
Professional Standard 201

Actuarial Advice to a Life Insurance Company or Friendly Society

January 2023

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1. Introduction

1.1 Application

- 1.1.1 This Professional Standard applies to Members providing actuarial advice to life insurance companies domiciled in Australia (including friendly societies and eligible foreign life insurance companies) registered under the Life Insurance Act 1995 (Cth) ("Act").

This Professional Standard also applies to Members who support another Member in providing advice under the Professional Standard, as relevant to their contribution to the Services.

- 1.1.2 A Member providing advice under this Professional Standard required under CPS 320, Attachment B:

- (a) must be an Eligible Actuary; and
- (b) must exercise his or her independent professional judgement and give impartial advice.

A Member providing advice under this Professional Standard not required under CPS 320, Attachment B does not need to be an Eligible Actuary.

Members supporting the Member providing advice under the Professional Standard are not required to be an Eligible Actuary.

- 1.1.3 All work performed under this Professional Standard, whether by the Member providing advice or by a Member supporting the Member providing advice, is designated as an Applicable Service. As such, Members' attention is directed towards Practice Guideline 1 (General Actuarial Practice) which applies to Applicable Services. In the case of a Member supporting the Member providing advice, Practice Guideline 1 applies as relevant to their contribution to the Services.
- 1.1.4 This Professional Standard was released in response to APRA's reconsideration of the functions of the Appointed Actuary role and subsequent release of CPS 320 Actuarial and Related Matters dated 6 June 2018, which was effective 1 July 2019.
- 1.1.5 The Act provides for APRA to issue prudential standards regulating the activities of, and imposing requirements on, life insurance companies and friendly societies. APRA Prudential Standards mandate their requirements of life insurance companies and friendly societies, with regard taken of the relevant Professional Standards of the Institute.
- 1.1.6 There are likely to be other matters or situations not directly referred to in this Professional Standard, whether or not referenced by the regulatory regime, in which a Member's advice will be sought or must be given to the management or

the Board of the life insurance company or friendly society. In such circumstances, the Member must take account of the general considerations in this Professional Standard along with relevant provisions of the Code.

1.1.7 In providing the Entity with written advice, Members must bear in mind the principal objective of the Act as stated in sub-section 3(1) thereof, namely "... to protect the interests of the owners and prospective owners of life insurance policies in a manner consistent with the continued development of a viable, competitive and innovative life insurance industry".

1.1.8 An Appointed Actuary giving advice to a life insurance company or friendly society has legal obligations to report certain matters, information or opinions to the Entity (including a director or officer of the Entity) or APRA (as relevantly set out in the Act). These obligations are referred to as "whistleblowing". The obligations, details about what must be reported, related powers and protections are provided in sections 98, 98A, 98B and 99 of the Act. An Appointed Actuary and Members supporting the Appointed Actuary must understand the obligations that apply to them in their circumstances. This may require the Appointed Actuary and/or Members to seek legal or other professional advice.

1.2 Previous Versions

This version of this Professional Standard replaces the version which was issued in March 2021 and incorporates the introduction of AASB 17 (effective from 1 January 2023) and changes to the APRA Standards to integrate AASB 17 (effective 1 July 2023).

The previous version of this Professional Standard replaces the version which was issued in March 2020 and incorporated conformance changes to align with the Institute's new Code (effective 31 March 2020). The initial version of this Professional Standard was issued in June 2019. Prior to June 2019 all actuarial advice to life insurers and friendly societies was governed by a single standard, Professional Standard 200 Actuarial Advice to a Life Insurance Company or Friendly Society (PS 200), which was most recently issued in July 2015.

1.3 About this Professional Standard

1.3.1 This Professional Standard:

- (a) has been prepared in accordance with the Institute's Policy for Developing Professional Practice Documents;
- (b) must be applied in the context of the Code;
- (c) must be applied by Members of the Institute when they perform work that the Professional Standard covers; and

(d) defines the Institute's requirements for all work the Professional Standard covers.

1.3.2 If a Member believes that this Professional Standard is ambiguous or wishes to seek clarification of it, then they may consult the Institute's Professional Practice Committee for an interpretation.

