

16 December 2022

██████████
Executive Director
APRA
Level 12, 1 Martin Place
Sydney, NSW, 2000

Dear ██████████,

Consultation – Remaking of four life insurance prudential standards

This submission is provided in response to APRA's request for feedback, via its letter to life insurers dated 21 November 2022, in relation to the remaking of four life insurance prudential standards. Our feedback on each of the standards is below; we have no significant feedback in relation to the four standards.

LPS 100 (Solvency Standard)

We note that the structure of this standard is based on the capital structure used prior to the introduction of LAGIC; whilst the runoff scenario previously covered by this standard is no longer required, we do not have an issue with retaining the same structure. However, we have no feedback regarding the content of the standard.

LPS 115 (Capital Adequacy: Insurance Risk Charge)

We believe the current standard is not in need of significant near-term review or upgrade and remains suitable in current condition.

Any meaningful review of the structure and content of this standard would likely require a more substantial consultation process and broad-based industry and professional consideration.

LPS 360 (Termination Values, Minimum Surrender Values and Paid-up Values)

Overall

Other than one issue noted below (discount rates) we would not suggest or propose any changes to the requirements of this standard.

While the standard is more prescriptive than principles based, compared to more contemporary standards, and in place references older life tables (such as A1924-29), which could theoretically be updated, there are a number of practical reasons why changes to update the standard are not warranted at this time:

1. The parts of the standard that might be updated relate to business that is now legacy business, closed for many years. The issues around early year poor surrender values are now largely past.
2. It is our understanding that most life insurers pay surrender values greater than the minimums on their mature conventional portfolio (e.g. via terminal bonus); that is the case for Resolution Life too. Any changes to the standard would require industry to make changes to legacy administration systems (to check against a changed minimum), which would be costly (including for participating policyholder expense charges) for no net benefit.
3. The contemporary management of traditional portfolios, by industry participants including Resolution Life, focuses on optimising policyholder outcomes, including adopting hedging strategies to limit financial risk and ALM mismatch while supporting policyholder outcomes. An elevated "minimum surrender value" floor reduces ALM flexibility and would detract from overall policyholder outcomes.

Discount rates

We note that the standard specifies fixed discount rates for use in the calculation of certain traditional policy values. As interest rates change over time, calculated values will remain stable due to the use of these fixed interest rates. As the traditional portfolios age and premium income declines, the surrender value calculations become dominated by the discount rate and remaining term to maturity.

While the fixed rates in the standard have not been an issue in recent years and remain reasonable given current interest rates, a significant increase in market interest rates and bond rates as seen in the late 1980's and early 1990's could raise some difficulties. This could drive an exit from long dated fixed interest at the wrong time of the cycle, leading to reduced long term outcomes and inequitable treatment of longer term policyholders to support elevated short term surrender values.

Consideration could be given to amending the standard to allow APRA the discretion to set an alternative interest rate if needed or specify a discount rate of the greater of the current rates and, say, the 10-year bond rates less relevant tax rate. We would be pleased to provide further input on this if APRA is willing to consider this issue.

LPS 370 (Cost of Investment Performance Guarantees)

No feedback regarding this standard.

Should you have any questions on Resolution Life's submission, please reach out to me at

[REDACTED]

Yours sincerely,

[REDACTED]

Greg Martin

Appointed Actuary, Resolution Life Australasia Limited