August 5, 2026

Angela L. Nelson, Chair
Timothy N. Schnott, Vice Chair
Casualty Actuarial and Statistical (C) Task Force
National Association of Insurance Commissioners (NAIC)

Re: CASTF Rate Regulation White Paper Draft

Dear Chair Bettencourt and Vice Chair Nelson:

On behalf of the Casualty Practice Council's Homeowner's Insurance Task Force (Task Force) of the American Academy of Actuaries[1], we appreciate the opportunity to comment on the June 26 draft Rate Regulation white paper from the Casualty Actuarial and Statistical (C) Task Force (CASTF). The Task Force has reviewed the exposure and offers the following comments.

Professionalism and Actuarial Standards of Practice

While the exposure draft touches on actuarial standards of practice (ASOPs)[2] and the duty of actuaries to adhere to professionalism standards, the Task Force recommends this point receive a heightened emphasis throughout the paper. ASOPs and the CAS Statement of Principles[3] provide guidance in how actuaries should provide a rate that is "the expected value of all future costs associated with an individual risk transfer." Precept 8 of the Code of Professional Conduct specifically calls out that an actuary "shall take reasonable steps to ensure that such services are not used to mislead other parties[4]," which can include regulatory audiences reviewing and approving actuarial communications. Deliberate implementation of cross-state subsidization in violation of ASOPs and actuarial principles could constitute a violation of the Code of Professional Conduct. Such violations could lead to disciplinary review and/or action by the Actuarial Board for Counseling and Discipline (ABCD).

Cost of Capital and Reinsurance

The exposure draft provides some detail on the possibility of cross-subsidization if an insurer charges a profit margin different than indicated by the actuarial data in certain states due to regulatory requirements around allocation of capital and profit. The underwriting profit provision in each state's rates compensates the insurer for the surplus allocated to that state based on risk. If the profit provision required by regulatory requirements differs from the indicated profit provision, or if profit provisions are not calibrated to each state's actual cost of capital, there may be cross-subsidization between states.

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[1] The American Academy of Actuaries is a 20,000-member professional association whose mission is to serve the public and the U.S. actuarial profession. For 60 years, the Academy has assisted public policymakers on all levels by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States.
[2] "Actuarial Standards of Practice", Actuarial Standards Board
[3] "Statement of Principles Regarding Property and Casualty Insurance Ratemaking", Casualty Actuarial Society, 2021
[4] "Code of Professional Conduct", American Academy of Actuaries, 2001

Within a reinsurance context, the cost of reinsurance is commonly purchased on a company basis, so the reinsurance premium would be allocated among states. For example, consider these four types of reinsurance and how their costs would be allocated among states:

1. Property excess reinsurance can pay when a natural disaster exceeds a specified dollar amount.
2. Parametric "insurance" can pay when a natural disaster meets or exceeds specified parameters, such as wind speed.
3. Facultative reinsurance may cover a specific unique structure, such as a sports stadium or a home along a beach, coast, or river.
4. Proportional reinsurance shares premiums or losses according to an agreed percentage.

Each of these four types of reinsurance has a cost to the primary insurer. There are several possible allocation methods for a catastrophic event that triggers a reinsurance payment, which, if not appropriately accounted for in the allocation methodology, could result in cross-subsidization among states:

- Cost can be allocated by incurred or paid losses by state.
- Cost can be allocated by premiums or exposures (such as average insured home value) by state.
- Cost can be allocated by output from statistical models (such as average annual loss or modeled variability)

CASTF may want to consider the following additional clarifications to identify the advantages and disadvantages of each allocation method, address best practices for allocation among states, or distinguish practices by type of reinsurance, while also showing how limits of reinsurance layers can also impact allocations.

