JUNE 2010

Actuarial UPDATE
THE NEWSMONTHLY OF THE AMERICAN ACADEMY OF ACTUARIES

# Practice Councils Stand Together on Retirement Security Policy

IT IS SIGNIFICANTLY MORE COST-EFFECTIVE for a person to insure longevity risk through risk pooling than to bear that risk alone—a reality the Academy's Pension Practice Council and Life Practice Council stressed in joint comments May 3 to the Department of Labor and Department of the Treasury. The comments were filed in response to the departments' request for information on lifetime income options for participants and beneficiaries in retirement plans.

Because any discussion of a national retirement policy must address longevity risk—the risk of outliving one's retirement income—the Academy councils support federal policymakers' increased interest in encouraging access to, and use of, lifetime streams of retirement income.

The request for information included nearly 40 questions for public consideration and comment, which the Academy councils responded to with the aid of the Pension Committee and the Life Products Committee. Their response emphasized that risk-pooling mechanisms (such as annuity purchases and lifetime income options in pension plans) offer more economically efficient ways to insure longevity risk compared to bearing the risk alone, or "self-insuring." The councils noted that a lifetime stream of retirement income achieves cost efficiency through longevity pooling and making full use of both principal and investment earnings—whereas self-insuring methods require 50 percent or more additional funds to be set aside than would be needed if an individual participated in a risk-pooling arrangement.

The councils stressed that public education about the financial risk of outliving retirement income must be an integral element of any strategy to achieve greater use of lifetime income options. Greater financial literacy is needed on such factors as determining a basic income level to meet essential needs, the interaction with Social Security benefits, and the risks of inflation and longevity.

In addition to consumer education, the councils wrote, strategies to achieve greater use of lifetime income options should be informed by the lessons of behavioral finance. These strategies may include reframing the language used in presenting options to participants, as well as restructuring the menu of choices and the default options. While

SEE **LIFETIME INCOME OPTIONS**, PAGE 4

# Academy Plunges into Regulatory Phase of Health Care Reform

LESS THAN TWO MONTHS AFTER THE PASSAGE in late March of the Patient Protection and Affordable Care Act and the Healthcare and Education Reconciliation Act, the regulatory phase of health care reform has hit full stride. The Health Practice Council responded to a flurry of regulatory requests in May from the Department of Health and Human Services (HHS) and the National Association of Insurance Commissioners, including one related to an HHS directive to oversee premium rate increases.

The Academy's newly formed Premium Review Work Group focused its May 14 comments to HHS on explaining the premium process and the actuarial principles used in determining appropriate premium rates that are neither excessive nor inadequate.

The work group included excerpts of its latest Critical Issues in Health Reform policy statement, *Premium Setting in the Individual Market*.

The new Section 2794 of the Public Health Service Act that was created by the Patient Protection and Affordable Care Act requires the HHS secretary to work with states to establish an annual review of "unreasonable rate increases," monitor premium increases, and award grants to states to carry out their rate review processes. In its comments, the Academy work group stressed the importance of understanding the many factors necessary to ensure premium adequacy, which is the approach generally taken by state regulations, in order to determine whether an increase is reasonable.

The Academy emphasized that the way Section 2794 is implemented could have a significant impact on the work of actuaries in preparing rate filings, as well as a major influence on the behavior of the insurance market—affecting issues such as:

- The number of insurers that remain active in the market;
- The market segments those insurers choose to service;

