2020 Summer National Meeting

LIFE RISK-BASED CAPITAL (E) WORKING GROUP
Thursday, July 30, 2020
3:00 – 4:00 p.m. ET / 2:00 – 3:00 p.m. CT / 1:00 – 2:00 p.m. MT / 12:00 p.m. – 1:00 p.m. PT
WebEx Call-in

ROLL CALL

Philip Barlow, Chair District of Columbia John Robinson Minnesota
Steve Ostlund Alabama William Leung Missouri
Perry Kupferman California Rhonda Ahrens Nebraska
Deborah Batista Colorado Seong-min Eom New Jersey
Wanchin Chou Connecticut Bill Carnello New York
Gilbert Moreau Florida Andy Schallhorn Oklahoma
Vincent Tsang Illinois Mike Boerner Texas
Tomasz Serbinowski Utah

NAIC Support Staff: Dave Fleming

AGENDA

1. Consider Adoption of its July 10, June 30, June 11 and Spring National Meeting Minutes—Philip Barlow (DC) Attachments A - D

2. Consider Adoption of the Life Risk-Based Capital (RBC) Newsletter—Philip Barlow (DC) Attachment E

3. Discuss 2019 RBC Statistics—Philip Barlow (DC) Attachment F

4. Continue Discussion of Industry Request for RBC Mortgage Reporting Guidance—Philip Barlow (DC) Attachment G

5. Discuss Working Agenda—Philip Barlow (DC) Attachment H

6. Discuss Upcoming Conference Calls—Philip Barlow (DC)

7. Discuss Any Other Matters Brought Before the Working Group—Philip Barlow (DC)

8. Adjournment

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The following Working Group members participated: Philip Barlow, Chair (DC); Steve Ostlund (AL); Perry Kupferman (CA); Deborah Batista (CO); Wanchin Chou (CT); Gilbert Moreau (FL); John Robinson (MN); William Leung (MO); Rhonda Ahrens (NE); Seong-min Eom (NJ); Bill Carmello (NY); Andrew Schallhorn (OK); Mike Boerner (TX); and Tomasz Serbinowski (UT).

1. Discussed an Industry Request for RBC Mortgage Reporting Guidance

Mr. Barlow said two of the four items the industry is requesting risk-based capital (RBC) reporting guidance on were addressed on the June 30 conference call with the Working Group adopting the requested guidance for construction loans and origination date, valuation date, property value, and 90 days past due. He said this call is to address the two remaining items, net operating income (NOI) and contemporaneous property values. With respect to the remaining two items, he said there were some concerns that the requested guidance seems to completely discount any potential impact on commercial mortgages of the current pandemic. He said the Mortgage Bankers Association (MBA) and the American Council of Life Insurers (ACLI) have provided updated recommendations (Attachments A and B) based on the feedback from the last call. John Waldeck (Pacific Life Insurance) said he is representing the MBA and the ACLI.

With respect to NOI, he said the first proposal suggested using the greater of 2020 or 2019 NOIs. He said they went back to see what would be more justifiable and have updated the proposal to use the greater of 2020 or 85% of 2019 NOI, and he presented the rationale supporting this revision. Mr. Barlow suggested addressing the two issues one at a time. He said the NOI guidance would not affect the 2020 RBC calculation, but it would affect the three subsequent years. He suggested that if the Working Group is inclined to support this proposal as is or with some modification, it should indicate this but consider revising the worksheet for 2021. Mr. Robinson noted the existing weighted average for NOI, and he is inclined to let it work in the way it was intended. He said he is in favor of gathering the information for the 2020 NOI and considering revisiting the construct for 2021 when they have information to base the decision on. Mr. Carmello asked about the timing requirements for getting the information and making the changes. Mr. Barlow said he believes these would be instructional changes subject to the June 30 deadline. Dave Fleming (NAIC) said changes would need to be exposed for comment by the end of April. Mr. Barlow said this is not information that will be captured in an NAIC filing, and he believes the Working Group would need to look to industry to provide that information. Mr. Waldeck indicated that the timeframe for getting this information for individual properties for the 2020 filings would be around June or July, which would be outside of the Working Group’s timeline. Mr. Barlow asked if there is information that could be obtained that could serve as a proxy in order for the Working Group make a more informed decision. Mr. Waldeck indicated that there may be some potential data points that could be used. He reminded the Working Group that part of the reason for this request is that the decision on the treatment of 2020 NOI will have an impact on the desire to place new investments this year, and that is why guidance now is important. He said this guidance is also important to companies in order to plan for their capital needs. Mr. Robinson made a motion, seconded by Ms. Eom, to defer the request subject to more information being provided. Mr. Waldeck said he would appreciate reconsideration of rejecting the proposal, and he reiterated the importance of having the Working Group address this now. He said the likelihood is that the additional information on the 2020 NOI might come late in the second quarter next year, which is past the time the Working Group would need to address it.

So industry has some indication on how to move forward, Mike Monahan (ACLI) suggested adopting the change for 2021, with it to be reconsidered for 2022 and 2023 as additional information becomes available. Mr. Carmello suggested that the Working Group indicate that it would reconsider before the end of this year. Mr. Barlow asked if industry could provide information that would influence the Working Group’s decision by the end of the year. Mr. Waldeck said one concern is decisions about new investments being made without clarity on the RBC considerations. He said another concern is that the 2020 NOI is not impactful to the 2020 RBC calculation but is for planning companies will do for the following year and the investments they make based on the 2020 NOI. Mr. Robinson and Ms. Eom accepted a friendly amendment to the motion to reconsider in time to make changes for next year. California, Colorado, Connecticut, Florida, Minnesota, Missouri and New Jersey voted in favor of the motion with Nebraska, New York, Oklahoma, Texas and Utah voting against the motion. Alabama abstained. The motion passed.

Mr. Waldeck said the requested guidance on contemporaneous property values affects only the 2020 year-end RBC calculation, and it is designed solely to adjust out any shock effect that could be in the National Council of Real Estate Investment Fiduciaries (NCREIF) price index. He said the proposal is to use the average of the 2019 and 2020 NCREIF values. If there is a decline, he said this would reflect only half of that decline, and it reflects the state insurance regulator concerns about totally...
discounting the decline. Mr. Carmello made a motion, seconded by Ms. Ahrens, to adopt the requested guidance on contemporaneous property values. The motion passed with Minnesota voting against the motion.

