



P&C PERSPECTIVES

Current Issues in Property and Casualty

The actuary and the board of directors

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The financial crisis will certainly increase the continuing discussion regarding corporate governance as well as the fiduciary responsibility of boards of directors in providing oversight. One measure already in effect requires the board of directors to appoint a qualified actuary to issue a statement of actuarial opinion each year regarding the unpaid claim liabilities of an insurance company. This is a responsibility that should not be taken lightly nor delegated without question.

The actuary is appointed directly by the board of directors for the purpose of issuing a statutory statement of actuarial opinion on the company's unpaid claim liabilities. It is the company management's responsibility to book its best estimate of the unpaid claim liabilities. It is then the actuary's responsibility to opine on whether management's booked reserve is a reasonable provision for the company's unpaid claim liabilities. Given this role, it is normally company management that works directly with the actuary. As such, management usually hires the actuary, but it should be understood that it is ultimately the board of directors that appoints the actuary to issue the reserve opinion.

The purpose of requiring the actuary to be appointed by the board of directors is to eliminate any pressure, real or perceived, by management to influence an actuary's opinion. This is meant to help ensure that the board and insurance regulator are getting an independent and objective opinion from the actuary.

When a company intends to change the opining actuary from the year before, it is required by regulation to send a letter to the domiciliary insurance regulator, notifying the regulator of the change and noting whether there have been any disagreements with the prior actuary in regard to the "content of the opinion on matters of the risk of material adverse deviation, required disclosures, scope, procedure, or data quality." The outgoing actuary is required to

review this letter and to write a response letter either agreeing or disagreeing with the company's assertions. There are various reasons why a company may want to change its appointed actuary, but the regulator wants to make sure a company is not changing its actuary because it wants a different opinion or a desired result. This assurance is also in the interest of the board of directors if company management is initiating the change. The board could contact the prior actuary and discuss the change privately. In most instances, there will not be much to discuss, but it allows the actuary the opportunity to express any concerns.

The actuary is required by statute to provide a report to the board of directors documenting and supporting the statement of actuarial opinion. This can be a written report alone or accompanied by an oral report. An oral report may be preferable because it provides an opportunity for the board to ask questions and discuss both broader topics and detailed factors that may influence the opinion. The actuary can inform the board of the major risks or concerns that affect the inherent uncertainty in the estimates. If desired, the actuary can offer other information that may be useful to the board, such as comparisons to industry performance benchmarks or discussion of current affairs that might impact future claims experience. If only a written report is provided, the board's responsibility to review and understand the main conclusions of the report should not be taken lightly. A board member should follow up with the actuary with any questions or concerns.

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In my view, it is good practice for a board to have some direct contact with the actuary outside of the presence of management. In most instances, actuaries and management teams work well together and can resolve differences professionally. However, should a disagreement arise, the direct contact would provide the board an opportunity to hear independently from both parties and provide direction from an informed position.

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Should a company choose to change actuaries, it is often a good practice to ask the new actuary to provide an analysis without relying on the previous actuary's work. This gives the company an opportunity to see an independent, alternative view. It is good practice for the new actuary to review the work of the prior actuary and attempt to reconcile any significant differences, but this could be after an initial independent analysis. If the management believes the prior actuary's estimates are too high or too low, it should not inform the new actuary. It should simply ask the actuary to provide his or her unbiased estimate. An independent analysis will be the most appropriate way to evaluate the management's assessment.

In summary, when it comes to the annual statutory statement of actuarial opinion, it is the responsibility of the board of directors to appoint the actuary and review the actuary's work. In this capacity, the actuary works for the board, not company management. Increasing contact and developing a more direct relationship with the appointed actuary should prove to be a prudent and beneficial experience for the board and the actuary.

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Because the articles and commentary prepared by the professionals of our firm are often general in nature, we recommend that our readers seek the counsel of their attorney and actuary before taking action.

Deadlines and responsibilities

The board of directors must appoint a qualified actuary before Dec. 31 of the calendar year for which the opinion is rendered.

If a company changes actuary, it must provide a letter explaining whether there have been any disputes with the prior actuary regarding the opinion. The company needs to have the prior actuary review this letter and provide a response letter agreeing or disagreeing with the company's letter.

In general, the actuarial opinion must be filed with the statutory annual statement by March 1.

In most states, a company is also required to provide a confidential actuarial opinion summary that compares the actuary's unpaid claim liability estimate to the company's booked reserves. If required, it must be submitted by March 15. Due to the confidential nature of this document, it should be filed separately from the actuarial opinion, which is a public document.

The actuary is required by statute to provide a report to the board of directors documenting and supporting the statement of actuarial opinion. This report can be delivered orally or in writing. The minutes of the board of directors should indicate that the actuarial opinion and actuarial report were made available to the board.

A final written report must be maintained at the company and available to the regulator by request by May 1 or within two weeks of request. This report must be kept by the company for at least seven years.

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