

# The Actuary's Role in the Financial Reporting Process: Interactions with Other Parties and Different Uses of the Loss Reserve Estimates

2012 Casualty Loss Reserve Seminar

Denver, Colorado

# The Panel: About Us

Moderator Paul Miotke – Chief Risk Officer & Chief Actuary, Ally Insurance

Panelists Marc Adee – President, Fairmont Specialty Group  
Patrick Devlin – Director, PricewaterhouseCoopers  
Lise Hasegawa – Vice President, MetLife

Perspectives President  
CFO  
Chief Actuary  
Reserving Actuary  
Chief Risk Officer  
Consultant  
Auditor

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# Discussion Themes

- The many uses and users of actuarial analysis
- Interactions with the many users of actuarial analysis
- Credibility destroying pitfalls
- Tips for working effectively with an actuary

# The many USES...

- Reserve opinion
- Financial statement / reporting
- Management accounts
- Capital requirements
- Reserve development schedules
- Experience monitoring
- Pricing
- Contingent commission or profit sharing

# The many USERS...

- Board / Audit Committee
- Management
- Finance
- Auditor
- Regulator
- Rating Agencies
- Buyers

# Interacting With Many USERS

- Know your audience – put yourself in their shoes
- Check your attitude – is it helpful
- Try to understand the underlying business
- Check the results of your analysis for reasonableness
- Tailor your presentation to audience – boil down to essentials (change from last time, action items)
- Calibration (help audience understand your bias regarding subjective elements of analysis)
- Recognize and explain limitations of analysis

# Credibility Destroying Pitfalls

- Attitude
- Data integrity issues
- Errors in analysis
- Lack of awareness on changes in business
- Inability to explain “Why?”
- Inconsistency between pricing and reserving
- Overly mechanical approach
- Careless versioning of exhibits
- Switching basis of data in mid discussion



# Tips for working effectively...

- With a Consulting Actuary
- With Auditors
- With Management
- With the Board / Audit Committee

# ...With a Consulting Actuary

- Much of the below also applies to working with internal actuaries.
- Does your actuary have sufficient experience in all relevant lines?
- Have you collaborated with your actuary to customize a report that fully meets your needs?
- Is your actuary aware of all intended uses of the actuarial report?
- How does your actuary stay informed about changes in your company's business?
- Is your actuary's quality control process sufficient?
- What is the succession plan for your consulting actuary?

# ...With Auditors

## **Actuary's interaction with auditor -- actuarial report items that help auditors**

- Some of the items below are already included in actuarial reports as part of adherence to actuarial standards of practice (especially ASOPs 41 and 43).
- Statement acknowledging the actuary's qualifications.
- Thorough documentation of report scope.
- Key summary information shown in one place.
- Change in estimates from prior to current actuarial report.
- Description of the business.
- Description of methods and assumptions, including key changes since prior report.
- Support for loss ratio assumptions (eg. For B-F method)
- Data tie-out exhibits

## **Actuary's role in setting booked reserves -- interaction with auditor**

- Document reconciling items between actuarial estimate and booked reserve.
- Adjustments such as roll forward to year-end, foreign exchange.
- Adjustments reflecting difference between management's view of reserves and actuarial estimate.
  - Does actuary still find resulting reserve reasonable?

# ...With Management

- Understands the business – and is helping run it
- Has control of data
- Proactively shares analyses
- Clear presentation of analysis – including assumptions and ranges and possible shortfalls in analysis
- Open minded approach – but knows how to hold the line

# ...With the Board / Audit Committee

- Know the background and experience of your Board / Audit Committee members
- Boards and Audit Committees benefit from interaction with their actuaries through better understanding of the loss reserve estimation process and the uncertainty inherent in its results
- Anticipate questions and be prepared to present and discuss
  - Process of setting reserves and who is involved in the process and in what capacity
  - How objectivity is achieved (e.g. segregation of duties, Reserve Committee)
  - How actuarial estimates are considered in the process
  - Key statistics and benchmarks (e.g. loss ratios, frequencies, severities)
  - Historical reserving accuracy
  - Level of uncertainty and major assumptions
- Good reference article: “An Overview for Audit Committee Members for P/C Insurers: Effective Use of Actuarial Expertise”

# ...With Outsiders

- Regulators – state(s) of domicile and SEC if public
- IRS
- Rating Agencies
- Buyers – usually limited or no opportunity to verbally communicate and/or explain

# The Last Word: DOs and DON'Ts

- DO understand the business
- DO understand all intended uses of your work
- DO know the “language” of the other parties
- DO provide clarity of analysis, finding, assumptions and risks
- DO explain results and changes in results sufficiently
  
- DON'T destroy your credibility
- DON'T forget that YOU have the biggest interaction with your past reserving estimates
  - You, your team, and your successor are the biggest customer of your documentation and the details that support your estimate

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