



## Prudential Standard GPS 320

### Actuarial and Related Matters

#### **Objective and key requirements of this Prudential Standard**

This Prudential Standard sets out the roles and responsibilities of a general insurer's Appointed Actuary and Level 2 insurance group's Group Actuary (Actuary). It also sets out the obligations of a general insurer and Level 2 insurance group to make arrangements to enable the Actuary to fulfil their responsibilities.

The ultimate responsibility for providing impartial advice in relation to the operations, financial condition and insurance liabilities of a general insurer or Level 2 insurance group rests with the Actuary. This advice is designed to assist the Board and senior management in carrying out their responsibility for the sound and prudent management of the general insurer or Level 2 insurance group.

The key requirements of this Prudential Standard include:

- the general insurer or Level 2 insurance group must make arrangements to enable the Actuary to undertake their roles and responsibilities;
- the Actuary must prepare the reports required in accordance with the requirements of and timeframes specified in this Prudential Standard;
- for the purposes of the capital standards and reporting requirements under the *Financial Sector (Collection of Data) Act 2001*, a general insurer's or Level 2 insurance group's insurance liabilities must be valued in accordance with this Prudential Standard;
- a general insurer must arrange to have the Insurance Liability Valuation Report of its Appointed Actuary peer reviewed by another actuary; and
- the general insurer or Level 2 insurance group must submit to APRA all reports required to be prepared by its Actuary.

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## Authority

1. This Prudential Standard is made under section 32 of the *Insurance Act 1973* (the Act) and includes a determination made under subsection 7(1) of the Act.

## Application

2. This Prudential Standard applies to each:
  - (a) **general insurer** authorised under the Act (insurer); and
  - (b) **Level 2 insurance group** as defined in *Prudential Standard GPS 001* (GPS 001).

Where a requirement applies to a Level 2 insurance group, the requirement is imposed on the **parent entity** of the Level 2 insurance group.

3. This Prudential Standard includes requirements that apply to all actuaries appointed under the Act.<sup>1</sup> These requirements are functions of an actuary for the purposes of 49K(1)(a) of the Act.
4. This Prudential Standard applies to insurers and Level 2 insurance groups (**regulated institutions**) from 1 January ~~2013~~2015.
5. Where specifically indicated in this Prudential Standard, certain requirements may be complied with on a **Level 2 insurance group** basis.

## Level 2 insurance groups

6. Paragraphs 8 to 78 apply to insurers only. Paragraphs 79 to 80 apply to all regulated institutions. Attachment C sets out additional requirements for Level 2 insurance groups including the requirement to appoint a **Group Actuary**.<sup>2</sup>

## Interpretation

7. Terms that are defined in GPS 001 appear in bold the first time they are used in this Prudential Standard.

## Obligations of an insurer

8. Under the Act, an insurer must appoint an actuary (**Appointed Actuary**).<sup>3</sup>
9. Under the Act, APRA may exempt an insurer from the requirement to appoint an Appointed Actuary.<sup>4</sup>
10. An insurer must make arrangements that are necessary to enable its Appointed Actuary to undertake their functions as required by the Act<sup>5</sup> and prudential

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<sup>1</sup> Refer to section 39 of the Act.

<sup>2</sup> Attachment C requires a Level 2 insurance group to follow the requirements for Insurance Liability Valuation in Attachment A. Attachment B applies to insurers only.

<sup>3</sup> Refer to section 39 of the Act and *Prudential Standard CPS 520 Fit and Proper* (CPS 520).

<sup>4</sup> Refer to paragraph 7(1)(c) of the Act.

standards made under the Act. These arrangements include ensuring that an insurer's Appointed Actuary is fully informed of all **prudential requirements** applicable to the insurer. These arrangements also include ensuring that an insurer's Appointed Actuary is provided with any other information that:

- (a) APRA has provided to the insurer and may assist the Appointed Actuary in performing their duties; and
  - (b) has been requested by the Appointed Actuary in performing their duties.
11. An insurer must ensure that its Appointed Actuary has access to all relevant data, information, reports and staff of the insurer (and must take all reasonable steps to ensure access to contractors of the insurer) that its Appointed Actuary reasonably believes is necessary to fulfil their responsibilities. This will include access to the insurer's **Board** and Board ~~Audit Committee~~committees, if any.<sup>6</sup>
12. Under the Act, an insurer must submit to APRA all reports required to be prepared by its Appointed Actuary.<sup>7</sup> An insurer must submit to APRA:
- (a) reports relating to a special purpose review in accordance with the time specified in paragraph 44; and
  - (b) unless otherwise specified under paragraph 25 or paragraph 40, other reports<sup>8</sup>:
    - (i) for **financial years** ending up to and including 31 March 2014, within four months of the end of the insurer's financial year; or
    - (ii) for financial years ending after 31 March 2014, within three months of the end of the insurer's financial year.<sup>9</sup>
13. Prior to submitting to APRA an Insurance Liability Valuation Report prepared by its Appointed Actuary, an insurer must ensure that the Insurance Liability Valuation Report has been peer-reviewed by another actuary (**Reviewing Actuary**).
14. Where an insurer is exempt from the requirement to have an Appointed Actuary, the insurer is not:
- (a) required to submit the reports required to be prepared by an Appointed Actuary; and
  - (b) subject to the requirements for peer review.

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<sup>5</sup> Refer to section 49K of the Act.

~~<sup>6</sup> Category C insurers are excluded from the requirement to have a Board Audit Committee, under Prudential Standard CPS 510 Governance (CPS 510).~~

<sup>7</sup> Refer to section 49L of the Act.

<sup>8</sup> This Prudential Standard sets out further detail regarding these reports.

<sup>9</sup> In exceptional cases, an insurer may apply to APRA to extend the time within which these reports are to be provided to APRA.

However, for the purposes of the **capital standards** and reporting requirements under the *Financial Sector (Collection of Data) Act 2001* (Collection of Data Act), the insurer must still value its insurance liabilities in accordance with this Prudential Standard. The value of the insurance liabilities is the sum of the central estimate and the risk margin for both outstanding claims liabilities and premiums liabilities for all classes of business written by an insurer. Attachment A provides further detail on the requirements of this insurance liability valuation.

### Exemption from requirement to appoint an actuary

15. A **small insurer** is exempt<sup>10</sup> from the requirement in paragraph 39(1)(b) of the Act to appoint an actuary when:
  - (a) the insurer has provided APRA with documentary evidence that the criteria to be a small insurer under GPS 001 have been met; and
  - (b) the insurer has attested to APRA, in writing, that it will meet these same criteria for the next 12 months. The chief executive officer (CEO)<sup>11</sup> of the insurer must provide this attestation.
16. In cases where APRA considers a small insurer to have a material amount of long-tail business inconsistent with the definition of a small insurer under GPS 001, APRA may notify the insurer in writing that APRA considers that:
  - (a) this criterion has not been satisfied; and
  - (b) the insurer is not exempt from the requirement to appoint an actuary.
17. To maintain the exemption, the CEO<sup>12</sup> of an insurer must annually attest to APRA, in writing, that the insurer:
  - (a) has met the criteria to be a small insurer under GPS 001 for the previous 12 months; and
  - (b) expects to meet these same criteria for the following 12 months.
18. Where an insurer fails to meet the criteria to be a small insurer under GPS 001, APRA may apply transition arrangements to the insurer for it to progressively meet the full actuarial requirements of this Prudential Standard. APRA may agree these transition arrangements with such insurers on a case-by-case basis. In agreeing these transition arrangements, APRA may take into account an insurer's rate of growth, which will be considered against both historic growth and expected growth according to the insurer's **Business Plan**.
19. An insurer may also be exempt from the requirement to appoint an actuary where APRA considers that the exceptional circumstances of the case merit an

<sup>10</sup> The exemption is pursuant to a determination made under subsection 7(1) of the Act at the time this Prudential Standard was determined.

<sup>11</sup> By whatever name called, or for a Category C insurer, the local equivalent.

<sup>12</sup> By whatever name called, or for a Category C insurer, the local equivalent.

exemption. An insurer may apply to APRA for an individual exemption under section 7 of the Act where it is of the view that its circumstances merit an exemption.

20. Notwithstanding any exemption, APRA may at any time require an insurer to commission, at the insurer's expense, an independent actuarial investigation of its insurance liabilities in accordance with the Act.<sup>13</sup> The insurer must appoint an actuary for this purpose who meets the criteria specified in the Act<sup>14</sup> and the criteria for an Appointed Actuary in *Prudential Standard CPS 520 Fit and Proper* (CPS 520).

### **Role and responsibilities of the Appointed Actuary (other than of a run-off insurer)**

21. In addition to and without derogation from the role of an Appointed Actuary as provided for under the Act<sup>15</sup>, an Appointed Actuary's primary roles are to provide:
- (a) advice on the valuation of an insurer's insurance liabilities; and
  - (b) an impartial assessment of the overall financial condition of the insurer.

An insurer may also seek the advice of its Appointed Actuary in relation to other matters where the insurer considers this to be appropriate.

