

**Title of Exposure Draft: Proposed Revision of Actuarial Standard of Practice (ASOP) No. 12**

**Comment Deadline: May 1, 2024**

Instructions: Please review the exposure draft and give the ASB the benefit of your recommendations by completing this comment template. Please fill out the tables within the section below, adding rows as necessary. Sample for completing the template provided at the following link: <http://www.actuarialstandardsboard.org/email/2020/ASB-Comment-Template-Sample.docx>

Each completed comment template received by the comment deadline will receive consideration by the drafting committee and the ASB. The ASB accepts comments by email. Please send to [comments@actuary.org](mailto:comments@actuary.org) and include the phrase 'ASB COMMENTS' in the subject line. Please note: Any email not containing this exact phrase in the subject line will be deleted by our system's spam filter.

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**I. Identification:**

Name of Commentator / Company
Amy Angell, MAAA, FCAS Vice President, Casualty, American Academy of Actuaries, on behalf of the Casualty Practice Council

**II. ASB Questions (If Any). Responses to any transmittal memorandum questions should be entered below.**

Question No.	Commentator Response

**III. Specific Recommendations:**

Section # (e.g. 3.2.a)	Commentator Recommendation (Please provide recommended wording for any suggested changes)	Commentator Rationale (Support for the recommendation)
1.2 Paragraph 1	<p><b>Replace the following wording:</b></p> <p>This standard applies to actuaries when performing actuarial services with respect to designing, developing, selecting, modifying, reviewing, evaluating, or opining on any elements of a risk classification framework in connection with financial or personal security</p>	<p>The second sentence in the section carves out “using” from the previous sentence and adds “to the extent practical and consistent with the scope of the actuary’s assignment.”</p> <p>1. Combine the list of verbs to include “using.”</p> <p>As currently drafted, it does not make sense for scope of the standard to treat “using” differently than “designing, developing, ...”</p>

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<p>systems. This standard also applies to actuaries when performing actuarial services with respect to using any elements of a risk classification framework in connection with financial or personal security systems, to the extent practical and consistent with the scope of the actuary's assignment.</p> <p><b>With the recommended wording below (additions are highlighted):</b></p> <p>This standard applies to actuaries when performing actuarial services with respect to designing, developing, selecting, modifying, reviewing, evaluating, opining on, or using any elements of a risk classification framework in connection with financial or personal security systems.</p> <p>If the actuary's actuarial services involve reviewing or evaluating a risk classification framework, the reviewing or evaluating actuary should be reasonably satisfied that the actuarial services performed by another party were performed in accordance with this standard. The actuary should also consider whether the risk classification services performed by a non-actuary were reasonably consistent with this standard. See section 3.6. The actuary should apply the guidance in this standard in conducting their review or evaluation.</p>	<p>When actuarial services involve using a risk classification framework, the actuary would be expected to take responsibility for such use. If the scope of the actuary's assignment excludes responsibility for the use of the risk classification framework, then the actuary should refer to sections 3.6, 4.1, and 4.2 regarding Reliance on Information Provided by Another Party.</p> <ol style="list-style-type: none"><li>2. Remove "to the extent practical and consistent with the scope of the actuary's assignment."</li><li>3. Add a new paragraph that provides scope clarification for an actuary who is reviewing or evaluating the work of another actuary, or similar work possibly performed by non-actuaries.</li></ol> <p>Practicality is specifically addressed in section 3.2.7 and should not be part of the section 1.2 Scope.</p> <p>This suggested wording is similar to the wording used in other standards, such as ASOP No. 53 and ASOP No. 56. ASOP No. 53 (section 1.2) states "This standard also applies to developing or reviewing the future cost estimates by class within a risk classification system." There is no reference in ASOP No. 53 to practicality or to the scope of the actuary's assignment. Section 3.2.7 of this ASOP addresses practicality separately, so it would be redundant and inconsistent for the standard to repeat "when practical" or "to the extent practical," in some sections, but not in other sections.</p> <p>If the actuary relies on another actuary or on other experts in the applicable field, the standard should include similar recommended practices, documentation, and disclosures as provided in ASOP No. 38, ASOP No. 53, and ASOP No. 56. In particular, ASOP No. 53 states, "When using models, the actuary should refer to ASOP No. 38, <i>Using Models Outside the Actuary's Area of Expertise (Property and Casualty)</i>." Consequently, we suggest adding to section 3, "When using a risk classification framework which is based on models (as defined in ASOP No. 56), the actuary should refer to ASOP No. 56, <i>Modeling</i>, and ASOP No. 38, <i>Using Models Outside the Actuary's Area of Expertise (Property and Casualty)</i>."</p>
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<p>1.2 Paragraph 1</p>	<p><b>Delete the following wording:</b></p> <p>“... to the extent practical and consistent with the scope ...”</p>	<p>Section 3.2.7 addresses practicality separately, so it is redundant and inconsistent for the standard to repeat “when practical” or “to the extent practical,” in some sections, but not in other sections.</p> <p>Similarly with respect to the wording, “consistent with the scope of the assignment” such conditions are problematic. In general, we would expect the actuary’s work to be relied upon with respect to the intended purpose and use of the <b>risk classification framework</b>. Consequently, the standard should not permit the scope of the actuary’s assignment to be established in such a way as to ignore any of the requirements otherwise set forth in the standard. However, the standard should allow for the situation where the requirements of the ASOP are not applicable or not practical and in such cases the actuary can make appropriate disclosures.</p>
<p>1.2 Paragraph 2</p>	<p><b>Add the highlighted language below:</b></p> <p>The guidance in this ASOP does not apply to actuaries when performing actuarial services with respect to individual pension benefit calculations or nondiscrimination testing <b>for pensions or benefit plans.</b></p>	<p>The additional language is recommended to clarify that the “nondiscrimination testing” reference refers to “pensions or benefit plans” rather than something that applies to all practice areas. This exclusion should not be a general exclusion for any type of non-discrimination testing or analysis across practice areas, particularly where “non-discrimination testing” can have different meanings for actuarial work.</p>
<p>2.1</p>	<p><b>Replace the following wording:</b></p> <p><u>Adverse Selection</u>—The result of actions regarding an element of choice taken by risk subjects, which could adversely impact the effectiveness of a risk classification framework or the viability of the financial or personal security system. Adverse selection is sometimes referred to as “anti-selection.”</p> <p><b>With the recommended wording below (additions are highlighted):</b></p> <p><u>Adverse Selection</u>—The result of actions taken by <b>risk subjects or other participants in the financial or personal security system, based on information known to or suspected by the participants,</b> which could adversely impact the ability of a <b>risk classification framework to satisfy its intended purpose.</b> For example, adverse impacts from <b>adverse selection</b> could arise from</p>	<p>Alternative language is proposed as more direct and easier to interpret than “effectiveness,” such as “the ability of a <b>risk classification framework</b> to satisfy its intended purpose” or simply “the fitness for purpose” of the framework (see comments for section 3.2.9). There is no guidance, common actuarial principles, or other authoritative references that address “effectiveness.” As a result, the proposed language is unnecessarily confusing and potentially vulnerable to subjective and inconsistent interpretation.</p> <p>Reference to the viability of the <b>financial or personal security system</b> is unnecessary because the intended purpose of the <b>risk classification framework</b> would normally incorporate consideration of protecting the viability of the <b>financial or personal security system</b>. For example, an insurer’s anticipated underwriting profit or loss from the use of the <b>risk classification framework</b>.</p> <p>Recommended edits to section 3.2.5 below describe what the actuary should do regarding adverse selection, with a focus on materiality. Additionally, the concept of information asymmetry is retained from the current ASOP wording.</p>

