



“L&HATF” Meeting in Kansas City

“XXX” Discussion Continues

Meeting on June 3

The Ad Hoc Industry Committee on the “XXX” Regulation (AHIC) made their initial presentation to the NAIC’s Life & Health Actuarial (Technical) Task Force (L&HATF). Steve Smith (First Colony) and Jim Van Elsen (Van Elsen Consulting) made the presentation, with the support of many other companies.

The regulators provided much feedback on the proposal. Often they objected to certain provisions; other times they just needed more justification. Some of the more significant questions include:

1. **Valuation mortality.** Much concern was expressed about the adequacy and appropriateness of the proposed valuation mortality standards.

2. **Regulation language.** Several items in the proposed regulation need more work. For example, the definition of “scheduled gross premium” is still too loose.

3. **Actuarial opinions.** There was a desire expressed by the regulators for more explicit requirements for the proposed actuarial opinions.

4. **Conflicts with existing laws.** The regulators requested that the committee review existing laws and regulations for potential conflicts. This would include the Standard Valuation Law, the Standard Nonforfeiture Law, and other state laws and regulations.

5. **Industry support.** Before this regulation proceeds, it will be necessary to demonstrate to the regulators that there is general industry support for the regulation. Some companies have already sent letter to L&HATF expressing such support. Much more will be needed. L&HATF is unwilling to support the new regulation if it will be shot down like the current version of the regulation. If your company wants to participate in this effort, please contact our office.

The proposed regulation was exposed with the minutes of L&HATF. If all goes well, it could be adopted by L&HATF and the “A” Committee in September. It could be adopted by the NAIC as early as December, although early 1999 is more likely.

The AHIC will continue to meet and work on responses to the regulators’ concerns. It is anticipated that there may be a conference call in mid to late August on “XXX”.

Handouts from the Kansas City meeting are available by e-mail from our office. If you need copies or if you want to assist the AHIC, please contact us. Those who receive *The Van Elsen Report* by e-mail will automatically receive a copy. For a summary of the AHIC proposal, look at the March edition of *The Van Elsen Report*.

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The Van Elsen Report

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VA Guaranteed Living Benefits

A work group of the American Academy of Actuaries (AAA) presented an interim report on variable annuities with guaranteed living benefits. The following recommendations were made in the report:

1. **CARVM reserves.** The reserving methodology should follow a CARVM framework.
2. **Approach.** Recommend an "integrated" reserve approach.
3. **Guideline 34.** Recommend the use of Actuarial Guideline 34 for guidance on reserving.
4. **Modify Guideline 34.** The report recommends that Actuarial Guideline 34 be specifically modified to address the guaranteed benefits.
5. **Modify Guideline ZZZ.** The report recommends that the proposed Actuarial Guideline ZZZ be modified to exclude these guaranteed benefits.

The report also proposed the following future steps:

1. **Guideline 34.** Will recommend appropriate changes to Actuarial Guideline 34 for these benefits.
2. **Other issues.** Will address other issues, including: accounting, valuation actuary, and financial reporting issues.
3. **Updates.** The work group has committed to quarterly updates to the L&HATF.

Copies of the report may be obtained from the AAA. Any questions or comments should be addressed to Steve Preston or Tom Campbell.

Guideline "ZZZ"

L&HATF is working to have Actuarial Guideline ZZZ adopted by the end of 1998. This actuarial guideline

addresses reserving issues for equity-indexed products.

Larry Gorski, actuary from the Illinois Insurance Department, updated ZZZ to incorporate the Black-Scholes methodology, subject to specific requirements for its use. He also intends to rewrite ZZZ to put it in a cleaner format for adoption.

This actuarial guideline could be adopted by L&HATF and the "A" Committee in September.

Guideline "ZZZZ"

Larry Gorski also drafted proposed Actuarial Guideline ZZZZ. This guideline is similar to ZZZ, except that it applies to life insurance. The draft contains limitations to the use of book value methodologies. Copies of the draft can be obtained from the NAIC.

