

NEW ZEALAND SOCIETY OF ACTUARIES
PROFESSIONAL STANDARD NO. 31
NON-LIFE INSURERS - FINANCIAL CONDITION REPORT
MANDATORY STATUS
EFFECTIVE DATE: 1 JANUARY 2013

INDEX

1	INTRODUCTION	2
1.1	Application	2
1.2	Purpose	2
1.3	Previous Versions	2
1.4	Legislation	2
2	EFFECTIVE DATE	2
3	DEFINITIONS	2
4	MATTERS TO CONSIDER AND REPORT	5
4.1	Statements by Member	5
4.2	Information	5
4.3	Matters for consideration	6
4.4	Materiality and Material risks	6
4.5	Business and operations	6
4.6	Recent experience and profitability	7
4.7	Pricing, underwriting and claim management	7
4.8	Insurance and other liabilities	7
4.9	Investments and other assets	8
4.10	Reinsurance arrangements	8
4.11	Capital management	9
4.12	Solvency assessment	9
4.13	Capital adequacy	9
4.14	Risk management	10
4.15	Conclusions and recommendations	10

1 INTRODUCTION

1.1 Application

- 1.1.1 This Professional Standard applies to Members producing a Financial Condition Report (FCR) under the Solvency Standard for Non-life Insurance Business made under Section 56 of the Insurance (Prudential Supervision) Act 2010 unless a more relevant Professional Standard applies.
- 1.1.2 If Members are preparing similar reports for other Entities providing non-life insurance coverage, then the relevant parts of this Professional Standard are applicable, to the extent that these are within any relevant legislation and/or any formal request made by the Entity to the Member.
- 1.1.3 This Professional Standard does not override the requirements of the Society's Professional Standard 4.

1.2 Purpose

- 1.2.1 The purpose of this Professional Standard is to provide Members with principles and directions that must be followed with regard to an impartial assessment of an Entity's financial condition and preparation of the FCR.
- 1.2.2 The assessment includes discussing the implications of Material risks identified during the assessment and, where these implications are adverse, making recommendations as to how to address these risks.

1.3 Previous Versions

There are no previous versions of this Professional Standard.

1.4 Legislation

- 1.4.1 From 7 September 2010, the Act provides for RBNZ to issue prudential standards, regulating the activities of and imposing requirements on Insurers.
- 1.4.2 The Solvency Standard mandates that the Appointed Actuary must prepare an FCR in accordance with Section 56 of the Act.
- 1.4.3 If there is a difference between this Professional Standard and the applicable legislation, the legislation takes precedence. In this context, legislation includes regulations, prudential standards, subordinate standards and rules.

2 EFFECTIVE DATE

This Professional Standard takes effect from 1st January 2013.

3 DEFINITIONS

“Act” means the Insurance (Prudential Supervision) Act 2010.

“Actual Solvency Capital” has the meaning given in the Solvency Standard.

“Advice” has the same meaning as defined in the Code.

“Appointed Actuary” means the person defined under Section 76 of the Act.

“Approved Rating Agency” has the meaning given in the Act.

“Board” means the directors of an Entity, or equivalent.

“Central Estimate” has the meaning given in the Society’s Professional Standard 4.

“Claims” has the meaning given in the Society’s Professional Standard 4.

“Class of Business” has the meaning given in the Society’s Professional Standard 4.

“Code” means the Society’s Code of Professional Conduct.

“Entity” means one or more companies, corporations or other bodies with a liability to pay Claims.

“Entity’s Plans” means the plans of the Entity, current at the Report Date, including but not limited to budgetary, business, strategic and capital management plans.

“FCR” means Financial Condition Report having the meaning given in the Solvency Standard.

“Insurance Liability Valuation” means a valuation of the non-life insurance liabilities of one or more Classes of Business carried out as at the Report Date.

“Insurer” means a licensed insurer as defined in the Act.

“Material” means significant in the professional judgement of the Member. **“Materiality”** and **“Materially”** have a consistent meaning to Material. The Member must have due regard to the definition of Materiality in the Solvency Standard.

“Member” means a member of the Society.

“Minimum Solvency Capital” has the meaning given in the Solvency Standard.

“Net Outstanding Claims Liability” has the meaning given in the Solvency Standard.

“Premium Liabilities” has the meaning given in the Solvency Standard.

“Professional Standard” means a Professional Standard of the Society.

“RBNZ” means the Reserve Bank of New Zealand.

“Report Date” means the Entity’s financial year end to which the FCR relates or such other date as requested by the Entity or the RBNZ.

“Risk Margin” has the meaning given in the Society’s Professional Standard 4.

“Society” means The New Zealand Society of Actuaries.

“Solvency Margin” has the meaning given in the Solvency Standard.

“Solvency Ratio” has the meaning given in the Solvency Standard.

