Statutory Accounting Principles (E) Working Group
Hearing Agenda 2
December 17, 2024

ROLL CALL

Dale Bruggeman, Chair	Ohio	Judy Weaver/Steve Mayhew	Michigan
Kevin Clark, Vice Chair	Iowa	Doug Bartlett	New Hampshire
Sheila Travis/Richard Russell	Alabama	Bob Kasinow	New York
Kim Hudson	California	Diana Sherman	Pennsylvania
William Arfanis/Michael Estabrook	Connecticut	Jamie Walker	Texas
Rylynn Brown	Delaware	Doug Stolte/Jennifer Blizzard	Virginia
Cindy Andersen	Illinois	Amy Malm/Elena Vetrina	Wisconsin
Melissa Gibson/Bill Werner	Louisiana		

NAIC Support Staff: Julie Gann, Robin Marcotte, Jake Stultz, Jason Farr, Wil Oden

Note: This meeting will be recorded for subsequent use.

REVIEW of COMMENTS on EXPOSED ITEMS

The following items are open for discussion and will be considered separately.

1. Ref #2024-05: Appendix A-791
2. Ref #2024-06: Risk Transfer Analysis of Combination Reinsurance Contracts

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2024-05 (Robin)	**Appendix A-791**	**2.1 – Agenda Item**	**Comments Received**	**ACLI – 2**

Summary:
At the Summer National meeting the Working Group noted that no written comments on the Spring 2024 exposure were received. However, at the verbal request of the ACLI, the Working Group re-exposed revisions to Appendix-791, paragraph 2c's Question and Answer. The comment deadline on this agenda item was subsequently extended to Dec. 9 at the request of the ACLI.

This agenda item was developed in response to the December 2023 Valuation Analysis (E) Working Group's (VAWG) referral to the Statutory Accounting Principles (E) Working Group which recommends making a clarifying edit to *Appendix A-791 Life and Health Reinsurance Agreements* (A-791), Section 2.c's Question and Answer by removing the first sentence, which reads, "Unlike individual life insurance where reserves held by the ceding insurer reflect a statutorily prescribed valuation premium above which reinsurance premium rates would be considered unreasonable, group term life has no such guide." The referral notes that:

> First, this sentence is unnecessary, as it is an aside in a discussion about group term life. More importantly, this statement is being misinterpreted as supporting the use of Commissioner's Standard Ordinary (CSO) rates as a "safe harbor," at or below which YRT rates would be automatically considered not to be excessive.

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> The 791 section 2c QA guidance does not provide a safe harbor based on CSO. It indicates that if the YRT reinsurance premium is higher than the proportionate underlying direct premium for the risk reinsured, then the reinsurance premium is excessive. VAWG observes that the prudent mortality under the *Valuation Manual*, Section 20: Requirements for Principle-Based Reserves for Life Products (VM-20), may appropriately be either higher or lower than the CSO rate depending on the facts and circumstances.

The Working Group also notified the Valuation Analysis (E) Working Group, the Life Actuarial (A) Task Force and the Reinsurance (E) Task Force of the exposure.

ACLI Comments
ACLI would like to express our sincere gratitude for your time and willingness to collaborate with us on these reinsurance matters. We value the open dialogue and believe it has contributed to a more informed and constructive regulatory process. Through our discussions, we have gained a deeper understanding of the concerns raised by SAPWG regulators while also conveying the perspectives of our members.

ACLI members continue to believe that the two proposals (Ref #2024-05 and Ref #2024-06) are inextricably linked and should be considered together.

Ref #2024-05: A-791 Paragraph 2.c.

ACLI members believe that retaining the language in Appendix A-791, paragraph 2.c., is consistent with the statutory accounting requirement that reinsurance should not deprive a ceding insurer of surplus. With that said, we propose changes below to SAPWG 2024-06 that, if adopted, would address our concerns with the exposed changes in SAPWG 2024-05.

ACLI agrees that statutory risk transfer requires a careful evaluation of the facts and circumstances of a reinsurance agreement and should never rely on a simplistic application of "safe harbor" rules. Appendix A-791 already provides an objective standard by which to assess whether YRT premiums are excessive. That is, premiums are considered excessive if they result in the deprivation of ceding insurer surplus. The adoption of the change proposed by 2024-05 might be interpreted as introducing some other standard to determine whether premiums are excessive. However, no objective criteria have been provided by which to apply such other standards and, as a result, the adoption of the proposed change serves to create the potential for a range of interpretations as to what constitutes an excessive YRT premium. Such differences in interpretation are already surfacing with some parties interpreting the combination of the two SAPWG exposures to indicate that all combination Coinsurance-YRT (Co-YRT) agreements are non-proportional and therefore do not provide reserve credit; a conclusion that ACLI believes is inconsistent with SAPWG intent based on conversations we have had with regulators.

To avoid the potential for misinterpretation, ACLI proposes that the 2024-05 exposed changes only be adopted if done concurrently with the ACLI version of SAPWG 2024-06 proposed below.

Another concern is that some may interpret the proposed 2024-05 exposure to require an assessment of YRT premiums using a standard other than the existing standard provided in SSAP No. 61 that precludes ceding insurer surplus deprivation. In such a case, there could be significant variation in regulatory interpretations as to what constitutes an "excessive" YRT premium leading to inconsistency rather than harmonization.

Recommendation:
NAIC staff continues to agree with the original Dec. 9, 2023 VAWG referral to the Working Group which noted that the sentence in A-791, paragraph 2c is an unnecessary sentence. The sentence proposed for deletion is to contrast that **individual life** insurance is different in a question / answer about **group term life** (see below). The reason that VAWG suggested deleting the sentence is that companies were misusing it to imply that the different individual life rules could be used for group term life and that is incorrect. NAIC staff defers to the Working Group on timing but continues to recommend deletion of this sentence.

March 2024 exposed revision to A-791, Life and Health Reinsurance Agreements, paragraph 2c QA:

2. No insurer shall, for reinsurance ceded, reduce any liability or establish any asset in any statutory financial statement if, by the terms of the reinsurance agreement, in substance or effect, any of the following conditions exist:

c. The ceding insurer is required to reimburse the reinsurer for negative experience under the reinsurance agreement, except that neither offsetting experience refunds against current and prior years' losses under the agreement nor payment by the ceding insurer of an amount equal to the current and prior years' losses under the agreement upon voluntary termination of in force reinsurance by the ceding insurer shall be considered such a reimbursement to the reinsurer for negative experience. Voluntary termination does not include situations where termination occurs because of unreasonable provisions which allow the reinsurer to reduce its risk under the agreement. An example of such a provision is the right of the reinsurer to increase reinsurance premiums or risk and expense charges to excessive levels forcing the ceding company to prematurely terminate the reinsurance treaty;

A-791, Life and Health Reinsurance Agreements, paragraph 2c's, Question and Answer):

Q – If group term life business is reinsured under a YRT reinsurance agreement (which includes risk-limiting features such as with an experience refund provision which offsets refunds against current and/or prior years' losses (i.e., a "loss carryforward" provision), under what circumstances would any provisions of the reinsurance agreement be considered "unreasonable provisions which allow the reinsurer to reduce its risk under the agreement" thereby violating subsection 2.c.?

A – ~~Unlike individual life insurance where reserves held by the ceding insurer reflect a statutorily prescribed valuation premium above which reinsurance premium rates would be considered unreasonable, group term life has no such guide.~~ So long as the reinsurer cannot charge premiums in excess of the premium received by the ceding insurer under the provisions of the YRT reinsurance agreement, such provisions would not be considered unreasonable. Any provision in the YRT reinsurance agreement which allows the reinsurer to charge reinsurance premiums in excess of the proportionate premium received by the ceding insurer would be considered unreasonable. The revisions to this QA regarding group term life yearly renewable term agreements ~~is~~ are effective for contracts in effect as of January 1, 2021.

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2024-06 (Robin)	**Risk Transfer Analysis on Combination Reinsurance Contracts**	**2.2 – Agenda Item**	**Comments Received**	**ACLI– 3 Stevenson –7**

Summary:
The Working Group exposed agenda item 2024-06 in March 2024 to address the risk transfer aspect of a December 2023 referral by the Valuation Analysis (E) Working Group (VAWG). The exposed *SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance* revisions were narrowly focused and incorporated guidance noting that interdependent contract features such as shared experience refunds must be analyzed in the aggregate when determining risk transfer. At the Summer National Meeting, the Working Group reviewed two letters. One that was in support of the exposed revisions and comments from the ACLI that requested further discussion. The Working

Group re-exposed the revisions previously exposed in March 2024 with a request for specific recommendations. The comment deadline on this agenda item was subsequently extended to Dec. 9 at the request of the ACLI.

The Working Group exposure is based on existing guidance that is in both U.S. GAAP and in *SSAP No. 62—Property and Casualty Reinsurance Exhibit A – Implementation Questions and Answers,* question 10. The exposed guidance **provides that contracts with interdependent features must be analyzed in the aggregate for risk transfer.** In addition, a reference to A-791, paragraph 6 which requires that the reinsurance contract include provisions that the agreement shall constitute the entire agreement between the parties with respect to the business being reinsured thereunder and that there are no understandings other than as expressed in the agreement was proposed to be added to the existing required YRT criteria.

The VAWG referral, excerpted below, included risk transfer concerns regarding interdependent contract features which had been analyzed for risk transfer separately instead of in the aggregate. It also raised several concerns regarding the classification of reinsurance contracts and the size of the reinsurance credit taken. The referral noted that **(bolding added for emphasis)**:

> VAWG has identified that issues arise when evaluating reinsurance for risk transfer in accordance with *SSAP No. 61—Life, Deposit-Type and Accident and Health Reinsurance*, when treaties involve more than one type of reinsurance, and there is **interdependence of the types of reinsurance, including but not limited to an experience refund that is based on the aggregate experience**. In such cases, VAWG regulators find that these types of reinsurance must be evaluated together and cannot be evaluated separately for the purpose of risk transfer. For example, where a treaty includes coinsurance and YRT with an **aggregate experience refund and the inability to independently recapture the separate types of reinsurance**, **it is not adequate to separately review the coinsurance and YRT pieces of the transaction for risk transfer**. The treaty as a whole is non-proportional. **This complexity is not immediately apparent to the regulatory reviewer, and it is important that this issue be raised broadly, so that individual state regulators are aware. In**dividual regulators are encouraged to contact VAWG if they would like additional perspective when reviewing such treaties.
>
> Generally, VAWG regulators observe that **some companies are reporting an overstated reserve credit due to a bifurcated risk transfer analysis.** Specifically, some companies reported a proportional reserve credit for a coinsurance component, despite in aggregate the reinsurer only being exposed to loss in tail scenarios. From an actuarial perspective, there is consensus among VAWG members that it is not appropriate for a ceding company to take a proportional reserve credit that reflects the transfer of all actuarial risks when not all actuarial risks are transferred.
>
> VAWG recommends that SAPWG discuss this issue, to 1**) increase familiarity with the issue and 2) consider whether any clarifications to risk transfer requirements is appropriate.**

As noted in the referral above, regulators have observed reinsurance transactions that combine both coinsurance and YRT, with interdependent features including an aggregate experience refund and recapture provisions that allow for recapture by the cedant, but only if both components are recaptured simultaneously.

VAWG observed that some insurers have assessed these components under A-791 as if they were separate agreements, concluding that the requirements for risk transfer are met for each. Reserve credit was then taken on each component; a proportional credit for the quota share on the coinsured policies, and a YRT credit for the YRT component. Note that YRT contracts ordinarily cover a percentage of the one-year mortality risk for the net amount at risk on a policy. A simple way to describe net amount at risk is the difference between the policy reserve held and the face value of the policy.

<u>*ACLI Comments*</u>
ACLI members continue to believe that the two proposals (Ref #2024-05 and Ref #2024-06) are inextricably linked and should be considered together.

