

Opinion on Profit Sharing : Guidance for Actuarial Function

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I. Purpose

Profit sharing is related to the statutory accounts of an insurance company. During the annual general assembly, the shareholders of the insurance company decide which part of the profit of the company can be distributed amongst the clients. Independently of legal requirements also company-specific requirements (as described in the profit sharing policy) have to be respected when determining this amount.

Article 59 of the Solvency II Law and the Royal Decree d.d. 14.09.2016 require that the Actuarial Function expresses an opinion on the profit sharing.

The purpose of this document is to provide guidance to the Actuarial Function when formulating this actuarial opinion. It focusses on the requirements as defined in the Royal Decree and in the Circular NBB_2016_31 as updated in September 2018.

In order to give a complete overview on the profit sharing, we start this document with some of its aspects :

- The difference between the determination of profit sharing amount and the attribution (distribution) of the profit sharing to the individual contracts;
- The overview of the requirements related to the profit sharing;
- The different forms of profit sharing;
- The different ways for distributing the profit sharing amount on the Belgian market.

In the rest of the document, we will comment on the different tasks of the Actuarial Function related to the profit sharing, its report and the communication of its conclusions.

All relevant regulatory texts can be found in Annex 1 as they exist on 27.09.2019. In order to be in line with the other guidance notes, we only mention the French version of the texts. In addition, we only take into account the prudential aspects of the profit sharing that fall into the scope of the NBB.

Annex 2 contains some guidance on the profit sharing policy.

This document only applies to the profit sharing of direct business. As such, the profit sharing in the ceded /accepted reinsurance is out of scope.

II. Profit sharing in a nutshell

II.1. The 2 steps related to the profit sharing

The report to the King concerning the Royal Decree d.d. 14.09.2016 describes the 2 steps related to the profit sharing and the premium refunds as follows :

Répartition et attribution des participations bénéficiaires

L'octroi de participations bénéficiaires fait l'objet de deux étapes distinctes :

a) Répartition des participations bénéficiaires

La première étape consiste en la répartition de la participation bénéficiaire telle que définie à l'article 213, 9° de la loi du 13 mars 2016 relative au statut et au contrôle des entreprises d'assurance ou de réassurance (ci-après, « la loi »), c'est-à-dire la cession, au profit de contrats d'assurance, de tout ou partie du bénéfice de l'entreprise d'assurance.

Cette étape consiste, pour une entreprise d'assurance, à déterminer le montant du bénéfice qu'elle a réalisé lors de l'exercice comptable clôturé qu'elle entend ristourner aux preneurs d'assurance et aux bénéficiaires pour compenser la prudence incorporée dans ses tarifs. Ce montant est dès lors déterminé globalement pour l'ensemble des preneurs d'assurance concernés et des bénéficiaires et aucun droit individuel n'y est encore attaché. Il est intégré aux provisions techniques de l'entreprise d'assurance sous la forme d'une provision pour participations aux bénéfices et ristournes de l'exercice.

b) Attribution des participations bénéficiaires

La seconde étape consiste en l'attribution de la participation bénéficiaire telle que définie à l'article 213, 10° de la loi.

Les règles d'octroi sont fixées par les entreprises d'assurance sur la base de critères qui leur sont propres dans le respect de la loi.

Ristournes

L'octroi de ristournes est également composé de deux étapes.

La première est le calcul du montant qui peut être octroyé globalement à un ensemble de contrats en fonction du bénéfice réalisé au cours de l'exercice écoulé. Ce montant est intégré aux provisions techniques sous la forme d'une provision pour participations aux bénéfices et ristournes de l'exercice. A ce stade, il n'y a aucun droit individuel sur le montant à ristourner.

La seconde étape est l'octroi des ristournes proprement dites. Contrairement aux participations bénéficiaires, les ristournes n'augmentent pas les prestations contractuellement prévues mais se traduisent par un remboursement d'une partie de la prime versée.

Les ristournes se rencontrent surtout dans les assurances non-vie et les participations bénéficiaires, dans les assurances-vie.

