ACTUARIAL SOCIETY OF INDIA

GUIDANCE NOTE (GN) 21:APPOINTED ACTUARY AND GENERAL INSURANCE BUSINESS

Classification: Practice Standard
Legislation or Authority:

1. **The Insurance Act 1938** (hereinafter referred to as the Act) and amendments thereto.
2. The **Insurance Regulatory and Development Authority Act, 1999** (hereinafter referred to as the **IRDA Act**).
3. **The Insurance Rules 1939** (hereinafter referred to as **the Rules**).
4. **IRDA (Appointed Actuary) Regulations 2000** (hereinafter referred to as **AA Regulations)**;

Application

This Guidance Note is applicable to an Appointed Actuary, appointed in accordance with the provisions contained under AA Regulations, by an Insurer carrying on the business of General Insurance (as defined under Section 2(6B),2(13A),2(13B) of the) under the Insurance Act 1938, and shall constitute 'Professional Standard' within the meaning of Regulation 2 (1) (e) of the AA Regulations. This is also applicable to all other actuaries, who as a matter of course, get associated with a general insurer and have to relate directly or indirectly to the Appointed Actuary of such a general insurer.

Status

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

Version	Effective from
1.0	01.08.2003

A: The Appointed Actuary

1.Legal Framework: The following regulations and amendments thereto from time to time issued under the IRDA, 1999 define the role of the Appointed Actuary in respect of General Insurance companies:

1.1 **IRDA (Registration of Indian Insurance Companies) Regulations 2000** (hereinafter referred to as **Registration of Indian Insurance Companies Regulations),**

1.2 **IRDA (Actuarial Report and Abstract) Regulations, 2000** (hereinafter referred to as **Actuarial Report Regulations)**;

1.3 **IRDA (Assets, Liabilities and Solvency Margin of Insurers) Regulations, 2000** (hereinafter referred to as **Solvency Regulations)**;

1.4 **IRDA (Investment) Regulations, 2000** (hereinafter referred to as **Investment Regulations**) as amendments issued thereto in 2001

1.5 **IRDA (Preparation of Financial Statements and Auditor's Report of Insurance Companies) 2000** (hereinafter referred to as **Accounting** R**egulations)** and amendments issued thereto in 2002

1.6 **IRDA (General Insurance -- Re-insurance) Regulations, 2000** hereinafter referred to as **Reinsurance Regulations)**.

1.7 **Section 13(6) of the Act** requires the Appointed Actuary to perform an annual investigation into the financial condition of certain sub classes of general insurance business unless exempted by the Authority in terms of proviso thereto..

2.Nature of Responsibility

2.1The responsibilities of an Appointed Actuary, who is appointed under the AA Regulations, are central to the financial soundness of the general insurance company to which he is so appointed.

2.2 An Appointed Actuary should ensure, so far as is within his / her authority, that the general insurance business of the company is conducted on sound financial lines and monitor any action / practice, which in his / her opinion, is unfair and likely to be prejudicial to the interests of the policyholders,

2.3 The essence of the profession lies in upholding its standards, technical and ethical, in the public interest. As a member of the Actuarial Society of India (ASI), every Actuary has the responsibility to maintain the highest professional standard envisaged by the ASI. Any Appointed Actuary, who is uncertain as to the proper course of action to adopt in relation to a potentially significant matter, is strongly advised to seek the help and the advice from the ASI.

3. Considerations affecting the position of Appointed Actuary

3.1 The role of the Appointed Actuary constitutes an **'Actuary-in- practice'** and in order to practise as Appointed Actuary, an actuary must at all times while in practice hold a **Certificate of Practice (CoP) issued by the ASI;**

3.2 Any actuary, before accepting the appointment as an Appointed Actuary, must consider most carefully in the light of individual knowledge and work, whether acceptance would be in line with proper professional behavior and standards. No actuary should act as Appointed Actuary if he / she does not have the adequate knowledge relevant to the assignment concerned. There may be exceptional circumstances where this need not apply, but in such cases the Appointed Actuary is to have recourse on a professional and formal basis to an actuary who has such knowledge and expertise and who himself / herself holds a CoP issued by the ASI and such an arrangement must be approved by the ASI as well as IRDA.

