Institute and Faculty of Actuaries

Towards Optimal Reserving Process

Solvency II Technical Provisions
Sharing the Pain

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Introduction

- TORP working party background
- Main survey conclusions considered by TP adjustment
- Discussion points (very interactive)
- Summary

TORP Working Party

- The Towards Optimal Reserving Party aims to develop practical thoughts around the design and operation of the reserving process to share current practices and issues.
- This is to promote and spread the expertise gained from those further along the process, to those not as far advanced
- Previous projects include Actual v Expected techniques in 2013, Fast close options and Reporting in 2014 and last year we focused on the Materiality limits and thresholds and Reinsurance options through the fast close
- The party looks to tackle a series of common problems that firms face, in order to move towards a robust and risk focused reserving process given the reserving and reporting pressures we all face
- Always open to suggestions for future papers

Headlines

Still a wide range of methods in market for producing TPs

Lloyd's and London Market more consistent

Mostly TPs made up of bolt on calculations from core reserving

Different assumptions updated at different times

Various Risk Margin methodologies used

Background for survey

Overall we had 124 responses, with about half completing the survey in full..

Good spread with 28% London market (two thirds of which were Lloyd's Syndicates)

Just under 40% GI Non-London Market

Review Process

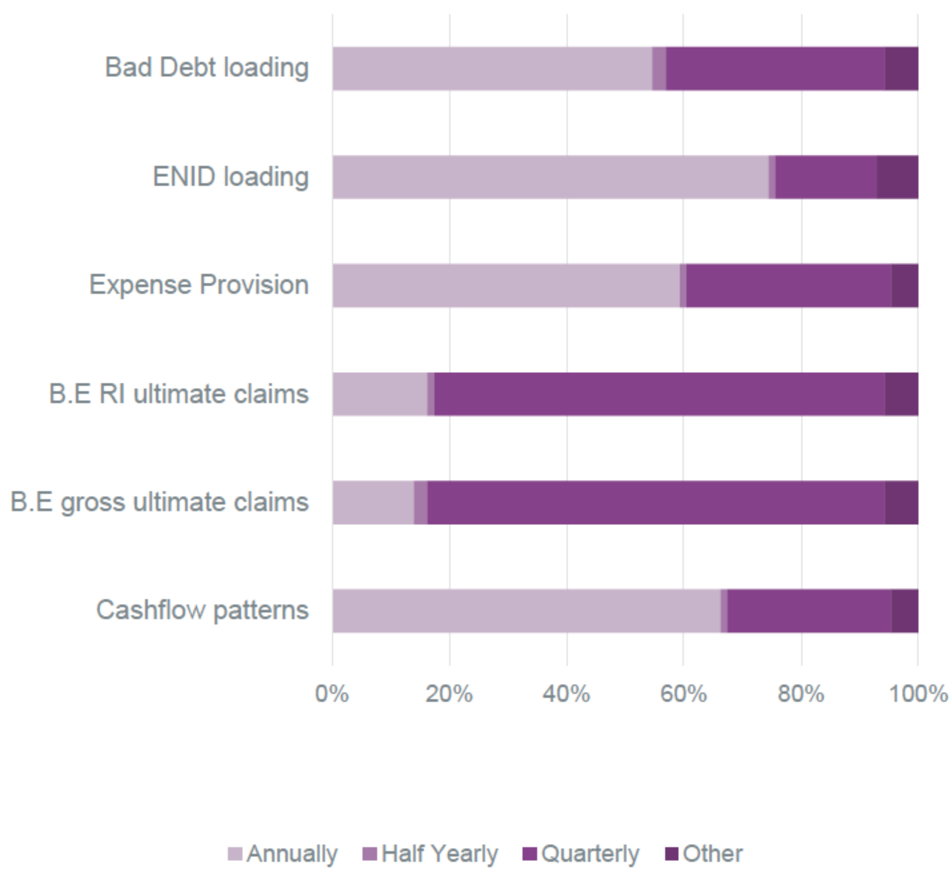
Survey showed…

- Varied (8% of firms use most common)
- Actuarial junior, review, finance, board
- Still heavily driven by actuarial

This may raise questions…

- Process appears robust however is it practical?
- Effect of shortening timetables with Pillar 3
- Consistency needs maintained between bases

