

**LHATF Conference Call regarding the Proposed Actuarial Guideline on CARVM for Variable Annuities**

On February 18, 2004, LHATF held a conference call regarding the proposed Actuarial Guideline VACARVM, CARVM for Variable Annuities Redefined. Insurance regulators from various states plus the District of Columbia participated in the conference call. Other participants were insurance companies, ACLI, actuarial consulting firms, accounting firms and other interested parties.

Ms. Leslie Jones of the South Carolina Department of Insurance was the leader of the conference call. Before the conference call, regulators and all other interested parties were provided with the following documents:

1. A memorandum from Mr. Ross Myers, Senior Counsel of National Association of Insurance Commissioners, regarding the promulgation of the new variable annuity reserve method. (MYER0115.DOC)
2. A draft copy of Actuarial Guideline VACARVM. (AGVARCR.DOC)
3. Two documents from the Variable Annuity Reserve Working Group (VARWG) of the American Academy of Actuaries regarding the new reserve method. (AAA-VARDF.DOC and AAA-0218.DOC)
4. A copy of a e-mail from Mr. Rod Bubke of FBL regarding questions on (a) the appropriateness of allocating a cohort reserve to individual policies, (b) the appropriateness of using expenses in the reserve calculation, and (c) the proper procedure to perform asset adequacy analysis for variable annuities if the new method is used to determine their statutory reserves. (BUBK1223.DOC)

Key Issues and comments were:

1. Can a newly enacted law have retrospective effect, requiring increased reserve levels for existing annuity contracts?

According to Mr. Myers, a newly enacted law has retrospective effect for existing annuity contracts. The key reason is that reserve level is set by statute and the statute may change at any time. There have been steady changes in insurance regulations in recent years and the insurance industry should expect future changes in insurance regulations.

2. Can a new interpretation (for example, an actuarial guideline) be applied retrospectively to all insurance contracts?

A new interpretation can be applied retrospectively to all insurance contracts if the new interpretation is authorized by regulation and statute.



3. From a legal perspective, what is the best way to recognize the proposed reserve method for variable annuities? Should it be recognized as a new statute, a new insurance regulation, or an actuarial guideline?

From a legal perspective, the new reserve method should ideally be recognized as a new statute so that it is enforceable and has retrospective effect.

The second preference is to use the current statute, Standard Valuation Law (SVL), to promulgate the new reserve method as a new insurance regulation. However, the provisions of the new reserve method have no force or effect if the provisions go beyond or vary from the parameters set by the legislature in the statute authorizing the regulation. If the new reserve method is perceived as setting out a completely different reserve method for variable annuities, the new regulation may become unenforceable if the specific authorities for such method cannot be reasonably construed to exist in the SVL.

The third choice is to recognize the method as an actuarial guideline. Because an actuarial guideline is not recognized as either a statute or a regulation in most states, it has no legal effect unless a state has promulgated it by regulation and become a part of the regulation by reference. Thus, an actuarial guideline may be subject to challenge.

4. Can the new method be adopted by the Accounting Practices and Procedure Manual (APPM) and accredited as a law? Is it appropriate to incorporate the new reserve method in APPM?

California indicates that APPM only applies to insurance contracts issued on and after 2001. Although it is possible for APPM to adopt the actuarial guideline VACARVM and be subsequently recognized as law, it may be problematic to retrospectively apply this new reserve method to all contracts issued prior to 2001. In addition, it should ensure that new method is not in conflict with SVL.

Mr. Ross Myers will perform additional research in the issue of (a) whether AAPM can or should adopt the new method and (b) the applicability to insurance contracts issued prior to 2001.

5. Is the proposed method consistent or in conflict with the principles of the Standard Valuation Law?

First, we must identify the principles of SVL before we can determine whether the new method is consistent or in conflict with the principles of SVL. Generally, if there are conflicts, SVL prevails. The new method involves a lot of new elements such as lapses and expenses in the calculation. As it is quite different from the



current calculation methods for variable annuities and other insurance contracts, it is important to know the legal interpretations of the words “consistent” and “principles.”

Mr. Ross Myers will perform research for this issue.

6. What are the consequences if there are conflicts between the proposed reserve method and the State Law?

California and Texas indicate that if there are conflicts between the new method and State Law, the State Law prevails.

7. If the new reserve method leads to a significant change in reserves, should there be a transition period?

A transition period is preferred if the reserve change is significant.

Regulators agreed that actual data is needed to determine the significance of reserve changes between the current method and new method for variable annuities. Regulators may then use the actual data as a guide to determine the proper course of action. New York expressed its preference to incorporate a minimum formulaic reserve floor.

Tom Campbell of Hartford Life briefly went over the documents for the actuarial guideline. Time ran out and all parties agreed that more discussions are needed.

Vincent Tsang, FSA, MAAA

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