

EQH

FASB Long Duration Targeted Improvements (FASB TI) Implementation - Accounting Policy Decisions

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Topic

Time

Slide

1. Overview of LDTI Accounting Policy Development Process
2. A deep dive example - DAC

- 5 minutes

3

- 25 minutes

4-11

Accounting Policy Development Cycle



DAC Guidance Interpretations

Based on our interpretations of the FASB guidance, there are four accounting decisions we have to make:

- **What's the scope of the DAC like balances that will be impacted by LDTI?**
 - Balances like Sales Inducement Assets (SIA), Unearned Revenue Liability (URL) and Terminal Dividend Liability (TDL) are required to be amortized on a straight-line basis (consistent with DAC) and would not be accreted with interest.
 - However, other balances like Cost of Reinsurance (COR) and Value of Business Acquisition (VOBA) are not required to follow the new DAC amortization approach, but permissible.
- **What's the unit of account for DAC?**
 - Explicitly, should we choose to amortize DAC on the seriatim approach or cohort approach? If cohort approach is chosen, it needs to be consistent with LFPB cohorting approach.
- **What's the amortization approach for DAC?**
 - Explicitly, should we pick the FASB amortization approach with experience adjustment or the Alternative approach proposed by PwC and endorsed by FASB?
- **What's the amortization basis for DAC?**
 - Explicitly, what should we pick among face amounts, policy counts, initial deposits, etc., and for which product?

Scope – DAC Like Balances

We designed our scoping template and collected the following information from our SME. These information help us to determine the products in scope, materiality of the block, and potential operational implementation complexity down the road.

					Current System Information	
Legal Entity	Product	Balance Type (DAC/URR/VOBA/Cost of Reinsurance)	Current Balances as of 12/31/18 (\$m)	Current Amortization Basis	Current Valuation System	Current Valuation Granularity
EQH	Product X	DAC	\$ XXX	Revenues	AXIS	Issue Year
EQH	Product X	DAC	\$ XXX	EGP	AXIS	Issue Year
EQH	Product X	DAC	\$ XXX	Revenues	AXIS	Issue Year

					Current System Information	
Legal Entity	Product	Balance Type (DAC/URR/VOBA/Cost of Reinsurance)	Current Balances as of 12/31/18 (\$m)	Current Amortization Basis	Current Valuation System	Current Valuation Granularity
EQH	Product X	URL	\$ XXX	EGPs	Excel	Product
ALA	Product X	URL	\$ XXX	EGPs	Excel	Product

					Current System Information	
Legal Entity	Product	Balance Type (DAC/URR/VOBA/Cost of Reinsurance)	Current Balances as of 12/31/18 (\$m)	Current Amortization Basis	Current Valuation System	Current Valuation Granularity
USFL	Product X	VOBA	\$ XXX	Premiums	Excel	6 cohorts
MLOA	Product X	Cost of Reinsurance	\$ XXX	Persistency	Spreadsheet	Product

3a. Analysis on DAC Unit of Account

Decision Point: Should the DAC Unit of Account be seriatim or cohort?

Recommendation:

We propose cohort to be the unit of account for DAC like balances on the basis of the following considerations.

