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Polysystems, Inc.

EDITOR
Jackie Smith

ASST. EDITOR
Tom Cook

PRODUCTION
Debbie Christensen

CHICAGO OFFICE
30 N. LaSalle Street
Suite 3600
Chicago, IL 60602
P 312.332.5670
F 312.332.2391

NJ OFFICE
2 Executive Campus
Suite 320
Cherry Hill, NJ 08002
P 856.663.8711
F 856.663.8712

www.polysystems.com

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VACARVM – Poly is Moving Forward, Are You?

—*Timothy P. Gaynor, FSA, MAAA, Vice President*

A Life and Health Actuarial Task Force (LHATF) conference call was held on July 10, 2008. The topic was VACARVM. During this call, regulators exposed a new version of VACARVM.

The Exposure Draft

The most recent exposure has a drafting date of 7/10/2008 and is available at www.naic.org under the “Life and Health Actuarial Task Force” section of the “Committees and Activities” page. LHATF will be accepting comments on the current exposure through August 14, 2008. Comments will be reviewed on a LHATF conference call scheduled for August 20, 2008 at 11:30 C.S.T.

The Dates

The most significant development is that the effective date has been changed from 12/31/2008 to 12/31/2009. This means that you will once again have more than a year to prepare. The difference this time around, however, is that it is more likely that VACARVM will be adopted. The 7/10/2008 exposure draft is the first version that has been exposed without opposition. Prior versions were exposed with strong opposition.

VACARVM must still be adopted before it can take effect. As of the date of this publication,

it looks like all parties could be in a position to adopt VACARVM by the end of 2008.

The Standard Scenario

At this point, it appears that the standard scenario amount will likely be the VACARVM reserve. The most recent exposure does permit higher, more realistic margins, but it also prescribes more severe initial drops and smaller recovery rates. If the standard scenario amount wins, it will win because it is a seriatim calculation that does not permit aggregation across contracts.

The standard scenario amount builds upon existing CARVM practices. As a starting point, the standard scenario amount requires the calculation of a Basic Adjusted Reserve. The Basic Adjusted Reserve is defined as CARVM reserves ignoring free partial withdrawals but including all contract charges. Even though our chart shows that VACARVM will be the only requirement for statutory reserves after adoption, there are still elements of CARVM that will be carried forward.

An additional component of the standard scenario amount is the greatest present value of the negative accumulated net revenue. The net revenue is calculated by determining

Your Requirements for Valuation of Variable Annuities

	STAT RESERVES	TAX RESERVES
Present: Until Adoption	AG33, AG34, AG39	AG33, AG34, AG39
Future: After Adoption	VACARVM – Retroactive to 1/1/1981	Policies Issued Before 1/1/2010: AG33, AG34, AG39 Policies Issued On or After 1/1/2010: VACARVM



VACARVM – Poly is Moving Forward, Are You? ...continued

the difference between what a contract pays (margins) and what a contract collects (benefits in excess of the account value).

The margins have been carefully defined to recognize some of the charges collected for the contract's riders. The margins were originally designed to be lower during the surrender charge period and higher after a contract is out of the surrender charge period. It is believed that some of the margins during the surrender charge period should be used to cover amortization of the surrender charge.

For single premium products, varying margins by whether a contract is in or out of the surrender charge period works. For flexible premium products, a recent premium would extend the surrender charge period. Thus, for flexible premium products, margins during the surrender charge period would be "artificially" low. To combat this perceived problem, the surrender charge amortization period was introduced to determine when a contract qualifies for higher margins in the net revenue calculation.

The surrender charge amortization period calculation relies on two pieces of information from the Basic Adjusted Reserve calculation (i.e., the CARVM calculation without free partials but with all contract charges). The first piece is the Basic Adjusted Reserve (BAR) duration. For an extra inning baseball game, the "BAR" duration might be 3 or 4 hours. For the standard scenario calculation, it is the duration in months from the valuation date until the greatest present value occurs.

The second piece is the calculation of the surrender charge not amortized at the BAR duration. This is the difference between projected account value and the projected cash value at the BAR duration.

The surrender charge amortization period is then calculated as the BAR duration plus the surrender charge not amortized divided by the account value at the valuation date times 100. This number is rounded to the nearest projection period frequency (i.e., monthly). Fortunately, PolySystems calculates this number for you.

PolySystems' Response

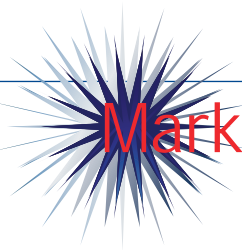
PolySystems has added the surrender charge amortization period calculation to AnnuityMaster. Additionally, our software has been updated to use the surrender charge amortization period in our standard scenario calculations. These new additions include the revised drops and recovery rates.

The Next Steps

PolySystems will continue to monitor all developments and update the Annuity Suite and related utilities as needed. We will release updated software so you can test what VACARVM means for you.

Regardless of what the future holds concerning VACARVM, you will still have to make all of your stochastic calculations. If you do not have an integrated platform for doing stochastic calculations, please consider our projection systems. For those of you that calculate GAAP reserves using PolySystems—your AnnuityDelphi system can be used for these purposes. Performing all of your runs within your existing valuation framework eliminates extra steps.

If you are interested in a personalized review of PolySystems Annuity software, please contact Bob Keating at 312.332.8740 or bkeating@polysystems.com. ☎



Marketing Corner

—Michelle D. Smith, Director of Marketing Services

Look for PolySystems at these upcoming functions:

Valuation Act. Symposium

September 24–26, 2008
Renaissance Washington Hotel
Washington, D.C.

Hospitality Suite, #1440
Sept. 24th ~ 6:30–9:30 p.m.
Sept. 25th ~ 7:30–10:30 p.m.

SOA Annual Meeting

October 19–22, 2008
Orlando World Center Marriott
Orlando, FL

Hospitality Suite
Oct. 19th ~ 7:00–9:30 p.m.
Oct. 20th ~ 8:00–10:30 p.m.

Exhibit Hall
Booth #416–418

User's Meeting

October 19, 2008
Lunch ~ 1:00–2:00 p.m.
Meeting ~ 2:00–3:30 p.m.

RSVP as space is limited.
Contact Michelle Smith:
P: 312.578.3092 *or*
E: msmith@polysystems.com.

We look forward to seeing you at one or more meetings! ☎