Regulatory Update

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Chair: NAIC Life Actuarial (A) Task Force (LATF)
NAIC PBR Review (EX) Working Group
NAIC Emerging Actuarial Issues (E) Working Group
Topics

- Principle-Based Reserves (PBR)
- Life Actuarial Task Force
- Emerging Actuarial Issues Working Group
- Other Regulatory Activities Including:
  - Life Risk Based Capital Working Group
  - ORSA
  - 2012 IAR Rule
Principle-Based Reserves (PBR)

Legislative Package (SVL & SNFL)
State Legislative Adoptions
NAIC PBR Implementation Efforts
Company Considerations
Legislative Package

Consists of Changes to:

- Standard Valuation Law (NAIC Model 820)
- Standard Nonforfeiture Law for Life Insurance (SNFL) (NAIC Model 808)
Standard Valuation Law Changes Include The Following

- Authorizes the Valuation Manual (VM) to Provide:
  - Reserve requirements for issues on and after VM operative date.
  - Principle-Based Reserve (PBR) requirements.
  - Actuarial opinion requirements
  - Experience reporting requirements
  - Corporate Governance requirements

- Commissioner authority to exempt domiciled companies doing business only in that state from requirements of the Valuation Manual.

- Commissioner authority to change any assumption or method that in the opinion of the Commissioner is necessary to comply with the VM.

- Commissioner authority to engage a qualified actuary at the expense of the company regarding the requirements in the law.
Standard Nonforfeiture Law Changes

- SNFL changes authorize the Valuation Manual to carry out timely coordination between the valuation interest rate and the nonforfeiture interest rate.
- SNFL changes include similar authorization to the Valuation Manual for coordination as appropriate for valuation and nonforfeiture mortality.
- A new SNFL change is possible for inclusion in the legislative package after the Fall NAIC meeting to provide a 4% floor for the nonforfeiture interest rate to support continued tax qualification of life insurance products under the Internal Revenue Code.
Super Majority Vote Required For VM to Become Operative

VM becomes operative on January 1 following:

1) SVL legislative enactment by at least 42 of the 55 jurisdictions (50 States, American Samoa, American Virgin Islands, District of Columbia, Guam, and Puerto Rico); and

2) SVL legislative enactment by states representing greater than 75% of direct premiums written as reported in 2008 life accident & health, fraternal, and health annual statements; and

3) NAIC adoption of VM by 42 members or 75% of members voting, whichever is greater
2013 State Legislative Adoption Status
Source: ACLI (June 25, 2013)

- 7 States have adopted the legislative package
  - Arizona
  - Indiana
  - Louisiana
  - Maine
  - New Hampshire
  - Rhode Island
  - Tennessee

- Additional State Activity
  - Connecticut – Bill died upon adjournment
  - New Mexico – Bill died upon adjournment
  - Texas – Bill died upon adjournment
# 2008 Direct Premium Percentages

**Source:** NAIC

<table>
<thead>
<tr>
<th>State</th>
<th>% Direct Premium</th>
<th>Cumulative %</th>
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<tbody>
<tr>
<td>New York</td>
<td>9.20</td>
<td>100.00</td>
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<tr>
<td>California</td>
<td>6.79</td>
<td>90.80</td>
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<tr>
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<tr>
<td>Texas</td>
<td>6.27</td>
<td>77.24</td>
</tr>
<tr>
<td>All other states</td>
<td>70.97</td>
<td>70.97</td>
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PBR Implementation (EX) Task Force

Plenary

Executive Committee

Principle-Based Reserving Implementation (EX) Task Force

Life Insurance and Annuities
A-Committee

Health Insurance and Managed Care B-Committee

Financial Condition
E-Committee

Financial Regulation Standards & Accreditation
F-Committee
NAIC PBR Implementation Efforts

PBR Implementation (EX) Task Force
Co-chaired by Commissioner McPeak (TN) & Superintendent Torti (RI)

- Adopted Documents:
  - PBR Legislative Brief
  - PBR Educational Brief
  - PBR Implementation Plan

- Formation of PBR Review (EX) Working Group
- PBR Training

Link to NAIC PBR Implementation (EX) Task Force:
http://www.naic.org/committees_ex_pbr_implementation_tf.htm
PBR Legislative Brief

