

Memorandum

To: All Property and Casualty Insurance Practitioners

From: Claudette Cantin, Chairperson
Committee on Property and Casualty Insurance Financial Reporting

Date: January 12, 2006

Subject: **Guidance for the 2005 Valuation of Policy Liabilities and DCAT for Property and Casualty Insurers**

Document 206002

The purpose of this memo is to act as a reminder to actuaries in several areas affecting the valuation of the 2005 year-end policy liabilities and Dynamic Capital Adequacy Testing (DCAT) of property and casualty insurers. As the year-end is approaching, the Committee on Property and Casualty Insurance Financial Reporting (PCFRC) would like to take this opportunity to remind actuaries involved in policy liabilities valuation and DCAT reporting that it is important to review the Rules of Professional Conduct¹, the Standards of Practice (SOP)¹ and relevant educational notes.

While all of the Rules and SOP are important, we would like to direct your attention to the following in particular:

- SOP Section 1600 – Another Person’s Work
- SOP Section 1800 – Reporting
- SOP Section 2100 – Valuation of Policy Liabilities: All Insurance
- SOP Section 2200 – Valuation of Policy Liabilities: P&C Insurance
- SOP Section 2400 – The Appointed Actuary
- SOP Section 2500 – Dynamic Capital Adequacy Testing

In addition, PCFRC has published the educational note entitled, *Discounting* (July 2005). This note replaces the 1999 educational note “*Discounting*” to make it consistent with the Canadian Institute of Actuaries SOP. It provides guidance in two areas where no such guidance is provided in the SOP, namely the selection of a discount rate for the estimation of ceded liabilities, and the discounting of future costs associated with premium liabilities.

The PCFRC has also published the educational note entitled, *Consideration of Future Income Taxes in the Valuation of Policy Liabilities* (July 2005). It provides guidance to actuaries in

¹ <http://www.actuaries.ca/members/professional>

valuing the impact of future income taxes on policy liabilities of Property and Casualty insurers.

Members should also be aware that PCFRC has requested the removal of Section 2210.02 of the Standards of Practice. Section 2210.02 reads: *Notwithstanding Section 2100 and this Section 2200, until standards have been developed, the actuary may ignore taxes in determining policy liabilities for property and casualty insurance.*

The Practice Standards Council (PSC) had requested that PCFRC develop a standard of practice addressing the consideration of future income tax for property and casualty companies, with a view to removing the above-noted exception. As illustrated in the note, however, income tax is unlikely to be a significant consideration for the valuation of property and casualty companies. Accordingly, the PCFRC provided guidance to members by way of this educational note, rather than a standard of practice.

Other recent PCFRC guidance includes:

- Educational Note: DCAT Minimum Regulatory Capital Requirement (July 2003)
- Educational Note: Valuation of Policy Liabilities P&C Insurance Considerations regarding Claim Liabilities and Premium Liabilities (June 2003)

For your convenience, all of these educational notes can be found on the PCFRC website in the members section (Organization/Practice Standards Council/Committees and Task Forces/Committee on Property and Casualty Insurance Financial Reporting).

In addition to the Rules, SOP and educational notes, the repealed memorandum of November 1993 entitled, Provision for Adverse Deviations (Property & Casualty)² provides useful guidance for the selection of margins for adverse deviation until a suitable replacement is published by the Canadian Institute of Actuaries. Specifically, it lists many important considerations influencing the selection of margins, and provides descriptions of high and low margin situations.

The PCFRC has prepared a document entitled, “Summary Appointed Actuary Seminar PD-9-Discounting Review of Current and Best Practice”. This document summarizes the round table discussions held at the Seminar for the Appointed Actuary (September 2005). It provides helpful insight into current and best practices in selecting the provision for adverse deviations. It will be posted on the website shortly.

As outlined in Section 1220 of the Standards, the “actuary should be familiar with relevant educational notes and other designated educational material,” considering that a practice described “for a situation is not necessarily the only accepted practice for that situation and is not necessarily accepted actuarial practice for a different situation.”

Members should also be aware that the Accounting Standards Board (AcSB) issued accounting guideline No. 19 (AcG-19) in May 2005, which is effective for 2005 year-end valuations. AcG-19, Disclosures by Entities Subject to Rate Regulation, applies to insurance activities subject to rate regulation, such as automobile insurance. This will require a note disclosure to the financial statements and the actuaries should be aware of that guideline and its implications.

Finally, PCFRC remains available for all of your questions and comments.

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² <http://www.actuaries.ca/members/publications/archives>