Having no further business, the Life Risk-Based Capital (E) Working Group adjourned.
The Life Risk-Based Capital (E) Working Group of the Capital Adequacy (E) Task Force met via conference call June 30, 2020. The following Working Group members participated: Philip Barlow, Chair (DC); Perry Kupferman (CA); Manuel Hidalgo (CT); Gilbert Moreau (FL); John Robinson (MN); Rhonda Ahrens (NE); Seong-min Eom (NJ); Bill Carmello (NY); Andrew Schallhorn (OK); Mike Boerner (TX); and Tomasz Serbinowski (UT).

1. Discussed an Industry Request for Risk-Based Capital Mortgage Reporting Guidance

Mr. Barlow said the Working Group received a request from industry for risk-based capital (RBC) commercial reporting guidance (Attachment 1). He said it is too late to make changes to the 2020 RBC instructions and what the Working Group will be considering is whether to provide some guidance to companies on completing the commercial mortgage worksheets in the life RBC formula for this yearend due to the impact of the current pandemic. John Waldeck (Pacific Life Insurance) said he is representing the Mortgage Banking Association and the American council of Life Insurers (ACLI). He said the request is to deal with the year 2020 but that it does impact more than just the 2020 yearend RBC calculation. With respect to construction loans and origination date, valuation date, property value, and 90 days past due, he said the requested guidance is to extend guidance provided by the Financial Condition (E) Committee until December 31 which, while most companies typically calculate RBC on a quarterly basis, is the period for which most companies will be submitting RBC filings.

With respect to the requested guidance on net operating income (NOI), Mr. Waldeck said the calculation for 2020 is going to be hampered by the fact that there was a long-term closure the economy had that impacted, in terms of the deferment of rent, on many of the commercial real estate properties held by insurers. He said the NOI for 2020 is used in the 2021, 2022 and 2023 RBC calculations done by insurers and this is used in making new loans for 2020 as well as RBC needs going forward so they are asking for the requested guidance at this time in order to understand the RBC impact in that process. He said the assumption is that the NOI is reflective of how the property operates and, unfortunately, during the COVID-19 closures the properties are not operating anywhere near a normal situation. Many of these were doing very well or exceeding prior year expectations but, with the closures, he said most of 2020 is going to be impacted. He said the request is to use the greater of the 2019 or 2020 NOI in the calculation as a proxy for how the property could have performed in 2020 absent the COVID-19 issue. Mr. Barlow said it seemed like the implication of making that change is that the current situation had zero impact on the riskiness of the underlying commercial mortgages. Mr. Waldeck said it is not that COVID-19 had no impact but that the 2020 statistics will not reflect that riskiness if the properties were allowed to be open and operating. While some commercial mortgages will revert to normal after the current situation, Mr. Barlow expressed concern that others will not and that those lingering impacts will not be reflected in the RBC calculation. Mr. Waldeck said that is accurate in that the components of the previous year’s NOI are weighted.

With respect to the requested guidance on contemporaneous property values, Mr. Waldeck said the two main statistics used in the RBC calculation are the debt coverage ratio (DCR), which is impacted by the NOI, and the loan-to-value (LTV) and this is impacted by property value. This takes the origination value and brings it forward to a current value by use of the NCREIF price index. Mr. Waldeck said the concern is that this will be impacted in a similar fashion as the NOI by COVID-19 in that this component of LTV will driven down and cause an RBC change. He said the requested guidance is to have these values held at the 2019 yearend NCREIF values for RBC calculations through 2020 yearend but revert back to the current NCREIF values with the first quarter 2021 calculation. He said this change would impact only the 2020 RBC calculation.

Mr. Barlow asked if, assuming the pandemic does not continue past 2020, the request for NOI guidance will affect 2021 through 2023 but will not affect 2020 yearend RBC calculations while the requested guidance for contemporaneous property values, construction loans and the origination date, valuation date, property value, and 90 days past due will affect the 2020 RBC calculation but not 2021 through 2023. Mr. Waldeck said that is correct and noted that what all four requests share is they are each dealing with the impact that occurs in 2020. Mr. Barlow asked if, similar to the concern he expressed on NOI, the request on contemporaneous property values would effectively treat the calculation as if the current situation had zero impact on the riskiness of the mortgages. Mr. Waldeck said that is correct but noted that none of these conditions really change the fact that, on an accounting basis, they are required to have each transaction as more than a short-term impact where other than temporary impairments would be addressed through the accounting guidance in a separate manner.
While acknowledging that the impact is not going to be uniform on commercial mortgages and some will come through fine, Mr. Barlow reiterated his concern that some are less likely to and said he is concerned with modifying the RBC calculation to ignore the impact of the current pandemic on the ultimate riskiness of commercial mortgages. Mr. Hidalgo he is also hesitant and suggested, if the Working Group is going to make a change, using an average of the values as opposed to just using the 2019 values. Ms. Ahrens said 2020 may be an extreme measure and using 2019 values may be a more realistic indicator of the true behavior. She said some averaging may be better and suggested this is why there is a three-year average used in the NOI calculation. She said the purpose of having a measurement of required capital is for cases like the current situation and, in this scenario, is it going to be a requirement to increase that measure, in effect, doubling down by increasing the denominator in the RBC calculation while the numerator is already impacted. Mr. Barlow said RBC does not work like the asset valuation reserve (AVR) where it is built up and released to help with a bad situation but is a snapshot of the risk of a company at year end and determining how much capital is needed. When bad situations occur, he said not only is the reported capital impacted but by the nature of the RBC calculation the riskiness increases and puts an additional element into the requirement.

Mr. Barlow suggested continuing the discussion on the request with respect to the NOI and contemporaneous property values on the July 10 conference call. With respect to the requested guidance on construction loans and the requested guidance for the origination date, valuation date, property value, and 90 days past due, Mr. Barlow said he has no issue with these and is comfortable with continuing the guidance provided by the Financial Condition (E) Committee through December 31 for use in the 2020 RBC calculation. Mr. Boerner made a motion to continue the guidance provided by the Financial Condition (E) Committee through December 31 as it relates to construction loans and the origination date, valuation date, property value, and 90 days past due. Mr. Carmello seconded the motion which passed unanimously.

