ASP Guidelines
Governing Implementation of
Amended Pre-Need Rule 31 (PNUCA)
Issued February 1, 2008

These Guidelines are being issued by the Actuarial Society of the Philippines for its members in their actuarial practice when "computing" and "validating" pre-need liabilities in accordance with Pre-Need Rule 31, as amended. Since these Guidelines pertain only to the implementation of Amended Pre-Need Rule 31, these Guidelines do not supersede the ASP's previously issued "Guidelines to Actuarial Practice in Pre-Need" adopted on November 18, 2005. Statements in the November 18, 2005 Guidelines not contradictory to statements in these Guidelines are deemed applicable to these Guidelines as well.

Pre-Need Rule 31 states that the "revised requirements on reserving and liability recognition of pre-need companies" cover the audited financial statements *for the period ended December 31, 2007 and thereafter.*

Pre-Need Rule 31 also states that Associates and Affiliates of the ASP will be allowed to compute and validate Pre-Need Reserves. Thus, these Guidelines apply to all members of the ASP.

The responsibilities of ASP members with respect to Pre-Need practice are as follows:

1. **Fellows (Actuaries) ---** Product Design and Pricing, Valuation of Actuarial Reserve Liability (ARL), Computation and Validation of Pre-Need Reserves (PNR)

2. **Associates and Affiliates ---** Computation and Validation of PNR

The following requirements under Pre-Need Rule 31, as amended require the special attention and interpretation of the Actuary / Associate / Affiliate:

1. "*12 (b) In recognizing the Pre-need Reserves (PNR) for educational and pension plans, the general requirements of PAS 37 on provisioning and the specific methodology provided under this item shall be complied with by the company. For life plans, the requirements of PFRS 4 (Insurance Contracts) shall be complied with by the company*"

    1.1. In using PAS 37 (please refer to the attached), the Actuary / Associate / Affiliate should not treat the PNR as a contingent liability. The Actuary should comment that this is a contractual, and not a contingent, liability.

2. "*12 (c) The amount recognized as a provision to cover the PNR shall be the best estimate of the expenditure required to settle the present obligation at the balance sheet date. The risks and uncertainties that inevitably surround many events and circumstances shall be taken into account in reaching the best estimate of a provision."*

    2.1. The Actuary / Associate / Affiliate should interpret "present obligation" as present value of the obligation, not literally as only the present obligation, as such becomes inconsistent with the subsequent paragraph under item 12(d) of Pre-Need Rule 31, as amended.

    2.2. Inflows and outflows from each policy are not guaranteed to occur, i.e. there are risks and uncertainties that may affect occurrence of the inflow or outflow. Given this, the Actuary / Associate / Affiliate should discount such inflows and outflows using interest and adjust the results to reflect the probability of occurrence of each risk or uncertainty. Risks and uncertainties include, but are not limited to, the following:

- o Lapse – Lapsed plans are plans which are delinquent in payment and whose delinquencies extend beyond the grace period. Such plans have the option of reinstating, thereby restoring premiums and benefits for the plan. Lapsed plans whose delinquencies extend beyond a stated period are cancelled and all benefits are forfeited.

- o Surrender – If a plan is surrendered, a termination benefit may be paid.

- o Reinstatement – If a lapsed plan is reinstated, benefits and premiums for the policy will again be payable.

- o Cancellation – If a plan is cancelled, all benefits, termination values, and installment payments will no longer be payable. Cancelled plans may not be reinstated.

- o Death – If the payor of a policy dies, installments will no longer be payable. Benefits, however, are preserved. For some plans, if the payor of a policy dies, benefits or services become due.

- o Disability – If the payor of a policy is disabled, premiums will no longer be payable. Benefits, however, are preserved.

3. "*12(d) Since the effect of the time value of money for pre-need plans is material, the amount of provision shall be the present value of the funding expected to be required to settle the obligation with due consideration of the different probabilities, as follows:*

"(i) For currently being paid plans,

"(1) Provision for termination values shall consider the surrender rate experience of the company. The trend of surrender experience shall be disclosed in the company's notes to financial statements."

