



**THIRD POINT RE**

# Practice Note for Statements of Actuarial Opinion on P&C Loss Reserves: Executive Summary and Preview of 2012 Changes

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**September 6, 2012**

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# Panelists

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# Motivation

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- The Practice Note on Statements of Actuarial Opinion on Property and Casualty Loss Reserves (“Practice Note”) is a resource that many actuaries use frequently
- There are several aspects of the Practice Note that are often misunderstood, and questions often arise
- Further, this is not a static document, and there are changes every year in response to changes in regulatory requirements
- The objectives of this session are the following:
  - Refresh your memory of the Practice Note
  - Clarify some topics that are often misunderstood
  - Provide a preview of changes expected for 2012 (and recap those from 2011)
  - Discuss any questions you have today

# What is COPLFR?

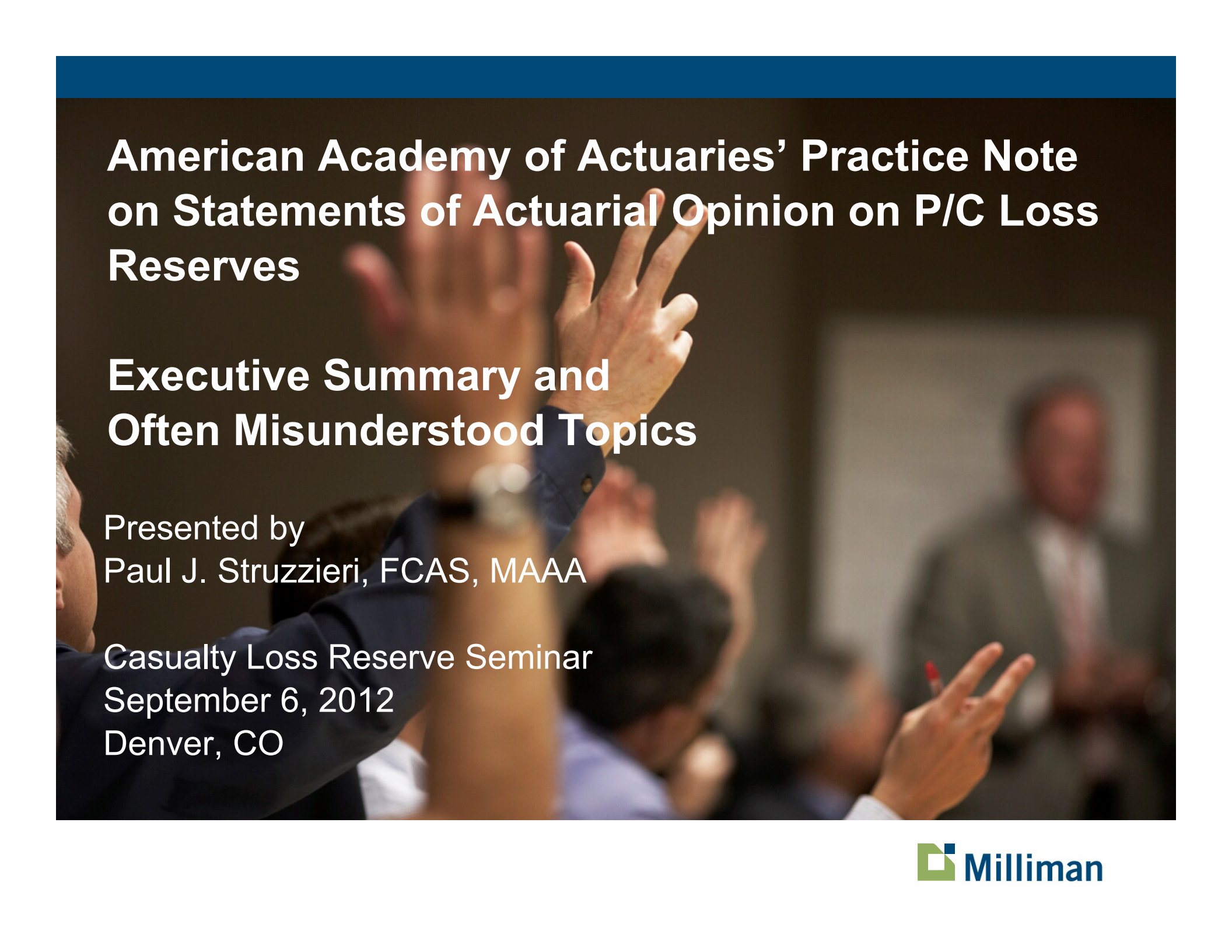
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- COPLFR stands for the Committee on Property Liability Financial Reporting, an American Academy of Actuaries (“Academy”) committee
- COPLFR serves as a liaison between the regulatory community and the actuarial community on financial reporting matters
- Members of COPLFR include a cross-section of experienced practitioners
  - Company actuaries, consultants, auditors, and regulators
- Several ongoing annual COPLFR initiatives benefit many Academy and CAS members:
  - Practice Note for Statements of Actuarial Opinion on Property Casualty Loss Reserves
  - Property/Casualty Loss Reserve Law Manual
  - P/C Effective Loss Reserve Opinion Seminar
- Helps provide guidance on other timely financial reporting matters, for example:
  - Risk transfer testing
  - Model Audit Rule

