

Comment #20 – 10/31/16 – 3:10 p.m.

October 31, 2016

Modeling (Third Exposure)
Actuarial Standards Board
1850 M Street, NW
Suite 300
Washington, DC 20036

Dear Sir or Madam,

Subject: Comments on Proposed Actuarial Standard of Practice (ASOP) on Modeling

We would like to thank the Task Force for the effort that went into the preparation of the proposed ASOP on Modeling. We appreciate the opportunity to provide our comments.

The following comments were developed by members of Aon's Health & Benefits Actuarial Practice Compliance Team and are being submitted on behalf of the Health & Benefits Actuarial Practice.

We will first address the specific issues where comments were requested:

- 1) While we do note several items for consideration below, we generally agree that yes, the standard provides sufficient and appropriate guidance for actuaries working with models.
- 2) The standard provides sufficient and appropriate guidance for models our team is familiar with, but we are not able to opine as to whether the guidance is sufficient and appropriate for **all** models.
- 3) The existence of the definition seems to be appropriate since the use of the term "model" is ubiquitous and often used to describe things that aren't really models. However, the wording in the definition is confusing. Part of the definition of a model in Section 2.7 says that a model has a production phase that consists of one or more **model runs**, and then the definition of simple model says "results... can be predicted **without an actual model run**." It appears a simple model isn't really a model. Perhaps Section 1.2 should simply state the ASOP includes "all types of models" with the definition of models (i.e., what is included in the scope of this ASOP) as shown in Section 2.7. Alternatively, if the ASB wishes to explicitly state what's excluded from the scope of this ASOP, we suggest doing so without using the word "model."
- 4) The guidance is appropriate and clear.
- 5) No further comments.

We also believe the following items merit further consideration.

1) Definition 2.4 Implementation

While we ultimately understood the definition of “implementation” as the phase during which “an executable form of a model” [is developed], the definition reads awkwardly because the word “implementation” implies action, while the phrase “executable form” alone does not.

We recommend an alternative definition: “[The phase during which] an executable form of a model is developed.” We believe this definition is clearer, fits better in context, and applies for all uses of the word “implementation” in this ASOP.

2) Section 3.1 Application of ASOP Guidance

The placement of the terms “and” and “or” when describing applicability could potentially lead to exclusion of modeling situations that should be covered by the standard. The first paragraph says “The guidance in this ASOP applies...when...intended users of the model rely heavily on the results, **and** the use of the results of the model has a material financial effect for the intended user.” The second paragraph says “In modeling situations where...the results (1) are not heavily relied upon by the intended users **or** (2) do not have material financial effect, then application of the guidance in this ASOP is not required...” Similar wording appears in section 1.2.

It narrows the scope of this ASOP to require that both conditions be satisfied for applicability to hold. The guidance in the ASOP would apply more broadly if either condition were to hold true as opposed to only in cases where both conditions hold true.

An example where the intended user relies heavily on model results but the results do not have material financial effect could be the use of a model designed to project the impact of the Excise Tax on High Cost Employer-Sponsored Health Coverage on an active medical plan. The results of the model have no current material financial effect on plan sponsors and may never have one, yet plan sponsors are relying heavily on results in presentations to senior management and unions. Would a model designed to project the impact of the Excise Tax, where results of the model may not have a material financial effect, not be subject to this ASOP?

Additionally, the numbering present in the second paragraph could be added to the first paragraph for consistency.

3) Section 3.4.4 Understanding the Model

Part a. generally mirrors Section 3.2 parts b. through d., with the exception of the wording “important relationships” replacing “major...dependencies.” Was the difference in wording intended to imply that these are somehow different concepts? Clearly “limitations” and “weaknesses” are interchangeable in this context, but relationships and dependencies are not always synonymous.

4) Section 3.4.7(d) Consistency

The first sentence of the second paragraph references section 4.1.3 which doesn't exist. Section 4.2.3 makes sense as the reference.

5) Section 3.5.1(c) Peer Review

We appreciate the ASB suggesting peer review as a way to mitigate model risk. However, we would rather see peer review addressed in ASOP 1, and therefore applicable to all actuarial services, as opposed to seeing it only applicable to modeling.

Adding Peer Review language to specific ASOPs individually could result in inconsistent guidance and application across actuarial services. Additionally actuarial services not covered explicitly in any ASOP other than ASOP 1 would not be subject to peer review.

6) Section 3.6.1 Explanation of Limitations of Models

The last sentence references section 4.1. Section 4.1 subsequently references sections 3.1 and 3.6-3.9. A reference to Section 4.2.2 would make more sense.

7) Section 3.6 Presentation of Results and Section 3.8 Documentation

The differentiation between these sections isn't clear, particularly because both mention an actuarial report. The sections also aren't consistent. The first sentence of section 3.6 noticeably excludes "data" from the list, while the first sentence of section 3.8 includes it. Since both sections reference ASOP 41, which includes data, it's reasonable to assume that data should be disclosed, but it's potentially confusing for the actuary to have to cross-reference and combine different lists to know what is required. We recommend a single section that includes the items the actuary should document/explain, should consider documenting/explaining, or may consider documenting/explaining.

8) Section 3.8 Documentation

Section 3.1 of this ASOP states that a condition that needs to be met for this ASOP to apply is the "intended users of the model rely heavily on the results." In a discussion about documentation, section 3.8 of this ASOP refers to ASOP 41, section 3.2, which says "the actuary should complete an actuarial report if the actuary intends the actuarial findings to be relied upon by any intended user." It, therefore, stands to reason that any work subject to this proposed ASOP requires an actuarial report; however, Section 3.8 specifically mentions the case when no actuarial report is created. We acknowledge that the actuarial report can take many forms, some of which are more formal than others, but creating no report at all is not consistent with other applicable guidance. It may be appropriate to consider documenting the points mentioned in the second paragraph of section 3.8 outside of the actuarial report, such as in working files or internal notes.

Again, we appreciate the Task Force's time and consideration.

Sincerely,

Health & Benefits Actuaries from Aon Consulting, Inc. and Hewitt Associates LLC, both Aon Hewitt companies

Rebecca Bodek Feldman
FSA, MAAA
Aon Health & Benefits
Actuarial Compliance Officer

Tiffany Arnold
ASA, MAAA
Aon Health & Benefits

Melissa Rawson
FSA, MAAA
Aon Health & Benefits

RBF:bsd

cc: Brian Alvers, Aon Benfield, National Practice Leader, Actuarial & Analytics
Eric Keener, Aon Hewitt, U.S Retirement Practice Chief Actuary
Joseph Kilroy, Aon Risk Solutions, National Practice Leader, Aon Global Risk Consulting
Michael Morrow, Aon Risk Solutions, U.S. Health & Benefits Practice Chief Actuary

About Aon

Aon plc (NYSE:AON) is the leading global provider of risk management, insurance and reinsurance brokerage, and human resources solutions and outsourcing services. Through its more than 72,000 colleagues worldwide, Aon unites to empower results for clients in over 120 countries via innovative and effective risk and people solutions and through industry-leading global resources and technical expertise. Aon has been named repeatedly as the world's best broker, best insurance intermediary, best reinsurance intermediary, best captives manager, and best employee benefits consulting firm by multiple industry sources. Read on for more information about Aon, and visit aon.com/manchesterunited to learn about Aon's global partnership with Manchester United.