



AMERICAN ACADEMY *of* ACTUARIES

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March 30, 2017

Lyn Asio Booz, Chief
Office of Self Insurance Plans
Department of Industrial Relations
State of California
Sent via email

Re: Informational Bulletin: Notice to Actuaries Submitting Actuarial Summaries and Studies for Private Self-Insured Employers

Dear Ms. Asio Booz:

The Workers' Compensation Committee of the American Academy of Actuaries¹ offers the following observations and recommendations regarding the Informational Bulletin referenced above. We appreciate your willingness to consider input in this regard.

The committee understands the need to establish appropriate collateral requirements for self-insured employers. We understand the role and importance that actuarial studies play in maintaining sufficient collateral requirements. Actuaries are uniquely qualified to provide meaningful and thorough analysis in this area. We also appreciate the need for the Department of Industrial Relations Office of Self Insurance Plans (OSIP) and the Self Insurers' Security Fund (SISF) to use the findings in the actuarial summaries and studies that are submitted and the need to retain consultants to assist in carrying out the requirements of 8 Cal. Code Regs. Section 15209 (the Regulation).

The overwhelming concern is that the Informational Bulletin appears to add requirements beyond those found in the Regulation, particularly in the area of reliance by, and the duty to, third parties. The items of concern are found in the third paragraph of the Informational Bulletin.

Actuaries who are members of the U.S.-based professional organizations² are bound by the Code of Professional Conduct promulgated by the American Academy of Actuaries³ to act honestly,

¹ The American Academy of Actuaries is a 19,000-member professional association whose mission is to serve the public and the U.S. actuarial profession. For more than 50 years, the Academy has assisted public policymakers on all levels by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States.

² The American Academy of Actuaries, the Casualty Actuarial Society, the Conference of Consulting Actuaries, the Society of Actuaries, and ASPPA College of Pension Actuaries.

³ The Code of Professional Conduct contains 14 precepts, many of which include annotations.

with integrity and competence.⁴ They must take appropriate steps to ensure that their actuarial communications, such as the actuarial communications that may be included in studies and summaries submitted to the OSIP, are clear and use language that is appropriate to particular circumstances, taking into account the intended users.⁵ They have a professional, and often contractual, responsibility to the principal (e.g., the self-insured employer) to cooperate with others (e.g., OSIP and SISF)⁶ in the principal's interest and to do so in a manner that fulfills the profession's responsibility to the public.⁷ They must also take reasonable steps to ensure that their work product is not used to mislead other parties.⁸ More specifically, actuaries submitting studies and summaries to OSIP and SISF on behalf of a self-insured employer have an obligation to provide sound actuarial work, to refrain from providing actuarial services "if the Actuary has reason to believe that such services may be used to violate or evade the Law,"⁹ and, as required by law or regulation, to cooperate with OSIP, SISF, and/or consultants retained by OSIP or SISF to carry out their regulatory duties. This obligation does not automatically go beyond the intended users of an actuary's work product, such as OSIP, SISF, and their retained consultants. For this reason, actuarial reports often specify those for whom there is an obligation and those for whom there is none.

The Regulation is clear in its specification of the entities that must use the actuarial studies and summaries, and the purpose for that use. It also provides language that should appear in these actuarial work products. With these considerations in mind, we respectfully recommend the following changes to the Informational Bulletin:

1. Reword the third paragraph of the bulletin, starting with "Actuarial reports..." so it more closely aligns with the Regulation.
 - a. Replace the first and second sentences with language that closely follows the language found in sections (e) and (f) of the Regulation: *An actuarial report and summary submitted under these regulations must specify that it is prepared for use by the Department of Industrial Relations, Office of Self-Insurance Plans and the Self-Insurers' Security Fund, and that they may share the study and report with consultants retained by the Department of Industrial Relations or the Self-Insurers' Security Fund for official purposes in accomplishing the purposes of 8 Cal. Code Regs. Section 15209. The actuary shall also declare that the study and report may be used by the State of California and the Self-Insurers' Security Fund to set appropriate collateral and deposit amounts, and for any other regulatory purpose under 8 Cal. Code Regs. Section 15209.*
 - b. Add third and fourth sentences: *Actuarial reports must not contain disclaimers or disclosures that limit the distribution and use described in 8 Cal. Code Regs. Section 15209(e) and (f). Such limitations may cause the summary and study to be rejected and the retention of another qualified actuary, at the self-insurer's*

⁴ Precept 1.

⁵ Actuarial Standard of Practice (ASOP) No. 41, Section 3.1.2.

⁶ Precept 10.

⁷ Precept 1.

⁸ Precept 8. See also Annotation 8-1: "The Actuary should recognize the risks of misquotation, misinterpretation, or other misuse of the Actuarial Communication and should therefore take reasonable steps to present the Actuarial Communication clearly and fairly and to include, as appropriate, limitations on the distribution and utilization of the Actuarial Communication." See also ASOP No. 41, Section 3.7.

⁹ Precept 1, Annotation 1-2.

expense, to provide a second study and summary that does fully satisfy the requirements of 8 Cal. Code Regs. Section 15209.

2. To further the instructional nature of the bulletin, it would be helpful to modify the fourth paragraph to add the specific results that are required:

As required by 8 Cal. Code Regs. Section 15209 (b), the actuarial study shall provide the self-insurer's losses at the undiscounted "expected level," also commonly referred to as the undiscounted "actuarial central estimate." The actuarial central estimate must be reported at both the gross and net amounts of excess insurance values, and must include each of the following components:

- 1) Incurred but not reported (IBNR) liabilities,*
- 2) Allocated loss adjustment expense (ALAE),*
- 3) Unallocated loss adjustment expense (ULAE), and*
- 4) Case reserves*

Where there is excess insurance, the actuarial study must clearly identify any excess coverage by carrier and policy year and provide the excess retentions by year.

