

GENERAL INSURANCE ISSUES

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2011 Academy Legislative/Regulatory Review

I. Introduction

The annual Academy legislative/regulatory year in review details significant legislative and regulatory activities affecting the actuarial profession, as well as the Academy's work on these issues during the past year. A great deal of the Academy's work in 2011 focused on the implementation of health care and financial services reform, lifetime income options for retirement, and the National Association of Insurance Commissioners' (NAIC) principle-based approach (PBA) to life reserves.

In addition, the Academy hosted its 2011 Summer Summit on July 11, focusing on enterprise risk management (ERM). Led by the Academy's ERM Task Force, whose work laid the foundation for the summit, Academy leadership examined the opportunities and risks associated with the Academy's work on public policy and professionalism through an ERM framework.

II. Major Issues

Health Care Reform

Implementation of the Affordable Care Act (ACA) continued throughout 2011. The Department of Health and Human Services (HHS) proposed regulations for risk-sharing mechanisms; issued initial guidance on essential health benefits; and issued final rules for medical loss ratio (MLR) reporting and rebates, the new rate review process, and accountable care organizations (ACOs).

The ACA's constitutionality garnered significant attention in 2011 as several appeals courts handed down decisions that illustrated the lack of consensus on the issue. The Fourth Circuit Court of Appeals heard cases from the state of [Virginia](#) and [Liberty University](#). The court ruled that both plaintiffs lacked standing to challenge the individual mandate, essentially negating the trial court's earlier decision that the mandate was unconstitutional. The Sixth Circuit, in [Thomas Moore Law Center vs. Barack Obama](#), found that the mandate was constitutional. In contrast, the Eleventh Circuit, in response to the [lawsuit](#) brought by Florida and 25 other states, ruled that the mandate was unconstitutional.

On Nov. 14, the Supreme Court agreed to accept the Eleventh Circuit case and to hear arguments regarding the constitutionality of the ACA. The Supreme Court said it will consider several issues, including:

- Whether the individual mandate is constitutional, and if not, whether that affects the viability of other provisions in the law;
- Whether the plaintiffs have standing to contest the law;
- Whether the expansion of the Medicaid program is constitutional.

The court is expected to hear arguments in March 2012. A decision isn't expected until June 2012.

Financial Services Reform

Implementation of the Dodd-Frank Wall Street Reform and Consumer Protection Act also continued throughout 2011. Treasury Secretary Timothy Geithner on March 22 appointed Michael McRaith, former Illinois Insurance Commissioner, as the first head of the Federal Insurance Office (FIO). The FIO is a component of the Dodd-Frank Act, the purpose of which is to identify potential risks in the stability of the financial services marketplace. While having no regulatory powers, the FIO will report its findings to Congress and other federal offices as requested.

The Financial Stability Oversight Council (FSOC), also created by the Dodd-Frank Act, released its first annual [report](#) to Congress on July 26. The FSOC's principal objectives are the identification of financial stability risks, assuring market discipline, and responding to emerging risks in the U.S. financial system.

On Jan. 18, the FSOC issued a [proposed rule](#) relating to the regulation of nonbank financial companies. The rule, later [revised](#) on October 18, describes the manner in which the FSOC intends to apply the statutory standards and considerations, and the processes and procedures that the council intends to follow, in ensuring the supervision of nonbank financial companies under the Dodd-Frank Act.

The Academy's Financial Regulatory Reform Task Force offered several sets of comments on this rule. The task force's Feb. 25 [comments](#) stressed that risk metrics should provide distinguishing information/data to identify where there is a substantial concentration of risks among companies and where a subsequent failure of these non-bank financial companies could have an adverse effect on U.S. financial stability. On June 24, the task force [specified metrics](#) to assist in identifying industry trends, including the possible accumulation of systemic risk. On Dec. 19, the task force submitted [comments](#) regarding terms related to systemically important non-bank financial institutions.

The FSOC also finalized one rule, [Authority to Designate Financial Market Utilities as Systemically Important](#) on July 27. The rule describes the criteria, and the processes and procedures established under the Dodd Frank Act (DFA) for the council's designation of Financial Market Utilities as systemically important under the DFA. The rule became effective Aug. 17.

