PGN 108: Transfer of Long-term Business of a Registered Insurer – Role of the Independent Actuary

Classification
Compliance with this professional guidance note is best practice for Actuaries performing the role of Independent Actuary.

Abstract
This professional guidance note outlines the factors that should be considered in accepting an appointment as an Independent Actuary. It also provides guidance on the investigations the actuary might conduct and recommended contents of the resulting report.

Purpose
The purpose of this Professional Guidance Note is to advise an actuary invited to act as the Independent Actuary in a section 37 transfer of the statutory and professional responsibilities such an appointment entails.

Legislation or Authority
The Long-term Insurance Act, 1998 under section 37

Application
An actuary invited to act as an Independent Actuary under section 37 of the Long- term Insurance Act, 1998

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Status
Version 1.0 Effective from January 2004

1. Introduction

1.1 Under section 37 of the Long-term Insurance Act, 1998 any scheme that provides for the whole or part of the long-term business carried on by a South African long-term insurer to be transferred to another body requires the prior sanction of the court. The court will consider the scheme on the basis of a petition by one of the parties, and the petition may be accompanied by a report on the terms of the scheme by an Independent Actuary.

1.2 The parties to the transaction can consider whether or not to appoint an independent actuary or the Registrar of Long-term Insurance may decide to appoint an independent actuary to report to him/her on the desirability or otherwise of the proposed transaction.

1.3 The Independent Actuary should ascertain whether a report may also be required by the courts or regulator in any foreign jurisdiction where the transferor or transferee insurer writes any business. If branch business has been written in a foreign jurisdiction and such business is impacted by the proposed transfer, the Long-term Insurance Act, 1998, and the host country's legislation will be applicable. If the business has been written through a foreign subsidiary, a report may be required in terms of the host country's legislation but not in terms of the Long-term Insurance Act, 1998.

1.4 The independent actuary shall at all times, during and after his/her appointment, observe complete secrecy in relation to the intellectual property of the insurers concerned, except insofar as the actuary's specific responsibilities in terms of the brief by the court or the Registrar may require otherwise.

2. Factors Influencing Acceptance of an Appointment as Independent Actuary

2.1 Before accepting an appointment as the Independent Actuary in any particular case, an actuary must

2.1.1 consider whether he/she has relevant practical knowledge and experience. Such experience would necessarily include familiarity with the role and responsibilities of a Statutory Actuary and with the types of long-term business transacted by the companies concerned.

2.1.2 disclose to all the parties any direct or indirect interest he/she may have or have had in either insurer. Clearly, an actuary cannot act if such interest would, in the opinion of any party or its legal advisers, be likely to prejudice his/her status in the eyes of the court. In case of doubt, the situation should be discussed with the Registrar of Long-term Insurance and the President or President- elect of the Actuarial Society of South Africa before the appointment is accepted.

2.2 The Act provides that a report on the terms of the scheme by an Independent Actuary may be requested by the Registrar. The Registrar will provide a mandate / terms of reference to the appointed actuary identifying the matters on which the actuary should report and any specific matters that the actuary should take into consideration when drafting the report. If so,

2.2.1 The Independent Actuary's primary responsibilities are to the Registrar, as the purpose of the appointment is to secure an independent opinion for the Registrar on the desirability of the transaction and the likely effects of the scheme on the long-term policyholders of both companies concerned.

2.2.2 The Independent Actuary must address specific issues if so required by the Registrar. The Independent Actuary is not, however, constrained to address only these issues if, in the course of his/her investigation, he/she concludes that there are other issues which are of relevance to the transaction or to the interests of policyholders affected by it.

2.2.3 With the exception of any instruction from the Registrar or the courts to advise them on any particular aspect of a transaction, it is improper for the Independent Actuary to take instructions from any of the parties on what should be included in, or excluded from, the report; or to be denied access by any of the parties to persons the Independent Actuary may wish to interview, or to information, reports and documents which the Independent Actuary may reasonably consider material to the formulation of an opinion on the likely effects of the scheme on the long-term policyholders of the companies concerned. An actuary should ensure that this is understood by the parties concerned before accepting an appointment.

2.3 If, for any reason other than the abandonment of the scheme, the Independent Actuary's appointment is revoked or the Independent Actuary resigns prior to his/her report being submitted to the court or being circulated (whether in summary or otherwise) to long-term policyholders, he/she should consider whether the circumstances are such that he/she should make them known to the Registrar. Any actuary offered an appointment as an Independent Actuary should enquire if the appointment has previously been accepted and subsequently vacated by another actuary; if so, he/she should take all reasonable steps to establish the circumstances in which the revocation of the previous actuary's appointment or the resignation of the previous actuary took place.

