

**Friday, September 28, 2007: Life & Health Actuarial Task Force**

LHATF devoted almost the entire day to Principles-Based Reserves (PBR).

Overview from the AAA PBA/SVL-2 Steering Committee. Donna Claire reported that the timetable continues to be NAIC passage of PBR in 2007/08, adoption by states in 2009 and effective date of 1/1/2010. To that end, various AAA subgroups are working full speed ahead to address consistency, modeling efficiency, auditability, accountability within an organization and economic scenario calibration criteria. Models and scenario-picking tools will soon be available at [www.actuary.org](http://www.actuary.org).

Report from the AAA Life Reserves Work Group. This group proposed these substantive changes:

- Use CTE 65,
- Clarify the treatment of policy loans and IMR,
- Require starting assets be within 98%-102% of the final reserve, and
- Add more rigorous requirements for reinsurance (see Reinsurance WG report later).

The WG must solve these major issues:

- Complete the definition of the Material Tail Risk test,
- Consider simplified approaches for modeling non-guaranteed elements and for calculating deterministic reserves,
- Address simplified methods to establish mortality assumptions, and
- Incorporate suggestions from ACLI/Treasury discussions.

NY also has its concerns:

- Effects of aggregation,
- Choice of discount rates,
- Selection of scenarios,
- Reflection of ALM risk in deterministic reserves, and
- Pre-tax vs. post-tax approaches.

Report from the AAA Annuity Reserves Work Group. This group, charged with non-variable annuities, reported that:

- The stochastic requirements are nearly complete,
- The deterministic reserve requirements have not yet been defined, and
- Market values of assets are only needed to the extent of liquidation to cover cash outflows.



The Analysis subgroup continues to wrestle with single scenario differences from five commercial modeling systems.

Report from the AAA Valuation Manual Work Group. The Valuation Manual (VM) now has some meat on its bones, but this WG enumerated outstanding “general” issues:

- Coordination with the SAPWG and APPM,
- Reserves for business not subject to PBR, and
- Inclusion of guidance in applying PBR requirements;

and “key” scope issues related to:

- Experience reporting requirements, and
- PBR requirements on the operative date of the VM.

Report from the AAA Valuation Manual Subgroup 3 Survey. This subgroup surveyed LHATF members regarding the scope of experience reporting requirements and received the following feedback:

- A bias for including all policies, issued both before and after the VM operative date,
- A preference for excluding only those products specifically exempted from PBR,
- Support for reduced requirements for small companies, with some qualifications, and
- A variety of comments on the VM draft itself.

Report from the AAA Valuation Manual Subgroup 4 Survey. This subgroup surveyed LHATF members regarding which products should be subject to PBR on the operative date of the VM. There is some support for a phase-in by product, although regulators want products such as variable life, UL with long-term secondary guarantees and term with X-factors less than 100% included in the first phase.

Report from AAA on Credit Insurance and Other Non-PBR. The over-arching question yet to be answered is whether and how the VM should refer to requirements for products not subject to PBR.

Report from AAA on PBR Reporting and Independent Review. This report from VM Subgroup 1 solicited feedback from LHATF on these key issues:

- The role of the domiciliary Commissioner,
- The authority of any Commissioner to waive certain requirements,
- Disclosure of material disagreements between company and independent reviewer,



and

- The reliance of the appointed actuary on other opinions.

LHATF members responded:

- CA and NY definitely want notice of who the reviewing actuary is,
- Some states like the idea of a centralized office for some functions,
- CA wants notice of disagreements that have been resolved, because it might be an indicator of “liberalism” on the part of the reviewing actuary,
- KS wants the differences quantified, not with an estimate, but with the actual rerunning of the scenarios, and
- Some states believe that there should be no reliance.

This subgroup also prepared a sample PBR actuarial report (for life insurance only) that provides an excellent guide for actuaries on whom this burden will fall.

PBR Discussion. This was a freewheeling discussion of what needs to go to state legislators, how complete it needs to be and the timeframe necessary to get PBR approved. The consensus is that LHATF must approve the revised Standard Valuation Law by March of 2008, but the VM could follow later in 2008.

Recognizing the urgency of this timetable, Larry Bruning (KS, Chair of LHATF) indicated that he will appoint subgroups to review sections of the SVL and VM, and that the December LHATF meeting will be a 3-day affair in which those documents will be critiqued “paragraph by paragraph”.

Mortality Tables. This session was a mini-version of the August 31 conference call, in which the SOA/AAA group outlined the development and use of the Underwriting Criteria Score (UCS) for determining appropriate valuation mortality tables. In short order, we should expect:

- Valuation basic tables and report in October,
- Addition of margins to basic tables, and
- Expansion of the UCS to a “debit/credit” approach.

Report from the AAA Variable Annuity Work Group. Based upon feedback from LHATF and others, this WG proposed a number of changes to the draft of VACARVM, the main ones being:

- Four alternatives for revenue sharing,
- Deletion of the 50 basis point reduction in the discount rate, and
- Required sensitivity tests on contractholder behavior.



## **NAIC LHATF and CADTF Meetings Washington, DC, September 28-30, 2007**

LHATF voted to revise and expose the guideline, all except NY in favor. NY indicated that it will likely propose a strengthened Standard Scenario.