The Academy submitted a [letter](#) to the Department of the Treasury on June 8 advocating actuarial participation on the Federal Advisory Committee on Insurance (FACI), an organization that will work in conjunction with the FIO. The Academy wrote that participation on the FACI of an individual with actuarial experience is critical. The Academy submitted additional [comments](#) reinforcing its position on Aug. 2.

The Financial Regulatory Reform Task Force offered [comments](#) to the FIO on Dec. 16 on its [study](#) on how to modernize and improve insurance regulation in the United States. The comments address the areas in which the actuarial skill set uniquely relates to insurance oversight, the regulation of insurance risk and, more specifically, systemic risk.

PBA: Standard Valuation Law and Valuation Manual

In 2011 the NAIC continued its work on the PBA project, an effort to modernize the framework for determining life insurers' statutory required capital and reserves in the United States. If the valuation manual is adopted by the NAIC in March as expected, state legislatures could begin adopting the new Standard Valuation Law (and the accompanying valuation manual) as early as 2013.

The Academy worked closely with the NAIC through 2011 on various issues relating to PBA such as life reserves, mortality tables, and the development of a “feedback loop.” The Academy continues to work with the NAIC to address several outstanding issues including the reinvestment rate, difficulties with the net premium reserve, credibility blending in determining the mortality assumption, and the margins on assumptions.

In addition, the Academy hosted webinars on [April 14](#) and [Nov. 22](#) to discuss recent NAIC/PBA activity and the Academy's related work. Finally, in conjunction with the Society of Actuaries (SOA), the Academy presented two PBA seminars: [Preparing for Change Under PBA: Life Company Reserves and Capital Seminar](#) (May 18), and [Preparing for Change under PBA for Life Products: Life Company Reserves and Capital Seminar](#) (Sept. 14).

III. Cross Practice

Lifetime Income Options for Retirement

In October, the Treasury Department announced a review of regulations pertaining to retirement plans to determine a method of better promoting retirement security in the form of retirement income. The Academy continued its work on the issue of lifetime income options for retirement with a Capitol Hill [briefing](#) on April 4. The Academy urged public policy reforms that could achieve the goal of lifetime income, such as providing incentives for workers to increase retirement savings, discouraging lump sum distributions from DC plans and encouraging annuitization of lump sum distributions, penalizing leakage of funds at the time of defined contribution (DC) rollovers or even mandating rollovers, supporting pooling of risk, and promoting lifetime income arrangements such as annuities.

The Academy's Public Interest Committee (PIC) in August released for comment a draft advocacy statement supporting lifetime income. The draft statement expressed support for policy initiatives that would encourage secure lifetime income protection and address the challenges of retiree longevity risk. As a result of feedback from Academy members, the PIC is expanding the scope of its work on this issue through 2012. The Academy's Lifetime Income Risk Task Force (a joint Life Practice Council and Pension Practice Council work group) is coordinating with the PIC on Academy activities related to lifetime income.

Solvency Modernization Initiative

The NAIC's Solvency Modernization Initiative (SMI) is a critical self-examination of the U.S. insurance solvency regulation framework. Included in this examination is a review of international developments regarding insurance supervision, banking supervision, and international accounting standards and their potential use in U.S. insurance regulation. To accomplish these goals, the NAIC has created a road map to set out the policy direction and priorities for SMI activities and clarify the role and scope of various task forces and working groups' SMI activities through 2012.

The Academy's Life, Health, and Property/Casualty RBC committees released a [joint report](#) on Jan. 31 to the NAIC's SMI RBC Subgroup in response to the NAIC's request for assistance with the SMI project. The report discusses intended and expected safety levels for risk-based capital (RBC) and identifies risks that are missing from the RBC formulas.

In addition, the Academy's Property /Casualty RBC Committee sent a [letter](#) to the subgroup on July 21, discussing the committee's progress in providing recommendations to improve the correlation/covariance methodologies used in the P/C RBC formula. The committee examined the theoretical underpinnings of the current NAIC methodology for taking risk interdependency into account with the P/C formula. The committee also surveyed alternative approaches. Once a general approach is chosen, the committee is expected to provide an update to the NAIC.

