Bruce and Bruce Company

CONSULTING ACTUARIES

NEWSLETTER

August 2016

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Valuation Interest Rates

Life
The life reserve rate stays at 3.50% for 2017.
Immediate Annuities
The SPIA valuation rate is 4% for 2016.

2012 IAR in Pennsylvania

The Pennsylvania Insurance Department has approved the use of the 2012 Individual Annuity Reserve Table to determine minimum reserves for immediate annuities. These new minimum standards will apply to annuities issued on or after November 1, 2016 in Pennsylvania. The 2012 IAR table is a generational table that incorporates projections for future mortality improvements, taking into account the fact that people are living longer. It would be appropriate to determine payment amount rates on this table as well.

Principles-Based Reserves (PBR) Update

As you probably know, Principles-Based Reserving (PBR) is to become effective nationally on January 1, 2017. A key component of the implementation of PBR is the Small Company Exemption (SCE) which attempts to address the needs of smaller insurers by providing an exemption from PBR rules for insurers with less than $300 million in annual life insurance premium and with an RBC ratio of 450%.

Earlier this month, the American Fraternal Alliance (AFA) informed its members that an amendment to the SCE has been drafted by regulators from those states in which a majority of fraternals are domiciled (Texas, Minnesota, Wisconsin, Pennsylvania, Ohio, and Illinois).

According to the AFA, the amendment "would exempt **all insurers with less than $50 million** in annual life insurance premium from the 450% RBC requirement when seeking an SCE from PBR. These insurers, which include a majority of fraternals, would submit a request to the commissioner under the requirements of the SCE but without the 450% RBC requirement". The AFA also indicated that consideration for approval of this SCE amendment will likely take place in 2017 and that, if adopted, this amendment would become effective on January 1, 2018.

Non-Qualified Deferred Compensation Plans

By David Chan, Enrolled Actuary

Most of us are familiar with qualified plans such as defined benefit pension plans for employees, 401(k) plans and profit sharing plans. These plans are qualified plans since they satisfy the requirements of Internal Revenue Code 401(a) and other non-discrimination codes. These plans enjoy many tax deferral benefits for employers and employees. But they also require more administration procedures including annual reporting to the IRS, the Department of Labor (DOL) etc. which will require more time and cost.

There also many types of so called Non-Qualified Deferred Compensation Plans (NQDC) that can provide recipients (employees, directors or independent service providers, etc.) with some tax deferred benefits but without the administrative burden of such annual reporting to the IRS or the DOL if certain requirements are met.

To enjoy the benefits of a NQDC one key requirement is that it generally must be an unfunded plan.

What is the difference between a funded plan and an unfunded plan? Why is it important for a NQDC plan to be unfunded?

NQDC plans are either funded or unfunded, though most are intended to be unfunded because of the tax advantages unfunded plans afford participants.

An unfunded arrangement is one where the employee or a non-employee such as a director, has only the employer's "mere promise to pay" the deferred compensation benefits in the future, and the promise is not secured in any way. The employer may simply keep track of the benefit in a bookkeeping account, or it may voluntarily choose to invest in annuities, securities, or insurance arrangements to help fulfill its promise to pay the employee. Similarly, the employer may transfer amounts to a trust that remains a part of the employer's general assets, subject to the claims of the employer's creditors if the employer becomes insolvent, in order to help keep its promise to the employee. To obtain the benefit of income tax deferral, it is important that the amounts are not set aside from the employer's creditors for the exclusive benefit of the employee. If amounts are set aside from the employer's creditors for the exclusive benefit of the employee, the employee may have currently includible compensation.

A funded arrangement generally exists if assets are set aside from the claims of the employer's creditors, for example in a trust or escrow account. A qualified retirement plan is the classic funded plan. A plan will generally be considered funded if assets are segregated or set aside so that they are identified as a source to which participants can look for the payment of their benefits. For NQDC purposes, it is not relevant whether the assets have been identified as belonging to the employee. What is relevant is whether the employee has a beneficial interest in the assets, such as having the amounts shielded from the employer's creditors or the employee has the ability to use these amounts as collateral. If the arrangement is funded, the benefit is likely taxable under IRC §§ 83 and 402(b).

DOL Fiduciary Rule

The Department of Labor (DOL) fiduciary rule will begin to take effect next April. The new rule requires all financial advisers to recommend what is in the best interests of their clients when they offer guidance on 401(k) plan assets, individual retirement accounts, or other qualified monies saved for retirement.

The DOL rule does not ban commissions or revenue sharing, but it requires advisers who accept them to have clients sign a best interest contract exemption or BICE. It pledges the adviser will act in the client's best interests and only earn "reasonable" compensation. The exemption also must disclose information to clients about fees and conflicts of interest.

Corporate Governance Annual Disclosure (CGAD)

According to the NAIC, the following states have adopted the Corporate Governance Annual Disclosure Model Act and Regulation (CGAD) for 2016: California, Indiana, Iowa, Louisiana and Vermont. Other states may be adopting it during this legislative season.

Among other requirements, the CGAD requires companies to determine whether its officers and key persons in control functions have the appropriate background, experience, and integrity to fulfill their respective roles. Thus, you may need to provide appropriate support to document the elements described. In addition, you will need to describe how the reporting responsibilities are organized for each critical area. Those risk areas include risk management processes, actuarial function, investment decision-making processes, reinsurance decision-making processes, compliance function, financial reporting/internal auditing, and market conduct decision-making processes.

New Board Member Training

4 - 6 hour training session in your Home Office or the remote location of your choice

Topics

1. Annual Statement financial information (pages 1 - 17 plus Schedule D and AVR and IMR);
2. Annual Actuarial Valuation;
3. Asset Adequacy Analysis and Cash Flow Testing;
4. Risk Based Capital;
5. New Plan Development;
6. Sales Illustrations (if applicable);
7. Other, such as mergers and regulatory environment (as time permits).

Training Materials: Society Annual Statement, sample Society plan manuals, and Society cash flow/RBC information

Contact us for more information or to set up a training session.

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