INSTITUTE AND FACULTY OF ACTUARIES

EXAMINATION

20 April 2018 (pm)

Subject SA2 – Life Insurance Specialist Applications

Time allowed: Three hours

INSTRUCTIONS TO THE CANDIDATE

1. *Enter all the candidate and examination details as requested on the front of your answer booklet.*

2. *You must not start writing your answers in the booklet until instructed to do so by the supervisor.*

3. *You have 15 minutes of planning and reading time before the start of this examination. You may make separate notes or write on the exam paper but not in your answer booklet. Calculators are not to be used during the reading time. You will then have three hours to complete the paper.*

4. *Mark allocations are shown in brackets.*

5. *Attempt both questions, beginning your answer to each question on a new page.*

6. *Candidates should show calculations where this is appropriate.*

AT THE END OF THE EXAMINATION

Hand in BOTH your answer booklet, with any additional sheets firmly attached, and this question paper.

In addition to this paper you should have available the 2002 edition of the Formulae and Tables and your own electronic calculator from the approved list.

1 Company A and Company B are UK life insurance companies. Company A is considering the purchase of Company B's existing unit-linked pension policies.

(i) Compare the roles of the PRA and FCA in a transfer of liabilities from one UK life insurance company to another. [3]

Company B's existing unit-linked pension business is made up of three different types of group pension business. None of these products are open to new business.

The products are:

- A group pension product that was targeted at company executives or directors. Each group scheme had a small number of members at outset but with a high average policy size. There are discounts available to the annual management charge when policy size reaches certain levels.

- A group pension product that was targeted at small employers. More administration is done by the insurance company than for other schemes, but at a higher annual management charge. Many of these schemes only have one employee left in them.

- A group pension product that was targeted at the medium-sized employer market. It offered optional additions to the pension of:

  - Pension contribution protection – where the employee's own pension contributions would be paid at the current level for a period of time if the employee was off work sick for more than a specified period and with medical evidence. This incurs an additional annual charge.

  - A loyalty bonus – where an employee's pension fund is increased by an additional 1% at each ten year anniversary, as long as it remains with the insurance company and pension contributions are still being paid.

(ii) Describe the concerns that the regulators would have regarding the policyholders in both companies, in respect of the potential transfer of the group pension policies. [6]

(iii) Suggest actions that Company A could take in order to address the regulators' concerns. [10]

The transfer will involve transferring across the assets backing Solvency II technical provisions for these products, plus an additional amount to be determined between the two companies.

(iv) Discuss the factors that Company A would take into account when determining an acceptable value for this additional amount. [8]

Company A was successful in acquiring Company B's existing unit-linked pension business. A few years after the acquisition have now passed. The UK government is considering changing the pensions tax regime.

(v) Suggest changes the government could make to the pensions tax regime. [7]

(vi) Discuss the potential impacts such changes could have on policyholder behaviour. [6]

(vii) Discuss the potential implications for Company A of a change to the pensions tax regime. [8]

[Total 48]

2 A UK proprietary life insurance company has been selling a term assurance product for some time through financial advisers. It has not sold any other products.

The company is launching a new single premium unit-linked bond. Policyholders will be able to invest in a range of unit-linked funds made available by the company. The death benefit is 101% of the value of the policyholder's units on death and the surrender value is equal to the value of the policyholder's units on surrender. An annual management charge, based on the value of the unit funds, is applied monthly. The policyholder can make additional single premium increments, or make withdrawals, at any time. The new product is to be sold to individual policyholders through the same financial advisers.

(i) Describe the additional requirements that the financial advisers must now meet to enable them to sell the new bond, including those requirements relating to advice and remuneration. [10]

The company adopts "Old UK GAAP" for reporting its financial results under International Financial Reporting Standards (IFRS).

(ii) Explain how the two products sold by the company would be classified under IFRS. [2]

(iii) Compare the accounting approaches under IFRS for the two products. [6]

Under Solvency II, the company uses the standard formula approach to determine its Solvency Capital Requirement (SCR).

(iv) Assess the likely implications of launching the new product for the various components of the SCR. [14]

The company is keen to seek opportunities to sell the new product to existing term assurance policyholders and to encourage the sale of term assurances to potential policyholders of the new single premium bond.

(v) Explain why this might be difficult in practice. [5]

(vi) Suggest actions that the company could take in order to address these difficulties. [4]

The company wants to understand which current term assurance customers are the most valuable to it. It has been suggested that use could be made of the existing cashflow models and the associated Solvency II Pillar 1 and IFRS calculations in order to determine a customer value.

(vii) Describe the adjustments that the company might need to make to its data to enable a customer value to be determined. [3]

(viii) Discuss how the company might use and adapt its existing calculations to determine a value for an individual customer. [8]

[Total 52]

END OF PAPER