Deficit Reduction Proposals

The Joint Select Committee on Deficit Reduction was charged with developing a proposal by Nov. 23, 2011 that would reduce the deficit by \$1.5 trillion over a 10-year period. The committee investigated deficit reduction via revenue increases, including raising taxes; tax reforms, such as simplifying the tax code and eliminating some tax breaks and loopholes; military spending cuts; and measures to reform and slow the growth of entitlement programs, including Medicare, Medicaid, and Social Security.

The Academy's Medicare Steering Committee sent a [letter](#) to all members of the Joint Select Committee on Aug. 31 encouraging the development of sound public policy proposals to improve the long-term solvency and sustainability of the Medicare program. The Social Security Committee sent a [similar letter](#) on Sept. 22 to President Obama, Senate Majority Leader Harry Reid (D-Nev.), and Speaker of the House John Boehner (R-Ohio) focusing on the long-term financial challenges facing Social Security and the importance of taking action to reform the program sooner rather than later.

On Nov. 21, the committee issued a [statement](#) announcing that its deliberations had been unsuccessful. As a result of the committee's inability to reach an agreement, \$1.2 trillion in across-the-board cuts will be implemented over the next nine years, starting in 2013. Any cuts to Medicare would be limited to provider payments and could not exceed 2 percent of the program's costs. The cuts will not affect Social Security, Medicaid, veterans' benefits, Pell Grants, disability insurance, Supplemental Security Income, the Children's Health Insurance Program, or war financing.

IV. Practice Council Issues

Casualty Practice Council

Medical Professional Liability

The House introduced legislation addressing medical liability reform on Jan. 24. [H.R. 5](#):

- Places a \$250,000 cap on noneconomic damages;
- Allows courts to restrict the payment of attorneys' contingency fees;
- Permits courts to require periodic payments for future damages instead of lump-sum awards in specific cases;
- Creates a "fair share" rule by which damages are allocated against each party in direct proportion to fault;
- Establishes limitations on punitive damages awards that would be limited to \$250,000 or twice economic damages, whichever is greater.

The legislation was approved by the House Judiciary Committee on Feb. 16 and by the Energy and Commerce Committee on May 11. The legislation has been awaiting a House vote since May 23.

National Flood Insurance Program

The National Flood Insurance Program (NFIP) was extended temporarily several times in 2011. In addition, three more comprehensive bills ([H.R. 1309](#), [S. 1091](#), and [S. 1940](#)) were introduced to extend the program an additional five years. H.R. 1309 and S. 1091 are currently in the Senate Committee on Banking, Housing and Urban Affairs awaiting further consideration, and S. 1940 is awaiting debate and a final vote on the Senate floor.

In addition to the five-year extension, the comprehensive bills make numerous changes to existing flood policy.

H.R. 1309

- Authorizes the administrator of the Federal Emergency Management Agency (FEMA) to suspend temporarily the mandatory flood insurance purchase requirement for areas designated as having special flood hazards;
- Prescribes minimum annual flood insurance deductibles of \$2,000 for subsidized rate properties and of \$1,000 for actuarial rate properties;

- Allows payment of flood insurance premiums in installments, at increased chargeable premium rates and with surcharges.

S. 1091

- Amends the National Flood Insurance Act (NFIA) of 1968 to direct the Secretary of Homeland Security to establish a system for allocating losses among insurers providing coverage against property losses due to wind and water peril;
- Requires adjustment of the flood insurance risk premium rate for property in an NFIP-participating area to reflect the current flood risk to the property;
- Requires the FEMA administrator to make flood insurance available in only those states or areas that have given assurance that, by Dec. 31, 2012, state-chartered lending institutions not insured by the Federal Deposit Insurance Corporation or by the National Credit Union Share Insurance Fund will be subject to state regulations consistent with NFIA flood insurance purchase and compliance requirements.

