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Session 44PD
Opportunities and Challenges in the Current Economic Environment

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Panelists: Donna R. Claire
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Summary: In an open-forum environment, the panel shares its perspectives concerning the most profoundly affected areas in the current economic environment and the modifications that will require actuarial skills. Discussions address the impact on the valuation environment, education and professional development, coping mechanisms, statutory and GAAP implications, and the changing role of the appointed actuary.

MR. DAVID A. RICCI: I am appointed actuary with Zurich Life. I'm the facilitator of this session, and I also will be making a small presentation after my distinguished partners, Donna Claire, president of Claire Thinking, Inc., and Doug Eckley, senior manager of Annuity Net. Donna's presentation will be directed at the regulatory environment, and Doug's will focus on the demographic environment. I will present a perspective from a corporate actuary's point of view.

MR. DOUGLAS A. ECKLEY: I have a high-level view of the current economic environment. Even with that, it is hard to decide what to cover. I wanted to focus on the insurance industry in some way. There are a few challenges that I decided to talk about that are important for the insurance industry.

"Demographics" is the topic that I will spend the most time on. Others are: rising health-care expenditure, investor scrutiny (which would be the increased investor scrutiny in this environment), and the cost of regulation (which always has been a burden for our industry).

If we have challenges, we must also have opportunities, right (at least, if you are an optimist)? So the flip side would be the increased importance of financial "intermediation."

On the rising cost of health care, the United States population is aging. I think that we should design health products that have an accumulation element. Then, with increased investor scrutiny, it is possible that our industry could come out looking pretty good. And we may gain an advantage in attracting capital that way.

Regarding the cost of regulation, I think a response is to develop a federal-regulation option. There is actually some movement toward that end within the ACLI.

Table 1 shows historic U.S. labor-force numbers and a couple of long-term projections. Obviously, you really do not know exactly what is going to happen, but these are reasonable guesses. From 2002 to 2020, there is very little growth. If you annualize that in a percentage, I think it is around 1%. Of course, we expect our economy to grow a lot faster than 1% per year over the next 18 years. If you consider projected statistics for 2040, we have, essentially, a flat labor-force growth. This excludes increased immigration, which, I think, can provide a solution to the situation. But the statistics illuminate a problem directly affecting insurance companies.

TABLE 1
Labor Force Growth (1980 Base Year)

1980	100
2002	150
2020	174
2040	180

The picture for the high-end labor force, most experts agree, looks even worse. University enrollment has been flat recently and is projected to stay flat. The 18-to-24 age range of population in our country, if we exclude immigration and minorities, has no growth at all. Therefore, most people agree that university enrollment is likely to decline, which then means that the high-end labor force may decline. Again, employers will face hiring problems.

The insurance industry needs both high-end and low-end employees, of course. So both aspects of this problem will affect insurance. What are some possible solutions? One thing that will happen naturally, I believe, is the retirement age will move beyond 65. There was a push, while we had the booming stock market, for people to try to retire a lot earlier. Most of that is not working out today. An older average retirement age may be part of a solution to hiring problems, but one thing to note is that men who are nearing age 65 are already fairly high up, percentage-wise, in the labor force—68%. Obviously, that 68 can go up, but that may not contribute all that much to a solution.

Women, of course, can work and are working; 77% of the female population is already in the labor force. So again, getting more women into the workforce may not be a complete solution. During the last labor crunch, some companies started hiring directly from the welfare rolls. I think that we will see that again. It is limited, though. It is not an ideal solution for obvious reasons. Speaking idealistically, it would be nice to make university education more affordable for low-income families, but I do not know how they would best do that.

Encouraging immigration, I believe, is a big part of the solution , but it is controversial.

In particular, Hispanic immigration is the phenomenon that can be of great assistance. Whenever I discuss this with my dad, for example, we have a big argument. He is older than I am. Some arguments, I think, are shortsighted, but I am going to try to be open-minded. If you say that they pay less in taxes than they consume in services, you are probably thinking of schooling and things like that, and that may be true now. Another argument is that if they do manual labor, we are exploiting them. Of course, Hispanics who immigrate to this country often do manual labor these days. You see them building the roofs in your neighborhood, etc. Is that exploitation? I do not think so, but you can make that argument. I think it is a shortsighted argument, and the long-term view might be dramatically different.

