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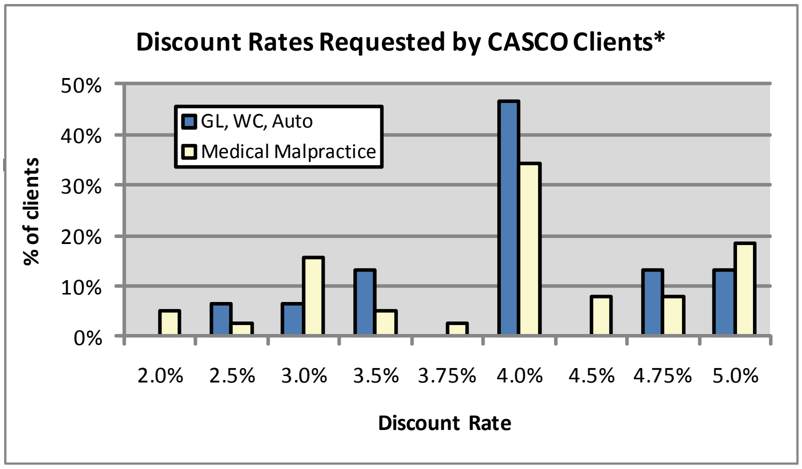
- GL, WC, and Auto discount rates requested by CASCO university clients currently range from 2.5% to 5.0%.
- Medical Malpractice discount rates currently range from 2.0% to 5.0%.

Ask the Actuary: Discount Rates

For insurance companies, risk retention groups, and self-insured programs, discounting of loss and loss adjustment expense reserves is required under GAAP and tax-basis accounting and sometimes permitted under statutory accounting. The rules for discounting under tax-basis accounting are issued by the IRS in very specific terms. For GAAP and statutory accounting, however, the guidance on discounting is more general in nature, and this has led to varying practices, as shown below for our university and healthcare entity clients. Actuaries provide input, but management selects the final discount rate after discussions with regulators and outside auditors.



*University and healthcare entities.

Q: What is an appropriate rate to use for discounting loss and loss adjustment expense outstanding liabilities?

For property and casualty liability discounting, auditors and regulators usually prefer using a “risk-free” rate of return. Generally, risk-free rates are approximated by yields on low-risk investments, such as U.S. Treasuries, with maturities close to the projected average payout duration of the outstanding liabilities being valued. Recent Treasury yields are shown below. The average payout duration varies by line of coverage. Lines such as workers’ compensation and medical malpractice have a longer payout duration than auto or general liability, and a much longer payout duration than property lines.

Recent Treasury Yield Curve Rates

	Maturity			
	1 year	3 years	5 years	10 years
July 30, 2010	0.29%	0.84%	1.60%	2.94%
August 31, 2010	0.25%	0.72%	1.33%	2.47%
September 30, 2010	0.27%	0.64%	1.27%	2.53%

Ask the Actuary:
Discount Rates (continued)

The choice of a discount rate for self-insured workers' compensation liabilities involves additional consideration and discussion, due to that line's similarities with two employee benefit areas: disability and medical benefits. Discount rate selections for those lines tend to be more consistent with the GAAP rules for pension and post-retirement benefits accounting (adjusting for any duration differences), where the selected rates are generally pegged to "high-quality" fixed-income securities whose yields are normally higher than those of "risk-free" securities such as U.S. Treasuries. Recent yields from the Citigroup Pension Discount Curve (a commonly used measure of average yields for high-quality fixed-income securities) are shown below.

Recent Yields for High-Quality Fixed-Income Securities *

	Maturity			
	1 year	3 years	5 years	10 years
July 31, 2010	1.16%	1.73%	2.73%	4.75%
August 31, 2010	1.09%	1.60%	2.48%	4.33%
September 30, 2010	1.01%	1.48%	2.39%	4.37%

* Based on the Citigroup Pension Discount Curve.

The discounting of loss and loss adjustment expense reserves in various financial reporting contexts is subject to different guidelines and widely varying practices. Currently, the International Accounting Standards Board (IASB) and the U.S. Financial Accounting Standards Board (FASB) are in the process of developing a single converged insurance standard. This standard would replace current U.S. GAAP and International Financial Reporting Standards (IFRSs) for entities that issue contracts containing insurance risk. The proposals require that cash flows be discounted at risk-free interest rates.

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