

RESERVE STANDARDS FOR INDIVIDUAL HEALTH INSURANCE POLICIES

Section 1. Active life Reserves – General

Active life reserves are required for all in force policies and are in addition to any reserves required in connection with claims. For policy Types A, B and C, described below, the minimum reserve is determined as specified herein. It is emphasized, however, that these are minimum standards and that (insert statutory reference) requires that higher, adequate reserves be established by the insurer in any case where experience indicates that these minimum standards do not place a sound value on the liability under the policy. For policy Type D, the minimum reserve should be the gross pro rata unearned premium.

Section 2. Types of Individual Health Insurance Policies

A. Policies which are guaranteed renewable for life or to a specified age, such as 60 or 65, at guaranteed premium rates.

B. Policies which are guaranteed renewable for life or to a specified age, such as 60 or 65, but under which the insurer reserves the right to change the scale of premiums.

C. Policies in which the insurer has reserved the right to cancel or refuse renewal for one or more reasons, but has agreed implicitly or explicitly that, prior to a specified time or age, it will not cancel or decline renewal solely because of deterioration of health after issue; however, policies shall not be considered of this type if the insurer has reserved the right to refuse renewal provided the right is to be exercised at the same time for all policies in the same category, unless premiums are based on the level premium principle.

D. All other individual policies.

Notes:

(a) The above does not classify "franchise" as a type of policy. Such policies are frequently written under an agreement limiting the insurer's right to cancel or refuse renewal. Usually the right is reserved to refuse renewal of all policies in the group or other categories such as those ceasing to be members of the association, and this would place such policies in Type D in accordance with the last clause under C above. However, if premiums are based on the level premium principle of if the renewal undertaking for the individual meets the requirements for Type A, B or C, the franchise policy should be so classified for reserve purposes.

(b) A policy may have guarantees qualifying it as Type A, B or C until a specified age or duration after which the guarantees, or lack of guarantees, may qualify it as Type A, B, C or D. In such case, the policy in each period should be considered for reserve purposes according to the type to which it then belongs.

(c) Where all of the benefits of a policy, as provided by rider or otherwise, are not of the same Type (A, B, C or D), each benefit should be considered for reserve purposes according to the type to which it belongs.

Section 3. Reserve Standards for Policies of Type A, B or C

(a) Interest. The maximum interest rate for reserves should be the greater of (i) the maximum rate permitted bylaw in the valuation of currently issued life insurance or (ii) the maximum rate permitted by law in the value of life insurance issues on the same date as the health insurance.

(b) Mortality. The mortality assumptions used for reserves should be according to the table permitted by law in the valuation of life insurance issued on the same date as the health insurance.

(c) Morbidity or other contingency. Minimum standards with respect to morbidity are those stated in Appendix A of this regulation, which is subject to revision from time to time with respect to dates of issue of contracts.

(d) Negative Reserves. Negative reserves on any benefit may be offset against positive reserves for other benefits in the same policy, but the mean reserve on any policy should never be taken as less than one-half the valuation net premium.

(e) Preliminary Term. The minimum reserves shall be on the basis of two-years preliminary term.

(f) Reserve Method. Mean reserves diminished by appropriate credit for valuation net deferred premiums. In no event, however, should the aggregate reserve for all policies valued on the mean reserve basis, diminished by any credit for deferred premiums, be less than the gross pro rata unearned premiums under such policies.

