A PUBLIC POLICY PRACTICE NOTE

Actuarial Standard of Practice (ASOP) No. 2: Non-Guaranteed Elements for Life and Annuity Products

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Developed by the Life Practice Council's Non-Guaranteed Elements Subcommittee

American Academy of Actuaries
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AMERICAN ACADEMY of ACTUARIES

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Comments are welcome as to the appropriateness of this practice note, desirability of periodic updating, validity of substantive disagreements, etc. Comments should be sent to lifeanalyst@actuary.org.

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Section 1. Scope, Purpose, Cross References, and Effective Date

Q 1: Which life insurance and annuity products are included within the scope of ASOP No. 2?

Many actuaries consider life insurance and annuity products for which the insurer has the right to exercise discretion to prospectively change a Non-Guaranteed Element (NGE) to be within the scope of ASOP No. 2.

Examples of these products include the following:

- Individual life insurance such as Universal Life (UL), Variable Universal Life, Indexed-Universal Life, Indeterminate Premium Term, and Whole Life.
- Annuities such as fixed, indexed, and variable deferred annuity products and certain income features within these products.
- Certain Group contracts such as Group Universal Life (UL) for which certificates are issued to each insured.
- Riders with NGEs, such as an indeterminate term rider, a disability waiver rider.

Some actuaries consider certain riders with NGEs that offer health benefits to be in scope of ASOP No. 2.

Q 2 The term "redetermination" is sometimes used in connection with inforce policies. What is meant by redetermination?

While ASOP No. 2 uses the term "determination" for both initial and subsequent determinations, actuaries have used the term "redetermination" in part because it was used in prior versions of ASOP No. 2. Some actuaries may still use "redetermination" or even "repricing" to refer to the process of reviewing NGEs that have already been through at least the initial determination process. Many actuaries would look to ASOP No. 2 to understand the differences between the initial determination and subsequent determinations.

Q 3: If a rider has NGEs, but the base policy does not, does ASOP No. 2 apply?

Yes. Because the definition of the policy within scope of ASOP No. 2is defined as the policy and attached rider, many actuaries would consider how ASOP No. 2 impacts any NGE in the policy or contract as a whole (i.e. base policy plus riders).

Q 4: If prior determinations were conducted before the effective date of the current version of ASOP No. 2 and were inconsistent with the current version, how do actuaries handle a subsequent determination?

Actuaries generally follow the guidance available in the current version of ASOP No. 2. There may be situations where prior determinations are not aligned with the current ASOP No.2. In a case where it is not practical or feasible to follow the current version of ASOP No. 2, many actuaries would disclose the circumstances and rationale for their recommendation including any deviations from the current ASOP.

Q 5: What is an example of a specific type of group policy that might be subject to ASOP No. 2?

Many actuaries consider Group UL with a non-guaranteed element and some worksite life insurance policies as examples of group policies that are subject to ASOP No. 2.

Section 2. Definitions

Q 1: What are examples of anticipated experience factors?

Examples of anticipated experience factors might include rates of investment income, mortality, morbidity, policy persistency, and expenses. Other examples that some actuaries might consider include tax rates, reinsurance charges, annuitization rates, recovery rates, hedging costs, inflation, or any other factors whose future expectations could impact the determination of NGEs, if permitted by contract language, law, and regulation.

Q 2: What approach do actuaries take to determine whether a policy element is an NGE, i.e., satisfies the definition of an NGE in Section 2.4, and what are some common examples?

Many actuaries would review the policy form as well as refer to the definition of an NGE in ASOP No. 2. They would use their professional judgment in evaluating whether the policy element can be characterized as a premium, charge, or benefit within an insurance policy and, if so, whether it meets the definition.

