ACLI
Financial Security for Life

Brian Bayerle
Chief Life Actuary
202-624-2169
BrianBayerle@acli.com

February 28, 2025

Rachel Hemphill,
Chair, NAIC Life Actuarial (A) Task Force (LATF)

Fred Andersen,
Minnesota Department of Commerce

Re: 1/28 Actuarial Guideline for Reinsurance Asset Adequacy Testing

Dear Chair Hemphill and Mr. Andersen:

The American Council of Life Insurers (ACLI) appreciates the opportunity to provide feedback on the January 28th exposure of the Actuarial Guideline for Reinsurance Asset Adequacy Testing (Guideline).

We support regulators having tools and information they need to determine whether the assets supporting liabilities for US policyholders are adequate, including in cases where the business has been reinsured. ACLI also supports LATF's effort to implement this initiative by year-end 2025. We note, however, that material components of the Guideline (see Miscellaneous in Appendix) are unresolved and warrant further discussion.

ACLI proposes a simplified version of the Guideline requiring the Appointed Actuary to provide an appropriate assessment of reinsurance-related exposures and potential risk indicators. The assessment would address identified risks and mitigating factors and allow for alternative forms of analysis or submission of non-US jurisdiction reports, along with any supplemental materials that meet the criteria specified by the Guideline. Such an approach would also provide for domestic regulator discretion regarding the analysis performed when certain criteria are met.

We submit the following recommendations in the initial version of this Guideline. The Guideline should:

1. Provide a degree of flexibility for the Appointed Actuary in their assessment of the adequacy of reserves while maintaining the discretion of the domestic regulator in enforcing their statutory authority with respect to acceptable forms of analysis and any additional analysis they deem necessary to adequately assess risks.

The American Council of Life Insurers is the leading trade association driving public policy and advocacy on behalf of the life insurance industry. 90 million American families rely on the life insurance industry for financial protection and retirement security. ACLI's member companies are dedicated to protecting consumers' financial wellbeing through life insurance, annuities, retirement plans, long-term care insurance, disability income insurance, reinsurance, and dental, vision and other supplemental benefits. ACLI's 275 member companies represent 93 percent of industry assets in the United States.
acli.com

2. Eliminate the introduction of the term "Associated Party," and, in tandem with the authority of the domestic regulator to require the level of analysis they deem necessary, target high-risk asset-intensive reinsurance transactions of concern whether affiliated or not.
3. Limit the scope to all transactions issued 2020 and later, while maintaining the authority of the domestic regulator to require additional asset-intensive reinsurance transactions to follow the requirements of this Guideline.

The outlined approach will allow the Appointed Actuary to align the information with the framework of the jurisdiction of the assuming company. Understanding how these frameworks reflect risk can provide valuable insights for US regulators and enhance their ability to effectively oversee reinsurance transactions.

Recognizing that the Guideline may need to be revisited after domestic regulators' review of initial submissions allows for a streamlined process and more comprehensive discussions post-adoption. This approach will help ensure smoother implementation and foster constructive dialogue among all stakeholders involved.

Additional details regarding these recommendations and other proposed edits to the Guideline can be found in Appendix A. A redlined version of the Guideline is provided as a separate document.

We look forward to further dialogue on the Guideline and to achieve a shared objective of bringing greater transparency regarding asset-intensive reinsurance transactions to domestic regulators.

Sincerely,

CC: Scott O'Neal, NAIC

Appendix A: Rationale of Material Edits to the Guideline

Flexibility (Add Guidance Note in Section 1; Edit 5.B, 5.F, 5.H)

Any regulation applied several years retroactively will necessitate accommodation for companies that could not have foreseen that this Guideline would be introduced in 2025.

From a modeling perspective, testing as anticipated by US regulators may present challenges due to the complexity and customized nature of most reinsurance transactions. Ready-made models may not be available for the intended testing exercise, particularly for transactions that are 100% ceded or established long before this guideline was considered.

Irrespective of the counterparty's relationship to the cedant, the required data may not be readily available. While asset information may be more accessible, especially if funds are withheld or held under Modified Coinsurance (ModCo) arrangements, the assets may not be segregated for that particular transaction but rather be part of a broader portfolio managing many transactions.

