



Ratemaking Documentation: Does Yours Make the Cut?

Practical Application of the ASOPs



Overview

- This is a hypothetical rate filing that will be sent to the department of insurance for review.
- Written Actuarial Report example intended to generate conversation on the ASOPs and how they could apply to a rate filing.



Format of Today's Session

■ Quick Review

- ASOP #41 – Actuarial Communications
- Statement of Principles on Ratemaking
- Statement of Principles on Risk Classification
- ASOP #12 – Risk Classification

■ Ten Minute Reading Period

- Evaluate the rate filing
- Feel free to ask any clarifying questions during the period
- We can extend beyond ten minutes if this does not provide sufficient time for review

■ Discussion Period

- Discussion of issues with the filing
- Application of Specific ASOPs and Standards of Practice



ASOP Review



ASOP 41 - Requirements for Actuarial Communications

- Identify Responsible Actuary
- Identify Principal for whom findings are made; clearly state scope and any limitations or constraints
- Communicate methods, procedures, assumptions, data and other information required to complete the work
- Form and content clear and appropriate to audience
- Issued in timely manner



ASOP 41 – Required Disclosures

- Uncertainty or Risk
- Conflict of Interest
- Reliance on Others
- Responsibility for Assumptions and Methods
- Information Date of the Report
- Subsequent Events



ASOP 41 – Other Key Provisions

- An Actuarial Report must state with sufficient clarity findings and identify methods, procedures, assumptions and data used
- Explanation of Material Differences
 - Necessary if a later communication includes materially different results or expresses a different opinion than a former communication on the same issue
 - Should make clear that earlier results are no longer valid, and it should explain the reasons for the change



Statement of Principles on Ratemaking

- Principle 1: *A rate is an estimate of the expected value of future costs.*
- Principle 2: *A rate provides for all costs associated with the transfer of risk.*
- Principle 3: *A rate provides for the costs associated with an individual risk transfer.*
- Principle 4: *A rate is reasonable and not excessive, inadequate, or unfairly discriminatory if it is an actuarially sound estimate of the expected value of all future costs associated with an individual risk transfer.*



Statement of Principles on Ratemaking - Considerations

- Data
- Organization of Data
- Homogeneity
- Credibility
- Catastrophes
- Classification Plans
- Actuarial Judgment



Statement of Principles on Risk Classification - Considerations

- Underwriting
- Marketing
- Program Design

Includes degree of choice available to buyer, experience based pricing, and premium payer

- Statistical Considerations
 - Homogeneity
 - Credibility
 - Predictive Stability



Statement of Principles on Risk Classification – Considerations (continued)

■ Operational Considerations

- Expense
- Constancy
- Availability of Coverage
- Avoidance of Extreme Discontinuities
- Absence of Ambiguity
- Manipulation
- Measurability



Statement of Principles on Risk Classification – Considerations (Continued)

- Hazard Reduction Incentives
- Public Acceptability
 - Not differentiate unfairly among risks
 - Based upon clearly relevant data
 - Respect personal privacy
 - Risks tend to identify with their classification
- Causality
- Controllability



ASOP 12 – Considerations in the Selection of Risk Characteristics

- Relationship of Risk Characteristics and Expected Outcomes
- Causality
- Objectivity
- Practicality
- Applicable Law
- Industry Practices
- Business Practices



ASOP 12 – Actuarial Considerations

- Adverse Selection
- Credibility
 - The actuary should balance considerations of predictability with considerations of homogeneity.
- Practicality
 - use professional judgment in balancing the potentially conflicting objectives of accuracy and efficiency



ASOP 12 – Communications and Disclosures

- significant limitations due to *compliance with applicable law*;
- significant departures from *industry practices*;
- significant limitations created by *business practices* related to the financial or personal security system;
- a determination by the actuary that experience indicates a *significant need for change*, such as changes in the risk classes or the assigned values; and
- expected material effects of *adverse selection*;
- the disclosure if any material assumption or method was prescribed by *applicable law* (statutes, regulations, and other legally binding authority);
- the disclosure 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;
- Disclosure if, in the actuary's professional judgment, the actuary has otherwise *deviated materially from the guidance of this ASOP*.



Questions to Consider During Ten Minute Reading Period

- Does it adhere to ASOP 41 – Actuarial Communications?
 - Does it meet all the requirements of an actuarial communication?
- Does it appropriately consider Statement of Principles for Ratemaking?
- Does it appropriately consider Statement of Principles for Risk Classification?
 - How do the statistical and operational considerations hold up?
- Does the filing adhere to ASOP 12 – Risk Classification?
 - Does it uphold the actuarial considerations of a risk classification plan?
- Does the analysis seem actuarially sound?



Discussion of Rate Filing



Rate Filing Issues

- Is Loss Ratio methodology the most appropriate?
- Does not fully describe data used or adjustments made
 - what kind of premiums used?
 - how were premiums adjusted for Current Rate Level?
- Risk Classification groups are ambiguous
- Does not mention any consideration for correlation between the two analyses
- Does not detail how risk classification grouping was selected
- Others?



ASOP 41 Actuarial Communication

- How does the filing measure up to the standards outlined in ASOP 41?
- Could the intended user of this filing assess the following?
 - Method
 - Procedure
 - Assumption
 - Data
 - Other Information



Statement of Principles

- How does the filing measure up to the standards of practice?

P&C Ratemaking Considerations

- Homogeneity
- Catastrophe

Risk Classification Considerations

- Protection of Program's Financial Soundness
- Avoidance of Extreme Discontinuities
- Absence of Ambiguity



ASOP 12 Risk Classification

- How does the filing measure up to the standards outlined in ASOP 12?

Actuarial Considerations

- Adverse Selection
- Credibility
- Practicality

Other Considerations

- Relationship of Risk Characteristics and Expected Outcomes



Others?

- Are there any other applicable ASOPs or SOPs?



Key Takeaways

- Know the Standards that apply to the work you are doing
- Thorough documentation is your best defense
- A quality peer review by a trusted colleague goes a long way to ensure the overall quality of your work!