Some examples of policy elements that actuaries commonly regard as NGEs for some common types of products include:

- For Universal Life Insurance, many actuaries consider non-guaranteed cost of insurance rates, loan interest rates, mortality and expense risk (M&E) charge, or other expense charge rates to be examples of charges that satisfy the definition. Many actuaries would consider a non-guaranteed interest credited rate, non-guaranteed cap rate, non-guaranteed floor rate, non-guaranteed participation rate, non-guaranteed multiplier, or loan credited rate all to be examples of benefits that satisfy the definition.
- For Non-Participating Whole Life Insurance, many actuaries would consider a non-guaranteed loan interest rate to be an example of a charge that satisfies the definition. Many actuaries would consider a non-guaranteed interest bonus to be an example of a benefit that satisfies the definition.
- For Indeterminate Premium Life Insurance, many actuaries would consider a non-guaranteed premium rate to be an example of a premium that satisfies the definition. For example, many actuaries would consider a post-level term, non-guaranteed premium rate to be an NGE.
- For Deferred Annuities, many actuaries would consider a non-guaranteed interest credited rate, a bonus rate, an indexed cap rate, indexed floor rate, indexed participation rate, or indexed multiplier to be examples of benefits that satisfy the definition.

Q 3: Is any element of a policy that may change after issue an NGE?

No. ASOP No. 2 defines NGEs as premiums, charges, or benefits that affect policy costs or values, are not guaranteed in the policy, can be changed at the discretion of the insurer, and reflect expectations of future experience. This ASOP defines guaranteed elements as premiums, values, charges, or benefits that limit NGEs and are specified in the policy.

Based on the definitions in ASOP No. 2:

- Actuaries generally would not consider policyholder dividends to be within the scope of ASOP No. 2 because they are subject to ASOP No. 15 and provide participation in past experience rather than reflecting expectations of future experience.
- Actuaries generally would not consider indeterminant premiums, values, charges, or benefits as NGEs within the scope of ASOP No. 2 if they cannot be changed at the discretion of the insurer. Such elements would include for example: (1) premiums or benefits tied to equity, interest, or cost of living indexes; (2) values tied to variable investment fund performance; (3) expense charges tied to state premium taxes, investment advisory fees, or other costs incurred by the insurer and passed through to the policyholder; (4) benefits that are tied to federally imposed limits in order to qualify for favorable tax treatment such as the HIPAA limit, etc.
- When policy elements are not specifically designed to reflect or allocate anticipated experience of an insurer, some actuaries would not consider such policy elements to be NGEs, such as: policy provisions that give insurers discretion to change minimum transaction amounts, maximum number of transactions, or limits on premiums or deposits.

Q 4: The definition of an NGE includes the requirement that an NGE can be changed at the discretion of the insurer. What are some examples of policy provisions where the premiums, charges, or benefits may change, but not at the discretion of the insurer?

Actuaries would generally look to the policy form to identify guaranteed premiums, charges, and benefits.

Some policies may include provisions which allow premium, charges, or benefits to change, but not at the discretion of the insurer, such as:

1) a formula stated within the policy
2) an indexed interest rate
3) a variable loan rate tied to an external index
4) a direct pass-through policyholder service fee from a third-party administrator
5) a direct pass-through of tax costs such as a state premium tax

Many actuaries would examine the feature to determine whether there is any parameter that could qualify as a discretionary element.

Q 5: Are NGEs that are not included in the policy form subject to ASOP No. 2?

Since ASOP No. 2's definition of NGE does not exclude non-contractual charges, premiums, or benefits, generally actuaries base the decision on whether the element meets the ASOP's definition of an NGE, subject to regulatory or contractual constraints.

Q 6: Are there different considerations for variable contracts relative to non-variable contracts when determining which features are NGEs?

Generally, actuaries review the features and terms of any contracts or prospectuses for variable products in order to determine which features are NGEs. For example, variable contracts may refer to mortality and expense charges while non-variable contracts generally do not. Some features have similar characteristics but may not be NGEs under both types of products. For example, variable investment rates of return for the separate account are similar to interest crediting rates for the general account, but if they are not under the discretion of the company to change, they might not be considered NGEs.

Many actuaries consider the above for determining which features are NGEs for registered life insurance or annuity products, whether they are variable or non-variable.

Q 7: What is an example of how to develop NGE scales based upon anticipated experience?

Many actuaries look to their NGE framework for how to translate anticipated experience factors into NGE scales. For example, when developing a credited rate for a UL product, the investment area of a company could help the actuary understand the anticipated yield on assets for a UL block with consideration for defaults and investment costs, to obtain a net investment earned rate. The actuary then looks to the NGE framework to understand potential profit goals and product structures to develop the credited rate, considering any pricing spread that ultimately impacts the final NGE credited rate.

Q 8: How can the actuary take experience trends into account when determining NGEs?

