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AMERICAN ACADEMY of ACTUARIES

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May 9, 2017

Mr. David Altmaier,  
Chair, Capital Adequacy (E) Task Force  
National Association of Insurance Commissioners (NAIC)  
2301 McGee Street, Suite 800  
Kansas City, Missouri 64108-2662

Re: Calibration of Risk Factors

Dear Mr. Altmaier,

On behalf of the Stop-Loss Factors Work Group of the American Academy of Actuaries<sup>1</sup>, we appreciate the opportunity to offer our response to the comments made by America's Health Insurance Plans (AHIP) in their March 25, 2017 letter to you as the Chair of the National Association of Insurance Commissioners' Capital Adequacy Task Force. The comments were concerning the *Stop-Loss Factors Report* from our work group produced on November 16, 2016.

### **Response to Comment Letter**

#### Issue 1

AHIP writes:

*We request that the Capital Adequacy Task Force return the Academy's Report and ask for a recommendation for factors consistent with a defined level of calibration. We believe that many factors for health insurance have been based on modeling that incorporates a surviving test standard of 95% over two or more years depending on the amount of time regulators may need to address an identified situation. As stop loss coverage is primarily utilized by well-informed [sic] major insurers, we believe two years is a sufficient time period.*

AHIP concludes:

*The latest accumulation of data was deemed usable by the Academy. We believe that the Task Force should ask the Academy to review their work in terms of the calibration standard adopted by the NAIC. It is possible that if a multi-year survival test is required by the NAIC, the Academy may find even this data is not sufficient. It is also possible that*

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<sup>1</sup> 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.

*the Academy may find reasons why the calibration standard is not appropriate for stop-loss coverage. If not, there should be a well-documented [sic] basis for an applicable different survival test standard.*

Our work group addressed the issues of data limitations using a Risk of Ruin model as follows:

The members of the work group considered options such as Monte Carlo and other stochastic analyses and Risk of Ruin calculations. We believe that we did not have enough data to build an appropriate model, given the limited number of contributors and CYs [Calendar Years] of data. We were concerned that any model built would imply a higher level of credibility than was warranted by the data.

## Issue 2

AHIP also wrote:

*The basis for the recommended factors in that report was to match the number of “surviving tests” based on the proposed new factors with the number of surviving tests based on the current factors which appears to be around 98%.*

The work group’s position is that this method was used because the current factor produced an acceptably low number of adverse results. If there had been a larger number of adverse results, it is possible that higher factors would have been proposed to reduce the failure rate to a level the work group believed reasonable. The work group’s recommended factors were developed using informed judgment, not applying a standard of 98% survival.

## **Additional Comments**

We would like to re-emphasize two points in the *Stop-Loss Factors Report*:

1. The report makes a convincing demonstration that the smaller the block of business, the more variable the block’s results, suggesting tiered factors varying by premium volume are more appropriate than today’s flat factor.
2. There is added volatility not captured in the data due to the unlimited annual and lifetime maximums now required by the Affordable Care Act.

Notwithstanding the data limitations and the consequent inappropriateness of undertaking a multi-year survival test, the work group believes that the tiered Stop-Loss factors recommended in the report are reasonable and not inconsistent with the defined level of calibration used in reports relating to other health products. (The recommended factors are 35% of the first \$25,000,000 in annual premium, 25% of the annual premium in excess of \$25,000,000.)

The work group further believes it would be best if 2014 and subsequent experience data (post-ACA elimination of annual and lifetime maximums) were collected and used to model Stop-Loss

factors on the same basis as other health coverage. We would be available to work with the NAIC on that effort.

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We appreciate the opportunity to provide these comments. If you have any questions or would like to discuss further, please contact David Linn, the Academy's health policy analyst, at 202-785-6931 or [linn@actuary.org](mailto:linn@actuary.org).

Sincerely,

David Olsho, MAAA, FSA  
Chairperson, Stop-Loss Factors Work Group  
American Academy of Actuaries