

Life Capital Work Group

Update to the Life RBC Working Group

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LCWG Charge

The charge of the AAA Life Capital Work Group is to review and evaluate the interest rate and market risk (C3) component of the current Life Risk-Based Capital framework in the context of life products valued under a Principles-based reserving approach. The AAA Life Capital Work Group will work with the AAA Life Reserves Work Group and recommend changes to the Life Risk-Based Capital formula, as necessary.

- Scope of the work does not include review of C1 or C2 components.
- C3P3 Project seen as next step toward a future comprehensive Principles-based approach to capital.



LCWG Working Construct: Scope

- Rules will apply to all life insurance products inforce. No restriction to those policies in LRWG scope.
- Recommend inclusion of Single Premium Life business in C3P3 and removal from scope of C3P1
- Variable Products
 - C3 amount will replace current C1 required capital on expense allowance
 - Recommend allocation of C3 amount into interest and market (variable) components consistent with C3P2



LCWG Working Construct: Scope (cont.)

- Considering Exclusions / Exemptions for blocks with no tail risk where it can be demonstrated that a simpler method produces an amount greater than that determined using the CTE(90) TAR calculation.
- LPC and LCAS recognize there may be significant practical implementation issues applying C3P3 to all inforce policies, but LPC believes that application to inforce is theoretically correct.



LCWG Working Construct: Calculation Basis

- C-3a Component of Risk-Based Capital = TAR - reserve
- TAR will be set at CTE(90) consistent with risk level set for other products.
- The C3P3 charge is an after-tax calculation reflecting stochastic interest rate and equity scenarios. TAR calculated as the Greatest PV of Accumulated Deficiency calculation.
- Discount rate
 - Tentatively using after-tax portfolio earned rate with adjustments deemed necessary to reflect Interest Rate hedging (to come out of ARWG work)
 - Monitoring work of LCAS Discount Rate group



LCWG Working Construct: Assumptions

- Projections reflect Prudent Best-estimate assumptions with margins, where margins will be left to actuary's judgment. Guidance on margins will come from the forthcoming LRWG principles. TAR uses Prudent Best-estimate assumptions with margins.
- Note that the use of PBE is appropriate within the C3P3 context; however, additional review may be necessary in overall context of PBA to capital.



LCWG Working Construct: Assumptions (cont.)

- Scenarios, at option of actuary, may be generated from either:
 - AAA supplied generator
 - Proprietary generator, subject to AAA ESWG calibration criteria (i.e. AAA Economic Scenario Work Group).
- Treatment of Hedges
 - Will be directly reflected in the C3P3 calculation, based on existing C3P2 framework
 - Need to monitor hedging treatment for consistency with C3P1 and ARWG developments.



LCWG Working Construct: Implementation

- Aggregation methodology is subject to actuarial judgment using the forthcoming LRWG guidance
- Certification Memo required; Principles-based Review will apply in future when permitted / required by NAIC



LCWG Timeline

- September LRWG update to Model Regulation and Actuarial Guidelines will serve as base for creating draft LCWG report.
- Draft LCWG report to be completed and exposed by September 30; report will be presented to NAIC's LRBC group at December, 2006 NAIC meeting
- Proposed 2007 LRBC Instructions changes necessary to enable C3P3 to become effective for year end 2007 will be presented to LRBC group at December, 2006 meeting. September LRWG update to Model Regulation and Actuarial Guidelines will serve as base for creating initial LCWG draft recommendation / report