Having no further business, the Life Risk-Based Capital (E) Working Group adjourned.

W:\National Meetings\2020\Summer\TF\CapAdequacy\LifeRBC\6_30_20 Call
The Life Risk-Based Capital (E) Working Group of the Capital Adequacy (E) Task Force met via conference call June 11, 2020. The following Working Group members participated: Philip Barlow, Chair (DC); Steve Ostlund (AL); Perry Kupferman (CA); Deborah Batista (CO); Wanchin Chou (CT); Carolyn Morgan (FL); Vincent Tsang (IL); John Robinson (MN); William Leung (MO); Rhonda Ahrens (NE); Seong-min Eom (NJ); Bill Carmello (NY); Andrew Schallhorn (OK); Mike Boerner (TX); and Tomasz Serbinowski (UT).

1. **Adopted the Instruction and Factors for 2020 Longevity Risk**

Ms. Ahrens reminded the Working Group that potential factors of zero were exposed for longevity risk for 2020 implementation. She said this would allow companies to complete the new structure, which will allow a study of the impact of the various methodologies, correlation and guardrail factors so they can be finalized in time for year-end 2021. Mr. Barlow said there were two comment letters received. Brian Bayerle (American Council of Life Insurers—ACLI) summarized the ACLI’s comment letter, indicating support for the proposed zero factors for year-end 2020 reporting. He said the ACLI believes this approach will provide the NAIC with the appropriate information for the necessary impact analysis of the factors, as well as give state insurance regulators valuable information to determine the level of correlation and guardrail factors. Paul Navratil (American Academy of Actuaries—Academy) presented the Academy’s comment letter (Attachment 1). He said there are two main sections with the first section being focused on suggested changes to the instructions for 2020 to provide added clarity along with suggested changes to the instructions and blank for the inclusion of adjustments for modified coinsurance. He said the second section of the letter may be something for discussion in conjunction with the review of 2020 results, but it deals with the impact of correlation and what the overall C2 component is going to look like. Mr. Barlow suggested that it was too late to make changes to the 2020 instructions. Dave Fleming (NAIC) said it was because the deadline for exposure of the changes was the end of April. Mr. Barlow suggested exposing the suggested edits for clarification so companies could have them available. Mr. Ostlund made a motion, seconded by Ms. Ahrens, to adopt the instructions before any of the Academy’s suggested edits indicating base factors of zero with the correlation and guardrail factors included in the blank schedules are determined. The motion passed unanimously. The Working Group agreed to expose the Academy’s suggested changes for a 60-day public comment period.

2. **Discussed Other Matters**

Mr. Barlow said the Mortgage Bankers Association (MBA) and the ACLI have submitted a letter requesting guidance on the risk-based capital (RBC) reporting of commercial mortgages for 2020 in light of the pandemic emergency and the impact it is having on commercial mortgages. He suggested having this distributed to Working Group members, and he said the Working Group will be scheduling calls in the short term to address this.

Mr. Barlow said there are a number of areas in which work is being done by the Academy so when calls not related to the pandemic can resume, these will be scheduled. He asked for a brief update on the work the Academy is doing on mortality. Chris Trost (Academy) said during the Working Group’s March 23 conference call, the Academy’s C2 Work Group introduced some of the work they are doing around a component of catastrophe risk or a more sustained event. He said it would be beneficial to get more detailed feedback from the Working Group on a future call.

Ms. Ahrens said the longevity risk component currently adopted does not include in scope longevity reinsurance transactions, which are currently not that common in the U.S. insurance industry. She said the Longevity Risk (E/A) Subgroup will be discussing this, and she asked for industry volunteers to contribute to these discussions.

Having no further business, the Life Risk-Based Capital (E) Working Group adjourned.
The Life Risk-Based Capital (E) Working Group of the Capital Adequacy (E) Task Force met via conference call March 23, 2020. The following Working Group members participated: Philip Barlow, Chair (DC); Deborah Batista (CO); Wanchin Chou (CT); Vincent Tsang (IL); John Robinson (MN); William Leung (MO); Rhonda Ahrens (NE); Seong-min Eom (NJ); Bill Carmello (NY); Mike Boerner and Rachel Hemphill (TX); and Tomasz Serbinowski (UT). Also participating was: Steve Drutz (WA).

1. **Adopted its Feb. 14 and 2019 Fall National Meeting Minutes**

Mr. Ostlund made a motion, seconded by Mr. Boerner, to adopt the Working Group’s Feb. 14 (Attachment Four-A) and Dec. 3 (see NAIC Proceedings – Fall 2019, Capital Adequacy (E) Task Force, Attachment Three) minutes. The motion passed unanimously.

2. **Exposed the Deletion of C-3 2019 Instruction for Public Comment**

Mr. Barlow said he believes the deletion of those items in the C-3 instructions that were specific to 2019 are straightforward, but he suggested that the Working Group expose the changes to make sure they were done properly and completely. The Working Group agreed to expose the deletion of the 2019 specific instructions for a public comment period ending April 22, 2020.

