Actuarial Opinions, Reports

A Regulators Perspective

Sage Advice

- Read the NAIC Regulatory Guidance from the CASTF
- Read the Academy Practice Note
- **Write a good actuarial report**

Disclosure

- **Disclosure will set you free**
- In a courtroom, or in front of the ABCD disclosure will protect you. How?
- What should you disclose if you think there is no risk of material adverse deviation.

More Advice

- Review the annual statement footnotes, general interrogatories, and schedule P interrogatories
  - Are they accurate? Are they consistent with your analysis and assumptions?

Be Clear- Accurate, Complete

- **Review your report as if you were in the reader's position, before sending. Is it not only accurate, but complete and not misleading ?**
- **PRECEPT 8. of the Code of Professional Conduct - Control of Work Product**
- An Actuary who performs Actuarial Services shall take reasonable steps to ensure that such services are not used to mislead other parties.

Changes to the Actuarial Opinion in 2014: Pooling

- ALL companies that are members of an intercompany pooling arrangement, not just those that have a 0% share must:
- Include a description of the pool
- Describe the lead company
- List all pool members, state of domicile, pooling percentages
- Exhibits A&B represent the company's share of the pool and reconcile to the respective annual statements (except for 0%)

Changes to the Actuarial Opinion in 2014: Pooling

- For company's that have 0% share, Exhibits A and B should be that for the 0% share (with $0 as the response to Exhibit B, Q5 and "not applicable" as the response to Exhibit B, Q6) and Exhibits A and B of the lead should be attached as an addendum to the PDF and/or hard copy being filed.
- Note also that the SAO for the 0% company should read similar to that provided for the lead (e.g., the IRIS Ratio, RMAD discussion and other Relevant Comments should relate to those risks of the pool).

Changes to the Actuarial Opinion in 2014: Pooling

- With the exception of intercompany pooling members that retain a 0% share, each statutory entity is required to have a separate Opinion with its own materiality standard.
- Where there are no unusual circumstances to consider, it may be acceptable to determine a standard for the entire pool and assign each member its proportionate share of the total.
- It is **not** appropriate to use the entire amount of the materiality threshold for the pool as the standard for each individual pool member.

Changes to the Actuarial Opinion Summary in 2014: Pooling

- Regulators expect that carried values reported in the Summary can be tied back to values reported in the Annual Statement and the Opinion, and that actuarial estimates can be tied back to the Actuarial Report.

Changes to the Actuarial Opinion Summary in 2014: RMAD

- 1) Identify the materiality standard …
- 2) Identify the basis, or rationale, for establishing this standard.
- 3) Describe the major factors, combination of factors or particular conditions underlying the significant risks and uncertainties that the actuary considers relevant …
- 4) **Explicitly** state whether he or she believes that those significant risks and uncertainties could result in MAD.
- Item 3 now precedes Item 4; the Appointed Actuary is asked to discuss risks whether or not he or she believes the company is exposed to RMAD.

Changes to the Actuarial opinion in 2014: Change in Actuary

- …When there is a change in Appointed Actuary, the newly Appointed Actuary may not be able to review the work of the prior actuary.
- If comparison to prior actuary’s methods and assumptions is not practical, then disclosure is required.

