

Exposure Draft

**Establishment of Enterprise Risk Management
(ERM) Practice-Specific Standards**

Actuarial Standards Board

July 2022

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MEMORANDUM

To: All Fellows, Affiliates, Associates and Correspondents of the Canadian Institute of Actuaries, and other interested parties

From: Edward Gibson, Chair and Josephine Marks, Immediate Past Chair
Actuarial Standards Board

Mario Robitaille, Chair
Designated Group

Date: July 14, 2022

Subject: **Exposure Draft for Standards of Practice – Establishment of Enterprise Risk Management (ERM) Practice-Specific Standards**

Comments Deadline: **September 30, 2022**

Introduction

The exposure draft (ED) for Standards of Practice – Establishment of Enterprise Risk Management Practice-Specific Standards was approved for distribution by the Actuarial Standards Board (ASB) on June 8, 2022.

Background

The ASB created a designated group (DG) responsible for developing these revisions to the Standards of Practice (SOP). The DG consists of Michel Dionne, Sharon Giffen, Bruce Langstroth, Étienne Massicotte, Altaf Rahim, Jean-Yves Rioux, Mario Robitaille (Chair), Sheldon Selby, and Lisa Zwicker.

A [notice of intent](#) to incorporate principles of International Standard of Actuarial Practice 6 – ISAP 6 – Enterprise Risk Management Programs and IAIS Insurance Core Principles into the Canadian SOP was issued on September 25, 2020.

Two groups (Enterprise Risk Management Practice Committee and Committee on Risk Management and Capital Requirements) and one individual have provided feedback.

A highlight of the feedback received for each of the four questions for which members were invited to comment is presented hereunder.

Question 1. Should the ASB include guidance related to ERM within the Canadian SOP?

The comments received unanimously mentioned that guidance related to ERM should be included in the Canadian SOP. Among the arguments cited in favour of its inclusion are:

- (1) The point of evolution of ERM at which we are.

- (2) The fact that ERM is closely related to other responsibilities of actuaries such as financial condition testing and ORSA.

Question 2. Do you agree that the SOP should cover practice areas beyond the ISAP 6 main focus area of insurance?

The comments received did not mention any objection to having a standard that would not be insurance specific.

Question 3. Are there situations where ISAP 6 may not be appropriate and modifications may be needed?

One comment pertains to the fact that the SOP should maintain the notion of proportionality in respect of nature, scale, and complexity and allow for judgment by the actuary as to the degree that the various sections and subsections would apply in the circumstances.

It was also noted that certain parts of ISAP 6 read in a manner akin to an educational note instead of a SOP. For example, this list of factors to be considered (but not limited to) in sections 2.3, 2.4, and 2.5.

Also, it was mentioned that ERM SOP could expand on some specific aspects, such as:

- ISAP 6 may be perceived as restrictive. It appears to focus on solvency aspects while it could also address the other sides of ERM, such as risk management from solvency vs. going-concern view, identification of opportunities within risk appetite, risk optimization, and management of strategic risk.
- ISAP 6 offers plenty of considerations about current risks but outlines little guidance specific to emerging risks.

Question 4. Would the introduction of an ERM SOP put the actuarial profession at a disadvantage compared to practitioners that are not actuaries?

The comments received support the view that expectations of the ISAP 6 are aligned with existing expectations regarding risk management and promote general principles of ERM.

One comment mentions that actuaries will benefit from a clarification of the language, and adoption of this standard will position the actuary well in the market. In addition, the SOP would provide the necessary framework (or anchor) for developing more guidance material to promote leading practices and to promote actuaries in ERM roles in the insurance industry as well as other areas.

The adoption of an ERM SOP is also seen as an opportunity to improve the position of actuaries in ERM roles, especially given other risk professionals do not benefit from similar SOP.

Comments on the ED

The ASB is soliciting comments on the ED from members of the CIA and other stakeholders **by September 30, 2022**. Please send them to Mario Robitaille at

Mario.c.Robitaille@desjardins.com, with a copy to Chris Fievoli at Chris.Fievoli@cia-ica.ca.

Feedback is specifically requested on whether any practical difficulties are foreseen in complying with the proposed changes.

No specific forums for expressing comments, other than through submission of written comments, are planned regarding this ED.

Due Process

The ASB's *Policy on Due Process for the Adoption of Standards of Practice* was followed in the development of the ED.

Timeline and Effective Date

It is the responsibility of the ASB to make final decisions regarding the revised standards of practice. The ASB plans to adopt final standards by the end of 2022, to be effective no later than June 30, 2023. Early adoption will likely be permitted.