S. 1940

- Requires the administrator of FEMA to make flood insurance available to cover residential properties containing more than four units;
- Amends the NFIA to exclude certain properties from receiving subsidized premium rates, to prohibit the extension of flood insurance subsidies to certain individuals at rates less than those of individuals residing in the 100-year flood plain, increases the annual limitation on premium increases from 10 percent to 15 percent, and allows certain policyholders to pay their premiums either annually or in more frequent installments;
- Provides for the creation and modification of mandatory flood insurance coverage areas;
- Amends the minimum annual deductible amount for pre- and post-FIRM properties covered by the NFIP.

The Academy's Flood Insurance Subcommittee submitted written [testimony](#) to the Senate Banking, Housing and Urban Affairs Committee regarding the NFIP on June 30, and also sent written [comments](#) to the committee on S. 1091 on July 11. In addition, the Casualty Practice Council held a Capitol Hill [briefing](#) on July 12 regarding the NFIP and the future of flood insurance in the United States. The briefing focused on current challenges facing the NFIP and the actuarial implications of those challenges. The briefing also served as a vehicle for the release of a [monograph](#), "The National Flood Insurance Program: Past, Present ... and Future?" Marty Simons, a member of the Academy's Extreme Events Committee, delivered a [presentation](#) on July 17 before the National Conference of Insurance Legislators' Property-Casualty Insurance Committee on the actuarial implications of the flood-mapping update being conducted within the NFIP.

Health Practice Council

Health Exchanges

HHS issued [proposed regulations](#) on July 15 addressing the [establishment of exchanges and qualified health plans](#). The exchanges, which should be operational by Jan. 1, 2014, are intended to provide a marketplace for individuals and small employers to compare private health insurance options on the basis of price, quality, and other factors.

The Academy's Exchanges Work Group offered [comments](#) on the proposed rule on Oct. 6. The work group urged the Centers for Medicare & Medicaid Services (CMS) to consider several general comments:

- The need for the regulations to ensure consistency between in-exchange and off-exchange market environments to mitigate adverse selection;
- The effect of choice on adverse selection;
- The need for more clarity and transparency related to administrative responsibilities.

Risk Sharing

CMS issued a [proposed rule](#) on July 15 addressing standards relating to reinsurance, risk corridors and risk adjustment. The proposed rule would put into effect the risk-sharing mechanisms in ACA—reinsurance, risk corridors, and risk adjustment. The risk-sharing provisions are intended to mitigate the impact of adverse selection and stabilize premiums in the individual and small group markets as insurance reforms and the new benefits exchanges are implemented.

The Academy's Risk Sharing Work Group presented [comments](#) to CMS on the proposed rule on Oct. 28. In addition to section-specific comments, the work group provided a number of general comments, including a request for clarification on whether “plan year” and “benefit year” are the same as “calendar year,” the need for information on methodologies in advance of 2014, the tradeoffs related to the timing of the risk-spreading programs' results, and the need for additional safeguards against risk selection.

Essential Health Benefits

The Institute of Medicine (IOM) on Oct 11 released a [consensus report](#) addressing essential benefits for health insurance offered through exchanges. The HHS Secretary asked IOM to recommend a process for determining what should be included in the essential health benefits package and how to update the package over time. The report does not contain any specific recommendations for what should be a part of any benefits package. The report recommends that HHS determine what the national average premium for a small employer plan would be in 2014 and use that as a threshold (i.e., the scope of benefits could not exceed that amount).

In December, HHS released a [bulletin](#) outlining its proposed regulatory approach in defining essential health benefits (EHB) under the ACA. The bulletin offers initial guidance and seeks public comment on the types of plans from which a state can choose its benchmark plan, ways to

supplement the benchmark plan so that it covers each of the 10 required benefit categories, treatment of state-mandated benefits, and benefit-design flexibility.

CLASS Act

A component of the ACA, the Community Living Assistance Services and Supports program (CLASS Act) would have established a voluntary long-term care services program. The act was designed to provide long-term care services for those who have become functionally disabled. The program, as initially envisioned, was to be funded entirely through insurance premiums and receive no taxpayer subsidies.

Concerns regarding the viability of the program had been present since it was first considered for inclusion in health reform legislation. In a July 2009 [letter](#) to the Senate Committee on Health, Education, Labor and Pensions, a joint Academy/Society of Actuaries (SOA) task force warned that the program, as designed, would suffer significant adverse selection due to the lack of an effective underwriting mechanism, a limited vesting period, and a lifetime cash benefit, among other design features. The group also noted that to meet the requirement that the program be actuarially sound for 75 years, the premium would be prohibitively expensive.

