37th India Fellowship Seminar

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Product Actuary – Empowering Policyholders Vs Marketability (Life - Professional)

Guide : Suresh Sindhi

Institute of Actuaries of India

Presented By :

1. Het J. Shah
2. Saachi A. Patel
3. Gargi G. Bhide
4. Bhakti S. Gaitonde

Introduction of Guide

Mr. Suresh Sindhi is currently working as a Consulting Actuary and Appointed Actuary with an international life insurance company and providing actuarial consulting services to various domestic & international corporate clients.

He has acquired almost 23 years of actuarial & leadership experience working with various life insurance, pension consulting & reinsurance companies. He is actively involved in the educational and examination activities of the Indian and UK Actuarial Institutes.

As an industry expert, he is the member of “Board of Studies” at Wadia College, Pune & instrumental in designing the syllabus of actuarial subjects at the degree level course, “Banking, Insurance & Actuarial Science”.

He is a regular speaker at various prestigious institutions including National Insurance Academy (NIA), Pune, & has delivered guest lectures on varied topics related to insurance and actuarial field at various institutions.

His interest is in learning & application of modern data science techniques such as AI, ML, Predictive Modelling, ’R’ programming language to insurance and risk industry.

Case Study

- As a young and newly qualified actuary in product & pricing team of a life insurance company, you are beaming with ideas constantly. Often, you have been appreciated for suggesting creative ideas in your work. However, the most recent idea that you suggested has not been received with the same level of appreciation by the **product strategy committee** that you are part of.
- For the company’s **newest product yet to be launched soon**, you have suggested that in addition to the standard format of the benefit illustration that is stipulated by the regulator, the company could take a step in the right direction and **publish policyholder IRR for that product in every benefit illustration.**
- The company’s **marketing** colleagues have **rejected the idea** stating that it will make it challenging for them to sell this otherwise exciting product. You tried explaining to them that this specific product has great return for the policyholder and that showing IRR in benefit illustration will substantiate their selling efforts. However, they still had **concerns** over how this makes it **easy for everyone** (policyholders, competitors to name a few) **to compare** with other financial products. They also had concerns over various other implications, for which they were not in favour of this idea.
- On the other hand, some of the **committee members** have also **raised** additional **concerns** that this will open floodgates and there will **expectations** that policyholder IRR be published for all future products of the company.

Context

Young and newly qualified Actuary in Products & Pricing team with creative and innovative ideas

Latest idea – To publish IRR in the standard format of BI for a new product to be launched, believes IRR in BI will substantiate selling efforts

Actuary's intent:

- Increased transparency during the process of sale
- Policyholder Empowerment

Opposition & Concerns:

- Marketing team – Challenging to sell an otherwise exciting product & ease in comparing returns with other financial products
- Product Committee – Formation of Policyholder Reasonable Expectation (PRE), in particular, IRR will be published for each product in future

Agenda

- Context
- Internal Rate of Return – Overview
- Publishing Internal Rate of Return (IRR) in Benefit Illustration (BI)
  - Comprehensive Evaluation of idea
  - Pros & Cons
- Regulations, Practice Standards and Guidance
- Suggestions
- Conclusions

IRR - Overview

IRR is the annual rate of growth expected to be generated on an investment.

- ❖ Advantages of IRR:
  - ✓ Easy to calculate
  - ✓ Incorporates time value of money
  - ✓ Easy to compare with other investments