SEE **HEALTH REFORM REGULATION**, PAGE 7

# CALENDAR

## JUNE

**17** Webinar on the Qualification Standards and the SOA's CPD requirements (Academy, ASPPA, CAS, CCA, SOA)

## JULY

**8-11** NCOIL summer meeting, Boston

**19** Academy Summer Summit, Washington

**26-28** 45th Actuarial Research Conference, Vancouver, Canada

## AUGUST

**10** Academy Executive Committee meeting, Washington

**14-17** NAIC summer meeting, Seattle

**26** Actuarial collaboration meeting, Ottawa, Canada

## SEPTEMBER

**5** Webcast on best of *Contingencies* "Up to Code" articles (Academy, ASPPA, CAS, CCA, SOA)

**16-17** Actuarial Standards Board meeting, Washington

**20-21** Casualty Loss Reserve Seminar (Academy, CAS, CCA), Lake Buena Vista, Fla.

**22** PBA implementation seminar (Academy, SOA), Chicago

**30** Council of U.S. Presidents meeting, Mont-Tremblant, Quebec, Canada

## OCTOBER

**1-2** North American Actuarial Council meeting, Mont-Tremblant, Quebec, Canada

**5** Academy Board of Directors meeting, Washington

**15** IAA meeting, Vienna, Austria

**17-20** ASPPA annual conference, National Harbor, Md.

**17-20** SOA annual meeting, New York

**18-21** NAIC fall meeting, Orlando, Fla.

**24-27** CCA annual meeting, Rancho Mirage, Calif.

## NOVEMBER

**1** Life and Health Qualifications Seminar, Arlington, Va.

To continue receiving the *Update* and other Academy publications on time, remember to make sure the Academy has your correct contact information. Academy members can update their member profile at the member log-in page on the Academy website.

Links to documents underlined in blue are included in the online version of this issue at **www.actuary.org/update/index.asp**

# Academy NEWS Briefs

## Academy Encourages Volunteerism

THE ACADEMY'S VOLUNTEER RESOURCE COMMITTEE recently kicked off its 2010 online volunteer survey. If you haven't taken the survey yet, members can still complete it any time between now and July 9.

Similar to last year's setup, the web-based survey is user-friendly and should take no more than five minutes to complete. Although the e-mail that you received took you directly to the survey, you can also access the form from your member log-in page. The survey is part of the Academy's efforts to encourage volunteerism among its members. Last year's volunteer recruitment efforts led to 102 placements of Academy members on various volunteer groups (committees, task forces, etc.).

The form contains a space to indicate volunteer groups on which you may be interested in serving, including the new Academy Advisors panel that will provide an instrumental perspective to the Academy leadership's decision-making processes by responding to short, periodic online surveys. There is also a space to describe your particular areas of experience and expertise that the Academy can help match to a particular group. A list of Academy groups and a short description of each group's primary activities are immediately accessible. You can also indicate if you have an interest in writing articles for Academy publications.

### STAFF ANNOUNCEMENTS

The Academy welcomed three new people to its staff in the last month. New Life Policy Analyst John Meetz joined the Academy on June 3 after serving as senior government and public affairs liaison for the Kansas Department of Insurance. He has also been involved in statewide political work on behalf of Kansas Insurance Commissioner Sandy Praeger.

Lou Baccam joined the Academy as assistant director for marketing on May 20. She has more than 10 years of professional experience developing and implementing marketing, communication, and business strategies in law, software, and financial services and products. Baccam has worked with a diverse range of U.S. and international companies, including membership-based organizations, nonprofits, start-ups, and *Fortune* 100s.

David Larkin joined the Academy as its new manager of web operations on May 19. Larkin has extensive experience designing, developing, and managing websites for both profit and nonprofit organizations, including PricewaterhouseCoopers and D.C. Goodwill. He was previously the website administrator for Inside Higher Ed, an online publisher of education news.

### BOARD UPDATE

At its May 20 meeting, the Academy Board of Directors approved undertaking an enterprise risk management analysis of the Academy. A new task force, which will be chaired by former Academy Risk Management and Financial Reporting Vice President Jim Rech, will prepare recommendations for the board to identify and manage risks to the Academy and the U.S. actuarial profession. For a summary of the board meeting, visit the members-only page of the Academy's website.

### DEFINITION DEFENDED

The Academy's Council on Professionalism and Committee on State Health Issues submitted a joint letter April 19 to the North Carolina Department of Insurance in response to the department's consideration of changing its definition of a qualified actuary in connection with signing health statements of actuarial opinion. While the state's regulations currently require membership in either the Academy or the Society of Actuaries, the department is considering requiring membership in both organizations. The Academy letter explained that the change wouldn't necessarily strengthen the definition because all actuaries who belong to any U.S.-based actuarial organizations and who issue statements of actuarial opinion in the U.S. are required to meet the profession's Qualification Standards.

