



STATE OF ARIZONA
DEPARTMENT OF INSURANCE

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CHARLES R. COHEN
Director of Insurance

Former Director J. Michael Low issued the following Circular Letter on July 24, 1981:

**REASONABLENESS OF BENEFITS IN RELATION TO
PREMIUM CHARGED**

July 24, 1981

You should be advised that Rule R4-14-607, entitled *Reasonableness of Benefits in Relation to Premium Charged*, took effect on July 14, 1981. This regulation, which establishes anticipated loss ratio standards for individual accident and health insurance policies, is designed to assist the Department in implementing ARS § 20-1342.02. That statutory provision provides that "The director may disapprove any disability policy form if the benefits provided in the policy form are unreasonable in relation to the premium charged." *id.*

Rule R4-14-607 is similar to the *NAIC Guidelines for Filing of Rules for Individual Health Insurance Forms*; however, there are some differences in our regulation. Essentially, every new individual policy and endorsement form must be accompanied by a rate filing, unless there is no rate charge involved. Every rate filing must include an actuarial memorandum, including an anticipated loss ratio which must be based upon the present value of the expected benefit to the present value of the expected premium over the entire period for which the rates are computed to provide coverage. The rate filing must also contain a certification by the actuary that the filing is in conformance with the regulation and that the benefits are reasonable in relation to the premium charged.

Actuarial memorandums should include the following information:

- 1) A description of the type of policy, benefits, renewability and issue age limits.
- 2) A description of how rates were determined, including the general description and source of each assumption used.
- 3) The estimated average annual premium per policy. This figure will be used to determine the minimum anticipated loss ratio presumed reasonable in the rule under the appropriate type of coverage and renewability features.

4) The anticipated loss ratio and a description of how it was calculated. For rate increases applying to existing in force business, the anticipated future loss ratio and the estimated cumulative loss ratio, past and future would be required. If any loss ratio less than the minimum anticipated loss ratio, the company would need to file substantial supporting documentation for the use of the particular rate.

5) The minimum anticipated loss ratio presumed reasonable in the rule for purposes of the particular type of coverage and renewability features.

It is suggested that the following certification be used by the actuary in submitting a particular rate filing:

I hereby certify that, to the best of my knowledge and belief, the rate filing submitted herein is in compliance with all applicable laws and regulations of Arizona, including ACRR R4-14-607; that the anticipated loss ratio submitted herein is expected to develop over the period for which the rates are computed to provide coverage; that the benefits of the policy form affected by the rate filing are reasonable in relation to the premiums charged.

Actuary

For all previously approved forms, any rate revision must also be filed, together with an appropriate statement describing the anticipated loss ratio for the particular form and whether the rate will apply only to new business or also to existing policies in force. Insurers must also maintain adequate records of earned premium and incurred losses for each policy form written so that credible data from the company's experience can be derived.

It should also be noted that, under this regulation, anticipated loss ratio standards will vary depending on the type of coverage (*i.e.*, either medical expense or loss of income) and whether the policy falls within a particular renewal category (optionally renewable, conditionally renewable, guaranteed renewable and non-cancellable). Although the rule makes provisions for special circumstances that might affect the anticipated loss ratios projected to develop, the burden is clearly on the insurer to justify a particular factor which warrants special consideration. *Additionally, notwithstanding the existence of special circumstances, all hospital indemnity and cancer insurance policies must develop the specific anticipated loss ratio standards prescribed in the rule.*

Rule R4-14-607 will apply to all individual accident and health insurance policy forms, other than Medicare supplement coverages and credit disability insurance, which must be filed with the Department on and after July 14, 1981. However, it is important to realize that notwithstanding the scope of this regulation, *all* individual accident and health insurance forms are subject to A.R.S. § 20-1342.02. Therefore, the Department will periodically monitor existing policy forms, regardless of whether a rate change has been made after July 14, 1981.

If you would like to receive a copy of this regulation, please write to Margaret McClelland, Department of Insurance Rules Analyst at 2910 N. 44th Street, Suite 210, Phoenix, Arizona 85018. Enclose a \$2.00 fee to cover the Department's reproduction and mailing costs. If you have any questions concerning the rule, ARS § 20-1342.02 or this circular letter, please contact Alexandra Shafer, Assistant Director of the Department's Life and Health Division at (602) 912-8460.

J. Michael Low
DIRECTOR OF INSURANCE