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# Summary of June 2009 NAIC/LHATF Meeting

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The June 2009 NAIC meeting was held in Minneapolis (which has wonderful lemon ricotta pancakes at Hell's Kitchen). First and foremost—**The SVL2 changes passed the NAIC's Life and Health Actuarial Task Force!** (It has since also passed the PBR (EX) Task Force and the Solvency Committee of the NAIC.) Having said that, there is still work to be done, particularly on the Valuation Manual.

A summary of the issues discussed:

**LHATF**—Larry Bruning, chair of LHATF, started off the Life and Health Actuarial Task Force (LHATF) reviewing where we've been and where we are going with PBA. He pointed out that we are changing a system that has been in force for about 150 years. As he stated, "What a wonderful time to be an actuary. We are making progress toward the ultimate goal of modernizing the regulatory framework."

**SVL2**—Before passing SVL2, LHATF looked at a few amendments. One important item was that LHATF agreed that the SVL and Valuation Manual should be presented to legislatures as a package (but LHATF did not amend the law to specifically say this).

**Net Premium Approach**—John Bruins gave a brief presentation regarding a net premium approach to PBA reserving, which the ACLI states is needed for federal income tax deductibility of reserves. The ACLI is in the process of developing an approach and expects to have information to present to LHATF in the fall.

**Mortality**—Mary Bahna-Nolan and I gave an update on the SOA/AAA mortality topics. We presented the pros and cons of going to a 2008 CSO mortality table versus some change to the interim solutions versus waiting for something like the 2012 CSO. LHATF voted not to go forward with the 2008 CSO; the SOA/AAA POG will continue work on refining margins to be used for PBA. There was also a discussion on guaranteed issue and simplified issue—LHATF voted to have the SOA/AAA do work on developing a mortality table for this business. In the meantime, LHATF will work on sending out a note to states saying that the 1980 CSO is a reasonable mortality basis for simplified issue/guaranteed issue business. LHATF also voted to give the SOA/AAA an assignment regarding Individual Annuity mortality: (1) to determine whether a new table is needed; (2) to see if projection factors should be built in; and (3) to see if the table should be striated in some fashion, considering that there was obvious

mortality differences between small payout annuities and large payout annuities.

**Default Costs on Existing Fixed Income Investments**—Gary Falde and Alan Routhenstein gave an update on a possible method for LHATF to come up with default costs under PBR. A lot of work has been done, but work is still needed on this to get results that look reasonable to all parties.

**Economic Scenarios**—Nancy Bennett’s Academy group gave a presentation from the Academy’s Economic Scenarios Implementation Work Group. The Economic Scenario group has released a new generator, and a paper discussing this and calibration criteria. The goal of the group is to have the same calibration criteria so that companies can use the same generators (interest and equity) for both reserves and capital.

**PBA Training for Regulators**—The regulators discussed having a PBA training session for regulators. This would educate regulators on what PBA is, and what the regulatory examiners should concentrate on. Mike Boerner will head the effort to get this seminar set up.

**Valuation Manual**—Much of the LHATF meeting was spent reviewing the work of the LHATF subgroups working on various sections of the Valuation Manual:

a. **VM-00, 01, Process and Coordination**—Mike Boerner heads the LHATF team on this part of the Manual (as well as heading the Academy team on the Valuation Manual in general). Bob DiRico heads an Academy subgroup on Consistency that is assisting with making sure there is one place (VM-01) for definitions used by various sections of the Valuation Manual. There is some additional tweaking of wording expected. In addition, there is an Academy project, headed by Alice Fontaine, to develop a pros and cons document on various scope alternatives (e.g., should PBA apply immediately to all life products, only to term and UL with secondary guarantees, should

there be phase-ins?). This will be discussed on a conference call.

- b. **VM-20**—As mentioned above, presentations on this subject include those from Gary Falde and Alan Routhenstein on a potential methodology that LHATF could use to set default rates and effectively limit the asset rates assumed in modeling for reserves. John Bruins gave an ACLI presentation on a net premium approach for life reserves. Pete Weber heads the VM-20 effort for LHATF. Additional amendments were discussed at this meeting. The latest VM-20 was then exposed for comments.
- c. **VM-20, Reinsurance**—Sheldon Summers heads the LHATF subgroup on reinsurance, as well as heading the Academy group on the same subject. Several amendments were discussed at LHATF, particularly on how to handle reserves gross and net of reinsurance.
- d. **VM-21**—This section would bring in the Variable Annuity CARVM Actuarial Guideline, which goes into effect at year-end 2009. The guideline is obviously already written, so this would be a matter of making sure it is in the right format. Mike Boerner is in charge of making this happen.
- e. **VM-25, 26**—These are the health sections. Julia Phillips heads this group. At this time, there are no changes expected to the health reserving requirements. These sections codify the current plans, and are basically complete. There are a couple of comments received on this, which will be discussed on a conference call.
- f. **VM-30, 31**—Katie Campbell heads this effort on PBR Reporting and Review. New versions of VM-30 and VM-31 were exposed in the last quarter. A few amendments were discussed at this meeting.

