

Reinsurance Credit Risk Exposure

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CAS Seminar on Reinsurance

May 19, 2008



Overview

- Introduction
- Schedule F
 - Overview
 - Provision for Reinsurance (Schedule F penalty)
- Different Approach to Estimating a Reinsurance 'Haircut'
 - Analysis of a Bad Debt Contingency
 - NAIC Proposed Reinsurance Modernization

2 May 19, 2008

Schedule F

- Part 1 – Assumed Reinsurance
- Part 2 – Portfolio Reinsurance
- **Part 3 – Ceded Reinsurance**
- Part 4 – Aging of Ceded Reinsurance
- Part 5 – Unauthorized Reinsurers
- Part 6 – Overdue Authorized Reinsurance
- Part 7 – Slow-Paying Authorized Reinsurers
- Part 8 – Restatement of Balance Sheet

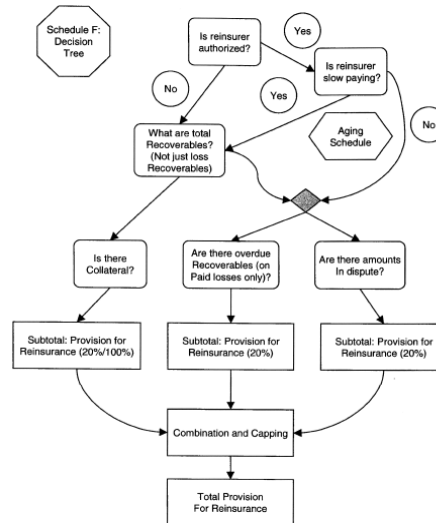
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Provision for Reinsurance

- Unauthorized Reinsurers
 - 100% of unsecured recoverable
 - 20% of recoverable more than 90 days past due
 - 20% of amounts in dispute
- Slow-Paying Authorized Reinsurers
 - Greater of 20% of unsecured recoverable or 20% of recoverable more than 90 days past due
- Other Authorized Reinsurers
 - 20% of recoverable more than 90 days past due
 - 20% of the amounts in dispute

4 May 19, 2008

Provision for Reinsurance



Source: Feldblum, S., "Reinsurance Accounting: Schedule F"

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Provision for Reinsurance

- SSAP No. 62 – "...Provision for Overdue Reinsurance provides for a minimum reserve for uncollectible reinsurance with an additional reserve required if an entity's experience indicates that a higher amount should be provided."

6 May 19, 2008

Ceded Reinsurance Bad Debt Analysis

- Total Reinsurance Recoverable by Reinsurer
 - Schedule F, Part 3
- Offsets
 - Amounts due to the Reinsurer, Funds Held By Company
 - Schedule F, Part 3 (All Companies)
 - Other Allowed Offsets (LOCs, Ceded Balances Payable, etc.)
 - Schedule F, Part 5 (Unauthorized Companies)
 - Potential Others Not Shown on Schedule F
 - Other Allowed Offsets (Authorized Companies)
- Net Recoverable = Total Recoverable – Offsets

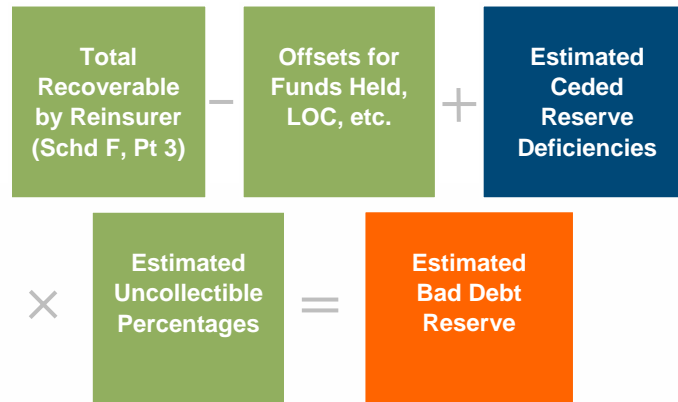
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Ceded Reinsurance 'Bad Debt' Analysis

