



AMERICAN ACADEMY of ACTUARIES

October 8, 2010

Technical Director
Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

Re: File Reference No. EITF100F
Proposed Accounting Standards Update, *Health Care Entities (Topic 954) – Accounting for Legal Costs Associated with Medical Malpractice and Similar Claims*

The Financial Reporting Committee of the American Academy of Actuaries¹ appreciates this opportunity to provide comments to the Financial Accounting Standards Board (FASB) concerning File Reference No. EITF100F, a proposed Accounting Standards Update amending Topic 954 (Health Care Entities). Our comments are based on our experience in the actuarial valuation, calculation, and review of reserves for unpaid malpractice claim liabilities for health care entities. We address two of the five Questions for Respondents posed in the exposure document, as well as one additional issue that surfaced during our review of the exposure document.

Question 1. *Do you agree that health care entities should be permitted to make an accounting policy election to determine whether to accrue or expense as incurred legal fees associated with malpractice claims? Are there factors unique to the defense of malpractice claims that warrant the accrual of legal fees before those fees are incurred?*

No, we do not agree that a policy election should be permitted. The losses for incurred malpractice claims are inextricably linked to the legal expenses incurred in defending such a claim. Some companies may choose a strategy to defend claims vigorously and incur greater legal expenses in return for an expected lower loss payment. Other companies may elect to settle claims as soon as possible, incurring fewer legal expenses but higher loss payments. Overall both companies may have the same expected total payments, yet under the proposed change one company could show a lower liability than the other on their balance sheet due solely to accounting policy elections.

Therefore, in order for users of the financial statements to gain a complete picture of the cost of incurred medical malpractice claims and provide comparability between medical institutions, we believe institutions should continue to be required to accrue legal fees for incurred claims.

¹ The American Academy of Actuaries (“Academy”) is a 17,000-member professional association whose mission is to serve the public on behalf of the U.S. actuarial profession. The Academy assists 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.

Question 2. *Do you believe the requirements should be different for the treatment of internal and external legal costs? If yes, how should they be different and why?*

We do not believe the treatment should be different for internal and external legal expenses, for reasons similar to those given in our answer to Question 1.

Additional Issue. We noted with interest the following sentence from page 1 of the exposure document, under the heading “Who Would Be Affected by the Amendments in This Proposed Update?”

“An entity within the scope of Topic 944, Financial Services—Insurance, would apply the amendments in the proposed Update to only its health care activities and would continue to follow Subtopic 944-40 for claims related to its insurance activities.”

This sentence could be viewed as indicative of a broader point of view that, in situations where it is unclear whether to apply guidance from Topic 944 (historically, FAS 60 et al) or guidance from Topic 954 (historically, the AICPA Health Care Organizations Audit Guide), the Topic 954 guidance is intended to take precedence.

Members of our committee who practice in the health insurance sector have occasionally expressed confusion in the past over this point, specifically with respect to corporate entities not explicitly listed in either Topic 944-10-15-2 or Topic 954-10-15-1B. (Many issuers of health insurance contracts are not organized as life insurers or as property & casualty insurers, and hence are not referenced in Topic 944-10-15-2; however, they are also not organized as health maintenance organizations and are not in the business of directly providing health services, so they are not referenced in Topic 954-10-15-1B.) To us, this situation reinforces the desirability of providing accounting guidance that is based on the type of obligation, not on the type of corporate entity bearing that obligation. We expect to return to this theme later in 2010 when we provide FASB with comments on its recent *Preliminary Views on Insurance Contracts* Discussion Paper.

Thank you again for this opportunity to comment. If we can be of further assistance, please contact Tina Getachew, the Academy’s Senior Risk Management & Financial Reporting Policy Analyst, at getachew@actuary.org or (202) 223-8196.

Sincerely yours,



Rowen B. Bell
Chair, Financial Reporting Committee
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