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Ref #2024-06: Risk Transfer Analysis for Combination Reinsurance Contracts

ACLI would like to thank SAPWG for the ongoing discussions regarding SAPWG 2024-06. During our discussions, we showed that combination Co-YRT agreements can be structured in ways that satisfy statutory risk transfer requirements as well as in ways that fail to satisfy statutory risk transfer requirements. We showed that when the YRT premiums were set at or below valuation level mortality, risk transfer was achieved (as ceding insurer surplus was protected against deprivation), but when YRT premiums were in excess of these amounts that risk transfer was not achieved (as ceding insurer surplus was not protected and could become negative). We concluded that taking a full proportional reserve credit for coinsured business and a ½ c_x credit for business ceded on a YRT basis (under a combination Co-YRT agreement) would be appropriate when agreements meet statutory risk transfer requirements such as having YRT premiums set at or below valuation mortality. To clarify SAPWG 2024-06 in order for it to recognize this result, we propose the following refinements to the exposure.

Proposed Risk Transfer Framework

ACLI proposes the following framework for assessing combination Co-YRT agreements for statutory risk transfer purposes:

- Any risk transfer assessment of combination Co-YRT agreements should be conducted in the context of applicable SAP guidance and based on the facts and circumstances of the relevant reinsurance agreement(s).
- SAP coinsurance guidance should be applied to the coinsurance component of the agreement(s) and SAP YRT guidance should be applied to the YRT component of the agreement(s).
- Additionally, an overall assessment of the combined agreement should be performed consistent with the requirement that "the agreement shall constitute the entire agreement between the parties with respect to the business being reinsured thereunder[.]"[1] to ensure that ceding insurer surplus is not deprived.

ACLI agrees that if any individual component of a combination Co-YRT agreement does not pass statutory risk transfer, then the aggregate transaction would not pass statutory risk transfer regardless of how it is structured. An overall assessment should include, among other things, an evaluation of:

i) the coinsurance agreement(s) to ensure that all significant risks inherent in the reinsured business are transferred, and

ii) the YRT agreement(s) to ensure that the conditions described in Appendix A-791, paragraphs 2.b., 2.c., 2.d., 2.h., 2.i., 2.j. or 2.k. are not violated, and

iii) the entire agreement to confirm that, when assessed in aggregate, it does not deprive a ceding insurer of surplus or require payments other than from the statutory net gain before adjustments (i.e., as defined in the 2023 SAP life blank line 29, hereinafter "net gain") realized from the reinsured policies.

ACLI agrees that agreements that inappropriately preclude any possibility of reinsurance losses being incurred because of excessive YRT premiums would be of concern from a statutory risk transfer perspective. In evaluating whether this is the case, YRT premium levels should be assessed using statutory principles as any resulting reserve credit will also have been established using statutory principles. In applying statutory principles, statutory valuation assumptions serve as an acceptable benchmark when assessing whether YRT premiums are excessive. More specifically:

- YRT reinsurance results in the assumption of mortality risk for the lifetime of the underlying business. In

[1] A-791 Page 6

such a context, the statutory valuation framework already defines a reasonably prudent valuation mortality basis for ceding insurers when reserving for such risks. As such, this same valuation mortality basis should also serve as a reasonable and prudent benchmark for reinsurers to consider when committing to the assumption of mortality risk for the lifetime of the underlying business.

- The determination of reserve credit relates to the underlying statutory reserves that are held by the ceding insurer and determined based on statutory principles and assumptions. It would be inconsistent to determine a reserve credit using GAAP principles and assumptions in relation to underlying reserves that are computed using statutory principles and assumptions.

Proposed Changes to SSAP No. 61 and Appendix A-791

In response to SAPWG's request for specific recommendations, ACLI proposes the following changes to SSAP No. 61 and the introduction of a new question to be added to Appendix A-791 in lieu of the exposed changes proposed in SAPWG 2024-06.

ACLI proposes the following paragraph be adopted in SSAP No. 61. This proposal aims to maintain SAPWG's objective of evaluating agreements in aggregate and ensuring the appropriate application of current risk transfer principles.

> 18. *For purposes of evaluating whether a reinsurance agreement satisfies statutory risk transfer requirements, the determination of what constitutes an agreement is essentially a question of substance. Multiple agreements should be evaluated together for risk transfer purposes when they are entered into together to achieve one overall commercial effect and where considerations to be exchanged under one agreement depend on the performance of the other agreement(s). For individual agreements that contemplate reinsurance on both a YRT and coinsurance basis, each of the YRT and coinsurance reinsurance components need to satisfy risk transfer requirements on their respective bases. In addition, when evaluated in its entirety, such agreements cannot deprive the ceding insurer of surplus nor require payments to the reinsurer for amounts other than the net gain realized from the reinsured policies.*

ACLI proposes a second question be added to Appendix A-791 2b:

Question

> *If business is reinsured under a combination reinsurance agreement where the reinsurer assumes certain risks on a coinsurance, modified coinsurance, and/or coinsurance funds withheld basis and other risks on a YRT basis, what conditions are required to ensure that the ceding insurer is neither deprived of surplus nor required to make payments to the reinsurer from other than the net gain realized from the reinsured policies such that risk transfer is achieved? How are these conditions impacted by the agreement having an experience refund formula?*
>
> a. *The reinsurance agreement cannot deprive the ceding insurer of surplus or assets. If treaty provisions limit payment of amounts to the reinsurer to the amount of net gain realized from the reinsured business, then the ceding insurer surplus is not deprived, and risk transfer is achieved.*
>
> *For example, risk transfer requirements are satisfied when YRT premiums are contractually stipulated to be equal to or less than the level of valuation mortality used by the ceding insurer in calculating reserves for the reinsured business at the time of inception of the reinsurance agreement and are contractually constrained not to exceed this level.*
>
> b. *The fact that there is an experience refund does not, in itself, cause an agreement to fail risk transfer. However, an experience refund that requires that the ceding insurer reimburse the reinsurer for negative*

> *experience using amounts it has in surplus is a violation of risk transfer requirements, except that neither offsetting experience refunds against current and prior years' losses under the agreement nor payment by the ceding insurer of an amount equal to the current and prior years' losses under the agreement upon voluntary termination of in-force reinsurance by the ceding insurer shall be considered such a reimbursement to the reinsurer for negative experience.*

Summary

Ultimately, our primary concern remains that some may interpret the proposed 2024-06 exposure to indicate that all combination Co-YRT agreements are non-proportional and therefore should not provide reserve credit. Such an interpretation would affect in-force combination Co-YRT agreements and create the potential for material volatility in surplus levels for ceding insurers who have previously entered into such agreements. In addition, such an interpretation would effectively eliminate the ability to use such agreements going forward. Based on our discussions with SAPWG, it is our understanding that neither of these outcomes are intended.

Another concern is that some may interpret the proposed 2024-05 exposure to require an assessment of YRT premiums using a standard other than the existing standard provided in SSAP No. 61 that precludes ceding insurer surplus deprivation. In such a case, there could be significant variation in regulatory interpretations as to what constitutes an "excessive" YRT premium leading to inconsistency rather than harmonization.

ACLI believes that one way to maintain the ability to use compliant combination agreements and not bring into question the reserve credits currently being taken by ceding insurers who are party to such agreements is by adopting proposed changes to SSAP No. 61 and Appendix A-791 consistent with those proposed by ACLI above. Such changes aim to make clear that compliant agreements cannot charge "excessive" YRT premiums and provide a clear basis for how an assessment of YRT premiums anchored to existing SAP guidance is to be performed.

Along with the suggested changes above, we propose forming a small working group consisting of regulators and industry experts to finalize language consistent with the objectives noted above within a defined timeline.

Jeffrey G. Stevenson FSA (Sevenson Associates, Inc) Comments

I am a retired actuary with years of experience in reinsurance, primarily with respect to transactions where the primary motivations are not primarily risk transfer. Not long ago I was asked about a treaty arrangement involving combinations of coinsurance and YRT and was told there was some controversy with respect to the accounting.

Combination coinsurance and YRT agreements have been around forever; there shouldn't be much controversy.

Traditionally, the YRT combined in coinsurance agreements is YRT reinsurance inuring to the benefit of the reinsured block.

In this respect, the cash flows of the coinsurance (or Modco) treaty (principally of those intended for purposes other than risk transfer) have traditionally been:

+Premiums
-Claims
-Surrender & Maturity Benefits
-Commissions and Expense Allowances

-Ceded Reins Prems (on Inuring agreements)
+Ceded Reins Dbs (on Inuring agreements)
+Ceded reins Exp Refunds (on Inuring agreements)

-Modco Res Incr (if Modco)

+Modco Interest (if Modco)

- Experience Refunds (if included)

The above result may result in an expense and risk charge with favorable experience.

The inuring agreements in the above could be YRT of mortality risk or other coinsurance of reinsured business of the benefits or even catastrophic stop loss arrangements. The inuring agreements could be traditional YRT with an experience refund arrangement. They could also be YRT agreements of a more financially motivated arrangement, i.e., a high YRT premium based on a high percentage of the valuation mortality basis, combined with a large experience refund.

There is no reason the YRT couldn't be additional quota share of the same block as the coinsurance. Why would ceding companies do this? Well in past circumstances, perhaps they were reinsuring the business with two reinsurers and one reinsurer does not want to retain catastrophic mortality risk but the second reinsurer is willing to take that additional risk in addition to the risks in its own portion of the reinsurer. Including such reinsurance in the single tradition would be done for administrative convenience and if structured as YRT would include additional impacts on reserve and capital requirements. This type of arrangement would not be uncommon for divestiture of the business (might be referred to as administrative reinsurance). My first impression of the combo YRT treaties presented to me is that the additional YRT is nothing more than inuring reinsurance regardless of what the reinsured business is, just like these arrangements in the past.

My understanding of the new variations of combo treaties is that the YRT is indeed an additional quota share of the coinsured business but the interpretation is that the YRT is not inuring to the benefit of the coinsured business. In fact, in the new interpretations the YRT is treated as a separate agreement with its own cash flows. Moreover, the YRT mortality risk treaty might be on the basis of a high percentage of the valuation table thereby generating a generous experience refund under expected assumptions.

The interpretation being made that the extra YRT arrangement is more like a standalone rider produces a result that in the event of adverse investment scenarios, the high experience refund (on the YRT mortality component) can be combined with adverse experience on the coinsured business to merely produce a lower experience refund with the reinsurer not necessarily reimbursing the ceding company for the adverse experience of the coinsured business.

That might look okay with the arithmetic but in my opinion, it is a clear violation of the life reinsurance model regulation. The reserve or capital credits associated with any treaty with such an arrangement (and with the YRT component not accounted for as inuring reinsurance) should be denied.

Here is the explanation.

Accounting requirements of the model regulation are:

1. Renewal expense allowances provided or to be provided to the ceding insurer by the reinsurer in any accounting period, a must be sufficient to cover anticipated allocable renewal expenses of the ceding insurer on the portion of the business reinsured
2. The ceding insurer can't be deprived of surplus or assets at the reinsurer's option or automatically upon the occurrence of some event
3. The ceding insurer is required to reimburse the reinsurer for negative experience under the reinsurance agreement
4. The reinsurance agreement can't involve the possible payment by the ceding insurer to the reinsurer of amounts other than from income realized from the reinsured policies.

The new interpretation of the added YRT component (an additional quota share of the underlying coinsured business) violates some of all of these accounting requirements.

First off, as for the YRT exemption from the requirements of the model regulation, the combo treaty "interpretation" does not allow for any YRT exemption because the surplus and capital aid of the combination exceeds that of a zero premium YRT treaty. The model regulation accounting requirements should apply to all the components of the treaty.

Let's assume the coinsured portion of the business produces negative cash flows as a result of poor investment experience and the additional YRT business produces an experience refund that more than offsets the negative experience.

Note that all reinsurance has a cost. The YRT portion of the business has a cost associated with it. The cost is Premiums minus Claims minus Experience Refund. (This typically nets to a cost equal to a risk fee or the profit margin of the reinsurer which may or not be a mere risk fee). But in this case the adverse experience of the coinsured business reduces the YRT portion's experience refund, that YRT reinsurance now has an additional cost in addition to the profit margin.

That cost is now a cost of the ceding company. Reinsurance costs of the ceding company have to be reimbursed by the reinsurer through the expense allowance. In this case then, the reinsurer has to reimburse its own charge, thereby resulting in a wash, so there is, in fact, no recovery of the adverse experience refund.

You can also think of the experience refund as an "optional experience refund." In this case a portion of the YRT experience refund is denied at the option of the reinsurer (it's automatically denied with the occurrence of the adverse experience on the coinsurance). So the use of the YRT as an offset to adverse experience is automatically denying the ceding company of surplus automatically on the occurrence of some event.