➔ CONTINUED ON PAGE 3

➔ CONTINUED FROM **PAGE 2**

### ACTUARY_DOT_ORG

Seeking new ways to reach its members, the Academy has expanded its communications efforts to include social media. To stay updated on the Academy's public policy work on behalf of the actuarial profession, you can now follow the Academy on Twitter under the name Actuary_Dot_Org. New to Twitter? Learn more at Twitter support.

### UNCLE SAM CALLING

Academy Senior Health Fellow Cori Uccello has been appointed to the Medicare Payment Advisory Commission (MedPAC). MedPAC is an independent congressional agency that advises Congress on payments to health plans participating in the Medicare Advantage program and to providers in Medicare's traditional fee-for-service programs. Uccello's term expires in 2013. The appointment was made by the Government Accountability Office and announced in its May 14 press release.

Academy board member Ron Gebhardtsbauer has been appointed by U.S. Secretary of Defense Robert Gates to the Department of Defense's board of actuaries. Gebhardtsbauer, head of the actuarial science program at Penn State University, joins a three-member board that advises the department's chief actuary and Secretary Gates on actuarial matters, including the Military Retirement Fund and the G.I. Bill's Education Benefits Fund.

### KUDOS

Academy member James Harlin, founder and president of actuarial consulting firm Fi-Source Inc. in Edmond, Okla., was awarded a 2010 Meritorious Achievement Award from his alma mater Pittsburgh State University in May. The award is the school's highest honor given to graduates based on career achievement.

### IN THE NEWS

The Academy Life Practice Council's April 6 webinar on principle-based approach updates from the March 2010 National Association of Insurance Commissioners (NAIC) meeting was discussed in an April 10 Insurance Bellwether article. Included in the article were comments from panelists Donna Claire, chairperson of the Academy's Life Financial Soundness/Risk Management Committee and president of Claire Thinking Inc. in Fort Salonga, N.Y.; Dave Neve, chairperson of the Academy's Life Reserves Work Group and vice president of corporate valuation for Aviva USA in Des Moines, Iowa; Nancy Bennett, Academy senior life fellow; Larry Bruning, chairperson of the NAIC's Life and Health Actuarial Task Force and chief actuary for the Kansas Insurance Department; and Philip Barlow, chairperson of the NAIC's Life Risk-Based Capital Working Group and associate commissioner of the insurance bureau of the Washington, D.C., Department of Insurance, Securities, and Banking.

An April 15 *Kiplinger's Personal Finance* article cited the Academy's Critical Issues in Health Reform paper regarding the Community Living Assistance Services and Supports (CLASS) Act. The Academy wrote that actuarially sound premiums for the new long-term care program could range from $125 to $160 per month. The article also was published in the *Orlando Sentinel* on April 21 and in the Newark, N.J., *Star-Ledger* on April 22.

Academy Senior Health Fellow Cori Uccello suggested possible ways that regulators could strengthen the individual health insurance coverage mandate contained in the Patient Protection and Affordable Care Act to limit adverse selection. As reported in *Money Magazine/CNNMoney.com* on April 22, one of the non-financial incentives Uccello discussed was placing limits on participants' ability to upgrade insurance plans.

An investigation by the staff of the U.S. House Energy and Commerce Committee found that companies that posted one-time, non-cash charges against earnings—in response to a provision in the new Patient Protection and Affordable Care Act that eliminates a tax deduction for providing retiree drug benefits—had acted properly and in accordance with accounting standards. As reported by the *New York Times* on April 26 and 27, the committee staff said that independent experts from the Financial Accounting Standards Board and the Academy had confirmed the findings. The Academy's confirmation was also referenced in, among others, a related April 27 *Investor's Business Daily* editorial.

