GROUP BUSINESS AND PRICING DISCRETION OF ACTUARIES

GROUP 4

INDIAN FELLOWSHIP SEMINAR
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AGENDA

- Why the discussion?
- Important Circulars
- Main Products under Group Schemes
- Participating structure
- Main Guidelines/ Regulations
- Regulatory controls / caps on expenses
- Ethical and professional issues
- Current Environment
- Areas of Discretion for actuary and the considerations involved
- Effects of new draft

Why the discussion?

- Group Business is an important portfolio
- It is a business where large number of members are part of the scheme and the group being homogeneous in nature allowing discerning treatment for each scheme
- Hence, the need of discretion and Judgment of the Actuary at the inception and at review based on experience is Critical
- Unique nature of scheme and its composition
- Sharing of risk and experience encourages the insurers and Sponsors
- Regulatory Restrictions – Is there a lack of confidence ? Or is to bring about consistency in the approach? Or Both?

Important Circulars

- **Circular IRDA/ACTL/FUP/Ver A/Aug 2003** on Profit sharing/ Experience rating under Group Insurance Schemes. This circular shows fair confidence in the discretion with AA
- ✓ Carry forward of loss to be decided by Appointed Actuary
- ✓ Profit sharing % not to exceed 90% or 75% based on no. of life years but discretionary in nature
- ✓ Mortality not to be lighter than 60% of standard mortality rates for profit sharing purpose
- ✓ Experience rating/profit sharing formula & related assumptions to be furnished at time of Product filing- This restricts the level of discretion but would be fair to both the insurer and scheme Sponsor

Important Circulars Cont.

- **Circular No 01/ IRDA/ ACTL/MC/2006-07** on compliance with F & U
- ✓ This again retains and acknowledges lots of discretion with AA
- ✓ Discretion to decide table of premium rates
- ✓ Approval of Appointed Actuary required for every premium quotation below filed rates
- ✓ AA should be satisfied about the appropriateness of premium rates charged relative to filed rates-- **clear discretion**
- ✓ Appointed Actuary advised by IRDA to draw the attention of

  the management to unhealthy practices- discretion of assessment and reporting

  - enhanced benefits without charging
  - unapproved premium discounts
  - rebates without prior approval
  - offering very low premium rates

Important Circulars Cont.

- **Circular No 01/ IRDA/ ACTL/MC/2006-07** on compliance with F & U
- ✓ Emphasis on Corporate Governance
- ✓ Internal audit and inspection to ensure policy issued

  in line with terms & conditions of product filing. This is just a way to ensure that the specified methods are not violated and does not infringe with the discretion of AA
- ✓ Deviations observed to be brought to the notice of AA &

  Senior management- This is again aimed at assisting the AA

Hence under both the circulars cited before, the AA is given fair discretion and responsibility for the matters related to quoting, reviewing and monitoring the premiums quoted.

Important Circulars Cont.

- **Circular 064/IRDA/ACTL/March – 2008** on Group products

- ✓ Emphasis on flexibility to Insurer- discretion flowing through the AA
- ✓ Insurer can offer premium quotes different from filed rates in respect of annually renewable pure life cover products
- ✓ Approval by AA on sound actuarial principles
- ✓ For immediate annuity products flexibility to vary annuity rates in the range of +10%/-10% of approved rates without prior approval of the Authority
- ✓ For Fund based products, quotes could vary from filed rates if duly certified by AA– HUGE DISCRETION

Important Circulars Cont.

- **Draft Circular** *no. IRDA/ACTL/REG/CIR/../../2013-14* on F&U procedure for Group Products and immediate annuity products
- ✓ "…It is observed that the premiums approved under file and Use procedure and the actual premium quoted to various groups differ significantly…..."– a big concern expressed by the regulator and hence probably putting an implicit question marks on the discretion
- ✓ Concern over undercutting of premium rates under group term- Again a question mark on the level of discretion and its judicious application and therefore insisting on firm premium tables at the stage of filing only
- ✓ Concern over declaring higher returns under Fund based products – again a concern on the judicious declaration of the returns and therefore insisting on the stated methodology for declaration of interest in advance and at later stages based on maximum Reduction on Yield cap

Important Circulars Contd.

