



NAIC Meeting in Seattle

Codification Sent to Ad Hoc Committee

Report in January

Codification proved to be a hot topic during the Executive Committee session at the winter meeting of the National Association of Insurance Commissioners (NAIC). Rather than resolving the conflicts at this meeting, it was proposed by Commissioner Musser (Wisconsin) that an Executive Ad Hoc Committee review the items in conflict. Commissioner Musser is the outgoing NAIC president. The committee, as charged, will be composed of at least six commissioners, including at least one from each of the zones. States expected to participate on the

committee include: Alaska, Illinois, Iowa, North Dakota, Ohio, and Virginia. Although they will be focusing on the issues listed below, they were

Executive Committee also adopted the MIL (defined standards) at this meeting. See next article.

Time to Renew!!!

This completes the 3rd year of *The Van Elsen Report*. The subscription cost for 1998 is \$25. Enclosed with this newsletter is an invoice for 1998.

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2. **Reinsurance Questions & Answers.** This is a document that was created to interpret the Life & Health Reinsurance Agreements Model Regulation. The NAIC, however, has never formally adopted the document. There are many that maintain that the document prohibits

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not restricted from reviewing other aspects of Codification.

The two major issues are as follows:

1. **Model Investment Law (MIL).** References to the MIL (defined limits) have been removed from the main Codification document. An appendix attached to the Codification, requires additional disclosure of amounts relative to the MIL (defined limits). This appendix contains specific references to the MIL (defined limits), which is ironic since the

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practices that are permitted by the model regulation. This document is attached as an appendix to the Codification.

The ad hoc committee is expected to report back to the Executive Committee by the end of January. It could then be reconsidered by the full Executive Committee in Salt Lake City in March. If the Executive Committee adopts it at that time, it could be considered by Plenary in June.

Earlier in the meeting, Patrick Shoumlin addressed the Codification of Statutory Accounting Principles Working Group regarding Codification's status as an "Other Comprehensive Basis of Accounting (OCBOA)." Attainment of this status is the primary reason that the Codification initiative was begun. Patrick Shoumlin is the chair of the Insurance Companies Committee (ICC) of the American Institute of Certified Public Accountants.

The ICC is scheduled to vote on OCBOA status for Codification in early January. Concern was expressed about Codification provisions which give the commissioner ability to make exemptions to Codification. Approval is also likely to be contingent on a significant number of states approving Codification.

MIL to Plenary

The defined standards version of the Model Investment Law (MIL) was adopted without much discussion by the Executive Committee. It will be considered by Plenary in March.

This model law, also known as the "Prudent Person MIL," has been the source of much controversy during the last several meetings.

NAIC Changes

Several changes in meeting procedures were made at the Seattle meeting. In addition, several

committee changes were recommended during the meeting.

1. The official meeting ended on Tuesday rather than on Wednesday.
2. Meetings tended to be scheduled earlier and ended later.
3. Minutes of sessions were no longer available to attendees during the meeting.
4. Minutes will now be available to everyone on the NAIC's web site (www.naic.org). They are expected to be available by January 12, 1998. Meeting registrants will be able to download the minutes free through the end of January. All others must pay \$25 per set. A set includes the parent committee, associated task forces, and working groups and attachments, when available. The minutes will be in Word 97 format only.
5. Most working group, task force, and committee reports were made without benefit of printed minutes.
6. **Annuity Working Group.** This "A" Committee working group recommended that it be disbanded. As part of this recommendation, the working group recommended that the Life Disclosure Working Group be assigned the charge to develop suitability standards for the sale of annuities to seniors. They further recommended that the "A" Committee change its name to the "Life Insurance & Annuities (A) Committee."
7. **Nonforfeiture Working Group.** This is a working group of the Life & Health Actuarial Task Force (LHATF). It also recommended that it be disbanded. See next article. It is likely that a new

working group will be formed that will focus on valuation, disclosure, and nonforfeiture matters.

8. **Annuity Working Group.** This LHATF working group recommended that it be renamed the Innovative Products Working Group.

