

Proposed Revisions to ASOP 2 May Impact Your Product Pricing and Litigation Exposure

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The Actuarial Standards Board (ASB) exposed wholesale changes to Actuarial Standard of Practice No. 2 - Nonguaranteed Charges or Benefits for Life Insurance Policies and Annuity Contracts (ASOP 2), which has not changed since 2004. ASOP 2 provides actuaries guidance for determining nonguaranteed elements (NGEs) in individual and certain group life insurance and annuity products. NGE determinations, such as cost of insurance (COI) rate increases, have spawned widespread class action litigation, state investigative and enforcement actions, and, most recently, new NGE-related state regulations (e.g., N.Y. Regulation 210).

Although ASOP 2 applies only to actuaries, insurers should be alert to its indirect impact on their NGE processes and pricing. The exposed changes mandate expanded and more prescriptive technical requirements for actuaries' NGE determinations, provide specific guidance concerning opinions and disclosures, and require a broader array of disclosures in actuarial reports. Some of the most significant proposed changes and potential implications include:

- Important definitional changes. For example, the respective lists of “examples” in the definitions of “Anticipated Experience Factor” and “Guaranteed Policy Factor” have been modified.
- The new definition, “NGE Framework” imposes enhanced duties on actuaries when considering each of the Framework elements and their interplay, including understanding a comprehensive list of methodologies and models used by the insurer.
- New, detailed requirements apply when actuaries are advising an insurer on: (i) developing or modifying its determination policy; (ii) applying the determination policy; (iii) establishing or changing policy classes, including separate, differing requirements in the context of new products, future sales of existing products, and in-force products; and (iv) the determination process of NGE scales, again with separate, context-based prescriptive requirements, including those for reviewing or reconstructing prior determinations, analyzing experience, considering whether to recommend revisions to NGE scales, and determining revised NGE scales.
- Requiring actuarial advice on in-force products to be consistent with two overriding principles — NGEs are revised only if anticipated experience factors have changed, and NGEs are not revised with the objective of recouping past losses or distributing past gains.
- Actuarial reports must include disclosures relating to, among other things, results and observations from any profitability or sensitivity analyses, use of prior analyses and any reconstructed determinations or reasonable approaches used when prior determinations were not available or could not be reconstructed, and results from tests performed to ascertain whether illustrated NGE scales are supportable when using anticipated experience factors that are not more favorable than actual recent historical experience.

Comments on the current exposure draft are due by July 15, 2019. After the comment period closes, it is expected that the ASB will take about six months to determine whether to adopt ASOP 2 as exposed (or with changes not requiring further exposure) or to reexpose an updated version for comment. Assuming no reexposure or modification of the effective date provision, new ASOP 2 would apply to all actuarial services performed four months after adoption, most likely during the second quarter of 2020. Nonetheless, it behooves actuaries and insurers to take immediate note of how the proposed changes may impact new products under development and prospective repricing of existing products, including considerations relating to contract language, the insurer's determination policy, state filing and approval timelines, and the management of ongoing and potential future litigation.

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