

Dates: Received	Reviewed by Staff	Distributed	Considered
11/18/22, updated 12/14	SO		
APF 2022-07			

Life Actuarial (A) Task Force/ Health Actuarial (B) Task Force
Amendment Proposal Form

1. Identify yourself, your affiliation and a very brief description (title) of the issue.

Brian Bayerle, ACLI – Clarification of adjustments to mortality for policies subject to the NPR and for policies that pass the Life PBR Exemption when anticipated experience exceeds the prescribed CSO table.

2. Identify the document, including the date if the document is “released for comment,” and the location in the document where the amendment is proposed:

Valuation Manual (January 1, 2022 edition), VM-20 Section 3.C.1.g, VM-20 Section 6.B.5.d.

3. Show what changes are needed by providing a red-line version of the original verbiage with deletions and identify the verbiage to be deleted, inserted or changed by providing a red-line (turn on “track changes” in Word®) version of the verbiage. (You may do this through an attachment.)

See attached.

12/14/22 Update: The redline indicates changes from the Valuation Manual. Redline sections that are highlighted indicate changes from the previous 9/8/22 exposure. Some deletions of text that was added in the 9/8/22 version but deleted in the 12/14/22 exposure were not included in the redline below, including the removal of mortality rate capping language from sections 3.C.1.g.i and 3.C.1.g.ii and replacement into section 3.C.1.g.ii.a and the deletion of references to “FUW” policies in the guidance note.

4. State the reason for the proposed amendment? (You may do this through an attachment.)

The purpose of this proposed amendment is to clarify the intent and calculation of the mortality adjustments to the CSO table when anticipated mortality exceeds the prescribed CSO table. The current wording of Section 3.C.1.g has led to confusion by many and a lack of consistent interpretations. The APF does not change the current requirements of VM-20, it only provides clarification. This APF revises the edits made by APF 2018-57.

There are five questions the APF is trying to answer:

1. **What policies are intended to be addressed by Section 3.C.1.g?**

The primary intent of Section 3.C.1.g is to address the higher anticipated mortality for policies that are not subject to full underwriting (FUW), such as simplified issue policies and final expense policies. It is typical for these types of policies to have mortality experience worse than the CSO table, and thus, an adjustment is necessary.

The intent of Section 3.C.1.g is not to test every possible FUW subset (e.g., attained age blocks, individual underwriting classes with lower credibility, etc.) to determine if its mortality experience is higher than the CSO table even though more aggregate mortality experience is lower than the CSO table. However, if a large, credible block or subset of FUW policies (e.g., a block of FUW business assumed from another company that has significantly different mortality experience than the rest of the assuming company’s FUW business, or a large block of business from an era when the company had significantly more permissive underwriting, etc.) is expected to have worse experience than the CSO table, then the adjustments in 3.C.1.g should be made.

A guidance note has been added following Section 3.C.1.g. to provide this clarification.

2. What is meant by the current language in Section 3.C.1.g that the “adjustments should be consistent with the adjustments made for the DET Net Premium test” in Section 6.B.5.d?

This wording has led to a lot of confusion. Some have interpreted this wording to mean that the adjustment factors should be the same as those defined in Section 6.B.5.d. Others have concluded that this means the form of the adjustments should be the same. Others have concluded that this means the same methodology should be used to determine the adjustments. And if the company does not elect to use the DET, there are no adjustment factors to be consistent with.

This APF clarifies that for the group of policies where the DET has been elected, the methodology to test whether adjustments are needed should be consistent with Section 6.B.5.d (that is, using a comparison of the PV of future death claims) and a reasonably consistent approach should be used to determine the adjustment factors). For groups of policies where the DET has not been elected, a reasonably consistent approach should be used.

3. Are the adjustments to the CSO table in Section 3.C.1.g determined on a seriatim basis or can policies be grouped to determine the adjustments?

The current wording is not clear as to whether the adjustments are determined on a seriatim basis or grouped basis, resulting in inconsistent interpretations. This APF clarifies that the adjustments to the CSO table for the NPR calculation are to be determined using a group of policies (consistent with the approach used in Section 6.B.5.d), not on a seriatim basis. Since the NPR is calculated on a policy-by-policy basis, the application of the adjustments must be applied to each policy on a seriatim basis, but the factors themselves can be determined using a group of policies.

Determining the adjustment factors on a seriatim basis is inconsistent with determining mortality experience for any other purpose. When data is not credible, the resulting mortality rates may not be smooth or consistent. For example, if the anticipated experience for male age 50 results in an adjustment factor of 1.3, but the adjustment factor for male age 48 is 2.1 (based on limited non-credible data), this results in the mortality rate for male 48 being higher than the rate for male 50.

This APF clarifies that the determination of the adjustment factors in Section 3.C.1.g. is to be done on a grouped basis. However, similar to the DET requirement, a company may not group together policies with significantly different risk profiles.

