COMPLETE ACTUARIAL SOLUTIONS COMPANY

The CASCO Bulletin

ISSUE I

4TH QUARTER 2010

Medicare Gets Tough

Recent actions by the Centers for Medicare/Medicaid Services (CMS) suggest that Medicare is increasing its enforcement of the Medicare Secondary Payer Act (MSP Act). Under the act, CMS can recoup medical expenses paid from parties "responsible" for paying the cost of injuries suffered by claimants. In December 2009, CMS filed a first-of-its-kind lawsuit against defendants, insurers, plaintiffs, and plaintiffs' attorneys in the case of a large 2003 Alabama pollution liability claim, as reported in the January 18, 2010 issue of Business Insurance. CMS also recently sought reimbursement from a CASCO client for costs related to a medical malpractice claim. Actions such as these, as well as other recent anecdotal evidence, suggest that CMS is enforcing the MSP Act more aggressively.

Beginning January 1, 2011, in an effort to eliminate payments that are subject to the MSP Act, CMS is implementing stricter reporting requirements for insurers and self-insurers relating to potentially Medicare-eligible claimants. Information on reporting and other requirements can be found on the CMS website.

Actuarial Perspective

From an actuarial perspective, issues raised by increased enforcement of the MSP Act include:

Claim frequency - The extent to which CMS successfully steers Medicare-eligible patients who have potential causes of action under workers' compensation or liability claims towards filing such claims will affect claim frequency.

Claim severity - Claims with significant medical expenses may be affected for a number of reasons. Claimants may be reluctant to settle and/or hold out for higher settlements as a result of the increased involvement of CMS. Also, insurers and self-insurers will likely be less inclined to pursue settlements due to a combination of CMS involvement and the uncertainty in projecting future medical expenses. CMS guarding against under-projection of future medical expenses will reduce the benefits to insurers and self-insurers of early settlement.

Actuaries need to pay close attention to the emerging loss trends and maintain clear lines of communication with our clients to understand their potential exposure to changes in claim frequency and severity considering the line of coverage and the applicable laws and statutes .

Adjustments to historical patterns - Historical patterns provide actuaries with an important tool for making projections. Changes in claim frequency, potential settlement amounts, rates of claim closure, and Medicare reimbursement levels may cause changes in these patterns that need to be taken into account.

INSIDE THIS ISSUE:

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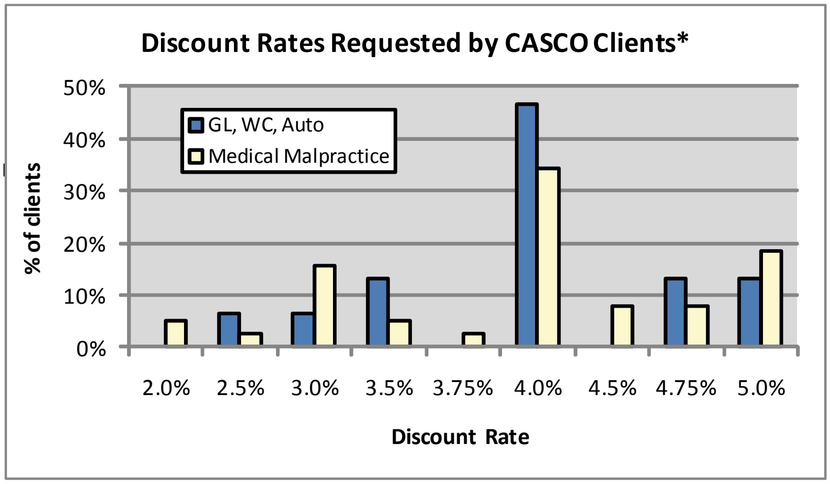
- GL, WC, and Auto discount rates requested by CASCO university clients currently range from 2.5% to 5.0%.
- Medical Malpractice discount rates currently range from 2.0% to 5.0%.

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.

