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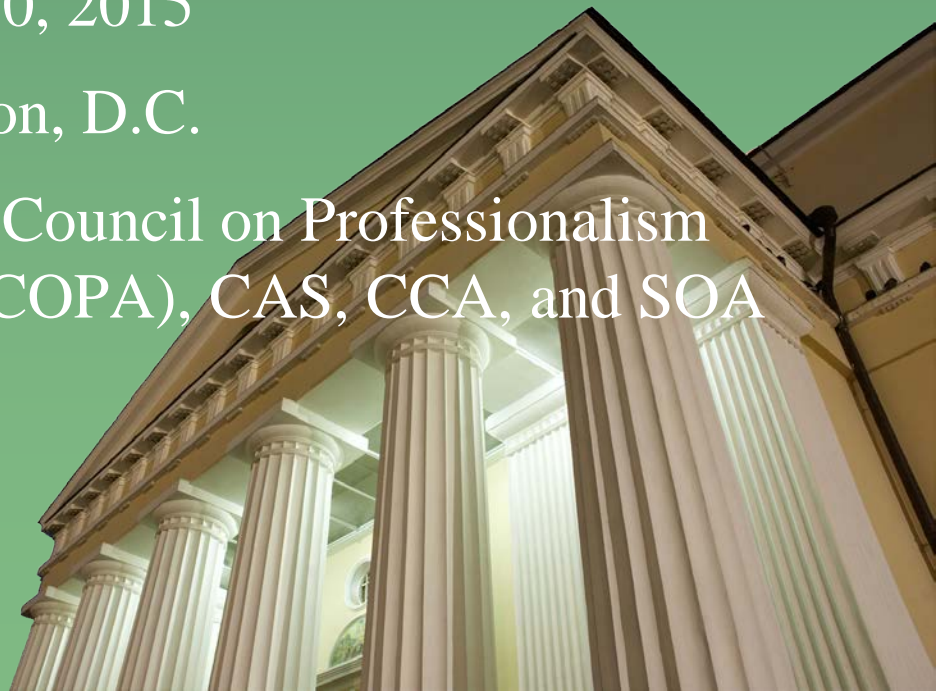
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Unknown Unknowns: Challenges to Professionalism

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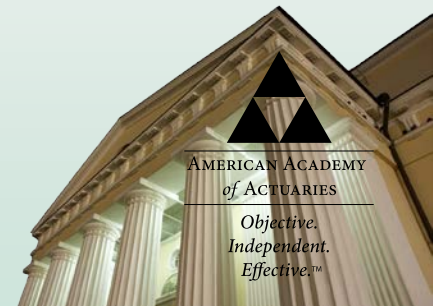
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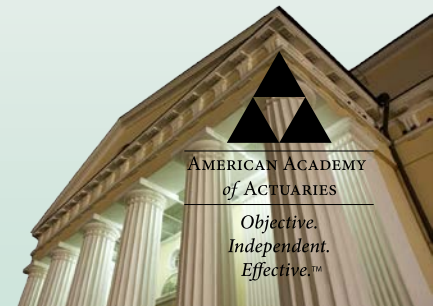
Agenda

- Professionalism Framework
- Pension: The Multiemployer Pension Reform Act
- Health: The Affordable Care Act (ACA)
- Casualty: Adverse Reserve Development
- Q&A



Administrative

- Submit questions on each section as it occurs: questions will be addressed after each practice area is discussed.
- Keep questions general/hypothetical, not specific to any assignment you may currently be working on.
- Groups



Professionalism Framework

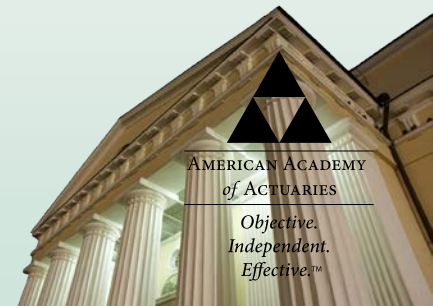
In general, three types of professional standards apply to all actuarial work:

- The Code of Professional Conduct (ethical guidance)
- The U.S. Qualification Standards
- The Actuarial Standards of Practice (ASOPs)



Unknown Unknowns

- Unknown unknowns can present a rare and difficult challenge.
- The practice areas we will be discussing are not “new.” These are areas where there was no way to know what applicable law or regulation would be promulgated (MPRA and ACA), or where what was thought to be known turned out to be unknown (Adverse Reserve Development).