Changes to the Actuarial opinion in 2014:Change in Actuary

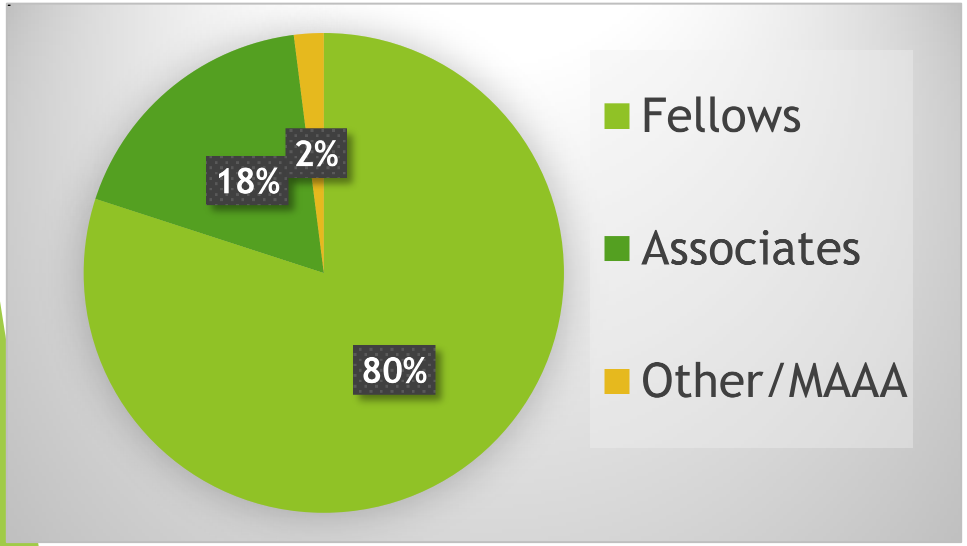
- …Regulators expanded on the types of disagreements that an insurer is required to report to the DOI
- Two additional types, "type of opinion issued" and "substantive wording of the opinion," were added and clarified.
- When such disagreements occur, … a description of the disagreement and the nature of its resolution, or non-resolution, [is to] be included in the letter…
- a reference to ASOP No. 43 [was included]

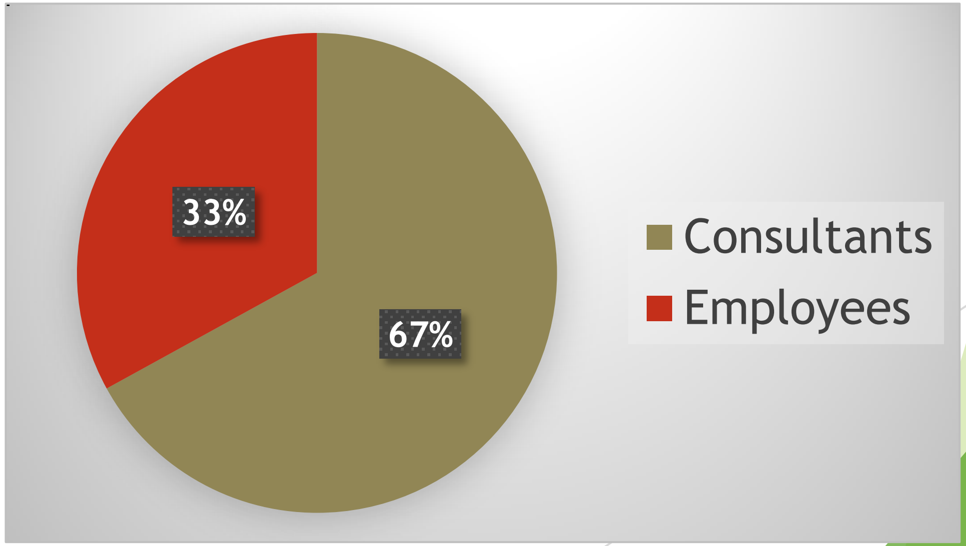
Opinion Statistics – 2013 (Approx.)

- About 2530 opinions (about 2300 excluding materiality of zero)
- About 60 companies without opinions
- About 550 Actuaries Signed Opinions (about 510 excluding zero materiality - likely misspellings)
- A small percentage, less than10% of CAS members sign statutory opinions
- Surplus on signed opinions about $870 Billion

Opinion Statistics – 2013

- 80% Fellows - 18% Associates -2% Other or MAAA
- 67% consultants 33% employees
- 99% Reasonable (less than 25 not reasonable)