NF Project Halted

The complexity of dealing with new product types and lack of a consensus has forced the LHATF to table the current nonforfeiture project. It is expected to be brought up again as progress is made on disclosure and valuation issues. A new working group is expected to be formed which will focus on these items.

Tom Foley, actuary from North Dakota & chair of the LHATF believes that nonforfeiture can be revisited at the fall meeting.

AOMR Postponed

A small working group of the LHATF was formed to resolve issues related to a new Actuarial Opinion & Memorandum Regulation (AOMR). Regulators from California, Illinois, South Carolina, and Utah are on the working group.

The LHATF believes that there is a consensus on many aspects of the new AOMR. These include:

1. Add a derivatives test to the Section 7 qualification tests.
2. Eliminate the actuarial certification of any required benchmark reserve statement.
3. Eliminate the requirement for the actuary to identify the change in surplus associated with the benchmark standard.

The benchmark has been proposed to allow regulators to evaluate how a company's reserves compare to a common standard. This could be

then used as a tool to evaluate compliance with individual state valuation requirements. Codification has been proposed as a standard for the benchmark.

The small working group will primarily consider issues related to the benchmark standard. This would include the basis of the standard, the effective date, and the level of detail required.

There is also dissension from several companies & the National Alliance of Life Companies (NALC) with regard to the gross premium valuation requirement proposed for Section 7 opinions.

The working group is expected to make a report at the spring meeting.

Annuity Illustrations

Two long meetings were held in Seattle to discuss the new draft of the Annuity Disclosure & Illustration Model Regulation. Several issues remain unresolved, however, and an interim meeting will be held in February.

The industry has been requested to provide specific input on the many drafting issues that remain. Another issue is the application of the life concepts of "disciplined current scale," "self-support test," and "lapse-support test" to annuities. The American Academy of Actuaries (AAA) has been asked to provide input on this matter for the February meeting.

"Re-GRET"

The 1998 version of the Generally Recognized Expense Table (GRET) was discussed by the Life Disclosure Working Group. The table will become effective on April 4, 1998. The issue is whether statements filed before April 4 need to be updated using the new GRET.

The working group declined to give specific guidance, deferring to

individual state requirements. The Society of Actuaries appears to be recommending that opinions after April 1, 1998 be based on the new GRET. Opinions prior to that would be based on the original GRET, with the opinion updated a year later based on the then-current GRET.

Replacements

Work continues in the Replacement Issues Working Group on a new Model Life Insurance & Annuities Replacement Regulation. Two meetings were held in Seattle discussing the many issues that have arisen from the draft.

Many issues still remain. The working group plans to have a conference call in January to resolve some of these issues. They hope to adopt the model regulation at the March meeting.

Gorski Gets Award

Larry Gorski, actuary for Illinois, received the Robert Dineen Award at the opening session of the Seattle meeting. The Robert Dineen Award is the NAIC's most prestigious individual award.

Larry has been with the Illinois Department of Insurance since 1973. Since that time, he has been very involved in NAIC matters. He has been particularly active on LHATF, the Risk-Based Capital Task Force, and the Valuation of Securities Task Force.

Most recently, Larry was active in developing standards for equity indexed annuities. He was a key member of the AAA task force on this matter.

I marvel at the amount of work that Larry accomplishes. While I don't always agree with Larry's positions, I can count on them being well researched and thought out. I have also found Larry very willing to listen to opposing viewpoints.

Congratulations Larry!!! It is an award well deserved.

AAA on Valuation

The AAA Valuation Task Force presented an interim report to LHATF in Seattle. This interim report was presented by Bob Wilcox, chair of the task force and former Utah Insurance Commissioner.

The report develops the concept of a Unified Valuation System (UVS). This system "addresses needs of all of the various users of the valuation system with a primary focus on policyholder interests in terms of current & future insurer solvency."

