

2009 Winter National Meeting
San Francisco, CA

**PRINCIPLES-BASED RESERVING (EX) WORKING GROUP
OF THE SOLVENCY MODERNIZATION INITIATIVE (EX) TASK FORCE**
Saturday, Dec. 5, 2009
11:30 a.m.—12:30 p.m.
Grand Salon A—Grand Ballroom Level

ROLL CALL

North Dakota, Chair	California	Kentucky	Oregon
Iowa, Vice Chair	Connecticut	Nebraska	Pennsylvania
Alabama	District of Columbia	New Hampshire	Utah
Alaska	Florida	New York	Virginia
Arkansas	Kansas	Ohio	

AGENDA

1. **Adopt July 8, 2009 Interim Minutes – Commissioner Hamm (ND)** *Attachment One*
2. **Status Reports**
 - o LHMATF – Valuation Manual – *Larry Bruning (KS)*
3. **Review Comments on Draft Memo to Membership – Commissioner Hamm (ND)** *Attachment Two*
 - o Commissioner Michie (UT) *Attachment Two-A*
 - o State Farm *Attachment Two-B*
 - o ACLI *Attachment Two-C*
4. Any Other Matters Brought Before the Working Group

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Draft: 7/30/09

Principles-Based Reserving (EX) Working Group
Conference Call
July 8, 2009

The Principles-Based Reserving (EX) Working Group of the Solvency Modernization Initiative (EX) Task Force met July 8, 2009. The following Working Group members participated: Thomas E. Hampton, Chair (DC); Susan Voss, Vice Chair (IA); Steven Ostlund (AL); Joe Musgrove (AR); Sheldon Summers (CA); Thomas Sullivan (CT); Al Willis (FL); Larry Bruning (KS); John Rink (NE); Lou Felice (NY); Mike Fix (ND); Mary Miller (OH); Dave DelBiondo (PA); Jake Garn (UT); and David Smith (VA).

1. Review Comments Received On Exposed Corporate Governance Document

Commissioner Hampton announced that the purpose of the call was to consider comments received from the four parties that submitted comments: Affordable Life Insurance Alliance (ALIA) (Attachment XX-A1), America's Health Insurance Plans (AHIP) (Attachment XX-A2), American Council of Life Insurers (ACLI) (Attachment XX-A3), American Academy of Actuaries (AAA) (Attachment XX-A4), and as incorporated into a summary document (Attachment XX-A5). Commissioner Hampton explained that the NAIC had suggested that the language proposed in many of the comments be accepted, and he did not intend to address those comments, but rather focus on the remaining, more significant, comments.

a) Oral Editorial Comment — Principle-Based Reserving

Paul Graham (ACLI) indicated that the Life and Health Actuarial Task Force adopted a change to all of its documents approximately one year ago wherein they now utilize the singular use of the word “principle” in the context of principle-based reserving. He requested the Working Group consider making a similar change in this document. The Working Group agreed and charged NAIC staff with incorporating that change into the document.

b) Comments #1, 2, 3, 12, 22, 25, 27, 30, 33, 37, 39, 46, 53

Mr. Graham summarized that these comments, and the associated proposed language changes, are intended to bring consistency between the document and the NAIC Annual Financial Reporting Model Regulation (#205), as well as address how boards might be structured differently from company to company. Dan Daveline (NAIC) requested clarification from Mr. Graham on whether the language was intended to modify which entity provides the annual certification of internal controls under the revised Standard Valuation Law (#820). Mr. Graham responded that the annual certification required by the Standard Valuation Law must be provided at the individual insurer, noting that if the group had 35 insurers, 35 certifications would be required. Mr. Musgrove noted that the language proposed by the ACLI for this document seems to only be indicating where such reports would be delivered. Mr. Bruning noted that the Standard Valuation Law did not define “insurer,” and suggested the Working Group consider revising the term “insurer” to “insurance companies.” Commissioner Hampton indicated his support for the change proposed by the ACLI, as modified by Mr. Bruning. A motion was made by Ms. Miller to adopt the language proposed within these comments and as modified. The motion was seconded by Commissioner Voss and unanimously adopted.

