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Summary of the December 2003 NAIC Meeting

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The weather at the Winter NAIC Meeting could have been better but the number of interesting topics discussed at the meeting more than made up for the poor weather.

Long Term Care Model Regulation

The NAIC Accident and Health Working Group (A&H WG) met on Thursday, December 4. The first item of business was the adoption of revisions to the NAIC Long Term Care Reserves Model Regulation. The contentious items had been the minimum standards for the voluntary lapse rate and mortality assumptions. During a conference call held after the September NAIC meeting, regulatory consensus concerning the minimum standard assumptions emerged. The revised mortality standard for long term care contracts and certificates issued after the effective date is the 1994 Group Annuity Mortality Table. The new voluntary lapse rate assumption varies by individual vs. group and policy year. For policy year one, the minimum standard is the lesser of 80 percent of the gross premium pricing lapse rate and 6 percent. For policy years two through four, the minimum standard is the lesser of 80 percent of the pricing lapse rate and 4 percent. For later policy years, the minimum standard is the lesser of 100 percent and 2 percent. For group insurance, the minimum standard for policy years five and later is the lesser of 100 percent of the pricing assumption and 3 percent. The other significant item in the revised Model is the prohibition against the use of morbidity improvement beyond the valuation date.

This specific revision is applicable to business inforce as of the effective date as well as business issued afterwards.

However, an insurer may continue to use the original reserve basis subject to the acceptability by the commissioner. The revised model was adopted by the NAIC A&H WG and it was adopted by the NAIC Life and Health Actuarial Task Force ("LHATF").

Discussion of Other Long Term Care Issues

The A&H WG continued its discussion of long term care insurance issues based on a memo received from the NAIC Long Term Care Working Group. The memo identified several items to review and comment on. The ideas in the memo had been used by states as one way of dealing with questions with the implementation of the NAIC Long Term Care Model Act and Regulation in their respective states. The items include such ideas as: required pooling, required filing of annual rate certification, content of rate filings, the definition of nonforfeiture benefits and several other items. While consensus was not reached, the discussions were interesting and will undoubtedly continue.

Rate Filing Task Force

The American Academy of Actuaries Health Insurance Rate Filing Task Force gave a status report concerning the regulatory effort to deal with several health insurance pricing issues, including the "closed block" problem. The report included a real-time presentation of a spreadsheet based model being developed by the Academy that can be used to evaluate different approaches to the closed block problem. The model will be used by regulators and other decision makers to evaluate and choose between competing alternatives. Alternative solutions include: pre-funding, inter-block subsidies, rate compression and individual medical

pools. The goal of the Academy is to present final results to the NAIC at the NAIC spring national meeting.

Other A&H WG Actions

The A&H WG adopted a motion to endorse deletion of Model Laws #130 and #133. Model Laws #130 and #134 deal with the filing and approval of accident and health insurance contracts. This effort is part of an NAIC effort to delete model laws that have been superseded by other model laws or otherwise are no longer needed.

The A&H WG also discussed the current status of the initiative to revise the Health Blank and the Life/Health Blank to achieve greater consistency, and the initiative to achieve consistency in HMO and HMDI reserve requirements. The first initiative is now focusing on revising the Accident and Health Policy Experience Exhibit, but more work needs to be performed before any changes can be recommended for adoption. A draft of the instructions that captures the current thinking as to changes was distributed at the meeting. The second item involves reviewing possible inconsistencies in the requirements for the reporting of certain reserve or other actuarial information.

Lastly, the A&H WG adopted an amendment to the NAIC Medicare Supplement Model Regulation. The revision gives the NAIC the ability to change the loss ratio benchmark for purposes of premium refund calculations. No specific changes are being proposed at this time. In light of the passage of the Medicare Prescription Drug, Improvement and Modernization Act of 2003, other modifications to the model regulation are expected, but there was insufficient time prior at the winter NAIC meeting to develop recommendations for consideration.

Annuity Nonforfeiture Regulation

The NAIC LHATF met on Friday, December 5. The morning session focused on projects involving significant input from the Academy.

The Academy presented a revised draft of an Annuity Nonforfeiture Regulation. The draft regulation focuses on requirements concerning the initial

and redetermination minimum nonforfeiture method and rate. In addition, the draft regulation provides rules for the use of an additional 100 basis point offset applicable to the calculation of nonforfeiture values for equity indexed annuities. In a "show of hands," the LHATF expressed support for the Academy to continue work on the draft including the notion of "value triggered methods." This idea refers to the mechanism for changing minimum nonforfeiture interest rates based on a specified value change in the index



rather than changing on a specified date. For the NAIC spring national meeting, the Academy will provide a draft regulation reflecting the ongoing discussions.

The Academy also gave a brief report on the valuation issues raised by the NAIC Annuity Nonforfeiture Law. In an October 2003 Report from the Academy, the valuation issues were discussed, analyzed and possible solutions analyzed. A conference involving the Academy group and LHATF working on this topic will be scheduled to discuss the report.

