



AMERICAN ACADEMY *of* ACTUARIES

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**Consistency Work Group Report's  
Definitions to include in VM-1 of the Valuation Manual**

**Presented to the NAIC's Life & Health Actuarial Task Force**

**March 2008**

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## Definitions to include in VM-1 of the Valuation Manual:

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1. “Accumulated Deficiency” means the projected Working Reserve, if any, less the annual statement value of projected assets and measured as of the projection start date and as of the end of each projection year. (This definition applies to Life & Annuity products only)
2. “Actuary” means a risk professional who meets the qualifications in Section [ ] of the Valuation Manual to certify that the reserves for the policies subject to these requirements have been calculated in accordance with all applicable laws, regulations, actuarial guidelines and Actuarial Standards of Practice.
3. “Annual Statement” means an annual statement required by state insurance law or regulation to be filed by the Company with the office of the Commissioner.
4. “Anticipated Experience Assumption” means an expectation of future experience for a risk factor given available, relevant information pertaining to the assumption being estimated and set in such a manner that it is reasonable to expect that the actual value of the risk factor is as likely to be greater than the assumed value as less than the assumed value.
5. “Appointed Actuary” means an individual who is appointed or retained in accordance with the requirements set forth in the statutory insurance laws and regulations to provide the actuarial opinion and supporting memorandum as required by the Standard Valuation Law.
6. “Cash Flow Model” means a model designed to simulate asset and liability cash flows.
7. “Cash Surrender Value” means the amount available to the Contract/ Policyholder, if any, due to surrender of the Contract/Policy, prior to any outstanding Contract/ Policy indebtedness and net of any applicable surrender charges. The Cash Surrender Value shall reflect any applicable market value adjustments where the underlying assets are reported at market value, but shall not reflect any market value adjustments where the underlying assets are not reported at market value. (Note: where there is a Group Certificate and it has a cash value, this applies to the certificate within the Group Contract/Policy)
8. “Commissioner” means the commissioner, superintendent or director of insurance for a state, district or territory where the Company is licensed.
9. “Company” means an entity subject to the provisions of this Valuation Manual.
10. “Conditional Tail Expectation” means a risk measure that is calculated as the average of all modeled outcomes (ranked from lowest to highest) above a prescribed percentile.
11. “Contract” means an individual annuity policy or group annuity policy or certificate.
12. “Derivative Instrument” means ‘an agreement, option, instrument or a series or combination thereof:
  - a. To make or take delivery of, or assume or relinquish, a specified amount of one or more underlying interests, or to make a cash settlement in lieu thereof; or
  - b. That has a price, performance, value or cash flow based primarily upon the actual or expected price, level, performance, value or cash flow of one or more underlying interests.’  
(Source: NAIC Accounting Practices and Procedures Manual)This includes, but is not limited to, an option, warrant, cap, floor, collar, swap, forward or future, or any other agreement or instrument substantially similar thereto or any series or combination thereof. Each derivative instrument shall be viewed as part of a specific derivative program.
13. “Derivative Program” means a program to buy or sell or open or close one or more derivative instruments to achieve a specific objective. Both hedging and non-hedging programs (e.g., for replication or income generation objectives) are included in this definition.

14. "Discount Rates" means the path of rates used to derive the present value.
15. "Fraternal Benefits" means payments made for charitable purposes by a fraternal life insurance company that are consistent with and/or support the fraternal purposes of the company.
16. "Gross Reserve" means the amount of the Reported Reserve that would have been held in the absence of any ceded reinsurance. This includes direct and assumed business.
17. "Gross Wealth Ratio" means the cumulative equity index return for the indicated time period and percentile (e.g., 1.0 indicates that the index is at its original level).
18. "NAIC" means the National Association of Insurance Commissioners.
19. "Path" means a time-indexed sequence of a set of values.
20. "Projection Interval" means the time interval used in the cash flow model to project the cash flow amounts (e.g., monthly, quarterly, annually).
21. "Projection Period" means the period over which the cash flow model is run. (This definition applies to Life & Annuity products only)
22. "Projection Start Date" means the date on which the projection period begins.
23. "Projection Year" means a 12-month period starting on the projection start date or an anniversary of the projection start date.
24. "Prudent Estimate Assumption" means a deterministic assumption used to represent a risk factor developed by applying a Margin to the Anticipated Experience Assumption for that risk factor.
25. "Valuation Date" means the date for which the Reported Reserve is to be valued as required by the Standard Valuation Law.

