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Case Study 9 - Way Forward For Appointed Actuary Amid Dissenting Expectations

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Content



- Case Study - Background
- Issues and Considerations
- Course of Action
- Conclusions / Decisions

Background



- A new Appointed Actuary joins a GI Company
- During interview, CEO mentioned following to AA:
 - Combined Loss Ratio is one of the main factor in deciding management bonus.
 - Improvement of Combined Loss Ratio would be one of the main KPIs for AA.
 - Actuary has been recognized as best placed to understand Combined Loss ratio and to communicate its importance to other stakeholders and guide them to minimize it.
 - AA's job would also be to convince various channels on minimizing loss making business and put some tight underwriting controls.

Background



- Also, CEO mentioned following to set expectations from AA:
 - AA should be realistic with estimating reserves as this is a critical component for management bonus.
 - AA was hired because he/she was found flexible and business friendly unlike his/her predecessor.
- Post joining, CEO introduced AA to the team as “practical and competent Actuary” .
- AA gets mixed versions of circumstances under which his predecessor left
 - HR describes the exit to be as planned
 - Team members describe the exit as abrupt
- AA could not contact the predecessor



Background

Ask: What course of action shall AA adopt now?
Discuss it in detail providing context to the relevant professional and regulatory requirements.



Issues and Considerations



Expectations

- Clarity on expectations of CEO and management from AA
- Are the expectations reasonable or not?
- Interaction with HR

Potential Conflict

- Compliance with professional standards and regulatory requirements
- Are professional ethics at stake?

Business Performance

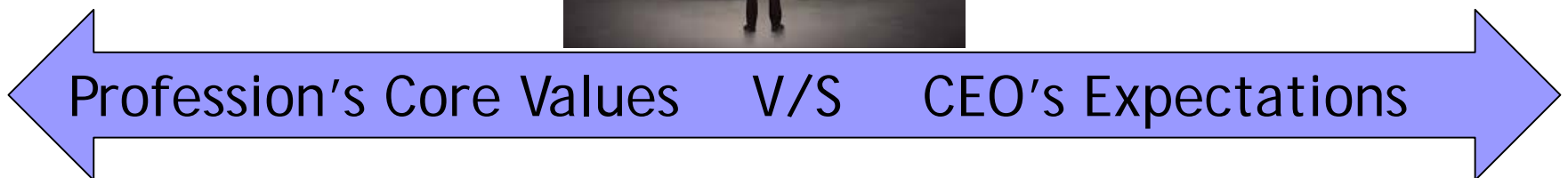
- Suitability of combined ratio as measure to determine management bonus?
- Are there any alternative metrics that can be used?
- Actions that AA can take to help minimize the combined ratio?

Stakeholder Management

- Understanding of AA's role and responsibilities among other departments
- Contribute in impressing upon various channels to minimize loss making business via tight underwriting and claims controls

If you have integrity, nothing else matters. If you don't have integrity, nothing else matters." -- Alan K. Simpson

Professional Attributes at Risk?



Course of Action



Course of Action



Professional Requirements

Professional Conduct Standards

- Provides generic guidance on professional conduct
- To be followed by all members

Actuarial Practice Standard

- Mandatory for all members
- APS 21 - Applicable to an Appointed Actuary of GI Company
- APS 33 - Peer Review of AA work

Guidance Note

- Related to a specific Actuarial Work Area
- GN 31 - specific to Financial Condition Report of GI Company

Regulatory Compliance

- AA Regulations 2017
- Corporate Governance Guidelines, 2016
- IBNR circular 2005

Course of Action



PCS

Professional Standards

- *“A member has a duty to the profession and must not act in a manner, which denigrates its reputation or impugns its integrity. Responsibility to any client must be consistent with that duty” - PCS, section 2.2*

Standards for Advice

- *“An actuary may provide advice if the circumstances are such that, having regard to all the relevant factors, it would be contrary to the client’s interests to decline to do so. However, the actuary must make clear to the recipient that, in the absence of the constraining circumstances, the actuary would have recommended referring the matter to someone with the relevant knowledge and experience - PCS, section 3.3*

Breach of Professional Guidance

- *“A material breach of the PCS or of a Guidance Note classified as Practice Standard or of the Act and Rules and Regulations made there under or Other Guidance, is of itself a ground for complaint under the disciplinary procedures and would amount to strong prima facie evidence of misconduct.”- PCS, section 4.1*

