



Financial Reporting Council

TAS 100 Guidance

Proportionality – Exposure Draft

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1 Introduction

Purpose

- 1.1 The purpose of this guidance is to assist practitioners in applying proportionality when complying with the requirements of the Technical Actuarial Standards (TASs).
- 1.2 Paragraph 1.8 of TAS 100 says:

In applying judgement to the application of the TASs it is important to be guided by the **reliability objective**.

The TAS 100 glossary defines the **reliability objective** as follows:

To allow the **intended user** to place a high degree of reliance on **actuarial information**, practitioners **must** ensure the **actuarial information**, including the communication of any inherent uncertainty, is relevant, based on transparent assumptions, complete and comprehensible.

- 1.3 The defined terms used in TAS 100 apply to this guidance.

Intended Audience

- 1.4 A 'practitioner' is a person carrying out work that is classified as Technical Actuarial Work as defined in TAS 100.
- 1.5 This guidance is aimed at practitioners who require guidance in exercising judgement in respect of proportionality in the application of the TASs.

2 Proportionality

Interpretation

- 2.1 The reliability objective underpins the TASs and, as stated in paragraph 1.8 of TAS 100, it is important to be guided by it when applying the requirements of the TASs.
- 2.2 The intent is that the requirements of the TASs should be met in a way that is proportionate to the nature, scale and complexity of the decision or assignment to which the technical actuarial work relates and the benefit that the intended user would be expected to obtain from the work.
- 2.3 Proportionality does not mean that a principle can be ignored. It does, however, allow the practitioner to judge the extent of the work required to comply with the principle.
- 2.4 In considering how to apply proportionality the following may be considered:
 - The materiality of the matter (see below)
 - The significance of the piece of work including any financial, reputational or other consequences for the intended user;
 - The complexity of the decision or factors to the decision;
 - The expectations of the intended user;
 - The knowledge and expertise of the intended user; and
 - The extent to which judgement is required.

TAS Principles and Application

- 2.5 Paragraphs 1.6 and 1.7 of TAS 100 set out the following:
 - 1.6 This standard consists of Principles and related Application statements. The Principles set out mandatory requirements.
 - 1.7 The Application statements set out regulatory expectations. Practitioners **must** have regard to these regulatory expectations; divergence may be acceptable but **must** be justified. The justification **must** demonstrate how compliance with the relevant Principles has been achieved despite not meeting regulatory expectations.
- 2.6 Divergence from application statements is permissible provided this can be justified. In some cases, proportionality may be a consideration.

Materiality

- 2.7 The TAS 100 Glossary defines 'material' as follows:

Material

A matter is **material** if it could, individually or in combination with other matters, influence the decisions to be taken by the **intended user**. Assessing whether a matter is **material** is a matter for judgement, requiring consideration of the **intended user** and the context in which **technical actuarial work** is performed and communicated.

- 2.8 When determining if something is 'material' for the purposes of TAS 100, practitioners should be mindful that the question of whether a matter is material is one which might change over time as the needs and circumstances of the user change. Similarly, materiality can depend on the context, for example:

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- something may be immaterial when considering the financial position of an entity as a whole, whereas the same thing may be material when considering only a small part of the portfolio of the entity; or
 - something may be material, irrespective of its relative financial value, by virtue of it being of particular interest to a particular group of users, a regulator or supervisor.

2.9 As stated in the Glossary, assessing whether a matter is material is a matter for judgement. P2.1 requires practitioners to base judgement on supporting justification and P6.1 requires practitioners to document judgements and their supporting justifications. Further A2.1 requires the following:

A2.1 The practitioner's supporting justification for a particular judgement **should** allow the **intended user** and other relevant parties (such as a peer reviewer, auditor or regulator) to conclude that the particular judgement is reasonable

- 2.10 Certain mandatory requirements apply only where something is material. Where different practitioners' views might differ on whether a matter is material, the practitioner is encouraged to adopt a cautious approach by complying with the requirements that apply where something is material.
- 2.11 For example, the risk identification principle (Principle 1) only requires regard to be had to material factors and material risks. If a risk is identified but is clearly not material in the context of the work carried out, then it is sufficient to note this (with a justification) and do nothing further in relation to this risk. In concluding that the risk is clearly not material, the practitioner would consider whether other practitioners would arrive at the same view.
- 2.12 In relation to the exercise of judgement, when exercising judgement which is not deemed to be material, then Principle 2 (Judgement) may be complied with in relation to that judgement by complying with P2.1 (and the associated application statement A2.1). As P2.2 to P2.4 relate to material judgements, these would not be applicable in relation to this particular judgement. Again, the practitioner would need to consider whether other practitioners would arrive at the same conclusion.

'Sufficient' and 'appropriate'

- 2.13 Taking a proportionate approach to compliance with the TAS is reflected by the use of the words 'sufficient' and 'appropriate' within the standard.
- 2.14 As an example, P5.2 requires an 'appropriate level' of model governance, requiring the practitioner to judge what is appropriate in relation to the work being carried out.
- 2.15 Similarly, P5.3 requires practitioners to 'consider sufficiently' whether models used contain unintended biases, allowing judgement in relation to amount of effort required to ascertain whether such biases are present.
- 2.16 Principle 6 (Documentation) requires documentation to contain 'sufficient detail' to allow persons responsible for reviewing, auditing or validating the technical actuarial work to understand the matters involved and assess the judgements made. This allows the practitioner to consider whether the work will be reviewed, audited or validated, and by whom and, based on this, decide on the level of detail required.

Communications

- 2.17 Principle 7 (P7.3) requires the exclusion of non-material information from communications if the inclusion of this information would obscure material actuarial information.
- 2.18 This also requires the practitioner to exercise judgement in the amount of detail to be included in communications.

