

SECOND EXPOSURE DRAFT—June 2013

Appendix 2

Comments on the Exposure Draft and Responses

The exposure draft of ASOP No. 25, *Credibility Procedures*, was issued in September 2012 with a comment deadline of December 31, 2012. Twenty comment letters were received, some of which were submitted on behalf of multiple commentators, such as by firms or committees. For purposes of this appendix, the term “commentator” may refer to more than one person associated with a particular comment letter. The Credibility Task Force and the General Committee of the Actuarial Standards Board carefully considered all comments received, and the General Committee and ASB reviewed (and modified, where appropriate) the changes proposed by the Task Force.

Summarized below are the significant issues and questions contained in the comment letters and the responses.

The term “reviewers” in appendix 2 includes the Task Force, General Committee, and the ASB. Also, unless otherwise noted, the section numbers and titles used in appendix 2 refer to those in the exposure draft.

GENERAL COMMENTS

Comment	Several commentators suggested wording changes that helped clarify, rather than change the meaning of, various sections of the standard.
Response	The reviewers agree with many of the suggestions and made modifications to language throughout the standard.
Comment	One commentator stated the ASOP needs a full rewrite since it does not provide the proper guidance for actuaries who need to make their communications intelligible to statistical colleagues or to laymen in forums where statistical usage dominates.
Response	The reviewers believe that this ASOP does provide appropriate guidance to actuaries using credibility procedures and does not require a full rewrite because the standard provides guidance for dealing with commonly encountered situations. The standard also provides the actuary with an analytical framework for exercising professional judgment. Further, communication guidance is outside the scope of this standard but is addressed in ASOP No. 41, <i>Actuarial Communications</i> .
Comment	One commentator stated that the title (“Credibility”) was misleading, since the term has a plain language meaning different from its meaning in the standard. Stating a work product meets ASOP No. 25, the ASB standard for credibility, would mean next to nothing about the credibility of the work product.
Response	The reviewers believe the title is appropriate. The title adequately reflects the purpose and scope of the ASOP, as discussed in section 1.

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Comment	One commentator questioned the need for an ASOP, stating that the existence of a standard creates possibility for labeling work product as substandard, negligent, or malpractice, when the work simply involved judgment. Raising the level of practice in the use of credibility would best be accomplished through educational material, which is not the province of the ASB.
Response	The reviewers believe a need does exist, since the practice of credibility procedures occurs in many different practice areas of the actuarial profession. ASOPs provide the actuary with an analytical framework for exercising professional judgment and identify factors that the actuary typically should consider when rendering a particular type of actuarial service. ASOP No. 25 has existed since 1986; it is not a new standard. Expanding ASOP No. 25 to include other practice areas will improve the support needed for actuaries using credibility procedures. However, the reviewers made some revisions to address situations where judgment-based credibility assessments are made.
Comment	<p>One commentator noted that pension practice makes very little use of statistical credibility procedures for selecting actuarial assumptions for specific reasons. Other than occasionally for mortality assumptions, pension actuaries generally have little or no statistically relevant historical experience for pension plans, and rarely have the homogeneity of pension data needed for selecting other demographic assumptions using credibility procedures. As a result, pension actuaries often don't use what has happened in the past to strongly influence future demographic expectations. Instead, general expectations about the future may be more relevant. Pension plan mortality assumptions are prescribed for most plan funding calculations and as a result rarely take into account plan-specific experience. In other circumstances, sufficient mortality data relevant to a participant group is rare, and actuaries usually default to variations on standard tables.</p> <p>The commentator also noted that ASOP No. 35 is the long-established standard of assumption setting for pension practice. ASOP No. 35 uses the word "credible" in a less mathematically rigorous way and does not deal with statistical credibility procedures at all. The commentator believes that having ASOP No. 25 apply to pension practice with different standards than in ASOP No. 35 will lead to ambiguities and confusion and may result in pension actuaries overlooking ASOP No. 25 because it is not cross referenced in ASOP No. 35.</p>
Response	The reviewers revised the scope to address situations where credibility procedures are not used in setting assumptions, and also made revisions to address situations where judgment-based credibility assessments are made. The reviewers also note that section 3.2 states that the credibility procedures may be different for different practice areas. The discussion in section 3.4 has been expanded and states that credibility procedures are not always precise mathematical processes.
SECTION 2. DEFINITIONS	
Comment	One commentator suggested replacing the word "definition" with "terms" in the lead-in sentence after the section header.
Response	The reviewers agree and made the change to reflect standard language.
Section 2.1, Credibility	
Comment	One commentator questioned defining "credibility" as a term and whether the parenthetical in the definition should instead be addressed in the purpose and scope in section 1. The commentator also questioned the narrowing of the standard to the use of predictive in the statistical sense and not in the sense of predicting the future.
Response	The reviewers disagree and made no change, noting that the definition of "credibility" appears in the existing ASOP No. 25 as well as ASOP No. 12, <i>Risk Classification (For All Practice Areas)</i> .