Course of Action



APS 21 & APS 33

APS 21

- *“An Appointed Actuary should ensure, so far as is within his / her authority, that the general insurance business of the company is conducted on sound financial lines and monitor any action / practice, which in his / her opinion, is unfair and likely to be prejudicial to the interests of the policyholders”*
- *“The AA must ensure that his / her conduct and reach and depth of his/ her functionalities enable him / her to discharge his / her duties and obligations in letter and script in accordance with regulation (9) of AA Regulations”*
- *“Any Appointed Actuary, who is uncertain as to the proper course of action to adopt in relation to a potentially significant matter, is strongly advised to seek the help and the advice from the IAI.”*
- *“The AA should have access to all relevant information, books and records so that the full range of his duties and obligations can be carried out satisfactorily.”*

Course of Action



APS 21 & APS 33

APS 33

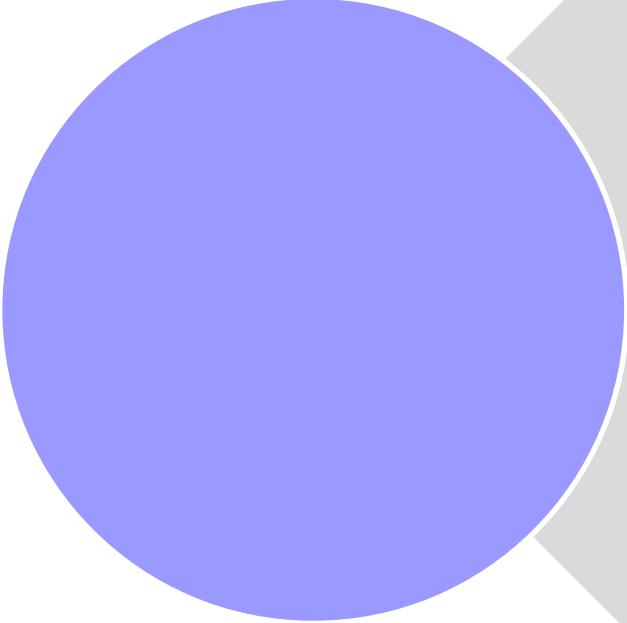
- APS 33 sets out Peer Review to become a standard element of all annual statutory actuarial valuations done by AA.
- APS 33 considers and provides guidance for
 - Scope of peer review
 - Choice of Peer Reviewer
 - Choice of Peer Reviewer
 - Communication
 - Resolution of peer review issues

Course of Action



Regulatory Compliance

Insurance Regulatory and Development Authority of India (Appointed Actuary) Regulations, 2017 - sets out the duties and obligations of AA. Key duties are :



9(vi)- Drawing the attention of management of the insurer, to any matter on which he or she thinks that action is required to be taken by the insurer to avoid-

- (a) Any contravention of the Act
- (b) Prejudice to the interests of policyholders

Course of Action



Regulatory Compliance

Insurance Regulatory and Development Authority of India (Appointed Actuary) Regulations, 2017 - sets out the duties and obligations of AA. Key duties are :

9(xiii) (a) - Ensuring that the premium rates of the insurance products are fair

9(xiii) (b) - Ensuring that the actuarial principles have been used in the determination of liabilities such as IBNR/IBNER/PDR

9(xiii) (e) - Ensuring the appropriateness of the methodologies and underlying models used, as well as the assumptions made in the calculation of IBNR and other reserves (including IBNER and PDR)

Course of Action



Regulatory Compliance

Insurance Regulatory and Development Authority of India (Appointed Actuary) Regulations, 2017 - sets out the duties and obligations of AA. Key duties are :

9(xiv)- informing the Authority in writing of his or her opinion, within a reasonable time, whether,

- a) the insurer has contravened the Act or any other Acts
- b) the contravention is of such a nature that it may affect significantly the interests of the owners or beneficiaries of policies issued by the insurer

Course of Action



Regulatory Compliance

Guidelines for corporate governance for insurers in India, 2016

Section 12 - Whistle-blower Policy

Insurers are advised to have a whistle blower policy in place for employees. The following section highlights AA's duty regarding 'whistle blowing':

12.2 'The appointed actuary and the statutory/internal auditors have the duty to 'whistle blow', i.e., to report in a timely manner to the IRDAI if they are aware that the insurance company has failed to take appropriate steps to rectify a matter which has a material adverse effect on its financial condition. This would enable the IRDAI to take prompt action before policyholders' interests are undermined.'

