

Potential Effects of Loss Reserve Adequacy For P&C Insurance



Carried Loss Reserve Position	Adequacy of Liabilities	Likely Implications on:				
		Earnings	Volatility	Pricing	Insurer Solvency	Tax
Optimistic (lower than expected)	Deficient	Earnings are overstated in the short term. Earnings in the long-term are reduced as adverse development is recognized.	Higher volatility of reserve position (and therefore earnings) as there is no margin to offset unexpected adverse claims experience.	Higher potential for inadequate pricing (may result in higher than expected loss ratios)	Higher likelihood of insolvency	Tax is paid sooner than necessary
Actuarial Expected	Adequate	Timing of earnings corresponds more closely with actual claim experience.	Average volatility	Consistent with accurate pricing		
Pessimistic (higher than expected)	Redundant	Earnings are understated in the short term. Earnings in the long-term are increased as favorable development is recognized.	Lower volatility of reserve position (and therefore earnings) as the reserve margin can potentially offset unexpected adverse claims experience.	Higher potential for redundant pricing (may result in adverse selection)	Lower likelihood of insolvency	Tax is paid later than necessary (may generate IRS scrutiny)

Disclaimer: This information is not actuarial advice. The purpose of this exhibit is to identify potential implications associated with optimistic or pessimistic reserve positions.

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