Institute and Faculty of Actuaries

CP10/18: Updates to internal model output reporting

IFoA response to the Prudential Regulation Authority

13 July 2018

About the Institute and Faculty of Actuaries

The Institute and Faculty of Actuaries is the chartered professional body for actuaries in the United Kingdom. A rigorous examination system is supported by a programme of continuous professional development and a professional code of conduct supports high standards, reflecting the significant role of the Profession in society.

Actuaries' training is founded on mathematical and statistical techniques used in insurance, pension fund management and investment and then builds the management skills associated with the application of these techniques. The training includes the derivation and application of 'mortality tables' used to assess probabilities of death or survival. It also includes the financial mathematics of interest and risk associated with different investment vehicles – from simple deposits through to complex stock market derivatives.

Actuaries provide commercial, financial and prudential advice on the management of a business' assets and liabilities, especially where long term management and planning are critical to the success of any business venture. A majority of actuaries work for insurance companies or pension funds – either as their direct employees or in firms which undertake work on a consultancy basis – but they also advise individuals and offer comment on social and public interest issues. Members of the profession have a statutory role in the supervision of pension funds and life insurance companies as well as a statutory role to provide actuarial opinions for managing agents at Lloyd's.

Institute and Faculty of Actuaries

CP10/18
Rachel Evans
Prudential Regulation Authority
20 Moorgate
London
EC2R 6DA

13 July 2018

Dear Rachel,

IFoA response to Consultation Paper CP10/18: Updates to internal model output reporting

1. The Institute and Faculty of Actuaries (IFoA) welcomes the opportunity to respond to the PRA's consultation paper (CP) on updates to internal model output reporting. Our General Insurance Standards and Consultations Committee and Board have both been involved in the drafting of this response. Members of the Committee and Board are heavily involved in the production and review of insurers' internal models, including for Lloyd's syndicates.

2. We would note that we broadly agree with the PRA's proposals for internal model outputs. We do however have some feedback on the separate discussion point relating to catastrophe risk, which we hope the PRA find useful.

Internal model outputs reporting

3. We welcome the PRA's proposals to reduce the overall scope of output reporting for internal models, and acknowledge that the changes should help increase the proportionality of the requirements. We note that the proposals include a small number of additional requirements. Here, we anticipate that some firms may have difficulties reporting sums insured at aggregate level, but it may be possible for firms to agree an appropriate workaround with the PRA, specific to their circumstances.

Discussion point: man-made catastrophe losses

4. The IFoA agrees with the PRA that cyber and terrorism risks are likely to increase in materiality over time. In the CP, two alternative approaches to splitting catastrophe losses are suggested:

    - requesting a split of catastrophe losses in the short term, to avoid the need for subsequent changes; or
    - deferring the need to split catastrophe losses until increased prominence of cyber/ terrorism losses warrants it.

5. We favour the latter option. This avoids the need for firms to split catastrophe losses in the short term. Adopting a 'wait and see' approach would also reduce the risk that a further re-design of requirements would be necessary, should it be realised in a few years' time that a less useful level of detail were captured by the first change.

6. We also suggest that the PRA bear in mind the diversity of the market when considering the future evolution of reporting of emerging risks. In the event that more granular catastrophe

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loss reporting were subsequently deemed necessary, then a proportionate approach would be to require additional segmentation only for material risks for each firm, as opposed to prescribed fixed risk categories for all firms.

7. In addition, more granular reporting should only be required for risk components which exceed a PRA-specified materiality threshold in the context of overall insurance risk. This approach would be more likely to align with firms' own modelling (and therefore reporting capability) and may encourage more meaningful modelling of risk components where they are both market issues and material.

Should you wish to discuss any of the points raised in further detail please contact Steven Graham, Technical Policy Manager (steven.graham@actuaries.org.uk / 0207 632 2146) in the first instance.

Yours sincerely

Marjorie Ngwenya

Immediate Past President
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