

**Using Your Professionalism GPS  
to Navigate the Actuarial World**

Ratemaking and Product Management  
Seminar  
March 16 & 17, 2010

Presenters: Susan Forray, Dustin Loeffler,  
Karen Terry

1

---

---

---

---

---

---

---

---

**Using Your Professionalism GPS  
to Navigate the Actuarial World**

Ratemaking and Product Management  
Seminar  
March 16 & 17, 2010

Presenters: Lynn Gehant, Jay Hieb, Sandra  
Ross

2

---

---

---

---

---

---

---

---

**Increased Scrutiny of Actuaries  
Since 2003**

- ▣ Standard and Poor's (2003)
  - ▣ "Insurance Actuaries: A Crisis of Credibility"
  - ▣ Blamed actuaries for reserve shortfalls in early 2000s
  - ▣ #1 Casualty Actuarial story for 2003 (CAS)
- ▣ Morris Review (UK, 2004-05)
  - ▣ Insolvency of Equitable Life (UK)
  - ▣ Led to oversight by Financial Reporting Council

3

---

---

---

---

---

---

---

---

## Increased Scrutiny of Actuaries Since 2003

- **AIG/Gen Re Sham Reinsurance (4/1/08)**
  - Convictions of actuaries Ron Ferguson and Chris Garand
  - Sentenced in spring 2009, appeals pending
- **NY Times article (5/21/08)**
  - “Actuaries Scrutinized on Pensions”
  - Issues with public pension funding in NY, AK, San Diego CA, Milwaukee County WI, and Evanston IL

4

---

---

---

---

---

---

---

---

## Actuarial Navigation

- Where do you turn when you are faced with an ethical “traffic jam” and need to navigate away from it?



5

---

---

---

---

---

---

---

---

## GPS Tools for the Actuary



- Code of Professional Conduct
- Actuarial Standards of Practice
  - Applicability Guidelines
- CAS Statement of Principles
  - Foundational Statements TBD
- Code of Ethics for Candidates

6

---

---

---

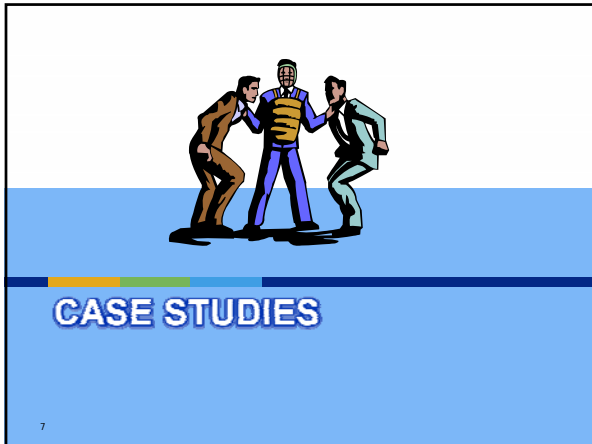
---

---

---

---

---



---

---

---

---

---

---

---

---

### CASE STUDIES OVERVIEW

- “Real life” predicaments
- Structure of session
  - Read the case together.
  - Seek ethical solutions from the audience
  - Discuss relevant Code and ASOPs
- Disclaimers:
  - Exercise is for education purposes only.
  - Opinions expressed do not represent the opinion of the respective employers or the Casualty Actuarial Society.
  - No authoritative guidance should be expected of the moderator or panelists.

8

---

---

---

---

---

---

---

---

### CASE STUDY #1 – “COASTAL RATES”

**As the chief actuary for your state’s insurance department**, you are reviewing a filing by a major personal lines insurer in the state. Due to a rash of recent catastrophes, the company is asking for a 200% increase along the coastline. After reviewing the data, you agree that the rate increase is justified.

**The Insurance Commissioner tells you** to disapprove the increase because it would result in rates that are not affordable. Your projections show that without the full 200% rate increase, the insurer may go bankrupt within two years. You have shared this information with the Commissioner, but she still refuses to agree to the large rate increase.

9

---

---

---

---

---

---

---

---

## Case #1 Course of Action

### What would you do?:

- a) Insist that the commissioner change her mind. If you cannot change her mind, then you have to document your recommendation and possibly let others know about your decision.
- b) Disapprove the filing per your instructions. After all, the insurance commissioner is ultimately responsible for regulating the industry both for rates and for solvency. You have done your job in notifying the commissioner of the implications of her decision.
- c) Contact the ABCD for guidance.
- d) None of the above.

---

---

---

---

---

---

---

---

## Professional Integrity

### PRECEPT I:

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.



11

---

---

---

---

---

---

---

---

## Principles of Ratemaking

### Principle 4:

A rate is reasonable and not excessive, inadequate, or unfairly discriminatory if it is an actuarially sound estimate of the expected value of all future costs associated with an individual risk transfer.

