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GENINS/986263/CPC

16th July 2010

The Director
Board for Actuarial Standards
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BY EMAIL AND POST

Dear Louise

**BAS Exposure Draft on Insurance (April 2010)
Response from Lane Clark & Peacock LLP**

We are pleased to respond to the exposure draft on insurance.

Lane Clark & Peacock LLP ("LCP") is a leading firm of actuaries and consultants, with over 90 partners and principals and more than 450 employees across Europe. The firm provides actuarial, employee benefit, investment, insurance and risk management advice as well as pensions administration services.

Our Insurance Consulting practice provides actuarial and consulting advice to clients including Lloyd's managing agents, insurance companies, public sector and regulatory bodies, mutuals, captives, brokers and auditors.

1. The proposed commencement date of the Insurance TAS

We think it is realistic that you have allowed about six months between the intended finalisation of TAS I and the implementation date.

However, we think the proposed 1st April start date will fall uncomfortably in the period during which some 31st December year-end work is being finalised and preliminary work on 31st March year ends is being done. These year ends account for a large number of insurers. We think a 1st June start date would be better.

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2. Inclusion of pricing work in the scope

We continue to believe that it is wrong to include actuaries' pricing work in the scope of TAS I.

We commented on this in more detail in our reply to your September 2009 consultation and we note that many actuaries in the London Market have now raised a number of points of concern with you in relation to the Exposure Draft.

We think the requirements of TAS compliance in this area will result in red tape and delays which are impractical if actuarial input is to be of any use in pricing activity. By including pricing work in scope, you may force insurers formally to opt out of TAS compliance, as is possible under the Scope & Authority for non-Reserved Work, or, if they find this unpalatable, to use non-actuaries for the work.

We urge you to rethink this issue and also to consider whether the concerns that have been identified give rise to similar issues in other areas of actuarial work.

3. Definition of "neutral"

We wonder whether you have fully considered the implications of introducing the concept of "neutral" measures, assumptions and judgments.

In particular, how should actuaries reconcile "neutral" with the definition of "best estimate" given in accounting standards and Solvency II? Would a "neutral" measure correspond to a probability-weighted average of all future outcomes?

If so, how does this make sense in, for example, a catastrophe reinsurance contract, where the loss ratio is likely to be either zero (with a high probability) or much greater than 100% (with a low probability)?

If the probability-weighted average loss ratio is estimated to be say 20% (a result which is highly unlikely to occur in practice) is this still a "neutral" estimate? A loss ratio of 20% may well lie at the 90th percentile of modelled outcomes - how is one to decide whether this loss ratio is optimistic or pessimistic?

We do not think these difficulties are insurmountable if suitable clarification is provided in the wording of the TAS.

Note: your definition of "neutral" contains the word "any", which does not appear in the corresponding definition in TAS M.

4. Requirements regarding "prudent" estimates

We do not support the proposed wording in paragraphs D.4.1 and D.4.2 requiring the actuary to explain the difference between prudent estimates and neutral estimates of the technical provisions of an insurer.

First, the present wording leaves it unclear who decides whether the estimate is a prudent one (and therefore whether it gets caught by these paragraphs). Is it where the report specifically claims the

estimate to be a prudent one? If so, the actuary could presumably just avoid using the term “prudent”.

Secondly, there are different understandings of the word “prudent”. Article 76 of the Solvency II Level 1 text states that: “*Technical provisions shall be calculated in a **prudent, reliable and objective manner.***” (Our emphasis added.)

As you know, the term “prudent” in this sentence does not mean that any margins for prudence are added. The technical provisions under Solvency II are the sum of a probability-weighted discounted best estimate and a risk margin which represents the cost of capital and has nothing to do with margins for prudence. It seems therefore that the word “prudent” in this case refers to performing the calculations with due care rather than taking a deliberately conservative approach.

Thirdly, there are the difficulties with the term “neutral”, which are covered in our comments in Section 3.

Note that we would support a reworded requirement for actuaries to disclose and explain any conscious margins for prudence (whether implicit or explicit) that are incorporated in their estimates.

5. Wording of Reliability Objective

In paragraph A1.2, our opinion is that it is out of place for the TAS to require that calculations are performed “without mistakes”. Despite best efforts, mistakes do happen and it is not clear how this phrase will help in preventing them. There is a danger that such wording creates unreasonably high expectations.

6. Definitions of “method” and “measure”

We find the definitions of “method” and “measure” (section B.2) unclear. As drafted, it is difficult to be sure what the implications of the distinction are. It is also unclear what activities, techniques and calculations will fall into which category. If this terminology is to be retained, it will need clarification.

7. Frequency severity wording needs additional clarification

It would be helpful if paragraphs D3.4 and D 3.5 could make it clear that in certain circumstances it may be appropriate to model claim frequency and severity together (ie to model the aggregate claims).

8. Sale/purchase work

In paragraph C1.20, in order to be consistent with wording used elsewhere, we suggest you replace the words “work concerning” with “work supporting”.

9. Mapping of principles from the insurance GNs to TAS I

We remain concerned at the notion that the various insurance Guidance Notes that have been built up carefully over the years can safely be deleted and replaced with the Insurance TAS (plus the generic TASs) as currently drafted. What transitional measures do you have in mind to deal with any issues that may emerge from the deletion of the present guidance notes?

Please contact us if you would like to discuss any of our comments.

Yours sincerely

{Sent as an attachment to an e-mail on 16th July 2010 at 17:54}

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Partner

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