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DISCUSSION PAPER

EXPOSURE DRAFT OF

EUROPEAN STANDARD OF ACTUARIAL PRACTICE 3

(ESAP 3)

Actuarial practice in relation to the ORSA process under Solvency II

DRAFT

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Preface

This European Standard of Actuarial Practice (ESAP) is a model for actuarial standard-setting bodies to consider.

The Actuarial Association of Europe (AAE) encourages relevant actuarial standard-setting bodies to maintain a standard or set of standards that is substantially consistent with this ESAP to the extent that the content of this ESAP is appropriate for actuaries in their jurisdiction. This can be achieved in many ways, including:

- adopting this ESAP as a standard with only the modifications in the Drafting Notes;
- customizing this ESAP by revising the text of the ESAP to the extent deemed appropriate by the standard-setting body while ensuring that the resulting standard or set of standards is substantially consistent with this ESAP;
- endorsing this ESAP by declaring that this ESAP is appropriate for use in certain clearly defined circumstances;
- modifying existing standards to obtain substantial consistency with this ESAP; or
- confirming that existing standards are already substantially consistent with this ESAP.

A standard or set of standards that is promulgated by a standard-setting body is considered to be substantially consistent with this ESAP if:

- there are no material gaps in the standard(s) in respect of the principles set out in this ESAP; and
- the standard or set of standards does not contradict this ESAP.

If an actuarial standard-setting body wishes to adopt or endorse this ESAP, it is essential to ensure that existing standards are substantially consistent with ESAP 1 as this ESAP relies upon ESAP 1 in many respects. Likewise, any customization of this ESAP, or modification of existing standards to obtain substantial consistency with this ESAP, should recognize the important fact that this ESAP relies upon ESAP 1 in many respects.

If this ESAP is translated for the purposes of adoption, the adopting body should select three verbs that embody the concepts of "must", "should", and "may", as described in paragraph 1.6. Language of ESAP 1, even if such verbs are not the literal translation of "must", "should", and "may".

This ESAP is binding upon an actuary only if so directed by the actuary's standard-setting body or if the actuary states that some or all of the work has been performed in compliance with this ESAP (e.g., if the actuary is directed by the principal to comply with this ESAP).

This ESAP was adopted by the AAE General Assembly on [day month year].

[Drafting Notes: when an actuarial standard-setting organization adopts this standard it should:

1. *Replace "ESAP" throughout the document with the local standard name, if applicable;*
2. *Modify references to ESAP 1 in paragraphs [] to point to the local standard(s) that are substantially consistent with ESAP 1, rather than referring to ESAP 1 directly, if appropriate;*
3. *Choose the appropriate phrase and date in paragraph* ***Error! Reference source not found.****;*
4. *Review this standard for, and resolve, any conflicts with the local law and code of professional conduct; and*
5. *Delete this preface (including these drafting notes) and the footnote associated with paragraph* ***Error! Reference source not found.****.]*

Introduction

This European Standard of Actuarial Practice (ESAP) provides guidance to actuaries when performing actuarial services in in relation to the processes of the group or undertaking Own Risk and Solvency Assessment (ORSA) as required under the Solvency II framework.

[Other background information]

