Why Your Actuary Really Matters

Brian Johnson, ACAS, MAAA, ARM
President, Risk International Actuarial Consulting

Robert Walling, FCAS, MAAA, CERA
Principal, Pinnacle Actuarial Resources
1) Introductions
2) Why you need an actuary
3) What actuaries are trying to prevent
4) Why an actuary really matters
Standard (and vitally important) actuarial services for captive insurance companies:

- Captive Feasibility Studies
- Actuarial Assistance/Support in Approval & Licensing
- Annual Reserve Reviews & Statements of Actuarial Opinion
- Annual Renewal Premium Pricing
- Assistance with Audits and Financial Condition Examinations
- Assistance with Financial Reporting (i.e. ASU 2015-09)
Captive Funding & Feasibility Studies

- Loss Projections
  - Experience and/or Exposure-based
  - Expected and Adverse Scenarios
  - Pricing of Reinsurance/Fronting Premiums
- Build-up of Recommended Premiums
  - Risk Load (Profit & Contingencies)
  - Captive Service Provider Expenses
  - Taxes and Regulatory Fees
- Recommendation of Initial Capital and Surplus
  - Based on Limits & Adverse Scenarios
Annual Renewal Premium Pricing

- Based on Loss History and Experience
- Accounts for Changes in:
  - Experience
  - Operations
  - Exposures
  - Limits
- New Coverages
- Reinsurance Pricing
Regulatory, Reserving and Audit Services

- Actuarial Assistance During Application, Licensing & Business Plan Changes
- Annual Reserve Review & Statement of Actuarial Opinion
  - Required in Most Domiciles
  - Key Component of Solvency Objective of Regulators
- Assistance with Audits and Financial Examinations
- Assistance with Financial Reporting
  - ASU 2015-09 – Optional
  - Ad hoc Reporting to Regulators & Auditors
What Could Possibly Go Wrong?

- Premium Projections
  - Too Low
    - Solvency Concerns/Need to Recapitalize
    - Examples - Trucking, Livery, Nursing Homes
    - Keep Insureds and Reinsurers
  - Common Causes
    - Data Errors (Omitted Large Loss(es))
    - Poor Benchmarks
    - New or Difficult Coverage, Growth/Expansion
    - Unexpected Changes in Trends (Trucking)
What Could Possibly Go Wrong?

- Premium Projections
  - Too High
    - Scrutiny for “Grossly Excessive Rates”
    - “Wild Ass” Guesses
  - Scrutiny of Model Manipulation
  - Not Market Comparable or Consistent to Traditional
  - Other Reasonableness Tests (e.g. Rate on Line)
  - Review by Credentialed Actuary at NAIC-accredited domicile doesn’t always help
What Could Possibly Go Wrong?

• Reserve Projections
  • Too Low
    • Solvency Concerns/Need to Recapitalize
    • Examples - Trucking, Livery, Nursing Homes
    • Regulatory, Audit, Front/Reinsurance Issues

• Common Causes
  • Claims Handling – Issues and Changes
  • Poor Benchmarks
  • New or Difficult Coverage, Growth/Expansion
  • Unexpected Changes in Trends (Trucking)
What Could Possibly Go Wrong?

- Reserve Projections
  - Too High
    - Less Frequent in Captives (Mainly 831(a) issue)
    - Scrutiny for Deferral of Income Taxes
    - Questions of Risk Margins, High End of Actuary’s Range, etc.
  - Example - Acuity
What Could Possibly Go Wrong?

- Regulatory Issues
  - Adverse Reserve Development
  - Reserves – Management’s Estimate vs. Actuary’s Central
  - Rate Changes – Inadequate?, Excessive?
- Capitalization
- Adverse Scenarios
- Collateral, Audit and Reinsurance Issues
  - Disagreement on Adequate Reserves
  - 2 Actuaries, 3 Answers (Levels of Conservatism)
Enterprise Risk Management (ERM)

- Notice Our Extra Letters? (ARM, CERA)
- ERM - the process by which “an organization in any industry assesses, controls, exploits, finances and monitors risks from all sources (emphasis added) for the purpose of increasing the organization’s short- and long-term value to its stakeholders.”
- Actuaries are uniquely qualified to contribute to ERM
- New coverages, coordination of structures/layers, captives as profit centers, incentives for locations
Innovation?

• Captive Actuaries See Lots of “Interesting” Coverages
  • Warranties (Sports Fields, Emergency Generators)
  • Cannabis (Crop, Product Liability, with Crypto Currency)
  • Crop (Swine Influenza, Potato Nematodes)
  • Renewable Energy
  • Credit Enhancement Coverages
  • Conservation Trusts
  • Crop Dusting Airplanes (Organic Overspray)
  • Tenant Liability Insurance
  • Tech Start-Ups – Uber, Lemonade, Task Rabbit
Risk Transfer and Risk Distribution

• Risk Transfer Assessment
  • Is there a significant chance of a material loss to the captive?
  • Expected Reinsurance Deficit (ERD)

• Risk Distribution Analysis
  • Unrelated Risk, including Pools
    • Lots of Details to Assess
  • Brother-Sister
  • Group Captive
  • Sufficient # of Statistically Independent Risk Units
Predictive Analytics

• The World Runs on Data Driven Decisions
  • Claims Models – Fraud, Explosive Claims
  • Vendor Evaluation – Medcor, SIUs, TPAs
  • Member or Insured Evaluations
  • Benchmarking – CRICO, Group Captives
  • Safety Devices – Telematics, Wearables, etc.
  • Improved Risk Selection
  • Lives (Not) Impacted by Safety and Loss Control
Your Actuary Can/Should Be Like a Smart Phone

Those products now fit in your pocket with a $200 iPhone