1.3.3 A Member may in rare circumstances be unable to carry out their work in full compliance with this Professional Standard. If a Member finds that they cannot carry out their work in a way that fully complies with this Professional Standard then they must:

(a) decline to carry out the work;

(b) end their agreement to do so; or

(c) perform the work to the fullest extent possible under this Professional Standard; and qualify the work accordingly as set out in clause 1.3.4.

The approach adopted in such circumstances will require the exercise of the Member's professional judgement having regard to Materiality as appropriate.

1.3.4 In the scenario described in clause 1.3.3 (c), the resulting work product must be clearly qualified, with both the title of the report and the scope of the work set out in the report acknowledging the relevant limitations. All reasonable attempts must be made to comply with this Professional Standard to the fullest extent possible. A description of the areas where change would be needed to enable the creation of an unqualified work product must be disclosed along with a description of the reasons for issuing qualified work.

1.3.5 If a Member does not comply with this Professional Standard then that may constitute Misconduct under the Institute's Disciplinary Scheme, although proper account will be taken of provisions of clauses 1.3.3 and 1.3.4.

1.3.6 This Professional Standard does not constitute legal advice. Any interpretation or commentary within this Professional Standard regarding specific legislative or regulatory requirements reflect the expectations of the Institute but does not guarantee compliance under applicable legislation or regulations. Accordingly, Members should seek clarification from the relevant regulator and/or seek legal advice in the event they are unsure or require specific guidance regarding their legal or regulatory obligations.

1.4 Other relevant documents

1.4.1 This Professional Standard must be applied in the context of the relevant law, and relevant accounting and auditing standards.

- 1.4.2 A reference to legislation or a legislative provision in this Professional Standard includes any statutory modification, or substitution of that legislation or legislative provision and any subordinate legislation issued under that legislation or legislative provision. Similarly, a reference to a Professional Standard includes any modification or replacement of that Professional Standard.
- 1.4.3 Apart from the Code, from legislation or from regulatory standards, no other document, advice or consultation (including Practice Guidelines of the Institute) can be taken to modify or interpret the requirements of this Professional Standard.
- 1.4.4 If there is a conflict between this Professional Standard and any legislation, then the legislation takes precedence. In this context, legislation includes regulations, prudential standards, subordinate standards, rules issued by government authorities and standards issued by professional bodies which have the force of law.

2. Commencement Date

This version of this Professional Standard applies to any relevant advice or Report given to an Entity on or after 1 January 2023.

3. Definitions

3.1 In this Professional Standard:

'Act' means the Life Insurance Act 1995 (Cth).

'Actuarial Advice Framework' means the Entity's framework for the provision of actuarial advice that enables the Appointed Actuary to perform the functions of the role, as required under CPS 320.

'Applicable Services' means Services that are designated in an Institute Professional Standard or Practice Guideline as being Applicable Services.

'Appointed Actuary' means a Member holding an appointment by the Entity under section 93 of the Act.

'APRA' means the Australian Prudential Regulation Authority.

'APRA Standards' means the Prudential Standards and Reporting Standards issued by APRA from time to time in accordance with the Act.

'Capital' means (unless otherwise specified) share capital, share premium, retained profits and subordinated debt approved for capital purposes by APRA.

'Capital base' is as defined in LPS 112.

'Code' means the Code of Conduct of the Institute.

'CPS 220' means APRA Prudential Standard CPS 220 Risk Management.

'CPS 320' means APRA Prudential Standard CPS 320 Actuarial and Related Matters.

'Discretionary Investment Benefit' means any participating benefit or non-participating benefit where the benefit is increased to reflect the investment experience of the assets backing the benefit, and where the amount of the increase in the benefit to reflect the investment experience is either subject to averaging over time or at the discretion of the Entity. For the purposes of this definition, the allowance for a certain rate of investment return in determining the premiums for a benefit does not imply that the benefit reflects the investment experience of the assets backing the benefit.

'Disciplinary Scheme' means the document of that name prepared by the Institute setting out the rules and procedures governing professional discipline of Member, as amended by Council from time to time.