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**g. VM-50, 51**—Fred Andersen is heading this effort on PBR Experience Reporting. Frank Horn reported for him and stated that New York is getting close to issuing an RFP for reporting mortality experience. Having this reporting was a condition of using the current interim preferred mortality tables on the 2001 CSO.

In summary, the Valuation Manual is close to being able to be passed on to the parent committees of LHATF. Perhaps the biggest outstanding item would be the changes needed if LHATF wishes to reflect a net premium approach to life reserving; this needs the ACLI to finalize their net premium methodology.

**Standard Nonforfeiture Law**—Work continues on modernizing the Standard Nonforfeiture Law. John MacBain is heading this effort, and expects a more detailed report in December.

**International Issues**—Kris DeFrain of the NAIC gave an update on the international arena regarding valuation issues. The point is to both study the international initiatives to see whether there are items the United States should adopt as well as sharing information to influence

international standards. Bottom line, although PBA and international standards may have some differences, both systems have a base which measures all relevant risks on assets and liabilities. One possible major difference is that, at this time, statutory U.S. accounting is mostly book value based, while the international area is generally on a market consistent basis.

#### Other Issues discussed at LHATF:

- 1. GLIBs**—Jim Lamson and Mike Ward gave an update on the work of the Academy's Annuity Reserve Work Group of answering how a new benefit—deferred annuities with guaranteed living income benefits that allow cash surrender before and during the payout phase—would be valued under Actuarial Guideline 33. The Academy group developed pros and cons of various interpretations of this benefit in terms of whether it should be interpreted as a Type A (higher) versus Type C (lower) valuation interest rate. LHATF determined that the correct answer was Interpretation 4 of the Academy's report. That is, bifurcate the benefit into two parts: the first part covers the benefits that exist during the time the cash values exist; the second part covers the payout benefits after the cash values no longer exist. The reserve for all the benefits in the first part would be discounted with Type C rates. The reserves for the payments in second part (which is an n-year deferred life annuity) are valued with Type A rates. Type A rates are used immediately (i.e., not just with the valuation dates after the cash values of the first part are gone). Note: This is a bandage approach, and is the type of issue PBA could handle better.
- 2. GRET**—The SOA is starting work on this year's Generally Recognized Expense Table that companies can use for life illustrations.

**Capital and Surplus Relief**—LHATF has been charged with fast-tracking the Capital and Surplus Relief items that were proposed last year due to the economic turmoil, but ultimately not enacted last winter because the industry did not prove that there was a



dire emergency. The three proposals LHATF is concentrating on are known as proposals 1a (the proposal to allow the 2001 Preferred tables to be used for all 2001 CSO business, even if issued prior to 1/1/2007); 1c (which clarified that the preferred smoker/non-smoker tables can be used in determining segments); and 2 (which allows X factors for deficiency reserves to go below 20 percent, and permits the X factors to decrease by duration). LHATF did a survey of how many companies expected to use the proposed relief. Of the 19 companies that responded to the survey: (a) for the proposals under 1, six companies said they would use the relief, 13 said they would not; (b) for proposal 2 it was nine no, 10 yes. Note that the total capital of the companies that responded had dropped from \$46 billion at year-end 2007 to approximately \$36 billion at year-end 2008. The year-end 2008 number reflects capital infusions. LHATF voted to adopt these proposals and passed them onto the next committee. They have since been passed by the A Committee.

**Accident and Health Working Group (a subgroup of LHATF):** There will be a long-term care survey sent to major writers regarding nonforfeiture and other issues. The Academy's Health group is working with the regulators on the Medicare Supplement Refund formula. The Medicare Supplement Compliance Manual has been adopted by the Accident and Health Working Group and is being passed on to the parent committee. There are changes to the Health Actuarial Opinion wording for 2009, so actuaries should pay attention to this—e.g., that the Board, not senior management, must appoint the actuary. Brad Spenny of the Academy PBR LTC work group mentioned that work is continuing on long-term care in a PBA environment. A new subgroup was formed under the A&H Working group separately looking at administrative expenses when insurers go for rate increases. Jack Luff of the SOA mentioned that the SOA is looking for companies to volunteer to participate in a cancer claim study to update the 1985 Cancer study.

**Life Risk-Based Capital Working Group:** Philip Barlow ran the RBC meeting from 5 p.m. to 6 p.m.

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on Friday June 13. The group discussed some comments received on the RBC C-3 Phase III report. This would apply a principle-based approach to life insurance capital, including in-force. Due to the number of comment letters received, a conference call was held to discuss the letters. Due to concerns about the companies being prepared to implement C-3 Phase III in a timely manner, the group decided to delay implementation to 2010. There will be an Academy seminar the day before the 2009 Valuation Actuary Symposium on capital issues, focusing in on the RBC C-3 Phase III implementation.

The ACLI change on the treatment of derivatives was exposed for comment and will be discussed on a conference call. Another issue discussed was the derivative risk mitigation proposal, which will be discussed in detail on a conference call. The ACLI discussed the mortgage experience adjustment factor, where work is continuing.

### Summary

In summary, PBA has made significant progress over the past couple of years. There is still work to be done, but the day is drawing nearer when PBA will be a reality. ■