

GI in a GFC World

General Insurance Impacts of the Global Financial Crisis



Institute of Actuaries of Australia

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THE WESTIN SYDNEY 1 MARTIN PLACE, SYDNEY

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**Some existing professional issues
which may be exacerbated by the GFC**

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Some existing professional issues which may be exacerbated by the GFC

- When is a central estimate arguably not really a mean – and what might actuaries and IAAust do about it?
- Importance of objectivity in reviewing draft estimates of insurance liabilities



When is a central estimate arguably not really a mean?

- Existing definition in PS 300 – “Central Estimate” is intended to be an unbiased estimate of the mean (statistical expectation) of the Outstanding Claim Liability or the Future Claim Liability
- Unchanged in proposed Exposure Draft of revisions to PS 300



When is a central estimate arguably not really a mean? (cont)

PS 300 definition is consistent with each of:

- accounting standard AASB 1023 (paragraph 5.1.4), and
- APRA GPS 310 (paragraph 18).



When is a central estimate arguably not really a mean? (cont)

- A matter of interpretation whether inclusion of the word “intended” in the PS 300 and GPS 310 definitions (but not in AASB 1023) provides any “wriggle room” for actuaries?
- But in some circumstances, arguably actuary’s “central estimates” can be no more than carefully and sensibly constructed **scenarios**, and should not be represented as means.



When is a central estimate arguably not really a mean? (cont)

Some common examples:

- GFC adjustments to estimates based on analysis of past experience (?);
- allowances for estimated effects of legislative change for accident compensation schemes and/or monoline insurers;
- start-up operations and/or a new line of business;
- dust disease liabilities;
- liabilities for other types of latent claim, particularly at early stage of manifestation,
- etc.

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What might actuaries do about it?

- Note my inevitable disclaimer that this presentation is not legal advice, etc!
- Disclose clearly the nature and limitations of the actuary's estimate



What might actuaries do about it? (cont)

- If preparing an ILVR in accordance with the GPS 310, bear in mind the requirements of paragraph 85 of GPS 310
“An Appointed Actuary must ensure that results are not presented in a way that gives the impression of greater reliability than is actually the case. This particularly applies in situations where materially different results could reasonably be justified.”
- Consider whether you're happy with the wording of PS 300.



What might IAAust do about it?

- Wording of PS 300:
 - requiring that a central estimate be a mean appears to be a desirable general objective, but
 - consider whether there might be a proviso that, if an actuary believes that it is not possible to estimate a mean soundly in particular circumstances, the actuary should be required to explain why and the nature and limitations of the estimate provided?
- Continue working with APRA and the accounting profession to try to ensure consistency of PS 300 with requirements of APRA and accounting standards.



Importance of objectivity in review of draft estimates of insurance liabilities

- Review of actuary's draft estimates by management:
 - a natural and routine part of the valuation process for most insurers and reinsurers, and
 - valuable for both actuary and management.
- However, potential for bias/manipulation does exist, eg selective raising only of issues which would imply lower estimates of liabilities whilst remaining silent about issues which would imply higher estimates.



Importance of objectivity in review of draft estimates of insurance liabilities (cont)

- Risk likely to be exacerbated by pressure on profitability, eg due to:
 - changes in competitive environment;
 - existing budgets (and possible linkage with remuneration);
 - analyst and/or rating agency expectations;
 - GFC, etc.



Importance of objectivity in review of draft estimates of insurance liabilities (cont)

- Actuaries need to consider and respond objectively to issues raised – a paranoid valuation actuary almost inevitably leads to a confrontational and problematic valuation process!
- But objectivity from management is also crucial
- Mutual trust between actuary and management is valuable, but difficult to restore once damaged



Importance of objectivity in review of draft estimates of insurance liabilities (cont)

- What's new about any of this?
 - nothing in principle, but
 - for Australian GI actuaries, involvement of actuaries in management and the process of reviewing draft estimates is much greater now than during the previous period of general pressure on profitability of insurers, and
 - hence greater responsibility of actuaries for maintaining objectivity