

R-5: “What Makes a Good Rate Filing?”

Carl Sornson, FCAS
Managing Actuary – Property/Casualty
NJ Dept of Banking & Insurance
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Overview

- Review what Actuarial Standards Of Practice (ASOP) tell us we should do
- Review what Statements of Principle tell us we should do
- Review what some regulation tells us we should do
- Review some things I have seen that you should not do

ASOP's

- Lots of considerations
- Specific methods not mandated
- Varying guidance regarding documentation

Old ASOP No. 9 - Documentation

- Repealed in March 2011 – the Committee believes that the topics are adequately covered in ASOP 41, other ASOPs , and the Code of Professional Conduct.
- However, ASOP 9 is still referenced in some ASOP's as the guidance regarding disclosure.

ASOP 39 – Catastrophes

- Does data reflect long-term loss potential?
- Adjust losses to reflect current conditions
- How sensitive is indication to experience period?
- Use non-insurance data if needed

- The actuary should be guided by the provisions of ASOP No. 9

ASOP 30 – Profit & Cost of Capital

- Consider leverage, investment income, taxes, reinsurance, debt structure, diversification, and some other items
- The actuary may use any appropriate method
- The actuary should be guided by the provisions of ASOP No. 9

ASOP 29 – Expenses

- % of premium /loss or unit costs
- Expense trends
- The rate filed with a regulator may differ from actuarially determined rate because of expense limitations... the actuary should develop a rate in accordance with the law or regulation
- The actuary should be guided by the provisions of ASOP No. 9

ASOP 25 – Credibility

- Reasonable, unbiased, practical, balance stability/responsiveness
- Not always “precise mathematical process”
- Whenever appropriate in the actuary’s professional judgment (?), the actuary should disclose the credibility procedures used. Any material changes from prior credibility procedures should be disclosed and supported.

ASOP 38 – Models outside area of expertise

- Applies whether proprietary or not
- Actuary should examine the model output for reasonableness, considering factors such as the following:
 - a. the results derived from alternate models or methods, where available and appropriate;
 - b. how historical observations, if applicable, compare to results produced by the model;
 - c. the consistency and reasonableness of relationships among various output results; and
 - d. the sensitivity of the model output to variations in the user input and model assumptions.
- 4.1 Documentation—This standard requires documentation whether or not a legal or regulatory requirement exists (?)

ASOP 13 – Trend

- Insurance or non-insurance data
- Credibility of data
- Length of period
- Known biases, e.g. catastrophes
- Economic/social changes

ASOP 13 – Trend (cont'd)

- Prepare/retain appropriate documentation regarding the methods, assumptions, procedures, and the sources of the data used. The documentation should be in a form such that another actuary qualified in the same practice area could assess the reasonableness of the actuary's work.
- The actuary should disclose changes to assumptions, procedures, methods or models that the actuary believes might materially affect the actuary's results or conclusions as compared to those used in a prior analysis, if any, performed for the same purpose.

Loss Development

- No ASOP on loss development

CAS Statement of Principles - Reserving

- Reasonableness - The incurred losses implied by the reserves should be measured for reasonableness against relevant indicators, such as premiums, exposures, or numbers of policies, and expressed wherever possible in terms of frequencies, severities, and loss ratios. No material departure from expected results should be accepted without attempting to find an explanation for the variation.
- No specific comments regarding documentation or use of judgment.

ASOP 41 - Communications

- Report should identify methods, procedures, assumptions, and data with sufficient clarity that another actuary... could make an objective appraisal of reasonableness
- If a later communication includes materially different results/opinions, explain why they have changed

CAS Statement of Principles – Ratemaking

- Considerations section states: Regardless of the ratemaking methodology utilized, the material assumptions should be documented and available for disclosure.
- Actuarial Judgment - Informed actuarial judgments can be used effectively in ratemaking. Such judgments may be applied throughout the ratemaking process and should be documented and available for disclosure.

NJ Ratemaking Regulations

- Premium trend factors, including **all data and judgments made**, and a description of the method used to select the factors

- Loss trend factors, including **all data and judgments made**, and a description of the method used to select the factors;

- If there is a proposed change to classification differentials, provide:
 - 1. **All data used and judgments made**; and
 - 2. A description of the method used to derive the differentials.