# What the Practice Note “is” and “is not”...

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- The Practice Note “is”...
  - A supplement to available actuarial and regulatory guidance, such as:
    - Actuarial Standards of Practice from the ASB
    - Property Casualty Annual Statement Instructions from the NAIC
    - U.S. Qualification Standards from the Academy
  - A description of practices that COPLFR members believe to be commonly employed
  - Meant to provide information to actuaries on current or emerging practices
  - An evolving document, responding to changes in regulation and practice
- The Practice Note “is not”....
  - An interpretation of actuarial standards
  - Binding on actuaries
  - An exhaustive description of all common practices
  - A source for regulatory requirements in a specific state or jurisdiction

The background of the slide is a photograph of a seminar or conference. Several people are visible, with their hands raised in the air, suggesting an interactive session or a Q&A period. The lighting is somewhat dim, and the focus is on the hands and the general atmosphere of the event.

# American Academy of Actuaries' Practice Note on Statements of Actuarial Opinion on P/C Loss Reserves

## Executive Summary and Often Misunderstood Topics

Presented by  
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Casualty Loss Reserve Seminar  
September 6, 2012  
Denver, CO

# EXECUTIVE SUMMARY



# Executive Summary

## Major Sections

- SAO
- AOS
- Appendices – many

## General structure:

- NAIC Instructions – repeated in **Bold**
- COPLFR description of possible practice
- COPLFR illustrative wording

# Executive Summary

## SAO Instructions –

- Paragraph 1 - Requirement for an SAO
- Paragraph 2 – Required SAO Contents
- Paragraph 3 – Identification
- Paragraph 4 – Scope
- Paragraph 5 – Opinion
- Paragraph 6 – Relevant Comments
- Paragraph 7 – Actuarial Report
- Paragraph 8 – Signature
- Paragraph 9 – Error
- Paragraph 10 – Filing the SAO

# Executive Summary

## Appendices

1. Evaluation and Reconciliation of Data
2. Frequently Asked Questions
3. CASTF Guidance – Pools & Associations Opinions
4. NAIC Instructions – Title Insurance Companies
5. Miscellaneous Illustrative Wordings
6. Intercompany Pooling
7. CAS Valuation, Finance and Investments  
Committee (VFIC) Note on Materiality (2000)

# Executive Summary

## Appendices (Cont'd)

8. Unearned Premium for Long Duration Contracts
9. CASTF Regulatory Guidance
  - a. P&C SAO
  - b. P&C AOS
10. NAIC Instructions
  - a. P&C SAO
  - b. P&C AOS
11. Data Testing Requirements
12. An Overview for Audit Committee Members – Effective Use of Actuarial Expertise (COPLFR)

