

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

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

Roles in the Reserving Process

- 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

- 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

- 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

- 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?

Key Assumptions

- 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

- 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

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

Asbestos, Environmental and Mass Tort Exposure

- 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?

General Data Concerns

- 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

- 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?

Risk Factors

- What are the company's primary risk factors?
- Could any of these specific factors cause material adverse deviation?

Legislative Changes

- Florida PIP
- 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

- 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?

Graphs and Charts

1 Year Development by Accident Year by Line of Business - Total US P/C Industry

<u>Acc Yr</u>	<u>WC</u>	<u>PPAL</u>	<u>CAL</u>	<u>CMP</u>	<u>OL-OCC</u>	<u>PL-OCC</u>	<u>FG/MG*</u>	<u>Subtotal</u>	All Lines <u>Total</u>
Prior	396,095	60,946	60,131	116,036	803,473	314,298	116,168	1,867,147	1,983,633
2007	96,230	-36,919	-4,189	-2,735	66,370	55,918		174,675	174,591
2008	82,476	-10,366	8,253	-11,924	15,219	22,213		105,871	132,246
2009	70,877	-50,577	-10,062	-9,348	101,062	39,810		141,762	184,951
2010	13,018	-68,424	6,540	15,262	146,339	10,925		123,660	165,164
2011	14,904	-27,636	7,322	8,104	81,659	21,841		106,194	-119,731
2012	2,143	95,161	104,811	105,284	206,440	3,444		517,283	598,630
2013	-25,968	145,757	308,025	151,377	341,228	-1,156		919,263	795,504
2014	-46,875	321,648	365,535	210,915	446,432	-12,644		1,285,011	1,492,630
2015	32,572	1,579,653	445,073	69,832	787,606	-21,253	205,657	3,099,140	3,120,184
Totals	635,472	2,009,243	1,291,439	652,803	2,995,828	433,396	321,825	8,340,006	8,527,802
% of All Lines	7.5%	23.6%	15.1%	7.7%	35.1%	5.1%	3.8%	97.8%	

Changes in Methods or Assumptions

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

Reliance on Principal for Alternate Assumption

- ASOP 43 – 3.6.2 – “When the principal is interested in the value of an unpaid claim estimate under a particular set of assumptions different from the actuary’s assumptions, the actuary may provide the principal with the results based on such assumptions, subject to appropriate disclosure.”

General Suggestions

- How have market conditions or rate changes influenced premium?
 - Do expected loss ratios need to be modified?
- Have you reviewed any large claims that have a significant impact?
 - Do they need separate mention in the actuarial report?
- Have there been any changes in the marketing, underwriting or claims departments in the past calendar year that would have a material impact on the loss reserve assumptions?

Thank You for Your Attention

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