Article from

The Financial Reporter

December 2015
Issue 103

Update on Regulatory Developments

By Francis de Regnaucourt

This is a quarterly update on developments at the National Association of Insurance Commissioners (NAIC), the International Association of Insurance Supervisors (IAIS), the Federal Reserve and its affiliates, as well as other groups who may get involved in insurance supervision, with emphasis on those that may be important to members of the Financial Reporting Section. In general, this update does not report on Principle-Based Reserves, as they are usually covered elsewhere.

The Life Actuarial Task Force (LATF) met at the NAIC Summer Meeting in August. We report below on a few items that may be of interest to members of the Section. LATF initiated a review of Variable Annuity (VA) captives in conjunction with the VA Issues Working Group (VAIWG). Notably, the New York Department of Financial Services announced a plan to change its requirements for VACARVM for 2015.

On International Capital Standards (ICS), the NAIC sent its comments to IAIS on the Higher Loss Absorbency (HLA) proposal. The NAIC generally agrees with the proposal, but feels that the HLA "uplift" (increase over the capital requirement for non-G-SIIs) should be limited to 20 percent. There was relatively little activity over the summer.

Likewise, there were no major insurance-related developments from the Financial Stability Oversight Council (FSOC) over the summer.

LATF MEETING AT THE NAIC SUMMER MEETING, AUG. 13 AND 14, 2015 (AND SUBSEQUENT EVENTS)

We report here only the highlights of the meeting; complete details are in the minutes produced by the NAIC and available on their website. There was forward progress on many ongoing projects, but without notable landmarks; we do not report on those. We also touch on a few action items by LATF subsequent to the Summer Meeting.

New Valuation Mortality Table

Mary Bahna-Nolan (AAA Life Experience Subcommittee) presented proposed changes to the Valuation Manual to incorporate the proposed 2017 CSO table. LATF voted to adopt the 2017 CSO table and some proposed amendments. One point to note: 2008 CSO will remain the valuation table for products with limited underwriting.

In September 2015, LATF adopted changes to the valuation manual to incorporate: (a) the 2017 CSO table, and (b) two options for calculating credibility for purposes of mortality margins. These items were required for AG 48 calculations at year-end 2015. While the credibility options were adopted, there is some concern among regulators that companies could pick and choose the method.[1] This issue will be discussed again in 2016.

Principle-based Reserves (PBR) Stochastic Exclusion Test (SERT)

Rich Daillak (AAA Life Reserves and Life Reinsurance Work Groups) presented an issue related to YRT reinsurance. The SERT criterion is based on the ratio of (b - a) / c where:

a is the baseline reserve,

b is the worst case (highest reserve among 16 specified scenarios), and

c is the PV of net benefits in the baseline case.

He pointed out that YRT reinsurance can affect the ratio, especially if the c term is reduced significantly by the ceded portion. By the same token, aggregating a block of life business with YRT reinsurance assumed on another block could be used to exclude a block that would not otherwise have been excluded ("a lot of things can be labeled as YRT"). He suggested that looking at the outcomes (especially the percentage spread between a and b) with and without reinsurance is important to understand the results.

An Academy proposal for SERT amendments intended to address these issues was exposed for 45 days.

AG43/C3P2 Subgroup

This subgroup is working with VAIWG on a review VA captives. It wants to understand: (a) the motivation for VA captives, (b) how they are used, and (c) what options are available to address the perceived problems with VA reserving and capital requirements. Fred Andersen (MN) asked the subgroup to address his concern that during good times, when guaranteed living benefits are not in the money, reserves may not be high enough.

This initiative is part of an effort to make the treatment of captives more uniform than in the past. The insurance industry had come under some criticism for "regulator shopping" and even "shadow banking."[2] The chairman mentioned that Long-Term Care captives would be addressed later as well.

Bill Carmelo (NY) stated that the New York Department of Financial Services planned to require a change of minimum assumptions for VA CARVM along the lines of the Amendment Proposal Form they had submitted in 2012;[3] no specific timing was mentioned.

IUL Illustrations

While AG 49 was adopted earlier this year, there remain some issues to be worked out by the IUL Illustrations Subgroup:

- For policies with more than one index fund, if one fund has low charges and a low cap and another fund has higher charges and a higher cap, the illustration could be different than the sum of two separate illustrations if each fund were in a separate policy. Likewise, if the two funds have different expenses, the same disparity could occur.
- The treatment of bonuses is still unclear and needs to be defined further.

Other issues came up:

- Why not make AG 49 effective earlier?
- Are we spending too much time on IUL at the expense of broader illustration issues?

The consensus was to ask for input on enhancements to AG 49 and consider them all together.

Francis de Regnaucourt, FSA, CERA, FCIA, MAAA, is a director at KPMG. He can be reached at *fderegnaucourt@kpmg.com.*

ENDNOTES

1 The current adopted version stipulates that: (a) after selecting a methodology initially, a company may not change without commissioner approval, and (b) the same credibility method must be used for all the company's business.

2 Moving business (through reinsurance captives, in this context) to reduce or avoid regulation or disclosure.

3 Essentially a significantly more adverse Standard Scenario. This change would affect only NY-domiciled and NY-licensed entities.