

# LIFE POST-NAIC UPDATE

## SPRING 2018 NATIONAL MEETING



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# Presenters

- **Moderator:** Dave Neve, MAAA, FSA, CERA  
Vice President, Life Practice Council
- **NAIC Update—Spring 2018**  
Mike Boerner, MAAA, ASA
- **Risk-Based Capital (RBC) Topics**  
Wayne Stuenkel, MAAA, FSA, CERA
- **Variable Annuity Issues**  
Tom Campbell, MAAA, FSA, CERA



# NAIC Update—Spring 2018

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# Topics

- ❑ 2017 PBR Activity
- ❑ Support for Regulators
- ❑ Life Insurance & Annuities (A) Committee Adoptions
- ❑ Life Actuarial Task Force (LATF) Spring Meeting:
  - ❑ Guaranteed Issue Mortality Table
  - ❑ VM-22—Fixed income annuity maximum valuation interest rates
  - ❑ VM-50 & VM-51 edits to reflect NAIC role
  - ❑ PBR Aggregation of Mortality Segments
  - ❑ VM-31 Phase 3
  - ❑ Model 805 Drafting Group
  - ❑ Other Spring meeting topics
- ❑ Selected Topics Anticipated for Calls Prior to Summer Meeting



# 2017 PBR Activity

- ❑ Early indications are about 20 companies who have applied PBR in 2017. As expected, most products involved are term products. However, there are a few applications of PBR for universal life with secondary guarantees (ULSG) products.
- ❑ The PBR reports are currently in the process of being requested for review by regulators.
- ❑ The Valuation Analysis (E ) Working Group (VAWG) will participate in the review of the PBR reports.
- ❑ VAWG will also participate with other regulators in the review of AG 51 memorandums.



# Support for Regulators

- The public VAWG website now has instructions to support regulators in their review of PBR and asset adequacy analysis. These instructions are copied below:

**NAIC Support** - Regulators can submit questions or request assistance from NAIC support staff relating to Principle-Based Reserves (PBR) or Asset Adequacy Analysis. Assistance that may be provided by NAIC support staff includes, but is not limited to: modeling of insurance cash flows to assist in conducting analysis and examinations; verification of PBR exclusion test calculations; and verification of the components of the PBR (Net Premium Reserve, Deterministic Reserve, Stochastic Reserve) on a sample of the company's contracts. Regulators can submit questions and requests for assistance to the NAIC support for the Valuation Analysis (E) Working Group (VAWG) at: [lbruning@naic.org](mailto:lbruning@naic.org) or [pallison@naic.org](mailto:pallison@naic.org).

**VAWG Support** - Regulators can also submit issues regarding PBR or Asset Adequacy Analysis directly to the VAWG. These submissions will typically relate to a significant concern regarding a PBR or Asset Adequacy Analysis review of a domestic company. However, there could be other reasons for a submission. To submit an issue to be discussed and addressed by the VAWG, regulators should complete the [submission form](#) and email the completed form to the NAIC support for the VAWG at: [lbruning@naic.org](mailto:lbruning@naic.org) or [pallison@naic.org](mailto:pallison@naic.org)



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# Life Insurance & Annuities (A) Committee Adoptions

- ❑ 16 Valuation Manual (VM) amendments were adopted by the A Committee at the Spring meeting.
- ❑ One of these amendments provides additional granularity in the table of the credibility percentages, which companies would use to determine when to grade to 100% of an industry table. The more granular table is found in VM-20, Section 9.C.6.b.iii and is required for valuations beginning in 2020.
- ❑ Other VM amendments adopted by the A Committee primarily relate to technical clarifications in VM-20. These amendments include clarification related to simplifications & approximations (Section 2G), collar language (Section 7D), and changing the references for underwriting criteria scoring (UCS) to refer instead to the Relative Risk Tool (Section 9C).
- ❑ The 17<sup>th</sup> amendment adopted by the A Committee relates to AG 42, which is referenced by the VM. This amendment contains AG 42 revisions that apply guidance for the use of the 2017 Commissioners' Standard Ordinary (CSO) Preferred Class Structure Mortality Table.