More recently, on March 17 Academy member Al Schmitz [testified](#) on behalf of the Academy during the U.S. House Committee on Energy and Commerce Subcommittee on Health's hearing regarding the CLASS Act.

In a [letter](#) dated Oct. 14, the Obama administration officially withdrew its support for the CLASS Act. HHS Secretary Kathleen Sebelius stated that there was no way to ensure the financial viability of the program but that HHS would continue to seek solutions to long-term care issues. The details of the CLASS Act and its funding methodology, as well as a detailed explanation of the reasons behind the withdrawal of support can be found in this [HHS report](#).

Medicare/deficit reduction

As mentioned above, the Academy's Medicare Steering Committee submitted an Aug. 31 [letter](#) to the Joint Select Committee on Deficit Reduction urging public policy proposals to improve the long-term solvency and sustainability of the Medicare program. The Academy reminded the members of the committee of the critical role Medicare plays in the provision of health care to the elderly and to permanently disabled young adults. The letter also restated the Academy's commitment to Medicare sustainability and offered links to previously released Academy documents addressing Medicare, including:

- *An Actuarial Perspective on Proposals to Improve Medicare's Financial Condition* (May 2011), which summarizes the key cost, access, and quality issues associated with some of the Medicare-related provisions in the various debt- and deficit-reduction proposals. http://www.actuary.org/pdf/Medicare_Financial_IB_Final_051211.pdf

- *Medicare's Financial Condition: Beyond Actuarial Balance* (May 2011), which highlights the key findings in the 2011 Medicare Trustees' Report.
<http://www.actuary.org/pdf/health/Medicare%20Financial%20IB%20Final%20052511.pdf>
- A presentation from a recent Capitol Hill briefing the Academy hosted that broke down some of the trustees' key findings and outlined several options for reforming the program.
http://www.actuary.org/pdf/health/MedicareTrusteesBriefing_Presentation_110527.pdf

Medical Loss Ratios

On March 17, Reps. John Barrow (D-Ga.) and Mike Rogers (R-Mich.) introduced a bill ([H.R. 1206](#)) that would amend the ACA by excluding agent compensation from the MLR formula. Under the ACA, no more than 20 percent (for individual and small groups) or 15 percent (for large groups) of premiums can go to “non-claims costs.”

HHS on Dec. 7 released [final rules](#) to implement MLR requirements for health insurance issuers under the ACA. Of particular interest, the final rule includes agent/broker compensation in the MLR calculation. The rule was released after the NAIC urged HHS to exclude commissions. The final rule also addresses the treatment of “mini-med” and expatriate policies, modifies the way existing regulations treat ICD-10 conversion costs, changes the rules on deducting community benefit expenditures, and revises existing regulations governing the distribution of rebates by issuers in group markets. The rule became effective Jan. 3, 2012.

Accountable Care Organizations

CMS issued the [final rule](#) on Nov. 2 for Accountable Care Organizations (ACOs), specifically the implementation of the Medicare Shared Savings Program (MSSP). Under the MSSP, providers of services and suppliers participating in an ACO can continue to receive traditional Medicare fee-for-service payments under Parts A and B, and be eligible for additional payments based on meeting specified quality and savings requirements.

The Academy's Health Care Quality Work Group sent a [letter](#) on June 6 to CMS regarding the initial proposed rule. The letter acknowledged that ACOs, as part of overall payment and delivery system reform, could play an important role in reforming Medicare. The work group stressed the need to “strike an appropriate balance between incentivizing provider participation through fewer restrictions and/or increased payments to ACOs and reducing Medicare cost growth.”

New Rate-Review Process

On May 23, CMS issued its [final rule](#) implementing the new process for the review and disclosure of “unreasonable” rate increases. About a month later, CMS requested public comments on the revised preliminary justification form and the consumer disclosure form.

Insurers are required to complete these forms to disclose and justify a rate increase that meets or exceeds 10 percent.

