SOCIETY OF ACTUARIES

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2001 CSO Adopted!—What Now?

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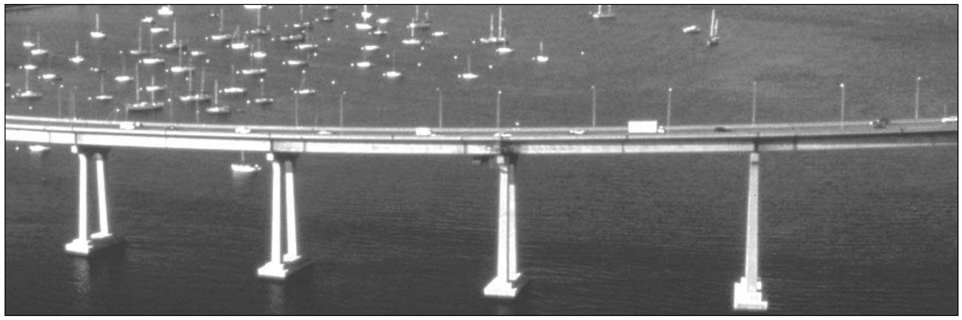

As many of you know, this past December in San Diego the NAIC adopted the new mortality table. Now things will get interesting as the states consider when they will adopt the table. Companies will have to keep track of when they will want to or have to use the new table for valuation, nonforfeiture, tax reserves and definition of life insurance (§ 7702).

This article is a reference to keep straight all the phase-in periods for the different uses of the new mortality table.

At Van Elsen Consulting we believe that 26 states will adopt the new mortality table in 2003 to be effective 1/1/2004. Another 12 states will adopt the table in 2004 to be effective 1/1/2005. The last 12 states will adopt the table in 2005 to be effective 1/1/2006.

Valuation

A little background is necessary here, since the use of the new table for valuation depends on whether the particular state has passed the new table and/or the new AOMR regulation. If the new AOMR regulation is passed with the "switch" turned on that allows companies to rely only on their domestic states' laws, then the new AOMR might help you use the new table in more states sooner, as long as the company's domestic state has passed the new table. Unfortunately there seems to be recent discussion about passing the AOMR without the switch turned on, meaning the regulation would provide no relief in dealing with state variations. Companies might want to consider talking to their state insurance departments about this issue.

Since we haven't had a new mortality table for 20 years, states will have to be thinking about what a good approach is.

Of course, to write a product using 2001 CSO, you ideally want to be able to value that business on this table in all states. Here is a summary:

- If you are domiciled in State X, which has passed 2001 CSO and the new AOMR, and
- You write business in State Y, which hasn't passed 2001 CSO but has passed the new AOMR and has turned on the switch within AOMR to allow a domestic state opinion,
- Then you might be able to sell a 2001 CSO product in State Y. The only reason this wouldn't work is if State Y wouldn't approve the filing of a 2001 CSO product. Your best chance to get a 2001 CSO product approved might be one without cash values, so that the issue of which table to use for nonforfeiture wouldn't come up. If you were past the nonforfeiture hurdle, then the last hurdle would be getting the actuarial memorandum approved. If your memorandum doesn't go into specifics about the mortality table used, this might not be a problem. This may be the 2003 situation if term product development efforts are active due to the new table.
- You might be able to get the filling approved on the following basis:
  - –2001 CSO will be used when required,
  - –otherwise 1980 CSO will be used.

Some states don't review actuarial memorandum real closely, and some states may think that this is a reasonable approach since the new table will be approved in the near future. Since we haven't had a new mortality table for 20 years, states will have to be thinking about what a good approach is.

- Even if all the above bullets are true, if State Z hasn't passed 2001 CSO or the new AOMR (with the switch turned on) you will have to reserve State Y's 2001 CSO product on 1980 CSO when you do financial reporting in State Z. This might make your financial reporting in State Z look so bad that you can't sell the 2001 CSO product yet.

One more detail: If your domiciliary state adopts the new table to be effective 1/1/2004 you can start using the new table for valuation anytime between 1/1/2004, and 1/1/2009 (a five-year phase-in).

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Nonforfeiture

This is much simpler to think about, although the result may be worse. You can't use the new table for nonforfeiture in a state until the table is adopted by that state.

So there is no way around this, either the state has not adopted it. Similar to valuation, you can start using the new table anytime between 1/1/2004 and 1/1/2009 (a five-year phase-in).

Tax Reserves and Definition of Life Insurance (§ 7702)

Once 26 states adopt the new table, the magic number will be reached, and the new table will start to be used for tax reserves and § 7702 testing. If this happens effective 1/1/2004, you can start using the new table for tax reserves anytime between 1/1/2004 and 1/1/2007 (a three-year phase-in.)

We look forward to working through this five year period of transition with the new table, as we are sure you are! ●

NAIC Members Adopt Revisions to Standard Nonforfeiture Law

Five-Year Constant Maturity Rate to Replace Fixed Rate

Members of the National Association of Insurance Commissioners (NAIC) adopted revisions to the Standard Nonforfeiture Law for Individual Deferred Annuities.

A key component of the modified law calls for the replacement of the fixed 3 percent minimum nonforfeiture interest rate with a rate based upon the five-year Constant Maturity Treasury Rate. However, the law states that in no event can the guaranteed minimum interest rate be required to exceed 3 percent, nor can it be less than 1 percent. "This revised law offers a permanent solution to economic inconsistencies," said Utah Insurance Commissioner Merwin Stewart, who is chair of the Life Insurance & Annuities Committee. "NAIC members can now move forward in presenting a viable solution on this issue to their legislatures during the current legislative session."

Industry officials expressed concern over the relevance of fixed rates to fluctuating market conditions. In February 2002, NAIC members voted to support the industry in their efforts to go to the legislatures and ask for a reduction in the nonforfeiture rate to 1.5 percent. In addition, NAIC members charged the Life & Health Actuarial Task Force with developing a more permanent solution.

The Life & Health Actuarial Task Force completed its work Friday, March 7, 2003, in making changes to the Standard Nonforfeiture Law for Individual Deferred Annuities.The Life Insurance & Annuities Committee then adopted the model law during a special session on Saturday, March 8, 2003.

The new language eliminates the need for state legislatures to reactively approve rate modifications on an annual basis. ●

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Disability Income

Is there any significance for the small-company in the disability income industry?

60% Yes
40% No

What are the leading general issues for disability income?

44% Trends and experience
22% Balance of Pricing, Sales and Underwriting
22% No Opinion
11% Miscellaneous

Medicare Supplement

Is there any significance for the small company in the Medicare supplement industry?

40% Yes
60% No

What are the leading general issues for Medicare supplement industry?

47% rates and costs
18% regulations and requirements
18% miscellaneous
12% no opinion
6% trends and experience

Hospital/Major Medical

Is there any significance for the small company in the in the Hospital/ Major Medical Industry?

20% Yes
80% No

What are the leading general issues for Hospital/Major Medical industry?

65% Rates and costs
12% Regulations and requirements
12% No opinion
6% Trends and experience
6% Miscellaneous

Critical Illness

Is there any significance for the small-company in the critical illness industry?

75% Yes
25% No

What are the leading general issues for Critical Illness?

35% Trends and experience
30% Lack of market and expertise, rates and costs
25% No opinion
5% Regulations and requirements
5% Miscellaneous