February 26, 2019

Via Electronic Delivery

Director Chlora Lindley-Myers
Missouri Department of Commerce & Insurance
P.O. Box 690
Jefferson City, MO 65102

Attention: John Rehagen, Jake Stultz and Dan Schelp

Re: Reinsurance (E) Task Force Exposure Comparing Model # 787 and AG 48

Director Lindley-Myers:

New York Life Insurance Company and The Northwestern Mutual Insurance Company offer the following comments on the February 5, 2020 memorandum (the "Memo") from NAIC Staff to the Reinsurance Task Force (the "Task Force") entitled "Comparison of *Term and Universal Life Insurance Reserve Financing Model Regulation (#787) and Actuarial Guideline XLVIII*". Our companies have engaged extensively with the NAIC and the Task Force over the years as it considered the recommendations made in the Rector Report and subsequently developed both AG 48 and Model 787.

Background of Accreditation Discussions

In 2017, we submitted several joint comment letters supporting the NAIC's efforts to make Model 787 an accreditation standard. We continue to believe that taking this step will strengthen the state-based system of insurance regulation, ensuring the consistent adoption of the NAIC's framework for regulating the solvency of XXX and AXXX life insurer captives.

At that time, the NAIC was contemplating making Model 787 an accreditation standard on an expedited basis so that it would become effective concurrently with the nation-wide transition to principles-based reserving. However, at the 2017 Fall National Meeting, the Financial Regulation Standards and Accreditation (F) Committee ("F Committee"), while strongly supporting moving forward, agreed to defer this recommendation in light of the then-pending changes to the Credit for Reinsurance Model Law and Regulation (respectively, "Models 785 and 786") to reflect the US-EU Covered Agreement. This step as articulated by F Committee members was intended to prevent state legislatures from needing to reopen the reinsurance-related provisions of the insurance code multiple times in a short period. It was the F Committee's clear intention that accreditation standards for Models 785, 786 and 787 would ultimately proceed alongside one another.

In the years since this decision, the NAIC has completed its revisions to Models 785 and 786 and a few states have moved forward with adopting Model 787, notwithstanding the absence of an accreditation standard. At the 2019 Fall National Meeting, the F Committee adopted a recommendation to make Model 787 an accreditation standard on an expedited basis, which would move in parallel with the accreditation standards for Models 785 and 786. This adoption

was consistent with the discussions in 2017, which focused not on whether Model 787 should be an accreditation standard, but rather the timing for the standard's effective date.

<u>Reliance on AG 48 for Accreditation Purposes</u>

The Memo explores whether states could, for accreditation purposes, rely on ongoing enforcement of AG 48 as a "substantially similar" provision to Model 787. While the definition of "substantially similar" is seemingly broad enough to encompass this position, there are meaningful differences between Model 787 and AG 48, including both the penalty provisions and the reliance upon the actuarial opinion.

The Penalty Provisions in AG 48 and Model 787 Differ Significantly

As noted in the Memo, the primary difference between Model 787 and AG 48 is the consequences to an insurer if an insurer fails to hold a sufficient level of Primary Security. Model 787 contains a penalty provision specifically aimed at deterring behavior that contravenes its positions: the loss of reinsurance credit for improperly reserved transactions.

AG 48's penalty provision, in contrast, is indirect. In the event of a deficiency in Primary Security, insurers are subject to an RBC penalty commensurate with the amount of the shortfall. As you know, RBC was designed as an early warning system for the identification of weakly capitalized companies. It was never intended to evaluate well-capitalized companies. Ultimately, while AG 48's penalty could have a meaningful effect on RBC ratios, reliance on such ratios to bring regulatory attention to Primary Security shortfalls or otherwise deter non-compliance with AG 48's requirements is inconsistent with the purposes for which RBC was developed.

The inclusion of an RBC penalty in AG 48 reflects several factors arising from the intensive negotiations regarding the implementation of the Rector Framework, including an acknowledgment that additional penalties could not be included in an Actuarial Guideline, and that AG 48 itself would ultimately sunset once Model 787 was adopted. A similar logic undergirds AG 48's reliance on the issuance of a qualified actuarial opinion as a trigger for these penalty provisions. Generally speaking, an actuarial opinion is designed to be an independent actuarial assessment of overall reserve adequacy, and is not intended as a compliance mechanism for a particular regulatory requirement. Indeed, the Academy of Actuaries, among others, expressed serious concerns with AG 48 being the permanent, or even the temporary, solution. However, all parties agreed to stand down on the issue when it became clear that AG 48 would be used in limited, short-term circumstances.

Regulators Intended AG 48 to be Temporary Solution

At the time that the NAIC first considered making Model 787 an accreditation standard, it was acknowledged that the expedited time frame could present challenges for some states. The solution to this was not to keep AG 48 in place forever and for all XXX and AXXX business, but rather to develop some exceptions for specific circumstances.

In states that were unable to comply with the expedited time frame, the Task Force acknowledged that compliance with AG 48 would be satisfactory for accreditation purposes. The Task Force's acknowledgment did not envision, however, that AG 48 would remain in place in those states indefinitely.

This is consistent with the introductory language of AG 48 itself, which notes that AG 48 was adopted to "quickly set minimum standards" for XXX/AXXX reinsurance transactions. The introductory language also contemplates that AG 48 would eventually sunset in most states as Model 787 was adopted to replace it. The only caveat to that expectation is a recognition that "in a small number of states," Model 787 would be adopted on a prospective basis (meaning it would only apply to policies issued after the date that the state adopted the model). In that minority of cases, AG 48 would remain in effect (*along with Model 787*) for the subset of policies issued after January 1, 2015 but before a state adopted the Model.

Conclusion

Finally, we would note that when the F Committee agreed in 2017 to delay the adoption of an accreditation standard for Model 787, they were responding to regulators' legitimate concerns that they would need to approach their legislatures several times in quick succession regarding revisions to Model 785. There was no discussion at that time about *never* approaching legislatures to obtain the requisite authority to issue Model 787. If regulators remain concerned with making repeated requests on similar topics then we would urge them to include both the changes responsive to the US-EU Covered Agreement and the authorizing language in their legislative packages. If regulators remain concerned with completing the revisions to Model 785, 786 and 787 on an expedited basis then we would suggest that a preferable solution is to extend the time frame for making Model 787 an accreditation standard rather than to allow states to rely on AG 48 in perpetuity for all XXX/AXXX business.

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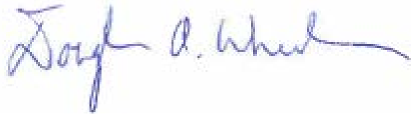
We are grateful for your time and attention to our comments. If you would like to discuss this letter with us, please let us know.

Sincerely,



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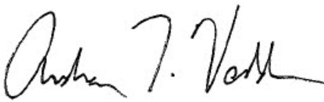

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