



ACTUARIAL STANDARDS BOARD

**Actuarial Standard
of Practice
No. 28**

**Compliance with Statutory Statement of
Actuarial Opinion Requirements for
Hospital, Medical, and Dental Service or Indemnity Corporations,
and for Health Maintenance Organizations**

**Developed by the
Health Committee of the
Actuarial Standards Board**

**Adopted by the
Actuarial Standards Board
April 1997**

Updated for Deviation Language Effective May 1, 2011

(Doc. No. 146)

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May 1997

TO: Members of Actuarial Organizations Governed by the Standards of Practice of the Actuarial Standards Board and Other Persons Interested in Statutory Statement of Actuarial Opinion Requirements for Hospital, Medical, and Dental Service or Indemnity Corporations, and for Health Maintenance Organizations

FROM: Actuarial Standards Board (ASB)

SUBJ: Actuarial Standard of Practice No. 28

This booklet contains the final version of Actuarial Standard of Practice (ASOP) No. 28, *Compliance with Statutory Statement of Actuarial Opinion Requirements for Hospital, Medical, and Dental Service or Indemnity Corporations, and for Health Maintenance Organizations.*

Background

This standard is a revised and reformatted version of Financial Reporting Recommendation (FRR) 10, *Statement of Actuarial Opinion for Health Service Corporation Statutory Annual Statements*. The reformatting was done to conform to the revised uniform format for actuarial standards of practice adopted by the ASB in 1996. FRR 10 offered guidance to actuaries providing statutory statements of actuarial opinion for health service corporations. FRR 10 followed the Instructions to the 1983 National Association of Insurance Commissioners (NAIC) Blank for Hospital, Medical, and Dental Service or Indemnity Corporations and the NAIC Blank for Health Maintenance Organizations.

This standard is based on the current versions of the above two Blanks, and it provides more detailed and comprehensive guidance than that provided in FRR 10. Note, as well, that this standard entirely replaces FRR 10.

Exposure Draft

The revising and reformatting of FRR 10 were completed by the Health Committee of the ASB, which also approved the proposed standard for submission to the ASB. The ASB reviewed the draft at the July 1996 meeting and approved its exposure. The standard was exposed for review in August 1996. Two comment letters were received. The committee considered the comments carefully. For a detailed discussion of the issues raised in the comment letters, and the committee's responses to such, please see appendix 2.

The Health Committee thanks those who provided input during the exposure process. The ASB voted in April 1997 to adopt the final standard.

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**ACTUARIAL STANDARD
OF PRACTICE
NO. 28**

**COMPLIANCE WITH STATUTORY
STATEMENT OF ACTUARIAL OPINION
REQUIREMENTS FOR HOSPITAL, MEDICAL, AND
DENTAL SERVICE OR INDEMNITY CORPORATIONS,
AND FOR HEALTH MAINTENANCE ORGANIZATIONS**

STANDARD OF PRACTICE

Section 1. Purpose, Scope, Cross References, and Effective Date

- 1.1 Purpose—This actuarial standard of practice delineates the responsibility of the actuary in signing the type of statement of actuarial opinion that is described in the Instructions to the National Association of Insurance Commissioners (NAIC) Blank for Hospital, Medical, and Dental Service or Indemnity Corporations (HMDI Blank), and the NAIC Blank for Health Maintenance Organizations (HMO Blank). Such opinion relates to the actuarial items contained in an annual statement of such health service corporations to a state regulatory authority, i.e., the *statutory statement*.
- 1.2 Scope—This standard applies to actuaries providing statements of actuarial opinion on reserves and related actuarial items contained in the statutory statements of health service corporations, as specified in the Instructions to the NAIC Blanks. This standard also applies to actuaries providing statements as required by individual state regulations to the extent that such regulations are consistent with the NAIC Blanks. It does not apply to state laws and regulations that differ substantively from the NAIC Blanks.
- If the actuary departs from the guidance set forth in this standard in order to comply with applicable law (statutes, regulations, and other legally binding authority), or for any other reason the actuary deems appropriate, the actuary should refer to section 4.
- 1.3 Cross References—When this standard refers to the provisions of other documents, the reference includes the referenced documents as they may be amended or restated in the future, and any successor to them, by whatever name called. If any amended or restated document differs materially from the originally referenced document, the actuary should consider the guidance in this standard to the extent it is applicable and appropriate.

- 1.4 Effective Date—This standard is effective for all applicable statements of actuarial opinion provided for annual statements prepared for fiscal periods ending after September 15, 1997.

Section 2. Definitions

The definitions below are defined for use in this actuarial standard of practice.

- 2.1 Health Service Corporation—A hospital, medical, or dental service or indemnity corporation, or a health maintenance organization.
- 2.2 Statement of Actuarial Opinion—A formal statement of an actuary’s professional opinion on a defined subject. It outlines the scope of the work but normally does not include descriptive details.

