

December 15, 2000

**TO: ALL VALUATION ACTUARIES OF LIFE INSURANCE COMPANIES AND  
FRATERNAL ORGANIZATIONS LICENSED IN ILLINOIS**

**FROM: LARRY M. GORSKI, FSA, MAAA**

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**RE: COMMENTS CONCERNING REGULATION XXX, GUARANTEED LIVING  
BENEFITS, THE REGULATORY ASSET ADEQUACY ISSUES SUMMARY, ET. AL. (CB #  
2000-12)**

With the statutory valuation for year-end 2000, the role of the Appointed Actuary continues to grow in importance. The major development this year for many Appointed Actuaries will be compliance with Regulation XXX. There are three questions that an Appointed Actuary must answer: Does Regulation XXX apply? How should Regulation XXX be applied? What X factors should be used? While professional and regulatory issues still exist concerning each of the three questions, over the first six months of 2001, I intend to meet with the Appointed Actuaries of several insurers, both domestic and foreign, and review the process used by the actuary to set the X factors. To facilitate the process I use to choose companies for the X factor review, the actuarial certification required by Regulation XXX should be submitted to the Illinois Insurance Department attached to the standard Section 7 or Section 8 actuarial opinion. Suggested, but not required, language for the Regulation XXX actuarial certification is attached to this document.

One question concerning Regulation XXX and the X Factors that has been asked several times is "How should changes in reserves due to changes in X Factors be reported in the statutory financial statement?" The position of the Life Actuarial Unit of the Illinois Department of Insurance is that changes in reserves due to changes in X factors should be reported through the Summary of Operations and not through the "below the line" changes in the Capital and Surplus Account. We do not equate changes in X factors with a change in valuation basis. Consistent with this position, we believe that changes in reserves due to asset adequacy analysis should be reflected in the Summary of Operations and not directly in the Capital and Surplus Account.

On the subject of actuarial opinions, all companies either insuring or reinsuring equity indexed annuity or life insurance products must submit the actuarial opinion required by Actuarial Guideline 35 and 36 respectively. The equity indexed annuity and life insurance opinions should be sent to me directly and not attached to the normal Section 7 or Section 8 opinion.

One of the "hot" topics this year is reserves for variable annuities with guaranteed living benefits. The issue is really much broader than just reserves. It includes benefit pricing and risk management. My intention is to meet with several insurers over the early part of 2001 to review the level of statutory reserves held for these benefits, the extent and quality of the work done by the Appointed Actuary relative to the testing of adequacy of the statutory reserves and the insurer's risk management program relative to these benefits.

This year we are again requesting that the Appointed Actuary submit a Regulatory Asset Adequacy Issues Summary (RAAIS) to us by March 15, 2001. See the attached document for a description of the items to be included in the RAAIS . The description has not changed from last year. This RAAIS is considered a confidential document by our Department, and will be destroyed each year upon receipt and review of the following year's RAAIS. Because it is considered confidential, the RAAIS should not be sent with the annual statement, but should be stamped "confidential" and submitted directly to Mr. Bruce Sartain, ASA, of the Illinois Department of Insurance in Springfield. The request for an RAAIS is a standing request.

#### Sample X Factor Actuarial Opinion

The X Factors, in conjunction with select factor adjusted mortality rates, reflect anticipated future mortality subject to the following conditions:

1. the X factors meet all the requirements of Section 5B(3) of the Model,
2. the X factors do not reflect mortality improvement beyond the date of valuation,
3. the X factors take into account relevant, emerging company experience, and
4. the appropriateness of the X factor has been evaluated using appropriate statistical techniques.

#### Details of the Regulatory Asset Adequacy Issues Summary

1. When an actuarial opinion under Section 8 is provided, the regulatory asset adequacy issues summary shall also be provided. It shall specify:
  - a. For each of the required interest rate scenarios which produce negative ending surplus values in the aggregate as defined in Section 10.A, the amount of additional reserve as of the valuation date which, if held, would eliminate such negative aggregate surplus values. Ending surplus values must be determined by either extending the projection period until the in-force and associated assets and liabilities at the end of the projection period are immaterial or by adjusting the surplus amount at the end of the projection period by an amount which appropriately estimates the value which can reasonably be expected to arise from the assets and liabilities remaining in force.
  - b. The extent to which the appointed actuary uses assumptions in the asset adequacy analysis that are materially different than the assumptions used in the previous asset adequacy analysis;
  - c. The amount of reserves and the identity of the product lines that had been subjected to asset adequacy analysis in the prior opinion but were not subject to analysis for the current opinion;
  - d. The number of additional interest rate scenarios tested identifying separately the number of deterministic scenarios and stochastic scenarios;
  - e. If sensitivity testing was performed, identify the assumptions tested;

- f. Comments shall be provided on any interim results that may be of significant concern to the appointed actuary;
  - g. The methods used by the actuary to recognize the impact of reinsurance on the company's cash flows, including both assets and liabilities, under each of the scenarios tested;
  - h. Whether the actuary has been satisfied that all options affecting cash flows embedded in fixed income securities and equity-like features in any investments have been appropriately considered in the asset adequacy analysis.
2. The regulatory asset adequacy issues summary shall contain the name of the insurance company for which the regulatory asset adequacy issues summary is being supplied and shall be signed by the appointed actuary rendering the opinion.