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Section 1. General

1.1	**Purpose** – This ESAP provides guidance to actuaries when performing actuarial services in relation to the processes of the group or undertaking Own Risk and Solvency Assessment (ORSA) as required under the Solvency II framework to give intended users confidence that • actuarial services are carried out professionally and with due care in compliance with the Solvency II framework; • the results are relevant to their needs, are presented clearly and understandably, and are complete in the context of the Solvency II framework; and • the assumptions and methodology (including, but not limited to, models and modelling techniques) used are disclosed appropriately.
1.2	**Scope –** This ESAP applies to all actuarial services performed by an actuary in relation to the ORSA processes. An actuary who is performing these actuarial services may be acting in one of several capacities such as an employee, management, director, external adviser, auditor, or supervisory authority of the reporting entity. Regardless of the role the actuary has within the group or the undertaking (e.g. a member of the actuarial function, the risk management function, any other key functions or any other roles), the guidance in this ESAP applies to the actuary in so far as the actuary provides actuarial services in relation to the processes of ORSA.
1.3	**Compliance** – [For this ESAP, this paragraph replaces paragraph 1.3. in ESAP 1] An actuary may fail to follow the guidance of this ESAP but still comply with it where the actuary:
1.3.1	Complies with requirements of law that conflict with this ESAP;
1.3.2	Complies with requirements of the actuarial code of professional conduct applicable to the work that conflict with this ESAP; or
1.3.3	Departs from the guidance in this ESAP and provides, in any report, an appropriate statement with respect to the nature, rationale, and effect of any such departure.
1.4	**Relationship to ESAP 1** – Where possible, this ESAP does not repeat guidance already provided in ESAP 1. Any actuary who asserts compliance with this ESAP (as a model standard) must also comply with ESAP 1. References in ESAP 1 to "this ESAP" should be interpreted as applying equally to this ESAP 3, where appropriate.
1.5	**Defined Terms** – This ESAP uses various terms whose specific meanings are defined in Section 2. These terms are highlighted in the text with a dashed underscore and in blue, which is a hyperlink to the definition (e.g. actuary).
1.6	**Cross references** – This ESAP refers to the content of the Solvency II Directive (Directive 2009/138/EC as amended on 23. 05.2014) and the Commission Delegated Regulation (EU) 2015/35 as published in the Official Journal on 17.01.2015 in compliance with the Solvency II Directive. If the Solvency II Directive or the Commission Delegated Regulation is subsequently amended, restated, revoked, or replaced after the dates mentioned above, the actuary should consider the guidance in this ESAP to the extent it remains relevant and appropriate.
1.7	**Effective Date** – This ESAP is effective for {actuarial services performed/actuarial services commenced/actuarial services performed relevant to an event}[1] on or after [Date].

[1] *[Phrase to be selected and date to be inserted by standard-setter adopting or endorsing this ESAP.]*.

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Section 2. Definitions

The terms below are defined for use in this ESAP.
[To be updated]

2.1	**Accepted Actuarial Practice** – A practice or practices that are generally recognized within the actuarial profession as appropriate to use in performing actuarial services within the scope of a ESAP or the applicable professional standards of practice.
2.2	**Actuarial Services** – Services, based upon actuarial considerations, provided to intended users that may include the rendering of advice, recommendations, findings, or opinions.
2.3	**Actuary** – An individual member of one of the member associations of the AAE.
2.4	**Adoption Date** – The date on which this ESAP was adopted as a final document by the General Assembly of the AAE.
2.5	**Communication** – Any statement (including oral statements) issued or made by an actuary with respect to actuarial services.
2.6	**Entity** – The subject, in whole or in part, of the actuarial services, including an enterprise, an insurer, a pensions or benefits plan, a social security scheme, an individual, a government department or agency, a group, etc.
2.7	**AAE** – The Actuarial Association of Europe
2.8	**Intended User** – Any legal or natural person (usually including the principal) whom the actuary intends at the time the actuary performs the actuarial services to use the report.
2.9	**Law** – Applicable acts, statutes, regulations, or any other binding authority (such as accounting standards and any regulatory guidance that is effectively binding).
2.10	**ORSA cycle** – The entirety of tasks to be performed regularly for the ORSA processes.
2.11	**ORSA run** – Those parts of the ORSA cycle that consist of making the risk assessment, setting the assumptions, running the models and draw the consequences of the results.
2.12	**Principal** – The party who engages the provider of actuarial services. The principal will usually be the client or the employer of the actuary.
2.13	**Professional Judgement** – The judgement of the actuary based on actuarial training and experience.
2.14	**Report** – The actuary's communication(s) presenting some or all results of actuarial services to an intended user in any recorded form, including but not limited to paper, word processing or spreadsheet files, e-mail, website, slide presentations or audio or video recordings.
2.15	**Subsequent Event** – An event of which the actuary becomes aware after the valuation date (or date to which the actuarial services refer) but before the actuary's communication on the results of these actuarial services is delivered.
2.16	**Work** – All actuarial activities performed by an actuary related to actuarial services. It usually includes acquisition of knowledge of the circumstances of the assignment, obtaining sufficient and reliable data, selection of assumptions and methodology, calculations and examination of the reasonableness of their result, use of other persons' work, formulation of opinion and advice, documentation, reporting and all other communication.