# OFTEN MISUNDERSTOOD TOPICS

# Often Misunderstood Topics

1. Electronic Filing (p. 8 of 2011 Practice Note)
  - a. To NAIC central office
    - i. Electronic file must be unsecure
    - ii. Can be unsigned
  - b. To state(s)
    - i. Electronic file can be secure

# Often Misunderstood Topics

## 2. Appointed Actuary (p. 9)

- a. Must be an individual, not a firm
- b. Must be appointed by December 31
- c. Upon initial Board appointment, 5 days to notify Commissioner
- d. Can be multiple year or indefinite appointment

## Often Misunderstood Topics

3. Multiple companies (p. 10)
  - a. Separate SAO and AOS for each company
  - b. Actuarial reports for affiliated companies can be combined
  - c. If affiliated pooling arrangement:
    - i. One actuarial report is sufficient, but
    - ii. Addendums are needed for unpooled business



## Often Misunderstood Topics

### 3. Multiple companies (continued)

#### d. CASTF Guidance for pooled companies:

- i. The Opinion for each pooled entity should disclose the pooling arrangements, including the percentage share for each pooled entity
- ii. The comments regarding reinsurance collectibility should indicate that the amount of the recoverables with affiliates is due to the pooling arrangement

## Often Misunderstood Topics

### 4. Qualified Actuary (p. 11)

- a. Meets specific Qualification Standards:
  - i. Basic education
  - ii. Experience
  - iii. Continuing education
- b. And is either
  - i. a CAS member in good standing, or
  - ii. an Academy member approved by Casualty Practice Council

## Often Misunderstood Topics

### 5. Data Reliance (p. 14)

- a. Actuary can rely on data provided by others
- b. SAO must disclose person responsible for data
  - i. Should be one or more senior officials of the company
  - ii. Could be the appointed actuary
- c. Actuary is still responsible for review of data (ASOP No. 23)

## Often Misunderstood Topics

6. Data Testing Requirement (Appendix 11)
  - a. Origin = NAIC Annual Statement Instructions
  - b. Appointed actuary “encouraged” to communicate to Management/Auditors which data items are deemed to be “significant” to the reserve analysis
  - c. Auditor responsible for testing the significant data underlying the loss reserve estimates

# Often Misunderstood Topics

## 7. Opinion Paragraph (p. 16)

- a. Categories of Opinions include:
- b. Deficient or Excessive?
  - i. Must disclose the minimum amount by which the carried reserve differs from a reasonable amount
- c. Qualified?
  - i. This means certain reserves have been excluded
  - ii. Can be qualified, but also reasonable
  - iii. Can also be qualified and deficient, excessive, etc.

## Often Misunderstood Topics

8. Risk of Material Adverse Deviation (p. 20)
  - a. Two separate considerations:
    - i. Materiality
    - ii. Significant Risks/Uncertainties
  - b. Materiality
    - i. How much adverse deviation would matter regardless of whether there are risks that are significantly likely to produce that much adverse deviation
  - c. Significant risks and uncertainties
    - i. Must consider the uncertainty in the loss reserves
    - ii. Must consider the materiality standard

# Often Misunderstood Topics

## 9. Exhibit B Disclosures (p. 38)

### a. Disclosure 4 – Type of Opinion

- i. If actuary reaches different conclusions as to the reasonableness of Gross and Net reserves =>
- ii. Then Exhibit B should reflect opinion on Net

### b. Disclosure 6 – Are there Significant Risks?

- i. Response (Y/N) should be consistent with Relevant Comment section of SAO as to RMAD

