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TO: Ratemaking Task Force – Actuarial Standards Board

RE: Comments on Proposed P/C Ratemaking SOP

My first reaction to the proposed SOP was that it added no value to what has already been published in the CAS Statement of Ratemaking Principles and the various SOPs related to ratemaking. My second reaction was that the proposed SOP did no harm to those of us that practice in the ratemaking arena. My third reaction was that the proposed SOP may cause some actuaries to read and reconsider the Principles and SOP's that have already been published. Causing actuaries to reread and reconsider previous publications would be a beneficial outcome.

I offer one compliment and three relatively minor concerns.

## **Compliment**

About 25 years ago the actuarial profession sought legal advice on antitrust limitations regarding ratemaking. The profession was advised that:

- i. We should not sponsor ratemaking seminars that bring together competing insurers to discuss best practices regarding the determination of insurance prices charged in the competitive market,
- ii. we should not make recommendations to insurers as to how they make their management decisions regarding prices, and
- iii. we should limit our principles and standards of practice to recommendations to actuaries regarding projected costs.

My career has been characterized as providing both actuarial consulting and management consulting. The actuarial component of my consulting work deals with projecting costs and opining on whether or not rates are reasonably consistent with the actuarial and statutory rate standards of adequate, not excessive, and not unfairly discriminatory. The management component of my consulting work deals with helping insurers design rating plans which are competitive in the markets they serve and will best meet their business objectives. The actuarial profession cannot prescribe recommended practices to insurers and their pricing managers, even if the pricing manager happens to be an actuary. If the actuarial profession does attempt to control the pricing manager's decisions and business judgments, my recommendation to my clients will be to fill the pricing manager position with a non-actuary.

I congratulate the Task Force on its definition of Ratemaking in Section 2.9. This definition reminds all actuaries that what uniquely defines the actuarial profession, and what gives value to a formal actuarial rate opinion, is the projection of costs. While many actuaries are well qualified to make pricing decisions, so are some MBA's, experienced underwriters, and product managers. No one but an experienced actuary is qualified to project the costs which should underlie an insurance rate.

If this proposed SOP, and its definition of ratemaking, causes the CAS to rethink the subject matter of its Ratemaking Seminars, something significantly positive will have been accomplished.

***Recommendation: Put the entire Section 2.9 definition in bold type.***

### **Concerns**

1. Section 2.7 – I'm a bit concerned with the use of the term "policyholder". I believe insurance is the transfer of risk and is not dependent upon the insured being in the possession of a policy. There are many situations where a person or entity is insured even though the insured is not in possession of a policy, or ever "holds" a policy.

I am currently involved in a lawsuit where plaintiffs contend that insurance did not exist because the insured was never in physical possession of a policy. Plaintiffs could use 2.7 to prove that actuaries also believe there is no insurance unless the insured holds a policy.

Consider these situations:

- i. A binder is proof that insurance exists, but it is not the policy. Insurance exists even before the insured receives and holds a policy.
- ii. Supplemental Liability Insurance is purchased by a renter at a car rental counter. The renter is insured even though the renter never receives a policy.
- iii. Force-placed collateral protection insurance provides coverage to both the lender and the borrower via a master policy in the possession of the lender. The borrower is clearly an insured, and is the ultimate ratepayer, but never sees or holds the policy.

Why not use the term "insured", rather than "policyholder"? It seems to me that would minimize the possibility that some would argue that rates charged when no policy is in the possession of the insured are not insurance rates, are not subject to actuarial considerations, and are not regulated by insurance laws.

2. Section 3.1 – Some insurers have traditionally included anticipated policyholder dividends in the rates. Accountants treat policyholder dividends as an expense. However, I think there is enough difference between a policyholder dividend and an administrative expense to warrant a separate listing of policyholder dividends. A separate listing would be consistent with how policyholder dividends are treated in the Ratemaking Principles.
3. Sections 1.1 and 1.2 – I am a bit concerned about the term "professional services related to P/C ratemaking" and the reference to "services with respect to developing, reviewing, or changing P/C insurance rates".

I suspect the Task Force intends the term "ratemaking services" to refer solely to the projection of costs. But this term is used before the reader gets to the definition of Ratemaking in 2.9. Some users of the SOP may attempt to expand the definition of ratemaking services to include every consideration by an insurer when it establishes its insurance prices. In other words, they will attempt to extend actuarial principles and standards of practice to the insurers' pricing manager.

My practice involves issuing formal actuarial opinions as to whether or not P/C rates are consistent with the actuarial and statutory rate standards of adequate, not excessive, and not unfairly discriminatory. These opinions are based entirely on projected costs. My opinions are provided to insurers, regulators, and courts. I do not "develop" or "change" rates. Maybe it could be said that I am "reviewing" rates.

Does this proposed SOP apply to my formal actuarial opinions? It definitely should, but it is not clear that I am developing, changing, or reviewing rates.

Could we make the Scope more precise by saying that the purpose and scope of this SOP is to provide guidance to actuaries when providing an actuarial opinion regarding the consistency of the rates with actuarial and statutory rate standards? This actuarial opinion could be for the benefit of the actuary's insurance company employer, or for use by a regulator or court.

Thank you for an opportunity to submit these comments.



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