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	<p>policyholder and insurer actions which influence insurance market functions such as <b>risk class</b> pricing, underwriting, claims handling, and policyholder buying and renewal habits, including price sensitivities, and other relevant actions by the participants. <b>Adverse selection</b> is sometimes referred to as “anti-selection.”</p>	<p>We have concerns that the exposure draft does not clearly portray the various types of <b>adverse selection</b> that actuaries are typically concerned about. There are many examples of <b>adverse selection</b> commonly available from insurance references and educational material. However, our concern is that the exposure draft definition is too vague and may not be sufficiently broad enough to clearly encompass actions by both the <b>risk subjects</b> and the protection providers (e.g., insurers) within the <b>financial or personal security system</b>.</p>
<p>2.6</p>	<p><b>Replace the following wording:</b></p> <p><u>Risk Measure</u>—A measurement of the outcomes of a contingent event mitigated by the financial or personal security system. Examples of risk measures include mortality rates, healthcare costs, and claim frequency and severity.</p> <p><b>With the recommended wording below (additions are highlighted):</b></p> <p><u>Risk Measure</u>—A measurement of the risk associated with the possible outcomes from contingent events covered or mitigated by a financial or personal security system. Examples of possible outcomes from contingent events include mortality rates, healthcare costs, and claim frequency and claim severity. Examples of risk measures include estimated covered costs based on the expected value or mean, the mean adjusted by a risk margin, or a quantile of the distribution of possible outcomes. Other risk measures may be appropriate for the intended purpose or intended use of the risk classification framework.</p>	<p>“Risk measure” is already a term of art in actuarial science, and it can refer to technical concepts such as deviance, variance, value-at-risk, tail-value-at-risk, expected policyholder deficit (EPD), etc. The items listed in the exposure draft are risk <i>outcomes</i>, not <b>risk measures</b>. Because actuaries may need to leverage concepts such as deviance or EPD when making <b>risk classification</b> decisions, the use of “risk measure” with a different meaning would be confusing.</p> <p>The examples of <b>risk measures</b> suggested are used in other ASOPs, such as the “intended measure” in ASOP No. 43 and ASOP No. 53. The exposure draft mixes examples of possible outcomes with examples of <b>risk measures</b>. The suggested wording attempts to clarify what is intended.</p>

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<p>2.8</p>	<p><b>Replace the following wording:</b></p> <p><u>Unintended Bias</u> —Impacts or outcomes on specific <b>risk subjects</b> resulting from the use of a <b>risk classification framework</b> that is not intentionally designed to result in such impacts or outcomes.</p> <p><b>With the recommended wording below (additions are highlighted):</b></p> <p><b>Risk Classification Bias</b>—The impacts or outcomes on <b>risk subjects</b> resulting from the use of a <b>risk classification framework</b> which contradicts or conflicts with applicable law or with the intended purpose of the <b>risk classification framework</b>.</p>	<p>“Bias” is a challenging term to define for actuarial practice. It has a colloquial meaning as well as technical definitions across multiple disciplines (e.g., statistics, data science, psychology, sociology, law). We believe the standard should include a much clearer definition of bias which the actuary can rely upon in order to comply with the standard.</p> <p>The definition proposed in the exposure draft does not provide a clear definition of “bias.” The exposure draft’s use of the term “unintended” is only described for a <b>risk classification framework</b> that is based on an intentional design to result in certain impacts or outcomes. However, there is no description of the characteristics of biased impacts or outcomes. We are concerned that the language proposed in the exposure draft seems to rely on some common interpretations or uses of the term “bias” with respect to a <b>risk classification framework</b>. In our discussions of this term, we found that interpretations varied significantly between actuaries, and the exposure draft definition did not help us determine the intended meaning. References to biased impacts or outcomes are not described sufficiently for the actuary to consider such impact or outcomes.</p> <p>Unfortunately, there are no common actuarial principles or generally accepted actuarial practices for defining different types of bias or the underlying causes of such bias. A more practical approach would be to define <b>risk classification bias</b> in terms of adverse impacts or outcomes on <b>risk subjects</b> resulting from the use of a <b>risk classification framework</b>. However, we feel that the application of such a definition should only apply when there is contradiction or conflict with the applicable laws or with the intended purpose of the <b>risk classification framework</b>.</p> <p>“Risk Classification Bias” is offered as a potential solution which connects the concept of bias to what is relevant to this ASOP, i.e., applicable law or intended purpose. See further rationale provided below in section 3.4 where this term is used.</p>
<p>Section 2</p>	<p><b>Add the following definition of “protected class” (additions are highlighted):</b></p> <p><b>Protected Class</b>—A group of individuals or entities as protected under applicable law based on attributes or characteristics as defined under such law. Note that protected attributes or characteristics may differ from the other definitions provided in this standard, such as</p>	<p>The term <b>Protected Class</b> should be defined in this standard, clarifying that it does not deviate from the legal definition. The application of <b>Protected Classes</b>, or protected attributes, is quite specific to the law or regulatory authority that governs the definition and the purpose of the protection imposed by such authority. This standard should simply recognize <b>protected classes</b> as something that may be imposed on the design or use of a <b>risk classification framework</b> or may have an effect on what attributes are used and how they are used.</p>

