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The Honorable Thomas Hampton  
Chairman – NAIC PBR Ex Working Group  
Commissioner – Dept. of Insurance, Securities, and Banking  
Union Center Plaza  
810 First Street, NE  
Washington, DC 20002

Re Experience Reporting Requirements of Principle-based Reserves

Dear Commissioner Hampton

The ACLI is pleased to submit the following comments regarding the experience reporting requirements of Principle-Based Reserves on behalf of our member companies. The American Council of Life Insurers represents three hundred fifty-three (353) member companies operating in the United States, of which three hundred forty-five (345) are legal reserve life insurance companies, and eight (8) are fraternal benefit societies. These 353 member companies account for 93 percent of total assets, 93 percent of the life insurance premiums, and 94 percent of annuity considerations in the United States.

One component of the proposed PBR framework for US life insurance industry is the mandatory experience reporting requirements. ACLI appreciates the opportunity to comment on this component of the PBR process, which has not yet received extensive comment and discussion. at the Working Group. Two aspects of the experience reporting requirements stand out as critical: a) a clear and realistic definition of the purposes of the mandatory experience requirements, and b) the establishment of cost controls and an appropriate funding mechanism. This letter outlines industry's view of those two critical elements, along with preliminary thoughts on the experience reporting framework as currently documented in the Standard Valuation Law Amendments and in the Valuation Manual sections 50 and 51. Industry's view is different than contained in the current drafts of those Valuation Manual sections.

### **Purposes Of The Experience Reporting Requirements**

The purposes of the experience reporting requirements should be clearly understood at the outset for the resulting processes to be effective and efficient. VM-50 Section A.2 identifies nine values of experience reporting. ACLI believes that these may be distilled into two primary intended uses for the experience reporting submissions:

1. As input to industry experience studies, with results ultimately summarized in industry tables and reports. These reports may include information of the range of company variation around the industry averages, done in a way that does not allow identification of individual companies. The resulting industry tables and reports may be used by companies to blend with less than fully credible company-specific experience, and by

regulators or others as a yardstick against which to measure companies' PBR assumptions.

2. As a "data source of record" for raw, company-specific experience data that state examiners, and possibly other PBR reviewers, may draw from to validate a company's experience assumptions.

It needs to be recognized that these two intended uses differ in the extent to which they require, or indeed benefit from, participation by all companies. On the one hand, an industry experience study can be done effectively and well—and most efficiently— by using data from fewer than 100 companies representing the majority of business sold. Trying to incorporate data from all companies in such a study would actually create overwhelming cost for the statistical agents and actuarial analysts for little additional benefit. (e.g., to scrub raw data; to determine appropriate mappings to comparable, homogeneous subclasses within the study; etc.). On the other hand, to be a "data source of record," every regulated company must submit data.

Industry experience studies can be useful and are integral to the proposed design of the new principles-based reserve system. Previously, such studies have been conducted on a voluntary and sometimes ad hoc basis. With the advent of PBR, ACLI agrees that studies should occur on a more regular basis and that the current voluntary structure should change to a more systematic structure, mandatory for some but not all companies. We stand ready to work with regulators to devise that requirement.

While ACLI believes that industry experience studies is an important purpose for data collection, we believe that the second use, as a raw data source of record, is unnecessary and inadvisable and should be replaced with simpler requirements addressing documentation of, and retention of, support for company experience assumptions. Our rationale is described below.