Frequency of updates



Gross Ultimate Claims mainly updated quarterly. Similar proportion with Nets

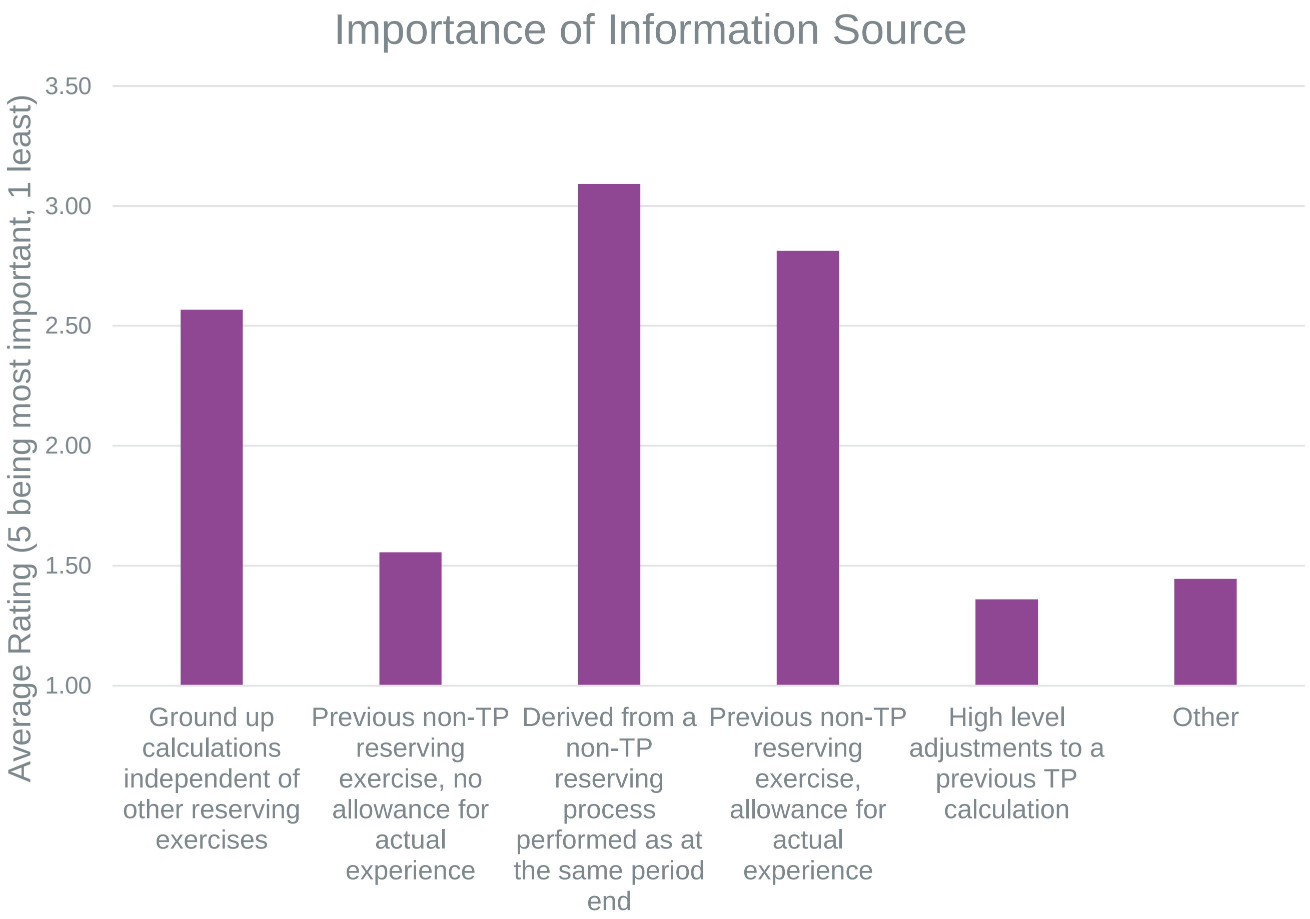
Volatile and material assumptions updated more regularly

Larger firms tended to update more regularly

Note: Order of ranking reversed from questionnaire

Calculation basis - Overall

- Over half of participants either use a non-TP calculation to derive their TP calculation, or use last quarters TP calculation with a roll forward process.
- Firms are still heavily reliant upon GAAP/IFRS, implying less confidence in SII process from first principles.