Section 3. Analysis of Issues and Recommended Compliance

- 3.1 Technical Requirements and Professional Qualifications—The Instructions to the NAIC Blanks each contain explicitly detailed instructions and technical requirements regarding many aspects of the statement of actuarial opinion.
- 3.1.1 NAIC Blank—The actuary preparing the opinion should be familiar with the NAIC Blanks and the Instructions thereto applicable to the type of statement of actuarial opinion being prepared, and any other applicable NAIC model laws and regulations that bear on valuation.
- 3.1.2 State Valuation Requirements—The actuary preparing the opinion should be aware of the valuation requirements of the regulatory authorities to whom the opinion is to be expressed and should be satisfied that the requirements of applicable duly adopted laws and regulations have been met.
- 3.1.3 NAIC Actuarial Guidelines—The actuary preparing the opinion should be aware of applicable NAIC “Actuarial Guidelines” published in the NAIC *Examiners Handbook*, if any, and make reasonable effort to be aware of generally distributed applicable interpretations of each regulatory authority.
- 3.2 Qualification Standards—Before accepting an assignment to issue a statutory statement of actuarial opinion, the actuary should determine that he or she meets the qualifications described in the *Qualification Standards for Public Statements of Actuarial Opinion*, promulgated by the American Academy of Actuaries.
- 3.3 Statement of Actuarial Opinion—The form, content, and recommended language of the statement of actuarial opinion are specified in the Instructions to the NAIC Blanks.

- 3.3.1 Statutory Reserve Requirements—The statement of actuarial opinion does include a statement that the amounts carried on the balance sheet on account of identified actuarial items “meet the requirements of the laws of (state of domicile)” and “make good and sufficient provision for all unpaid claims and other actuarial liabilities of the corporation [organization for HMOs] under the terms of its contracts and agreements.”

The actuary preparing the statement of actuarial opinion should be familiar with the requirements of the applicable laws and regulations of each state in which the opinion is filed. It is important to note that the actuary is expressing an opinion of the adequacy of the aggregate liabilities and that possible deficiencies for individual components may be offset by margins in other items. Documentation concerning compliance with the requirements of the state of domicile and the minimum aggregate amounts required by each state in which the opinion is filed should be maintained by the actuary.

In forming an opinion as to whether the actuarial items “make good and sufficient provision for all unpaid claims and other actuarial liabilities,” the actuary should be satisfied that the actuarial judgments made give recognition to any relevant factors, including the time periods over which the liabilities will extend. The actuary should be satisfied that the reserves and related items opined on are adequate to cover obligations under moderately adverse conditions. To hold liabilities so great that a company could withstand any conceivable adverse circumstances, no matter how improbable, would be excessive, and good actuarial practice does not encompass such a degree of conservatism.

- 3.3.2 Provision for All Actuarial Items That Ought to Be Established—The actuary should ensure that provision has been made for all actuarial items that ought to be established. A significant element in the examination of actuarial assumptions and methods is consideration of the policy and contract provisions affecting the reserves or other actuarial items. The actuary’s judgment in developing actuarial assumptions and methods should take into account the specific characteristics of the policy and contract provisions with respect to which the actuary is expressing an opinion.
- 3.3.3 Change in Assumptions or Methods—If there is a material change in the actuarial assumptions or methods from those previously employed, the change should be described in the statement of actuarial opinion. The introduction of new coverages requiring underlying assumptions that differ from assumptions used for prior coverages is not a change in assumptions or methods within the meaning of this paragraph. Similarly, when the determination of reserves or unpaid claim liabilities is based on periodic updating of experience data, such periodic updating is not a change in actuarial assumptions or methods within the meaning of this paragraph.

- 3.3.4 Items Covered by the Opinion—The statement of actuarial opinion should list the items and amounts on which the actuary expresses an opinion.
- 3.4 Other Applicable Standards—The actuary should note that other actuarial standards of practice may apply in the reserving process and impose requirements beyond the NAIC Instructions.

Section 4. Communications and Disclosures

- 4.1 Format and Content of Statement—Detailed specifications for the statement of actuarial opinion are contained in the Instructions to the NAIC Blanks. If the actuary departs significantly from the recommended language or gives an adverse opinion, such departure or adverse opinion should be clearly disclosed in the opinion.
- 4.2 Reliance on Others for Data and Supporting Analysis—Reliance on another person or firm for any aspect of the data or analysis supporting the actuary’s opinion should be disclosed. Such disclosure should be in the manner prescribed in the Instructions to the NAIC Blanks. The actuary should refer to ASOP No. 23, *Data Quality*, for guidance on the subject.
- 4.3 Opinions of Other Actuaries—When more than one actuary contributes to forming an opinion, statements of actuarial opinion from the contributing actuaries should be maintained by the actuary preparing the opinion as part of the documentation of compliance with this actuarial standard of practice. The actuary preparing the statement of actuarial opinion should review and evaluate the contributions of the other actuaries, and then form an overall opinion.
- 4.4 Disclosures—The actuary should include the following, as applicable, in an actuarial communication:
- a. the disclosure in ASOP No. 41, *Actuarial Communications*, section 4.2, if any material assumption or method was prescribed by applicable law (statutes, regulations, and other legally binding authority);
 - b. the disclosure in ASOP No. 41, section 4.3, if the actuary states reliance on other sources and thereby disclaims responsibility for any material assumption or method selected by a party other than the actuary; and
 - c. the disclosure in ASOP No. 41, section 4.4, if, in the actuary’s professional judgment, the actuary has otherwise deviated materially from the guidance of this ASOP.

