ZAMBIA INSTITUTE OF CHARTERED ACCOUNTANTS

LIQUIDITY ADEQUACY TEST AND TRIENNIAL ACTUARY INVESTIGATION

Introduction

The Zambia Institute of Chartered Accountants received a request from one of the Insurance Companies for guidance on the application of IFRS 4 on Liability Adequacy Test in comparison with the requirements of Section 48 of the Insurance Act of Zambia.

Scenario

IFRS 4 [IFRS 4.15] requires an insurance company to assess at each reporting date whether its recognised insurance liabilities[less related deferred acquisition costs and related intangible assets] are adequate, using current estimate of future cash flows under the insurance contracts.[Liquidity Liability Test]

Section 48 of the Insurance Act of Zambia states: The Actuary of the Life Insurer shall make, at the end of every **THIRD FINANCIAL YEAR**, an investigation into the financial condition of the insurer's life insurance business for the purposes of ascertaining whether there is a surplus for distribution, and shall make a report there on.

Issues considered

What is the difference between **Liquidity Adequacy Test [IFRS 4.15]** and **Actuary Triennial Investigation** as per Insurance Act Section 48?

Is there a conflict between the **IFRS 4 requirement of annual Liquidity Adequacy Test** and the **triennial requirement by the Insurance Act Section 48**?

Who should perform the Liquidity Adequacy Test?

Guidance

What is the difference between Liquidity Adequacy Test [IFRS 4.15] and Actuary Triennial Investigation per Insurance Act Section 48

The objective for the Liquidity Adequacy Test is to assess at each reporting date whether recognised insurance liabilities are adequately covered. Should a deficit be identified then such a deficit is recognised in the statement of comprehensive income immediately. The extent of the assessment is dependent on the nature and complexity of the insurance contracts. It may be based on a model developed by management or performed by an expert such as an Actuary.

The objective of the Actuary investigation required by the Insurance Act Section 48 is to assess the financial position of the Insurer's life insurance business for the purpose of ascertaining whether there is a surplus for distribution. This assessment is specifically required to be performed by an Actuary.

Both activities are targeted at establishing the extent to which insurance liabilities are funded. However, the Insurance Act Section 48 requires it for purposes of establishing a surplus for distribution while the Liquidity Liability Test is to establish whether or not a deficit exists.

Is there a conflict between the IFRS 4 requirement of annual Liquidity Adequacy Test and the triennial requirement by the Insurance Act Section 48

Based on the explanation of the difference above, there is no conflict between the two requirements. The Liquidity Adequacy Test is performed at every reporting date in order to comply with IFRS 4.15 i.e. annually. Triennial Actuary investigation should be performed every third year as required per the Insurance Act Section 48. The results of the triennial Actuary investigation can be used as input into the Liquidity Adequacy Test decisions for that year.

Who should perform the Liquidity Adequacy Test: Management or an Actuary?

The overriding factor is the reliability of the results. Therefore the following factors may affect the selection of the party that performs the task:

- Nature and complexity of insurance contracts; and
- Capacity and competence of management.

Accordingly, in practice, short term insurers may perform the task themselves while Life insurers may engage specialists mainly actuaries.

You may contact the undersigned to clarify any matter related to the foregoing.

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