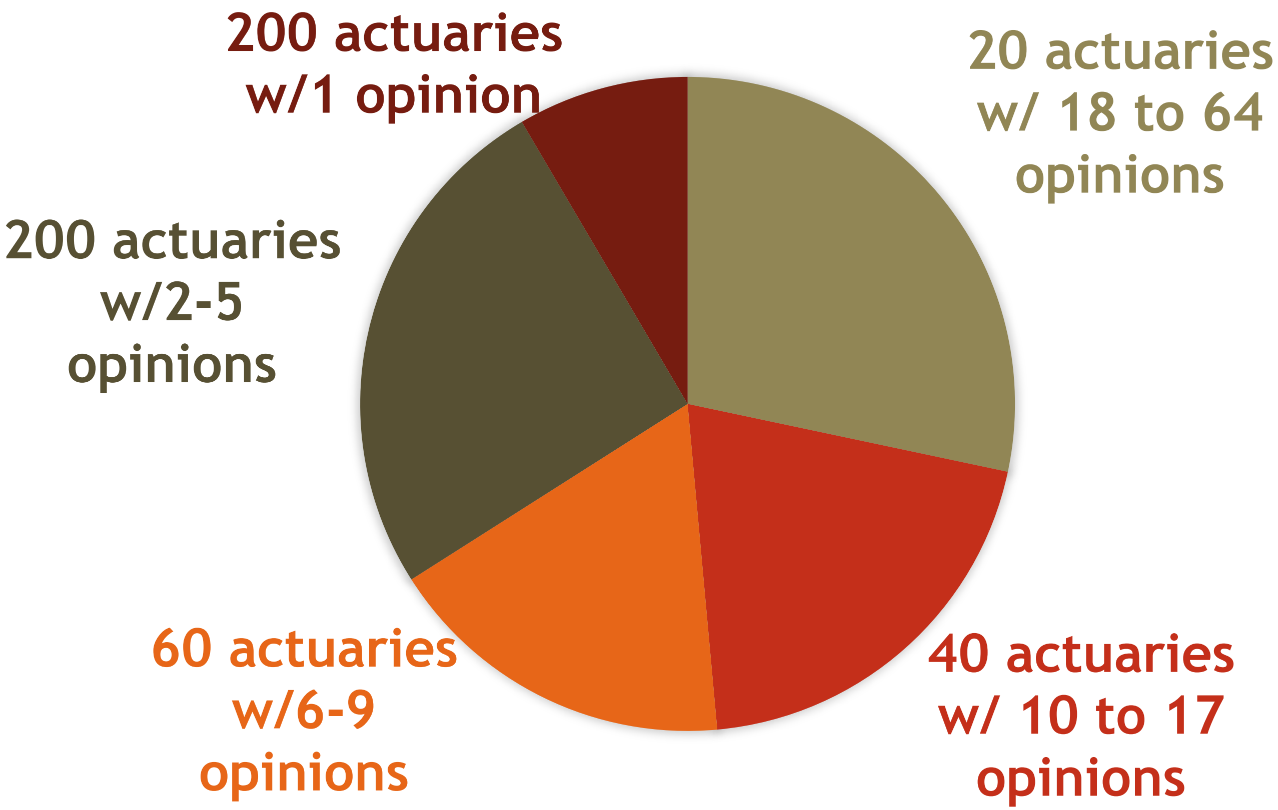


Opinion Statistics – By Number of Opinions

- The top 20
- Sign between 640 & 719 opinions (over 25%)
  - Opine on companies with about $300 billion of surplus (between 25 & 30%)

- The top 60 actuaries
- Sign about half of the opinions (over 1100)

Approximate Distribution Excluding Opinions with Zero Materiality



Opinion Statistics – By Number of Opinions

- The top 20 US opiners, by # of opinions
  - Range from 65 opinions to 19 opinions per actuary
- How many opinions can one actuary sign and adhere to the Actuarial Code of Conduct?
  - If all the companies are affiliated
  - If the companies are not affiliated.

Code of Conduct

- **Professional Integrity**
- An Actuary shall act honestly, with integrity and competence, and in a manner to fulfill the profession’s responsibility to the public and to uphold the reputation of the actuarial profession.
- ANNOTATION 1-1. An Actuary shall perform Actuarial Services with skill and care.

Regulator Questions

- Aren’t you the actuary that told me (argued with me) that company XXX was solvent? The one that just went under? Why should I believe you this time?

