



ACTUARIAL STANDARDS BOARD

• EXPOSURE DRAFT •

**Proposed Revision of
Actuarial Standard
of Practice
No. 24**

**Compliance with the
NAIC Life Insurance Illustrations
Model Regulation**

**Comment Deadline:
September 30, 2016**

**Developed by the
Task Force to Revise ASOP No. 24 of the
Life Committee of the
Actuarial Standards Board**

**Approved for Exposure by the
Actuarial Standards Board
June 2016**

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June 2016

TO: Members of Actuarial Organizations Governed by the Standards of Practice of the Actuarial Standards Board and Other Persons Interested in Compliance with the NAIC Life Insurance Illustrations Model Regulation

FROM: Actuarial Standards Board (ASB)

SUBJ: Actuarial Standard of Practice (ASOP) No. 24

This document contains an exposure draft of a proposed revision of ASOP No. 24, *Compliance with the NAIC Life Insurance Illustrations Model Regulation*. Please review this exposure draft and give the ASB the benefit of your comments and suggestions. Each response will be acknowledged, and all responses will receive appropriate consideration by the drafting committee in preparing the final document for approval by the ASB.

The ASB accepts comments by either electronic or conventional mail. The preferred form is e-mail, as it eases the task of grouping comments by section. However, please feel free to use either form. If you wish to use e-mail, please send a message to **comments@actuary.org**. You may include your comments either in the body of the message or as an attachment prepared in any commonly used word processing format. **Please do not password protect any attachments. If the attachment is in the form of a PDF, please do not “copy protect” the PDF.** Include the phrase “ASB COMMENTS” in the subject line of your message. Please note: Any message not containing this exact phrase in the subject line will be deleted by our system’s spam filter. Also please indicate in the body of the e-mail if your comments are being submitted on your own behalf or on behalf of a company or organization.

If you wish to use conventional mail, please send comments to the following address:

ASOP No. 24 Revision
Actuarial Standards Board
1850 M Street, NW, Suite 300
Washington, DC 20036

The ASB posts all signed comments received to its website to encourage transparency and dialogue. Unsigned or anonymous comments will not be considered by the ASB nor posted to the website. The comments will not be edited, amended, or truncated in any way. Comments will be posted in the order that they are received. Comments will be removed when final action on a proposed standard is taken. The ASB website is a public website, and all comments will be available to the general public. The ASB disclaims any responsibility for the content of the comments, which are solely the responsibility of those who submit them.

Deadline for receipt of responses in the ASB office: **September 30, 2016**

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Background

The ASB adopted ASOP No. 24, *Compliance with the NAIC Life Illustrations Model Regulation*, in 1995. Since the promulgation of the original standard, life insurance product innovation has continued. In 2007, ASOP No. 24 was revised to be consistent with the current ASOP format and to update and reflect current, appropriate actuarial practices with respect to illustrations prepared in compliance with the *Life Insurance Illustrations Model Regulation (Model)*. In 2015, the National Association of Insurance Commissioners released Actuarial Guideline 49 (AG 49) to clarify certain requirements of the *Model* related to policies with index-based interest credits. The Task Force to Revise ASOP No. 24 of the Life Committee of the ASB prepared this revision to reflect the changes effected through AG 49 and to add some clarification, in particular to section 3.6, Requirements to Prevent Lapse-Supported Illustrations.

Request for Comments

The ASB would appreciate comments on the proposed revisions to this ASOP and would draw the reader's attention to the following areas in particular:

1. Does the exposure draft appropriately reflect the new Actuarial Guideline 49?
2. Does section 3.6 provide sufficient guidance to actuaries practicing in this area?

The ASB voted in June 2016 to approve this exposure draft.