New Group Products

L&HATF discussed a new series of group products being offered which have specified cash value strategies. These might, for example, include growth strategies, or blue-chip strategies. This product can expect rough going from L&HATF in future months. It can also be anticipated that there will be increased regulatory scrutiny of these products in many states.

UVS

Bob Wilcox presented the final report of the AAA task force on a unified valuation system (UVS). This report may be obtained from the AAA. In this report, many choices were offered to the regulators:

- A. **Basis for determining earnings.**
 1. GAAP.
 2. Traditional reserves.
 3. Probability of insurer survival.
- B. **Review of actuarial opinion & memorandum.**
 1. By the NAIC.
 2. By a Central Actuarial Bureau.
 3. By an independent actuary.

4. None of the above.

- C. **Appointment of the actuary.**
 1. By insurer's board of directors.
 2. Authority can be delegated.
- D. **Basis for assets reserved to support policyholder interests.**
 1. Probability of insurer survival.
 2. RBC formula.
- E. **Dynamic financial condition analysis.**
 1. Mandatory report to the board of directors.
 2. Optional report to the board of directors.

The discussion of the regulators seemed to focus on options A1, A3, B3, C1, D1, and E1.

The report contained a draft model law incorporating the various requirements of the above options. The task force voted to recommend that this project be forwarded onto the NAIC's new financial reporting group, which is headed up by Commissioner Terri Vaughn of Iowa. The task force also received correspondence from Richard Roth, actuary from the California Insurance Department and chairman of the Casualty Actuarial (Technical) Task Force. He expressed his task force's opinion that they have exclusive jurisdiction over issues related to property & casualty liabilities, including health insurance reported in the yellow property & casualty blank.

Nonforfeiture Again?

The L&HATF announced that they will once again resume work on a new nonforfeiture law. This project, which has been worked on for years, was tabled last year. The task force intends to use the New York requirements to develop new guidelines. These could be ready for discussion at the September NAIC meeting.

In an Instant

Several instances in the last few weeks have given me new-found appreciation for the delicacy of life. How a single event, lasting only a few seconds, totally out of a person's control, can change a life forever.

It all began when I was called for jury duty. I was impaneled for a six-day trial. A family was suing a school for an accident on the playground. In an instant, their child forever lost his sight in his right eye.

About a week later, Sarah was leaving the school building for recess. She passed a fence that was protecting the kids from gas lines. Unfortunately, some children had been playing on the fence and caused some loose ends to stick out. One of these wires caught Sarah in the face as she ran by. She ended up with a 3" gash across her face, very close to her right eye. All is fine, however, and it appears that the scar will eventually fade out.

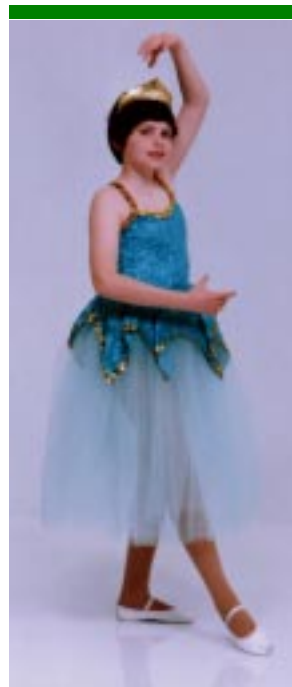
Last week I was returning from Kansas City when I got a call from Beth (my wife). Apparently her parents had just been hit by a tornado (her parents are our nearest neighbor). At the time both families were unaware of the coming storm. There had been no warnings or watches. In fact, my wife was on the phone with her mother when the tornado hit.

Fortunately, the tornado never touched the ground. It did destroy 18 trees from all sides of her parents' home. Many of these, including century-old pines, were uprooted. Except for the tree that fell on the roof, there was no damage to the house. The tornado had passed directly over the house.

Several days later, Beth & Sarah were on their way to the Des Moines airport with 3 older ladies when the

tornado sirens went off. They sought shelter in a nearby school basement. It turns out that the tornado hit about 6 blocks away.

