Draft: 4/29/25

Statutory Accounting Principles (E) Working Group

and the Life Actuarial (A) Task Force

Virtual Meeting

April 10, 2025

The Statutory Accounting Principles (E) Working Group of the Accounting Practices and Procedures (E) Task Force met April 10, 2025, in joint session with the Life Actuarial (A) Task Force. The following Working Group members participated: Dale Bruggeman, Chair (OH); Kevin Clark, Vice Chair (IA); Richard Russell (AL); Kim Hudson (CA); Michael Estabrook (CT); Rylynn Brown (DE); Cindy Andersen (IL); Shantell Taylor (LA); Steve Mayhew and Kristin Hynes (MI); Doug Bartlett (NH); Bob Kasinow (NY); Diana Sherman and Dave Yanick (PA); Jamie Walker (TX); Doug Stolte and Jennifer Blizzard (VA); and Levi Olson (WI).

The following Life Actuarial (A)Task Force members participated: Cassie Brown, Chair, represented by Rachel Hemphill (TX); Scott A. White, Vice Chair, represented by Craig Chupp (VA); Lori K. Wing-Heier represented by Sharon Comstock (AK); Mark Fowler represented by Sanjeev Chaudhuri (AL); Ricardo Lara represented by Ahmad Kamil (CA); Andrew N. Mais represented by Wanchin Chou (CT); Doug Ommen represented by Mike Yanacheak (IA); Ann Gillespie represented by Matt Cheung (IL); Holly W. Lambert represented by Scott Shover (IN); Vicki Schmidt represented by Nicole Boyd (KS); Marie Grant represented by Nour Benchaaboun (MD); Grace Arnold represented by Fred Andersen and Ben Slutsker (MN); Angela L. Nelson represented by William Leung (MO); Eric Dunning represented by Michael Muldoon (NE); Justin Zimmerman represented by Seong-min Eom (NJ); Scott Kipper represented by Maile Campbell (NV); Adrienne A. Harris represented by William B. Carmello and Amanda Fenwick (NY); Judith L. French represented by Peter Weber (OH); Andrew R. Stolfi represented by Tashia Sizemore (OR); Michael Humphreys represented by Steve Boston and Dave Yanick (PA); and Jon Pike represented by Tomasz Serbinowski (UT).

1. Discussed Agenda Items 2024-05 and 2024-06

Bruggeman called on Hemphill to provide an overview of the Valuation Analysis (E) Working Group referrals. Hemphill stated that the Valuation Analysis (E) Working Group met throughout 2023 to discuss risk transfer analysis issues arising for treaties that involved cessions both on a coinsurance basis and a yearly renewable term (YRT) basis, with interdependent features, such as an inability to independently recapture or a combined experience refund. She stated that several regulators shared perspectives from past reviews of specific transactions. The Valuation Analysis (E) Working Group also requested that certain reinsurers provide their perspective and engage in a question-and-answer (Q&A) session while the issues were considered.

Hemphill stated that as a result of the Valuation Analysis (E) Working Group’s meetings throughout 2023, a referral was sent to the Statutory Accounting Principles (E) Working Group in December 2023 with the consensus of the Valuation Analysis (E) Working Group after the 2023 discussions, and a request for the Statutory Accounting Principles (E) Working Group to consider targeted revisions to address the observed issues.

Hemphill stated that regarding agenda item 2024-05, as part of the review process, the Valuation Analysis (E) Working Group observed that an aside statement in the *Accounting Practices and Procedures Manual*, Appendix A-791—Life and Health Reinsurance Agreements (A-791), the Q&A on group life was, in some cases, being misconstrued as a safe harbor for individual life YRT premium rates. She noted that for both principle-based reserving (PBR) and pre-PBR business, such a safe harbor could result in the deprivation of surplus. The Valuation Analysis (E) Working Group recommended removing the aside.

Hemphill stated that regarding agenda item 2024-06, the Valuation Analysis (E) Working Group had observed instances of a bifurcated risk transfer analysis being performed for these interdependent, combined coinsurance/YRT treaties. She stated this led to an overstated reserve credit, as a proportionate reserve credit was being taken for the coinsurance piece, while it was observed that in its entirety, the treaty only transferred tail risk. In response, the Statutory Accounting Principles (E) Working Group proposed edits clarifying that risk transfer must be evaluated in the aggregate for interdependent cessions.