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Section 3. Appropriate Practices

3.1	**Considerations in relation to the ORSA processes**

3.1.1	Establishing a structured and documented approach to uncertainty
	
	The actuary should bear in mind that the ORSA processes should form recurring tasks, to be done at least in an annual cycle, that need a structured and documented approach to uncertainty consistent with the business planning which:
	• enables the understanding and management of the areas of uncertainties[2] ("risks") and the evolving exposures[3] to those risks to be maintained and increased;
	• facilitates identification of all material risks to be covered by ORSA, to which the underlying group or entity is or will be exposed, considering the nature and level of risk, and thereby classifying risks to be quantified using models or treated using qualitative methods;
	• enables new areas of uncertainty to be incorporated as they are identified, even if they are not material but potentially growing (emerging risks);
	• is consistent with the fact that this is not a linear process: new information or understanding in one area may aide another, and this transfer should be carried through.
	• enables the evolving nature of the interactions of the risks and exposures to be understood;
	• enables the changes to the understanding of risk, or the approach thereto, to be incorporated;
	• ensures that the assumption setting process considers potential future management actions appropriately;
	• ensures that back-testing of past assumptions versus experience is properly carried out and the consequences are properly incorporated into assumptions for the future;
	• is a dynamic, integral part of the ORSA and the ERM framework:
	  ○ Changes to the understanding of risk, or the approach thereto, should be incorporated into the ORSA/ERM framework. If not incorporated, the reasons should be documented.
	  ○ Changes in the ORSA/ERM framework may require changes to the approach to uncertainty
	• facilitates the effective maintenance and transfer of the knowledge of risks, exposures and the ORSA process to other interested parties (e.g. an actuary working in a similar role, reviewers, auditors, regulators, other risk management professionals, business managers, the board of directors, etc.)

3.1.2	Considerations for consistency with or deviation from Solvency II requirements The actuary should consider • to what extent the ORSA processes are consistent with, or deviate from, the principles and the rules of Solvency II and the consequences of any deviations;

Comment [HG1]: This formulation takes into account that the actuary may not be responsible for the overall structure of the ORSA; nevertheless the actuary should bear in mind that these are requirements against the ORSA process

Comment [HG2]: Into the EAN

Comment [HG3]: Into the EAN

Comment [HG4]: Into the EAN

[2] Uncertainties: things which happen in the larger world (e.g. movements in the equity markets, lapses, policyholder behaviour, etc) which we commonly refer to as "risks".
[3] Exposures: the nature and extent to which an entity is exposed to areas of uncertainty (e.g. increases in reserves, gains and losses, liquidity events, reputation, etc).

	• the extent to which the ORSA supports the intended business uses, the limitations, and the differences from the Solvency II Internal Model / Standard Formula which should be understood and communicated to the stakeholders.

3.1.3	Considerations for the business planning period and the interactions among risk, capital, and value
	
	Relative to the business planning period taken into account within the ORSA, the actuary should consider:
	• that the risk profile can be expected to evolve for a number of reasons, including
	  ○ the run-off of the existing business;
	  ○ the run-off of the new business acquired in the future;
	  ○ expected changes in the environment; and
	  ○ unexpected changes in the environment.
	• the appropriateness of the business planning period in relation to the business itself, and in forming a basis by which the ORSA supports business processes, with special attention to considering if the business planning period is sufficiently long to capture all implications of the current and evolving risk profile;
	• the interaction of risk, capital and value over the business planning period, with proper attention to shorter term requirements and longer term run-off of the businesses;
	• expected and stressed effects of the business plan on various stakeholders over the business planning period with proper attention to shorter term requirements and longer term run-off of the businesses.

3.1.4	Involvement of the business in the ORSA processes The actuary should work with business units to identify, understand, quantify or qualify, monitor, manage and report on all the identified areas of uncertainty as well as the exposures in order that these can be properly considered in the ORSA.
3.1.5	Risk management and the ORSA The actuary should • understand the extent to which the risk management strategy and the day-to-day risk management practices are reflected in the ORSA; • understand the extent to which any current risk management actions may be contraindicated or inefficient relative to the assumptions of ORSA or its output; • understand the extent to which the Enterprise Risk Management (ERM) framework is incorporated, supported, and consistent with the ORSA or its outputs; • ensure that the ORSA process is reviewed regularly for appropriateness; • use, develop and document the undertaking's "common sense" as it relates to risk management.

