

UL Working Group Presentation to LHATF

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Objectives for Today's Session

- Clarify the purpose of the ULWG
- Review definition of a “principle-based” approach
- Summarize the level of industry support for a principle-based approach
- Describe basic framework of new approach
- Discuss future LHATF involvement with ULWG

Purpose of the ULWG

- Our focus is the development of a principle-based framework for products in our scope (UL with SG, term, and VUL) that can be universally applied to **ALL** life products
- Part of the Academy's principle-based initiative, along with the SVL 2, VACARVM, and C3 P2 work groups
- We are not addressing possible solutions to the issues raised by the AG38 controversy -- we are deliberately staying out of the AG38 debate.

Update on Timing and Deliverables

- We have worked very hard to meet our very aggressive intermediate deadlines
- Still on track to hit our goal of providing the Task Force with a recommendation at the December 2005 NAIC meeting to expose for comment
- Prior to the June NAIC meeting, we will provide the Task Force with the first draft of our recommendation, which will include a list of Basic Principles

Update on Timing and Deliverables (cont)

- At the June NAIC meeting, we hope to accomplish two things:
 1. Discuss in some detail the first draft of our recommendation
 2. Ask the Task Force to formally adopt the Basic Principles
- Need high level of involvement from the Task Force in order to meet our goals

Overview of Principle-based approach

- Captures all of the material risks, benefits and guarantees of the contract
- Uses basic principles of risk analysis and risk management
- Does NOT necessarily require a modeling and/or stochastic approach – only when necessary to properly capture the risks of the contract

Overview of Principle-based approach (cont)

- For some products, a deterministic, single scenario is adequate to capture the risks of the contract
- But for products with material “tail risk” or a high level of uncertainty in cash flows arising from optionalities in the contract, a stochastic approach may be necessary to adequately capture the risk
- A stochastic approach does not require that all assumptions be stochastically modeled

Support for moving to a Principle-based approach

There is strong support from the industry

- The ULWG has over 40 members representing companies on both sides of the AG38 debate
- The ACLI Board and ACLI Actuarial Committee have recently passed resolutions to support the efforts of the ULWG.
- The ACLI has formed a tax work group to address tax issues (so has the Academy)
- We have not heard of any company opposed to the concept of moving to a principle-based approach.

Basic framework of Proposed Methodology

Reserve is the greater of:

1. A deterministic, seriatim, single scenario reserve calculation
2. A stochastically derived reserve (if needed) using a prescribed CTE level

Basic framework of Proposed Methodology (cont)

Deterministic Reserve:

- Uses a single set of assumptions that is aligned with economic reality, yet still provides an appropriate level of conservatism
- May help address tax issues

Stochastic Reserve: Multiple scenarios will be defined to properly capture the “tail risk” for assumptions that involve a high level of optionality

Basic framework of Proposed Methodology (cont)

For both deterministic and stochastic calculations:

- Gross Premium Valuation. A GPV approach will be used that captures all material risks (interest rate movements, mortality, lapse, premium patterns, expenses, etc)
- Prudent Best Estimates. For assumptions not stochastically modeled, margins will be established using the principles of “prudent best estimates”

Basic framework of Proposed Methodology (cont)

- Company Experience. For risks that the company has some control over (e.g. mortality through underwriting policies) assumptions based on company experience will be allowed if credible experience can be demonstrated (i.e. a blend of prescribed assumptions and company experience)
- Prescribed Assumptions. For risks that the company has little or no control over (e.g. interest movements) prescribed assumptions will be used

LHATF Involvement

- The ULWG respectfully requests a high level of Task Force involvement moving forward
- Possible options:
 1. Task Force forms a subgroup to work with ULWG
 2. Task Force members join a ULWG subgroup
 3. One-on-one meetings with Task Force members to solicit comments