Hemphill stated that during discussions in early 2024, the American Council of Life Insurers (ACLI) requested that these edits not be rushed, which at that time was generally agreeable, as the edits primarily act as clarifying edits and the primary need from a Valuation Analysis (E) Working Group perspective is awareness on the part of regulators of the greater complexity and additional analysis required when reviewing risk transfer for these interdependent, combined coinsurance/YRT treaties. Hemphill stated that she believes regulator awareness is the primary concern here, and clarifying edits will be helpful. She noted that she generally supported the drafts from Statutory Accounting Principles (E) Working Group staff as responsive to the issues presented by the Valuation Analysis (E) Working Group.

Hemphill stated that the Statutory Accounting Principles (E) Working Group has now had items 2024-05 and 2024-06 pending since their exposure over a year ago at the 2024 Spring National Meeting. There have been regulator-only presentations during that time, and part of today’s meeting is to ensure key materials, such as examples previously presented by the ACLI, are available for public discussion. She stated that another goal of today’s meeting is to begin a detailed public discussion to work through any remaining issues on the draft for 2024-06. There appears to be general consensus on 2024-05, but the ACLI had previously requested that agenda items 2024-05 and 2024-06 be considered in tandem.

1. Heard a Presentation from the ACLI on Statutory Risk Transfer Considerations

Jeremy Starr (ACLI consulting representative) provided a presentation (Attachment 1) on statutory risk transfer considerations relating to combination coinsurance and YRT reinsurance agreements. This presentation attached an October 2024 presentation with single-year examples and additional multi-period examples. This presentation focused on addressing the A-791 requirement regarding no surplus deprivation. The ACLI recommended that the YRT premiums that are set equal to the valuation mortality should not result in surplus deprivation to the ceding entity. He stated that the examples demonstrate that if a reinsurance agreement in aggregate passes risk transfer requirements, including that it does not deprive a cedant of surplus, it should be accorded reinsurance accounting treatment. Starr stated that a key tenet of the ACLI’s position on combined coinsurance and YRT agreements is the standard by which an agreement should be judged as to whether risk has been transferred. He stated that the ACLI’s position is centered on current statutory guidance on reinsurance, which allows for an independent review of each component of the coinsurance and YRT for risk transfer and then requires that the reinsurance agreement in aggregate does not deprive the cedent of surplus. It also includes the agreement complying with other regulatory requirements relating to such items as recapture and experience refunds, among others. He stated that a reinsurance agreement deprives the reinsurer of surplus when payments are made from surplus rather than the experience of the ceded business. Starr stated that the ACLI believes that to determine risk transfer, you need to review the terms of the agreement and not look at only its form. He stated that a potential way to assess deprivation of surplus is via a model demonstrating that net gain after reinsurance is positive for all durations. He stated that agreements should pass risk transfer based on whether treaties have YRT rates calculated based on the lowest mortality rates used in calculating the reserves.

Clark, Hemphill, and John Di Meo (Hannover Life Reassurance Company of America—Hannover Re) discussed various items the Working Group would like to see in the next round of examples, including an example where the coinsured block incurs a loss, as the concern is that the YRT premiums offset coinsurance losses in a way that could result in a deprivation of surplus. They also stated that regulators want to see the presentation data in an Excel spreadsheet.

1. Heard a Presentation on Combined Coinsurance Funds Withheld YRT Agreements

Hemphill gave a presentation (Attachment 2) on combined coinsurance funds withheld YRT agreements, highlighting concerns regarding risk transfer on some contracts when there are interdependent features, such as the inability to independently recapture and an aggregate experience refund. She noted requirements in *Statement of Statutory Accounting Principles (SSAP) No. 61—Life, Deposit-Type and Accident and Health Reinsurance*, that reinsurance credit should not be given if the terms limit or diminish the transfer of risk, and in A-791 that surplus relief should not be temporary. She highlighted concerns that a bifurcated risk transfer analysis does not reflect the economics of the interdependent contract.

Hemphill highlighted that companies presented that YRT premiums were automatically acceptable if they were based on the valuation mortality. The Valuation Analysis (E) Working Group identified that an aside statement was being misinterpreted as a YRT safe harbor. She provided a simple example of how such a safe harbor could still result in a deprivation of surplus. This resulted in the referral which led to agenda item 2024-05.