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	<p><b>risk characteristics</b> and protected attributes or characteristics may not align with <b>risk characteristics</b>.</p>	<p>Alternatively, the recommended addition could define protected attributes or protected characteristics, instead of “protected class.” The use of the term “protected class” seems to be used more often, but the classification of “protected class” tends to be defined in law according to a list of characteristics or attributes associated with individuals or groups of people.</p>
<p>3.2</p>	<p><b>Replace the following wording:</b></p> <p>The actuary should exercise professional judgment when providing actuarial services related to risk classification. The actuary may use data, information, or studies that are reasonable in the actuary’s professional judgment.</p> <p><b>With the recommended wording below (additions are highlighted):</b></p> <p>The intended purpose of and approaches to <b>risk classification frameworks</b> can vary significantly. The actuary may use data, information, models, studies, analytical tools, or professional judgment when providing actuarial services related to <b>risk classification frameworks</b>.</p>	<p>The deleted sentence is redundant with the last sentence of this section. Also, the standard should not point out that the actuary should exercise professional judgment for some considerations while being silent on others.</p> <p>The last sentence refers to “reasonable” actuarial judgment. Such wording seems to emphasize the use of professional judgment that the actuary considers to be reasonable, but that should be implicit in all actuarial standards. The exceptions are addressed in section 3.6 or section 4 disclosure when the actuary relies on information, assumptions, methods, etc., provided by someone else. Models and analytical tools would be valuable additional examples of what the actuary uses to provide actuarial services which uses the data and information.</p>
<p>3.2.1 and 3.2.9</p>	<p><b>Replace the following wording:</b></p> <p><u>3.2.1 Intended Purpose</u>—The actuary should confirm that the risk classification framework is appropriate for the intended purpose and intended use.</p> <p><u>3.2.9 Effectiveness</u>—The actuary should evaluate the effectiveness of the risk classification framework at supporting the viability of the financial or personal security system.</p> <p><b>With the recommended combined wording below (additions are highlighted):</b></p>	<p>The current ASOP No. 12 includes section 3.3.1 on intended use which has been eliminated in the exposure draft. Reference to both intended purpose and intended use appears in the exposure draft (first sentence). “Intended Use” should be included in the title of this section for consistency and importance.</p> <p>Other ASOPs largely govern the intended use of <b>risk classification frameworks</b>, but those various uses are not covered in ASOP No. 12. For P&amp;C pricing for example, ASOP No.12 would cover the grouping of <b>risk subjects</b> into <b>risk classes</b>, while ASOP No. 53 would be the standard for estimating the future costs for each <b>risk class</b>.</p> <p>Section 3.2.9 (on effectiveness) is only one sentence and is closely related to section 3.2.1 (intended purpose). Combining these two sections into one section would be clearer for the reader. The added sentence is taken from section 3.2.9, which does not need to be its own section, and can be better understood when combined with section 3.2.1.</p>

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	<p>3.2.1 <u>Intended Purpose and Intended Use</u>—The actuary should evaluate and confirm that the <b>risk classification framework</b> is appropriate for <del>the</del> its intended purpose and intended use. The actuary should evaluate the ability of the <b>risk classification framework</b> to satisfy its intended purpose or to support the viability of the <b>financial or personal security system</b>.</p>	
<p>3.2.3</p>	<p><b>Replace the following wording:</b></p> <p><u>Relationship of Risk Characteristics and the Risk Measures</u>—The actuary should have a rational explanation that the relationship between a risk characteristic and a risk measure is not obscure, irrelevant, or arbitrary; however, the actuary is not required to demonstrate a causal relationship.</p> <p>In some cases, the actuary may lack clear evidence or face other practical impediments to demonstrate a consistent relationship between risk characteristics and a risk measure. In such circumstances, the actuary may use professional judgment to select risk characteristics.</p> <p>Whether it is appropriate to use a risk characteristic may depend on societal, regulatory, and industry practices or may depend on the scope and context of the actuary’s work.</p> <p><b>With the recommended wording below (additions are highlighted):</b></p> <p><u>Relationship of Risk Characteristics and the Risk Measures</u>—The actuary should consider the extent to which the relationship between a <b>risk characteristic</b> and a <b>risk measure</b> is reasonable for the intended purpose of the <b>risk classification framework</b>.</p>	<p>Seeking a “rational explanation” and avoiding “obscure, irrelevant, or arbitrary” relationships have intuitive appeal. However, in practice these concepts are subjective. They are prone to cognitive biases (using the term here as defined by psychologists) such as availability bias and confirmation bias. Actuaries should primarily justify <b>risk characteristics</b> based on the relationship with anticipated experience, not with rhetoric or personal opinions. Additional concerns with these terms are explained below.</p> <p>If these terms remain in the final standard, the actuarial community will need a practice note or similar type of non-binding guidance to discuss the application of such terms in actuarial practice.</p> <p>This revision reintroduces the first paragraph of the current section 3.2.1, edited to change “expected outcome” to “<b>risk measure</b>” in alignment with the new definitions. This idea is a core actuarial concept – because insurance prices must be set prior to incurred costs, the justification for a risk classification system is based on anticipated loss experience. We believe it should not be removed from the ASOP.</p> <p>The actuary might be able to justify why the relationship between the <b>risk measure</b> and <b>risk characteristic</b> appears to exist, i.e., the relationship is plausible. For this standard, “plausible” might be more appropriate than “rational.” Plausibility relies on either common sense or having some basic evidence, such as historical correlations in the data. Also, the plausibility of a relationship would not normally be based on an anomaly, e.g., risk classification should not rely on a <b>risk measure</b> that outweighs a single large claim.</p> <p>In a disputed or adversarial situation, plausibility would give the actuary better guidance and flexibility without simply relying on the professional judgment of the actuary. The Code of Professional Conduct certainly covers the actuary’s responsibility to avoid misrepresentation. However, we recommend adding reference to “reasonable</p>