Recommended Revisions to the White Paper

- **Executive Summary.** The discussion should recognize that actuaries have independent professional obligations to use appropriate methods, assumptions, and standards when estimating prospective costs. References to ASOP No. 53[5] and the Statement of Principles would clarify that this discipline applies regardless of the filing framework.
- **II A. Homeowners Insurance Rating: Homeowners Rating Overview.** Consider adding references to ASOP No. 12[6] for risk classification and ASOP No. 30[7] for profit, contingencies, investment income, and required capital.
- **II A. Homeowners Insurance Rating: Homeowners Rating Influences.** Consider adding a reference to ASOP No. 25[8] in the discussion of credibility.
- **II B. Homeowners Insurance Rating: Catastrophe Risk and Pricing.** We recommend distinguishing modeled catastrophe perils from other severe weather or high-severity losses. The text should not imply that every listed model consideration is specifically mandated by regulation or an ASOP. Actuaries should consult applicable standards, including ASOP No. 38[9], ASOP No. 39[10], and ASOP No. 41.[11] Add "among other factors" to the illustrative list of rating variables.

[5] "Estimating Future Costs for Prospective Property/Casualty Risk Transfer and Risk Retention", Actuarial Standards Board
[6] "Risk Classification (for All Practice Areas)", Actuarial Standards Board, 2005
[7] "Treatment of Profit and Contingency Provisions and the Cost of Capital in Property/Casualty Insurance Ratemaking", Actuarial Standards Board
[8] "Credibility Procedures", Actuarial Standards Board, 2013
[9] "Using Models Outside the Actuary's Area of Expertise (ASOP No. 38, Revised Edition)", Actuarial Standards Board
[10] "Treatment of Catastrophe Losses in Property/Casualty Insurance Ratemaking", Actuarial Standards Board
[11] "Actuarial Communications", Actuarial Standards Board, 2010

- **II B. Homeowners Insurance Rating: Cost of Reinsurance.** Consider broadening "aggregate" to "individual event and/or aggregate" to recognize per-occurrence, per-risk, aggregate, and blended structures. Also consider revising the concluding objective to state that premiums should be an actuarially sound estimate of the expected future cost of the risk transferred during the policy period.
- **III B 2. What is Cross-Subsidization?: Rate Filing Timing Differences.** Carriers may sequence filings strategically because filing laws differ, such as prior-approval versus use-and-file systems, and because approval may be perceived as easier in some jurisdictions. Staffing constraints at departments of insurance can also lengthen reviews. The paper should consider acknowledging these operational factors because additional agency funding and hiring could improve oversight and reduce perceptions of cross-subsidization.
- **III B 3. What is Cross-Subsidization?: Mix of Business.** Consider framing rapidly growing books as a credibility and data-reliability issue, as their experience may be less credible or less predictive of future experience.
- **III B 5. What is Cross-Subsidization?: Use of Non-State Data.** Consider replacing "external" with "external to the state" or "non-state data" to accurately describe the contrast with state-specific data.
- **IV B. What State-Based Ratemaking Means for Consumers and Markets: How Insurers Deploy Capital and Reinsurance.** The enterprise-level capital discussion is central and warrants elaboration. Each state's underwriting profit provision is intended to compensate the surplus allocated to that state based on risk, generally through a target return on surplus. The paper should examine how often that target return is set at a flat enterprise-wide level rather than calibrated to each state's actual cost of capital, as this may be a potential source of cross-subsidization.
- **IV G. What State-Based Ratemaking Means for Consumers and Markets: Terminology and Methodology.** Replace "CAT model" with "catastrophe model;" add "among other factors" to the listed indication inputs; use "reasonable range" instead of "plausible range;" and clarify that comparing an indication with later emerged losses does not establish that it was over- or under-indicated.
- **IV G 3. What State-Based Ratemaking Means for Consumers and Markets: Indicated versus Implemented Rates.** The paper should more fully explain why an insurer may file below its full actuarial indication. In particular, the paper should describe what competitive pricing entails and why insurers and regulators may accept it as a valid basis for implementing less than the indicated rate in a state.

The Task Force looks forward to the continued collaborative dialogue with the NAIC as CASTF continues work on this project. If you have any questions or would like to discuss these comments further, please contact Rob Fischer, policy project manager, casualty (fischer@actuary.org, 202-785-7865).

Sincerely,

Ken Doss, MAAA, FCAS
Chairperson, Homeowners Insurance Task Force