

LHATF Possible Changes to Standard Valuation Law (SVL)

Background

The Life Health and Actuarial Task Force is charged with reviewing a list of potential changes to the Standard Valuation Law. Currently there are 9 items on the list for review (see Appendix for listing of all 9 items). The purpose of the call was to look at the third item on the list, "Review the theoretical basis on which deficiency reserves are computed."

Description of Issue

The question arises as to whether deficiency reserves, as a separate formulaic calculation, are still necessary in light of the fact that asset adequacy analysis is now required. Asset adequacy analysis is now well established and will test whether reserves in the aggregate are sufficient. Should the separate calculation of deficiency reserves be eliminated and should actuarial judgment and analysis be relied upon? Or, should the use of what was at the time a patchwork be continued to address the specific situation where the net premium was larger than the gross premium? Also, with the advent of the 2001 CSO table will this situation occur less frequently anyway?

Discussions

The meeting was attended by a number of regulators, including TX, NY, CA, FL and IL, to name a few. Frank Dino (FL) mentioned that there is currently an American Academy of Actuaries Working Group looking at this very issue. The Academy representative gave a brief summary of the scope of this project and its time frames. He mentioned that no conclusions had been drawn at this point. The Academy Work Group is currently in the middle of their analysis and plan to provide a written report to the LHATF Task Force by March 2004.

According to the Academy, arguments in favor of eliminating deficiency reserves rely on the use of asset adequacy testing. Also, the changes in XXX to use X factors based on company experience is consistent with the use of best estimate mortality assumptions when doing asset adequacy analysis. Arguments against the replacement of deficiency reserves, according to the Academy, are the fact that X factors warrant a higher standard of validation than is currently required by the mortality assumption used in asset adequacy analysis.

The Academy is planning on doing a survey of 75 companies on their deficiency reserves practices, which will be included as part of their report.

The discussion was then open to the regulators in attendance. One state suggested, "leaving things alone." Since you will still have base reserves calculated by formula, what do you gain by eliminating the deficiency reserve formula?



Another state suggested abandoning deficiency reserves in lieu of using a gross premium valuation as a floor for minimum reserves. This has the advantage of reflecting lapses and expenses, which the current formulaic approach ignores (for base and deficiency reserves). This sentiment was echoed by at least one other state. One state expressed concerns over relying on cash flow testing, since there are perceived deficiencies with that form of analysis. In particular, it doesn't include new business, it is more a long-term analysis, and it is done for blocks of business in the aggregate.

The conclusion of the call was that the Task Force would wait for the AAA report before making a final decision on this issue.

Thomas Nace, FSA, MAAA

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Appendix

Possible Changes to the Standard Valuation Law

1. Should the SVL be altered to allow companies to file a "state of domicile" opinion in all states?
2. Is there a need for the certificate of valuation issued by insurance departments; is there a need to expand it to include A&H; is there a need to expand it to include a certification of the asset adequacy analysis?
3. Review the theoretical basis on which deficiency reserves are computed.
4. Should life CRVM be changed to CARVM given the many benefit streams in life insurance now; if so, will that require a more precise definition of "voluntary" and "involuntary" benefits?
5. Revisit annuities exempt from CARVM.
6. Should the standard for UL reserves be put in statute?
7. Should A&H reserves be established in statute, or at least a minimum gross premium valuation basis?
8. Should Section 3A be expanded to include a "good and sufficient" provision?
9. Should we eliminate old tables and have all in force business valued on current tables?

