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Balancing Clients and Professional Boundaries

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Agenda

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CASE BACKGROUND

Case Summary

- Senior actuary at a large life insurance company is approached by the Sales officer of life insurance company.
- Client concerns about increased gratuity liabilities following a change in the appointed actuary for valuation.
- The new actuary's valuation shows higher liability due to conservative discount rate compared to the previous actuary.
- Both actuaries are senior professionals known for their expertise; The CFO seeks help in resolving client dissatisfaction.
- The dilemma involves maintaining respect for fellow actuaries, upholding professional integrity, protecting client's confidence, and managing the company's relationship with a key client.

Discount Rate – Key Drivers & Differences in Actuarial Practice

Factors Affecting the Discount Rate

- Driven by current market conditions and the liability profile (duration and expected cashflows).
- For Gratuity valuation, actuaries typically use government bond yields (e.g., 5-year yield for 5-year average duration).
- Discount rates move with market conditions - changes in economic environment directly affect bond yields.
- Future expectations of economic trends (interest rates, market volatility, inflation) also influence the chosen discount rate.

Discount Rate – Key Drivers & Differences in Actuarial Practice

Why Discount Rates Differ Between Actuaries

- Differences in government bond yield outlooks lead to varying discount rate assumptions.
- Shifts in the risk-free yield curve may be interpreted differently by actuaries, resulting in varied assumptions.
- Different views on future inflation can shift discount rate choices.
- Variation in actuarial philosophy: some prefer aggressive assumptions, while others take a conservative approach with higher margins for prudence.

Core Dilemma

- You want to help your CFO & protect the client relationship
- Issues:
 - No official appointment
 - No mandate to review another actuary's work
 - Potential risk of being seen as interfering
 - Duty to uphold professionalism
- Must balance:
 - Organization's interest
 - Client relationship
 - The other actuary's independence
 - Professional obligations

PROFESSIONAL STANDARDS IN INDIA

Overview of the Professional Framework



All members of Institute of Actuaries of India are guided by the following while performing their duties:

- Actuaries Act, 2006 and the rules prescribed under it
- Professional Code Of Conduct Version 4.0
- Actuarial Practice Standards
- Guidance Notes

PCS

Professional Conduct Standards

- Applies to all actuaries in India
- Covers ethics, communication, objectivity, courtesy, conflicts, confidentiality, honesty, integrity, relation with other members

APS

Actuarial Practice Standards

- Technical + professional requirements.

Criticality of PCS

The problem is NOT technical - it is about **boundaries, conduct, interference, and communication.**

PCS governs:

- Ethics
- Professional behavior
- Courtesy with other actuaries
- Avoiding conflict of interest
- Managing client expectations



Relevant APSs



APS 27 : Employee Benefits : Governs valuation of employee benefits

APS 34 : General Actuarial Practice - this governs all actuaries for any actuarial services carried out professionally.

Interpretation in this case:

You **cannot form an opinion** on another actuary's report because you do NOT have formal engagement. However, we can guide CFO on which standard and guidance the actuary must have used and where a professional judgement would have been applied resulting in a higher liability.



Relevant APSs - APS 27



APS 27: Employee Benefits - governs Indian GAAP (AS 15) and Ind AS 19 valuations.

APS 27 Clause 8.5.2.1 – Discount Rate

This clause briefly states that, the rate of interest should be based on investment pattern, nature, term and yields and any time lags in obtaining investment income and reinvestment thereof.

APS 27 Clause 8.5.2.5 – Application of assumptions in actuarial work

“In the case of new schemes or where the question of choice of assumptions comes up for the first time, the member will have to use his experience of other schemes, currently accepted actuarial opinion and his/her judgement”

Relevant APSs - APS 27

Interpretation based on APS 27 clauses 8.5.2.1 and 8.5.2.5:

The discount rates are based on nature, term, yield and investment pattern along with reinvestment of cashflows. In India, however, the discount rates are derived based on market rates as prescribed in the accounting standards.

When an actuary sets the assumptions for the first time, they will be determined considering all of the above factors based on his judgement, data used and his experience in other schemes.



Relevant APSs - APS 34

APS 34 Clause 2.6 to 2.9 – Assumptions and methodology

“Assumptions and methodology may be:

- a. Set by the Actuary (2.7);*
- b. Prescribed by the principal or another Party (2.8); or*
- c. Mandated by law (2.9).”*

Interpretation:

- The discount rates are mandated by law (AS 15 or IndAS 119) however, the data and methodology in this case are set by actuary, We can further refer to clause 2.7 for detailed guidelines on applying different discount rates. How discount rate differs based on data and methodology can be referred in the Appendices.

Relevant APSs - APS 34

APS 34 Clause 2.7 lists following considerations when setting up the assumptions:

- 2.7.1 - Selection of assumptions and methodology
- 2.7.2 - Appropriateness of assumptions
- 2.7.3 - Margins for adverse deviations
- 2.7.4 - Discontinuities
- 2.7.5 - Individual vs aggregate assumptions
- 2.7.6 - Consistency
- 2.7.7 - Alternative assumptions and sensitivity testing



Relevant APSs - APS 34

Interpretation based on subclauses to APS 34 Clause 2.7: Interpretation:

- The discount rate may change compared to those applied by previous actuary based on any of the considerations listed in clause 2.7.
- The actuary must have applied appropriate MADs to allow for uncertainty in data, assumptions or methodology as prescribed in clause 2.7.3.
- Reasonably check the change in liability using discount rates through sensitivity testing and referring methodology for deriving discount rates from the valuation report.