c) Comment #7

Mr. Graham suggested the Working Group remove the word “generally” from the last part of paragraph two. He explained how the word adds ambiguities that could increase legal liability for the board of directors and the senior management. A motion was made by Commissioner Voss to remove the word “generally,” as suggested by the ACLI in the comment. The motion was seconded by Ms. Miller and unanimously adopted.

d) Comment #9

Randi Reichel (Reichel Consulting, representing AHIP) discussed how this comment and its proposed language was intended to address the fact that some insurers might have a relatively small amount of business that is subject to principle-based reserving. She discussed that in these cases it could result in significant changes to the non-PBR process. Commissioner Hampton stated that he believed management needed to be aware of all such processes, and questioned whether the change should only be made to the board of directors. Ms. Reichel did not disagree that senior management should be responsible for all of the reserves of the company, but noted that she did not believe that an insurer's risk processes should change when the reserves are immaterial. Mr. Felice stated that he believed the issue of materiality was beyond the scope of this paper. He explained that it might be necessary to work on that issue somewhere within this project, but not within this paper. After further discussion between Ms. Reichel and Mr. Felice, Ms. Miller stated that she was opposed to the language proposed by AHIP, because for some companies it is expected that the product would become material, and she was concerned with the determination of when that would occur. A motion was made by Mr. Ostlund to reject the proposed change included in this comment. The motion was seconded by Mr. Bruning and unanimously adopted.

e) Comments #13, 21, 69

Ms. Reichel explained that excluding materiality from paragraph three does not allow the concept to be considered between an insurer and a regulator. Commissioner Hampton suggested Ms. Reichel consider the inclusion of the language being proposed in paragraph four only, because that deals with the board of directors. After further discussion, Mr. Musgrove made a motion to accept the language proposed in paragraph four, but reject the materiality language proposed elsewhere within the document. The motion was seconded by Mr. Felice and unanimously adopted.

f) Comments #16, 18, 49

Ms. Reichel discussed how she believed it was appropriate for this document to allow the insurer to determine how often they need to receive reports. Mr. Ostlund agreed, but noted that adding the word "periodically" might create a greater requirement for the board of directors. Mr. Felice agreed, but noted that the concept included in this sentence speaks to the issue of materiality. He discussed how if the insurer can articulate the process they use to address the issue, then that is what regulators would consider. Mr. Ostlund made a motion to reject the proposed change to add the word "periodically" to the document, as proposed by AHIP. The motion was seconded by Ms. Miller and unanimously adopted.

g) Comment #23

Ms. Reichel explained that this comment suggested removing paragraph 4i, as the idea is already expressed within the main paragraph and did not add value and might cause confusion. A motion was made by Mr. Musgrove to delete paragraph 4i, as suggested in the comment. The motion was seconded by Commissioner Voss and unanimously adopted.

h) Comments #28, 31

Ms. Reichel discussed how requiring consistency across products was not appropriate for this document, because it "shoehorns" the treatment of products into a specific treatment. Mr. Felice noted that he was sympathetic to this comment relative to the board of directors, but believed the concept should be retained in some form in the senior management section. Kalman Ketzlach (AAA) discussed how they proposed the language be retained, but modified and included in paragraph five for senior management. A motion was made by Ms. Miller to delete this language in paragraph four, as proposed by AHIP in comment #28. The motion was seconded by Mr. Bruning and unanimously adopted.

