

GN12: GENERAL INSURANCE BUSINESS: ACTUARIAL REPORTS

Classification

Recommended Practice

Legislation or Authority

There is little United Kingdom legislation specifically relating to actuarial reporting on general insurance business, although such legislation exists in some other countries.

There are separate Guidance Notes for actuaries appointed in terms of Lloyd's Byelaws and for Appropriate Actuaries reporting on the technical provisions of a friendly society and those Guidance Notes make reference in turn to the need to produce reports in accordance with this Guidance Note. In addition the UK Supervisory Authority may request a formal report on the adequacy of an insurance company's technical provisions and this Guidance Note would apply to such a report.

Application

Any actuary preparing a formal report covering actuarial aspects of a general insurance undertaking which is not restricted to the investments of the undertaking, whether as an employee of that undertaking or as a consultant.

Author

General Insurance Board.

Status

Approved under Due Process.

<i>Version</i>	<i>Effective From</i>
1.0	01.08.87
1.1	01.09.90
2.0	01.07.91
3.0	01.09.99

1 Introduction

- 1.1 The purpose of this Guidance Note is to assist an actuary who makes a formal report covering actuarial aspects of a general insurance undertaking (not restricted to the investments of the undertaking) and does so in a professional capacity, whether as an employee of that undertaking or as a consultant.
- 1.2 In considering whether a report is formal, and therefore within the scope of this Guidance Note, the actuary should consider the uses to which the report may be put. In particular, if significant decisions are likely to be taken based on the content of the report without the further involvement of the actuary, or the report is likely to be used by people other than those who directly commissioned it, there is a greater need for the report to be self-contained and complete, and therefore subject to this Guidance Note. However work which is

incomplete, of an interim nature or intended only as a basis for further discussion, would not normally be considered formal for this purpose.

- 1.3 The actuary should state that the report has been prepared in accordance with this Guidance Note, if in fact this is the case. Where a formal report has been prepared which does not conform with this Guidance Note, the actuary should state the fact and indicate key areas where the report fails to conform.
- 1.4 In preparing a formal report, the actuary should have regard to any relevant technical guidance issued by the General Insurance Board in the form of an Advisory Note.

2 Definition of Terms

- 2.1 Some words and expressions commonly used in general insurance can be unclear, ambiguous or have different meanings in different jurisdictions. The actuary should consider whether some of the words and expressions used in the report may be open to misinterpretation and therefore need to be defined.

3 Purpose and Scope

- 3.1 The report should:
 - include a statement of its purpose and scope;
 - make plain whom the actuary is advising;
 - indicate the intended recipients;
 - point out that third parties reading the report may not have the background information necessary for a full understanding of the report;
 - address the key issues;
 - give sufficient information to allow another experienced actuary to form an opinion on the appropriateness of the actuary's key judgements and, together with the files, be sufficient to allow any other suitably experienced actuary to reproduce the results without access to the actuary.
- 3.2 The scope of a report on the technical provisions of an insurance entity would be assumed to cover, in the absence of any specific disclaimer to the contrary, outstanding claims provisions (both gross and net of reinsurance), adequacy of liabilities assessed on a funded basis, provisions for claims handling expenses (both direct and indirect), unearned premiums, provisions for unexpired risks, claims equalisation provisions and reinsurance bad debts.

4 Uncertainty

- 4.1 To the extent that it is feasible to do so, the actuary should indicate in the report the degree of uncertainty surrounding the estimates that he or she has made and sensitivities to changes in key assumptions. There is, however, no obligation to quantify the uncertainty or sensitivity if, in the actuary's judgement, this would not assist the recipient. Furthermore, notwithstanding such uncertainty it is acceptable for the actuary to give, or comment upon, point estimates.
- 4.2 If there are specific features of the business that present potential concerns or significantly increase the uncertainty of the recommendations, beyond that which an informed reader of the report would reasonably expect, then this fact should be clearly highlighted in the corresponding reservations, or limitation of scope, included in the report.