An April 28 Insurance Bellwether report on responses to Notice 2010-29, which was issued by the Internal Revenue Service on March 25 regarding calculating U.S. statutory reserves for variable annuities under a principle-based approach, included comments from the Academy Life Reserve Principles Work Group. Co-chairpersons Barbara Gold, vice president and tax actuary for Prudential Insurance Co. in Newark, N.J., and Tom Campbell, vice president and corporate actuary for Hartford Life in Simsbury, Conn., were quoted in the article. They said that their initial belief is that the guidance in the recent notice is fundamentally consistent with the views the Academy Life Practice Council expressed in its comments to Notice 2008-18 but that there are still areas of uncertainty that need to be addressed—such as the inclusion of the stochastic reserve in the statutory reserve limitation on the tax reserves.

An April 30 *USA Today* personal finance column cited longevity and life expectancy data provided by the Academy. The Academy said that the average 65-year-old male's life expectancy is about 84.5 years and the average female's life expectancy is about 87 years and noted that the average 65-year-old male has a 30 percent chance of living beyond 90, while the average female has a 40 percent chance.

To find out about other actuaries in the news and for external links, visit the Academy's newsroom.

### CASUALTY BRIEFS

➥ **Rowen Bell**, forecasting actuary for Health Care Service Corp. in Chicago; **Mary Miller**, assistant director of the Ohio Department of Insurance in Columbus; and **Darrell Knapp**, executive director for Ernst & Young in Kansas City, Mo., have joined the Academy's Model Audit Rule Practice Note Subgroup.

# White Paper Stresses Need for Systemic Risk Regulator

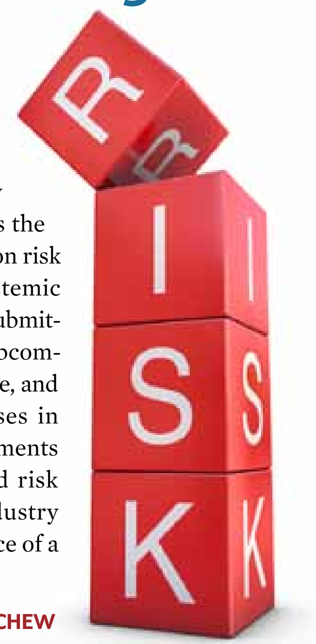
AS PART OF THE ACADEMY'S CONTRIBUTIONS TO discussions of governmental reform of the financial sector in the wake of the financial crisis, the Academy's Financial Regulatory Reform Task Force released in May a new white paper, *Role of the Systemic Risk Regulator*. The paper provides a review of the insurance industry and the broader financial sector and expands upon previous Academy work on systemic risk, asserting that new key functions are necessary for effective regulation.

The paper states that federal regulation of systemic risk is needed for all sectors of the financial services industry, including the insurance industry. A federally based systemic risk regulator, the paper says, should compile data and use metrics to facilitate national and global monitoring of systemic risk, establish criteria for active regulatory intervention or takeover of financial institutions, and work with functional regulators from within the U.S., other countries, and international regulatory bodies to take action to mitigate any identified systemic risk.

"The U.S. insurance industry is subject to risks arising from both capital markets and insurance liabilities," the paper says. "While the insurance industry did not generate systemic risk during the latest crisis, the task force recognizes the importance of a system that would monitor any development of insurance-related risk on a nationwide basis."

The effectiveness of the systemic risk regulator to regulate systemically important companies requires the evaluation of company risk management processes. The new regulator, the task force says, should recognize the ability of the current state-based functional regulatory system to help provide oversight and supervision of systemic risk within the insurance industry.

The paper also discussed issues regarding systemic risk regulation of the insurance industry, including governance and structure, systemic risk regulation data requirements, the relationship of the system risk regulator to other regulators, a range of possible regulator actions, and the relationship of the regulator with the actuary.




The white paper was one of the initiatives born out of the financial summit the Academy hosted last July, and it supplements the task force's April 2009 white paper on risk management requirements for systemic risk regulation. The task force also submitted testimony to the U.S. House Subcommittee on Capital Markets, Insurance, and Government Sponsored Enterprises in May 2009 on the concepts and elements needed for effective oversight and risk management in the insurance industry and in March 2009 on the importance of a systemic risk regulator.