Comment [HG5]: Into the EAN

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3.1.6	Events triggering an ORSA run In addition to Business as Usual (BAU), an ORSA run is required when an ORSA-triggering event occurs. An ORSA-triggering event is a material change in the nature of the uncertainties or exposure thereto, or in the understanding of those uncertainties or exposures. For example, a material change in: • the nature of one or more areas of uncertainty • the nature of the company's exposure to one or more areas of uncertainty • the nature of the company's aggregate exposure, whether or not the areas of uncertainty and/or the individual exposures have changed • the understanding of the areas of uncertainty, or the individual or aggregate exposures • events which may change the aggregate exposure, or the acceptable levels thereof, include changes to: the risk appetite, risk limits, risk tolerance, ERM/RM strategy, business plan, nature of the business (M&A…), etc. The actuary should consider whether the processes are appropriate to identify the occurrence of an ORSA-triggering event. Considering a potential ORSA-triggering event, the actuary should determine whether the change is material.
3.1.7	Effectiveness of the model(s) supporting the ORSA methodology as a risk management tool In considering the effectiveness of the model(s) supporting the ORSA as a risk management tool, the actuary should consider: • whether the ORSA provides useful information to decision making; • the extent to which the ORSA supports the ERM framework; Material risks difficult, impossible or not worth quantifying should be incorporated into the ORSA using qualitative methods regardless of: • whether reliable probabilities (PF or PDF) can be assigned to various outcomes, • whether the whole range of outcomes can be understood, or • the extent to which the company's exposures can be accurately measured. The inclusion of such risks and exposures should not introduce spurious accuracy into the ORSA. When risks could be captured quantitatively but are captured only qualitatively, then a proper explanation should be given and documented.
3.2	**Considerations in relation to the model(s) supporting the ORSA methodology**
3.2.1	ORSA methodology and structure — connections with Solvency Capital Requirement (SCR) methodology At the beginning of the process the actuary should consider the ORSA methodology and structure. In the case of the former, the actuary should consider how the ORSA time horizon and risk measure is consistent with that used in the SCR to ensure multi-year projections are coherent. There should be a coherent link between the ORSA, the strategy of the entity, as reflected in the business planning, and the decision-making framework.

Comment [HG6]: Into the EAN

Comment [HG7]: Into the EAN

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	The methodology should also consider the significance of the risks being modelled, the extent to which the risks may be modelled reliably, and the level of proportionality that could be applied to modelling these risks. The methods applied should allow an assessment of the compliance, on a continuous basis, with the capital requirements along the entire time horizon.
3.2.2	Risk coverage considerations for the model(s) supporting the ORSA methodology The actuary should consider that there may be risks that although can be captured quantitatively are better managed using qualitative methods only. In identifying and quantifying (to the extent possible) the risks in the ORSA, the actuary should consider the risk appetite and the full risk profile of the business throughout the entire time horizon. The actuary should also consider to what extent these are covered within the Solvency II balance sheet and the SCR. All risks to which the underlying group or the entity has material exposures should be considered to be covered by the ORSA. The actuary should consider the nature and level of uncertainty associated with the risk itself as well as the extent of exposure (e.g. the extent of potential losses due to changes in this risk). The actuary should consider whether to include the risk within the ORSA models. This should be an on-going process as the actuary's understanding of the risk changes and the nature of the (re)insurer's exposure to that risk changes. Reasons for exclusion should be documented. With regard to risk measurement and proportionality: • the actuary should quantify risks to the extent possible, taking account of the precision required for the intended purposes. • where the required precision has not been attained, risks should be handled qualitatively. The qualitative measurement thereof should consider the nature of the remaining uncertainty as well as the need for precision (proportionality).
3.2.3	Combining quantitative and qualitative risks coherently The actuary should determine which risks can and should be quantified (e.g. through percentiles, loss distributions) and which cannot easily or should not be quantified. In the case of the latter, the actuary should be aware of the qualitative tools to identify, describe and report those risks and should consider whether it would be appropriate to carry out separate scenario tests to demonstrate the effect of particular scenarios on the group or entity. The actuary should ensure that these scenarios are coherent and can allow for management actions. [E.g. effect of downgrade could lead to increase in surrenders, lower new business (or closure)]. These scenario tests should determine which scenarios the entity can survive and which it cannot. Professional judgment should be used when incorporating qualitative risks into the ORSA or the models supporting the ORSA. It may be inappropriate to utilise continuous probability distributions for qualitative risks. Qualitative risks should be incorporated as appropriate. In some cases, it may be most appropriate to assign discrete probabilities to representative risk events. In other cases, it may not appropriate to assign probabilities. Consideration should be given to the ultimate use or users of aggregated risk information and how the inclusion of qualitative risks may affect this.
3.2.4	Considerations for stress-testing, reverse stress-testing, and scenario-testing Testing groups of assumptions which are assumed to change in a related way is sometimes described as "scenario testing", whereas varying individual assumptions independently is typically