Finally, the rains have come and the river is rising. In 1993, the Skunk River, which is a 1/4-mile away, reached within a block of this office. Flood stage is 17'. At 21', this office will be flooded. The last report is that the river is at 18.3'. There were heavy rains upstream last night. Rain is forecast for the rest of the week.



Our Ballerina

Father's Corner

It's the change of seasons for Sarah's activities. Basketball and dance are over, but swimming is just beginning.

The dance recital was last weekend, and she was beautiful. For the second year out of three, she was the "most improved" in ballet.

The first swim meet was last week. She received a 1st place

(50-meter butterfly), a 2nd place (100-meter individual medley), and a 4th place (200-meter free relay).

Tae-kwon-do continues to be a major activity for Sarah. At the Des Moines championships, she received a 2nd-place medal and 3 3rd-place medals. She received a 2nd-place and 3rd-place medal at the AAU Festival of Champions. She will compete at the National Junior Olympics in Norfolk, VA in August. She is currently scheduled to test for her black belt in September.

She is showing much more interest in the piano during the last few weeks. This seems to be motivated by finding music for the theme from "Titanic".

Van Elsen Consulting

Van Elsen Consulting is an actuarial consulting firm. **James N. Van Elsen, FSA, MAAA** is the firm's owner and is responsible for the work completed. We specialize in serving the needs of smaller life insurance companies. Most of our experience relates to product development for individual life (universal life, traditional life, and term insurance) and individual annuities.

In addition, this firm is an advocate for the interests of smaller life insurance companies. We commit significant resources to work within the regulatory environment to help reduce the burden on the smaller companies. As your company prepares for the future, please consider **Van Elsen Consulting**.

We represent smaller company interests and are ready to help.

James N. Van Elsen, FSA, MAAA
Lois Mast

Mike Staudacher

Beth Ann Van Elsen

Sarah Ann Van Elsen

Merger-Mania

It's soon to be official. When Nationwide completes its acquisition of ALLIED Life, it will also complete my personal record. Every company that I have worked for since graduating from college will have been purchased, merged, or liquidated. Ernst & Ernst became Ernst & Young, General United was merged out of existence into All American & Lincoln Liberty (General United was a consolidation of several small Iowa companies that was purchased by USLife, now an American General company), Farmland was purchased and later dissolved by Nationwide, Inter-State merged with Central with the shell later sold to Irish Life, Integrated Resources (formerly Guardsman until sold by American General) disintegrated, and now ALLIED is to be purchased by Nationwide.

I suspect that my experience is not really that unique. Just in Iowa there have been many mergers & acquisitions during the last few years. Equitable of Iowa purchased Golden American and was later purchased by IMG. Central merged with American Mutual, eventually forming AmerUS. This company has now formed an upstream mutual holding company. Continental Western was purchased by The Mutual Group. American Life & Casualty was purchased by Conseco. American Equity Investment was formed from the remains of Vulcan. Aegon, Farm Bureau and Interstate have made recent acquisitions. There have even been published rumors of a merger between Principal and Northwestern Mutual. Principal recently formed an upstream mutual holding company. Small companies have been snapped up at increasing rates by larger companies. Some of the ones that I am more familiar with include: Milwaukee, Westfield, Meridian, and New American (a Silvey company). Larger companies have also been affected. Lincoln National purchased the individual life business of CIGNA. Travelers and Citicorp are merging. Provident was purchased by Aegon. In other business sectors, we see Boeing merging with McDonnell Douglas, Boatman's Bank merging with NationsBank (which is now merging with BankAmerica), Norwest merging with Wells Fargo, SBC Communications (including Southwestern Bell) merging with Ameritech, and Chrysler merging with Daimler-Benz. Contrary to the press releases surrounding these mergers, there are always winners and losers in these consolidations.