'Eligible Actuary' means:

- (a) a Fellow or Accredited Member of the Institute; or
- (b) a Member who is eligible to act in an actuarial capacity pursuant to a requirement under legislation.

'Entity' means the legal entity registered under the Act as the life insurance company, as the friendly society or otherwise, as the context requires. A reference in the Professional Standard to advice to the Entity includes advice to the board of directors of the Entity as the context requires under the regulatory regime.

'General Fund' means, in accordance with the APRA Standards, the shareholders fund in the context of a life insurance company (other than a friendly society) or the management fund in the context of a friendly society.

'ICAAP' means the Internal Capital Adequacy Assessment Process of an Entity, as required under LPS 110.

'LPS 001' means APRA Prudential Standard LPS 001 (Definitions).

'LPS 100' means APRA Prudential Standard LPS 100 Solvency Standard.

'LPS 110' means APRA Prudential Standard LPS 110 Capital Adequacy.

'LPS 112' means APRA Prudential Standard LPS 112 Capital Adequacy:

Measurement of Capital.

'LPS 360' means APRA Prudential Standard LPS 360 Termination Values, Minimum Surrender Values and Paid-up Values.

'LPS 370' means APRA Prudential Standard LPS 370 Cost of Investment Performance Guarantees.

'Material' means relevant to the Entity's circumstances and is either important or essential in the opinion of the Member (clause 4). For this purpose, 'Material' does not have the same meaning as in Australian accounting standards.

'Policy Owner' means the owner of a life policy as defined in the Act, and includes reference to a member of a benefit fund of a friendly society as the context requires.

'Prescribed Capital Amount' (PCA) is as defined in LPS 10.

'Prudential Capital Requirement' is as defined in LPS 110.

'Reasonable Benefits' – Under participating and Discretionary Investment Benefit policies either the premium or the benefits may be varied. This may enable an Entity to accept risks more confidently in the knowledge that adjustments can be made as experience unfolds. A purchaser of such a policy shares the risk to some extent and is entitled to be treated equitably in the light of that experience. The expression "reasonable benefits" is used in connection with such policies to describe benefits which fall within a range which could reasonably be held to recognise these features and all the matters described in clause 6.4 of this Professional Standard.

'Report' means a report or written advice prepared by a Member under this Professional Standard.

'Statutory Fund' means, as the context requires, the statutory fund or benefit fund, as defined under the Act.

'To disclose' means to include information within a written communication, such as a Report where one is prepared.

'To record' means to include information within working papers or other documentation, but this information does not need to be included in written Reports or similar communication.

3.2 A word that is derived from a defined word has a corresponding meaning.

3.3 Other capitalised terms used in this Professional Standard have the same meaning

as set out in the Code.

4. Materiality

4.1 The Member must take Materiality into account when performing work under this Professional Standard. In determining whether something is Material, the Member must take into account the purpose of the actuarial advice being given. Whether something is Material or not will always be a matter requiring the exercise of the Member's professional judgment.

4.2 If a Member has formed the opinion that a matter required to be considered under this Professional Standard is not Material to the actuarial advice in the circumstances, then:

4.2.1 the Member must record that the matter is not Material and provide reasons for forming that opinion, but does not have to further consider that matter; and

4.2.2 if the matter is not relevant to the Entity's circumstances, the matter may be omitted from the applicable Report; or

4.2.3 if the matter is relevant to the Entity's circumstances, but is not Material because it is neither important nor essential in the Member's opinion, the Member must include in the applicable Report that the matter is not Material and provide reasons for such opinion.

5. Overall Principles

5.1 Items for consideration

5.1.1 When providing advice in terms of this Professional Standard, the Member must consider all relevant items below and any other matters considered relevant:

(a) the premium rates and charges on which existing business has been, and current new business is being, written;

(b) the nature, terms and conditions, and disclosures of the contracts in force and currently being sold with particular reference to all options and guarantees, and the scope for adjusting the terms and conditions in the light of emerging experience;

(c) the existing investments, the continuing investment policy and a range of plausible future investment experience;

(d) the business plans, in particular the expected volumes and capital demands of sales;

- (e) the current and a range of plausible future experience items which could materially impact the advice, given the nature of the product or reinsurance proposal under consideration;
- (f) the Entity's risk management framework;
- (g) the arrangements for reinsurance and other risk mitigation strategies and arrangements;
- (h) the operational capability of the Entity to effectively administer the business and the ability of the Entity to monitor emerging experience, including new items of experience likely to emerge under any proposal, and;
- (i) the impact on other business the Entity conducts.