Note: Order of ranking reversed from questionnaire

Calculation basis – Premium Provisions

Methodology for Premium Provisions (rank priority 5 = most important)	5	4	3	2	1	Average response
Ground up calculations by policy	23%	7%	12%	5%	53%	2.42
Applying constant patterns to underwriting year ultimates	23%	17%	8%	1%	51%	2.60
Applying constant patterns to accident year ultimates	27%	27%	7%	4%	36%	3.08
Applying seasonal/specific patterns based on the premium writing pattern and the quarter being reported	23%	20%	12%	5%	40%	2.81
Other	8%	15%	15%	23%	38%	2.29

The majority of Standard Formula firms with no IM use accident year patterns, consistent with non-Lloyd's entities not considering results on an underwriting year basis. This is similar for Standard Formula firms that do have an IM available.

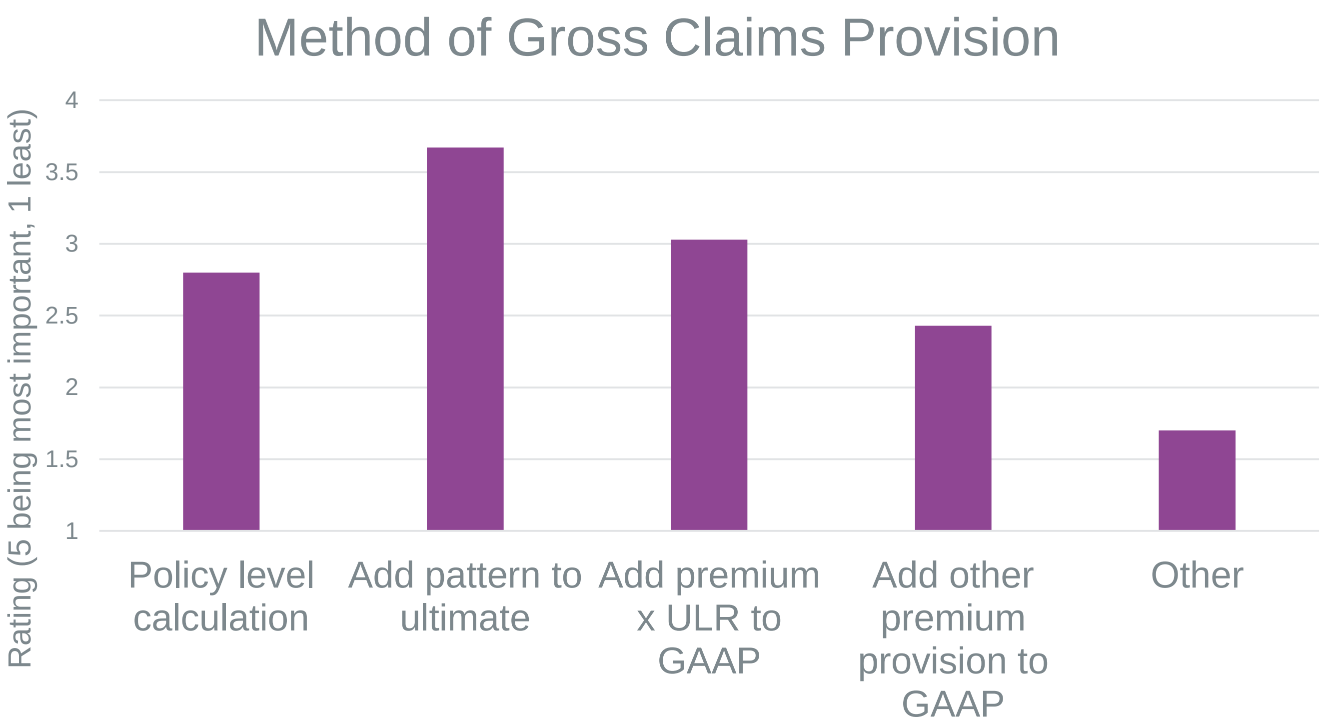
Most common methodology used was applying constant patterns to accident or underwriting year ultimate claims.

Just under half of respondents use ground up calculation by policy with 23% ranking it number 1. Of these over 80% have UK plus EU/US operations.

76% of respondents use more than one method to calculate premium provisions.

Note: Order of ranking reversed from questionnaire

Calculation basis – Gross Claims Provision



Of 68 respondents, 22 (31%) use one method (including 13 firms using an approved IM).

Of the 46 that use two or more methods (23 use 2, 8 use 3, 11 use 4 and 4 used all five methods, including ‘Other’).