Appendix 1

Background and Current Practices

Note: This appendix is provided for informational purposes, but is not part of the standard of practice.

Background

In the early 1980s, the NAIC developed standards for a statement of actuarial opinion as to reserves and related actuarial items that was to be included in the annual statement filed by health service corporations. In response to this requirement, the American Academy of Actuaries promulgated Financial Reporting Recommendation 10, *Statement of Actuarial Opinion for Health Service Corporation Statutory Annual Statements*, setting forth the actuary's professional responsibilities in providing such an opinion.

The form and content of these actuarial opinions, as specified in the instructions to the statutory statements, deal specifically with reserves and related actuarial items. Prior to the development of professional standards, some actuaries began to address other issues in forming their opinions, including asset adequacy analysis, claim settlement expense reserves, and the financial condition of capitated providers under health maintenance organization contracts.

The type of asset adequacy analysis most widely used by actuaries is multiscenario cash flow testing. To guide actuaries choosing to use this technique, the Actuarial Standards Board (ASB) adopted Actuarial Standard of Practice (ASOP) No. 7, *Performing Cash Flow Testing for Insurers*, in October 1988 (revised July 1991). In July 1990, the ASB adopted ASOP No. 14, *When to Do Cash Flow Testing for Life and Health Insurance Companies*, to provide guidance in determining whether or not to do cash flow testing in forming a professional opinion or recommendation.

To guide actuaries in the development of incurred health claim liabilities, the Interim Actuarial Standards Board approved an actuarial standard of practice, *Incurred Health Claim Liabilities*, in April 1988, which was subsequently reformatted and adopted by the ASB as ASOP No. 5 in January 1991. Among other things, ASOP No. 5 requires that provision be made for claim settlement expenses.

To guide actuaries in several important areas requiring special consideration for health maintenance organizations (HMOs) and other managed-care health plans in several areas, including establishing actuarial reserves relating to the transfer of risk to providers and the financial condition of capitated providers, the ASB adopted ASOP No. 16, *Actuarial Practice Concerning Health Maintenance Organizations and Other Managed-Care Health Plans*, in July 1990.

Current Practices

Statements of actuarial opinion as to reserves and related items have been generally required since 1975 for life and health insurance companies, and since 1983 for health service corporations, and practice regarding the basic elements of the opinion is well established. Financial Reporting Recommendation 10, which was issued in 1984, together with the additional requirements of ASOP Nos. 5, 14, 16, and 23 (*Data Quality*), embody current practice.

Appendix 2

Comments on the Exposure Draft and Committee Responses

The proposed standard of practice was exposed for review in August 1996. The comment period ended December 2, 1996. Two comment letters were received. Summaries of substantive issues raised in the comment letters are in lightface, and the committee's responses to such are in **boldface**. The general comment received is addressed first, followed by comments relating to specific sections of the exposure draft.

General Comments

A concern was expressed that a number of areas of guidance included in Financial Reporting Recommendation 10, which this standard of practice replaces, have been omitted. **Financial Reporting Recommendation 10 offered guidance to actuaries providing statutory statements of actuarial opinion for health service corporations. FRR 10 followed the Instructions to the 1983 National Association of Insurance Commissioners (NAIC) Blank for Hospital, Medical, and Dental Service or Indemnity Corporations, and the NAIC Blank for Health Maintenance Organizations. This standard of practice is based on the current versions of the above two Blanks and, the committee believes, provides more detailed and comprehensive guidance than that provided in FRR 10. It does not, however, duplicate the NAIC Instructions with regard to the content of the opinion.**

Section 4. Communications and Disclosures

Section 4.2, Reliance on Others for Data and Supporting Analysis—It was suggested that it is inappropriate to refer to the actuary signing the opinion as the *appointed* actuary. **The word *appointed* was removed from section 4.2.**

Section 4.3, Opinions of Other Actuaries—A concern was expressed that the standard of practice precludes multiple actuaries from signing an opinion or any one actuary from expressing reliance on another actuary. It was also pointed out that the previous financial reporting recommendation specifically allowed for such a contingency. **Financial Reporting Recommendation 10 did make provision for multiple opinions for a single entity. However, in light of current requirements, including the implications of the good and sufficient reserves provision (see section 3.3.1, Statutory Reserve Requirements, of this standard) and cash flow testing requirements, the committee believes it is appropriate to require a *single* opinion for each entity. But note that the ASOP was revised from the exposure draft to eliminate the prohibition on the signing actuary from claiming reliance on the opinions of other actuaries, when the signing actuary reaches an overall opinion.**