The recovery of the adverse experience on the coinsurance is also technically a payment that is not made out of the profits on that coinsured business. It is coming out of an additional premium payment to the reinsurer (the YRT premium).

I recognize that some might make nuanced arguments against these above arguments. However, and most importantly, let's look at the essential substance of the YRT portion of the transaction. The companion YRT arrangement typically has a YRT premium which is a high percentage of valuation mortality (let's say 90%) and any premiums in excess of the claims are experience refunded net of a risk charge. The substance of this transaction is that there is a risk charge paid and claims in excess of 90% of valuation mortality are experience refunded back to the ceding company. (Now this might be structured as YRT because there are other accounting entries such as face amount ceded and reserve credits accompanying the accounting, but the essence of the transaction is essentially a non- proportional stop loss arrangement). The YRT component of the transaction is basically a stop loss arrangement with a risk charge for a premium. In exchange for this risk premium, the reinsurer will pay claims only if they exceed the percentage of the valuation basis mortality relating to the premium. It is an excess of loss structure.

So if we think of the companion YRT agreement in this true economic form, the companion treaty in addition to the coinsurance is nothing more than a risk premium paid to the reinsurer for catastrophic mortality. From this standpoint, the combo treaty arrangement's result in the event of adverse experience on the coinsurance is that the reinsurer is receiving a payment in addition to the risk charge from the ceding company to cover that adverse experience (as is argued above). This is because in order for the transaction to provide for an offset to the losses on the coinsurance, the ceding company would be required to make a payment to the reinsurer in addition to the risk charge! When viewed from this true economic perspective, this is clearly a violation of the model regulation.

To argue that merely changing the companion contract from a stop loss format to an equivalent YRT structure would change the above interpretation (that the contract violates the model regulation) seems just plain wrong.

One can also think of this additional payment as essentially the same as using an artificially high interest rate (like 12%) to calculate coinsurance experience refunds or modco profits. Everyone should recognize that this provision

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would be a violation of the model regulation as it would be an additional payment or a payment outside of profits in the business. Likewise, any additional premium paid, or reduction in experience refund of associated treaty provisions, would similarly be a violation of the model regulation.

In P&C arrangements, there is often reference to this type of arrangement as a "reinstatement premium." This has no place in a life reinsurance transaction.

This concluding argument of looking through to the substance of the transaction validates all the other above arguments that this new interpretation of the combo structure violates the model regulation!

If the additional YRT is, in essence, accounted for as an inuring agreement, just has it has always been done, the appropriate cash flows fall out in the treaty accounting and the reserve credits are justified.

Recommendation:
NAIC staff notes that the exposed revisions are narrowly focused on the issue that interdependent contracts, and/or interdependent contract features, must be analyzed in aggregate and (including all relevant facts and circumstances). As all of the parties who have commented agree that the entirety of the contract must be analyzed, NAIC staff continues to support adoption of the exposed revisions, with timing subject to the discretion of the Working Group. If the Working Group wants to continue discussions on this topic, NAIC staff recommend a joint meeting of the Statutory Accounting Principles (E) Working Group and the Life Actuarial (A) Task Force. This is because actuarial expertise would be beneficial in discussing some of the comments received on the actuarial risk transfer analysis. In addition, the Dec. 2023 referral was from the Valuation Analysis (E) Working Group. The exposed revisions to SSAP No. 61 are below for reference:

> 18. For purposes of evaluating whether a contract with a reinsurer transfers risk, what constitutes a contract is essentially a question of substance. It may be difficult in some circumstances to determine the boundaries of a contract. For instance, the profit-sharing provisions of one contract may refer to experience on other contracts and, therefore, raise the question of whether, in substance, one contract rather than several contracts exist. The inconsistency that could result from varying interpretations of the term contract is limited by requiring that features of the contract or other contracts or agreements that directly or indirectly compensate the reinsurer or related reinsurers for losses be considered in evaluating whether a particular contract transfers risk. Therefore, if agreements with the reinsurer or related reinsurers in the aggregate do not transfer risk, the individual contracts that make up those agreements also would not be considered to transfer risk, regardless of how they are structured.

In addition, the following was exposed as addition to existing SSAP No. 61, paragraph 19 on YRT.

> YRT agreements shall follow the requirements of A-791, paragraph 6, regarding the entire agreement and the effective date of agreements.

NAIC staff does not recommend exposing the ACLI proposed revisions to add a new paragraph 18 to *SSAP No. 61—Life, Deposit-Type and Accident and Health Reinsurance* and to add a second question to Appendix A-791, question 2b for reasons which are further detailed below. In short, the ACLI proposed revisions would codify a bifurcated risk transfer analysis that VAWG has previously noted as problematic. In addition, the proposed ACLI safe harbor of YRT premium that is not greater than the valuation mortality is problematic as detailed below. Also included below are a few key points regarding the comments received from Jeffrey Stevenson (retired actuary commenter). NAIC Staff has limited the key points below for brevity but can provide a more detailed analysis if needed for a joint call.

1. **Areas of agreement –** NAIC staff concurs with the comments that reinsurance agreements need to be evaluated using all of the relevant facts and circumstances and existing guidance. NAIC staff agrees that some combination reinsurance agreements of YRT and Coinsurance with interdependent features will pass risk transfer and some contracts will not.

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- Comments from VAWG and from Stevenson note that not all such combination contracts are concerning, but also noted that some of the more concerning combination contracts have structural variations or assumptions on the cash flows that differ from the historic structure / assumptions of many such contracts.
- Stevenson notes that, "Traditionally, the YRT combined in coinsurance agreements is YRT reinsurance inuring to the benefit of the reinsured block." He provides further comments on variations that are concerning on newer interpretations and newer combination structures in his comments on inuring agreements compared to separate agreement cash flow evaluation.

2. **Bifurcated analysis** - ACLI proposed revisions to SSAP No. 61 and to A-791 QA would formally require a bifurcated risk transfer analysis. This type of bifurcated analysis would look at each type of coverage in the contract separately and evaluate an interdependent contract under two separate criteria for risk transfer (Ex. one set of criteria for YRT and one set for the coinsurance piece). This type of bifurcated analysis was noted as concerning by the VAWG referral because of the interdependent contract features of a shared experience refund and the inability to separately recapture the parts of the contract. Because interdependent contract features require aggregated analysis, NAIC staff does not recommend codifying bifurcated risk transfer analysis.

3. **Use of a Valuation Mortality Measure** - The ACLI recommendation is that risk transfer for the entire combination reinsurance contract is achieved if the YRT premium does not exceed the cedent valuation mortality at the time of contract inception. Conversations with actuaries note that the valuation mortality is not fixed under principles-based reserving. The valuation mortality could be based on the net premium reserve, or the modelled reserve. In addition, the reinsurer's valuation mortality can be different than the ceding entity's valuation mortality because the valuation mortality can change over time. Using the valuation mortality at inception does not guarantee that there will not be a future deprivation of surplus to the ceding entity. Therefore, this risk transfer measurement method will not work as a proposed safe harbor. In addition, the Stevenson comments also noted that YRT reinsurance that was a higher percentage of the valuation mortality as being more financially motivated.

4. **YRT requirements** - Note that all the Appendix A-791 requirements apply to coinsurance and only a subset of the A-791 requirements apply to certain types of YRT agreements. SSAP No. 61, paragraph 19 excerpted below specifies the paragraphs of A-791 which apply. Part of the reason noted in the A-791 QA (excerpted below) for excluding YRT from being required to follow all of A-791, is that YRT reinsurance typically only resulted in limited reserve credit. This is typically a portion of the current year mortality benefit (commonly referred to as ½ cx). However, if the YRT treaty credit is higher as specified in A-791 excerpt below, **that type of higher credit YRT treaty is not intended to be excluded from any of the A-791 requirements.**

   One of the VAWG concerns that was echoed by comments from Stevenson, is that the concerning type of combination contracts are resulting in a larger type of reinsurance credit that was not intended to be excluded from A-791 requirements. **Stevenson noted that some of the concerning contracts are resulting in a reinsurance credit that is greater than that of a zero premium YRT treaty (see A-791 QA excerpt below), which indicates that the YRT treaty of this type was not intended to be excluded from A-791.**

From A-791 QA paragraph 1. (Bolding added)

Q – Aside from assumption reinsurance, what other types of reinsurance are exempt from the accounting requirements?

A – Yearly renewable term (YRT) and certain nonproportional reinsurance arrangements, such as stop loss and catastrophe reinsurance are exempt because these do not normally provide significant surplus relief and therefore are outside the scope of this Appendix. If a catastrophe

arrangement takes a reserve credit for actual losses beyond the attachment point or the unearned premium reserve (UPR) of the current year's premium, there will most likely be no regulatory concern.

Similarly, if a YRT treaty provides incidental reserve credits for the ceding insurer's net amount at risk for the year with no other allowance to enhance surplus, there will most likely be no regulatory concern. **For purposes of this exemption, a treaty labeled as YRT does not meet the intended definition of YRT if the surplus relief in the first year is greater than that provided by a YRT treaty with zero first year reinsurance premium and no additional allowance from the reinsurer.**

Additional pertinent information applicable to all YRT treaties and to non-proportional reinsurance arrangements is contained in paragraphs 19 and 20 of SSAP No. 61R.

From SSAP No. 61, paragraph 19:

19. Yearly renewable term (YRT) reinsurance agreements that transfer a proportionate share of mortality or morbidity risk inherent in the business being reinsured and do not contain any of the conditions described in Appendix A-791, paragraphs 2**.b., 2.c., 2.d., 2.h., 2.i., 2.j. or 2.k.,** shall follow the guidance for reinsurance accounting, including paragraphs 55-57 of this statement that apply to indemnity reinsurance. Contracts that fail to meet the requirements for reinsurance accounting shall follow the guidance for Deposit Accounting. For all treaties entered into on or after January 1, 2003, the deferral guidance in paragraph 3 of A-791 shall also apply to YRT agreements. Since YRT agreements only transfer the mortality or morbidity risks to the reinsurer, the recognition of income shall be reflected on a net of tax basis, as gains emerge based on the mortality or morbidity experience.

5. **Prohibited Elements in Part of a Combination Contract**– Steveson is noting that the YRT combination contract is resulting in the surplus and capital aid that exceeds that of a zero premium YRT treaty which is not intended to be excluded from A-791 (from the discussion and quotes above). Therefore the A-791 accounting requirements should apply to all the components of the treaty. **Stevenson commented that having contract terms in an interdependent contract which are prohibited in a coinsurance agreement on a standalone basis under A-791 would not be compliant with the model law. This is similar to some of the comments and concerns noted by VAWG.**

6. **Stevenson also makes comments about the overall result of the reinsurance contract coverage from the combination of the coverages which echoed other parts of the concerns of VAWG.**

Comments are in Attachment 2.3

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Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: A-791 Paragraph 2.c.

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☐	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue:
The Valuation Analysis (E) Working Group sent a referral to the Statutory Accounting Principles (E) Working Group which recommends making a clarifying edit to A-791, Life and Health Reinsurance Agreements, Section 2.c's, Question and Answer by removing the first sentence, which reads, "Unlike individual life insurance where reserves held by the ceding insurer reflect a statutorily prescribed valuation premium above which reinsurance premium rates would be considered unreasonable, group term life has no such guide." **(See Existing Authoritative Literature)** The referral notes that:

> First, this sentence is unnecessary, as it is an aside in a discussion about group term life. More importantly, this statement is being misinterpreted as supporting the use of Commissioner's Standard Ordinary (CSO) rates as a "safe harbor," at or below which YRT rates would be automatically considered not to be excessive.
>
> The 791 section 2c QA guidance does not provide a safe harbor based on CSO. It indicates that if the YRT reinsurance premium is higher than the proportionate underlying direct premium for the risk reinsured, then the reinsurance premium is excessive. VAWG observes that the prudent mortality under the *Valuation Manual*, Section 20: Requirements for Principle-Based Reserves for Life Products (VM-20), may appropriately be either higher or lower than the CSO rate depending on the facts and circumstances.