3. **Discussed the Academy’s Bond Proposal**

Mr. Barlow reminded Working Group members that this proposal has been discussed by the Investment Risk-Based Capital (E) Working Group for many years. He said there have been some questions raised by industry and some state insurance regulators about the American Academy of Actuaries’ (Academy’s) proposal and a request for an additional review. He said he believes that there needs to be a resolution on this because the bond factors have not been updated since they were initially developed. He noted a real estate proposal that is related to this. He said he has been on the Investment Risk-Based Capital (E) Working Group and following this from the beginning, and he believes that the Academy has done what they were asked to do and developed a proposal that is in line with the original methodology. He said the Working Group would ultimately be asked to approve any changes, so he asked for Working Group members’ thoughts. Mr. Chou said Connecticut has been closely monitoring the discussions, and he would like to see a more enhanced study on this because the impact to the industry is quite significant. Mr. Tsang said he believes the questions raised are not about questioning the Academy’s factors but a desire to have another viewpoint to consider. While he recognizes that this is a significant change, Mr. Barlow said the Academy’s proposal has been presented with extensive documentation and exposed for comment by the Investment Risk-Based Capital (E) Working Group with those comments being reviewed and considered. He questioned whether it will significantly affect the primary purpose of risk-based capital (RBC), which is identifying weakly capitalized companies because the life insurance industry is very well capitalized. He said there is one area where he would favor making a non-actuarial adjustment to the Academy’s proposal and that is to the portfolio adjustment because he believes that it may adversely affect smaller insurance companies. He said he is not completely clear on what the Working Group would gain by additional work on the proposal that has been presented. Ms. Ahrens agreed and questioned what will come from an additional review with the Academy’s proposal being vetted for several years. While sympathetic to companies that will see higher C-1 charges, she said the reason the bonds were reviewed was due to companies seeking a higher yield in this interest rate environment, and it seems clear that the yield comes with risk. Mr. Barlow said the Working Group will schedule a conference call to devote more time to this discussion. Nancy Bennett (Academy) said the Academy will provide any information or presentation that the Working Group needs. Paul S. Graham (American Council of Life Insurers—ACLI) said the industry still has significant concerns with the proposal, and it is still working on a request for proposal (RFP) with the intention to communicate with state insurance regulators to ensure that it yields information that is useful in making the final decision because it will have a significant impact.

4. **Heard an Update from the Academy C2 Work Group**

Chris Trost (Academy) provided a follow up from the update given at the 2019 Fall National Meeting where he discussed what the Academy C2 Work Group would change relative to the original work done. He said the Work Group’s evaluation of level
risk was less than what came out of the original work. Based on the feedback that the Work Group received, he said the Work Group should be vetting emerging sustained mortality events, which it believed are better categorized as catastrophe risk, and this is what the work has been focused on. He said he just wanted to introduce this concept, and he indicated that it could be more fully discussed on a subsequent conference call. He presented an update (Attachment Four-B) that described the overall approach being taken, highlighted the inclusion of this new element of a sustained mortality increase from an emerging mortality risk, and noted the ongoing discussion of the correlation between the various risks. With respect to the current C-2 life mortality, he said the Work Group has been primarily focused on individual, but it has started work on group mortality. He discussed in more detail about the additional catastrophe component and product differentiation, and he presented the Work Group’s next steps.

5. Heard an Update from the Academy C3 Life and Annuities Work Group

Link Richardson (Academy) provided a brief overview of the work being done by the Academy’s C3 Life and Annuities Work Group (Attachment Four-C). He discussed the request that the Work Group received and the high-level conceptual recommendations the Work Group has developed, and the desire is to get feedback before developing specific recommendations. Mr. Barlow said a conference call will be scheduled to have a more detailed discussion of this topic.

6. Discussed Longevity Risk Correlation

Mr. Barlow reminded the Working Group that it adopted a structural change to include the covariance adjustment and the guardrail with further discussion needed to determine what those factors will be before the end of June. Ms. Ahrens noted the discussion on the bond proposal and the concern about the impact and the need to rethink at that. She said she has been thinking about how to get a feel for the actual impact of adding the longevity factors at different correlations. She said one of the reasons the guardrail was included in what was recommended was a concern that there may be companies that actually get a reduction to the overall C-2 charge, and this needs to be more fully explored. She said the information needed to calculate the recommended longevity charge is not readily available in the current annual statement format, and trying to do an impact study is difficult to do. Trying to get that study done in the existing deadlines for RBC is going to be challenging, so she suggested that the Working Group could contemplate a different effective date or a field study based on companies using the 2019 information and making the needed adjustments. She said another alternative is to use the structure that has been adopted to capture the needed data for year-end 2020 to determine what the appropriate factors are.

7. Received an Update on the Health Test Language Proposal

Mr. Drutz said the Health Risk-Based Capital (E) Working Group formed the Health Test Ad Hoc Group that has been looking at possible changes to the health test, which helps determine what blank insurers file. The basis for the possible change to the health test is to ensure that health data written by life and property/casualty (P/C) companies is available in sufficient detail to help state insurance regulators make informed decisions. Mr. Drutz said he believes that about 25% of health premium is reported on the life blank, and the detail provided on that blank is often not detailed enough to help in health-related analyses.

The approach of the ad hoc group has been to look at possible changes to the health test itself, while also looking at possible blanks changes to capture more health data written by P/C and life blank filers and try to make the data already captured on those blanks consistent with the data captured on the health blank. Mr. Drutz said the health test language changes were recently exposed, but work will likely now turn to the blanks themselves in more detail as changes in the blanks might affect how much state insurance regulators believe the health test language should be modified.

Mr. Drutz said the ad hoc group wants to ensure that state insurance regulators and interested parties are aware of the work being done, and he encouraged anyone interested to join the ad hoc group to help ensure that any proposed changes to the blanks or health test language have been thoroughly vetted to avoid any unintended consequences. He said the ad hoc group has pondered getting rid of the reserve ratio in the health test and changing the premium test threshold, but he is aware that by moving some life and possibly a few P/C companies to the health blank, state insurance regulators may lose useful data that is specific to those two blanks. He said the ad hoc group is trying to avoid that. He said he believes that the work the ad hoc group is doing is necessary but complicated, and having additional input from state insurance regulators and interested parties as the ad hoc group proceeds would be valuable to assure that it ends up with proposals that are well vetted and provides state insurance regulators with the data they need.

Having no further business, the Life Risk-Based Capital (E) Working Group adjourned.

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What RBC Pages Should Be Submitted?

For year-end 2020 life and fraternal risk-based capital (RBC), submit hard copies of pages LR001 through LR049 to any state that requests a hard copy in addition to the electronic filing. Starting with year-end 2007 RBC, a hardcopy was not required to be submitted to the NAIC. However, a portable document format (PDF) file representing the hard copy filing is part of the electronic filing.

If any actuarial certifications are required per the RBC instructions, those should be included as part of the hard copy filing. Starting with year-end 2008 RBC, the actuarial certifications were also part of the electronic RBC filing as PDF files, similar to the financial annual statement actuarial opinion.

