Milliman Study Recommends Ways to De-Risk VA Living Benefits

By Editor Test *Wed, Jun 10, 2009*

A new report from Milliman recommends ways that variable annuity issuers can simplify their living benefits to minimize a potential increase in reserves when "VACARVM" kicks in later this year.

Coincidentally or not, the variable annuity guaranteed living benefit arms race ended only about one year ahead of the December 31, 2009 deadline when issuers of those products must adopt changes in the way they account for the risks of those products and the level of reserves they must maintain for them.

A recent report from Milliman, **A Discussion of Actuarial Guideline 43 for Variable Annuities**, explains this changing situation and recommends ways that issuers could simplify their products to minimize a potential increase in reserves.

The study, published in April by Milliman actuaries Novian Junus and Zohair Motiwalla, advises variable annuity issuers to:

- Introduce longer wait periods for GMIB (guaranteed minimum income benefit) and GMAB (guaranteed minimum accumulation benefit) designs.
- Use deductibles on the benefit available to the policyholder where there are roll-ups or ratchets, so that the guaranteed increase each year—five percent, for instance—is based on only 90% of the initial premium rather than the entire premium. On the roll-up dates, the contract owner could increase the guaranteed income base either by an amount equal to five percent of 90% of the current income base or to the current account value, if greater.
- Put a cap on the roll-up guarantees, so that there's a ceiling on the guaranteed amount that can be reached.

The authors also recommend a number of protective measures that some issuers have already taken, such as restricting investment options, raising rider charges, using the benefit base rather the account value (or the higher of the benefit base or account value) as the basis for calculating rider fees, automatically shifting assets to a fixed account during market declines, and using dynamic hedging.

As of December 31, 2009, under a rule finalized by the National Association of Insurance Commissioners in September 2008, insurance companies will have to adopt a reserving standard, known as AG VACARVM (Actuarial Guideline covering the Commissioners' Annuity Reserving Valuation Method for VAs).

VACARVM is based on a "principles-based," stochastic (that is, randomly-determined) method of quantifying the sensitivity of variable annuities with living benefits to market risks. It is considered more predictive of unusual events than the deterministic method currently in use.