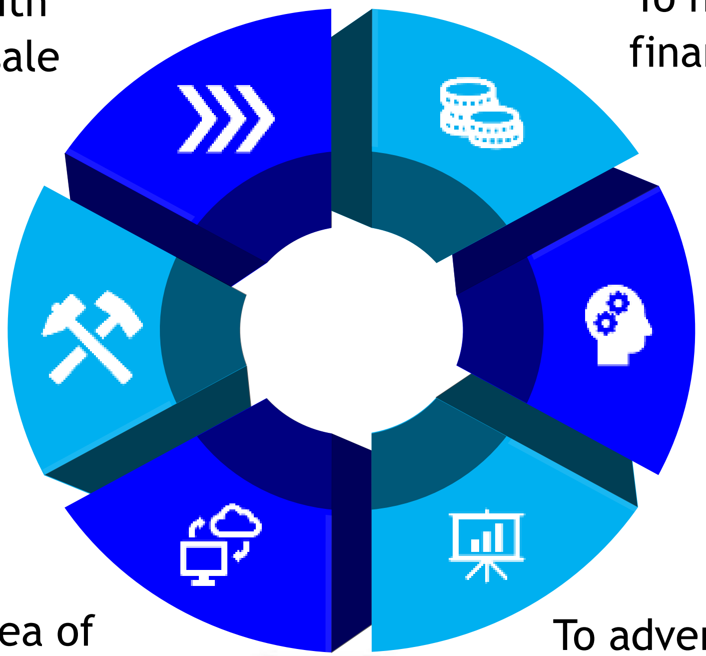
- ❖ Use of IRR in Insurance Policies:
  - ✓ To evaluate the investment returns of different products by comparing the premiums paid with maturity & survival benefits
  - ✓ To compare investment returns under insurance products with returns under other instruments

- ❖ Challenges

Comprehensive Evaluation - Reasons for publishing IRR in BI

To increase transparency with customer in the process of sale

To help policyholder make better financial choices and an informed decision



To explore a cross sell opportunity to attract existing customers

To take an initiative as part of educating customers

To improve upon the idea of publishing IRR if something similar is already done by a competitor

To advertise the high returns of the product which will result in higher product sales

Considerations / Implications (1/2)

Regulator
- Currently silent
- Approval requirement
- Explanation of move

New Policyholder
- Additional information
- Informed decision
- Formation of PRE

Existing Policyholder
- Existing products
- May feel aggrieved
- Lapse & re-entry risk

Admin & IT Systems
- System implementation
- Time, effort & cost

Distribution Channels
- Training on understanding IRR
- Training on explaining IRR to customer

Competitors
- Current practice
- Potential time to implement this change

AA & BoD
- Approval requirement
- Cost-Benefit analysis

Considerations / Implications (2/2)

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New Business

- Boost sales if successful
- Reduce sale of certain products if low IRR

Impact of GST

- Usually shown without GST
- Policyholder pays premium with GST

Impact of Income Tax

- Tax treatment of benefits
- Tax slab of individual

Impact on Niche Segments

- No / low competition
- May be detrimental to show IRR

Other Factors

- Rider premium
- Annuity / pension products
- Extra premium on account of EMR

Pros & Cons of Publishing IRR in BI

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Pros

- Increased transparency
- Competitive Advantage
- Non-Participating Savings Products
- Increase Policyholder confidence
- Better pitch for Sales
- Regulator’s response
- Comparison within product made easier

Cons

- Protection vs. Savings
- Product type
- Level of Satisfaction
- Competitor move
- Setting Standards
- Bundled/ package products
- Product type

Pros in detail (1/2)

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Increased transparency

- Policyholders will have more awareness and knowledge

Competitive Advantage

- Company happens to be the first to publish IRR in BI, may give an edge over the competitors

Non Participating Savings product

- Benefits are known and guaranteed at outset
- IRR in BI can be considered as actual returns that can be earned

Increase policyholder confidence

- Can help to increase policyholder confidence as it shows that the product provides this guaranteed rate (for Non-Participating Savings products)
- Quantitative figure to compare with alternative investments

Pros in detail (2/2)

Better pitch for Sales

- Easier to sell in case of competitive products

Regulator’s response

- Taking a step towards increasing transparency and awareness may be seen as being aligned with one of the IRDAI's objectives of ensuring that policyholder’s interests are protected

Comparison within product made easier

- Sales team can now show the impact on IRR by changing Premium Payment Term , Policy Term, Premium size, etc

Cons in detail (1/2)

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Protection vs. Savings

- Savings products - IRR is significant
- Term products - Sole purpose is protection

Level of Satisfaction

- For Linked or Participating products, benefits are non – guaranteed
- If actual returns lower than IRR shown in BI, can lead to dissatisfaction of policyholders and attract bad press