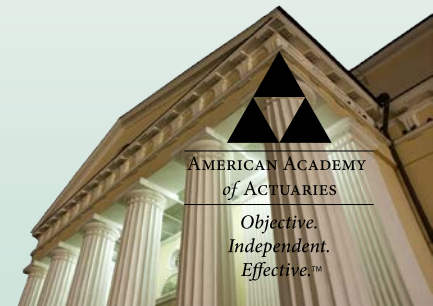
Unknown Unknowns

- Consider Precepts 2 and 3 of the Code
 - An Actuary shall perform Actuarial Services only when the Actuary is qualified to do so on the basis of basic and continuing education and experience, and only when the Actuary satisfies applicable qualification standards. (Precept 2)
 - An Actuary shall ensure that Actuarial Services performed by or under the direction of the Actuary satisfy applicable standards of practice. (Precept 3)



Unknowns and the Code

- The Code also gives this additional guidance:
 - Annotation 2.2 – The absence of applicable qualification standards for a particular type of assignment...does not relieve the Actuary of the responsibility to perform such Actuarial Services only when qualified to do so....
 - Annotation 3.2 – Where a question arises with regard to the applicability of a standard of practice, or where no applicable standard exists, an Actuary shall utilize professional judgment, taking into account generally accepted actuarial principles and practices.



PENSION



Multiemployer Plans (A Primer)

- A benefit plan sponsored by 2 or more employers
- Pursuant to at least one collective bargaining agreement
- Most run jointly by a labor/management Trustee board
- Common in construction, transport, service, sports, and entertainment industries
- Could cover funds for DB, DC, health, vacation
- 1,400 DB plans with 10 million participants



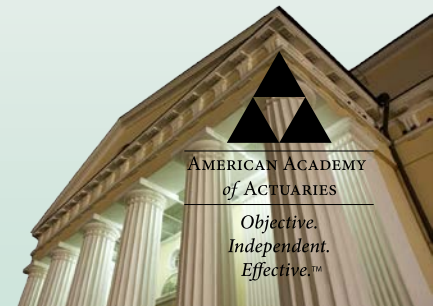
A Developing Crisis

- Since 2008, actuary annually certifies plan in a “zone”
- About 25-30% of plans in “critical status” (Red Zone)
 - 100+ moving toward insolvency despite “all reasonable measures”
- PBGC insurance coverage:
 - Far lower than for single-employer plan
 - 1.5 million participants at risk
 - 2014: PBGC projected large Multi program deficit (\$40+B)
 - With program insolvency likely within 8-10 years
- Academy on record as supporting congressional action
- Industry group lobbying “Solutions, Not Bailouts”



Multiemployer Pension Reform Act

- “MPRA” enacted mid-December 2014
- Part of “Cromnibus” budget bill needed to keep government running
- No prior legislative history
- Contained controversial provisions – especially “Benefit Suspensions”
- Created new actuarial responsibilities
- Required PBGC/Treasury regulations within 180 days



MPRA: Short-Term Actuarial Concerns

- New “Critical and Declining” status (C&D)
 - For plans facing insolvency within 15-20 years
 - Gateway to suspensions
 - Pension Protection Act (PPA) plan-level actuarial certifications –
Directly after enactment? Certainly by end of March!
 - Reliance on sponsor for industry activity inputs
- “Special Emergence” rules—unintended consequences
- Ability to elect “Early Critical” status—IF actuary so certifies
- “Zone” notices to critical status participants
 - Suspension exposure not mandated by MPRA
 - Annual funding notice due 13 months later



MPRA: Longer-Term Actuarial Concerns

- Suspension application rules – awaiting regulations
 - Academy submitted several comments
- Length of solvency projection: indefinite? 30 years?
- Suspensions certified by actuary to avoid insolvency
 - But “not materially exceed” level needed to do so
- Other actuarial issues:
 - Sensitivity testing
 - Timing (current assets)
 - Ongoing annual testing to remain in force



Where to Turn for Advice

- Code of Professional Conduct
- Plan legal counsel
- Internal legal counsel
- Colleagues, other actuaries
- Professional meetings & webinars
- ABCD request for guidance?