Many actuaries look at historical experience data to assess if the experience trend is credible, significant, and ongoing. Once a trend is determined to be credible, significant, and ongoing, some actuaries would reflect the trend in the anticipated experience factor, consistent with any guidance in the NGE framework.

Q 9: Does there need to be a one-to-one relationship between anticipated experience factors and specific NGEs?

Many actuaries believe there does not need to be a one-to-one relationship but do consider the policy form and NGE framework when developing NGEs. Some actuaries develop NGEs based on more than one experience factor or a singular factor. For example, many actuaries look at multiple factors when developing a cost of insurance NGE, while some focus only on mortality.

Section 3. Analysis of Issues and Recommended Practices

Section 3.1 NGE Framework

Q 1: What sources of information would help to understand the NGE framework?

Beyond the elements of the NGE framework noted in Section 3.1 of ASOP No. 2, additional sources of information may include documentation from prior NGE determinations, policy class determinations, NAIC Annual Statement Interrogatories, product documentation, internal memos, internal emails, pricing and profitability standards, marketing objectives, marketing materials, institutional knowledge from actuaries involved in past NGE determinations, and any other sources of information concerning the determination of NGEs.

Q 2: What parts of ASOP No. 2 would help the actuary to evaluate whether the company's NGE framework is incomplete, absent, or needs updating?

To determine whether an NGE framework is complete, many actuaries would first consider the definition of NGE Framework (Section 2.5) and the definition of the Determination Policy (Section 2.2), which is an element of the NGE framework.

Many actuaries would then consider Section 3.1, NGE Framework, which states that the actuary should understand the insurer's NGE framework in relation to the actuarial services requested, including the examples listed there. Many actuaries would also consider any other practices, methods, or criteria used by the insurer to determine NGE scales which are relevant to the services requested.

If the actuary is unable to complete their assignment because the NGE framework is incomplete, absent, or needs updating, Section 3.1 requires the actuary to recommend that the NGE framework be created, completed or updated. Many actuaries would include a potential solution as part of that recommendation.

Q 3: What are examples of circumstances where the NGE framework is incomplete or needs to be updated?

Documentation of elements of the NGE framework may be found in multiple company sources. If so, many actuaries would review and summarize the documentation to understand the framework.

The following are situations where the NGE framework may be incomplete:

a) The company recently purchased another company or reinsured a block of business.
b) The company is entering a new line of business.
c) Changes in underwriting requirements or criteria.
d) Loss of information due to technical difficulties or employee turnover.

If the NGE framework is incomplete, many actuaries would recommend that the NGE framework or major parts of the NGE framework be developed and documented.

Q 4: How do I decide whether there is enough information about the NGE framework to move forward with my assignment?

Actuaries generally use professional judgment to decide if they have enough information about the NGE framework to move ahead with the assignment. Many actuaries would consider whether missing information or conflicting documents would materially affect the results of the assignment. For example, when setting a crediting rate, if information concerning the targeted spread is not available, it may not be possible to make a recommendation.

Q 5: Can companies have differences between what is included in the determination policy and the NGE framework?

Variations in how companies develop and decide which items are part of their determination policies and NGE frameworks are common. Since companies vary their approach to product design, risk management, target markets, and distribution methods, some companies include certain elements in their determination policy, while other companies might include the same elements in their NGE framework.

Section 3.2 Providing Advice on the Actuarial Aspects of the Determination Policy

Q 1: What sources may be helpful to an actuary seeking to understand the actuarial aspects of an insurer's determination policy?

In addition to reviewing any formal determination policy with respect to ASOP No. 2, many actuaries would consider reviewing previous pricing memos, emails from the principal assigning the project, and relevant corporate policies to understand the actuarial aspects of the determination policy. In the absence of a formal determination policy, many actuaries would also consider reviewing the insurer's relevant governance processes, operating practices, Board minutes, NAIC Annual Statement NGE interrogatory instructions and opinions, documentation of prior determinations, and possibly other sources to build a more complete understanding of the actuarial aspects of the informal determination policy.

Q 2: Can changes be made to any NGE scale based on changes in any anticipated experience factor?

Many actuaries would consider recommending a revision in an NGE scale due to a change in any anticipated experience factor, as long as the change to the NGE scale is compliant with ASOP No. 2. Many actuaries would consider relevant circumstances, including the policy form, all anticipated experience factors, applicable law, and the NGE framework when determining NGE scales for that policy.