Asian immigration is also controversial. But it is becoming evident that the countries of India and China have a lot of brain power. You may say that that's just because they have a lot of people, and that may well be true, but if we can get the best brains, the best people, then we benefit. Some people will have to overcome prejudices.

What does all of this mean for the valuation actuary? I think that the people in this room, being visible people in the insurance industry, will be among the first to face labor-shortage problems. I believe that the economy has to go up, and I also believe that it will come up in a big way. We can contribute something to the coming debate about things like immigration. We are capable of long-term thinking and that is what is needed.

Turning to health care, it's interesting to note that since the 1980s, employees have gained nearly first-dollar coverage of health-care cost. It is a very nice thing to have, and we have won it. The employers have paid for it. The average employee spends roughly the same amount on health care now as he did then. Of course, there have been tremendous increases in health-care costs since then. The employer's share has skyrocketed.

Table 2 shows recent health-care-cost statistics. As actuaries, we can understand that some of this may be understated. Most health-care costs occur in the last few years of life, and as we have increasing life spans, some of it actually gets pushed back.

TABLE 2
Health Care Costs

Year	Medical Cost per Employee*
1999	100 (Business Health Magazine)
2000	110
2001	127
2002	146

* Increasing lifetimes may hide some increases for retireds!

What are some solutions? We have a couple of entries in place in this country right now: medical spending accounts—which are what self-employed people use—and flexible spending accounts with rollover, offered by some employers. I think that, as an industry, we need to develop some other health-care products that will help people accumulate money for those later years when they need to spend a lot on health care. It should not be an excuse for our insurance companies to say, "We can't do much of that right now because we don't have enough people in the product-development area," which is something I've heard recently. They say that they are too busy. To me, that means that you did not hire enough people.

Turning to increased scrutiny on the part of investors—we have an enlarged social responsibility right now as a visible industry in the United States. Our problem is that insurance is opaque in nature. Two examples are deferred acquisition costs and reinsurance. Both are hard to understand for us. Imagine how the public feels.

I think that mutuals have a chance to brag a little bit. There are not many mutuals left, unfortunately, but the Blue Book is "awful tough to cook," and mutuals could actually stake a claim there. For stock companies, I suggest improving footnotes as a first step. If you actually have looked at a few footnotes, you will see that they are very hard to understand or they do not say anything at all. We should educate the public, and actuaries might be able to assist.

We all know the categories of inefficiency and regulation. Defenders of state regulation will point to the interchange of ideas and the value of having different state insurance departments, having meetings like this one and others. That argument does deserve some credence. I think that what we want is the option. If we get the chance to be federally chartered or to stay with state chartering and regulation, under real-option theory, you want options. We have a chance, I think, to create some. There are some bills that are being developed that relate mostly to reinsurance at this stage.

MS. DONNA R. CLAIRE: Mr. Eckley gave a treetop perspective on the opportunities and challenges; I'm getting down to details on the practical level. I am going to be concentrating more on the investment opportunities and challenges in the current economic environment. As Mr. Ricci mentioned, I am actually going to do it from a regulatory perspective. I am not a regulator; however, as I had mentioned before, there are a number of states (particularly New York) that hire outside consultants, on occasion, to assist in evaluating various companies. I happen to be part of that program. As my husband has pointed out, it is a perfect job for me, because I am able to make people's jobs visible, while getting paid for it as a consultant. But typically, when I am going into a company, it is as a peer reviewer. A favorite phrase is, "We're from the regulators, and we're here to help." Most people do not believe it, but in general, that is really what the regulators are trying to do. They often have a global perspective, and they really want the companies to be healthy. About half of my presentation is going to focus on what is happening at the NAIC in response to the current economic environment. The last half gets practical. When we are going into a company, what types of questions are we currently asking the appointed actuary?

