



# Society of Actuaries in Ireland

## **ACTUARIAL STANDARD OF PRACTICE LA-5**

### **THE PRUDENTIAL SUPERVISION OUTSIDE THE REPUBLIC OF IRELAND OF LIFE ASSURANCE BUSINESS**

#### **Classification**

Recommended

**MEMBERS ARE REMINDED THAT THEY MUST ALWAYS COMPLY WITH THE CODE OF PROFESSIONAL CONDUCT AND THAT ACTUARIAL STANDARDS OF PRACTICE IMPOSE ADDITIONAL REQUIREMENTS UNDER SPECIFIC CIRCUMSTANCES.**

#### **Legislation or Authority**

Any applicable insurance legislation or regulations in the relevant country

#### **Application**

Actuaries appointed to report, in fulfilment of a regulatory requirement, on the solvency and/or other aspects of the financial management of life assurance companies or other organisations writing life assurance business which are domiciled outside the Republic of Ireland, except in any country in which a full member of the International Actuarial Association or a regulatory or supervisory body provides formal guidance on the subject matter of this Actuarial Standard of Practice, provided that the work in question is performed in accordance with that formal guidance.

<b>Version</b>	<b>Effective from</b>
1.0	25.04.1995
2.0	30.12.2006
2.1	01.11.2010
2.2	01.10.2017

#### ***Definitions***

“*ASP*” means Actuarial Standard of Practice

“*the Code*” means the Code of Professional Conduct of the Society of Actuaries in Ireland

“*Company*” means the life assurance company or other organisation writing life assurance business for which the actuary acts

*“Liabilities to Policyholders”* means any liability of a Company to or in respect of a policyholder, including any obligation arising out of any broader regulatory requirement to treat its policyholders fairly

*“should” or “should normally”* indicates that members of the Society of Actuaries in Ireland to whom this ASP applies must comply with a particular requirement or prohibition, unless the circumstances are such that the requirement or prohibition is inappropriate and non-compliance is consistent with the standards of behaviour, integrity, competence and professional judgement which other members or the public might reasonably expect of a member.

## **1 General**

- 1.1 This ASP should be interpreted in the context of the legislation, regulations and practice of the country(ies) in which the Company is domiciled, with which an actuary to whom this ASP applies should be familiar. In addition, members of the Society of Actuaries in Ireland are reminded of their obligations under ASP PA-2, General Actuarial Practice. Members must ensure compliance with all relevant aspects of ASP PA-2 which should normally take precedence if any points of overlap cause a contradiction with this ASP.
- 1.2 The responsibilities of an actuary to whom this ASP applies are central to the financial soundness of the life assurance business of the Company in respect of which he or she is appointed. Insurance regulators may also rely on the actuary to confirm that the Company in respect of which he or she acts is financially sound or that it complies with the regulatory requirements in other ways (e.g. certification of the method of calculation of premiums).
- 1.3 In accordance with the Code, an actuary should not accept an appointment requiring him or her to determine the financial soundness of a Company if he or she does not have the appropriate knowledge and practical experience relevant to the Company and types of business concerned. Regulations may also specify additional requirements. Before taking up an appointment, an actuary should ensure that the relevant requirements of the Code have been met, including, in particular, appropriate contact with his or her immediate predecessor, if any, if this is required by the Code.
- 1.4 An actuary to whom this ASP applies should take all reasonable steps to ensure that the Company understands whether he or she is providing advice in accordance with regulations or related ASPs.
- 1.5 An actuary should be aware of the requirements of the Code relating to Open Communication. Advice provided by an actuary to the Company should normally include sufficient information and discussion about each relevant factor and about the results of his or her investigations to enable the recipient of the advice to judge both the appropriateness of any recommendations and the implications of accepting them, including the implications for the Company’s policyholders.
- 1.6 An actuary should be objective in the performance of his or her duties and take reasonable steps to satisfy himself or herself that he or she is free from bias. The Code provides relevant guidance on conflicts of interest.

- 1.7 An actuary should pay due regard to generally accepted actuarial best practice given the purpose of the work. The Code and ASPs establish some elements of generally accepted best practice. An actuary to whom this ASP applies should also consider whether there are any other practices that may be considered as generally accepted best practice. Where a materially different practice is adopted from one which is a non-mandatory generally accepted best practice, the actuary should disclose the reasons for the practice actually adopted.
- 1.8 Each of sections 4 to 8 of this ASP applies only to an actuary who performs work referenced in that section for the purposes of a Company's compliance with legislative or regulatory requirements. An actuary should ensure that his or her terms of engagement are clear about whether these legislative or regulatory requirements apply or not.

