

# Your 2021 Statement of Actuarial Opinion and Reserve Report

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# Presentation Topics

1. COVID 19 and the impact on your Statement of Opinion and Reserve Report
2. Review of Qualification Changes Implemented by NAIC in 2020 and upcoming CAS CE log changes for 2021
3. Appointed Actuary Qualification Documentation

## 2020 Casualty Loss Reserve Seminar

# Current Issues for your 2021 Statement of Actuarial Opinion and Reserve Report – COVID-19

Jeff Carlson

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## Session Overview

### COVID-19 Issues

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- Statement of Actuarial Opinion
    - Scope, Relevant Comments, and Opinion Sections
  - Actuarial Report
  - Questions & Answers
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- These materials are provided for general educational purposes only and should not be relied upon for any purpose.

## COVID-19 issues may affect many aspects of reserve analysis

DATA	APPROACH	ASSUMPTIONS	COLLECTABILITY	USE OF WORK OF ANOTHER
<ul style="list-style-type: none"><li>• Types</li><li>• Sources</li><li>• Segmentation</li><li>• Adjustments</li></ul>	<ul style="list-style-type: none"><li>• Methods used</li><li>• Weights to methods</li></ul>	<ul style="list-style-type: none"><li>• Adjustments</li><li>• Judgments</li></ul>	<ul style="list-style-type: none"><li>• Reinsurance cessions</li><li>• Large deductibles</li></ul>	

- In addition, views on uncertainty, risk factors and the potential for the risk of material adverse deviation (RMAD) may differ from the past.
- These issues need to be considered when drafting the Statement of Actuarial Opinion (SAO) and the Actuarial Report.
- We will look at several examples.



## SAO – Scope section

### Provider of Data

#### NAIC SAO Instructions example language:

- *“In forming my opinion on the loss and loss adjustment expense reserves, I relied upon data prepared by \_\_\_\_\_ (officer name and title at the Company).”*
- Generally, data and information may be received from the Chief Actuary or CFO.
- Material additional information may be received related to COVID claims .
  - E.g. estimates for a large block of business interruption claims reflecting assumptions regarding the outcome of coverage disputes and applicability of reinsurance.
  - This information may be received from the Chief Claims Officer.
- Should consider if appropriate to list two Company officers as data providers.
  - Depends on the materiality of the additional information.
- Might encourage a single officer (e.g. the Chief Actuary or CFO) to take responsibility for the entire body of data and information.
  - Cleaner, mitigates the possibility of misunderstanding or gaps in responsibility.

## SAO – Scope section

### Valuation Date

#### ASOP No. 36:

- *“2.13 Valuation Date: The date through which transactions are included in the data used in the unpaid claim estimate analysis.”*
- Certain data for specific analysis may be valued at a different date than the standard data.
  - E.g. The value of COVID-19 business interruption and D&O claims may reflect judicial decisions through January 31 after year-end.
- In that case and if material, should list multiple valuation dates.
- This may be similar to prior instances of large natural catastrophe events occurring late in the year, where the value of the related claims reflected a valuation date later than year-end.



## SAO – Relevant Comments section

### Material Changes in Assumptions and/or Methods

#### NAIC SAO Instructions :

- *“Methods and Assumptions: If there has been any significant change in the actuarial assumptions and/or methods from those previously employed, that change should be described in a RELEVANT COMMENT paragraph.”*
- According to ASOP No. 36, the actuary should consider whether the changes are likely to have had a material effect on the actuary’s unpaid claim estimate.
- If the changes likely had a material effect, the nature of the changes should be disclosed.
  - The actuary is not required to quantify the impact of the changes.
- If the actuary is not able to determine if the changes likely had a material effect, the actuary should disclose the nature of the changes and that the materiality is unknown.
- In the SAO, the description of the changes may be brief.
- But in the Actuarial Report, the description should be comprehensive with supporting exhibits as appropriate.