5.2 Written advice and record keeping

- 5.2.1 Written actuarial advice provided to the Entity must be clearly identified as such, incorporating reference to the requirements and authorities of the Actuarial Advice Framework pertinent to the advice. If, in addition, the advice is required by the regulatory regime this must be clearly identified as such, including reference to the particular regulatory requirement.
- 5.2.2 A statement must be included that written advice has been prepared in accordance with this Professional Standard.
- 5.2.3 The Member must include with his or her advice the reasons for giving the advice, any conditions or limitations imposed on the use of that advice, and any related, significant commercial factors or risks to which the Entity and Policy Owners would be exposed.
- 5.2.4 Reference must be made to other information, if any, that may have been relied upon in providing the advice. Where the Member relies on work undertaken by others, the Member must consider how to communicate this to the others and how to verify the reasonableness of the investigations undertaken, and results obtained, by the others. Where the Member cannot form an opinion as to reasonableness, alternative analyses must be undertaken and recorded.
- 5.2.5 In providing written actuarial advice in relation to matters covered by this standard, the Member must, at a minimum, prepare a statement which includes references to relevant supporting Information. The Member must make and keep sufficient and appropriate records about relevant matters to enable a formal Report to be prepared later if required.
- 5.2.6 Such modelling or other work that has been carried out in support of finalised advice must be included in working papers.

5.2.7 CPS 320 requires an Entity to take all reasonable steps to ensure that working papers and other documentation of an Appointed Actuary in relation to prudential requirements are retained for a period of seven years. An Appointed Actuary must assist an Entity by identifying their working papers and other documentation and retaining this information and/or providing it to the Entity. They must also make this information available to APRA where requested in writing.

5.2.8 A Member must include in their documentation all items required by this Standard to be recorded. The items required by this Standard to be recorded must contain sufficient detail and clarity that another actuary qualified in the same practice area could make an objective assessment of the reasonableness of the Member's work.

5.3 Responsibility for advice given

5.3.1 In carrying out his or her responsibilities, the Member must, among other things:

- (a) comply with the requirements of the regulatory regime;
- (b) satisfy the constitution, articles of association, and other by-laws constituting the Entity;
- (c) provide advice that aims to achieve, within the bounds of reasonable probability, the long term financial soundness of the life insurance business of the Entity;
- (d) provide advice that seeks to achieve equity in the allocation and distribution of profits or benefits to participating Policy Owners in general, non-participating Discretionary Investment Benefit Policy Owners, between different groups of such Policy Owners, and to shareholders (refer to clause 10.2 of this Professional Standard); and
- (e) comply with the relevant provisions of the Code.

5.3.2 While a Member may delegate certain tasks required under this Professional Standard, the Member nonetheless remains ultimately responsible for the advice provided.

5.4 Information and data requirements

5.4.1 The Member providing actuarial advice must make the Entity aware that the responsibilities of providing that advice cannot be properly carried out unless it makes available adequate and relevant information.

5.4.2 In this regard the needs of the Member must be specified and, if the appropriate information is not forthcoming, the Report or advice must be qualified or state the Member's inability to give advice as the case may be.

- 5.4.3 The Member must summarise in the Report all Material information relied upon in preparing the Report. Material issues or concerns with information or data, which cannot be resolved and may affect the quality or nature of advice provided, must be outlined, together with the consequent limitations of the Report.

