

Conference Call

**Financial Analysis Solvency Tools (E) Working Group
Wednesday, September 23, 2020
2:00 p.m. – 3:00 p.m. Central**

ROLL CALL

Judy Weaver, Chair	Michigan	Lynn Beckner	Maryland
Patricia Gosselin, Vice Chair	New Hampshire	Debbie Doggett	Missouri
Sheila Travis	Alabama	John Sirovetz / Diana Sherman	New Jersey
Kurt Regner / David Lee	Arizona	Victor Agbu	New York
Kim Hudson	California	Dwight Radel / Tim Biler	Ohio
Kathy Belfi	Connecticut	Ryan Keeling	Oregon
N. Kevin Brown	District of Columbia	Kimberly Rankin	Pennsylvania
Carolyn Morgan/Helen McGhin	Florida	Jack Broccoli	Rhode Island
Eric Moser	Illinois	Amy Garcia	Texas
Roy Eft	Indiana	Kristin Forsberg	Wisconsin

Staff Support: Rodney Good, Bill Rivers, Ralph Villegas

AGENDA

1. Consider Exposure of the Following Proposed Revisions to Certain Procedures, Benchmarks, and Guidance in the *Financial Analysis Handbook 2020/2021 Edition—Judy Weaver (MI)* Attachments 1-3
 - Revised Certain Non-Troubled Quarterly Automated Procedures for Insurers with No Retention – *Attachment 1* Pg. 1
 - Update Guidance within the Special Analysis Procedures for Captive Insurers – *Attachment 2* Pg. 3
 - Updated Guidance and Procedures regarding Long-term Care Insurance and Separate Accounts – *Attachment 3* Pg. 7
2. Discuss Any Other Matters Brought Before the Working Group—*Judy Weaver (MI)*
3. Adjournment

III.A.3. Risk Assessment (All Statement Types) – Quarterly Quantitative Assessment of Non-Troubled Insurers

Quantitative Risk Assessment~~-----DETAIL ELIMINATED TO CONSERVE SPACE-----~~

C. Based on the results of the automated system calculations, a full quarterly risk assessment analysis may be completed if the insurer has the following number of “yes” responses from the automated calculations:

1. Four or more for P/C insurers, title insurers and health entities or
2. Three or more for life/A&H/fraternal insurers

Special Notes: Any automated results in D where the denominator is 0 return a “yes” response.

NOTE: A default “no” response will be returned for insurers with no net retention for automated results #8 and #9.

~~Special note:~~ For companies that have not filed a prior year-end or quarterly statement (e.g., either a new start-up insurer or exempt from filing), all responses in section D will default to a “yes.” In this scenario, it is recommended the analyst perform a full quarterly risk assessment analysis.

D. Automated system calculations:

1. Are unassigned funds negative? (ST)
2. Has surplus/capital and surplus (based on business type) increased \geq 12.5% (for first quarter), 25% (for second quarter), or 37.5% (for third quarter)? (ST)
3. Has surplus/capital and surplus (based on business type) decreased \geq 5% (for first quarter), 10% (for second quarter), or 15% (for third quarter)? (ST)
4. Has any individual asset category that is greater than 5% of surplus/capital and surplus (based on business type) changed by more than +/- 10% from the prior year-end? (CR, MK, LQ)
5. Has any individual liability category that is greater than 5% of surplus/capital and surplus (based on business type) changed by more than +/-10% from the prior year-end? (RV, OP, ST)
6. Are affiliated investments greater than or equal to 75% of surplus/capital and surplus (based on business type), OR unrealized capital loss less than -15% of prior year-end surplus/capital and surplus (based on business type)? (CR, LQ)
7. Does the net loss exceed 20% of surplus/capital and surplus (based on business type)? (OP)
8. For property/casualty insurers, title insurers and health entities, is the combined ratio greater than or equal to 100%? (PR/UW, OP)
9. Has net premiums written changed by more than +/- 5% (for first quarter), +/- 10% (for second quarter), or +/- 15% (for third quarter) from the prior year-to-date? (PR/UW)

~~NOTE: A default “no” response will be returned for insurers with no net retention.~~

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III.C.1. Special Analysis Procedures – Risk Retention Groups and Captives and/or Insurers Filing on a U.S. GAAP Basis Worksheet (P/C Only)

Note: These procedures are designed for all risk retention groups (RRGs) and captive insurers filing on a U.S. generally accepted accounting principles (GAAP) (or modified GAAP) basis, regardless of accounting treatment (GAAP/SAP) or organizational structure (captive/traditional laws), after the completion of the traditional Risk Assessment Procedures. Certain procedures are specific to insurers that file on a GAAP basis. For RRGs and captive insurers that file on an SAP basis, the analyst can indicate “Not Applicable” or “NA” in response to the GAAP specific procedures.

