

22. (2.75 points)

A company domiciled in State X has reserves with significant net asbestos exposure (all figures are in thousands of dollars):

	Carried Reserves	Appointed Actuary's Range of Reasonable Estimates	
		Low End	High End
Unpaid loss and LAE (direct and assumed)	16,000	12,000	25,000
Unpaid loss and LAE reserves (net)	7,000	5,000	14,000

The Appointed Actuary selects the materiality standard for the Statement of Actuarial Opinion (SAO) as 50% of the net carried reserves.

a. (1.25 points)

Propose language for the OPINION section of the SAO.

b. (1 point)

Propose language for the RELEVANT COMMENTS paragraphs of the SAO related to the risk of material adverse deviation and the materiality standard.

c. (0.5 point)

Identify an alternative materiality standard for this SAO, and briefly describe why it is preferable.

SAMPLE ANSWERS AND EXAMINER'S REPORT

<p>Common errors include:</p> <ul style="list-style-type: none"> • Not including adjusting and other unpaid costs in the LAE calculation • Calculating case and bulk IBNR reserves as opposed to loss and LAE reserves.
<p>Part b</p> <p>Candidates were expected to set up the reserve tables, showing columns for low, point estimate, and high end of range. Format and order of the rows was not critical. Candidates were expected to show both gross and net tables.</p> <p>Since the actuary's point estimate was not included, candidates were not expected to fill in this number.</p> <p>Common errors include:</p> <ul style="list-style-type: none"> • Calculating a point estimate difference, rather than the range difference. It is expected that the estimates in the AOS must follow the Appointed Actuary's analysis, so because the data was provided as a range it was expected that the difference was a range as well. • Mis-calculating the reserve; sometimes by not including adjusting and other.
<p>Part c</p> <p>Candidates were expected to identify that the opinion should be reasonable, because it falls within the range of reasonable estimates. If the reserve falls outside of the range provided in part b because of an error in part b, candidates were expected to identified a deficient or redundant reserve, consistent with the range provided in b.</p> <p>A common error was providing only the type of opinion without a justification.</p>

FALL 2018 EXAM 6US, QUESTION 22	
TOTAL POINT VALUE: 2.75	LEARNING OBJECTIVE: D
SAMPLE ANSWERS	
Part a: 1.25 points	
<p><u>Sample 1</u></p> <p>In my opinion, the amounts carried in Exhibit A on account of the items identified:</p> <p>[A.] Meet the requirements of the insurance laws of State X.</p> <p>[B.] Are computed in accordance with accepted actuarial standards and principles.</p> <p>[C.] Make a reasonable provision for all unpaid loss and loss adjustment expense obligations of the Company under the terms of its contracts and agreements.</p>	
<p><u>Sample 2</u></p> <p>The reserves shown in Exhibit A:</p> <ol style="list-style-type: none"> 1. Are in accordance with the laws of State X 2. Are in accordance with accepted actuarial standards and practices 3. Are reasonable on a gross and net basis as they fall within the range of reasonable estimates. 	
Part b: 1 point	
<u>Sample 1</u>	

SAMPLE ANSWERS AND EXAMINER'S REPORT

My materiality standard has been established as 50% of the net reserves or \$3.5 million. There is risk of material adverse deviation. I have identified the key risk factor as the asbestos exposure.

Sample 2

- Materiality was selected by using 50% of net carried reserves
- The materiality standard is \$3,500
- Risk of Material Adverse Deviation (RMAD) exists as the materiality standard + comp carried reserves is within the actuary's range of net reserves
- Risk factor contributing to this is significant asbestos exposure

Part c: 0.5 point

Sample 1

(5-20%) Percent of net carried reserves. This is preferable since it is smaller so more conservative.

Sample 2

(5-20%) Percent of surplus. This is preferable since it is tied to solvency.

Sample 3

(5-20%) Percent of surplus. A company may have a large amount of surplus to pay for reserves so a 50% change in reserves may not be material for the company.

Sample 4

Amount that would cause a drop in financial rating. This might impair the company in generating new business or acquiring reinsurance.

Sample 5

Amount that would cause a drop in RBC level since this is directly related to regulatory intervention.

Sample 6

Amount that would cause a drop to Company Action Level. This would result in regulatory action that could negatively impact the company even more.

EXAMINER'S REPORT

Candidates were expected to draft language for the OPINION section of the Statement of Actuarial Opinion (SAO) as well as the Risk of Material Adverse Deviation portion of the RELEVANT COMMENTS section of the SAO including the materiality standard, and to propose an alternative materiality standard.

Part a

Candidates were expected to provide language for the OPINION section of the SAO, including all the necessary components identified in the NAIC SAO instructions.

Common errors include:

- Excluding the statement that the opinion is in reference to the amounts in Exhibit A.
- Using the term "adequate" or "sufficient" to describe the type of opinion. The NAIC uses the term "Reasonable".

SAMPLE ANSWERS AND EXAMINER'S REPORT

<p>Part b</p> <p>Candidates were expected to provide language for the paragraphs related to the risk of material adverse deviation (RMAD) and materiality standard in the RELEVANT COMMENTS section of the SAO, including all the necessary components identified in the NAIC SAO instructions.</p> <p>Common errors include:</p> <ul style="list-style-type: none"> • Excluding either the amount of the materiality standard (\$3,500) or the basis for it (50% of net carried reserves). • Excluding the risk factor contributing to RMAD (asbestos exposure). • Incorrectly identifying that RMAD does not exist for this company and not providing sufficient explanation as to why there isn't RMAD.
<p>Part c</p> <p>Candidates were expected to identify an alternative materiality standard than the one given in the question and provide a reason why it is preferable.</p> <p>Common errors include:</p> <ul style="list-style-type: none"> • Providing an insufficient reason why the other standard is preferable (for example, stating that the standard is more reasonable without explaining why or explaining that it is an amount that would concern company management). • Incorrectly interpreting a larger materiality standard as more conservative. • Incorrectly stating that a percentage of surplus is preferable because it can't be manipulated by company management, unlike carried reserves. The amount of carried reserves has an impact on the company's surplus.

FALL 2018 EXAM 6US, QUESTION 23	
TOTAL POINT VALUE: 1.75	LEARNING OBJECTIVE: D
SAMPLE ANSWERS	
Part a: 0.25 point	
SCOPE	
Part b: 1 point	
<p>Any four of the following:</p> <ul style="list-style-type: none"> • Filing is not with US Department of Commerce. It is with State DOI. • Missing statement whether the actuary reconciled data to Schedule P Part 1. • Actuary should disclose that he/she reviewed the data for reasonableness and consistency. • The provider of the data should be an officer of the company. • Missing statement that the SCOPE items included in the SAO reflected disclosures in Exhibit B. 	
Part c: 0.5 point	
<p>One of the following</p> <ul style="list-style-type: none"> • If the portion of the reserves is material, I would issue a qualified opinion. • If the portion of reserves is immaterial, then a reasonable/deficient/excessive opinion, depending on position of reserves within the reasonable range. 	