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<p>The actuary should select <b>risk characteristics</b> that are related to <b>risk measures</b>. For example, a relationship between a <b>risk characteristic</b> and a <b>risk measure</b> is demonstrated if it can be shown that the variation in actual or reasonably anticipated experience correlates to the <b>risk characteristic</b>.</p> <p>In demonstrating a relationship, the actuary may use relevant information from any reliable source, including statistical or other analysis of available data. The actuary may also use clinical experience and expert opinion. However, the actuary is not required to demonstrate a causal relationship.</p> <p>In some cases, the actuary may lack clear evidence or face other practical impediments to demonstrate a consistent relationship between <b>risk characteristics</b> and a <b>risk measure</b>. In such circumstances, the actuary may be able to use professional judgment to select <b>risk characteristics</b> which are plausible and explainable by the actuary.</p> <p>The actuary should take into account the practicality and the appropriateness of using a <b>risk characteristic</b> depending on the societal, regulatory, and industry practices, consistent with the intended purpose and intended use of the actuary's work.</p>	<p>for the intended purpose" in the first sentence and including "plausible" in the suggested edits. We believe these edits are preferable to simply removing the term "rational explanation."</p> <p>An NAIC P&amp;C task force introduced the term "rational explanation" in its discussions recently. This term may or may not become part of laws or have the force of law. The standard should not use this term until there is a common usage in actuarial practice, especially across practice areas, or until there is a law or regulatory guidance which defines it.</p> <p>With respect to the wording in the last paragraph, "Whether it is appropriate ... may depend on the scope and context of the actuary's assignment," such conditions are problematic. In general, we would expect that the actuary's work to be relied upon with respect to the intended purpose and use of the <b>risk classification framework</b>. Consequently, the standard should not permit the scope of the actuary's assignment to be established in such a way as to ignore any of the requirements otherwise set forth in the standard. However, the standard should allow for the situation where the actuary is unable to comply with the requirements in the standard and in such cases the actuary can make appropriate disclosures. In such a disclosure, the actuary should provide an explanation concerning the reason(s) the actuary is unable to comply. If the scope of the actuary's assignment excludes certain considerations or actions by the actuary which the standard requires, then the actuary should disclose such exclusions from the actuary's assignment.</p> <p>The language in the exposure draft appears to direct the actuary to be confident that the relationship is "<b>NOT obscure, irrelevant, or arbitrary</b>." This language is awkward and problematic, especially in an actuarial standard. It would be onerous for the actuary to prove such "not" attributes about the relationship in such terms. The Code of Professional Conduct is sufficient in general with respect to an actuary not relying on a relationship that is obscure, irrelevant, or arbitrary.</p> <p>The recommended rewording would clarify what the standard requires of the actuary. The exposure draft wording is too passive and does not clearly impose any consideration by the actuary. Use of the term "context" is vague and unrelated to other sections of the exposure draft. The recommended edit explicitly refers to the "intended purpose and intended use," which better aligns with the other sections of the exposure draft and the other recommended edits.</p>
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		<p>Some actuaries may have concerns about the potential for misuse or misapplication of “societal” practices. These concerns focus on how to apply these considerations. We found evidence that this is not a new concept. For example, there is reference to “social criteria” such as controllability and affordability in Chapter 5: Risk Classification of <i>Foundations of Casualty Actuarial Science</i> (1989). As such, we do not object to its inclusion in the ASOP.</p>
<p>3.2.4</p>	<p><b>Replace the following wording:</b></p> <p><u>Multivariate Effects</u>—The actuary should assess whether multivariate effects, interdependencies, or correlations among risk characteristics are material to the assignment of risk subjects to an appropriate risk class. To the extent practical, the actuary should take into account multivariate effects, interdependencies, or correlations.</p> <p><b>With the recommended wording below ( additions / deletions are marked):</b></p> <p><u>Multivariate Effects</u>—The actuary should assess whether multivariate effects or <del>correlations</del> interdependencies among <b>risk characteristics</b> are material to the assignment of <b>risk subjects</b> to an appropriate <b>risk class</b>. To the extent <del>practical</del> <b>material</b>, the actuary should take into account such <b>multivariate effects</b> or <del>correlations</del> interdependencies, including statistical correlations, which could have a material adverse impact from the potential misclassification of <b>risk subjects to risk class</b>.</p>	<p>Correlations can be spurious or immaterial and should be reviewed for reasonableness. The term “correlations” is a subset of multivariate effects and interdependencies and is typically referred to as statistical correlations. The standard does not need to reference correlations as distinct from multivariate effects and interdependencies.</p> <p>The actuary’s obligation to “take into account” should be based on the actuary’s assessment of the potential for material misassignments of <b>risk subjects to risk classes</b>. Practicality is a limitation on what the actuary might be able to accomplish. Practicality is addressed in section 3.2.7 and applies to the entire standard.</p>
<p>3.2.4</p>	<p><b>Delete the following wording:</b></p> <p>“To the extent practical ....”</p>	<p>The wording, “To the extent practical” should be deleted because section 3.2.7 addresses practicality separately, so it is redundant and inconsistent for the standard to repeat “when practical” in some sections, but not in other sections.</p>