—TINA GETACHEW

## HEALTH BRIEFS

- **Matt Klaus**, senior manager for Deloitte Consulting in Chicago, and **Shawna Meyer**, corporate vice president for New York Life Insurance Co. in Austin, Texas, have joined the Academy/SOA Long-Term Care Valuation Work Group.
- **Kathleen Tottle**, senior vice president and chief actuary for AMERIGROUP in Virginia Beach, Va., and **Michelle Raleigh**, managing member for schramm-raleigh Health Strategy in Scottsdale, Ariz., have joined the Academy's Medicaid Work Group.
- **Donna Novak**, president and chief operating officer of NovaRest Consulting in Sahuarita, Ariz., has joined the Academy's Committee on State Health Issues.

## Lifetime Income Options, continued from page 1

sponsors should not be required to make annuitization the default option, individual plan sponsors should be permitted to make it the default option should they so choose.

The councils recommended that the government require some form of guaranteed lifetime income as one of the investment or distribution options offered in individual account plans—but only if accompanied by a set of reasonable and practical regulations. The Academy response also discussed particular lifetime-income options that could facilitate greater mainstream use, including partial annuitization, refund-type annuities, incremental annuitization, and "longevity insurance" (the trade name for income annuities that are deferred to an advanced starting age, such as age 80 or 85).

—JESSICA THOMAS

## Pension Relief Questions

The Academy's Pension Committee and Multiemployer Plans Subcommittee sent comments May 4 to the Senate on the multiemployer pension plan relief provisions contained in an amendment to H.R. 4213, the American Jobs and Closing Tax Loopholes Act, which the Senate passed on March 10.

The Academy committees sought in their letter to clarify some of the provisions in the relevant legislation, including the manner in which net investment loss is determined, the number of years the relief provision will be amortized, and the implementation of the relief as it relates retroactively to previously issued certifications. H.R. 4213 is still being considered by the House.

# New General Counsel Brings Range of Experience

THE ACTUARIAL PROFESSION'S HALLMARK reputation for evaluating and managing risk is something to which new Academy General Counsel Gino Vissicchio can readily relate. Vissicchio, who is also the Academy's director of professionalism, has for years helped clients navigate challenging legal issues related to complex litigation and provided strategic counseling on compliance and risk mitigation issues.

Now, he is excited to contribute his own perspective and experience to aid the actuarial profession. That experience spans private practice with some of the nation's most prominent law firms, in-house corporate work with a publicly held *Fortune* 500 company, and public service as a trial lawyer with the Department of Justice—where he received a special commendation for outstanding service. Over his career, Vissicchio has represented a broad spectrum of clients in matters involving a host of substantive legal areas, such as antitrust regulation, securities law, corporate governance, and commercial litigation.

"My experience has been somewhat uncommon in the variety of work I have had and the different environments in which I've practiced," Vissicchio says. "It's been challenging and rewarding, and it has provided me with a lot of versatility as a lawyer."

That broad experience positions him well to oversee the diverse legal practice at the Academy, where he says he will continue to keep an anticipatory eye toward assessing and managing risk.

"Thinking proactively about both legal and professionalism issues will be more likely to reduce legal risk and enhance the quality of the profession. I'm a big proponent of trying to identify potential issues before they arise, as opposed to merely reacting after they become truly problematic," Vissicchio says.

From a professionalism perspective, he says that is accomplished through developing and maintaining carefully considered standards that provide clarity for actuaries and maintain their high caliber of practice. As Vissicchio immerses himself in standards of practice, qualification, and conduct, he says that he's impressed with the breadth and clarity of what he sees—and with the commitment of the member volunteers who serve on the Council on Professionalism and other important bodies, such as the Actuarial Standards Board and the Actuarial Board for Counseling and Discipline.

"We are fortunate to have so many members who are engaged in serving on committees that look at different aspects of the profession and are constantly striving to improve it," he says.

One area that continues to hover on the actuarial horizon is international involvement in accounting and actuarial standards. With experience in international litigation, Vissicchio understands the significance of global coordination.