3. The Extent of the Independent Actuary's Involvement

3.1 Given that the court is unlikely to sanction the scheme if the Independent Actuary indicates serious dissatisfaction with its terms, it is in the interest of all the parties that, once an actuary has been appointed to that role, he/she is informed of the draft terms and provisions of the proposed scheme at the various stages of its development. The Independent Actuary should therefore actively seek such information and be prepared to indicate with impartiality any terms or provisions which by their inclusion in or omission from the scheme as drafted, as the case may be, would be likely to cause him/her to express reservations about the scheme in the report.

3.2 The Independent Actuary should establish, at an early stage, whether there are any matters pertaining to the scheme that the Registrar wishes to draw to his/her attention. The Independent Actuary should maintain this line of communication until the scheme is presented to the court.

3.3 The amount of investigative work that the Independent Actuary will need to do will depend on the circumstances of the case. The Independent Actuary should communicate with the Statutory Actuaries of all affected companies. It is reasonable for the Independent Actuary to expect the Statutory Actuary of the transferor company to provide such valuations of the assets and liabilities as the Independent Actuary may require, and to disclose information on such matters as how bonus rates have been determined in recent years in respect of any with-profit business. If the transferee company already conducts long-term business similar information from the Statutory Actuary of that company may be necessary. In cases of any complexity, it is desirable for the petition to be accompanied by a report from any Statutory Actuary concerned, although this may not be a legal requirement unless the Registrar specifically requests such report in terms of section 38(1)(a)(ii). There may also be private actuarial reports to one or more of the parties, production of which would assist the Independent Actuary in appraising the terms of the scheme. The Independent Actuary must, however, form an independent judgment on the quality of the information supplied, the reasonableness of the work of other actuaries, and, therefore, the extent of any investigative or verification work the Independent Actuary needs to do.

3.4 The Independent Actuary might be asked to attend a meeting with the policyholders organised by the management of one of the companies. If so, the Independent Actuary should consider carefully whether to do so would give the impression that he/she is not completely independent. If the Independent Actuary decides to attend the meeting, his/her position should be properly explained, and nothing that the Independent Actuary does or says at the meeting should undermine the perception of independence.

3.5 In the case of a transfer involving a composite company, writing both long-term and short-term business, the Independent Actuary will need to understand the relevance of the short-term insurance business to the security of the long-term policyholders, and he/she may need to seek independent specialist advice on this.

3.6 Special considerations may also be called for where the transfer forms part of a chain of events including restructure, reinsurance or changes in ownership, and the Independent Actuary should seek explanations regarding corporate plans to the extent necessary for the whole picture to be clear.

3.7 If the Statutory Actuary of any affected company has held that position only for a relatively short period of time, it may be appropriate for the Independent Actuary to seek information from the previous Statutory Actuary.

3.8 Other documents the Independent Actuary will normally wish to examine in relation to each of the companies involved in the transfer will include:

3.8.1 its memorandum and articles of association and, if the company is currently trading, its latest annual financial statements and statutory returns;

3.8.2 the latest report submitted by its Statutory Actuary to the directors on the financial soundness of the long-term insurer,

3.8.3 any reports, actuarial or otherwise, dealing specifically with policyholders' reasonable expectations;

3.8.4 the bases used for illustrations of possible future benefits;

3.8.5 sample quotations and policy documents which state or illustrate how policies will participate in profits, qualify for discretionary benefits, or be subject to future variations in charges.

3.8.6 any reports dealing with the composition of any portfolio of assets to be transferred, the appropriateness of such assets when compared to the liabilities, and the relevant investment policies of the insurers;

3.8.7 any reports evaluating alternative schemes;

3.8.8. any reports detailing the ability of the transferee insurer to absorb the business transferred into their systems environment; and

3.8.9 any other relevant documents associated with the transfer.

3.9 In addition, the Independent Actuary should ask about the operational plans of any company which, after` the effective date, will have policyholders who fall within the ambit of the Independent Actuary's report.

4. The Report

4.1 The Independent Actuary's report on the desirability of the scheme is usually commissioned by the Registrar and will accompany the Registrar's report to the court. However it is likely that the full report will be made available for inspection by any person and therefore by any policyholder or shareholder. The Independent Actuary should therefore bear in mind in preparing the report that policyholders and shareholders may rely on it when considering how to cast their vote in any extraordinary general meeting called to approve the terms of the scheme, and any member of the public may rely on it when considering whether or not to make representations to the court about the likely adverse effect of the scheme on him or her.

4.2 Similar considerations apply to any summary of the Independent Actuary's report that is to be sent to policyholders and shareholders of the companies concerned. It is the Independent Actuary's responsibility to ensure that the contents of the summary are adequate, and that neither it nor any document that will accompany it gives a misleading impression of the findings in the full report. The summary need not contain background factual matter contained in the accompanying documents.