2.19 In addition, many of the communications requirements are expressed as regulatory expectations in the form of 'the practitioner should' (in application statements – see also [2.6](#) above).

3 Scenarios

This section contains a few illustrative examples in the form of scenarios. In practice actuaries will have to make their own judgements dependent on the specific circumstances.

Scenario 1: Non-material Judgement

- 3.1 A life insurer's portfolio of insurance obligations includes very little morbidity risk and the solvency ratio of the portfolio as a whole is known from past experience to be relatively insensitive to changes to the morbidity assumptions. For this reason, the actuary has decided to review the morbidity valuation assumptions only once every three years.
- 3.2 The judgement exercised is that reducing the frequency of review of this solvency valuation assumption will not have a significant impact on the overall outcome of the solvency assessment of the insurer's portfolio of liabilities and will thus not materially affect any decisions taken based on that outcome. Further, the reduced frequency of review will save time (and cost).
- 3.3 In this case, the actuary concludes that for the purpose of the solvency valuation of the insurer's portfolio of insurance obligations Principle 2 (Judgement) can be complied with by documenting in a couple of paragraphs the justification for this judgement. The documentation is likely to be relevant to the colleague carrying out peer review and to the firm's auditors and is written with these parties in mind.
- 3.4 Communications for the Board should provide sufficient information to allow the Board to understand the judgement made. In this case the communications for the Board will include a general statement to say that non-material judgements have been exercised but do not warrant further commentary given the low materiality.

Scenario 2: Material Judgement

- 3.5 The same life insurer has a significant portfolio of annuity contracts and it is known from past experience that the outcome of the solvency valuation of the insurer's portfolio as whole is highly sensitive to the annuitant mortality assumptions.
- 3.6 The actuary decides to propose the use of a new in-house mortality table based on the firm's own experience. This is a change from the past approach of using industry mortality tables.
- 3.7 The judgements exercised include that the firm's own book of annuities is sufficiently large for developing a 'house-table', that the work carried out to develop the table is sufficiently reliable and that the new table will lead to a more representative result overall.
- 3.8 This is deemed to be a very material combined judgement. Therefore, P2.2 to P2.4 and the associated Application statement would need to be complied with in full (as would the related Documentation and Communication requirements). The actuary decides that the documentation of the supporting justification will need to be in the form of a detailed paper which is then summarised in communications to the intended user. In this case, communications should provide sufficient information to allow the intended users to understand the materiality of the combined judgement exercised relative to the alternative reasonable judgement of retaining the existing approach of using industry tables. The actuary may in this case have two intended users: a senior manager and the Board. The communications to the senior manager may include more technical information than the communication to the Board.

Scenario 3: Materiality and Proportionality - pensions

- 3.9 Following a recent acquisition, 30 employees have been admitted to a large pension scheme on special benefits and their circumstances are not fully covered by established valuation methodologies, so the actuary needs to

advise on what methodology should apply to these cases. The members concerned are not paid significantly above the average for the sponsoring firm.

- 3.10 The actuary first needs to consider the context; will the methodology be used for assessing the value of individual members' benefits or for the triennial valuation of the pension scheme as a whole or both.
- 3.11 In the case of a methodology for use in assessing the value of individual members' benefits, the advice is 'technical actuarial work' falling within TAS 100, and the associated decision of the intended users (the Trustees) could have a non-negligible effect on the individual beneficiaries affected. It is therefore unlikely to be reasonable for the actuary to conclude that his or her advice could not influence the Trustees as to the methodology to apply. Consequently, the actuary's communications will need to reflect this by including sufficient relevant information to allow the Trustees to make informed decisions.
- 3.12 In the case of a methodology for use in the triennial valuation of the pension scheme, the advice is 'technical actuarial work' falling within TAS 100. However, it is likely to be 'immaterial' to the intended users and so the principle of 'proportionality' might appropriately be applied to keep the extent of the advice (or even the choice of methodology) within the level of benefit that the intended user might expect to derive from that work. In particular, for 'communications' because their financial significance for the company is negligible, a 'proportionate' approach under TAS 100 may justify no details being communicated (in relation to these members' special benefits) under several of the TAS provisions.

Scenario 4: Materiality and Proportionality -insurance

- 3.13 A With-Profits Actuary is recommending revised final bonus rates to the Board. The firm has numerous funds, and each fund has multiple bonus series, many of which have different underlying asset mixes. Each bonus series contains multiple bonus rates for different policy terms and types. Consequently, the actuary is recommending changes to many thousands of different bonus rates. Whilst many of these bonus rate changes will not be financially material to the firm, they could be material to individual policyholders. However, there are no sharp changes in approach and no exceptional changes in particular bonus rates.
- 3.14 In this case, the advice is 'technical actuarial work' falling within TAS 100, and the associated decision of the intended users (the Board) could have a non-negligible effect on the individual beneficiaries or policyholders affected. It is therefore unlikely to be reasonable for the actuary to conclude that his or her advice could not influence the Board as to the bonus rates to apply. Consequently, the actuary's communications will need to reflect this by including sufficient relevant information to allow the intended users to make informed decisions.
- 3.15 However, in the context of materiality to the insurance company as a whole, the advice might be 'immaterial' (in a wider financial sense) to the intended user. In this case the principle of 'proportionality' might appropriately be applied to keep the extent of the advice to a level proportionate to the level of benefit that the intended user might expect to derive from that work. In particular, for 'communications' in relation to those bonus rates to which the Board would not give individual consideration because their financial significance for the company is negligible, a 'proportionate' approach under TAS 100 may justify no details being communicated in relation to those particular bonus rates under several of the TAS provisions.



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