The following framework for UVS is quoted from the report:

1. Provide information to policyholders, regulators, and others to assist them in making informed judgments about insurers' financial condition.
2. Support financial analysis both at points in time and over time.
3. Be built upon best estimate assumptions with explicit determinable margins.
4. Address overall solvency, not just contract reserves; in particular, address resources consistently with obligations.
5. Produce auditable and verifiable results and incorporates an actuarial "feed back loop" in which assumptions and projected results are compared to emerging experience.
6. Cover all insurance activities; it is holistic, considers the entire enterprise, rather than merely representing a sum of independent parts.
7. Balance practicality, cost, and resource effectiveness in relation to the value of the information to the audience.
8. Be consistent for all companies and among regulatory jurisdictions.

9. Be flexible, e.g., be able to accommodate unidentified future needs.
10. Utilize actuarial judgment in the development and interpretation of results in preference to prescribed methods and assumptions.
11. Accommodate materiality issues. The following objectives were identified in developing the UVS:
 1. Evaluation of ability of a company to execute various business alternatives.
 2. Evaluation of the adequacy of resources relative to obligations.
 3. Measurement of changes in resources relative to obligations.

The next phase of the project includes the following:

1. Evaluation of the methods and tools needed to implement the UVS.
2. A strategy for implementing the UVS.
3. A draft model law on the UVS.

The task force hopes to present the final report on the UVS to LHATF at the 1998 winter NAIC meeting.

Final EIP Report

Donna Claire and Steve Preston presented the AAA final report of the Equity Indexed Products Task Force. The comprehensive report addressed many actuarial aspects of these products (EIP's). Among the significant highlights of the report are the following:

1. Concluded that EIP's were similar to other insurance products.
2. Determined that the Standard Nonforfeiture Laws could accommodate EIP's.
3. Recommended clear disclosure.
4. Proposed reserve methodologies.

5. Recognized that investment methods must conform with any investment limitations for insurance companies.
6. Drafted a Practice Note for appointed actuaries responsible for signing off on the asset adequacy analysis.
7. Responded to the SEC request for comment.
8. Discussed the effect of reserving methodologies on tax reserves.
9. Worked with the risk-based capital and AVR/IMR task forces on proper classification of EIP's.
10. Recommended that EIP's be treated on par with other annuities and life insurance with regard to guarantee funds.

LHATF is currently working on Actuarial Guideline ZZZ, which addresses reserves for EIP's. Although LHATF has not finished its review of the guideline, Illinois has announced that they will expect compliance with the guideline for the 1997 Annual Statement.

Jerry Fickes Retires?

Jerry Fickes, actuary from New Mexico, announced at the A&H Working Group of LHATF that he will be retiring in 1998. He indicates that he won't be making plans until he leaves the department.

Jerry retired once before when he left consulting. During this "retirement" he served for a period as Acting Commissioner for New Mexico.

I have known Jerry since the late '70's, when he worked for FIC & Associates in Kansas City.

Good luck Jerry in however you choose to "retire."

Father's Corner

First, an update on Tae-Kwon-Do. You will recall that **Sarah** needed to break 1" boards in order to receive her **red** belt. The testing was going very fine until it was time to break the boards. She was down to her last chance to qualify for her red belt. Receiving this belt was **very** important to her. She slowed down, focused, and the boards finally broke! In January, she will be testing for her **red-black** belt. The boards will be much more difficult. If successful, she will test in April for her black belt, recommended. She could earn her black belt in July.

She also competed in a couple of tournaments. At the Mid-Iowa Championships in Des Moines, she received three trophies and a medal. One of the trophies was 1st place in sparring. She was the only girl in the event and most of the boys were black belts.

At the tournament in Appleton, Wisconsin, **Sarah** competed well and received two medals.

Sarah had her 1st piano recital this fall and did very well. She also did very well at two Christmas programs where she played solos. She has her mother's gift for music.

Basketball is her current focus. Her grandfather (former girls' basketball coach) has high hopes for her.

Sarah will turn nine on January 4.

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. 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. This mortality table won't be used for tax purposes until 26 states have adopted it. Again, this could be a pricing factor to consider for 1998.

