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

**Amendment Proposal Form**

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| --- | --- | --- | --- |
| **Dates:** Received | Reviewed by Staff | Distributed | Considered |
| 04/16/2019 | RM |  |  |
| **Notes:** VM APF 2019-39 (CA OPBR & NAIC PBR) |

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

This APF was jointly prepared by the Staff of Office of Principle-Based Reserving, California Department of Insurance and NAIC Support Staff.

This APF develops an **interim solution for 2020** to address recommendation #26 from VAWG’s 10/24/2018 memo regarding PBR Recommendations and Referrals to LATF.

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

Valuation Manual (January 1, 2019 edition), as amended by APF 2018-48, VM-20 Section 8.C

1. 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.)

Please see the attached Appendix.

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

Please see the attached Appendix.

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NAIC Staff Comments:

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# Appendix

#### ISSUE:

#### During the review of 2017 PBR reports, regulators noted wide variance in the modeled future YRT premium rates. During the review of the 2018 PBR reports, regulators noted that this wide variance was persisting. This wide variance does not appear to be driven by differences in the situations of, and increases likely to be experienced by, the different companies. Companies expressed uncertainty in how to develop this prudent estimate assumption. Many companies also expressed a desire that additional guidance be added to the Valuation Manual on this aspect of PBR.

While regulators were concerned with the lack of support for the assumptions applied in the PBR reports, this appeared to be an inevitable result of the difficulty of determining an appropriate prudent estimate assumption for future YRT premium rates. Regulators found that even more concerning was the apparent unfairness across companies that the diverse approaches created.

Several proposals have been put forward. One recent suggestion was to go with a ½ cx approach as an interim measure until a consensus can be developed around something more principles-based. This APF sets forth language for this interim solution.

#### SECTIONS:

VM-20 Section 8.C

#### REDLINE OPTION 1:

**VM-20 Section 8.C**

C. Reflection of Reinsurance Cash Flows in the Deterministic Reserve or Stochastic Reserve

For policies issued on or after 1/1/2020, and optionally for policies issued on or after 1/1/2017 and before 1/1/2020:

For non-guaranteed YRT reinsurance ceded or assumed, the cash-flow modeling requirements in Sections 8.C.1 through 8.C.14 below do not apply since non-guaranteed YRT reinsurance ceded or assumed does not need to be modeled; see Section 8.C.18 below. YRT shall include other reinsurance arrangements that are similar in effect to YRT.

In calculations of the deterministic reserve or stochastic reserve pursuant to Section 4 and Section 5:

**…….**

1. For policies issued on or after 1/1/2020, and optionally for policies issued on or after 1/1/2017 and before 1/1/2020:

When the reinsurance ceded or assumed is on a non-guaranteed YRT or similar basis, the corresponding reinsurance cash flows do not need to be modeled. Rather, for a ceding company, the post-reinsurance-ceded DR or SR shall be the pre-reinsurance-ceded DR or SR pursuant to Section 8.D.2 plus any applicable provision pursuant to Section 8.C.15 and Section 8.C.17, minus the NPR reinsurance credit from Section 8.B. For an assuming company, the DR or SR for the business assumed on a non-guaranteed YRT or similar basis shall be set equal to the NPR from Section 3.B.8 plus any applicable provision pursuant to Section 8.C.16 and Section 8.C.17. In the case where there are also other reinsurance arrangements that are not on a non-guaranteed YRT or similar basis, the reinsurance credit shall include the modeled reinsurance credit reflecting those other reinsurance arrangements. In particular, where there are also other reinsurance arrangements that are dependent on the non-guaranteed YRT or similar arrangements, actuarial judgment shall be used to project cash flows consistent with the above outlined treatment for non-guaranteed YRT or similar arrangements.

**Guidance Note:** The above method is an interim approach. A longer-term solution to YRT is intended to be adopted by regulators, after regulators and industry have had additional time to consider and evaluate the variety of approaches that have been put forward as potential longer-term solutions.

***REDLINE OPTION 2:***

For non-guaranteed YRT reinsurance ceded or assumed, the cash-flow modeling requirements in Sections 8.C.1 through 8.C.14 below do not apply since non-guaranteed YRT reinsurance ceded or assumed does not need to be modeled; see Section 8.C.18 below. YRT shall include other reinsurance arrangements that are similar in effect to YRT.

In calculations of the deterministic reserve or stochastic reserve pursuant to Section 4 and Section 5:

**…….**

1. When the reinsurance ceded or assumed is on a non-guaranteed YRT or similar basis, the corresponding reinsurance cash flows do not need to be modeled. Rather, for a ceding company, the post-reinsurance-ceded DR or SR shall be the pre-reinsurance-ceded DR or SR pursuant to Section 8.D.2 plus any applicable provision pursuant to Section 8.C.15 and Section 8.C.17, minus the NPR reinsurance credit from Section 8.B. For an assuming company, the DR or SR for the business assumed on a non-guaranteed YRT or similar basis shall be set equal to the NPR from Section 3.B.8 plus any applicable provision pursuant to Section 8.C.16 and Section 8.C.17. In the case where there are also other reinsurance arrangements that are not on a non-guaranteed YRT or similar basis, the reinsurance credit shall include the modeled reinsurance credit reflecting those other reinsurance arrangements. In particular, where there are also other reinsurance arrangements that are dependent on the non-guaranteed YRT or similar arrangements, actuarial judgment shall be used to project cash flows consistent with the above outlined treatment for non-guaranteed YRT or similar arrangements.

**Guidance Note:** The above method is an interim approach. A longer-term solution to YRT is intended to be adopted by regulators, after regulators and industry have had additional time to consider and evaluate the variety of approaches that have been put forward as potential longer-term solutions.

#### REASONING:

#### As PBR becomes mandatory in 2020, the 2020 Valuation Manual should include clear guidance on the handling of YRT reinsurance.

#### While this treatment is mandatory for 2020, it is intended to be an optional approach for 2019 as well, while other approaches are being more thoroughly vetted.

#### Note that if the approach currently used or planned to be used by a company for modeling YRT is clearly more conservative than this approach, the company is permitted but not required to continue to hold the resulting higher reserve.