# Guaranteed Issue (GI) Mortality Table

- ❑ Mary Bahna-Nolan (Academy Life Experience Committee and Society of Actuaries Preferred Mortality Oversight Group – “Joint” Committee) discussed information requested by LATF to help determine GI table and level of loading. This information included the GI table developed by the Joint Committee with loads of 35%, 45%, 55%, and 75%. Information also included the reserves produced for a sampling of issue ages using these loaded tables.
- ❑ LATF exposed for a 30-day comment period the information for the various GI table loads and analysis provided by the Joint Committee comparing these tables alongside other tables including the 1980 CSO and the 2017 CSO. LATF also exposed for a 30-day comment period the amendment proposal form that would implement the GI table to be determined by LATF (APF 2018-01).





# Guaranteed Issue Mortality Table

- ❑ LATF will discuss this exposure and any comments on a call after the comment period ends. On that call, LATF may consider adoption of one of the exposed tables and the amendment proposal form to implement that table for GI.
- ❑ The exposed amendment proposal form provides that the selected GI table may be used for nonforfeiture and reserves for issues 1/1/19 through 12/31/2021. Otherwise the 2001 CSO ultimate table would be used. Beginning 1/1/2022 the selected GI table must be used for nonforfeiture and reserves.



# VM-22 – Fixed Income Annuity Maximum Valuation Interest Rates

- ❑ LATF exposed edits to VM-22 for a 30-day comment period ending May 3<sup>rd</sup> (APF 2018-20).
- ❑ These edits strive to provide greater clarity and be responsive to a number of questions that followed the adoption of VM-22 for the 2018 VM.
- ❑ In particular the edits add an original intent of VM-22, which expands its scope in Section 2.B.5 of the exposure. The cover page for the exposure discusses this expansion of scope to address potential reserve inadequacy for fixed payout annuities from host contracts issued prior to the VM-22 operative date. Comments are requested for this as well as for an alternative to address through an actuarial guideline.
- ❑ Note the exposure also invites any comments on VM-22 appendices, which are posted on the Industry tab of the NAIC website. These appendices are informational to inform how calculations are made to support the rates provided by VM-22.



# VM-50 & VM-51 Edits to Reflect NAIC Role

- ❑ LATF exposed for a 30-day comment period ending April 25<sup>th</sup> edits to VM-50 and to VM-51 to reflect the role of the NAIC as the Experience Reporting Agent. The exposed APFs for VM-50 & VM-51 are referenced as 2017-81 and 2018-19, respectively.
- ❑ The exposed edits to VM-50 address a number of comments made to the prior exposure for VM-50. Such edits include adding the role of the Health Actuarial Task Force (HATF), addressing the appropriate structure for agreements between the experience reporting agent and state insurance departments, and revisions to language regarding confidentiality and information sharing.
- ❑ Additional edits to both VM-50 and VM-51 follow a construct that VM-50 would include the roles and responsibilities of the NAIC whereas VM-51 would focus on the specific statistical data plan(s), which would include what business is to be reported and criteria for which companies to report.



# PBR Aggregation of Mortality Segments

- ❑ The American Academy of Actuaries' Life Reserves Work Group (LRWG) provided an amendment proposal form to assist companies in determining when experience from different mortality segments may be aggregated for purposes of PBR and credibility.
- ❑ LATF exposed this amendment for a comment period ending May 10, 2018. The amendment is referenced as APF 2018-17.
- ❑ Comments are encouraged on this exposure including whether there are any additional questions in need of address regarding mortality for PBR.
- ❑ LATF will discuss this exposure and any comments on a conference call prior to the Summer national meeting.



