We would like to address some comments made at the 2014 Spring National Meeting regarding the use of VM-20 as the actuarial method in the Rector Report’s proposed framework (Feb. 17, 2014). Please note our input below represents our views and has not been vetted with LATF.

One issue was whether it is more appropriate to use one aggregate margin versus the individual margins by risk. For many years regulators have employed the methodology of applying individual margins assumption by assumption. Said another way, each key assumption (e.g. mortality factors, etc.) is made a bit more conservative than otherwise indicated. This same methodology was used for principle-based reserves (PBR) when VM-20 was developed. While we are interested in the theory of using an aggregate margin, we do not believe that we will be ready to revise VM-20 to use an aggregate margin in the timeframe needed for the actuarial method. But VM-20 can be used in the short-term and for initial implementation for PBR. Just as we do for all other parts of our financial regulatory regime, we can make improvements over time.

A second issue is that a simpler, more auditable approach could be used rather than VM-20. One idea is to lower the key assumption of mortality for level premium term insurance and to develop a similar alternative for universal life with secondary guarantees. While this would lower reserves it would tend to be a one-size-fits all approach and would, therefore, not achieve a better “right-sizing” of reserves given the products and experience company by company are significantly different. VM-20 would get closer to being right-sized and the aim of the reserve level being an economic reserve plus a margin(s).

Lastly, the NAIC will need to decide whether adjustments should be made to VM-20. We believe that some changes can be made to VM-20 for use in this framework which will minimize the differences between what would be implemented in this framework and what eventually may be implemented for initial PBR. We are not saying that VM-20 is perfect, even with consideration of certain adjustments, but the Towers Watson Study, industry and professional comments regarding PBR seem to support that VM-20 is a major step in the right direction for right-sizing reserves.

We hope these comments are useful in the Task Force’s efforts to address their charge regarding these types of captives and we would be glad to answer any questions or provide additional information as needed.