The Appointed Actuary should disclose the methodology used to evaluate the reinsurance transactions by counterparty. The disclosure should include a rationale regarding why the analysis is suitable for the counterparty and related liabilities, including an evaluation of the data utilized. Data limitations should be explicitly addressed, e.g., by including sensitivities, and result ranges to mitigate such limitations. The Appointed Actuary should explain their analytical basis and how they considered the baseline run, in addition to other analysis, to substantiate the adequacy of reserves. As a note, we recommend using the term "baseline" rather than "mandatory" because the run is only mandatory in the context of cash flow testing.

There will always be a need for some elements of simplification and judgment in this type of analysis. While improvements can be expected over time, these limitations will never be entirely eliminated. There will always be data and assumption constraints for certain transactions. Appointed Actuaries may not be able to demonstrate that results would be more favorable than approximations due to data limitations. Rather, domestic regulators can challenge any simplifications they believe to be inappropriate.

This approach is consistent with the implementation of Actuarial Guideline 53, where regulators were able to gather extensive information to make informed judgments, follow up as necessary, and adjust as deemed appropriate. Companies are already performing robust analysis that should be considered during regulator reviews. Regulators will have the ability to assess the submissions for year-end 2025 and enhance guidance if warranted.

Domestic Regulator Discretion (Edit 5.H):

The domestic regulators often have a high degree of comfort with the reinsurance deals of their domestic carriers. This can be true regardless of the size of the transaction and regardless of the cedant's relationship to the counterparty. For this reason, we recommend allowing the domestic regulator authority to both exempt transactions from all or portions of the Guideline framework and allowing alternative analyses.

Remove "Associated Party" (Remove 3.C, 5.A.(1), 5(A).2, 5.H.(1); Edit 4.C):

As we have discussed in previous comments, we believe the scope of the framework should be based on the risk of the transactions. There is no need to differentiate transactions based on the cedant's relationship (or lack thereof) with the counterparty, particularly if LATF moves forward with our recommendations related to flexibility as detailed above. Further, we do not feel it is

appropriate or necessary to introduce a new concept of "Associated Party" into the framework given the Guideline will apply to transactions with both affiliated and non-affiliated counterparties. State regulators maintain their authority to require additional analysis and testing for any transactions not in scope of the Guideline.

More broadly, the concept of "Associated Party," would create an entirely new classification within the NAIC that may cause confusion and/or conflict with existing definitions related to insurer relationships. We believe this concept—particularly the additions of sections 3(c)(2) and 3(c)(3)--is a deviation from the "affiliated" and "ownership" definitions of Model #440 and #450. It is imperative that any new concepts that relate to ownership and control be sufficiently understood by NAIC leadership and approved utilizing the Financial Regulation and Accreditation Standards Committee approval processes in order to ensure there is continuity across the US statutory framework, consistent implementation of the concepts across states, and certainty to insurers and other stakeholders.

For these reasons, we recommend striking the concept.

Scope should cover 1/1/2020 and later transactions (Edit 2.A and 2.B):
The NAIC adopted a principle-based reserving (PBR) statutory framework for US life insurance products under VM-20 with an effective date of January 1, 2017, to be mandatory for new business sold on January 1, 2020, and later. Therefore after 2020, the reserve determined by a cedant and an assuming company can be different.

As previously noted, there will need to be accommodation for older transactions prior to the implementation of these requirements.

We note that the domestic regulator will continue to have the authority to require companies to test additional transactions at their discretion.

Remove NY 7 Scenarios (Remove [renumbered] 3.J.(6).(a), 6.D, Edit 9.A):
The NY 7 Scenarios, while commonly included in the analysis of the Appointed Actuary, are not required to be tested under VM-30. It would be inappropriate to create a scenario standard for ceded business that does not currently exist for retained business. Testing performed by the Appointed Actuary needs to consider moderately adverse conditions, which may or may not include consideration of the NY 7 Scenarios.