Other pages, such as the mortgage and real estate worksheets, do not need to be submitted. However, they still need to be retained by the company as documentation.

Bond Designation Structure

The Capital Adequacy (E) Task Force adopted proposal 2019-16-CA to incorporate the 20 designation categories for bonds into the life and fraternal RBC formula to be used in conducting an impact analysis study for year-end 2020 reporting during its April 30, 2020 conference call. The 20 bond designation categories were incorporated into the Bonds page (LR002), Asset Concentration page (LR010) and Off Balance Sheet Collateral page (LR017).

Longevity Risk

As a result of the adoption of proposal 2019-13-L by the Capital Adequacy (E) Task Force on its April 30, 2020 conference call, changes developed by the Longevity Risk (E/A) Subgroup and recommended to the Life Risk-Based Capital (E) Working Group to implement the structure for a longevity risk charge were incorporated into the life RBC formula. On it’s June 30, 2020 conference call, the Task Force adopted the instructions with proposal 2020-06-L, which includes factors of zero for 2020. The structure adopted will provide information to be used in the ultimate determination of factors for 2021 reporting.

Capitation Tables

The Capital Adequacy (E) Task Force adopted proposal 2018-17-CA to capture the Capitation Tables electronically through the file submission of the life RBC formula during its June 28, 2019 conference call.

RBC Preamble

As a result of the adoption of proposal 2019-07-CA by the Capital Adequacy (E) Task Force at the 2019 Fall National Meeting, the Risk-Based Capital Preamble was added to the RBC instructions to provide a clear understanding of the purpose or RBC and goals of RBC as the Capital Adequacy (E) Task Force and RBC Working Groups review referrals and proposals.

Overview and Table of Contents

As a result of the adoption of proposal 2020-05-CA by the Capital Adequacy (E) Task Force during its June 30, 2020 conference call, the page iv instructions were modified to insert the word “Overview” in the page heading and the Table of Contents were modified to include only the page heading and delete references to the individual sections of the Overview.
RBC Forecasting and Instructions

The Life and Fraternal RBC forecasting spreadsheet calculates RBC using the same formula presented in the 2020 NAIC Life and Fraternal Risk-Based Capital Forecasting & Instructions for Companies, and is available to download from NAIC Account Manager. The 2020 Life and Fraternal Risk-Based Capital Forecasting & Instructions for Companies publication is available for purchase in hardcopy or electronic format through the NAIC Publications Department. This publication is available on or about Nov. 1 each year. The User Guide is no longer included in the Forecasting & Instructions.

**WARNING:** The RBC Forecasting Spreadsheet CANNOT be used to meet the year-end RBC electronic filing requirement. RBC filing software from an annual statement software vendor should be used to create the electronic filing. If the forecasting worksheet is sent instead of an electronic filing, it will not be accepted and the RBC will not have been filed.
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</tr>
<tr>
<td>Total C-2a Interest Rate Risk</td>
<td>10,852,994,992</td>
<td>12,635,324,824</td>
<td>14,123,582,918</td>
<td>15,230,988,812</td>
<td>14,970,305,244</td>
<td>14,530,667,343</td>
<td>13,910,164,816</td>
<td>13,584,290,744</td>
<td>12,312,656,198</td>
<td>11,334,885,440</td>
<td>11,442,899,879</td>
<td>11,199,533,980</td>
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<tr>
<td>Total C-4b Business Risk Admin. Expenses</td>
<td>8,618,807,588</td>
<td>8,042,886,588</td>
<td>7,729,509,134</td>
<td>7,747,940,444</td>
<td>7,307,039,841</td>
<td>6,930,522,856</td>
<td>6,839,090,654</td>
<td>6,389,205,722</td>
<td>6,121,944,814</td>
<td>5,869,210,202</td>
<td>5,667,482,022</td>
<td>5,467,052,222</td>
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<tr>
<td>Median RBC %</td>
<td>86%</td>
<td>94%</td>
<td>94%</td>
<td>93%</td>
<td>96%</td>
<td>97%</td>
<td>96%</td>
<td>93%</td>
<td>90%</td>
<td>86%</td>
<td>93%</td>
<td>82%</td>
</tr>
<tr>
<td>% of RBC Companies</td>
<td>96%</td>
<td>94%</td>
<td>92%</td>
<td>92%</td>
<td>90%</td>
<td>88%</td>
<td>88%</td>
<td>88%</td>
<td>88%</td>
<td>88%</td>
<td>88%</td>
<td>88%</td>
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<tr>
<td># of Companies with RBC Ratio &gt;250 &amp; &lt; 500%</td>
<td>68</td>
<td>58</td>
<td>50</td>
<td>57</td>
<td>53</td>
<td>52</td>
<td>49</td>
<td>76</td>
<td>69</td>
<td>84</td>
<td>107</td>
<td>115</td>
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<tr>
<td># of Companies Filed RBC</td>
<td>772</td>
<td>703</td>
<td>704</td>
<td>716</td>
<td>725</td>
<td>727</td>
<td>750</td>
<td>761</td>
<td>786</td>
<td>804</td>
<td>814</td>
<td>847</td>
</tr>
</tbody>
</table>

**AGGREGATED LIFE RBC AND ANNUAL STATEMENT DATA**

© 2018 National Association of Insurance Commissioners
### Source: NAIC Financial Data Repository

#### 2018 Data as of 3/30/2019

**Year-End 2018** | **Year-End 2017** | **Year-End 2016** | **Year-End 2015** | **Year-End 2014** | **Year-End 2013** | **Year-End 2012** | **Year-End 2011** | **Year-End 2010** | **Year-End 2009** | **Year-End 2008** | **Year-End 2007**
---|---|---|---|---|---|---|---|---|---|---|---
**# of Companies Filed/Reported RBC** | 72 | 73 | 75 | 75 | 73 | 76 | 77 | 79 | 83 | 84 | **Attachment F**
**# of Companies Filed Annual Statement** | 73 | 74 | 77 | 79 | 79 | 80 | 80 | 83 | 91 | 93 | 97
**% of RBC Companies** | 99% | 99% | 97% | 95% | 92% | 93% | 84% | 92% | 89% | 89% | 87%