### c. Disclosure 13 – Other Items on which Actuary is providing Relevant Comments

- i. Disclose in SAO why actuary is providing comments

## Often Misunderstood Topics

### 10. Actuarial Opinion Summary (p. 40)

- a. Estimates shown in the AOS shall follow the actuary's analysis:
  - i. Include Range when calculated
  - ii. Include Point Estimate when calculated
  - iii. Include Range and Point Est., when calculated
  - iv. There is no requirement to produce both a Range and a Point Estimate
- b. AOS applies to loss and LAE reserves only, and not premium reserves



American Academy of Actuaries  
Practice Note on Statements of Actuarial  
Opinion on P&C Loss Reserves:

Preview of 2012 Changes and  
Recap of Major 2011 Changes

Dave Heppen, FCAS, MAAA  
Deloitte Consulting

# Requirements and Guidance

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- Actuarial Opinion requirements from NAIC's Annual Statement Instructions
- Regulatory Guidance from NAIC's Casualty Actuarial and Statistical Task Force (CASTF)

# Preview of Changes for 2012

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- Paragraph 1 – Requirement for an SAO
  - New required disclosure when the Appointed Actuary changes
- Paragraph 7 – Report
  - Several new requirements related to information provided in the Report
- Paragraph 8 – Signature
  - Additional information required

# Change in Appointed Actuary

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## **Old Requirement – Disclose Disagreements in last 24 months on:**

- Risk of Material Adverse Deviation
- Required Disclosures
- Scope
- Procedure
- Data Quality

# Change in Appointed Actuary

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## **New Requirement – Disclose Disagreements in last 24 months on:**

- Risk of Material Adverse Deviation
- Required Disclosures
- Scope
- Procedure
- *Category of Opinion Issued*
- *Wording of Opinion*
- Data Quality

# Report – New 2012 Requirements

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## **New or Additional Information Related to:**

- Actuary's Relationship to Company
- Comparison of Actuary's Conclusions to the Carried Amounts
- Schedule P Reconciliation
- Changes in Estimates

# Report – Relationship to Company

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## Old Guidance/Instruction

- 2011 CASTF guidance recommended that the Appointed Actuary disclose relationship to Company in Report
- However, no requirement for Appointed Actuary to disclose relationship to Company in Report

# Report – Relationship to Company

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## New Requirement

- Report must include:
  - Description of actuary's relationship to the Company
  - Clear presentation of the actuary's role in advising the Board/Management regarding the carried reserves
  - How and when the actuary presents the analysis to the Board and where applicable the Company officers responsible for determining the carried reserves



# Report – Relationship to Company

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## Guidance

- Practice Note includes examples of potential disclosures in the “*Actuarial Report and Underlying Work Papers*” section
- CASTF 2012 Guidance references this section of the Practice Note, and notes that it provides relevant examples of regulators’ expectations with regard to this disclosure

# Report – Comparison to Carried

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## Old Requirement

- Exhibit that ties to the Annual Statement and compares the actuary's conclusions to the carried amounts
- CASTF Guidance recommended including an exhibit that compares the actuary's conclusions to the carried amounts consistent with the segmentation of exposure or liability groupings used in the analysis

# Report – Comparison to Carried

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## New Requirement

- Exhibit that ties to the Annual Statement and compares the actuary's conclusions to the carried amounts *consistent with the segmentation of exposure or liability groupings used in the analysis*
- *The actuary's conclusions include:*
  - *Point estimate(s)*
  - *Range of reasonable estimates*
  - *(or both)*

# Report – Comparison to Carried

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## Note

- NAIC 2012 Instructions remove the previous requirement to include summary exhibit(s) of actuary's point estimate(s), range of reasonable estimates, or both that led to conclusions in the Opinion paragraph regarding the reasonableness of the unpaid loss & loss adjustment expense obligations

# Report – Schedule P Reconciliation

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## Old Requirement

- Documentation of the required reconciliation from the data used for the analysis to the Annual Statement Schedule P
- CASTF Guidance recommended reconciliation in a manner consistent with the exposure or liability grouping used in the analysis

