

CURRENT ISSUES IN LIFE ASSURANCE

SEMINAR, 26 APRIL 1995

This one-day seminar, which was attended by some 180 actuaries and chaired by Mr Chris Daykin and Mr Paul Grace, reflected a number of innovations. Firstly, it was held in the International Convention Centre, Birmingham, which will be the venue for the 1998 International Congress of Actuaries. Secondly, there was a dinner on the evening before, attended by the vast majority of participants. Thirdly, there were breakout sessions on three of the six topics discussed. However, as always, the CILA covered a range of topics, some of which were new, while others were being revisited.

Mr Hugh Scurfield welcomed and introduced Mr Michael Lyons, Chief Executive of Birmingham City Council, who spoke most entertainingly after dinner, primarily about the city and recent developments in its facilities, management and surrounding area. Mr Scurfield then outlined plans for the 1998 Congress, which include workshops and breakout sessions as well as the traditional plenary sessions, and encouraged the audience to return to Birmingham in 1998.

The breakout sessions which followed a plenary presentation on each of the first three topics were approved of by almost all participants, mainly because they enabled many more actuaries to express their opinions or seek clarification on specific points. However, it was widely felt that the report back session was somewhat less than satisfactory, essentially because the rapporteurs, particularly those for session C, had insufficient time to merge their comments into a coherent presentation. Some two thirds of the topics discussed were covered by almost all of the groups.

The New Valuation Regulations in Practice

Mr Malcolm Breingan explained that there were no accounting developments meriting discussion at the moment, and introduced the topic, giving some examples of possible issues and problems for discussion.

The report back session confirmed that, apart from the reduction in the interest rate margin from $7\frac{1}{2}\%$ to $2\frac{1}{2}\%$, the overall impact on the value of liabilities and assets had been minimal, although significant effort had had to be devoted to demonstrating that bases complied with the regulations, and certain asset problems had arisen, in particular with regard to Eurobonds and derivatives. Policyholders' reasonable expectations' considerations had posed a range of issues, and had had some impact on the published liabilities for with-profits business.

The application of the resilience test generated much comment, there being some uncertainty as to whether the September 1993 Government Actuary's Department (GAD) working rules remain applicable. A GAD representative confirmed that they do. Nevertheless, it was suggested that an updated GAD letter might be helpful.

The term 'arbitrary changes' in Regulation 65(5) generated substantial debate, and the eventual agreement was only that no one was confident that they knew exactly what it meant. Any strengthening of a with-profits basis in order to increase shareholder transfers was agreed to be arbitrary. The most contentious area was perceived to be whether the Inland Revenue might challenge any basis change as being arbitrary, if its apparent purpose was to reduce tax.

It was reported that two offices had had queries from their local Tax Inspectors regarding the allowability of certain reserves, apparently because the need to demonstrate the adequacy of each element under new regulations seemed to require the establishment of tier upon tier of excess reserves.

In conclusion, it was suggested that it would be useful if the GAD would prepare and share with the profession an overview of the impact of the new regulations on the industry.

CPD and Criteria for the Appointed Actuary Certificate

Mr Howard Webb introduced this subject, identifying two main topics for discussion:

- The CPD requirement is 15 hours p.a., of which 10 are relevant, the interpretation of relevance being fairly wide ranging. He asked whether this requirement created any problems for actuaries working in specialised areas such as disability and health, and also for specific suggestions for widening the range of CPD events.
- Paragraph 8 of the Memorandum on Professional Conduct requires the actuary to consider whether a conflict of interest makes it proper for him or her to act, and if it is, requires full disclosure. Mr Webb posed the question of the appropriate attitude for the profession to take regarding the Appointed Actuary's participation in share options or profit-related remuneration.

A wide-ranging CPD discussion exposed a number of useful ideas, and should provide some helpful guidance for the Committee. The consensus was that CILAs are generally valuable, and that there is a shortage of 'good' CPD events for comparatively junior actuaries.

The conflict of interest question provoked much discussion. Generally, it was agreed that the Appointed Actuary was well placed to handle apparent conflicts, but that it was important that all deliberations, particularly those regarding the determination of bases, should be well documented, in which case the actuary's position would not be too different from that of any other director on a similar remuneration basis.

Disclosure — Opinions of GN22 and Analysis of Company Methods and Results

Mr Mike Kipling presented a very clear summary of the responses to the February 1995 questionnaire which had been received from Appointed Actuaries. This provided an excellent basis for discussion, the conclusions of which will be considered by the Regulation Committee in reviewing the need for changes to GN22.

