

Financial Reporting of Portfolio Retroactive Reinsurance

CLRS Meeting
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Agenda

- Problem definition
- Current retroactive reinsurance accounting
 - Including gaps in the guidance
- What we observed given those gaps
- Resulting distortions
- Latest developments



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Problem definition

- The current statutory accounting guidance (SAP) is deficient with regard to retroactive reinsurance
- As a result, RBC results and Schedule P analysis can be distorted.



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Current treatment of retroactive reinsurance under SAP

- Ceded and assumed losses not in “losses”
- Retroactive Reins. Reserves are write-in liabilities
 - Hence retroactive reinsurance doesn’t reduce:
 - Reported Net Loss Reserves
 - RBC Capital Requirement
 - Any surplus benefit recognized, but “restricted”
- In contrast, prospective reinsurance
 - Lowers reserves for cedant
 - Lowers required RBC, (generally) improves leverage ratios.

Prospective treatment more “favorable”

Some retroactive reins can get Prospective treatment



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Retroactive treatment versus Prospective treatment

- Balance sheet impact of transfer of \$1,000 in loss reserves

Liabilities	BEFORE		AFTER - Retropective Treatment		AFTER - Prospective treatment	
	cedant	reinsurer	cedant	reinsurer	cedant	reinsurer
L&LAE o/s	7000	0	7000	0	6000	1000
write-in liab.	0	0	-1000	1000	0	0



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When can Retroactive Reins. get Prospective Reins. Treatment?

Per SSAP 62R, paragraph 36 (2019 version)

- Novations
 - When cedant's liability is "completely extinguished"
- Intercompany reinsurance agreements
 - Among companies 100% owned by common parent
 - As long as no surplus gain as a result
- "Runoff agreements" *per paragraphs 102-105*
- (2 other misc. situations not relevant to our discussion)



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What is required for a “Runoff Agreement” to get Prospective treatment?

- Transfer “*essentially all the risks and benefits of a specific line ... or market segment **that is no longer actively marketed** by the [cedant]*”
- Only applies to non-affiliate agreements.
- No profit sharing, retrospective rating, etc.
- Agreement can’t include other lines.



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Accounting for “Runoff Agreements”

- Ceded premium recorded as a paid loss by both cedant and assuming company.
 - Cedant – premium recorded as positive paid loss
 - (presumably split to line, AY)
 - Assuming co. – premium recorded as negative paid
- Assuming co. reports the business in same lines as ceding company.
- Result should eliminate distortion in loss development of cedant, industry.



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Market observation

- Recent agreements transfer prior accident years of existing lines, markets, while still active in those lines, markets. (retroactive reins. acting)
- Some seem to move the liabilities to runoff entities, sometimes for transfer outside the group or country (sale or reinsurance)
- Don't qualify for "Runoff Agreement" status if with non-affiliates
- No guidance on Schedule P treatment if with affiliates.



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COPLFR 5/21/19 Letter

Pointed out the Inconsistent Treatment of Loss Portfolio Transfers in Schedule P reporting.



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Industry Inconsistency in Reporting Transactions



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Allianz 2015 Cessions

- In 2015 Allianz Global Risks US Insurance Company (“Allianz”) ceded much of its 2012 & prior Workers Compensation (“WC”) business to a US affiliate, San Francisco Reinsurance (“San Francisco Re”). San Francisco Re is now named Allianz Reinsurance of America, Inc. (“Allianz Re”). In doing so it treated all the consideration paid as calendar year (CY) 2015 ceded earned premium. Initially, as of December 31, 2015, Allianz included all of the ceded losses in accident year (“AY”) 2015. However, for the following year (as of December 31, 2016), Allianz recorded the ceded losses across the subject AYs 2012 and prior.



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Allianz 2015 Cessions (continued)

- This approach distorted the 2015 CY and AY loss ratios and the loss development patterns for AYs 2015 and 2012 & prior. We have attached the relevant Schedule P excerpts from Allianz's 2015 and 2016 Annual Statements as Attachment A. Descriptions of the transaction are described in the Allianz Re Statement of Actuarial Opinion as of December 31, 2018, also a public document, in Attachment A1SAO. The Management Discussion and Analysis for Allianz Re as of December 31, 2018 is attached as Attachment A2MDA.