## **2 The actuary's duties**

- 2.1 The actuary should carry out the actuarial investigations specified and report in accordance with the relevant legislation or regulations. Where the actuary believes that the regulatory basis or format materially fails to make the real financial circumstances of the Company clear, the actuary should draw the attention of the Company to this in a supplementary report.
- 2.2 All material valuation methods and assumptions should be stated.
- 2.3 All material risks to the solvency of the Company should be identified, unless the actuary has reported these previously in a report of the type referred to in paragraph 7.1 below, or otherwise, and this information remains valid.
- 2.4 If the actuary considers that the report contains matters of significant concern which need to be addressed by the Company, he or she should normally seek permission to present the report in person.
- 2.5 Where a material risk to the solvency of the Company has been identified, the actuary should consider advising the Company that the report, together with any relevant risk management reports or the other reports referred to in paragraph 2.3 above if any, or at least a specifically drafted summary of it or them, should be sent to the management or controlling body, as appropriate, of any organisation in the parental hierarchy of the Company which exerts significant influence on the decisions of the Company.
- 2.6 The actuary should bear in mind that any report required by the regulator which is publicly available may be used by third parties, including financial advisers and actual and potential policyholders.
- 2.7 The actuary should consider whether to notify the regulator if, when he or she resigns from that role or when his or her appointment in that role is terminated or not renewed, there are circumstances concerning the cessation of the appointment which he or she thinks ought to be brought to the regulator's

attention. Such considerations should take into account the duty of confidentiality to the client and the extent, if any, to which legislation overrides or exempts the actuary from that duty.

- 2.8 If the Company also carries out general insurance business or any non-insurance activities, the actuary should consider that business to the extent to which it might impact on the life assurance business. Even where the life assurance business fund and other funds are legally separated, poor performance of the other business can affect the apportionment of overheads between the businesses and the capital available outside the life assurance business fund to meet any regulatory minimum margin. Where necessary, the actuary should seek advice from an actuary with relevant experience in general insurance or, in the case of non-insurance business, a recognised expert in that business.
- 2.9 The actuary should advise the Company if he or she believes that it may not currently be meeting Liabilities to Policyholders as they fall due or might not have done so in the past, or might in reasonably foreseeable circumstances fail to do so, either as a result of insufficient financial resources or otherwise. If the actuary believes that the Company is not able to, or may not in the reasonably foreseeable future be able to, meet any solvency capital levels required by regulation or considered appropriate by the actuary, this is a sufficient (but not necessary) condition to provide this advice.
- 2.10 Liabilities to Policyholders may include obligations arising from a regulatory requirement for the Company to treat its policyholders fairly, and may include implicit liabilities created by literature, illustrations or precedent. If so, the actuary should ensure that the Company's management is aware of his or her interpretation of its obligations to treat its policyholders fairly which need to be taken into account. In general terms, this interpretation should have regard to the broad nature of the Company's practices and its approach to the treatment of policyholders both individually and (where appropriate) collectively as a group vis-à-vis shareholders.
- 2.11 An actuary fulfilling a regulatory role should consider whether he or she is required to inform the regulator without undue delay if, having first informed the Company of matters envisaged in paragraph 2.9 above, the Company does not take appropriate action to remedy the situation. Such considerations should take into account the duty of confidentiality to the client and the extent, if any, to which legislation overrides or exempts the actuary from that duty. The actuary should ensure that the Company is aware of this professional consideration prior to informing the regulator.
- 2.12 If the actuary considers that the Company's reinsurance arrangements are inappropriate or inadequate in the context of the risks borne by the Company, he or she should advise the Company on the modifications necessary to protect the position of the policyholders.
- 2.13 The actuary should determine whether the investment policy pursued by the Company is, or could become, inappropriate having regard to the nature and

term of the Company's liabilities and to the investments available. If this is the case, the actuary should advise the Company of the changes in investment policy necessary to protect the position of policyholders.

