

Friday, November 30, 2007 - Sunday, December 2, 2007: Life & Health Actuarial Task Force

Outlined against a grey November sky rode the Four Horsemen of the Apocalypse - Famine, Pestilence, Destruction and Death. Not quite, but Friday morning in Houston was in fact quite foggy outside.

LHATF spent all day Friday, all day Saturday and most of Sunday afternoon reviewing the documents related to Principles-Based Reserves. Much of this work involved a lot of fine-tuning such as tightening definitions, moving sections around in the documents, defining how changes get approved by regulators, deciding whether certain items should be in the Standard Valuation Law (SVL), the Valuation Manual (VM) or both, etc. - necessary surely for the success of the project, but not necessarily affecting the hands-on practical aspects of what companies will have to do or how they will have to do it.

Thus, most of this report is a summary of the major PBR discussions and actions over the course of the three days that will have the greatest practical impact on actuaries actually performing or supervising the work. At the end I will cover some other LHATF matters and the meeting on capital (RBC).

Discount rates

NY repeated its request to use risk-free rates plus some as yet undetermined margin in the calculation of present values. The Academy has recommended using company earned rates less default provisions. There was no resolution as it is not yet certain how far apart these positions are.

Independent actuarial review

In a surprising action to most observers, LHATF voted to remove the requirement of having an independent review. Although not unanimous, there was little resistance. The ACLI had lobbied for increased reliance upon the reviewing actuary, while states did not want to cede that power. LHATF members observed that a state Commissioner still retains the right to review any company as extensively as desired.

Minimum seriatim reserve

For some products, such as community-rated health plans and group term life, seriatim reserves are inappropriate. LHATF will address this later in the VM.

Calculation of reserves prior to the valuation date

The current draft allows companies to use data up to 6 months prior to the valuation date. In a major change strongly opposed by industry, LHATF reduced the period to 3 months. So if you will be doing your company's PBR, your summer just became idyllic, while your autumn just got relocated to Dante's inferno.



Aggregation

This refers to cash flows within a line of business, not extending to all lines. NY is leery of letting products with good results offset products with poor results. UT defended the practice and felt that it should be encouraged. Industry cited the deterministic seriatim cash value floor as a damper on the effects of aggregation. This issue remains open.

CTE level

NY raised the possibility of varying CTE levels by product. Industry effectively rebutted it, getting Chairman Bruning (KS) to agree, but he also cited the potential need for more scenarios if CTE does not vary. Note that the CTE level has not been established, but most discussions about it revolve around CTE 65.

Stochastic modeling exclusion

Industry has proposed a test (once known as the “material tail risk test” but now called the “test for dependence on the economic scenarios”) similar in nature to the “New York seven” but involving a dozen scenarios. The NAIC would generate the scenarios each year to apply to all companies trying to get the exclusion. LHATF thought it was too permissive, but no resolution occurred.

Products using a Clearly Defined Hedging Strategy are eligible for the exclusion under certain conditions. LHATF removed most of the exemptions, making it tougher to qualify.

Margins vis-à-vis sensitivity testing

Some regulators proposed requiring higher margins for assumptions subject to higher sensitivity. Industry argued that uncertainty, not sensitivity, is the driving force behind margins. All parties agreed that this topic needs more guidance, and compromised that higher sensitivity requires greater analysis and justification of margins.

Catastrophic events

LHATF decided to require companies to consider catastrophic events when determining margins. Industry rejoined that that belongs in capital and surplus, to no avail.

Reinsurance

A long discussion about various aspects of reinsurance ensued, and will continue in the future. These were the main issues:

- The use of consistent assumptions between ceding companies and assuming companies,
- The determination of gross reserves, since PBR calculations are done net of reinsurance ceded,
- Retention of current risk transfer rules, and
- NY wondered if permitting companies to reinsure everything but the extreme tail risk would encourage cheap reinsurance to get substantial reserve credit.



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Process

LHATF entertained the possibility of a 3-5 year transition period. NY still wants companies to report on both the old and new bases. The next draft of the VM will reflect life insurance only, with non-variable annuities expected to be finished a year later.

LHATF will schedule a series of conference calls to continue the PBR discussions, possibly starting as early as this month.

Other Matters

The A&H Working Group met and continued prior discussions on revisions to the Health actuarial opinion, a Health actuarial memorandum and premium-based reserves; the AHWG also initiated its review of the Health aspects of PBR.

Chairman Bruning expects LHATF's revision to AG 39 to be adopted by the NAIC at this meeting. It changes the sunset date to January 1, 2009 and introduces a reserve release mechanism.

LHATF will schedule conference calls for group term life waiver reserves and pre-need life insurance reserves.

AG VACARVM will have a high priority in 2008 once the survey results are compiled.

The next webcast for PBR will be December 18, with a number of LHATF members scheduled to present.

Monday morning, December 3, 2007: Capital Adequacy Task Force

Items of interest to Life and A&H actuaries:

- The Life RBC Working Group had no calls since the last meeting, but plans to have some in the 1st quarter of 2008; C-3 Phase 3 was supposed to be ready for 12/31/2008, but at the last meeting the ACLI asked for a postponement and that is looking like a good possibility now,
- The Health RBC Working Group carved out vision coverage as a separate line and reduced the applicable RBC charges,
- CADTF referred comments on a draft Governance proposal (related to PBR) to the PBR Working Group,
- CADTF is quite interested in the RBC aspects of the VACARVM survey of LHATF,
- CADTF formed a subgroup to study two types of coinsurance: (a) with funds withheld and (b) with trusteed funds; only the former type gets credit in RBC, but industry contends that they are essentially equivalent and thus the latter should get the same



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- credit, and
- PA (not a member of the TF but has applied to be) desires to initiate a trend test for A&H and tighten the life trend test.

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