

21 September 2016

Mr Pat Brennan
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Dear Mr Brennan

Submission on APRA's Discussion Paper: The role of the Appointed Actuary and actuarial advice within insurers

Finity Consulting appreciates the opportunity to provide our comments on APRA's recent discussion paper. Our comments, which reflect the broad views of Finity actuaries as a group, are set out in this letter.

The context of our feedback is that we work mostly within the general insurance and private health insurance sectors, and have Appointed Actuary roles in those areas. Our comments therefore relate to the implications of APRA's proposals for actuaries working in those industries. We understand that the proposals largely respond to issues for actuaries within the life insurance sector – and we cannot comment on the expected impact of the proposals for life insurance, as we do not hold Appointed Actuary roles in life insurance.

General Comments

We are generally supportive of the proposals. Our interpretation is that they will mean little change to the way actuaries operate in general insurance.

Before making comments on some of the specific proposals set out in APRA's paper, we raise one area of concern which we believe needs clarification from APRA:

The current paper could be interpreted as implying that the Appointed Actuary needs to be an internal appointment. While we do not believe this is APRA's intention, we take this opportunity to note that we believe that the current arrangements – which allow both internal and external Appointed Actuaries – are positive for the industry as a whole. In particular, we believe that the option of an external Appointed Actuary gives smaller companies the opportunity to benefit from high quality, independent and cost efficient advice from a consulting firm as external Appointed Actuary; it would be hard for smaller companies to source, or afford, the same level of advice if they were required to have an internal Appointed Actuary.

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Some of the specific section of APRA's discussion paper which appear to imply the Appointed Actuary should be internal are:

- The third paragraph of Section 2.1, which begins "Depending on the size and complexity...". This paragraph does not seem to allow for the option of an external Appointed Actuary – particularly in the use of the term "actuarial function"
- Section 2.2.1.3, relating to temporary delegations, could be seen as indirectly implying an internal Appointed Actuary. Would APRA expect a similar formal delegations framework to be in place if the Appointed Actuary were external?

Purpose Statement for Appointed Actuaries

We support APRA's proposal to introduce the purpose statement. In relation to the proposed wording in the discussion paper, we make the following suggestions:

- At the end of the first paragraph, the words "protection of policyholder interests" may need clarification – what is meant by this? In the general insurance context, we believe this relates to the ability for an insurer to pay claims in a timely fashion.
- In the second paragraph, we believe the word "relevant" should be inserted as follows: "...able make a significant contribution to the debate of **relevant** strategic issues". We discuss the involvement of the Appointed Actuary in strategy further below.
- We suggest that the final words "as well as the treatment of policyholders" could be removed. It is not clear what would be meant – particularly in the general insurance context – and in our view they are not necessary.

To the extent that APRA may assess that the purposes fulfilled by Appointed Actuaries in life and general insurance are different, it may make sense to differentiate via different purpose statements. We would encourage APRA to continue not to 'harmonise for the sake of harmonising'.

The Appointed Actuary as Strategic Advisor

The discussion paper includes the expectation that the Appointed Actuary will be a "strategic advisor" to the board. Taken at face value, this implies that the Appointed Actuary will be expected to advise across strategic issues of all kinds. This would include (for example) marketing strategies, as well as other areas where the Appointed Actuary would not have relevant background or skills.

In our view the Appointed Actuary role would be better expressed as an individual who has the experience and capabilities to **provide strategic input in relevant areas**. We see value in expecting actuarial input in areas which will impact on the financial condition of the company – and for this advice to be sought in a timely fashion (before the fact, not being asked for comment after the fact).

In our view the Appointed Actuary being seen as a strategic advisor in the broad sense would be something that Appointed Actuaries should aspire to – a sign of their success in the role – rather than being something expected or mandated by APRA. We don't believe that it would be possible

for anyone (including APRA) to ‘force’ companies to view their Appointed Actuaries as strategic advisors on all issues.

We also note that if an Appointed Actuary were indeed playing a primary role in driving an insurer’s strategy, it may be difficult for them to achieve the required independence in the regulatory requirements of the Appointed Actuary role (valuation and FCR).