Annuity 2000 Scorecard

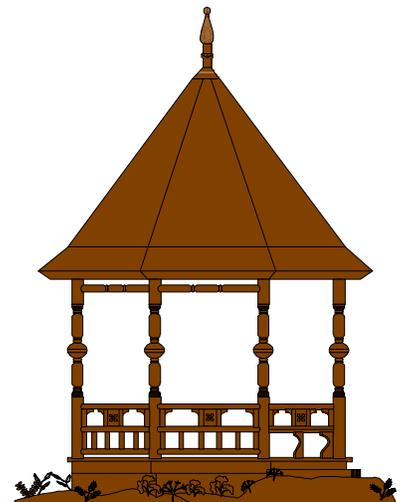
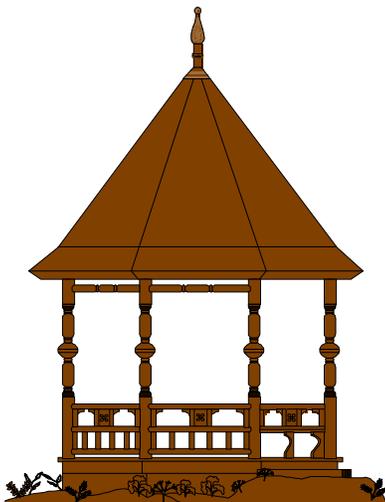
States Adopting with January 1, 1998 Effective Date

California Oregon Virginia

States In Process

Alaska	Will adopt early in 1998.
Connecticut	Hope June 1, 1998.
Illinois	On agenda for 1998.
Louisiana	In process. Hope January 1, 1999.
Minnesota	In process. Anticipate January 1, 1998 effective date.
Washington	Pending.
Wisconsin	In drafting stage.

Seattle Skyline



"XXX" Update

The summary below shows the states that have a position on "XXX." Illinois adopted it with a unique provision in 1996. This regulation will not become effective until states representing 51% of the population have adopted similar regulations. Several states have adopted "XXX" with a provision similar to the Illinois provision.

As you can see from the table, states that have adopted the regulation now total 21.89%. Another 9.91% are in process of adopting for a potential total of 31.80%. California, representing 11.97%, has chosen not to adopt "XXX," although they are currently reevaluating that position. Currently, states representing 25.69% of the population do not appear to be adopting the regulation. The

remaining states (representing 42.51%) have not taken a position on "XXX."

It would appear that it is not likely that enough states will adopt "XXX" in order for the 51% provision to be effective. With Wisconsin & Texas moving to certain dates, however, the issue becomes more complicated. This is a situation sure to cause chaos in the term & universal life insurance markets.

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

NALC Proposal

The Actuarial Committee of the NALC has issued a statement outlining a recommended alternative to "XXX." The statement acknowledges that the Standard Valuation Law (SVL) is the governing law for these policies. Basic reserves, therefore, are to be

calculated according to the SVL.

The statement further recommends that the Actuarial Opinion & Memorandum Regulation be modified to require a separate gross premium valuation for term insurance and universal life with secondary guarantees.

Contact us if you need additional information about the proposal. You may find additional information in *The National Underwriter* on October 6, 1997 (reprint attached) and December 8, 1997.

The NALC is expected to present its alternative to LHATF's new Innovative Products Working Group in March.

"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 Effective January 1, 1998. Expected to modify to have 51% provision.
Wisconsin Effective January 1, 1999.

