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Insurance TAS Exposure Draft April 2010

We are writing to give a formal response from Hiscox Insurance Company Ltd to BAS's Insurance TAS Exposure Draft dated April 2010. Our most significant comment is that we disagree with the proposed scope of the Insurance TAS. We do not think that it should cover pricing, business planning and production of management information for monitoring business performance. Compliance with the Insurance TAS would make it impossible for our actuaries to perform the work they currently do as there would be excessive documentation and reporting requirements which are not required for us to manage our business effectively. It would be likely that we would request our actuaries to depart from the requirements of the Insurance TAS for a lot of the work they perform. This is a situation we would be uncomfortable with. External parties such as auditors, regulators, investors, brokers and clients may not view this instruction to depart from actuarial standards in a positive manner. Therefore, we ask that the BAS redraft the Insurance TAS. Our detailed comments are set out in the sections below.

Pricing

Paragraph C.1.13 puts "the pricing of insurance products" in the scope of the Insurance TAS. Actuarial involvement in the pricing of General Insurance business is a relatively recent development. At Hiscox Insurance Company Ltd, we had no dedicated qualified pricing actuaries supporting the pricing of the business prior to 2010. We do now have pricing actuaries supporting certain business lines, but it is the case that the majority of the business is priced by other professionals: underwriters, cat modellers and statisticians, with no input from pricing actuaries. Paragraph 11 of BAS's Scope & Authority of Technical Standards July 2008 states that "Any TAS developed by BAS will be targeted at work that is commonly performed by actuaries". As the majority of General Insurance pricing work is not performed by actuaries we believe that the inclusion of pricing in scope of the Insurance TAS will not comply with Paragraph 11 of the Scope & Authority document. Further, we note that Paragraph 2.42 of the Insurance TAS Exposure Draft states that for investment related work "Given that by no means all or even most of such work is carried out by actuaries and it is not clear what work is actuarial and what is not, we propose not to include such work in the scope of the Insurance TAS. Respondents agreed with this decision." Some of the General Insurance pricing work is ad hoc in nature and not always easily defined as actuarial, and also the majority of it is not performed by actuaries. Therefore, in a similar way to investment work, we believe that pricing work should not be included in the scope of the Insurance TAS.

In paragraph B.2.1, the materiality definition states "Matters are material if they could, individually or collectively, influence the decisions to be taken by the users of the related actuarial information." In pricing work, analysis is often provided to underwriters on the price to charge on a risk, or an assessment of the adequacy of the offered price. By the nature of this advice, it is designed to influence the decision made by an underwriter. Therefore, from the definition in B.2.1, nearly all actuarial pricing work will be classified as material and so will be covered by all the requirements of the Insurance TAS and of TAS's R/D/M. BAS are fully aware of these requirements. We give a high level list below of a few requirements for reporting to users and documentation so that you are reminded how broad in scope they are and how onerous they could be:

TAS R – State purpose and intended users, describe data and state its source, describe the uncertainty in the data, state assumptions and explain rationale in setting, explain and rationalise calculations, indicate nature and extent of uncertainty in results, state nature and significance of material risks and approach taken to them, compliance statement.

TAS M – Explain rationale for grouping data, explain limitations of any models used, explain how models meet the users' needs, why the model is a satisfactory representation, model checks performed.

TAS D – Perform data checks, and treatment of inaccurate and incomplete data.

Insurance TAS – Explain rationale for a changed approach, use sensitivity testing to indicate uncertainty, explain how claim severity and frequency are modelled.

Clearly there are a lot of requirements which could take a significant amount of time for each piece of work performed. Whereas this may be justified for large pricing projects covering a homogenous group of risks, the task would be quite onerous for some of the specialist risks that we write where the data is often very sparse. Our pricing actuaries are sometimes required to develop bespoke models for a single risk, in very short timescales, using whatever data is available. The results are presented to underwriters who are expert professionals in their field and understand very well the data limitations and uncertainty in the results of the modelling. Our pricing actuaries would not be able to do this work if they had to comply with all reporting and documentation requirements of the TAS's. Further, we do not want them to provide this documentation and reporting, as we want them to work closely with the underwriters providing fast analysis to the best of their abilities, in this challenging commercial environment. We provide comprehensive and rigorous training for all of our underwriters, which includes understanding the risks and uncertainties of the business they are writing.