## SAO – Relevant Comments section

### Material Changes in Assumptions and/or Methods (continued)

- Examples of changes in assumptions and/or methods that may be material:
  - Segregating direct COVID-19 related claims and estimating separately.
    - COVID claims may have “unexpected” effect on claim frequency, severity, expected loss ratio, loss development, average LAE, and may cause distortions to the analysis
    - COVID claims may be considered to have higher uncertainty than non-COVID claims and require a wider range of reasonable estimates.
    - COVID claims may be considered “not estimable” due to high degree of uncertainty.
    - May choose to use different projection methods or models for COVID-19 claims.
  - Consideration of exposure/premium volume decreases due to economic recession, and possible resulting mix changes.
    - May consider different risk and claim characteristics for the reduced volume (e.g. auto claim frequency and severity, workers compensation claims in a work-from-home environment).
    - May consider the timing of recognition of exposure/premium decreases versus loss decreases (e.g. workers compensation payroll/premium decrease may not be recognized until premium audit, timing of auto premium rebates).
    - May adjust various assumptions due to estimated mix change by geography or class (e.g. claim frequency, claim severity, expected loss ratio, loss development).

## SAO – Relevant Comments section

### Material Changes in Assumptions and/or Methods (continued)

- More examples of changes in assumptions and/or methods that may be material:
  - Reflection of changes in the claim notification, quantification and settlement processes.
    - Business slowdowns may cause delays throughout the claim life-cycle.
    - Potential for greater propensity to settle claims.
  - Reflection of a revised “seasonality” of premium and/or loss volume.
    - E.g. volume reduction in March, followed by gradual increase toward normal level.
    - May affect premium earning pattern, realization of price changes, loss development patterns.
- Example of SAO language.
  - “A material change in actuarial methods was made in the analysis supporting this opinion. The workers compensation COVID-19 related claims were excluded from the data used in the standard methods. The unpaid losses for the COVID-19 related claims were estimated using a model utilizing specific assumptions for claim frequency and severity by state and class.”

## SAO – Relevant Comments section

### Ceded Reinsurance

#### NAIC SAO Instructions :

- *“The Appointed Actuary’s comments on reinsurance collectability **should address any uncertainty associated with including potentially-uncollectable amounts in the estimate of ceded reserves.** ... The comment should also reflect any other information the Appointed Actuary has received from management or that is publicly available about the capability or willingness of reinsurers to pay claims.” (emphasis added)*
  
- There is potential for disputes between insurers and reinsurers regarding coverage. For example, for business interruption claims:
  - Differences in coverage language between primary and reinsurance contracts.
  - Definition of an “event” for reinsurance aggregations in catastrophe covers.
    - Time clauses, number of occurrences.
    - Definition of “natural perils”.
  
- The Appointed Actuary should understand what assumptions regarding collectability are reflected in the carried reserves and in his/her estimates, and the uncertainties related to those assumptions.

## SAO – Relevant Comments section

### Ceded Reinsurance (continued)

- Example SAO language:
  - “The Company has a large ceded reserve with regard to business interruption claims related to COVID-19. The Company’s reinsurers are disputing a portion of the cession totaling \$XX million. The inability of the Company to collect on that cession would be material to its [surplus/reserves]. My analysis assumes that such cession will be [collectable/ uncollectable/ partially collectable].
  - Description of approach and rationale for the estimated ceded amount should be included in the Actuarial Report.
- Potential for a “binary” situation.
  - Result could either be fully collectable or fully uncollectible.
  - Consider if a reasonable basis to estimate the likelihood of collectability.
  - Consider if it is reasonable to assume full collectability (or no collectability).
  - If no reasonable basis, might consider a qualified opinion which excludes the cession from the scope.

## SAO – Relevant Comments section

### Company-Specific Risk Factors

#### NAIC SAO Instructions :

- *“Company-Specific Risk Factors: The Appointed Actuary should include an explanatory paragraph to describe the major factors, combination of factors or particular conditions underlying the risks and uncertainties the Appointed Actuary considers relevant.”*
- For many companies, the effects of COVID-19 have likely increased the company’s risks and uncertainties related to the reserves.
- It is appropriate to include a concise list of the risks and uncertainties in the relevant comment.