5 Documentation of Methodology and Assumptions

- 5.1 The report should outline and discuss the key assumptions made including those as to the legal and claims environment.
- 5.2 If the report includes illustrations based on assumptions that the actuary does not regard as appropriate, this should be made clear in the report.
- 5.3 Where the actuary has used a method that is standard and well understood by the recipient (such as the chain-ladder or link-ratio approach to claims provisioning or the generalised linear modelling approach to pricing), it is not necessary to do more than make a brief reference to the method and explain to which elements of the data the method has been applied.
- 5.4 Where an unusual or non-standard method has been used, a more detailed description of the method should be given. Subject to satisfying paragraph 3.1 above, this would not apply if the recipient might be presumed to have an understanding of the method.
- 5.5 In view of inherent uncertainty, it will often be appropriate for the actuary to use more than one method. The key assumptions implicit in each method should be stated in the report.
- 5.6 Where the results of different methods differ significantly, the actuary should comment on the likely reasons for the differences and explain the basis for the choice of results.
- 5.7 The report should include commentary on any material difference in the assumptions or conclusions in the present work from those in earlier reports of a similar kind on the same issue by the same actuary. In view of the subjective nature of much of the work, the actuary would not normally be expected to comment on the choice of methods or assumptions made by another actuary in an earlier report.

6 Information and Data used by the Actuary

- 6.1 The actuary may need to rely on or utilise the work of other professionals. If there is a risk of confusion as to the division of responsibilities between the actuary and other persons or organisations, the respective responsibilities should be made clear in the report.
- 6.2 The report should indicate the sources of the data that the actuary has used and make clear what he or she is taking responsibility for. Many of the sources available for use in general insurance, and consequently the data also, have some degree of imperfection. This does not prevent the use of data from such sources (with appropriate caveats in the report, if necessary), provided the actuary is satisfied that the results appear reasonable.
- 6.3 The actuary should draw attention to any material shortcomings in the available data including the effect on the appropriateness of the data of changes in underwriting, claim processing or reinsurance arrangements, changes in policy coverage and legal decisions affecting claims settlement. The actuary should make particular reference to circumstances in which the shortcomings have materially added to the uncertainty surrounding the estimates that he or she has made.

7 Additional Considerations Relating to Reports on Reserving

- 7.1 The actuary should ensure that amounts he or she recommends for inclusion as technical provisions in financial statements or returns to supervisory authorities are in accordance with the governing accounting principles. It may be advisable to outline in the report the main features of those principles.
- 7.2 The actuary should state the basis on which he or she has assessed the provisions or claims estimates (i.e., best estimate or some other basis). Where the actuary states that his or her estimate of outstanding claims is on a “best estimate” basis, this should mean that it represents the expected value of the distribution of possible outcomes of the unpaid liabilities. This definition is intended to clarify the concept. It will generally be impossible to apply it directly in practice.

7.3 The actuary should indicate in the report, where appropriate, how the following issues have been dealt with:

- the grouping of the data by class of business, category of risk and currency;
- the nature and spread of the reinsurance arrangements, with particular reference to any significant changes therein and the treatment of any financial reinsurance;
- potential exhaustion of the reinsurance coverage and the possibility of non-performance of reinsurance;
- future claims handling expenses, both direct and indirect;
- the treatment of any abnormal types of claim;
- the treatment of future premiums in and out (including reinstatement premiums), profit commission and portfolio transfers
- the basis used for discounting.

7.4 The actuary should take care to distinguish between a range of amounts that might be reasonable for the provisions and the typically much larger range of amounts that might in due course be paid. If there is a substantial possibility that the future outgo will differ so much from the recommended provisions that the reported profit or balance sheet strength could, as a result of this fact alone, turn out to be materially incorrect, the actuary should draw attention to this in the report.