“Solvency Standard” means the RBNZ Solvency Standard for Non-life Insurance Business made under Section 55 of the Act and includes any conditions imposed by the RBNZ.

4 MATTERS TO CONSIDER AND REPORT

4.1 Statements by Member

- 4.1.1 The Member must sign and state the date of completion of the FCR.
- 4.1.2 Statements must be provided setting out who commissioned the Member's report, the scope of and purpose of the FCR, the Report Date, the specific terms of reference and any restrictions or limitations placed upon the Member.
- 4.1.3 The Member must state that the FCR has been prepared in accordance with this Professional Standard.
- 4.1.4 In addition to the contents of this Professional Standard, in deciding on the content and the level of detail for reporting, the Member must have regard to the reporting requirements given in the Society's Professional Standard 9 and any applicable legislation.
- 4.1.5 The Member may need to deal with issues that are not within the relevant skills and experience of the Member. In this situation the Member will need to utilise the skills and experience of others and may rely on other relevant experts provided adequate disclosure is included on the nature of that reliance.

4.2 Information

- 4.2.1 The Member must advise the Entity of the information required, including data and reports that the Member will need, as well as the staff and relevant contractors of the Entity with whom the Member will need to consult, in order to prepare the FCR.
- 4.2.2 The Member must document in the FCR the steps taken to verify to the extent possible the consistency, completeness and accuracy of the information provided by the Entity. Material discrepancies that cannot be resolved with the Entity must be reported in the FCR, together with the consequent limitations of the FCR.
- 4.2.3 Where the Member places reliance upon others to provide information required, and this information is limited, or not forthcoming, the Member must note this in the FCR, together with an assessment of the consequent limitations of the FCR.
- 4.2.4 Where the Entity does not provide adequate and timely access to information (including data and reports) and staff as required by the Member, and the information cannot otherwise be practically obtained, the Member may omit from the FCR analysis that is dependent on that information, but must provide an explanation as to why it has been omitted and an assessment of the consequent limitations of the FCR.
- 4.2.5 The Member must identify in the FCR all information upon which he or she has placed Material reliance in preparing the FCR.

4.3 Matters for consideration

4.3.1 The Member must consider each of the matters listed below, with consideration as at the Report Date of historical analysis and future implications, where applicable:

- (a) business and operations;
- (b) recent experience and profitability;
- (c) pricing, underwriting and claim management;
- (d) insurance and other liabilities;
- (e) investments and other assets;
- (f) reinsurance arrangements;
- (g) capital management;
- (h) solvency assessment;
- (i) capital adequacy; and
- (j) risk management.

4.4 Materiality and Material risks

4.4.1 The Member must take Materiality into account when preparing the FCR. Whether something is Material or not will always be a matter requiring the exercise of the Member's judgement.

4.4.2 The level of detail to be provided in the FCR will depend on the size and complexity of the operations of the Entity and considerations of Materiality.

4.4.3 If, in the opinion of the Member, a matter referred to in paragraph 4.3.1 poses no Material risks to the Solvency Margin, the Member may note this in the FCR and no further reporting is required in respect of this matter.

4.4.4 If the Member identifies additional Material matters, not detailed in 4.3.1, the Member must include such matters in the FCR.

4.5 Business and operations

4.5.1 The FCR must include general background information about the corporate structure operations of the Entity, including financial strength rating from an Approved Rating Agency where applicable. It must also include relevant information about the external environment in which the Entity operates.

(a) General background information includes relevant information about the Entity's Plans, including any conditions imposed on the Entity by RBNZ that do not form part of the Act or regulatory standards.

4.5.2 The Member must comment on Material risks arising from the Entity's Plans at the Report Date.

4.5.3 In preparing the FCR, the Member must comment on whether there is any potential for other parts of the corporate group to which the Entity belongs to Materially affect the Solvency Margin of the Entity.

4.5.4 Unless otherwise required by RBNZ, a single FCR may be produced for an Entity. Where the FCR is produced for an Entity, this single FCR must address separately the operations of each Insurer within that Entity.

4.6 Recent experience and profitability

4.6.1 The Member must comment on the past profitability of the Entity, including consideration of significant features or trends in the Entity's recent experience, over a period of at least three previous years, to the extent that it is available. This assessment must consider premiums, claims, expenses, commissions, investment return, and profits/losses, including any abnormal features.

4.6.2 Deviations of actual experience from the expected experience in the Entity's Plans over at least the period since the previous balance date must also be discussed, including an assessment of the reasons for these deviations.

4.6.3 The Member must comment on the steps taken, or proposed to be taken, by the Board or senior management of the Entity to address areas of deviation from expected experience.

4.6.4 The Member must comment on budget projections, if available, and the extent to which these incorporate recent deviations in actual vs expected experience.