22. An Appointed Actuary must, on an annual basis (subject to paragraph 23), undertake an investigation to enable the preparation of the reports as required by this Prudential Standard.<sup>16</sup> These reports are:
- (a) the 'Financial Condition Report' (FCR); and
  - (b) the 'Insurance Liability Valuation Report' (ILVR) (which may form part of the FCR).
23. APRA may, in writing, specify that an FCR or ILVR (or both) in respect of an insurer are to be prepared:
- (a) more frequently than as required in paragraph 22 if, having regard to the particular circumstances of the insurer, APRA considers it necessary or desirable to obtain the reports more frequently for the purposes of the prudential supervision of the insurer; or
  - (b) less frequently than as required in paragraph 22 if, having regard to the particular circumstances of the insurer, APRA considers it unnecessary to obtain the reports on an annual basis for the purposes of the prudential supervision of the insurer.

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<sup>13</sup> Refer to section 49E of the Act.

<sup>14</sup> Refer to section 49G of the Act.

<sup>15</sup> Refer to section 49K of the Act.

<sup>16</sup> Refer to paragraphs 49K(1)(a) and (b) of the Act.

24. An Appointed Actuary must provide the FCR and ILVR to the insurer within such time as to give the Board of the insurer a reasonable opportunity to:
- (a) consider and use the FCR and ILVR in preparing the insurer's yearly statutory accounts;
  - (b) provide the ILVR to the Reviewing Actuary for the purpose of peer review; and
  - (c) provide the FCR and ILVR to APRA within the time specified in paragraph 12.
25. Where APRA has specified that an FCR or an ILVR (or both) are to be prepared more or less frequently under paragraph 23, APRA may also specify, in writing, the time within which:
- (a) the Appointed Actuary must provide the reports to the insurer; and
  - (b) the insurer must provide the reports to APRA.<sup>17</sup>

In doing so, APRA will have regard to the particular circumstances of the insurer and the need to obtain the reports for the purposes of the prudential supervision of the insurer.

#### *Insurance Risk Charge*

26. For the purposes of *Prudential Standard GPS 115 Capital Adequacy: Insurance Risk Charge* (GPS 115), the Appointed Actuary must determine the most appropriate category or categories in which to assign 'other' insurance business that does not fit within the definition of the classes of business in GPS 001.
27. The Appointed Actuary must document in the ILVR the reasons and method used for selecting the specific category or categories to which the 'other' insurance business has been assigned.

#### *Insurance Concentration Risk Charge*

28. Where the insurer is required to determine the natural perils horizontal requirement for the purposes of *Prudential Standard GPS 116 Capital Adequacy: Insurance Concentration Risk Charge* (GPS 116), the Appointed Actuary must determine the portion of net premiums liabilities which relates to catastrophic losses (PL offset) using the method prescribed in GPS 116.
29. Where the insurer is required to determine the other accumulations vertical requirement under GPS 116, the Appointed Actuary must determine the amount of losses within the other accumulations scenario that has already been allowed for in the insurer's net premiums liabilities.
30. For a **lenders mortgage insurer** (LMI) that is required to determine the Lenders Mortgage Insurance Concentration Risk Charge under GPS 116, the

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<sup>17</sup> Refer to paragraph 49L(1)(b) of the Act.

Appointed Actuary must determine the amount of net premiums liabilities that relates to an economic downturn.

31. The Appointed Actuary must:
- (a) provide the information required in paragraphs 28 to 30 in a timely manner that allows the insurer to lodge reporting forms to APRA within the timeframes specified by reporting standards made under the Collection of Data Act; and
  - (b) comment in the ILVR on the method and approach taken to calculate the amounts required in paragraphs 28 to 30.

### Run-off insurers

32. Paragraphs 33 to 41 relate to a run-off insurer and its Appointed Actuary.
33. In addition to and without derogation from the role of an Appointed Actuary as provided for under the Act<sup>18</sup>, the primary roles of the Appointed Actuary of a run-off insurer are to provide:
- (a) advice on the valuation of the insurer's insurance liabilities; and
  - (b) an impartial review of the insurer's run-off plan.

An insurer may also seek the advice of its Appointed Actuary in relation to other matters where the insurer considers this to be appropriate.

34. The Appointed Actuary must, on an annual basis (subject to paragraph ~~38~~44), undertake an investigation to enable the preparation of the reports as required by this Prudential Standard.<sup>19</sup> These reports are:
- (a) the report on the review of the insurer's run-off plan; and
  - (b) the ILVR.
35. The Appointed Actuary must review the run-off plan and provide a report indicating the Appointed Actuary's opinion as to whether the run-off plan and the supporting financial projections are reasonable and adequate having regard to the nature of the insurer, its historical performance and expected future trends in the industry.
36. Where the Appointed Actuary believes the assumptions made in the run-off plan and the supporting financial projections are not reasonable or adequate, the Appointed Actuary must propose recommendations designed to address the issues.

<sup>18</sup> Refer to section 49K of the Act.

<sup>19</sup> Refer to paragraphs 49K(1)(a) and (b) of the Act.



37. The report on the review of the run-off plan must include the matters listed in the right column of the table at Attachment A of *Prudential Standard GPS 110 Capital Adequacy (GPS 110)*~~220~~.
38. APRA may, in writing, specify that the report on the review of the insurer's run-off plan or ILVR (or both) in respect of an insurer are to be prepared less frequently than as required in paragraph 34 if, having regard to the particular circumstances of the insurer, APRA considers it unnecessary to obtain the reports on an annual basis for the purposes of the prudential supervision of the insurer.
39. An Appointed Actuary must provide the report of a review of the insurer's run-off plan and ILVR to the insurer within such time as to give the Board of the insurer a reasonable opportunity to:
- (a) consider and use the report of a review on the insurer's run-off plan and ILVR in preparing the insurer's yearly statutory accounts;
  - (b) provide the ILVR to the Reviewing Actuary for the purpose of peer review; and
  - (c) provide the report of a review of the insurer's run-off plan and ILVR to APRA within the timeframe specified in paragraph 12.
40. Where APRA has specified that the report on the review of the insurer's run-off plan or an ILVR (or both) are to be prepared less frequently under paragraph 38, APRA may also specify, in writing, the time within which:
- (a) the Appointed Actuary must provide the reports to the insurer; and
  - (b) the insurer must provide the reports to APRA.<sup>20</sup>
- In doing so, APRA will have regard to the particular circumstances of the insurer and the need to obtain the reports for the purposes of the prudential supervision of the insurer.
41. For run-off insurers seeking to repatriate capital, the liability valuation must be assessed at a higher level of sufficiency. This is explained in greater detail in *Prudential Standard GPS 110 Capital Adequacy* (GPS 110).

### Special purpose review

42. When APRA specifies in writing, an Appointed Actuary must:
- (a) undertake a special purpose review of matters specified by APRA relating to the insurer's operations, risk management or financial affairs; and
  - (b) prepare a report in respect of that review.<sup>21</sup>

<sup>20</sup> Refer to paragraph 49L(1)(b) of the Act.

<sup>21</sup> Refer to paragraphs 49K(1)(a) and (b) and subsection 49K(3) of the Act.

43. The review must be completed with regard to any relevant professional standards issued by the Institute of Actuaries Australia (as appropriate to the nature of the special purpose review), to the extent that they are not inconsistent with the requirements of this Prudential Standard. Where APRA considers, having regard to the nature of the insurer's operations and the purpose of the special purpose review, that the review should not be completed with regard to those professional standards, APRA may advise the insurer in writing that an alternative standard must be used.
44. The cost of a special purpose review will be borne by the insurer. The Appointed Actuary must submit the report to APRA and the insurer simultaneously within three months of the review being commissioned unless APRA requires that the report be supplied within a shorter period, or APRA grants an extension of time in writing.

### **Non-routine reporting by Appointed Actuaries**

45. The Act specifies certain circumstances where Appointed Actuaries are required to report to APRA on a non-routine basis.<sup>22</sup> This may be where:
- (a) APRA requests specific information; or
  - (b) an Appointed Actuary has information that is specified in the Act or information they consider would assist APRA in performing its functions.
46. APRA may require an Appointed Actuary to provide information, or to produce books, accounts or documents, about an insurer if it will assist APRA in performing its functions under the Act.<sup>23</sup> To ensure that an Appointed Actuary is able to comply with any such request from APRA, the Appointed Actuary must retain all working papers and other documentation in relation to the insurer for a period of seven years after the date of the report to which the working papers or documentation relate, as required under the *Corporations Act 2001*.
47. In assessing whether the interests of policyholders may be materially prejudiced<sup>24</sup>, an Appointed Actuary must not consider a single activity or a single deficiency only in isolation. Policyholder interests may be materially prejudiced by a number of activities or deficiencies that may not individually result in a material threat to policyholder interests but, when considered in total, do amount to a material threat. In such cases, the Appointed Actuary must provide such information to APRA as required under the Act if they have reasonable grounds for believing that the interests of policyholders may be materially prejudiced.<sup>25</sup>

<sup>22</sup> Refer to sections 49 and 49A of the Act for details of these requirements. -See also section 49B of the Act in relation to voluntary reporting.

