

Institute of Actuaries of India

Actuarial Practice Standard (APS) 3 – Financial Condition Report

Classification: Practice Standard

Legislation or Authority:

The Insurance Act 1938 (hereinafter referred to as the Act).

The Insurance Rules 1939 (hereinafter referred to as the Rules).

Insurance Regulatory and Development Authority (Appointed Actuary) Regulations 2000 (hereinafter referred to as AA Regulations)

Application

Appointed Actuaries of life insurers having registration to transact life insurance business under Section 3 of the Act.

Status

Issued under Due Process in accordance with the “Principles and Procedure for issue of Guidance Notes (APSs) {adopted by EC on 16.11.1997}.

Issued by the Executive Committee under Rule 29(l) of Rules of the Society in its meeting held on 04 03 2003.

Version: 1.00 effective from 01 04 2003

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1. Introduction

- 1.1 Section 13 of the Act requires that every insurer carrying on life insurance business shall, in respect of the life insurance business transacted by him, every year, cause an investigation to be made by an actuary who shall be the Appointed Actuary of the life insurer into the financial condition of the life insurance business carried on by him in terms of the provisions of the section and IRDA (Actuarial Report and Abstract) Regulations, 2000. In addition to this obligation, it is advisable for the Appointed Actuary to provide to the Board of Directors of the life office with a more extensive written report into the current solvency position of the life office and its possible future development.
- 1.2 While the statutory report shall be in the format prescribed by the IRDA (Actuarial Report and Abstract) Regulations, 2000, the purpose of this APS is to suggest a possible format and contents for a Financial Condition Report to the Board of Directors of a life office.
- 1.3 The Financial Condition Report should be addressed to the Board of Directors of the life office. It is essential that the report is expressed in a form which is accessible to its readers and does not conceal important issues because of

any reason such as undue length or complexity of the report. An Appointed Actuarial shall also provide an executive summary drawing attention to important issues in the report.

- 1.4 In this report, the Appointed Actuary shall assess the ability of the life office to withstand changes in both the external economic environment and the particular experience of the life office. The combined effect of a change in two or more related assumptions will in many cases be more important than a change in any one of them in isolation.
- 1.5 The Appointed Actuary should use whatever techniques he or she considers appropriate to the business written by their office to assess the ability of an office to withstand changes in both the external economic environment and the particular experience of the life office.
- 1.6 The Appointed Actuary should address the issue of what actions are open to the life office for dealing with the particular circumstances and, where appropriate, make suitable recommendations.
- 1.7 It is not essential to have a single report covering all the items in this APS, where the Appointed Actuary has already reported to the Board on some aspects previously.

2. General Points

2.1 The Financial Condition Report should normally include:

- 2.1.1 The purpose of the report.
- 2.1.2 The assessment of the financial position of the life office at the time the investigations were carried out.
- 2.1.3 Any historical development of the life office which may have implications for the future of the life office.
- 2.1.4 Comments on particular aspects of the historical development of the life office, such as any policy condition, prospectuses, methods of selling etc. which has led to Policyholders' Reasonable Expectations being formed with financial consequences for the life office.
- 2.1.5 A review of the business of the life office and the environment in which it is operating.
- 2.1.6 A review of the financial investigations with special reference to any future external factors which present a threat to the life office's financial security and the options open to the life office to deal with those factors.

2.2 The Appointed Actuary shall comment in greater detail on:

- 2.2.1 The methods and assumptions that have been used. The report shall distinguish between those assumptions which are important and those which are less important as also those which are within the life office's control and those which depend on the external situation.
- 2.2.2 Any changes made to the methods or assumptions used in the last similar report.
- 2.2.3 Any inadequacies in his or her analysis due to factors such as non availability of data or any other matter.
- 2.2.4 The differing nature of the assumptions and the extent to which those can be relied upon. He or she shall also comment on the factors that are outside the control of the life office.
- 2.2.5 How the assumptions made compare with the recent experience and explain the reasons where the assumptions significantly differ from the recent experience.
- 2.2.6 Any specific financial characteristics of the existing business or new business being written that may require special consideration.
- 2.3 The report should indicate, where appropriate, how the following items have been addressed:
 - 2.3.1 Any unusual features of the existing business, new business being written or proposed product development.
 - 2.3.2 Any financially significant reinsurance arrangement.
 - 2.3.3 Effects of any known or planned changes in the life office's method of operation.
 - 2.3.4 Any use made by the life office of derivatives, its purpose and its financial significance.
 - 2.3.5 Post Balance Sheet events/ developments since the end of the financial year/report period.
3. The Appointed Actuary needs to be vigilant about the factors that might affect the life office, such as:
 - (i) Concentration of assets in particular risk areas;
 - (ii) Derivatives;
 - (iii) Assets containing unusual provisions which may be susceptible to particular risks;
 - (iv) Sources of new business which have unusual characteristics;
 - (v) Impending major claims or litigation that might affect the life office;
 - (vi) Risks arising out of product literature or policy documentation;
 - (vii) Loss of a distribution channel;

(viii) The impact of options and guarantees in the insurance liabilities in different scenarios.

3.1 In each scenario tested, the Appointed Actuary should provide for all elements of the statutory liability.

4. If the Appointed Actuary identifies situations or sets of situations, which lead or could lead to financial difficulty for which no satisfactory remedial action can be found, the Appointed Actuary should ensure that such matters have special prominence in the report and include any recommendations as to what might be done to avoid such circumstances.