American Academy of Actuaries

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February 13, 2019

Mr. Peter Weber
Chair, Variable Annuities Capital and Reserve (E/A) Subgroup
National Association of Insurance Commissioners

Re: Use of the terms "actuary" and "qualified actuary" in drafts of revision of VM-21

Dear Pete,

The VM-21 Requirements Drafting Group requested that the American Academy of Actuaries[1] Life Practice Council (LPC) review drafts of certain sections of Valuation Manual Chapter VM-21 (VM-21) and give advice regarding the use of the terms "actuary" and "qualified actuary." The LPC's Role of the Actuary Subgroup of the PBR Governance Work Group was assigned this task. Since that time, drafts of these sections have been exposed for comment. These exposure drafts would make changes in the use of the terms "actuary" and "qualified actuary" that in most cases are in line with the comments that Role of the Actuary Subgroup would propose. As we understand it, the VM-21 Drafting Group will now review the exposure drafts and make proposed changes that relate to reporting and disclosure in general to accommodate variable annuities in particular. These comments were first sent to the VM-21 Reporting Drafting Group. After reviewing the comments, the Reporting Drafting Group asked the Academy to forward them to your group, since the majority of the comments involved VM-21 rather than VM-31. The following are some observations that we believe could be helpful.

In the following, we have assumed that that the VM-21 Drafting Group intends to adopt many of the conventions used in VM-20 in carrying out its revisions of VM-21. In particular, we have assumed that the revised VM-21 will address its requirements to "the company" rather than to "the actuary," as was the case in Actuarial Guideline 43 (and thus in the pre-revision version of VM-21). Also, we note that the definition of "actuarial opinion," which formerly limited such opinion to "the opinion of an appointed actuary regarding the adequacy of reserves and related actuarial items" (i.e., the reserve opinion) was removed from the Valuation Manual, so that the definition of "qualified actuary" in VM-01—which reads, "The term 'qualified actuary' means

[1] The American Academy of Actuaries is a 19,500+ member professional association whose mission is to serve the public and the U.S. actuarial profession. For more than 50 years, the Academy has assisted public policymakers on all levels by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States.

an individual who is qualified to sign the applicable statement of actuarial opinion in accordance with the Academy qualification standards for actuaries signing such statements and who meets the requirements specified in the *Valuation Manual*" [2]—now applies to statements of actuarial opinion other than the reserve opinion, including, for example, the statements of opinion required to be made by a qualified actuary assigned responsibility for a group of policies or contracts under VM-G. Such qualified actuaries must meet the Academy's General Qualification Standard and not the Specific Qualification Standards that an actuary must meet to sign the reserve opinion in the annual statement.

We have reviewed drafts of sections 1 through 6, 8, 9, 11, and 12 of the revised VM-21. In the attachments, we have identified particular instances in the draft sections where each of the following numbered observations would appear to be applicable.

Observation 1: Qualified Actuary vs. Company

> In most places, we would suggest that documentation functions assigned to the qualified actuary should be assigned instead to the company, in accordance with similar practice in VM-20. In a few cases, simple substitution of "company" for "qualified actuary" might not capture the original intent of the requirement. For example, in the early draft of Section 12 that we received, Section 12.B.4.c states:
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> > "Even for a large company, the quantity of life exposures and deaths are such that a significant amount of smoothing may be required to determine expected mortality curves from mortality experience. Expected mortality curves, when applied to the recent historic exposures (e.g., three to seven years), should not result in an estimate of aggregate number of deaths less (greater) than the actual number [of] deaths during the exposure period for plus (minus) segments. If this condition is not satisfied, **the actuary** must document the rationale in support of using expected mortality that differs from recent mortality experience."
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> The last sentence of this reference was deleted in the exposure draft, but it illustrates our point: "document(ing) the rationale in support of" some action or decision is, in effect, "justifying" that action or decision. Such a requirement could apply to the company, but in a context, such as this, where actuarial judgment is most likely relied upon for the justification, it might be more appropriate to replace "the actuary" with "a qualified actuary."

Observation 2: Documentation and Disclosure Requirements Generally Should Be in VM-31

> Many of the statements in VM-21 that refer to "the actuary" are documentation and disclosure requirements. In VM-20, similar requirements were, for the most part, moved

[2] All Valuation Manual references are from the 2019 Edition; added emphasis in bold face is ours.

to VM-31, with a reference to the section of VM-20 that the documentation or disclosure supports. Both the company and a qualified actuary are given responsibilities with respect to the Life PBR Actuarial Report. In VM-31, the requirements are addressed to "the company"; in fact, all the requirements of Section 3.C, Life PBR Actuarial Report, are continuations of a sentence that begins, "The company shall include in the Life PBR Actuarial Report and of any sub-report thereof…" However, according to Section 4.A.4 of VM-G, a qualified actuary assigned responsibility for a group of policies or contracts has responsibility for preparing the PBR Actuarial Report for that group of policies or contracts and, in fact, the qualified actuary assigned by the company to prepare each sub-report of the PBR Actuarial Report must be identified in the Report's Executive Summary.

Due to this joint responsibility, most documentation and disclosure requirements could be moved to VM-31, with a reference to the appropriate section of VM-21. This would result in the company being required to provide the documentation or disclosures that would constitute part of a report prepared by the qualified actuary.

Observation 3: Requirements that Need Rewording if Carried Out by an Entity Rather Than a Human Being

Some of the requirements that were phrased in terms of "the actuary" involved actions normally carried out by human beings, such as "believing" and "being mindful of": e.g., from Sections 11.F and 12.A.1, "in light of the products being valued, the company should **be mindful of** the general characteristics of those scenarios likely to represent the tail of the loss distribution and consequently use prudent estimate assumptions for behavior that are reasonable and appropriate in such scenarios." Such statements could be clarified by rewording (e.g., "consider" instead of "be mindful of").

Observation 4: Statements Formerly Addressed to "the Actuary" That Might Better Appear in Guidance Notes

In some cases, statements formerly addressed to "the actuary" read more like guidance notes than requirements when addressed to "the company"; e.g., from Section 11.D.6,

"However, the company **should exercise caution** in assuming that current behavior will be indefinitely maintained. For example, it might be appropriate to test the impact of a shifting asset mix and/or consider future deposits to the extent they can reasonably be anticipated and increase the calculated amounts."

We recommend this paragraph be restated as a guidance note.

We appreciate the opportunity to comment and will be happy to respond to any questions you may have. Please feel free to share this letter with the VM-21 Requirements Drafting Group and any other NAIC work group or task force that may have an interest in our comments. Please contact Ian Trepanier (trepanier@actuary.org), life policy analyst at the American Academy of Actuaries, if you have questions or would like to discuss further.

Sincerely,

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