April 8, 2002

Casualty Actuarial Task Force
Actuarial Opinion Instructions Working Group
c/o Mr. John M. Purple
Chief Actuary
State of Connecticut Insurance Department
P.O. Box 816
Hartford, CT 06142-0816

Dear Mr. Purple:

The Committee on Property and Liability Financial Reporting (COPLFR) of the American Academy of Actuaries[1] is pleased to provide comments regarding the Casualty Actuarial Task Force's (CATF's) proposed revisions to the instructions for the Property/Casualty statements of actuarial opinion. We believe an assessment of the framework for these opinions after more than 10 years of practical experience is a sensible undertaking and appreciate that the CATF has taken on this task.

COPLFR has reviewed the CATF Working Group Draft dated 3/4/02 ("Draft"). At this stage we have prepared an analysis of several major issues rather than a review of details and editorial comments. There are details that we find troublesome, but we believe it would be more constructive to concentrate on four high level issues.

An important consideration in our response is Actuarial Standard of Practice (ASOP) #36. This standard had only been in effect for one year of statutory opinions when that Draft was prepared. COPLFR strongly believes that this standard was intended to address many of the concerns that seem to underlie that Draft, and suggest that the regulators more closely examine the year-end 2001 Opinions to better assess whether this has occurred.

[1] The American Academy of Actuaries is the public policy organization for actuaries practicing in all specialties within the United States. A major purpose of the Academy is to act as the public information organization for the profession. The Academy is non-partisan and assists the public policy process through the presentation of clear and objective actuarial analysis. The Academy regularly prepares testimony for Congress, provides information to federal elected officials, comments on proposed federal regulations, and works closely with state officials on issues related to insurance. The Academy also develops and upholds actuarial standards of conduct, qualification and practice, and the Code of Professional Conduct for all actuaries practicing in the United States.

Point Estimate/Range of Estimates

COPLFR believes that the Opinion is intended to be an expression of the Appointed Actuary's conclusion that the reserve is or is not reasonable. This formulation allows for the fact that actuaries may have different "best estimates" but agree that each is a reasonable estimate. It is not necessarily the case that one such number is better than the other. Both are estimates. The requirement of including the Appointed Actuary's number in the opinion elevates it to a status that is neither intended nor necessarily appropriate.

Reserve ranges are not well defined in actuarial literature either at the line of business level or at a combined lines level, assuming dependence or independence. ASOP #36 requires that the actuary only state that reserves are reasonable when they are within a range of reasonable reserves. It is the Appointed Actuary's professional responsibility to do this, and the Actuarial Board for Counseling and Discipline provides a process for regulators (and other users) to address specific issues.

Inclusion of ranges and best estimates in the Opinion, without the context that would typically be contained in the underlying report, can easily lead to misinterpretation by possible readers of the Opinion.

Confidentiality

We are aware of no other instance where there are two sets of numbers in the public domain for items on an entity's balance sheet. We do not see persuasive arguments for making loss reserves of P/C insurers an exception to this situation. The Appointed Actuary's possible alternative estimates are generally contained in the actuary's report, which is required to be available for regulatory review. In fact, the existence of such a second set of numbers in the public domain has significant tax, rating agency, Management Disclosure and Analysis, and Securities Exchange Commission disclosure implications for such insurers. To the extent the regulator believes that additional access is needed to these estimates, it is critical that these estimates be put in context and that their confidentiality continue to be protected. This may require a model law.

Materiality

The draft establishes, perhaps on a de facto basis, an extremely narrow standard of materiality. COPLFR believes that this standard would encompass the vast majority of companies and therefore require the associated disclosure of risk of adverse deviation. This has the consequence of not providing differentiation for those companies where such disclosure is of greater importance. We also note that a standard of 10 percent of surplus is significantly less than that used in current IRIS tests.

Audit

The Draft requires commentary on the last audit of the underlying data, including requiring the actuary to state that the purpose of the audit was to "… verify the accuracy and completeness of the data…" and to state that the audit is available for regulatory inspection.

COPLFR believes that robust data is vital to loss reserve analysis. The National Association of Insurance Commissioners (NAIC) regulatory process requires an audit. The Appointed Actuary is bound by existing professional standards to examine the data for reasonableness and obvious errors. The actuary should reconcile the data used in the loss reserve analysis to the financial statement, but he or she should then be able to reasonably rely on the data in that statement. The actuary should not be responsible for the audit, nor can the actuary state that such audit is available for regulatory inspection as that material belongs to the auditor, not the actuary. Any perceived failings in current data testing procedures can only be addressed efficiently and effectively through the audit process.

The timing of the audit is also an issue. The current year audit is often not complete when the Statement of Actuarial Opinion is signed, and prior years' audits have not included the most current data.

Actuarial Report

The NAIC regulatory system imposes three related but different tasks on the Appointed Actuary: form an opinion on the carried reserves, prepare a report documenting this opinion in accordance with ASOP #9, and communicate the findings to the company Board of Directors (or equivalent authority). COPLFR believes that the mechanism used to communicate with the Board should be left to the Appointed Actuary. Boards differ in their make-up and level of technical understanding such that a document prepared under ASOP #9 will very often not be appropriate to communicate findings to the Board.

Other Editorial Issues

We note that the last bullet on unusual IRIS ratios might be amended to read "… why the regulator should have confidence that *such* unusual factors should not be expected next year." The omission of "such" implies that there will not be any unusual factors in the future.

We note that wording surrounding the new disclosure Item D in the Opinion paragraph and the items enumerated at the top of the proposed Exhibit C may need to be clarified in that it could be read as implying separate opinions on the reasonableness of the individual reserve items involved rather than a simple disclosure. This has not been the focus of the opinion in the past and had not been considered an efficient application of resources.

We note that pools and associations are singled out for particular discussion. We would suggest a focus on assumed reserves in general may be more productive.

COPLFR appreciates the opportunity to provide these comments. The Committee and its individual members devote considerable professional time to the statutory Statement of Actuarial Opinion and are committed to an Opinion process that satisfies all users of the Opinion: the company; its Board; the regulators; and the public. We would be pleased to meet with the CATF to further explore ways to accomplish this objective.

Very truly yours,

Andrea M. Sweeny, FCAS, MAAA, FCA
Chairperson
Committee on Property and Liability Financial Reporting

cc: Steve Lehmann
Greg Vass