Market Focus

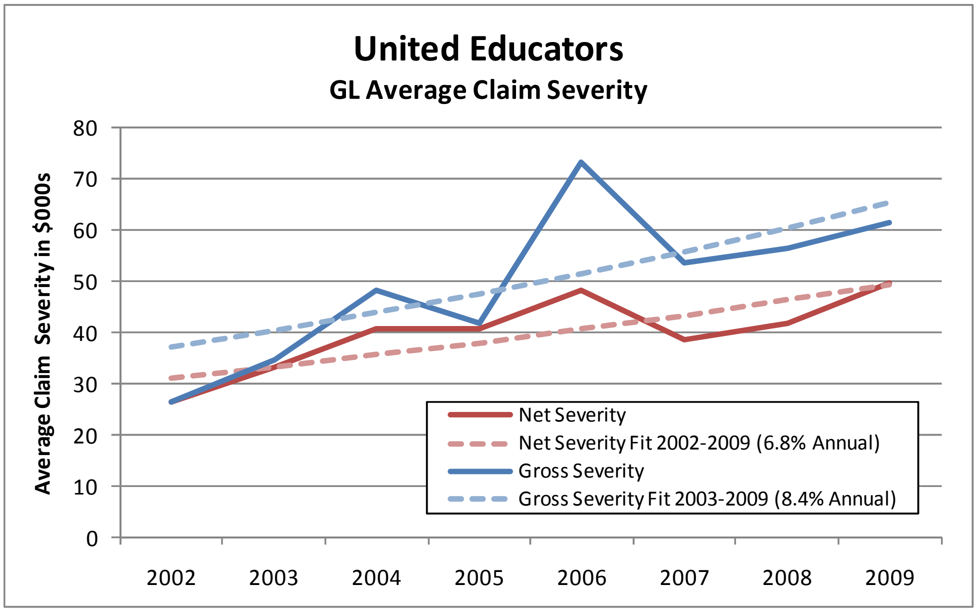
In this issue, we show results for the largest risk retention group in the education sector.

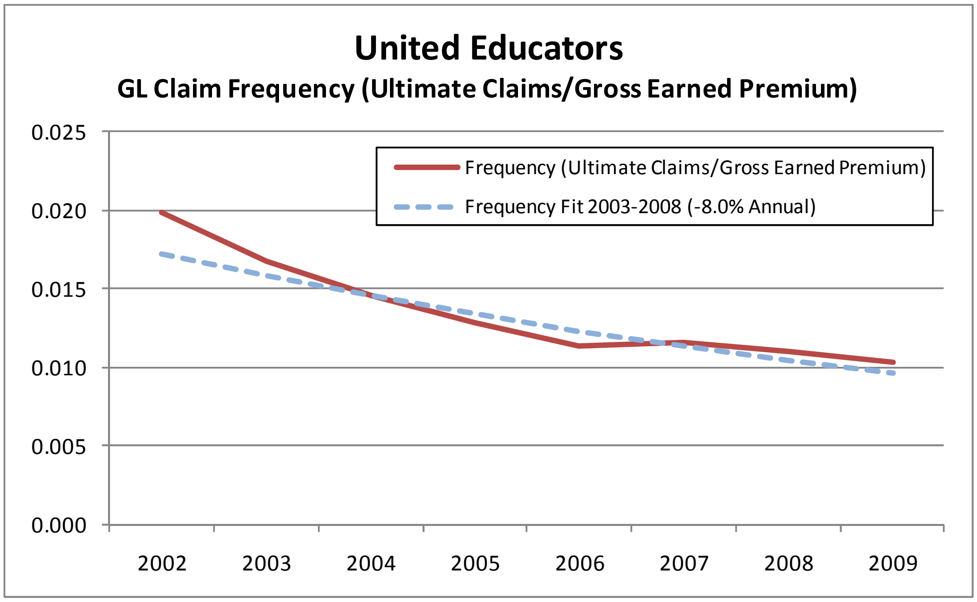
UE's GL results

- Claim Severity has been increasing at a rate of about 7%-8% annually.
- Frequency relative to premium has been decreasing by about 8% annually.
- Net loss ratios have been fairly stable.
- Net underwriting ratios have increased over the last five years.