The Academy's Premium Review Work Group submitted a [letter](#) on June 28 to HHS and CMS in response to the revised preliminary justification and consumer disclosure forms. In addition to more technical comments, the work group encouraged CMS to ensure that there is consistency between the rate summary worksheet and the consumer disclosure form.

Life Practice Council

Annuity Disclosure Model Regulations

The NAIC adopted amendments to its [Annuity Disclosure Model Regulation](#) on Oct. 12. The amendments seek to increase uniformity, reduce consumer confusion with regard to the purchase of annuities, and improve disclosure. The amendments further provide insurers uniform guidance on developing disclosure information to better inform consumers about the annuity product purchased and how it works. The amendments address the increasing use of annuity illustrations during the sales process, improving the requirements for an illustration's development. In the preceding two years, the council submitted six comment letters and participated in numerous conference calls on this issue.

The Annuity Illustrations Subgroup of the Life Products Committee also submitted [comments](#) on Feb. 17 to the National Association of Fixed Annuities regarding the annuity disclosure model regulation. The regulation requires that clients receive a buyer's guide when purchasing an annuity. The work group stated that while it supported the premise of the regulation, changes were necessary for its proper implementation. The changes the work group suggested are intended to address two major issues: Ensuring that the requirements include enough detail so that the preparer of the illustration knows what is required and guaranteeing that the prospective contract owner will be able to compare illustrations from one company to another as easily as possible.

Pension Practice Council

IRS Guidance

Tax Return Preparers

The Academy's Pension Committee submitted [comments](#) on June 13 to the Internal Revenue Service (IRS) regarding [proposed changes](#) to existing regulations, specifically as they relate to retirement plan professionals. The committee stated its concern that the proposed changes may be applied to a broader group than is needed to achieve regulatory objectives.

The Committee urged the IRS to provide further clarification regarding the application of the Preparer Tax Identification Number (PTIN) requirements to the work that ultimately might support the determination of excise taxes reportable on IRS Form 5330. The committee also encouraged the IRS to exempt Form 5330 from the PTIN requirement or provide clarification as to when the requirement may apply to individuals involved in calculations that may be used in an

excise tax determination. In addition to Form 5330, the comments addressed IRS Form 5310-A, which the committee believes should be exempt from the PTIN requirement, as well as Form 5500, which the committee believes falls outside the definition of a tax return. Finally, the committee stated that if enrolled actuaries are required to obtain a PTIN as a matter of course due to any of the forms or responsibilities discussed in the proposed rule changes, then a reduction in the renewal fee similar to that proposed for enrolled agents and enrolled retirement plan agents would be appropriate.

Enrolled Actuaries

The Joint Board for the Enrollment of Actuaries (JBEA) issued [final regulations](#) on March 31 establishing standards and qualifications for actuaries serving employee benefit plans covered by ERISA. The final rules address eligibility for enrollment, requirements for continuing professional education, professional standards for performance of actuarial services, bases for disciplinary actions, and the procedures to be followed in taking those actions.

Pension Protection Act Implementation Issues

Multiemployer Pension Plans

The IRS [guidance document](#) on employee plans, released on Dec. 20, 2010, includes information specific to multiemployer pension plans, providing guidance through the form of questions and answers for sponsors of multiemployer defined benefit (DB) plans. On Jan. 27, 2011, the Multiemployer Plans Subcommittee presented a [webinar](#) addressing funding relief for multiemployer defined benefit plans.

Comments and Recommendations for Future Guidance

The Pension Committee submitted a [letter](#) to the Department of the Treasury and the IRS on June 1 regarding implementation issues of the Pension Protection Act (PPA) of 2006. The comments addressed future guidance on merger and spinoff issues related to the measurement of assets and liabilities for pension funding purposes and funding ratios. The committee suggested several alternatives to address the issues raised by mergers and spinoffs, including:

- Provide specific guidance on how to handle most situations that might arise and principles that could be applied to other situations;
- Provide a workable approach given the timing and data constraints that often accompany these transactions—particularly spinoffs;
- Make use of available valuation results to the extent possible so that results may be computed and verified easily, especially for any interim period measurements;
- Limit opportunities to manipulate results to achieve outcomes that are inconsistent with the PPA benefit restriction and funding rules.

