



AMERICAN ACADEMY of ACTUARIES

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ASB Comments  
American Academy of Actuaries  
1850 M Street NW, Suite 300  
Washington, DC 20036  
Sent via email

Thank you for the opportunity to provide comments on the proposed actuarial standard of practice (ASOP), *Setting Assumptions*. The American Academy of Actuaries<sup>1</sup> Casualty Practice Council (CPC) has reviewed the document and offers the comments below:

As practicing actuaries, we are struggling with how we would apply this ASOP as currently written. We believe the language is so open to interpretation that an actuary with the best intentions would have difficulty being compliant. The comments in this letter point to the specific areas that are unclear to us following the order of the ASOP itself. Because we are not certain of the original intent of the ASOP (i.e., what specific gaps in other ASOPs need to be filled), it is hard to recommend revised language in each instance where the current language is unclear to us.

The sections that cause the most concern are Section 1.2—Scope and Section 4.1—Required Disclosures. Our concerns stem from confusion about the order of application of all possibly relevant ASOPs. In addition, the level of required documentation of an actuary’s assumptions has the potential to become burdensome without further clarification of the language within the proposed ASOP.

### **Section 1.2—Scope**

The fifth paragraph sets up a hierarchy of application of ASOPs relative to this proposed ASOP that is not clear and seems to add difficult complexity. The hierarchy is that practice-area ASOPs take precedence over the *Setting Assumptions* ASOP, which in turn takes precedence over cross-practice ASOPs. We assume that the hierarchy has been developed so that this *Setting Assumptions* ASOP fills in previously identified gaps that exist within the existing practice-area ASOPs. The aspects we find unclear are:

- a. What are cross-practice ASOPs? Are these the ASOPs labeled as “General” on the ASB website? Do these also include ASOPs like ASOP No. 7, *Analysis of Life, Health, or Property/Casualty Insurer Cash Flows*, which covers three practice areas?

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<sup>1</sup> The American Academy of Actuaries is a 19,500-member professional association whose mission is to serve the public and the U.S. actuarial profession. For more than 50 years, the Academy has assisted public policy makers on all levels by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States.

- Consider adding a definition for cross-practice within this ASOP such as “any ASOP defined as a General ASOP on the ASB webpage.”
- b. Potential confusion given multiple “cross-practice” ASOPs that could apply. For example, for the *Modeling ASOP* under development, would this *Setting Assumptions ASOP* take precedence over that more specific “cross-practice” ASOP when it comes to setting assumptions for models?
  - c. ASOP No. 41, *Actuarial Communications*, Section 4.3 discusses documentation regarding assumptions and methods set by someone other than the actuary. Is this intended to supersede that guidance when the “someone else” is an actuary?
  - d. Because of the potential confusion about the order of application, and the original intention for this ASOP to fill in gaps where guidance does not exist, would language around the proposed order of application be easier to articulate as “if another ASOP addresses the use of the assumption selection and disclosure, use that ASOP, otherwise use this ASOP”? Or a specific topic ASOP applies over a more general ASOP? There also would be less confusion if the hierarchy rules were all one way, in comparison to the current wording, which can go in both directions. The standard as written seems open to varying interpretations by different actuaries.

### **Section 2.1—Definition of Assumption.**

Section 2.1 indicates that an assumption is limited to a value. This is a new concept for some of us who consider method choice also as an assumption. In order to make that clearer in the definition of the assumption, we recommend using the phrase “numeric value” in the definition. We recognize the redundancy of the language but are interested in clarity.

In addition, many of the current standards of practice use “Assumptions and Methods” mostly in combination in the terminology, and this treatment of assumptions exclusively would be a departure from that practice.

### **Sections 2.4 and Section 2.5—Definition of Source of Prescribed Assumptions**

Section 2.4 and Section 2.5 provide definitions of two different sources of assumptions that may be provided to the actuary – the “Prescribed Assumption set by another party” and the “Prescribed Assumption set by law.” In later parts of the ASOP, these definitions only appear in the Disclosures Section 4.2 and there is no different treatment or requirements of the assumptions coming from those two sources. This separation into two distinct items may have been added for clarity for certain practice areas but is confusing to those of us in the casualty practice area. Would it be possible to combine into a single definition of prescribed assumptions set by law or another party without losing the intent? Or we suggest adding some explanation for the needed specificity.