II.2. Requirements concerning the profit sharing

One can distinguish 2 sets of requirements :

• Legal requirements

The legal requirements related to the profit sharing can be found in different legal sources. They can be divided in :

- Requirements related to the amount of profit that the shareholder is willing to give to the clients as profit sharing : these requirements can be found in the Royal Decree dd. 14.09.2016. They are applicable to direct Life and Non-Life business;
- Special requirements related to the old Royal Decree 69 : these requirements can be found in the Royal Decree 14.11.2003 "concernant l'octroi d'avantages extra-légaux aux travailleurs salariés visés par l'arrêté royal n° 50 du 24 octobre 1967 relatif à la pension de retraite et de survie des travailleurs

salariés et aux personnes visées à l'article 32, alinéa 1er, 1° et 2° du Code des Impôts sur les Revenus 1992, occupées en dehors d'un contrat de travail ». It is generally assumed that those requirements will be adapted to be in line with the new legislation. As such, we will not comment on this kind of profit sharing in this document;

- Requirements related to the way that the profit sharing provision is afterwards distributed (“attribution”) to the clients : these requirements are only related to the Life business. The general requirements are specified in article 33 of the Royal Decree Life dd. 14.11.2003. The requirements related to the “separated accounts” are specified in article 58, §2 of the same Royal Decree.

- **Company specific requirements**

The insurance company also has its own profit sharing principles for both Life and Non-Life business. They are described in a profit sharing policy which has to be approved by the Board of Directors.

More information about a possible content of a profit sharing policy can be found in Annex 2. Although this policy is written in the context of a Life Insurance company it can easily be transposed to a Non-Life profit sharing policy as the main principles apply to both kinds of business.

A special form of profit sharing is related to the “separated accounts” and “experience rating”. As they are commonly specified in the insurance contracts, one could consider that these forms of profit sharing belong to the underwriting practices.

II.3. Discretionary versus contractual versus legal profit sharing

One can distinguish the following forms of profit sharing amounts :

- **Discretionary profit sharing**

It concerns general rules applicable for all policies that comply with certain general conditions. The company decides whether or not this kind of profit sharing is distributed to the clients in a given year, for instance :

- Life business : x% of the reserves; y% of the death capital; z% of the premium income;
- Non-Life business : z% of the premium income.

- **Contractual profit sharing**

It concerns special rules that are only applicable for certain contracts or clients. The profit sharing rules are included in the contract with the client. It concerns :

- Separated accounts in Life;
- Experience rating in Life and Non-Life;
- Solidarity part of social sectoral pension plans.

- **Legal profit sharing**

For the former RD1969 portfolio, there exists legal requirements concerning the profit sharing. These can be found in the Royal Decree 14.11.2003; art.15 and 16. As said before the former RD1969 portfolio is not included in the scope of this note.

II.4. Different ways for distributing the profit sharing amounts to the clients

In general the following forms of distribution of profit sharing amounts towards the clients are commonly used within Belgium :

- As a lump sum in the contract : mainly in Life business;
- As an increase of the death capital when the insured person dies : mainly in Life business;
- As premium refund : in Life and Non-Life business.

III. Tasks of the Actuarial Function related to the profit sharing

The minimum tasks of the Actuarial Function related to the profit sharing are defined in article 5 of the Royal Decree dd. 14.09.2016 and further detailed in chapter 5.3.1.5 of the Circular NBB_2016_31 as updated in September 2018.

Those tasks can be split according to the 2 phases of the profit sharing.

III.1. Tasks related to the profit sharing amount

The Actuarial Function has to confirm the following items, both for Life and Non-Life business :