#### Company Action Level - Trend Test at 30%

|  | 2 | 0 | 2 | 1 | 3 | 1 | 0 | 1 | 3 | 2 | 0

#### Company Action Level - Trend Test at 25%

|  | 0 | 0 | 1 | 1 | 0 | 1 | 0 | 1 | 1 | 3 | 1

#### Regulatory Action Level

| 1 | 2 | 1 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0

#### Authorized Control Level

| 3 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0

#### Mandatory Control Level

| 4 | 0 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | 3 | 10 | 4

### Total

| 5.56% | 2.74% | 5.33% | 6.67% | 5.48% | 6.76% | 2.99% | 2.63% | 5.19% | 7.59% | 14.46% | 4.76%

#### # of Companies with RBC Ratio > 10,000%

| 0 | 2 | 1 | 1 | 2 | 2 | 1 | 2 | 2 | 2 | 2 | 4

#### # of Companies with RBC Ratio < 1000 & > 0%

| 24 | 28 | 29 | 25 | 21 | 28 | 23 | 25 | 29 | 33 | 32 | 43

#### Total Authorized Control Level RBC

| 1,733,245,430 | 1,452,835,509 | 1,347,832,577 | 1,255,700,071 | 1,280,942,505 |

#### Total Adjusted Capital


#### Total C-4a Business Risk

| 146,809,544 | 146,269,571 | 147,055,169 | 139,216,623 | 132,853,826 |

#### Total C-3c Market Risk


#### Median RBC %

| 773% | 872% | 822% | 802% | 751% | 571,136 | 55,334,343 | 48,811,031 | N/A | N/A | N/A

#### Total C-4a Business Risk - Aliases

| 5,580,367 | 6,102,267 | 61,793,400 | 60,343,051 | 56,399,609 | 57,710,136 | 55,334,343 | 48,811,031 | N/A | N/A | N/A

#### Total C-1a Asset Risk - Common Stock

| 2,015,985,165 | 1,983,689,106 | 1,963,367,296 | 1,928,886,045 | 1,901,289,576 | 1,302,632,382 | 1,209,071,765 | 1,085,187,524 | N/A | N/A | N/A

#### Total C-2 Insurance Risk

| 408,509,044 | 361,345,746 | 347,034,048 | 348,958,190 | 342,027,279 | 329,579,505 | 321,457,634 | 315,521,778 | N/A | N/A | N/A

#### Total C-4b Business Risk Admin. Expenses

| 1,886,744 | 1,551,129 | 1,564,002 | 1,716,479 | 1,663,913 | 1,967,688 | 2,076,144 | 2,052,481 | N/A | N/A | N/A

#### Total Asset Risk - Affiliates

| 75,630,367 | 68,102,267 | 61,793,400 | 60,343,051 | 56,399,609 | 57,710,136 | 55,334,343 | 48,811,031 | N/A | N/A | N/A

#### Total C-3c Market Risk - All Other

| 1,488,768,764 | 1,229,721,949 | 1,169,846,355 | 1,034,286,056 | 975,579,588 | 933,361,216 | 1,153,872,821 | 1,158,338,657 | N/A | N/A | N/A

#### Total C-2 Insurance Risk - All Other

| 767,272,236 | 720,305,211 | 673,932,001 | 713,965,314 | 865,468,813 | 806,064,397 | 638,182,548 | 603,032,128 | N/A | N/A | N/A

#### Total C-3d Health Credit Risk

| 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | N/A | N/A | N/A

#### Total C-4c Business Risk - All Other

| 1,294,464,102 | 1,184,640,402 | 3,843,811,516 | 3,603,820,214 | 3,665,265,644 | 3,584,291,885 | 3,519,079,128 | 3,333,807,725 | N/A | N/A | N/A

#### Total C-3d Health Credit Risk - All Other

| 0.14% | 129% | 1246% | 1234% | 1146% | 1119% | 1013% | 969% | 912% | 590% | 101% | 131%

#### Total C-1a Asset Risk - All Other

| 30.31% | 29.87% | 30.95% | 30.70% | 26.82% | 26.19% | 32.85% | 34.75% | 30.31% | 29.87% | 30.95% | 30.70% | 26.82% | 26.19% | 32.85% | 34.75% |

#### Total C-2 Insurance Risk - All Other

| 30.31% | 29.87% | 30.95% | 30.70% | 26.82% | 26.19% | 32.85% | 34.75% | 30.31% | 29.87% | 30.95% | 30.70% | 26.82% | 26.19% | 32.85% | 34.75% |

#### Total Claims Incurred (Page 4 Lines 10 Through 13)

| 5.56% | 2.74% | 5.33% | 6.67% | 5.48% | 6.76% | 2.99% | 2.63% | 5.19% | 7.59% | 14.46% | 4.76%

#### Source: NAIC Financial Data Repository

© 2018 National Association of Insurance Commissioners
July 23, 2020

Philip A. Barlow, FSA, MAAA
Chair, Life Risk-Based Capital (E) Working Group
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

Re: Progress Report for July 30, 2020 Working Group Meeting

Dear Mr. Barlow:

The Mortgage Bankers Associations (MBA)\textsuperscript{1} and the American Council of Life Insurers (ACLI),\textsuperscript{2} on behalf of our respective member insurers, respectfully submit to the Life Risk-Based Capital Working Group of the National Association of Insurance Commissioners (NAIC) the attached materials to support our report on the July 30, 2020 call, reporting on our progress following up on the Working Group’s July 10, 2020 call.

We appreciate the Working Group’s approval on that call of our requested reporting guidance on Contemporaneous Property Valuation, and we look forward to continuing to engage on reporting of 2020 Net Operating Income (NOI).