Existing Authoritative Literature:

A-791, Life and Health Reinsurance Agreements, paragraph 2c:

> 2. No insurer shall, for reinsurance ceded, reduce any liability or establish any asset in any statutory financial statement if, by the terms of the reinsurance agreement, in substance or effect, any of the following conditions exist:
>
> c. The ceding insurer is required to reimburse the reinsurer for negative experience under the reinsurance agreement, except that neither offsetting experience refunds against current and prior years' losses under the agreement nor payment by the ceding insurer of an amount equal to the current and prior years' losses under the agreement upon voluntary termination of in force reinsurance by the ceding insurer shall be considered such a reimbursement to the reinsurer for negative experience. Voluntary termination does not include situations where termination occurs because of unreasonable provisions which allow the reinsurer to reduce its risk under the agreement. An example of such a provision is the right of the reinsurer to increase reinsurance premiums or risk and expense charges to excessive levels forcing the ceding company to prematurely terminate the reinsurance treaty;

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A-791, Life and Health Reinsurance Agreements, paragraph 2c's, Question and Answer (Underlining added for Emphasis):

> **Q – If group term life business is reinsured under a YRT reinsurance agreement (which includes risk-limiting features such as with an experience refund provision which offsets refunds against current and/or prior years' losses (i.e., a "loss carryforward" provision), under what circumstances would any provisions of the reinsurance agreement be considered "unreasonable provisions which allow the reinsurer to reduce its risk under the agreement" thereby violating subsection 2.c.?**
>
> **A** – Unlike individual life insurance where reserves held by the ceding insurer reflect a statutorily prescribed valuation premium above which reinsurance premium rates would be considered unreasonable, group term life has no such guide. So long as the reinsurer cannot charge premiums in excess of the premium received by the ceding insurer under the provisions of the YRT reinsurance agreement, such provisions would not be considered unreasonable. Any provision in the YRT reinsurance agreement which allows the reinsurer to charge reinsurance premiums in excess of the proportionate premium received by the ceding insurer would be considered unreasonable. The revisions to this QA regarding group term life yearly renewable term agreements is effective for contracts in effect as of January 1, 2021.

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups): On January 10, 2024, the Statutory Accounting Principles (E) Working Group received the referral from the Valuation Analysis (E) Working Group and directed NAIC staff to prepare an agenda item for future Working Group discussion.

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group: None

Convergence with International Financial Reporting Standards (IFRS): Not applicable.

Staff Recommendation:

NAIC staff recommends that the Working Group move this item to the active listing of the maintenance agenda, categorized as a SAP clarification, and expose revisions to remove the first sentence of the A-791, paragraph 2c's Question and Answer as illustrated below. In addition, the Working Group should notify the Valuation Analysis (E) Working Group, the Life Actuarial (A) Task Force and the Reinsurance (E) Task Force of the exposure.

As noted by the referral, the sentence is not necessary as it is more of an introductory aside. If it is causing confusion and misapplication, as noted by the VAWG, it is better to remove the sentence.

Proposed revision to A-791, Life and Health Reinsurance Agreements, paragraph 2c:

2. No insurer shall, for reinsurance ceded, reduce any liability or establish any asset in any statutory financial statement if, by the terms of the reinsurance agreement, in substance or effect, any of the following conditions exist:

   c. The ceding insurer is required to reimburse the reinsurer for negative experience under the reinsurance agreement, except that neither offsetting experience refunds against current and prior years' losses under the agreement nor payment by the ceding insurer of an amount equal to the current and prior years' losses under the agreement upon voluntary termination of in force reinsurance by the ceding insurer shall be considered such a reimbursement to the reinsurer for negative experience. Voluntary termination does not include situations where termination occurs because of unreasonable provisions which allow the reinsurer to reduce its risk under the agreement. An example of such a provision is the right of the reinsurer to increase reinsurance premiums or risk and expense charges to excessive levels forcing the ceding company to prematurely terminate the reinsurance treaty;

A-791, Life and Health Reinsurance Agreements, paragraph 2c's, Question and Answer):

> **Q – If group term life business is reinsured under a YRT reinsurance agreement (which includes risk-limiting features such as with an experience refund provision which offsets refunds against current and/or prior years' losses (i.e., a "loss carryforward" provision), under what circumstances would any provisions of the reinsurance agreement be considered "unreasonable provisions which allow the reinsurer to reduce its risk under the agreement" thereby violating subsection 2.c.?**
>
> **A** – ~~Unlike individual life insurance where reserves held by the ceding insurer reflect a statutorily prescribed valuation premium above which reinsurance premium rates would be considered unreasonable, group term life has no such guide.~~ So long as the reinsurer cannot charge premiums in excess of the premium received by the ceding insurer under the provisions of the YRT reinsurance agreement, such provisions would not be considered unreasonable. Any provision in the YRT reinsurance agreement which allows the reinsurer to charge reinsurance premiums in excess of the proportionate premium received by the ceding insurer would be considered unreasonable. The revisions to this QA regarding group term life yearly renewable term agreements ~~is~~ are effective for contracts in effect as of January 1, 2021.

Staff Review Completed by: Robin Marcotte – NAIC Staff, February 2024

Status:
On March 16, 2024, the Statutory Accounting Principles (E) Working Group exposed the above illustrated revisions to remove the first sentence of *Appendix A-791—Life and Health Reinsurance Agreements* (A-791), paragraph 2c's Question and Answer. In addition, the Working Group directed NAIC staff to notify the Valuation Analysis (E) Working Group, the Life Actuarial (A) Task Force and the Reinsurance (E) Task Force of the exposure.

On August 13, 2024, the Statutory Accounting Principles (E) Working Group re-exposed this agenda to allow more time for comments and discussion on this agenda item.

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2024/08-13-24 Summer National Meeting/Exposures/24-05 - A791 par 2c.docx

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Statutory Accounting Principles (E) Working Group
Maintenance Agenda Submission Form
Form A

Issue: Risk Transfer Analysis on Combination Reinsurance Contracts

Check (applicable entity):

	P/C	Life	Health
Modification of Existing SSAP	☐	☒	☒
New Issue or SSAP	☐	☐	☐
Interpretation	☐	☐	☐

Description of Issue:
This agenda item is to address a December 2023, referral by the Valuation Analysis (E) Working Group (VAWG) regarding reinsurance risk transfer and reserve credit for a particular form of reinsurance being observed by regulators in the life industry. The referral noted that:

> VAWG has identified that issues arise when evaluating reinsurance for risk transfer in accordance with *SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance*, when treaties involve more than one type of reinsurance, and there is interdependence of the types of reinsurance, including but not limited to an experience refund that is based on the aggregate experience. In such cases, VAWG regulators find that these types of reinsurance must be evaluated together and cannot be evaluated separately for the purpose of risk transfer. For example, where a treaty includes coinsurance and YRT with an aggregate experience refund and the inability to independently recapture the separate types of reinsurance, it is not adequate to separately review the coinsurance and YRT pieces of the transaction for risk transfer. The treaty as a whole is non- proportional. This complexity is not immediately apparent to the regulatory reviewer, and it is important that this issue be raised broadly, so that individual state regulators are aware. Individual regulators are encouraged to contact VAWG if they would like additional perspective when reviewing such treaties.
>
> Generally, VAWG regulators observe that some companies are reporting an overstated reserve credit due to a bifurcated risk transfer analysis. Specifically, some companies reported a proportional reserve credit for a coinsurance component, despite in aggregate the reinsurer only being exposed to loss in tail scenarios. From an actuarial perspective, there is consensus among VAWG members that it is not appropriate for a ceding company to take a proportional reserve credit that reflects the transfer of all actuarial risks when not all actuarial risks are transferred.
>
> VAWG recommends that SAPWG discuss this issue, to 1) increase familiarity with the issue and 2) consider whether any clarifications to risk transfer requirements is appropriate

SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance contains guidance for life and health reinsurance agreements. Additionally, SSAP No. 61R refers to Appendix *A-791, Life and Health Reinsurance Agreements* for risk transfer criteria applicable to all forms of life and health reinsurance other than Yearly Renewable Term (YRT) agreements and certain non-proportional contracts such as stop loss and catastrophe reinsurance. YRT agreements are required to comply with specific parts of A-791. Furthermore, contracts that do not meet the conditions for reinsurance accounting in SSAP No. 61R, including the applicable parts of A-791, receive deposit accounting.

As noted in the referral above, regulators have observed reinsurance transactions that combine both coinsurance and YRT, typically applicable to different underlying policies, but that are interdependent. There exists an aggregate experience refund and recapture provisions that allow for recapture by the cedant, but only if both components are recaptured simultaneously.

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VAWG observed that some insurers have assessed these components under A-791 as if they were separate agreements, concluding that the requirements for risk transfer are met for each. Reserve credit was then taken on each component; a proportional credit for the quota share on the coinsured policies, and a YRT credit for the YRT component. Note that YRT contracts ordinarily cover a percentage of the one-year mortality risk for the net amount at risk on a policy. A simple way to describe net amount at risk is the difference between the policy reserve held and the face value of the policy.

The concern raised by regulators is that the substance of this interdependent agreement design is more akin to the risk transferred under a nonproportional reinsurance agreement. This is because in aggregate, proportionate amounts of the risk are not transferred. The agreements are designed to compensate the cedant for aggregate experience only in tail scenarios, which is accomplished through the design of the aggregate experience refund. In most reasonably expected scenarios, the net effect of the reinsurance is such that the cedant pays a financing charge to the reinsurer for a designated period of time until an expected recapture date and no additional net funds exchange hands. As a result, taking a full proportional reserve credit on the coinsured component is not reflective of the actual risk being transferred. SSAP No. 61R, paragraph 36 notes that the reinsurance credit is only for the risk reinsured. As noted in the referral, there was consensus among VAWG members that it is not appropriate for a ceding company to take a proportional reserve credit that reflects the transfer of all actuarial risks when not all actuarial risks are transferred. NAIC staff agrees with the VAWG consensus and proposes to incorporate a version of existing guidance from SSAP No. 62R that addresses this point. The inclusion of this guidance is intended to require risk transfer to be analyzed for the entire contract when multiple interdependent types of reinsurance are present.

SSAP No. 62R—Property and Casualty Reinsurance Exhibit A – Implementation Questions and Answers, question 10 provides guidance on interdependent contract features. This agenda item proposes to incorporate key aspects of the SSAP No. 62R, Exhibit A question 10 into SSAP No. 61R to provide more clarity on evaluation of risk transfer on contracts with interdependent features. The answer requires that features of the contracts(s) that directly or indirectly compensate the reinsurer or related reinsurers for losses be considered in determining if a particular contract transfers risk. The *SSAP No. 62R—Property and Casualty Reinsurance Exhibit A – Implementation Questions and Answers* question 10 provides the following:

> 10A: A contract is not defined, but is essentially a question of substance. It may be difficult in some circumstances to determine the boundaries of a contract. **For example, the profit-sharing provisions of one contract may refer to experience on other contracts and, therefore, raise the question of whether, in substance, one contract rather than several contracts exist.**
>
> The inconsistency that could result from varying interpretations of the term *contract* is limited by requiring that features of the contract or other contracts or agreements that directly or indirectly compensate the reinsurer or related reinsurers for losses be considered in evaluating whether a particular contract transfers risk. Therefore, if agreements with the reinsurer or related reinsurers, in the aggregate, do not transfer risk, the individual contracts that make up those agreements also would not be considered to transfer risk, regardless of how they are structured.

As historical background, the guidance for SSAP No. 62R, Exhibit A, question 10, originated from *GAAP EITF Topic D-34, Accounting for Reinsurance: Questions and Answers about FASB Statement No. 113* (EITF D-34) NAIC staff recommends that the Working Group move this item to the active listing of the maintenance agenda, categorized as a SAP clarification, and expose revisions to *SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance* as illustrated below. The proposed revisions incorporate guidance to SSAP No. 61R which is consistent with the guidance currently in SSAP No. 62R, Exhibit A Implementation Questions and Answers, question 10 and also add reference to A-791, paragraph 6 guidance in the YRT guidance paragraph. (See Authoritative Literature). FASB Statement No. 113 was adopted with modification in both SSAP No. 62R and SSAP No. 61R. Topic 944 Reinsurance Contracts in the current FASB Codification Implementation Guide continues to include the guidance from EITF D-34

The example reinsurance contract that VAWG observed contained yearly renewable term reinsurance. Per SSAP No. 61R, paragraph 19, only certain parts of *A-791 Life and Health Reinsurance Agreements* apply to YRT contracts. Specifically, YRT contracts only have to pass A-791, paragraphs 2.b., 2.c., 2.d., 2.h., 2.i., 2.j. or 2.k. to result in reinsurance accounting. In addition, paragraph 3 of A-791 on deferral of gain on cession of prior year blocks of business also applies. As described above, YRT contracts do not transfer all of the risk inherent in the contract as they typically only cover a percentage of the net amount at risk for typically one year. Note that the reinsurance accounting credit from a YRT contract per the guidance in SSAP No. 61R, paragraph 37 is computed as the one-year term mean reserve on the amount of insurance ceded. Therefore, a YRT credit is typically less than what a proportional coinsurance contract which transfers all significant risks would typically provide.