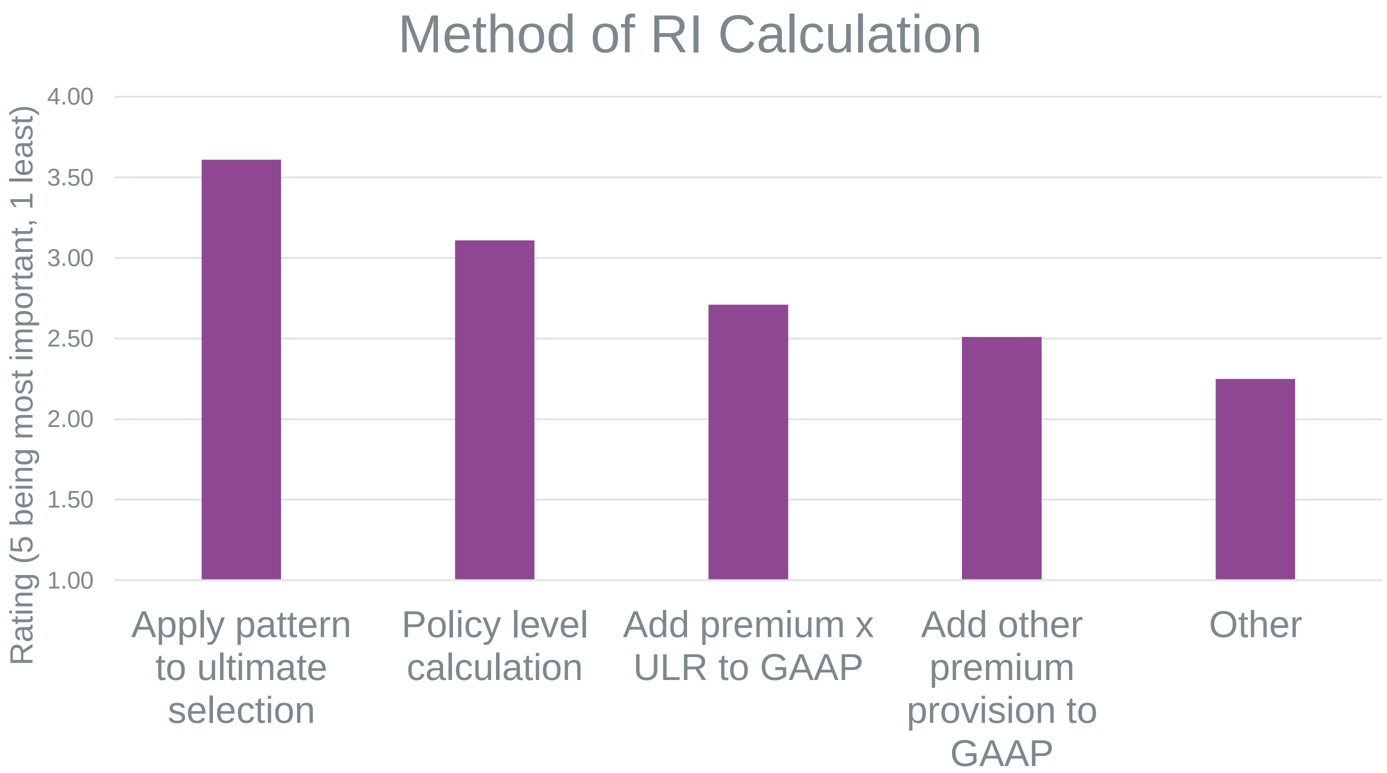
In terms of dealing with PPO liabilities, 44% (17 of 39) used the same method as for non-PPOs. PPO liabilities should be considered based on their materiality

The most popular type of method is to apply patterns (58 or 85%).