- The Solvency II ratio as per annual closing exceeds 100% : this can easily be checked based on internal reporting and/or official reporting in the following QRT's :
 - SCR : S.25.01 or S.25.02 (in case of internal model);
 - Balance sheet : S.02.01.17.
- The P&L for direct Life, resp. direct Non-Life business is positive before the profit sharing dotation : this can be easily checked based on the detailed annual accounts direct Life, resp. direct Non-Life business. The result of the accepted reinsurance business may not be taken into account.
- The amount of profit sharing dotation does not exceed the profit Life, resp. Non-Life. This can easily be checked based on the detailed annual accounts.
- In case the “Fund for future appropriations¹” is used for financing (part of) the profit sharing dotation, it is recommended to clearly explain this in the actuarial opinion.
- The change in Zillmerisation is correctly calculated. As these amounts are not reported in the annual account, some extra controls have to be performed by the Actuarial Function.
- The principles used to determine the amount of profit sharing dotation must be in line with the latest version of the profit sharing policy. This can be done by comparing the outcome of the principles used when determining the profit sharing amount with the outcome of the principles in the latest version profit sharing policy. Some tolerance level is admitted. If no such tolerance level is defined in the company, the Actuarial Function determines himself a tolerance level and applies it consequently over the subsequent years. It is recommended to include such a tolerance level in the profit sharing policy.
- The principles of the latest version of the profit sharing policy must be correctly/sufficiently taken into account in the Best Estimate models used in the Solvency II balance sheet.² This can be verified :
 - by doing back testing on the profit sharing amount in the first year of the simulation. Some tolerance level is admitted;
 - an analysis of the Best Estimate models (e.g. by reading the documentation or the validation report related to the modelling);
 - ...
- For the “separated accounts” and the “experience rating” (Life and Non-Life) the Actuarial Function should verify if the contractual rules are correctly applied.

The timing of these tasks is linked to the annual closing of the BGAAP Balance sheet.

III.2. Tasks related to the allocation of the profit sharing to the contracts (“attribution”)

The Actuarial Function has to comment on the following topics:

- Control if the amount distributed to the clients is lower than the provision for profit sharing at the end of the previous year. If this provision is exceeded, one should look at the reasons for this excess and how the excess is treated in the annual account. The remaining of the provision for the profit sharing (i.e. the part that is not used for the “attribution”) should stay in this provision. This has to be verified too. [The

¹ Fonds voor toekomstige toewijzingen

² This assessment is mainly related to the businesses where the Solvency II contract boundary goes further than 1 year.

provision for profit sharing belongs to the insurance takers and can as such never return to the own funds of the insurance company.]

- For Life business :
 - 80% of the last year's profit sharing amount and 12,5% of the remaining profit sharing amount has to be allocated to the insurance contracts during the year. This test should at least be performed on the total amount in the profit sharing fund in the balance sheet, i.e. including risk (i.e. death) profit sharing but without the amounts related to experience rating;
 - Special attention should be given to the "fund for future appropriations".

III.3. Tasks related to the profit sharing plan

The Actuarial Function is invited to comment on the profit sharing plan before it is sent to the controlling authorities.

III.4. Tasks related to the profit sharing policy

The Actuarial Function should challenge the technical aspects of the profit sharing policy :

- Feasibility (does the policy contain enough information for the modelling of the profit sharing, ...);
- Impact on the profitability in combination with the ALM-policy;
- Methodology used for the determination of some parameters;
- Existence of a tolerance level to apply in the subsequent year in the context of the comparison between the model outcome and the actual figures and what has to be done in case this tolerance level is exceeded;
- ...

The above topics mainly concern portfolios (Life and Non-Life where the contract boundary is beyond 1 year³).

Specifically for the yearly renewable Non-Life business one should verify if the existing profit sharing provisions are treated as a cash out in the Best Estimate models.

III.5. Special topics

Experience rating in multiyear contracts

In some insurance contracts (Life insurance contracts, Collective health insurance contracts, ...), the experience rating can be defined over a long time period. It is recommended to challenge those experience rating clauses on a regular basis taking into account the current situation of the company and the general economic environment. It is worthwhile to mention that the underlying insurance contracts should stipulate that the experience rating can only be given to the client in case that the general conditions of the profit sharing are met (Solvency II ratio and profitable business).

Experience rating in large employee benefit plans combining Life and Health activities

The Actuarial Function should obtain sufficient assurance that the split between Life and Non-Life is correctly done.

Experience rating in Non-Life contracts where different insurance Lines of Business are combined

The Actuarial Function should obtain sufficient assurance that the split between the different insurance Lines of Business is correctly done.

³ Mainly Health business

IV. Report & Communication of the conclusions of the Actuarial Function

IV.1. Report

The output of the tasks above should be included in an actuarial opinion (a separate one or in a separate chapter in the actuarial opinion on the statutory provisions).

The conclusions of this actuarial opinion should be included in the activity report of the Actuarial Function.