Q 3: Does the determination policy need to be the same for all parts of an insurer's business or can it vary?

Many actuaries would consider recommending variations in an insurer's determination policy for determining NGEs, as long as the recommended variations are not inconsistent with ASOP No. 2. Some examples include different lines of business, jurisdictions, year of issue, duration of the policy, or distribution channel. Some additional examples include:

- Advising an insurer that their profitability objective could vary by line of business.
- Advising an insurer that their cost of capital and capital objectives could vary by year of issue.
- Advising an insurer that the expense recovery objectives could vary by policy duration or distribution channel.
- Advising an insurer that something may vary between an older closed block that is exempt from PBR vs a PBR block.

Q 4: What are examples of providing advice on the actuarial aspects of developing or modifying a determination policy?

Many actuaries would consider the following to be examples of advising on developing or modifying a determination policy:

- Reviewing whether an existing determination policy should be extended to a new line of business.
- Formalizing an insurer's informal principles and objectives for determining NGEs.
- Developing a principle for analyzing the impact on the determination policy due to the variability and credibility of experience data.

Q 5: What are examples of applying the determination policy?

The determination policy would generally be applied when determining initial NGE scales, evaluating whether to revise existing NGE scales, or revising existing NGE scales. For example:

- When providing advice on setting the cost of insurance rates for a new life insurance UL product, an actuary would generally use the relevant guidance of the company's determination policy.
- When deciding whether to recommend a change to an Indexed Universal Life segment cap rate many actuaries would look to the determination policy to understand how investment income should be taken into account.
- When providing advice on setting the current credited rate for a fixed deferred annuity, many actuaries would apply approaches included in the determination policy to determine anticipated investment experience factors.

Q 6: What are examples of competing objectives when recommending the development, modification and/or application of the actuarial aspects of the determination policy?

Some examples of competing objectives are:

- There is a change in the experience upon which a non-guaranteed element is based, but the cost for implementing the change to the NGE scale is high.
- The determination policy calls for the company to review experience for possible changes to NGEs every five years, but there is evidence of a drastic change in experience after three years.
- The company assumes business from another company and needs to determine whether to treat the new assumed block the same as existing blocks.

Many actuaries would document any conflicts as well as recommendations for handling competing objectives when advising as to whether to change the determination policy.

Q 7: If past profits have been other than expected, does Section 3.2.b apply?

Unlike participating products providing dividend payments, NGEs are generally expected to be determined prospectively. Many actuaries reserve consideration of past losses/gains for dividend determination as ASOP No. 15.

Section 3.3 Establishment and Changes to Policy Classes

Q 1: How do I develop a policy class?

Generally, actuaries look to Section 3.3.1 of ASOP No. 2 for the considerations the actuary should follow in establishing policy classes for a new product. Actuaries generally will use their professional judgment to determine the number of classes needed and the granularity of those classes for future sales of a new or existing product.

For example, an actuary might consider what type of product they are selling or whether they can measure the granularity of the experience factors they are developing.

- An Accidental Death Benefit product might not vary its policy classes by gender or risk class but could consider varying their policy class by age grouping or occupation.
- Considerations for policy classes might also vary between Group Life products (group products that issue individual certificates) and Individual Life Insurance products. The characteristics of a group for a particular distribution channel, e.g. a voluntary plan offered to an affinity group, might impact the policy class developed which would not be a consideration on the Individual Life Insurance product.

In advising how to determine policy classes, some actuaries might consider how anticipated experience factors may vary, such as mortality expectations that vary by the level of underwriting, issue age, face amount, tobacco use, etc. Some actuaries might advise that differences in marketing methods may indicate a need for different policy classes.

Q 2: Under what circumstances might an actuary recommend a change in policy classes after issue?

Many actuaries will consider recommending a change in a policy class after issue depending on the circumstances, if in the actuary's professional judgment such change is appropriate. Some examples of how a policy class might be changed after issue are combining policy classes to use the same NGE scale, splitting policy classes to be more granular, or combining policy classes to have the same relative change in NGE scale applied but still having different underlying scales.