6. Product Advice

6.1 Principles of product advice

- 6.1.1 Attachment B of CPS 320 requires the Entity's Actuarial Advice Framework to include advice provided with respect to pricing for new products and changes in products. The advice must cover proposed terms and conditions (which includes premium rates, commissions, fees and charges, surrender bases), and (unless the Member determines not applicable due to the nature of the policy) unit pricing.
- 6.1.2 Written advice, provided in accordance with the Entity's Actuarial Advice Framework, is required when there are proposed modifications in terms and conditions, or when the Member recognises that there is a change in circumstances relating to a group of policies that has Material financial implications.
- 6.1.3 When providing advice on proposed new terms and conditions or changes to terms and conditions, the Member must consider whether the proposals have an impact on business already issued or other products not directly the subject of the proposals. Changes in sales mix, volumes, lapses and claims assumptions are possible. If the Member considers the impacts may be Material, the Member must comment on these.
- 6.1.4 With respect to any advice provided by the Member under Attachment B of CPS 320, the Member, by reference to the Actuarial Advice Framework, must clearly establish to whom in practice the advice is to be directed.

6.2 Premium rates and charges

- 6.2.1 When providing advice on premium rates and charges, the Member must make a statement on their 'suitability' or 'adequacy' in terms of meeting corporate pricing standards, contributing to marginal and overhead expenses and return on financing capital. The statement of their suitability cannot be an absolute statement - it is inevitably a probability. The adequacy or otherwise of premium rates and charges cannot, therefore, be other than a matter of judgment and should take into account contracts containing various options or guarantees.
- 6.2.2 In particular, apart from any general advice that the Member provides, if the premium rates and charges for a product are considered to be materially unsuitable or inadequate, the Member must state why that opinion is held and indicate the potential or likely financial consequences of their adoption by the Entity. The Member must indicate actions the Entity could take to counteract the potential risks.

6.3 Assumptions about future experience

- 6.3.1 The Member must be satisfied as to the suitability of all Material assumptions about the expected future experience used in setting premium rates and charges, surrender bases and reinsurance arrangements.
- 6.3.2 In providing an opinion as to the likely future experience of underwriting new types of risk where no specific past experience is available, the Member must take into account such statistics relating to similar events or conditions as can be obtained and are considered relevant. The Member must comment on any limitations that apply to the terms and conditions of policies while experience is being gained. Where appropriate, and quite apart from any general monitoring that the Entity undertakes for risks, the Member must specify that close monitoring of experience of new risks is required.
- 6.3.3 The experience underlying the assumptions may have had past volatility and confidence about the likely future will vary. The Member must consider the degree of uncertainty in each of the assumptions and the potential effects of experience being relatively adverse. The Member must consider the Entity's capacity to finance such adverse experience.

6.4 Equity

- 6.4.1 In the case of a participating policy, a Policy Owner will be entitled to a share of the profits made by the Entity during the life of the policy. In the case of a non-participating Discretionary Investment Benefit policy, a Policy Owner pays premiums for benefits where one or more of the elements can be varied during the life of the policy at the discretion of the Entity. The Member must consider changes which may arise from the proposed product changes in the benefit levels or emerging profits to the various cohorts, including existing Policy Owners, shareholders or to new Policy Owners relative to existing Policy Owners. If the Member considers such changes likely or reasonably possible, comment is required.
- 6.4.2 In the case of a non-participating policy, which has no provision for the terms to be varied, consideration of equity may have regard to the fact that potential Policy Owners can choose whether to buy the product or a competing product based on the terms being offered.
- 6.4.3 In the cases outlined above, the Member, at the time of advising on the premium rates and benefits, must consider aspects which could impact the maintenance of equity during the life of the policy.

6.5 Finance

- 6.5.1 Benefits paid plus expenses incurred plus the required increase in policy liabilities to be held in respect of the future liabilities may exceed premiums received in certain circumstances, for example, in the early years of a policy. Where this is the case, the

Member must consider:

- (a) amount and incidence of the estimated required finance;
- (b) capacity of the Entity to meet this requirement for finance and the source of this finance; and
- (c) constraints which should be imposed on the volume of new business, the period for which it may be written, size of policy, or otherwise.

