HIH commission falls short on technicals

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In “Actuaries must satisfy high standards” (AFR, November 20, page 67), the president of the Institute of Actuaries Helen Martin, in response to my letter (``HIH debacle reveals monitoring flaws"', AFR, November 15, page 79), does not address many of the substantive issues I raised.

Martin also argued that the actuarial ``profession's capacity to contribute in this field was recognised in the major regulatory changes implemented following the collapse of HIH".

In view of the regulator's acknowledged lack of experience in general insurance, its imprimatur on actuarial contributions and submissions made before and after the HIH collapse means very little, if anything at all.
Furthermore Martin's assertion: ``matters relating to HIH are being appropriately dealt with by the HIH Royal Commission", is transparently mistaken. The commission's investigation of a technical failure is appallingly misguided.

What is perhaps equally disturbing is Tony McGrath's (the HIH liquidator) remark on Channel Nine's Business Sunday (November 24, 2002), ``I think there's a need to ascertain what were the causes of failure", when a special report in Best Week (``P/C insolvency trends continued in 2001", June 24, 2002) published by AM Best Company Inc, the eminent US insurance rating agency, asserts: ``Inadequate reserves, improper pricing and unsustainable growth levels were by far the most significant causes of the 2001 insolvencies".

Moreover, would it not have been the responsibility of the Institute of Actuaries, the two actuaries advising the commission and the actuary advising the liquidator to announce the unassailable contentions listed below, on the first day (or even before) the commission convened?

The root cause of the HIH collapse was chronic and massive under-reserving.
The exponential snowballing failure in progress for over 10 years was easily detectable from, inter alia, the high current to total liability ratios of 40 per cent, 38 per cent and 39 per cent reported by HIH in its 1996, 1997 and 1998 financial accounts respectively.

A company writing long tail liabilities can be woefully under-reserved and still be cash flow positive for many years before running out of cash abruptly.
The so-called $5.3 billion ``loss" did not disappear, was not spent, is a ``non-cash" item, accrued over the last 25 years and largely represents premiums (revenue) not collected from the long tail liability policyholders.

The HIH type failure was part of a global phenomenon in insurance that is still continuing. HIH was not a One.Tel, WorldCom or Enron type failure, where the key issue was corporate malfeasance.
Instead, advice by actuaries to the royal commission, including the 2001 president of the IAA and the actuary for the liquidator, are at odds with the unique risk properties of long tail liabilities.