What’s Your Opinion?

Actuarial Opinion Requirements Across jurisdictions

September 17, 2020

Casualty Loss Reserve Seminar

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Agenda

- Introductions
- Content Block 1
  - Qualifications & Requirements
  - Opinion Scope
- Q&A Break 1
- Content Block 2
  - Data, Methodology, and Documentation
  - Key Areas of Recent Focus
- Q&A Break 2

Actuarial Opinions - Canada

- Qualifications & Requirements
- Opinion Scope

Qualification Process

- AA Requirements/Education
  - Each Company (Canadian insurance company, provincial companies, fraternal benefit societies and Canadian branches of foreign insurance companies and foreign fraternal benefit societies) must appoint an actuary of the company and notify the Superintendent in writing
  - Must be a Fellow of the Canadian Institute of Actuaries (FCIA)
  - Work in Canada for at least three of last six years, of which at least one year was performing valuation of Canadian actuarial liabilities of an insurance company
  - Has experience with the CIA's Standards of Practice, and relevant insurance legislation and regulation
  - Is up to date with the CIA's Continuing Professional Development requirement (https://www.cia-ica.ca/membership/continuing-professional-development-(cpd))
  - Has not been subject of an adverse finding by a CIA Disciplinary Tribunal
- Approval Process
  - OSFI (Office of the Superintendent of Financial Institutions) must be notified of the appointment of the actuary of the company in writing
  - No AA may accept an appointment before requesting and receiving a written statement from the previous AA
  - The appointment may only be accepted if there is no reply to the written statement request after fifteen days or if the written statement received and no issues noted
- Internal resource vs external resource
  - - Mostly external except for few big insurance entities

Scope

- Accounting Basis
  - Report under IFRS 4
  - Claim and Premium Liabilities must be estimated by AA
  - Expression of opinion must state whether the liabilities make appropriate provision and represent the financial statements fairly
  - Valuation work by AA is in accordance with Accepted Actuarial Practice in Canada (https://www.cia-ica.ca/docs/default-source/standards/sg010120e.pdf)
- Bad Debt (on R/I Recoverables)
  - No requirement to make explicit estimation from AA
  - Reflected through Reinsurance MfAD (ranging from 0% to 15%)
- ULAE Calculation
  - Commonly estimated via paid-to-paid ratio from a claims liability analysis
- Tax implications
  - The income tax deduction in respect of an insurer's claim liabilities is less than the amount of the claim liabilities recorded in the Annual Statement. This creates a "future tax temporary difference" that gives rise to an asset for Future Income Taxes.
  - AA estimates the effect of discounting this asset for future income taxes. If it is material, the actuary's estimate of the policy liabilities should be reduced accordingly.

Scope: Premium Liabilities

- ## Maximum Deferrable Policy Acquisition Expense
  - AA is required to test the adequacy of premium liabilities in the insurer’s financial statements, including all future costs arising from the unexpired portion of in-force policy,
  - May do so, by comparing if the carried Deferrable Policy Acquisition Expense (DPAE) is less than or equal to the Maximum DPAE
  - Maximum DPAE = Net Unearned premium + Unearned (reinsurance) commissions - the estimated premium liabilities (including Expected incurred loss, Internal loss adjustment expense and expected future reinsurance costs)
  - Net basis and all line combined basis
  - If carried DPAE is higher than Maximum DPAE, need to reduce to the Maximum DPAE
  - If Maximum DPAE is negative, need to reduce carried DPAE to 0 and book premium deficiency
- ## Premium Deficiency
  - Premium deficiency liability is established in the amount by which the estimated premium liabilities exceed the sum of the net UPR and unearned (reinsurance) commissions (when Maximum DPAE is negative)

Scope: Discounting

- ## Policy Liabilities considerations
  - Claim and Premium liabilities should be subdivided into reasonably homogeneous groups based on payment pattern, length of payout period and any predetermined schedule of payments
  - Premium liabilities must also consider average accident date and average payment date underlying future claim costs
- ## Discounting Basis
  - Net = Gross - Ceded
  - Two of these bases are selected based on data availability, cash flow volatility and the reinsurance program
- ## Discount Rates
  - Cash flow analysis/duration weighted yield
  - Method of valuing assets and reporting investment income
  - Allocation of assets and income among lines of business
  - Return on assets at the balance sheet date
  - Yield on assets acquired after the balance sheet date
  - Capital gains and losses on assets sold after the balance sheet date
  - Investment expenses, and losses from default
  - IFRS 17 will have a material impact on this calculation

Scope: Risk Margins (MfADs)

- Margins for Adverse Deviations (MfADs)
  - reflect the degree of uncertainty of the best estimate assumption
- Three Categories:
  - Interest return rate MfAD (25 bps to 200 bps)
  - Recovery from reinsurance ceded MfAD (0% to 15%)
  - Claims Development MfAD (2.5% to 20%)

Actuarial Opinions – Lloyds/UK

- Qualifications & Requirements
- Opinion Scope

Qualifications / Requirements

- The Actuary providing an Actuarial Opinion for a Lloyd's Syndicate must hold the relevant Practising Certificate (PC)