As I have mentioned, in the current economic environment, companies have to become more illiquid, where both assets and liabilities are concerned. The NAIC Life and Annuity Working Group did finalize a liquidity report, and it should be available at the NAIC Website right now. To assist, the Academy also has come up with a liquidity report, and that is available on the Academy Website. That report was finalized in December 2000. In general, this is one area where we recognized that a formulary approach really was not going to work. So we recommended what we called "the New York approach," in which a circular letter or a series of questions is asked to various companies. If necessary, they will ask follow-up questions or invite another company in. The NAIC group does recommend certain annual statement changes, and they also recommend that the financial examiners get more involved in this.

Specifically, in risk management, there are some NAIC risk-assessment groups that are starting to look at this. They are interested in what the banks are doing. The banks do not have a prescriptive formula. They audit the liquidity and risk management—what classes are in place, what types of modeling are performed, and what types of feedback loops are being done. Again, there are various Academy groups that are helping.

In terms of capital management in the current economic environment, a lot of states have recognized that this is an important area. New York, specifically, has a dedicated capital-management staff that is concentrating on the asset side. These guys work with the financial examiners—people like me, the outside actuaries that work with the actuaries on staff. The information that the states are obtaining comes from both the annual statement, and, for example, their ties into Bloomberg data and investment banks. The Morgan Stanleys of the world may be hired to look at various assets of a company to find out what type of risk you really have in the current economic environment. In general, straight ratios are not really used. Once we find what companies were concerned about, they will come up with follow-up questions.

Risk-based capital has gotten a lot of attention, as it should. Because this is a tool that the regulators are using, it is a tool that rating agencies are using to determine where the risks are and which companies potentially have the risk. The C-3 Phase II risk-assessment project, which is currently focusing just on guaranteed benefits and variable products, was probably the starting place. But they already realize that it is not going to be the only place in which there are risks or challenges or opportunities in the current economic environment. There are already plans for a C-3 Phase III risk-assessment project. So if you’re not in the variable-annuity market right now, my guess is, eventually, whatever market you’re in, the C-3 risk-assessment project will be covering your product.

There are also a number of recent actuarial guidelines and regulations in which it is realized that in the current economic environment, a formula will not work. So you have to look at what is happening in the world today. For example, equity-indexed annuities offered the first guideline in which we recognized that it really matters whether or not you hedged well. What are the reserves? First off, the figure is based on the actual option cost of what would be needed in order to hedge the risk. Second, if you are hedging, you cannot hold low reserves. For variable annuities guaranteed-living benefits (VAGLBs), our favorite guideline, quad-M, applies. The actuary has to make his own judgment in terms of what his product is and what risks exist, as well as come up with the correct reserve and sign off on it. That is going to be the minimum reserve standard starting this year-end. Even on the mortality side—for example, "X" factors under XXX and also under the 2001 CSO mortality—the actuary has to get more involved in signing off on what is reasonable. Again, because the current economic environment is changing, a single formula cannot work. We are saying that somebody has got to step up to the plate and actually try to measure these risks. The actuary is the person that is best-suited for that.

The world has moved to solvency risk assessment. It is not good for the reserve adequacy to be done well, if the company happens to become insolvent because of something that they did not anticipate. As commented, a number of regulators are asking more questions. For example, when a company is peer reviewed, it is not just a risk assessment on reserves; it is also done on solvency testing.

Several questions are asked by me or the capital management person that sometimes comes with me when we go to review a company and its financial examiners. "What is the concentration of risk? Have you taken a lot of risk in one particular area?" If so, that could be a problem—for example, in real estate or mortgage loans. Same thing on the liability side—"Do you have big exposures to corporate-owned life insurance or business-owned life insurance, in which case large amounts of money could move at one time?"

If the economy goes sour, typically the disability income costs go up. Are you very heavily involved in disability income without any offsetting products? Group insurance could be a problem. After September 11, New York officials called specific companies and asked, "Do you have particular concentrations of risk in a particular building, a particular area of the country? If so, how are you mitigating those risks?" Sometimes the unthinkable can happen, and your senior manager has to realize that something like that could happen. You should have some plan as to what you are going to do.