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ACTUARIAL STANDARD OF PRACTICE NO. 24

**COMPLIANCE WITH THE
NAIC LIFE INSURANCE ILLUSTRATIONS
MODEL REGULATION**

STANDARD OF PRACTICE

Section 1. Purpose, Scope, Cross References, and Effective Date

- 1.1 Purpose—This actuarial standard of practice (ASOP) provides guidance to actuaries when performing professional services pursuant to applicable law based on the National Association of Insurance Commissioners (NAIC) *Life Insurance Illustrations Model Regulation (Model)* and related NAIC actuarial guidelines or when performing professional services with respect to illustrations represented to be in accordance with the *Model*.
- 1.2 Scope—This standard applies to actuaries when performing professional services to provide or support an actuarial certification pursuant to an applicable law based on the *Model*. The *Model* applies to illustrations, both for proposals and in-force policies, as described in the *Model*, for group and individual life insurance other than variable life insurance. The *Model* does not apply to individual and group annuity contracts, credit life insurance, and life insurance policies with no illustrated death benefits on any individual exceeding \$10,000. NAIC Actuarial Guideline 49 (AG 49) is related to the *Model* and applies to certain life insurance policies that are subject to the *Model* and that provide interest credits linked to an external index or indices.

This standard applies to actuaries when performing professional services with respect to illustrations in the absence of applicable regulations if the illustrations are to be represented as being in accordance with the *Model*.

This standard does not apply to actuaries when performing professional services with respect to the determination of **nonguaranteed elements** payable. Determination of these items, as well as illustrations not included in the scope of this ASOP, are covered by ASOP No. 2, *Nonguaranteed Charges or Benefits for Life Insurance Policies and Annuity Contracts*, or ASOP No. 15, *Dividends for Individual Participating Life Insurance, Annuities, and Disability Insurance*.

If the actuary departs from the guidance set forth in this standard in order to comply with applicable law (statutes, regulations, and other legally binding authority), or for any other reason the actuary deems appropriate, the actuary should refer to section 4.

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- 1.3 Cross References—When this standard refers to the provisions of other documents, the reference includes the referenced documents as they may be amended or restated in the future, and any successor to them, by whatever name called. If any amended or restated document differs materially from the originally referenced document, the actuary should consider the guidance in this standard to the extent it is applicable and appropriate.
- 1.4 Effective Date—This standard is effective for actuarial services performed on or after four months following adoption by the Actuarial Standards Board.

Section 2. Definitions

The terms below are defined for use in this actuarial standard of practice. Definitions 2.2, 2.3, 2.6, 2.7, and 2.8 are intended to conform to those in the *Model*.

- 2.1 Actual Experience—Historical results and trends in those results.
- 2.2 Currently Payable Scale—A scale of **nonguaranteed elements** in effect for a policy form as of the preparation date of the illustration or declared to become effective within the next 95 days.
- 2.3 Disciplined Current Scale—A scale of **nonguaranteed elements**, certified annually by the **illustration actuary**, constituting a limit on illustrations currently being illustrated by an insurer that is reasonably based on actual recent historical experience and that satisfies the requirements set forth in the *Model*.
- 2.4 Experience Factor—A value or set of values that represents the **actual experience** of a policy form. Examples of **experience factors** include rates of mortality, expense, investment income, termination, and taxes.
- 2.5 Experience Factor Class—A group of policies for which **nonguaranteed elements** are determined by using common numerical values of a particular **experience factor**.
- 2.6 Illustrated Scale—A scale of **nonguaranteed elements** currently being illustrated that is not more favorable to the policyholder than the lesser of the **disciplined current scale** or the **currently payable scale**.
- 2.7 Illustration Actuary—An actuary who is appointed in accordance with the requirements set forth in the *Model*.
- 2.8 Nonguaranteed Element—Any element within an insurance policy that affects policy costs or values that is not guaranteed or not determined at issue. A **nonguaranteed element** may provide a more favorable value to the policyholder than that guaranteed at the time of issue of the policy. Examples of **nonguaranteed elements** include policy dividends, excess interest credits, mortality charges, expense charges, indeterminate premiums, and participation rates and maximum rates of return for indexed life insurance products.

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- 2.9 Nonguaranteed Element Framework—The structure by which the insurer determines **nonguaranteed elements**. This includes the assignment of policies to **experience factor classes**, the method of allocating income and costs, and the structure of the formulas or other methods of using **experience factors**. For participating policies this would be the dividend framework defined in ASOP No. 15. For life policies within the scope of ASOP No. 2, the **nonguaranteed element framework** would include the concepts of policy class, determination policy, and anticipated **experience factors**.