"The international landscape presents unique challenges," he says. "But the importance of cross-border relationships and the advancement of the profession on a global scale is undeniable."

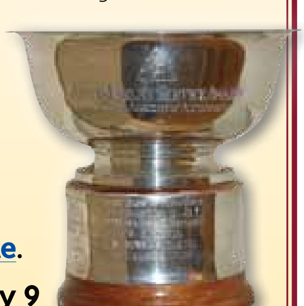
The Queens, N.Y., native, who grew up on Long Island, also has a personal interest in international affairs as a dual citizen of the U.S. and Italy, where he and his family visit regularly.

Vissicchio has spent his legal career in the Washington and New York metro areas. He is an honors graduate of the University of North Carolina, where he was a member of the law review, and the University of Pennsylvania.

## Jarvis Farley Service Award

The Academy is requesting nominations for the 2010 Farley Award, which is presented annually to an actuary who has provided sustained exemplary volunteer service to the profession.

With the exception of current Academy officers, all Academy members are eligible for the award. Past Academy presidents are eligible for consideration only for the volunteer work they have done after completing their terms of office.



**For more information, visit the Academy website.**

**Nomination Deadline: July 9**

## Nominations Sought for 2010 Myers Service Award

The award, named for the former chief actuary of the Social Security Administration, recognizes actuaries with a single noteworthy public service achievement or those who have devoted careers to public service. Please visit http://www.actuary.org/awards/myers.asp for more information about the Myers Award or to nominate an outstanding actuary online.

**Deadline: July 9**

# Lehmann Checks In After Travels Abroad

*Former Academy President Steve Lehmann succeeded the late Dan McCarthy as the Academy's international secretary in 2008. The* Update *caught up with Lehmann following his recent globe-trotting to ask about his experiences in the past year and a half representing the Academy and the U.S. actuarial profession on the international stage. Lehmann attended the International Actuarial Association (IAA) meeting in Cape Town, South Africa, March 3–6 and the International Congress of Actuaries March 7–12.*

**_Update_: You were the Academy's alternate delegate to the IAA when the international secretary position was created. How much has your international work changed from your prior involvement to now being the international secretary for the Academy?**

Lehmann: The international secretary position was created in 2007 to coordinate the Academy's involvement with IAA committees and to increase the effectiveness of the Academy and other U.S. actuarial organizations at the IAA—ultimately to represent all U.S. actuaries at the IAA.

As an alternate delegate, I was there to help the decision-making process and to follow activities at the IAA Council. As international secretary, I'm now responsible for coordinating all Academy activity at the IAA and other international venues. It's a dramatic change of duties, and an interesting time in my career.

**You were president when the position was created by the board, and you appointed the late Dan McCarthy, former Academy president, to the post. Now being in the position yourself, how has the position evolved?**

Dan was a wonderful representative of the Academy and the U.S. profession. He had a depth of understanding and network of connections, making him very effective as our international secretary. Dan's passing left some big shoes to fill.

This position was created with the knowledge that it was becoming more and more important for the Academy and the U.S. profession to coordinate our activities at the IAA. Since then, international developments have continued to increase at an exponential rate. In terms of international accounting standards, international actuarial standards, and the need to closely monitor solvency regulation developments, now more than ever, U.S. actuaries need to be represented at the table. As part of the elected Executive Committee of the IAA, I am able to become more involved and, as a result, more effective in my role.

**What does that position entail? How is the Executive Committee constituted?**

The Executive Committee has recently undergone dramatic change. Previously, the Executive Committee consisted of the chairpersons of all the IAA committees. It was a very large group, much too large—and met too infrequently—to be able to effectively fill an operational management function. We and others had strongly urged the IAA to develop a strategic plan, giving a good, hard look at its overall governance structure. The IAA did that and as part of the strategic review, the committee was reduced in terms of members and given a much stronger operational role. Currently, there are four officers and eight general members of the Executive Committee. The eight general members represent all the committees, sections, and member organizations. The guidelines for the eight general members require that there are at least two members from North America, at least two from Europe, and at least two global members from outside those regions. All were elected by the IAA delegates by electronic vote within the last year, just before the Cape Town meeting. We held our first in-person meeting in Cape Town this spring.

