



# Actuarial bored reports are more interesting than you think

**Every year, friendly society boards have to cope with what seems to be an increasing number of reports presented by their Actuarial Function Holder. The Board will be informed the society is currently solvent (hopefully), whether it can withstand shocks to solvency in the current year (for some societies) and the key risks it faces over the next five years. In reality though, how much of this information is actually used by societies in the day to day running of their business?**

For some societies the three main reports – the Statutory Valuation, the Financial Condition Report ('FCR') and the Individual Capital Assessment ('ICA') – are seen as a regulatory burden, something to put on file, all done to keep the FSA happy. However, with the introduction of the ICA especially, the FSA is not looking for evidence that the reports have been completed - it wants evidence that they are actually being used.

Each of the three reports brings something different to the table. The Statutory Valuation is very much a snapshot of a society's financial position. It informs the society if it is solvent, provides an analysis of change from one year to the next and highlights the key risks to the society. In spite of this, it does not provide information on how much capital is required to support the key risks or how the society's solvency position may develop in the longer term. This is where the other two reports are so useful.

The FCR provides a society with (usually) a five year projection of its statutory solvency position on a best estimate basis. One of the key aims of the FCR is to describe ways in which remedial action could be taken by a society to reduce any risk to its solvency position. The key risks are identified using stress and scenario testing. However, a common problem is that the FCR is usually produced after a society has developed its business plans. It would be more beneficial if it was an integral part of the business planning exercise and became an interactive exercise between the actuary and the Board / Senior Management.

While the FCR demonstrates the key risks based on subjective stresses, the ICA shows the society how much capital is required to support the risks it faces over the next year on a defined basis – usually the ability to withstand a 1 in 200 year event.

Many societies have a risk register, and a growing number have a risk management committee. However, feedback from the FSA suggests that very few societies discuss the results of their ICA at committee meetings or use them to develop their risk register. This is the area where the FSA would most like to see societies use their reports more fully. The information provided by an ICA can be useful to a society in a whole number of ways. Using the five main risk categories in an ICA as examples it can show:

- The effect of demonstrating tighter expense controls (Insurance risk)

- The change in capital due to introducing a new reinsurance strategy (Credit & Insurance risk)
- The risk of increasing equity holdings (Market risk)
- The benefits / risks of introducing a new IT system (Operational risk)
- The effect of closer matching of liability cashflows (Market, Liquidity & Credit risk)

The FSA is keen to see a society's ICA as an integral part of its risk management framework and for societies to develop their own risk appetites. In our experience it is vital that, when instilling a risk framework in an organisation, the attitude to risk is developed and championed by the Board. Once framed, the risk appetite should then be cascaded down through the organisation in such a way that day to day staff on the "front line" act in a manner consistent with the principals and aims laid down by the Board. It is important here that the Board actually "walks the walk" and actively encourages adoption throughout the company rather than merely paying lip service to the risk framework.

Societies should actively look to integrate all the reports presented by their Actuarial Function Holder into the day to day running of their business. In our experience, a clear tangible benefit is a reduced capital requirement, but the society should view the most important benefit as an improvement to risk management processes. All of this allows those societies that embrace these reports to benefit from the increased regulatory reporting requirement rather than be burdened by it.

- The change in capital due to introducing a new reinsurance strategy (Credit & Insurance risk)

**by Courtney Marsh (Oliver Wyman)**