Section 3. Analysis of Issues and Recommended Practices

- 3.1 Regulatory Requirements—The *Model* contains detailed instructions, technical requirements, and prohibitions regarding many aspects of illustrations. Actuaries providing professional services within the scope of this standard should be familiar with the *Model*, AG 49, any applicable state law based on the *Model* (including state variations), and this standard.
- 3.2 Appointment as Illustration Actuary—Before accepting an appointment as an **illustration actuary**, the actuary should determine that he or she meets the qualifications described in the *Qualification Standards for Actuaries Issuing Statements of Actuarial Opinion in the United States*. The appointment should be in writing and should describe the scope of the **illustration actuary's** responsibilities and establish the effective date. Acceptance of or withdrawal from the position should also be in writing.
- 3.3 Illustrated Scale Requirements—The actuary should ensure that the **illustrated scale** meets the requirements imposed by the *Model* as follows.
- 3.3.1 Currently Payable Scale—The **illustrated scale** must not be more favorable to the policyholder than the **currently payable scale** at any duration.
- 3.3.2 Disciplined Current Scale—The **illustrated scale** must be no more favorable to the policyholder than the **disciplined current scale** at any duration.
- 3.3.3 Interest Credited Rate—For policies with interest credits linked to an external index or indices, the interest credited rate for the **illustrated scale** for each indexed account shall be limited in accordance with AG 49.
- 3.4 Developing the Disciplined Current Scale—The actuary should consider the following when developing the **disciplined current scale**:
- 3.4.1 Assumptions Underlying the Disciplined Current Scale—The actuary should use experience as analyzed within the insurer's **nonguaranteed element framework** when setting **experience factors** underlying the **disciplined current scale**. To the extent **actual experience** is determinable, available, and credible, the actuary should use **actual experience** when setting **experience factors** underlying the

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disciplined current scale. When such suitable data are lacking, **experience factors** should be derived in a reasonable and appropriate manner from **actual experience** of other similar classes of business. Similar classes may be found within the same company, may be found in other companies, or may be from other sources, in that order of preference. When determining the extent to which **actual experience** is credible, the actuary should refer to ASOP No. 25, *Credibility Procedures*. As required by the *Model*, the **experience factors** underlying the **disciplined current scale** may not include any projected trends of improvement nor any assumed improvements in experience beyond the effective date of the **illustrated scale**, except as provided in section 3.8.

The actuary should consider the following when setting assumptions:

- a. Investment Return—The **experience factor** used for investment income (the investment return factor) underlying the **disciplined current scale** should be reasonably based on recent actual investment experience, net of default costs, of the assets supporting the policy block.

If interest credits are linked to an external index or indices, then the investment return factor is sensitive to business or economic cycles. In such cases, the actuary should consider an appropriate time frame commensurate with such cycles and the characteristics of the underlying index or indices in determining recent **actual experience**. When determining the investment return factor for policies within the scope of AG 49, actuaries should comply with limitations imposed on the assumed earned interest rate underlying the **disciplined current scale**.

The actuary should have a reasonable basis for allocating investment income to policies, whether using the portfolio, segmentation, investment generation, or any other method. The actuary should develop the investment return factors using the same method that is used to allocate investment income to policies. The investment return factors may be net of investment expenses or, alternatively, investment expenses may be treated separately as expenses.

The actuary should use procedures that have a reasonable theoretical basis for determining the investment return factors. In determining the investment return factors, the actuary should reflect the insurer's actual practice for **nonguaranteed elements** with respect to realized and unrealized capital gains and losses, investment hedges, policy loans, and other investment items.

- b. Mortality—The actuary should base the mortality **experience factors** on the insurer's mortality experience, if credible, adjusted for risk class. In setting mortality **experience factors**, the actuary should consider credible variations by age, gender, duration, marketing method, plan, size of policy,

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policy provisions, risk class, and other items (or a combination thereof) consistent with the insurer's structure of mortality **experience factor classes**. To the extent that the insurer's **actual experience** is not sufficiently credible, the actuary should consider using other credible industry mortality experience, appropriately modified to reflect the insurer's underwriting practices. If no credible industry mortality experience is available, the actuary should use professional judgment in modifying other sources of information (for example, general population mortality tables) in order to obtain the mortality assumption.