6.6 Tests of suitability

- 6.6.1 The Member must test the suitability of premium rates and charges, such as using 'profit testing' projection methods with all reasonable contingencies and the cost of capital taken into account. However, there may be occasions when it is not necessary to adopt a 'profit testing' approach, in which case another suitable method must be used. The Member must test not only on the 'best estimate' view of future experience but also on a range of plausible variations from that best estimate.
- 6.6.2 For each variation in the view of future experience, the Member must make a number of assumptions about items such as mortality, morbidity, lapse and surrender rates, expenses, taxes and investment experience and reinsurance arrangements.
- 6.6.3 The range of matters to be taken into account when considering suitability may well vary, depending upon the particular circumstances. In each case, the Member must be in a position to justify any decision to limit the range of scenarios tested.

6.7 Other policy terms and conditions

- 6.7.1 The Member advising an Entity on the structure of a life insurance product must consider all policy terms and conditions, not just the adequacy or otherwise of premium rates and charges. The Member must give advice on the financial impact or risks of the proposed policy definitions, any guarantees and options, and any other matter the Member considers relevant.
- 6.7.2 The Member's advice must contain commentary on whether they are satisfied that the Entity has controls in place, such that the promotional material related to the product is consistent with the terms and conditions upon which the Member's advice is based.
- 6.7.3 If the Member identifies risks of differences between the (prospective) Policy Owners' understanding of how the policy operates and its actual operation, these must be commented on in the Member's advice.

6.8 Surrender basis

- 6.8.1 Attachment B of CPS 320 requires the Entity's Actuarial Advice Framework to include advice on the proposed basis for determining surrender values, if applicable.
- 6.8.2 When providing advice on the surrender value basis for a life insurance product, the Member must consider the impact the proposed basis would have on the capital position of the Entity. Whilst it may be appropriate or unavoidable to incur losses on some policies surrendering, the Entity must be advised if surrenders could cause serious loss. If the surrender value basis is guaranteed, the extent of this guarantee and its possible financial effect must be commented upon in the advice.
- 6.8.3 The Member, when providing advice on a surrender value basis, must consider equity between surrendering and continuing Policy Owners, and practical implementation issues, as well as the requirements of any APRA Standards applicable.

6.9 Unit pricing

- 6.9.1 If policies provide benefits by reference to units, Attachment B of CPS 320 requires the Entity's Actuarial Advice Framework to include advice on the proposed means by which unit values are determined.
- 6.9.2 The Member must comment on the extent to which the unit pricing system determines a unit price so that new, continuing and terminating Policy Owners are treated equitably and in accordance with policy terms and conditions.
- 6.9.3 The Member must comment on the robustness of the unit pricing approach and system.
- 6.9.4 The Member must comment on the discretions that the Entity has in determining unit prices and on the equity and the manner in which the Entity proposes to exercise those discretions.
- 6.9.5 The company's approach to unit pricing for a new or changed product (in relation to the aspects noted in clauses 6.9.2, 6.9.3 and 6.9.4) may be the same as for an existing policy. Where this is the case, and provided that the considerations for assessing the appropriateness of these aspects are the same (between the existing and new or changed product), it is considered sufficient under this Standard for the Member to advise the company of this, including a reference to the previous advice.

6.10 Commission

- 6.10.1 The Member must have regard to all expenses when advising on product terms and conditions. The Member must provide advice on the financial risks that the commission terms may impose and on the appropriateness of the proposed

commission arrangements (including the total commission allowed for in the pricing of a product).

- 6.10.2 Consideration must be given to the recoverability of commission in the case of early termination of policies. If appropriate, the risks associated with a high level of policy termination, and a subsequent failure to realise the assumed recoverability of commission, must be highlighted.

7. Reinsurance Arrangements

- 7.1 Attachment B of CPS 320 requires the Entity's Actuarial Advice Framework to include advice on changes to the reinsurance strategy, new reinsurance arrangements, or changes to existing reinsurance contracts.
- 7.2 When providing advice on the reinsurance arrangements, the Member must consider the issues listed above in clause 5.1.1 where relevant, and the financial impact of the proposed reinsurance and retention limits.
- 7.3 The Member must comment on the circumstances under which the reinsurance arrangements, in his or her judgment, could become inappropriate.