Commissioner Hampton asked for comments from the Working Group regarding comment #31. Mr. Felice responded that he thought the proposed language addition was appropriate, but he would prefer to replace "recognizing potential differences" with "identifying and documenting potential differences." Mr. Bruning noted the point, and stated that the language used is to identify the language used in the Standard Valuation Law. He discussed what the Life and Health Actuarial Task Force was considering when including that language was the difference between statutory accounting principles and generally accepted accounting principles. Mr. Graham indicated that the Valuation Manual requires identification and disclosure by the actuary, as opposed to senior management. Mr. Felice explained that it needs to be clear why there is a disconnect between this

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feature and some other feature, and expressed his concerns with it not being a responsibility of senior management. Mr. Musgrove stated that he believed “recognizing” was strong enough. Mr. Ostlund questioned whether anything after “assessment processes” was needed. Mr. Ketzlach explained why he thought that language was necessary, because it might require the same processes to be used in places where it is not needed. A motion was made by Mr. Musgrove to accept the language proposed by the AAA in comment #31. The motion was seconded by Mr. Bruning and adopted, with New York abstaining.

i) Comments #32, 34, 35

Ms. Reichel discussed how the suggestion to remove “established risk tolerances” was suggested, because it was removed from the remainder of the document. She discussed how risk tolerances were an enterprise risk-management concept, but not a reserve concept. Mr. Felice disagreed, noting that New York believes this is an important part of the document. Mr. Graham noted that he believed the concept of this language was to suggest that if the insurer has a risk tolerance at a specific level, which results in reinsurance at that level, then that should be consistent with the models used to develop the reserves. Mr. Graham noted that there is no requirement to regulate the tolerance itself. Mr. Felice agreed. A motion was made by Mr. Felice to retain the words “risk tolerances” in paragraph 5iii and reject the change proposed in comments #32 and 34. The motion was seconded by Mr. Ostlund and unanimously adopted.

j) Comment #41

Scott Harrison (ALIA) discussed that this was a different materiality issue, particularly when using it in the context of understatement of reserves and a bright line test was not appropriate. Mr. Felice agreed, but noted the language pertains to whether the model produces a bias toward something, and not materiality of the liability itself. Mr. Musgrove noted that any model that produces a bias toward under-reserving is a material error. A motion was made by Mr. Ostlund to reject the comment, and, therefore, not add the word “material” to paragraph 7ii as proposed. The motion was seconded by Ms. Miller and unanimously adopted.

k) Comment #44

Mr. Graham noted that the proposed deletion of this sentence was because the sentence is out of place. He discussed how the burden of proof was on the insurer, and not senior management, and is already required of the insurer in the Standard Valuation Law. Mr. Musgrove agreed that it was not a requirement of senior management. A motion was made by Mr. Musgrove to accept the comment and, therefore, remove this sentence of paragraph 7ii. The motion was seconded by Ms. Miller and adopted, with New York abstaining.

l) Comment #59

Mr. Ketzlach discussed how the changes in this paragraph distinguish those between the appointed actuary and those of any other qualified actuary assigned by the insurer. A motion was made by Mr. Musgrove to accept the language proposed by the AAA in comment #59. The motion was seconded by Mr. Bruning and unanimously adopted.

m) Comment #61

Mr. Graham noted that, given the changes made by the document to distinguish between the appointed actuary and the qualified actuaries, this comment could be withdrawn. The Working Group agreed that no change was needed to address this comment.

n) Unwritten Comments

Mr. Bruning suggested adding the word “qualified” before actuaries, in the heading of Section IV. Mr. Bruning also suggested deleting paragraph nine, because the text in that paragraph is either self-evident or described elsewhere within the document. A motion was made by Mr. Bruning to adopt the changes proposed. The motion was seconded by Mr. Ostlund and unanimously adopted.

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o) Other Written Comments Received

A motion was made by Mr. Ostlund to accept the other comments as suggested by NAIC staff, provided they were consistent with the other decisions made by the Working Group. The motion was seconded by Ms. Miller and unanimously adopted.

2. Next Steps

Commissioner Hampton proposed that the document be exposed to allow one more review by the Working Group and interested parties in order to address any concerns that the industry has with the document. He noted that in doing so, it would allow the Working Group to record that the document adequately addressed all comments. A motion was made by Mr. Ostlund to charge NAIC staff with modifying the document as discussed during the meeting and exposing the document for 30 days once it was approved by the chair. The motion was seconded by Mr. Felice and unanimously adopted.