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Section 2.2, Full Credibility	
Comment	One commentator suggested removing the last phrase “based on a selected confidence interval.” In addition, it was suggested that the definition be changed to read, “The assignment of full predictive value to the subject experience.”
Response	The reviewers disagree and did not remove the last phrase but added the word “often” to clarify the language.
Section 2.3, Relevant Experience	
Comment	One commentator suggested adding a more exhaustive list to the parenthetical, or changing “such as” to “including, but not limited to.”
Response	The reviewers agree and added the suggested wording, noting it is not practical to make the list more exhaustive, as there can always be more examples added to the list, and it should not be read as fully complete.
Comment	One commentator suggested expanding the definition to include parameters calculated based on “sets of data” that are described in current definition, by beginning the definition with “[s]ets of data <i>or parameters calculated using sets of data that,...</i> ”
Response	The reviewers disagree and made no change, noting that parameters developed for use in credibility work are a result of analysis of data or sets of data.
Comment	One commentator suggested expanding the defined term from “Relevant Experience” to “Relevant Experience and Analyses” to account for the fact that some models may provide relevant contribution to an actuary’s judgment regarding credibility weighting of different estimates.
Response	The reviewers disagree and did not expand the definition.
Comment	One commentator suggested restoring the wording from the existing ASOP No. 25, which states “other relevant data for coverage analogous to the coverage under consideration.”
Response	The reviewers disagree and did not restore the wording.
Section 2.4, Risk Characteristics	
Comment	One commentator suggested removing the definition of “risk characteristics” because the term is only used once in section 3 and may not justify inclusion in the definitions.
Response	The reviewers disagree and believe it is instructive to include this definition.
Section 2.5, Subject Experience	
Comment	One commentator suggested substituting “subject” for population in the definition, because in statistical usage, population refers to all subjects, not just class under consideration.
Response	The reviewers removed the word “population.”
Comment	One commentator suggested adding a definition of “subject” to clarify that the word can refer to either a class or a single risk.
Response	The reviewers disagree.
Comment	One commentator suggested that the phrase “drawn from the experience of the population” is too restrictive and should be removed.
Response	The reviewers believe that the phrase should remain and made no change.

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SECTION 3. ANALYSIS OF ISSUES AND RECOMMENDED PRACTICES	
Section 3.1, Purpose and Use of Credibility Procedures	
Comment	Several commentators asked for more guidance regarding when credibility procedures are required.
Response	The reviewers agree and revised sections 1.2 to clarify when the standard applies.
Comment	Several commentators asked for clarification between the words “credibility procedure” and “credibility methodology.”
Response	The reviewers agree and added the definition of “credibility procedure” to section 2. The reviewers also replaced “method(s)” and “methodology(ies)” with “procedure(s)” throughout ASOP No. 25 to clarify the guidance provided.
Comment	One commentator suggested substituting a new term for “expected value” in section 3.1, since the term seems too narrow.
Response	The reviewers believe the term is appropriate and did not change it.
Comment	Several commentators addressed the second paragraph of section 3.1, suggesting that an actuary could assign partial credibility to subject experience.
Response	The second paragraph of section 3.1 was deleted. Reference to partial credibility is found in section 3.4.
Comment	One commentator suggested adding a sentence to the effect of, “If the actuary does decide to assign full or zero credibility to the subject experience, the actuary should disclose and discuss the rationale for this decision in the actuarial communication.”
Response	The reviewers disagree and believe that this concern is appropriately addressed in section 4.1, which indicates that the actuary should use professional judgment in determining the appropriate disclosure, if any.
Section 3.2, Selection of Credibility Methodologies	
Comment	One commentator suggested changing the title of the section from “Credibility Methodologies” to “Credibility Analyses.”
Response	The reviewers replaced “method(s)” and “methodology(ies)” with “procedure(s)” throughout ASOP No. 25 to clarify the guidance provided.
Comment	Several commentators questioned the opening sentence in section 3.2, which requires the actuary be familiar with and consider various credibility methodologies.
Response	Wording in section 3.2 was changed to state that the actuary should use an appropriate procedure.
Comment	Several commentators asked if the same credibility method must be used to determine whether the subject experience was fully credible and for blending purposes.
Response	The reviewers note that the guidance does not include this restriction.
Comment	One commentator suggested mentioning some common credibility methodologies in section 3.2.
Response	The reviewers note that common procedures are listed in appendix 1 and do not believe that they should be mentioned in section 3.2.
Comment	One commentator saw no reason to replace “regulations and statutes” with “applicable law.”
Response	The reviewers note that this is common language used by the ASB in many standards and made no change.