Regulators Said

- The numbers in the actuarial opinion and the Summary should match each other and also numbers in other public documents.
  - Surplus (Exhibit B, Item #7)
  - Net salvage and subrogation (Exhibit B, Item #8)
  - Non-tabular discount (Exhibit B, Item #9.1)
  - Tabular discount (Exhibit B, Item #9.2)
  - Voluntary and involuntary pools and associations (Exhibit B, Item #10)
  - Net asbestos (Exhibit B, Item #11.1) and environmental (Exhibit B, Item #11.2) reserves
  - Extended loss and expense reserves (Exhibit B, Item #12.1 and #12.2),

So, You Want to Talk to a Regulator?

- Make mistakes in the actuarial opinion & summary – have dates, numbers that don’t make sense or don’t match other sources.

- Regulator Thinks: If there are mistakes in your actuarial opinion it makes it more likely that there are mistakes in the actuarial report. Perhaps I should request a copy.

Regulators Said

- A regulator has little time and few resources. He/she must look at many opinions, summaries and reports. The regulator expects the company to do its best to fill out the opinion and the AOS correctly, and to read about changes to the opinion and the AOS in the guidance and practice notes. If you do not fill these out correctly it gives the impression that at the very least attention to detail was not important, and that other documents from this company and/or consulting actuary should perhaps be scrutinized more closely.

Statistics - Materiality as a % of Surplus

- Median is 10% of surplus
- 91st percentile is 20% of surplus
- 25th percentile is 5% of surplus
- Is 25% of surplus an acceptable materiality standard? When?
- If the materiality standard is over 25% of surplus and there is no RMAD what does it mean?