Hemphill stated that risk transfer requirements differ depending on the type of treaty. Proportional (e.g., coinsurance), YRT, and non-proportional (e.g., excess of loss) treaties each have unique standards for statutory reporting. She stated that regulators have challenged a bifurcated approach (analyzing coinsurance and YRT separately), as it overlooks their interdependence. This commingling of economics creates risk transfer concerns. A-791 notes that YRT is not a concern if it only provides incidental reserve credits without surplus enhancement. She noted that risk transfer issues arise when there is significant surplus enhancement for interdependent coinsurance funds withheld and YRT treaties, as it raises the issue of the YRT functioning to enable or subsidize the coinsurance cession. She stated that, for interdependent coinsurance funds withheld and YRT treaties to meet risk transfer standards, the YRT cession and premiums must not act to support or enable the coinsurance cession. If YRT creates high reserve credits or significant surplus relief, it fails to qualify as true YRT under A-791, which must only provide “incidental reserve credits for the ceding insurer’s net amount at risk for the year with no other allowance to enhance surplus,” and cannot be exempt from its requirements. She stated that this highlights the importance of qualitative evaluations alongside quantitative analyses and that, while examples may demonstrate outcomes, principle-based assessments are crucial for identifying whether the transaction meets risk transfer requirements. She stated that misinterpretation of a “YRT safe harbor” is another concern. The notion that YRT premiums, if aligned with prescribed Commissioners’ Standard Ordinary (CSO) Tables or valuation mortality rates, automatically validate the agreement is incorrect. She stated that simplified examples, such as a 10-year level term policy with no deficiency reserves and flat mortality, where the reinsurance premium exceeds the gross premium, illustrate that even when YRT premiums align with valuation mortality rates, they can still lead to surplus deprivation. She stated that this undermines the safe harbor concept and so any analysis depending on a comparison of the YRT premiums to valuation mortality fails to address combined YRT and coinsurance transaction risk transfer issues. She stated that, ultimately, YRT must not subsidize or support coinsurance since, without this independence, such agreements fail risk transfer evaluations.

Bruggeman stated that earlier he asked about a situation where a direct writing company (i.e., cedant) knows a block of whole life business will not generate future profits. To mitigate losses, they might pay a reinsurer to take the business. If an immediate payment occurs, the cession happens, the reserve reduction disappears, and any future gains or losses transfer to the reinsurer, eliminating them for the cedant. He stated that reinsurers will not take on this business out of goodwill—they expect compensation. Compensation could be cash paid upfront or, in some cases, financed by YRT premiums from another block of profitable business. This financing aspect raises concerns. Bruggeman asked whether what was being addressed was the issue of YRT premiums on a separate profitable block being used to subsidize the transfer of an unprofitable block. He stated that if future losses are anticipated, someone must bear the cost, and the cedant would need to pay something to halt those losses. Bruggeman asked whether the payment is made upfront in cash or financed through expected future profits from a different block. He questioned whether either of these approaches raises concerns from a risk transfer perspective.

Hemphill stated that paying upfront is a separate issue, but the concern arises when a profitable YRT block is used to pay for the coinsurance cession. In this case, the coinsurance terms cannot independently stand on their own, which aligns with ACLI stance that the coinsurance piece must stand on its own. If the reinsurer would not accept the coinsurance cession without the YRT, this raises the question of whether the YRT is really exempt from any part of A-791 since it is providing more than incidental surplus relief.

Bruggeman stated that trying to finance a coinsurance cession using another block, such as a profitable YRT block, does not constitute true risk transfer when assessed in aggregate. Financing through another block essentially uses profits from elsewhere, which could result in a deprivation of surplus. For example, a high YRT premium acts as a buffer on the experience for both blocks, enabling this arrangement and undermining risk transfer. If future coinsurance losses are being covered by inflating YRT premiums, this fails to meet risk transfer requirements. He stated that Hemphill’s point aligns with this. Each component, coinsurance and YRT, must demonstrate risk transfer individually and in combination. Even if the combination seems to satisfy risk transfer requirements, the individual pieces must stand on their own. He stated that you cannot rely on one to support the other. This complexity makes drafting clear guidelines challenging. Every time wording is proposed, new scenarios arise that could violate A-791, which is why this discussion is necessary. He stated that any guidance must remain consistent with A-791. Adding new wording risks creating scenarios that inadvertently conflict with its core principles. Ultimately, when evaluating transactions, it is important to avoid violating A-791, including surplus deprivation or requiring payments to the reinsurer that undermine compliance. Regulators often need to step in to address cases where requirements are misunderstood or unmet. The Valuation Analysis (E) Working Group has worked hard to clarify these points, but creating universally applicable examples remains challenging without delving into company-specific cases.

Starr stated that coinsurance must stand independently. He said its terms should not rely on a YRT agreement to function, as Hemphill pointed out. While there may be situations where combined analysis shows coinsurance performing well while YRT underperforms, or vice versa, the critical point is that each component must stand alone. Together, in combination, they must ensure there is no surplus deprivation. He stated that they are focused on the minimum reserve, not necessarily the CSO table reserve, when calculating, and that while their language has not always been as precise as it could be, Hemphill’s example clarified that in such cases, the YRT premium should be three, not six, due to the one-half X factors.