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Comment	One commentator suggested adding the phrase “or develop” to the first sentence in the second paragraph of section 3.2.
Response	The reviewers changed the lead-in sentence to, “In selecting or developing a credibility procedure, the actuary should consider the following criteria.”
Comment	One commentator implied that deleting “in the professional judgment of the actuary” from the first bullet point in section 3.2 produces ambiguity in determining “reasonable results.”
Response	The reviewers note that the reference to professional judgment in section 3.4 covers all aspects of applying actuarial judgment in credibility procedures and made no change.
Comment	Many commentators addressed bullet point c (“are unbiased with respect to the results in any material way”) in section 3.2. Some suggested the bullet be deleted, while some suggested restoring to the original language.
Response	The reviewers deleted the bullet.
Comment	Many commentators addressed the last bullet in section 3.2, referring to “resulting in blended data that reflects current experience” rather than “resulting in results that reflect.”
Response	The reviewers simplified the bullet points, and this point was deleted.
Section 3.3, Selection of Relevant Experience	
Comment	One commentator suggested changing the title of the section from “Selection of Relevant Experience” to “Selection of Relevant Experience or Analysis.”
Response	The reviewers disagree and believe the title was appropriate.
Comment	One commentator stated that using the phrase “population characteristics” was not clear and reinforced the idea that relevant experience must be a data set.
Response	The reviewers agree and changed “population characteristics” to “demographics.”
Comment	One commentator asked if the “should” statement in the second sentence of section 3.3 means that the proposed blending experience is ruled out if just one of the criteria is not met.
Response	The reviewers believe that no change is necessary since the list includes examples of characteristics that should be considered and is not a comprehensive list.
Comment	Many commentators addressed the appropriateness of the second paragraph in section 3.3.
Response	The reviewers believe the paragraph provides useful guidance and made no change.
Comment	Two commentators stated that the standard fails to suggest what should be done if the actuary is unable to find or develop sufficiently credible “relevant experience.”
Response	The reviewers agree with the comments and added a new paragraph to section 3.3 to address this situation.

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Section 3.4, Actuarial Judgment	
Comment	One commentator stated that the revised term “professional judgment” is less clear and possibly more restrictive than the existing term “informed judgment” in section 3.4. Presumably professional judgment involves the actuary’s judgment within the limits of his standards of practice and expertise, whereas informed judgment may allow for information provided by other experts, such as accountants, IT experts, and operations personnel.
Response	The reviewers believe that the term “professional judgment” is better terminology and that the commentator’s interpretation is too narrow.
Section 3.5, Homogeneity of Data	
Comment	One commentator suggested that “appropriate treatment” should replace “separate treatment” in the last sentence of section 3.5 to remove the implication that “separate” treatments are necessary to handle non-homogenous segments.
Response	The reviewers disagree and made no change because the sentence states that “[t]he predictive value can <i>sometimes</i> be enhanced....”
APPENDIX	
Comment	Several commentators suggested that the section, Credibility Bases, should be revised to give examples of bases for credibility analyses outside of historically common applications to include reference to more “modern” credibility methodologies.
Response	The reviewers agree and added a section discussing “Emerging Practice Involving Generalized Linear Models.”
Comment	One commentator suggested that the description of “credibility bases” could be clarified.
Response	The reviewers believe the description is sufficient for its purpose and made no change.