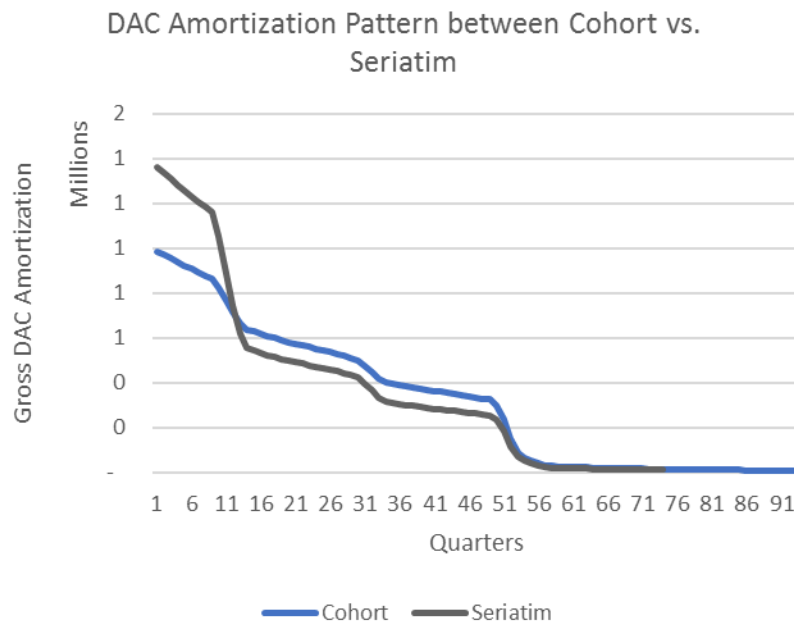
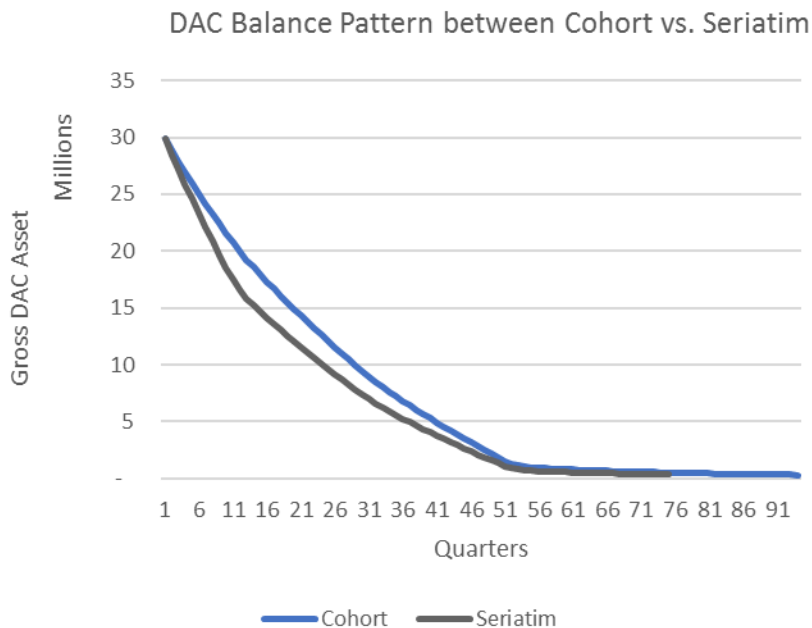
Considerations:

Financial	Operational	Industry Peers
<ul style="list-style-type: none">Representative cohorts are selected and sensitivity analysis are performed.	<ul style="list-style-type: none">Prototyping exercise was performed in selected valuation system.	<ul style="list-style-type: none">Participated in industry survey and reviewed results.
<ul style="list-style-type: none">DAC is amortizing slower on the cohort basis compared to seriatim basis.This effect is amplified for the term business.	<ul style="list-style-type: none">Run-time: prototyping observes up to 50% savingsData: seriatim expense allocation requires developing a process for non-commission expenses	<ul style="list-style-type: none">X% of the insurers participated in the survey now expect to amortize DAC on a cohort basis.Y% expected to amortize DAC on a seriatim basis.

Accounting Topic: DAC Unit of Account

Additional Details on Financial Considerations

The following chart is based on one Term Cohort using face amount as amortization basis.



Cohort approach provides a smoother amortization pattern. This pattern is amplified for term business.

3b. Analysis on DAC Amortization Approach

Decision Point: Should we pick FASB approach or Alternative approach

Recommendation:

We propose to use Alternative approach for DAC amortization on the basis of the following considerations..