- Withdrawal of Circulars issued in 2006 & 2008 mentioned earlier- the discretions withdrawn and allowed only to the extent as envisaged at the stage of filing.
- Is it appropriate or not is a subject matter of discussion and introspection. Coming straight from the regulator it is a circular with lots to read in between the line for the profession.

Main Products under Group Schemes

1. Group Term Insurance – Single Premium or One year renewable
2. Fund based Group Products
3. Group Savings Variable Insurance Product
4. Group Credit Insurance
5. Group Health Insurance
6. Group Immediate Annuity Product

Therefore the regulations specify the product design which can be filed for approval

Group Term Insurance:

Salient Features:

- Employer-employee/Non Employer-Employee
- Single Premium/ One year Renewable
- Benefit payable upon death of members
- Under renewable TI, premium rates can be unit rate or age dependent
- Quoted premiums based on Underwriting policy of the Insurer
- Usually requires Actively at Work clause and Min membership
- Free Cover Limit

Fund Based Group products:

Salient features:

- Employer-employee/Non Employer-Employee (Govt. sponsored)
- Non Linked Platform
- Operates under Variable Insurance platform- No discretion
- Contributions to be made as per Actuarial valuations to fund the employee benefits
- Employee benefits includes Group Gratuity, Leave encashment and Superannuation
- Term insurance can be provided with explicit premium for insurance cover . Premiums to be aligned with other term insurance products - discretion

Fund Based Group products: contd.

- Insurer manages the Fund of the Sponsor
- Positive-non zero Interest credited at specified intervals by the Insurer to the Fund i.e. Policy Account Value
- Benefits payable on death and other exits as specified by Scheme rules

  Other exits – resignation, voluntary retirement,..
- Sum Assured / Fund Value payable upon death of the member

Fund Based Group products contd.

Salient features:

- Linked Platform
- Contributions allocated to segregated funds
- Value of Funds depend on performance of underlying assets
- Explicit charging
- Benefits as per scheme rules payable upon exit of the member

Group Savings VIP:

Salient features:

- Employer-employee/Non Employer-Employee
- Non Linked Platform
- Simple and easy to understand
- Operates on lines of Individual VIP but with the administrative efficiency of Group Schemes
- Min group size 50 & Max 5000
- Min term of 5 years- No discretion for shorter terms
- Discounts based on group size and premium size etc to be stated at the outset explicitly and hence no scope for future discretions

Group Credit Insurance:

Salient features:

- ❖ Employer-employee/Non Employer-Employee
- ❖ Level / Decreasing Term Insurance
- ❖ Usually covered on the lives of borrowers
- ❖ Can be offered to micro insurance groups also
- ❖ Benefit Payable upon death
- ❖ Single Premium policies
- ❖ Surrender Value differs considerably between Companies – discretion with AA

Group Health Insurance:

Salient features:

- One year renewable
- Single Premium is not allowed
- Critical Illness rider comes under this product

Group Immediate Annuity Product:

Salient features:

- Employer-employee only
- Annuity payable to members upon retirement
- Options available ex. Payable till death, ROPP,..

Main Guidelines/ Regulations

IRDA Regulations (Non Linked), 2013

- Sets out types of group products that can be offered to Employer-employee (EE) and Non EE groups

  These have been dealt in previous slides
- Fund based products can be offered on VIP platform
- Interest Crediting structure for VIP
  a) Non negative Interest rate – to be credited with frequency not less than quarterly
  b) Additional Interest Rate – to be credited with frequency not less than quarterly
  c) Residual interest rate – to be credited at the end of Policy year to ensure maximum RIY as allowed is not breached
- Creation and Maintenance of Shadow Fund
- All these specify the constrains within which the product is to be shaped and hence no room for discretion

Main Guidelines/ Regulations

IRDA Regulations (Non Linked), 2013 contd.

