



AMERICAN ACADEMY *of* ACTUARIES

**Updated Principles-Based Approach Principles from the American Academy of Actuaries'
Consistency: Principles, Summary, Definitions & Report Format Work Group**

**Presented to the National Association of Insurance Commissioners'
Life and Health Actuarial Task Force**

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The American Academy of Actuaries is a national organization formed in 1965 to bring together, in a single entity, actuaries of all specializations within the United States. A major purpose of the Academy is to act as a public information organization for the profession. Academy committees, task forces and work groups regularly prepare testimony and provide information to Congress and senior federal policy-makers, comment on proposed federal and state regulations, and work closely with the National Association of Insurance Commissioners and state officials on issues related to insurance, pensions and other forms of risk financing. The Academy establishes qualification standards for the actuarial profession in the United States and supports two independent boards. The Actuarial Standards Board promulgates standards of practice for the profession, and the Actuarial Board for Counseling and Discipline helps to ensure high standards of professional conduct are met. The Academy also supports the Joint Committee for the Code of Professional Conduct, which develops standards of conduct for the U.S. actuarial profession.

Consistency: Principles, Summary, Definitions & Report Format Work Group

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The Work Group would also like to recognize the following individual for their valuable input: Bill Weller.

A **Principles-Based Approach (PBA)** of statutory Risk-Based Capital (RBC) and minimum reserve requirements incorporates the following common statements that should be considered together and not in isolation from one another. Further, these statements should be interpreted in the context of the value being calculated (i.e. reserve or RBC component).

1. Captures all of the benefits and guarantees associated with the contracts and their identifiable, quantifiable and material risks, including the 'tail risk' and the funding of the risks.
2. Utilizes risk analysis and risk management techniques to quantify the risks and is guided by the evolving practice and expanding knowledge in the measurement and management of risk. This may include, to the extent required by an appropriate assessment of the underlying risks, stochastic models or other means of analysis that properly reflect the risks of the underlying contracts.
3. Incorporates assumptions, risk analysis methods and models and management techniques that are consistent with those utilized within the company's overall risk assessment process. Risk and risk factors explicitly or implicitly included in the company's risk assessment and evaluation processes will be included in the risk analysis and cash flow models used in the PBA. Examples of company risk assessment processes include economic valuations, internal capital allocation models, experience analysis, asset adequacy testing, GAAP valuation and pricing.
4. Permits the use of company experience, based on the availability of relevant company experience and its degree of credibility, to establish assumptions for risks over which the company has some degree of control or influence.
5. Provides for the use of assumptions, set on a prudent estimate basis, that contain an appropriate level of conservatism when viewed in the aggregate and that, together with the methods utilized, recognize the solvency objective of statutory reporting.
6. Reflects risks and risk factors in the calculation of reserves and capital that may be different from one another and may change over time as products and risk measurement techniques evolve, both in a general sense and within the company's risk management processes.

The aforementioned statements should be applied in a manner consistent with statutory requirements and company risk measurement practices then in effect.