

# CLRS Workshop – Maximizing the Value of Your Actuarial Opinion and Report

*As Viewed by Company Management*

*Commitment Beyond Numbers*



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# Outline of Presentation

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- Roles in the reserving process
- Suggestions for Documentation and Discussion
- Communications with Management
- Consultant Perspective

# Roles in the Reserving Process (Intended Users of the SAO)

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- Board of Directors / Audit Committee
  - Fiduciary responsibility and regulators' expectation for overseeing the financial reporting process
  - Board is required to appoint a qualified actuary to render an opinion on the recorded loss reserves for the regulatory year-end financial statements
- Company Management
  - The final decision on the loss and LAE reserve estimate to book is the responsibility of company management
  - Ultimately held accountable for the financial performance of the company

# Roles in the Reserving Process (Intended Users of the SAO)

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- Appointed Actuary

- Appointed by the Board of Directors to render a statement of actuarial opinion on the company's held reserves
- Reserves being opined on are defined in the opinion
- Appointed actuary may be internal or external
- Identify significant data used in developing opinion and communicate with auditor
- Identify number of disclosures communicated in SAO

- Auditor

- It is the auditor's responsibility to evaluate the reasonableness of the reserve established by management
- The auditors should identify components of loss reserves that could be material or are of higher risk to the financial statements that have been considered in developing the overall reserve estimate

# Roles in the Reserving Process

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- Regulators
  - Periodic financial examinations occur on a scheduled basis
  - These exams verify and validate what is presented in the company's annual statement to ascertain whether the company is in good financial standing

# Suggestions for Documentation and Discussion

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- What would management need to know in order to come up with their “best estimate” of loss reserves?
- What information gathered while preparing a Statement of Actuarial Opinion would be useful to the Board of Directors?
- Which items in the Statement of Actuarial Opinion or the ensuing report may trigger questions from auditors or regulators?
- Where does the documentation belong (SAO, AOS, Actuarial Report)?

# Key Assumptions

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- Loss development assumptions
  - Use of patterns
  - Tail Factor Selections
- Adjustments for operational changes
- Bornhuetter-Ferguson “*a priori*” assumptions
  - Did this change from last year?
- Expense assumptions – How are Defense & Cost Containment (DCC) and Adjusting & Other (A&O) expenses treated

# Reserve Releases or Increases

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- Reserve releases or adverse development
  - Which line(s) of business
  - What accident years?
- Actuarial opinion summary
  - Extended commentary if company had 1 year adverse development over 5% of prior year's surplus in 3 of the past 5 calendar years
- IRIS Tests
  - Extended comments on factors that led to any unusual values



# Reinsurance Issues

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- Retroactive and Financial Reinsurance
- Reinsurance Collectability
  - Reserves ceded to a reinsurer with an AM Best rating below A-
  - Ceded paid amounts overdue
  - Reinsurer is not reviewed by rating agency
- Assumed reinsurance from Pools & Associations

# Asbestos, Environmental and Mass Tort Exposure

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- Does the Relevant Comments of the SAO include extended commentary on Asbestos and Environmental exposure?
- Does the Relevant Comments of the SAO mention other mass tort exposure in the Risk of Material Adverse Deviation or IRIS section?
- How have these reserves changed over the past calendar year?

# Other Items

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- Anticipated Salvage and Subrogation
- Policyholder Deductibles
- Discounting
- Risk Margins

# General Data Concerns

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- Reliance on industry data
- Changes in underwriting
- Expansion into new lines of business or states
- Changes in retention
- Treatment of large (unusual) claims

# General Data Concerns - Operational Changes

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- Changes that affect loss development
  - New claims manager
  - New Software
- Changes that affect the initial reserve
  - New claims manager
  - New Third Party Adjustor (TPA)
- Are any modified actuarial techniques such as the Berquist-Sherman method used?

# RMAD

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- Materiality
  - What is it?
  - How was it selected?
- Risk Factors
  - What are the company's primary risk factors?
  - Interactions?
  - Could any of these specific factors cause material adverse deviation?

# Legislative Changes

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- Florida PIP / Florida Assignment of Benefits (AOB)
- Florida Workers Compensation
  - Castellanos Decision
- SCHIP
  - Reporting requirements for Non-Group Health Plan (NGHP) insurers
  - Distortion of historical claim counts and claim severities

# Communications with Management

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- Management shouldn't be “surprised” by the SAO
- Management or the Appointed Actuary will need to communicate concerns to the Board of Directors
- Has there been a change in management?
  - Do they have the same reserving philosophy?



# Changes in Methods or Assumptions

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- What is the reason for the change?
  - New line of business?
  - More reliance on emergence / less reliance on benchmarks
  - Change in case reserve philosophy that affects incurred methods

# Less Common Situations

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- Differing opinions – direct vs. net
- No Opinion or Qualified Opinion
- Changes in Data/Accounting (sinkhole accident date)
- UPR for long duration contracts (including ERE, DD&R)
- Turmoil in company leadership
- Rehabilitation/Liquidation
- GAAP vs. SAP – Captive/RRG SAOs
- Transitioning Appointed Actuaries
- Errors or changes impacting a filed SAO

# Feedback from Regulators and Auditors

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- Schedule P reconciliation
- Documentation of adverse IRIS Test Results
- Reasons for adverse development by accident year and line
- Reasonableness of held DD&R reserves

# Thank You for Your Attention

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