
EXPLANATORY MEMORANDUM TO PRACTICE GUIDELINE 5: INSURER ENTERPRISE RISK MODELS

September 2018

A. About this Explanatory Memorandum

This Explanatory Memorandum has been prepared by the Risk Management Practice Committee (RMPC) to provide advice to Members on Practice Guideline 5: Actuarial Practice in Relation to Insurer Enterprise Risk Models (PG 5).

PG 5 is the Australian adaptation of International Standard of Actuarial Practice 5 - Insurer Enterprise Risk Models (ISAP 5) as adopted by the International Actuarial Association (IAA) Council on 21 November 2016.

The intention of the ISAPs issued by the IAA is to promote a greater consistency of approach to actuarial practice internationally in a given situation, so as to increase the confidence of clients and the public in the actuarial work product, but without unnecessarily constraining the exercise of actuarial judgment or creativity.

B. Background

The ISAP Working Group of the Risk Management Practice Committee (the Working Group) reviewed ISAP 5, as well as the approach to two other Australian Practice Guidelines based on ISAPs, being PG 1 based on ISAP 1, and PG 3 based on ISAP 3.

The Working Group has recommended that an amended version of ISAP 5 be adopted as a new Practice Guideline, PG 5, consistent with the approach for PG 1 and PG 3. In addition, certain defined terms in PG 5 are to be added to the Glossary of General Defined Terms used in Practice Guidelines.

C. Development of International Standards of Actuarial Practice (ISAPs)

ISAPs are model standards of practice issued by the IAA. An ISAP is a statement of actuarial practice expected of actuaries operating within a specified context. It sets minimum expectations on matters such as the methodology to be employed, the approach to be used in setting assumptions, the contents of the resulting report or opinion, and the way in which the report or opinion should be presented.

The IAA encourages its member associations (of which the Institute is one) to have in place professional practice documents that are substantially consistent with the ISAPs, bearing in mind the needs of their members. In September 2014, Council confirmed the intention of the Institute to achieve a degree of congruence, as far as is appropriate to the circumstances

of Members, between ISAPs issued by the IAA and the professional practice documents issued by the Institute. In adapting ISAP 5 to create PG 5 for application by Members, the aim has therefore been to follow ISAP 5 as far as is appropriate given local circumstances.

D. ISAP 5 and PG 5

PG 5 is the Australian adaptation of ISAP 5 as adopted by the IAA Council on 21 November 2016.

ISAP 5 provides guidance to Members when performing actuarial services involving the use of enterprise risk models for insurers.

The key differences between PG 5 and ISAP 5 are:

- References to ISAP 1A have been removed. At this time, the Institute has not yet adopted ISAP 1A (or an Australian adaptation thereof). Should this change, then we expect that the reference to ISAP 1A will be re-incorporated into PG 5.
- Definitions of the terms "Evaluation Date", "Insurer" and "Insurer Enterprise Risk Model" have been added.

Based on the nature and extent of the differences between PG 5 and ISAP 5, the Institute has assessed that there is "strong convergence" between PG 5 and ISAP 5. PG 5 materially conforms to international standards of the IAA, with allowance for local modification to fit local conditions. However, given the differences, it should be noted that compliance with PG 5 will not necessarily result in compliance with ISAP 5. Therefore, where a Member is required to perform work in conformity with ISAP 5 (e.g. because the work is being undertaken in an overseas jurisdiction) the Member should refer to the specific requirements of ISAP 5.

E. Relationship of PG 5 to PG 1

The actuarial services under PG 5 have been designated as Applicable Professional Services for the purposes of PG 1. This means that the requirements of PG 1 are applicable to the services performed under PG 5. PG 5 includes a requirement that compliance with PG 1 is a prerequisite to compliance with this PG.

F. Member consultation

An Exposure Draft of PG 5 (and Explanatory Memorandum) was released to Members on 28 May 2018. No feedback was received.

G. Commencement Date

The new PG 5 will take effect for actuarial services performed on or after 1 October 2018.

END OF EXPLANATORY MEMORANDUM