Note: Order of ranking reversed from questionnaire

Calculation basis – Reinsurance

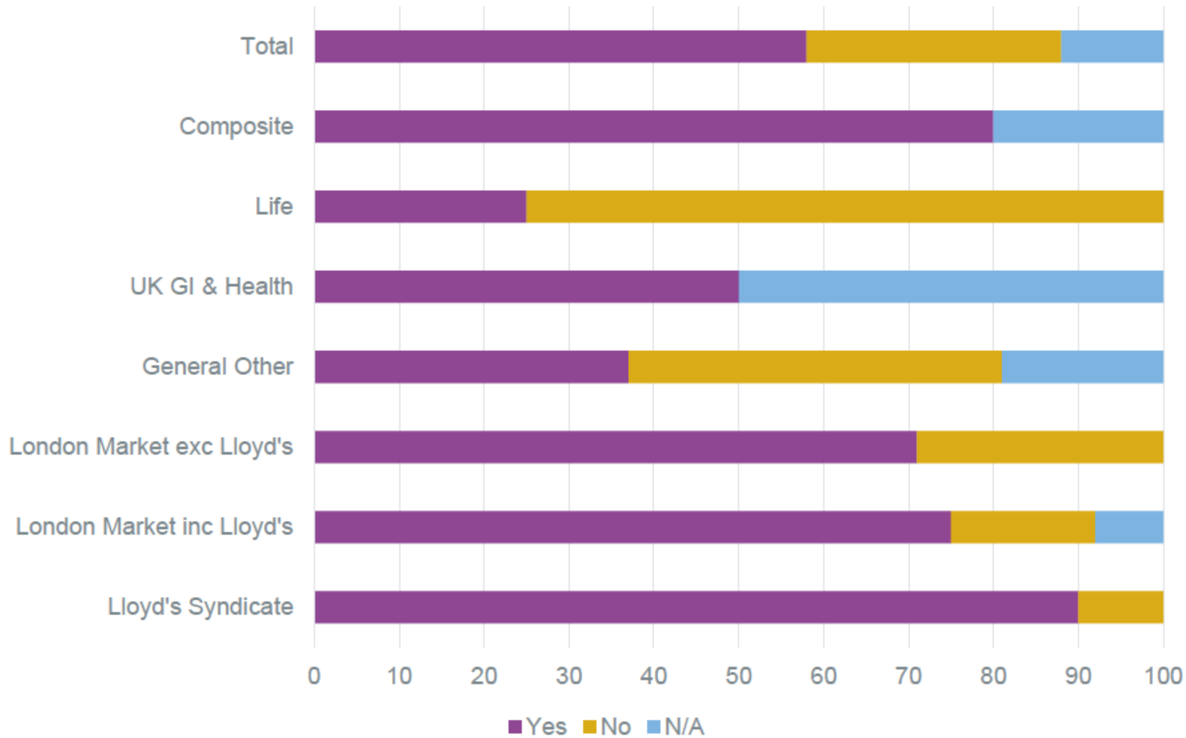
Of the 67 respondents, the most popular method allows for correspondence – ranked 5 or 4 by 96%



Note: Order of ranking reversed from questionnaire

Calculation basis – Reinsurance BBNI

The question was asked if an allowance was made to the RI BBNI if there were contract boundary differences between the RI contracts and the gross contracts



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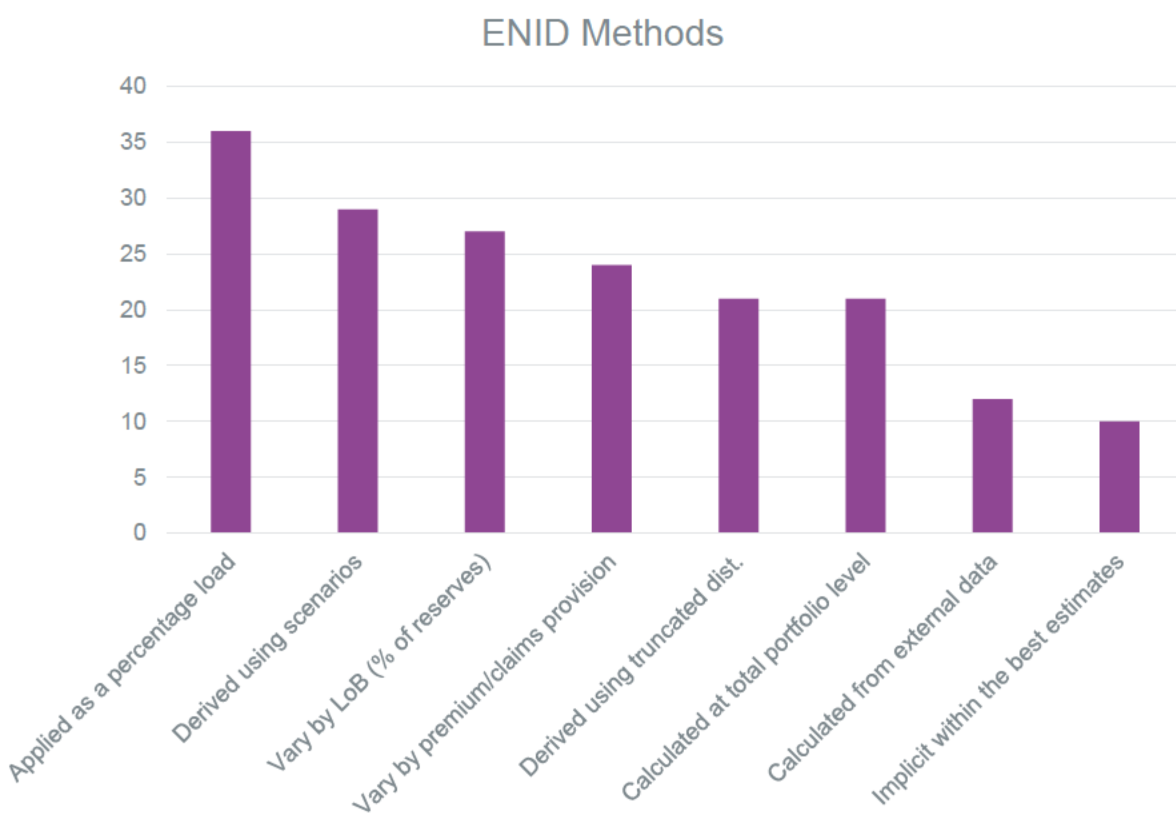