Comment [c8]: there ay be some overlap on the quantitative/qualitative issue with 3.1.7 and 3.2.3

Comment [HG9R8]: True enough. To be reviewed later how this aspect can be captured in the best way

Comment [HG10]: The S2 texts phrase it as 'scale, nature and complexity". I do not know what "complexity" adds to "nature", so I would use nature and scale", or as Sam put it, "nature and level"; I am uncertain about what the "exposure" adds to this. What we mean by "nature and level" could be better explained in the EAN.

Comment [HG11]: Into the EAN

Comment [HG12]: Into the EAN

Comment [HG13]: Into the EAN

Comment [HG14]: Into the EAN

referred to as "sensitivity testing". Stochastic modelling will normally incorporate the scenario concept by assuming specific statistical relationships between variables, such as inflation and investment returns.

The projections, or point-in-time stresses, should include a base scenario and several plausible adverse scenarios. Each scenario should take into account not only in-force policies but also the policies assumed to be sold during the projection period (where applicable).

The base scenario should reflect a realistic set of assumptions used to forecast the expected financial position over the projection period. However, the actuary should be cognisant that the past relationships between assumptions may be different from those applicable in the future. A plausible adverse scenario is a set of adverse, but plausible, assumptions about matters to which the Company's financial condition is sensitive. Plausible adverse scenarios will vary between companies and may vary over time for a particular company.

Plausible adverse scenarios should normally include plausible combinations of adverse developments in multiple factors as well as adverse developments in individual factors. In constructing or reviewing plausible adverse scenarios, the actuary should normally consider the potential impact of shareholder, policyholder, cedant and broker behaviour (if applicable) in adverse conditions.

Certain assumptions, in particular those which are a consequence of the economic environment, are best treated as a group. The Company's ability to withstand a period of inflation or recession, rising or falling stock markets, increasing market sizes or increasing competitiveness, should normally be investigated using coherent sets of assumptions. Where non-economic assumptions are expected to react in a certain manner to changes in the economic environment, these changes should be incorporated into the combined scenario.

In determining the stresses and scenarios to be considered, the actuary should consider the exposures of the particular business to risk concentrations (e.g. assets, lines of business, distribution channels, geographical). Where there is a significant risk concentration, the actuary may wish to carry out additional research into this area when determining the appropriate stresses and scenarios.

Where there is a significant risk exposure, the actuary should also consider stresses and scenarios that may be considered more extreme in the current environment or that have not occurred in the recent past.

In determining the stresses and scenarios to be considered, the actuary should be aware that

- risk measures exhibit non-linear behaviour, especially when various individual risks are aggregated; and
- the value-at-risk measure required for calculating the SCR is not sub-additive.

Where there is potential non-linearity in outcomes, the actuary should consider what stresses and scenarios trigger severe losses (cliff-edge effects). For instance, this may apply to options that are "out of the money" or successive events which could lead to significant losses (e.g. change in mortality basis followed by changes in interest rates for annuities).

For the appraisal of some risks, the projections can be on a deterministic basis. However, the actuary should consider, depending on the circumstances and nature of the risk profile, whether stochastic techniques should be used to identify additional risks. Stochastic techniques may also be valuable in comparing the relative level of probability of adverse circumstances occurring.

The actuary should be wary of potential biases in choosing and reviewing stresses and scenarios. That is, the actuary should not necessarily restrict stresses and scenarios to those that:

- do not exhaust available capital;

Comment [d15]: Into the EAN

Comment [HG16]: Into the EAN

Comment [HG17]: Into the EAN

Comment [HG18]: Into the EAN

Comment [SDA19]: We could generalise this as…

With respect to the risk exposures (i.e. losses), the Actuary should be aware of exposures with intrinsic optionality, guarantees, or other non-linear behaviour. The Actuary should understand the nature of single, combined or multi-period risk events which lead to a change in the nature of the exposure (i.e. cause options to bite, move into a region of non-linear losses, etc).