Having no further business, the Principles-Based Reserving (EX) Working Group adjourned.

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To: Executive (EX) Committee
From: Commissioner Adam Hamm (ND), Chair of the Principles-Based Reserving (EX) WG
Date: TBD
Re: Statistical Agent Process

As you are aware, the revised NAIC Standard Valuation Law (Model 820) provides the legal authority for principle-based reserving to be utilized by life insurers. For those of you who are less familiar with the project, you should understand that one of the most critical aspects of regulators' decision to move to principle-based reserving for life and annuity products was the understanding that regulators would be provided with periodic reporting on insurers' experience. Because of that, included in the Standard Valuation Law is a requirement that a company shall submit mortality, morbidity, policyholder behavior, or expense experience and other data as prescribed in the Valuation Manual. The Life and Health Actuarial Task Force has drafted VM-50 *Experience Reporting Requirements* (VM-50) to address these requirements, which require companies to file statistics with state insurance departments, either through a statistical agent, the NAIC, or directly to the department. VM-50 includes specific discussion of the roles and responsibilities of the statistical agent, NAIC task forces/working groups, and actuarial professional organizations. VM-50 also includes a discussion of data quality, access rights, and confidentiality of experience data. It should be noted that VM-50 has not yet been completed, in part because the Life and Health Actuarial Task Force is still trying to determine the most appropriate mechanism for the collection, analysis and storage of this data. The current draft of VM-50 contemplates various means in which this process could be performed.

The purpose of this letter is to request specific direction from the NAIC membership on how the NAIC process should be set forth. More specifically, the Principles-Based Reserving (EX) Working Group hereby requests input on whether the NAIC should serve as the statistical agent for the principle-based reserving needs. The Principles-Based Reserving (EX) Working Group believes it may be appropriate for the NAIC to be considered as a statistical agent, and it should be noted that the Working Group has drafted the attached criteria, which it feels may be appropriate for this function. The Principles-Based Reserving (EX) Working Group believes that regardless of whether the NAIC is considered or determined to be a statistical agent, it would be appropriate for the NAIC to serve as an agent for the states by being the central collection point for all statistical data that is provided to the states. Thus, in the event the NAIC is not the statistical agent, all data on experience reporting should be submitted from the statistical agents to the NAIC, and made available to states via an NAIC system. The NAIC should determine the costs associated with serving in this capacity and determine if any new model laws are needed to provide the specific authority it needs to act as this agent and keep any information confidential.

Please don't hesitate to call me if you have any questions.

EXECUTIVE OFFICE	444 N. Capitol Street, NW, Suite 701	Washington, DC 20001-1509	p 202 471 3990	f 816 460 7493
CENTRAL OFFICE	2301 McGee Street, Suite 800	Kansas City, MO 64108-2662	p 816 842 3600	f 816 783 8175
SECURITIES VALUATION OFFICE	48 Wall Street, 6th Floor	New York, NY 10005-2906	p 212 398 9000	f 212 382 4207

Attachment Two-A

----- Original Message -----

From: Michie, Kent
To: Daveline, Dan
Cc: Sullivan, Thomas; Sevigny, Roger A.; Beal, Andrew; Serbinowski, Tomasz; Cline, Jane
Sent: Thu Sep 24 17:44:12 2009
Subject: Re: PBR EX Working Group-Comments Due November 9th, 2009

Dan:

I believe that the data collection should be specified by LHATF and collected under the governmental authority of the states. It should be shipped to a central collection spot in Kansas City at the NAIC. The Executive Committee should task the COO (Andy Beal) to make a recommendation as to how the data can be aggregated, stored and made available for access by LHATF and other appropriate and authorized groups along with an analysis of the cost of collection, storage and convenient accessing.