# VM-31 Phase 3

- ❑ An amendment proposal form for VM-31 was previously exposed for comment. The amendment proposal form provided Phase 3 edits for VM-31 to: 1) Clarify the VM-31 scope to more explicitly include VM-21 and VM-20 exclusion tests; 2) Provide additional clarity via rewording and/or reordering of requirements for consistency with VM-20; and 3) Provide other edits as needed including additional requirements deemed necessary by regulators.
- ❑ At the Spring meeting, LATF discussed additional edits proposed based on comments from the prior exposure. LATF re-exposed the amendment proposal form (2017-94) with these additional edits for a 21-day comment period ending on April 16<sup>th</sup>.
- ❑ LATF will consider any comments on this exposure on a call prior to the Summer national meeting.



# Model 805 Drafting Group

- ❑ Tomasz Serbinowski leads the Model 805 Drafting Group and discussed a proposed actuarial guideline intended to provide uniformity among states for product designs not anticipated at the time the prospective test was implemented in Model 805.
- ❑ Tomasz also provided a sample illustrating the proposed actuarial guideline methodology using a product with a premium bonus.
- ❑ LATF exposed this proposed actuarial guideline and the sample illustration for a 60-day comment period ending on May 28<sup>th</sup>. LATF will discuss comments received on a conference call prior to the Summer national meeting.



# Other LATF Spring Meeting Topics

- ❑ Simplified Issue Mortality
- ❑ Accelerated Underwriting
- ❑ Academy Annuity Reserves Work Group (ARWG) Update
- ❑ Academy SVL Interest Rate Modernization Work Group (IRMWG) Update
- ❑ LRWG presentation on VM-20 deterministic reserve considerations for Indexed Universal Life
- ❑ Impact of Tax Reform on Life PBR Exemption
- ❑ VM-20 Supplement Edits Submitted to Blanks
- ❑ Certificate of Valuation
- ❑ C-3 Phase II/AG43 (E/A) Subgroup



# Selected Topics Anticipated for Calls Prior to Summer Meeting

In addition to the exposures discussed in the preceding slides the following are some of the additional topics anticipated for calls prior to the Summer National meeting:

- ❑ APF 2017-70 relating to riders & supplemental benefits (VM-20 Section 2.A, VM-20 Section 3)
- ❑ APF for VM-26 relating to use of credibility for company experience and use of gender and smoker/nonsmoker tables for reserves.
- ❑ APF 2018-02 from the Academy Role of the Actuary Subgroup (ROAS)
- ❑ APF 2017-88 relating to UL policies with multiple secondary guarantees
- ❑ Academy Life Reinsurance Work Group YRT Issue





# Risk-Based Capital (RBC) Topics

Wayne Stuenkel, MAAA, FSA, CERA



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# RBC Topics

- Possible effect of tax reform on Life RBC
- National Association of Insurance Commissioners (NAIC) Investment RBC Working Group
- Other topics



# Tax Reform Effect on RBC

- Federal tax reform is effective for 2018
  - ▣ Corporate tax rate reduced from 35% to 21%
  - ▣ Several other provisions affecting life insurers
- Questions for regulators to answer
  - ▣ Change Authorized Control Level (ACL) RBC due to tax reform?
  - ▣ If so, what changes should be made, and when should changes be effective?



# Tax Reform Effect on RBC

- NAIC Life RBC compares two calculated items:
  - ▣ Total Adjusted Capital (TAC) is compared to—
  - ▣ ACL RBC
- Academy's letter focuses on possible changes to RBC factors within ACL RBC
- Additionally, TAC is affected in many ways by tax reform



# Tax Reform Effect on TAC

- TAC changes from tax reform (all in effect for 2018)
  - Tax rate changes from 35% to 21%
  - Tax reserve redefined; difference spread over 8 years
  - Deferred acquisition cost tax—higher capitalization rate, longer amortization period
  - Dividends received deduction changed
  - Deferred tax asset/liability revalued
  - Asset adequacy testing uses lower tax rate