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Allianz Re 2015 Schedule P, Assuming Company



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ANNUAL STATEMENT FOR THE YEAR December 31, 2015 OF THE Allianz Reinsurance Amer Inc. (NAIC #21911)

SCHEDULE P - PART 1 - Workers' Compensation
(\$000 Omitted)

		1	2	3	4	5	6	7	8	9	11	26	27	28	35	36	
		Premiums Earned			Loss and Loss Expense Payments											Net Reserves	
Years in Which Premiums	Were Earned and Losses Were Incurred	Direct and Assmd	Ceded	Net (Cols. 1-2)	Loss Payments		DCC Payments		A&O Payments		Total Net	Total Losses and Loss Expenses Incurred			After Discount		
					Direct and Assmd	Ceded	Direct and Assmd	Ceded	Direct and Assmd	Ceded	Paid (Cols. 4 - 5 + 6 - 7 + 8 - 9)	Direct and Assumed	Ceded	Net	Losses Unpaid	Loss Exp.	
1	Prior	XXX	XXX	XXX	24,464	188	2,586	0	1,750	0	28,611	XXX	XXX	XXX	818,272	54,692	
2	2006	0	0	0	834	0	88	0	49	0	971	19,770	0	19,770	17,205	1,594	
3	2007	0	0	0	681	0	70	0	41	0	792	20,888	0	20,888	18,458	1,638	
4	2008	0	0	0	893	0	135	0	46	0	1,074	16,185	0	16,185	13,492	1,619	
5	2009	0	0	0	1,796	0	116	0	48	0	1,960	17,287	0	17,287	13,336	1,992	
6	2010	0	0	0	1,562	0	282	0	63	0	1,906	28,451	0	28,451	22,981	3,565	
7	2011	0	0	0	3,093	0	471	0	97	0	3,661	51,122	0	51,122	41,890	5,570	
8	2012	0	0	0	4,899	0	595	0	106	0	5,600	48,172	0	48,172	35,576	6,995	
9	2013	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	
10	2014	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	
11	2015	1,093,283	0	1,093,283	0	0	0	0	0	0	0	0	0	0	0	0	
12	Totals	XXX	XXX	XXX	38,222	188	4,343	0	2,200	0	44,575	XXX	XXX	XXX	981,210	77,665	



ANNUAL STATEMENT FOR THE YEAR December 31, 2015 OF THE Allianz Reinsurance Amer Inc. (NAIC #21911)

SCHEDULE P - PART 2 - Workers' Compensation

		1	2	3	4	5	6	7	8	9	10	11	12	
		INCURRED NET LOSSES AND DEFENSE AND COST CONTAINMENT EXPENSES REPORTED AT YEAR END (\$000 OMITTED)											DEVELOPMENT	
Years in Which Losses Were Incurred		2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	One Year	Two Year	
1	Prior	755	4,782	6,660	9,018	9,184	11,628	18,993	18,696	18,911	896,993	878,082	878,297	
2	2006	0	0	0	0	0	0	0	0	0	19,346	19,346	19,346	
3	2007	XXX	0	0	0	0	0	0	0	0	20,534	20,534	20,534	
4	2008	XXX	XXX	0	0	0	0	0	0	0	15,788	15,788	15,788	
5	2009	XXX	XXX	XXX	0	0	0	0	0	0	16,875	16,875	16,875	
6	2010	XXX	XXX	XXX	XXX	0	0	0	0	0	27,910	27,910	27,910	
7	2011	XXX	XXX	XXX	XXX	XXX	0	0	0	0	50,287	50,287	50,287	
8	2012	XXX	XXX	XXX	XXX	XXX	XXX	0	0	0	47,260	47,260	47,260	
9	2013	XXX	XXX	XXX	XXX	XXX	XXX	XXX	0	0	0	0	0	
10	2014	XXX	XXX	XXX	XXX	XXX	XXX	XXX	XXX	0	0	0	XXX	
11	2015	XXX	XXX	XXX	XXX	XXX	XXX	XXX	XXX	XXX	0	XXX	XXX	
12	Total											1,076,082	1,076,297	



ANNUAL STATEMENT FOR THE YEAR December 31, 2015 OF THE Allianz Reinsurance Amer Inc. (NAIC #21911)