Guidelines on estimation of IBNR Claims provision under General Insurance Business, 2005

6.2 'The ultimate incurred claims ratios for the successive years should be credible as compared to ratios of other insurers in the market and for the same insurer over time. There should be logical explanations for any variations or sharp fluctuations.'

Course of Action



CEO and HR

CEO

Direct conversation with regards to clarity around CEO's expectations
Seek examples from CEO's previous experience
Make CEO aware about potential breach of regulatory and professional compliance
Mention to him about qualified report in case minimum requirements aren't met

HR

True reasons behind leaving of predecessor
Other means to contact predecessor

Course of Action

Combined Ratio & Alternatives

Limitations to Combined Ratio

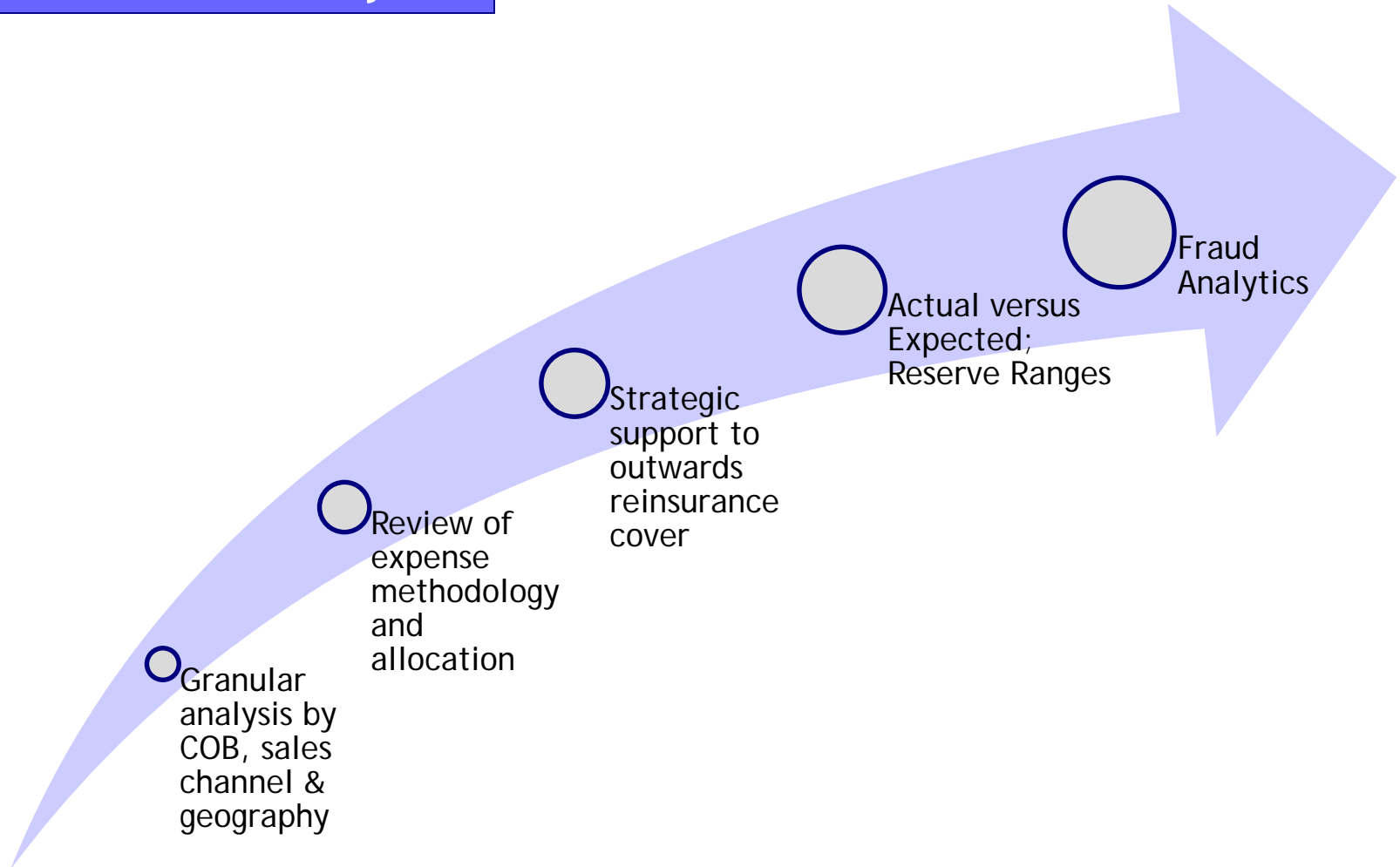
- Doesn't consider return to shareholder capital
- Ignores long term profit generation
- Ignores investment income
- Impacted by one time expenses, loss leaders, compulsory products, etc.