<sup>23</sup> Refer to section 49 of the Act.

<sup>24</sup> Within the meaning of paragraph 49A(2)(d) of the Act.

<sup>25</sup> Refer to subsection 49A(2) of the Act.

48. In most cases, matters reported to APRA by an Appointed Actuary must also be reported by the Appointed Actuary to the insurer to which the matter relates.<sup>26</sup> An Appointed Actuary must not notify the insurer where:
- (a) the Appointed Actuary considers that, by doing so, the interests of policyholders would be jeopardised; or
  - (b) there is a situation of mistrust between the Appointed Actuary and the Board or senior management of the insurer.
49. An Appointed Actuary who is required to provide information to APRA on a non-routine basis<sup>27</sup> is not excused from such a requirement on the grounds that doing so would tend to incriminate them or make them liable to a penalty.<sup>28</sup> Certain protection is provided under the Act<sup>29</sup> to Appointed Actuaries who supply information to APRA in these circumstances.

### **Meetings with Appointed Actuaries**

50. APRA liaison with an Appointed Actuary will normally be conducted under trilateral arrangements involving:
- (a) APRA;
  - (b) the insurer; and
  - (c) the insurer's Appointed Actuary.
51. Any one of these parties may initiate a meeting or discussion when the party considers it necessary. Notwithstanding the trilateral relationship, APRA and an insurer's Appointed Actuary may meet on a bilateral basis where either party considers this to be necessary.

### **Financial Condition Report**

52. An Appointed Actuary must prepare an FCR.<sup>30</sup> The FCR must:
- (a) be addressed to the Board of the insurer;
  - (b) provide the Appointed Actuary's objective assessment of the overall financial condition of the insurer; and
  - (c) be presented in a form that enables the Board and senior management to use the FCR as an input into decision making in respect of the operations of the insurer.

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<sup>26</sup> Note the operation of section 38E of the Act in relation to disclosure of certain information to directors and officers of the insurer.

<sup>27</sup> Refer to sections 49 or 49A of the Act.

<sup>28</sup> Refer to subsection 38F(1) of the Act.

<sup>29</sup> Refer to section 49C and subsection 38F(2) of the Act.

<sup>30</sup> Refer to paragraph 49K(1)(b) and subsection 49K(3) of the Act.

53. Paragraph 52 does not apply to the Appointed Actuary of a run-off insurer provided that:
- (a) the run-off insurer prepares a run-off plan; and
  - (b) the Appointed Actuary prepares a report of the review of the run-off plan.

Where APRA is of the view that a run-off plan is not adequate in a particular case, APRA may, in writing, require that the Appointed Actuary prepare an FCR in accordance with this Prudential Standard in respect of the run-off insurer.

54. The FCR must be:
- (a) prepared on an annual basis; and
  - (b) provided to the insurer within the time required by paragraph 24 (unless APRA requires more regular or less frequent reporting under paragraph 23).

55. In preparing an FCR, an Appointed Actuary must have regard to relevant professional standards issued by the Institute of Actuaries of Australia, to the extent that they are not inconsistent with the requirements of this Prudential Standard. In the event of any inconsistency arising from application of the professional standards and this Prudential Standard, the requirements of this Prudential Standard prevail.

56. An FCR must include (but need not be limited to) the matters listed in Attachment B.

57. The Appointed Actuary must consider the future implications and outlook for each of the matters listed in Attachment B. Where these implications are adverse, the Appointed Actuary must propose recommendations designed to address the issues.

58. As a general rule, an Appointed Actuary must complete an FCR in respect of each insurer. An insurer may submit to APRA an FCR in respect of its insurance group where:

- (a) the Appointed Actuary completing the FCR is the Appointed Actuary for each insurer included in the insurance group FCR; or
- (b) it is practical to produce a single over-arching FCR.

59. This insurance group FCR must adequately consider and address the operations of each insurer within that insurance group. Where APRA is of the view that the insurance group FCR does not adequately address the operations of each insurer or that a separate FCR is desirable to ensure that the requirements of this Prudential Standard are met, APRA may, in writing, do either or both of the following:

- (a) require the Appointed Actuary to prepare and submit to APRA a separate FCR for one or more insurers within the insurance group; and/or
  - (b) require the preparation and submission to APRA of an FCR for a different insurance group within the **corporate group** by a time specified by APRA.
60. For Category C insurers, the Appointed Actuary must prepare the FCR in respect of the Australian branch operation, but with consideration given to the financial position of the head office.

### Valuation of insurance liabilities

61. An insurer must value its insurance liabilities in accordance with this Prudential Standard, whether or not the insurer is required to have an Appointed Actuary. For further details on this valuation, refer to Attachment A. The valuation must then be used for the purpose of:
- (a) calculating the insurer's **prescribed capital amount** in accordance with the capital standards; and
  - (b) completing the insurer's yearly statutory accounts in accordance with reporting standards made under the Collection of Data Act.
62. Where an insurer includes in its yearly statutory accounts a value for insurance liabilities which is inconsistent with the advice of its Appointed Actuary, the insurer must notify APRA in writing at the same time it submits its yearly statutory accounts to APRA. This written notification must include:
- (a) the reasons for not accepting the Appointed Actuary's advice; and
  - (b) where relevant, details of the alternative assumptions and methodologies used for determining the value of the insurance liabilities.

### Insurance Liability Valuation Report

63. An Appointed Actuary must prepare an ILVR on an annual basis and provide that ILVR to the insurer within the time required by paragraph 24.<sup>31</sup>
64. The ILVR must:
- (a) be addressed to the Board of the insurer; and
  - (b) provide the Appointed Actuary's advice in respect of the value of the insurer's insurance liabilities, determined in accordance with this Prudential Standard.
65. In preparing an ILVR, an Appointed Actuary must have regard to professional standards issued by the Institute of Actuaries of Australia, to the extent that they are not inconsistent with the requirements of this Prudential Standard. In the

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<sup>31</sup> Refer to paragraph 49K(1)(b), subsection 49K(3) and paragraph 49L(b) of the Act.

event of any inconsistency arising from application of the professional standards and this Prudential Standard, the requirements of this Prudential Standard prevail.

66. The ILVR must, in respect of each class of business underwritten by the insurer, provide details (or abbreviated details for classes of business that are not material) of the matters listed in paragraph 55 of Attachment A.
67. The Appointed Actuary must, at least annually, reassess the appropriateness of the assumptions and valuation methods used to determine the insurance liabilities of the insurer. Where a change in assumptions or method is made, the effects of that change on the value of the insurance liabilities must:
  - (a) emerge in the current calculation period; and
  - (b) not be spread over future calculation periods.

The effects must be disclosed in the ILVR.

68. The ILVR must provide sufficient information in relation to the assumptions and methods used for the valuation of liabilities so that another actuary reading the ILVR will be able to obtain a sound understanding of:
  - (a) the valuation process and results;
  - (b) any inherent limitations in the process and results; and
  - (c) the key risks pertaining to the insurance liabilities of the portfolio.
69. An Appointed Actuary must ensure that results are not presented in a way that gives the impression of greater reliability than is actually the case. This particularly applies in situations where materially different results could reasonably be justified.

### **Peer review**

70. An insurer must arrange to have the ILVR prepared by the Appointed Actuary peer reviewed by a Reviewing Actuary. An insurer may apply to APRA for an exemption from this requirement where its exceptional circumstances merit an exemption. An exemption may be subject to any specified period of time or other conditions as APRA deems appropriate to the insurer's circumstances.
71. The FCR or a report of the review of a run-off plan is not required to be subject to review by the Reviewing Actuary. However, an insurer may choose to have the FCR or a report of the review of a run-off plan subject to peer review if the insurer considers it appropriate to do so.
72. An insurer must ensure that its Reviewing Actuary meets the eligibility and fit and proper criteria required to be met by Appointed Actuaries.<sup>32</sup> Where APRA does not consider that the Reviewing Actuary meets these criteria, APRA may,

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<sup>32</sup> Refer to CPS 520.

in writing, require that the insurer engage an alternate actuary to conduct the peer review.