- c. **Persistency**—The actuary should base the premium continuation and policy persistency rates on the insurer's **actual experience**, if credible, for this or similar policy forms. The actuary should consider credible variations by age, gender, duration, marketing method, plan, size of policy, policy provisions, risk class, and other items (or a combination thereof) consistent with the insurer's structure of persistency **experience factor classes**. To the extent that the insurer's recent experience is not credible, the actuary should consider using other credible industry experience such as that from the Life Insurance Marketing Research Association, appropriately modified to reflect the actuary's professional judgment regarding differences between the policy form and the basis for the industry experience.
- d. **Direct Sales Expenses**—The actuary should reflect agent commissions, overrides, and other direct compensation determined by formula or incurred as a consequence of sales in a manner consistent with new business activities that generate the cost and are excluded from the expense factors given in sections (e)(1), (2), and (3) below.
- e. **All Other Expenses**—As described in the *Model*, the actuary should consider whether the minimum expenses to be used in the calculation of the **disciplined current scale** for all policy forms during the certification year are based on sections (1), (2), or (3) below and are subject to the criteria that follow them:
 1. **Fully Allocated**—Unit expenses reflecting total expenses recently incurred by the insurer when applied to both in force or newly issued policies are considered fully allocated. Some expenses are direct in that they can be specifically related to a particular policy form. Other expenses, such as general overhead costs, are indirect. The actuary should charge direct expenses to the groups of policies generating the related costs. Indirect expenses should be fully allocated using reasonable principles of expense allocation. Nonrecurring costs, such as systems development costs, may be spread over a reasonable number of years (for example, system lifetime) in determining the allocable expenses for a particular year.

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2. Marginally Allocated—Marginally allocated expenses are unit expenses calculated in a manner similar to fully allocated unit expenses except that indirect expenses, such as corporate overhead and general advertising, are not allocated to the policy forms.
3. Generally Recognized Expense Table (GRET)—GRET unit expenses are obtained from an industry expense study based on fully allocated expenses representing a significant portion of insurance companies and approved for use by the NAIC or by the commissioner.

If no GRET is approved and available, the *Model* requires the use of fully allocated expenses. If a GRET is approved and available, the *Model* allows the use of either a GRET or fully allocated expenses. The *Model* permits the use of marginally allocated expenses only to the extent that they generate aggregate expenses that are at least as large as those generated by a GRET.

The actuary should make the comparison and choice of expense factor bases in the aggregate for all policy forms. The actuary should use the same unit expense basis for all policy forms tested. For example, the actuary should not use marginal expenses for one policy form and fully allocated expenses for another policy form. Once the actuary selects the unit expense basis, the actuary should use that basis for the entire certification year. When calculating unit expenses, the actuary should select average policy size and volume of sales assumptions that are appropriate for the policy form.

- f. Taxes—The actuary should reflect all cash flows arising from applicable taxes. Income taxes should be recognized in accordance with their impact by duration in the development of the **disciplined current scale**. Non-income taxes that are classified as investment taxes may be treated as a deduction from the investment return or may be treated separately. Other categories of taxes, such as premium taxes or employment taxes, may be handled separately or included in the category of all other expenses, as outlined in section 3.4.1(e) above.

Details of taxation vary widely, depending on the application of law and regulation in various jurisdictions. The actuary should consider the insurer's actual practices for allocating taxes for **nonguaranteed elements** in determining the tax **experience factor**.

- g. Changes in Methodology—When an insurer changes its methodology in determining **nonguaranteed elements** (for example, changing from portfolio rate methodology to a new money rate methodology or adding a new underwriting class), the actuary should appropriately modify

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assumptions underlying the **disciplined current scale** to reflect the new methodology.