IV.2. Communication to the different governance bodies

The communication of the conclusions of the Actuarial Function depends on the requirements within the company.

It seems logic that the Management Board and the Audit Committee is informed before the approval of the annual accounts by the Board of Directors.

IV.3. Change of the profit sharing policy

A separate actuarial function opinion could be given whenever the profit sharing policy will be changed. This actuarial opinion should be available for the different governance bodies before the decision on the changes is taken. At least the feasibility of the implementation of these changes in the cash flow models should be challenged.

Annex 1 : Regulatory texts i.r.o. profit sharing

Belgian Solvency II Law (dd. 13.03.2016)

- Article 15 “Définition 78 participation bénéficiaire” :
Montant de tout ou partie des bénéfices de l’entreprise d’assurance qui est octroyé aux contrats d’assurance;
- Article 212 « dispositions Non-Vie » : Aucune participation bénéficiaire ni ristourne ne peut être garantie, de quelque manière que ce soit, avant la date de la répartition du bénéfice.
Le Roi peut, sur avis de la Banque et de la FSMA, déterminer les règles à suivre par les entreprises d’assurance en ce qui concerne la répartition et l’attribution des participations bénéficiaires en ce compris les groupes de contrats ou d’engagements auxquels ces règles s’appliquent, ainsi que les informations que les entreprises d’assurance fournissent à la Banque aux fins de leur contrôle. La Banque peut, par la voie d’un règlement pris conformément à l’article 12bis, § 2, de la loi du 22 février 1998, compléter lesdits groupes de contrats ou d’engagements.
- Article 213 « dispositions Vie » :
Définition 9 : répartition de la participation bénéficiaire: cession, au profit de contrats, d’une participation bénéficiaire;
Définition 10 : attribution de la participation bénéficiaire: octroi définitif mais, le cas échéant, conditionnel de la participation bénéficiaire à des contrats déterminés.
- Article 217 (dispositions Vie). Aucune participation bénéficiaire ni ristourne ne peut être garantie, de quelque manière que ce soit, avant la date de la répartition du bénéfice.
- Article 218 (dispositions Vie) Un contrat d’assurance-vie peut être lié à un ou plusieurs fonds à actifs dédiés. Dans ce cas, l’entreprise d’assurance s’engage, en plus des bases tarifaires, à répartir et à attribuer, sous la forme de participation bénéficiaire, une part du bénéfice réalisé provenant des placements de ces actifs dédiés.
- Article 219 (dispositions Vie) Un contrat d’assurance-vie peut être lié à un ou plusieurs fonds d’investissement gérés par une ou plusieurs entreprises d’assurance. Dans ce cas, le risque d’investissement est supporté par le preneur d’assurance et aucune participation bénéficiaire ne peut être octroyée provenant d’un bénéfice sur les placements.
- Article 224. Les entreprises visées à l’article 2234 gèrent séparément les activités vie et les activités non-vie.
En outre, si ces entreprises exercent également des activités de réassurance, elles gèrent séparément, d’une part, les activités d’assurance et de réassurance non-vie et, d’autre part, les activités d’assurance et de réassurance vie.
Les entreprises visées à l’article 223 veillent à respecter les intérêts respectifs des preneurs d’assurance-vie et d’assurance non-vie. En particulier, elles n’accordent de participation bénéficiaire, de ristourne de prime ou d’avantage équivalent aux contrats d’assurance sur la vie qu’en fonction des revenus liés à cette activité comme si l’entreprise n’exerçait que cette activité. Il en va de même pour ce qui concerne l’activité d’assurance non-vie.
- Article 508. Mesures de redressement. — Mesures contraignantes
§ 1er. Lorsque la Banque constate qu’une entreprise d’assurance ou de réassurance ne fonctionne pas en conformité avec les dispositions de la présente loi, des arrêtés et règlements pris pour son exécution ou les mesures d’exécution de la Directive 2009/138/CE, ou qu’elle dispose d’éléments indiquant que cette entreprise risque de ne plus fonctionner en conformité avec ces dispositions au cours des douze prochains mois, la Banque fixe le délai dans lequel il doit être remédié à cette situation.
§ 2. Aussi longtemps qu’il n’a pas été remédié par l’entreprise d’assurance ou de réassurance à la situation visée au paragraphe 1er, la Banque peut, à tout moment:
.....

