Actuarial Risk Management
Global Actuarial Consultancy

Strategies & Risk Solutions for Executives

To Our Subscribers

We want to thank our new subscribers and welcome everyone to the sixth issue of the ARM quarterly newsletter! During the past 3 months, our list of subscribers has reached a total of 300! We hope that you all find this publication valuable. With a few short articles meant to provide unique insights, we present ideas about how to address specific problems and introduce potential risks that may not yet be on your radar.

The primary authors are Dave Ingram and Max Rudolph. We have been active participants in the risk management, actuarial, investment and insurance spaces for many years.

Subscribers are encouraged to suggest topics for articles and ask questions of the authors during our follow-up webinars and podcasts. Ever cognizant of regulatory requirements, leveraging them to add value to your company in practical ways, will be our focus.

Published by Actuarial Risk Management (ARM), the Strategic and Risk Solutions for Executives (SRSE) subscription is free to all.

A free webcast is also available and our podcasts covering these topics is called Crossing Thin Ice. If you would like to further engage the authors as consultants or for continuing education purposes, please reach out. More info can be found throughout this newsletter. We hope to help you find a solution that meets your needs!

For more details
Visit actrisk.com

Listen to Crossing Thin Ice on your favorite podcast platform

We hope you will join us on our journey!

Sign-up to receive future newsletters automatically at https://www.surveymonkey.com/r/AMRSRSE

The content of this newsletter is meant to be educational and thought provoking. Nothing in it should be construed to be investment advice.

+1 512-345-5200 | info@actrisk.com | www.actrisk.com | 5914 West Courtyard Drive, Suite 190. Austin, Texas 78730

AG53 Primer

Actuarial Guideline LIII, more commonly referred to as AG53, was adopted in 2022 and is effectively an extension of long-standing asset adequacy analysis requirements for life insurers.

A team of ARM consultants authored a research paper on AG53. This paper, Practitioner Considerations for Guideline Excess Spread Attribution Methodology under Actuarial Guideline LIII (AG53) | SOA, was sponsored by the Society of Actuaries Research Institute. The paper lays out a number of considerations and defines a set of principles that appointed actuaries could take into account when performing some of the work required by AG53.

What Led to the Adoption of AG53?

AG53 was adopted when insurance regulators became more concerned about the increasing complexity of investments on life insurer balance sheets. This was partly driven by the recent sustained low interest rate environment and insurers searching for higher yields. A concern is that the increased investment risk on insurer balance sheets has outpaced the level of disclosure and stakeholders' understanding of these risks.

More specifically, there has been concern about how these increasingly complex assets are being modeled in cash flow testing, the most commonly used method of asset adequacy analysis. The concern is that the complexity of the assets has gotten beyond the capabilities of many actuarial models and also beyond the expertise of many of the modelers. Modeling simplifications that may have been acceptable in the past when these assets were a smaller proportion of insurers' balance sheets may no longer be appropriate, potentially understating risk and reserve adequacy.

What Does AG53 Require Companies To Do?

AG53 requires increased disclosures, but there is no prescribed impact to reserves or risk-based capital for most companies.

One key focus area for AG53 is Projected High Net Yield (PHNY) assets. Assets are considered PHNY if they have a net market spread in excess of stated investment grade benchmark levels.