Management Assessment

	<i>Risks</i>
a. Refer to the Risk Assessment Procedures for the review of the insurer’s most recent business plan <u>(plan of operation) to ensure that it is unchanged from the prior year.</u>	OP, ST
<u>i. If changes were made to the plan, ensure that the changes have been approved.</u>	<u>OP, ST</u>
<u>ii. Review General Interrogatory, Part 2, Question 13.1 and ensure the amount agrees with the approved plan.</u>	<u>OP, ST</u>
<u>iii. Ensure that the financial projections on file accurately reflect the operations as presently conducted.</u>	<u>OP, ST</u>
<u>iv. Ensure that the notes relating to the operation of the company agree with the approved plan.</u>	<u>OP, ST</u>
b. Summarize the insurer’s level of reliance on captive managers, TPAs, or MGAs to run its business operations (e.g., underwriting, claims, record and reporting).	OP, ST
i. If significant reliance exists, describe the services provided, any additional relationships, whether the expense ratio is in line with industry standards, and whether those parties service other insurers.	OP, ST

Balance Sheet Assessment

	<i>Risks</i>
a. If risk-based capital is required, reassess the impact of total adjusted capital if the insurer recorded assets typically non-admitted according to the NAIC <i>Accounting Practices and Procedures Manual</i> . If risk-based capital is not required, consider various methods to assess the capital sufficiency of the insurer.	OP, ST
i. Consider the potential impact differences between GAAP and SAP investments, and/or deferred acquisitions costs could have on the total adjusted capital component of the RBC calculation.	OP, ST
b. Have there been any changes in assets permitted by the state, such as letters of credit compared to the prior period? If “yes,” indicate the line item that changed, current and prior period balances, the amount of the change, and any resulting impact on the insurer.	CR, MK, ST
c. Review any new letters of credit, principal or interest paid and whether any necessary approvals were obtained, if required.	LG, ST
d. Review the Annual Financial Statement, Notes to Financial Statements, Note 1 and document any individual asset category that is greater than 5% of total admitted assets that would	LQ

III.C.1. Special Analysis Procedures – Risk Retention Groups and Captives and/or Insurers Filing on a U.S.-GAAP Basis Worksheet (P/C Only)

typically be non-admitted according to the NAIC <i>Accounting Practices and Procedures Manual</i> . Indicate the asset category (e.g., deferred acquisition costs, fixed assets, prepaid expenses, and deferred taxes), current period-end balance, and the percentage change from the prior period-end. In addition, identify any potential impact these balances may have on liquidity.	
e. Under U.S. GAAP, FAS 113 requires insurers to present reinsurance recoverables on unpaid claims as an asset, as opposed to a contra liability. Consider the impact this presentation has while reviewing the balance sheet of the reporting entity and document the components that are presented differently as well as any significant period-to-period changes.	LQ
f. If the insurer has presented its reinsurance recoverables in accordance with FAS 113, consider the impact this presentation may have on liquidity and the ratio of total liabilities to surplus.	LQ
g. Under U.S. GAAP, reserves can be discounted in some instances. i. Determine if the reporting entity has discounted any reserves that would not be discounted under NAIC SAP, and consider the impact of such difference on the overall evaluation of the insurer's financial position. ii. Determine whether permission regarding the discount was received from the Department of Insurance and if the rate of the discount was approved.	LG, RV
h. Under U.S. GAAP, insurers are <u>not</u> required to establish a liability for "provision for reinsurance," but instead are required to establish a contra asset for an allowance for doubtful accounts. Consider the impact this may have on liquidity and the ratio of total liabilities to surplus.	LQ