Alternatives

- Risk-adjusted return on capital (RAROC)
- Economic income created (EIC) = the quantity of return generated by a unit of activity
- Shareholder Value (SV) = the present value of all future cashflows
- Separate internal accounts to evaluate bonus

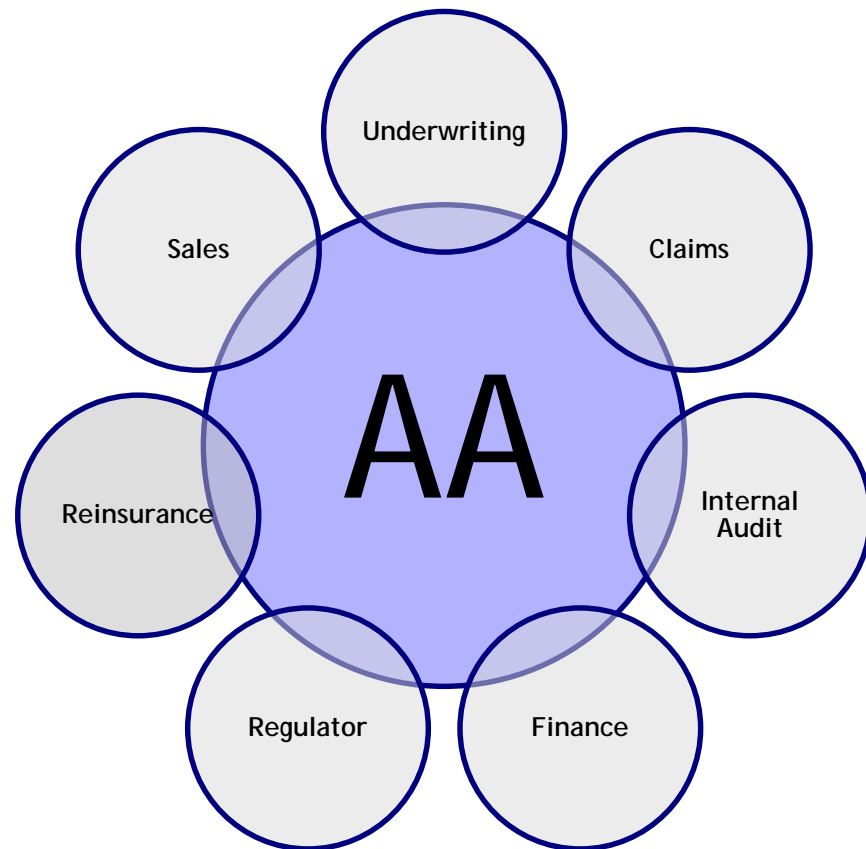
Course of Action

Advanced Actuarial Analytics



Course of Action

Engagement with Stakeholders



Regular engagement to ensure and communicate:

1. Reasonability and sensitivity of assumptions used in actuarial analysis
2. Underwriting Strategy
3. Claims controls mechanism
4. Enhanced risk management systems
5. Regulatory compliance
6. Training of sales and other staff

Course of Action



Simple Tests

Legal: Is it allowed?

Transparency - Do you mind others knowing what you have decided or done?

Effect - Does your decision hurt your current stakeholders adversely?

Fairness - Would your actions be considered fair by those affected?

Reflection - Do you see yourself as you want to see yourself?

Conclusions / Summary



- Institute of Actuaries of India provides a suitable framework for members to maintain high professional standards through the professional conduct standards, various guidance notes, and actuarial practice standards
- As a member of the profession, it is imperative to be thoroughly aware of this framework to not just fulfill the responsibility of maintaining the profession's credibility but also to avoid being subject to disciplinary action in case of misconduct breach AA shall maintain the highest standard of integrity and competence.
- AA's work / conduct shall be compliant with Regulatory requirement and professional standards. AA shall function without getting influenced by any unfair and unreasonable expectation from CEO.
- In such situations, a true professional will make a distinction between being technically right in just the letter or being technically right in spirit as well.
- In case of continued dilemma, AA shall explore consulting the institute and regulator.

Contact Details



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Thank you

Questions?