- h. **Other Lines of Business**—If other lines of business are considered investments of the illustrated block of business, the actuary should consider whether cash flows originating in such lines are recognized in the assumptions underlying the **disciplined current scale**. In deciding whether and how to reflect these cash flows, the actuary should consider the time horizon of the investment/investor relationship and the insurer's actual practice for reflecting these cash flows in determining **nonguaranteed elements**.

- 3.4.2 Relationship of Actual Experience to Disciplined Current Scale—The actuary should select assumptions underlying an insurer's **disciplined current scale** that logically and reasonably relate to **actual experience** as reflected within the insurer's **nonguaranteed element framework**. The actuary should reflect changes in experience once changes have been determined to be significant and ongoing.

Actual experience may exhibit improvements from year to year. As required by the *Model*, such trends in improvement may not be assumed to continue into the future beyond the effective date of the **disciplined current scale** underlying the illustration.

If trends indicate that significant and continuing deterioration in an **experience factor** has occurred or, in the actuary's professional judgment, is likely to occur between the date of the experience study and the effective date of the **disciplined current scale** underlying the illustration, the actuary should recognize such deterioration in determining the assumptions to be used.

When an insurer introduces a change in underwriting practice (for example, adding a new underwriting class) that is not expected to change the insured population, the actuary should divide the **actual experience** into the new underwriting classes in such a way that **actual experience** is reproduced in the aggregate.

- 3.5 Requirements for Self-Support—The *Model* requires every policy form illustrated by an insurer to be self-supporting according to the assumptions underlying the insurer's **disciplined current scale**. This requirement applies to the illustration of policies in force for less than one year.

The *Model* requires the following self-support test. At every illustrated point in time starting with the fifteenth policy anniversary (with the twentieth policy anniversary for second-or-later-to-die policies), the accumulated value of all policy cash flows, when using experience assumptions underlying the **disciplined current scale**, should be equal to or greater than the illustrated policyholder value, i.e., the cash surrender values and any other illustrated benefit amounts available at the policyholder's election. When policies

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expire according to their terms prior to 15 years (20 years for second-or-later-to-die policies), the **illustrated scale** should be self-supporting at the point of expiration.

Each illustration reflects underwriting classification, as well as certain factors that are subject to policyholder choice. The underwriting classification includes factors such as age, gender, and risk class. Policyholder choices reflected in the preparation of an illustration include, but are not limited to, the size of policy, premium payment pattern, dividend option, coverage riders, and policy loans.

In performing the self-support test for a policy form, the actuary may test the underwriting classification and policyholder choice factors in aggregate if, in the actuary's professional judgment, such combinations would be appropriate. If testing is done in the aggregate, the actuary should select assumptions for the distribution between underwriting classes and policyholder choices that are based on **actual experience**, if available, recognizing possible shifts in distribution toward any portions of the business that do not meet the self-support test in their own right.

- 3.6 Requirements to Prevent Lapse-Supported Illustrations—The *Model* prohibits illustration of **nonguaranteed elements** in policies that are deemed to be lapse-supported and establishes a lapse-support test to demonstrate compliance with this requirement. The lapse-support test requires that the policy form in question be self-supporting under the same assumptions and with the same level of aggregation as described in section 3.5, changing only the persistency assumption. The modified persistency rate assumption will use the persistency rates underlying the **disciplined current scale** for the first five policy years and 100% policy persistency thereafter. In performing the lapse-support test for a policy form, the actuary should assume that benefits that are conditional only upon policy continuation will be provided to all policies in force at the end of year five and surviving to the date of such benefits. For policy forms that provide benefits that are conditional upon certain premium payment patterns, the actuary should consider whether all policies in force to the end of year five will qualify for such benefits.

As stated in the *Model*, policy forms that can never develop nonforfeiture values, such as certain term coverages, are exempt from the lapse-support test. The *Model* requires that these policy forms pass the self-support requirement.