- For each plan currently being paid, there is a possibility that a surrender will occur in the future. Upon such surrender, a termination benefit will be payable. The value of the termination benefit for each year in the future, discounted to the present, using interest and probability of surrender, will reflect the provision for termination values of this set of plans. The Actuary / Associate / Affiliate must disclose the surrender rate experience per policy year, or per relevant period, to the auditor, to be included in the company's Notes to Financial Statements. Installment inflows are not considered in the provision for termination values as these are considered in the succeeding section discussing liability for plans that will become fully paid up.

"(2) A liability for plans that will become fully paid shall be computed as equal to the present value of future maturity benefits reduced by the present value of future trust fund contributions required in accordance to the "Product Model". The discounting interest rate to be used is the 'approved hurdle rate' per Product Model."

- Each plan currently being paid which is neither surrendered nor cancelled will be entitled to benefit(s) in the future. For each such plan, the benefit(s) at each designated period after valuation date should be discounted to the present using interest and probability of persistency. Similarly, for each plan, the installment payment at each designated period after valuation date should be discounted to the present using interest and probability of persistency. The difference between the 2 discounted values will reflect the provision for benefit payment(s) for this set of plans.

- The Actuary / Associate / Affiliate should note that the provision resulting from the use of the hurdle rate per product model may not be sufficient to fund the benefits if investment income rates actually earned are lower than the hurdle rate used for valuing the provision/liability. This fact should be disclosed by the Actuary / Associate / Affiliate in any report to be submitted and in any certification to be issued by him/her.

"(ii) On lapsed plans (meaning plans that have not completed missed due installment contributions within the 60-day grace period) *within the allowable reinstatement period, provision for termination values applying the reinstatement experience of the company. The trend of reinstatement experience shall be disclosed in the company's notes to financial statements;"*

- There is a probability that some of these plans could resume paying contributions. The Actuary / Associate / Affiliate should:

    - compute for the provision for such plans based on the actuary's estimate of the probable number of plans that will be reinstated, and,

    - disclose the assumed rate of reinstatement to the auditor, and whether such assumption is based on the experience of the company or of other companies, for such disclosure to be indicated in the financial statements.

"(iii) Fully Paid Plans, (Plans that have completed the required contributions to the Trust Fund). Pre-Need Rule 31, as amended allows that these be grouped in two batches, and separate provisions be computed for each.

*"(1) For those due for payment within the next (5) five years (*following the date provisions are computed)*, the reserve shall be the present value of future maturity benefits discounted at the attainable rate, as determined and certified by the company's trustee , using industry best practices and principles which shall be indicated in such certification."*

- In disclosing the assumptions, the Actuary / Associate / Affiliate should state that the provision resulting from the use of the interest rate determined by the trustee of the fund may not be the sufficient amount needed to represent the liability that should be in the trust fund to assure payment of the promised benefits defined in the pre-need contract, since the said rate assumed as of the date the plan's trust fund contributions were computed may differ from the actual average of the yield rates of the trust fund following that date.

*"(2) For those not yet due for payment within the next five (5) years (*from date provisions are computed)*, the reserve shall be the present value of the future maturity benefits discounted at the approved hurdle rate per Product Model of the company."*

- The effect of using the hurdle rate could reduce the amount of provisioning, should the hurdle rate be higher than the projected attainable yield rate of return of the trust fund.

- In disclosing the assumptions, the Actuary / Associate / Affiliate should state that the provision resulting from the use of the hurdle rate may not be the sufficient amount needed to represent the liability that should be in the trust fund to assure payment of the promised benefits defined in the pre-need contract, since the hurdle rate assumed at the date the plan's trust fund contributions were computed may differ from the actual average of the yield rates of the trust fund following that date. This fact should be disclosed by the actuary in any report to be submitted and in any certification to be issued by him/her.

4. *"12 (e) Future events that may affect the foregoing amounts shall be reflected in the amount of provision for PNR, where there is sufficient objective evidence that they will occur."*

   4.1. To comply with this requirement, the Actuary / Associate / Affiliate should disclose all assumptions used in determining the PNR. Refer to the paragraphs above requiring that the Actuary state that the provision resulting from use of such assumptions may not be sufficient to assure payment of promised benefits defined in the pre-need contract.