- 2.14 The following list, which is not exhaustive, sets out the most usual items of information which are likely to be relevant to this section, particularly paragraph 2.3:
- (a) the current and likely future economic, investment, and regulatory environment;
  - (b) the terms on which existing business has been, and current new business is being, written, with particular reference to all options and guarantees, together with the entitlements and reasonable expectations, (where the actuary has a regulatory/statutory responsibility to consider such expectations), of the policyholders of those contracts;
  - (c) the existing investments of the life assurance fund (including the free assets contained in that fund) and the continuing investment policy, including the use of derivative instruments;
  - (d) the nature, extent and availability of the Company's assets outside the life assurance fund;
  - (e) the marketing plans, in particular the expected volumes and costs of sales;
  - (f) the current and likely future level of expenses;
  - (g) the current and likely future levels of mortality and morbidity;
  - (h) the reinsurance, underwriting and (for health insurance) claims handling arrangements;
  - (i) the Company's policy with regard to the nature and timing of allocations of profits to policyholders and/ or shareholders;
  - (j) the current and likely future taxation position of the Company;
  - (k) the persistency of the business written both in the short and long term, and the terms for discontinuance;
  - (l) the extent to which assets and liabilities are matched by term, by type and by currency;
  - (m) counterparty risk exposures;
  - (n) contingency action plans relating to the management of risks under adverse scenarios; and

- (o) information on the current and expected future liquidity position;

### **3 The actuarial valuation**

- 3.1 The actuary should satisfy himself or herself as to the material correctness and completeness of the valuation data and should seek such additional information from the Company as he or she considers necessary for this purpose. If the actuary has doubts about the material correctness and completeness of the valuation data, but considers that the establishment of additional reserves will compensate for any shortcomings in the valuation data, then such additional reserves should be established. If the actuary is unable to satisfy himself or herself as to the material correctness and completeness of the valuation data, any certificate of solvency required to be provided to a regulator should be appropriately qualified.
- 3.2 The actuary should be satisfied that the appropriate valuation procedures have been correctly carried out and adequately documented.
- 3.3 The actuary should use liability valuation methods that comply with the relevant regulatory requirements and are appropriate to the contracts in question, taking into account not only the principal benefits but also any ancillary benefits, including surrender values and any options or guarantees. Depending on the nature of the regulatory requirements, the valuation may be required to be prepared on a best-estimate or prudent basis. When assessing the liabilities of the Company, the actuary should also have due regard to any obligations arising from any regulatory requirements to treat policyholders fairly.
- 3.4 Appropriate provision should be made for future expenses of administering the business existing at the date of the investigation. Allowance should be made for the possibility that preferential service agreements or outsourcing arrangements might be altered or terminated. If appropriate in the context of the regulatory environment, prudent allowance should be made for the loss of future margin as policies are made paid-up and, if the number of policies is declining or expected to decline, for the possibility of more slowly declining overhead costs. Any regulations which specify that the provisions should be sufficient in the event of closure to new business at a specified future time should be taken into account.
- 3.5 Assumptions about future mortality and morbidity should take into account the recent relevant credible experience and trends of the country, the industry or the Company.
- 3.6 If the value to be placed on the assets is the responsibility of the actuary, he or she should satisfy himself or herself that adequate systems of control are in place to ensure that appropriate values are placed on the assets and that any limits on exposure to individual investments, classes of investment or counterparties imposed by regulation are properly applied. If it is difficult to determine an accurate value for a material proportion of the assets, the actuary should establish reserves, if necessary, in respect of the risk of over-valuation.

- 3.7 The actuary should decide the rates of discount to be used in the valuation of the liabilities, except where the rates to be used are prescribed by regulation. Where assets are valued at current market value, the deterministic or stochastic discount factors used should be consistent with those market values, making allowance, where appropriate, for credit risk exposures relating to the assets. Where assets are valued on a different basis, the rates of discount should be determined consistently with that basis. In addition, due allowance should be made for the current and future taxation position of the Company. Any such allowance should be consistent with any allowance made for tax relief on expenses.
- 3.8 The actuary will need to ensure that allowance has been made for the effect or possible effect of derivatives and other financial instruments when choosing the valuation basis. The actuary should particularly bear this in mind when choosing the basis used in the changed investment conditions envisaged in paragraph 3.11 below. The appropriate valuation interest rates should allow for the return on the assets held as adjusted to reflect credit risk exposure and economic exposure under futures contracts and contracts for differences. Consideration should also be given to the treatment of, and allowance for, financial options, particularly when close to an option date.
- 3.9 The actuary should take account of the Company's reinsurance arrangements in the valuation, including any implicit financing provision. The actuary should take account of the likelihood of payment by the relevant reinsurer in valuing benefits from a reinsurance contract.
- 3.10 Where appropriate in the context of the regulatory requirements, the actuary should ensure that adequate margins are included in the valuation assumptions or methods, having regard to the actuary's own assessment of the risks inherent in the nature and conduct of the Company's business.
- 3.11 Where there is any mismatching of assets and liabilities, the actuary should ensure that there is adequate explicit or implicit provision for reasonably foreseeable adverse movements in asset values or yields, recognising that this may be addressed explicitly in solvency capital standards in some regulatory environments.
- 3.12 On occasions, expenses or the return on new investments may be at a level which, if it persisted, would render it unlikely that the Company would be able to meet Liabilities to Policyholders. If there are well-founded reasons for believing that these matters will change for the better in the foreseeable future, the actuary is not obliged to assume their indefinite continuation at the present level. However, the actuary should clearly state in all written reports regarding both valuation and premium bases his or her assumptions about future change in these items.