Operations Assessment

	Risks
a. Under U.S. GAAP, FAS 115 provides that debt and equity securities that are "being traded" (i.e. trading securities) and are reported at fair value with the change presented through the statement of income. Also under U.S. GAAP, in some cases reserves are allowed to be discounted. Document the impact these differences, as well as any other known differences have on the reporting entity's profitability.	MK, OP, RV

Investment Practices

	Risks
a. Under U.S. GAAP, FAS 115 provides that debt and equity securities that are "available for sale" are reported at fair value with the change presented as unrealized gains and losses through equity (capital and surplus). Document any significant impact of "available for sale" or "trading securities" on the capital and surplus or statement of income of the reporting entity.	OP, MK

Review of Disclosures

III.C.1. Special Analysis Procedures – Risk Retention Groups and Captives and/or Insurers Filing on a U.S. GAAP Basis Worksheet (P/C Only)

	<i>Risks</i>
a. Review the Annual Financial Statement, Notes to Financial Statements to assess the adequacy of disclosures regarding the reconciliation from the NAIC <i>Accounting Practices and Procedures Manual</i> to U.S. GAAP, as well as NAIC validation cross/checks to ensure cross checks failures were adequately explained. Document any inconsistencies with disclosures and validation cross/checks and consider follow-up with the company, if necessary.	LG
b. Review in the Annual Financial Statement, General Interrogatories, Part 2, #13.1 to identify the insurer's largest net aggregate risk insured. Measure this exposure as a percent of surplus to ensure that it is in compliance with state guidelines.	LG

Assessment of Results from Prioritization and Analytical Tools

	<i>Risks</i>
a. Analysts should be aware that the Financial Analysis Solvency Tools were designed to assess potential risks within statutorily filed financial statement in conformity with the NAIC Accounting and Practices and Procedures Manual and not in conformity with GAAP. Based on the reconciliation found in the Annual Financial Statement, Notes to Financial Statements, Note #1 as well as observations made with the aforementioned questions; review any key ratios for factors that may influence the calculation. Provide an explanation for any unusual or significant fluctuations or trends noted. (A few examples include liquidity ratio, investment yield, etc.)	

III.B.6.b. Pricing/Underwriting Risk Repository – Life/A&H/Fraternal Annual

Proposed changes below are also proposed to apply to the same procedure in the Health pricing/underwriting risk repository.

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4. Review the Annual Financial Statement, Long-Term Care (LTC) Experience Reporting Forms (April 1 filing) to investigate underwriting results for LTC business.

	<i>Other Risks</i>
<p>a. Did the insurer report an underwriting loss on the “Other Health” line of business on page 7, Analysis of Operations by Line of Business, and the insurer writes long-term care insurance (LTCI)?</p> <p>If “yes,” further investigate the underwriting loss by reviewing the Annual Financial Statement, LTC Experience Reporting Forms, and A&H Policy Experience Exhibit, <u>and the Actuarial Guideline-51 reporting (if required to file). Request a department actuary to assist in the review, if available.</u></p> <p>i. Review or request the state insurance department actuary to <u>Review the operational results in conjunction with the actuarial</u> review <u>of</u> the LTC Experience Reporting Forms, <u>the Actuarial Guideline-51 reporting, actuarial memorandum, or other related information filed to the department:</u></p> <ol style="list-style-type: none"> 1. to i identify by policy form or in aggregate trends in premiums, benefits and the LTC loss ratio (benefits divided by premiums). 2. Review or request the state insurance department actuary to review the LTC Experience Reporting Form 3 to i identify trends in under-reserving that may affect underwriting results. (Refer to the Actuarial Risk Repository for A&H and Statement of Actuarial Opinion review procedures.) <p>ii. Compare results to prior years to identify any concerns with multi-year trends.</p>	

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III.B.6.d. Pricing/Underwriting Risk Repository – Analyst Reference Guide

******TEXT NOT SHOWN TO CONSERVE SPACE********Quantitative and Qualitative Data and Procedures – Life, Accident & Health (A&H), Fraternal**