- It is inconsistent with risk-focused examinations. Examinations have been moving toward being risk focused. Comparing experience data with assumptions for a detailed validity check is not consistent with the general direction being taken by the NAIC for examinations and should only occur on rare occasions.
- Company information should be accessed directly from the company. While Insurance Departments generally have broad rights to ask companies for information, we do not believe that they should be able to obtain such information from third parties.
- It is redundant. Documentation of the basis for all assumptions, and of the underlying experience studies and results, is already required and should be the focus of any review. In general, there should be no need to go to the raw data, nor is such access useful. If the documentation requirement needs strengthening, we should address that directly, not obliquely through raw data collection from all. If the integrity of the documentation, data or the analysis is suspect, that can be pursued through the audit process in the few cases where it is necessary.
- It would provide minimal benefits. Because raw data is so difficult to work with, in practice an examiner would need to turn to the submitting company for assistance in grouping, analyzing and interpreting the data. We see no utility in the examiner pursuing a review of the raw data without notice to the company, and no practical likelihood of completing that review effectively without company assistance. Even if the data can be reviewed, such a review does not validate whether or not the valuation assumptions were appropriate.
- It would impose unnecessary additional costs. As noted above, a blanket requirement that all companies submit raw data in an industry standard format is costly for submitting companies, costly for the statistical agent and analysts, and unnecessary and impractical to develop good industry experience studies. For companies, there is the cost of converting internal data to the industry standard format. For the statistical agent and

data analysts, there is a cost to incorporate each additional data contribution, as actuaries who have been involved in industry studies can well attest. (This is true regardless of whether the data is pre-scrubbed thoroughly by the submitting company, and doubly true if it is not.) The point of diminishing returns is quickly reached.

### **Cost Controls and Funding Mechanism**

At the end of the day consumers will pay for the experience reporting process and only necessary costs should be incurred. ACLI believes that the first and most important aspect of cost control is to focus the experience reporting requirements on the key intended use: developing industry experience studies. Targeting efforts toward that end will allow for a more streamlined, less costly process, involving fewer than all industry participants.

A second aspect of cost control is restraint and discipline in determining the analyses to be made of the data. The Valuation Manual currently places few limits on the analyses to be performed. ACLI believes that that could invite waste, because so many “interesting questions” could be explored as we enter the new world of principles-based analysis. We believe that there should be an intensive dialogue between regulators and industry to define a limited set of truly essential reports at the inception of PBR. Later as experience with PBR develops, the report list can be revised via changes to the Valuation Manual. At all times, there should be at least some requirement to justify the benefits versus cost of any additions to the reports.

A third aspect is the payment structure or mechanism funding for the experience studies. The new SVL currently does not authorize any form of tax, nor does it specify who is to pay, or on what basis. ACLI believes that the funding should adhere to the following basic approach:

- All companies that benefit from the studies should contribute to the cost whether or not they contributed data.
- Those companies whose data contributions are more expensive to process due to data quality defects in their submissions should expect to pay more.
- A fee structure should be established in advance. Allocating costs after the fact provides no incentive for cost control.

One possible approach is to have the NAIC pay the statistical agent, and collect the requisite funding from companies through filing fees.

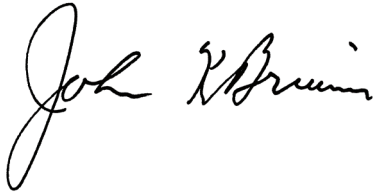
In closing, we believe it is essential that a clear, focused and cost effective experience reporting and analysis process be developed. This new mandatory system will replace a long-standing voluntary system. While some aspects of that voluntary system may carry over to the new system, many aspects will need to be rethought.

In addition to the above two issues, there are a host of other issues that need to be addressed. These issues include:

- Authority & legal structure – What is the legal framework around engaging the statistical agent(s) and paying for the collection, analysis and reports?
- Regulatory oversight – Does the Commissioner enforce submission for domestic companies, or for all companies?
- Scope – what products are covered? What types of experience are to be studied?
- Reports – What reports are expected at the end of the analysis? To whom are the reports provided?
- Work Flow – role of statistical agents, professional organizations and others, confidentiality and access to data, and various levels of reports.

We look forward to further discussions of these critical matters at the NAIC Winter National Meeting.

Sincerely

A handwritten signature in black ink, reading "John R. Brennan". The signature is written in a cursive style with a large, looping initial "J".

CC    Todd Sells  
      John Engelhardt  
      Fred Andersen  
      Life and Health Actuarial Task Force