**Any major updates from the Cape Town meeting?**

International actuarial standards of practice were discussed vigorously in Cape Town. There's a new model of international actuarial standard of practice that is being worked on by the IAA, dealing with actuarial standards of practice under international financial reporting standards. This received a lot of discussion.

Also, last fall at the IAA meeting in Hyderabad, India, there was an agreement among actuarial organizations in 12 countries throughout the world to establish the first international designation for enterprise risk management (ERM), based on the Society of Actuaries' chartered enterprise risk analyst (CERA) designation. There were meetings in Cape Town to discuss developments of this ERM qualification, as the CERA designation will now be used in connection with international practice. It isn't formally within the IAA structure, but the treaty was signed as part of IAA meetings.

**How do your international experiences enable you to view certain issues differently?**

I think what has really come home to me as I've worked at the IAA is the growing global economy and the importance for U.S. actuaries to be involved in that global activity. Along with that is the need to be active in following the development of a new model of international standards of practice, financial reporting, and regulation.

Over time, I've had an opportunity to see what methods are being used by actuaries worldwide as new actuarial techniques are developed and applied. Many of these new methods may ultimately be used by U.S. actuaries to improve their practice. For instance, the U.K. can now make changes in rates instantaneously without any filings. Perhaps U.S. actuaries may one day incorporate these techniques for operating in environments without rate regulation.

**Could you talk a little bit about the International Congress of Actuaries?**

Every four years, the congress provides a forum for actuaries to attend educational sessions and to discuss actuarial developments throughout the world. This year the congress focused on a variety of topics with four concurrent tracks: life, health, property/casualty, and pension. The 2014 Congress will meet in Washington, D.C., and I encourage U.S. actuaries to become involved at the international level. Connecting with colleagues from around the world has certainly been a rewarding experience for me. The 2014 Congress in Washington will be an excellent opportunity to expand the U.S. profession's horizons.

Health Reform Regulations, continued from page 1

- The premium levels charged by insurers for their products;
- The willingness of providers of capital to invest in the health insurance industry.

The Academy reiterated to HHS that it had a "long history of providing objective technical advice on areas that affect health insurance regulation," drawing on its unique professional expertise.

"Our intent in this response is to provide a balanced perspective on these important issues, in the hopes of contributing to the development of technically sound rulemaking regarding Section 2794," the work group wrote.

Also on May 14, the Academy's Medical Loss Ratio (MLR) Regulation Work Group submitted lengthy comments to HHS regarding MLR reporting and rebates. Both comments to HHS expanded upon previous comments the Academy submitted to the NAIC in April on premium oversight and MLR reporting.

### PENSION BRIEFS

- **Janet Barr**, associate actuary for Milliman in Chicago, has been appointed the chairperson for the Academy's Social Insurance Committee.

### Reviewing Rebate Requirements

In addition to the medical loss ratio (MLR) calculation comments the Academy submitted to Health and Human Services (HHS) and the National Association of Insurance Commissioners (NAIC), an NAIC subgroup asked the Academy for its input as the NAIC assists HHS in developing recommendations regarding pooling for rebates based on the MLR calculations. The Academy MLR Regulation Work Group's comments on May 12 and follow-up comments on May 20 specifically focused on defining an appropriate way to maintain statistical validity within the rebate process.

The new Section 2718 of the Public Health Service Act requires a health insurance issuer to provide an annual rebate under certain circumstances in which the reported MLR differs from the required MLR. The Academy work group, however, noted that certain margins must be built in to allow for normal statistical fluctuation.

"It may not be good public policy to require the payment of rebates based on essentially random results beyond the insurer's control," the comments acknowledged, "which underscores the need for some method to maintain statistical validity in the rebate calculation process."

The comments outlined three approaches for maintaining greater validity, including credibility analysis based on the size of certain experience pools.

