

Source: SNL Financial
Friday, December 07, 2012 9:48 AM CT

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While 43 insurance commissioners approved the NAIC's new directive for implementing principles-based reserving, as few as three could block the process indefinitely. As the NAIC prepares a renewed focus on enacting principles-based reserving, opposing sides may be digging in.

The [Valuation Manual](#), which establishes minimum reserve and related requirements for enacting the NAIC's Standard Valuation Law, must be adopted by at least three-quarters of member jurisdictions — 42 states. Those states must also represent greater than 75% of the direct premiums written on 2008 life statements, annuity and health statements and fraternal statements, according to the valuation law.

New York and California, the two largest states in terms of direct premiums and annuity considerations, are strongly opposed to the implementation process as currently constituted and [voted against](#) the manual at the conclusion of the NAIC's fall national meeting Dec. 2. Combined, they held 19.1% of 2008 premium volume, according to SNL data. (SNL's analysis does not include fraternal insurers, but given the relatively limited number of such institutions, the impact would likely be minimal.) If just a few of the states whose regulators also voted against the manual take no action — or if Texas or Florida alone changes sides — the 75% threshold will not be reached.

The shift to principles-based reserving — which proponents estimate could take as long as [eight years](#) — is a dangerous loosening of standards, New York State Superintendent of Financial Services Benjamin Lawsky contends. For insurers, the potential for eliminating perceived reserve redundancies is understandable, he said in a statement.

States attracting large amounts of life business in 2008
Ranked by premiums & considerations, top 20 shown

State	Direct premiums & considerations (\$B) ¹	Amount in state/total US (%) ²
New York	77.2	10.22
California	66.9	8.85
Texas	45.7	6.05
Florida	45.3	5.99
Delaware	34.4	4.56
Pennsylvania	31.5	4.17
New Jersey	29.4	3.89
Illinois	28.9	3.83
Ohio	27.0	3.58
Michigan	21.7	2.87
Massachusetts	21.1	2.80
Connecticut	20.2	2.67
North Carolina	20.0	2.65
Georgia	17.5	2.31
Virginia	17.4	2.31
Iowa	16.7	2.21
Indiana	15.0	1.99
Wisconsin	15.0	1.98
Missouri	13.9	1.84
Colorado	13.9	1.84
Top 20 total	578.8	76.61

A&H = Accident and health.
 Data compiled on Dec. 5, 2012.
 1 Reflects sum of life insurance, annuity considerations, A&H, deposit-type contract funds, disability, long-term care and other considerations, as reported in the Schedule T section of annual filings with the NAIC.
 2 Includes District of Columbia and U.S. territories.
 Selected business lines are based on the NAIC's Valuation Manual, which outlines reserve requirements for various products, including A&H, credit life and disability.
 Based on NAIC statutory life statements. U.S. filers only.
 Source: SNL Financial

"As we move into an era of long-term low interest rates and other investment challenges, there appears no clear benefit for consumers to let insurance companies have a smaller cash cushion," Lawsky said. "We should not ignore one of the clear lessons of the financial crisis — that deregulation and laissez-faire attitudes by regulators can have disastrous consequences for all parties involved."

Incoming NAIC President and Louisiana Insurance Commissioner James Donelon rebutted Lawsky's assessment.

"We've talked ad nauseam with them about the fact that this is not a lesser standard. It's a different standard and one that's more relevant to the modern, complex life insurance industry that we live with, that we regulate," Donelon told SNL. "They feel more comfortable with the system that's been there for decades. Change comes slowly, and we recognize that."

"Self-regulation, incomplete oversight and untransparent complexity were major causes of the recent financial crisis. We should be very careful before proceeding back down that road," Lawsky replied through a spokesman.

The NAIC will review and manage the Valuation Manual and principles-based reserving issues through a new [joint operation](#) of its life insurance and financial condition committees. Part of the mission, Donelon said, will be to consider life insurers' use of captives for reinsurance, which has been the subject of intense review by an existing NAIC subgroup and New York state regulators, among others.

Proponents of adopting the manual and implementing principles-based reserving have said its acceptance will make concerns over such captives no longer necessary. Industry groups have generally [taken](#) the position that the captive use is worthy of study, but that risks are overrated. [New York Life Insurance Co.](#), however, [warned](#) that some insurers may be abusing the practice by inadequately transferring risk.

Some of California's Valuation Manual concerns should be more readily addressed, Donelon said. California Insurance Commissioner Dave Jones cited uncertainties about the costs of complying with new standards, both for his large department and for smaller insurers.

North Carolina Insurance Commissioner Wayne Goodwin seconded California's concerns about resources, particularly for the small domestic life insurance market in his state. The Tar Heel State accounted for approximately 2.7% of direct premiums written in 2008. "There were still too many unanswered questions," he told SNL.

If either New York or California can be persuaded to endorse the process, smaller states that objected may be persuaded to sign on, Donelon said. "It falls to us at the NAIC to support those states that are unable to make the transition to this new system themselves. We can do that, and we will do that," he said.

Click [here](#) for a downloadable template showing life market share rankings based on direct premiums, for groups and individual companies.

Click [here](#) for a template showing demographic data for each state, along with state-level insurance market share.