2011 Social Security Trustees' Report

The Social Security Administration released its [annual report](#) from the Social Security Board of Trustees on May 13. The report details the actuarial status of the Social Security program to Congress and is required each year. Details from the 2011 trustees' report include:

- As of 2010, 54 million people were receiving benefits;
- Trust fund assets are projected to be adequate over the next 10 years under the intermediate assumptions;
- Annual cost for the Social Security program is projected to exceed non-interest income in 2011 and remain higher throughout the remainder of the long-range period.

The Social Insurance Committee released an [issue brief](#) in May and held a Capitol Hill [briefing](#) on May 26 addressing the trustees' report. The briefing summarized how financial projections had changed from 2010, the degree of actuarial balance present in the program, and what policymakers can do to address the program's long-term financial challenges.

Measurement of Pension Assets and Liabilities

Public Employee Pension Transparency Act

Representatives Devin Nunes (R-Calif.), Paul Ryan (R-Wis.), and Darrell Issa (R-Calif.) on Feb. 9 reintroduced a bill ([H.R. 567](#)) that would require state and local governments to report their methods and assumptions in addition to their existing financial data disclosures. Public employee pension plans also would be required to report their liabilities using a uniform accounting standard. The bill also would prohibit the federal government from providing any financial assistance or bailouts to public pension funds in the future. Senator Richard Burr (R-N.C.) introduced the companion bill in the Senate on Feb. 15.

IAS 19 Changes

The International Accounting Standards Board (IASB) issued a [press release](#) on June 16 announcing changes to International Accounting Standard No. 19 (IAS 19), an accounting rule addressing long-term employee benefits, including pension plans. Amendments to the rule include the recognition of all estimated changes in the cost of providing defined benefits and all changes in the value of plan assets, the use of a new presentation approach that would clearly distinguish between different types of gains and losses arising from DB plans, and improved disclosure requirements. The changes are expected to go into effect after Jan. 1, 2013.

The Academy joined with the SOA on July 20 to host a webinar discussing changes to IAS 19. The presenters provided background information on the changes, how U.S. GAAP will differ from the amended IAS 19, and what these changes mean for actuaries practicing in the United States.

Governmental Accounting Standards Board Activity

The Governmental Accounting Standards Board (GASB) issued exposure drafts on June 27 addressing [Accounting and Financial Reporting for Pensions](#) and [Financial Reporting for Pension Plans](#).

The proposed amendments to GASB Statement No. 27, outlined in the exposure draft on accounting and financial reporting for pensions, seek to improve accounting and financial reporting by state and local governments whose employees are provided with pensions. The proposed changes would amend the requirements of Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers*, as well as the requirements of Statement No. 50,

Pension Disclosures, as they relate to government employers that account for pensions provided through trusts, or equivalent arrangements, meeting certain criteria. Requirements of those statements would remain applicable to employers whose pensions are not covered by the scope of the proposed statement.

The amendments to GASB Statement No. 25, introduced in the financial reporting for pension plans exposure draft, seek to improve financial reporting by state and local governmental pension plans. Similar to the exposure draft on accounting and financial reporting, this proposal would amend the requirements of Statements No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*, and No. 50, *Pension Disclosures*, as they relate to pension plans that are administered through trusts, or equivalent arrangements, that meet certain criteria. Requirements of those statements would remain applicable to pension plans that are not covered by the scope of the proposed revision. Requirements applicable to DC plans that provide post-employment benefits other than pensions would remain effective for those plans.

Both exposure drafts would establish a definition of pension plan that reflects the primary activities of a fund that is used to provide pensions—the accumulation and management of assets dedicated for pensions and the payment of pensions to plan members as the benefits come due.

The Academy’s Pension Practice Council submitted a [comment letter](#) to the GASB on Oct. 14 regarding the two exposure drafts that included separate comments from the Academy’s Public Plans Subcommittee and Joint Academy/SOA Pension Finance Task Force. The subcommittee and task force voiced their support for the draft’s recognition of a net pension liability, the stipulation of a single actuarial method to calculate liabilities and annual costs, the proposals to reduce significantly deferrals of current costs, and the expansion of required disclosures. The subcommittee and task force also put forward their opposition to the rules for determining discount rates and the choice of entry age normal as the mandated method to determine liabilities and periodic costs.