⁴ i.e. the multi branche companies with Life and Non-Life business in the same entity.

2° limiter ou interdire la répartition de participations aux bénéficiaires et de ristournes ou l'attribution de participations bénéficiaires réparties, après consultation de la FSMA;

Belgian Royal Decree dd. 14.11.2003 i.r.o. Life business

- Article 33
 - § 1er. Sauf pour les opérations visées par l'arrêté royal du 14 novembre 2003 concernant l'octroi d'avantages extra-légaux aux travailleurs salariés visés par l'arrêté royal n° 50 du 24 octobre 1967 relatif à la pension de retraite et de survie des travailleurs salariés et aux personnes visées à l'article 32, alinéa 1er, 1° et 2° du Code des Impôts sur les Revenus 1992, occupées en dehors d'un contrat de travail, la répartition des bénéfices au profit des contrats d'assurances implique pour l'entreprise d'assurances la cession définitive de ces montants.) <AR 2004-06-10/37, art. 4, 002; En vigueur : 01-01-2004>
 - § 2. Toute somme répartie au cours d'un exercice au titre de participation bénéficiaire est, à concurrence de quatre cinquièmes au moins, attribuée au plus tard à la date anniversaire des contrats qui suit l'exercice dont le résultat a permis la répartition ou, pour les contrats liquidés avant cette date anniversaire, au plus tard à la date de liquidation.
Toute somme qui n'a pas été attribuée à la fin d'un exercice, mais qui a été répartie au titre de participation bénéficiaire au cours des exercices précédents, est, à concurrence d'un huitième au moins, attribuée au plus tard à la date anniversaire des contrats qui suit la fin de cet exercice ou, pour les contrats liquidés avant cette date anniversaire, au plus tard à la date de liquidation.
 - § 3. L'attribution de la participation bénéficiaire ne peut être conditionnelle.
L'alinéa 1er n'est pas applicable dans la mesure où le contrat est lié à un crédit hypothécaire.
 - § 4. L'entreprise d'assurances qui utilise la faculté prévue à l'article 24, §§ 4 et 7, ne peut répartir de participation bénéficiaire en faveur des contrats concernés qu'au terme de la période de garantie des bases techniques visées à ces paragraphes.
Les dispositions du § 2 s'appliquent au terme de la période de garantie.
- Article 58, §2 « Fonds cantonnés »
 - § 2. Le contrat stipule que l'octroi du rendement du fonds est subordonné à la condition que les opérations du fonds soient rentables.
Pour chaque fonds cantonné, la dotation à la provision pour participation aux bénéfices et ristournes ne peut excéder le bénéfice technico-financier net avant dotation, augmenté de la variation des valeurs de zillmerisation non activées qui ne doivent pas faire l'objet d'un remboursement.
Pour l'application de ce paragraphe, on entend par bénéfice technico-financier net avant dotation, la somme des postes "solde technico financier net" et "dotation de l'exercice à la provision pour participations aux bénéfices et ristournes" des statistiques visées à l'article 11bis du règlement général, afférents à un fonds cantonné, si cette somme est positive

Belgian Royal Decree dd. 14.09.2016 i.r.o. profit sharing

- Article 3
 - La répartition de participations bénéficiaires et l'octroi de ristournes sont subordonnés à la condition que le ratio de couverture du capital de solvabilité requis soit supérieur ou égal à 100 % sans le bénéfice des mesures transitoires.
- Article 4
 - Le montant qui, par groupe d'activités, peut être réparti sous forme de participations bénéficiaires ou octroyé sous forme de ristournes au cours d'un exercice ne peut être supérieur au bénéfice technico-financier net avant dotations du groupe d'activités de cet exercice.
- Article 5
 - La fonction actuarielle atteste au minimum, dans l'avis visé à l'article 59, § 1er, 10° de la loi :
 - 1° que le montant de la participation bénéficiaire est conforme à la politique écrite approuvée par l'organe légal d'administration;
 - 2° que cette politique écrite a été correctement modélisée dans le modèle de déroulement de cash-flows intervenant dans le calcul de la meilleure estimation (best estimate) visée à l'article 126 de la loi;

3° le montant de la variation de la valeur de zillmerisation non activée.