- 3.7 Illustrations on Policies In Force One Year or More—The **illustration actuary** is required to annually certify that the **disciplined current scale**, for both new business and in force illustrations, complies with the *Model* and this standard. The *Model* requires that the **illustrated scale** be no more favorable to the policyholder than the lesser of the **currently payable scale** and the **disciplined current scale**. The **disciplined current scale**, for a policy in force one year or more, continues to be in compliance with the *Model* and this standard, if any of the following apply:
- a. the **currently payable scale** has not been changed since the last certification and the **illustration actuary** determines that experience since the last certification does

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not warrant changes in the **disciplined current scale** that would make it significantly less favorable to the policyholder; or

- b. the **currently payable scale** has been changed since the development of the **disciplined current scale** most recently certified only to the extent that changes are reasonably consistent with changes in experience assumptions underlying the **disciplined current scale**; or
- c. the **currently payable scale** has been made less favorable to the policyholder since the last certification and the change is more than the change in the current experience would dictate.

If none of the conditions in (a), (b), or (c) above is met, the **illustration actuary** should (1) review the **experience factors** underlying the **disciplined current scale** and revise as necessary, and (2) develop a new **disciplined current scale** for this policy form.

In the context of in-force illustrations for policies receiving distributions of accumulated surplus or prior gains (including those resulting from the formation of a closed block), the actuary should consider including these distributions both in the **disciplined current scale** and in the **illustrated scale**, only to the extent that (1) such distributions are currently being paid to the policyholders by the insurer, and (2) the insurer has indicated its intent and ability to continue to do so for the foreseeable future. Such accumulated surplus or prior gains may be used in conducting the tests for self-support and lapse-support.

- 3.8 Changes in Practice—An insurer may introduce certain changes in the way it conducts its business, which may have significant positive or negative effects on future experience. If the action has already occurred, but not enough time has elapsed for it to be reflected in the insurer’s **actual experience**, it may nevertheless be reflected in the assumptions underlying the **disciplined current scale**. The actuary should consider recognizing actions, such as the following, to the extent known to the actuary:
 - 3.8.1 Changing Underwriting Standards—Introducing preferred risk, guaranteed issue, or simplified underwriting may impact the mortality assumption.
 - 3.8.2 Varying Commission Levels—Changing commission levels (either decreasing or increasing) will have a known effect on policy expenses.
 - 3.8.3 Reducing Staff—Staff reductions may have an effect on the expense assumptions.
 - 3.8.4 Changing Investment Policies—Changes in investment policies, including hedging activities, and changes in asset class allocations may impact the investment assumption.
 - 3.8.5 Reinsurance Agreements—New or revised reinsurance agreements may impact experience assumptions such as mortality, investment income, and tax.

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The changes should have occurred in order to be reflected in the **disciplined current scale** and not simply be planned for in the future.

- 3.9 Reliance on Data or Other Information Supplied by Others—When relying on data or other information supplied by others, the actuary should refer to ASOP No. 23, *Data Quality*, for guidance.
- 3.10 Documentation—The documentation that supports the actuarial certification described in section 4.1 with respect to the construction of the **disciplined current scale**, maintained in conformance with ASOP No. 41, *Actuarial Communications*, should include the following:
- a. description of, and rationale for, the investment income, mortality, persistency, expense, tax, and other assumptions;
 - b. description of, and rationale for, any other calculation methods and assumptions used to carry out the tests and demonstrations described herein; and
 - c. demonstration that the self-support and lapse-support tests have been met.

Section 4. Communications and Disclosures

- 4.1 Certification—The *Model*¹ requires the **illustration actuary** to certify annually that the **illustrated scale** and the **disciplined current scale** are in compliance both with the requirements as set forth in the *Model* and with the requirements set forth in this ASOP. Certifications should also be made for newly introduced forms before a new policy form is illustrated.²

The certification should disclose the following:

- a. for business issued in the last five years and within the scope of the certification, whether or not the **currently payable scale** has been reduced since the last certification for reasons unrelated to experience changes;³
- b. the choice of expense assumptions as discussed in section 3.4.1(e);⁴
- c. any inconsistencies between the illustrated **nonguaranteed elements** for new policies and similar in-force policies;⁵ and

¹ As stated in *Model* sections 11.B, C(5)-(6), and D(1)(a).

² As stated in *Model* section 11.D(1)(b).