# Should ACL RBC Be Changed?

- Underlying premises
  - ACL RBC estimates surplus needed for “stress” events
    - Examples of stress event—bond default, high mortality
  - In general, RBC factors were developed on a post-tax basis
    - Most life insurers are assumed to be profitable and pay taxes
    - When stress event happens, net surplus impact to insurer is cushioned by reduction in reported tax expense



# Should ACL RBC Be Changed?

- Because Life RBC is on a post-tax basis, there is solid logic to change LRBC factors as tax rates change
- Illustrative example
  - Assume a \$100 pre-tax “stress” event
  - At 35% tax rate, after-tax cost (and RBC) is \$65
  - Same event at 21% tax rate has after-tax cost of \$79
  - So ACL RBC should go up



# ACL RBC Effective Date Considerations

- Possible date to implement proposed changes
  - For 2018 RBC filings
  - For 2019 RBC filings
  - Some type of phase-in
- Effective date decision will take into account public policy considerations





# ACL RBC Change Date Considerations

- RBC factors should change as tax rates change
- “Discontinuities” in the trend of ACL RBC
  - Items that will likely raise ACL RBC
    - C-1 bond changes (targeting 2019)
    - RBC tax factor changes (date TBD)
  - Regulators should consider whether ACL RBC trend discontinuities should be focused in one year, or graded in



# ACL RBC Effective Date Considerations

- As ACL RBC rises, more companies could be flagged as “weakly capitalized”
  - Suggest deeper monitoring of insurers with low ratios of TAC to ACL RBC until RBC changes are fully made
- RBC “Trend Test” will need careful interpretation
- Tax items that impact TAC are generally effective in 2018



## Recommendations if ACL RBC Is Changed for Relevant Year \*

C-1 bonds	<b>For 2018 RBC filing –</b> <b>Multiply pre-tax RBC factors by 0.97</b> <b>Change tax factor to 0.1575 or 0.1680</b>  <b>For 2019+ RBC filing –</b> <b>Use IRBC-updated bond factors, recalculated with 21% tax rate</b> <b>Change tax factor to 0.1680</b>
C-1 other than bonds	Change 0.35 tax factors to 0.21 (for 2018 and 2019+ RBC filing) Change 0.2625 tax factors in line with C-1 bond tax factors



## Recommendations if ACL RBC Is Changed for Relevant Year \*

C-2 life insurance	<p><b>For 2018 RBC filing –</b> <b>Multiply pre-tax RBC factors by 0.97</b> <b>Change tax factor to 0.21</b></p> <p><b>For 2019+ RBC filing –</b> <b>Until underlying RBC factors are updated – same pre-tax RBC factor and tax factor changes as for 2018</b> <b>When underlying RBC factors are updated – use updated pre-tax RBC factor and tax factor of 0.21</b></p>
C-2 A&H	To be determined in consultation with the Academy's Health Solvency Subcommittee



## Recommendations if ACL RBC Is Changed for Relevant Year \*

C-3	<p>For all RBC filing years – Change pre-tax minimum factors to 0.0063, 0.0127, and 0.0253 Change tax factor to 0.21</p> <p>(Note that C-3 Phase 1 and C-3 Phase 2 calculations should use current tax rate)</p>
C-4	<p>For all RBC filing years – Change 0.35 tax factor to 0.21</p>



# Tax Reform – Recent Activity

- NAIC Life RBC has five conference calls to discuss how to proceed (Thursdays @ noon ET, started 3/29/18)
- To be effective for 2018 filings, any changes should be –
  - ▣ Exposed by 4/30/18 (limited extension possible)
  - ▣ Adopted by 6/30/18
- Life RBC Tax Reform WG letter to Life Risk-based Capital Working Group



# Investment RBC Activity



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# NAIC Investment RBC Working Group