### **Section 3.1—General Considerations**

The activity required in order to “identify” assumptions is not totally clear. Does the actuary need to formally document these in the work papers? Do the work papers need to include this identification? We believe neither should be required and recommend that the sentence be changed to “The actuary should set assumptions that...”

### **Section 3.2—Information Used When Setting Assumptions**

What is meant by market data? Is this stock market data or industry data? If the latter, we recommend the word “market” be replaced with “industry” data.

### **Section 3.3—Assumption Margins**

Section 3.3a refers to “company or industry” data. The entity being examined might not be a “company.” We recommend referring to “entity or industry” data.

### **Section 3.4—Reasonableness of Assumptions**

This section lists the characteristics of reasonable assumptions. While we agree that the actuary will use professional judgment in selecting a reasonable assumption, that in and of itself is not a characteristic of a reasonable assumption. We recommend adjusting the wording as follows. “For assumptions for which the actuary is taking responsibility, the actuary should set assumptions that are reasonable *based on the actuary’s professional judgment.*” Then remove 3.4.b from the listing of characteristics.

### **Section 3.6—Reasonable Assumptions in the Aggregate**

While the commentary about the changes from the prior exposure draft describes that wording related to the results in the aggregate are taken out, how can an actuary set “reasonable assumptions in the aggregate” without a view on the reasonability of the aggregate outcome?

### **Section 3.9—Reliance on Assumptions Set by Another Actuary and Section 3.10—Reliance on Assumptions Set by Others**

As we read these two sections and noted that there is a distinction between “another actuary” and “others,” we had some confusion. Both sections say the performing actuary needs to disclose the reliance on assumptions from someone else. The difference is that if the “someone else” is an actuary (3.9), the performing actuary also needs to make sure the other actuary followed the ASOPs and the assumption is appropriate for the assignment. Do we not also need to make sure the assumption is appropriate for the assignment whether the other person is an actuary or not? It is not clear why sections 3.9 and 3.10 require separate treatment.

### **Section 3.11—Documentation**

The preparation of documentation in a form such that another actuary qualified in the same practice areas could assume the assignment if necessary is tremendously difficult and much too onerous. We believe the requirement of enabling assessing reasonableness of the work is sufficient, and recommend the phrase about being able to assume the assignment be removed.

### **Section 4.1—Significant Assumption Disclosures**

The word “significant” is used to modify “assumption(s).” We have several separate comments about the use of the term “significant” as used in this proposed standard:

- ASOP 41, Section 3.4.4 uses the word “material.” Because the latter is already in an ASOP that addresses assumptions, if the intent is similar, consider using the same language.
- Within the casualty practice area, an example we are working with to determine how this disclosure would work relates to loss development factors used in an unpaid claim analysis. Loss development factors assumption selection in the aggregate is “significant” for any given analysis, but each individual selection may not be “significant” or “material.” In a given analysis there may be hundreds to thousands of loss development factors selected. The appropriate level of disclosure in this situation is highly judgmental and each actuary will use ASOP No. 1, *Introductory Actuarial Standard of Practice*, Section 4.2 to inform his or her level of documentation. As a result, there may be great variation in the application of this ASOP.

- We recommend adjusting the words in Section 4.1.a to “a description of each set of assumptions as appropriate.”
- Because assumptions are defined as values, is a description of a value intended to mean the description of what the assumption represents, or a description in more general terms of what the loss development factors are? Consider revising Section 4.1a to “a description of what each significant assumption or set of assumptions represents.”
- Section 4.1.c requires the disclosure of “material changes in significant assumptions.” Can the actuary comply with this by evaluating whether the change in assumption has a material impact on the results of the analysis?

We agree with the goals of the ASOP, which we consider to be setting assumptions in a transparent, professional manner based upon appropriate and documentable support without increasing the overall documentation burden on actuaries. We recommend additional clarity within the language in order to achieve this goal.

The CPC appreciates this opportunity to provide comments to the ASB. We hope these observations are helpful, and we welcome further discussion. If you have any questions about our comments, please contact Marc Rosenberg, the Academy’s senior casualty policy analyst, at [rosenberg@actuary.org](mailto:rosenberg@actuary.org) or 202-785-7865.

Sincerely,

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American Academy of Actuaries