Underwriting Performance

PROCEDURE #4 assists analysts in evaluating the underwriting performance of long-term care insurance (LTC) line of business through a review of the Annual Financial Statement, Long-Term Care Experience Reporting Forms, [the Actuarial Guideline-51 reporting \(if required to file\), actuarial memorandum or any other related actuarial information filed to the department](#) including trends in premiums, claims and loss ratios. Analysts should consider requesting the assistance of the department actuary to review trends in reserving that may affect underwriting results. [\(See additional guidance in the Reserving Risk Repository Analyst Reference Guide of this Handbook\)](#)

******TEXT NOT SHOWN TO CONSERVE SPACE********Quantitative and Qualitative Data and Procedures – Health**

Underwriting Performance

PROCEDURE #4 assists analysts in evaluating the underwriting performance of the LTC line of business through a review of the Annual Financial Statement, Long-Term Care Experience Reporting Forms, [the Actuarial Guideline-51 reporting \(if required to file\), actuarial memorandum or any other related actuarial information filed to the department](#) including trends in premiums, claims and loss ratios. Analysts should consider requesting the assistance of the department actuary to review trends in reserving that may affect underwriting results. [\(See additional guidance in the Reserving Risk Repository Analyst Reference Guide of this Handbook\)](#)

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III.B.8.b.ii. Reserving Risk Repository – Life/A&H/Fraternal Analyst Reference Guide

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Reserve Requirements Associated with Separate Account Products & Guarantees

PROCEDURES #6–#9 assists the analyst in identifying situations where separate accounts products may be creating contingent liabilities to the general account. This is largely a function of the types of separate accounts products offered by the insurer, and the analyst should rely on general knowledge of the insurer’s products at this stage of the analysis.

The analyst should review disclosures in Separate Accounts General Interrogatories y #2, Analysis of Operations by Line of Business (Page 5), Analysis of Increase in Reserves During the Year (Page 6), and the Notes to the Financial Statements of the general account to gain an understanding of the types of products included in the separate account, the general account guarantees on separate account products and identify any concerns with reserving or asset adequacy that may require additional analysis of actuarial filings. The analyst should gain an understanding of any products in the separate account that contain guarantees that are held in the separate account instead of the general account and the types of guarantees (guaranteed minimum death benefit (GMDB), guaranteed minimum income benefit (GMIB), etc.).

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Proposed changes below for LTCI are also proposed to apply to the Health reserving risk reference guide.

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Long-Term Care Insurance (LTCI) Reserves Overview

Long-Term Care Insurance (LTCI) provides coverage for the cost of care supporting activities of daily living (ADL) (e.g. dressing, bathing, eating, etc.) beyond a predetermined period. Historically, insurers that wrote LTCI encountered difficulties accurately projecting claims costs, lapse rates, investment returns and other factors associated with LTCI, and subsequently many writers have experienced unprofitability in older (legacy) blocks of LTCI business. This has led many companies to request significant rate increases, modify product benefits, or exit the product line altogether. Therefore, many insurers continue to experience significant solvency challenges related to this line of business, and state insurance regulators should continue to carefully evaluate and monitor the solvency position of all insurers with a material amount of LTCI business.

- These same risks also affect reinsurers, because the reinsurance contract cannot arbitrarily allow for ceded premium increases. Additionally, in order to effectuate a true transfer of risk, the reinsurer does not have the ability to require the direct writer to request rate increases. Furthermore, it would not qualify for reinsurance accounting. As some insurers look for avenues to minimize or eliminate its risk from the LTCI block, they may look to new reinsurance opportunities, non-traditional buyers and A&H Data from the Life Blank:
 - Exhibit 6 & 8
 - Leverage Ratios – trend over years:
 - Reserves to premium ratios (FAH#10 benchmarks)
 - A&H Reserves to Surplus (FAH#15 benchmarks)
 - A&H Reserve Adequacy – trend over years

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- A&H Reserve deficiency ratio (reserves to surplus, schedule H test and H part 3 by line, FAH#17 benchmarks)
- A&H Loss ratios: YoY, trend helps explain reserve deficiency. (FAH#18 benchmarks)

In addition, periods of economic downturn and low interest rates increase the risk that LTCI writers will be challenged to generate sufficient returns to support this line. In addition, declines in projected investment returns could have a significant impact on LTCI reserve assumptions.