Competitors' Move

- Competitive advantage may be short lived or end depending on how fast competitors react

Cons in detail (2/2)

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Bundled / Packaged Products

- It may be inaccurate or impossible to show a combined IRR on bundled products. For eg. Savings product with add-on Critical Illness benefit

Setting Standard

- If IRR is shown for one product, it will set expectation for all future products For eg. Setting PRE, providing direct metric of comparison to customers and competitors

Product type

- Appropriateness of showing IRR in BI depends on the underlying product type i.e. guarantee provided in terms of benefits

Cons by Product Type

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Term Products

- Pure risk : No Maturity Benefit. IRR can be calculated using the death benefit
- Return of Premium : Maturity benefit is % of total of premium paid. IRR can be very low for long term contracts

At time of sale, comparison should be made basis premium rather than IRR

Participating Products

- Illustrations shown in BI at 4% and 8% expected projected returns and bonus
- Not reflective of true situation and hence policyholder IRR is not certain from outset

Unit-Linked Products

- Fund value projection shown in BI at 4% and 8% expected returns
- Not reflective of true situation and hence policyholder IRR is not certain from outset

Professional Guidance, Regulations & Practice Standards

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- Professional Conduct Standards (PCS) version 4
- Circular on (a) Benefit Illustration; and (b) other market conduct aspects vide Circular No. IRDAI/ LIFE/ CIR/ 173/09/2019 dated 26 September 2019

Professional Guidance

- Insurance Regulatory and Development Authority of India (Non-Linked Insurance Products) Regulations, 2019
- Insurance Regulatory and Development Authority of India (Linked Insurance Products) Regulations, 2019
- Insurance Regulatory and Development Authority of India (Protection of Policyholders' Interests) Regulations, 2017

Regulations

- Actuarial Practice Standard 5 – APS 5 Appointed Actuary and Principles of Life Insurance Policy Illustrations (Ver 1.00)
- Actuarial Practice Standard 1 – APS 1 Appointed Actuary and Life Insurance Business

Actuarial Practice Standards

Professional Guidance (1/2)

Professional Conduct Standards (PCS) Version 4

- 1.3. A member who has any doubt about the interpretation of professional guidance should seek advice from an actuary with relevant experience or guidance from professional body in case of residual doubts.
- 2.2. Members have a duty to the actuarial profession and clients and must always act honestly and with integrity.
- 2.4. Healthy debates and expressing different opinions on matters of professional interest are good for the betterment of the actuarial profession considering they do not bring any disrepute to the profession or other members or the professional body.
- 4.1. An actuary is expected to use best judgement in formulating advice and must have proper regard to any relevant professional guidance or other guidance
- 6.1. Actuaries must ensure that their professional judgement is not compromised, and is not seen to be compromised, by any bias, conflict of interest or the undue influence of others.

Professional Guidance (2/2)

Circular on (a) Benefit Illustration; and (b) other market conduct aspects vide Circular No. IRDAI/LIFE/CIR/173/09/2019

- 2.4. Annexures 2.4.1 to 2.4.7 provide the format of Benefit Illustrations for various lines of business.
- 2.6. The illustrations shall be clear and fair to enable a customer to make an informed decision.

Clarification on Circular on BI and Market Conduct Aspects

- Query No. 8) the format prescribed for BI is the minimum information format and that the insurer can add more information as per product specifics or to enable the policyholder make an informed decision
- Clarification: No. It is advised to follow the format in toto. Only if the product specifically requires additional columns/information then it may be run through the products team of Life department and filed before using the same.