The VAWG reinsurance contract example also included coinsurance contracts which must pass all of A-791 to receive reinsurance accounting. The example contract contained a shared experience refund between the two contract types. This interdependent feature is a key element. NAIC staff agrees with VAWG that an interdependent reinsurance payment in a contract requires a single risk transfer assessment. However, the combined interdependent contract when assessed in aggregate would likely cause it to either not meet the conditions for reinsurance accounting or would result in a smaller reinsurance credit than VAWG observed some entities taking.

A-791, paragraph 2e contains the guidance which limits the amounts paid to the reinsurer to the income realized on the underlying reinsured policy and paragraph 2f contains the guidance on transferring all the significant risk of the business reinsured. Adding YRT coverage with coinsurance would likely result in a “fail” of the criteria in A-791 because not all of the significant risks of the underlying reinsured policies would be likely to be passed to the reinsurer (thus failing the criteria in A-791, paragraph 2f). Combining YRT and coinsurance in the same contract could also cause that contract to fail A-791 if the reinsurance contract charged more than the income on the underlying policy.

In addition, A-791, paragraph 6 requires that the reinsurance contract include provisions that the agreement shall constitute the entire agreement between the parties with respect to the business being reinsured thereunder and that there are no understandings between the parties other than as expressed in the agreement. This paragraph does not currently apply to YRT but is being recommended to apply.

Existing Authoritative Literature:

- ***SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance***

Types of Reinsurance Arrangements

11. Once an entity has decided to reinsure amounts in excess of its desired retention, it may proceed in one of several basic arrangements—coinsurance, modified coinsurance, yearly renewable term or non-proportional. Such contracts may have funds withheld.

Coinsurance

12. In this arrangement, the risks are reinsured on the same plan as that of the original policy. The direct writer and the reinsurer share in the risk in the same manner. The ceding entity pays the reinsurer a proportional part of the premiums collected from the insured. In return, the reinsurer reimburses the ceding entity for the proportional part of the death or accident and health claim payments and other benefits provided by the policy, including nonforfeiture values, policy dividends, experience rating refunds, commissions, premium taxes, and other direct expenses agreed to in the contract. The reinsurer must also establish the required reserves for the portion of the policy it has assumed. A single policy can be coinsured with more than one entity or under more than one reinsurance contract with the same entity as long as the combined total of reinsurance and the retention of the ceding entity is not more than 100% of the risk.

13. In coinsurance of participating policies, the reinsurer may reimburse the ceding entity for its portion of the dividends paid to the policyholder. In determining its schedule of dividends, the ceding entity takes into account the experience on the business as written. If the reinsurer reimburses dividends it will typically accept the ceding entity’s schedule but may require input into the schedule. Changes to the schedule may

have to be agreed to by the reinsurer. Coinsurance of all or a portion of a block of business also is used in situations where a severe strain is placed on the direct writing entity's surplus in the first policy year. For example, the premium received by the direct writer during the first policy year usually is insufficient to pay the high first-year commissions and other costs of issue and to establish the initial reserve. In such an example, coinsurance relieves some of the surplus strain of adding large amounts of new insurance.

Modified Coinsurance

14. The "modified coinsurance" or "modco" arrangement is a variation of coinsurance. The ceding entity has transferred all or a portion of the net policy liabilities on the reinsured policies to the reinsurer, and the reinsurer is required to indemnify the ceding entity for the same amount. The assets necessary to support the reserves for the original policies are maintained by the ceding entity instead of the reinsurer. This is accomplished by designating in the contract the transfer of the net policy liabilities to the assuming entity and an immediate transfer back to the extent of the modco deposit. Under modified coinsurance, the assuming entity shall transfer to the ceding entity the increase in the reserve on the reinsured portion. This transaction reflects the reinsurer's risk with respect to the reinsured business and its obligation to maintain the reserves supporting such obligation. In some cases, a policy may be reinsured partially on a coinsurance arrangement and partially on a modified coinsurance arrangement. This may be accomplished through the use of two contracts or in a single contract.

Yearly Renewable Term (YRT)

15. Under this arrangement of reinsurance, the ceding entity transfers the net amount at risk on the portion reinsured to the reinsurer and pays a one-year term premium. The "net amount at risk"—as defined in the contract—is usually the amount of insurance provided by the policy in excess of the ceding entity's reserve on it.

Non-Proportional

16. Other forms of reinsurance are also available, such as catastrophe and stop loss coverage. These arrangements provide for financial protection to the ceding entity for aggregate losses rather than providing indemnification for an individual policy basis as described in the preceding three reinsurance arrangements. Catastrophic and stop loss reinsurance are written on an annual basis to protect the ceding entity from excessive aggregate losses. Usually, the coverage does not extend over the life of the underlying policy nor is there any requirement on the ceding entity to renew the arrangement.

Transfer of Risk

17. **Reinsurance agreements must transfer risk from the ceding entity to the reinsurer in order to receive the reinsurance accounting treatment discussed in this statement.** If the terms of the agreement violate the risk transfer criteria contained herein, **(i.e., limits or diminishes the transfer of risk by the ceding entity to the reinsurer), the agreement shall follow the guidance for Deposit Accounting. In addition, any contractual feature that delays timely reimbursement violates the conditions of reinsurance accounting.**

18. This paragraph applies to all life, deposit-type and accident and health reinsurance agreements except for yearly renewable term reinsurance agreements and non-proportional reinsurance agreements such as stop loss and catastrophe reinsurance. All reinsurance agreements covering products that transfer significant risk shall follow the guidance for reinsurance accounting contained in this statement. All reinsurance contracts covering products that do not provide for sufficient transfer of risk shall follow the guidance for Deposit Accounting.

19. **Yearly renewable term (**YRT) reinsurance agreements that transfer a proportionate share of mortality or morbidity risk inherent in the business being reinsured and do not contain any of the conditions described in **Appendix A-791, paragraphs 2.b., 2.c., 2.d., 2.h., 2.i., 2.j. or 2.k.,** shall follow the guidance for reinsurance accounting, including paragraphs 55-57 of this statement that apply to indemnity reinsurance. Contracts that fail to meet the requirements for reinsurance accounting shall follow the guidance for Deposit Accounting. For all treaties entered into on or after January 1, 2003, the deferral guidance in paragraph 3 of A-791 shall also apply to YRT agreements. Since YRT agreements only transfer

the mortality or morbidity risks to the reinsurer, the recognition of income shall be reflected on a net of tax basis, as gains emerge based on the mortality or morbidity experience.

20. For non-proportional reinsurance agreements such as stop loss and catastrophe reinsurance agreements, contract terms shall be evaluated to assess whether they transfer significant risk to the reinsurer. For example, prepayment schedules and accumulating retentions from multiple years are contractual features inherently designed to delay the timing of reimbursement to the ceding entity limits the risk to the reinsurer. Regardless of what a particular feature might be called, any feature that can delay timely reimbursement violates the conditions for reinsurance accounting. Transfer of insurance risk requires that the reinsurer's payment to the ceding entity depend on and directly vary with the amount and timing of claims settled under the reinsured contracts. Contractual features that can delay timely reimbursement prevent this condition from being met. Reinsurance accounting shall apply to all non-proportional agreements that transfer significant risk and do not contain any provisions that protect the reinsurer from incurring a loss. Contracts that fail to meet the requirements for reinsurance accounting shall follow the guidance for Deposit

Credits for Ceded Reinsurance

36. The credit taken by the ceding entity under the coinsurance arrangement is calculated using the same methodology and assumptions used in determining its policy and claim reserves. It is, of course, only for the percentage of the risk that was reinsured. Under modified coinsurance, the reserve credit is reduced by the modco deposit retained by the ceding entity. If the entity reinsures on a yearly renewable term basis, it is itself buying insurance for the portion of the ceded amount at risk. The amount of yearly renewable term reinsurance that is required on a given policy generally decreases each year as the entity's reserve increases. The net amount at risk may increase, however, on interest sensitive products such as universal life. The amount at risk on accident and health yearly renewal term reinsurance will remain level and the reinsurance premium will increase each year.

37. The reserve credit taken by the ceding entity is reported as a reduction to the reserves and not as an asset of the entity. **The ceding entity's reserve credit and assuming entity's reserve for yearly renewable term reinsurance shall be computed as the one year term mean reserve on the amount of insurance ceded. The ceding entity must use the same mortality and interest bases which were used for valuing the original policy before reinsurance.** The credit may also be computed on a pro rata basis if the result is not materially different from the credit computed on the mean reserve basis. For all types of reinsurance, the ceding entity also takes credit for other amounts due from the reinsurer such as unpaid claims and claims incurred but not reported. If contemplated by the reinsurance contract, recognition of related assets and liabilities must occur (policy loans, due and deferred premiums, etc.).

38. Non-proportional reinsurance is entered into on an annual basis to limit the claims experience of the ceding entity and thereby protect its financial integrity. When the period of the arrangement exceeds one year, the contract must be carefully reviewed to determine if the end result more closely follows proportional reinsurance. **No reserve credit is taken for non-proportional reinsurance unless the aggregate attachment point has in fact been penetrated. In order for an entity to reflect reserve credits on a prospective basis, the entity will need to demonstrate that the present value of expected recoveries using realistic assumptions, to be realized from the reinsurer are in excess of the present value of the reinsurance premiums guaranteed to be paid by the ceding entity under the terms of the contrac**t. Because non-proportional reinsurance aggregates experience, and does not indemnify the ceding entity for each policy loss, the use of statutory assumptions underlying the insured policies is inappropriate for determining any reserve credit to be taken by the ceding entity. Historical experience, pricing assumptions and asset shares shall be considered in determining if the reinsurer may be reasonably expected to pay any claims. The reserve credit taken shall only reflect these reasonable expectations. **This treatment of non-proportional reinsurance is similar to the way property and casualty (P&C) reinsurance is considered. This is because these modes of reinsurance more closely follow P&C indemnification principles than life insurance formula basis, and because these coverages are very similar to excess insurance on P&C products. In determining the appropriate reserve credit, the probability of a loss penetrating to the reinsurer's level of coverage (using reasonable assumptions) must be multiplied by the expected amount of recovery.** This is the same as reserve credits on coinsurance where the probability of a claim (i.e., mortality) is multiplied by the expected return (i.e., death

benefit). In that the coverage is for aggregate experience, the mortality assumptions underlying any one policy risk are inappropriate to analyze the appropriate credits for non-proportional coverage.

- **SSAP No. 61R, adopts FAS 113 with modifications.**

Relevant Literature

86. This statement adopts with modification *FASB Statement No. 113, Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts*. The statutory accounting principles established by this statement differ substantially from GAAP, reflecting much more detailed guidance, as follows:

a. Reserve credits taken by ceding companies as a result of reinsurance contracts are netted against the ceding entity's policy and claim reserves and unpaid claims;

b. First year and renewal ceding commissions on indemnity reinsurance of new business are recognized as income. Ceding commissions on ceded in-force business are included in the calculation of initial gain or loss;

c. As discussed in SSAP No. 50, statutory accounting defines deposit-type contracts as those contracts which do not include any mortality or morbidity risk. GAAP defines investment contracts as those that do not subject the insurance enterprise to significant policyholder mortality or morbidity risk. (The distinction is any mortality or morbidity risk for statutory purposes vs. significant mortality or morbidity risk for GAAP purposes.) Therefore, a contract may be considered an investment contract for GAAP purposes, and that same contract may be considered other than deposit-type for statutory purposes. A reinsurance treaty covering contracts that have insignificant mortality or morbidity risk (i.e., contracts classified as other than deposit-type contracts for statutory purposes, but investment contracts for GAAP purposes) that does not transfer that mortality or morbidity risk, but does transfer all of the significant risk inherent in the business being reinsured (e.g., lapse, credit quality, reinvestment or disintermediation risk) qualifies for reinsurance accounting for statutory reporting purposes, but would not qualify for reinsurance accounting treatment for GAAP purposes;

d. Initial gains on indemnity reinsurance of in-force blocks of business have unique accounting treatment. A portion of the initial gain (equal to the tax effect of the initial gain in surplus) is reported as commissions and expense allowances on reinsurance ceded in the statement of operations. The remainder of the initial gain is reported on a net-of-tax basis as a write-in for gain or loss in surplus in the Capital and Surplus Account. In subsequent years, the ceding entity recognizes income on the reinsurance ceded line for the net-of-tax profits that emerged on the reinsured block of business with a corresponding decrease in the write-in for gain or loss in surplus;

e. This statement prohibits recognition of a gain or loss in connection with the sale, transfer or reinsurance of an in-force block of business between affiliated entities in a non-economic transaction. Any difference between the assets transferred by the ceding entity and the liabilities, including unamortized IMR, shall be deferred and amortized under the interest method;

f. This statement requires that a liability be established through a provision reducing surplus for unsecured reinsurance recoverables from unauthorized reinsurers;

g. This statement prescribes offsetting certain reinsurance premiums.