All the best

State Farm®
Providing Insurance and Financial Services
Home Office, Bloomington, Illinois 61710



Attachment Two-B

Corporate Headquarters
One State Farm Plaza
Bloomington, Illinois 61710-0001

November 2, 2009

Mr. Dan Daveline
NAIC
2301 McGee Street
Kansas City, MO 64108

VIA EMAIL

Re: PBR EX Working Group – Statistical Agent Process

Dear Mr. Daveline:

State Farm appreciates the opportunity to comment on whether the NAIC should serve as the statistical agent for the principle-based reserving needs. We would like to offer the following observations regarding this consideration:

1. It would be appropriate for the NAIC to serve as the keeper and distributor of the compiled experience data/studies because of its experience in collecting data and providing resources that all member insurers can access.
2. We encourage having a “statistical agent/agents” selected from those groups who have past experience in collecting, analyzing, and reporting experience data submitted by insurers in an unbiased manner, organizations who have built a reputation for maintaining confidentiality, professionalism and have expertise required for the analysis, such as LIMRA, SOA, or LOMA.

Thank you for considering our comments.

Sincerely,

A handwritten signature in black ink that reads "Julie M. Kirby".

Julie M. Kirby, CPA, CPCU, CLU, ChFC, FLMI
Finance Director – Office of Accounting Policy
State Farm



John Bruins
Senior Actuary
202.624.2169 t
866. 953.4097 f
johnbruins@acli.com

November 9, 2009

The Honorable Adam Hamm
Chair, NAIC Principles-Based Reserves (EX) WG
Commissioner
North Dakota Insurance Department
600 E. Boulevard Avenue, Dept. 401
Bismarck, North Dakota 58505-0320

Re Draft Letter re Statistical Agent Process

Commissioner Hamm

The ACLI is pleased to submit the following comments regarding the exposed letter to the Executive Committee regarding Statistical Agent Process on behalf of our member companies. The American Council of Life Insurers represents 340 member companies operating in the United States, of which 332 are legal reserve life insurance companies, and 8 are fraternal benefit societies. These 340 member companies account for 93% of total life insurance company assets, 94% of the life insurance premiums, and 94% of annuity considerations in the United States.

ACLI recommends that changes be made to this letter both in the background as well as in the questions posed.

The letter starts with the premise that the data collection was for the purpose of tracking individual company experience. In fact, data collection was proposed for the purpose of developing industry level experience reports. Companies do their own internal studies, and provide documentation of company experience with the required PBR documentation. The most efficient way for regulators to assess the appropriateness of company assumptions is to understand the industry overall experience, and to have the company demonstrate how their experience might differ from that average. As a result, other than in the initial steps of validating the data submitted, there would be no reason to store data with a company identifier since its primary purpose is for industry level experience. Such data becomes less relevant to the regulators as many companies would not submit data for such a study. In order to provide valid industry studies, data needs to be collected generally from enough companies to represent 75 % of the

industry, which in most cases is a small percentage of the companies. Creating a database for the purpose of validating individual company information would be a very expensive exercise and would not be appropriate.

From ACLI's perspective, there are several important issues with the data collection project. First, expense needs to be controlled. This is an area which can become very expensive very quickly, even while providing little value. There may be a role for the NAIC to play helping in helping to select or coordinate statistical agents to reduce duplication and so that companies who contribute need to do so only once for any given experience study.

Second, we support a competitive process for determining statistical agent for at least two reasons – the competition helps to manage the expense levels, and that competition fosters quality of process.

Thirdly, data must be kept confidential. By this we mean that no one other than the company should be able to see either individual data, or data that represents the experience of the company and identifiable to the company. Storing data with company identifiers makes compliance with the confidentiality provisions of the SVL difficult to maintain.

It is also important to note that there are numerous firms that specialize in the collection and processing of large volumes of data. It would take time and money for the NAIC to build a comparable level of expertise. For these reasons, we do not believe that the NAIC should serve as the statistical agent or as the collector of data, nor should a data warehouse be established either at the NAIC or at the statistical agent for any purpose other than long term industry trends..