- Contributions to be made as per Actuary's certificate in accordance with AS 15 (revised)
- No top-ups under Fund Based Group Products unless to address underfunding
- Fund Based Group Gratuity & Group leave encashment products should have mortality benefit with explicit mortality charges

Main Guidelines/ Regulations

IRDA Regulations (Non Linked), 2013 contd.

- Fund Based products

a) Defined Benefit / Defined Contribution structure

b) Minimum Assured benefit to be specified

c) Benefits payable on death, retirement or any other exit as per scheme rules from superannuation funds

d) Option to purchase immediate annuity from any one of the insurer among all the insurers where the superannuation fund is maintained

Main Guidelines/ Regulations

IRDA Regulations (Non Linked), 2013 contd.

- Emphasis on Group Administration and specified limits of expenses which can be reimbursed
- MVA to be applicable only for Fund Based Group products upon bulk surrender provided there is an investment guarantee– method to be specified

Main Guidelines/ Regulations

IRDA Regulations (Non Linked), 2013 contd.

- Financial viability of Group Products
- ✓ Products to be reviewed each year for financial viability
- ✓ If found unviable, AA should revise the product under F & U procedure
- ✓ Products to be re-filed every 5 years along with experience of past 5 years
- ✓ If Pricing assumption is less than 50% of prescribed table, AA should justify using past 3 years experience

Main Guidelines/ Regulations

IRDA Regulations (Linked), 2013

- Only fund based products allowed under linked platform
- Offered to Employer-employee groups only
- Fund based products consist of

a) Superannuation Product

b) Gratuity Product

c) Leave encashment product

Main Guidelines/ Regulations

IRDA Regulations (Reinsurance), 2013

- This regulation clearly puts the limit on the retention levels ranging from 5 lakhs to 20 lakhs based on the age of the company but leaves the scope of lower retention limit for new type of risk being introduced

- Here the AA would have the discretion to apply the limits based on his assessment of new risk in reference to existing products

Regulatory controls / caps on expenses

Caps on commission

- Fund based scheme - 2% of premium received (NB & subsequent) with max of ` 1 lakh per scheme per year
- SP group term & SP credit Insurance – 2% of Single premium with max of ` 200000 per Scheme
- One year group renewable term insurance/ health insurance - 2% of premium with max of ` 50000 per Scheme per year

Regulatory controls / caps on expenses

- Surrender charge

  0.05 % of Policy Account Value with maximum of 5lakhs if surrendered within third policy anniversary
- Not clear on the methodology to calculate Surrender Value under Group Credit Insurance. **AA holds discretion over the methodology.**
- Other Controls
- ✓ The new Product regulations, 2013 puts restrictions on the innovative products and which can only be submitted after satisfaction of regulator.
- ✓ Moreover the guidelines specify the type of products which can be designed
- ✓ Many restrictions on the design and pricing aspects as detailed in the previous slides

Current Environment

- **Term Insurance**
- Cut throat competition on Premiums
- No minimum floor prices
- No proper standardisation on reinsurance limits
- Significant importance attached to policy servicing
- **Fund Based Products**
- Corporate clients are highly educated and want value for money and not averse to switches

Areas of Discretion for actuary and the considerations involved

Mortality rates

- Range of Premium rates filed with IRDA
- Actuary has the discretion on the table that can be used to price the group of lives
- Actuary’s discretion if quoted rates are lower than filed Premium rate

Areas of Discretion for actuary and the considerations involved Cont.

Other areas of discretion

- Life years to arrive at credibility factor – applied to past mortality experience
- No. of years of mortality experience to consider
- Amortization of stamp duty
- Amortization of acquisition expense
- Expense loading and discounts
- Free cover limits
- Waiver of terms & conditions like waiver of actively at work clause
- Fix the profit sharing % within the cap
- Carry forward loss

Areas of Discretion for actuary and the considerations involved Cont.