Provision of Actuarial Advice

Actuarial Advice Framework

We believe the introduction of an actuarial advice framework would be a positive step, encouraging insurers to obtain timely actuarial input in relevant areas. The framework will provide clarity for both insurer and Appointed Actuary about where actuarial input is sought.

We imagine that smaller companies and branches will require only a simple framework, which may consist of a single overarching statement.

Materiality Policy

Our view is that a financial definition of materiality would not be appropriate – but that the materiality of any issue would need to be assessed by the Appointed Actuary using judgment, i.e. the question would be whether the item is “material in the eyes of the Appointed Actuary”. The materiality policy would therefore need to define a ‘threshold’ for referral to the Appointed Actuary – this could potentially work along the lines of ‘notifiable circumstances’ in the private health insurance sector.

Areas Requiring Actuarial Advice

We are comfortable with APRA’s list of minimum requirements for general insurers (in Section 2.2.1.1), but believe that the FCR – as one of the two key requirements of a general insurance Appointed Actuary – warrants specific mention here.

Actuarial Reports

FCR

We are supportive of APRA’s proposal to define the minimum requirements of an FCR. We expect that in practice our FCRs will not change materially in their coverage or depth of analysis. We would certainly expect that an FCR will always comment on the insurer’s capital adequacy – current and projected – as the capital position is crucial to financial condition.

We would hope that smaller companies in particular would retain the flexibility to incorporate the annual ICAAP Report into the Appointed Actuary’s FCR.

ILVR

We support APRA’s proposal that boards need not receive the full ILVR. We would expect to provide an executive summary to boards.

Due Date of Reports

We continue to be of the view that a four-month deadline for the FCR is more appropriate:

- It allows more time for the preparation of the report – which in some circumstances is helpful for the Appointed Actuary
- It provides boards with a better opportunity to consider the FCR separately from other year-end reporting (accounts and ILVR).

We refer APRA to our previous correspondence on this issue.

Comments – Private Health Insurance Sector

While the proposals are not addressed to private health insurance, the discussion paper notes that many of the principles may eventually be relevant in that context. Based on our work as Appointed Actuaries in private health insurance, our feedback is:

- We are generally supportive of the proposals, and do not see them having a material impact on the work of actuaries in private health insurance
- The Notifiable Circumstances regime has very strong support from actuaries working in private health insurance, and appears to be well aligned to APRA's objectives. If the proposals are extended to private health insurance, we believe that the Notifiable Circumstances regime should be retained as part of the actuarial advice framework (see further comments below)
- If the Appointed Actuary role is to include protection of policyholder interests, we believe it would be helpful for APRA to consult further on what this would and would not include in the context of private health insurance.

Notifiable Circumstances

The actuarial purpose statement states that “The actuary plays a key role in, and provides effective challenge to, the activities and decisions that may materially affect the insurer’s financial condition”. APRA also proposes that “only material matters would be required to be the subject of formal actuarial advice”.

The current Notifiable Circumstances regime in private health insurance has been in place since 2007, but “notifiable events” arrangements have operated since the 1990s. The insurer is required to notify the Appointed Actuary of material financial matters being considered by the insurer; however, the Appointed Actuary has discretion as to whether or not advice is required.

Even in situations where no formal advice is provided, there is valuable dialogue (and perhaps challenge) between the Appointed Actuary and the insurer’s management or board. The Notifiable Circumstances regime therefore appears to be strongly aligned with APRA’s proposals for life and general insurance.

Health insurance actuaries have suggested Notifiable Circumstances be required contents of the board's actuarial advice framework. We would welcome the opportunity to discuss this further when APRA considers the private health insurance Appointed Actuary role.

Prudential Standards

Without seeing proposals in detail, we are generally supportive of APRA's proposals relating to GPS 320 and the introduction of a new standard GPS 340.

Other Areas

In relation to parts of APRA's proposal not mentioned in this letter, we are comfortable with APRA's proposals – once again noting that we are largely unfamiliar with the detail of the life insurance context.

Yours sincerely



Gae Robinson