Another issue involves parents, affiliates, and subsidiary exposures. Sometimes the life insurance company may be well-managed, but you have an affiliate or a subsidiary that became aggressive in particular investments. If that is going to affect you, the regulators may ask questions about it.

We are into year-three of a down market. We have been working on quad-M and VAGLBs for four or five years. Luckily, the original proposals work on that because, according to the original modeling, it was absolutely impossible for you to get to three years of a down economic environment in the U.S. (Although the impossible sometimes does happen.) As everybody realizes, those guarantees are real; they cost a lot of money. Right now, some regulator questions actuaries. What types of guarantees do you have? How have you hedged it? Have you reinsured it? How are you measuring these types of risks? Specifically, has the Japanese scenario been tested? Right now, Japan's market has been at its worst in 19 years. Sometimes things do not turn around. I am a natural optimist. My husband keeps saying, "Why do you have any money in the stock market?" And I say, "Eventually it will turn around." But I am also practical; that is why I do not have all of my money in the stock market. Maybe the stock market will not turn around in my lifetime, either. You must realize that certain things that we didn't think could happen can, and you should have a plan as to what you're going to do about it. For some companies, we'll ask, "If you can't get reinsurance, have you actually set a limit as to how many guarantees you're light on—either variable annuities with a minimal-death set of guarantees or variable annuities with living-benefit guarantees, or even funding accounts with guarantees in them?"

There have been a few reinsurers that have gotten into trouble. A lot of people in the last few years have been using reinsurers that may not necessarily be U.S.-based. The thing is, until a few years ago, they were not getting into trouble, so no one paid that much attention to them. Now the regulators are noticing that reinsurance trouble—like that of General American Life Insurance Co.—could contribute problems. So they are asking, "How much does the company depend on the reinsurer? Do you have any large exposures to a particular company?" If the answer is "yes" to those questions, we ask, "Exactly what type of checking is done on your reinsurer?" I will admit, I have asked a number of actuaries this question. Oftentimes, the only replies that I will get are, "Yes, they've been around," or "They're investment-grade rated." But that is as far as it goes. Especially if it is large exposure, this is not a good answer. Because if you have a large exposure, if it is a problem, you may not be able to collect quickly on any of the money owed to you. So it is something that you may want to consider. I strongly recommend that you get a sign-off from your reinsurance actuary, so at least you will have somebody else to blame if something goes wrong if you're an appointed actuary.

From the reinsurance side, one thing that is becoming fairly common is a credit-rating downgrade: it is put that you are giving away, in effect. Again, a lot of reinsurers feel that this is a "freebie." However, with the rating agencies being a lot harder on reinsurers, it is no longer a freebie, necessarily. If you have that situation, you should realize that it might be a real risk. Measure how much you're giving away, and realize that you may wind up having to move a lot of cash back to the ceding company quickly.

On credit-risk exposure, we are asking typical questions like, "How much do you have in junk bonds?" But there are assets that a lot of appointed actuaries ignored; for example, "What do you have in your Schedule BA?" (Which is typically the more interesting type of asset.) The thing is, if you have a lot there, it can affect the solvency of the company. Because in the current economic environment, a lot of them are not worth what they may be listed for in the annual statement.

Collateralized-debt obligation is another area in which, recently, insurance companies have gotten into. Typically, in collateralized-debt obligations, there is "insurance" on one hand, and, on the other hand, there is nice, solid, AAA insurance on the top, with guys underneath that would take default. People were thinking that if it's AAA-rated from Moody's, or whatever, it doesn't have default risk. Well, surprise! Some of them are either going into default or are being restructured at this point. So it's something you have to look into if your company has a large exposure to it.

In addition, a lot of appointed actuaries are modeling assuming corporate-bond spreads, like "A" spreads to Treasuries of 200 basis points, which may be close to what it is currently. But the default rate that they're assuming in their cash-flow testing is an historical default rate. The market right now is anticipating higher defaults. If you're using current spreads and historical defaults, you're probably underestimating what your potential risk is in this area.