Main consideration to choose rates

- Age profile
- Size of the Group
- Average Sum assured and sum assured distribution
- Occupation / Job profile
- Participation - Voluntary/ Involuntary (% of minimum take up if voluntary)
- Employer-employee/ Non Employer –employee
- Past experience

Actuaries – decision making

Wider Picture

- Integrity : Members will act honestly and with the highest standards of integrity.
- Competence and Care : Members will perform their professional duties competently and with care.
- Impartiality : Members will not allow bias, conflict of interest, or the undue influence of others to override their professional judgement.

Actuaries – decision making

Wider Picture

- Compliance : Members will comply with all relevant legal, regulatory and professional requirements, take reasonable steps to ensure they are not placed in a position where they are unable to comply, and will challenge non-compliance by others.
- Communications : Members will communicate effectively and meet all applicable reporting standards.

Source: The Actuaries’ Code

Suggestions

- As regards the withdrawal of the circular No. 064/IRDA/ACTL/March – 2008 dated 18.03.2008---

- ✓ The premiums under medium to long term protection product shall be as per the file and use only.

- ✓ The flexibility to vary the annuity rates based on the investment conditions up to 10% & filing of assumptions within 7 days of such changes restricts the misuse of this provision and is welcome.

- ✓ Under the one year renewable term insurance products the existing flexibility available to the insurers should be allowed.

Suggestions Contd.

- ✓ However, the method for arriving at such rates should be on sound actuarial basis and to be described in the file and use filed with the authority.

- ➢ Our observations under the circular No. IRDA/ACTL/FUP/Ver. A/Aug 2003 dated 02.09.2003.

- ✓ The condition that the mortality assumption shall not be less than 60% of the standard mortality table may be removed. As mentioned earlier, the appointed actuary shall on the basis of sound actuarial principles allow premiums with mortality assumption less than 60% of the standard mortality table.

Suggestions Contd.

- The mechanism of profit sharing, reviewability of the rates and the credibility of the group as to its self insurability may in certain cases allow the appointed actuary to quote premium rates below 60% threshold mentioned in the circular. Hence the authority should revisit clause 2e of the circular.
- Such cases, where the insurer quotes rates less than the filed rates (in case of products with/without provision for experience rating) may be informed to the authority in such frequency as decided by the authority.
- In summary, we are of the opinion that flexibility based on sound actuarial principles and to be exercised only by the appointed actuary on the one year renewable group term product may be allowed by the authority.

Conclusions

- Renewability of GTI is very important as it increases the scope of profitability
- Enhances brand name in the market which helps to acquire more new business
- Appropriate reinsurance arrangement required
- Facultative reinsurance helps to offer competitive quotes
- Ensure that parameters under discretionary areas are set with sound actuarial principles
- Compliance with regulations and group guidelines
- Ensure appropriate investment strategy for fund based products to enable to declare high returns
- Ensure proper customer / policy service is provided
- Lot of scope under Micro Insurance as it is an untapped market

Conclusions Contd.

- Under Group Credit Insurance, target different types of borrowers educational, credit card, gold loan….
- Proper loading to be given to classify the financial institutions
- The nature of Group Products needs discerning treatment to the different policyholders based on the profitability and experience unique to the scheme
- The scheme holders are much more participative and demanding necessitating dynamic review of the products. Because of the larger unit size of the Group Products this helps limit risks and is also cost efficient to use dynamic review and pricing of the Group Products.

Conclusions Contd.

- **Therefore the nature of business requires application of discretion, however which are justified and professionally taken with sense of competence and care**

- Further in light of the provision of annual review and once in five year re-filing, it is important to allow the actuaries to have fair discretion which are judiciously applied in the client and public interest

- The indiscriminate and unjustified discretions wherever done without merit and application of professional principles need to be dealt with profession

- **However over-prescriptive framework would not encourage the innovation in this dynamic sector**

THANK YOU