87. This statement incorporates Appendices A-785 and A-791.

- **SSAP No. 61R, Glossary Excerpts:**

Net Amount at Risk
The excess of the death benefit of a policy over the policy reserve. It is the amount which must come from surplus in the event of a death claim.

Non-Proportional Reinsurance
Reinsurance that is not secured on individual lives for specific individual amounts of reinsurance, but rather reinsurance that protects the ceding entity's overall experience on its entire portfolio of business, or at least a broad as noted in paragraph 19 of SSAP No. 61 segment of it. The most common forms of non-proportional reinsurance are stop loss reinsurance and catastrophe reinsurance.

Non-proportional reinsurance is a form of casualty insurance. Usually neither the premium nor continuance of coverage is guaranteed beyond a specified term.

Pool
A method of allocating reinsurance among several reinsurers. Using this method, each reinsurer receives a specified percentage of risk ceded into the pool. Percentages may vary by reinsurer.

Proportional Reinsurance
Reinsurance on a particular life for a specified amount or share generally, though not necessarily, secured at the time the policy is issued to the insured. The continuation of coverage guarantees for the reinsurance generally parallel those in the life insurance coverage reinsured. Most life reinsurance conducted in the United States is done so on a proportional basis.

Yearly Renewable Term (YRT)
A form of life reinsurance under which the mortality or morbidity risks, but not the permanent plan reserves, are transferred to the reinsurer for a premium that varies each year with the amount at risk and the ages of the insureds. The amount of reinsurance, which may change annually, is generally the amount of insurance provided by the policy in excess of the primary insurer's reserve.

- ***SSAP No. 62R—Property and Casualty Reinsurance* Exhibit A – Implementation Questions and Answers**

10. Q: For purposes of evaluating whether a contract with a reinsurer transfers risk, what constitutes a contract?

- A: A contract is not defined, but is essentially a question of substance. It may be difficult in some circumstances to determine the boundaries of a contract. For example, the profit-sharing provisions of one contract may refer to experience on other contracts and, therefore, raise the question of whether, in substance, one contract rather than several contracts exist.

  The inconsistency that could result from varying interpretations of the term *contract* is limited by requiring that features of the contract or other contracts or agreements that directly or indirectly compensate the reinsurer or related reinsurers for losses be considered in evaluating whether a particular contract transfers risk. Therefore, if agreements with the reinsurer or related reinsurers, in the aggregate, do not transfer risk, the individual contracts that make up those agreements also would not be considered to transfer risk, regardless of how they are structured.

The original GAAP source of the above in SSAP No. 62R is *EITF D-34* *Accounting for Reinsurance: Questions and Answers about FASB Statement No. 113*, ***question 13***

13. Q—For purposes of evaluating whether a contract with a reinsurer transfers risk, what constitutes a contract?

A—Statement 113 does not define what constitutes a "contract," which is essentially a question of substance. It may be difficult in some circumstances to determine the boundaries of a contract. For

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example, the profit-sharing provisions of one contract may refer to experience on other contracts and, therefore, raise the question of whether, in substance, one contract rather than several contracts exist.

Statement 113 limits the inconsistency that could result from varying interpretations of the term contract by requiring that features of the contract or other contracts or agreements that directly or indirectly compensate the reinsurer or related reinsurers for losses be considered in evaluating whether a particular contract transfers risk. Therefore, if agreements with the reinsurer or related reinsurers, in the aggregate, do not transfer risk, the individual contracts that make up those agreements also would not be considered to transfer risk, regardless of how they are structured.

Certain guidance relevant to determining the boundaries of a contract is provided in the accounting literature. As described in paragraph 8 of Statement 113, provisions of other related contracts may be considered part of the subject contract under certain circumstances. Likewise, paragraphs 59 and 60 of Statement 113 indicate that the Board did not intend for different kinds of exposures combined in a program of reinsurance to be evaluated for risk transfer and accounted for together, because that would allow contracts that do not meet the conditions for reinsurance accounting to be accounted for as reinsurance by being designated as part of a program. In addition, Question 12 above refers to the fact that an amendment of a contract may create a new contract. [Revised 12/98.]

The legal form and substance of a reinsurance contract generally will be the same, so that the risks reinsured under a single legal document would constitute a single contract for accounting purposes. However, that may not always be the case. Accordingly, careful judgment may be required to determine the boundaries of a contract for accounting purposes. [Revised 12/98.]

If an agreement with a reinsurer consists of both risk transfer and nonrisk transfer coverages that have been combined into a single legal document, those coverages must be considered separately for accounting purposes. [Revised 12/98.]

Topic 944 Reinsurance Contracts in the current FASB Codification Implementation Guide continues to include the guidance from EITF D-34

Reinsurance Contracts
Implementation Guidance

What Constitutes a Contract

944-20-55-27
This implementation guidance discusses, for purposes of evaluating whether a contract with a reinsurer transfers risk, what constitutes a contract, which is essentially a question of substance. It may be difficult in some circumstances to determine the boundaries of a contract.

944-20-55-28
For instance, the profit-sharing provisions of one contract may refer to experience on other contracts and, therefore, raise the question of whether, in substance, one contract rather than several contracts exist.

944-20-55-29
The guidance in the Financial Services—Insurance Topic on reinsurance limits the inconsistency that could result from varying interpretations of the term contract by requiring that features of the contract or other contracts or agreements that directly or indirectly compensate the reinsurer or related reinsurers for losses be considered in evaluating whether a particular contract transfers risk. Therefore, if agreements with the reinsurer or related reinsurers, in the aggregate, do not transfer risk, the individual contracts that make up those agreements also would not be considered to transfer risk, regardless of how they are structured.

944-20-55-30
Certain guidance relevant to determining the boundaries of a contract is provided in the accounting literature.

944-20-55-31
Paragraph 944-20-15-40 states that provisions of other related contracts may be considered part of the subject contract under certain circumstances.

944-20-55-32
Different kinds of exposures combined in a program of reinsurance shall not be evaluated for risk transfer and accounted for together, because that would allow contracts that do not meet the conditions for reinsurance accounting to be accounted for as reinsurance by being designated as part of a program.

944-20-55-33
In addition, paragraph 944-20-15-65 refers to the fact that an amendment of a contract may create a new contract.

944-20-55-34
The legal form and substance of a reinsurance contract generally will be the same, so that the risks reinsured under a single legal document would constitute a single contract for accounting purposes. However, that may not always be the case. Accordingly, careful judgment may be required to determine the boundaries of a contract for accounting purposes.

944-20-55-35
Paragraph 944-20-15-56 states that, if an agreement with a reinsurer consists of both risk transfer and nonrisk transfer coverages that have been combined into a single legal document, those coverages shall be considered separately for accounting purposes.

- ***A-791 Life and Health Reinsurance Agreements***

A-791, paragraph 1, provides the following:

1. This Appendix shall not apply to assumption reinsurance, yearly renewable term reinsurance or certain nonproportional reinsurance such as stop loss or catastrophe reinsurance.

Q – Aside from assumption reinsurance, what other types of reinsurance are exempt from the accounting requirements?

A – Yearly renewable term (YRT) and c**ertain nonproportional reinsurance arrangements, such as stop loss and catastrophe reinsurance are exempt** because these do not normally provide significant surplus relief and therefore are outside the scope of this Appendix. If a catastrophe arrangement takes a reserve credit for actual losses beyond the attachment point or the unearned premium reserve (UPR) of the current year's premium, there will most likely be no regulatory concern.

Similarly, if a YRT treaty provides incidental reserve credits for the ceding insurer's net amount at risk for the year with no other allowance to enhance surplus, there will most likely be no regulatory concern. For purposes of this exemption, a treaty labeled as YRT does not meet the intended definition of YRT if the surplus relief in the first year is greater than that provided by a YRT treaty with zero first year reinsurance premium and no additional allowance from the reinsurer.

Additional pertinent information applicable to all YRT treaties and to non-proportional reinsurance arrangements is contained in paragraphs 19 and 20 of SSAP No. 61R.

A-791, paragraph 2e contains the guidance which limits the reinsurance to the amount realized on the reinsured policy.

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2. No insurer shall, for reinsurance ceded, reduce any liability or establish any asset in any statutory financial statement if, by the terms of the reinsurance agreement, in substance or effect, any of the following conditions exist:

e. The reinsurance agreement involves the possible payment by the ceding insurer to the reinsurer of amounts other than from income realized from the reinsured policies. For example, it is improper for a ceding company to pay reinsurance premiums, or other fees or charges to a reinsurer which are greater than the direct premiums collected by the ceding company;

A-791, paragraph 2f contains the guidance on transferring all of the significant risk of the business reinsured.

2. No insurer shall, for reinsurance ceded, reduce any liability or establish any asset in any statutory financial statement if, by the terms of the reinsurance agreement, in substance or effect, any of the following conditions exist:

f. The treaty does not transfer all of the significant risk inherent in the business being reinsured. The following table identifies for a representative sampling of products or type of business, the risks which are considered to be significant. For products not specifically included, the risks determined to be significant shall be consistent with this table.

Risk categories:

i. Morbidity

ii. Mortality

iii. Lapse

This is the risk that a policy will voluntarily terminate prior to the recoupment of a statutory surplus strain experienced at issue of the policy.

iv. Credit Quality

This is the risk that invested assets supporting the reinsured business will decrease in value. The main hazards are that assets will default or that there will be a decrease in earning power. It excludes market value declines due to changes in interest rate.

v. Reinvestment

This is the risk that interest rates will fall and funds reinvested (coupon payments or monies received upon asset maturity or call) will therefore earn less than expected. If asset durations are less than liability durations, the mismatch will increase.

vi. Disintermediation

This is the risk that interest rates rise and policy loans and surrenders increase or maturing contracts do not renew at anticipated rates of renewal. If asset durations are greater than the liability durations, the mismatch will increase. Policyholders will move their funds into new products offering higher rates. The company may have to sell assets at a loss to provide for these withdrawals.

+ - Significant 0 - Insignificant

RISK CATEGORY

	i.	ii.	iii.	iv.	v.	vi.
Health Insurance - other than LTC/LTD*	+	0	+	0	0	0

Health Insurance - LTC/LTD*	+	0	+	+	+	0
Immediate Annuities	0	+	0	+	+	0
Single Premium Deferred Annuities	0	0	+	+	+	+
Flexible Premium Deferred Annuities	0	0	+	+	+	+
Guaranteed Interest Contracts	0	0	0	+	+	+
Other Annuity Deposit Business	0	0	+	+	+	+
Single Premium Whole Life	0	+	+	+	+	+
Traditional Non-Par Permanent	0	+	+	+	+	+
Traditional Non-Par Term	0	+	+	0	0	0
Traditional Par Permanent	0	+	+	+	+	+
Traditional Par Term	0	+	+	0	0	0
Adjustable Premium Permanent	0	+	+	+	+	+
Indeterminate Premium Permanent	0	+	+	+	+	+
Universal Life Flexible Premium	0	+	+	+	+	+
Universal Life Fixed Premium	0	+	+	+	+	+
Universal Life Fixed Premium dump-in premiums allowed	0	+	+	+	+	+

*LTC = Long Term Care Insurance
LTD = Long Term Disability Insurance

6. The reinsurance agreement shall contain provisions which provide that:

   a. **The agreement shall constitute the entire agreement between the parties with respect to the business being reinsured thereunder and that there are no understandings between the parties other than as expressed in the agreement**; and

   b. Any change or modification to the agreement shall be null and void unless made by amendment to the agreement and signed by both parties.

Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups): The referral from VAWG was formally received by the Working Group on January 10, 2024 and NAIC staff was directed to draft an agenda item for discussion.

Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group: None

Convergence with International Financial Reporting Standards (IFRS): None

Staff Review Completed by: Robin Marcotte – NAIC Staff - February 2024

Staff Recommendation:
NAIC staff recommends that the Working Group move this item to the active listing of the maintenance agenda, categorized as a SAP clarification, and expose revisions to *SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance* as illustrated below. The proposed revisions incorporate guidance to SSAP No. 61R which is consistent with the guidance currently in SSAP No. 62R, Exhibit A Implementation Questions and Answers, question 10 and also add reference to A-791, paragraph 6 guidance in the YRT guidance paragraph.

As described in the summary of issues, NAIC staff agrees that risk transfer analysis of a reinsurance contract or contracts with interdependent features that directly or indirectly compensate the reinsurer, requires that all parts of the contract be evaluated in aggregate. Appendix A-791, paragraph 6 already contains guidance that the agreement must constitute the entire agreement. While NAIC staff agrees with the concern that VAWG raised regarding some entities taking too large of a reinsurance credit, the existing guidance in SSAP No. 61R regarding risk transfer requires that reporting entities should not take reinsurance credit for

amounts greater than the risk ceded should be sufficient to address those concerns. However, NAIC staff would be willing to develop a more extensive implementation guidance or other revisions if desired.

Status:
On March 16, 2024, the Statutory Accounting Principles (E) Working Group exposed revisions to incorporate guidance to *SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance* that is consistent with the guidance currently in *SSAP No. 62R—Property and Casualty Reinsurance*, Exhibit A Implementation Questions and Answers, question 10. This guidance requires risk transfer to be evaluated in aggregate for contracts with interrelated contract features such as experience rating refunds. The revisions also adds a reference in *Appendix A-791 Life and Health Reinsurance Agreements* (A-791), paragraph 6 regarding the entirety of the contract. In addition, the Working Group directed NAIC staff to notify the Valuation Analysis (E) Working Group, the Life Actuarial (A) Task Force and the Reinsurance (E) Task Force of the exposure.

Proposed Revisions SSAP No. 61R:

Transfer of Risk

17. Reinsurance **agreements must transfer risk from the ceding entity to the reinsurer in order to receive the reinsurance accounting treatment discussed in this statement.** If the terms of the agreement violate the risk transfer criteria contained herein, **(i.e., limits or diminishes the transfer of risk by the ceding entity to the reinsurer), the agreement shall follow the guidance for Deposit Accounting. In addition, any contractual feature that delays timely reimbursement violates the conditions of reinsurance accounting.**

~~17.~~18. For purposes of evaluating whether a contract with a reinsurer transfers risk, what constitutes a contract is essentially a question of substance. It may be difficult in some circumstances to determine the boundaries of a contract. For instance, the profit-sharing provisions of one contract may refer to experience on other contracts and, therefore, raise the question of whether, in substance, one contract rather than several contracts exist. The inconsistency that could result from varying interpretations of the term contract is limited by requiring that features of the contract or other contracts or agreements that directly or indirectly compensate the reinsurer or related reinsurers for losses be considered in evaluating whether a particular contract transfers risk. Therefore, if agreements with the reinsurer or related reinsurers in the aggregate do not transfer risk, the individual contracts that make up those agreements also would not be considered to transfer risk, regardless of how they are structured.

~~18.~~19. This paragraph applies to all life, deposit-type and accident and health reinsurance agreements except for yearly renewable term reinsurance agreements and non-proportional reinsurance agreements such as stop loss and catastrophe reinsurance. All reinsurance agreements covering products that transfer significant risk shall follow the guidance for reinsurance accounting contained in this statement. All reinsurance contracts covering products that do not provide for sufficient transfer of risk shall follow the guidance for Deposit Accounting.

~~19.~~20. **Yearly renewable term (**YRT) reinsurance agreements that transfer a proportionate share of mortality or morbidity risk inherent in the business being reinsured and do not contain any of the conditions described in **Appendix A-791, paragraphs 2.b., 2.c., 2.d., 2.h., 2.i., 2.j. or 2.k.,** shall follow the guidance for reinsurance accounting, including paragraphs 55-57 of this statement that apply to indemnity reinsurance. Contracts that fail to meet the requirements for reinsurance accounting shall follow the guidance for Deposit Accounting. For all treaties entered into on or after January 1, 2003, the deferral guidance in paragraph 3 of A-791 shall also apply to YRT agreements. YRT agreements shall follow the requirements of A-791, paragraph 6, regarding the entire agreement and the effective date of agreements. Since YRT agreements only transfer the mortality or morbidity risks to the reinsurer, the recognition of income shall be reflected on a net of tax basis, as gains emerge based on the mortality or morbidity experience.

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20. For non-proportional reinsurance agreements such as stop loss and catastrophe reinsurance agreements, contract terms shall be evaluated to assess whether they transfer significant risk to the reinsurer. For example, prepayment schedules and accumulating retentions from multiple years are contractual features inherently designed to delay the timing of reimbursement to the ceding entity limits the risk to the reinsurer. Regardless of what a particular feature might be called, any feature that can delay timely reimbursement violates the conditions for reinsurance accounting. Transfer of insurance risk requires that the reinsurer's payment to the ceding entity depend on and directly vary with the amount and timing of claims settled under the reinsured contracts. Contractual features that can delay timely reimbursement prevent this condition from being met. Reinsurance accounting shall apply to all non-proportional agreements that transfer significant risk and do not contain any provisions that protect the reinsurer from incurring a loss. Contracts that fail to meet the requirements for reinsurance accounting shall follow the guidance for Deposit Accounting.

On August 13, 2024, the Statutory Accounting Principles (E) Working Group re-exposed this agenda item to allow for further discussion. The Working Group direct NAIC staff to forward the comments received to the Valuation Analysis (E) Working Group, Life Actuarial (A) Task Force and the Reinsurance (E) Task Force.

The Working Group requested industry input on the following:

1. Industry examples.
2. Details on both the dollar impact and the number of existing YRT combination contracts might not meet risk transfer from the exposed revision.
3. Specific language regarding the concept that interdependent contract features should be analyzed in aggregate.

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2024/08-13-24 Summer National Meeting/Exposures/24-06 - RT YRT-Combo contracts.docx

Statutory Accounting Principles (E) Working Group
Dec. 17, 2024
Comment Letters Received – Agenda 2

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Jeffrey G. Stevenson FSA (Stevenson Associates, Inc) Comments – December 11, 2024 o Ref #2024-06: Risk Transfer Analysis of Combination Reinsurance Contracts	7-10

December 9, 2024

Mr. Dale Bruggeman, Chairman
Statutory Accounting Principles Working Group
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

Re: Request for Comments on SAPWG 2024-05 and 2024-06

Submitted Electronically

Dear Mr. Bruggeman:

The American Council of Life Insurers (ACLI) appreciates the opportunity to comment on the above referenced items that were re-exposed for comment by the Statutory Accounting Principles (E) Working Group (SAPWG) during the NAIC Summer National Meeting in Chicago.

ACLI would like to express our sincere gratitude for your time and willingness to collaborate with us on these reinsurance matters. We value the open dialogue and believe it has contributed to a more informed and constructive regulatory process. Through our discussions, we have gained a deeper understanding of the concerns raised by SAPWG regulators while also conveying the perspectives of our members.

ACLI members continue to believe that the two proposals (Ref #2024-05 and Ref #2024-06) are inextricably linked and should be considered together.

Ref #2024-05: A-791 Paragraph 2.c.

ACLI members believe that retaining the language in Appendix A-791, paragraph 2c, is consistent with the statutory accounting requirement that reinsurance should not deprive a ceding insurer of surplus. With that said, we propose changes below to SAPWG 2024-06 that, if adopted, would address our concerns with the exposed changes in SAPWG 2024-05.

ACLI agrees that statutory risk transfer requires a careful evaluation of the facts and circumstances of a reinsurance agreement and should never rely on a simplistic application of "safe harbor" rules. Appendix A-791 already provides an objective standard by which to assess whether YRT premiums

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.
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are excessive. That is, premiums are considered excessive if they result in the deprivation of ceding insurer surplus. The adoption of the change proposed by 2024-05 might be interpreted as introducing some other standard to determine whether premiums are excessive. However, no objective criteria have been provided by which to apply such other standards and, as a result, the adoption of the proposed change serves to create the potential for a range of interpretations as to what constitutes an excessive YRT premium. Such differences in interpretation are already surfacing with some parties interpreting the combination of the two SAPWG exposures to indicate that all combination Coinsurance-YRT (Co-YRT) agreements are non-proportional and therefore do not provide reserve credit; a conclusion that ACLI believes is inconsistent with SAPWG intent based on conversations we have had with regulators.

To avoid the potential for misinterpretation, ACLI proposes that the 2024-05 exposed changes only be adopted if done concurrently with the ACLI version of SAPWG 2024-06 proposed below.

Ref #2024-06: Risk Transfer Analysis for Combination Reinsurance Contracts

ACLI would like to thank SAPWG for the ongoing discussions regarding SAPWG 2024-06. During our discussions, we showed that combination Co-YRT agreements can be structured in ways that satisfy statutory risk transfer requirements as well as in ways that fail to satisfy statutory risk transfer requirements. We showed that when the YRT premiums were set at or below valuation level mortality, risk transfer was achieved (as ceding insurer surplus was protected against deprivation), but when YRT premiums were in excess of these amounts that risk transfer was not achieved (as ceding insurer surplus was not protected and could become negative). We concluded that taking a full proportional reserve credit for coinsured business and a ½ c_x credit for business ceded on a YRT basis (under a combination Co-YRT agreement) would be appropriate when agreements meet statutory risk transfer requirements such as having YRT premiums set at or below valuation mortality. To clarify SAPWG 2024-06 in order for it to recognize this result, we propose the following refinements to the exposure.

Proposed Risk Transfer Framework

ACLI proposes the following framework for assessing combination Co-YRT agreements for statutory risk transfer purposes:

- Any risk transfer assessment of combination Co-YRT agreements should be conducted in the context of applicable SAP guidance and based on the facts and circumstances of the relevant reinsurance agreement(s).
- SAP coinsurance guidance should be applied to the coinsurance component of the agreement(s) and SAP YRT guidance should be applied to the YRT component of the agreement(s).
- Additionally, an overall assessment of the combined agreement should be performed consistent with the requirement that “the agreement shall constitute the entire agreement between the parties with respect to the business being reinsured thereunder[.]”[1] to ensure that ceding insurer surplus is not deprived.

ACLI agrees that if any individual component of a combination Co-YRT agreement does not pass statutory risk transfer, then the aggregate transaction would not pass statutory risk transfer regardless of how it is structured. An overall assessment should include, among other things, an

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evaluation of:

i) the coinsurance agreement(s) to ensure that all significant risks inherent in the reinsured business are transferred, and

ii) the YRT agreement(s) to ensure that the conditions described in Appendix A-791, paragraphs 2.b., 2.c., 2.d., 2.h., 2.i., 2.j. or 2.k. are not violated, and

iii) the entire agreement to confirm that, when assessed in aggregate, it does not deprive a ceding insurer of surplus or require payments other than from the statutory net gain before adjustments (i.e., as defined in the 2023 SAP life blank line 29, hereinafter "net gain") realized from the reinsured policies.

ACLI agrees that agreements that inappropriately preclude any possibility of reinsurance losses being incurred because of excessive YRT premiums would be of concern from a statutory risk transfer perspective. In evaluating whether this is the case, YRT premium levels should be assessed using statutory principles as any resulting reserve credit will also have been established using statutory principles. In applying statutory principles, statutory valuation assumptions serve as an acceptable benchmark when assessing whether YRT premiums are excessive. More specifically:

- YRT reinsurance results in the assumption of mortality risk for the lifetime of the underlying business. In such a context, the statutory valuation framework already defines a reasonably prudent valuation mortality basis for ceding insurers when reserving for such risks. As such, this same valuation mortality basis should also serve as a reasonable and prudent benchmark for reinsurers to consider when committing to the assumption of mortality risk for the lifetime of the underlying business.

