



NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

MEMORANDUM

TO: David Smith (VA) and Doug Stolte (VA), Co-Chairs of the Restructuring Mechanisms (E) Subgroup
Judith L. French (OH), Chair of the Capital Adequacy (E) Task Force

FROM: Tom Botsko (OH), Chair of the Property and Casualty Risk-Based Capital (E) Working Group

DATE: Oct. 25, 2021

RE: Response to Request for Input Regarding Runoff Companies

The Property and Casualty Risk-Based Capital (E) Working Group formed a small ad hoc group to discuss this topic and try to determine the best course of action. The Restructuring Mechanisms (E) Subgroup requested that the Working Group take the lead in addressing the charge to “consider the need to make changes to the RBC formula to better assess the minimum surplus requirements for companies in runoff. “

After several discussions about what adjustments should be made to the risk-based capital (RBC) formula, the ad hoc group concluded that the best course of action is to monitor these companies through the state analysis and exam team functions. The characteristics and financial conditions of these runoff companies are very diverse, and it would be difficult to incorporate these varied characteristics into one adjusted formula. Many international countries monitor these companies through the analysis and exam processes and do not have a separate RBC formula.

Of the 2020 RBC filers, we identified 111 companies out of 2,477 that have the characteristics of a runoff company. Most of these companies have an RBC ratio greater than 300%. Five are below 200%.

During a series of discussions, the ad hoc group agreed that a runoff company, voluntary or involuntary, should include the following characteristics: 1) no renewing of policies for at least 12 months; 2) no new direct or new assumed business; and 3) no additional runoff blocks of business. In addition, the amount of renewal premium to reserves has also been identified as a characteristic of these types of companies when this ratio is de minimis.

The ad hoc group also recommends that a general and RBC interrogatory be added for the purpose of identifying a runoff company. The domiciliary state shall have the ability to verify the interrogatory response during the annual company financial analysis process.

As the ad hoc group considered various types and conditions of runoff companies, it became apparent that while many of these companies share the characteristic of very long tail liabilities, there are other characteristics of these companies that are so diverse that it made it difficult to summarize them into their own RBC formula.

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The ad hoc group reviewed several international perspectives of runoff companies. The international treatment of runoff companies is handled through the Analysis and Exam Teams. The ad hoc group agrees that a similar treatment of runoff companies is warranted.

The ad hoc group has some recommendations for the Working Group regarding the RBC instructions, specifically to the runoff companies. These include the following:

- Remove the Trend Test from the RBC calculation. These are runoff companies, and the possible retrospective premium should not complicate the already diverse situation.
- Remove the charge for premium growth if the company is no longer writing business.
- Remove R_{cat} from the formula. Because one of the characteristics of a runoff company is to not have written any new business for at least 12 months, we believe this short-term liability risk is not warranted.

As the ad hoc group shares its findings with the other two RBC working groups, we expect to hear other perspectives regarding the unique conditions of runoff companies from the Life Risk-Based Capital (E) Working Group and the Health Risk-Based Capital (E) Working Group.

Please contact Eva Yeung, NAIC staff support for the Property and Casualty Risk-Based Capital (E) Working Group, at eyeung@naic.org with any questions.

Cc: Robin Marcotte; Dan Daveline; Jane Barr; Eva Yeung