## SAO – Relevant Comments section

### Company-Specific Risk Factors (continued)

- Example SAO language:
  - *“In my evaluation, I considered the following risk factors which increase the uncertainty inherent in the Company’s loss and loss adjustment expense reserves:*
    - *Uncertainty related to regulatory, legislative and judicial decisions regarding coverage of COVID-19 related claims*
    - *Potential slowdown in claim notification, quantification and settlement processes which could affect future loss development patterns and settlement amounts*
    - *The effects of changes in mix of business by geography and class on claim frequency, severity, loss ratio, loss development, ...*
    - *Potential premium reduction upon premium audit of workers compensation policies*
    - *The aggregation of COVID-19 related losses for outwards reinsurance purposes, and the collectability of disputed reinsurance cessions related to business interruption claims*
    - *The collectability of workers compensation large deductible recoveries*
    - *... (many more examples are possible!)”*



## SAO – Relevant Comments section

### Risk of Material Adverse Deviation (RMAD)

#### NAIC SAO Instructions :

- *“Risk of Material Adverse Deviation: ... The Appointed Actuary should explicitly state whether or not he or she reasonably believes that there are significant risks and uncertainties that could result in material adverse deviation.”*
- The presence and effects of COVID-19 may not require change to the structure of the RMAD relevant comment.
- However, the potential for increased risks and uncertainties may cause the actuary to more seriously consider if an RMAD is present, even for companies which have not previously had an RMAD.

## SAO – Relevant Comments section

### IRIS Test 13

#### NAIC SAO Instructions :

- *“If the Company’s reserves will create exceptional values under the NAIC IRIS Tests for One-Year Reserve Development to Policyholders’ Surplus, Two-Year Reserve Development to Policyholders’ Surplus or Estimated Current Reserve Deficiency to Policyholders’ Surplus, **the Appointed Actuary must include RELEVANT COMMENT on the factors that led to the unusual value(s).**” (emphasis added)*
- IRIS Test 13 is based on the assumption that the ratio of unpaid losses and LAE to the latest year net earned premium should be consistent from year to year.
- There are various reasons why COVID-19 may cause the reserves to premium ratio to be higher than in prior years.
  - Level of unpaid [business interruption/ medical malpractice/ workers comp/ D&O] claims much higher than normal.
  - Reduced premiums for some segments results in a change in mix by line of premiums and reserves.
- Actuary must explain in the SAO the cause of the failed test.

## SAO – Relevant Comments section

### Other topics

- Workers compensation retrospective premium asset or unearned premium liability.
  - Negative premium audits could be significant in 2021.
  - Thus an asset for retrospective premium could be overstated (or a liability could be understated).
  - The actuary could consider if the item is material, and if a relevant comment is warranted.
  - If including a relevant comment, would list the amount of the item on Exhibit B, line 14

## SAO – Opinion section

### Qualified opinion or No opinion

- Referring back to the “binary” claim situation on page 10, of disputed reinsurance cessions:
  - If the potential claim amounts are material enough, and
  - If the actuary concludes that they do not have a reasonable basis to estimate the liabilities, then
  - Could consider issuing a qualified opinion, excluding the disputed cession amounts.
- If the actuary concludes that they do not have a reasonable basis to estimate the majority of the reserves:
  - Which could arise due to a lack of necessary data and information for a very material portion of the reserves,
  - Consider a “No Opinion” opinion.
  - The actuary is required to describe the reasons why no opinion is given.
  - A regulator (and the company) may not look favorably on a “No Opinion” opinion, so every effort should be made to obtain the needed information.

## SAO – Opinion section

### Use of Work of Another

#### NAIC SAO Instructions :

- *“If the Appointed Actuary has made use of the work of a non-actuary (such as for modeling) for a material portion of the reserves, that individual must be identified by name and affiliation and a description of the type of analysis performed must be provided.”*
- Example 1: Use the work of the company’s General Counsel (or outside counsel) for assessment of the outcome of suits and disputes related to coverage for a large number of business interruption claims and related reinsurance coverage.
- Example 2: Use the work of a workers compensation third party administrator (TPA) for assumptions about long-term health effects of COVID-19 on claimants (and the corresponding effects on unpaid losses).

## SAO – Opinion section

### Use of Work of Another (continued)

#### ASOP No. 36 takes the disclosure requirement further:

- *“The actuary should only make use of another’s analyses or opinions when, in the actuary’s professional judgment, it is reasonable to do so. In making this determination, the actuary should consider the following:*
  - *a. the amount of the reserves covered by another’s analyses or opinions in comparison to the total reserves subject to the actuary’s opinion;*
  - *b. the nature of the exposure and coverage;*
  - *c. the way in which reasonably likely variations in estimates covered by another’s analyses or opinions may affect the actuary’s opinion on the total reserves subject to the actuary’s opinion; and*
  - *d. the credentials of the individual(s) that prepared the analyses or opinions.”*
- *And further: “If the actuary makes use of an analysis or opinion of another not within the actuary’s control for a material portion of the reserves, **the actuary should disclose whether the actuary reviewed the others’ underlying analysis.** If a review was conducted, **the actuary should disclose the extent of the review including items such as the methods and assumptions used and the underlying arithmetic calculations.**” (emphasis added)*

