Regulatory comment letter

To: -Third-Party Data and Models (H) Working Group, Interested Regulators, and Interested Parties
-Colorado DORA - Proposed Amended Regulation 10-1-1 regarding governance and risk management requirements for the use of external data and predictive models in insurance
From: David Schraub
Date: 5/28/2025
Subject: Response to Request for comments

Introduction

This letter is submitted as comments to both (1) the email from Kris DeFrain dated May 22, 2025, titled “Request for Third-Party Definitions”[1] and the Big Data and AI (H) Working Group AI Request for Information[2] (RFI), as well as (2) the draft Proposed Amended Regulation 10-1-1 regarding governance and risk management requirements for the use of external data and predictive models in insurance from Colorado Department of Regulatory Agencies, Division of Insurance[3] (“draft Colorado regulation 10-1-1”).

I am David Schraub, an independent actuarial consultant specializing in artificial intelligence and bias testing.

Please note that I also contribute as a volunteer with the American Academy of Actuaries to offer comments on related topics, including this one.

Concerns Regarding Bias Testing of External Data

Section 5.A.9. of the draft Colorado regulation 10-1-1 states:

> “Documented evaluation of ECDIS for statistical bias, statistical representativeness, data quality, data validity, and appropriateness for the intended purpose and steps taken to address and correct such data quality issues.”

Additionally, the RFI asks:

> “Given feedback from industry representatives about the amount of staff resources that could be devoted to implementing a governance program, the ability and

[1] Appendix 1
[2] Appendix 2
[3] Appendix 2

effectiveness of smaller insurance companies in negotiating with third-party vendors... should requirements vary by company size?"

Although Actuarial Guideline 23 – Data Quality – supports the evaluation of third-party data, requiring individual insurers to test for bias poses several challenges:

- Inconsistent outcomes across business lines: A company might interpret the same data differently depending on its line of business.
- Competitive disparities: Different insurers may reach conflicting conclusions, potentially affecting market fairness.
- Impracticality with certain sources: Testing data from government agencies or highly regulated entities may be problematic.
- Undue burden to small companies, as noted above.
- Negotiation effectiveness with vendors, when the latter are significantly larger than the insurer, as noted above.

Definitional Clarification: What Is a Third Party?

It is not immediately obvious to me whether an external company working as an agent for the insurance company would be considered as part of the insurer (similar to captive agents) or third party. For example, an external vendor performing insurance functions (e.g., underwriting, claim triage) using tools such as generative AI (e.g., ChatGPT), predictive algorithms, or PDF summarizers—whether working with insurer-provided data or data directly from the insured.

Proposed Solution

To promote consistency and fairness, I recommend a centralized certification requirement focused on bias auditing. This could take numerous forms, similar to HIPAA, ISO or SOC 2 compliance certification, to financial audit, or to ratings provided by the Nationally Recognized Statistical Rating Organizations (not pass fail criteria, but grade). The regulatory community should be an active actor in articulating the requirements and/or the testing criteria. Verification of the effectiveness of such mechanism would be part of the regulatory oversight.

Advantages of this option include:

- Provide insurers with confidence in third-party tools;
- Eliminate redundant and potentially inconsistent bias testing by individual insurers;
- Establish a higher baseline for consumer data protections across the industry.

Thank you for offering the opportunity to comment on these documents. I believe these questions are critical to developing a sound regulatory framework for a thriving fair industry for the benefit of the society.

Respectfully submitted,
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Appendix 1: Excerpt from DeFrain Email (May 22, 2025)

To Third-Party Data and Models (H) Working Group, Interested Regulators, and Interested Parties:

The Third-Party Data and Models (H) Working Group met today and requested proposed definitions of third-party data vendor and third-party model vendor for use in a regulatory framework. Please send to Kris DeFrain (kdefrain@naic.org) by Friday, June 20.

-----Some discussion from the Working Group's virtual meeting-----

Jason Lapham, Chair, noted complications regarding these definitions to get the conversation started:

1. The simple definition of "third party" is "anyone other than the insured and insurer." He said there are nuances to discuss needed for a regulatory framework.
2. Should we focus on vendors that market at least one model or dataset for use in insurance operations?
3. What would insurance operations include? Does that exclude models such as those that may be used by HR or anything that might be part of the company's AI system? Are there different buckets of third-party models and data to consider?
4. Should a third-party vendor within the insurance group be distinguished from or treated differently than unrelated/unaffiliated third parties?
5. How far would we ideally want the regulatory system extended or are there limits on what types of data we would want to be able to get more information?
6. Should we distinguish data vendors such as Google, Facebook, or the U.S. government where our review methods may differ?

Note: Jason Lapham said there was nothing "magical" about these questions or the priority of such; these were provided to get conversation started.

Some additional issues regarding definitions were noted by Working Group members, interested regulators, and interested parties:

1. There could be different treatment of different types of 3rd party data. For example, government (e.g., motor vehicle reports); weather data; and 3rd party aggregators gathering data from different sources.
2. Facebook: may not want insurers to comb Facebook; but then again, Facebook is useful in fraud investigations.
3. Third party vs. holding company and affiliate
4. A definition of "other than insured or insurer" seems to count agents as third parties. Agents would be 1st party, representing the insurer.
5. When we say "3rd party data"... we really mean 1st party data - policyholder data - that 3rd parties have collected. I think we want to say an entity outside the insurance transaction that has data about one or more parties to the insurance transaction and for which the data is used in the insurance transaction"
6. For usefulness, may need sub definitions.

Appendix 2: Regulatory links

Big Data and AI (H) Working Group AI Request for Information
https://content.naic.org/sites/default/files/inline-files/RFI%20-%20AI%20Model%20Law_0.pdf

Draft Proposed Amended Regulation 10-1-1 regarding governance and risk management requirements for the use of external data and predictive models in insurance from Colorado Department of Regulatory Agencies, Division of Insurance

https://drive.google.com/file/d/1Wd60KO1wIIcsYtsA2eOy7p46imaG-KTZ/view