- To award a PC, the following are considered:
  - The Actuary is fit and proper to hold a PC; and
  - Meets the criteria set down by the Institute and Facualty of Actuaries (IFoA) in force at the date of the application.
- The criteria to be awarded a PC is considered annualy and includes:
  - Recent and relevant experience;
  - Technical Experience;
  - Validation and Verification of Data;
  - CPD;
  - Attestation from an existing PC holder; and
  - Identity and Criminal Record Checks.
- Typically the signing actuary for Lloyd's SAO will be external with a few exceptions
- Lloyd's SAO: Independent of the reserving team but will need close collaboration

Scope of the SAO

- A fully independent estimate of the liabilities of Syndicate as at 31 December with the purpose of providing the Statements of Actuarial Opinion (“SAOs”) for Syndicate. This may include SAOs on:
  - Worldwide Business, gross and net of reinsurance, as required by the Council of Lloyd’s and the International Insurers Department (“IID”) of the National Association of Insurance Commissioners (“NAIC”) – the “Worldwide SAO”;
  - the gross reserves in the Lloyd’s U.S. Situs Surplus Lines Trust Fund (“SLTF”) as required by both the IID and by the New York Department of Financial Services (“NYDFS”) – the “Surplus Lines SAO”; and
  - the gross reserves in the Lloyd’s U.S. Situs Credit for Reinsurance Trust Fund (“CRTF”) as required by the NYDFS – the “Credit for Reinsurance SAO”.
- SAOs are required on each of these figures, split by three underwriting years, i.e. years X, X-1 and X-2. The underwriting years prior to X-2 would typically have previously been closed into the X-2 year of account.

SAO and Reporting for Lloyd’s

- The SAO is conducted under the Lloyd’s Valuation of Liabilities Rules and timetable. This will include the calculations and reporting deliverables of the following:
  - Its outstanding claims liability, both gross and net of reinsurance, and, where relevant, both gross and net of future premiums;
  - its outstanding liabilities relating to periods of cover that remained unexposed as at 31 December;
  - Its future claims handling expenses, both allocated and unallocated;
  - Reinsurance bad debt provision;
  - Worldwide and US Trust Fund opinion for each year of account;
  - SAO template;
  - An analysis of any reserve margin;
  - Movement analysis, and
  - Formal SAO report.
- Lloyd’s requires that all releases of earned “reserve margins” claimed for capital setting in the Solvency II balance sheet be no greater than that identified by the SAO Actuary. The test is applied for each open year of account
- Additionally, Lloyd’s requires the reporting of unearned ultimate premium and claims including ALAE and ULAE, under solvency II basis, so that Lloyd’s may derive the profit on unearned to be used for capital setting
- A tax opinion is usually provided based on the analysis carried out to confirm that the reserves held are not excessive for years X-2 & Prior

Actuarial Opinions – Bermuda

- Qualifications & Requirements
- Opinion Scope

LRS Requirements—Criteria for Actuaries

- Insurers subject to the opinion requirement must appoint an actuary.
- The regulator (Bermuda Monetary Authority, or BMA) determines whether the actuary "possesses the appropriate integrity, competency, resources, qualifications and experience…commensurate with the nature, scale and complexity of the insurer's business" as well as the regulator's requirements.

Criteria for Actuaries

- Approval is entirely at BMA's discretion; however, a person will generally be accepted if they meet all of the following:
  - Qualified member in good standing of a prominent actuarial society.
  - Meets requirements to be considered qualified to sign statutory reserve opinions by their credentialing body.
  - Has experience evaluating technical provisions for the insurer's business with respect to BMA's economic balance sheet (EBS)
  - Free from conflicts of interest.

Scope of the LRSO

- BMA licenses different classes of insurers; higher license classes have fewer operational restrictions but more regulation.
- The highest classes are required to produce an economic balance sheet that evaluates the risk-adjusted net present value of all future cash flows resulting from business already bound.
- The LRS opines that the total technical provisions (premium provision, L&LE provision and risk margin) meet the legal requirements and make a “reasonable provision” for their ultimate value.

Scope of the LRSO

- Technical Provisions are comprised of:
  - Earned and unearned L&LAE reserves
  - BBNI reserves (Bound but Not Incepted)
  - Provision for Uncollectible Reinsurance
  - ENIDs (Events Not In the Data)
  - Future expenses
  - Premium Receivables
  - Discounting
  - Risk margin.
- EBS was new for the YE 2017 reporting.

Actuarial Opinions - Canada

- Data, Methodology, and Documentation
- Key Areas of Recent Focus

AA Opinion versus AA Report

- AA Opinion statement does not delve into specifics of assumptions made
- AA Report outlines all assumptions and their justifications
  - Valuation methodology
  - MfAD selections
  - Discounting selections, including discount rate and payment patterns
  - Additional considerations, such as catastrophes, auto reforms, other emerging issues
- AA relied on auditor for data reconciliation

AA Expression of Opinion: Sample

9. Appendix I - Expression of Opinion

I have valued the policy liabilities [and reinsurance recoverables] of [the Company] for its [consolidated] [statement of financial position] at [31 December XXXX] and their changes in the [consolidated] [statement of income] for the year then ended in accordance with accepted actuarial practice in Canada including selection of appropriate assumptions and methods.