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<p>3.2.5</p>	<p><b>Replace the following wording:</b></p> <p><u>Effect of Adverse Selection</u>—The actuary should assess the potential for <b>adverse selection</b> effects that may result or have resulted from the design, development, selection, modification, or continued use of the <b>risk classification framework</b>. The actuary should take into account that a lack of ongoing monitoring of the <b>risk classification framework</b> may increase the risk of <b>adverse selection</b>. When practical and appropriate within the scope of the actuary’s assignment, the actuary should consider estimating the potential impact of <b>adverse selection</b> or mitigating the impacts of material <b>adverse selection</b>.</p> <p><b>With the recommended wording below:</b></p> <p><u>Effect of Adverse Selection</u>—The actuary should consider the potential for <b>adverse selection</b> to have a material adverse impact on satisfying the intended purpose of the <b>risk classification framework</b> or in supporting the viability of the <b>financial or personal security system</b>. The actuary should also take into account that a deficiency in ongoing monitoring of the <b>risk classification framework</b> may increase the risk of <b>adverse selection</b>.</p> <p>When the actuary considers there to be a potential material adverse impact, then the actuary should assess the adverse impact. Such an assessment may include estimating the potential impact of <b>adverse selection</b> or providing suggestions for mitigating the material adverse impacts of <b>adverse selection</b>. If the actuary is unable to make such an assessment, then the actuary should refer to section 4 for appropriate disclosures.</p>	<p>Recommended revised first sentence helps the actuary focus on the main issue that <b>adverse selection</b> could potentially pose a material threat to the usefulness and appropriateness of the <b>risk classification framework</b> in achieving its intended purpose or in supporting the viability of the <b>financial or personal security system</b>. Use of the verb “consider” is preferable to the verb “assess” because an assessment suggests that the actuary should express an opinion on the materiality of the potential adverse impact. An assessment may not be necessary in every situation.</p> <p>The ASOP should better address <b>adverse selection</b> as a potential material issue for the actuary. The recommended practice (section 3) of the standard should describe what the actuary should do regarding <b>adverse selection</b>. Additional paragraphs are recommended to be added, as shown, to achieve this.</p> <p>It seems superfluous to include “practical and appropriate” in this standard. Without those as stated conditions, the actuary would not need to make a judgment as to whether “estimating” or “mitigating” would be “practical and appropriate.”</p> <p>Having the condition “within the scope of the actuary’s assignment...” is problematic. This wording should be deleted because the section on practicality is addressed separately (see section 3.2.7 and recommended edits to move 3.2.7 to a new section 3.8). It is redundant and inconsistent for the standard to repeat “when practical” in some sections, but not in other sections.</p> <p>In general, we would expect the actuary’s work to be relied upon with respect to the intended purpose and use of <b>risk classification framework</b>. Consequently, the standard should not permit the scope of the actuary’s assignment to ignore <b>adverse selection</b>. However, the suggested edits allow for the situation where the actuary is unable to assess <b>adverse selection</b> and in such cases the actuary can make appropriate disclosures.</p> <p>In such a disclosure, the actuary should provide an explanation concerning the reason(s) the actuary is unable to comply. If the scope of the actuary’s assignment excludes certain considerations or actions by the actuary which the standard requires, then the actuary should disclose such exclusions from the actuary’s assignment.</p>
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<p>3.2.6</p>	<p><b>Change the language as follows (additions / deletions marked):</b></p> <p><u>Objectivity</u>—The actuary should take into account the extent to which the <b>risk characteristics</b> can be objectively determined. <b>The actuary may judge that a risk characteristic</b> can be objectively determined <del>if it is</del> based on verifiable facts or <del>if, in the actuary’s judgment,</del> that the potential for <b>inconsistencies or risk classification bias</b> in such a determination is not <b>material</b>. <del>manipulation is not significant</del>. For example, “blindness” may not be an objectively determinable <b>risk characteristic</b>, whereas “vision corrected to no better than 20/100” is a <b>risk characteristic</b> more clearly based on verifiable facts.</p>	<p>Objectivity is seldom a definitive YES or NO. Rather, the actuary will typically make observations and judgments to assess the degree of objectivity for determining <b>risk characteristics</b>.</p> <p>ASOP No. 1 addresses materiality and is quite helpful in this regard. ASOP No. 1 also addresses use of the words “significant” and “significance,” which can be rather nebulous, especially in the context of objectivity. In particular, ASOP No. 1 notes that “a result may be significant because of its consequence.” Materiality more directly connotes that consequences can be severe and corrective actions should be taken.</p> <p>The suggested definition of “risk classification bias” provided by this commentator for section 2.8 connects objectivity to the intended purpose of the <b>risk classification framework</b>.</p>
<p>3.2.7</p>	<p><b>Expand the language as follows (additions are highlighted):</b></p> <p><u>Practicality</u>—The cost, time, and effort associated with <b>risk classification</b> may increase as the complexity increases. The actuary should take into account the following:</p> <ol style="list-style-type: none"> <li>a. the balance among homogeneity within <b>risk classes</b>, heterogeneity between <b>risk classes</b>, and credibility <b>of the data for</b> individual <b>risk classes</b>;</li> <li>b. <b>the availability and accuracy of the needed data</b>; and</li> <li>c. simplicity, ease of use, ease of explanation, and market acceptance.</li> </ol>	<p>The exposure draft refers to “practical” in several sections, listed above in the response to section 1.2.</p> <p>Practicality is addressed in section 3.2.7, so it is redundant and inconsistent for the standard to repeat “when practical” or “to the extent practical,” in some sections, but not in other sections.</p> <ol style="list-style-type: none"> <li>(a) Credibility is an attribute of data, rather than of <b>risk classes</b>. The recommended edit clarifies this.</li> <li>(b) The exposure draft doesn’t clarify that while some <b>risk characteristics</b> may theoretically be desirable to use, it may be impractical to obtain the needed data and to ensure that data is accurate. Edits are recommended to address this point.</li> </ol>
<p>3.2.8</p>	<p><b>Change the language as follows (additions / deletions marked):</b></p> <p><u>External Environment</u>—The actuary should take into account known or emerging external influences that have the potential for material adverse impacts on the <del>effectiveness</del> <b>ability</b> of the <b>risk classification framework</b> <b>to satisfy its intended purpose</b> or <b>to support</b> <del>on</del> the viability of the <b>financial or personal security system</b>.</p>	<p>Alternative language is proposed as more direct and easier to interpret than “effectiveness,” such as “the ability of a <b>risk classification framework</b> to satisfy its intended purpose” or simply “the fitness for purpose” of the framework (see comments for section 3.2.9). There is no guidance, common actuarial principles, or other authoritative references that address “effectiveness.” As a result, the exposure draft language is unnecessarily confusing and potentially vulnerable to subjective and inconsistent interpretation. This recommendation is consistent with the recommended edits for section 3.2.9.</p>