Winners

1. **Stockholders.** They benefit from increased markets and reduced unit costs. Stockholders of acquired company may benefit from a premium price for their stock and may participate in the benefits of the larger company.
2. **Management of acquiring company.** Increased markets and reduced unit costs should help compensation plans. Stock options and other incentives usually mature for management of the acquired company.
3. **Policyholders of acquiring company.** Should benefit from reduced unit costs.
4. **Agents of acquiring company.** Often receive new products from acquired company.
5. **Large consulting firms.** Large fees from mergers & acquisitions.

Losers

1. **Policyholders of acquired company.** This group is usually promised much during the merger or acquisition. As their total size, however, becomes very small in comparison to the total, they tend to not receive the benefits afforded new business.
2. **Employees.** One of the primary ways to pay for an acquisition is to reduce expenses. This usually equates to reduced manpower. There are often commitments to handle the reductions through attrition. The same cannot be said for existing employees of the acquiring company. One of the biggest lies in these transactions is that "jobs will not be cut, in fact, we plan to increase the number of jobs locally." Often the company is able to renege on this commitment several years later when "conditions are not as favorable as we originally anticipated." Supervisory and management jobs will tend to be replaced by clerical positions.
3. **Agents.** As there are fewer companies offering products, their ability to negotiate with companies will also diminish.
4. **Competitive market.** With each company that is consolidated, there are fewer choices available to the purchaser of insurance products.
5. **Small consulting firms.** The number of potential clients keeps reducing.
6. **Regulators.** When there are only national and international companies left, there will be little need for state regulation. Each of these merged companies was originally formed by individuals with a vision for their success. Much of many people's lives have been devoted to the success of these companies. It is unfortunate that the recent merger activity will wash away all these efforts. We are hopeful that regulators will consider all the affected parties when considering future mergers & acquisitions. While these may look very good individually, the large number of such transactions cannot be good for the long-term benefit of consumers and employees.

Annuity 2000 Update

The Annuity 2000 table has been adopted by the NAIC as a new valuation standard for individual annuities. States that have progressed on adopting the table are shown in the following Annuity 2000 Scorecard and the map at the bottom of this page. Darkened states (such as Alaska) are those that are effective in 1998 or earlier. The hashed states (such as Arkansas) are expected to adopt for 1999. The bricked states (such as Alabama) have taken some action to adopt the regulation. The remaining states are on hold or in review status. Caution is advisable in reviewing this table. Many of the states contacted were not aware of the table. It is likely that many more states will be moving to adopt the table during 1998. Companies need to carefully consider the impact of the new valuation table. It may be necessary to review guaranteed settlement option rates on life insurance and annuity policy forms. It is conceivable that older guaranteed rates could result in higher required reserves, particularly for annuities. Companies should also review their current settlement option and immediate annuity rates. It may be necessary to reduce purchase rates because of the increased reserves. Tax reserves will not reflect the new mortality table until adopted by 26 states.

Annuity 2000 Scorecard

States Adopting with 1998 or Earlier Effective Date (6 States)

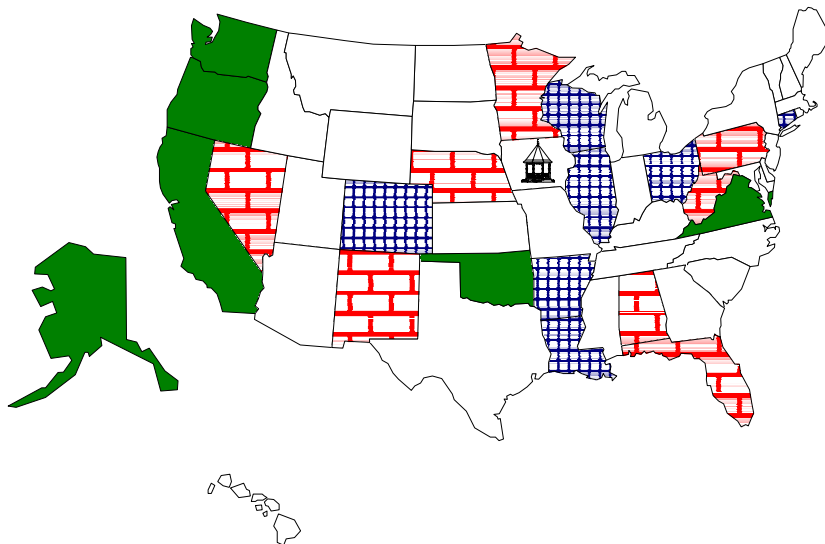
Alaska California Oklahoma Oregon Virginia Washington