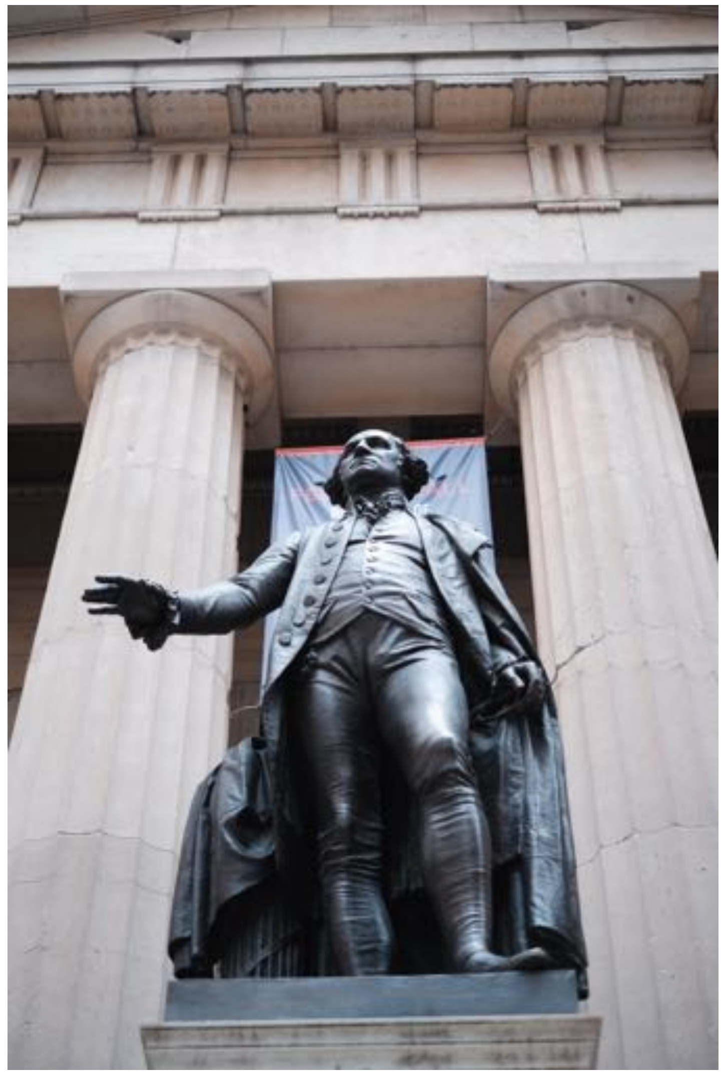
+1 512-345-5200 | info@actrisk.com | www.actrisk.com | 5914 West Courtyard Drive, Suite 190. Austin, Texas 78730

AG53 Primer (cont'd)

There are required sensitivity tests for assumed reinvestment PHNY assets, both for fixed income and equity-like assets. Spreads or returns are capped at levels lower than most companies would set their best estimate assumptions for many asset classes.

There is also a requirement to perform, disclose results of, and comment on an Excess Spread Attribution. This Attribution, which is to be performed for both existing and reinvestment assets, decomposes the total amount of a PHNY asset's net market spread in excess of a benchmark into various risk buckets. These risks include credit, illiquidity, and others as the appointed actuary deems appropriate. This is the most complex part of AG53 and the analysis is new for most, if not all, companies.

Why is AG53 Important for Risk Management?
Effective risk management requires a conscious balance between risk and return. AG53 focuses on asset risks – specifically the more complex risks that are more difficult to model and quantify. Appointed



+1 512-345-5200 | info@actrisk.com | www.actrisk.com | 5914 West Courtyard Drive, Suite 190. Austin, Texas 78730

AG53 Primer (cont'd)

actuaries have increased regulatory responsibilities regarding investment risks and how they are incorporated into their models.

Companies can look beyond the regulatory aspect of AG53 work to how they can fully lever the analytics embedded in the report. Consider questions like these:

- Do my investments appear to be efficient when looked at from a risk-return perspective?
- Do investment classes have higher expected returns relative to their modeled risks?
- Do the return profiles for these asset classes make sense prospectively? Are these above-market yields sustainable for the foreseeable future?
- Are there concentrated risks in the company's asset exposure? What happens if this risk actually occurs? Have these risks been incorporated into the company's risk management reports (e.g., ORSA, stress tests, Board-level risk reports) to ensure awareness of risks and exposures?