#### **4 Ongoing monitoring of solvency**

- 4.1 This section applies to an actuary who has been given the responsibility of monitoring on an ongoing basis the Company's ability to continue to meet Liabilities to Policyholders in respect of life assurance business contracts as they fall due.
- 4.2 The actuary should ensure that he or she has sufficient information and resources to enable this task to be carried out. The actuary should request the Company to provide such information and should advise the Company as to the systems reasonably needed to enable it to do so. If the Company is unable to supply any of the requested information, the actuary should inform the Company of the consequences of this for the advice to be provided.
- 4.3 The information required, and the nature and frequency of such monitoring, will depend on the nature and extent of the risks to which the Company is exposed and the extent of the solvency margin or other capital available. The list in paragraph 2.14 above should be taken into consideration.
- 4.4 Paragraphs 2.5, 2.9 and 2.11 should be applied as if they referred to the outcome of an ongoing rather than an annual assessment.

#### **5 Premium rates and policy conditions**

- 5.1 This section applies to an actuary who is responsible for recommending premium rates.
- 5.2 The actuary should be satisfied that the premium rates being charged for new business are appropriate. That is to say, they should be sufficient to enable the Company in due course to meet its emerging liabilities, having regard to the items listed in paragraph 2.14 above and to the extent of the Company's free assets available, at present and in future, for this purpose.
- 5.3 For almost all types of policy, it is impossible to be certain that a premium rate will be sufficient, because sufficiency depends on the future course of factors such as mortality, persistency, the return on investments, and the Company's expenses. However, sound techniques should be used to enable the circumstances and extent of potential insufficiency to be identified and quantified.
- 5.4 The actuary should pay special attention to contracts involving guarantees and policyholder options, including circumstances in which the policyholder or an intermediary could gain by surrender and re-entry.
- 5.5 The actuary should also consider the implications for the Company and for policyholders if future economic, demographic or business circumstances were to be radically different from those of today, particularly where the policy contains guarantees and options.
- 5.6 It may be that a practicable premium basis, whilst commercially justifiable, will involve significant new business strain. The actuary should be satisfied



that the Company will be able to set up the necessary reserves (and additional solvency margin where applicable).

- 5.7 Should premium rates be such that business is expected to be written on terms which require support from the Company's free assets, the actuary should assess the Company's ability to continue to write business on such terms and should inform the Company of this, indicating any limits on the volume of business that may prudently be accepted. Where the actuary is assuming support from free assets held outside the life assurance fund, he or she should inform the Company of the extent of such assumed support.

## **6 Exercising discretion over charges or other conditions**

- 6.1 This section applies to an actuary who is required to exercise discretion over charges or other policy conditions. This may arise where the Company has included in its policy documents a statement that certain terms will be determined by the actuary or other similar wording.
- 6.2 In determining such terms, or in providing advice to the Company in this area, the actuary should have regard to any requirements to treat policyholders fairly, to any other relevant regulations (including any covering unfair contract terms) and to policyholder expectations created by literature, illustrations or precedent.