Paragraph B.1.3 states that "this standard should not be interpreted as requiring work to be performed that is not proportionate to the scope of the decision..." We would like to be able to argue that the numerous requirements the TAS's would impose on every small pricing task are excessive and hence not proportionate, so it would not be required to comply to the Insurance TAS. However, the materiality definition seems to define the analysis supporting each pricing decision as material, and so it does not seem from our reading of the Insurance TAS, that we can argue that they would not apply on grounds of proportionality. Therefore, if the Insurance TAS was adopted as set out in the Exposure Draft, we believe we would have the following options in relation to our pricing actuaries:

1. Instruct them to depart from the requirements of the TAS.
2. Ask them to resign from the UK actuarial profession.
3. Seek to employ actuaries from overseas actuarial professions or numerate non-actuaries.
4. Massively reduce their expected workload so that they can spend time on reporting to users and on documentation which we do not see as necessary.

It is likely that we would reluctantly take the first of these options. We think a lot of other insurers would also take this route. We do not think that it would be good for the actuarial profession to have a lot of their members being instructed to depart from their standards. Therefore, for the reasons set out above we ask the BAS to remove pricing from the scope of the Insurance TAS.

Business Planning, Management Information for Business Performance

Paragraphs C.1.16 and C.1.17 bring financial projections for business planning and the production of management information for monitoring business performance into the scope of the Insurance TAS. We see very similar arguments for why these should not be included in the scope as for pricing. These are listed at a high level below:

1. The majority of this work is done by non actuaries in our company and the actuarial involvement is a mixture of actuarial and non-actuarial work. So similarly to investment work, pricing should be excluded from the scope.
2. For a lot of the smaller, quicker tasks it is impractical and unnecessary to provide all of the documentation and reporting requirements of the TAS's.
3. The users of the information are highly trained professionals who are fully aware of the uncertainties of the actuarial projections.

Insurance Transformations

Paragraph C.1.18 to C.1.20 brings insurance transformations into the scope of the Insurance TAS. We believe that it is appropriate to include the largest transactions, like the purchase of an insurance company, into the scope of the TAS. These individual transactions can be very significant when viewed at the company level. They tend to happen infrequently and we believe that these should be included in the scope of the TAS. However, for smaller pieces of work like a commutation of a small reinsurance contract, we think that they should be excluded from the scope for similar reasons set out for pricing.

Other areas of work to be included in the Insurance TAS

We agree with the areas of work to be included in the Insurance TAS as set out in Paragraphs C.1.2, C.1.5, C.1.7, C.1.11, C.1.12 and C.1.24.

Reliance Objective

We strongly support BAS's promotion of the Reliance Objective and believe it is very important for the users of actuarial information in certain circumstances. We support the Insurance TAS in the areas set out in the above paragraph and believe that it will help to ensure that the objective is met in those areas.

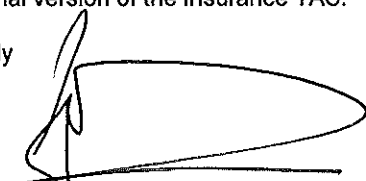
Questions In Section 7 of the Exposure Draft

7.1.1 – We believe that the commencement date of 1 April 2011 is too early. Most insurance companies are working flat out on preparing for Solvency II, and have not focused on the full implications of the Insurance TAS. We think it would be better to delay the commencement date until after the introduction of Solvency II.

7.1.2 – We believe that Section 6 of the Exposure Draft massively underestimates the cost to the insurance industry that the full implementation of the Insurance TAS would have. Although we do think that a lot of insurers will opt out of adopting the TAS for non-Required and non-Reserved areas. We have already incurred significant costs in relation to Solvency II and we will incur more costs with implementation of the Insurance TAS. Paragraph 6.3 states that "practitioners apply reasonable judgement, especially on materiality and proportionality". As stated above in relation to pricing, the materiality definition makes all pricing analysis material so in practice it will not be possible to adopt the TAS without a lot of additional work. We disagree with the statement in Paragraph 6.10 that the TAS would not require a disproportionate amount of work.

Please contact us if you need clarification of any of the above comments. We thank you for giving us the opportunity to comment on the Exposure Draft. We hope you will take our comments into consideration in drafting the final version of the Insurance TAS.

Yours faithfully



Gary Head
Underwriting Director



Paul Cooper
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