3. (2 points)

A personal auto insurer has a highly-refined classification rating plan. In the calculation of a rate level indication for this insurer, fully assess the use of the following methods to adjust premium to current rate level:

i. Parallelogram method
ii. Extension of Exposures method

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EXAM 5 FALL 2014 SAMPLE ANSWERS AND EXAMINER'S REPORT

QUESTION 3	
TOTAL POINT VALUE: 2	**LEARNING OBJECTIVE: A3**

SAMPLE ANSWERS

i. Parallelogram method is easier to calculate than extension of exposure, but it is not as accurate as extension of exposure. Parallelogram assumes policies are written evenly throughout the year, which may not be accurate. Parallelogram calculates rate level indication on an aggregate basis. It doesn't fit for the personal auto insurer which has a highly-refined classification. Rate level at each class may not be calculated correctly.

ii. Extension of Exposure is the most accurate method, but it requires more detailed data and more computation.

I would recommend Extension of Exposure to be used here.

EXAMINER'S REPORT

This question was very open ended. The candidate received full credit if they commented on underlying assumptions, the pros and cons of each method, and related these to the specifics of the company's situation in the problem.

- Which method is easier/more difficult
- Which method is more accurate and why
- Assumption of equal writing/earning throughout policy term for parallelogram method
- One additional pro/con including the heavy IT requirement or resource intensity for EoE, the need for and difficulty of getting historical exposure data for EoE, etc.