Lessons Learned from PPA '06

- 18-month statutory lead time helped, despite lack of meaningful and timely regulation
- Reliance on plan legal counsel for difficult issues
- Academy draft Practice Note “Multiemployer Plan Actuarial Certifications under the Pension Protection Act of 2006”
 - Q&A helpful, but took time to develop
 - Reflect evolving practice



Pension

Questions?



HEALTH



Health: The ACA

The Affordable Care Act

- Completely restructured the individual health insurance market
- Required a whole new federal regulatory structure to be built from scratch
- Required numerous policy decisions to implement the law

All this occurred in a deeply polarized political environment.



Challenge: Am I Qualified?

- Many actuaries had decades of experience in what was effectively an entirely different market.
- Work now had to be done under an entirely new set of rules—many of which were still being written.
- Answer cannot be:
 - Business as usual—of course I’m qualified (even if I do nothing else)
 - No one is qualified



Challenge: Am I Qualified?

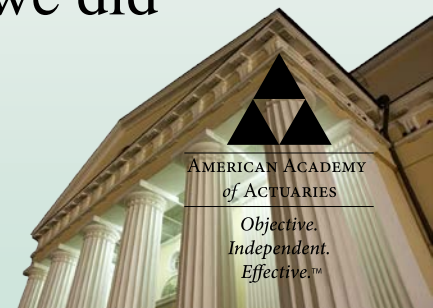
Possible questions to ask myself

- Have I familiarized myself with the new law?
- Am I reading and understanding the new rules as they are released?
- Am I following sub-regulatory guidance as it's released?
- Am I talking to others about how to practice in the new environment?
- Are the techniques and principles I've used in the past still relevant?



Challenge: What Can I Sign?

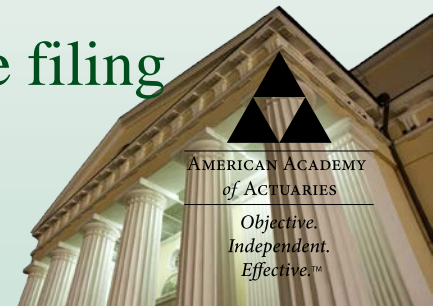
- Past experience data were of limited relevance.
- Guidance was changing right up to—and past—the deadline for products and rates.
- No one knew how the program would be received or what the insured population would look like.
- New nonprofit co-ops had no prior experience, no existing customer base, and limited capital.
- Answer cannot be:
 - Business as usual—run things through the way we did them last year.
 - It's impossible to file anything.



Challenge: What Can I Sign?

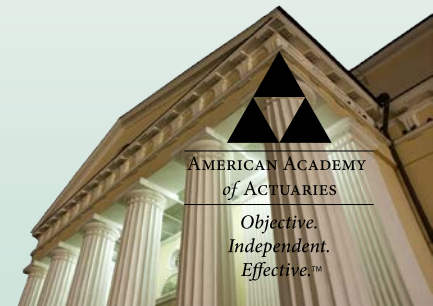
Possible questions to ask myself

- What assumptions am I making about the new market?
- Are there significant aspects of the new rules that I'm not including in my calculations? If so, why not?
- What outstanding regulatory questions could affect my work?
- What additional explanations do I need to provide for my assumptions?
- What caveats and qualifications do I need to include for the regulator to understand the applicability of my certification?
- What opportunity—if any—do I have to modify the filing if new guidance is issued?



Health

Questions?



CASUALTY



Casualty: “Naiveté or Knavery”

- 2002 Annual Statements showed significant adverse development on 2001 reserves.
- S&P report paraphrased: Whether by “knavery or naiveté,” actuaries are signing off on inadequate loss reserves.
 - Questioned the integrity and/or competency of opinion signers
 - Stimulated activity on many fronts to understand what was happening
- Why? What was unknown?



