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Auditor's Perspective Principle-Based Reserving for Traditional Life Products Southeastern Actuaries Conference | November 19, 2021

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Audit Risk Assessment

PBR, based on company experience and product complexity, introduces a new set of risks.

- Apply VM-20 guidance to different products
- Exclusion testing
- Small company exemption

Product Evaluation

Model Risks

- Model complexity
- Valuation process requires multiple models to be coded, aggregated and compared.
- Includes models for product evaluation and financial reporting

- New assumptions are introduced.
- Prudent best estimate assumptions, driven by company experience, require a lot of work and iteration.
- Assumptions are now subject to the judgment of the actuary instead of using only a set of prescribed assumptions.
- Stochastic models based on economic scenarios are introduced into the processina.

Assumptions

Process Changes

- New valuation process, with coordination across many areas
- New reporting requirements, e.g. VM-31
- New model audit rule controls
- More data collection for both valuation and assumption setting, transformation and load procedures exist.

Scope Responsibilities

Deliverables are changing under PBR in alignment with new risk assessment.

Scoping Memo

Actuarial specialists and accountants agree upon responsibilities of procedures

Examples:

- Assess the adoption of VM-20 methodology and inspect compliance by the company.
- Evaluate classification of products, including modeling of applicable material benefits.

Assumption Heat Map

Assumptions are ranked based on risk profiles.

Examples:

- Covers anticipated company experience, including credibility level, blending, and relevance as well as prescribed regulatory tables
- Reviews margin for adverse deviation and estimation error in developing anticipated experience rates.

Data and Reliance

Completeness and accuracy of underlying data, and controls

Examples:

- Comprise Company's VM-31 Actuarial Report, VM-50/51 Experience Reporting, and VM-G Corporate Governance Guidance
- Include starting asset summary
- Include deterministic and stochastic interest rate scenarios

Substantive Testing Procedures

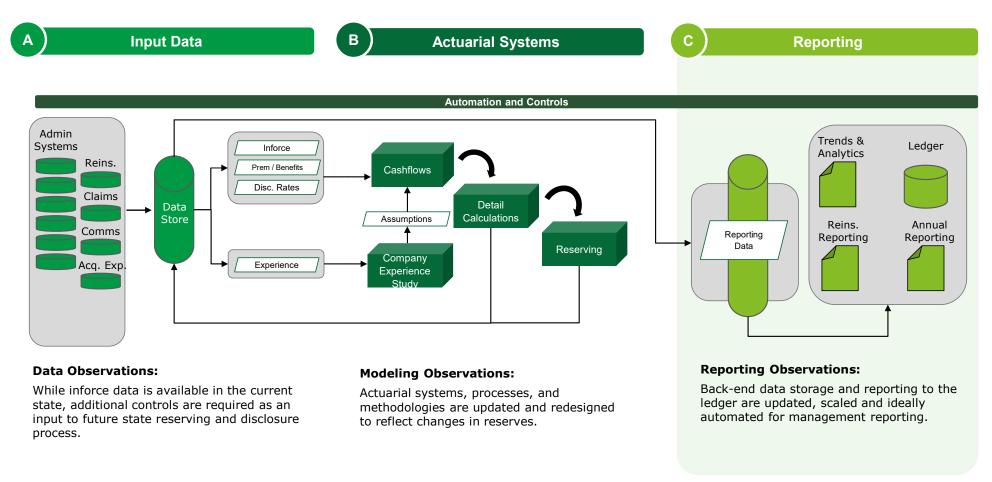
Model validation

Examples:

- Confirm exemptions and exclusions
- Perform independent testing for selections including Net Premium Reserve, Deterministic Reserve, and Stochastic Reserve
- Assess impact on riskbased capital and tax reserve

Audit End-to-End Roadmap

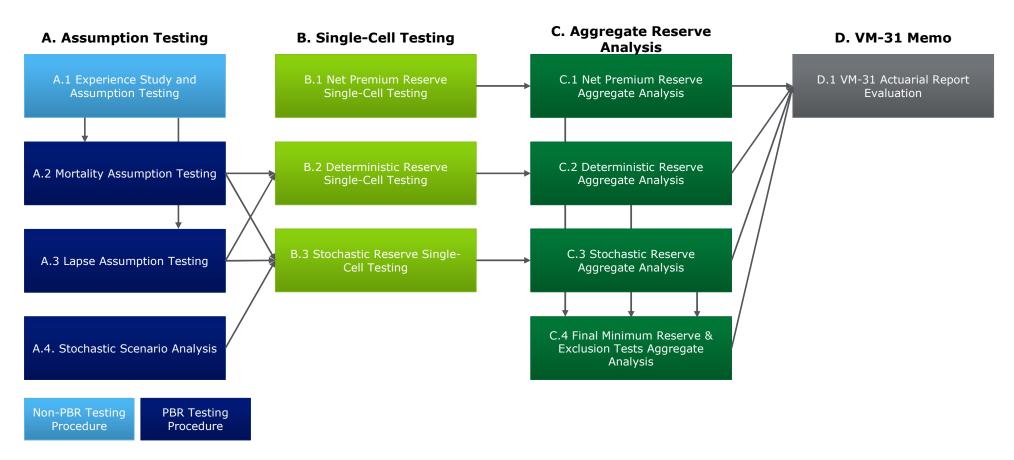
The full scope of PBR comes into focus when viewed as an end-to-end data flow and system architecture.



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Actuarial Procedure for PBR Audits

Consideration are given to sequencing PBR actuarial procedure while relying on auditors for completeness and accuracy of data



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Deloitte's Recommendations for a Low-Stress PBR Audit Experience

Insurers can take action to make the process as smooth and efficient as possible for the auditors.

Audit Procedure Changes

- Evaluation of accuracy and completeness of experience studies and assumption setting process
- Evaluation of asset models and assumptions
- Validation for adoption of VM-20 principles as well as confirmation of model accuracy
- Review of exclusion tests and modeled cash flows
- New risk assessment may classify complex models as high risk; overall the impact may be low due to immaterial balance.

Audited Company Preparation

- Document clearly applicable assumptions, methodology and results; retain evidence not just in email form.
- Make PBR actuarial report robust
- Include model risk management with validation, change procedures, and controls and governance
- Increase controls to cover increased processes
- Don't wait; set schedule to begin the audit process before year-end due to complexity and dependency of new processes