

**LIFE PRACTICE NOTE 1995-14**  
**December 1995**

**Report Preparation**

**Introduction**

This practice note was prepared by a work group organized by the Committee on Life Insurance Financial Reporting of the American Academy of Actuaries. The work group was charged with developing a description of some of the current practices used by valuation actuaries in the United States. This work group was originally formed in 1992 and issued the first set of Life Practice Notes that year; changes have been made to this set of practice notes on an annual basis to reflect additional information on current practices.

The practice notes represent a description of practices believed by the work group to be commonly employed by actuaries in the United States in 1995. The purpose of the practice notes is to assist actuaries who are faced with the requirement of adequacy testing by supplying examples of some of the common approaches to this work. However, no representation of completeness is made; other approaches may also be in common use. It should be recognized that the information contained in the practice notes provides guidance, but is not a definitive statement as to what constitutes generally accepted practice in this area. Moreover, these practice notes are based upon the model Standard Valuation Law of the National Association of Insurance Commissioners (NAIC). To the extent that the laws of a particular state differ from the NAIC model, practices described in these practice notes may not be appropriate for actuarial practice in that state. This practice note has not been promulgated by the Actuarial Standards Board, nor is it binding on any actuary.

The members of the work group responsible for the original practice notes are as follows:

Donna R. Claire, chairperson

Arnold A. Dicke

Steven A. Smith

Douglas C. Doll

Stephen J. Strommen

Craig F. Likkell

Charles N. Vest

Linn K. Richardson

Michael L. Zurcher

Henry W. Siegel

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Additional review for the 1995 Life Practice Notes was provided by the following members of the American Academy of Actuaries' Committee on Life Insurance Financial Reporting:

Donna R. Claire  
Andrew R. Creighton      Frank W. Podrebarac  
James E. Hohmann      Meredith A. Ratajczak  
Michael J. O'Connor      Henry W. Siegel

Comments are welcome as to the appropriateness of the practice notes, desirability of annual updating, validity of substantive disagreements, etc. Comments should be sent to Donna R. Claire at her Directory address.

**Q. What type of actuarial reports should be prepared in connection with asset adequacy analysis?**

**A.** Many states require the preparation of an actuarial opinion, which is generally filed with the annual statement. In addition, most states require that an actuarial memorandum be prepared, although, at this time, companies may not be required to file the actuarial memorandum with the state insurance department, except as requested. However, New York Regulation 126 requires that the actuarial memorandum be submitted by all licensed insurers (not only domestic companies), unless the company gets a letter from an accredited state that has reviewed the company's actuarial memorandum from the prior year.

Some states have also requested an executive summary of the actuarial memorandum. The NAIC model *Actuarial Opinion and Memorandum Regulation* may be changed to require such a document.

**Q. What is typically contained in an executive summary?**

**A.** A number of actuaries prepared management executive summaries for years-end 1993 and 1994. These differed, depending on which items were of interest to company management. Some executive summaries gave a brief history of why the asset adequacy testing was done, the areas that contributed to the study, and results that highlighted the particular concerns of management. For example, some actuaries provided projections of risk-based capital levels at certain future points; others showed interim results for the next few years.

For years-end 1993 and 1994, certain regulators, such as Larry Gorski, Life Actuary of the Illinois Insurance Department, have requested an executive summary. Some actuaries provided the same

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executive summary given to company management; others prepared a separate document specifically addressing the items requested by the regulators.

**Q. What is required to be covered in the regulator's executive summary?**

**A.** Any regulator requiring an executive summary will inform companies of such requirements, either by a letter or regulation. The following is a preliminary list of items to be covered in the memorandum executive summary that would be required under proposed changes to the NAIC model *Actuarial Opinion and Memorandum Regulation*:

1. the amount needed to eliminate all *market value* negative surplus at the end of the testing period;
2. any material differences in assumptions from the year before;
3. the reserves subject to asset adequacy the year before, but not subject in the current opinion;
4. the number of additional interest rate scenarios tested, and the number that produced negative *market value* of surplus;
5. the types of sensitivity tests performed;
6. the comments on the interim results;
7. the method used to recognize the impact of reinsurance; and
8. whether the actuary recognized all options embedded in assets.