We look forward to resolving the issues that will allow development of better industry experience studies in support of the implementation of Principle-Based Reserves for life insurance.

A handwritten signature in black ink, appearing to read "John P. Bruen".

cc Dan Daveline, NAIC



National Association of Insurance Commissioners

To: Executive (EX) Committee
From: Commissioner Adam Hamm (ND), Chair of the Principles-Based Reserving (EX) WG
Date: TBD
Re: Statistical Agent Process

As you are aware, the revised NAIC Standard Valuation Law (Model 820) provides the legal authority for principle-based reserving to be utilized by life insurers. For those of you who are less familiar with the project, you should understand that one of the ~~most critical~~key aspects of regulators' decision to move to principle-based reserving for life and annuity products was the understanding that ~~regulators would be provided with periodic industry-level studies of reporting on~~ insurers' experience ~~would be done as a basis of validating assumptions used in the reserve process.~~ Because of that, included in the Standard Valuation Law is ~~the ability for commissioners to~~ a requirement that a company ~~shall~~ submit mortality, morbidity, policyholder behavior, or expense experience and other data as prescribed in the Valuation Manual. The Life and Health Actuarial Task Force has drafted VM-50 *Experience Reporting Requirements* (VM-50) to address these requirements, which require companies to ~~submit experience~~ file statistics with state insurance departments, either through a statistical agent, ~~the NAIC, or directly to the department.~~ VM-50 includes specific discussion of the roles and responsibilities of the statistical agent, NAIC task forces/working groups, and actuarial professional organizations. VM-50 also includes a discussion of data quality, access rights, and confidentiality of experience data. It should be noted that VM-50 has not yet been completed, in part because the Life and Health Actuarial Task Force is still trying to determine the most appropriate mechanism for the collection and, analysis and storage of this data. The current draft of VM-50 contemplates various means in which this process could be performed.

A critical issue to this collection is the need to streamline the process by having companies who submit data do so only once for any given set of data, and for the industry data to be consolidated to provide an industry-level experience analysis. The purpose of this letter is to request specific direction from the NAIC membership on how the NAIC might enhance this process ~~should be set forth~~. More specifically, the Principles-Based Reserving (EX) Working Group hereby requests input on the following questions:

- How should the statistical agent for PBR Experience studies be established? Some possibilities include:
 - whether t~~The NAIC sh~~ould serve as the statistical agent, ~~for the principle-based reserving needs.~~
The Principles-Based Reserving (EX) Working Group believes it may be appropriate for the NAIC to be considered as a statistical agent, ~~and it should be noted that the Working Group has drafted the attached criteria, which it feels may be appropriate for this function.~~
 - The NAIC could serve in a role on behalf of the states to identify appropriate statistical agents to serve for any given experience study.
 - The NAIC could serve in a role on behalf of the states to contract with appropriate statistical agents to serve for any given experience study.
 - It should be noted that the Working Group has drafted the attached criteria, which it feels may be appropriate for this function.
- The Principles Based Reserving (EX) Working Group believes that regardless of whether~~Should~~ the NAIC establish a database to ~~is considered or determined to be a statistical agent, it would be appropriate for the NAIC to serve as a repository for experience data that is submitted from the statistical agents to the NAIC?~~ an agent for the states by being the central collection point for all statistical data that is provided to the states. Thus, in the event the NAIC is not the statistical agent, all data on experience reporting should be submitted from the statistical agents to the NAIC, and made available to states via an NAIC system. What value would this data-base provide to the regulators if analytical reports are already developed? We note that LHATF has concluded that regulators are best served getting the company information directly from the companies.

Further, in order to ensure the success of this project:

- The NAIC should determine the costs associated with serving in any of the above~~this~~ these capacities.
- The NAIC should ~~and~~ determine if any new model laws are needed to provide the specific authority it needs to act as any of these roles. this agent and keep any information confidential.

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Please don't hesitate to call me if you have any questions.

DRAFT