

Integration of Pricing and Reserving - Talking to the "Other" Actuaries

E&S Company Perspective

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Not Integrating Pricing and Reserving Functions

- Blame Game
 - Reserving Actuaries blame pricing actuaries and UW for all loss emergence greater than the initial loss estimate in the pricing study.
 - Pricing Actuaries ignore the reserving actuaries since they are irrelevant – Blames UWs or UW Cycle.
 - Management blames both groups of actuaries and wonders how come they always give different answers about the business based on looking at the same data.

Integrating Pricing and Reserving Functions

Agenda

- ASI Background
- Actuarial Department
- Differences in Focus
- Differences in Data and Analysis
- Interdependencies
- Beyond the “Others”
- Important Considerations

Integrating Pricing and Reserving Functions

- Background at ASI
 - Small E&S Carrier
 - \$250 million
 - Mostly Casualty Business
 - No filing requirements for rate and form

Integrating Pricing and Reserving Functions

- Background
 - Specialize in “Difficult” risks
 - Environmental Contractors
 - Assisted Living Facilities
 - Contractors
 - Specialty Programs
 - Special Niche Market or Agency Contract
 - May involve risk sharing (captives, swing commissions...)
 - May require independent reinsurance arrangements

Integrating Pricing and Reserving Functions

- Actuarial Department
 - Consists of 2 Actuaries who sit within shouting distance of each other
 - One Actuary assumes the primary role for reserves and other assumes primary role for pricing
 - Both get into each others' business and provide peer review to each other
 - Small Company Advantages

Integrating Pricing and Reserving Functions

- Differences in Focus
 - Reserving
 - Reports to CFO, involved with Finance and Claims
 - Answers the question - How much should we post as liabilities on current and prior years for the Company(s)?
 - Worries about external audiences - Auditors, State Regulators, AM Best, Reinsurers, IRS, stockholders, consulting actuaries,
 - Must be balanced to disappoint each of the above parties as fairly as possible. Optimization is reached when each party is severely angry enough to yell at you but not so much that they put it into writing.
 - Focused on “What was”

Integrating Pricing and Reserving Functions

- Differences in Focus
 - Pricing
 - Embedded with the Underwriting Department – Can result in rose-colored glasses syndrome
 - Answers the question How should I change the rates or change our business mix to have a decent chance to make a profit and grow the business.
 - Worries about UWs and their need to keep their producers happy enough to work with us. Some concern given to reinsurers and State regulators.
 - Monitors price changes and hopes that UW effectively implements the agreed pricing changes and production goals.
 - Focused on “What will be”

Integrating Pricing and Reserving Functions

- Difference in Data and Scope of Analysis
 - Reserving -
 - Calendar/Accident Year World
 - ASLOBs by Company, may split by profit center or not.
 - Must be SOX compliant – analysis and data must follow strict rules.
 - All deviations must be explained so changing analysis to fit today's environment is discouraged unless it is forced by a regulator, auditor, or consultant
 - Losses are paid or incurred, net or direct (meaning before/after reinsurance)

Integrating Pricing and Reserving Functions

- Difference in Data and Scope of Analysis
 - Pricing
 - Exploits any data that may exist internally or externally.
 - Policy/Treaty year data bases developed to make sure all rating criteria is captured for profitability analysis.
 - Looks at limited losses to smooth result or remove the impact of large losses
 - Removes or modifies data for known changes to best reflect the book going forward

Integrating Pricing and Reserving Functions

- Interdependencies
 - Reserving to Pricing
 - Identification of coverage issues
 - Loss development trends
 - Average severity trends
 - Mass tort issues
 - Claims Department Changes

Integrating Pricing and Reserving Functions

- Interdependencies
 - Pricing to Reserving
 - Current loss ratio projections
 - Reinsurance modeling
 - Mix of business changes
 - Price change history
 - Coverage Changes

Integrating Pricing and Reserving Functions

- Communications beyond the “Other” Actuaries
 - Be prepared to discuss all apparent discrepancies between pricing analysis and reserving analysis
 - Be considerate of the “Other’s” Audience

Integrating Pricing and Reserving Functions

- Important Considerations
 - Communication is Key
 - Share Information
 - Know your differences
 - Pricing Analysis versus Reserving
 - Opinion
 - Know your Limitations