73. The insurer must take all practical steps to ensure that the Reviewing Actuary is given full access to the insurer's Appointed Actuary and the ILVR, including appendices. Where the Reviewing Actuary believes the provision of further information is necessary, the insurer must provide access to other items on file supporting the report, relevant source data and staff or relevant contractors. The insurer must provide all information electronically if available in this form. This will include informing the Reviewing Actuary of all prudential requirements applicable to the insurer.
74. An insurer must ensure that its Reviewing Actuary prepares a report (review report) that:
  - (a) is addressed to either the insurer or the insurer's **Appointed Auditor**; and
  - (b) provides an assessment of the reasonableness of the Appointed Actuary's investigations and report(s) (including the results specified within).
75. The insurer must ensure that its Reviewing Actuary provide copies of the review report to its:
  - (a) Appointed Actuary;
  - (b) Appointed Auditor; and
  - (c) Board and senior management of the insurer

within the time specified by paragraph 76. The review report is not required to be provided to APRA but the insurer must make it available to APRA upon request.
76. The insurer must ensure that the Reviewing Actuary provides copies of the review report to the parties referred to in paragraph 75:
  - (a) for financial years up to and including 31 March 2014, within four months of the insurer's financial year; or
  - (b) for financial years ending after 31 March 2014, within three months of the end of the insurer's financial year.
77. The review report must have regard to relevant professional standards issued by the Institute of Actuaries of Australia, to the extent that they are not inconsistent with the requirements of this Prudential Standard. In the event of any inconsistency arising from application of the professional standards and this Prudential Standard, the requirements of this Prudential Standard prevail.
78. An insurer must ensure that a review report includes:

- (a) a description of the scope of the review, including details of the investigations and the reports being reviewed and the processes followed in the review;
- (b) a description of the extent to which the Reviewing Actuary had access to relevant data, information, reports and staff (and contractors) of the insurer, and to the Appointed Actuary;
- (c) an assessment of the appropriateness to the ILVR of the data, information and reports to which the Reviewing Actuary had access; and
- (d) an assessment of the reasonableness of the Appointed Actuary's investigations and report(s) (including the results specified within).

### Adjustments and exclusions

79. APRA may, by notice in writing to a regulated institution, adjust or exclude a specific requirement in this Prudential Standard in relation to that regulated institution.

### Determinations made under previous prudential standards

80. An exercise of APRA's discretion with respect to actuarial matters (such as an approval, waiver or direction) under a previous version of an actuarial prudential standard continues to have effect as though exercised pursuant to a corresponding power (if any) exercisable by APRA under this Prudential Standard.<sup>33</sup> ~~For the purposes of this paragraph, a 'previous version of an actuarial prudential standard' includes:~~

- ~~(a) Prudential Standard GPS 310 Audit and Actuarial Valuation and Reporting (GPS 310) made on 18 June 2010;~~
- ~~(b) GPS 310 made on 23 June 2008;~~
- ~~(c) GPS 310 made on 9 February 2006;~~
- ~~(d) Prudential Standard GPS 311 Audit and Actuarial Reporting and Valuation: Level 2 Insurance Groups (GPS 311) made on 23 September 2011; and~~
- ~~(e) GPS 311 made on 17 December 2008.~~

<sup>33</sup> The continuation of an exercise of APRA's discretion with respect to audit matters under a previous version of *Prudential Standard GPS 310 Audit and Actuarial Valuation and Reporting* is captured in *Prudential Standard GPS 310 Audit and Related Matters*.



## Attachment A

### Insurance Liability Valuation

1. Where an insurer is required to have an Appointed Actuary, it is the role of the Appointed Actuary to provide advice to the insurer in respect of the value of the insurer's insurance liabilities. This advice must be included in an ILVR.
2. This Attachment sets out requirements relating to the measurement and reporting of insurance liabilities that must be considered by insurers and Appointed Actuaries in determining or providing advice in respect of an insurer's insurance liabilities. Requirements for the measurement and reporting of insurance liabilities for Level 2 insurance groups are set out in Attachment C of this Prudential Standard.<sup>34</sup> In relation to data, materiality and uncertainty, Appointed Actuaries must comply with paragraphs 4 to 14 of this Attachment when preparing an ILVR. The remainder of this Attachment must be complied with by:
  - (a) all insurers in relation to the valuation of their insurance liabilities (whether or not the insurer is required to have an Appointed Actuary); and
  - (b) all Appointed Actuaries when preparing an ILVR.
3. Where an Appointed Actuary has provided the insurer with any other actuarial report in relation to liability valuation during the preceding 12 months, the Appointed Actuary must note this in the ILVR and attach the actuarial report to the ILVR where relevant. An Appointed Actuary must exercise judgement in the amount of detail included in the ILVR in respect of advice already given.

### Data

4. An insurer must make the arrangements that are necessary to enable its Appointed Actuary to prepare an ILVR.<sup>35</sup> The Appointed Actuary must therefore advise the insurer of:
  - (a) the data, information and reports that the Appointed Actuary will need; and
  - (b) staff and relevant contractors of the insurer with whom the Appointed Actuary will need to consult

in order to prepare the ILVR. Where the insurer does not provide adequate and timely access to data, information, reports and staff as required, the Appointed Actuary may omit from the ILVR, analysis that is dependent on that information but must provide details as to why it has been omitted and explain any consequential limitations of the ILVR.

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<sup>34</sup> The Level 2 insurance group must also value its insurance liabilities in a manner that is consistent with this Attachment.

<sup>35</sup> Refer to subsection 49K(2) of the Act.

5. The Appointed Actuary must take reasonable steps to verify the consistency, completeness and accuracy of the data provided by the insurer with reference to the insurer's financial and other records. The Appointed Actuary must specify in the ILVR:
  - (a) any discrepancies that cannot be resolved with the insurer; and
  - (b) any consequent limitations of the ILVR.
6. The Appointed Actuary must be familiar with:
  - (a) the administration and accounting procedures for policies and claims for the insurer; and
  - (b) the characteristics of the insurance policies and claim processes that may materially impact upon the estimation of insurance liabilities.
7. The Appointed Actuary must be familiar with, or obtain advice on, the economic, technological, medical, legal and social trends within the broader community that may impact upon the value of insurance liabilities.
8. The Appointed Actuary must explain in the ILVR together with any consequent limitations of the ILVR, the degree to which the Appointed Actuary relies on:
  - (a) data, information or reports provided by the insurer; or
  - (b) testing of the data or other information by the insurer's internal auditor, Appointed Auditor or other external auditor.
9. Where the Appointed Actuary is relying on work undertaken by other actuaries, the Appointed Actuary must be satisfied as to the suitability of assumptions and methods used by the other actuaries. Where the Appointed Actuary is not satisfied, the Appointed Actuary must use alternative methods and explain them in the ILVR.

### **Materiality**

10. The Appointed Actuary must take into account materiality when preparing an ILVR. Where information, if misstated or omitted, would cause the results or opinions of the Appointed Actuary to be misleading to users of the ILVR, that information would be considered material.<sup>36</sup> Whether something is material or not will always be a matter for an Appointed Actuary's judgement.

### **Uncertainty**

11. The Appointed Actuary must:
  - (a) describe, qualitatively, the key drivers of uncertainty for each class of business or portfolio being valued; and

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<sup>36</sup> 'Materiality' for this purpose is independent of materiality within the meaning of Australian Accounting Standards.

- (b) explain and, if appropriate, quantify in the ILVR material changes in these key drivers, or uncertainty generally, since the previous valuation.
12. The Appointed Actuary must explain by class of business in the ILVR any material changes or significant emerging experience since the previous valuation of insurance liabilities.
  13. The Appointed Actuary must explain in the ILVR the practical consequences of the uncertainty of the estimates included in the ILVR. In many cases, the range of reasonable values of the liabilities will be very large. The conclusions that may be drawn from a value at one end of this range may be very different from the conclusions drawn by a value at the other end.
  14. In addition to paragraph 13 of this Attachment, the Appointed Actuary must specifically explain in the ILVR their assessment of the uncertainty in the gross estimate of insurance liabilities. The explanation may include commentary on gross uncertainty at the 75 per cent probability of sufficiency level, or other analysis such as measures of skewness or potential gross-loss scenarios.

### **Valuation of insurance liabilities**

15. An insurer must determine a value for both its outstanding claims liabilities and its premiums liabilities for each class of business underwritten by the insurer (after taking advice from its Appointed Actuary).
16. Outstanding claims liabilities relate to all claims incurred prior to the valuation date, whether or not they have been reported to the insurer. The value of the outstanding claims liabilities must include an amount in respect of the expenses that the insurer expects to incur in settling these claims. An insurer must determine the outstanding claims liabilities on a prospective basis, both net and gross of:
  - (a) **reinsurance recoverables**; and
  - (b) **non-reinsurance recoveries**.
17. Premiums liabilities relate to all future claim payments arising from future events post the valuation date that will be insured under the insurer's existing policies that have not yet expired. The value of the premiums liabilities must include an amount in respect of the expenses that the insurer expects to incur in administering and settling the relevant claims and allow for expected premium refunds. In respect of premiums liabilities for which **reinsurance** has not yet been purchased, allowance must be made for this reinsurance in the premiums liabilities valuation (refer to paragraphs 42 to 51 of this Attachment for further details on the assumptions relating to this reinsurance). Premiums liabilities are to be determined on a prospective basis, both net and gross of:
  - (a) **expected reinsurance recoveries**; and
  - (b) non-reinsurance recoveries.