Relevant APSs - APS 34

APS 34 Clause 2.12 - Peer review:

“The actuary should consider to what extent, if at all, it is appropriate for any report to be independently reviewed, in totality or by component, before the final report is delivered to the principal or distributed to intended users. The purpose of peer review is to ensure the quality of a report, with the process tailored to the complexity of the work and the specific environment in which the actuary works.”

Interpretation based on clause 2.12 of APS 34

Based on the above clause, an actuary's work is always peer reviewed by an independent and experienced peer and it ensures quality of the work.

APPLYING PROFESSIONAL STANDARDS TO THE CASE

PCS clauses relevant to the case

PCS Clause 2.4 –

“Healthy debates and expressing different opinions on matters of professional interest are good for the betterment of the actuarial profession. However, such debates and opinions must demonstrate due respect and must not bring disrepute to the actuarial profession or other members or the professional body.”

Key message:

- Professional disagreements are acceptable, but respect and professionalism are mandatory.
- Two senior actuaries used different assumptions - both are valid.
- Respect their judgement; avoid criticism or undermining their work.

PCS clauses relevant to the case

PCS Clause 2.2 –

“Members have a duty to the actuarial profession and clients and must always act honestly and with integrity.”

PCS Clause 2.3 –

“Clients are entitled to have absolute confidence in the skill, objectivity and integrity of any member.”

Key message:

- Maintain transparency with the CFO and client without interfering in another actuary's work.

PCS clauses relevant to the case

PCS Clause 6.1 –

“Actuaries must ensure that their professional judgement is not compromised, and is not seen to be compromised, by any bias, conflict of interest or the undue influence of others.”

PCS Clause 6.2 –

“If there is or might appear to be a conflict of interest between two or more clients of an actuary or of the actuary's firm, or a conflict between a client and the actuary or the actuary's firm, the actuary must consider the nature and extent of the conflict and whether it is such as to make it improper for the actuary to provide actuarial services to one or more of the clients involved in the conflict.”

PCS clauses relevant to the case

Key message:

- Avoid any real or perceived conflict of interest.
- The company recommended the actuary informally - this created a perceived link.
- Do not influence assumptions or valuation; clarify your limited role.



PCS clauses relevant to the case

PCS Clause 4.1 –

“An actuary is expected to use best judgment in formulating advice and must have proper regard to any relevant professional guidance or other guidance.”

Key Message:

- Actuaries must use best judgement and follow professional guidance.
- Both actuaries exercised judgement within acceptable ranges.
- Explain this to CFO/client factually, without suggesting changes.



PCS clauses relevant to the case

PCS Clause 2.1 –

“The actuarial profession has an obligation to serve the public interest within the context of building and promoting confidence in the work of actuaries and in the actuarial profession. Collectively it seeks to do so by informed contribution to debate on matters of public interest and by influencing those with power to protect and enhance the public interest. Individually members must maintain and observe the highest standards of conduct. The standing of the actuarial profession depends on the judgment of individual members.”

Key Message:

- Serve the public interest and uphold the profession’s reputation.
- Your conduct reflects on the profession.
- Maintain high standards and avoid actions that could damage trust.

CONCLUSION

Next Steps : Do's and Don'ts

We can:

- ✓ Explain to CFO *general reasons* why liabilities increase (e.g., falling bond yields)
- ✓ Explain **how discount rate affects liability**
- ✓ Clarify that **differences between actuaries are normal.**
- ✓ Help CFO draft a communication to client, where the references to APS can be drawn.
- ✓ Suggest the client to directly discuss with the appointed actuary.
- ✓ Reassure client the professional ethics and framework ensuring the quality of an actuary's work.



Next Steps : Do's and Don'ts

We CANNOT:

- ✗ Suggest that the previous actuary was “right”
- ✗ Suggest alternative discount rates
- ✗ Provide an informal second opinion
- ✗ Validate or dispute assumptions
- ✗ Influence the assumptions to be used for valuations
- ✗ Comment on competence of the new actuary



Recommended Communication Strategy

Step 1 – Acknowledge client concerns

Step 2 – Provide neutral, high-level explanation

Step 3 – Emphasize independence of actuary & compliance with APS 27
and APS 34

Step 4 – Recommend direct discussion of client and appointed actuary

Step 5 – Offer to facilitate the discussion without giving technical
opinion



Key Takeaways

- Liability increase = technical market-based effect
- Professional standards prevent interference
- Ethical behavior (PCS) must be preserved
- You can support the CFO **without** reviewing/criticizing another actuary
- Proper communication resolves the issue while respecting boundaries



Thank You / Q&A



APPENDICES



Appendix : Gratuity Benefit

Main components of employee benefits is Gratuity, leave encashment and pension. Gratuity is a statutory benefit governed by the payment of gratuity Act 1972.

Gratuity = $15/26 \times \text{last drawn salary} \times \text{years of service}$ as governed by Gratuity act. 26 are the average working days in a month.

- Example : If someone worked for 15 years with a last salary drawn of INR 30,000,
- Gratuity = $15/26 * 15 * 30,000 = \text{INR } 259,615$.

Appendix : Assumptions for valuation

Demographic Assumptions:

- Mortality Rates: Expected mortality pre and post employment
- Attrition rate: Rates of resignation, dismissal, retirement
- Disability Rates: Probability of employees becoming disabled
- Salary growth rate
- Discount Rate : Government bond yields or high quality corporate bonds are used to determine the discount rate. The actuarial discount rate is a forward-looking assumption.

Discount Rate:

- Exhibits an inverse relationship with the liability.
- Even small movements in the discount rate can materially affect the liability.