June 2, 2025

Rachel Hemphill
Chair, Life Actuarial (A) Task Force (LATF)
National Association of Insurance Commissioners

Re: LATF Exposure APF 2025-04

Dear Chair Hemphill,

On behalf of the Economic Scenario Generator Subcommittee (Subcommittee) of the American Academy of Actuaries,[1] we appreciate the opportunity to offer comments on the recent exposure of APF 2025-04.

The Subcommittee supports the proposed use of non-prescribed scenario generators (i.e., proprietary economic scenarios) in PBR and C3 Phase I and II capital. This provision supports a company's need for operational flexibility in managing their economic risk and balance sheet volatility. The availability of fully understood and documented economic scenario methodologies can help practicing actuaries ensure that the reserves and capital are aligned with core principles of PBR while also helping them fulfill their obligations under ASOP No. 56. The Subcommittee also recognizes the complexities that come with developing proprietary economic scenarios and their associated calibrations. We recommend that LATF consider the use of our previously developed Acceptance Criteria as a central element in evaluating the quality of the proprietary economic scenarios. Since many companies will want to be able to tailor their scenarios to the products that they manage, the ability to use non-prescribed scenario generators within this exposure provides the necessary flexibility they are seeking. When a company is afforded the flexibility to change their scenarios, they are better able to adapt to structural changes in financial market conditions. One limitation of the GOES model we have noted is the challenge it has in addressing a longer governance cycle involving new parameterization or structural model changes.

The sudden movement to a "low for long" world in the wake of the financial crisis introduces situations where the prescribed economic scenarios were not fit for purpose. Generally, prescribed scenarios may no longer be fit for purpose when the market undergoes a rapid structural change. We recommend that the NAIC provide guidance on permitting the actuary more discretion under stressed market conditions. Detailed governance procedures that focus on how well a scenario set currently meets the adopted acceptance criteria will be vital. Ideally, the acceptance criteria should have features that adapt to current market conditions. It is never easy to determine when the prescribed scenarios have "broken," but we recommend that identifying and removing them be an actionable part of ongoing governance. The governance process should permit flexibility to an actuary to use appropriate scenarios, especially when prescribed scenarios may no longer be relevant and provide a mechanism for addressing such situations in the short to medium term.

[1] The American Academy of Actuaries is a 20,000-member professional association whose mission is to serve the public and the U.S. actuarial profession. For 60 years, the Academy has assisted public policymakers on all levels by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States.

We recommend that there be a requirement for a non-prescribed model to pass acceptance criteria, with an allowance for professional judgment in applying the acceptance criteria. Currently, it appears that the test for the admissibility of a non-prescribed model is to provide a description of the models and that the model output be subject to a reserve comparison. If the NAIC would like to pursue this idea, the Subcommittee will be able to assist.

Companies that need to consolidate international businesses will require scenarios that are calibrated to conditions in other economies. These situations will require flexibility in developing their own economic scenario generators. Specific examples include lines of business, such as longevity insurance.

We strongly encourage LATF to address previously raised concerns related to GOES models documentation, as we believe that a resolution is unlikely in 2026. Specifically, we believe that additional guidance and specificity around the documentation for the interest rate and equity models would be greatly beneficial, as we look to move beyond basic model specifications. For example, documentation has been posted for the corporate yield model which provides little to no details on the model dynamics. The Subcommittee believes that additional documentation on a shorter anticipated timeline would greatly benefit both the companies and the regulators.

The SERT method, as adapted to the GOES model, is quite complex and should have detailed documentation available. Should LATF desire the documentation, the Subcommittee would be happy to provide it to the NAIC.

We did note that there may not have been sufficient testing on deterministic reserve (DR) versus stochastic reserve (SR) for the GOES SERT methodology, as we noted in our November 14, 2024 comment letter. There is no description of how corporate credit is handled for the 16 SERT scenarios. We recommend that there be some description of how the corporate credit SERT scenarios are generated. As currently drafted, APF 2025-04 does not provide a description of how corporate credit SERT scenarios are produced, as there is no detailed information on the dynamics of the GEMS corporate bond model. This could effectively challenge an actuary's ability to answer any questions or provide any insight.

With non-prescribed models, an actuary would have to opine on an appropriate SERT methodology in much the same way that a new process had to be developed, in order to have SERT available for the GOES model. This presumes a company using their non-prescribed model has full knowledge of how the model dynamics work and is, therefore, in a position to develop an appropriate SERT methodology.

In the subsection VM-20, Appendix 1: Additional Description of Economic Scenarios, Section D, it states that, "The corporate model used to develop the prescribed bond fund return scenarios is a multi-factor model referred to as the Corporate Yield Model." The Subcommittee has previously asked if a decision has been made concerning whether to use the Conning Corporate Yield Model or the Simplified Corporate Model developed by the Subcommittee and ACLI for GOES. The Subcommittee reiterates our advice to the NAIC that the benefits of using an undocumented and complex model do not outweigh the advantages of having a transparent and fully documented model that produces equally sound credit.
In the Subcommittee's opinion, the Simplified Corporate Credit model is preferable when considering the need to facilitate the necessary level of understanding and discussion of the GOES models.

In the subsection VM-20, Appendix 1: Additional Description of Economic Scenarios, Section D, the important issue of calibrating the GOES model to mean reversion levels is briefly touched on. Mean reversion benchmarks and their implementation for the GOES model are quite complex when compared to current experience in the AIRG, primarily because there is no MRP parameter for the GOES model. The process of calibrating the GOES model to mean reversion benchmarks is complicated and involves expert judgment. We recommend that this process be documented, and that the documentation be referenced in the VM. In this same subsection, the document refers to “link for PEW documentation” and the process for updating PEWs in a governance document. This reference is confusing as-is and the Subcommittee would be willing to offer LATF appropriate documentation of the PEW approach and recommendations on the process and timing of updates, if that would be helpful.

We appreciate the ongoing opportunity to provide comments to LATF on the exposure. If you have any questions or would like to discuss these comments further, please contact Amanda Barry-Moilanen, policy project manager—life (barrymoilanen@academy.org).

Sincerely,

Hal Pedersen, MAAA, ASA

Chairperson, Economic Scenario Generator Subcommittee

American Academy of Actuaries