EG, JM, MR

8000 – Enterprise Risk Management

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8100 Scope

- .01 Part 1000 applies to work within the scope of this Part 8000.
- .02 The standards in Part 8000 apply to an actuary with responsibility for, or significant involvement in, the development, implementation, maintenance, or review of some or all of the components of enterprise risk management programs.
- .03 The standards apply only to the extent of the actuary's responsibility and involvement.
- .04 The purpose of Part 8000 is to increase users' confidence that:
- Actuarial work is carried out professionally and with due care;
 - The results are relevant to users' needs, are presented clearly and understandably, and are complete; and
 - The assumptions and methodology used are disclosed appropriately.

8200 General**8210 Circumstances affecting the work**

- .01 When performing actuarial services in connection with enterprise risk management, the actuary should apply the requirements of this Section 8200. [Effective Month XX, 202X]
- .02 The actuary would have, or obtain, sufficient understanding of the risk management system and enterprise risk management framework of the entity.
- .03 The actuary would consider whether the risk management elements required by regulations are in place, such as:
- a. risk management policies;
 - b. risk tolerance statements;
 - c. a capital assessment such as the Own Risk and Solvency Assessment (ORSA); and
 - d. the entity's assessment of its regulatory capital requirements.
- .04 The actuary would consider proportionality in respect of the nature, scale, and complexity of the operations and risk profile of the entity.

8220 Identification, assessment, and management of risks

Identifying risks

- .01 When identifying risks, the actuary would consider factors including, but not limited to, the following:
- The strategic objectives of the entity;
 - The processes for collecting information and whether the staff have adequate qualifications, training, and experience to understand and identify the risks;
 - Whether the risk identification process is sufficient to identify current and emerging risks that are reasonably foreseeable, relevant, and material including risks that directly or indirectly impact the financial condition and other objectives of the entity (e.g., reputational risk);
 - The time frame over which the risks may emerge and may impact the entity;
 - The risks that may arise from reasonably foreseeable changes in the business of the entity (operations, markets, products) and from business conduct;
 - Whether underlying risks within financial structures that have limited transparency have been sufficiently identified (e.g., off-balance sheet exposures, complex asset or risk transfer structures);
 - Whether the reasonably foreseeable causes of risks and their consequences have been sufficiently identified;
 - Risks arising or increasing as a consequence of risk management activities (e.g., credit risk arising from the transfer of risk);
 - The impact that an entity's culture, governance structure and remuneration systems may have on the ability and willingness of the management and staff to identify and manage risks, and whether culture, governance structure, or remuneration generates, magnifies, or mitigates risks; and
 - Input regarding the identification of risks from management, other knowledgeable persons within the entity, other subject matter experts, and regulators.

Assessing the probability and impact of the entity's risks

- .02 When assessing the probability and impact of the entity's risks, the actuary would consider factors including, but not limited to, the following:
- The qualitative assessment of risks in addition to, or instead of, assessing them quantitatively;
 - Risk correlations, risk aggregations and tail risks (e.g., catastrophe and pandemic risks, and complex outsourcing risks);
 - The appropriateness of the risk modelling, stress testing, reverse stress testing, and scenario testing techniques that are applied;
 - The extent to which the risk models that measure the probability and impact of risks provide results that are consistent with information expressed by market prices, where applicable, for the risks concerned or related risks;
 - The consistency among the various valuation methodologies underlying the enterprise risk management program;
 - The operation and effectiveness of the processes and mechanisms used to address risk control and risk mitigation;
 - The appropriateness of the assumptions regarding future actions taken by management and by external parties, taking into account prior experiences in the industry with similar actions;
 - Input regarding probability and impact from management, other knowledgeable persons within the entity, other subject matter experts, and regulators; and
 - Consistency of risk assessments over time.

Risk management controls, mitigation, monitoring, and reporting of the entity's risks

.03 When implementing or maintaining risk management controls, mitigation, monitoring, or communication and reporting of the entity's risks, the actuary would consider factors including, but not limited to, the following:

- The entity's risk management policies and risk appetite and tolerance statements;
- The relationship between the entity's financial strength and risk profile, and the entity's risk management system;
- Any significant inconsistency in the evaluation of the entity's risk tolerances and risk limits;
- The extent to which the results of the risk models used to measure the economic costs and benefits of risk mitigation are consistent with information expressed by market prices, where applicable, for the risks concerned or related risks;
- The operation and effectiveness of the processes and mechanisms used to address risk control and risk mitigation;
- The appropriateness of the assumptions regarding future actions taken by management and by external parties, taking into account prior experiences in the industry with similar actions;
- The culture within the entity to commit to, and implement, risk mitigation actions when needed;
- The impact of reasonably foreseeable future adverse circumstances on the availability and effectiveness of future risk mitigation practices;
- The existence and effectiveness of feedback loops in the risk management process; and
- How the nature and relative importance of risks may change over time.