Actuarial Guideline 51—The Application of Asset Adequacy Testing to Long-Term Care Insurance Reserves (AG 51)

Effective for reserves reported with the Dec. 31, 2017, financial statement, Actuarial Guideline 51—The Application of Asset Adequacy Testing to Long-Term Care Insurance Reserves (AG 51) now applies. The *Health Insurance Reserves Model Regulation* (#10) and the NAIC *Valuation Manual* VM-25, Health Insurance Reserves Minimum Reserve Requirements, contain requirements for the calculation of LTCI reserves. AG 51 requires companies with over 10,000 LTCI enrollees to submit standalone LTCI asset adequacy analyses to the state. AG 51 is intended to provide uniform guidance and clarification of requirements for the appropriate support of certain assumptions for the asset adequacy testing applied to a company’s LTCI block of contracts. AG 51 requires reporting to the department within the appointed actuary’s actuarial memorandum required by VM-30, Actuarial Opinion and Memorandum Requirements, or in a special actuarial memorandum containing LTCI-specific information on the results of the analysis, assumptions on mortality, voluntary lapse, morbidity, investment returns and rate increase assumptions.

Factors Impacting LTCI Reserves and Rates

This following guidance provides additional information that may assist state insurance department staff in understanding of differences in premium rate review and approval, and valuation review of reserve adequacy assumptions in order to maintain or improve state insurance departments’ current intra-departmental coordination/communication practices between the states’ rate reviewers, valuation actuaries and analysts/examiners.

Reserve Increase Factors

1. Background

Ever since asset adequacy testing became a requirement for life insurers in the 1980s, actuaries have been required to analyze reserve adequacy assumptions on an annual basis and make the assumptions more conservative when experience or expectations become more adverse. If the result of the more conservative assumptions was inadequate reserves, companies have been required to establish higher reserves to ensure future claims could be paid in the more adverse environment.

In some cases, the chain of events is straightforward. For instance, for life insurance, if more people die at earlier ages than expected and the experience is highly credible, then the actuary increases mortality rates in the upcoming year-end filing, leading to higher reserves being established.

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In other cases, the chain of events is less straightforward. For instance, it is expected that cash surrenders on deferred annuity products will increase if interest rates rise. However, most deferred annuities have been sold during a period of decreasing interest rates. Actuarial and regulatory practice require reserves to be adequate in moderately adverse conditions, even if those conditions have not been recently experienced. There is typically judgment by the company actuary and another layer of judgment by regulators in play in this type of complex situation. The NAIC Standard Valuation Law Model 820 (SVL), NAIC Valuation Manual (VM), and the Actuarial Standards Board’s Actuarial Standards of Practice (ASOPs) describe how these complex situations should be handled.

2. Long-Term Care Insurance

For LTCI blocks of business that experience higher morbidity than expected, this experience will likely lead to changes in expectations on future morbidity for both the observed block and other blocks.

With LTCI, some factors are likely to play out in a straightforward manner. A combination of higher life expectancy and lower lapses will lead to more people than expected reaching prime LTCI claims ages of 80 and above, which leads to companies holding higher reserves than originally anticipated. Similarly, all companies have experienced the decreasing interest rate environment, which have led to lower-than-expected investment returns and the need to hold higher reserves, because investment income is relied upon to help pay claims.

It is important to note that mortality, lapse, and interest rate factors become observable and credible during the early premium-paying years.

3. Morbidity Assumptions:

Morbidity, however, has tended to fall into the category of a complex factor. The three main aspects of LTCI morbidity are: (1) incidence, the percentage of people at a given age who start a claim; (2) average length of claim; and (3) utilization, which is less than 100 percent if, e.g., the daily nursing home cost is lower than the maximum daily benefit in the insurance policy.

There has not been uniform experience development in morbidity, except that length of claim has tended to increase, likely because cognitive (e.g. dementia and Alzheimer’s) claims tend to be longer than average and incidence has been higher than expected, likely due to more people reaching the age when cognitive claims tend to occur.