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	<p>Such external influences include applicable law and business, government, and industry practices.</p>	<p>Alternatively, revising section 3.2.9 from “effectiveness” to “Fitness for Purpose” could be a useful way to streamline the verbiage in this and other sections.</p> <p>“Fitness for Purpose” is a more relevant term and a better fit for this section. This term has a legal basis in contract law which fits this section well. The term “fitness for purpose” simply refers to a product or service that meets its intended purpose.</p> <p>When a professional is engaged for a particular purpose, Fitness for Purpose is an implied condition that the services will be reasonably “fit” for that purpose (the principal’s requirements, needs, or desires). Alternatively, adding a definition for “Fitness for Purpose” could be a useful way to streamline the verbiage in several sections.</p>
<p>3.2.9</p>	<p><b>Replace the following wording:</b></p> <p><b>Effectiveness—The actuary should evaluate the effectiveness of the risk classification framework at supporting the viability of the financial or personal security system.</b></p> <p><b>With the recommended wording below (additions are highlighted):</b></p> <p><b>Fitness for Purpose—The actuary should evaluate the ability of the risk classification framework to satisfy its intended purpose or to support the viability of the financial or personal security system.</b></p>	<p>“Fitness for Purpose” is a more relevant title and a better fit for this section. This term has a legal basis in contract law which fits this section well. The term “fitness for purpose” simply refers to a product or service that meets its intended purpose.</p> <p>When a professional is engaged for a particular purpose, Fitness for Purpose is an implied condition that the services will be reasonably “fit” for that purpose (the principal’s requirements, needs, or desires). Alternatively, adding a definition for “Fitness for Purpose” could be a useful way to streamline the verbiage in several sections.</p> <p>An alternate approach would be to combine this section with 3.2.1 (Intended Purpose). These concepts are closely related and combining them would be clearer for the reader. The recommended combination would also eliminate the need for a title for this section.</p>
<p>3.3</p>	<p><b>Change the language as follows (additions / deletions marked):</b></p> <p><b>Existing Risk Classification Frameworks—When modifying, using, reviewing, evaluating, or opining on <del>any elements of</del> an existing risk classification framework, the actuary should understand the frequency of past reviews and the extent of previous changes made to the risk classification framework. The actuary should take into account whether past, recent, or expected changes or lack of changes made to the risk classification</b></p>	<p>The wording “any elements” is too broad and can be onerous for the actuary to consider “any” element even when simply using the <b>risk classification framework</b> for an intended purpose for which it was designed. There should not be a requirement for the actuary to test the <b>risk classification framework</b> for “any” elements which the actuary would otherwise reasonably and professionally consider to be insignificant and immaterial.</p> <p>The recommended edits for this section are consistent with our recommended edits to other sections, including the recommended edits for section 3.2.9. Alternatively, replacing “effectiveness” with “Fitness for Purpose” could be a useful way to streamline the verbiage in this and other sections.</p>

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	<p><b>framework</b> have the potential to have a material adverse impact on the <b>effectiveness</b> ability of the <b>risk classification framework</b> to satisfy its intended purpose or to support <del>on</del> the viability of the <b>financial or personal security system</b>.</p> <p>The actuary should take into account whether the <b>risk classification framework</b> will remain appropriate for its intended purpose and <b>intended</b> use. Such changes could include those affecting the <b>risk characteristics</b> or <b>risk measures</b> used <del>for</del> by the <b>risk classification framework</b>.</p> <p>When reviewing or evaluating a <b>risk classification framework</b>, the actuary should consider testing the <b>risk classification framework</b>, which might involve alternative <b>risk classes</b> using different <b>risk characteristics</b> or <b>risk measures</b> than used for the <b>risk classification framework</b>.</p>	<p>ASOP No. 12 currently includes a separate section on testing the risk classification system. This part of the standard should be retained in some form. The recommended edits provide a short and simple way to accomplish keeping testing as an essential part of the standard.</p>
<p>3.4</p>	<p><b>Change the language as follows (additions / deletions marked):</b></p> <p>Potential for <b>Risk Classification Unintended Bias</b>—The actuary should consider the potential for <b>risk classification unintended bias</b> as appropriate within the <del>scope of the actuary’s assignment</del> that could result in material adverse impacts on the ability of the <b>risk classification framework</b> to satisfy its intended purpose or to support the <b>viability</b> of the <b>financial or personal security system</b>.</p>	<p>“Bias” is a challenging term to define for actuarial practice. It has a colloquial meaning as well as technical definitions across multiple disciplines (e.g., statistics, data science, psychology, sociology, law). We believe the standard should include a much clearer definition of bias which the actuary can rely upon in order to comply with the standard. A recommended definition of <b>risk classification bias</b> is suggested in place of <b>unintended bias</b> in section 2.8. Our recommended edit seeks to provide a clearer definition of a more useful concept.</p> <p>This standard should not require the actuary to determine the intentions for the design or use of the <b>risk classification framework</b>.</p> <p>The actuary should consider whether <b>risk classification bias</b> is material. The standard should limit the scope to types of bias relevant to common purposes for a <b>risk classification framework</b> in terms of capturing how the actuary should deal with this type of bias (i.e., <b>risk classification bias</b>).</p> <p>Some users may refer to bias in the context of risk classification based on “expected” outcomes, rather than actual outcomes. However, the use of the term “expected” should not be limited to a probability-weighted “expected value” or a statistical</p>