8230 Enterprise level risk management

Aggregate risk assessment of the entity

- .01 When performing an aggregate risk assessment of the entity, the actuary would, in addition to assessing the elements as addressed in subsection 8220, consider factors including, but not limited to, the following:
- The financial strength, risk profile, business management, governance structure, and risk environment of the entity;
 - Whether the risk management processes are suitably aligned with the entity's objectives and strategy, regarding aggregate risk taking and regarding each major risk category, as reflected by the risk appetite, risk tolerance and risk limits;
 - The interdependence of risks relating to the entity's assets and liabilities, noting that correlation of risks between different asset classes, products, and business lines may not be linear, and may change under stressed conditions;
 - Off-balance sheet exposures that may revert to the entity in times of difficulty; and
 - Diversification benefits that result from aggregation of risks.

Developing, implementing, maintaining, or reviewing the enterprise risk management framework

.02 When developing, implementing, maintaining, or reviewing the entity's enterprise risk management framework, the actuary would, in addition to assessing the elements as addressed in paragraph 8230.01, consider factors including, but not limited to, the following:

- The engagement of the board in assessing, setting, monitoring, and reviewing the entity's risk appetite and risk profile, and whether the interests of its clients and other relevant stakeholders are considered appropriately within those processes;
- The adequacy of the risk management resources and capabilities within the entity for the current and expected risk profile and risk management strategies;
- The quality, extent, and effectiveness of independence, challenge and monitoring reflected in the framework;
- The extent and results of recent reviews and audits of control effectiveness, and management's response to the findings;
- The management of potential conflicts of interest;
- The extent to which risk management and risk assessments are used in the decision-making practices of the entity;
- The effectiveness of risk communication channels within the entity, including risk escalation processes, and with its regulators;
- The effectiveness and timeliness of the reporting of, and response to, incidences and breaches related to the operation of the enterprise risk management framework within the entity;
- The operational quality and effectiveness of key enterprise risk management framework related policies, processes, and mechanisms, including, but not limited to, outsourcing management, business continuity management (including pandemic response management), whistle blowing policies, fraud and privacy risk management, model risk management and business conduct risk management;
- The extent to which the enterprise risk management framework is adaptive to changes to the entity and to its environment;
- The extent that the enterprise risk management framework complies with regulatory requirements and guidelines applicable to it;
- The adequacy of the entity's Own Risk and Solvency Assessment (ORSA); and
- Contingency plans to restore the entity's financial strength and viability in severe adverse circumstances.

Entity is part of a group

- .03 In applying paragraphs 8230.01 and 8230.02 for an entity that is part of a group, the actuary would consider factors including, but not limited to, the following:
- The risks and benefits of belonging to a group structure, recognizing potential limits on fungibility of capital and on transfer of assets between separate legal entities;
 - Reasonably foreseeable changes in the group structure which could impact the capital and solvency of the entity and its ability to continue in business;
 - Risk modelling, stress testing, reverse stress testing and scenario testing would include changes in the group structure and in the support that the entity receives from other members of the group;
 - Assumptions that may be suitable for a self-standing entity may not be suitable when the entity is part of a larger group;
 - Imposition of risk management controls and tolerance limits by group management;
 - Differences in legal and regulatory requirements between jurisdictions; and
 - Contagion effect of adverse circumstances in other members of the group which could impact the entity (e.g., the entity's capital and solvency).

8240 Own Risk and Solvency Assessment (ORSA)

.01 When developing, implementing, maintaining, or reviewing an ORSA, the actuary would consider, in addition to the items in subsections 8220 and 8230, factors including, but not limited to, the following:

- The time horizon considered by the ORSA;
- Whether the qualitative and quantitative risk assessments and the financial projections used in the ORSA are appropriate for their intended purpose;
- Any changes to the entity's risk profile and risk appetite since the previous ORSA;
- The various accounting bases of the entity;
- Reasonably foreseeable changes in the external environment;
- Allowance for new business, and for the run-off of existing and new business;
- Access to new capital in times of financial stress;
- Differences between the entity's regulatory capital requirements and the entity's own assessment of its capital needs;
- The quality and adequacy of the entity's capital resources in relation to quality and adequacy criteria established by the regulatory body;
- The degree of severity reflected in the risk modelling, stress testing, reverse stress testing and scenario testing; and
- The circumstances that may trigger an ORSA to be performed at a time other than during the regular review schedule.

Definitions to be added to Subsection 1120

Enterprise risk management is a process, effected by an entity's board of directors, management and/or other staff, applied in conducting business and strategy setting across the enterprise, designed to identify potential risks that may affect the entity, and manage the impact of those risks to be within the entity's risk appetite, to provide reasonable assurance regarding the achievement of the entity's objectives.

Enterprise risk management framework is a set of components, including governance, policies, and practices through which enterprise risk management is effected.