³ As stated in *Model* section 11.C(5).

⁴ As stated in *Model* section 11.C(6).

⁵ As stated in *Model* section 11.C(5).

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- d. any inconsistencies between the illustrated **nonguaranteed elements** for new and in-force policies and the **nonguaranteed element** amounts actually paid, credited or charged to the same or similar forms.⁶

As required by the *Model*,⁷ if an **illustration actuary** is unable to certify the **illustrated scale** for any policy form the insurer intends to use, the actuary should notify the board of directors of the insurer and the commissioner promptly of his or her inability to certify.

- 4.2 Notice of Error in Certification—As required by the *Model*,⁸ if an error in a previous certification is discovered, the **illustration actuary** (or successor **illustration actuary**) shall promptly notify the board of directors of the insurer and the commissioner.

The certification should be considered in error if the certification would not have been issued or would have been materially altered had the error not been made. The certification should not be considered to be in error solely because of data that become available, or information concerning events that occurred, subsequent to the certification date.

- 4.3 Disclosures—The actuary should include the following, as applicable, in the certification:
 - a. the disclosure in ASOP No. 41, section 4.2, if any material assumption or method was prescribed by applicable law (statutes, regulations, and other legally binding authority);
 - b. the disclosure in ASOP No. 41, section 4.3, if the actuary states reliance on other sources and thereby disclaims responsibility for any material assumption or method selected by a party other than the actuary; and
 - c. the disclosure in ASOP No. 41, section 4.4, if, in the actuary’s professional judgment, the actuary has otherwise deviated materially from the guidance of this ASOP.

⁶ See note 5 above.

⁷ As stated in *Model* section 11.E.

⁸ As stated in *Model* section 11.D(2).

Appendix

Background and Current Practices

Note: This appendix is provided for informational purposes but is not part of the standard of practice.

Background

Sales illustrations have been of concern to regulators for over a century, going back at least to the Armstrong Commission (1905-1906). Developments prior to 1995 involving insurance products, illustration technology, and the volatility of financial markets led to heightened concern and to the adoption of the NAIC *Life Insurance Illustrations Model Regulation (Model)*.

Actuaries have been involved in the process of establishing scales of dividends and other nonguaranteed elements to be illustrated by insurance companies for decades. Until the 1980s, nonguaranteed elements were essentially synonymous with participating dividends, and the sources of scales of illustrated dividends were tables prepared by the respective insurance companies. Since that time, there has been a proliferation of policies with nonguaranteed elements other than dividends. Improving technology has also made possible the development of software that enables insurance agents to produce sales illustrations based on a variety of assumptions, potentially with little or no direct involvement on the part of the insurer. The *Model* assigns major responsibilities regarding compliance to an actuary who is appointed by the insurer.

Illustrations generally have three primary uses:

1. to show the buyer the mechanics of the policy, i.e., how a particular financial design or concept works, and how policy values or premium payments may change over time;
2. to compare the cost or performance of different policies; and
3. to show how the policy fits into the policyholder's financial plan.

A sales illustration simply shows the performance of one particular scale of nonguaranteed elements into the future. Actual nonguaranteed elements will almost certainly vary from those illustrated. Different policies will experience different variances from illustrated values.

Current Practices

Since the promulgation of the original standard in 1995, product innovation has continued as pricing structures have been refined, secondary guarantees have been developed, an increasing variety of equity-indexed and other indexed life insurance products have been developed, and

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additional new underwriting classes have been added. Until the release of Actuarial Guideline 49 (AG 49), it had been common practice to illustrate these new products pursuant to the *Model* and this standard as it existed. With the introduction of AG 49, illustrations of contracts providing interest credits linked to an external index or indices will be subject to AG 49 and this updated standard.

Varying degrees of flexibility are provided by insurers to their agents in customizing sales illustrations, depending somewhat on whether the producers are brokers or career agents. Generally, the tools that insurers provide allow flexibility with respect to column selection and formats, variations on nonguaranteed elements, and different premium patterns. Along with this flexibility may be the requirement that the buyer also be given a ledger illustration in an insurer-approved format.