

DISCUSSIONS OF PAPER PUBLISHED IN VOLUME LVIII

ACTUARIAL NOTE ON
WORKMEN'S COMPENSATION LOSS RESERVES

RONALD E. FERGUSON

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DISCUSSION BY EDWARD M. SMITH

In this presentation Mr. Ferguson has noted an error in reserving which he believes to be common practice where there is excess of loss reinsurance on long term disability losses. Having recognized the error he also presents a means of correctly reserving the greater portion of these cases.

The reserving error which he discusses involves the calculation of the net retention on such cases. This net value is often set at the contractual retention level rather than at the present value of the retention amount recognizing interest and mortality over the term of disability. The result is an overstatement of the direct writer's portion of the loss and an understatement of the reinsurer's portion of the loss reserve by a like amount.

I think that there is little question as to the validity of his estimate that many companies are making these calculations incorrectly. The procedure recommended for properly establishing the net retention is correct for most cases and represents an improvement in all cases. For most companies this error in reserve is probably of little significance. My company is fairly typical of large writers of Workmen's Compensation and we have only a handful of Workmen's Compensation cases involving reinsurance. These are all old cases involving substantial amounts of continuing medical expenses.

Mr. Ferguson has suggested the lack of N_x and D_x values has been responsible for failure to use correct reserving techniques. This is a kindness, at least in my instance. I found that we did have the Q_x values underlying the Survivorship Annuitants Table of Mortality and was able to spot check some of the D_x values in the table presented in the paper. With a little effort we could have developed a complete table of values.

Until now we had not considered the problem. In our case the impact of changing our reserves on these losses would not be sufficient to make the establishment of new procedures worthwhile. For those companies which find that this reserve area is one they must correct, Mr. Ferguson's presentation will provide the basis for a good start.

There will remain the problem of handling the reserve calculations for permanent disability losses in states which do not use Table XI in Bulletin 222, and some decision must be made in regard to the proper method to be used in establishing present value reserves on those large losses involving continuing medical care. Some thought must be given as to whether or not such cases, involving permanent hospital care, can be expected to incur mortality rates similar to those used in creating the valuation tables presently in use.

It seems to me that few companies will decide to change their reserving methods concerning net retention in these cases, for the effect on their total loss reserve will be insignificant. However, it may well be a problem for reinsurers covering substantial amounts of Workmen's Compensation. If this is a problem to them it probably will only be solved through the establishment of precautionary reserves on their part. I am fairly certain that this will not be the only area where such reserves are needed.