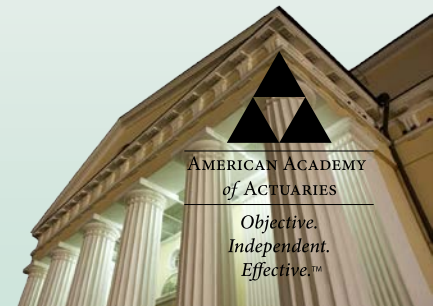
Casualty: The Results

- Nearly a quarter of the companies reported an increase on the prior year's reserves that was greater than 10%.
- Of the \$23.1 billion in adverse development, just 30 companies accounted for 80%.
 - Large reinsurers were in the top group.
 - Most of the companies were large or subsidiaries of large companies.
 - Commercial lines dominated—especially asbestos and environmental claims and workers' compensation.



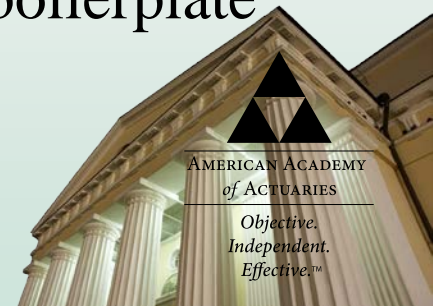
Casualty: Perspective

- Subsequent analysis of what happened in Academy's 2010 Financial Soundness and Risk Management (FSRM) white paper
 - Nine of the 30 companies were technically insolvent in 2001 based on development through 2008.
 - Eleven more would have been in an RBC action level.
 - Larger companies generally survived and grew their surplus.
 - Five of the smallest companies of the 30 are no longer in business.



Casualty: The Investigation

- Initial implication was that the majority of the industry was seriously underreserved.
- Regulators looking to actuarial opinions for answers were not finding them.
 - New ASOP No. 36, *Statements of Actuarial Opinion Regarding Property/Casualty Loss and Loss Adjustment Expense Reserves*, required comments if actuary believed there was a significant risk of material adverse deviation.
 - CASTF (then known as CATF) had already begun to rewrite the opinion instructions to remove much of the boilerplate and require a real discussion of issues.



Casualty: The Results

- Effective with 2004 reserves, opining actuaries now were required to assert whether or not they believed there was a risk of material adverse deviation (RMAD).
- Regulators required actuaries to discuss risks more completely in their own words.
- Academy's Effective P&C Loss Reserve Opinion Seminar (affectionately known as “opinion boot camp”) was born.



Casualty: What Does This Mean for Me?

■ Discuss, Discuss, Discuss

- Remember: A&E claims often emerged decades after policies were written.
- Another mass tort situation will probably emerge down the road.

■ Disclose, Disclose, Disclose

- Admit what you know and what you don't know.
- If unknown amounts may be material, consider a qualified opinion.
- Consider calling your regulatory actuary—they are likely already aware of the uncertainties.
- Remember, there is more to your analysis than numbers.



Casualty

Questions?

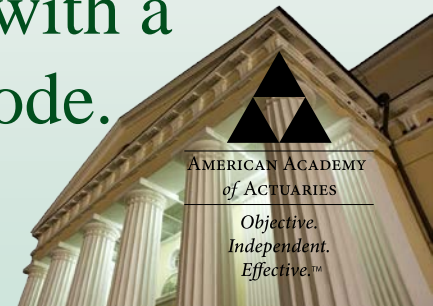


Unknown Unknowns

■ Lessons Learned

- Be aware of the “big picture” – when something unexpected happens, how do you approach it?
- Consider the Code, USQS, ASOPs
- Consider all relevant information as it becomes known or available, e.g. Practice Notes, White Papers, Seminars
- Network with colleagues, create a culture of sharing information within your organization—connect the dots.

■ Professionalism requires you to act with integrity and competence. Confront unknown unknowns with a decision-making framework based on the Code.



Poll

Please answer the polling questions.

Thank you!