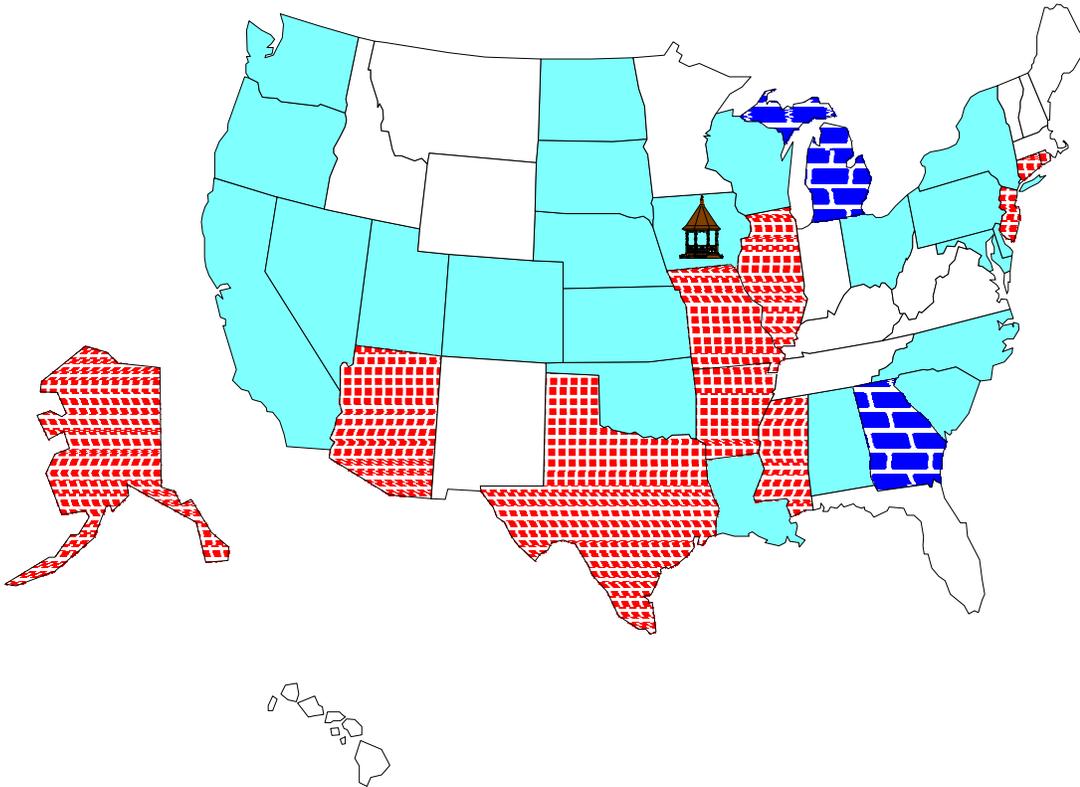
States Not Adopting (25.69%)

Arkansas No action intended until 51% of population adopts.
California Current bulletin requires special analysis of term reserves. Does not meet the definition for the 51% provision. Considering changing position to adopt "XXX".
Connecticut Believed to be working on an approach similar to the California bulletin.
Delaware No plan to adopt.
Florida Regulation would conflict specifically with current law.
Georgia No plan to adopt.
Oregon No plan to adopt.
South Dakota No plan to adopt.
Tennessee Not going to adopt.

States Currently In Process (9.91%)

Colorado In drafting process. No hearing date set.
Minnesota Moving forward. Still in early stages.
Texas Anticipate hearing in January. Current draft would be effective on December 31, 1998 for policies issued on or after December 31, 1998.

Illustration Regulation Update



This map shows the status of the illustration regulation. **Darkened states** (such as Alabama) are those that we expect to have the regulation effective on January 1, 1998 or earlier. The **hashed states** (such as Arizona) are currently progressing on adoption. **Bricked states** (Georgia & Michigan) do not intend to adopt the regulation. The remaining states (not shown in the tables below) are on hold or in review status. Experience this year, however, shows us that a state may go very quickly from review status to having the regulation in effect.

The following summary was updated December 20. 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 Effective on Or Before January 1, 1998 (22 States)

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

* 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.

New York Regulations for implementation have not been adopted. Effective date will be January 1, 1998.

Pennsylvania Review annuity provisions.

Status in Other States

State	Status	Effective Date	Comments
Alaska	Final drafting stage.	Planned March 1, 1998	
Arizona	Drafting stage.		
Arkansas	Reviewed. No hearing date set.		
Connecticut	Submitted to legislature.	June 1, 1998	
Georgia	No plan to adopt.		
Illinois	Moving forward.	Proposed June 1, 1998	Some variations from model regulation.
Michigan	Don't anticipate adopting.		Rule has been issued which permits the use of the model regulation format. Do not intend to adopt other provisions.
Mississippi	Moving forward.	1998	
Missouri	Governor vetoed bill.		
New Jersey	Draft to be proposed in January.		
Rhode Island	Died in session.		
Texas	Moving forward.	1998	Closer to NAIC model. Still significant differences.

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.

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