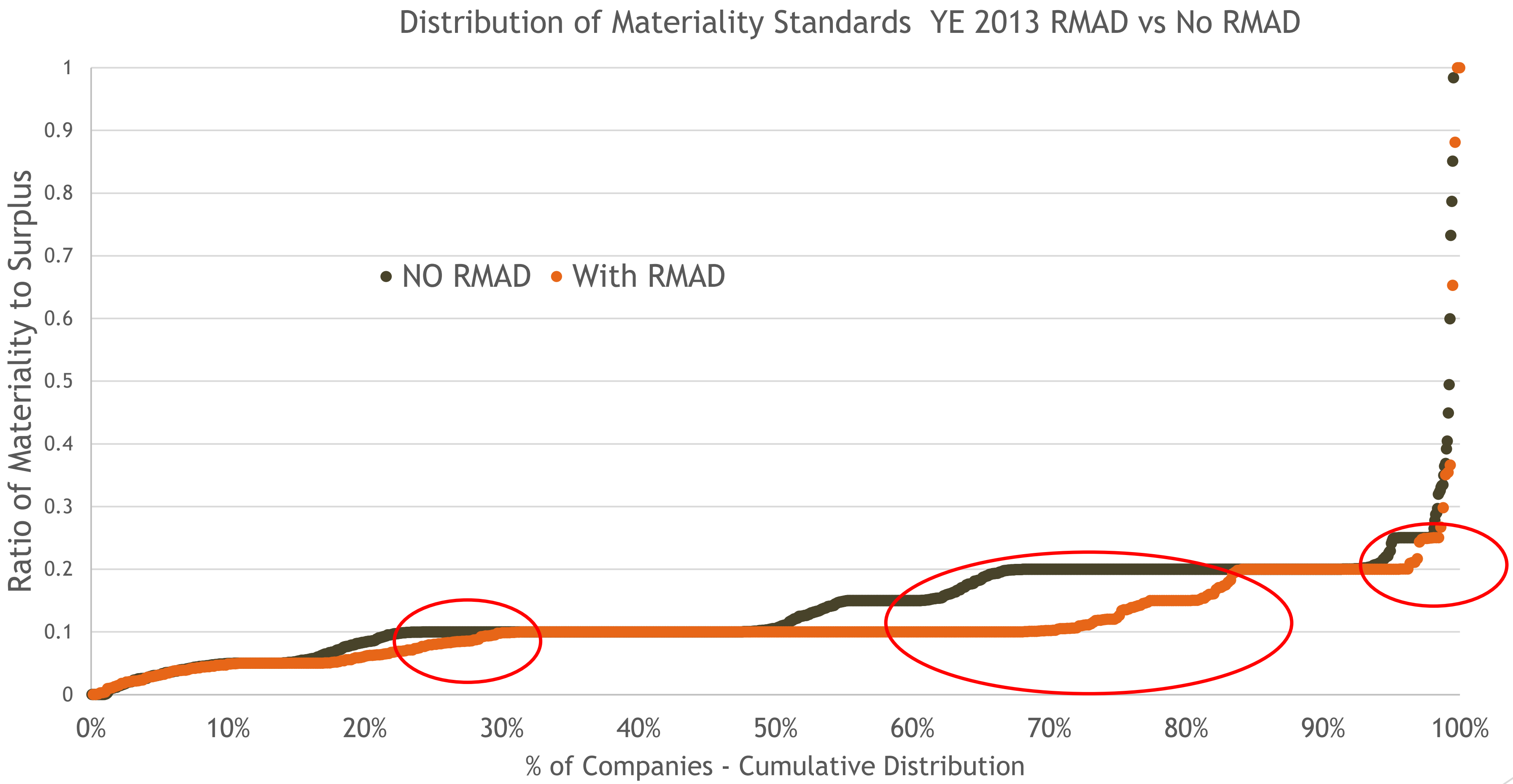
More Statistics - RMAD

- About 26% of Non-RRG s disclose RMAD
- Over 40% of RRGs disclose RMAD (RRGs tend to be smaller)
- The materiality standard for companies with NO RMAD tends to be higher. Why?

How do you select RMAD?

- Large companies?
- Small Companies?
- % of reserves?
- % of surplus?
- What if the company is close to “Action Level?”
- Is $1 a legitimate RMAD

The Selected Materiality Standard



Could materiality standards be selected to avoid disclosure of the risk of material adverse deviation? Note several ratios over 1 were removed from “NO RMAD” since they distorted the graph.

So, You Want to Talk to a Regulator?

- Set your materiality standard at over 25% of surplus & provide no explanation of “Why”
- Or better yet, don’t set a materiality standard and…
- Don’t give the name of a company officer responsible for the data

Regulators Requested – More Disclosure on Actuarial Assumptions

- Even If actuarial methods and assumptions have NOT changed, it would be useful to include this in the disclosures. This will allow the regulator reviewer to distinguish between
- a) nothing changed and
- b) something changed but the actuary forgot to mention it.

Regulators Requested – Continued

- Provide a clear data reconciliation that you do yourself. Don’t just paste in a data reconciliation that was provided by the company.
- Provide reconciliations not just of loss & DCC but of salvage & subrogation and of A&O
- If you use premiums, please explain how you checked the data.

Regulators Requested – Continued

- Provide the SOURCE of your industry data
- Explain how company and industry factors are weighted and WHY.
- Put PAGE NUMBERs on the pages
- Put all of the triangles into the report.

Defending Your Opinion & Report

- Regulator Thinks: You have said that these factors come from "industry" but have not supplied a source, triangles or a reference. How do I know the industry data is credible or applies to your company or that you didn't just make it up?

- Regulator Says: Please describe the source of your industry data and the triangles. Show that this data applicable to the company for which it is being used. Describe its credibility in terms of a reliable source and/or premiums & claim counts.

Defending Your Opinion and Report

- Why did you not describe sources of risk? Where do you explicitly state that there is, or is not , a risk of material adverse deviation?
- Why did you file the combined group opinion with this company. Why did you use the same materiality standard for each company in the group? This company retains 10% of the pool. Did you not read the practice note or the regulatory guidance?
- Why did you not disclose that your IRIS ratio was out of acceptable range?