SCHEDULE P - PART 4 - Workers' Compensation

	Years in Which Losses Were Incurred	BULK AND IBNR RESERVES ON NET LOSSES AND DEFENSE AND COST CONTAINMENT EXPENSES REPORTED AT YEAR END (\$000 OMITTED)									
		1 2006	2 2007	3 2008	4 2009	5 2010	6 2011	7 2012	8 2013	9 2014	10 2015
1	Prior	395	0	500	392	-1,084	1,605	6,723	5,900	5,708	331,108
2	2006	0	0	0	0	0	0	0	0	0	5,676
3	2007	XXX	0	0	0	0	0	0	0	0	5,533
4	2008	XXX	XXX	0	0	0	0	0	0	0	8,706
5	2009	XXX	XXX	XXX	0	0	0	0	0	0	9,115
6	2010	XXX	XXX	XXX	XXX	0	0	0	0	0	15,233
7	2011	XXX	XXX	XXX	XXX	XXX	0	0	0	0	23,113
8	2012	XXX	XXX	XXX	XXX	XXX	XXX	0	0	0	26,990
9	2013	XXX	XXX	XXX	XXX	XXX	XXX	XXX	0	0	0
10	2014	XXX	XXX	XXX	XXX	XXX	XXX	XXX	XXX	0	0
11	2015	XXX	XXX	XXX	XXX	XXX	XXX	XXX	XXX	XXX	0



Allianz Global Risks US
Insurance Company (“Allianz”)
2016 Schedule P, Ceding
Company



ANNUAL STATEMENT FOR THE YEAR December 31, 2016 OF THE Allianz Global Risks US Ins Co (NAIC #35300)

SCHEDULE P - PART 1 - Workers' Compensation (\$000 Omitted)

	1	2	3	4	5	6	7	8	9	10	11	26	27	28	35	36	
	Premiums Earned			Loss and Loss Expense Payments										Total Losses and Loss Expenses Incurred		Net Reserves	
Years in Which				Loss Payments		DCC Payments		A&O Payments		Total Net				After Discount		Loss	
Premiums	Direct and Assmd	Ceded	Net (Cols. 1-2)	Direct and Assmd	Ceded	Direct and Assmd	Ceded	Direct and Assmd	Ceded	Salv. and Sub. Received	Paid (Cols. 4-9)	Direct and Assumed	Ceded	Net	Losses Unpaid	Exp.	
Were Earned and											5 + 6 - 7 + 8 - 9)						
Losses Were Incurred																Unpaid	
1 Prior	XXX	XXX	XXX	60,328	55,605	5,347	5,261	1,922	1,952	0	4,779	XXX	XXX	XXX	-33,120	851	
2 2007	180,051	849	179,202	82,235	2,489	6,736	146	48,686	31	454	134,991	154,018	8827	145,191	10,154	46	
3 2008	140,259	795	139,464	68,516	2,009	5,917	212	43,170	70	1,186	115,312	141,629	12885	128,744	14,525	-1,092	
4 2009	120,600	640	119,960	69,979	1,564	6,033	172	43,507	66	600	117,717	133,176	11983	121,193	3,601	-126	
5 2010	127,176	856	126,320	80,871	2,184	8,186	440	11,236	107	586	97,562	124,613	19405	105,209	7,551	96	
6 2011	139,307	812	138,495	90,678	6,935	10,187	840	14,517	142	654	107,465	151,493	27194	124,300	16,798	37	
7 2012	139,822	573	139,249	69,447	26,850	9,626	3,365	13,628	199	288	62,287	130,702	59529	71,173	9,173	-287	
8 2013	117,182	66	117,116	42,795	-1,616	6,645	-72	24,952	155	171	75,925	89,427	-30361	119,788	28,542	15,320	
9 2014	95,298	-1	95,299	22,207	-2,432	3,669	582	26,280	158	3,041	53,848	89516	1858	87658	21496	12314	
10 2015	84,691	1,096,983	-1,012,292	15,672	-182	2,254	-1	11,536	192	-34	29,453	30657	-38494	69151	36342	3356	
11 2016	81,500	37,233	44,267	6,229	24	546	4	0	0	4	6,747	56004	-793	56797	41804	8245	
12 Totals	XXX	XXX	XXX	608,957	93,430	65,146	10,949	239,434	3,072	6,949	806,086	XXX	XXX	XXX	156,866	38,760	



ANNUAL STATEMENT FOR THE YEAR December 31, 2016 OF THE Allianz Global Risks US Ins Co (NAIC #35300)