## The Actuarial Report should explain and elaborate on all aspects of the SAO

### NAIC SAO Instructions:

- *“The Actuarial Report must contain both narrative and technical components. **The narrative component should provide sufficient detail to clearly explain to Company management, the Board of Directors, the regulator or other authority the findings, recommendations and conclusions, as well as their significance. The technical component should provide sufficient documentation and disclosure for another actuary practicing in the same field to evaluate the work. This technical component must show the analysis from the basic data (e.g., loss triangles) to the conclusions.**” (emphasis added)*
  - And further: *“The Actuarial Report must also include: ... Extended comments on trends that indicate the presence or absence of risks and uncertainties that could result in material adverse deviation.”*
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- The Actuarial Report is a confidential document, versus the SAO which is a public document. Thus, the Actuarial Report should be more comprehensive and transparent in its presentation.



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# **Review of NAIC Changes in 2020 and upcoming CE log changes for 2021**



# Updated Actuarial Opinion Instructions



# Updates to the Actuarial Opinion Instructions

- Main changes

- Need annually to provide a qualification document to the Board, but can go through management
  - Confidential, but available to the regulator on request
- Requires an accepted designation
  - New FCAS, ACAS, FSA-GI accepted if they meet basic education standard
  - Starting with designations earned in 2021, AA must have current exam 6 US and 7, substitutions are not allowed
  - Clarifies that all appointed actuaries (AA's) must be subject to the Code of Conduct and the ABCD
    - CAS, SOA, or AAA membership does this



# Do I meet Basic Education Standard?

- If you are currently signing Actuarial Opinions, the answer is most likely yes.
- FCAS
  - Passed Exam 6 U (2011 to present)
  - Passed Exam 7 US (2000-2010)
  - Passed Exam 7 & 8 (prior to 2000)
- ACAS + Exam 7
  - Exam 6 U & 7 (2011 to present)
  - Exam 6 & 7 US (2000 – 2010)
  - Exam 7 & 8 (2000 and prior)

Some obtaining ACAS's prior 2000 need to document obtainment of knowledge from 6 U





# Recertification Initiative

New CE recording requirements for Appointed  
Actuaries (AA's)



# Updates to the Recertification Process (Activities)

- Started with the reviewing consultants' comments proposing more formal recertification process
- NAIC accepted the CAS/SOA offer to help
  - Joint CAS/SOA task force formed to provide input
  - Task force examined recertification process in other professions (accounting, medical, legal)
  - Proposed a recertification process centered on CE
  - NAIC accepted the proposal, and the task force is implementing





# Updates to the Recertification Process

- 2020

- Annual attestation expanded to include current requirements for AA's
- i.e. you could attest you meet the USQS, or that you both meet the USQS and NAIC AA qualifications even if you aren't currently an AA

**Edit - Individual CE Attestation** close

name: Williams Kendall P.

attestation year: 2020

compliance attestation: I have complied

method: US Qualification Standard

**Edit - Individual CE Attestation** close

name: Williams Kendall P.

attestation year: 2020

compliance attestation: I have complied - NAIC Statem

method: US Qualification Standard



# Updates to the Recertification Process (CE Documentation)

- 2021

- Expanded mandatory confidential NAIC reporting of CE detail log by AA's to their organization (CAS, SOA, AAA)
- Anonymous annual reporting of CE summary statistics by CAS/SOA to the NAIC
- The CE requirements for AA's **do not change**. Just reporting and review processes
- NAIC may wish to change requirements for AA's once they have seen the summary reporting



# Updates to the Recertification Process (CE Documentation)

- Expanded requirements would apply to AA's only, not to all CAS/SOA/AAA members
  - Or those that wish to be qualified to sign opinions
- For documentation of 2020 CE for 2021 attestations, all appointed actuaries will need to add an additional documentation of NAIC CE categories in their existing process
- Preference is to be in Excel to ease reporting
- **Optional** Excel reporting form will be available on CAS website
- Excel reporting form may become **standard** for all appointed actuaries in 2021 for 2022 attestations.
- Required reporting to your organization (CAS, SOA, AAA) in the specified format
- Focused higher coverage of review of CE
- Reporting summary statistics to NAIC on types of CE AA's are taking



