**Life Actuarial (A) Task Force/ Health Actuarial (B) Task Force**

**Amendment Proposal Form\***

1. Identify yourself, your affiliation and a very brief description (title) of the issue.

**Identification:**

Richard Harris, Vice President & US Appointed Actuary, John Hancock Life Insurance Company (U.S.A.);

Ross Zilber, Vice President & Deputy Appointed Actuary, John Hancock Life Insurance Company (U.S.A.);

Nik Godon, Vice President & Chief Actuary, Transamerica Life Insurance Company;

Art Wallace, Chief Actuary, U.S. Businesses, Prudential Financial;

**Title of the Issue:**

VM-20 Treatment for YRT Reinsurance Premiums in Modeled Reserves

2. Identify the document, including the date if the document is “released for comment,” and the location in the document where the amendment is proposed:

VM-20 Section 8.C

January 1, 2019 NAIC Valuation Manual

3. Show what changes are needed by providing a red-line version of the original verbiage with deletions and identify the verbiage to be deleted, inserted or changed by providing a red-line (turn on “track changes” in Word®) version of the verbiage. (You may do this through an attachment.)

See attached.

4. State the reason for the proposed amendment? (You may do this through an attachment.)

Currently, VM-20 does not specify how YRT reinsurance should be incorporated into the reserve calculations for the DR and SR. The industry is searching for guidance on how to apply YRT reinsurance, and this APF offers direction on the appropriate way to incorporate YRT reinsurance in the modeled reserves.

The NPR YRT reinsurance credit is set at ½\*Cx. The post-reinsurance reserves are floored at Net NPR which is using a prescriptive ½\*Cx. Since NPR is acting as the modeled reserve floor, a principles-based solution makes sense when modeling DR or SR. Additionally, using a principles-based approach allows the actuary to accurately reflect the details of the reinsurance agreement under consideration.

This proposal uses a principles-based approach along with prescriptive margins on YRT reinsurance rates to ensure that assumptions that are too aggressive are not used in calculating the modeled reserve. The prescriptive margins for YRT reinsurance rates are the exact same margins that are prescribed for mortality. The proposal is similar to approach #6 from the “Academy Discussion Paper on Need for VM-20 Guidance for YRT Reinsurance Premiums.”

This APF determines prudent estimate YRT reinsurance rates in an analogous manner to how prudent estimate mortality rates are established in the DR/SR. The current YRT reinsurance rates would be increased by a margin that was equal to the ratio of DR/SR mortality (including prescribed margins) to the company’s anticipated mortality assumption. This approach harmonizes the treatment of mortality and YRT reinsurance in the DR/SR using a principles-based approach which is the intent of the DR/SR.

\* This form is not intended for minor corrections, such as formatting, grammar, cross–references or spelling. Those types of changes do not require action by the entire group and may be submitted via letter or email to the NAIC staff support person for the NAIC group where the document originated.

NAIC Staff Comments:

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| --- | --- | --- | --- |
| **Dates:** Received | Reviewed by Staff | Distributed | Considered |
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| **Notes:** | | | |

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**VM-20 Section 8.C**

(The edit proposed below inserts a new Sec. 8.C.8 and renumbers the following sections accordingly)

7. The company shall assume that the counterparties to a reinsurance agreement are knowledgeable about the contingencies involved in the agreement and likely to exercise the terms of the agreement to their respective advantage, taking into account the context of the agreement in the entire economic relationship between the parties. In setting assumptions for the NGE in reinsurance cash flows, the company shall include, but not be limited to, the following:

a. The usual and customary practices associated with such agreements.

b. Past practices by the parties concerning the changing of terms, in an economic environment similar to that projected.

c. Any limits placed upon either party’s ability to exercise contractual options in the reinsurance agreement.

d. The ability of the direct-writing company to modify the terms of its policies in response to changes in reinsurance terms.

e. Actions that might be taken by a party if the counterparty is in financial difficulty.

1. When projecting non-guaranteed future reinsurance cashflows, the company shall use prudent estimate reinsurance premiums in projecting the cashflows. The company shall project reinsurance cashflows pursuant to all provisions within a reinsurance agreement and shall determine the prudent estimate reinsurance premiums using the following procedure:
   1. Use the reinsurance rates and provisions from the relevant reinsurance agreement as the anticipated experience reinsurance assumption.
   2. Determine the prescribed reinsurance margins as the ratio of prudent estimate mortality as provided in Section 9.C.1 to company experience mortality as provided in Section 9.C.2.
   3. Reinsurance margins may be modified if in the company’s judgment the prescribed margins do not appropriately reflect the expected reinsurance experience. In cases where the reinsurance margins are modified, the modifications must not result in reinsurance margins that are lower than those prescribed in Section 8.C.8.b without approval by the commissioner.

**Guidance Note:** Examples of reasons to modify the reinsurance margins include, but are not limited to, counterparty default concerns, reinsurance contract language that contains particularly restrictive or permissive provisions regarding reinsurance rate increases and potential recapture of the reinsured business.

9. The company shall account for any actions that the ceding company and, if different, the direct-writing company have taken or are likely to take that could affect the expected cash flows of the reinsured business in determining assumptions for the modeled reserve.

[Renumber following sections accordingly]