18. The value of outstanding claims liabilities and premiums liabilities must not include any Government charges imposed such as levies, duties and taxes. Also, a deferred acquisition cost asset must not be reported as part of the value of outstanding claims liabilities or premiums liabilities valued under this Prudential Standard.
19. Premiums liabilities relating to insurance and reinsurance contracts written on a long-term (or continuous) basis, with the option for the party accepting the risk to cancel the contract prior to the expiry date, must make allowance for future claims anticipated to arise from risks covered up to the next possible cancellation date. For instance, a multi-year contract may be written on the basis that it may be cancelled by the risk carrier on a particular date (cancellation date) or within a particular period (so that the earliest cancellation date may be determined). In this case, the insurer or reinsurer would need to account for premiums liabilities for any unexpired risks which may:
  - (a) arise up to and including the cancellation date; or
  - (b) remain after the cancellation date.
20. In determining the value for outstanding claims liabilities and premiums liabilities, an insurer must determine a value for the central estimate and associated risk margin by class of business (subject to considerations of materiality and the professional judgement of the Appointed Actuary). The insurer must therefore calculate and report separately to APRA, and by class of business, central estimates and risk margins for outstanding claims liabilities and premiums liabilities.<sup>37</sup> However, this should not prevent analysis being undertaken on a basis which is more suitable, taking into account the nature of the data and the particular circumstances of the insurer.
21. The valuation of insurance liabilities reflects the individual circumstances of the insurer. In any event, the minimum value of insurance liabilities must be the greater of a value that is:
  - (a) determined on a basis that is intended to value the insurance liabilities of the insurer at a 75 per cent level of sufficiency; and
  - (b) the central estimate plus one half of a standard deviation above the mean for the insurance liabilities of the insurer.
22. The principles of this Prudential Standard must be applied to the calculation of both gross and net insurance liabilities.

### *The central estimate*

23. The central estimate is intended to reflect the mean value in the range of possible values for the outcome (that is, the mean of the distribution of probabilistic outcomes). The determination of the central estimate must be

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<sup>37</sup> Such reporting is required in both an ILVR and in statutory reporting (refer to reporting standards made under the Collection of Data Act).

based on assumptions as to future experience which reflect the experience and circumstances of the insurer and which are:

- (a) made using judgement and experience;
  - (b) made having regard to available statistics and other information; and
  - (c) neither deliberately overstated nor understated.
24. Where experience is highly volatile, model parameters estimated from the experience can also be volatile. The central estimate must therefore reflect as closely as possible the likely future experience of the insurer. Judgement may be required to limit the volatility of the assumed parameters to that which is justified in terms of the credibility of the experience data.
25. The central estimate will be measured as the present value of the future expected payments. This measurement process will involve prospective calculations and modelling techniques, and will require assumptions in respect of the expected future experience, taking into account all factors which are considered to be material to the calculation, including:
- (a) discount rates;
  - (b) claims escalation;
  - (c) claims and policy management expenses; and
  - (d) claims run-off.
26. In establishing the central estimate assumptions, regard must be given to the materiality of:
- (a) the class of business being considered; and
  - (b) the effect of particular assumptions on the determined result.
27. The assumptions used must be consistent for the estimation of both outstanding claims liabilities and premiums liabilities. Where they are not, the reasons must be documented.

#### *The risk margin*

28. The risk margin is the component of the value of the insurance liabilities that relates to the inherent uncertainty that outcomes will differ from the central estimate. It is aimed at ensuring that the value of the insurance liabilities is established at an appropriate and sufficient level. The risk margin does not relate to the risk associated with the underlying assets, such as asset-liability mismatch risk.
29. Risk margins must be determined, for each class of business and in total, on a basis that reflects the experience of the insurer. In any event, the risk margins

must be valued so that the insurance liabilities of the insurer, after any diversification benefit, are not less than the greater of a value that is:

- (a) determined on a basis that is intended to value the insurance liabilities of the insurer at a 75 per cent level of sufficiency; and
  - (b) the central estimate plus one half of a standard deviation above the mean for the insurance liabilities of the insurer.
30. When selecting the methodology and assumptions to be used in determining the risk margin for a class of business, consideration should be given to a range of factors, including:
- (a) the robustness of the valuation models;
  - (b) the reliability and volume of the available data and other information;
  - (c) past experience of the insurer and the general insurance industry; and
  - (d) the particular characteristics of each class of business.
31. Estimation of a standard deviation above the mean may present technical difficulties when components of the uncertainty in the central estimate do not permit statistical analysis to be undertaken. Estimation of a standard deviation above the mean will generally require both the exercise of judgement and technical analysis.
32. The risk margin plays a role in achieving an appropriate pattern of profit emergence for a class of business. However, the risk margin must not be used as a tool for smoothing the effect of changes in assumptions or valuation methods.
33. From year to year, risk margins would generally be a similar percentage of the central estimate for each class of business, unless there has been a material change in uncertainty. Changes in uncertainty may derive from changes in a number of elements such as reinsurance arrangements, the insurer's risk profile or volume of business, or external factors (for example, legislative requirements). The Appointed Actuary must document any material changes.
34. Allowance for diversification, reinsurance or both may be made in determining the risk margin. The reporting standards made under the Collection of Data Act require the insurer to report a stand-alone risk margin and a diversified risk margin for each of the insurer's classes of business. The stand-alone risk margin refers to the risk margin that would be applied to a class of business where no allowance for diversification with other classes of business has been allowed. The diversified risk margin refers to the risk margin that has been applied to the class of business after allowance for diversification across the whole insurance portfolio. The Appointed Actuary must clearly document the justification for and method of determining such diversification allowance (which must be assessed on a holistic basis for the insurer) and **reinsurance assets**.

*Discount rates*

35. The rates to be used in discounting the expected future claims payments of insurance liabilities denominated in Australian currency for a class of business are derived from yields of Commonwealth Government Securities (CGS), as at the calculation date, that relate to the term of the future insurance liability cash flows for that class.
36. Where the term of the insurance liabilities denominated in Australian currency exceeds the maximum available term of CGS, other instruments with longer terms and current observable, objective rates are to be used as a reference point for the purpose of extrapolation. If there are no other suitable instruments, or the Appointed Actuary elects to use an instrument that does not meet this requirement, the Appointed Actuary must justify the reason for using that particular instrument in the insurer's ILVR. Adjustments must be made to remove any allowances for credit risk and illiquidity that are implicit in the yields of those instruments.
37. For foreign insurance liabilities not denominated in Australian currency, the risk-free discount rate must be based on the yields of highly liquid sovereign risk securities with current observable, objective rates, in the currency of the insurance liabilities and with counterparty grade 1. If there are no securities satisfying this requirement, or the Appointed Actuary elects to use an instrument that does not meet this requirement, the Appointed Actuary must justify the reason for using that particular instrument in the insurer's ILVR. Adjustments must be made to remove any allowances for credit risk and illiquidity that are implicit in the yields of those instruments.

*Methods for valuing insurance liabilities*

38. A method, or methods, must be adopted for valuing an insurer's insurance liabilities. Comprehensive actuarial analysis and modelling techniques should be employed, subject to considerations of materiality. The appropriateness of any method, or methods, will depend on:
  - (a) the class of business being considered;
  - (b) the nature, volume and quality of the available data in relation to the experience of the insurer and the industry;
  - (c) the circumstances of the insurer; and
  - (d) considerations of materiality.
39. Approximate methods may be used when valuing an insurer's insurance liabilities subject to the principles of this Prudential Standard, and where the result is not material or not materially different from that which would result from a full valuation process. Approximate methods may, for example, be justified for short-tail classes of business where the effect of not discounting future expected claims is not material.



40. The onus for justification of the appropriateness of any valuation method rests with:
- (a) the Board of the insurer; and
  - (b) the Appointed Actuary. Where an Appointed Actuary has been involved in the valuation of the insurance liabilities, the Appointed Actuary must explain in the ILVR the reasons for any valuation methods used.

#### *Claims escalation*

41. Appropriate allowance must be made for future claims escalation when determining the central estimates of both outstanding claims liabilities and premiums liabilities. Future claims payments may increase over current levels as a result of wages or price increases (inflation) and/or court-awarded interest, other environmental or economic causes (superimposed inflation). Claims payments include third party costs incurred in settling those claims, for example, investigation, medical and legal fees.

#### **Estimation of reinsurance recoverables**

42. The estimation of the value of the insurance liabilities may be undertaken on a gross basis, with a separate estimate of the value of reinsurance recoveries (that is, amounts expected to be recovered under the insurer's reinsurance arrangements), or on a net basis. In either case, the principles of this Prudential Standard must be applied. Where the process is undertaken on a net basis, it is still necessary to value separately the estimates of the gross insurance liabilities and the reinsurance recoverables and expected reinsurance recoveries.<sup>38</sup>

#### *Documentation of reinsurance arrangements*

43. For the purpose of calculating an insurer's insurance liabilities, it must be assumed initially that:
- (a) reinsurance arrangements are fully documented;
  - (b) reinsurance arrangements are 100 per cent placed, that is, there are no gaps in the insurer's reinsurance arrangements; and
  - (c) reinsurance recoverables and expected reinsurance recoveries will be received in full.<sup>39</sup>

Where reinsurance arrangements are not fully documented or are not fully placed, or there is a risk that reinsurance assets will not be received from a

<sup>38</sup> This is also required to comply with reporting standards made under the Collection of Data Act.