There was also some discussion on AG 39, mainly reflecting industry's growing dissatisfaction with the extension of the sunset date, the lack of release of reserves and the seeming permanence of that "temporary" measure.

At this point, with frustration in the room mounting, NE with some sharp words proposed dumping AG 39 completely, drawing a tepid sitting ovation from some interested parties. That proposal died.

AG VACARVM Subgroup Report. LHATF sent surveys to 26 companies and received 14 responses. KS will compile the results for discussion on a conference call.

The ACLI introduced a proposal to modify AG 39 to provide for a reserve release mechanism (2.5% per quarter). LHATF voted to expose the proposal, with NE the only holdout.

Pre-Need Mortality Regulation. There is a split in the pre-need segment of the industry over the proposal to require 1980 CSO instead of 2001 CSO. One company could not support the proposal because its mortality is much better than 1980 CSO. The ACLI questioned whether the proposal solves the tax basis mortality, which is the real crux of the matter. LHATF will continue discussion at its next meeting.

### **Saturday morning, September 29, 2007: Accident & Health Working Group**

Did not attend; see the summary report of this Working Group on Saturday afternoon.

### **Saturday morning, September 29, 2007: Life & Health Actuarial Task Force**

CTE Metric. Larry Bruning (KS, LHATF Chair) put together some studies that illustrated that CTE might be inappropriate in some cases if the number of scenarios is less than 1,000. He indicated that the AAA is working on a variance reduction technique that might provide a solution. One interested party urged LHATF to keep in mind that the number of scenarios required for PBR should not be so large as to be impractical.

### **Saturday afternoon, September 29, 2007: Life & Health Actuarial Task Force**

Report of the A&H Working Group. Saturday morning this WG:



- Recommended changes to the Federal Social Security Act. This affects the refund formula for Medicare Supplement policies,
- Produced new LTC experience forms to replace the existing ones,
- Approved a white paper on Individual Medical regulations to address high rate increases,
- Revised the A&H Policy Exhibit,
- Continued to review issues related to the Actuarial Opinion on Health reserves, and
- Adopted charges for 2008, which include PBR for LTC, a new Cancer claim cost table, LTC rating issues, the Actuarial Opinion for Health and the Med Supp refund formula.

Risk Assessment Subgroup Report. This LHATF subgroup sent a report to the NAIC Risk Assessment Implementation Subgroup that provided guidance on actuarial aspects of state examinations. This project is complete.

Statistical Agent Subgroup Report. This LHATF subgroup is defining a process for the selection and oversight of statistical agents and the scope of data collection. This is especially relevant to the experience reporting requirements of PBR. A major concern is costs, both to states and companies.

SVL-2 Subgroup Report. LHATF voted to expose the draft with minor changes. The ACLI has comments that will be deferred to a conference call. NY indicated that it has issues related to:

- Discount rates,
- Authority of the Commissioner,
- Penalty reserves,
- Seriatim cash value floor on the deterministic reserve,
- Market values for assets and liabilities, and
- Reporting PBR and formulaic reserves on policies subject to PBR.

Group Term Life Waiver of Premium Model Rule. LHATF will schedule a conference call to discuss this project.

Report from the AAA Reinsurance Work Group. This was somewhat strange, in that Sheldon Summers (CA), as the Chair of the WG, presented the report, and then Sheldon Summers, as a regulator, had some questions for the WG.

The gist of the report is that the Life & Health Reinsurance Agreements Model Regulation, one that among other things requires appropriate risk transfer, is no longer needed under PBR because the modeling takes care of all cash flows, whether or not risk is transferred.



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Sheldon then indicated that he had a number of questions and NY also chimed in. Most of the questions were not covered because of lack of time, so this discussion will continue at the next meeting.

Having covered all the projects related to PBR, LHATF then voted unanimously to expose the entire VM for comments. LHATF members then gave NY a rousing standing ovation for voting Yes and not being the lone holdout. Mirabile dictu!

Nonforfeiture Improvement. This AAA subgroup will issue a broad report on regulatory issues and marketplace dynamics that argue for a new standard nonforfeiture law.

2008 Charges. LHATF recommended a number of projects, most of which continue from 2007. The “essential” ones (the others are merely “important”) are PBR and VACARVM.

Other Matters. LHATF asked the AAA to develop valuation mortality tables for pre-need, funeral and limited underwriting individual policies.

LHATF asked for 3 conference calls to discuss SVL-2 and the VM.

The Houston meeting is scheduled for Saturday (12/1) and Sunday (12/2), but LHATF will also meet on the preceding Friday to go over PBR/SVL-2/VM with a fine-tooth comb.

### **Sunday morning, September 30, 2007: Capital Adequacy Task Force**

This Task Force covers Life, P&C and Health RBC. These were the relevant discussions on Life:

#### C-3, Phase 3

- 1) The Life RBC Work Group timetable is to adopt by 2007 and implement for 2008.
- 2) That Group indicated that it is still possible to meet that deadline, but many things still have to be resolved.
- 3) The ACLI has commented that the implementation should be postponed beyond year-end 2008.

#### C-3, Phase 2

- 1) There were no conference calls in the last quarter.
- 2) Some formula changes have been discussed, but resolution has not yet occurred.



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