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26. "Asset-Associated Derivative" means a derivative program whose derivative instrument cash flows are combined with asset cash flows in performing the reserve calculations.
27. "Deterministic Reserve" means the amount determined on a seriatim basis using one or more specified scenarios. Deterministic Reserves include reserves calculated using formula based methods.
28. "Liability-Associated Derivative" means a derivative program whose derivative instrument cash flows are combined with liability cash flows in performing the reserve calculations.
29. "Margin" means an amount included in the assumptions used to determine the minimum reserve that is intended to incorporate conservatism in the calculated value consistent with the requirements of the various sections of this Manual. It is intended to provide for estimation error and adverse deviation.
30. "PBR Actuarial Report" means the supporting information prepared by the Company as required by VM-31.
31. "Reinsurance Aggregate Cash Flows" means the difference between the Reinsurance Cash Flows and Reinsurance Discrete Cash Flows, as defined in VM-1.
32. "Reinsurance Cash Flows" means the net amount paid between the company and its reinsurer. Positive reinsurance cash flows shall represent amounts payable from the reinsurer to the company; negative reinsurance cash flows shall represent amounts payable from the company to its reinsurer.

March 20, 2008

33. “Clearly Defined Hedging Strategy” means a type of prospective Derivative Program of the company that:
- a. is established to hedge risks through the future purchase or sale of derivative instruments or opening or closing of hedging positions;
  - b. may be dynamic, static or a combination thereof; and
  - c. meets the requirements specified in the applicable reserve standard.
34. “Derivative Program” means a program to buy or sell one or more derivative instruments or open or close hedging positions to achieve a specific objective. Both hedging and non-hedging programs (e.g., for replication or income generation objectives) are included in this definition.

[Note: this is a change to #13 above and the requirements section should discuss the following phrase that was removed from the definition - 'that has been defined or approved by the company's Board of Directors or a subcommittee thereof.' ]

35. “Non-guaranteed Elements (NGE)” means either: (a) dividends under participating policies or contracts; or (b) other elements affecting life insurance or annuity policyholder/contract holder costs or values that are both established and subject to change at the discretion of the insurer.

[Note: the requirements section needs to reflect issues associated with this new wording; the Consistency Work Group has recommended wording]

36. “Policyholder Behavior” means any action or nonaction (excluding the use of non-elective benefits) by a policyholder, contract holder, or other party having rights or options under the policy or contract including, but not limited to, lapse, withdrawal, transfer, deposit, premium payment, loan, annuitization, or benefit election.
37. “Reinsurance Policy Cash Flows” means reinsurance cash flows that can be directly attributable to each covered policy.
38. “Revenue Sharing” means any arrangement or understanding by which an entity responsible for providing investment or other types of services makes payments to the company or to one of its affiliates. Such payments are typically in exchange for administrative services provided by the company or its affiliate, such as marketing, distribution and recordkeeping. Only payments that are attributable to charges or fees taken from the underlying variable funds or mutual funds supporting the policies or contracts that fall under the scope of the given standard shall be included in the definition of “Revenue Sharing.”
39. “Risk Factor” means an aspect of future experience that is not fully predictable on the valuation date.
40. “Scenario” means a sequence of outcomes used in the cash flow model, such as a path of future interest rates, equity performance, or separate account fund performance.

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