



NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

MEMORANDUM

TO: Financial Examiners and Other State Insurance Regulators

FROM: Philip Barlow, Chair of the Life Risk-Based Capital (E) Working Group

DATE: Dec. 16, 2021

RE: Interpretation of the 2021 Life Risk-Based Capital (RBC) Results in Light of the 2021 Bond Factor Changes

Purpose and Intended Audience for this Document

This document is intended to assist financial examiners and other state insurance regulators as they review the results of 2021 RBC calculations for life insurers in light of the 2021 bond factor changes. There were also changes related to longevity risk, real estate and reinsurance that state insurance regulators may want to consider but this document is specifically addressing the bond factor changes as they have the most potential to impact the action level, including through the trend test.

More detailed information about this topic is contained in the minutes of the Life Risk-Based Capital (E) Working Group, and related documents are included on the websites for both the Working Group and the Capital Adequacy (E) Task Force. The changes to the Life RBC formula factors for bonds were adopted by the Working Group on June 11 and by the Task Force on June 30.

Executive Summary

The work to update the RBC charges applied to bonds has been ongoing for several years and reflects the efforts of many participants. The Working Group appreciates the considerable work of the American Academy of Actuaries (Academy) on this project, as well as the work done by Moody's Analytics on behalf of the American Council of Life Insurers (ACLI). The Working Group discussed the proposals presented during numerous conference calls over the past year. The Working Group also reviewed estimates of the impact the proposals would have had on the RBC results for life insurers' year-end 2020 filings. The Working Group concluded that both proposals presented a sound and appropriate update to the factors applied to bonds, and it ultimately adopted the proposal presented by Moody's.

How should the effects of the change in bond factors be factored into the interpretation of RBC results?

The estimated impact of the change in bond factors the Working Group reviewed on individual companies and the life insurance industry in aggregate indicated less than a 2% increase in the authorized control level (ACL) RBC on an aggregate basis. However, a small

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number of companies experienced a much larger impact when the 2019 results were recalculated with the new factors. The Life RBC Trend Test (LR035) will be affected by the change in bond factors and may be an area where this change is most evident. The Trend Test calculates a margin, which is the excess of total adjusted capital (TAC) over ACL RBC, for each of the current year, prior year, and third prior year. To the extent that the current year margin is lower than the prior year or third prior year margin, regulatory action may be indicated.

For the 2021 Trend Test, the margin for 2021 is compared to the margins for 2020 and 2018. As noted, a company's ACL RBC is expected to be increased for 2021 compared to prior years. The changes to ACL RBC due to the change in bond factors may cause some companies to trigger the Trend Test for 2021, solely because of the change in bond factors.

If state insurance regulators find that a life insurer has triggered the Trend Test, triggers an Action Level for 2021, or has a significant decline in its RBC ratio from 2020 to 2021, they could have additional discussions with the company and request additional calculations. It is likely that companies would have done some analysis of significant changes in ACL RBC, and that analysis could be shared with state insurance regulators.