

Title of Exposure Draft: ASOP 2

Comment Deadline: November 13, 2020

I. Identification:

Name of Commentator / Company
Jesse Kling, FSA, MAAA

To Whom It May Concern:

Thank you for the opportunity to provide the following comments on the second exposure draft of ASOP 2.

In my previous letter, I commented that the first exposure draft contained rules that could create an inherent conflict of interest between a company actuary and his or her employer (i.e., applying the determination policy in Section 3.2.2 if the determination policy is inconsistent with Sections 3.2 and 3.2.1). Having reviewed the other comment letters, I see that many other actuaries shared my concern.

Presumably in response to these comments, the ASB added the following paragraph at the end of Section 3.4:

“If, in the actuary’s professional judgment, the actuary believes that following the determination policy when determining NGE scales would conflict with the guidance in sections 3.2 and 3.2.1, the actuary should document the conflict and should consider providing advice consistent with section 3.2.2.”

While I am pleased to see this language, I am concerned that the distinction between Sections 3.2 and 3.4 is not obvious, and 3.2 can easily be interpreted as creating rules that apply to an actuary when determining nonguaranteed elements.

Furthermore, the changes made in the exposure draft do not sufficiently address my concerns, because Section 3.2 continues to prescribe a rule that does not exist in the vast majority of state insurance statutes or regulations. Indeed, very few states have any sort of restriction on the practice of recouping past losses or distributing past gains.

As a result, there are a number of unintended consequences associated with the prescribed rules in Section 3.2. First, if Section 3.2 continues to be more strict than prevailing law, the possible result will be that companies move the determination function outside of the actuarial department and into an area with less insurance education and fewer professional standards.

Second, Section 3.2 could create a scenario in which, under the proposed standard, an actuary may not be able to recommend changes to non-guaranteed elements that would otherwise bolster the solvency position of a struggling insurer and would be compliant with both contract provisions and applicable statute and regulations.

Third, Section 3.2 is ambiguous in its broad application of the terms “past losses” and “past gains.”

Overall, this exposure draft continues to be too prescriptive and overly restricts the actuary’s ability to set rates that are equitable, sustainable, and consistent with laws, regulations, and contractual requirements. I therefore recommend changes to the language as shown in Section III.

Thank you again for the opportunity to provide feedback on the standard.

Regards,

Jesse Kling, FSA, MAAA

II. ASB Questions (If Any). Responses to any transmittal memorandum questions should be entered below.

N/A

III. Specific Recommendations:

#	Commentator Recommendation	Rationale
3.2 & 3.4	Create clearer distinction between Sections 3.2 and 3.4.	I am concerned that the distinction between Sections 3.2 and 3.4 is not obvious, and 3.2 can easily be interpreted as creating rules that apply to an actuary when determining nonguaranteed elements.
3.2(b)	<p>In order to directly address the concern and risk noted above, I would propose to strike reference to past gains and losses in Section 3.2(b):</p> <p>b. NGE scales are determined based on reasonable expectations of future experience, subject to any existing legal or regulatory constraints. and are not determined with the objective of recouping past losses or distributing past gains.</p>	<p>The Determination Policy may have been established prior to the revision of this ASOP, and/or may have been established by Company management neither familiar with nor bound by this ASOP. As a result, Company management may not agree that losses occurring after initial pricing cannot be factored into future modifications of the NGE scales.</p> <p>As a result, this revised passage puts the actuary’s role in the NGE management process at risk. A company may not feel obligated to abide by this Actuarial standard, which is more restrictive than the applicable law and regulation in most jurisdictions. As a result, the actuary may be removed from the process entirely to avoid potential conflicts of interest. The result would likely be a negative impact to both the industry and the consumer.</p> <p>In addition, the passage could create a scenario in which an actuary may not be able to recommend changes to non-guaranteed elements that would otherwise bolster the solvency position of a struggling insurer.</p> <p>Finally, this passage is ambiguous in its broad application of the concept of “past losses” and “past gains.”</p>
3.2(b)	<p>If the above change is not made, I would suggest removing the ambiguity in the application of the concept of “past gains and losses,” particularly as the term may apply to hedging costs. The following definitional language is suggested:</p> <p>Past Gain, Past Loss – A variance from expected profitability resulting from deviations from assumptions set at the time of initial pricing, or at a prior point of setting NGE scales. Past gains or losses do not include deviations in hedging costs that were incurred in prior crediting periods.</p>	<p>There is a specific set of circumstances, related to the practice of hedging, which could be mistakenly construed as gains or losses under this section, where I expect that this was not the intention of the Task Force.</p> <p>For example, when dynamic hedging is utilized to support the index caps, participation rates, and/or spreads, the ending cost is not fully known at the establishment of that cap, rate, or spread. Instead, an estimated cost may be used, with variances to the cost, positive or negative, occurring during the subsequent crediting period. At the conclusion of the crediting period, the company may have experienced an actual-to-expected variance in the cost. This variance, positive or negative, may then be reflected in the resetting of the non-guaranteed cap, rate, or spread in the following crediting period.</p>

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3.4	<p>I recommend the following language:</p> <p>If, in the actuary's professional judgment, the actuary believes that following the determination policy when determining NGE scales would conflict with the guidance in sections 3.2 and 3.2.1, the actuary should <u>consider discussing these differences with management.</u></p>	<p>This requirement could place the actuary in a position of conflict with Company management, where, as noted above, management may decide not to abide by an Actuarial standard that unnecessarily imposes requirements beyond those required under existing law or regulation, and may place restrictions on the company's contractual rights that were not contemplated at the time of product development. Rather than creating and documenting this conflict, some companies may elect to remove the actuary from the process entirely. This would likely cause a negative impact to both the industry and the consumer.</p>

IV. General Recommendations (If Any):

Recommendation	Rationale
N/A	

V. Signature:

Commentator Signature	Date
 Jesse Kling, FSA, MAAA	11/13/2020