3.3 An Actuary before accepting the appointment as an Appointed Actuary must satisfy himself/herself that all stipulations as specified under regulation 3(2) of AA Regulations are complied with and will continue to be complied with as long as he / she continues as Appointed Actuary.

3.4 The AA Regulations require the Appointed Actuary to be an employee of the insurer or an external consultant to an insurer, to which he / she is or will be an Appointed Actuary. There must be a clear understanding between the insurer and the actuary about his appointment as the appointed actuary of the insurer specifying the conditionalities of the appointment. It shall be ensured that the engagement is in a manner where the responsibilities as Appointed Actuary do not get compromised.

3.5 The Appointed Actuary must have a right of access to the Board of Directors in general and the Principal Officer in particular and should have access to all relevant information, books and records so that the full range of his duties and obligations can be carried out satisfactorily. This must be made explicit in the appointment letter. Where there is a group structure, the Appointed Actuary should bear in mind any possible implications on his / her right to information and ensure a right of direct access exists to the relevant decision making bodies and / or persons.

3.6 Where an actuary has financial interest in an Insurance Company or a Group of Companies which by their nature and size are or become such that a material conflict of interest would in the normal course of events, arise or seem to arise (or where a material conflict arises from some other reasons), the actuary should not accept the position of the Appointed Actuary or if already appointed continue in it, as the case may be.

3.7 The appointed actuary shall follow the regulations of the Authority in regard to his note as such and shall be guided by Guidance Note and other Guidance Notes specifically issued, if any, in respect of the provisions of the regulations

4.Extent of the Appointed Actuary's responsibility

4.1 Every actuary has a responsibility to the profession and his / her responsibilities to a client must be consistent with this. An Appointed Actuary is however also in a special position as he / she has statutory responsibilities to the IRDA. If these two aspects materially conflict, the Appointed Actuary has to advise the company as soon as he / she feels that the company has initiated any action – or a situation has arisen outside the control of the company – that materially threatens its solvency. If the company does not remedy the situation, the Appointed Actuary is required to advise the IRDA – but not before informing the company first. This duty applies, notwithstanding any provision or provisions contained in the code of conduct of the ASI which might seem to restrict or inhibit discharge of this responsibility.

4.2 The Appointed Actuary must ensure that his / her conduct and reach and depth of his / her functionalities enable him / her to discharge his / her duties and obligations in letter and sprit in accordance with regulation (8) of AA Regulations.

5.The duties of the Appointed Actuary

5.1 The Appointed Actuary shall certify the IBNR reserves and the premium rates as stipulated in the regulation.

5.2 For the purposes of the regulation the Appointed Actuary must have the above information made available to him / her and he / she must make sure that the company understands the necessity of this information and makes suitable arrangements to ensure that the information is made available.

5.3 The Appointed Actuary shall also perform those duties as may be called upon by the Authority (IRDA) from time to time.

5.4 The Appointed Actuary must have regard to all aspects likely to affect the financial condition of the company, including but not limited to the following;

(i) Premium deficiency, if any, in respect of existing policies and policies to be written;
(ii) The expected volumes and costs of sales ;
(III) The current and likely future underwriting policies;
(iv) the current and likely future claims experience including claims handling expenses;
(v) the reinsurance treaty & co insurance arrangements;
(vi) The current and likely future level of expenses including compliance with limitation of expenses provision in the Act;
(vii) The extent of the company's free assets;
(viii) The company's current and likely future taxation position
(ix) Investment policy and its implications on Assets matching Liabilities

6. Premium rates and policy conditions for new products and existing products on sale

6.1 The Appointed Actuary must satisfy himself that premium rates for new business or renewal of existing business are fair, i.e., are neither excessive nor inadequate, that is to say sufficient in due course to enable the company to meet its liabilities both in tariff and non-tariff classes of business. If in future, such business is likely to be written on inadequate terms, it will require support from the free assets in the shareholders fund. The Appointed Actuary should consider the company's ability to continue to write such business in the context of how much capital is required and should inform the Board of Directors accordingly.