Examples of circumstances where some actuaries might recommend a change in policy class after issue are:

1) If expense charges were set separately for business with simplified underwriting versus full underwriting, but emerging experience is not materially different, many actuaries would consider combining the policy classes for expense charges.
2) If a change in a state's premium tax affects some policies within a class differently than others, many actuaries would consider assigning the policies affected by the tax change to newly established policy classes to reflect those differences.

3) If experience within a policy class is not credible, many actuaries would consider combining policy classes to determine the relative change in the NGE scale, while maintaining separate underlying scales.
4) If a company changes its investment income allocation methodology many actuaries would consider matching the new methodology to the crediting rate classes. Subject to regulatory and policy requirements, many actuaries would recommend changes to a policy class for in-force policies after reviewing underlying material relevant to anticipated experience factors and documenting the considerations for change in policy class definition. Many actuaries would consider whether such changes in policy class are consistent with specifically the NGE determination policy and more generally the NGE framework.

Q 3: Must there be a one-to-one alignment between risk classes (per ASOP No. 12) and policy classes (per ASOP No. 2)?

Many actuaries do not believe it is necessary to establish a one-to-one alignment of policy classes and risk classes. For example, a policy class used for determining interest credited rates would not necessarily have an equivalent risk class under ASOP No. 12. On the other hand, for policy classes involving risk characteristics such as mortality or morbidity, many actuaries use the same policy classes for ASOP No. 2 as the risk classes developed under ASOP No. 12 for those risk characteristics.

Q 4: How can an actuary establish the policy class to mitigate antiselection that could impact profitability?

To mitigate the risk of antiselection, many actuaries refine policy classes to be consistent with their business objectives and to reflect material differences in expected costs. For example, some actuaries may create smoker-distinct policy classes to mitigate the antiselection risk embedded in a combined unismoke class. Many actuaries may refer to ASOP No. 54 for additional pricing considerations that may not be considered or referenced in ASOP No. 2.

Q 5: What is an example of a practical consideration when developing or changing policy classes?

An example of a practical consideration could be any perceived advantages of more granularity versus less data credibility, as well as the cost of developing and managing additional policy classes.

Many actuaries would consider that, per ASOP No. 2, Section 3.3.1.a, the actuary should recommend the establishment of or changes to the policy classes that are consistent with the guidance in ASOP No. 12, Risk Classification.

Q 6: What happens if changes in experience impact a subset of a policy class for determining an NGE? For example, a policy class is defined to cover several product forms and changes in experience impact only one of the product forms.

There are many reasons why experience changes may only impact a subset of policies within a policy class. Some actuaries consider whether to recommend changes to policy classes and how the experience changes will be reflected in an NGE. Many actuaries would consider whether the change is material to the anticipated experience factors for the policies within the impacted subset as well as the remaining non-impacted policies. Many actuaries would consider the impacts of reassigning the subset of policies to a different policy class and the practical implications of making the change. Many actuaries would review ASOP No. 2, Section 3.3.2, and prepare an analysis and documentation to support any recommendations which may be disclosed as per Section 4.1.

Q 7: Can policy classes span multiple products, or do they have to be product specific?

ASOP No. 2 defines policy class as "policies that are grouped together for the purposes of determining an NGE". This definition does not specify whether a policy class has to be product specific. However, the ASOP's definition of NGE framework states that it includes "the methodology for establishing policy classes." Therefore, actuaries generally would refer to the insurer's NGE framework in evaluating whether a policy class is or is not product specific.

With respect to future sales of a new or existing product, Section 3.3.1 states that "policy classes may be defined by grouping policies at various levels, for example, at a product level, across multiple products, or within a product or products." Therefore, many actuaries would consider that policy classes may be—but are not required to be—defined at a product level, and that they may also be defined at narrower or broader levels.

Section 3.3.1 then goes on to say that the actuary "should take into account the policy provisions, the structure of guaranteed elements and NGEs, the date on which the recommended policy classes would take effect (for example, policies issued before or after a particular date could be in different policy classes), and the underwriting characteristics and marketing objectives for the product."

With respect to in-force policies, Section 3.3.2 states that "the actuary may recommend combining or redefining policy classes if, in the actuary's professional judgment, such combinations or redefinitions would be appropriate. For example, if the experience for a policy class is not credible, the policy class could be combined with other policy classes for the purposes of determining anticipated experience factors."

