AMERICAN ACADEMY *of* ACTUARIES

Principles from the American Academy of Actuaries'
Consistency: Principles, Summary, Definitions & Report Format Work Group

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

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The American Academy of Actuaries is a national organization formed in 1965 to bring together, in a single entity, actuaries of all specializations within the United States. A major purpose of the Academy is to act as a public information organization for the profession. Academy committees, task forces and work groups regularly prepare testimony and provide information to Congress and senior federal policy-makers, comment on proposed federal and state regulations, and work closely with the National Association of Insurance Commissioners and state officials on issues related to insurance, pensions and other forms of risk financing. The Academy establishes qualification standards for the actuarial profession in the United States and supports two independent boards. The Actuarial Standards Board promulgates standards of practice for the profession, and the Actuarial Board for Counseling and Discipline helps to ensure high standards of professional conduct are met. The Academy also supports the Joint Committee for the Code of Professional Conduct, which develops standards of conduct for the U.S. actuarial profession.

Consistency: Principles, Summary, Definitions & Report Format Work Group

Robert DiRico, A.S.A., M.A.A.A., Chair

Tom Campbell, F.S.A., M.A.A.A.
Donna Claire, F.S.A., M.A.A.A.
John Morris, F.S.A., M.A.A.A.
Dave Neve, F.S.A., M.A.A.A.
Kory Olsen, F.S.A., M.A.A.A.

Principles-based Approach (PbA) means an approach to calculate statutory reserves and capital requirements for insurance companies that incorporates the following concepts:

1. Captures all of the material financial risks, benefits, and guarantees associated with the contracts, including the 'tail risk' and the funding of the risks.

2. Utilizes risk analysis and risk management techniques to quantify the risks and is guided by the evolving practice and expanding knowledge in the measurement and management of risk. This may include, to the extent required by an appropriate assessment of the underlying risks, stochastic models or other means of analysis that properly reflect the risks of the underlying contracts.

3. Incorporates assumptions and methods that are consistent with, but not necessarily identical to, those utilized within the company's overall risk assessment [1] process.

4. Permits the use of company experience, based on the availability of relevant company experience and its degree of credibility, to establish assumptions for risks over which the company has some degree of control or influence.

5. Provides for the use of assumptions, set on a prudent best estimate basis, that contain an appropriate level of conservatism when viewed in the aggregate and that, together with the methods utilized, recognizes the solvency objective of statutory reporting[2].

(1) Company risk assessment processes include but are not limited to experience analysis, asset adequacy testing, GAAP valuation and pricing.

(2) The stated objectives of statutory reporting according to paragraph 27 of the preamble to the Accounting Practices and Procedures Manual (March, 2005) is "solvency for the protection of policyholders" and "the regulator's ability to effectively determine relative financial condition using financial statements." Note, that this second objective is unlikely to be promoted by PbA, while the ability to determine the financial condition of the company relative to varying risks would be increased.