4.3 It follows from 4.1 that the Independent Actuary needs to consider and report as appropriate on the likely effects of the scheme on any person who has an interest in the matter which will include

(a) all transferring long-term policyholders,
(b) any long-term policyholders of the transferor company whose policies will remain with that company, and
(c) any long-term policyholders of the transferee company.

Whilst not directly concerned with the effect of the scheme on those who become policyholders on or after the date when, subject to the approval of the court, it will become effective, the Independent Actuary will need to consider whether the development plans of any of the companies involved may adversely affect policyholders with whom he / she is concerned.

4.4 It is a responsibility of the directors and managers of the relevant long- term insurance company to consider alternative arrangements in order that the company may fulfil its obligations to conduct its business with due regard to the interests of policyholders and potential policyholders. The term 'Independent Actuary' might be interpreted by members of the public to indicate that the actuary was advising on the relative merits of one scheme of transfer against other possible arrangements, although this is not specifically required by the legislation. Consistent with the nature of the legal requirements, the report must include a comparison of the likely effects on the long-term policyholders of the relevant companies if the scheme of transfer being presented to the court is or is not implemented. In addition, the Independent Actuary should state clearly whether or not reports of alternative arrangements were considered.

4.5 The contents of the Independent Actuary's report will be influenced by the circumstances of each case; the following are, however, some of the matters which the Independent Actuary should, where appropriate, cover in it:

4.5.1 The name of the party that has appointed the Independent Actuary and a statement of who is bearing the costs of that appointment.

4.5.2 A statement of the Independent Actuary's professional qualification.

4.5.3 Whether or not the Independent Actuary has a direct or indirect interest in any of the parties that might be thought to influence the Independent Actuary's independence; if the Independent Actuary has an interest, it should be disclosed.

4.5.4 The scope of the report in accordance with Paragraph 4.4 above.

4.5.5 The purpose of the scheme.

4.5.6 A summary of the terms of the scheme in so far as they are relevant to the contents of the Independent Actuary's report.

4.5.7 What documents and reports the Independent Actuary has considered in relation to each of the companies involved in the transfer and whether there was any additional information that was requested but not provided.

4.5.8 The cost and tax consequences of the scheme, in so far as these may affect policyholders' benefits.

4.5.9 The effect of the scheme on the security of policyholders' contractual benefits.

4.5.10 The effect of the scheme on the nature and value of any rights of policyholders to participate in profits. In particular, if any such rights will be diluted by the scheme, how any compensation being offered to those policyholders as a group (which might take the form of an injection of funds, an allocation of shares, or cash payments) compares with the value of that dilution, and whether the extent and method of its proposed division is equitable as between different classes and generations of policyholders.

4.5.11 The likely effect of the scheme on the approach used to determine the amounts of non-guaranteed benefits such as reversionary and terminal bonuses, vested and non-vested bonuses and surrender values, and the levels of discretionary charges, for example under unit-linked policies; and what safeguards are provided by the scheme against a subsequent change of approach that could act to the detriment of existing policyholders of either company and is not due to external circumstances beyond its control.

4.5.12 The likely effects of the scheme on matters such as investment management, new business strategy, administration, expense levels and valuation bases, in so far as they may affect the ability of the companies to meet throughout the lifetime of existing policies the reasonable expectations of the holders of those policies.

4.5.13 In the case of any mutual company involved in the scheme, the effect of the scheme on the proprietary rights of members of that company and, in particular, the significance of any loss or dilution of the rights of those members to secure or prevent further constitutional changes which could affect their expectations as policyholders (for example, losing the ability to change the board and therefore control over a board's decision to convert to a closed fund). The Independent Actuary should state whether, and to what extent, members will receive compensation under the scheme for any diminution in their proprietary rights, and comment on its appropriateness. Also, when commenting on the fairness of the scheme, the Independent Actuary should pay particular attention to any differences in treatment between policyholders with voting rights and those without. It will assist the Independent Actuary if the issues involved are adequately explained in the directors' circular to policyholders.

4.5.14 Where a particular portfolio of assets will form part of the transfer, the effect of the transfer of such assets on the relevant investment policies of the transferee and transferor insurers and any impact that the transfer may have, positive or negative, on the ability of the relevant insurer to satisfy the reasonable expectations of policyholders.

4.5.15 Which matters, if any, the Independent Actuary have not taken into account or evaluated in the report that might nevertheless be relevant to policyholders' consideration of the scheme.

4.5.16 The Independent Actuary's overall assessment of the likely effects of the scheme on the reasonable expectations of long-term policyholders; whether the Independent Actuary is satisfied that for each of the companies concerned the scheme is equitable to all classes and generations of its policyholders; and whether for each relevant company the scheme places obligations on the directors, or provides for future certification by its Statutory Actuary, sufficient in the Independent Actuary's opinion for the protection of those expectations.

4.6 Where the Independent Actuary expresses an opinion in the report, he/she should outline the reasons for it.