Because of divergent experience among companies and because morbidity becomes observable and credible during the later claim-paying years, establishing and regulating LTCI morbidity assumptions has not been straightforward. However, as with other factors and other products, the handling of these situations is addressed in the SVL, VM, and ASOPs. Examples of these standards include:

- SVL Section 12A(3)(a): “Assumptions shall, to the extent that company data is not available, relevant, or statistically credible, be established using other relevant, statistically credible experience.”
- SVL Section 12A(4): “Provide margins for uncertainty ... such that the greater uncertainty the larger the margin and resulting reserve.”

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- Actuarial Guideline 51 (providing guidance on VM-30) Section 4.B.: “The analysis shall comply with applicable Actuarial Standards of Practice, including standards regarding identification of key risks. Material assumptions associated with the LTCI business shall be determined testing moderately adverse deviations in actuarial assumptions.”

The result is that whether credible experience exists or not, the company actuary needs to set assumptions underlying reserves, and the factors underlying the assumptions are often complex and frequently changing. Company and regulatory actuaries are experienced in working in this complex, changing environment with many life insurer products, such as variable annuities, indexed products, and LTCI having product features and factors underlying reserves that are complex and changing.

4. Rate Increases:

A unique aspect of LTCI products is being a long-term product with rate increases that require review by states. Besides states with the largest insurance departments, the actuaries reviewing LTCI reserves are often the same staff reviewing LTCI rate increases. For larger states, there is typically coordination or training to ensure the reserve and rate teams are on the same page regarding developments in for example, life expectancy and morbidity. State insurance regulator experience in reviews of LTCI reserves and rate increase filings show that the same factors reporting reserve increases and requests for rate increases are due to similar factors including higher life expectancy, lower lapses, lower investment returns, and worsened morbidity.

There has been additional regulatory attention on ensuring the companies asking for rate increases based on adversity of certain factors are holding reserves based on at least the same level of adversity in those factors. The questions used in many states’ rate increase reviews requires the company to explain the consistency between the rate increase filing assumptions and reserve adequacy assumptions.

To date, the most common complex, non-straightforward case is the applicability of a company’s adverse morbidity experience of an older LTCI block to morbidity assumptions on a newer block. This complex dynamic comes into play when establishing reserve and rate increase assumptions.

The reserve assumption changes can occur with initiation by the company, through formal or informal agreement between regulators or companies, or by relying on SVL Section 11.6., which allows a commissioner to require a company to change reserve assumptions and adjust reserves.

Example:

A typical example of a chain of events would first involve a block issued in 1995 to 1998 to policyholders with issue ages ranging from 52 to 62. By 2019, enough policyholders have reached prime LTC claim ages of 80+, that experience has developed that drives reserve assumption changes. As policyholders enter ages in the upper 80s and 90s, additional experience will be attained that will predict future LTCI costs and result in further changes in reserve assumptions. The development of older-age morbidity experience is expected to generate volatility in LTCI reserves. For some companies, the older-age morbidity experience will likely be unfavorable, with increased reserves needed. For most other companies, the older-age morbidity experience will likely be as expected, leading to no significant, unforeseen reserve increases.

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Companies will be expected to apply lessons learned from older blocks of business to their newer blocks. Those lessons will likely differ by situation. For example, to the extent underwriting is different, the newer and older blocks may experience different morbidity trends.

5. Rate Increase Factors

All of the above-mentioned reserve-related dynamics have occurred, are occurring, or will occur with rate increase requests. Prior to the last few years, rate increases were based on higher life expectancy, lower lapses, and lower investment returns. As morbidity experience has developed, regulators have started receiving more morbidity-driven LTCL rate increase requests.

As the credibility of morbidity experience on older blocks expands, consideration is given to the applicability of the older-block data to newer blocks. This consideration is required with reserves and is driving some of the recent, substantial reserve increases in the industry. The same consideration is now driving some rate increase requests, in some cases before prime claims years begin on the newer LTCL block.

To assist state insurance department staff performing reserve valuation analysis to gain an understanding of the rate review process, communication and coordination with the rate review staff may be necessary. The following example describes how lessons learned on an older block's morbidity experience and/or the need for more credible experience on the newer blocks may factor into a rate increase review.