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		<p>average or mean value, or to situations where there is a high probability of a narrow range of outcomes.</p> <p>Unfortunately, there are no common actuarial principles or generally accepted actuarial practices for detecting different types of bias or the underlying causes of such bias. A more practical approach would be to define <b>risk classification bias</b> in terms of adverse impacts or outcomes on <b>risk subjects</b> resulting from the use of a <b>risk classification framework</b>, but only when there is contradiction or conflict with the applicable laws or with the intended purpose of the <b>risk classification framework</b>. We believe that our recommended approach would be more relevant for an actuarial standard than requiring the actuary to try to determine if an unintentional bias exists.</p> <p>These recommended edits are consistent with the recommended edits for sections 2.8 and 3.2.9. Alternatively, adding a definition for “Fitness for Purpose” could be a useful way to streamline the verbiage in this and other sections. Fitness for Purpose would eliminate the need to repeat wording, such as “could result in material adverse impacts on the ability of the <b>risk classification framework</b> to satisfy its intended purpose or to support the viability of the <b>financial or personal security system</b>.”</p>
3.4	<p><b>Delete the following wording:</b></p> <p>“...as appropriate within the scope...”</p>	<p>The wording “...as appropriate within the scope...” should be deleted because the actuary’s work should be relied upon with respect to the intended purpose and use of the <b>risk classification framework</b>. Consequently, the standard should not permit the scope of the actuary’s assignment to be established in such a way as to ignore any of the requirements otherwise set forth in the standard. However, the standard should allow for the situation where compliance with the ASOP is not applicable or practical, or the actuary is unable to comply with the requirements in the standard, and in such cases the actuary can make appropriate disclosures. In such a disclosure, the actuary should provide an explanation concerning the reason(s) the actuary did not comply. If the scope of the actuary’s assignment excludes certain considerations or actions by the actuary which the standard requires, then the actuary should disclose such exclusions from the actuary’s assignment.</p>
3.5	<p><b>Change the language as follows (additions / deletions marked):</b></p>	<p>The recommended edits clarify that the actuary should understand both the applicable laws and accepted practices with regard to <b>protected classes, risk classification bias</b>, and methods for assessing the potential for prohibited impacts or outcomes.</p>

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	<p><b>Potential Impacts on Protected Classes</b>—The actuary <del>must follow applicable law regarding</del> should consider the potential for <del>unintended bias</del> prohibited or restricted impacts or outcomes on <b>risk subjects in protected classes</b>. <del>When doing so,</del>The actuary should understand the applicable laws and the practices used to comply with the laws with regards to the following:</p> <ol style="list-style-type: none"> <li>how <b>protected classes</b> are defined and identified <del>according to applicable law</del>;</li> <li>how <b>risk classification bias</b> is treated <del>under applicable law, if applicable</del>; and</li> <li><del>methods for estimating the impact of the risk classification framework on protected classes are addressed under applicable law, if applicable.</del> the methods and data the actuary may select and apply in order to assess the potential for prohibited or restricted impacts or outcomes on <b>risk subjects in protected classes</b> due to use of the <b>risk classification framework</b>.</li> </ol>	<p>The phrase in the first sentence in this section “must follow applicable law” is redundant with section 1.2 which states that “...the actuary should comply with applicable law.” Also, this wording is not an appropriate use of “must follow” given the requirements in sections 1.2 and 4.2 (a) and (c) regarding conflicts with applicable law and departures from the standard in order to comply with applicable law. These parts of many standards cover the actuary’s responsibilities with regard to applicable law and address how to handle the guidance in the standard if it conflicts with applicable law.</p> <p>The application of <b>Protected Classes</b>, or protected attributes, is very specific to the law or regulatory authority that governs the definition and the purpose of the protection imposed by such authority. The ASOP should simply recognize <b>protected classes</b> as something that may be imposed on the design or use of a <b>risk classification framework</b> or have an effect on what attributes are used and how they are used.</p> <p><b>Protected Class</b> should be defined for purposes of this standard. A suggested definition is submitted under section 2.</p> <p>The recommended edits are intended to provide guidance that is clear about the relationship of how such protected attributes are defined and treated under laws and regulations, and points to the actuary’s obligations to understand the requirements of such laws with respect to the actuary’s work.</p>
<p>3.2.7 - Change to 3.8</p>	<p><b>Change the language as follows (additions / deletions marked):</b></p> <p>Practicality— The actuary may face practical issues and limitations which affect the actuarial services performed or the use of the actuary's work within the scope of this standard. The actuary <del>should</del> may take into account the following <b>practical considerations</b>:</p> <ol style="list-style-type: none"> <li>the cost, time and effort associated with the <b>design, development, selection, modification, review, evaluation, opinion on, or use of the risk classification framework</b>;</li> </ol>	<p>Practicality should be covered more broadly than in the current exposure draft wording for 3.2.7. We recommend that the Practicality section be moved to a higher level in the standard, possibly 3.8, rather than being a subsection under 3.2.</p> <p>There are other 3.x sections where practicality is also an important consideration. Generally, it would be better to have one section on this topic, rather than repeated references to "practical considerations" in many sections of the standard. And it also avoids the issue that sections that do not mention practical considerations would be somehow treated differently than sections that do.</p> <p>Additional edits may be needed in some sections to more clearly direct the reader to the section in the standard on practicality.</p>

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	<p>b. the balance among homogeneity within <b>risk classes</b>, heterogeneity between <b>risk classes</b>, and credibility of the individual <b>risk classes</b>; and</p> <p>c. simplicity, ease of use, ease of explanation, and market acceptance of the <b>risk characteristics and the risk classification framework</b>.</p> <p>As the complexity of the <b>risk characteristics</b> increases and the intended purpose of the <b>risk classification framework</b> broadens, implementation becomes more challenging and practicality considerations becomes more important. The actuary should consider practicality as it may have an impact on each section of this standard.</p>	
<p>4.1 e-h</p>	<p><b>Change the language as follows (additions / deletions marked):</b></p> <p><u>Required Disclosures in an Actuarial Report</u>—When issuing an actuarial report, the actuary should refer to ASOP Nos. 23, 41, and 56. In addition, the actuary should disclose the following in such actuarial reports, if applicable:</p> <p>e. the impact of significant <b>adverse selection</b> on the <b>effectiveness ability</b> of the <b>risk classification framework to satisfy its intended purpose</b> or <del>or</del> <b>to support</b> the viability of the <b>financial or personal security system</b> (see section 3.2.5);</p> <p>f. external influences that have a known material adverse impact on the <b>effectiveness ability</b> of the <b>risk classification framework to satisfy its intended purpose</b> or <del>or</del> <b>to support</b> the viability of the <b>financial or personal security system</b> (see section 3.2.8);</p> <p>g. the <b>effectiveness ability</b> of the <b>risk classification</b></p>	<p>Recommended edits for subsections 4.1 (e) through (h) are consistent with the recommended edits for sections 3.2.5, 3.2.8, 3.2.9, and 3.3, respectively.</p> <p>Subsection 4.1 (g) should refer to a new 3.2.1 if the corresponding recommended combination of 3.2.9 into 3.2.1 is accepted.</p>