# Report – Schedule P Reconciliation

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## New Requirement

- An exhibit that reconciles or maps the data used by the actuary, *consistent with the segmentation of exposure or liability groupings used in their analysis*, to the Annual Statement Schedule P line of business reporting

# Report – Schedule P Reconciliation

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## Guidance

- Practice Note includes discussion on Schedule P Reconciliation in Appendix 1 *Evaluation and Reconciliation of Data*
- This section includes discussion and guidance on approaches to demonstrating data reconciliation given the segmentation used in the actuary's analysis versus the segmentation in Schedule P

# Report – Changes in Estimates

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## Old Guidance/Instruction

- 2011 CASTF Guidance recommended that the Appointed Actuary include an exhibit showing the change in the actuary's estimates from the prior report, including extended discussion of factors underlying any material changes
- However, no requirement for actuary to include such an exhibit in the Report



# Report – Changes in Estimates

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## New Requirement

- An exhibit or appendix showing the change in the estimates from the prior Report, including extended discussions of factors underlying any material changes

# Report – Changes in Estimates

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## Guidance

- 2012 CASTF Guidance notes:
  - Should at least illustrate change on a net basis; may also show on a gross basis
  - Material change in total should be discussed
  - Explanation should also be included for significant fluctuations by accident year or segment

# Opinion Signature

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## Old Requirement

- Signature of Actuary
- Printed Name of Actuary
- Address of Actuary
- Telephone number of Actuary
- E-mail address of Actuary
- Date Opinion was Rendered

# Opinion Signature

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## New Requirement

- Signature of Actuary
- Printed Name of Actuary
- *Employer's Name*
- Address of Actuary
- Telephone number of Actuary
- E-mail address of Actuary
- Date Opinion was Rendered

# Recap of Major Changes in 2011

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- Revised Actuarial Standard of Practice No. 36 applies to all Statements of Actuarial Opinion (SAOs) issued on or after May 1, 2011
- Resulted in several new disclosure requirements (*Section 4, Communications and Disclosures*)
- Included additional disclosure requirements related to review date and use of the work of another actuary

# Required Disclosures from ASOP No. 36, Section 4 – new in 2011

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- Intended users of SAO
- Intended purpose of SAO
- Stated basis of reserve presentation
- Whether any material assumptions were required by law
- Whether the actuary disclaims responsibility for any material assumption or method that originated from another source

# Review Date

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- Defined in ASOP No. 36 as the date, subsequent to the valuation date, through which material information known to the actuary is included in forming the reserve opinion
- 2012 CASTF Guidance notes that silence on Review Date could indicate either
  - Review Date that is the same as the date the Opinion is signed, or
  - The actuary overlooked this requirement

# Review Date – Guidance

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- 2012 CASTF Guidance suggests that when the Review Date is the same as the date the Opinion is signed, that the actuary clarify such in the Opinion
- Suggested language includes, “...and reviewed information provided to me through the date of this opinion.”



# Use of the Work of Another Actuary

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- ASOP No. 36: only when, in the actuary's professional judgment, it is reasonable to do so
- The actuary should:
  - Understand the intended purpose of the analysis/opinion
  - Assess whether the analysis/opinion is consistent with stated basis of the presentation of reserves

# Use of the Work of Another Actuary

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- Considerations include:
  - The amount of reserves covered by another's analysis/opinion in relation to total reserves subject to the actuary's opinion
  - The nature of the exposure and coverage
  - The way in which reasonably likely variations in estimates covered by another's analysis/opinion may affect the actuary's opinion on total reserves subject to opinion
  - The credentials of the individual(s) that prepared the analysis/opinion

# Use of the Work of Another Actuary

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- CASTF Guidance: when the actuary determines it is reasonable to make use of another's analysis/opinion, the actuary should state whether the related portion of reserves is material
- If material, the actuary should disclose:
  - Whether (s)he reviewed the other actuary's analysis
  - If a review was performed, the extent of the review