

EXAMINATION

26 May 2014

Subject F203 — General Insurance Specialist Applications

Time allowed: Three hours

INSTRUCTIONS TO THE CANDIDATE

1. *Candidates will be issued with instructions to log-in using a password (which you will be provided with at the exam center).*
2. *Candidates are required to submit their answers in Word format only using the template provided.*
3. *Save your work continuously throughout the exam, on your computers' hard drive that you have been provided.*
4. *You have 15 minutes at the start of the examination in which to read the questions. You are strongly encouraged to use this time for reading only, but notes may be made. You then have three hours to complete the paper.*
5. *You must not start typing your answers until instructed to do so by the invigilator/supervisor.*
6. *Mark allocations are shown in brackets on exam papers.*
7. *Attempt both questions, beginning your answer to each question on a new page.*
8. *Candidates should show calculations where this is appropriate.*

Note: The Actuarial Society of South Africa will not be held responsible for loss of data where candidates have not followed instructions as set out above.

AT THE END OF THE EXAMINATION

Save your answers on the hard drive.

In addition to this paper you should have available the 2002 edition of the Formulae and Tables and your own electronic calculator from the approved list.

QUESTION 1

You are an actuary employed by Ahead Ltd., a large South African short-term insurance company offering a breadth of personal and commercial lines cover. Ahead Ltd. is considering creating a cyber liability insurance product and has asked for your assistance with this.

- i) Outline the typical risks that would be covered under a cyber liability product. [9]
- ii) List potential clients that would be interested in cyber liability cover. [3]

The Chief Underwriting Officer (CUO) has provided the following information:

- At the launch of this product the company will accept up to R30 million of net risk on each individual policy.
- The company can choose one of the following business models:
 - a. Reinsure with a well-known Lloyd's syndicate specialising in cyber liability insurance products. Under this arrangement the syndicate will provide full underwriting and claims management as well as technical support to launch the product.
 - b. Recruit and appoint a well-known experienced cyber liability underwriter from the UK. Under this arrangement the company will have control over underwriting and claims management. Your company's reinsurance broker has affirmed that it will be possible to find reinsurance cover in the market on the condition that the underwriter is appointed.
- iii) Discuss the relative advantages and disadvantages under each model. [24]
- iv) Recommend which business model will be the best approach for the company to follow, giving reasons for your recommendation. [2]

By the first quarter end after launch the company had written 32 annual policies. Each policy was underwritten as R150 million sum insured with a R30 million deductible on a risk excess of loss reinsurance treaty basis.

Three days before the first quarter-end one of the clients reported a claim estimated at R95 million. This is the first and only claim reported on the cyber liability product to that date.

The CUO is very concerned about the impact such a large claim will have on the company's immediate financial position and suggests that "rates should be increased immediately".

- v) Outline the impact of the claim on Ahead Ltd.'s quarter-end technical provisions and discuss the validity of the CUO's suggestion. **[12]**

[Total 50]

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QUESTION 2

Springbok Insurance is a South African short-term insurer writing mainly personal lines business to the retail market via brokers. Springbok's market share has been decreasing and they are considering diversifying the selling of their existing products from the single distribution channel.

- i) List the alternative distribution channels that Springbok could consider and discuss the potential impact of moving to each channel, including regulatory requirements. [26]

You have received the following in an email from the Financial Director:

"I have been thinking about our previous discussion to diversify distribution channels. Maybe as an alternative we should be more client-focused and change the brokers' remuneration structure? Instead of paying the maximum commission by default, the onus should be on the broker to negotiate commission with the client. Reduced commission will improve our competitiveness and thereby increase our market share."

- ii) Discuss what you would include in a debate with the Financial Director on his statement. [8]
- iii) Explain how you would monitor the impact of an alternative commission structure on Springbok's business. [5]

The Financial Director's email also contains the following:

"Do you remember Tom Clarke, the new non-executive board member from London? We had a telephone conversation yesterday and he mentioned that South Africa's inflation is much higher than what they are experiencing in the UK. He is concerned that our liabilities might be exposed to inflation risk. He arrives tomorrow to attend the board meeting. I know it is short notice but could you please prepare a "back-of-the-envelope" calculation to present to him?"

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- iv) Explain how you would determine a high-level estimate of the extent of Springbok's exposure to inflation, including any assumptions that may need to be made.

[11]

[Total 50]

TOTAL 100

END OF EXAMINATION