



AMERICAN ACADEMY *of* ACTUARIES

Report of the American Academy of Actuaries' Valuation and Law Manual Team

Presented to the National Association of Insurance Commissioners' Life and Health Actuarial Task Force (LHATF)

LHATF Fall 2007 NAIC Meeting

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Valuation Law and Manual Team

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The American Academy of Actuaries' Valuation Law and Manual Team (VLMT) is continuing its work to propose further development of the June 2007 exposure of the NAIC Valuation Manual (VM). Team efforts or additional documents since the June NAIC meeting include the following:

- The Introduction and the first section were modified to clarify that the Valuation Manual covers all reserve valuations for life, annuity, accident and health, and deposit-type contracts whether principles-based or not.
- Sections 2 and 3 in the VM were combined and provide direction on the reserve requirements applicable to various products. LHATF will determine which product types are subject to a principles-based reserve (PBR) valuation. The VLMT continues to provide input to LHATF by surveying LHATF members and other interested regulators regarding which product types should be subject to PBR on the operative date of the VM. Another survey was drafted and sent to LHATF and interested regulators and the results of the survey will be presented at the September LHATF meeting and responses from these surveys will be considered by the VLMT in drafting proposed changes to the VM requirements for LHATF consideration.
- The current draft VM Sections 2 thru 5 provide applicability of specific requirements which are included in Section 6 of the VM. Specific requirements listed in Section 6 have descriptive titles and a designation such as "VM-20." These VM designations will be used to help locate requirements and for reference purposes.
- The Academy's Life Reserves Work Group (LRWG) is proposing a number of changes to the draft Requirements for Principles-Based Reserves for Life Products. This revised draft will be provided to LHATF at the September meeting for consideration. This draft is found in the VM as "VM-20."
- The Academy's Annuity Reserves Work Group (ARWG) has completed a first draft of proposed principles-based valuation requirements for fixed annuities. This draft will be provided to LHATF at the September meeting for consideration. This draft is found in the VM as "VM-22."
- The Academy's VLMT is proposing that a separate Credit Life and Disability Insurance section be added to the VM. The proposed requirements in this section consist of the credit life mortality table model regulation for credit life and the credit disability requirements from the Health Reserves Model Regulation for credit disability, as well as reserve components from SSAP 59 in the Accounting Practices and Procedures Manual. The draft of these credit requirements are found in the VM as "VM-26."
- VLMT is proposing technical, non-substantive changes to the health reserve requirements in the VM. The proposed health reserve requirements are a redrafted version of the Health Reserves Model Regulation requirements. One of the suggested changes removes the credit disability reserve requirements and places these requirements in a separate Credit Life and Disability Insurance section in the Valuation Manual. Note that it is not the intent to suggest developing PBR for health products by the operative date of the valuation manual, but rather that health reserve requirements remain the same as current requirements. The current draft of these health reserve requirements are found in the VM as "VM-25."
- VLMT is proposing revisions to the Actuarial Opinion and Memorandum (AOMR) requirements to incorporate PBR. This proposal will be included in the VM that is presented to LHATF at the September meeting. The current draft of these AOMR requirements are found in the VM as "VM-30."
- A survey was drafted and sent to LHATF members and interested party regulators to get input on experience reporting requirements, including the scope of the requirements. The results of this survey will be presented at the September LHATF meeting.
- Work is continuing on development of a proposal for a material tail risk test in the draft Requirements for Principles-Based Reserves for Life Products that would determine whether stochastic modeling is required.
- Work is underway to develop a proposal for a simplified approach to model non-guaranteed elements (NGEs) for Life Products. The current draft Requirements for Principles-Based Reserves for Life Products requires a full projection of NGEs within the cash flow model. However, under some conditions, NGEs offset modeled experience changes such that the resulting reserve is essentially independent of projected experience changes. This simplified approach would define these conditions and define a simplified calculation method that does not require a full projection of NGEs.

Key issues to be discussed at the September 2007 LHATF meeting include the following:

PBR Review Actuary and Appointed Actuary Issues:

1. Should the appointed actuary be allowed to rely on the opinion of other valuation actuaries with respect to compliance with PBR requirements?
2. To what extent should areas of disagreement between PBR review actuary and appointed actuary be disclosed? Should the reserve impact of the areas of disagreement be quantified? Should only unresolved areas of disagreement be disclosed (in either the work papers or the PBR review report)?
3. Should the commissioner have the authority to waive qualification and/or independence requirements, retention requirements, etc.? If yes, should it be only the domiciliary commissioner or each state's commissioner?

LRWG-Related Issues:

1. Material Tail Risk Test for stochastic modeling exclusion -- methodology and setting the "pass mark."
2. Possible simplified method for Deterministic Reserve if a company passes the material tail risk test.
3. Simplified method to model non-guaranteed elements.
4. Simplified approach for determining mortality assumptions.
5. Refinements to credibility weighting process for setting mortality assumption.
6. What are the "objectives of statutory reporting" for purposes of setting assumptions and margins?
7. In determining mortality assumptions for blocks of business with little or no credibility, should a company be able to use a loaded valuation table (for example, by mapping to an appropriate valuation table based on underwriting criteria)? Or must the method outlined in the LRWG requirements be used for all blocks of business?
8. Must a company use fully allocated expenses: 1) if the company is small; or 2) for a new line of business? Or, could the company use an industry-type or exit-value basis to ensure consistency in reserves across companies?

ARWG-Related Issues:

The Academy's ARWG has submitted a report on efforts to date and it's draft of the ARWG requirements. The ARWG report includes key issues and future developments for LHATF consideration. Please refer to this report for more discussion of issues and future developments that includes those listed below:

1. Deterministic reserve to be developed.
2. Consideration of a stochastic modeling exclusion/simplified requirements.
3. Scope issues.
4. Reconciliation of margins in aggregate vs. individual assumptions.
5. Provision for model understatement.
6. Definition of anticipated experience assumptions.
7. Effect of IMR on stochastic reserve.

Scope Issues on VM Operative Date:

1. What is the scope of the experience reporting requirement? Only products subject to PBR? Certain life products? Who will set the priorities and details for the risks that need experience reporting and how the data needs to be submitted? See results of Subgroup 3 survey.
2. What products should be subject to PBR on the operative date of valuation manual? See Subgroup 4 survey results.
3. Consider whether any exemptions or phase in are based on product type, company size, or a combination. Scope issues are relative to experience reporting and any PBR requirements such as LRWG, ARWG, and PBR review requirements.

Reinsurance Related Issues:

1. Should the Academy's Reinsurance Work Group recommendation on the treatment of reinsurance risk transfer within a PBR be incorporated into the VM?

General Valuation Manual Related Issues/Considerations:

1. The process for coordination with the SAPWG and the APPM is deferred to LHATF. The general goal is for the APPM and the Valuation Manual to use the same reserve requirements at the same time after the VM operative date for a minimum scope of new issues. A rough draft for a start to this process is provided in the Valuation Manual.
2. A related coordination consideration is whether the Valuation Manual should refer back to reserve requirements in the APPM for non-PBR reserve requirements for new issues. This direction is currently reflected in the VM except for health and credit non-PBR requirements where these have been drafted into the Valuation Manual. Alternative directions to reference non-PBR requirements will be discussed at the September LHATF meeting.
3. LHATF may want to consider inclusion of guidance with examples to explain how to apply the PBR requirements provided in the Valuation Manual. Such guidance would be clearly qualified as such and can be integrated within the Valuation Manual.