STATE OF CONNECTICUT

INSURANCE DEPARTMENT

Testimony

Insurance and Real Estate Committee

March 12, 2013

H.B. No. 6613 (Raised) AN ACT CONCERNING THE STANDARD VALUATION LAW

Senator Crisco, Representative Megna, and members of the Insurance and Real Estate Committee, The Insurance Department thanks the Committee for raising H.B. 6613, an Act Concerning the Standard Valuation Law, at the Department's request, and appreciates the opportunity to provide written testimony.

H.B. 6613 is being introduced to bring life insurance and annuity reserving techniques from the 19^{th} Century to the 21^{st} Century.

These amendments to the Standard Valuation Law enable the introduction of a concept known as Principle Based Reserving of life insurance companies' actuarial liabilities. That concept has been developed by state insurance regulators working through the National Association of Insurance Commissioners, and is being introduced in state legislatures throughout the nation. It will ultimately replace a formulaic system of insurance reserves that has been in use since at least 1885 and possibly much earlier.

The formulaic reserve approach worked well for over a century as insurers sold similar life and annuity products with relatively standard basic features. That approach has become overly static, however, as insurance companies have developed increasingly sophisticated life and annuity products. Those formulas do not always work without modification or clarification. Regulators and insurers now find that use of those formulaic reserves can result in reserves being redundant in some cases and inadequate in others.

Principle based reserving uses risk analysis techniques such as modeling and simulation to better capture and evaluate various risks inherent in modern life insurance policies and annuity contracts. It sets up a regulatory system so that these reserves can be established to be consistent with the unique characteristics of the different products of different companies. The purpose is to establish reserves at a better level so they are neither under reserved -- with a risk to solvency -- nor over reserved -- which can lead to unnecessarily expensive policies and contracts. It is based on company-specific and product-specific actuarial data.

The bill requires life insurance companies to submit to regulators mortality, morbidity, policyholder behavior experience and other data as prescribed in the Valuation Manual. It also protects confidentiality of sensitive financial and actuarial data provided to the Insurance Department so that the Department can have uninhibited access to this data. This makes for effective monitoring of reserves, and ultimately solvency.

The SVL revisions under consideration provide for life and health reserve requirements to be consolidated in a Valuation Manual to support state uniformity along with the PBR method for determining life insurance reserves. The initial version of the Valuation Manual was recently adopted by the NAIC. However, the manual will not go into effect until a supermajority of states enacts both the manual and revisions to state Standard Valuation Laws. Specifically the supermajority calls for approval of the SVL amendments or substantially similar legislation by legislative approval in 42 jurisdictions and in states representing greater than 75% of direct written premium for life, accident and health business. As mentioned, one trigger has already been met, namely approval of the Valuation Manual by a supermajority of jurisdictions at the NAIC. This is an admittedly unusual provision, but it is intended to allow a uniform transition to PBR and to prevent differing reserving practices and standards being used in different states. Reserving standards in life insurance and annuity products is one of those regulatory functions where national uniformity is critically important to the state-based system of insurance regulation and the maintenance of a financially sound life insurance industry. The reserving requirements for life insurance and annuity business written before the effective date of the Valuation Manual will remain unchanged.

While uniformity is important to establish uniform reserve methodologies, the amendments to the SVL preserve my authority and the authority of individual insurance commissioners to require companies to change any assumption or method as appropriate and to engage a qualified actuary at the expense of the company to review compliance with Valuation Manual requirements.

The Valuation Manual is intended to be dynamic to allow consideration of ongoing changes of products offered in the marketplace, much as the NAIC Accounting and Procedures Manual -- which sets out the details of statutory accounting -- works now. Future changes in the manual will require approval by a supermajority of 42 NAIC jurisdictions so that they will be implanted uniformly and with appropriate controls.

I note that there are some technical changes that my staff has noted that we would like changed in the bill as printed. We will work with members of the committee and legislative staff on those changes.

The Department appreciates the opportunity to submit these comments today. We strongly urge passage of H.B. 6613. Thank you.