6.2 Whether the premium rates are appropriate is a probability statement and hence the Appointed Actuary must exercise his / her judgement. This judgement needs to be based on the use of sound techniques and the Appointed Actuary should also consider, among others,

[a] types of products and product mix
[b] claims costs including claims handling expenses
[c] the adequacy of the provision for expenses and acquisition costs
[d] the impact of future inflation
[e] the impact of likely changes in marketing and underwriting strategy
[f] the adequacy of premium rates in context of solvency.
[g] the impact of taxation
[h] implication of any legislative amendments, which may not

have been fully reflected in the claims data

6.3 Premium Rate Components

The Appointed Actuary should also analyse the insurer's own claims experience and, where possible, compare it with the industry experience. The analysis should consider both claims frequency and claim size. The Appointed Actuary should consider, as far as is practical, the extent to which the insurer's and [industry's] reinsurers' claims experience is influenced by:

data quality;
claims management policies;
portfolio mix;
marketing and underwriting strategies;
case reserving;
infrequent large losses; and
random variations.

7. Capital Requirements

7.1 One of the important factors that will affect the financial position of a general insurance company is its marketing strategy and the projected volume of new business likely to be generated. The Appointed Actuary should form an assessment as to whether the projected volumes are realistic and advise the Board of Directors as to the capital requirements associated with writing the required volume of business.

7.2 The Appointed Actuary should be satisfied that for a new product or a new area of operations or change in underwriting policies, the company will be able to meet the necessary reserves and solvency margin requirements from capital within the shareholders funds.

7.3 The Appointed Actuary should as far as possible assess the capital requirements.

8. Actuarial investigations

8.1 Section 13(6) of the Act requires the Appointed Actuary to perform an annual investigation into the financial condition of certain sub classes of general insurance business unless exempted by the Authority in terms of the proviso thereto..

8.2 If the Appointed Actuary desires to assess the value of any given liabilities using discounting methods,consideration must be given to the liabilities, the assets and the relationship between the two and the Appointed Actuary should be satisfied as to the resilience of the financial position of the company in all reasonably foreseeable circumstances that might affect the position.

8.3 The Appointed Actuary should be satisfied as far as possible that the data are accurate, reliable and consistent. If there are any doubts on the data, the Appointed Actuary is expected to seek assurance from the company as to their accuracy and completeness. The Appointed Actuary should also be satisfied that the company is correctly adopting appropriate statistical formats and procedures and that adequate documentation exists in respect of them.

8.4 The assumed value for each valuation parameter should consist of two parts. The first part should represent the expected level and the second should represent a margin for adverse deviation. The expected level should be appropriate for the coverage being valued and, where possible, should be based on the insurer's experience for similar products. If such data is not available or is not appropriate, then it can be based on industry data. The size of the margin for adverse deviation should reflect the degree of confidence the Appointed Actuary has in the expected level of the parameter and his / her perception about the extent of such deviation. Further, the margin for adverse deviation should be such that its addition to the expected level results in an increase in the reserve.

8.5 The value placed on the liabilities must make appropriate provision for future expenses and this provision must at least equal that required if the company were to close new business one year after the valuation date. The possibility that preferential service agreements, if any, might be altered or terminated also needs to be taken into account.

8.6 Responsibility for investment policy and the value placed on the investments in any balance sheets rests with the company's Board of Directors. However, where the Appointed Actuary desires to assess the liabilities by discounting future fund flow, the Appointed Actuary should estimate the likely future proceeds of the existing assets and the rate at which future investment will be possible. The first requires an assessment of the nature of the company's investments and consideration of the rate of return, in terms of both capital and income likely over the future lifetime of the liabilities. The Appointed Actuary should have regard to the relationship between the term of the assets and of the corresponding liabilities in carrying out his / her investigations.

8.7 Keeping in view tax regime as applicable to general insurance companies, due allowance must be made for tax, taking into account the taxation provision of the company. This allowance must then be consistent with any allowance made for the tax relief on expenses.

8.8 The Appointed Actuary must judge and decide whether the investment policy pursued by the company is appropriate having regard to the nature and term of the liabilities. If it is not, the company must be informed of any constraints on investment policy needed and additional reserves, which may need to be set up.

8.9 The Appointed Actuary must review the reinsurance arrangements from time to time and consider alternative approaches with regard to retentions and type[s] of reinsurance arrangements. This would require the actuary to develop necessary statistics and statistical analyses for studying actual experience and recommend possible alternatives where considered necessary.