In view of the sections referenced above, many actuaries would consider the definition of policy classes which are either product-specific or not product-specific to be permissible, depending upon the circumstances, the nature of their assignment, and the relevant principles and practices of the insurer's NGE framework.

Q 4: If a policy has different minor variations, such as variations to reflect state of issue language differences, do these need to be in different policy classes?

Many actuaries would ask themselves whether the state variation changes the approach to setting an NGE in deciding whether to recommend a separate policy class. A unisex regulation would be an example of a requirement that some actuaries would consider in setting mortality classes.

Section 3.4 Determination Process for NGE Scales

Q 1: How do actuaries consider the relationship of anticipated experience factors to NGE scales when determining NGE scales?

Some actuaries will consider the pattern or level of anticipated experience factors when setting the pattern or level of an NGE scale.

Examples of NGE scales and anticipated experience factors that may have closely linked patterns or levels are:

- credited interest rates and investment earned rates
- expense loads and maintenance expenses and/or issue expenses
- cost of insurance rates and mortality

Unless restricted by contract language or law, many actuaries would consider additional factors such as policy persistency when determining NGE scales.

Q 2: Can an actuary change the profitability metric when recommending a change in NGEs?

Yes, as per Section 3.4.2.3, a different metric may be appropriate for inforce determinations. However, to assess consistency with Section 3.2, when appropriate, some actuaries may compare the prospective profitability using the new metric and the original or prior assumptions versus the prospective profitability with the updated assumptions.

Q 3: If a new profitability measure is being used or if the original profitability metric is no longer meaningful for in force NGE determinations, how does an actuary evaluate profitability vs the previous determination?

Some actuaries may choose a new profitability metric to evaluate subsequent NGE determinations. For example, the use of Internal Rate of Return (IRR) after the first year may no longer be as meaningful. Actuaries generally try to compare the prospective profitability of the current and previous determination using the new metric. Some actuaries consider the pattern of profits when performing subsequent determinations. For example, if a product was anticipated to have losses at certain durations, many actuaries would consider the amount and duration of those losses, and then determine NGEs in a manner that reflects the previously anticipated pattern of profits and losses.

Q 4: Is it appropriate for an actuary to recommend a change to the NGE scale solely due to changes in the profitability metrics?

If it has been decided to change profitability metrics, many actuaries would consider reviewing prior determinations under these new profitability metrics, holding all other assumptions constant in the comparison between the determinations. Many actuaries would then consider this pattern of profitability as the standard against which to measure future determination efforts. Many actuaries would not make a recommendation to change NGE scales solely due to a change in profitability metrics unless there also was a change in anticipated experience factors.

Q 5: Does an actuary need to change NGEs when experience changes?

There is no requirement in ASOP No. 2 to change NGEs every time experience changes. Many actuaries follow their NGE framework as to when NGEs may change and by how much when experience emerges and potentially deviates from anticipated experience factors. The NGE framework of some insurers may lead to more frequent updating of anticipated experience factors for NGEs. For example, many actuaries change credited interest rates monthly or quarterly based on changes in experience.

Per Section 3.4.2.2, when analyzing how experience is emerging relative to anticipated experience factors there are various considerations to take into account, for example, the credibility of the experience or the materiality of any change in the experience relative to the existing anticipated experience factors. If warranted by the results of the analysis, many actuaries would also consider Section 3.4.2.3 when deciding whether to recommend that the NGEs be updated.

Q 6: Can an actuary recommend changing NGE scales for changes which are anticipated to be temporary?

ASOP No. 2 does not prohibit actuaries from changing NGE scales for changes that are anticipated to be temporary, though actuaries might analyze the materiality of the temporary changes relative to the existing anticipated experience factors (ASOP No. 2, Section 3.4.2.2.d) before determining whether to revise NGE scales due to the changes. If the changes are determined to be material enough to warrant an update in anticipated experience factors, actuaries might analyze the change in the prospective profitability due to the change in anticipated experience factors (ASOP No. 2, Section 3.4.2.3.f).

Many actuaries would follow the guidance in ASOP No. 2, Section 3.4.2.3, to determine whether to revise NGE scales. Actuaries might also consider how the temporary changes relate to the deviations in emerging experience from what was assumed in prior determination of NGE scales.

