General Insurance Practice Note 1 (GIP 1)

Authority

This Practice Note is issued by Council in accordance with Appendix 3 to GN 20 (ROI) - Statement of Actuarial Opinion on Non-Life Technical Reserves to the Department of Enterprise, Trade and Employment. The Appendix sets out a procedure for the issue of Practice Notes "to handle the possibility of abnormal uncertainty surrounding the quantification of liabilities covered by the Statement of Actuarial Opinion or to ensure uniformity of practice in relation to specific assumptions made in actuarially estimating reserves". Council considers that the position in relation to the 2001 High Court "McEneaney Judgement" meets the criteria for the issue of a Practice Note.

Application

Applicable to Fellow Members of the Society of Actuaries in Ireland holding current Practising Certificates to act as Signing Actuary to a Non-Life Insurance Company. GIP 1 is effective as at 31/12/2001. In accordance with Appendix 3 to GN 20 (ROI), GIP 1 will be reviewed by the General Insurance Committee at least once every three months and may be cancelled by the Committee if deemed no longer relevant but, otherwise, will remain in force for 12 calendar months from date of issue unless renewed by Council.

Background

Prior to the McEneaney case, calculations of the value of loss of earnings and future medical care in personal injury cases had been based on a standard real discount rate of 4% (the actual rate underlying settlements could vary around this rate, reflecting the negotiating circumstances of individual cases). The assessment of damages in the McEneaney judgement, however, was based on real discount rates for calculating the value of loss of earnings at 2.5% and future medical care at minus 0.5%, significantly below this benchmark. It is unclear at this stage how the judgement may affect future settlements and Court decisions. It is understood that the judgement is not, formally speaking, a precedent in that it was uncontested in the particular case and the basis of the judgement may well be contested in future cases. The situation is, therefore, one of considerable uncertainty as to the levels of real discount rates that may ultimately be determined. Nevertheless, Signing Actuaries must endeavour to establish best estimate reserves, taking a balanced view of the various factors involved.

Recommended "Best Estimate" Framework

The Signing Actuary should carry out appropriate investigations and calculations to establish the levels of reserves required (i) on the basis of existing reserving standards and assumptions and (ii) on the basis of the application of the standards set in the McEneaney judgement. This will give an estimate of the total reserve uplift required if the standards of the McEneaney judgement were to be implemented in full. The review could be carried out on a case-by-case basis or by representative sampling where appropriate. "Worst case" positions should be determined on both a gross of reinsurance and net of reinsurance basis. The Signing Actuary should then consider, in the context of the uncertainties detailed above, the various factors that might be relevant in arriving at best estimate reserves, for example:

- the basis currently being used in the undertaking concerned to establish reserves

- the timeframe to ultimate settlement of the claims likely to be affected by McEneaney (both pending cases and IBNR)

- the distribution of claims sizes in cases likely to be affected by McEneaney

- the relative mix of future loss of earnings and future cost of care elements

- the overall materiality of the "worst case" position in relation to total reserves

- the undertaking's claims settlement experience and corporate policy in relation to claims settlements

- market trends in relation to claims settlement levels.

Having investigated these issues, a best estimate should be established by applying a probability factor to the additional reserves required in the "worst case" scenario. On the basis of the deliberations of the Working Party set up to consider this issue, the recommended range for this probability is 30% to 50% for gross of reinsurance reserves. To determine the equivalent net of reinsurance reserves, the gross probability factor should be applied on a case by case basis to all claims affected by non-proportional reinsurance. The actual net equivalent should then be determined individually for these claims, taking into account the individual retentions applying to each claim. As a significant amount of the gross additional costs may be borne by non-proportional treaties, it should be noted that the net reduction could be a smaller percentage than the gross reduction. Aggregate methods can be used for injury claims not affected by non-proportional treaties.

Reporting

In the Actuarial Report to the insurance undertaking supplementing the Statement of Actuarial Opinion (see Section 2 of GN 20 (ROI)), the Signing Actuary should explain how the McEneaney issue has been dealt with. The Actuarial Report should, inter alia, state the “worst case” and “best estimate” positions for both gross of reinsurance and net of reinsurance reserves. A rationale for the probability factor selected in establishing the best estimate reserve should be included. In accordance with Appendix 2 to GN 20 (ROI), a Signing Actuary who does not comply with this Practice Note should specify reasons for this in the Actuarial Report and should qualify the Statement of Actuarial Opinion accordingly.