Comment [HG20]: Into the EAN

	• are "linear" (ignoring events such as changes to the shape of the yield curve or the mortality curve); • repeat recent events (i.e. within the last generation); and • relate to current investment and economic issues. However, the scenarios should remain plausible. The actuary should consider the merits of performing reverse stress-testing to identify various combinations of risks that may lead to the failure of the business, whether that failure is defined as insolvency, loss of a certain credit rating, parental difficulties or other outcome. These reverse stress tests may be more extreme than plausible scenarios. In testing variations in the outcomes above, the actuary should allow for plausible management actions. A guide to the plausible management actions can be taken from the criteria covered in the Commission Delegated Regulation. This list is not exhaustive, and the actuary should consider other risks which are likely to materially impact on the group's or Company's financial stability or have done so in the past. The actuary should pay heed to stress and scenario tests issued by insurance and/or banking supervisors and other relevant bodies.
3.2.5	Time horizons: business planning period and risk-specific timeframes Normally, the base scenario should be consistent with the Business Plan, unless those assumptions are so inconsistent or unrealistic that the resulting ORSA report would be misleading. Where the ORSA is not consistent with the Business Plan, it is good practice to disclose this and outline potential implications. (although it is obvious…) Risks with distinct measurement periods should be brought onto a consistent measurement period, where possible. The risk measurement period should be incorporated into the ORSA coherently (e.g. via a multi-year projection using 1-year risk distributions)

3.2.6	Special issues specific to group ORSA
	For the group ORSA, the actuary should ensure that:
	• the scenarios are consistent across the group;
	• there is proper allowance for fungibility constraints/tax issues;
	• specific risks within subsidiaries and branches (but are not group wide) are covered;
	• risks in business units which are
	  ○ non-regulated;
	  ○ regulated outside the Solvency II scope but in jurisdictions deemed equivalent to Solvency II; or
	  ○ regulated outside the Solvency II scope, in jurisdictions not deemed equivalent to Solvency II
	are covered properly;
	• allowance is made for implied guarantees on subsidiary capital.

Comment [HG21]: Into the EAN

Comment [HG22]: Into the EAN

Comment [HG23]: Into the EAN

Comment [c24]: Separate section perhaps on issues relating to group ORSA?

Comment [HG25R24]: This suggestion will be considered later

Comment [HG26]: David: Should we restrict this to insurance subsidiaries? Otherwise, will actuaries be competent to give opinions on trading subs that may have nothing to do with insurance – or a bank sub, say?

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3.2.7	Understanding and documenting the key similarities and differences between the real world and the modelled world from an ORSA point of view (i.e. the world implicitly assumed within the model(s) supporting the ORSA) The actuary should demonstrate an understanding of (and document) the key similarities and differences between the real world and ORSA model. In considering this the actuary may wish to consider: • the appropriateness of the risk measures used; • the appropriateness of the risk modelling, especially where the modelled risk may differ in nature from its counterpart in the real world, and what this means for the ORSA; • the stresses and scenarios used and the appropriateness of the results; • management actions assumed as mitigating factors, their associated time delay and any track record of their effectiveness; • the appropriateness of the model to the risks of the Company; • the risks not covered by the model; • the reasonableness and robustness of the business assumptions underlying the base scenario used for the projections; and • whether there are any concerns over the appropriateness, completeness and accuracy of the data used and document the reasons of use professional judgement.
3.3	**Considerations in relation to "Business as Usual" (using ORSA)**
3.3.1	Entity interactions with business processes and business units The actuary should bear in mind that • the risk owners in different business units should be included in the risk profile assessment considering the risk appetite, risk tolerances and limits, and the organizational structures of the business units; • materiality in a business unit from the group perspective may not be the same as from the perspective of the business unit locally; • it is necessary to consider, where applicable, whether risks in relation to the undertaking and its major branches should be first assessed individually and then aggregated or they should be assessed as one unit; • the AMSB should take an active part in the ORSA process by steering how the assessment is to be performed and challenging its results; • the implementation of ORSA should be consistent with the Business Plan used by the group or undertaking and the Business Plan should consider the risk appetite, the expected and stressed risk profile and the cost of capital generated as elements for the strategy definition process.
3.3.2	The ORSA run: set-up, reproducibility, and documentation The actuary should bear in mind that • the ORSA run should be achieved within a periodic, annual or more frequent, ORSA cycle or upon an ORSA-triggering event. This triggering event should be defined and regularly monitored.

