May 17, 2024

Ms. Rachel Hemphill
Chair, Life Actuarial (A) Task Force (LATF)
National Association of Insurance Commissioners (NAIC)

Re: LATF's March 17, 2024 AAT Reinsurance Exposure

Dear Ms. Hemphill,

I am submitting this comment letter to you as President and Consulting Actuary of Routhenstein & Co, rather than on behalf of the Academy. Please note that I am Co-Chair of the Academy's Asset Adequacy and Reinsurance Issues Task Force (AARITF), which provided a May 17 comment to LATF on this topic.

I strongly believe that the March 17 exposure is not a good starting point to address regulator concerns. Instead, I am supportive of the alternative disclosure-based approach described in the Academy's May 17 comment letter. I believe that most LATF members would also be supportive if they could envision how the details might be filled in to address regulatory concerns raised in the March 17 exposure. However, with the current absence of such details I suspect that some of those LATF members might find that it difficult to support the Academy's May 17 alternative disclosure-based approach over a refined version of March 17 exposure. **Below I summarize one possible way to implement the Academy's May 17 alternative disclosure-based approach, and then summarize some of the advantages of such an approach over the March 17th exposed approach**.

As one way to implement the Academy's May 17 alternative disclosure-based approach, I suggest that the quantitative disclosure in the confidential filing be required to include a principles-based measurement of the cedant's exposure to noncollectible reinsurance. There would be a description of one or more simplified ways to perform the calculation, where more sophisticated approaches would be encouraged, and where all calculations would be based upon the actuary's professional judgment. The required quantitative disclosure might include the following:

a. The present value of future reinsurer default costs (calculated i) by the insurer in a manner similar to VM-20 requirements for corporate bonds or to how the insurer calculates corporate bond default costs for Asset Adequacy Testing / Analysis (AAA), and ii) net of acceptable collateral that mitigates the insurer's credit exposure. If the company has any reinsurance ceded to a reinsurer for which a PBR Credit Rating could be determined, the filing would require the actuary to document how default costs are determined for any such reinsurers.
b. The present value of any future reinsurer default costs currently reflected in the insurer's AAA.

c. The insurer's modified total adjusted capital (TAC) if a provision for "a" were reflected in AAA requirements.
d. The insurer's modified Company Action Level RBC Ratio if a provision for "a" were reflected in AAA requirements.

Below is a summary (the details of which could be provided to LATF as follow-up) of the many advantages that such a principles-based default cost disclosure approach ("DCD") has over the 2024-03-17 exposure which I'll refer to as a vanishing treaty calculation approach ("VTCA").

a. DCD could easily be applied to a much broader span of inforce and new treaties than VTCA.
b. In a manner substantially better than VTCA, DCD helps the cedant's regulator fulfill its most important AAA oversight responsibility - to ascertain whether the cedant's reserves and supporting assets (including reinsurance ceded) make adequate provision for the cedant's policy liabilities.
c. It would be much easier for the Valuation Analysis (E) Working Group to determine DCD outliers than VTCA outliers.
d. DCD involves principles-based collectability risk assumptions, where VTCA does not.
e. DCD, unlike VTCA, could be used as a comprehensive credit risk monitoring tool by the NAIC's Financial Stability (E) Task Force.
f. DCD could be prudently implemented more quickly than VTCA, as the latter would warrant a field test to determine what impact it might have on the industry.

I would be pleased to discuss this concept further with LATF.

Best regards,

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