

Life Risk Based Capital Working Group Conference Call

Dennis Lauzon of NY led the call. Various regulators and interested parties were present. The four agenda items were:

- 1- Review of Allen Elstein's (CT) comment letter regarding the appropriateness of assuming 65% of the MGDB mortality for formulaic RBC and reserves,
- 2- A survey of views from the regulators regarding mortality assumptions,
- 3- Review of return assumptions, and
- 4- Uses of a specified scenario.

Item 1 – Propriety 65% of MGDB mortality assumption.

Allen Elstein did some independent analysis comparing the MGDB to the 2001 CSO and drew three conclusions:

- 1- 65% of MGDB seemed to be a stretch and concluded that 80-85% may be more appropriate. He encouraged someone to step forward and do some more analysis.
- 2- He suggested that loaded tables should be used because annuity mortality may be underreported.
- 3- He saw no reason why any mortality should be allowed to be different based on a company's size. He argued that data for deferred annuity mortality is not reliable.

Item 2 – Survey of views from the regulators regarding mortality assumptions.

The results of the survey will serve as a recommendation to the Life RBC Working Group.

NY suggested that formulaic reserves should use 100% of the 94 MGDB mortality table and that modeled results could use 85% of the 94 MGDB table. Several other states agreed. Most argued that 65% was too low and that a comprehensive study of deferred annuity mortality needs to be done. Most feel that deferred annuity mortality is underreported because benefits that are out of the money may be treated as a lapse.

Some interested parties disagreed and claimed that credible studies exist. These studies develop exposure by only using policies that have death benefits that are in the money. This eliminates the problem of underreporting. The states welcomed review of such studies. If such studies warrant the use of lower mortality, most seemed likely to accept a lower minimum.

Item 3 – Review of return assumptions.

The monthly returns of the S&P500 for the past 50 years have been used to develop parameters for a two regime-switching model. This model has been used to develop calibration points. The calibration points are used to test whether or not a company's scenarios develop enough exposure (i.e. they develop fat tails). The calibration points are used such that a company's equity model must produce a minimum number of scenarios above and below cumulative values at various durations.



NY raised two concerns:

- 1- The method to develop the calibration points is strictly statistical and
 - 2- The average return for the model is approximately 12.5% (seems high).
- Some argued that a return of 10.5% seems more reasonable.

Item 4 – Uses of a specified scenario.

NY proposed using a specified scenario. It is not clear how this single scenario would be used. The specified scenario could be run against the model or the entire portfolio. These results could be used to:

- 1- Establish minimum reserve requirements,
- 2- Compare the modeled reserves to seriatim reserves,
- 3- Compare results among companies,
- 4- Develop standard results over time, and
- 5- Move 9/30/xx results to the end of the year.

An interested party expressed concern over the use of a specified scenario to establish a minimum reserve. If the reserve level were too high, any modeled reserves would be mute.

Next steps.

A third conference call is scheduled for November 20th to discuss the return assumptions and the relative merits of a single scenario.

Tim Gaynor, FSA, MAAA

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