- One page document providing four statements, background paragraph, and a list of six key points.
- Four statements describe life insurance policy reserves, law changes to enable PBR and the Valuation Manual (VM), and requirement for supermajority adoption.
- Background paragraph provides some history, need for change, concept of right sizing reserves, less incentive for workarounds, and more information regarding supermajority adoption needed.
- Six key points include when states can begin legislative adoptions, legislative package (SVL & SNFL), ongoing VM work, three-year transition, and purpose of exclusion criteria.
PBR Educational Brief
Topics & Questions Covered

- Standard Valuation Law and Standard Nonforfeiture Law
  - What are the changes to the Standard Valuation Law?
  - What are the changes to the Standard Nonforfeiture Law?
  - What is the Valuation Manual?

- Principle-Based Reserving
  - What is PBR?
  - Why is PBR needed?
  - Is PBR more or less conservative?
  - What will make PBR successful?
  - How will PBR affect consumers?
  - How will PBR affect insurance companies?
  - How will PBR affect insurance regulators?
PBR Implementation Plan
Eight Sections

I. Review Process and Staffing
II. Pre-Implementation and Training
III. Valuation: Actuarial and Accounting
IV. Capital Requirements – RBC
V. Captives and Special Purpose Vehicles (SPV)
VI. Accreditation
VII. PBR Legislative Packet (finished)
VIII. Timeline
Section I – Review Process and Staffing

- Discusses NAIC Actuarial Resource, PBR Valuation Analysis Working Group, standardized financial reporting and analysis Tools, and defining the experience data collection process.
- Provides charges to NAIC groups to carry out Section I including charges to a new PBR Review (EX) Working Group.
Develop a framework (or blueprint) for development of risk-focused examination (analysis/examination/actuarial) procedures for PBR, aiming for coordination and consistency of all such activities.


Develop review tools and propose means to obtain the data. Test the tools and data for usefulness and accuracy.

Identify the data and other reporting needs for actuarial review, financial analysis, and public transparency. Recommend changes to other NAIC groups to modify the Blanks, financial statement instructions, and the Valuation Manual to obtain such needed data and disclosure. Utilize confidentiality where needed, maintaining an ability to share data appropriate for valuation improvements.

Identify the ideal staffing resources for PBR reviews, including ideal NAIC assistance, and any new financial modeling or software reviewers. After review processes are better defined, conduct another PBR state resource survey.
Section II – Pre-Implementation and Training

- Discusses training for non-actuarial regulators, actuarial regulators, and industry & consulting actuaries.
- Provides for the PBR Implementation (EX) Task Force to carry out charges for training.
- First training session was provided to regulators via a three hour NAIC webinar on October 9th.
- More training to come for both regulators and non-regulators.
NAIC Regulator Only PBR Training
Held on 10/9/13 – 3 Hour Webinar

Unit 1 Overview of Principle-Based Valuation
Unit 2 Overview of VM 20
Unit 3 Exclusion Tests
Unit 4 Modeling and Cash Flow Models
Unit 5 Economic Scenarios, Discount Rates, & Reinvestment Cash Flows
Unit 6 Policyholder Behavior and Other Key Assumptions
Unit 7 Documentation and Review Considerations

NAIC to make available for non-regulators.
PBR Implementation Plan
Charges to LATF

- Consider use of independent actuarial peer reviews.
- Recommend any requirements for PBR actuarial certification.
- Consider continuing education requirements for PBR.
- Assist the PBR Implementation (EX) Task Force with PBR implementation including training, regulatory guidance, actuarial aspects of model evaluation, and PBR review procedures.
- Further refine the Valuation Manual (VM).
- Coordinate with the Accounting Practices and Procedures (E) Task Force on implementation and changes to the VM.
- Accounting smoothing to address reserve volatility.
LATF Valuation Manual (VM) PBR Work

http://www.naic.org/committees_a_latf.htm

- VM Amendment Proposal Forms (APFs) Include:
  - Policy loan modeling clarification – Adopted
  - Direct Iteration Method proposal to provide simpler option to calculate the Deterministic Reserve.
  - Proposal to include in PBR scope group life individually underwritten certificates.
  - Treatment of due premiums.
- 2014 Valuation Basic Table & CSO Table
- Updating Asset Default Costs & Spread Tables
Work continues on PBR for non-variable annuities with the LATF VM-22 Subgroup and the American Academy of Actuaries’ Annuity Reserves Work Group. Current efforts include:

- Replacing a large number of stochastic interest / market scenarios with a small number of scenarios for each significant risk for a product group.
- Providing a floor reserve equal to a modified AG-33 approach with prescribed lapse and incidence rates.
- Field test in progress to evaluate these calculations.
The LATF Aggregate Margin Subgroup and the American Academy of Actuaries’ Aggregate Margin Task Force current efforts for an Aggregate Margin methodology include:

- Current preference for an aggregate margin methodology is the cost of capital approach.
- Calculation option: A representative scenario approach would use a limited number of adverse scenarios for each major risk driver to develop the capital measure for the cost of capital calculation.
- Will continue to consider both the cost of capital approach & the confidence interval approach for some period of time.
Considerations Relating to PBR Exclusion Tests or Timing of Applying Requirements.

ACLI small company consideration

- Possible additional time to implement PBR based on:
  - Some premium level &/or other thresholds.
  - Risk consideration related to RBC &/or type of products

Other considerations:

- More clarification regarding the Stochastic exclusion test demonstration such as providing a safe harbor demonstration.
Stochastic Reserve (SR) Exclusion Tests

Products can be excluded from the SR if:

- Certification provided by qualified actuary of no material interest rate risk or asset return volatility risk (cannot be used for certain products); or
- Stochastic exclusion ratio test is passed; or
- Demonstration provided that reserves will not increase under stochastic requirements
Deterministic Reserve Exclusion Test

- Products can be excluded from the deterministic reserve requirements if the sum of the net valuation premiums are less than the sum of the corresponding gross premiums
- Cannot be used for universal life products with secondary guarantees or for products required to calculate the stochastic reserve
Other LATF Work

- Contingent Deferred Annuities (CDAs):
  - New charge to evaluate AG 43 to determine whether reserving would be deficient for CDAs and recommend any changes or guidance as appropriate.
  - Included in this charge is to consider revisions to the Standard Nonforfeiture Law for Individual Deferred Annuities (Model 805) to exclude CDAs from scope.
- Consider recommendations regarding the applicability of the NAIC variable annuity regulatory framework to separate account index-linked products filed as variable, including but not limited to product definition and nonforfeiture requirements.
Emerging Actuarial Issues WG (EAIWG)
http://www.naic.org/committees_e_emerging_actuarial_issues_wg.htm

- Adopted over 30 interpretations since being formed in November 2012 to answer questions regarding 2012 adopted changes to Actuarial Guideline 38 (AG38).
- The working group is currently dealing with several questions regarding both Sections 8D and 8E of AG 38.
- Per the requirements of AG38 the NAIC Financial Analysis Working Group (FAWG) is reviewing submissions in response to the requirements of AG38, 8E & 8D. Interpretations adopted by the EAIWG are used by FAWG in these reviews.
AG 38, 8D provides a reserve floor for applicable universal life with secondary guarantee business (ULSG) starting for year-end 2012 valuations.

This reserve floor uses a modification of the PBR Deterministic Reserve in the Valuation Manual.

Domestic states and consultants to the NAIC Financial Analysis Working Group (FAWG) are continuing reviews of the year-end 2012 AG 38, 8D valuations.

AG 38, 8D valuations provide a unique opportunity to assess such a modification to the PBR Deterministic Reserve, given it applies to existing business vs. a hypothetical study, and make any changes in the Valuation Manual as appropriate.
Other Regulatory Activities

Life Risk Based Capital Working Group
http://www.naic.org/committees_e_capad_lrbc.htm
  • Recent exposures regarding treatment of unauthorized reinsurers and regarding conflicting use of AVR.

ORSA
http://www.naic.org/committees_e_orsa_wg.htm
  • Pilot project reviews underway

2012 IAR Rule
  • States working to make effective beginning 1/1/2015 versus 1/1/2014
Thanks

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