



AMERICAN ACADEMY of ACTUARIES

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September 16, 2015

Commissioner Julie Mix McPeak and Superintendent Joseph Torti, III  
Co-Chairs, NAIC Principle-based Reserving Implementation (EX) Task Force  
National Association of Insurance Commissioners

Via email: kdefrain@naic.org

Dear Commissioner McPeak and Superintendent Torti:

On behalf of the American Academy of Actuaries<sup>1</sup> Life Practice Council (LPC) I appreciate the opportunity to provide its comments on the August 6, 2015 draft proposal for “*Substantially Similar Terms and Provisions*” to Determine the Valuation Manual Operative Date exposed by the NAIC Principle-Based Reserving Implementation (EX) Task Force (the Task Force).

We support the process outlined in the proposal, as we believe that it appropriately defines a way to determine whether a state’s adoption of the Standard Valuation Law (SVL) has “substantially similar terms and provisions” to the Model Law. That being said, we would like to make further comments on the key issues recommended for further discussion (underlined below).

A. The meaning of the phrase “substantially similar terms and provisions” in the SVL will be interpreted such that an objective third party would agree.

We suggest that the Task Force consider an outcome-based definition of “substantially similar;” that is, terms and provisions are “substantially similar” if terms and conditions would likely result in minimum reserve levels that are *similar* to, and procedures that are not *materially different* from those prescribed by the SVL and Valuation Manual (VM). By “similar” minimum reserve levels, we mean minimum reserve levels for any individual company that is within a reasonable range of the minimum reserve calculated per the SVL and the Valuation Manual (VM) (i.e., not materially higher or lower). By “materially different” procedures, we mean procedures that are sufficiently different from those required by the SVL and VM that they compromise the consistency of procedural compliance relied

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<sup>1</sup> The American Academy of Actuaries is an 18,500-member professional association whose mission is to serve the public and the U.S. actuarial profession. The Academy assists public policymakers on all levels by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States.

upon by other states. We recognize that this definition of “substantially similar” would involve judgment, but we believe an outcome-based criteria for reserve levels and required procedures is important. NAIC staff could provide the necessary technical expertise to assist in this process.

This proposed definition of “substantially similar” departs from the definition used for determination of a state’s accreditation: “State statute should prescribe *minimum* standards for the establishment of liabilities and reserves resulting from insurance contracts issued by an insurer...”<sup>2</sup> (*emphasis added*). We believe it is important that the process adopted for making decisions as to what constitutes “substantially similar” for determining the Valuation Manual operative date threshold does not default to the standard used for accreditation. If a state’s law requires minimum reserves to be substantially higher than the NAIC model law’s minimum reserve levels, the goal of uniformity between states is less likely to be achieved.

B. We support the five general steps in the determination process.

C. The Task Force evaluation would be conducted in line with the details identified for Step 3. Our comments on the issues that the Task Force may want to discuss (bolded) follows:

**Should the Task Force have pre-agreed decisions about specific situations being “substantially similar” or not?**

We believe that pre-agreed decisions pose some risks in that they would not cover every situation leading to the deviations in the terms and provisions.

**If pre-agreed decisions are made, are the examples for Step 3 included in the proposal appropriate?**

We consider these examples as guidance rather than pre-agreed decisions. That being said, our comments follow:

Deviation #1 – Use of exact effective date: In general, the recommendation seems appropriate. The survey of the current states would be needed to ensure that “x” is a reasonable number, given the circumstances surrounding the state requirement.

Deviation #2 – Adoption of VM by regulation: In general, the recommendation seems appropriate, but as with Deviation #1, the survey of the current states would be needed to ensure that “x” is a reasonable number, given the circumstances surrounding the state requirement.

Deviation #3 – Small company exclusion:

- 3.b.ii - We believe that a third consideration should be added to 3.b.ii.: “Would the companies subject to a broader exemption than the VM be allowed to hold substantially higher or lower reserves?” We are comfortable with this being a judgment call, but we believe that it is an important question to consider.
- 3.c. – We generally agree with this position for the following reasons:
  - In 3.c.i, there are many consequences of such an exemption. Substantially higher or lower minimum reserves could be one of those consequences. In addition, we are concerned with the precedent for a company not needing to comply with

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<sup>2</sup> From the NAIC’s August 2015 summary pamphlet of the **Financial Regulation Standards and Accreditation Program**.

required procedures of the VM (e.g., for the contribution of experience data), even if it is a small company with limited experience to contribute.

- In 3.c.ii, holding reserves other than CRVM produces “substantially higher or lower minimum reserves,” by definition.

**If the Task Force prefers to eliminate specific examples from the proposal and would rather opt for an agreed principle, what should the principle be?**

- Evaluate the precedent set for states still considering SVL adoption and/or other NAIC decisions.
- We believe that the principle currently included in 3.b., “evaluate whether a difference would impact uniformity of the system” is too vague to stand on its own. It should be followed by the phrase, “and whether the difference produces minimum reserves that are substantially higher or lower than the NAIC model law.”
- The Drafting Group’s discussion included a possible need to assess the “harm to solvency” that would result from a deviation in the law. If such an assessment were desired, a subsequent suggestion is that the NAIC process to validate deviations be required to provide a demonstration of the harm a deviation does to the uniform application of the SVL. We agree that such a demonstration is necessary and that it is also important to consider any precedent that might be set by allowing a deviation.

As the details of this process are being finalized or implemented, the LPC is willing to assist in resolving specific questions that arise.

Please contact Scot Davies, the Academy’s life policy analyst ([davies@actuary.org](mailto:davies@actuary.org); 202-223-8196) if you have any questions.

Sincerely,

Mary Bahna-Nolan, FSA, MAAA  
Vice President  
Life Practice Council  
American Academy of Actuaries

Cc: Kris DeFrain