8. Investment Strategy

- 8.1 Attachment B of CPS 320 requires the Entity's Actuarial Advice Framework to include advice on changes in the investment strategy, including asset-liability management in respect of participating business and business with participating features. Unless the impact of the change is determined to be not Material, the Member must consider the matters set out in this section.
- 8.2 The Member must consider the reasonable expectations of Policy Owners. This includes consideration of disclosures previously made, the effect of the change on future crediting or bonus rates, any change in the risk borne by Policy Owners, and the effect on continuing Policy Owners if the withdrawal rates of policies were to change. If the Member considers the reasonable expectations of Policy Owners will not be met following the change, the Member must include this in the advice given.
- 8.3 The Member must consider how the change affects the return for shareholders, the risks they are bearing, the capital support they are providing, and the rewards provided to shareholders via distribution of profits or other means. If the Entity is a mutual, the members of the Entity replace shareholders in this clause.
- 8.4 The Member must consider the effect of the change on the equity between shareholder and Policy Owners, between the affected Policy Owners, and between all other Policy Owners. If the Member considers the proposed changes give rise to inequity, this must be included in the advice given. In this circumstance, the Member must consider advising on possible means by which the equity can be restored, for example possible changes in the future share of profits.

9. Apportionments

9.1 Principles of apportionments

- 9.1.1 A number of items must be apportioned between different businesses and/or funds of an Entity. The Act requires that the Entity receive written advice from the Appointed Actuary before these apportionments are made.
- 9.1.2 Sections 78 and 79 of the Act require an Entity to apportion income and outgoings relating to the mixed business of two or more statutory funds, classes, categories or sub- categories of business. Section 80 of the Act requires that any apportionment be made on an equitable basis and according to generally accepted accounting principles. The Appointed Actuary must provide written advice as to whether the apportionment is appropriate.
- 9.1.3 In preparing the advice, the Member must give consideration to the nature of the item being apportioned and the business to which it relates, such that apportionments to a statutory fund relate to the business of the fund.
- 9.1.4 As well as the requirement of the Act, further apportionments may be required for taxation purposes or for determining assumptions for calculating policy liabilities or premium rates.
- 9.1.5 As well as the requirements of the various laws, the Member must also consider the following principles:
- (a) promoting the financial soundness of the Entity;
 - (b) promoting the meaningful disclosure of the business of the statutory fund;
 - (c) consistency of treatment between reporting periods; and
 - (d) equitable treatment between Policy Owners and shareholders.

9.2 Equity of apportionments

- 9.2.1 Equity of the apportionment is a matter of judgment for the Member. The Member must consider the following factors and any other factors considered relevant:
- (a) the relationship between the nature of the item and the business of the statutory fund or account to which it is allocated;
 - (b) the objectivity of the basis of apportionment, noting that the basis should result in consistent treatment from one period to the next and avoid significant changes in basis resulting from differences in opinion of the person making the apportionment;

- (c) the magnitude of the effect of the item being apportioned on the statutory fund or account;
- (d) Materiality, noting that it is acceptable for a simplistic basis to be used for apportionment of small items, where the financial effect on any statutory fund or account is not Material; and
- (e) the existence of discretionary or participating business, and the impact that the proposed apportionment between such business and other non-participating business would have on the implicit allocation of income and expenditure between Policy Owners and shareholders.

9.3 Intergroup apportionments and outsourcing

- 9.3.1 Intergroup apportionments may occur because the Entity is a part of a group of companies sharing the same resources. While these are outside the scope of section 80 of the Act, the Member's written advice must consider whether the net result of such apportionments to the Entity and to statutory funds is reasonable and commercial for the services received or provided.
- 9.3.2 Outsourcing to intergroup companies represents another area where attention is required by the Member such that section 30(d) of the Act is not breached. This commonly includes investment management, distribution and data processing.
- 9.3.3 In general, the Member must be satisfied that the outsourcing arrangements are on reasonable and commercial terms. In this regard, the Member is also reminded of the requirements of section 98 of the Act.