<sup>39</sup> For further detail in respect of documentation of reinsurance arrangements, refer to *Prudential Standard GPS 230 Reinsurance Management*.



reinsurer, the insurer will either not be able to recognise the reinsurance assets or will be required to hold capital against these risks.<sup>40</sup>

#### *Assessment and comment by the Appointed Actuary*

44. The Appointed Actuary<sup>41</sup> must make a specific assessment of and comment on the recoverability of reinsurance assets and expected reinsurance recoveries from **non-APRA authorised reinsurers**. The Appointed Actuary must consider all relevant matters, including:
- (a) quality of information and data available on potential reinsurance recoverables;
  - (b) credit risk;
  - (c) willingness to pay;
  - (d) documentation and placement of contracts; and
  - (e) any legal or other issues that may create an impediment to the insurer realising the reinsurance asset.
45. Aggregate reinsurance assets and expected reinsurance recoveries must be separated into subsets which identify those that derive from documented and non-documented reinsurance arrangements, those that derive from reinsurance arrangements that are fully placed and not fully placed, and those likely to be recoverable and those not likely to be recoverable from reinsurers. In providing this advice, the Appointed Actuary must consider the materiality of reinsurance assets. If they are material, the Appointed Actuary must assess the potential range of amounts not recoverable from reinsurers, based on the uncertainty of individual and aggregate gross losses. For the purposes of *Prudential Standard GPS 114 Capital Adequacy: Asset Risk Charge*, the reinsurance recoverables due from non-APRA-authorized reinsurers for each accident year must be identified in the ILVR.

#### *Treatment of reinsurance expenses and deferred reinsurance expense*

46. APRA maintains a consistent approach in allowing for the cost of all types of reinsurance arrangements. The principle is that APRA requires an insurer to ensure in all prudential reporting that reinsurance coverage matches the risk exposures in the underlying portfolio, irrespective of the type of reinsurance contract.
47. This Prudential Standard requires insurers to capitalise the cost of reinsurance at inception as **deferred reinsurance expense** (DRE), and expense that capitalised amount over the life of the reinsurance coverage. The establishment of the DRE

<sup>40</sup> Refer to reporting standards made under the Collection of Data Act for recognition of assets. Refer to *Prudential Standard GPS 112 Capital Adequacy: Measurement of Capital* (GPS 112) and GPS 110 for detail in respect of capital requirements in relation to these risks.

<sup>41</sup> If an insurer is exempt from the requirement to appoint an actuary, the insurer must make the assessment and comment as required by this paragraph.

will be associated with the establishment of a liability to pay a reinsurance premium; the liability will be reduced as payments are made. The payment of the premium occurs according to the reinsurance contract, and the expensing of the DRE occurs in accordance with the expected pattern of the incidence of risk.

48. For the calculation of premiums liabilities, the premiums liabilities must include the purchase cost for reinsurance arrangements where existing reinsurance arrangements are insufficient to fully cover the exposure period for premiums liabilities. The existence of DRE on the balance sheet indicates the existence of reinsurance that may provide partial cover for the premiums liabilities. To the extent that the current reinsurance arrangements cover the premium liability exposure, insurers are not required to include the cost of reinsurance in the premiums liabilities. However, an additional reinsurance cost must be included for any part of the premiums liabilities not covered by current reinsurance arrangements.<sup>42</sup>
49. For any part of the current reinsurance arrangements that cover future business that has not yet been written, that portion of the associated DRE asset cannot be used to reduce premiums liabilities calculated under this Prudential Standard. To the extent DRE from the underlying reinsurance is not deducted in GPS 112, the future business portion of the DRE can be used to increase the surplus (or decrease the deficit) in premiums liabilities calculated in accordance with GPS 112. This revised surplus (or deficit) is included as part of adjusted net assets in Australia for Category C insurers and the capital base for all other insurers.

*Allowance for future reinsurance expense*

50. The estimation of expected reinsurance recoveries in respect of premiums liabilities for which reinsurance has not yet been purchased can assume that the necessary reinsurance related to those liabilities will be purchased and documented. Allowance must be made for the purchase cost of this future reinsurance expense in the premiums liabilities valuation. This assumption must only be made when:
  - (a) existing reinsurance arrangements are documented;
  - (b) the estimated expected reinsurance recoveries relate to the same classes of business that are currently covered by the existing documented reinsurance arrangements; and
  - (c) it is fully expected that the reinsurance will be replaced on similar terms when current arrangements expire.

*Estimation undertaken on the combined claims experience of several classes of business*

51. The estimation of the value of reinsurance recoverables and expected reinsurance recoveries would normally be undertaken on the basis of each class of business written by the insurer. However, there are certain forms of

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<sup>42</sup> See paragraph 50 of this Attachment.

reinsurance where reinsurance assets and expected reinsurance recoveries receivable depend on the combined claims experience of several or all classes of business underwritten by the insurer. In such instances, the estimation will be required to factor in all the individual results by class of business covered by the reinsurance arrangements.

### **Non-reinsurance recoveries**

52. Non-reinsurance recoveries are amounts that may be recovered under arrangements other than reinsurance arrangements, such as salvage, subrogation and sharing agreements. The treatment of non-reinsurance recoveries must be consistent with that required by reporting standards made under the Collection of Data Act.

### **Reporting current period claims expense**

53. The reporting forms under the Collection of Data Act require the reporting of claims expense divided into two parts - current period and non-recurring. In determining the current period claims expense the approach has some important differences from that used in the valuation of insurance liabilities described above.
54. The change in outstanding claims liabilities (including risk margins) over a period, added to the net claim payments in that period, results in the net claims expense for that period. A component of the net claims expense is the current period net claims expense; this component arises from claims incurred in the current period, defined as the financial year to date. The insurer must calculate and report the value of the current period net claims expense. The remaining balance of the net claims expense represents the non-recurring component which also must be reported. Both items must be calculated by APRA class of business. The current period net claims expense must include:
- (a) gross claims payments, less any associated recoveries received and receivable, from reinsurance and non-reinsurance, including salvage, subrogation and GST recoveries;
  - (b) outstanding claims liabilities, net of any associated recoverable amounts from reinsurance and non-reinsurance, including salvage, subrogation and GST recoveries. The net outstanding claims must be determined before any allowance for discounting or risk margins; and
  - (c) claims handling expense attributable to the paid and outstanding claims incurred in the current period.

Quarterly actuarial reviews are not required to be completed specifically for the calculation of the current period net claims expense. However, the insurer should seek advice from the Appointed Actuary regarding establishing a suitable approach for its calculation.

## Matters to be included in an ILVR

55. For the purposes of paragraph 66 of this Prudential Standard, details of the following matters must be provided in an ILVR:
- (a) the value of insurance liabilities determined in accordance with this Prudential Standard;
  - (b) assumptions used in the valuation process, including the extent to which the assumptions used are based on the experience of the insurer;
  - (c) availability and appropriateness of the data;
  - (d) significant aspects of recent experience;
  - (e) the methodologies used to model the central estimates of outstanding claims liabilities and premiums liabilities;
  - (f) an assessment of the uncertainty in the gross and net central estimates;
  - (g) the sensitivity analyses undertaken;
  - (h) a description of probability distributions and parameters, or approaches adopted to estimate uncertainty if these are not specifically determined;
  - (i) risk margins (both stand-alone and diversified for each class of business)<sup>43</sup> that relate to the inherent uncertainty in the central estimate values for outstanding claims liabilities and premiums liabilities, including any relevant statistics used to derive the risk margins including standard deviations and correlations;
  - (j) a reconciliation on an accident year basis of the change since the previous valuation of the net outstanding claims liabilities, including, where possible and relevant<sup>44</sup>, separate quantification of the impact of:
    - (i) significant differences between actual and expected claims experience;
    - (ii) significant differences caused by valuation basis and/or methodology change; and
    - (iii) additional liability associated with new claims incurred since the previous valuation; and
  - (k) any other matters that a prudential standard requires to be included in the insurer's ILVR.

<sup>43</sup> As defined in paragraph 34 of this Attachment.

<sup>44</sup> The extent to which this information is relevant should be specific to the circumstances of the insurer. For example, APRA would expect larger insurers to be better equipped to conduct more analysis, and long-tail business not to be well described by claim year performance.

## Attachment B

### Matters to be included in an FCR

For the purposes of paragraph 56 of this Prudential Standard, the following matters must be included in an FCR, where relevant:

- (a) a business overview including the background, structure and operations of the insurer;
- (b) a summary of the key results of the ILVR (prepared in accordance with this Prudential Standard);
- (c) an assessment of the adequacy of past estimates for insurance liabilities (where appropriate, this may include references to the ILVR or past ILVRs);
- (d) an assessment of pricing, including adequacy of premiums;
- (e) an assessment of the insurer's recent experience and profitability, including the current year and prior year performance of its insurance portfolios and analysis of any changes in business volumes, exposures, mix of business and pricing during the year ending on the valuation date;
- (f) an assessment of asset and liability management, including the insurer's investment strategy;
- (g) an assessment of current and future capital adequacy, and a discussion of the insurer's **Internal Capital Adequacy Assessment Process (ICAAP)**, including any assumptions made and methodologies used in calculating the insurer's prescribed capital amount and capital base;
- (h) an assessment of the adequacy of the calculation of the insurer's ICRC, including an assessment of the impact of multiple events in a year for an insurer with exposures to other accumulations as defined in GPS 116;
- (i) an assessment of the suitability and adequacy of reinsurance arrangements, including the documentation of reinsurance arrangements and the existence and impact of any limited risk transfer arrangements, and whether the reinsurance arrangements are sufficient to cover the Probable Maximum Loss defined in GPS 116; and
- (j) an assessment of the suitability and adequacy of the **risk management framework** ~~as required under GPS 220~~.