(Qualifications should be included here)

In my opinion, the amount of policy liabilities [net of reinsurance recoverables] makes appropriate provision for all policy obligations and the [consolidated] financial statements fairly present the results of the valuation.

The results of my valuation together with amounts carried in the Annual Return are the following:

Claim Liabilities	**Carried in Annual Return($'000)**	**Appointed Actuary's Estimate($'000)**
(1) Direct unpaid claims and adjustment expenses		
(2) Assumed unpaid claims and adjustment expenses		
(3) Gross unpaid claims and adjustment expenses		
(4) Ceded unpaid claims and adjustment expenses		
(5) Other amounts to recover		
(6) Other net liabilities		
(7) Net unpaid claims and adjustment expenses (3)-(4)-(5)+(6)		

Premium Liabilities	**Carried in Annual Return ($'000) (Col. 1)**	**Appointed Actuary's Estimate ($'000) (Col. 2)**
(1) Gross policy liabilities in connection with unearned premiums		
(2) Net policy liabilities in connection with unearned premiums		
(3) Gross unearned premiums		
(4) Net unearned premiums		
(5) Premium deficiency		
(6) Other net liabilities		
(7) Deferred policy acquisition expenses		
(8) Maximum policy acquisition expenses deferrable $[(4)+(5)+(9)]_{\text{Col. 1}} - (2)_{\text{Col. 2}}$		
(9) Unearned Commissions + Ceded Deferred Premium Taxes + Ceded Deferred Insurance Operations Expenses		

__________________ FCIA
Signature of Appointed Actuary

____
Date opinion was rendered

__________________ FCIA
Printed name of Appointed Actuary

____
Location opinion was rendered

The language in square brackets is variable and other language may be adjusted to conform to interim financial statements and to the terminology and presentation in the financial statements.

AA Report: Sample Table of Contents

Source: https://www.osfi-bsif.gc.ca/Eng/Docs/PC_AA_Memo_2019.pdf

Key Areas of recent focus

- Covid related considerations and they will be addressed in CIA PCFRC falls newsletter
- Economical environment/discount rate
- 17 development/impact on AA work

Actuarial Opinions – Lloyds/UK

- Data, Methodology, and Documentation
- Key Areas of Recent Focus

Data

- Rely upon data supplied by the managing agent.
- Only reasonableness checks carried out all data underlying the SAO and report although the managing agent will confirm that all data supplied are accurate.
- Lloyd’s expects that a Data Accuracy Statement is provided by a nominee of the Managing Agent’s Board. The provision of inaccurate, incomplete or misleading information to the Signing Actuary can lead to disciplinary proceedings against the Managing Agent.
- The data is supplemented with conclusions drawn from data compiled from general industry sources (benchmarks).
- There is strong reliance placed on the information supplied regarding estimates of future unearned premiums and claims.

Key Areas of Focus

- Covid-19
- Social Inflation
- Recession
- Opioids related claims
- Structured settlements
- Catastrophes
- Run-off classes

Actuarial Opinions – Bermuda

- Data, Methodology, and Documentation
- Key Areas of Recent Focus

Data/Methods/Assumptions

- LRSO is comprised of nine parts:
  - Identification
  - Scope
  - Conditions and Limitations
  - Expression of Opinion
  - Summary of Methodology
  - Relevant Comment
  - Reliance on Opinions of Other Actuaries
  - Work Papers
  - Signature

Data

- LRS should comment on the extent to which (unaudited) EBS data reconciles to (audited) GAAP financial statement data.
- Disclose the senior official at the insurer upon whom the actuary relied for preparation of data.
- Cover any additional checks of the data performed by the LRS
- Describe main types and sources of data, describe data processing steps.

Methods/Assumptions

- In a 2019 Market Feedback letter, BMA stated the LRSO is intended to sit between a full Actuarial Report and a basic attestation.
- The LRSO should be sufficient to enable BMA to understand how the insurer derives its Technical Provisions without the need to request the underlying working papers.
- Discussion should include reserving thought process, validation, segmentation, reserving basis, reserving models, selections, adjustments and key parameters.

Key Areas of Recent Focus

- BMA issued a market feedback letter on EBS opinions in March 2019, mainly addressing the issue that the balance in the opinion content was skewed too far toward an attestation and not enough in the direction of a full actuarial report.
- Bermuda-specific issues:
  - Dynamic insurance market—constant formations and M&A
  - High staff turnover
  - Huge variety of insurance business models

Key Areas of Recent Focus

- BMA's EBS framework is fairly new and ambitiously complex.
- In our experience, the most engaged stakeholders are company actuaries and company management.
  - The BMA EBS concept has a learning curve; company actuaries wish to confirm their understanding and interpretation of the instructions.
  - Company management is at pains to ensure that BMA can be satisfied they have thoroughly accounted for their future obligations, particularly if their strategy or products are unique or challenging to explain.

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