- Article 6

Par dérogation à l'article 3, la Banque peut s'opposer à toute répartition de participations bénéficiaires et octroi de ristournes lorsque cette répartition ou cet octroi risque de compromettre la situation financière à court ou à long terme de l'entreprise d'assurance.

Annex 2 : Template profit sharing policy (Life business)

Information

Issued by	
Target audience	
Effective date	
Implementation date	
Contact person	

Version Number	
Date	
Approved By:	

1. Introduction

1.1. Goal

- The goal of this document is to provide a written policy on the methodology, assumptions and the process applied by the insurer for the determination, attribution and assignment of profit sharing;
- The requirements captured in the profit sharing Policy are mandatory in a sense that all participants involved in the profit sharing process are obliged to comply;
- This policy does not have to be reviewed on an annual basis but only in case of material changes regarding to the principles, legislation, assumptions or process.

1.2. Scope

Profit sharing is given to the following products : xxx

1.3. Roles and responsibilities

The roles and responsibilities of the different parties are described. This is normally already available in the Governance Memorandum. However, it has an added value to the profit sharing policy to repeat these responsibilities in this chapter.

Examples :

- The Board of Directors needs to approve the profit sharing policy;
- The CEO is accountable for compliance with this profit sharing policy including implementation, monitoring, documentation and evidencing;
- The Chief Commercial Officer is responsible for monitoring the objective, design and evidence of the profit sharing process. The CCO must monitor if a profit sharing process is in place, and if the requirements stated in the profit sharing policy are met;
- The CRO does the sign-off on the models, assumptions and methodology used to calculate the Best Estimate of the Technical Provisions. Hence, he/she will sign-off on the following:
 - that the assumptions used correspond with the profit sharing mechanism decided by the Board of Directors;
 - that figures and explanations are complete and materially accurate;
 - that sufficient controls were put in place to obtain a satisfactory level of comfort;
 - that validations and checks have been performed on the reported figures with satisfactory result and have not uncovered any material facts.

When procedures deviate significantly from those prescribed in this Policy, the CRO of the Business Unit must justify the deviation and report to the CEO;

- The CFO does the sign-off on the annual accounts. Hence, he/she will sign-off on the following:
 - that the profit sharing attribution as taken in the annual account complies with the figures stated in the profit sharing plan;
 - that sufficient controls were put in place to obtain a satisfactory level of comfort;
 - that validations and checks have been performed on the reported figures with satisfactory result and have not uncovered any material facts.
- The Actuarial function needs to confirm that:
 - the amount of profit sharing is in line with the approved written policy of the insurer;
 - the calculation of the Best Estimate is fully according this written policy.

2. General principles

- This chapter contains the principles designed and applied by the insurer for granting profit sharing. For instance:
 - Strategic guidelines / management actions ;
 - Minimum conditions for a contract to receive profit sharing;
 - High level description of the process & milestones to determine the profit sharing %;
- Describe also the mechanism used by the insurer to determine the profit sharing → this should of course be fully compliant with the rules set by the local regulator and the related legislation

3. Modelling assumptions

- Describe how the profit sharing is modelled in the different exercises, for instance in the cash flows for calculating the Solvency II technical provisions.
- Describe how 2nd line risk management does the validation / checks : for instance by means of a back-testing analysis.

4. Process

- This chapter gives an overview of the most important milestones in the process to determine the profit sharing percentages, the attribution to the profit sharing fund and the profit sharing that will be assigned to the contracts.

Appendix 3 : List of abbreviations

- ALM Asset & Liability Management
- BGAAP Belgian General Accepted Accounting Principles
- CCO Chief Commercial Officer
- CFO Chief Financial Officer
- CEO Chief Executive Officer
- CRO Chief Risk Officer
- FSMA Financial Services & Markets Authority
- NBB Nationale Bank van België
- P&L Profit & Loss
- PS Profit Sharing
- QRT Quantitative Reporting Template
- SCR Solvency Capital Requirement
- SII Solvency II
- TM Transitional Measures