Variable Annuity Reserves and RBC

One of the major items of discussion was the report of the Academy Variable Annuity Reserve Work Group. The report of the reserve work group was preceded by a status report from the Academy Life Capital Adequacy Subcommittee C-3 Phase II Group. Since the reserving project and risk based

capital project are closely tied together, a status report on several key ideas that are common to both projects was given. The Academy representative reported that the pre-packaged representative return scenarios were available on the Academy Web page and the highly sought after Alternate Method Factors would be ready in the near future.

After these comments, the Academy Variable Annuity Reserve Work Group representative presented a draft actuarial guideline. The draft guideline was exposed for comment. The issues discussed in the Academy report and at the meeting included the nature of the

focused on the Academy C-3 Phase II group's decision to calculate Alternate Method Factors using 65 percent of the 1994 GMDB Mortality Table and the recommendation concerning using "Prudent Best Estimates" as the basis for the mortality assumption when modeling. After much discussion, the regulators did not reject or modify the recommendation from the Academy. A motion was adopted to expose for comment the "AAA Proposed Actuarial Guideline VACARVM – CARVM for Variable Annuities Redefined."

Other Life and Annuity Topics

While discussions took place on other agenda items, no definitive action took place. The LHATF continues discussions of a General Nonforfeiture Law revision, but it is not clear whether any substantial progress will soon be made. A possible revision to the Standard Valuation Law is in the early stages, and possible revisions include elimination of deficiency reserve requirements. Return of premium term insurance was discussed primarily with regard to nonforfeiture requirements. A survey of regulators with the goal of identifying the reasons for approval or disapproval of term products with return of premium benefits will be conducted. A new credit life insurance mortality table (2001 CSO male composite ultimate) is being exposed for comment as part of a draft regulation.

Propose Change to LHATF's Charges

The most interesting discussion during the two-day meeting was the proposed revisions to the 2004 charges. Subsequent to the fall NAIC meeting, potential revisions to the charges were developed by one regulator. The proposal includes a charge to develop a new Standard Valuation Law that combines life, health and long term care insurance. The charge identified several items that LHATF should consider when developing the proposal including the valuation laws of Canada and other countries, a capital adequacy approach that links together reserves and risk



regulatory guidance (guideline vs. regulation), whether to include inforce business, the conditional tail expectation (CTE) level (tentatively, 65 percent), the need for a minimum reserve floor, flexibility to use prior period reserves to estimate current period reserves, the need for a phase-in, and methods for dampening volatility.

Regulators have been very much involved in the development of the actuarial guideline. One technical issue of significant interest to regulators that was discussed during the meeting was the mortality assumption underlying the Alternate Method Factors, and limitations on the actuary when using the modeling approach. The discussion

based capital, a safe harbor for small companies with simple products if the capital adequacy approach is too complicated, and minimum capital adequacy requirements for small or new companies. The proposed revision to the charges also included a charge concerning a new Standard Nonforfeiture Law. In responding to this charge, LHATF was asked to consider many ideas, including removal of constraints by minimums or formulas, consumer protection and disclosure. In addition to charges related to deliverables, the charges also included merging all life and health risk based capital work into LHATF. Lastly, the charges included a change in the group that LHATF directly reports to. If the proposed revision to the charges was adopted, LHATF would have a direct link to the Executive and Plenary Committees for specific projects involving proposals concerning solutions to the A&H closed block problem and long term care reserves in addition to its current linkage to the A and B Committees.

Needless to say, this proposed revisions created many interesting comments from regulators and interested persons. The vote on the revised charges was to take place at the Plenary Committee meeting on Sunday, December 7. It was announced at that meeting that the vote on the proposed revisions to the 2004 Charges was deferred for further study.

Actuarial Guideline 34

The recently revised Actuarial Guideline 34 (VA GMDB reserves), which allows for partial withdrawals to be ignored in CARVM calculations but requires a stand-alone asset adequacy analysis, was officially adopted by the NAIC at the plenary session during the December NAIC meeting.

Life Risk Based Capital Working Group

At the Life Risk Based Capital Working Group meeting, changes to the Instructions for the Life RBC formula concerning the C-3 Phase II project were adopted. This action does not mean that the modeling approach being devel-

oped by the Academy was adopted. What it does mean is that it is still possible for the NAIC to adopt the Academy recommendations for the 12/31/2004 Life RBC filing. Because of time deadlines, any changes to the Life RBC diskette have to be adopted at least one year in advance of implementation. The adopted instructions are sufficiently flexible to permit the Life RBC Working Group to adopt the Academy recommen-



dations by June 2004 and have the requirements in place by December 31, 2004.

Many of the issues discussed during the LHATF meeting concerning variable annuity reserves were again discussed in the context of Risk Based Capital. During the discussion of the mortality assumption underlying the GMDB Alternative Method factors, the Academy agreed to provide a set of factors based on 100 percent of the 1994 MGDB Mortality Table in addition to factors based on 65 percent of the table. Discussions on appropriate mortality will continue in March. □



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