**MEMORANDUM**

TO: Dale Bruggeman, Chair of the Statutory Accounting Principles (E) Working Group

Kevin Clark, Vice-Chair of the Statutory Accounting Principles (E) Working Group

FROM: Rachel Hemphill, Chair, Life Actuarial (A) Task Force

Craig Chupp, Vice-Chair, Life Actuarial (A) Task Force

RE: Life Actuarial (A) Task Force Response on Negative IMR

DATE: June 5, 2023

**Background**

On March 27, 2023 a memorandum from the Statutory Accounting Principles (E) Working Group (SAPWG) was received by the Life Actuarial (A) Task Force (LATF) with a referral for consideration of the Asset Adequacy Testing (AAT) implications of negative IMR. Specifically, the Working Group recommended a referral to the Task Force to consider the following:

1. Development of a template summarizing how IMR (positive and negative) is reflected within AAT.
2. Consideration of the actual amount of negative IMR that is to be used in AAT, noting that as negative IMR is included, there is a greater potential for an AAT liability.
3. Better consideration and documentation of cash flows within AAT, as well as any liquidity stress test considerations.
4. Ensuring that excessive withdrawal considerations are consistent with actual data. (Insurers selling bonds because of excess withdrawals should not use the IMR process.)
5. Ensuring that any guardrails for assumptions in AAT are reasonable and consistent with other financial statement / reserving assumptions.

**Recommendation**

On its April 27th call, LATF discussed the referral from SAPWG. LATF agreed on the following actions:

Develop IMR Template

LATF is drafting a template with additional disclosures on the reflection of IMR in Principle-Based Reserving (PBR) and AAT. We have requested input from the American Academy of Actuaries and the American Council of Life Insurers on a potential template. The template’s disclosures would aim to support verification of the requirements SAPWG is considering for potential admittance of negative IMR, including confirming:

1. That IMR is appropriately allocated for PBR and AAT,
2. That any negative IMR amounts reflected in starting assets do not generate income and so increase reserves in PBR and/or decrease reserve sufficiency in AAT,
3. That admitted negative IMR does not reflect bonds sold due to historical or anticipated future excess withdrawals, and
4. That admitted negative IMR only reflects bonds sold and replaced with similar bonds.

For items three and four above, we note that while LATF can request verification and justification from companies, this may be difficult for companies to demonstrate. For item three, we can require additional disclosures including actual to expected experience for withdrawals. For item four, it is not yet clear what verification companies could provide.

This template would be optional but recommended starting with 2023 reporting and could be required starting in 2025. Individual regulators could request this information during reviews if warranted before 2025.

Issue Guidance on Consistency

LATF is drafting guidance for year-end 2023 and 2024, consistent with the guidance LATF issued for year-end 2022 but updated for SAPWG’s potential admittance of some portion of aggregate negative IMR. That is, LATF continues to affirm that a principle-based, reasonable, and appropriate allocation of IMR for PBR and AAT would be consistent with handling of the IMR asset for statutory reporting. LATF will also consider an Amendment Proposal Form to make changes directly in the Valuation Manual to clarify the treatment of negative IMR starting with the 2025 Valuation Manual. This work continues to address the concern raised that there would be a “double hit” if negative IMR were not admitted while being required to be reflected in PBR and/or AAT.

Recommendation to SAPWG Regarding AAT

LATF recommends to SAPWG that any decision to admit or not admit aggregate negative IMR should not rely on AAT at this time. We wish to clarify that AAT is not formulaic, is heavily judgment-based, and generally does not contain prescriptive guardrails on that judgment, such as the reinvestment guardrail and other guardrails that apply in PBR. In response to specific concerns around a lack of consistency in AAT asset assumptions, Actuarial Guideline (AG) 53 was developed to provide regulators with additional disclosures, but again does not contain guardrails. AG 53 review work is currently under way. Moreover, this is not the only area where concerns could arise regarding the reliability of specific AAT results. We do not believe it would be appropriate to admit negative IMR if doing so was depending on AAT as the sole or primary safeguard for any related solvency concerns.