- Three potential approaches for regulatory consideration of such rate increases are, (1) disapprove the rate increase and force the new block to have credible experience before approving an increase, (2) allow partial consideration of the "lessons learned" on the older block and partially approve the rate increase, or (3) allow full consideration of the older-block lessons learned and fully approve the rate increase.
- The downside of option (1) is that it will lead to higher rate increase requests in the future if newer block experience plays out similarly to older block experience. The downside of option (3) is that rates would end up being too high if experience plays out more favorably than expected.
- After multiple, public, regulatory actuarial discussions on the topic, general (but not unanimous) consensus was that most rate approvals should land in a spot between options (2) and (3). To the extent the rate increase approval is towards option (3), the department should ensure the company has a mechanism to lower future premium rates if experience plays out more favorably than expected.

6. Intra-Department Communication and Coordination of Actuarial Review Work

While every state insurance department may be structured differently, many state insurance department have the same staff members perform work on both LTCL reserve valuation analysis and rate increase reviews, while other have separate staff perform these functions. In the latter instance, department staff should be aware of or coordinate the intra-department review work related to each function.

The following are suggested steps a state may consider to ensure that actuarial assumptions associated with the rate increase request are consistent with the assumptions embedded in the asset adequacy testing.

- Inquire of the company's actuary or senior management regarding:

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- The relationship of the actuarial assumptions embedded in the rate filing versus those made for annual statement reporting
- Explanation if there is inconsistency between assumptions reported
- How Actuarial Guideline 51 impacts the company’s rates and reserves
- Affirmation that the assumptions underlying the projections are consistent with the assumptions used in asset adequacy analysis
- A copy of the company’s rate increase plan when rate increase filings disclose that future rate increase filings, beyond what is currently being requested, are planned
- Consider reviews of different filings for consistency. For example:
 - Compare reserving assumptions to rate increase assumptions,
 - e.g. review the Regulatory Asset Adequacy Issues Summary (RAAIS) and the Actuarial Opinion and Memorandum (AOM) to ensure that assumptions used for pricing and reserving are similar in nature
 - Identify assumptions underlying the asset adequacy testing memorandum that appear to be an outlier and then compare against a subsequent rate increase filing

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Quantitative and Qualitative Data and Procedures

PROCEDURE #20 instructs the analyst to review the LTC Experience Reporting Form of the Annual Financial Statement and the Actuarial Guideline-51 reporting (if required to be filed to the department), if the insurer writes long-term care insurance (LTCI) to gain an understanding of the reserve adequacy of the LTCI line of business. If concerns exist, consider requesting additional information as necessary to assess actual vs. projected results, legacy vs. newer blocks of business separately, any recent rate increases and capital support. If the insurer has recently filed for rate increases on LTCI blocks, consider intra-departmental discussion with the rate increase analysis and outcome with the rate review staff (if different person than the analyst/actuary performing the valuation reserve analysis).

******TEXT NOT SHOWN TO CONSERVE SPACE******

III.B.8.b. Reserving Risk Repository – Life/A&H/Fraternal Annual******TEXT NOT SHOWN TO CONSERVE SPACE********9. Determine the type of products included in the separate account to further understand and assess separate account reserve liabilities.**