- Objective—to update many Investment RBC factors, including bonds, to be effective for 2019 RBC filings
- At Milwaukee meeting
  - Requested NAIC staff to proceed with systems work necessary to expand bond categories from 6 to 20
  - Continued discussion of the treatment of bond exchange-traded funds (ETFs) in portfolio adjustment factor
- Discussion of exposed C-1 bond factors to continue on the level of credit risk assumed in statutory reserves





# Other Life RBC Topics

- Changes to 2018 Life RBC filings
  - Federal Home Loan Bank (FHLB) C-0 charge adopted
  - Operational Risk charge
- Report from Academy Longevity Risk Task Force to Life Actuarial Task Force (LATF) and Life RBC Working Group – proposing a field study to support the assumptions for mortality stress



# Variable Annuity Issues

NAIC Variable Annuities Issues Working Group (VAIWG) proposed changes to reserve and risk-based capital (RBC) requirements for VAs



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# VAIWG 2018 Charges (emphasis added)

- Oversee the NAIC's efforts to **study and address**, as appropriate, regulatory issues resulting in variable annuity **captive reinsurance transactions**
- Develop a model guideline that represents narrowly defined statutory language the states may use in **removing the limitations** that may exist within their **investment statutes** that may otherwise limit the extent of hedges an insurer may use in its risk management
- Consider **proposed changes** to the statutory framework designed to reduce the level and volatility of the **non-economic aspect** of current **reserve and risk-based capital (RBC) requirements** and refer to the C-3 Phase II/AG 43 (E/A) Subgroup once overall policy decisions are made and finalization of actual proposed changes are ready for consideration



# Progress to Date

- ❑ Most of 2017 spent on 2<sup>nd</sup> quantitative impact study
- ❑ December 5 exposures – AG 43 and C3P2
  - ❑ 28 recommendations
- ❑ Comments due March 2, 2018  
(see Academy AG43/C3 Phase II Work Group Comments)
- ❑ All-day meeting in Milwaukee on March 21



# Anything You [VM-20] Can Do. . .

- VM-20 economic scenario generator for interest rates
  - Proprietary generators to be considered by separate NAIC WG
- Remove Working Reserve in stochastic reserve calculation
- VM-20 spreads and defaults
  - Consistency with Asset Valuation Reserve (AVR) and RBC may need more discussion by other NAIC groups



# The Song Remains the Same

- Calibration criteria for equity funds
- Revenue Sharing
  - Affiliated vs. non-affiliated
  - Margins may change



# Money (Assets)

- Net asset earned rate (discount rate) based on “available assets”
  - ▣ Academy WG suggested it be based on approach used in modeling
  - ▣ Wording may be modified to clarify that this is allowed
- Starting Asset Amount
  - ▣ Flexibility with disclosure
  - ▣ Clarification that iterative approach is allowable
- Liquidate hedges for CTE Amount (adjusted)
- Lower minimum error (E) factor for hedging with back-testing
  - ▣ Updated formula



# Stop Right There. . .

- Treatment of hedges in CTE Amount calculation
  - Is clearly defined hedging strategy (CDHS) optional?
  - Is modeling hedges that meet CDHS criteria optional?





# Meet the New Boss. . .

- Proposed changes to Standard Scenario (SS)
  - Rebranded as Standard Projection (SP)
  - Align with CTE Amount (adjusted)
  - Aggregate calculation
  - Industry “average” assumptions
- Bigger issue is the role of the SS/SP
  - Floor reserve?
  - Disclosure / tool to review model assumptions?



# Coming Up

- Implied volatility assumptions
- RBC
  - C-3 calculation
  - Smoothing
- Disclosures
- VA Hedge accounting
- Allocation of final reserve



# Next Steps

- Additional face-to-face meeting (May 16 in Kansas City, MO)
- VAIWG to complete recommendations
- NAIC C-3 Phase II/AG 43 Subgroup will incorporate recommendations into potential revisions
  - ▣ Currently working in parallel
- Timing of final adoption – TBD
  - ▣ Note that both C-3 Phase II/AG 43 (E/A) Subgroup requirements apply to all inforce



# Questions?

