AMERICAN ACADEMY of ACTUARIES

September 15, 2026

Rachel Hemphill, Ph.D., MAAA, FSA, FCAS
Chair, Life Actuarial (A) Task Force (LATF)
National Association of Insurance Commissioners (NAIC)

Re: Life Actuarial (A) Task Force Request to Review VM Prescribed Spreads and Defaults Response Letter

Dear Chair Hemphill:

On behalf of the Life Practice Council of the American Academy of Actuaries[1], we appreciate the opportunity to provide an additional response to the Life Actuarial (A) Task Force (LATF) regarding the prescribed default and spread methodology in the Valuation Manual.

Regarding the overall framework, the prescribed default methodology is not intended to reproduce the exact aggregate loss distribution of a specific asset portfolio. Rather, it provides a practical and transparent approximation of moderately adverse default costs by applying factors calibrated to a 70 CTE (Conditional Tail Expectation) target for assets grouped by credit quality and Weighted Average Life (WAL). While explicit default correlation is not modeled, this omission is unlikely to materially undermine the suitability of the methodology for a reserve framework targeting moderately adverse conditions. Any gain from modeling correlation more explicitly would need to be weighed against the increased complexity, reduced transparency, and greater implementation burden of a portfolio credit model.

While this prescribed methodology serves as a practical baseline, we note a constraint regarding its application to reinvestment assets. Currently, for reinvestment assets, VM-20 requires the actuary to use prescribed gross spreads over treasuries when modeling purchases of public non-callable corporate bonds, as the prescribed spreads are developed from public non-callable corporate bond experience data. VM-20 also permits the actuary to use professional judgment to set assumed gross spreads for other fixed income assets in a manner that is consistent with, and results in reasonable relationships to, the prescribed spreads for public non-callable corporate bonds (Section 7.E.1.f).

However, the discretion to modify the prescribed assumptions for reinvestment assets only applies to spreads. The actuary must use the prescribed default costs for all types of fixed income assets, even though the prescribed default costs were developed only using experience data from public non-callable corporate bonds.

Therefore, we suggest that LATF consider amending VM-20 to permit the actuary to use professional judgment to set assumptions for default costs on fixed income assets other than public non-callable corporate bonds. Allowing this flexibility, similar to what is already permitted for spreads, would

[1]The American Academy of Actuaries is a 20,000-member professional association whose mission is to serve the public and the U.S. actuarial profession. For 60 years, the Academy has assisted public policymakers on all levels by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States.

maintain internal consistency within VM-20 and recognize that default data derived strictly from public corporate bonds may not appropriately reflect the distinct risk profiles of other asset classes.

We thank LATF for the opportunity to provide these observations and look forward to further discussions. If there are any questions or if you would like to discuss this response further, please contact Marie Fabienne Amisial, the Academy's life policy project manager (amisial@actuary.org).

Sincerely,

Kirsten Pedersen, MAAA, FSA
Vice President, Life Practice Council