- The determination of reserve credit relates to the underlying statutory reserves that are held by the ceding insurer and determined based on statutory principles and assumptions. It would be inconsistent to determine a reserve credit using GAAP principles and assumptions in relation to underlying reserves that are computed using statutory principles and assumptions.

Proposed Changes to SSAP61 and Appendix A-791

In response to SAPWG's request for specific recommendations, ACLI proposes the following changes to SSAP61 and the introduction of a new question to be added to Appendix A-791 in lieu of the exposed changes proposed in SAPWG 2024-06.

ACLI proposes the following paragraph be adopted in SSAP61. This proposal aims to maintain SAPWG's objective of evaluating agreements in aggregate and ensuring the appropriate application of current risk transfer principles.

18. *For purposes of evaluating whether a reinsurance agreement satisfies statutory risk transfer requirements, the determination of what constitutes an agreement is essentially a question of substance. Multiple agreements should be evaluated together for risk transfer purposes when they are entered into together to achieve one overall commercial effect and where considerations to be exchanged under one agreement depend on the performance of*

the other agreement(s). For individual agreements that contemplate reinsurance on both a YRT and coinsurance basis, each of the YRT and coinsurance reinsurance components need to satisfy risk transfer requirements on their respective bases. In addition, when evaluated in its entirety, such agreements cannot deprive the ceding insurer of surplus nor require payments to the reinsurer for amounts other than the net gain realized from the reinsured policies.

ACLI proposes a second question be added to Appendix A-791 2b:

Question

If business is reinsured under a combination reinsurance agreement where the reinsurer assumes certain risks on a coinsurance, modified coinsurance, and/or coinsurance funds withheld basis and other risks on a YRT basis, what conditions are required to ensure that the ceding insurer is neither deprived of surplus nor required to make payments to the reinsurer from other than the net gain realized from the reinsured policies such that risk transfer is achieved? How are these conditions impacted by the agreement having an experience refund formula?

a. *The reinsurance agreement cannot deprive the ceding insurer of surplus or assets. If treaty provisions limit payment of amounts to the reinsurer to the amount of net gain realized from the reinsured business, then the ceding insurer surplus is not deprived, and risk transfer is achieved.*

   For example, risk transfer requirements are satisfied when YRT premiums are contractually stipulated to be equal to or less than the level of valuation mortality used by the ceding insurer in calculating reserves for the reinsured business at the time of inception of the reinsurance agreement and are contractually constrained not to exceed this level.

b. *The fact that there is an experience refund does not, in itself, cause an agreement to fail risk transfer. However, an experience refund that requires that the ceding insurer reimburse the reinsurer for negative experience using amounts it has in surplus is a violation of risk transfer requirements, except that neither offsetting experience refunds against current and prior years' losses under the agreement nor payment by the ceding insurer of an amount equal to the current and prior years' losses under the agreement upon voluntary termination of in-force reinsurance by the ceding insurer shall be considered such a reimbursement to the reinsurer for negative experience.*

Summary

Ultimately, our primary concern remains that some may interpret the proposed 2024-06 exposure to indicate that all combination Co-YRT agreements are non-proportional and therefore should not provide reserve credit. Such an interpretation would affect in-force combination Co-YRT agreements and create the potential for material volatility in surplus levels for ceding insurers who have previously entered into such agreements. In addition, such an interpretation would effectively eliminate the ability to use such agreements going forward. Based on our discussions with SAPWG, it is our understanding that neither of these outcomes are intended.

Another concern is that some may interpret the proposed 2024-05 exposure to require an assessment of YRT premiums using a standard other than the existing standard provided in SSAP61 that precludes ceding insurer surplus deprivation. In such a case, there could be significant variation in regulatory interpretations as to what constitutes an "excessive" YRT premium leading to inconsistency rather than harmonization.

ACLI believes that one way to maintain the ability to use compliant combination agreements and not bring into question the reserve credits currently being taken by ceding insurers who are party to such agreements is by adopting proposed changes to SSAP61 and Appendix A-791 consistent with those proposed by ACLI above. Such changes aim to make clear that compliant agreements cannot charge "excessive" YRT premiums and provide a clear basis for how an assessment of YRT premiums anchored to existing SAP guidance is to be performed.

Along with the suggested changes above, we propose forming a small working group consisting of regulators and industry experts to finalize language consistent with the objectives noted above within a defined timeline.

Thank you for the opportunity to provide feedback on these two exposures. ACLI is committed to collaborating with the NAIC and state regulators and welcome further discussion.

Sincerely,

Marc Altschull, CFA, FSA, MAAA
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To the Statutory Accounting Practices Accounting Working Group for issue 2024-06

I am a retired actuary with years of experience in reinsurance, primarily with respect to transactions where the primary motivations are not primarily risk transfer. Not long ago I was asked about a treaty arrangement involving combinations of coinsurance and YRT and was told there was some controversy with respect to the accounting.

Combination coinsurance and YRT agreements have been around forever; there shouldn't be much controversy.

Traditionally, the YRT combined in coinsurance agreements is YRT reinsurance inuring to the benefit of the reinsured block.

In this respect, the cash flows of the coinsurance (or Modco) treaty (principally of those intended for purposes other than risk transfer) have traditionally been:

+Premiums
-Claims
-Surrender & Maturity Benefits
-Commissions and Expense Allowances

-Ceded Reins Prems (on Inuring agreements)
+Ceded Reins Dbs (on Inuring agreements)
+Ceded reins Exp Refunds (on Inuring agreements)

-Modco Res Incr (if Modco)
+Modco Interest (if Modco)

- Experience Refunds (if included)

The above result may result in an expense and risk charge with favorable experience.

The inuring agreements in the above could be YRT of mortality risk or other coinsurance of reinsured business of the benefits or even catastrophic stop loss arrangements. The inuring agreements could be traditional YRT with an experience refund arrangement. They could also be YRT agreements of a more financially motivated arrangement, i.e., a high YRT premium based on a high percentage of the valuation mortality basis, combined with a large experience refund.

There is no reason the YRT couldn't be additional quota share of the same block as the coinsurance. Why would ceding companies do this? Well in past circumstances, perhaps they were reinsuring the business with two reinsurers and one reinsurer does not want to retain catastrophic mortality risk but the second reinsurer is willing to take that additional risk in addition to the risks in its own portion of the reinsurer. Including such reinsurance in the single tradition would be done for administrative convenience and if structured as YRT would include additional impacts on reserve and capital requirements. This type of arrangement would not be uncommon for divestiture of the business (might be referred to as administrative reinsurance). My first impression of the combo YRT treaties presented to me is that the additional YRT is nothing more than inuring reinsurance regardless of what the reinsured business is, just like these arrangements in the past.

My understanding of the new variations of combo treaties is that the YRT is indeed an additional quota share of the coinsured business but the interpretation is that the YRT is not inuring to the benefit of the coinsured business. In fact, in the new interpretations the YRT is treated as a separate agreement with its own cash flows. Moreover, the YRT mortality risk treaty might be on the basis of a high percentage of the valuation table thereby generating a generous experience refund under expected assumptions.

The interpretation being made that the extra YRT arrangement is more like a standalone rider produces a result that in the event of adverse investment scenarios, the high experience refund (on the YRT mortality component) can be combined with adverse experience on the coinsured business to merely produce a lower experience refund with the reinsurer not necessarily reimbursing the ceding company for the adverse experience of the coinsured business.

That might look okay with the arithmetic but in my opinion it is a clear violation of the life reinsurance model regulation. The reserve or capital credits associated with any treaty with such an arrangement (and with the YRT component not accounted for as inuring reinsurance) should be denied.

Here is the explanation.

Accounting requirements of the model regulation are:

1. Renewal expense allowances provided or to be provided to the ceding insurer by the reinsurer in any accounting period, a must be sufficient to cover anticipated allocable renewal expenses of the ceding insurer on the portion of the business reinsured
2. The ceding insurer can't be deprived of surplus or assets at the reinsurer's option or automatically upon the occurrence of some event
3. The ceding insurer is required to reimburse the reinsurer for negative experience under the reinsurance agreement

4. The reinsurance agreement can't involve the possible payment by the ceding insurer to the reinsurer of amounts other than from income realized from the reinsured policies.

The new interpretation of the added YRT component (an additional quota share of the underlying coinsured business) violates some of all of these accounting requirements.

First off, as for the YRT exemption from the requirements of the model regulation, the combo treaty "interpretation" does not allow for any YRT exemption because the surplus and capital aid of the combination exceeds that of a zero premium YRT treaty. The model regulation accounting requirements should apply to all the components of the treaty.

Let's assume the coinsured portion of the business produces negative cash flows as a result of poor investment experience and the additional YRT business produces an experience refund that more than offsets the negative experience.

Note that all reinsurance has a cost. The YRT portion of the business has a cost associated with it. The cost is Premiums minus Claims minus Experience Refund. (This typically nets to a cost equal to a risk fee or the profit margin of the reinsurer which may or not be a mere risk fee). But in this case the adverse experience of the coinsured business reduces the YRT portion's experience refund, that YRT reinsurance now has an additional cost in addition to the profit margin.

That cost is now a cost of the ceding company. Reinsurance costs of the ceding company have to be reimbursed by the reinsurer through the expense allowance. In this case then, the reinsurer has to reimburse its own charge, thereby resulting in a wash, so there is, in fact, no recovery of the adverse experience refund.

You can also think of the experience refund as an "optional experience refund". In this case a portion of the YRT experience refund is denied at the option of the reinsurer (it's automatically denied with the occurrence of the adverse experience on the coinsurance). So the use of the YRT as an offset to adverse experience is automatically denying the ceding company of surplus automatically on the occurrence of some event.

The recovery of the adverse experience on the coinsurance is also technically a payment that is not made out of the profits on that coinsured business. It is coming out of an additional premium payment to the reinsurer (the YRT premium).

I recognize that some might make nuanced arguments against these above arguments. However, and most importantly, let's look at the essential substance of the YRT portion of the transaction. The companion YRT arrangement typically has a YRT premium which is a high percentage of valuation mortality (let's say 90%) and any premiums in excess of the claims are experience refunded net of a risk charge. The substance of this transaction is that there is a risk charge paid and claims in excess of 90% of valuation mortality are experience refunded back to the ceding company. (Now this might be structured as YRT because there are other accounting entries such as face amount ceded and reserve credits accompanying the accounting, but the essence of the transaction is essentially a non-proportional stop loss arrangement). The YRT component of the transaction is basically a stop loss

arrangement with a risk charge for a premium. In exchange for this risk premium, the reinsurer will pay claims only if they exceed the percentage of the valuation basis mortality relating to the premium. It is an excess of loss structure.

So if we think of the companion YRT agreement in this true economic form, the companion treaty in addition to the coinsurance is nothing more than a risk premium paid to the reinsurer for catastrophic mortality. From this standpoint, the combo treaty arrangement's result in the event of adverse experience on the coinsurance is that the reinsurer is receiving a payment in addition to the risk charge from the ceding company to cover that adverse experience (as is argued above). This is because in order for the transaction to provide for an offset to the losses on the coinsurance, the ceding company would be required to make a payment to the reinsurer in addition to the risk charge! When viewed from this true economic perspective, this is clearly a violation of the model regulation.

To argue that merely changing the companion contract from a stop loss format to an equivalent YRT structure would change the above interpretation (that the contract violates the model regulation) seems just plain wrong.

One can also think of this additional payment as essentially the same as using an artificially high interest rate (like 12%) to calculate coinsurance experience refunds or modco profits. Everyone should recognize that this provision would be a violation of the model regulation as it would be an additional payment or a payment outside of profits in the business. Likewise, any additional premium paid, or reduction in experience refund of associated treaty provisions, would similarly be a violation of the model regulation.

In P&C arrangements, there is often reference to this type of arrangement as a "reinstatement premium". This has no place in a life reinsurance transaction.

This concluding argument of looking through to the substance of the transaction validates all the other above arguments that this new interpretation of the combo structure violates the model regulation!

If the additional YRT is, in essence, accounted for as an inuring agreement, just has it has always been done, the appropriate cash flows fall out in the treaty accounting and the reserve credits are justified.

Respectfully submitted,

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