States In Process with 1999 Effective Date (7 States)

Arkansas Colorado Connecticut Illinois Louisiana Ohio Wisconsin

Other States (8 States)

Alabama	Draft in process. Ready for hearing, but hasn't been scheduled.
Florida	In process of adoption.
Minnesota	Rule published. Moving forward in process.
Nebraska	In process. Hearing will be held this summer.
Nevada	In process. Hearing scheduled for June.
New Mexico	In process. Hearing held June 16.
Pennsylvania	Draft complete. Plan to publish within 6 weeks.
West Virginia	HB 4283 in legislature with the effective date undetermined at this time.



“XXX” Update

As you can see from the table below, there has been very little progress in the last 3 months on adopting “XXX”. It can be assumed that some states are waiting to see if the new proposal will be a viable model regulation. It is anticipated that states will begin to more aggressively adopt “XXX” in the coming months. It is yet to be seen whether this will be the current model regulation or a new model regulation. In the map below, darkened states (such as Illinois) are those that have adopted “XXX” with the 51% provision.. The hashed states (such as New York) are those that have adopted “XXX” without the 51% provision. The bricked states (such as Arizona) do not intend to adopt the regulation. The wavy states (such as Colorado) are in the process of adopting the regulation. If nothing changes, the current model regulation will be effective in Wisconsin on January 1, 1999. It is still anticipated that West Virginia will move back their current January 1, 1998 effective date.

The Van Elsen Report will continue to monitor progress on this regulation.

“XXX” Scorecard

States Adopting with 51% Provision (11.97%)

Illinois Kansas Maine Maryland New Mexico North Carolina Utah

States Adopting without 51% Provision (9.92%)

New York Currently effective. Currently considering change.
 West Virginia Currently effective. See article in March *The Van Elsen Report*. Call if you need a copy.
 Wisconsin Effective January 1, 1999.

States Not Planning to Adopt (25.69%)

Arizona Arkansas California Connecticut Delaware Florida Georgia Oregon South Dakota Tennessee Vermont

States Currently In Process (9.91%)

Colorado In drafting process. No hearing date set.
 Minnesota Still in early stages of drafting process. Waiting to see latest draft.
 Texas Still being considered. The effective date, unchanged at this point, would be effective on December 31, 1998 for policies issued on or after December 31, 1998.

