NAIC National Association of Insurance Commissioners
& The Center for Insurance Policy and Research

TO: Reinsurance (E) Task Force

FROM: NAIC Staff

RE: Comparison of *Term and Universal Life Insurance Reserve Financing Model Regulation* (#787) and *Actuarial Guideline XLVIII*

DATE: February 5, 2020

Executive Summary

At the 2019 Fall National Meeting, the Financial Regulation Standards and Accreditation (F) Committee adopted the *Term and Universal Life Insurance Reserve Financing Model Regulation* (#787) as an accreditation standard. The NAIC Executive (EX) Committee and Plenary are expected to consider it for final adoption at the Spring National Meeting, to be effective Sept. 1, 2022. On its conference call on Jan. 29, the Reinsurance (E) Task Force discussed whether compliance with *Actuarial Guideline XLVIII* (AG 48) should be considered "substantially similar" to Model #787 for accreditation purposes. Acting Chair John Rehagen (MO) directed NAIC staff to distribute a memorandum comparing the significant differences between AG 48 and Model #787 for a 21-day public comment period requesting comments on whether compliance with AG 48 should be considered substantially similar to Model #787.

2017 Recommendation on Accreditation

In its memorandum dated August 24, 2017, the Reinsurance Task Force recommended that "a state's adoption of AG 48 will serve to satisfy this accreditation standard until such time that the state adopts the significant elements of Model #787." (Attachment A). This recommendation was based on an expedited effective date for the accreditation standard of January 1, 2020. The Task Force recognized that " meeting the expedited date may not be feasible for some states in instances due, in whole or part, to other legislative priorities of the states. It is the recommendation of the Task Force that, in such cases, a state's compliance with AG 48 should be considered as satisfactory to the Financial Regulation Standards and Accreditation (F) Committee as substantial compliance with Model #787."

At that time the Committee deferred its consideration of Model #787 as an accreditation standard due to concerns expressed with respect to the impending *Bilateral Agreement Between the United States of America and the European Union on Prudential Measures Regarding Insurance and Reinsurance* (Covered Agreement), which was signed on September 22, 2017. In 2017 AG 48 was amended "to redraft AG 48 to make it as consistent as possible with the provisions of Model #787."

Comparison of Model #787 and AG 48

The primary difference between AG 48 and Model #787 are the consequences to an insurer if the requirements of either are not met. Paragraph 6B(1) of AG 48 (Attachment B) provides, as follows:

B. Qualified Actuarial Opinion; Remediation

(1) **The appointed actuary of the ceding insurer performing the analysis required by Section 6A above must issue a qualified actuarial opinion** as described in Section 6.D. of the AOMR or Section 3A(10) of VM-30 of the *Valuation Manual*, as applicable, unless:

(a) The requirements of Section 6A(1) and 6(A)(2) were fully satisfied as of the valuation date as to such reinsurance treaty; or

(b) Any deficiency has been eliminated before the due date of the Annual Statement to which the valuation date relates through the addition of Primary Security and/or Other Security, as the case may be, in such amount and in such form as would have caused the requirements of Section 6A(1) and 6A(2) to be fully satisfied as of the valuation date; or

(c) The ceding insurer has established a liability equal to the excess of the credit for reinsurance taken over the amount of Primary Security actually held pursuant to Section 6A(1).

[Emphasis Added]. A Drafting Note to this paragraph provides that the "remediation option set forth in Section 6B(1)(c) mirrors that set forth in Model #787." In addition, the following proposals related to the XXX/AXXX Reinsurance Framework were adopted by the Capital Adequacy (E) Task Force on its June 30, 2015, conference call:

1. 2014-33-L-Mod Qualified Actuarial Opinion – This proposal modifies the interrogatory on LR027 Interest Rate Risk and Market Risk. This interrogatory allows companies submitting an unqualified opinion to receive a one-third reduction in the factors. It was modified to prevent an opinion qualified solely due to the direction in AG 48, which is line of business specific, from impacting all lines of business.

2. 2014-35b-L-Mod Primary Securities Shortfall – This proposal adds a new schedule showing the primary security shortfall by individual cession. The cumulative amount of primary security shortfall, with no offset for any surpluses, is then taken as a dollar-for-dollar addition to the reporting company's Authorized Control Level.

3. 2014-42-L-Mod RBC Shortfall – This proposal adds a new schedule which shows the RBC calculation by individual captive. The cumulative amount of RBC shortfalls, with no offset for any surpluses, is then taken as a dollar-for-dollar reduction to the reporting company's Total Adjusted Capital.

In summary, the Qualified Actuarial Opinion under paragraph 1-above does not constitute an RBC penalty in and of itself, but is a required element to trigger the RBC penalty under paragraph 2 and is applicable only with respect to AG 48. The RBC penalty under paragraph 3 is applicable to both noncompliance with AG 48 and Model #787. Section 7B of Model #787 then provides the following additional consequences for failure to follow its requirements:

B. Requirements at Inception Date and on an On-going Basis; Remediation

(1) The requirements of Section 7A must be satisfied as of the date that risks under Covered Policies are ceded (if such date is on or after the effective date of this regulation) and on an ongoing basis thereafter. Under no circumstances shall a ceding insurer take or consent to any action or series of actions that would result in a deficiency under Section 7A(3) or 7A(4) with respect to any reinsurance treaty under which Covered Policies have been ceded, and in the event that a ceding insurer becomes aware at any time that such a deficiency exists, it shall use its best efforts to arrange for the deficiency to be eliminated as expeditiously as possible.

(2) Prior to the due date of each Quarterly or Annual Statement, each life insurance company that has ceded reinsurance within the scope of Section 3 shall perform an analysis, on a treaty-by-treaty basis, to determine, as to each reinsurance treaty under which Covered Policies have been ceded, whether as of the end of the immediately preceding calendar quarter (the valuation date) the requirements of Sections 7A(3) and 7A(4) were satisfied. **The ceding insurer shall establish a liability equal to the excess of the credit for reinsurance taken over the amount of Primary Security actually held pursuant to Section 7A(3),** unless either:

(a) The requirements of Section 7A(3) and 7A(4) were fully satisfied as of the valuation date as to such reinsurance treaty; or

(b) Any deficiency has been eliminated before the due date of the Quarterly or Annual Statement to which the valuation date relates through the addition of Primary Security and/or Other Security, as the case may be, in such amount and in such form as would have caused the requirements of Section 7A(3) and 7A(4) to be fully satisfied as of the valuation date.

[Emphasis added]. Finally, Paragraph 8 of AG 48 provides that it will sunset when a state adopts a regulation substantially similar to Model #787, but will continue to apply only with respect to the limited number of states in which their version of Model #787 applies prospectively only.

Substantially Similar

The NAIC Financial Standards and Accreditation Program provides the following definition of "substantially similar":

> For those standards included in the Part A: Laws and Regulations Standards where the term "substantially similar" is included, a state must have a law, regulation, administrative practice or a combination of the above which addresses the significant elements included in the NAIC model laws or regulations… It is NOT required that states adopt every "significant" element in the interim annual review form by law or regulation. Instead, it is required that the state demonstrate that the law, regulation, administrative practice or a combination of the above enforced by a state insurance department results in solvency regulation that is similar in force and no less effective than the NAIC model law or regulation for that standard.