## LIFE NEWS

# Embedded Value Practice Note Updated

**BY PATRICIA MATSON**

THE ACADEMY'S Life Financial Reporting Committee (LFRC) released an exposure draft of a practice note on market-consistent embedded values, which discusses common practices related to performing market-consistent embedded value (MCEV) calculations as governed by the European Insurance CFO Forum principles published in June 2008 and updated in October 2009. The practice note provides an update to a prior one on European embedded value that was based on the requirements laid out by the CFO Forum in 2004.

The practice note provides background on MCEV, including outlining its purpose and identifying principal differences between MCEV and other calculations, such as total embedded value and European embedded value. The paper also discusses MCEV formulas and mechanics, detailing the basic components and defining adjusted net worth, among other areas. The committee lists MCEV disclosure requirements and the assumptions required for MCEV calculations, which are categorized into economic and noneconomic assumptions.

Another topic in the paper is the time value of future options and guarantees. In particular, it discusses assumptions needed to calculate the value and the effect hedging has on it. Non-hedgeable risks, their quantified costs, and their costs included in MCEV are also defined in the paper.

The contributors to the practice note include Academy members Mark Alberts, Robert Frasca, Larry Gulleen, Noel Harewood, Novian Junus, Kenneth LaSorella, Jeffrey Lortie, James Norman, Christopher Olechowski, Nicholas Ranson, Leonard Reback, Jack Walton, and myself. The draft will be exposed for comment until Aug. 2. Any comments should be sent to lifeanalyst@actuary.org.

**Patricia Matson, principal for Deloitte Consulting in Hartford, Conn., is a member of the Academy's Life Financial Reporting Committee.**

### Variable Annuity Work Group Requests Input

The Academy's Variable Annuity Practice Note Work Group is developing an update of the July 2009 practice note on C3 Phase 2 and Actuarial Guideline No. 43. The work group requests input for the update, which is expected to be published later this year. Actuaries who have had questions arise related to the guideline's provisions during the completion of the year-end valuation as of Dec. 31, 2009, are invited to send those questions and, if possible, how the issue was handled to vapn@share.actuary.org. The information must be submitted by July 15, 2010, for consideration in the practice note. For further questions, please contact work group co-chairpersons Tim Gaule (tgaule@aegonusa.com) or Marc Slutzky (marc.slutzky@milliman.com).

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# Academy Explains Methodology of RBC Factors

THE ACADEMY'S Property and Casualty Risk-Based Capital (RBC) Committee issued a follow-up letter May 18 to the National Association of Insurance Commissioners' (NAIC) Property Risk-Based Capital Working Group to elaborate on the effect on the reinsurance industry of the updated RBC underwriting factors the committee submitted in March.

The letter came in response to the comments the Reinsurance Association of America (RAA) submitted to the NAIC working group following the exposure of the Academy report on March 18. During the working group's call on May 4, which included participation by members of the RBC Committee, the RAA presented its view that the Academy's report could result in unfavorable changes to the RBC formula as applied to the reinsurance industry.

In its subsequent letter, the RBC Committee noted that the capped indications were not affected by the filtering or the pooling issues identified by the RAA. The filtering procedure, the letter explained, significantly reduced the number of companies whose data were utilized for calculating RBC reserve factors for the non-proportional liability reinsurance line. The committee observed that the experience of this line in the early part of the 2000s was extremely adverse and that such adverse experience would influence any calculation, regardless of the existence or degree of the filter.

The committee tested the impact of filtering, using the same methodology with a broader filter and with no filter at all. Each time, the indicated underwriting risk factor for reserve runoff was higher than the current indicated capped factors by a significant margin. The committee concluded that the increases in the indicated underwriting risk factors for the reinsurance line were due to the underlying data and not to the use of filtering or the treatment of pooling.

The committee disagreed with the RAA's assertion that the indicated factor should not be applied to the reinsurance line because of anomalies in the data. Based on the fact that the issues the RAA raised do not affect the capped indications, the committee did not recommend treating the reinsurance line any differently than any other line of business in the NAIC's possible application of the indicated underwriting risk factors.

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