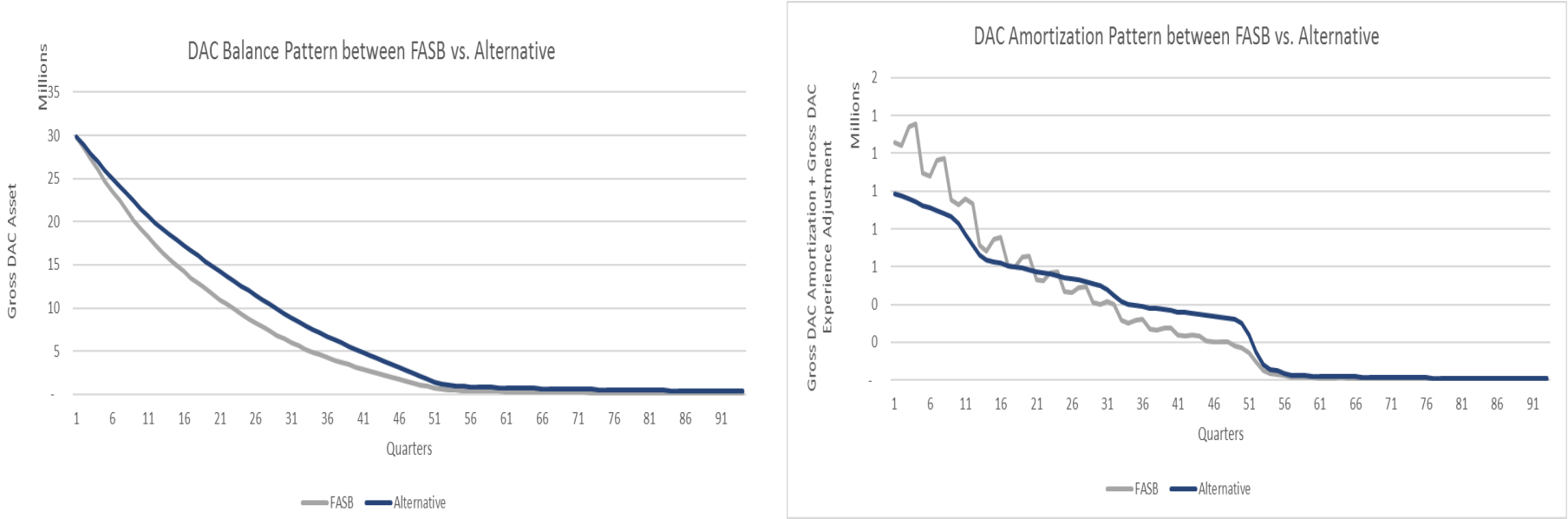
Considerations:

Financial	Operational	Industry Peers
<ul style="list-style-type: none">Representative cohorts are selected and sensitivity analysis are performed.	<ul style="list-style-type: none">Prototyping exercise was performed in selected valuation system.	<ul style="list-style-type: none">Participated in industry survey and reviewed results.
<ul style="list-style-type: none">If experience emerges as expected, minimal difference between approaches.If not, Alternative projects favorable DAC results (i.e., slower amortization)Alternative is less volatile due to lack of adjustment	<ul style="list-style-type: none">For FASB, more line items in disclosures, SOX controls, and audit effort.For FASB, additional input requirements sourced from prior valuation results	<ul style="list-style-type: none">X% of the insurers participated in the survey are choosing AlternativesY% expected to choose FASB approach.

Accounting Topic: DAC Amortization Approach

Additional Details on Financial Considerations

The following chart is based on one Term Cohort using face amount as amortization basis, assuming 5% more lapses than expected annually.



Alternative approach provides a smoother and slower amortization pattern in early years than FASB approach

3c: Analysis on DAC Amortization Basis

Decision Point: Which amortization basis should we pick for each product?

Recommendation:

We propose to use face amounts for life business; policy counts for annuity business on the basis of the following considerations.