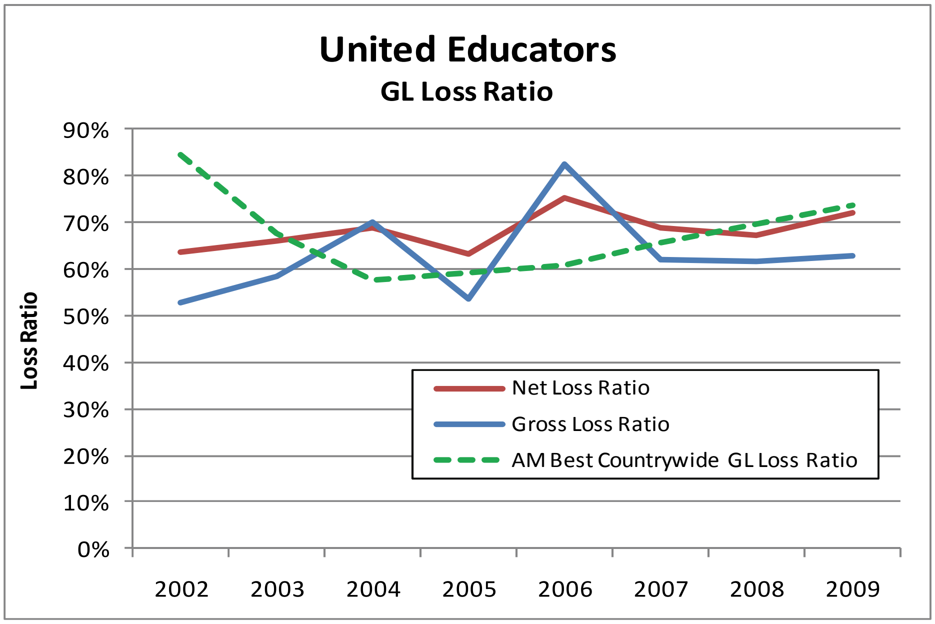
Market Focus: United Educators

United Educators (UE) is a Vermont-based risk retention group insuring over 1,000 universities and other educational institutions. UE's general liability (GL) average claim severity, claim frequency, and loss ratios for the last eight coverage years, and underwriting and operating ratios for the last five years, are shown below. This information is based on their most recent publicly filed annual statement, a copy of which can be obtained from the National Association of Insurance Commissioners.





Market Focus:
United Educators (continued)



United Educators Financial Results

	2005	2006	2007	2008	2009
Net Underwriting Ratio (Excl. Investment Income)	89.2%	89.4%	91.7%	92.7%	95.5%
Net Operating Ratio (Incl. Investment Income)	76.1%	60.7%	71.2%	70.6%	72.1%

Interesting Articles

Impact of Health Care Reform on Medical Professional Liability
The health care reform law, signed by President Barack Obama on March 23, 2010, could potentially have a positive effect on medical malpractice liability, actuaries were told at the Casualty Actuarial Society (CAS) seminar on reinsurance.

Legal System Changes Affecting the General Liability Environment
Substantial changes in the U.S. legal system over the past decade should make the country's tort system more manageable and predictable, a panel on litigation told attendees at the CAS spring meeting.

Reinsurers Face Pricing Pressure
Reinsurers face pressure to lower rates and expand coverage after the industry enjoyed one of its most profitable underwriting years in nearly a decade in 2009, according to a panel of senior reinsurance executives speaking at the CAS seminar on reinsurance.

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About CASCO

We provide ongoing actuarial services to over 100 clients in several areas:

- Professional and General Liability
- Directors' & Officers' Liability
- Workers' Compensation
- Automobile Liability
- Managed Care Errors & Omissions
- Medical Benefits Stop Loss Risk
- Disability Benefits

We help clients with:

- Annual funding/pricing analyses
- Liability and cost projections for accounting and budgeting
- Formal opinions and reports to meet regulatory and audit needs
- Communication with auditors, regulators, and excess insurers
- Other regulatory or administrative problems
- Impact analysis of judicial/law changes affecting program costs
- Strategic risk financing studies
- Retention limit analysis (single and multi-line)
- Internal cost allocation
- Pro-forma projections of program results under varying scenarios
- Cash-flow forecasts to help in setting investment strategy
- Evaluation of insurance products
- Projecting costs for acquisitions and new ventures
- Expert witness testimony
- Benchmarking data on loss costs, trends, retention limits, and more

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