# Updates to the Recertification Process (CE Documentation)

- For CE that meets Specific Education Requirements (USQS 3.3)

<https://content.naic.org/sites/default/files/inline-files/Appointed%20Actuary%20CE%20Categories.docx>

1. Law and Regulation
2. Policy form/coverage/underwriting/marketing
3. Reinsurance
4. Reserves
5. Requirements & Practice Notes
6. Business Skills
7. Other



# Updates to the Recertification Process (CE Documentation)

- Several categories have sub-categories
- 2. Policy form/coverage/underwriting/marketing
  - Form/Coverage
  - Premium rates/Ratemaking
  - Underwriting and/or marketing
- 3. Reinsurance
  - Statutory accounting
  - Reinsurance collectability
  - Reinsurance collateral
  - Reinsurance reserving
- 4. Reserves
  - Reserving Data
  - Reserving Adjustments
  - Reserving Calculations
  - Reserving Analysis
  - Statutory accounting



# Updates to the Recertification Process (CE Documentation)

- Other CE that should be tracked
  1. Risk management
  2. Emerging Issues
  3. Accounting other than Statutory accounting
  4. Analytics
  5. Modeling
  6. Professionalism





# APPOINTED ACTUARY QUALIFICATION DOCUMENTATION

Miriam Fisk – Texas Department of Insurance





# Overview

- Brief recap of the qualification documentation requirements
  - For the Appointed Actuary
  - For the Board of Directors/company
- Regulator observations from the first year



# Appointed Actuary Requirements

- Provide at appointment and annually thereafter
- Provide to Board of Directors, directly or through company management
- Should include:
  - Brief biographical information
  - How the definition of “Qualified Actuary” is met or expected to be met for that year
- Should describe the Appointed Actuary’s responsible experience relevant to the subject of the Actuarial Opinion

Source: 2019 NAIC Instructions



# Definition of “Qualified Actuary”

## NAIC SAO Instructions:

“Qualified Actuary” is a person who:

- (i) Meets the **basic education, experience and continuing education** requirements of the Specific Qualification Standard for Statements of Actuarial Opinion, NAIC Property and Casualty Annual Statement, as set forth in the Qualification Standards for Actuaries Issuing Statements of Actuarial Opinion in the United States (U.S. Qualifications Standards), promulgated by the American Academy of Actuaries (Academy);
- (ii) Has obtained and maintains an **Accepted Actuarial Designation**; and
- (iii) Is a **member of a professional actuarial association** that requires adherence to the same Code of Professional Conduct promulgated by the Academy, requires adherence to the U.S. Qualification Standards, and participates in the Actuarial Board for Counseling and Discipline when its members are practicing in the U.S.

(emphasis added)



# Company/Board Requirements

- Review the qualification documentation
  - May request additional information from Appointed Actuary
- Document the company's review
- Provide the qualification documentation to regulators upon request or during a financial examination



# Regulator Review of Qualification Documentation

- Qualification documentation is provided to regulators “upon request”
- Timing/frequency of request may vary widely by state
- May commonly be requested by regulators:
  - When an Appointed Actuary is newly appointed by a company
  - During a financial examination
- Purpose of request may vary



# Observations from a Small Sample of 2020 Qualification Documentation

- All documents reviewed seemed to meet the basic requirements
- All provided clear information that addressed the basic education and Accepted Actuarial Designation requirements
- Level of detail regarding the experience and continuing education requirements varied widely
  - Most stated detail would be made available upon request



# Observation:

## Specific Qualification Standard – Experience Requirement

From the USQS, section 3.2:

“An actuary must obtain at least three years of responsible experience relevant to the subject of the Statement of Actuarial Opinion **under review by an actuary who was qualified to issue the Statement of Actuarial Opinion at the time the review took place** under standards in effect at that time. Although this experience need not necessarily be recent, it must be relevant to the subject of the Statement of Actuarial Opinion.” **(emphasis added)**

- Many of the documents reviewed did not explicitly state that any of the experience was under the review of a qualified actuary.



# Conclusion

- All documents reviewed seemed to meet the basic requirements
- Do these documents fulfill the intended purpose of the requirements?
- Further insight will come over time, especially as companies go through financial examinations





# Thank You

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