Valuation Manual Holds the Details

The NAIC took an important step toward a principles-based approach to insurance reserving with its September 23, 2009 vote to approve a revised Standard Valuation Law (SVL). The model law represents the core of the NAIC’s new framework for setting reserves for life and annuity products. Some observers thought the 2008-2009 financial crisis would slow down PBA efforts, but this vote signals the NAIC’s resolve to enable a regulatory regime based on modern principles of risk analysis and stochastic modeling.

However, approving revisions to the SVL represents the first stage of the initiative; getting through the next stage will be an even bigger feat. The model law won’t begin its long march through the state approval process until the Valuation Manual (VM) is completed and approved by the NAIC (Life Insurance and Annuities Committee). The NAIC means to send state legislatures a package that includes both the Law and the Valuation Manual. In effect, the states will vote on the SVL, which references the VM, and not the VM itself. For now, the new SVL is parked while it waits for the manual, which is still a work in progress, to catch up.

Details Are in the Manual

The SVL was left intentionally general and free of the technical reserve requirements; the manual carries that weight. No one is expecting adoption of this package to be easy or conflict-free, either at the NAIC level later this year or within the individual states later on. Partitioning the details into a manual separate from the law may simply shift the focus of debate from the content of the law to the content of the manual. But most observers agree that the approach the NAIC is taking will move the industry closer to the goal of uniform valuation laws across states.

Once the new framework is in place, changes to valuation guidelines will be made much more quickly and uniformly than the current process. It’s important to note that the NAIC alone will review and approve changes to the manual; individual states do not need to do so. The VM will serve as a living document that can be updated as needed and implemented without having to wait for individual states to approve the changes to become effective. In this respect, the manual will function similar to the NAIC Accounting Practices and Procedures Manual or the RBC Instructions.

The Valuation Manual is expected to be completed and presented to the NAIC for approval in mid-2010. At the December NAIC meeting, it was voted that the manual would be voted on at the August 2010 NAIC meeting. Assuming the manual is completed and approved by the NAIC in 2010, the model law and the manual likely will begin winding its way through the state adoption process.

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process during 2011. The new law/manual will not become effective until the first day of the first January after 42 states have adopted it. At this point, a five-year grade-in period is also part of the adoption process.

Once the SVL/VM is passed by the states, it will become the standard without the usual vetting process for which the industry has become accustomed. This represents a significant departure from the past, so uncertainty around state adoption is understandable. Will all states adopt SVL and VM as approved by the NAIC or will they make significant changes to both? We’ll have to wait and see, and, perhaps, do as Bette Davis advised in the movie All About Eve: “Fasten your seatbelts, it’s going to be a bumpy night.”

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Most sections of the valuation manual are complete, but some of the toughest issues are still being crafted by members of the NAIC Life and Health Actuarial Task Force with industry input. The life products section (VM-20) has the most critical outstanding issues, notably those related to a net premium reserve calculation, taxation and maintaining deductions for reserve credits, stochastic modeling requirements and the frequency of reviews.

The current sections of the manual include:
- VM-00 Valuation Manual Minimum Standards
- VM-01 Definitions
- VM-02 SVL
- VM-20 Life Products
- VM-21 Variable Annuity
- VM-22 Non-Variable Annuity
- VM-25 Health Insurance
- VM-26 Credit Life and Disability
- VM-30 Actuarial Opinion and Memorandum Requirements
- VM-31 Reporting and Documentation Requirements
- VM-50 Experience Reporting Requirements
- VM-51 Experience Reporting Formats
- VM-Appendix A: Non-PBR Requirements
- VM-Appendix C: Actuarial Guidelines
- VM-Appendix G: Corporate Governance
- VM-Appendix I: Reserve Methodology
- VM-Appendix II: Capital Methodology
- VM-Appendix III: US v. International
- VM-Appendix IV: Governance