4. How do the requirements of Section 3.C.1.g apply to policies that pass the Life PBR Exemption?

Policies that pass the Life PBR Exemption are still subject to the requirements of Section 3.C.1 (per Section II.G.4 of the Valuation Manual). But Section 3.C.1.g includes references to the NPR and the DET which do not apply to these policies. To clarify, section 3.C.1.g. has been split into two sections: 1) policies that pass the Life PBR Exemption and 2) policies that are not utilizing the Life PBR Exemption and are subject to the NPR requirements. For policies that pass the Life PBR Exemption, all references to the NPR and DET have been removed.

5. How do the requirements in Section 3.C.1.g. apply when calculating deficiency reserves?

Policies that pass the Life PBR Exemption still must determine deficiency reserves, which has led to confusion on how the requirements of section 3.C.1.g apply when determining deficiency reserves. Section 3.C.1 is based on the basic reserve calculation (Section 3.B.6). Once the valuation mortality rates have been adjusted (if needed) by Section 3.C.1.g for the basic reserve, then the calculation of X-factors for the deficiency reserve follows the normal approach as described in VM-A and VM-C. This APF clarifies that the mortality adjustment in 3.C.1.g only applies to the basic reserve for policies that pass the Life PBR Exemption, and not the deficiency reserve.

Deficiency reserves are not needed for policies that are not utilizing the Life PBR Exemption. The NPR for policies other than term and ULSG equals the basic reserve defined in VM-A and VM-C, the NPR for term and ULSG follow the requirements of Section 3.4 and 3.5, and the DR and SR calculations already reflect the circumstances that give rise for the need for a deficiency reserve.

Section 3: Net Premium Reserve

C. Net Premium Reserves Assumptions

- 1.g For a group of policies where the anticipated mortality experience materially exceeds the prescribed CSO mortality rates determined in Section 3.C.1.a through 3.C.1.d above, the company shall adjust the CSO mortality rates as follows:
- i. For policies that pass the Life PBR Exemption, the CSO mortality rates used to determine the basic reserve for each policy shall be adjusted in a manner commensurate with the anticipated mortality experience for the policies. The methodology used to test whether adjustments are needed can be performed on an aggregate basis for the group of policies using a reasonable method to compare the respective mortality rates, such as comparing the present value of future death claims discounted at the valuation interest rate used for VM-A and VM-C. However, for the purposes of this comparison, a company may not group together policies with significantly different risk profiles. If an adjustment is needed, the determination of the adjustment factors should use a reasonable methodology, subject to a cap that ensures that mortality rates do not exceed 1,000 per 1,000.
 - ii. For policies where the Life PBR Exemption is not utilized, the CSO mortality rates used in the NPR calculation shall be adjusted in a manner commensurate with the anticipated mortality experience for the policies.
 - a) When the company elects to use the DET in Section 6.B for a group of policies, the methodology used to test whether adjustments are needed should be consistent with the methodology used in Section 6.B.5.d (that is, using a comparison of the PV of future death claims discounted at the valuation rate used for the NPR) . For the purposes of this comparison, a company may not group together policies with significantly different risk profiles. If an adjustment is needed, the determination of the adjustment factors should use a reasonably consistent methodology to the one used in Section 6.B.5.d., subject to a cap that ensures that the mortality rates do not exceed 1,000 per 1,000.
 - b) For the group of policies where the DET is not used, the company should use a reasonably consistent approach to the one described in paragraph a) above to test whether adjustments are needed and to determine the adjustment factors. The resulting adjustment factors are not required to be identical to the adjustment factors determined in paragraph a) above.

The resulting NPR must not be lower than the NPR calculated without adjustments to the CSO mortality rates.

Guidance Note: It is anticipated that the 3.C.1.g adjustments are generally applicable but not limited to policies with limited underwriting, such as simplified issue or final expense. The intent of Section 3.C.1.g. is not to test every possible group of policies (e.g., attained age blocks, individual underwriting classes with lower credibility, etc.) to determine if its mortality experience is higher than the CSO table even though more aggregate mortality experience is lower than the CSO table. However, if a large, credible block or group of policies (e.g., a block of business assumed from another company that has significantly different mortality experience than the rest of the assuming company's business, or a large

block of business from an era when the company had significantly more permissive underwriting, etc.) is expected to have worse experience than the CSO table, then the adjustments in 3.C.1.g should be made.

Section 6: Stochastic and Deterministic Exclusion Tests

B. Deterministic Exclusion Test (DET)

- 5.d. If the anticipated mortality for the group of policies exceeds the **prescribed CSO mortality rates for the NPR determined in Section 3.C.1.a through 3.C.1.g**, then the company shall use anticipated mortality to determine the valuation net premium. For this purpose, mortality shall be measured as the present value of future death claims **as of the valuation date** discounted at the valuation interest rate used for the NPR.