- Allocate ceded reserve deficiency to reinsurer
 - Mapping by year, business segment, case reserves, LOB
- Estimate a range of uncollectible percentages by reinsurer
 - Ratings from S&P, AM Best, Moody's
 - Historical default percentages for S&P and Moody's ratings are available
 - Discussion with company personnel (relationships with reinsurers, etc.)
 - Discussion with lawyers
 - Various other publicly available information
- Apply the range of uncollectible percentages for each reinsurer to the net recoverable including allocated reserve deficiencies

8 May 19, 2008

Ceded Reinsurance 'Bad Debt' Analysis



9 May 19, 2008

Ceded Reinsurance 'Bad Debt' Analysis

<u>Segment</u>		<u>Low</u>	<u>Best</u>	<u>High</u>
Line A	Recorded Recoverable (Schd F)	1,905	1,905	1,905
	Estimated Uncollectible Based on Recorded	107	203	298
	Estimated Deficiency	1,179	1,179	1,179
	Estimated Uncollectible on Deficiency	66	125	184
Line B	
TOTAL	Recorded Recoverable (Schd F)	26,285	26,285	26,285
	Estimated Uncollectible Based on Recorded	425	620	815
	Estimated Deficiency	2,493	2,493	2,493
	Estimated Uncollectible on Deficiency	257	352	442
	Provision for Disputes	85	100	125
	Company Booked Bad Debt	195	195	195
	Additional Provision for Bad Debt	572	877	1,188

10 May 19, 2008

NAIC Proposed Reinsurance Modernization

- Re-evaluating Regulatory Framework for Reinsurance
 - Market changes are the impetus for the shift
 - Globalization
 - Increased cross-border reinsurance
 - International accounting standards
 - Regulatory harmonization
- Goal of NAIC Reinsurance Task Force
 - ‘Facilitate cross-border transactions and enhance competition within the U.S. market while ensuring that U.S. insurers and policyholders are adequately protected against the risk of insolvency.’

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NAIC Proposed Reinsurance Modernization

- Reinsurance Supervision Review Department (RSRD)
 - Determines which non-U.S. jurisdictions are entitled to enter into mutual recognition agreements
- Port of Entry State (POE)
 - A single state regulator for all reinsurers doing business in the U.S.
 - Assigns a rating to each reinsurer
 - Evaluation of financial strength
 - Operating integrity
 - Business operations
 - Claims paying history
 - Management expertise, etc.

12 May 19, 2008

NAIC Proposed Reinsurance Modernization

- POE assigned Reinsurer Ratings

<u>Rating Band</u>	<u>Collateral Required*</u>	<u>A.M. Best</u>	<u>S&P</u>	<u>Moody's</u>	<u>Fitch</u>
1	0%	A++	AAA	Aaa	AAA
2	10%	A+	AA+, AA-	Aa1 to Aa3	AA+, AA-
3	20%	A, A-	A+ to A-	A1 to A3	A+ to A-
4	75%	B++ to B+	BBB+ to BBB-	Baa1 to Baa3	BBB+ to BBB-
5	100%	B to F	BB+ to R, NR	Ba1 to C	BB+ to DD

* For POE Reinsurers

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NAIC Proposed Reinsurance Modernization

- U.S. Licensed reinsurers
 - 0% collateral for Tier 3 or above
 - 75% collateral for Tier 4 (same as POE Reinsurer)
 - 100% collateral for Tier 5 (same as POE Reinsurer)
- Unlicensed reinsurers
 - 100% collateral requirements

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NAIC Proposed Reinsurance Modernization

2006

Reinsurance Task Force directed to develop alternatives to current reinsurance regulatory framework

2006-2008

Ideas and discussion ensue regarding potential changes. Goal is to complete revised regulator framework by the end of 2008

2009

Implementation?

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NAIC Proposed Reinsurance Modernization

- Outstanding Issues
 - Establish collateral levels on a prospective basis
 - Runoff issues
 - Treatment of downgrades
 - Slow pay reinsurers
 - Amount of collateral relative to perceived risk
 - Uniformity among the states
 - Implementation issues

16 May 19, 2008