## Attachment C

### Level 2 insurance groups

#### Appointment of a Group Actuary

1. A Level 2 insurance group must appoint a 'Group Actuary'. The Group Actuary of a Level 2 insurance group must:
  - (a) meet the fit and proper criteria to hold a responsible person position under CPS 520;
  - (b) have appropriate formal qualifications;
  - (c) have a minimum of 5 years relevant experience, since obtaining the qualifications referred to in paragraph (b), in the provision of actuarial services to entities carrying on insurance business and it would be prudent to conclude that the person is familiar with current issues in the provision of actuarial services to such entities;
  - (d) be a member of a recognised professional body for actuaries; and
  - (e) not be:
    - (i) the **Group Auditor**;
    - (ii) the auditor of an entity within the Level 2 insurance group carrying on insurance business;
    - (iii) an employee or director of an entity of which a person referred to in paragraph (i) or (ii) is an employee or director;
    - (iv) a partner of a person referred to in paragraph (i) or (ii); and
    - (v) the Chief Executive or a director of any entity within the Level 2 insurance group or its wider corporate group (where applicable).

#### Obligations of a Level 2 insurance group

2. A Level 2 insurance group must ensure that its Group Actuary:
  - (a) performs for the group the functions of a Group Actuary set out in this Prudential Standard and any other prudential standard; and
  - (b) prepares, and gives to the group, any reports required to be prepared by the Group Actuary under this Prudential Standard.
3. A Level 2 insurance group must:
  - (a) ensure that the reports required to be prepared by the Group Actuary deal with all the matters required by this Prudential Standard; and

- (b) lodge with APRA the reports required to be prepared by its Group Actuary under this Prudential Standard.
4. A Level 2 insurance group must make any arrangements necessary to enable its Group Actuary to undertake their functions as required by this Prudential Standard. These arrangements include ensuring that its Group Actuary is fully informed of material prudential requirements applicable to the group. These arrangements also include ensuring that the Group Actuary is provided with any other information that:
- (a) APRA has provided to the group and may assist the Group Actuary in performing their duties; and
  - (b) has been requested by the Group Actuary in performing their duties.
5. A Level 2 insurance group must ensure that its Group Actuary has access to all relevant data, information, reports and staff of the group (and must take all reasonable steps to ensure access to contractors of the group) that its Group Actuary reasonably believes are necessary to fulfil their responsibilities. This will include access to:
- (a) the Board of the parent entity;
  - (b) the Board ~~Audit Committee committees, if any,~~ of the parent entity, if any;
  - (c) the Board of any other entity within the group; and
  - (d) the Board ~~Audit Committee committees,~~ if any, of any other entity within the group.
6. A Level 2 insurance group must submit to APRA:
- (a) reports relating to a special purpose review in accordance with the time specified in paragraph 22 of this Attachment; and
  - (b) unless otherwise specified under paragraph 14 of this Attachment, other reports<sup>45</sup>:
    - (i) for **financial years** ending up to and including 31 March 2014, within four months of the end of the insurer's financial year; or
    - (ii) for financial years ending after 31 March 2014, within three months of the end of the insurer's financial year.<sup>46</sup>
7. Subject to paragraph 23 of this Attachment, APRA does not require the Insurance Liability Valuation Report of a Level 2 insurance group to be subject to external peer review.

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<sup>45</sup> This Attachment sets out further details regarding those reports.

<sup>46</sup> In exceptional cases, a Level 2 insurance group may apply to APRA to extend the time within which these reports are to be provided to APRA.

## Role and responsibilities of the Group Actuary

8. A Group Actuary's primary role is to provide advice on the valuation of the group's insurance liabilities. A Level 2 insurance group may also seek advice of its Group Actuary in relation to other matters where the group considers this to be appropriate.
9. A Level 2 insurance group must ensure that its Group Actuary, on an annual basis (subject to paragraph 12 of this Attachment), undertakes an investigation to enable the preparation of an ILVR.<sup>47</sup>
10. A Level 2 insurance group must seek the advice of its Group Actuary for an actuarial assessment of the group's insurance liabilities for each half-yearly report<sup>48</sup> submitted to APRA. There is no requirement to prepare or submit a mid-year ILVR.
11. In each ILVR, the Group Actuary must comment on the advice provided to the group in relation to the two half-yearly reports immediately preceding the date of the ILVR. Those comments should cover the extent to which the advice was accepted by the group in preparing its half-yearly reports and the extent to which the actuary has amended the valuation of insurance liabilities in the ILVR compared to the last advice given to the group for the half-yearly report at the group's balance date.
12. APRA may, in writing, specify that an ILVR in respect of a Level 2 insurance group be prepared:
  - (a) more frequently if, having regard to the particular circumstances of the group, APRA considers it necessary or desirable to obtain the ILVR more frequently for the purposes of the prudential supervision of the group; or
  - (b) less frequently if, having regard to the particular circumstances of the group, APRA considers it unnecessary to obtain the ILVR on a yearly basis for the purposes of the prudential supervision of the group.
13. The Level 2 insurance group must ensure that it provides the ILVR to APRA within the timeframe specified in paragraph 6 of this Attachment.
14. Where APRA has specified that an ILVR is to be prepared more or less frequently under paragraph 12, APRA may also specify, in writing, the time within which:
  - (a) a Level 2 insurance group must receive the report from its Group Actuary; and
  - (b) the group must provide the report to APRA.

<sup>47</sup> See requirements of paragraph 39 of this Attachment.

<sup>48</sup> Prepared with regard to reporting standards made under the *Financial Sector (Collection of Data) Act 2001*.



In doing so, APRA will have regard to the particular circumstances of the group and the need to obtain the reports for the purposes of the prudential supervision of the group.

### *Insurance Risk Charge*

15. For the purposes of *Prudential Standard GPS 115 Capital Adequacy: Insurance Risk Charge*, the Group Actuary must determine the most appropriate category or categories for 'other' insurance business that does not fit within the definition of the classes of business in GPS 001.
16. The Group Actuary must document in the ILVR the reasons for selecting the specific category or categories to which the 'other' insurance business has been assigned.

### *Insurance Concentration Risk Charge*

17. A Level 2 insurance group must ensure that its Group Actuary reviews the determination of the **Insurance Concentration Risk Charge** (ICRC) for the group and includes relevant comments on this review in the ILVR. The review should include consideration of the adequacy of the Level 2 insurance group's ICRC given the business being undertaken and the reinsurance arrangements. A Level 2 insurance group may apply to APRA to complete the annual review of the determination of the ICRC in a separate written report to the Board rather than within the ILVR.
18. For a Level 2 insurance group to determine the ICRC, the Group Actuary is required to, where appropriate:
  - (a) for the determination of any natural perils horizontal requirement, as defined in *Prudential Standard GPS 116 Capital Adequacy: Insurance Concentration Risk Charge* (GPS 116), determine the portion of the Level 2 insurance group's net premiums liabilities which relates to catastrophic losses (PL offset) using the method prescribed in GPS 116;
  - (b) for the determination of any other accumulations vertical requirement, as defined in GPS 116, determine the amount of losses within the other accumulations scenario that has already been allowed for in the Level 2 insurance group's net premiums liabilities for other accumulations; and
  - (c) for the determination of any lenders mortgage insurance concentration risk charge, as defined in GPS 116, determine the amount of net premiums liabilities that relates to an economic downturn.
19. The Group Actuary must:
  - (a) provide the information required under paragraph 18 of this Attachment, in a timely manner that allows the Level 2 insurance group to lodge reporting forms to APRA within the timeframes specified by the reporting standards made under the Collection of Data Act; and

- (b) comment in the Level 2 insurance group's ILVR on the methodology and approach taken to calculate the amounts required for paragraph 18 of this Attachment.

### **Special purpose review**

20. When APRA specifies in writing, a Group Actuary must:
  - (a) undertake a special purpose review of matters specified by APRA relating to the group's operations, risk management or financial affairs; and
  - (b) prepare a report in respect of that review.
21. The review must be completed with regard to any relevant professional standards (as appropriate to the nature of the special purpose review), to the extent that they are not inconsistent with the requirements of this Prudential Standard. Where APRA considers, having regard to the nature of the group's operations and the purpose of the special purpose review, that the review should not be completed in accordance with those professional standards, APRA may advise the insurer in writing that an alternative standard must be used.
22. The cost of a special purpose review will be borne by the Level 2 insurance group. The Group Actuary must submit the report to APRA and the Level 2 insurance group simultaneously within three months of the review being commissioned unless APRA requires that the report be supplied within a shorter period, or APRA grants an extension of time in writing.