\textsuperscript{1} The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 280,000 people in virtually every community in the country. Its membership of over 2,300 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, credit unions, thrifts, REITs, Wall Street conduits, 70 life insurance companies engaged in real estate finance, and others in the mortgage lending field. For additional information, visit MBA’s website: www.mba.org

\textsuperscript{2} The American Council of Life Insurers (ACLI) is the leading trade association driving public policy and advocacy on behalf of the life insurance industry. 90 million American families rely on the life insurance industry for financial protection and retirement security. ACLI’s member companies are dedicated to protecting consumers’ financial wellbeing through life insurance, annuities, retirement plans, long-term care insurance, disability income insurance, reinsurance, and dental, vision and other supplemental benefits. ACLI’s 280 member companies represent 94 percent of industry assets in the United States. Learn more at www.acli.com
We want to thank you and other regulators, and NAIC staff, for your considerable time and attention to this request. Please feel free to contact Bruce Oliver at boliver@mba.org or 202-557-2840 or Mike Monahan at mikemonahan@acili.com or 202-624-2324 for any additional information.

Sincerely,

Mike Flood

Paul S. Graham, III

Attachment: Supplement to June 8, 2020 Request for Risk-Based Capital Reporting Guidance

cc: Dave Fleming, NAIC Senior Insurance Reporting Analyst
I. BACKGROUND

A. The need for RBC guidance generally

Owners of properties that secure mortgage loans are experiencing temporary decreases in income, including rent income, from mandatory shutdowns and other governmental actions taken to flatten the COVID-19 pandemic curve. This is especially the case for properties in the retail and hospitality sectors.

RBC reporting standards were not designed with these circumstances in mind. Accordingly, the Financial Condition (E) Committee issued RBC guidance to adapt current RBC reporting standards to these unique circumstances. That guidance addresses RBC reporting treatments that would otherwise discourage or penalize reasonable and prudent temporary modifications of loans affected by the pandemic.

The E Committee delegated to the Life RBC Working Group the task of addressing further RBC reporting guidance, at a more detailed level, that may be appropriate to similarly address these unique circumstances.

Consistent with that delegation, the Life RBC Working Group has (1) extended the E Committee RBC Guidance to December 31, 2020 reporting, (2) adopted guidance on RBC treatment of construction loans paused under governmental directives, and (3) adopted guidance on reporting of Contemporary Property Values for 2020 RBC reporting.

The Working Group determined to defer consideration of a COVID-19-related adaptation of the reporting of 2020 Net Operating Income (NOI), which will affect 2021, 2022, and 2023 RBC reporting.

B. NOI and RBC reporting

NOI is the net of all operating income from a property, less all reasonably necessary operating expenses. Income for a property includes rents received, and operating expenses excludes principal and interest payments on loans.

For performing loans, the CM category is based on a matrix of Debt Service Coverage (DSC) and LTV. NOI affects RBC reporting because NOI is an element of DSC.

\[ DSC = \frac{\text{Net Operating Income (NOI)}}{\text{RBC Debt Service}} \]

In 2013, regulators determined to dampen the direct impact of changes in NOI on RBC reporting by adopting a weighted-average approach to applying NOI values, as follows:

- 50% of preceding year NOI
- 30% of next preceding year NOI; and
- 20% of next preceding year NOI.

C. The need for RBC reporting guidance on 2020 NOI

NOI can provide insights into future credit risk where one can reasonably assume that future NOI will be similar to current NOI.

Given the unique nature of the COVID-19 pandemic, however, one cannot reasonably assume that 2021, 2022, and 2023 NOIs will be similar to 2020 NOI.

As a result, absent an adjustment to how 2020 NOI is reported at year end 2021, 2022, and 2023, RBC reporting would overstate the future credit risk impacts of temporary reductions in rent income that occur in 2020.
II. INDUSTRY 2020 NOI RECOMMENDATIONS

A. Revised Recommendation

For 2021, 2021, and 2023 RBC reporting:

- **Initial recommendation.** To prevent 2020 NOI values affected by temporary impacts of COVID-19 from overstating credit risk, industry initially recommended that, where a value of 2020 NOI is an input into the computation of the Rolling Average NOI, insurers should use the greater of:
  - 2020 NOI; or
  - [100% of] 2019 NOI.

- **Revised recommendation.** To address regulator feedback received in the June 30 WG conference call, industry revised its recommendation July 7 to reflect reductions in income in 2020, but with a floor. Specifically, industry recommends that, where a value of 2020 NOI is an input into the computation of the Rolling Average NOI, insurers should use the greater of:
  - 2020 NOI; or
  - 85% of 2019 NOI.

B. Why Revised Recommendation is Reasonable

- **Benchmark for 85%.** An NOI drop to 85% of a prior year’s NOI is recognized as substantial by FHFA, which used a 15% drop in NOI (i.e., to 85% of the prior-year NOI) as a key “stress” assumption to calibrate multifamily credit risk in proposed GSE risk-based capital standards.

- **Consideration of historical data.** An NOI drop to 85% of a prior-year NOI represents roughly three times the historical worst four-quarter decline in NCREIF NOI values over the past 20 years, which includes the great financial crisis.

- **Non-performing loans are effectively excluded from recommendation.** A non-performing loan is classified in category CM6 or CM7, without regard to NOI. As a result, the recommended treatment of 2020 NOI would apply only to loans that are performing as of December 31, 2021, or a later reporting date.

- **2021 reductions in property valuation will be fully recognized.** The treatment of property valuations adopted by the WG on July 10 applies only for 2020 RBC reporting. As a result, 2021 reductions in property valuations (including those resulting from reduced NOI), will be fully reflected in LTVs for 2021 year-end RBC reporting.

C. Why Guidance is Necessary Now

While 2020 NOI is not incorporated into RBC reporting until year-end 2021, a lack of guidance on 2020 NOI RBC reporting has impacts now.

- **Evaluating new loans.** Insurers evaluating new loans as appropriate investments consider the return on capital as well as credit risk. Uncertainty as to RBC treatment of new loans impairs the ability to conduct that analysis. As a result, RBC considerations can prevent insurers from being competitive when seeking to make sound and appropriate mortgage investments.

  This impact would be most pronounced for loans on properties in states and regions that are hardest hit by actions to curb the COVID-19 pandemic.

- **Capital planning.** Regulators expect insurers to conduct robust capital planning, as do ratings agencies and investors and other stakeholders.

