

Draft Pending Adoption

Attachment Five
Capital Adequacy (E) Task Force
11/19/20

Draft: 11/3/20

Property and Casualty Risk-Based Capital (E) Working Group
Virtual Meeting (in lieu of meeting at the 2020 Fall National Meeting)
October 27, 2020

The Property and Casualty Risk-Based Capital (E) Working Group of the Capital Adequacy (E) Task Force met Oct. 27, 2020. The following Working Group members participated: Tom Botsko, Chair, and Dale Bruggeman (OH); Richard Ford (AL); Mitchell Bronson, Rolf Kaumann and Eric Unger (CO); Wanchin Chou (CT); Robert Ridenour (FL); Judy Mottar (IL); Anna Krylova (NM); Sak-man Luk (NY); Miriam Fisk (TX); and Randy Milquet (WI).

1 Adopted the Report of the Catastrophe Risk (E) Subgroup

Mr. Chou said the Catastrophe Risk (E) Subgroup met Oct. 19 and took the following action: 1) adopted its Summer National Meeting minutes; 2) exposed proposal 2020-08-CR (Clarification to PR027 Interrogatories); 3) discussed the possibility of adding wildfire peril to the Rcat component; 4) discussed the internal catastrophe model evaluation process; and 5) discussed the additional internal and commercial models evaluation process. He stated that the Subgroup also met July 29 and took the following action: 1) adopted its Feb. 3 joint minutes with the Working Group; 2) heard a presentation from Karen Clark & Company (KCC) on its catastrophe model; 3) discussed the possibility of allowing additional third-party commercial vendor models; and 4) discussed the internal catastrophe model evaluation process.

Mr. Chou made a motion, seconded by Ms. Krylova, to adopt the report of the Catastrophe Risk (E) Subgroup (Attachment Five-A). The motion passed unanimously.

2. Adopted its Summer National Meeting Minutes

Mr. Chou made a motion, seconded by Ms. Krylova, to adopt the Working Group's July 30 minutes (Attachment Five-B). The motion passed unanimously.

2. Exposed Proposal 2020-11-CR (Remove Operational Risk Factor from Rcat)

Mr. Botsko said the operational risk is now separately addressed in the risk-based capital (RBC) formula as a stand-alone capital add-on. The purpose of this proposal is to remove the embedded 3% operational risk charge in the Rcat component to avoid double counting of the charge. Scott Williamson (Reinsurance Association of America—RAA) said the RAA supports this proposal. He also stated that the embedded operational risk is duplicative and is inadvertently being applied to the Rcat component.

The Working Group agreed to expose proposal 2020-11-CR for a 35-day public comment period ending Dec. 1.

3. Discussed Ref #2019-49: Retroactive Reinsurance Exception from the Statutory Accounting Principles (E) Working Group

Mr. Botsko said the Casualty Actuarial and Statistical (C) Task Force has organized a small group tasked with responding to the referral from the Statutory Accounting Principles (E) Working Group regarding Ref #2019-49: Retroactive Reinsurance Exceptions (Attachment Five-C) to clarify the accounting and reporting for retroactive reinsurance that meets the *Statement of Statutory Accounting Principles (SSAP) No. 62R—Property Casualty Reinsurance* exceptions to be accounted for as prospective reinsurance. He said the small group is receiving assistance from the Statutory Accounting Principles (E) Working Group staff. In addition, Mr. Botsko summarized an update by Gordon Hay (NE) at the last Casualty Actuarial and Statistical (C) Task Force meeting. It was stated that the small group is currently reviewing SSAP No. 62R holistically, with emphasis on retroactive agreements that receive prospective accounting treatment. It was also stated that the small group intends to expand SSAP No. 62R, clarifying Annual Statement, Schedule P expectations when retroactive agreements receive prospective accounting treatment. This work may imply some change to prospective reinsurance accounting prescriptions in SSAP No. 62R paragraphs 30–32 and 49–54 (cedants' accounting and credit taken) and/or paragraphs 42–48 (reinsurers' accounting).

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4. Discussed a Referral from the Restructuring Mechanisms (E) Subgroup

Mr. Botsko said a response from the Restructuring Mechanisms (E) Subgroup to request for extension was received earlier. He stated that the Subgroup requests a response by the 2021 Summer National Meeting to allow the Subgroup adequate time to review and incorporate the Working Group's response into its work product. Mr. Botsko also indicated that the Subgroup requests a short progress update at the 2021 Spring National Meeting. He said that the completion date for the Property and Casualty Risk-Based Capital (E) Working Group would need to be updated to the 2021 Summer National Meeting to accommodate the Subgroup's deadline. Mr. Milquet said he is concerned about who should be the one to identify whether a company is in runoff status or not. Mr. Williamson said he thinks state insurance regulators may consider using the Annual Statement Jurat page and the Schedule F to identify those companies. Mr. Chou said asking NAIC staff to provide data to assist the discussion will be a good starting point. Ralph Blanchard (Travelers) asked the Working Group to consider dividing the runoff companies into voluntary basis versus involuntary basis. Mr. Botsko said he believes that creating an ad hoc group to discuss this issue would speed up the entire process. The Working Group agreed with Mr. Botsko. He encouraged interested parties to join the ad hoc group so this project will be completed in time.

5. Discussed its 2020 Working Agenda

Mr. Botsko summarized the changes to the Working Group's 2020 working agenda: 1) removed "Evaluate the RBC impact on the modification of the installment fees and expenses reporting guidance" as the Ref #2019-40: Reporting of Installment Fees and Expenses was adopted by the Statutory Accounting Principles (E) Working Group on March 18; and 2) added "modify instructions to PR027 Interrogatories that clarify how insurers with no gross exposure to earthquake or hurricane should complete the interrogatories" and "remove the embedded 3% operational risk component contained in the reinsurance contingent credit risk factor of Reat" in the new items section. He stated that both items have been exposed for a 30- and 35-day comment period, respectively.

Mr. Chou made a motion, seconded by Mr. Luk, to adopt the Working Group's 2020 working agenda. The motion passed unanimously.

6. Discussed Line 1 Underwriting Risk Reserves and Premiums Methodology

Mr. Botsko said as the Working Group discussed during the Summer National Meeting, some state insurance regulators asked the Working Group to determine the impact to the industry RBC result if the weighted average approach calculation were used across all lines. He said some industry parties are concerned that using a weighted average approach could distort the industry experience adjustment if a large entity did a retroactive with prospective reinsurance treatment. He recommended the Working Group consider using the weighted average approach across all lines and monitoring the result closely on any material distortion. Mr. Botsko asked the American Academy of Actuaries (Academy) to determine the impact on line 4 by using the consistent approach with line 1 and share comments with the Working Group during its upcoming meeting. Lauren Cavanaugh (Academy) recommended the Working Group consider using other alternatives, such as filtering based on the company sizes or pools. She said the Academy will be able to provide the necessary information to accomplish this project.

7. Discussed Other Matters

Mr. Botsko said the Working Group is still reviewing the possibility of adding an equivalent reinsurer designation column in the *NAIC Listing of Companies*. Currently, the NAIC Legal Division and the Securities Valuation Office (SVO) are investigating different issues regarding this matter. Thoughts and findings will be provided during the Working Group's upcoming meetings.

Having no further business, the Property and Casualty Risk-Based Capital (E) Working Group adjourned.

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