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Do any of the separate accounts have guarantees that are designed to mirror an established index (Annual Financial Statement, Note #35B)?	OP	> 0	[Data]	[Data]
b. Do any of the separate accounts have non-indexed guarantees greater than 4% [Annual Financial Statement, Note #35 B)?	OP	> 0	[Data]	[Data]
				<i>Other Risks</i>
c. If material guarantees exist, or if non-insulated products exist, determine whether the assets associated with these products are being invested in accordance with statutory guidelines.				OP
d. <u>Review Separate Account General Interrogatory #5 to identify if the insurer reported a material amount of assets in the separate account at amortized cost rather than fair value. If yes, consider additional analysis of actuarial and asset adequacy reporting.</u>				<u>OP</u>
e. <u>Review Separate Account Analysis of Operations by Line of Business (Page 5) and Analysis of Increase in Reserves During the Year (Page 6) to identify if any concerns exist regarding the types of products included in the Separate Account and reserving for those products. If yes, consider additional analysis of actuarial and asset adequacy reporting.</u>				<u>OP</u>
d.f. Based upon an overall understanding of the insurer's separate accounts products, is there evidence that such products may be creating contingent liabilities to the general account with product features such as minimum guaranteed death benefits, minimum guaranteed interest rates, etc.?				OP
e.g. If concerns or questions are noted, contact the state insurance department's actuary or other actuarial resource to discuss the nature and scope of the valuation procedures performed relating to guarantees included with separate accounts products. If determined to be necessary, contact the company's qualified actuary.				
f.h. Determine whether growth in separate accounts appears to be financed through borrowings of the general account and, if so, whether any concerns exist regarding the terms of repayment or collateralization.				OP
g.i. Determine whether the insurer writes any modified guaranteed annuities and, if so, the overall materiality and potential negative impact on the insurer's general account.				OP
h.j. Through the analyst's quarterly interdepartmental communication with the policy forms department, inquire as to whether the insurer filed any new and unusual separate account policy forms during the past 12 months.				OP
i.k. If concerns are noted about the types of policies included in separate accounts, review the insurer's separate accounts plan descriptions and/or policy forms to better understand the				OP

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types of plans offered and the specific policy features and benefits, particularly minimum guarantees	
<u>j-l.</u> If concerns are noted about reserving for separate accounts, consider a target examination of reserves, request that the field examination staff request a valuation listing by plan and issue year, and test a sample of the individual policy reserves for accuracy.	

*****TEXT NOT SHOWN TO CONSERVE SPACE*****

Proposed changes below for LTCI are also proposed to apply to the same procedure in the Health reserving risk repository.

*****TEXT NOT SHOWN TO CONSERVE SPACE*****

20. Review and assess long-term care (LTC) insurance reserves.

	Other Risks
<p>a. Review the information reported in the LTC Experience Reporting Form <u>of the Annual Financial Statement, the Actuarial Guideline-51 reporting (if required to file), actuarial memorandum or any other related actuarial information filed to the department;</u> and identify any concerns with reserve adequacy of LTC insurance business. <u>Request a department actuary to assist in the review, if available.</u></p> <ul style="list-style-type: none"> i. <u>Gain an understanding of the asset adequacy and cash-flow testing for LTCI on a stand-alone basis.</u> ii. <u>Consider any negative development in total LTCI reserve, asset adequacy reserves (if available), active life reserves, disabled lives reserves and premium deficiency reserves over the last five years,</u> iii. <u>Evaluate the appropriateness of investment return assumptions factoring in the status of the current economic and low interest rate environment.</u> <p>b. <u>If concerns exist:</u></p> <ul style="list-style-type: none"> i. <u>Evaluate actual results vs. original or revised assumptions and financial projections to identify trends and concerns.</u> ii. <u>Consider evaluating legacy blocks of business separately from newer blocks of business.</u> iii. <u>Rate Increases: Obtain and review the following information related to the status of rate increases and reduced benefit options. Consider that some information may be available from rate review staff for recent rate increase filings.</u> <ul style="list-style-type: none"> 1. <u>Track the progress of rate increases across states where a material amount of business is written.</u> 	

III.B.8.b. Reserving Risk Repository – Life/A&H/Fraternal Annual

<p><u>1.2. Review projections illustrating the impact of proposed rate increases or reduced benefit options on the company’s future profitability.</u></p> <p><u>3. Determine the extent that future rate increases are included in the amount (\$) of reserve offsets, asset adequacy/cash-flow testing and the reasonableness of the assumptions.</u></p> <p><u>4. Consider the impact of historical approvals on the company’s ability to obtain the rate increases presented in the projections. If concerns are identified in this area, obtain and review information on the company’s plans to address these issues.</u></p> <p><u>5. Compare the average percent of rate increases requested to the average approved.</u></p> <p><u>6. Identify the amount of written premium change due to approved rate increases.</u></p> <p><u>iv. Regarding the adequacy of internal capital to support the LTCl business, compare the current total LTC reserves (active life and other), net of reinsurance, to the amount of internal capital the company has set aside for LTCl (e.g., internal capital per ORSA if applicable, or rating agency if higher than internal). If necessary, request information to gain an understanding of the degree of conservatism in such capital assumptions.</u></p>	
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