67 respondents to question, with scenarios still most prevalent method. Within Lloyd's Syndicates/ London Market, use of truncated distribution was most common

Most that vary the load by class also vary it by premiums and claims provisions.

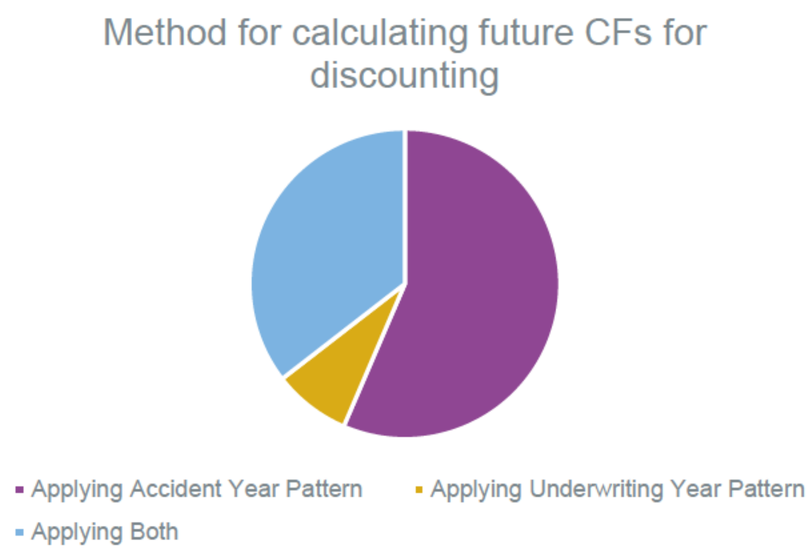
It is evident from responses that many have used multiple calculation approaches

Discounting

Vast majority of Lloyd's respondents use underwriting year patterns…

Outside Lloyd's accident year patterns are most common…

60% of those who have PPOs do discounting the same for PPOs as for other business – this is true for nearly all Lloyd's and London Market firms with other firms taking a more mixed response



Risk Margin Analysis

60 respondents – perhaps reflective of more complicated question

L2 models are most popular (82%), with L3 second (57%) and L1 least used (40%).

Life companies seem to be most likely to use L1 (small sample), with London Market least likely. Firms with a Life element are also most likely to only calculate RM annually.

Most companies update their RM more often than annually (68%), with large companies, and those using L1 only, more likely to have annual updates.

Standard Formula firms are more likely to do annual updates only, and also to rely on L2 and L3 rather than L1.

L3 were more likely to be applied more frequently than annually, with L1 less likely, as is expected.

Discussion Points

- Are there any odd results as presented?
- Will your current method be able to cope with reduced timeframes? What is the extent of roll-forward/fast close processes?
- What do you think the most natural conversion process is? GAAP + UPR + BBNI, UY split etc? Does this depend on the current main reserving basis?
- What diagnostics do you find helpful in reviewing the TP output?
- Do the frequency of updates seem reasonable?
- What do you think would be the best amendments to the TPs i.r.o Brexit?
- Would you like to see this exercise repeated/modified?

WP members

- Alastair Lauder
- Amy Williams
- Cameron Heath
- Fergal Dolan
- Keith Taylor
- Laura Hobern
- Neil Bruce (Chair)
- Katherine Norris
- Wan Heah

- We are looking for a new Chair!

Questions

Comments

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