Real-estate exposure. There were a few companies back in the early 1990s that got in trouble when the real-estate market experienced a downturn. In the current economic environment, in both directly owned and commercial mortgages, the regulators realize this could be a potential problem area, especially on signature buildings such as the Sears Tower. Terrorism insurance is really hard to get on those buildings because it is not a zero-percent risk anymore. The unthinkable really can happen again, unfortunately. Secondly, some of the bigger buildings in a number of areas are having trouble getting people to rent. The economy is low, but there are also people who do not want to be on top floors of certain buildings right now. This is something that I think, as an appointed actuary, you really have not thought about. Unfortunately, you have got to think about it now.

In terms of general risk management, it is an area that you are going to hear a lot more about. From a regulatory perspective, we go in and ask, "Do you have a risk-management function? What's more important is, if you have that function, is it being discussed with your senior management? It is useless for you to know the answer, and your senior management not to know the answer. They are the ones who ultimately run the company. You have to be a little bit more creative as to what types of scenarios you are testing. The old New York seven interest-rate scenarios are completely fallacious—it's useless to test, for example, variables annuities. What is the potential loss on your guarantees that you are giving away?

What type of contingency planning have you had in case something does go wrong? Luckily, the answer to that one is that typically, because of "Y2K," some companies at least do some sort of back up. Again, the regulators are asking these types of questions, and there is no one right answer. They recognize that you have to look at the whole company together.

For example, on risk management, the actuaries should not be the only ones involved. The most important involvement is that of senior management. However, the actuary should definitely be a player. We are uniquely qualified to measure the potential risks, and we cannot rely just on formulated reserves. The asset adequacy testing is moving beyond that. But in risk management, we must go further. We should inform management of potential risk exposure. Again, I have been concentrating on the regulatory end of it, but the most important audience that you have is your senior manager. You must really communicate with them because, the bottom line is, the company's health is actually in senior management's hands.

MR. RICCI: I think it's ironic to note that certain businesses outside of the traditional insurance network highly prize actuarial expertise, maybe before the insurance companies ever did.

Communication is a large part of the issue. You have got to emphasize teamwork, even with your outside auditors and regulators. It is extremely important to bring them into the show. You have to make people really aware of the issues because they are changing rapidly. Senior management demands knowledge and answers. It is a risk-management function, and it has completely changed in the last two or three years. They might have thought that they had the answers before, but they really are in a situation where they are going to need to understand what kinds of risks they are faced with.

The regulators, particularly the state regulators, have more and more dependence upon company resources. They are being squeezed. With international accounting standards, fair value, current statutory issues, the impending influence of federal agencies, and that kind of thing—the state regulators really are depending upon the various companies under their control to act as a team to keep them informed and to let them know what's going on. The actuarial staff, of course, is a precious resource. You may take a look at your actuarial staff and realize that the mix of people—technical versus creative—is not exactly what you need going forward. So you may have to reexamine that whole situation and get it working appropriately. You obviously have to partner with accounting. Accounting is facing a lot of accounting-standard issues that you are going to need to deal with. Also important are IT and marketing (which got us into this situation in the first place).

Consultant use will become more and more urgent, but there is going to be an emphasis to make maximum efficiency of it. So there is going to be more and more pressure to justify the use of consultants.

Underwriting mortality, particularly in the last three or four years, has been influenced, to some degree, by the competition and changing underwriting classes. You need to decide whether the rules now being enforced coincide with the mortality assumptions that you made in the product. This is particularly true, of course, of the reinsurers that gain information second-hand.

Overhead expenses. There's a cyclical reaction in the market. For a long time, in the 1980s, it was economies of scale. As long as you grew out of it, it did not matter what you spent. Then, for a long time, we were trying to trim the fat and keep the unit costs low. Unfortunately, these swings are so wide that when you get to one end, you already should have been heading toward the other. I think that it is important to attempt to keep the swings as small as possible.