4.7 Pricing, underwriting and claim management

4.7.1 The Member must outline and comment on Material issues arising from the Entity's pricing processes and underwriting and claim management practices.

4.7.2 The Member must comment on the risk profile of the business that has been underwritten. This commentary may include an analysis by sum insured, number of policies written, geographical spread of risks and by Class of Business.

4.7.3 The Member must assess historical premium adequacy and comment on whether expected future profitability is Materially in line with the Entity's Plans.

4.8 Insurance and other liabilities

4.8.1 The FCR must include a summary of the Net Outstanding Claims Liability and Premium Liabilities, and Material considerations arising from, the Insurance Liability Valuation.

(a) The Member must comment on any Class of Business for which the outstanding claims provision adopted by the Board for the statutory accounts is different from the Net Outstanding Claims Liability noted in 4.8.1.

4.8.2 The Member must include an assessment of the adequacy of past Central Estimates of Net Outstanding Claim Liabilities against the subsequent actual claims experience over a period of at least three years, if available.

4.8.3 The Member must include comments on any Material implications for the adequacy of current estimates of Net Outstanding Claims Liabilities arising out of the review of historical estimates.

4.8.4 The Member must comment on the Material risks arising from the Entity's other liabilities, including off balance sheet liabilities.

4.9 Investments and other assets

4.9.1 The Member must comment on the Entity's approach to asset management, state its investment philosophy if any, and summarise the asset allocation.

4.9.2 The Member must comment on Material risks arising from the Entity's:

(a) liability profile and liquidity needs;

(b) investment assets;

(c) other assets;

(d) currency and duration mismatch of assets with respect to insurance liabilities;

(e) methods for valuing assets and non-insurance liabilities, particularly, changes in those methods since the previous valuation; and

(f) treatment of derivatives and the impact on the Solvency Margin.

4.10 Reinsurance arrangements

4.10.1 The Member must state the Entity's reinsurance approach.

4.10.2 The Member must outline and comment on Material risks arising from the use of the Entity's specified reinsurance strategy, having regard to the Entity's liability profile.

4.10.3 The Member must outline and comment on Material risks arising from the Entity's reinsurance arrangements, having regard to the documentation and extent of placement of reinsurance arrangements, obligations to pay future reinsurance premiums and the degree of certainty of the Entity's ability to make reinsurance recoveries under these arrangements.

4.10.4 The Member must outline and comment on Material risks arising from its use of limited risk transfer products.

4.10.5 The Member must comment on the method used to calculate the Entity's Catastrophe Risk Capital Charge and comment on the limitations of the method.

4.11 Capital management

4.11.1 The Member must describe and comment on Material risks arising from the Entity's approach to setting and monitoring capital resources over time, including dividend policy and needs for future capital to support the Entity's Plans.

4.12 Solvency assessment

4.12.1 The Member must summarise the Solvency Standard assessment as at the Report Date and include historical assessments if available. The summary must show the Actual Solvency Capital and Minimum Solvency Capital and detail the individual capital charges as defined in the Solvency Standard.

4.12.2 The Member must comment on trends in the Entity's compliance with its Minimum Solvency Capital, and its capital targets, for the last three years, if available. The Member must comment on the extent of, and reasons for, identified breaches of the Entity's Solvency Margin or of its capital targets since the previous FCR, and the actions that were taken by the Entity to rectify such breaches.

4.12.3 The Member must identify the key inputs to which the Insurer's Solvency Margin is most sensitive and quantify the impact on the Solvency Margin of changes to those inputs.

4.13 Capital adequacy

4.13.1 The Member must report and comment on the Insurer's projected Solvency Margin over the three year period starting from the Report Date. The forward looking assessment of the Solvency Margin must take account of:

- (a) the Insurer's business plans;
- (b) the Insurer's risk management practices;
- (c) the external environment; and
- (d) variations in key assumptions.

4.13.2 The Member must consider and comment on the Entity's capacity to meet its Minimum Solvency Capital and its capital targets over at least the next three years.

4.13.3 The Member must comment on the adequacy of the projected Solvency Margin. The Member must note the basis used to carry out the forward looking assessment of the Solvency Margin.

4.14 Risk management

4.14.1 The Member must comment on Material risks arising from the Risk Management Programme as defined under Section 73 and 74 of the Act.

4.15 Conclusions and recommendations

- 4.15.1 The Member must comment on the Material risks (of which it is reasonable to expect the Member to be aware) facing the Insurer that, in the Member's opinion, pose a threat to the Insurer's ability to maintain an adequate Solvency Margin as at the Report Date and subsequent three years, and where practicable quantify such risks.
- 4.15.2 The Member must comment on any steps being carried out by the Insurer to mitigate these risks and provide recommendations to further address these risks, if required.
- 4.15.3 The Member must state the recommendations set out in the previous FCR and comment on the extent to which the Entity has addressed them.