9.4 Expenses

- 9.4.1 A major item to be apportioned will be expenses (including the expenses in a Friendly Society Management Fund). Where expenses relate to a specific fund, class, category or sub category, they must be allocated directly. Indirect expenses must be allocated on an objective basis using the principles outlined above.
- 9.4.2 The level of detail involved in the apportionment process will vary depending on the financial information available to produce results.
- 9.4.3 Expenses must also be split between acquisition and maintenance for determination of assumptions for calculation of policy liabilities and an assessment of the capital base and prescribed capital amount.
- 9.4.4 Expenses must also be split between directly attributable and not directly attributable for determination of assumptions for calculation of insurance liabilities under AASB 17.
- 9.4.5 The split between acquisition and maintenance expenses, and directly attributable

and not directly attributable expenses, has a direct effect on the reported profit of the Entity and particular attention must be paid to it. Consistency of treatment from year to year is particularly important to avoid distortion of results.

9.5 Investment income

- 9.5.1 Where separate assets are maintained for particular blocks of business, then investment income relating to those assets must be allocated directly. Where separate assets are not maintained, then investment income must be allocated allowing for cash flows and assets invested unless the associated policy documents require otherwise.

9.6 Taxation

- 9.6.1 In many cases, it is not possible to charge tax directly to a statutory fund or component of the fund and apportionments must be made.
- 9.6.2 The apportionment basis for taxation must be clearly specified and make allowances for the method of taxing investment income in funds with more than one class of business, treatment of expense deductions and imputation credits. Where imputation credits earned by one block of business are passed on to other blocks of business or shareholders, this must be done on a consistent basis.

10. Distributions of Profits and Capital

10.1 Principles of distributions

- 10.1.1 The Board of the Entity is responsible for deciding the distribution of retained profits and shareholders' capital after receiving written advice from the Appointed Actuary as required by section 62 of the Act. In addition, Entity by-laws and benefit fund rules may impose additional constraints on the distribution and/or requirements on the Member.
- 10.1.2 Advising as to likely consequences of a distribution of retained profits, surplus or shareholders' capital is complex and requires judgment. The professional framework within which the Member must exercise this judgment is set out in clauses 4, 5, 6 and 7 of this Standard. The written advice as to the likely consequences of the distribution of retained profits or shareholders' capital must give the reasons upon which the advice is based and must also report on the outlook for future distributions to Policy Owners and transfers between statutory funds and shareholders' funds. Significant trends in profit or the capital adequacy position must be interpreted, and the impact of any subordinated debt must be considered.
- 10.1.3 In advising in relation to overseas business, the Member must also consider the relevant overseas regulatory requirements.

10.2 Equity of distributions

10.2.1 There is no universally agreed definition of equity and a decision about it can only be a matter of judgment. In making this judgment, the Member must give consideration to:

- (a) the sources of the profit disclosed, the relative contribution to it by the different groups of Policy Owners and by the shareholders, and the release of capital previously committed to support existing business;
- (b) the relative risks taken by the participating and Discretionary Investment Benefit Policy Owners in paying premiums for benefits, either of which may be varied, by profits being retained on their behalf, and by the shareholders in contributing capital;
- (c) the need to maintain the overall viability of the Entity for existing and future Policy Owners; and
- (d) prevailing practices within the actuarial profession.

10.2.2 Likewise, a decision about Reasonable Benefits for the different groups of participating and Discretionary Investment Benefit Policy Owners can only be a matter of judgment. In making this judgment, the Member must give consideration to each of the following (and the inter-relationships between them):

- (a) the terms and conditions including the premium rates, options and guarantees on which the policies were issued;
- (b) the information conveyed by the Entity to the Policy Owners in connection with the sale of the policy and subsequently;
- (c) the experience of the Entity, subsequent to the issue of the policies, in relation to each of the elements relevant to the policy such as mortality, morbidity, the return on investments, tax and expenses of administration, lapse and surrender experience;
- (d) the Entity's past practices; and
- (e) the need, if any, for each policy to make a contribution, from the profit it generates, to the Entity's capital in recompense for, and appropriate to, the support it may have received from the Entity in the past, including capital support.

End of Professional Standard 201