Utilization factor—I am really speaking in the context of variable annuity guarantees here, but this could pertain to anything. One of the big problems is that there is no relevant data available; you do not know what is going to happen. You can take a look at withdrawal rates that are occurring currently with a portfolio. But if you have guarantees that are not going to come into play until the end of the surrender period. You just have had the product for three years, it is really a guessing game. So I think that a great deal of conservatism and a knowledge of what sensitivity would be given the utilization is necessary.

Fund volatility. We have had funds for five years. If we use the volatility that we have taken a look at, obviously the skies are limited in terms of the reserve. So what do you use? Do you use some kind of Guideline 34 fund-type solution? Or do you use some other historical analysis? Exactly what is your company doing?

People never remember that you delivered the information on time. What they remember is that you screwed up. It is true of everything in this nature. Sometimes you screw up because you really did not pay attention to the quality of your work, and that is unfortunate. But sometimes you screw up through no fault of your own. You have been given bad data, or there were absolute pressures on bringing the information in. We have to be more acutely aware of that criticism, and that will involve some degree of struggle with those managers that need numbers and values and facts. But that's just the way it goes.

Obviously, there has to be independence on the financial side, but you must be aware of the current initiatives in pricing. Make sure the assumptions are validated properly, and then determine what you need to process the product. Products are so complex, particularly these variable annuity guarantees. I doubt that any company that developed them over the last three years really has the data to accurately measure them. Maybe I am wrong about that, but I know that my company does not.

As I mentioned before, you ought to seriously consider swapping the resource. Look at your capacity to handle environmental changes and make changes where they are appropriate.

I have touched on the secondary variable benefits annuities. We all know of the quad-M committee. They have made an "about face" in April and decided to go with a minimum standard, with an asset adequacy approach. Maybe I'm wrong, but this is the first time that I can recall there being so much responsibility heaped on the appointed actuary to come up with a true measurement of the liability. It is true that in the asset adequacy process there have been some subjective measurements as to what the assumption would be. But in this particular area, it is extremely important to be able to justify the assumptions that you employ. You may come up with answers that are not going to be all that popular with either your company or with the regulators.

Matching the liability of the product—there are many different flavors of VAGLBs. Of course, there are many different flavors of secondary guarantees. It is important to be sure that the assumptions associated with developing the liability match the actual values in a product. If you have a ratchet and a roll-up, it is going to be important for you. Even though the roll-up might be the only thing that's operating currently, it's going to be important for you, stochastically, to be able to use that ratchet in future periods. When in doubt, use standards of practice. Keep informed and up-to-date on that.

Basic principles—I am talking about variable annuities, but this applies to everything. There are fairly simple statutory principles. With regard to guaranteed minimum death benefits (GMDBs), Guideline 34 is supposed to be the operative measurement. We do a stochastic analysis and compare the most positive integrated benefit stream with that under Guideline 34, and that is really the stochastic reserve because we have both the guaranteed minimum death benefit and the VAGLB. Part of that stochastic reserve is related to GMDB (and you cannot separate it), and part of it is related to the VAGLB.

Under a GAAP basis, we use a fractional percentage of Guideline 34 numbers for GMDB. The GAAP principle for VAGLBs basically states that unless you have a contract, you cannot really provide for a GAAP liability. We are assuming that any contract substantially "in the money" and with withdrawal has opted to go for another type of contract. They may not have explicitly done so, but they are in the process of doing so. Therefore, we include as a GAAP reserve, all those contracts that we feel now really have "changed their colors." (They're still in as a so-called variable annuity.)

How do you survive? The mettle of your boss and the board is going to be severely tested. You must insist on their backing and trust, otherwise it really won't work. They will be shy about using consultants, particularly in critical situations. You must document. You have to have documentation that can be peer-reviewed and understandable. Professional resources will be essential, particularly when generating economic scenarios. Get the regulators involved early because you will need to point to them when things go wrong.