Regulations

Insurance Regulatory and Development Authority of India (Non-Linked Insurance Products) Regulations, 2019	• Chapter X – Point 33 of the said regulation is dedicated to Benefit Disclosure at the point of sale. • However, the regulation is silent on publishing the IRR in the Benefit Illustration
Insurance Regulatory and Development Authority of India (Linked Insurance Products) Regulations, 2019	• Chapter IX – Point 31 of the said regulation is dedicated to Customized Benefit Illustration at the point of sale. • The net yield is demonstrated currently with respect to gross investment return of 8% as stipulated by the Authority. • However, the regulation is silent on publishing the IRR in the Benefit Illustration
Insurance Regulatory and Development Authority of India (Protection of Policyholders' Interests) Regulations, 2017	• 5.1.i Steps must be taken to enhance Insurance Awareness • 5.1.iv Benefits / returns of the product are not mis-stated / mis-represented during policy solicitation and sale stages. • 6.2 All material information in respect of a proposed cover must be provided to the prospect to decide on the best cover that would be in his or her interest.

Actuarial Practice Standards (1/2)

Actuarial Practice Standard 5 – APS 5 Appointed Actuary and Principles of Life Insurance Policy Illustrations

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- Defines the framework within which the Appointed Actuary shall discharge the responsibilities as required under the **Standards of Conduct and Sound Practices (SCSP)**

- Framework for illustrations is set out in the SCSP and Section 4 refers to Illustrations. It states elaborately the exact requirements for a BI.

- Guiding Principles state that-
  - C.1. Educate the potential customer with some level of quantification
  - C.3. In some cases, it may be appropriate to indicate that further information will be made available on request.
  - C.5. Overly complex illustrations can confuse more than explain
  - C.6. There is some trade-off between putting in all possible information and keeping an illustration simple.
  - C.7. The company must ensure that intermediaries and the employees responsible for sales receive appropriate training and are supervised and monitored with regard to the use of policy illustrations.

Actuarial Practice Standards (2/2)

Actuarial Practice Standard 1 – APS 1 Appointed Actuary and Life Insurance Business

- 2.2. An Appointed Actuary should ensure, so far as is within his/her authority, that the life insurance business of the company is conducted on sound financial lines and that he/she has regard to Policyholders' Reasonable Expectations (PRE).

- 4.3. states that the Appointed Actuary must take all reasonable steps to ensure that new policyholders are not misled with regard to their expectations, e.g. in connection with illustrations at the point of sales.

Suggestions – Alterations and Modifications

- Conduct a time bound pilot exercise of the idea
- Explain the concept of IRR at the time of sale. Show IRR on case-to-case basis depending on the demand from customer
- Prepare a comparison of range of IRRs that can be achieved in a product
- Decide to show IRR only for specific products such as Non-Participating Savings
- For Unit-Linked products / Participating products, illustrate the range of possible IRRs
- Alternatives – Give/Get ratio, distinction of guaranteed and non-guaranteed IRR, etc

Synopsis (1/2)

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- Actuary is required to convince the senior management of the company
- Actuary must ensure to present all the facts and practical aspects to the management in an unbiased manner
- Actuary must not only propose additional information to be added to BI but also suggest a process to be undertaken operationally to cover all aspects
- Balanced approach must be suggested that will take into consideration all the stakeholders and the possible interactions between them

Synopsis (2/2)

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- Overall implications of the idea must be considered in terms of cost-benefit analysis, various disclosures to regulator and policyholders, conflicts arising if any and possible resolutions and impact on existing and future new business
- Success depends on appropriate and clear communication with policyholders and with the sales force.
- Calculator may be devised by the company which will clearly compute the IRR for the product and for various benefit payouts under the product.
- Actuary should evaluate the idea of publishing IRR by product type and have in place separate approaches for Pure Term policies, Savings-cum-Protection plans (Non-Participating & Participating), Unit Linked Plans with appropriate disclosures

Our View

Publishing IRR in BI may be considered appropriate, assuming regulations allow and provided a product wise, contingency based range of IRRs is published

It is require that a balanced approach be considered that includes:

- ✓ Satisfying all the required regulatory requirements
- ✓ Addressing Stakeholder concerns, in particular the Marketing team and Product strategy committee
- ✓ Identifying Various risks involved & appropriate measures to mitigate the same
- ✓ Well devised, robust and approved process to be followed,
- ✓ Technical training to all concerned especially sales force

Policyholders may be educated by imparting knowledge, increasing transparency thus empowering them and ensuring an appropriate PRE is set.

Thank you

Questions?