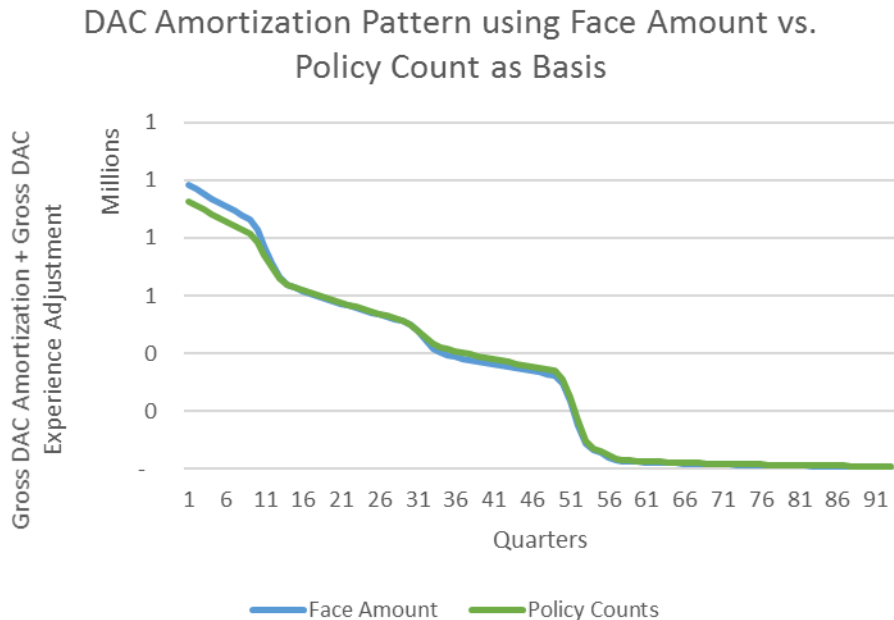
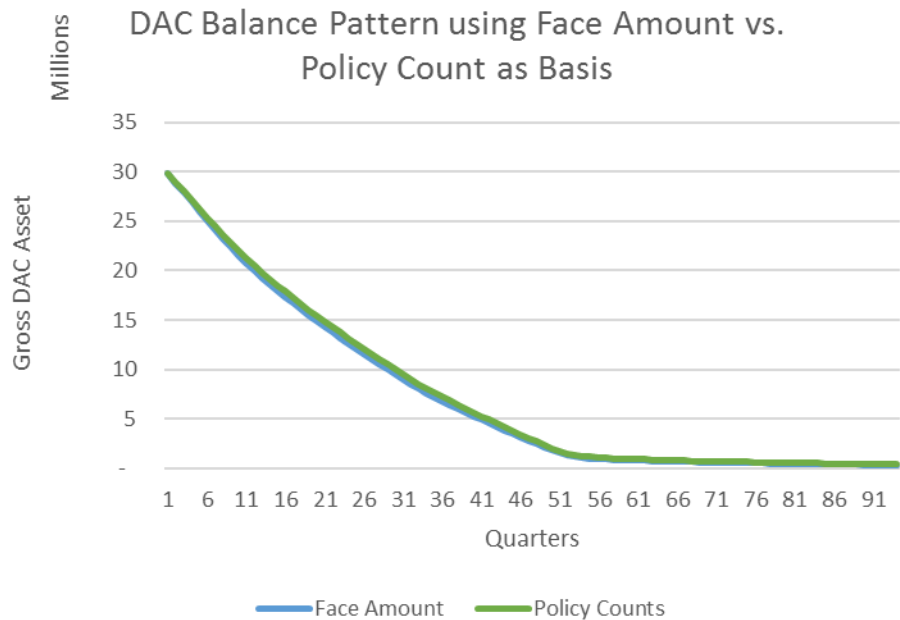
Considerations:

Financial	Operational	Industry Peers
<ul style="list-style-type: none">Representative cohorts are selected and sensitivity analysis are performed.	<ul style="list-style-type: none">Prototyping exercise was performed in selected valuation system.	<ul style="list-style-type: none">Participated in industry survey and reviewed results.
<ul style="list-style-type: none">Financial impact is only marginally different under different amortization basis.	<ul style="list-style-type: none">Operational considerations are comparable among different amortization basis.	<ul style="list-style-type: none">For life, X% of the insurers participated in the survey are choosing face amounts compared to Y% choosing policy counts.For annuity, W% of the insurers participated in the survey are choosing policy counts compared to Z% choosing initial deposits.

Accounting Topic: DAC Amortization Basis

Additional Details on Financial Considerations

The following chart is based on one Term Cohort:



Face Amount is only marginally higher amortization amounts in early years than Policy Counts.

Thank you

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