SCHEDULE P - PART 2 - Workers' Compensation

	1	2	3	4	5	6	7	8	9	10	11	12	
	INCURRED NET LOSSES AND DEFENSE AND COST CONTAINMENT EXPENSES REPORTED AT YEAR END (\$000 OMITTED)											DEVELOPMENT	
Years in Which	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	One Year	Two Year	
Losses Were Incurred											Year	Year	
1 Prior	1,363,472	1,464,398	1,469,018	1,506,222	1,705,343	1,774,182	1,772,283	1,813,625	1,393,292	779,869	-613,423	-1,033,756	
2 2007	96,498	98,577	98,810	115,352	107,525	117,505	118,394	117,295	107,759	96,490	-11,269	-20,805	
3 2008	XXX	92,774	85,884	87,822	83,678	90,600	89,155	88,497	96,718	86,286	-10,432	-2,211	
4 2009	XXX	XXX	72,007	83,965	77,066	87,258	89,632	90,983	91,622	77,877	-13,745	-13,106	
5 2010	XXX	XXX	XXX	91,281	86,700	99,699	115,477	112,953	113,569	93,984	-19,585	-18,969	
6 2011	XXX	XXX	XXX	XXX	116,821	119,114	143,200	135,068	136,858	109,898	-26,960	-25,170	
7 2012	XXX	XXX	XXX	XXX	XXX	104,076	110,637	115,235	-504,584	58,031	562,615	-57,204	
8 2013	XXX	XXX	XXX	XXX	XXX	XXX	75,542	85,604	92,304	90,977	-1,327	5,373	
9 2014	XXX	XXX	XXX	XXX	XXX	XXX	XXX	62,935	68,190	57,715	-10,475	-5,220	
10 2015	XXX	XXX	XXX	XXX	XXX	XXX	XXX	XXX	44,320	67,856	23,536	XXX	
11 2016	XXX	XXX	XXX	XXX	XXX	XXX	XXX	XXX	XXX	51,517	XXX	XXX	
12 Total											-121,067	-1,171,069	



ANNUAL STATEMENT FOR THE YEAR December 31, 2016 OF THE Allianz Global Risks US Ins Co (NAIC #35300)

SCHEDULE P - PART 4 - Workers' Compensation

Years in Which Losses Were Incurred		BULK AND IBNR RESERVES ON NET LOSSES AND DEFENSE AND COST CONTAINMENT EXPENSES REPORTED AT YEAR END (\$000 OMITTED)									
		1	2	3	4	5	6	7	8	9	10
		2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
1	Prior	317,103	317,821	251,603	217,303	355,281	381,466	358,102	377,962	12,591	-210
2	2007	50,160	27,859	20,236	23,857	9,244	19,248	15,838	13,735	8,454	0
3	2008	XXX	50,888	23,883	20,728	8,753	11,767	11,280	9,109	14,285	5,363
4	2009	XXX	XXX	37,460	24,602	8,924	13,316	13,882	12,162	12,096	0
5	2010	XXX	XXX	XXX	45,939	15,898	16,524	23,679	17,695	17,658	0
6	2011	XXX	XXX	XXX	XXX	60,402	24,431	38,698	22,723	22,258	26
7	2012	XXX	XXX	XXX	XXX	XXX	58,843	40,415	33,034	32,912	0
8	2013	XXX	XXX	XXX	XXX	XXX	XXX	45,641	36,464	35,609	31,146
9	2014	XXX	XXX	XXX	XXX	XXX	XXX	XXX	35,763	36,534	23,394
10	2015	XXX	XXX	XXX	XXX	XXX	XXX	XXX	XXX	22,846	36,913
11	2016	XXX	XXX	XXX	XXX	XXX	XXX	XXX	XXX	XXX	31,365



GEICO 2014 Cessions

- In 2014 Government Employees Insurance Company (“GEICO”) ceded half of its loss and Loss Adjustment Expense (hereinafter collectively referred to as “loss”) reserves as of January 1, 2014 to its indirect parent, National Indemnity Company (NICO). In doing so it treated the consideration paid as ceded earned premium spread to prior CYs (based on the allocation of loss reserves by AY as of January 1, 2014), with the ceded losses also spread across prior AYs. This avoided distorting the CY/AY loss ratios but did distort the loss development patterns. We have attached the Schedule P and Note 21 excerpts from the 2014 GEICO Annual Statement as Attachment B.



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ANNUAL STATEMENT FOR THE YEAR December 31, 2014 OF THE Government Employees Ins Co. (NAIC #22063)

SCHEDULE P - PART 1 - Private Passenger Auto Liability (\$000 Omitted)

Table with 12 columns and multiple rows showing financial data for Private Passenger Auto Liability, including premiums earned, loss payments, and adjustments.

Table with 25 columns and multiple rows showing financial data for Private Passenger Auto Liability, including losses unpaid, defense and cost containment, and adjusting other unpaid.

Table with 36 columns and multiple rows showing financial data for Private Passenger Auto Liability, including total losses and expenses incurred, loss and expense percentage, and net balance sheet reserves.



