ACLI
Financial Security for Life

Brian Bayerle
Senior Actuary

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Mr. Mike Boerner
Chair, NAIC Life Actuarial Task Force (LATF)

Mr. Fred Andersen
Chief Life Actuary, Minnesota Department of Commerce

Re: March Exposure of Actuarial Guideline Asset Adequacy Testing

Dear Messrs. Boerner and Andersen:

The American Council of Life Insurers (ACLI) appreciates the opportunity to submit the following comments on the March 31st exposure of Actuarial Guideline on Asset Adequacy Testing (AAT, collectively Guideline). Our comments will elaborate on some prior comments but will generally focus on the sensitivity testing.

Scope of the assets:
Reiterating our prior letter, we recommend removing the following asset types from the scope of the Guideline:

- Insulated Separate Accounts
- "Vanilla" Bonds (default risk is primary risk, and cashflows are predictable)
- Direct Mortgage Loans (Commercial, Agricultural, Residential)
- Real Estate
- Mortgage Pass-Through Securities (not complex Mortgage-Backed Securities)

We wanted to elaborate on the rationale for this reduction in scope. The stated asset classes and their associated risks are well understood by both companies and regulators. Further, inclusion of such assets takes attention away from the assets of concern to regulators and creates significant work for companies that does not appear to provide any insights to regulators.

Sensitivity Testing:
While the Guideline addresses important concerns, industry believes some materials (potentially sensitivities, attribution, and template) should be allowed to be provided after the Opinion is submitted. Preparing these materials will take significant time, and it should not interfere with the normal process of development and submission of the Opinion. Allowing additional time to provide

The American Council of Life Insurers (ACLI) is the leading trade association driving public policy and advocacy on behalf of the life insurance industry. 90 million American families rely on the life insurance industry for financial protection and retirement security. ACLI's member companies are dedicated to protecting consumers' financial wellbeing through life insurance, annuities, retirement plans, long-term care insurance, disability income insurance, reinsurance, and dental, vision and other supplemental benefits. ACLI's 280 member companies represent 94 percent of industry assets in the United States.

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these materials will hopefully improve the quality of what is submitted and foster dynamic conversations between the domestic regulator and their companies.

Regarding the sensitivity tests, we believe that common stock, real estate (were it to be in scope) and other equity-oriented assets should be sensitivity tested separately from Bonds. ACLI supports applicability to reinvested assets only and apply only the level scenario for fixed income; this approach would reduce the complexity of the sensitivity and still allow for meaningful insights into the concerns around these assets.

ACLI also would support exemption from the sensitivity test for companies that have demonstrated adequate sufficiency in a more conservative scenario (e.g., the equity sensitivity if performing the CA equity scenario).

We have the following comments regarding the sensitivities, separated between bond and non-bond sensitivities:

Bond sensitivities:

- ACLI would support a NY-style benchmark spread approach applicable for reinvestment assets rather than a benchmark yield approach. Such an approach is operationally easier.
- ACLI suggests 3 consistent sensitivities across companies – benchmark spread, benchmark spread [+50], benchmark spread [+150].
- Perform the capping of future reinvestment yields at the level of aggregation used in the asset adequacy analysis model (rather than applying seriatim).

Non-bond sensitivities:

- ACLI suggests a simple equity sensitivity, which ACLI is still contemplating and will provide suggestions at a future date.

Attribution Analysis:

- Attribution is an open and challenging investment problem: how to attribute excess yield into different components. As far as we know, there is no agreed and defendable approach, either from academia or Wall Street, to achieve such attribution. The components of excess yield could include real (credit convexity) or perceived (new asset classes) credit risks, liquidity risk, product complexity, operational risk (uncertainty on future realized CFs vs initial expectations), etc. Even if we use some subjective way to do certain attribution, it is unclear how the final work product would be used.
- 2022 attributions may be more qualitative vs quantitative in nature; credit may be easier to quantify; other components (illiquidity, complexity, etc.) may need to be qualitative. 2022 requirements should let companies decide how to best do the attribution, acknowledging this approach would not have consistency between companies.
- We recommend revisiting the attribution analysis after the first year and periodically thereafter in order to confirm that it is providing regulatory value. In any case, year 1 should be on a “best efforts” basis as this will be a challenging exercise.

Template:

- It would be beneficial to develop instructions to assist in the population of the template. Specifically, the instructions should address definitions (and how to separate equity-like assets from Schedule BA assets)
- Our preference would be that the template only include those assets that are in scope and have yields in excess of the benchmark. Companies could provide a column (by categories) showing all assets; a column showing the assets included in the analysis; and a column

that is a subset of the assets included in the analysis column with the assets in scope of the Guideline.

- ‘Asset Summary’: “Amount” maybe more appropriate than “count”. Asset Counts might double count due to how assets are allocated to portfolios. Is there a standardized mapping around “asset type” from the blue books? Otherwise, allocation may be arbitrary. This could potentially be addressed in instructions.
- “Asset Yields – Initial Assets”: Suggest removing max gross/net yield since mostly will reflect the rate environment when things were purchased vs. any risk signaling. Further, some companies may have loss assumptions at the collateral level rather than bond level, which may create situations in which investments appear to have “0 defaults”.
- “Asset Yields – Reinvestments”: It is not clear why this should have the same level of specificity as initial assets. We would suggest, if there is a “cap spread” concept, simplifying this approach to be more similar to how it’s generally done today (a blended rate from VM-20/VM-21 spreads).
- “Sensitivity Test”: “Amount” may be more appropriate than “count”. This approach may not properly capture the rate environment in which the business being backed was written (e.g. it is more punitive for high yields stemming from high interest rate environment). Codifying this approach may lead to non-economically justified investment behaviors.
- “Attribution Initial Assets”: The current version seems reliant on how assets were bucketed. If we want to have market vs market approach, the key categories to focus on are 1) credit risk, 2) illiquidity risk, and 3) prepayment risk.
- “Attribution – Reinvestment Assets”: Not clear why this should have the same level of specificity as initial assets.

ACLI is appreciative of your consideration of our comments and looks forward to a future discussion.

Thank you for your consideration,

cc: Reggie Mazyck, NAIC