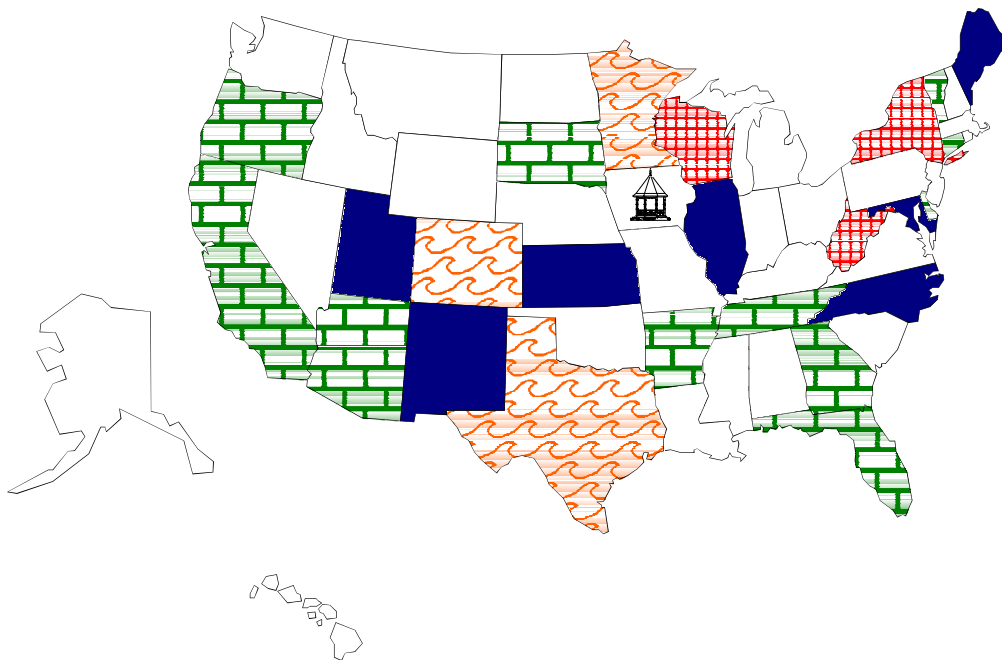


Illustration Regulation Update

The map on page 8 shows the status of the illustration regulation. Darkened states (such as Alabama) are those that are effective July 1, 1998 or earlier. The hashed states (such as Arizona) are expected to adopt on or before January 1, 1999. The bricked state (Georgia) does not intend to adopt the regulation. The remaining states (shown in the tables below) are on hold or in review status. Experience shows, however, that a state may go very quickly from review status to having the regulation in effect.

The following summary was updated June 21. It is based on interviews with insurance department personnel and other sources. We believe the information contained in this summary is accurate at the time of printing. If you have concerns or questions about a specific state's status, we encourage you to contact us. Also, please contact us if you are aware of any errors in this table. **We will be publishing an update with each of our regular newsletters in 1998.**

States Expected to be Effective on Or Before July 1, 1998 (24 States)

Alabama California Colorado Delaware Illinois *Iowa *Kansas Louisiana Maryland Nebraska Nevada *New York North Carolina North Dakota Ohio Oklahoma Oregon Pennsylvania *Rhode Island South Carolina South Dakota Utah Washington Wisconsin

States Expected to be Effective on or Before January 1, 1999 (8 States)

Alaska Arizona Connecticut *Michigan Mississippi *Missouri *Texas Vermont

* Specific State Comments

- Iowa** Liberalized \$10,000 exemption provision.
- Kansas** Deviation from model regulation. As written, it applies to changes to existing policies which are achieved through a new sales effort or for which underwriting is required.
- Michigan** Permits companies to use the same interest rate illustrations as in states adopting the Illustration Regulation.
- Missouri** Bill passed & waiting governor's signature. Hope to be effective January 1, 1999. Adds exemptions for companies with less than \$25 million in premiums, single premium policies, and for policies with only guaranteed elements.
- New York** Regulation of life insurance illustrations is effective January 1, 1998. The annuities illustration regulation is still under development. The anticipated effective date of June 30, 1998 will probably be set back. The illustration regulation for variable life insurance and annuities is scheduled for January 1, 1999.
- Rhode Island** Passed Senate. Hoping for an effective date of June 30, 1998.
- Texas** Hope for September 1, 1998 effective date. May be postponed. Still differences with model regulation.

Status in Other States

State	Status	Comments
Arkansas	No plan to implement.	
District of Columbia	On hold.	
Florida	On hold.	
Georgia	No plan to adopt.	
Hawaii	Review status.	
Idaho	No proposed action to 1998 legislature.	

Status in Other States

State	Status	Comments
Indiana	Review status.	
Kentucky	Reviewed. On hold.	
Maine	Reviewed & moving to rule making.	
Massachusetts	On hold.	
Minnesota	Review status.	
Montana	Review status. No legislature until 1999.	
New Hampshire	Drafting process.	
New Jersey	Still pending.	
New Mexico	Hearing held June 16.	Similar to NAIC model.
Tennessee	On hold.	
Virginia	Review status.	
West Virginia	Currently in final evaluation.	Will consider for legislative action in 1999.
Wyoming	On hold.	