ANNUAL STATEMENT FOR THE YEAR December 31, 2014 OF THE Government Employees Ins Co. (NAIC #22063)

SCHEDULE P - PART 2 - Private Passenger Auto Liability

Table with 12 columns and multiple rows showing incurred net losses and defense and cost containment expenses reported at year end, including development data.



Impact on Schedule P and RBC of Different Reporting Treatments



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Impact on Schedule P

- Both transactions had the potential to materially distort industry totals with regard to loss development. They also most likely did distort data used in the RBC calculations for those companies. We note that neither SSAP 62R nor Schedule P instructions provide guidance as to what should be done in these cases. Whether to record ceded earned premium all to one CY (Allianz 2015), or to all the CYs with impacted Ays (Geico Schedule P Part 2 CY 2014), appears to be up to the individual company's option (possibly subject to regulatory approval and/or direction). We also note that these transactions can distort other schedules on the Annual Statement such as Page 3, the Underwriting and Investment Exhibits, and Schedule F.



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Impact on Schedule P (continued)

- For those agreements meeting the definition of “Run-Off Agreements” in SSAP 62R (paragraph 81), the required accounting is clear. The ceded earned premium from such agreements is to be recorded as a negative paid loss, so as not to distort the incurred development data by AY. But neither the GEICO nor Allianz agreements were “run-off” agreements, as they transferred only a portion of the prior book (and the ceding companies were still writing new business for that line/market). In addition, the “run-off” agreement accounting guidance in SSAP 62R does not apply to affiliate transactions (per SSAP 62, paragraph 102, last sentence).



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How was RBC impacted?

Premium Risk (R5) Impacts

- Charge by line based on NWP for that line
 - If $NWP < 0$, charge is zero, despite ongoing writings
 - Under “runoff agreement” method, charge would still exist.
- Overall premium charge adjusted for diversification
 - Premium Concentration Factor (PCF) distorted
 - $PCF = \text{largest line NWP} / \text{Total all lines NWP (incl. } < 0 \text{ lines)}$
- Company Experience adjustment
 - Average loss ratio for 10 AYs, company compared to industry
 - Years with negative premium removed from the average
 - For company, that CY/AY may be removed
 - What happens to the industry number? Distortion removed or kept in?



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How was RBC impacted?

- Reserve Risk (R4) Impacts
 - Company Experience adjustment distorted

AY	Net incurred at year-end										one yr	
	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	Dvlpmnt	
Prior	1,363	1,464	1,469	1,506	1,705	1,774	1,772	1,814	1,393	780	-613	
2007	96	99	99	115	108	118	118	117	108	96	-12	
2008		93	86	88	84	91	89	88	97	86	-11	
2009			72	84	77	87	90	91	92	78	-14	
2010				91	87	100	115	113	114	94	-20	
2011					117	119	143	135	137	110	-27	
2012						104	111	115	-505	58	563	
2013							76	86	92	91	-1	
2014								63	68	58	-10	
2015									44	68	24	
2016										52		
										Total	-121	
	Current values for those years				739							
	Initial values for 9 prior AY				756							
	Current to Initial				0.9775							
	<u>If AY 2012 & Prior had zero dvlpmnt post 2014</u>											
	Current values for those years				876							
	Initial values for 9 prior AY				756							
	Current to Initial				1.1587							

Diagram annotations: A blue line starts at the 2007 value (96) and trends downwards to the 2016 value (52). An arrow labeled "initial" points to the 2011 value (117). An arrow labeled "current" points to the 2010 value (94).



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How was RBC impacted?

- Reserve Risk (R4) Impacts, cont.
 - Prior slide shows how company avg dvlpmnt distorted.
 - Company value is divided by industry value.
 - How is industry value impacted?
 - That is one reason why we asked NAIC P&C RBC Working Group to look into the issue.
 - If industry value is impacted, everyone's RBC is affected that wrote that line.



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Other Distortions

- Line of business mix for transaction year
- Leverage ratios based on NWP
- Average development data for company, industry(?)
- IRIS ratio tests based on loss development



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Latest news

- COPLFR letter sent to NAIC:
 - CASTF – normal source of Schedule P instructions
 - Statutory Accounting Working Group (SAPWG)– source of SSAPs
 - Cc'd to P&C RBC Working Group – source of P&C RBC formula
- CASTF and SAPWG have this on their future working agendas.
- On a related note, new NAIC Working Group -
Restructuring Mechanisms Working Group



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