Risk Management and Financial Reporting Council

Rules to Define Swaps

The U.S. Securities and Exchange Commission (SEC) and the Commodity Futures Trading Commission (CFTC) on April 27 issued [proposed regulations](#) on the definition of “swaps.” The proposed rules would define the majority of existing swap products and transactions as swaps, but insurance products would not be considered swaps or security-based swaps. According to the SEC’s [fact sheet](#) on the proposed rules and interpretative guidance, products offered by a regulated insurance company that would qualify as insurance include bonds, life insurance, health insurance, long-term care insurance, title insurance, property and casualty insurance, and annuity products in which income is subject to tax treatment under Section 72 of the Internal Revenue Code.

Both agencies are required by the Dodd-Frank Wall Street Reform and Consumer Protection Act to work together to create a system for regulating swaps, security-based swaps and agreements, and mixed swaps.

Credit for Reinsurance Model Law and Regulation

The NAIC on July 26 released exposure drafts for the [Credit for Reinsurance Model Law \(#785\)](#) and [Regulation \(#786\)](#). These documents are the result of ongoing efforts to reform reinsurance laws in the United States. The NAIC had determined that recently effective legislation, the Nonadmitted and Reinsurance Reform Act, did not implement its desired reform framework. The legislation, however, does preempt the extraterritorial application of state credit for reinsurance law and permits states of domicile to move forward with reinsurance collateral reforms on an individual basis if they are accredited. The legislation also does not prohibit states from acting together to achieve the reinsurance modernization framework goals.

The Academy's Reinsurance Subcommittee submitted [comments](#) to the NAIC on Sept. 1 regarding these drafts. The subcommittee suggested that the use of actuarial judgment be permitted to make required adjustments based upon the best available market information, actuarial standards, and common actuarial practice as outlined in applicable actuarial practice notes. The subcommittee also suggested that it not be constrained by overly restrictive regulatory language.

Insurance Core Principles

The International Association of Insurance Supervisors' (IAIS) revised its [Insurance Core Principles \(ICP\)](#) at its October 2011 general meeting. ICPs provide a globally accepted framework for the supervision of the insurance sector. Among the revisions were updates to ICP No. 14, *Valuation for Solvency Purposes*. The Academy's Solvency Committee submitted [comments](#) regarding the revised ICPs on May 18.

Own Risk and Solvency Assessment

The NAIC's Group Solvency Issues (EX) Working Group adopted the revised NAIC [Own Risk and Solvency Assessment \(ORSA\) Guidance Manual](#) in November. The goal of introducing ORSA into U.S. solvency proceedings is to provide regulators with meaningful insights into a company's risk management practices and, as a result, increase the efficiency and effectiveness of the regulatory review process.

The ERM Committee issued comments to the NAIC regarding ORSA on [Aug. 25](#) and [Oct. 28](#). To avoid any confusion, the committee urged the NAIC to add specific language into the manual that reiterates that the ORSA is an internal process to which regulators will have access rather than a new regulatory process. In addition, the committee stated that the ORSA should be reported on the same basis as risk is managed within a group. The committee recommended that the working group ensure that the manual appropriately captures the distinction between an ORSA, which is an internal process, and an ORSA report, which may include a summary of the ORSA process, its results at a specific point, and any significant changes to those results over

time with further references to internal documentation. The committee stated it would like clarification on how frequently regulators will require an ORSA report to be filed.

Credit Rating Agency Ratings

The Academy's Solvency Committee on Feb. 3 submitted [comments](#) to the Financial Security Board on its October 2010 paper, [Principles for Reducing Reliance on CRA Ratings](#). The committee urged more direct regulation of firms rather than imposing discipline on those that use Credit Rating Agency (CRA) services. The committee also noted that forcing a multitude of financial institutions around the world to develop identical analytic talents by eliminating the role of the few CRAs that already possess these talents seems inefficient.

If you have any questions regarding these issues, please contact Zack Bailey, the Academy's legislative assistant (202/223-8196; bailey@actuary.org).

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