Defending Your Opinion & Report

- How did you pick your loss ratios (loss costs) for BF?
  - It looks like you picked management's initial estimate, but this estimate appears to be low.
  - It looks you picked the same loss ratios (loss costs-trended) as last year, but is this a legitimate reason?
  - What loss ratio do you get by using Cape Cod? Why not use this loss ratio?

Defending Your Opinion & Report

- Does your opinion apply to both gross and net?
- Is there risk of adverse development in gross but not net?

Regulators Said

- If there has been adverse deviation in 3 of the last 5 years, then the explanation should at a minimum discuss specific reserve elements and applicable management decisions.
- If you made a mistake in your past reserve analysis and have corrected it, your explanation could increase credibility with the regulator.

Defending Your Opinion & Report

- What evidence do you have that the reinsurance is collectable? What did you check? How did this affect your discussion of RMAD?
- Why does the assuming company (on Schedule F) show different amounts assumed than your company shows as ceded?
  - Are you underestimating gross? (reinsurer thinks ceded will be more?)
  - Are you overestimating ceded? (reinsurer disputes insurability of the event)

Defending Your Opinion & Report

Why didn't you separate line (personal auto, work comp, med mal) by state (maybe county). It is well known that loss development is different in different regions.

Personal auto- different rules on PIP, limits, no fault

Med Mal – Some states have tort reform others not – some regions are notorious.

WC – NCCI factors are very different by state.

Defending Your Opinion & Report

- If you used premiums in your calculations did you reconcile the premiums to schedule P? Why not? What have you done to check the accuracy?
- Where is your reconciliation for salvage & subrogation? A&O
- Do you have exposure data other than premiums? Why didn't you use it? Why didn't you ask for it?

Defending Your Opinion & Report

- How did you select the trend in the Loss Ratio or loss/exposure used in the BF?
- Describe how you came up with the variability in your reserve estimate?
- How did you incorporate price changes into your analysis?
- How do you justify using industry factors when company experience shows factors that are higher?

Defending Your Opinion & Report

- How do you communicate with the pricing actuary? Are you reserving and pricing using consistent assumptions with regard to price per exposure? Are your prices up, down or stable?
- Why is there adverse development in year 20XX? Don't assume that the regulator is only concerned about the overall result.

Defending Your Opinion & Report

- How do you justify using 100% company factors? How do you calculate the credibility of the company factors?
- How do you determine the weights applied to industry, company factors?
- Why do you develop net losses to ultimate, isn't it better to develop gross losses then apply the reinsurance details to come up with net? Or maybe do both and compare results.

Defending Your Opinion & Report

- Are you aware of the fact that the company is reinsured with a swing premium so that the gross losses are extremely important in calculating the company liabilities?
- Are you aware of the specifics associated with the swing premium?

Defending Your Opinion & Report

- Why is it that the actuary doing the risk transfer analysis for your company’s reinsurance is coming up with much larger reserve estimates (loss development factors) than you?
- What if you use the reinsurers loss development factors?
- How is it that the actuary doing the risk transfer analysis (reinsurance actuary) is calculating expected losses that aren’t even in your range of estimates?

These Increase Your Chances of getting a call from the Insurance Department

- There is a change in the appointed actuary, especially if the insurer did not notify the domiciliary state promptly, or there is no letter stating whether or not there were any disagreements with the former actuary or the company did not furnish the former actuary's letter.
- The materiality standard is high
- Schedule F sessions are very different from those of the Reinsurance company

So, You Want to Talk to a Regulator?

- Book excess ceded reinsurance to get your net numbers down.
- Understate the amount of assumed reinsurance materially.
- Sell Med Mal and have no DDR UEPR, and no RMAD.

So, You Want to Talk to a Regulator?

- Show adverse deviation in 3 of the last 5 years and explain that the reason is “Adverse development” or “Reserve strengthening”
- Book reserves materially below the actuary’s central estimate

Opinion Statistics – By Surplus

- The top 10 US opiners, by surplus
  - Sign 297 opinions
  - Opine on companies with about $450 billion of surplus (over half)
- The top 20 US opiners, by surplus
  - Sign 421 opinions
  - Opine on companies with about $573 billion of surplus