8.10 Premium and Claim Reserving

8.10.1 The Unearned Premium Reserve [UPR]

The method of computation of UPR should inter- alia take into account the incidence of the risk over the policy term. If the UPR is computed by using the time apportionment or n/365 method, which assumes uniform incidence of risk over the policy period, necessary adjustments to the value calculated should be made for the uneven incidence of risk. The Appointed Actuary should state the method used in the computation and the underlying assumptions.

8.10.2 Unexpired Risks Reserves [URR]

The Appointed Actuary should judge the adequacy of the UPR to cover the likely cost of the claims including claim handling charges and administrative expenses in respect of unexpired risks taking into account the possible impact of inflation. If the UPR is not assessed to be adequate for the future outgo, additional reserves have to be set up over and above UPR and the total amount is to be included as URR.

8.10.3. Claims Reserves

Claims reserves comprise –

(a) Reported claims where estimates of loss have been determined;

(b) Reopened claims;

(c) Reported claims where the estimate of loss has not been fully assessed — the reserve is referred to as Incurred But Not Enough Reported Claims {IBNER Claims Reserve};

(d) Incurred but not reported claims {IBNR Claims}; and

These reserves are required to be disclosed in the Annual Accounts. The Appointed Actuary is required to certify the adequacy of the IBNR and IBNER claims reserves in the solvency statement both for direct and inward reinsurance business. In accordance with accounting regulations a certificate from an appointed actuary must be attached as to the fairness of liability claims made in respect of contracts where the claim payment period exceeds four years, which shall be recognized on an actuarial basis, and the assumptions disclosed by way of notes to the accounts. In addition, the actuary may have to certify reported claims reserves in respect of overseas and inward reinsurance business. The actuary should ensure that actuarial methods are used in determination of these reserves. The actuary need to mention the methodology adopted giving a brief description and the underlying assumptions made.

8.10.4 Reserve methods noted above shall be used where appointed actuary is called upon to estimate, whether by statute or not.

8.11 Expenses including Acquisition Costs

The Appointed Actuary, if he is called upon to do so, must –

(a) analyse the insurer’s expenses according to fixed and variable expenses and type of expense;

(b) examine whether or not adequate provision is made in respect of the expenses in premium rating for each product line;

(c) alert the insurer if compliance with the expense limitation provision is unlikely;

(d) alert the insurer about the occurrence of cross subsidies, if any between product lines in respect of expenses except to the extent required to meet rural and social insurance obligation.

9. Written reports

10.1 The Appointed Actuary must report in writing to the Board of Directors of the company on the results and implications of any valuation carried out for statutory purposes before any report is made to the IRDA. In any report to the IRDA, the Appointed Actuary should use his / her best endeavors to ensure that;

[a] the financial results are presented in a way that demonstrates the true underlying position of the company, and

[b] these results are not distorted by any undisclosed valuation methods or assumptions.

10. The Appointed Actuary or any other Actuary to whom this guidance note applies shall specifically confirm in his / her written report that he / she has complied with this guidance note and other applicable Guidance Notes. If he/she is not in a position to confirm his / her compliance to the guidance note he / she shall explain the reasons for the same in the report.

B: Guidance to Actuaries who are Directors, Employees or Consultants (other than Appointed Actuary in a consulting position) of a General Insurance Company

1. An actuary should make suitable enquiries and satisfy himself / herself about the affairs of a company before and after joining its board, as the public and the other directors will assume that he / she is satisfied with the way the company is being run;

2. Where the Appointed Actuary is also a member of the Board of Directors or the senior management, he / she needs to take all reasonable steps to ensure that other members of the Board of Directors or other senior managers know the capacity in which he / she is expressing any views.

3. Any other actuary who is on the Board of Directors owes a special responsibility to the Appointed Actuary and should take care to respect the status of the Appointed Actuary.

4. The requirement of paragraph (3) above also applies to any other actuary holding a managerial or other position of authority in the company.

5. As regards guidance to actuaries - external to a particular company - who are asked either by the company or someone with a legitimate interest in it to comment on either a valuation carried out by the Appointed Actuary or a report he / she has made to the company, the guidance for such actuaries is that, although there is room for differences of opinion with regard to actuarial advice and judgement, they should always take care to respect the status of the Appointed Actuary. This does not though stop them from making properly reasoned comments on the work of the Appointed Actuary, if need be.

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