### **Special purpose external peer review**

23. APRA may require any advice or report of the Group Actuary which is prepared in accordance with this Prudential Standard to be subject to peer review by an external actuary.<sup>49</sup> The external actuary appointed to this role, and the scope of the review, is to be agreed with APRA. The external actuary must prepare a report in respect of the review. The review must be completed with regard to any relevant professional standards. The cost of the review is to be borne by the Level 2 insurance group. The external actuary must submit the report to APRA and the Level 2 insurance group simultaneously within three months of the review being commissioned unless APRA requires that the report be supplied within a shorter period, or APRA grants an extension of time in writing.

### **Non-routine reporting by Group Actuaries**

24. A Level 2 insurance group must ensure that its Group Actuary report to APRA on a non-routine basis where APRA requests specific information or where the Group Actuary has information that they consider would assist APRA in performing its functions.<sup>50</sup>

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<sup>49</sup> The external actuary must have appropriate formal qualifications and must not be an employee of the Level 2 insurance group or its wider corporate group.

<sup>50</sup> Also note Part IV Division 2 of the Act sets out the duties of actuaries of insurers, authorised NOHCs or subsidiaries to give information to APRA.

25. If APRA requests information or documents from the Group Actuary, the Level 2 insurance group must ensure that such information or documents are provided to APRA.

### **Meetings with Group Actuaries**

26. APRA liaison with the Group Actuary of a Level 2 insurance group is normally conducted under trilateral arrangements involving:
  - (a) APRA;
  - (b) the group; and
  - (c) the Group Actuary.
27. Any one of these parties may initiate a meeting or discussion when the party considers it necessary. Notwithstanding the trilateral relationship, APRA and a Group Actuary may meet on a bilateral basis where either party considers this to be necessary.

### **Valuation of insurance liabilities**

28. A Level 2 insurance group may consist of Australian business only (insurers authorised by APRA) or may comprise both Australian and **international business**.
29. Subject to paragraph 33 of this Attachment, a Level 2 insurance group must determine the value of its insurance liabilities in a manner consistent with that set out in Attachment A. The valuation must then be used for the purpose of:
  - (a) calculating the Level 2 insurance group's **prescribed capital amount** in accordance with the capital standards; and
  - (b) completing the Level 2 insurance group's **accounts** in accordance with reporting standards made under the Collection of Data Act.
30. Where a Level 2 insurance group includes in its accounts a value for insurance liabilities which is inconsistent with the advice of its Group Actuary, the Level 2 insurance group must notify APRA in writing at the same time it submits its accounts to APRA. This written notification must include:
  - (a) the reasons for not accepting the Group Actuary's advice; and
  - (b) where relevant, details of the alternative assumptions and methodologies used for determining the value of insurance liabilities.

### *Australian business*

31. In respect of **Australian business**, the insurance liability valuation for a Level 2 insurance group should be consistent with that for an insurer under Attachment A subject to identified consolidated adjustments such as intra-group transactions and diversification. In the case of a Level 2 insurance group with only

Australian business, the valuation of group insurance liabilities must be based on the ILVR of each insurer in the group and must be compiled as follows:

- (a) the sum of the insurance liabilities for each insurer in the group; plus or minus
  - (b) consolidation adjustments for intra-group transactions (which are likely to be eliminations); plus or minus
  - (c) consolidation adjustments for diversification benefits in risk margins (if any); plus or minus
  - (d) any other adjustments the Group Actuary considers necessary to comply with this Prudential Standard.
32. On the application of the parent entity of a Level 2 insurance group, APRA may determine that the Group Actuary of the Level 2 insurance group can apply the method set out in paragraphs 33 to 37 of this Attachment in relation to its Australian business. APRA's determination may be subject to conditions.

#### *International business*

33. In the case of a Level 2 insurance group with international business, the Group Actuary must also determine appropriate values in respect of outstanding claims and premiums liabilities for the international controlled entities before applying the steps described in paragraph 31 of this Attachment.
34. In respect of outstanding claims, the consolidated accounts of the group prepared in accordance with **Australian Accounting Standards** will include consolidated gross outstanding claims liabilities (and corresponding recovery assets). Given that those standards are, in most respects, the same as APRA requirements for outstanding claims, the Group Actuary may adopt the outstanding claims liabilities from the consolidated accounts of the group subject to:
- (a) ensuring that the risk margins are in accordance with APRA standards; and
  - (b) any other adjustments that are needed, in the Group Actuary's opinion, to materially comply with APRA standards.
35. In respect of premiums liabilities, the consolidated group accounts prepared in accordance with Australian Accounting Standards will not include prospective estimates of premiums liabilities. The Group Actuary must make an appropriate estimate of premiums liabilities and advise the group accordingly.
36. In respect of international business, the insurance liability valuation for a Level 2 insurance group may be based on accounting entries premiums liabilities, subject to:
- (a) assessment by the Group Actuary of the appropriateness of these entries relative to the requirements of Attachment A; and

- (b) any adjustments required as a consequence of this assessment.

The requirements specified in paragraphs (a) and (b) will not apply to international consolidated entities which APRA deems to be immaterial. The parent entity of a Level 2 insurance group will need to consult with APRA prior to excluding any international consolidated entities from the requirements in paragraphs (a) and (b). Consolidation adjustments referred to in paragraph 31 ~~of~~ this Attachment may also be required.

37. For international business the premiums liabilities may be recorded as the equivalent accounting entries<sup>51</sup> provided they are subject to a liability adequacy test by the Group Actuary, in accordance with the requirements of Australian Accounting Standards, at a 75 per cent level of sufficiency. The business segments used should not, however, combine Australian and international businesses in the same segments because the Australian business already has a premiums liability estimate from its ILVR that is used as a component of the group results.
38. The determination of the capital base of a Level 2 insurance group where premiums liabilities are reported on the basis of paragraphs 36 and 37 ~~of~~ this Attachment will, in some circumstances, differ to that prescribed under GPS 112. Any amount of premiums liabilities determined using accounting entries which is higher than the corresponding amount calculated under the prescribed liability adequacy test (i.e. a surplus) cannot be included in the capital base of the Level 2 insurance group as a surplus technical provision. Any amount of premiums liabilities determined using accounting entries which is lower than the corresponding amount calculated under the prescribed liability adequacy test (i.e. a deficit) must be included in the capital base of the Level 2 insurance group as a deficit technical provision.

### Insurance Liability Valuation Report

39. The parent entity of a Level 2 insurance group must ensure that its Group Actuary prepares an ILVR as required by this Prudential Standard and provides that ILVR to the group within the time required by paragraph 13 of this Attachment. The ILVR must:
- (a) be addressed to the Board of the parent entity;
  - (b) provide the Group Actuary's advice in respect of the value of the group's insurance liabilities, determined in accordance with this Prudential Standard; and
  - (c) in respect of the group, provide details on the same matters as required under this Prudential Standard for an insurer's ILVR.<sup>52</sup>
40. Preparation of the ILVR for a Level 2 insurance group must have regard to professional standards issued by the Institute of Actuaries of Australia that

<sup>51</sup> The net premiums liabilities are estimated as unearned premiums less deferred acquisition costs less the relevant reinsurance items plus any liability adequacy test adjustments.

<sup>52</sup> Refer to paragraph 55 of Attachment A.

relate to the preparation of ILVRs for insurance groups, where these have been issued. Any such professional standards apply to the extent that they are not inconsistent with the requirements of this Prudential Standard. In the event of any inconsistency arising from application of the professional standards and this Prudential Standard, the requirements of this Prudential Standard prevail.

41. The ILVR for a Level 2 insurance group must provide sufficient information in relation to the assumptions and methods used for the valuation of liabilities so that another actuary reading the ILVR will be able to obtain a sound understanding of:
  - (a) the suitability of accounting figures for overseas business relative to the requirements of this Prudential Standard;
  - (b) the nature and quantum of consolidation adjustments;
  - (c) any inherent limitations in the process and results;
  - (d) the key risks pertaining to the insurance liabilities of the portfolio; and
  - (e) any other matters that a prudential standard requires to be included in the Level 2 insurance group ILVR.
42. Further detail on the measurement and reporting of insurance liabilities is provided in paragraphs 28 to 38 of this Attachment. The ILVR may refer to other actuarial reports in respect of the Australian business or international business of the group and the group must also ensure the Group Actuary's access to those actuarial reports.

### **Engagement of the Group Actuary**

43. Where this Prudential Standard requires a Level 2 insurance group to ensure that its Group Actuary performs a particular task or service or complies with a requirement, the parent entity of a Level 2 insurance group must ensure the contract engaging the Group Actuary (if external to the Level 2 insurance group) includes a term requiring the Group Actuary to perform the task or service or comply with the requirement.