An example of anticipated temporary changes could be Market Volatility driving hedging costs higher. In this case, some actuaries may consider changing the cap rates on indexed accounts to reflect the increase in hedging cost.

Q 7: Can an actuary use the same approach for determining NGEs for in-force as for new business?

Actuaries generally think there is significantly more flexibility for new business than for inforce with respect to the following:

- establishment or changes to policy classes
- setting of profit objectives
- selection of profit metrics
- designing the product
- the structure of the NGEs

However, contractual provisions may limit the flexibility of NGE determinations after issue.

Actuaries generally refer to the insurer's NGE framework, applicable law, and the guidance in the ASOPs, such as ASOP Nos. 2 and 12, when selecting the approach used for (1) establishing or changing policy classes and (2) the determination process for NGE scales. As a result, many actuaries would be influenced by different principles, objectives, methodologies, practices, criteria, or requirements in selecting the approaches used when providing actuarial services with respect to NGEs for new products and those used for in-force policies.

For example, with respect to policy classes for in-force policies, actuaries would generally look to the guidance in ASOP No. 2 on keeping policies assigned to their policy classes or reassigning them to new policy classes, as well as its guidance on combining or redefining policy classes. As another example, with respect to the determination of NGE scales for in-force policies, actuaries would generally look to the guidance in Section 3.4.2 of ASOP No. 2 on four distinct stages of the in-force policy determination process:

- reviewing prior determinations (including the original determination at policy issue)
- analyzing how actual experience for an in-force product is emerging relative to anticipated experience factors
- considering whether to recommend a revision to NGE scales
- determining revised NGE scales

Q 8: What are some examples of additional considerations mentioned in Section 3.4.2.5?

Many actuaries would consider whether anticipated experience factor assumptions need to be made with respect to policyholder choice factors such as partial withdrawal/loan utilization, premium funding for flexible premium policies, or utilization of nonforfeiture options such as reduced paid-up or extended term insurance for traditional policies. Many actuaries would also consider the insurer's determination policy in their reflection of any such additional policyholder choice factors.

Many actuaries would consider changes in profitability due to changes in factors such as policyholder choice factors (for example, average policy size, premium payment patterns, election of dividend options, utilization of policy distributions or living benefits) that were not anticipated or explicitly recognized as experience factors having a material effect within previous determinations to fall within the category of changes in additional factors. Some actuaries consider other previously unanticipated changes related to reserve and capital requirements, new forms of taxation or regulatory requirements, technological developments such as application of artificial intelligence to policy administration, or availability of new investment vehicles.

Q 9: In reviewing anticipated experience factors, when might an actuary consider sources of experience data outside of company experience?

When reviewing anticipated experience factors, many actuaries look to the NGE framework's methodology for evaluating experience and developing the anticipated experience factors. Many actuaries would consider the sources of data used in developing the existing anticipated experience factors, for example consideration of industry (including reinsurers and consultants) and population data. If the insurer's experience is not deemed credible or does not reflect recent emerging trends many actuaries would consider other sources of data.

Q 10: What do some actuaries consider when managing NGEs for products with riders that may impact the base policy?

Examples of what some actuaries consider when determining NGEs for products that have riders include:

1) whether the rider is automatic or elective
2) the contractual provisions
3) how assumptions are determined and how the product was priced
4) whether the rider materially affects the profitability
5) how the rider benefits interact with the base policy
6) whether there are different classes for policies with and without the rider
7) whether the rider has different experience factors

Q 5: If a policy issued by one company is fully reinsured to another company, which company should determine the NGEs?

Many actuaries would look to the language of the reinsurance treaty and supporting documentation to determine company responsibilities with respect to recommending NGEs.

Generally, the actuaries involved on behalf of the ceding company and reinsurer would confirm that NGEs are determined in compliance with ASOP No. 2.

Section 3.5 NGEs Used in Illustrations Not Subject to ASOP No. 24

Q 1: How do some actuaries determine whether the illustrated NGE scales, for products not subject to ASOP No. 24, can be supported by anticipated experience factors?

Depending upon the product design and how the illustrated NGE scales were determined, some actuaries use approaches such as:

- Profitability analysis
- Asset share/cash flow analysis
- Break-even analysis
- Scenario testing

Some actuaries may follow methods and standards similar to those in ASOP No. 24.