Hemphill stated that in prior discussions, the complexity of evaluating both PBR and pre-PBR business was emphasized. For PBR, they understood that the valuation mortality could change over time, which added to the complexity. However, it is now clear that straight valuation mortality is not suitable for pre-PBR business either. Even when using the lowest valuation mortality, this is not a fixed threshold; it can change over time as X factors are reevaluated and potentially updated by the company. As a result, a safe harbor still cannot be established, even when considering the lower valuation mortality.

Di Meo stated that Hemphill articulated it well in her presentation that there should not be payments for amounts where the cedant has established no liability. He stated that, conceptually, parties appear to agree on this standard and applies in these unique scenarios, such as when using X factors on term business or secondary guarantees. He stated that he is encouraged by the progress made over the past weeks. This example and the discussions have helped all involved move forward and find common ground.

Clark stated that the key area of difference between the regulatory and industry conversations is fairly narrow, and all agree that both components of reinsurance must be evaluated separately for risk transfer and also analyzed together to ensure there is no potential for surplus deprivation. He stated that the disagreement lies in the industry proposal to include a statement in the standard suggesting that, as long as YRT premiums do not exceed the minimum valuation mortality, surplus deprivation is essentially impossible. He stated that Hemphill’s examples have effectively demonstrated that this is not always true, highlighting the limitation of such a statement. So, while there is alignment on the principle of evaluating both components separately and together, and ensuring no surplus deprivation occurs, the challenge is that there is no single, universally applicable “safe harbor” statement that holds true in all scenarios. He stated that he is unsure where the ACLI or the industry currently stands on this point, given the discussions. However, the language proposed that reinsurance should be evaluated both separately and in aggregate is about as good as can reasonably be achieved.

Di Meo stated that they can bring additional clarity to this and that they all agree on the proposed language regarding assessing transactions together and the conclusion that these transactions may not meet the required standards. He said he thinks there is room to refine the approach further. He stated that it is his understanding that the market is effectively shut down because these transactions are deemed non-compliant and unapproved. Unless this is the regulator’s intent, he proposed that the parties involved continue collaborating to develop language that clearly defines a place for these transactions in a prudent and appropriate way. He stated that this is a complex issue, and while there is no silver bullet safe harbor language, that does not mean that language allowing the industry to move forward with these types of transactions cannot be drafted. He stated that many of these have been in place for years and have served cedants and the industry well, and that the goal is to preserve and support those benefits while addressing compliance concerns effectively.

Bruggeman stated that he has been working on wording that combines the best elements of the initial exposure draft and the ACLI's comments, but he wanted to wait for this discussion to finalize it. He stated his goal is to act as a bridge to find common ground. He asked whether industry, or the ACLI specifically, could propose adjustments to their original suggestions for paragraph 18 after hearing these discussions. He said that all would benefit from seeing those changes. He stated that he would revisit the wording he has been working on, with input from Hemphill and others, to see if a balanced approach that avoids missing anything critical in A-791 can be achieved. He stated that, ultimately, they need a solution that makes sense for both perspectives and that if industry can provide updated suggestions, they can collaborate further with NAIC staff and the ACLI to refine the language. He stated that, until then, it seems these transactions are effectively on hold and that if the industry truly needs this, it may require a broader policy decision.

Di Meo stated that the insights gained from these conversations have been invaluable in addressing potential gaps and understanding the concerns and sensitivities expressed. He said the ongoing discussions and examples shared with regulators have been particularly eye-opening.

Bruggeman stated that the wording is crucial, but there is also flexibility in how it is presented. For example, a new paragraph, as proposed; or provide more detailed explanations in a Q&A format; or even combine both approaches. He stated that he is not in favor of using an interpretation, which the Statutory Accounting Principles (E) Working Group occasionally does. He stated that, instead, incorporating changes into a new paragraph 18 in SSAP No. 61 or expanding the A-791 Q&A seems like a more practical approach. He stated that, as Hemphill pointed out, many of these issues require a qualitative rather than purely quantitative evaluation. It is about recognizing when something does not seem right, when something raises yellow or even red flags. This approach can help ensure they address the nuances effectively.

Having no further business, the joint meeting of the Statutory Accounting Principles (E) Working Group and Life Actuarial (A) Task Force adjourned.

https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2025/08-11-25 Summer National Meeting/Hearing/02 - Meeting Minutes 04-10-25.docx