NJ Ratemaking Regulations (cont'd)

- Filers shall provide the following information regarding selected credibility factors:
 - 1. **All data used and judgments made**; and
 - 2. A description of the method used to derive the factors.

- All information related to the selected expense provisions, specifically including **all data used and judgments made**;

- Filers shall provide all information related to the derivation of the profit and contingency loading ... Filers shall specifically include **all data used and judgments made**, as well as a description of the method used to arrive at the selected loading.

Takeaway from ASOP's, etc.

- Methods are generally not specified for filings
- **Any method is ok**, provided it is well-thought out, well documented, and not in conflict with statute or regulation

Now What?

- How do we know what constitutes “not good”?
- Justice Potter Stewart said that objectionable material was hard to define, but “I know it when I see it”
- We will discuss some things I have seen that you should not do

Example 1

Filer addresses cover letter to 2nd-prior Commissioner who has been out of office for almost 2 years

Discussion points

- Seems like minor, non-substantive administrative error
- BUT – may indicate at least two things

Example 1 (cont'd)

- Filing may not have been double-checked for accuracy and/or peer-reviewed
- Filer may not have visited state website recently to review state requirements
- <http://www.state.nj.us/dobi/index.html>
- When in doubt – please contact your regulator!

Example 2

- **Prior Indication +24%; Implemented +8%; 15% residual indication**
- **Current indication +52% (1 year later)**
- **After review, filer finds calculation errors; revised indication now +19%**

Example 2 (cont'd)

Discussion points

- All filings should be compared to previous filings, and significant differences should be reconciled
- Reasonability checks should also be performed by those who know the market

Example 2A

- **Prior filing process included multiple DOBI requests for additional supporting data and calculations**
- **Current filing methodology and documentation replicates prior filing exactly**
- **DOBI sent requests for additional data again (and the next year also...)**

Example 2A (cont'd)

Discussion points

- Filers should review prior correspondence and address any deficiencies or outstanding issues
- Each filing must be separately documented, as they are considered public records (mostly)

Example 3

- **DOBI question to filer: Provide a discussion of the changes to your model.**
- **Filer Response: The model has been updated to reflect more recent experience.**

Example 3 (cont'd)

Discussion points

- Please be specific, e.g. “factor assigned to variable A changed from 1.0 to 1.5” or provide side-by-side comparisons
- DOBI should not have to lay out 20 pages of a model to find 2 changes. This will significantly add to filing review time.

Example 4

- **DOBI question to filer: How were factor selections determined? Provide indicated relativities or competitor information as appropriate**
- **Filer Response: We hired an outside Actuarial Firm to do the analysis**

Example 4 (cont'd)

Discussion points

- Filers often do not know or state they cannot share information used to develop the rating system
- Similar responses often received regarding various modeling vendors (whether insurance score, catastrophe, or other)
- Filers are ultimately responsible for supporting the filing, not vendors

Example 5

- **DOBI Question: Please discuss the reasons for the increase in profit provision from previous filings**
- **Filer Response: This current filing utilizes a profit load that more closely aligns with corporate profit targets**

Example 5 (cont'd)

Discussion points

- Why was company not previously aligned?
- What does "more closely" mean - is current provision still different? If so, why?
- Need to explain why new method is better than old method – applies to all filing steps

Example 6

- **Filer has no rate activity for 5+ years**
- **Filed indication of +100%**
- **Filer requesting +25% increase**

Example 6 (cont'd)

Discussion points

- Where has filer been for 5 years?
- DOBI prefers regular, moderate changes – prevent rate shock to policyholders
- NJ has Public Advocate - Rate Counsel for all personal lines filings in excess of 7%

Example 6 (cont'd)

Discussion points

- Filers need to find resources to make filings more regularly, if necessary
- Good filings do not have to have 1000's of pages
- Contact us to discuss strategy when significant changes needed

Summary

PLEASE DO:

- Visit state website for information regarding filing requirements
- Compare all filings to previous filings, and reconcile significant differences
- Ensure filing addresses previous filing questions/concerns

Summary (cont'd)

PLEASE DO:

- Understand and document how you decided on what is proposed
- Consider whether discussions/responses are truly informative

Summary (cont'd)

PLEASE DO:

- Contact us – Phone, email, in person
- Keep regular lines of communication open