

The Actuarial Ethicist: DAC Expectations

By Frank Grossman

This short article sets out a hypothetical workplace dilemma. We invite SOA members to submit comments and suggested solutions which will be summarized and published in the following issue of The Stepping Stone. All member submissions will be received in confidence, and any identifying details removed prior to their inclusion in the discussion of the case.

Mary the FSA accepted an internal rotation to her insurance company's corporate area just in time for financial reporting year-end, and reports to Irwin the FSA and chief actuary. Once Mary's year-end assignments were wrapped up, Irwin gave her a couple of important off-cycle responsibilities. One was to first review the mortality and lapse rate assumptions—including dynamic lapse rates—within the valuation models, and revise them as required. And second, to prepare actuarial projections for Phillip the CFO which will be used to update the company's financial plan.

Mary prepared a written summary of recommended assumption changes, based on her thorough analysis of the relevant experience studies, and they were approved by Irwin. Mary then updated her models to reflect the assumption changes along with sundry model "fixes" which were identified during year-end. These model revisions caused the projected expected gross profits [EGPs] for one product line to change such that the deferred acquisition cost [DAC] asset had a negative unlocking of \$25 million (i.e. the DAC balance would be written down by this amount).

Mary subsequently received a telephone call from Phillip, during which he said that "a certain amount of DAC unlocking this year was committed to during last year's planning process"—namely \$15 million of *positive* unlocking (i.e. the DAC balance would be written *up* by this amount). Mary checked the final projections prepared by her predecessor during last year's planning process, which confirmed the positive \$15 million figure. Mary called Phillip back, and tried to explain why the EGPs changed. Phillip simply said, "That's not good enough."

What should Mary do?

Send your suggestions before November 15, 2010, to Craigmore54@aol.com. The discussion of Mary's dilemma will be published in the February 2010 issue of The Stepping Stone.