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	<p>framework to satisfy its intended purpose or <del>en</del> to support the viability of the financial or personal security system (see section 3.2.9);</p> <p>h. changes made to the risk classification framework, and the impact such changes could have on the effectiveness ability of the risk classification framework to satisfy its intended purpose or <del>en</del> to support the viability of the financial or personal security system (see section 3.3); and</p>	
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**IV. General Recommendations (If Any):**

<b>Commentator Recommendation (Identify relevant sections when possible)</b>	<b>Commentator Rationale (Support for the recommendation)</b>
<p>Consider withdrawing the Exposure Draft and issuing a Discussion Draft or a less formal Request for Comments.</p>	<p>The ASB Procedures Manual (Section C) encourages the committee or task force “to seek a wide range of ideas and views on the subject...” Because ASOP No. 12 is not a new standard, the possibility of issuing a discussion draft or other document to request comments regarding revisions to ASOP No. 12 may not have been considered. However, we believe that there are a number of critical questions where many actuaries have various views and opinions regarding the exposure draft.</p> <p>The Procedures Manual also states, “While requests for comments and discussion drafts have been a common means, outside of formal exposure drafts, for soliciting input, the ASB is not limited to these approaches and may approve other formats for soliciting input.”</p> <p>We support the goal of revising this ASOP to help actuaries, and those who rely on the work of actuaries, better address some issues which have been the subject of concern to actuaries and their principals, public debate, and proposed and issued regulations and legislation. However, to our knowledge, there has been no attempt by the Task Force to solicit input from the community of those practicing actuaries most likely affected by these changes to the standard.</p> <p>The references in the exposure draft to “bias,” rational explanation,” “unintentional,” “protected classes,” “adverse selection,” the phrase “not obscure, irrelevant or arbitrary,” and other changes are of critical concern to us. Actuaries in different practice</p>

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	<p>areas have already commented that the wording in exposure draft is too vague and would be onerous to follow in practice. We agree with and echo those comments.</p> <p>We suggest that much of the existing wording regarding expected costs remains important and should be incorporated into the revised standard. At a minimum, reference to expected costs as an example would alleviate concerns that something more than expected costs is required. The change to risk measure can be appropriate if there are reasons for when expected costs are not sufficient for the intended purpose of the risk classification framework.</p>
Clarify how the standard aligns with common insurance laws and regulations.	Common state insurance laws and regulations for P&C insurance require that rates shall not be "excessive, inadequate or unfairly discriminatory." There is also a Statement of Principles, and those P&C principles have the same language regarding rates and also refer to actuarial soundness. These laws, regulations, and principles are difficult to pair up with the exposure draft. In particular, is actuarial fairness or actuarial soundness the same as "not unfairly discriminatory"—and how does an actuary reference the concept of unfairly discriminatory with respect to unintended bias (or any type of bias)?
Consider providing more opportunities for ASB presentations and public discussions on the standard.	We believe that having opportunities for exposure and discussion about the changes at actuarial meetings or webinars, virtually and/or in person, can provide opportunities for the ASB to receive valuable input and engage in discussions about the implications of the drafted changes. Our suggestion for a Discussion Draft could be very helpful to iron out some of the concerns about some of the wording in the exposure draft and the implications to actuaries in following the standard.
Consider holding a public hearing.	The ASB Procedures Manual outlines the process for holding a public hearing regarding a proposed ASOP. We believe that the factors listed in the manual for deciding to hold a public hearing, such as complexity, level of controversy, and significance to the profession of the guidance provided, all are very relevant for this standard.
For section 1.1 or 1.2, clarify that several other ASOPs largely govern how <b>risk classification frameworks</b> are applied to specific types of actuarial work. For example, ASOP No. 53 has importance for certain actuarial tasks which are not specifically covered in ASOP No. 12.	<p>It could be clearer (perhaps with examples) of how ASOP No. 12 connects with other standards for actuarial tasks. For P&amp;C pricing for example, ASOP No.12 would cover the grouping of <b>risk subjects</b> into <b>risk classes</b>, while ASOP No. 53 would primarily be the guidance for estimating expected future costs for each <b>risk class</b>. As the standard and the exposure draft are currently written and based on common industry usage of the term "risk classification," many P&amp;C actuaries would not make the connections between ASOP No. 53 and ASOP No. 12 as both being relevant for the estimation of expected future costs by <b>risk class</b>.</p> <p>A sentence to exposure draft section 3.2.1 could be added as an example that references the connection between ASOP No. 12 and ASOP No. 53.</p>

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<p>References to the viability of <b>the financial or personal security system</b> seem unnecessary. The intended purpose and intended use of the <b>risk classification framework</b> is sufficient for this standard.</p>	<p>Removing the references to “the viability of the <b>financial or personal security system</b>” would help improve the readability of the standard.</p> <p>The current ASOP No. 12 has very few references to “the viability” of the <b>financial or personal security system</b> – mainly regarding testing the risk classification system with respect to long-term viability issues, such as from adverse selection and from using gender-neutral classes when compared to gender-specific classes.</p> <p>Recommended edits to section 3.3 are provided in order to retain the essential reference to testing.</p>
<p>Retain some language from section 3.4 of the existing standard.</p>	<p>Section 3.4 of the current ASOP No. 12 on testing the risk classification system should largely be retained. While some of the content has been folded into section 3.3 of the exposure draft, the current section 3.4.2 covers the use of different <b>risk classes</b> for testing the system than the <b>risk classes</b> used for the intended purpose of the <b>risk classification framework</b>. However, some of the current ASOP No. 12 language should be retained, as the need to test <b>risk classification frameworks</b> will continue to be an important aspect of actuarial services and may become increasingly important with accentuated public policy concerns about bias and discrimination.</p> <p>Recommended edits to section 3.3 are provided in order to retain the essential references to testing.</p> <p>The current wording of ASOP No. 12, section 3.4 is as follows:</p> <p>Testing the Risk Classification System—Upon the establishment of the risk classification system and upon subsequent review, the actuary should, if appropriate, test the long-term viability of the financial or personal security system. When performing such tests subsequent to the establishment of the risk classification system, the actuary should evaluate emerging experience and determine whether there is any significant need for change.</p>

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**I. Signature:**

Commentator Signature	Date
Amy Angell, MAAA, FCAS	May 1, 2024