   4.2. If validation is made by an Actuary:

   - the Actuary should disclose the Actuarial Reserve Liability (ARL) computed in accordance with the Actuarial Society of the Philippines' "Guidelines to Actuarial Practice in Pre-Need".

   - the Actuary may apply the Liability Adequacy Test to determine the best estimate of the rate to be used. He/She should also disclose the basis used in determining the best estimate, and take into consideration all the applicable decrements in the formula for determining the liability.

5. *"12 (k) The disclosure requirements under PAS 1, relative to methods and assumptions used to estimate the PNR, including sensitivity of the PNR amount, shall be complied with."*

   5.1. The Actuary should include disclosures on the funding and reserving gaps.

   5.2. The Actuary / Associate / Affiliate should disclose sensitivity of the PNR to adverse deviations in assumptions.

6. *"13 Other Reserves*

   "The company shall set up other provisions in accordance with PAS 37 to cover its obligations such as Insurance Premium Reserve."

   6.1. Such amounts are to be valued by an actuary.

   "Unless the Commission shall so specifically require, a company may at its option set up other provisions as a prudent measure."

   6.2. The Actuary / Associate / Affiliate should advise the pre-need company to set up as part of other provisions, i.e. Other Reserves, the excess of the ARL computed over the PNR, as a prudent measure.

7. Finally, for computations or validations being done by:

   7.1. <u>An Associate or Affiliate of the ASP</u>, the attached validation certificate template in Annex "A" should be used in lieu of the validation certificate templates provided by the SEC in Interpretative Bulletin Number 1. Notably, Annex "A" contains the following qualifications not present in the original SEC template:

      7.1.1. That the Pre-Need Reserves (PNR) were computed according to item 12 of SEC Pre-Need Rule 31, as amended, and may not be adequate to pay for all the contractual benefits of the Pre-Need Company

7.1.2. That the Actuarial Reserve Liability (ARL), computed in accordance with the Actuarial Society of the Philippines' "Guidelines to Actuarial Practice in Pre-Need", is the actuarially accepted measure of liabilities of a pre-need company and that the PNR may be significantly different from the ARL

7.1.3. That an accompanying Pre-Need Reserve Computation Report be prepared subject to the following guidelines

7.1.3.1. The Pre-Need Reserves for each type of plan should be shown

7.1.3.2. The assumptions for each class of reserves should be indicated. The Associate/Affiliate should ensure that such assumptions are NOT referred to as "Actuarial Assumptions". Such assumptions should instead be referred to as "Pre-Need Reserve Assumptions"

7.1.3.3. The basis for the assumptions listed should be disclosed e.g. Discount Rate - based on SEC Pre-Need Rule 31, as amended.

7.1.4. That he/she is an Associate or Affiliate of the ASP as the case may be, and that he/she recommends that a Fellow of the ASP be asked to determine the ARL

7.2. <u>an Actuary or Fellow of the ASP</u>, the attached validation certificate template in Annex "B" should be used in lieu of the validation certificate templates provided by the SEC in Interpretative Bulletin Number 1. Notably, Annex "B" requires the following:

7.2.1. That the Actuary determine and disclose the ARL following the Actuarial Society of the Philippines' "Guidelines to Actuarial Practice in Pre-Need"

7.2.2. That an accompanying Actuarial Valuation Report be prepared in accordance with the Actuarial Society of the Philippines' "Guidelines to Actuarial Practice in Pre-Need".

<u>Annex "A"</u>

Declarations on Computation of Pre-Need Reserves

I have undertaken the computation of the Pre-Need Reserves of the *<u>(specify whether education plan, life plan or pension plan)</u>* of *<u>(name of Pre-Need corporation)</u>* as of *<u>(date of computation)</u>*.

I have relied on data submitted by *<u>(Name and Position of Responsible Person)</u>* and have conducted the tests necessary to satisfy myself on the reasonableness and integrity of such data.