## **7 Financial condition reports**

- 7.1 This section applies to an actuary responsible for preparing an "actuarial financial condition report" or other forward-looking assessment of the solvency position of the Company.
- 7.2 This should be prepared in compliance with any relevant regulations or in accordance with ASP LA-2 or in whatever alternative format the actuary considers necessary to ensure that the Company is sufficiently well informed of the foreseeable risks which could jeopardise the Company's financial condition and the extent to which they may do so.
- 7.3 When preparing this report, the actuary should consider whether there are risks particular to the environment to which the Company is exposed. The list in paragraph 2.14 above should be considered in making this assessment. If inadequate historical data is available for the construction of financial or other models, the actuary should take care to make any necessary adjustments before using models based on data from other countries.
- 7.4 In particular, the actuary should advise the Company of the actions that could be taken if the solvency of the Company were to deteriorate, as a result of factors either within or outside the control of the Company. This advice should include details of the options available as the probability of failure to meet Liabilities to Policyholders progressively increases and should also refer to the desirability of having documented plans and processes for dealing quickly and effectively with the situation were it to arise.

## **8 Recommendations on allocation of profits**

- 8.1 This section applies to an actuary who is required by either regulation or the Company to advise on the distribution or allocation of profits.
- 8.2 The actuary should determine, in accordance with any applicable regulations, any excess of the assets available for its life assurance business over its liabilities attributable to that business. If the rights of any life assurance business policyholders to participate in profits relate to a part of the business, the actuary should also identify separately any excess which relates to that part.
- 8.3 The actuary should advise the Company on the extent to which it would be appropriate to distribute any excess to policyholders or transfer it to shareholders and, where required to do so, should make recommendations for its specific allocation.
- 8.4 In making recommendations in respect of any proposed allocation of profits, the actuary should carry out appropriate financial investigations including an appraisal of the relevant past experience.
- 8.5 In the report that includes the recommendations, the actuary should include sufficient information and discussion about each factor, and about the results of any financial investigations, to justify the recommendations, and to enable the Company to judge the appropriateness of the allocation and to understand its implications for the future course of the Company's business. In particular, the actuary should state his or her:
- (a) conclusions from the appraisal of the relevant experience including, if asset share techniques are used, the way in which the recommendations are derived from those techniques;
  - (b) understanding of the Company's financial and business objectives to the extent that they are relevant to the recommendations;
  - (c) assessment of the Company's ability to meet any minimum required solvency margin following the recommended allocation;
  - (d) interpretation of any legal advice given to the Company constraining or potentially constraining the Company's discretion when allocating surplus and how this has been reflected in the recommendations;
  - (e) interpretation of any requirements to treat policyholders fairly having regard in particular to (a), (c), and (d). What constitutes fair treatment may be influenced by policy literature and other publicly available information such as future benefit and by past and current distribution practice;
  - (f) opinion of the extent to which it is appropriate to distinguish between groups of participating policies having regard, inter alia, to the nature

of the policies, their duration and their relevant pooled experience, and taking account of (d) and (e); and

- (g) opinion of how the recommendations maintain fairness between different categories of policy or policyholder and between policyholders and the Company.

The extent of information and discussion appropriate for any factor may depend upon the extent to which, if at all, the factor has been covered in a report formally presented to the Company in the previous eleven months. In particular, the actuary may report in an appropriately abridged form when interim or terminal bonus rates are being reviewed during the eleven months following an investigation and full report.

- 8.6 If the recommendations anticipate the results of a determination of surplus, the actuary should include in the report the estimated results of the determination and show how the recommendations can be financed.
- 8.7 The actuary should discuss the relationship between the recommended allocation and recent and expected future experience. In the case of with-profits business, the report should address bonus prospects, including terminal bonus if applicable, in different future investment scenarios. If the recommended allocation is excessive relative to the recent and expected experience (excluding any non-recurrent elements) and if the continuation of this relationship in future years could result in a material deterioration in the Company's financial position, the report should indicate whether and how this could appropriately be avoided, taking any requirement to treat policyholders fairly into account.
- 8.8 Where, in the opinion of the actuary, there is uncertainty regarding the extent to which the Company can exercise its discretion when allocating surplus to policyholders, he or she should state in the report the nature of the uncertainty, the assumptions made with regard to the uncertainty when making the recommendations and the consequences were the uncertainty to be resolved differently.

## **EXPLANATORY NOTE**

### **ACTUARIAL STANDARD OF PRACTICE LA-5, VERSION 2.2**

*This Explanatory Note does not form part of the ASP.*

Version 2.2 was introduced to address requirements to use a ‘best-estimate’ rather than prudent valuation under prudential supervisory regimes such as Solvency II.

#### Changes:

- To reflect that valuations may be prudent or best-estimate depending on the country.
- Update some text on risk management areas, as actuaries may also be involved in providing risk management reports.
- Refresh of some other text.