March 21, 2022

AMERICAN ACADEMY *of* ACTUARIES

Mr. Mike Boerner,
Chair
Life Actuarial (A) Task Force (LATF)
National Association of Insurance Commissioners

Re: Comments on the exposed draft Actuarial Guideline on Asset Adequacy Testing

Dear Mr. Boerner,

The Asset Modeling and Reporting Task Force of the American Academy of Actuaries ("the Task Force") is pleased to provide the following comments on the draft Actuarial Guideline (AG) on Asset Adequacy Testing (AAT) which was exposed during LATF's February 10 meeting.

The Task Force appreciates the need to provide guidance in this area and believes that appointed actuaries should be able to explain the drivers of asset performance and how they've reflected the asset risks in their AAT. We support the principle-based guidance and required disclosures in the AG which will help facilitate consistent practice by appointed actuaries and understanding by regulators. However, the Task Force believes the constraints in the AG (e.g., arbitrary yield caps) are at odds with the independence and judgment appointed actuaries need to perform AAT given the wide variety of products and risk profiles of insurers. We strongly recommend the AG focus on principle-based guidance and required disclosures instead of prescribing non-principle-based constraints which could hamper the appointed actuary's ability to assess the risks affecting an insurer's specific mix of assets and liabilities, and how to best reflect those risks in AAT.

Regarding the AG's scope, the Task Force believes company-wide exclusions from the AG should be based on a company's current and future asset portfolio, not an arbitrary company size threshold (whether measured on a gross or net basis). For example, exclusions could be allowed based on a defined maximum weighted average assumed spread in AAT or defined criteria on the mix of assets a company uses for asset adequacy testing, e.g., considering the quality, volatility, and liquidity characteristics of those assets.

Regarding the AG's method of identifying high risk assets based solely on asset ratings, we note that due to limitations of and potential inconsistencies among ratings of complex assets, the asset rating alone does not always provide sufficient information regarding an asset's risk profile. Therefore, we suggest using principle-based approaches to identify assets with high risk relative to their yield, rather than basing their identification solely on asset ratings.

Regarding reinsurance, we note that U.S. actuaries are required to follow ASOP 11**,** *Treatment of Reinsurance or Similar Risk Transfer Programs Involving Life Insurance, Annuities, or Health Benefit Plans in Financial Reports***,** which has recently been revised (with an effective date of December 1, 2022). Our task force believes that the judgment of the appointed actuary, following actuarial standards of practice in revised ASOP 11, is preferable to prescribing certain situations when AAT must be performed on a gross basis.

Regarding the treatment of equities in the AG, we believe it will be difficult to apply some of the requirements in the exposed AG to equities and suggest considering the development of separate guidance that is specific to the treatment of equities.

The exposure specifically asked for comments on the pros and cons of an individual asset-specific versus aggregate sensitivity test as required in Section 5.A of the AG. The Task Force believes that many companies would perform 5.A's sensitivity test at the individual asset (or asset group when there is asset compression) level, however we recommend leaving this decision up to the appointed actuary since some companies may need or want to perform this sensitivity test at more aggregate levels for practical reasons, e.g., when portfolios are managed to an aggregate mix of assets. Also, in line with our comments regarding constraints above, the Task Force believes it is appropriate that the sensitivity test in Section 5.A remain a disclosed sensitivity test, rather than becoming a prescribed constraint in 2023 as is currently the case in the AG.

The exposure specifically asked for comments on the inclusion of board of director and senior management responsibilities on the quality of complex asset-related assumptions like those stated in the Valuation Manual's Governance section (VM-G). Our task force believes that the inclusion of such responsibilities would be beneficial. If additional such responsibilities are added to VM-G we recommend materiality be a consideration.

The Task Force is concerned the amount of work required to comply with the AG by year-end 2022 will be a challenge for some appointed actuaries. In particular, the seriatim attribution analysis required in Section 5.B requires extensive effort, and judgment on how elements are attributed, so we suggest considering alternatives such as limiting the analysis to a handful of assets, postponing the analysis to year-end 2023, doing the analysis at a more aggregate level, or relying on the other required disclosures in Section 4. In addition, if a company is required to make certain model enhancements per Section 4.E, implementing those enhancements in a well-governed and controlled environment by year-end 2022 may be challenging.

Finally, the Task Force appreciates the urgency on this issue however we would prefer the requirements in the AG be implemented directly through the Valuation Manual's section on the Actuarial Opinion and Memorandum (VM-30) rather than first being implemented as an Actuarial Guideline to accomplish an earlier effective date for the requirements.

Thank you for your consideration of these comments. Please contact the Academy's deputy director for public policy Devin Boerm (boerm@actuary.org), with any questions.

Sincerely,

Jason Kehrberg, MAAA, FSA
Chairperson
Asset Modeling and Reporting Task Force
American Academy of Actuaries