(g) Alternative Valuation Procedures and Assumptions. Provided the reserve on all policies to which the method or basis is applied is not less in the aggregate than the amount determined according to the applicable standards specified above, an insurer may use any reasonable assumptions as to the interest rate, mortality rates, or the rates of morbidity or other contingency, and may introduce an assumption as to the voluntary termination of policies. Also, subject to the preceding condition, the insurer may employ methods other than the methods stated above in determining a sound value of its liabilities under such policies, including but not limited to the following: (i) the use of mid-terminal reserves in addition to either gross or net pro rata unearned premium reserves; (ii) optional use of either the level premium the one-year preliminary term, or the two-year preliminary term method; (iii) perspective valuation on the basis of actual gross premiums with reasonable allowance for future expenses; (iv) the use of approximations such as those involving age groupings, groupings of several years of issue, average amounts of indemnity; (v) the computation of the reserve for one policy benefit as a percentage of, or by other relation to, the aggregate policy reserves, exclusive of the benefit or benefits so valued; (vi) the use of a composite annual claim cost for all or any combination of the benefits included in the policies valued.

For statement purposes the net reserve liability may be shown as the excess of the mean reserve over the amount of net unpaid and deferred premiums, or, regardless of the underlying method of calculation, it may be divided between the gross pro rata unearned premium reserve and a balancing item for the "additional reserve."

Section 4. Claim Reserves

(a) Reserves are required for claims on all health insurance policies, whether of Type A, B, C or D, providing benefits for continuing loss, such as loss of time for hospitalization.

(b) Claim Reserve Standards for Total Disability due to Accident or Sickness

(i) Interest. The maximum interest rate for reserves should be the maximum posted rate permitted by law in the valuation of life insurance issued on the same date as the date the claim is incurred.

(ii) Morbidity. Minimum standards with respect to morbidity are those stated in Appendix A of this regulation, except that for the reported claims and resisted claims and, at the option of the insurer, claims with a duration of disablement of less than two years, reserves may be based on the individual insurer's experience or other assumptions designed to place a sound value on the liabilities. Reserves based on such experience or assumptions should be verified by the development of each year's claims over a period of years along the lines of Schedule O.

(iii) For policies with an elimination period, the duration of disablement should be considered as dating from the time that benefits would have begun to accrue had there been no elimination period.

(iv) A new disability connected directly or indirectly with a previous disability which had a duration of at least one year and termination within six months of the new disability should be considered a continuation of the previous disability.

(c) Reserve Standards for All Other Claim Reserves

(i) Interest. The maximum interest rate for reserves should be the maximum rate permitted by law in the valuation of life insurance issued on the same date as the date the claims is incurred.

(ii) Morbidity or other contingency. The reserve should be based on the individual insurer's experience or other assumptions designed to place a sound value on the liabilities. The results should be verified by the development of each year's claims over a period of years along the lines of Schedule O.

Section 5. Valuation Procedures

The insurer may employ suitable approximations and estimates, including but not limited to groupings and averages, in computing claim reserves.

APPENDIX A (effective January 1, 1981)

Minimum morbidity standards for valuation of individual health insurance policies are as follows:

1. Total Disability due to accident or sickness.

Active Life Reserves: Policies issued on or after January 1, 1965:

The 1964 Commissioners Disability Table.

Claim Reserves:

The minimum morbidity standard in effect for active life reserves on currently issued policies, as of the date the claim is incurred.

2. Benefits payable for hospitalization or surgery on account of accident and sickness or for maternity.

Policies issued on or after January 1, 1955 and before January 1, 1982:

The 1956 Intercompany Hospital and Surgical Tables, Transactions of the Society of Actuaries, Vol. IX, p. 334.

Policies issued on or after January 1, 1982:

The 1974 Medical Expense Tables for Hospital, Surgical or Maternity, Transactions of the Society of Actuaries, Vol. XXX, p. 9 (The Major Medical and Cancer Tables in this article are not adopted herein.)

3. Benefits payable for hospital and medical care services on account of cancer.

Policies issued on or after January 1, 1986:

The 1985 NAIC Cancer Claim Cost Tables.

4. Accidental Death Benefits

Policies issued on or after January 1, 1965:

The 1959 Accidental Death Benefits Table.

5. All other benefits, including major medical and other than total disability.

The insurer should adopt a standard which will produce reserves that place a sound value on its liabilities under such benefit.