Comment [HG27]: It may be fully covered by ESAP1

Comment [HG28]: It may be fully covered by ESAP1

Comment [HG29]: Into the EAN

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- the group or undertaking should have in place at least the following documentation on the ORSA:
  - ORSA policy;
  - record of each ORSA cycle in such detail that, together with the ORSA policy, the material methods, assumptions and results are captured;
  - the ORSA report, or reports if there is a difference between the internal report and the supervisory report, suitable for decision making and follow-up;
  - the ORSA report should include at least the following:
    - identification of the risk profile;
    - assessment of the overall solvency needs and stress test for principal risks in a forward-looking perspective in light of the risk appetite;
    - reconciliation of the overall solvency needs with the regulatory capital requirements, if relevant;
    - compliance, on a continuous basis, with the capital requirements;
    - deviations from assumptions underlying the SCR, if relevant;
    - analysis of deviations between old evaluations on the same year;
    - the reasons of professional judgements use.

3.4 Considerations in relation to Governance

3.4.1 Processes for design, use and monitoring

In applying the ESAP 1 paragraph [x.x Model Governance], the actuary should consider the following items when designing, using/applying and monitoring ORSA processes

- the ORSA processes need to be aligned with the business planning processes including the consistency of the risk profiles considered;
- the need to have appropriate processes to identify and monitor changes in the risk profile;
- the need to have triggers for detecting significant change in the risk profile of the undertaking or group that requires a recalculation of the SCR;
- scenarios developed, applied and updated need to be appropriately adverse but realistic;
- the need for the ORSA processes to yield itself to verification/review/audit;
- the need for processes that allow for regular updates to the ORSA;
- the need to develop and maintain an ORSA policy;
- all information required by law and by the ORSA policy are dealt with proportionately and appropriately in both the internal and the external ORSA reports.

If material, the actuary should be able to distinguish between the materiality of the outcome as reflected through the ORSA process and, if distinct, the materiality in the real world (i.e. that which is and is not captured within the ORSA process or models supporting the ORSA). Where the materiality within the ORSA process and the materiality in the real world are materially different, the difference should be understood and documented.

3.4.2 Communication and consultation with stakeholders

In applying the ESAP 1 section 4 Communication, the actuary should bear in mind that

Comment [HG30]: To be developed as the IAA develops its extension of ISAP 1

Comment [HG31]: This is not specific to ORSA; refers to all models that capture the real world in an incomplete way

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	• the ORSA process consists of a cycle of sub-processes and should be designed in a way requiring data and opinion from all relevant units of the undertaking or group; • ORSA is intended to help decision-making by the AMSB and/or senior management in the first place and therefore the main intended users of the work will be the AMSB and/or the senior management of the undertaking or group; • the external ORSA report shall be shared with the respective supervisory authority for information purposes; • parts of the internal ORSA report may be shared with the staff of the undertaking in order to generate feedback and raise risk awareness.
3.4.3	Review and update of appropriateness of methodologies, model structures and model output, including risk coverage of the model(s) supporting the ORSA methodology and emerging risks In reviewing and updating the appropriateness of the ORSA processes, including • the ORSA policy; • the applied methodologies; • model structures; • data used; • assumptions made, including any management actions; • scenarios designed; • model output and reports; • any other shortcomings the actuary should seek feedback from all relevant units of the undertaking or group focusing on the input from the AMSB and/or senior management.
3.4.4	Review and update of users and uses of the ORSA output and the suitability thereof considering the difference between real world and modelled world Throughout the ORSA cycles, the actuary should consider: • the previous ORSA and real world developments; • feedback from users of the ORSA, especially if recommendations approved earlier have been implemented properly; • to what extent the results of the ORSA have been used in decision-making; • the implications of the changes in relevant factors affecting the users and uses of the ORSA output, such as consequences of the changes in the organization, responsibilities, management information systems and risk appetite; • the tolerances and limits versus the risk profile of the undertaking or group, overall and in the relevant segments.

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