17 (IFRS 17) for insurance contracts is currently very topical. While we believe that this standard will improve the quality of financial reporting, we are concerned at the level of principles and assumptions involved, and the scope for deviation in outcomes. We propose that the actuarial profession (and the regulated actuarial function in Solvency II) should have a designated role in preparing and providing assurance for IFRS17 accounts in Europe.

Actuaries are in a strong position, given their deep understanding of financial economics and the construction of retail financial products, to play a prominent role in consumer protection, especially in creating better tools to analyse costs and returns. This could for instance apply to the creation of better risk factors for the Packaged Retail and Insurance-based Investment Products regulation (PRIIPS). We also think the PEPP is an important initiative and are happy to support its development.
Consumer protection in the financial sector has gained importance, especially following the financial crisis. Financial products are often complicated, and consumers do not have the time or capability to make informed decisions. Regulation tries to address this question by requiring good disclosure, appropriate selling practices and short summaries aimed at making comparisons easy. While the intention is good, the situation is currently not optimal as customers are often flooded with information. Without expert help it is often impossible for the customer to make informed choices. Expert advice is however expensive and not available to most customers.

Two key trends in Europe in the coming years will be the ongoing ageing of populations, and the increasing use in financial services of methods and service models which are based on larger amounts of data and better technologies to make use of this data.

Actuaries have essential tools to support the management of demographic change. Actuaries are well equipped to aid in pricing and management of demographic risks.
With the change in demographics there are challenges not only for our social security systems but also for the ways in which people are served in their financial choices. People preparing for their early retirement years, and later for the need for long term care type solutions, need effective advice and solutions to save and prepare themselves.

Costs associated with savings products and returns available in the context of risks being run must be well understood by those who manufacture and distribute long term financial products aimed at providing saving and protection. These costs can easily erode a substantial part of the returns in some products and must be transparent.

Actuaries who practice in the field of predictive analytics are required by their code of conduct to treat data responsibly in their work. Their actuarial background provides them with a valuable ability to distinguish between causality and correlation
Technological innovation can provide the answer to many of our current challenges, though today there can be excess hype expectations as to what technology can deliver. There is a huge need for analytical skills to ensure that solutions built can be appropriate, financially as well as ethically, when we look at the creation of innovative tools which use artificial intelligence, machine learning, etc. Technological disruption will have many benefits for societies. If used sensibly we will benefit from better services and lower costs. Insurance will play a valuable role in a wider set of fields in providing a facility to pool risks. At the same time there will be new risks resulting from inappropriate use of technology. There will be a need to regulate the use of data, but this needs to be balanced to prevent the suppression of innovation. Generally, practitioners of data science do not today have professional codes of conduct which can provide appropriate boundaries around the use of data and engender trust on the part of wider populations.

The use of novel technologies also creates new risks, i.e. cyber risks. While it is essential to do what is possible to prevent these risks from materialising, there will be a need for insurance cover against damage caused by these risks. This presents new challenges for insurers and for actuaries.

Actuaries support the European agenda of reaching a more sustainable future. We feel we have much to contribute in the area of sustainable finance and we will commit to making a strong contribution in that area. We would also point to the actuarial technique of pooling as an early example of achieving more with limited resources through sharing.
In a world with climate challenges and limited resources, with globally interwoven social problems and sometimes inappropriate governance, sustainable development is becoming more and more important.

Actuaries can play a significant role in increasing the understanding of the potential impact of Environment, Society and Governance (ESG) on insurers and pensions, and facilitating integration of ESG criteria into both asset and liability side considerations in business and/or investment decisions. ESG factors are included in the IORP stress test of 2018, and we encourage including these factors in stress tests of other sectors as well. We are happy to give our input into work in this area.
In the area of climate change we work together with the IAA. Actuaries in Northern America have created a tool called Actuaries' Climate Index and we are trying to find ways to introduce this also to Europe.

We would like to stress that sustainability is needed in many areas. We would like to see intensification of discussions on the sustainability and adequacy of social security pension systems in Member States. Actuaries can contribute, inter alia, to the analysis of inter-generational fairness, intentional and non-intentional transfers between subgroups of insured persons, and assessment of generosity or adequacy of the systems. We encourage Member States to implement a statutory requirement for regular monitoring and actuarial reporting on the finances of their social security systems, as this can be an important factor in ensuring sustainability of social security pension promises.

Actuarial modelling approaches and methodologies should be used to project future cash flows, and assess the short, medium and long-term impact of pension policies and reforms on adequacy and sustainability of pension system provision in an integrated way. This is not being done consistently across the EU at present. International guidelines for reporting on social security should be followed, both for actuarial work in individual Member States and for EU level exercises such as the triennial Ageing Report.

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