The apparent contentment with GN22 revealed by the survey appeared inconsistent with the discomfort expressed about the range of practices that had been adopted. This was considered to be a consequence of the timing of its completion, i.e. before contributors were aware of the range of practices adopted by other offices.

Participants were critical of the PIA's approach to the production of rules. The lack of prescriptive rules at an early stage had been aggravated by its practice of giving private advice to individual offices rather than publishing general advice. The consequential discrepancies and inconsistencies between the practices adopted by different offices is embarrassing, but any changes to enhance uniformity could cause even more embarrassment. It is, therefore, most important that the process is very carefully managed if the PIA is to issue further, more prescriptive, rules.

Many detailed topics attracted significant comment, most of which related to, or revealed, the wide range of approaches adopted. This was of great interest to participants, but cannot readily be summarised.

Business Risk Management for Actuaries

Mr Stuart Thompson introduced this topic, and showed a large number of slides, starting by listing the wide range of losses incurred by United Kingdom life offices in recent years and also some of the larger losses incurred by life offices overseas or by other financial institutions. The main aim of this was to encourage Appointed Actuaries to consider risk in a very open minded fashion.

He then summarised work by the United States profession, which had categorised types of risk, using C4 as shorthand for 'other risks', which they defined as 'any development which adversely affects the business as a going concern'. They have established a working party to research 'boundaries of risk', but it has yet to publish any output.

Mr Thompson recommended a risk audit. Company assets and resources would first be evaluated to identify major exposures to loss. Management would then decide whether the various risks were acceptable, or whether action was needed to reduce a risk, or whether the risk should be transferred to another party (e.g. removing guarantees or reinsuring them). The level of resources available for financing possible future losses is relevant. Emerging profits would only suffice to cover small losses. The existence of risk-based capital or free assets would represent greater protection.

Finally, he posed some questions for discussion:

— Should directors or Appointed Actuaries be responsible? The consensus was

that it did not matter, provided that the Actuary was involved and the issue was taken seriously.

- Should guidance be developed? This attracted little support, on the basis that it would tend to inhibit lateral thought.
- Should companies set up reserves for C4 risk? Again, there was little support for what was considered a spurious calculation. The emphasis should be on identification and avoidance rather than reserving.

Do With-Profits League Tables lead to Unreasonable Policyholder Expectations?

Mr Bernard Brindley presented the results of his analysis of 10 years' published data (DTI returns, with-profits guides and magazine surveys) for the largest 25 offices. He identified a number of surprising features:

- gross investment returns were surprisingly similar;
- investment returns net of expenses (based on RIY data) were much more varied;
- payouts exceed estimated asset shares, as expected under current investment conditions, but the excess varied widely with a surprising maximum of 57%; and
- with-profits payouts exceed unit-linked ones by the same office, as expected, but again the excess varied significantly.

Mr Brindley posed the question of whether the size of current payouts, which presumably reflected competitive considerations, and certainly appeared to conflict with the fundamental reality, was generating unreasonable expectations regarding future payouts.

One participant had prepared and circulated a summary of calculations for the same offices, which quantified the average tax rate payable over the last 10 and 25 years. There was a surprisingly wide range (about 25%) between offices, and a significantly higher average rate over 10 years than 25 (19% rather than 13%). This might indicate that competitive considerations were influencing claim values to such an extent that offices were not ensuring equity of treatment as between assurance and pensions business.

General discussion revealed widespread concern regarding the apparently unjustified level of with-profits claim values. There was some support for two suggestions: firstly, that the profession should instigate a formal investigation based on offices' internal data, despite the inherent confidentiality issues; and secondly, that all companies should have clearly defined and formally recorded approaches to bonus smoothing, any adjustments to the claim payments so determined being separately identified and the responsibility of the board, rather than of the Appointed Actuary.

Pensions — Opt-Outs and Transfers

Mr Peter Nowell, chairing the session, outlined the background to the problem of pension transfers and opt-outs, and stated that SIB had agreed to take advice

from an actuarial panel regarding any relevant issues which might arise. He expressed the view that the year-end reserving process appeared to have gone well, and suggested that the discussion should concentrate on matters concerning the role of the Appointed Actuary. In introducing the speaker, he pointed out that the paper produced for the meeting was dated 20 April, so it could not take account of the latest PIA guidance note issued that day.

Mr Stuart Ferguson then outlined the salient features of that PIA note, and identified various other topics for possible discussion. A wide ranging discussion ensued, the comments being essentially topical.

Finally, Mr Grace, in his closing remarks, commented on the efficiency of the Institute conference organisers, the attractiveness of the Conference Centre facilities and the general success of the breakout sessions, sentiments which were endorsed by all those present.

GRAHAM CLAY