What is Next for AG53?
Since AG53 is new and requires some analyses that are fairly novel (e.g., Excess Spread Attribution), the Guideline actually states that the initial AG53 reports for year-end 2022 should be produced with a "best efforts" approach. We expect that the bar will be raised in the near term as regulators review company

AG53 reports and provide feedback both privately to individual companies and publicly to the industry.

Each year when insurers prepare this report, they will have to step back and think about risk with a fresh set of eyes because market conditions are always evolving. The perceived level and price of risk for each risk type will likely change; therefore, companies won't be able to reuse the same basic approach to AG53 every year. Insurers and their appointed actuaries will need to be more attuned to how changing market dynamics impact their investment portfolios.

Sign up for the associated June 22 webinar

+1 512-345-5200 | info@actrisk.com | www.actrisk.com | 5914 West Courtyard Drive, Suite 190. Austin, Texas 78730

ARM

Actuarial Risk Management

Strategic Risk Focus for Insurance Company Board Members and Executives

Two-part training program on May 24 and June 7 at 2 pm ET leveraging CGAD requirements to demonstrate the importance of risk management processes and the most common current concerns. Register for free: Part 1 and Part 2

Additionally for a fee, we offer a private session customizing Part 1 and/or Part 2 to incorporate specific information that reflects your company's unique ERM program, key risks and Board role for just your Board members and Executives.

Part 1 (May 24)

ERM & Board Role

- General introduction designed for new board members and executives and as a refresher for current board members and executives who have been less involved in ERM in the past
- Primary components of Insurer ERM Program
- Fundamental Board roles in ERM

Part 2 (June 7)

Current Focus of Insurer ERM Programs

- Provides broad perspective on risks most concerning to over 200 insurance executives for 2023 (identified in ARM's Dangerous Risks Survey) and the level of ERM practice by over 60 insurers (from ARM's ERM Practices Study)
- Essential background for board members to provide meaningful oversight to management in the area of ERM

Free registration for Part 2 here

> "While Enterprise Risk Management is a continuous process, Own Risk Solvency Assessment (ORSA) and NAIC Corporate Governance Annual Disclosure (CGAD) require insurance company leaders to annually report on their risk management program including direct Board involvement."

DAVID INGRAM | SENIOR ERM CONSULTING ACTUARY

BDO ALLIANCE USA

ARM is the leading next generation actuarial and consulting firm and since 2006 continues to work with many Top 30 accounting firms, including BDO USA, LLP and members of the global BDO network.

Insurance companies continue to trust and rely on ARM. You can too. It's that simple.

info@actrisk.com | 1-512-345-5200 | Visit us on LinkedIn | 5914 West Courtyard Drive, Suite 190. Austin, Texas 78730

Actuarial Risk Management
Global Actuarial Consultancy

Strategies & Risk Solutions for Executives

Now providing three ways for you to get insights, strategies and solutions from ARM consultants to help resolve your risk issues.

Newsletter

- 3 to 6 articles quarterly
- Written by Dave Ingram, Max Rudolph and other ARM consultants focusing on risks faced by insurers and risk management strategies
- Available on the ARM website

Webcast

- One-hour live webcast once each quarter following the newsletter publication
- Webcast includes brief presentations, interviews with authors and live Q&A with your questions answered regarding the newsletter topics

Podcasts

- Two per month
- Delivered by Dave Ingram & Max Rudolph
- Presenting material from the newsletters and webcasts in a totally audio format.
- Available wherever you usually download podcasts

* No charge to subscriptions to all three services

"While insurers have been challenging by low interest rates and the pandemic, the next few years will see a radically changing environment for insurers. We will be using this provocative platform to identify emerging risks and delve into what we see as the drivers of future success."

DAVE INGRAM | SENIOR ERM CONSULTING ACTUARY

Sign-up to receive notices for all three automatically at https://www.surveymonkey.com/r/AMRSRSE

+1 512-345-5200 | info@actrisk.com | www.actrisk.com | 5914 West Courtyard Drive, Suite 190. Austin, Texas 78730