I hereby state that:

1. The assumptions used in this computation are based on item 12 of SEC Pre-Need Rule 31, as amended, and may not be adequate to pay for all the contractual benefits of the Pre-Need Company;

2. The Actuarial Reserve Liability (ARL), computed in accordance with the Actuarial Society of the Philippines' "Guidelines to Actuarial Practice in Pre-Need", is the actuarially accepted measure of liabilities of a pre-need company and that the PNR may be significantly different from the ARL;

3. All insurance benefits included in the plan agreement are adequately covered under a separate insurance contract. Reserves for the Pre-Need benefits and guarantees, on the other hand, are valued in accordance with the assumptions based on item 1 above;

4. The pre-need reserves for *<u>(specify type of plan)</u>* aggregating to P __________ in this computation are in accordance with the above formulation and assumptions;

5. The amount of insurance premium reserves for the cost of purchasing the insurance benefits after the payment period is P_______________

6. The dividends amounting to P __________ of the participating pre-need plans were computed based______________________.

7. The Trust Fund Equity based on the Trustee's Certification has a net balance of P _________ as of *<u>(date of computation)</u>*.

This document forms part of the Pre-Need Reserves Computation Report.

Lastly, I am an (Associate / Affiliate) of the Actuarial Society of the Philippines (ASP) and I recommend that a Fellow of the ASP be asked to determine the Actuarial Reserve Liability.

Name & Signature of Associate / Affiliate
SEC Accreditation Number _____
Issued in ____________ on ___________

<u>Annex "B"</u>

ACTUARIAL VALUATION CERTIFICATE

I have undertaken the actuarial valuation of the *<u>(specify whether education plan, life plan or pension plan)</u>* of *<u>(Name of Pre-Need Corporation)</u>* as of *<u>(date of valuation)</u>*.

I have relied on data submitted by *<u>(Name and Position of Responsible Person)</u>* and have conducted the tests necessary to satisfy myself on the reasonableness and integrity of such data.

I hereby certify that:

7. The actuarial assumptions and formulations used in this actuarial valuation are in accordance with generally accepted actuarial principles and practices;

8. The reserves for all benefits and guarantees therein are valued in accordance with the assumptions, and all insurance benefits included in the plan agreement are adequately covered under a separate insurance contract;

9. The Actuarial Reserves for *<u>(specify type of plan)</u>* aggregating to P ___________ in this actuarial valuation are in accordance with the above actuarial formulations and assumptions;

10. The amount of insurance premium reserves for the cost of purchasing the insurance benefits after the payment period is P___________.

11. The dividends amounting to P ___________ of the participating pre-need plans were computed based ____________________; and,

12. I have also computed the Pre-Need Reserves amounting to P___________ in accordance with the guidelines in item 12 of SEC Pre-Need Rule 31, as amended. The difference between the PNR and the Actuarial Reserves as computed in the foregoing is *<u>(indicate if an excess or a deficiency)</u>* of P____________, and *(if the difference is a deficiency)* is booked by the corporation under "Other Reserves".

or

I have also computed the Pre-Need Reserves amounting to P___________ in accordance with the guidelines in item 12 of SEC Pre-Need Rule 31, as amended. The difference between the PNR and the Actuarial Reserves as computed in the foregoing is (indicate if *an excess or a deficiency)* is P____________, and *(if the difference is a deficiency)* should be reflected as an additional liability of the company.

I further certify that I compared the amount of the Actuarial Reserves as of *<u>(date of valuation)</u>* with the amount of the Trust Fund Equity and the result of the comparison reflects the following information:

The Trust Fund Equity based on the Trustee's Certification has a net asset balance of P___________ as of *<u>(date of valuation)</u>*.

Case A. If the Trust Fund Equity is sufficient:

The Trust Fund Equity, excluding the dividends of participating pre-need plan products, *(if applicable)* is sufficient to cover the Actuarial Reserves.

OR

Case B. If the Trust Fund Equity is deficient:

The Trust Fund Equity, excluding the dividends of participating pre-need plan products, *(if applicable)* is deficient to cover the Actuarial Reserves and the deficiency amounting to P ____________ should be in the Trust Fund within the time limit prescribed by SEC regulations.

Attached is the Actuarial Valuation Report, prepared in accordance with the Actuarial Society of the Philippines' "Guidelines to Actuarial Practice in Pre-Need".

Name & Signature of Pre-Need Actuary
SEC Accreditation Number _____
Issued in _________ on __________