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**PERSONAL & CONFIDENTIAL**

**Comment #12 - December 12, 2014 – 5:54 p.m.**

Life Insurance and Annuity Pricing ASOP  
Actuarial Standards Board  
1850 M Street, NW, Suite 300  
Washington, DC 20036-4601

**Re: Request for Comments—Life and Annuity Pricing ASOP**

Thank you for the opportunity to comment on the proposed Actuarial Standard of Practice on Life Insurance and Annuity Pricing. By way of background, I have been responsible for pricing of life insurance and/or annuity products at three direct writing life insurance companies and one reinsurer and have consulted on pricing issues. I served on the Task Force to Revise ASOP No. 12, Risk Classification (for all Practice Areas) and chaired the American Academy of Actuaries work group that developed its monograph On Risk Classification.

I agree that an actuarial standard of practice covering the proposed subjects would be useful. However, I have several concerns:

1. Pricing is a management function, not an actuarial function. While the actuary's advice may be sought and even relied upon, the actual decision is management's. Pricing is part of management's strategy in approaching a market. There is, for example, no reason that a product need be priced to return a profit if corporate strategy dictates otherwise. To categorize management's role in pricing as "management adjustments" is to put the cart before the horse—strategic considerations naturally come first and the detailed development of rates is secondary to such considerations. Actuaries may advise management on pricing (or an actuary may be given a management position in which he or she actually does set prices), but pricing itself is a management function
2. Labeling the Standard as guidance on "pricing" opens the Standards Board up to accusations of price-fixing. While it is common in the profession to refer to the work

actuaries do in producing sets of rates as “pricing,” outside the profession the term “pricing” refers to the final setting of the price. It is inappropriate for the Board to attempt to constrain the pricing process used by insurers and annuity writers.

3. The ASOP should not give any guidance regarding the choice of profitability method or assumptions. Any statements that imply that the setting of profitability method or assumptions should be done "consistently" between companies or that actuaries should follow specified procedures in choosing pricing assumptions smack of price-fixing. Moreover, such guidance could constrain innovation. Paradigm changes like preferred class pricing depended on some actuaries choosing assumptions in a way that was not accepted by other actuaries at the time. Both because of restraint of trade concerns and to avoid stifling innovation, the ASOP should stay away from placing any constraints on profitability method or assumption selection for pricing.
4. The ASOP should address advice given regarding product design. The “pricing actuary” in most companies is relied upon not only to advise on pricing and new product profitability, but also to assure that products will function as expected. Specifically, management is usually incapable of determining whether a proposed product satisfies non-forfeiture laws and regulations and tax laws, such as Internal Revenue Code Section 7702 without actuarial advice. While the Code of Conduct makes clear that actuaries are responsible for compliance with applicable laws and regulations, I am aware of several situations in which an actuary designed or reviewed products that did not reflect non-forfeiture and tax laws properly and caused enormous difficulties for their employer or client, in one case leading to bankruptcy. I am also aware of designs that were actuarial in nature that created unexpected administrative expense. I believe explicit reference to the responsibility for appropriate advice on actuarial design matters would be welcome and would fit well within the proposed ASOP.
5. The ASOP should be limited to new product pricing. The pricing issues relating to in-force policies are covered by ASOP No. 2 and ASOP No. 15. In fact, several states require filings based on ASOP No. 2. ASOPs No.2 and 15 seem to me to satisfactorily cover the actuarial guidance necessary for the two kinds of re-pricing of inforce products. If these are thought to be inadequate, they should be changed or enhanced. Having two separate Standards that apply to the same situation would be confusing. Moreover, the procedures used in advising about the pricing of new products are for the most part different from those that apply for in-force products and the two situations should not be treated in a single Standard.
6. The ASOP should not require actuaries to opine on “fairness” or “equity.” Fairness and equity are concepts on which there is not now, nor is there likely ever to be, universal agreement. It would be inappropriate to require an actuary to give his or her opinion on such matters. The Academy monograph, On Risk Classification, has a section dealing with these issues and the difficulties in obtaining consensus on them.

7. The ASOP should be named something like “Requirements when advising on the pricing and design of new life insurance and annuity products.” As mentioned above, the actuary, when acting as an actuary, is normally advising on pricing, not actually setting the price. An alternative, based on the Request for Comment’s statement that “the proposed standard would focus on the actuary performing profitability analysis when pricing new and in-force products,” would be “Requirements when performing profitability analysis with respect to new life insurance and annuity products.” This would be appropriate if it is decided that product design issues, such as those I mentioned above, will not be covered by the Standard.

With respect to your specific requests for comments:

1. **Would an ASOP on life insurance and annuity pricing be beneficial to the profession?**

Yes, provided care is taken to avoid possible allegations of price-fixing and any constraints on innovation. To this end, the ASOP should be labeled in such a way that it is clear that the actual setting of price as such is not an actuarial function and the ASOP should avoid any guidance on the choice of profitability method or pricing assumptions.

2. **Are there areas where appropriate practice needs to be defined or current practice needs to be improved? If so, what are those areas?**

I am not aware of any significant deficiencies in profitability analysis of new (or in-force) products. As I mentioned above, I have seen instances where non-forfeiture or tax laws have been ignored or inappropriately applied, or where the interaction of these design elements was not properly understood. Also, I am aware of product designs that incorporated actuarial niceties but proved to be excessively expensive to administer. I would like to see the ASOP cover such design issues. Going forward, the interaction of the pricing actuary with the valuation actuary will become more critical as we move into principle-based reserving. The ASOP should cover this interaction.

3. **Does the proposed ASOP cover the appropriate subject areas? If not, what changes do you suggest?**

As just mentioned, I believe the ASOP should cover certain design issues that are actuarial in nature, such as non-forfeiture and the tax definition of life insurance and overly complex actuarial features. Another such area is the illustration regulation, which can also constrain product design and has elements that require actuarial analysis. While

there is a Standard focused on illustrations, the implications for product development are not covered there.

**4. How should the proposed ASOP interact with existing ASOPs that provide guidance regarding policyholder dividends and other non-guaranteed elements?**

As I mentioned above, I believe the new ASOP should be restricted to new products and any needed enhancements for setting dividends or non-guaranteed elements should be included in ASOPs No. 15 or 2, respectively.

Thank you again for the opportunity to comment on the proposed Standard. If you have any questions on my comments, feel free to contact me at 303-881-5351 or [adicke@newworldactuarial.com](mailto:adicke@newworldactuarial.com).

Sincerely,

A handwritten signature in black ink that reads "Arnold A. Dicke". The signature is written in a cursive style with a large initial 'A'.

Arnold A. Dicke