Rationale for Including Additional Assets in Alternate Run (Remove 6.B.(4), Edit [renumbered] 6.B.(3)):
In the event of an adverse event, the cedant may have dedicated assets backing the reinsurance transaction that exceeds the amount of the reserve held by the assuming company. For example, in situations where a trust is over-collateralized (e.g., 105% of statutory reserves), it seems logical that a company could use all of those assets in their analysis. The same transaction with an overcollateralized trust is less risky than one without, and that should be reflected in the Alternative Run. Also, we support the principle that assets used for ceded reinsurance analysis be treated no differently than assets used for analysis of retained liabilities; that is, any type of investment that can be used for testing retained business should be able to be used when testing ceded business.

While we acknowledge a regulatory desire for a consistent basis for review in the baseline run, we believe there needs to be greater flexibility in the Alternative Run. We request that the Appointed Actuary be permitted to make the determination of what assets should be included and how they

should be valued, noting that other assets and protections aside from Primary Securities have value in this analysis. Asset returns can be haircut to achieve a moderately adverse standard, with clear documentation on the anticipated return on those assets.

Similar Memorandum (Remove 5.G.(1), Edit [renumbered] 3.J):
We would like to suggest that for an assuming company in a Certified or Reciprocal Jurisdiction, a Similar Memorandum could be submitted to their regulator who can share it confidentially with the domestic regulators of the companies ceding to the assuming company. For Unauthorized Reinsurers, such a report should be submitted to the domestic regulator of its US affiliate (if it has one) as such domestic regulator would be a member of its Supervisory College and would be most familiar with it. Such a regulator could, in turn, share it confidentially with the domestic regulator of the assuming company's cedants. If an Unauthorized Reinsurer had no US affiliate, it would need to provide such a report directly to its cedants' domestic regulators.

Attribution Analysis (Edit 7.A)
Previously, regulators agreed to use the ACLI version of the template that reconciled to the cedant's best estimate reserve. This should, to the extent practical, reflect any adjustments that would be anticipated to be made in the regulatory framework of the assuming company.

Remove US-Specific Requirements (Edit 6.C, [renumbered] 3.J, 3.K; future discussions on Sections including [renumbered] 3.D, 3.J.(6), [renumbered] 3.L):
Several items were US-specific requirements that would be applied to non-US jurisdictions or requirements. Where feasible, we attempted to retain the spirit of the item. There should be a broader discussion for the next exposure on remaining US-specific concepts and how they could be adapted to be applicable for other frameworks.

Aggregation (Remove 6.B.(1); Edit 5.D, 8):
While aggregation is not a direct consideration of this exposure, we wish to comment on the importance of addressing it in the Guideline now rather than later. Aggregation of testing results at the counterparty level ensures that the Guideline aligns with the underlying economics and actual risks of a counterparty failure (i.e., a counterparty would fail at the entity level rather than a product, treaty, etc. level). Further, as a fundamental principle for the insurance business model, aggregation should not just be allowed at the counterparty level. The cedant should also be allowed to aggregate results of the counterparty level reinsurance analysis with the results for retained business to align with how testing would apply if the cedant were to recapture the business. Both pieces of information are needed to appropriately assess the risks of a counterparty failure.

Given this section appears to only apply to Section 6, we recommend that Section 8 be moved to subbullets of that section.

Miscellaneous:
- The list of unresolved material components includes how to handle existing AAT Reserves held on transactions in scope, the appropriate basis of starting assets (market vs book value), accounting concepts such as "significant collectability," among others.
- Edit Section 2.A.(1) and 2.B.(1): Reserve credit is determined based upon the statutory annual statement filed by the cedant for the prior year. For treaties that are ceded on a coinsurance with funds withheld basis, including both the reserve credit and the funds withheld would be double counting certain amounts. Suggest clarification.

- Remove 4.B.(1) and 4.D: A transaction would not be in scope if it met the criteria, so this consideration is redundant and should be removed. Risk identification also only applies to reinsurance transactions outside of the US.
- Move 6.B.(3).(iii): These examples are more appropriate as an appendix rather than in the body of the Guideline. We recommend dialogue on these examples during a future exposure.