12

---

---

---

---

---

---

---

---

## Case Study#2 – “New Product”

You have been the VP of underwriting for the large accounts market for the last three years. The actuary supporting your market along with the marketing department have developed a new product with forms, rates and a 5-year proforma of the expected results of this new product on the market's financial statements. You have reviewed the work and you believe there are some flaws in the pricing and financial modeling. Instead of generating a profit in year 1, the new product will not generate a profit until year 5, if at all. What do you do?

13

---

---

---

---

---

---

---

---

---

---

## Case #2 Course of Action

### What Would You Do?

- a) Have a conversation with the actuary and discuss your concerns.
- b) Bring the entire work team together to reveal the faulty work and delay the roll-out of the new product indefinitely until problems are solved.
- c) Ignore the problem; you are not qualified to make an actuarial opinion.

14

---

---

---

---

---

---

---

---

---

---

## Standards of Practice

### PRECEPT 3:

An Actuary shall ensure that Actuarial Services performed by or under the direction of the Actuary satisfy applicable standards of practice.



15

---

---

---

---

---

---

---

---

---

---

## Ratemaking ASOPs

- #12 Risk Classification
- #13 Trending in P/C Ratemaking
- #29 Expense Provisions
- #30 Profit & Contingency Provision
- #39 Treatment of Catastrophe Losses in P/C Ratemaking

16

---

---

---

---

---

---

---

---

## Case Study#3 – “Draft Report”

A consulting actuary has delivered a draft report to its client/principal. During a subsequent discussion of the results, the actuary and the Controller talk about the potential surplus impact of a possible strategic course of action. After this conversation the consulting actuary does a thorough proforma analysis and provides a final report in which the results vary from the draft report discussions due to some changes in assumptions as provided by the CEO and CFO. The Controller has already implemented some of the originally discussed strategy and is now complaining to the CEO and CFO that the actuary misled him and has produced faulty work. What should the actuary do?

17

---

---

---

---

---

---

---

---

## Case #3 Course of Action

### What Would You Do?

- a) Meet with the CEO and CFO to discuss the misinterpretation of your work product and verify that your final work product fulfills the work contract.
- b) Meet with the Controller to discuss the changes and why your earlier conversation should not have been relied upon.
- c) Do nothing.
- d) None of the above.

18

---

---

---

---

---

---

---

---

## Control of Work Product

### PRECEPT 8:



An Actuary who performs Actuarial Services shall take reasonable steps to ensure that such services are not used to mislead other parties.

19

---

---

---

---

---

---

---

---

## Communications and Disclosure

### PRECEPT 5:

An Actuary who issues an Actuarial Communication shall, as appropriate, identify the Principal(s) for whom the Actuarial Communication is issued and describe the capacity in which the Actuary serves.

20

---

---

---

---

---

---

---

---

## Case Study #4 – “Rate Hearing”

**A recent rate filing** of yours went to hearing. During the hearing, the Department’s Actuary (FCAS) made several misrepresentations of the data and suggested several alternatives that are in conflict with the Statement of Principles on Ratemaking and with certain Actuarial Standards of Practice.

21

---

---

---

---

---

---

---

---

## Case Study #4 Course of Action

### What Would You Do?

- a) Let comments go. Actuaries are allowed to use judgment in their analysis and communications.
- b) Report to the ABCD.
- c) Talk to regulator.
- d) None of the above

22

---

---

---

---

---

---

---

---

## Violations of the Code of Professional Conduct

### PRECEPT 13:

An Actuary with knowledge of an apparent, unresolved, material violation of the Code by another Actuary should consider discussing the situation with the other Actuary and attempt to resolve the apparent violation. If such discussion is not attempted or is not successful, the Actuary shall disclose such violation to the appropriate counseling and discipline body of the profession, except where the disclosure would be contrary to Law or would divulge Confidential Information.

23

---

---

---

---

---

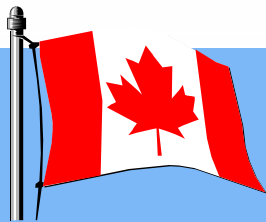
---

---

---

## Canadian Rules of Professional Conduct

- The Rules of Professional Conduct in Canada require that certain procedures must be followed when a member is aware of a violation of the Rules.
  - Affirmative responsibility to act to correct violation
  - No confidentiality agreement or employment protections exist



24

---

---

---

---

---

---

---

---



## Violations of the Code of Professional Conduct

### PRECEPT 14:

An Actuary shall respond promptly, truthfully, and fully to any request for information by, and cooperate fully with, an appropriate counseling and disciplinary body of the profession in connection with any disciplinary, counseling or other proceeding of such body relating to the Code. The Actuary's responsibility to respond shall be subject to applicable restrictions on Confidential Information and those imposed by Law.