To facilitate your review of the above suggestions, we have attached a mock-up of the Informational Bulletin with these proposed changes.

The committee appreciates the opportunity to provide input to the OSIP regarding this Informational Bulletin. We would be happy to discuss any of the issues raised in this letter at your convenience. Please contact Marc Rosenberg, senior casualty policy analyst, at 202-785-7865 if you have any questions or would like to discuss this further.

Sincerely,

John R. Pedrick, MAAA, FCAS
Chairperson, Workers' Compensation Committee
American Academy of Actuaries

Attachment: mark-up of bulletin

Informational Bulletin:

Notice to Actuaries Submitting Actuarial Summaries and Studies for Private Self-Insured Employers

Under 8 Cal. Code Regs. Section 15209(a), actuarial studies and summaries are due to OSIP from active and former private self-insurers no later than May 1, 2017. Under the electronic filing platform, copies of these summaries and studies are simultaneously transmitted to the Self-Insurers' Security Fund. These required summaries and studies are expressly relied upon by OSIP and the Self-Insurers' Security Fund to determine collateral requirements and assessments.

Pursuant to 8 Cal. Code Regs. Section 15209(e), "[t]he actuary shall declare in the study and the summary that the study and report may be used by the State of California and the Self-Insurers' Security Fund to set appropriate collateral and deposit amounts, and for any other regulatory purpose under these regulations." Further, "[t]he actuarial study and summary shall specify that it is prepared for use by the Department of Industrial Relations, Office of Self Insurance Plans and the Self Insurers' Security Fund. The Office of Self Insurance Plans and the Self Insurers' Security Fund may share the study and report with consultants retained by the Department of Industrial Relations or the Self Insurers' Security Fund for official purposes in accomplishing the purposes of these regulations." 8 Cal. Code Regs. Section 15209(f).

An actuarial report and summary submitted under these regulations must specify that it is prepared for use by the Department of Industrial Relations, Office of Self-Insurance Plans and the Self-Insurers' Security Fund and that they may share the study and report with consultants retained by the Department of Industrial Relations or the Self-Insurers' Security Fund for official purposes in accomplishing the purposes of 8 Cal. Code Regs. Section 15209. The actuary shall also declare that the study and report may be used by the State of California and the Self-Insurers' Security Fund to set appropriate collateral and deposit amounts, and for any other regulatory purpose under 8 Cal. Code Regs. Section 15209. Actuarial reports and summaries submitted under these regulations must not contain ~~this required language, and MUST NOT contain other~~ disclaimers or disclosures that limit the distribution and use described in 8 Cal. Code Regs. Section 15209 (e) and (f). Such limitations may cause the summary and study to be rejected and the retention of another qualified actuary, at the self-insurer's expense, to provide a second study and summary that does fully satisfy the requirements of 8 Cal. Code Regs. Section 15209.

~~are contradictory or inconsistent with this required language. For example, standard actuarial disclaimers prohibiting all third party distribution, stating that the reports cannot be relied upon by third parties other than the client, or declaring that nothing in the report may create a legal duty to any third party recipient, will not be allowed and may cause the summary and study to be rejected by OSIP. Such disclaimers are permissible only if OSIP and the Self Insurers' Security Fund are expressly excluded from them.~~

As required by 8 Cal. Code Regs. Section 15209 (b), the actuarial study shall provide the self-insurer's losses at the undiscounted "expected level," also commonly referred to as the undiscounted "actuarial central estimate." The actuarial central estimate must be reported at both the gross and net amounts of excess insurance values, and must include each of the following components:

- 5) Incurred but not reported (IBNR) liabilities,
- 6) Allocated loss adjustment expense (ALAE),
- 7) Unallocated loss adjustment expense (ULAE), and
- 8) Case reserves

Where there is excess insurance, the actuarial study must clearly identify any excess coverage by carrier and policy year and provide the excess retentions by year.

~~Under 8 CCR section 15209, actuaries must provide both a study and a summary containing an actuarial central estimate. Per the regulations, “[t]he actuarial central estimate shall be reported at both the gross and net amounts of excess insurance values.” Where there is excess insurance, “(d) The actuarial study and summary shall clearly identify any excess coverage by carrier, policy year and self-insured retentions, by year.”~~

Please note that while self-insurers may maintain specific excess workers' compensation coverage and/or aggregate stop loss insurance, only specific excess workers' insurance may be credited toward their security deposit requirement. Aggregate stop loss policies, risk transfer agreements not approved by the DIR, and similar arrangements cannot be used to reduce actuarial central estimate. In the actuarial central estimate, only specific excess workers compensation may be used to reduce gross liabilities to net liabilities.

It is important that all actuaries understand the type of policies held by the self-insurer.

All actuarial reports submitted to OSIP go through an extensive review process. In the event an actuarial study and summary is rejected, OSIP may require a second study and summary that does conform with the regulatory requirements be prepared and submitted by another qualified actuary at the self-insurers' expense. 8 Cal. Code Regs. Section 15209(i). Unless a corrected conforming study and summary is timely submitted, the self-insurer may be subject to adverse regulatory action, including but not limited to revocation of its Certificate of Consent to Self-Insure and/or imposition of a higher assigned collateral requirement in the discretion of OSIP. Additionally, the Self-Insurers' Security Fund may downgrade or exclude the self-insurer from participation in the Alternative Security Program ("ASP") and/or assess additional fees based on a higher collateral requirement.