  A lack of clarity now as to impacts of 2020 NOIs on RBC reporting for 2021 and later years reduces insurers’ ability to account for their portfolios of mortgages in such capital planning.
Update to Life RBC Working Group (July 30, 2020)
Industry Progress Report on Revised 2020 NOI Recommendation

III. PROGRESS REPORT

Industry actions following up on July 10 call

To provide the WG with additional information to support its re-consideration of the revised NOI recommendation, industry will:

A. Review and assess 2Q 2020 NOI information from various sources.
   This will include review and assessment of properties for which insurers receive quarterly NOI values, and any other similarly information that is available.

B. Consider market forecasts and projections from credible sources.
   See, e.g., MBA Commercial Real Estate Finance Forecast, by Jamie Woodwell; Reggie Booker (July 16, 2020) (excerpt below).

“...For multifamily properties, much appears to depend on the federal government. Despite major disruptions in the labor markets and the unemployment rate rising above 14 percent, renters have continued to make their payments. This can largely be attributed to the federal stimulus bills, the one-time checks and expanded unemployment insurance. Should such support for displaced workers continue as the economy rebounds, the apartment market should remain relatively balanced. This forecast anticipates continued federal support with a decline in property net operating income (NOI) roughly between that seen in the recession of 2001 and that of the Global Financial Crisis (GFC) - relatively light given the amount of labor market distress.

For office properties, the outcome will hinge on the tug-of-war between how dramatically companies embrace teleworking and shed office space on the one hand, and how companies reconfigure their space (and increase space per worker) to promote social distancing on the other. We anticipate that for most properties in most markets, the latter could largely mute the former, and that the greatest impact will come through shorter-term decision-making that generally maintains the leasing status quo.

Looking across all property types, we expect the aggregate decline in NOI this recession could exceed that of the 2001 recession or GFC, but that impacts will be very different across different property types. The overall decline will also be concentrated in 2020.”

* * *

Mike Flood
SVP, CMF, Policy & Member Engagement

Paul S. Graham, III
SVP, CMF, Policy & Member Engagement
<table>
<thead>
<tr>
<th>2020 #</th>
<th>Owner</th>
<th>2020 Priority</th>
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<th>Working Agenda Item</th>
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<tr>
<td>1</td>
<td>Life RBC</td>
<td>Ongoing</td>
<td>Ongoing</td>
<td>Make technical corrections to Life RBC instructions, blank and/or methods to provide for consistent treatment among asset types and among the various components of the RBC calculations for a single asset type.</td>
<td></td>
<td></td>
<td></td>
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</tbody>
</table>
| 2     | Life RBC | 1 | 2020 or later | **A.** Evaluate the overall effectiveness of the C3 Phase 2 and AG 43 methodologies by conducting an in-depth analysis of the models, modeling assumptions, processes, supporting documentation and results of a sample of companies writing variable annuities with guarantees and to make recommendations to the Capital Adequacy Task Force or Life Actuarial Task Force on any changes to the methodologies to improve their overall effectiveness.  
**B.** Develop and recommend changes to C-3 Phase II and AG 43 that implement, for 2018 adoption, the Variable Annuities Framework for Change.  
1. Monitor the impact of the changes to the variable annuities reserve framework and risk-based capital (RBC) calculation and determine if additional revisions need to be made.  
2. Develop and recommend appropriate changes including those to improve accuracy and clarity of variable annuity (VA) capital and reserve requirements. | CATF | Being addressed by the Variable Annuities Capital and Reserve (E/A) Subgroup | |
<p>| 3     | Life RBC | 1 | 2020 or later | Provide recommendations for recognizing longevity risk in statutory reserves and/or RBC, as appropriate. | New Jersey | Being addressed by the Longevity (E/A) Subgroup | |
| 4     | Life RBC | 1 | 2020 or later | Update the current C-3 Phase I or C-3 Phase II methodology to include indexed annuities | AAA | | |
| 5     | Life RBC | 2 | 2020 or later | Develop guidance, for inclusion in the proposed NAIC contingent deferred annuity (CDA) guidelines, for states as to how current regulations governing risk-based capital requirements, including C-3 Phase II, should be applied to contingent deferred annuities (CDAs). Recommend a process for reviewing capital adequacy for insurers issuing CDAs and prepare clarifying guidance, if necessary, due to different nomenclature then used with regard to CDAs. The development of this guidance does not preclude the Working Group from reviewing CDAs as part of any ongoing or future charges where applicable and is made with the understanding that this guidance could change as a result of such a review. | 10/21/13 Referral from A Committee | It is important to consider the implications of work being done by the CDA and VA Issues Working Groups to ensure consistency in addressing these charges. The Working Group is monitoring the progress of that work. | |
| 6     | Life RBC | 1 | 2020 | Review and evaluate company submissions for the RBC Shortfall schedule and corresponding adjustment to Total Adjusted Capital. | | | 10/16/2015 |
| 7     | Life RBC | 1 | 2020 | Review and evaluate company submissions for the Primary Security Shortfall schedule and corresponding adjustment to Authorized Control Level. | | | 10/16/2015 |
| 8     | Life RBC | 1 | 2020 | Continue consideration impacts and modifications necessary due to the Federal Tax Cuts and Jobs Act and develop guidance for users of RBC on those impacts. | | | 3/24/2018 |
| 9     | Life RBC | 1 | 2020 | Determine if any adjustment is needed to the XXX/AXXX RBC Shortfall calculation to address surplus notes issued by captives. | 11/1/17 Referral from the Reinsurance (E) Task Force | | 3/24/2018 |
| 10    | Life RBC | 1 | 2019 | Address changes needed due to elimination of the fraternal annual statement blank. | | | 9/1/2018 |</p>
<table>
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<th>Owner</th>
<th>2020 Priority</th>
<th>Expected Completion Date</th>
<th>Working Agenda Item</th>
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<th>Date Added To Agenda</th>
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<td>10</td>
<td>Life RBC WG</td>
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<td>2020</td>
<td>Determine if any adjustment is needed due to the changes made to the Life and Health Guaranty Association Model Act, Model #520.</td>
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<td>9/1/2018</td>
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<tr>
<td>11</td>
<td>Life RBC WG</td>
<td>1</td>
<td>2020</td>
<td>Determine if any adjustment is needed to the reinsurance credit risk in light of changes related to collateral and the changes made to the property RBC formula.</td>
<td></td>
<td></td>
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</table>

New Items – Life