25

---

---

---

---

---

---

---

---

## Case Study #5 – “Ratemaking Review”

A consulting actuary is hired by the regulator to review a company's rate filing. The consulting actuary believes the rate request is excessive and as a result intends to recommend disapproval. The company actuary disagrees with the approach taken by the consulting actuary and discussions between the two become heated. Eventually, the consulting actuary issues a statement to the regulator not only recommending disapproval but also alleging the company actuary's analysis violates the applicable ASOPs. The regulator requests a meeting with you, the company actuary and the consulting actuary.

26

---

---

---

---

---

---

---

---

## Case Study #5 Course of Action

### What Would You Do?

- a) Apprise your principal of the situation and recommend that you not attend the meeting since the consulting actuary is not being reasonable; realizing this will most likely result in a disapproval of the filing.
- b) Disclose the situation to your principal and recommend you meet with the regulator and the consultant to make another attempt to work out the differences.
- c) Refuse to meet and report the consulting actuary to the ABCD.
- d) Refer to the ABCD for guidance.

27

---

---

---

---

---

---

---

---

## Courtesy and Cooperation

### PRECEPT 10:

An Actuary shall perform Actuarial Services with courtesy and professional respect and shall cooperate with others in the Principal's interest.



28

---

---

---

---

---

---

---

---

## Case Study #6 – “Use Of Supplemental Data”

**You are the actuary** for a reinsurance company trying to set an excess reinsurance rate for a small domestic company that writes a specialty class commercial auto but does not have credible data. You also reinsure a larger company, which writes basically the same business in the same state, and who has supplied you with ample data that could be used to set the rates for the smaller company. Do you use the data, as a collateral source, to develop rates for the smaller company?

29

---

---

---

---

---

---

---

---

## Case Study #6 Course of Action

### What Would You Do?

- a) Use the data. No one will know and you can protect the confidentiality of the company and the data.
- b) Don't use the data. The data was supplied confidentially and should not be used for any other purpose.
- c) Seek permission from the large carrier to use the data as long as you keep it confidential.

30

---

---

---

---

---

---

---

---

## Confidentiality

### PRECEPT 9:

An Actuary shall not disclose to another party any Confidential Information unless authorized to do so by the Principal or required to do so by Law.



31

---

---

---

---

---

---

---

---

## Other Code of Conduct Precepts

- #2 – Qualification Standards
- #4 – Communications and Disclosure
- #6 – Communications and Disclosure (compensation disclosure)
- #7 – Conflict of Interest
- #11 – Advertising
- #12 – Titles and Designations

32

---

---

---

---

---

---

---

---

## ASOPs –

The Actuarial Standards of Practice (ASOPs) identify what the actuary should consider, document, and disclose when performing an actuarial assignment.

33

---

---

---

---

---

---

---

---

## Applicability Guidelines

- ▣ ASOPs that apply to all practice areas
  - ▣ Introduction to the ASOPs
  - ▣ 9 Documentation & Disclosure
  - ▣ 23 Data Quality
  - ▣ 41 Communications
- ▣ Reserving ASOPs
  - ▣ 20, 36, 43
- ▣ Ratemaking ASOPs
  - ▣ 13, 29, 30, 39
- ▣ Other Key ASOPs
  - ▣ 7, 12, 17, 19, 21, 25, 32, 38

34

---

---

---

---

---

---

---

---

---

---

## Common Allegations Received by ABCD

Alleged Violation	# Number Disposed or in Process (2005)	Number Disposed or in Process (2006)	Number Disposed or in Process (2007)	Precept
Failure to act with integrity	19	18	11	1
Calculation or data errors	7	2	2	1
Failure to perform services with competence	3	3	5	1
Other errors in work	3	3	2	1
Work fails to satisfy ASOP	3	3	7	3
Improper reserve estimate for insurer	3	0	1	3
Use of unreasonable assumptions	3	1	1	3
Failure to cooperate with other actuary	3	3	3	10
Inadequate actuarial communication	2	1	3	4

35

Source: ABCD 2005-07 Annual Reports

---

---

---

---

---

---

---

---

---

---

## Common Allegations Received by ABCD

Alleged Violation	Total Number Disposed or in Process			
	2005	2006	2007	2008
Conduct or Practice	46	34	35	37

36

Source: ABCD 2005-08 Annual Reports

---

---

---

---

---

---

---

---

---

---

Now It's Your Turn...

---

Any Situations Involving a  
"Friend of Yours"?

37

---

---

---

---

---

---

---

---