How do you survive? You keep everyone aware of the issues; that is your greatest single contribution. When everybody knows the issues and understands them, then you can get to the objective phase of the problem. Understanding the issues is important. Keep current with ASA and the other supporting actuarial bodies. They are doing some really good work, and it is very important for you to be able to know what's going on in that arena. You may not agree with all that they do, and if you don't, then by all means, get involved in the process. Network with people in similar companies with similar products. Commiserate, if nothing else. Plan for the very worst scenarios. I think that going to, say, a conditional tail expectation (CTE) of 90 is along those lines.

When I was in consulting, my partner used to say to me, "The trick to managing a successful business is to be the last person down the funnel." Everybody is in a funnel, and the last person down is the one that wins. In this particular environment, your products have to hold back a little. Let the others jump into the caldron, and then you might be able to survive. It may be an opportunity.

I think that people have to treat reinsurers more like partners now. They have to get involved. I think that the attitude toward reinsurers in the last ten years or so has been, "Well, let's see what we can get. We can always do better. Pin them against each other and see if we can get the lion's share of the profit without giving much away. Get rid of most of the risk."

Now, more than ever, a professional contribution is really important. We are in a new era where actuarial opinion is valued. We are migrating, very quickly, to a Canadian-style system of asset adequacy, and it will place actuaries in a situation in which they are going to have to feel comfortable making decisions and being knowledgeable. Of course, getting the data is half the problem or maybe more, so it is important to keep in touch with IT.

MR. FRANK LONGO: I am an appointed actuary for a small company that does business in New York. I submit an actuarial opinion and memorandum to New York. So what is the likelihood that I am going to get a visit from you, Ms. Claire? What are the circumstances that cause New York to ask you to visit companies to do this type of detailer peer review? There must be some sort of categorization or something.

MS. CLAIRE: Originally, New York was doing selected peer reviews of interesting companies. There was an A-list. However, they found it so valuable that it has actually become a part of the financial examination process. So in New York, the answer is, basically, it is part of your quiennial , so you are probably going to wind up with a visit from me or somebody else in relation to your quiennial examinations. It is part of that process. Right now, just domestics are involved, but it may move to any big writers. If you work in New York, the answer is, within the next five years, you're probably going to get a visit from me or somebody like me.

FROM THE FLOOR: This may be unrelated, but about two weeks ago, I got an e-mail from Larry Gorski. Our investment company is domiciled in Illinois, and he said, "The New York people have been asking about secondary guarantees, and I guess everybody that does business in New York with any kind of secondary benefit has got one." He was wondering what we filled out and could we give him a copy? Well, I told him that we have a term company in New York—that's it—but that we would keep him informed as to exactly what the parameters were from that report. New York is probably just on the forefront of this. I think that all the states are going to want to know what the net amount risks are, what the overall reserves are, and the trend in the reserves. I am sure they will want to keep up-to-date on this.

MS. CLAIRE: Actually there's a group of regulators that meet on an informal basis monthly. They discuss what you are doing in terms of reserve adequacy or solvency testing and what the new things are. Other states probably are going to adopt that.

FROM THE FLOOR: Donna, you made the comment in your presentation that a few states are thinking of moving from reserve adequacy to solvency testing. Does that mean that certain states are thinking about changing their laws in that direction? Because, at the moment, am I not rendering a reserve opinion only?

MS. CLAIRE: You are rendering reserve opinion, and this actually gets a little tricky. The financial examiners look at the health of a company, overall. Therefore, as part of the overall financial examination, there are more solvency questions that can be asked. Legitimately, when I first started with a couple of the actuaries, their answer was, "But I'm doing reserve adequacy opinion." I said, "Yes, that's fine, but these questions have to be answered." Sometimes it is not just the actuary I am meeting with; it is actually the CIO. In fact, a couple of times we actually went all the way up to the president to talk about solvency and risk management. We pointed out to those guys that it is important for them at least to be acquainted with the names of their actuaries.

MR. RICCI: As the appointed actuary, you are appointed by the board. I think that part of your responsibility should be some degree of solvency testing in that regard. They are not necessarily regulatory, so it may be that you are only, in terms of reporting, responsible for the actuarial opinion memorandum. The board depends upon you to keep them informed of solvency.