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Interview with Jack Lay, CFO of Reinsurance Group of America

By Reinsurance News

First, thank you, Mr. Lay, for taking the time to speak with us. For our readers who may not be familiar with your company, could you begin by telling us about yourself and what you do at Reinsurance Group of America (RGA)?

Thanks for the opportunity to offer my thoughts on the industry and the changes taking place across a number of the markets.

I currently serve as the chief financial officer for Reinsurance Group of America, Incorporated, our holding company, as well as a number of our subsidiary companies. Like many financial executives, my educational background was focused on finance and accounting. I have a degree from the University of Missouri, and practiced as a certified public accountant for years before taking on responsibilities in private industry.

My responsibilities at RGA are fairly broad. They include all external financial reporting, including our filings with the Securities Exchange Commission here in the United States since RGA has gone through several issuances of equity and debt securities to the public over the years. As you can imagine, we also have a significant number of other financial filings around the world with various regulatory and taxing authorities, since the company now has subsidiary companies, branches or representatives offices in 25 different countries.

I also have responsibility for a number of other financial functions aside from the finance and accounting team. Those include our valuation function, which develops our reinsurance treaty reserving and related reporting, and more broadly any enterprise modeling efforts related to our various business projections and economic capital framework. We have a strong team of actuaries involved in these efforts, upon which I depend a great deal since I'm not trained as an actuary (even though I sometimes think I am).

Additionally, our tax department reports through the office of the CFO, as well as our investment and internal audit functions. That audit function also reports on a direct-line basis to our board of directors, so my involvement in that regard could be better characterized as administrative rather than strategic oversight. The investment department oversees the company's portfolio of investments that now totals over $30 billion.

Could you tell us about your career path? What are the highlights of your career that you remember most?

As I indicated, my background was in public accounting before joining what was the parent company of RGA's operations over 20 years ago. I was a partner in the financial institution practice of the KPMG office in St. Louis. The experience gained in public accounting during that part of my career has really served me well in my current role.

One of the highlights of my career relates to the genesis of RGA. That involved extracting the life reinsurance business from RGA's prior parent company in 1993 and transferring it to a newly created holding company, the current Reinsurance Group of America, Incorporated. The process was quite complex, but we were able to accomplish that transfer of all the existing reinsurance business, which paved the way for the initial public offering of the stock of RGA in May of 1993. Since that time, the majority ownership was transferred to MetLife in 2000, and ultimately the majority shares were transferred to broad public ownership in 2008. At this point, RGA has no parent company as all of the shares are openly traded in the public market.

You joined RGA in 1994, just as the company began entering international markets. What were some of the challenges you faced during this time of expansion?

There were a number of challenges associated with the expansion of our business into a number of international markets. Financial reporting systems needed to be broadened to accommodate internal and external reporting; new risks to which the organization became exposed needed to be thoroughly analyzed; and enterprise corporate governance needed to be continually expanded. These efforts are ongoing, and likely will always be subject to refinement as business environ-

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ments change, regulatory regimes continue to evolve, and lessons learned call for changes in our systems, policies and structure.

For a business that has been traditionally dominated by European reinsurers, how has RGA been able to grow so successfully in international and even European markets?

RGA brought a different focus to many of the international markets it has entered over the last 15 years or so. We believe in a very client-centered approach to delivering business solutions. That means doing everything possible to find an appropriate solution to a particular client's risk management needs. We believe that sort of open-minded approach serves our clients well. Of course, there are instances when the nature of the risks being discussed aren't a good fit for a solution involving RGA, or when the commercial terms associated with a solution just don't fit a client's needs. In those instances, we at least have demonstrated to our client a willingness to exhaust our full regimen of ideas and potential risk mitigation structures, even if we couldn't ultimately assemble a transaction that worked for all parties.

How does RGA differentiate itself from the major European reinsurers?

We think we have differentiated our business approach somewhat from that of the large European reinsurers in subtle ways that are apparent to our clients. We have described our approach as a relentless focus on client service. That doesn't mean our European reinsurance competitors don't likewise have a client service focus, but in many markets we think the degree to which we try to work with our clients sets us apart.

Execution of reinsurance transactions has historically been accommodated at the local business level. That includes the identification and discussion of the need, the negotiation of pricing and related commercial terms, etc. But, as everyone knows, markets and business practices continually change, and we see more and more centralization of reinsurance decisions within our clients' operations. Like many of our European competitors, we need to consider this sort of shifting business practice as we determine how to best serve the market.

Since RGA is headquartered in the United States, do you believe that your company has an advantage over your European counterparts because of the ongoing issues with Solvency II? Will Solvency II have much of an effect on RGA, outside of your European legal entities?

It isn't always clear to what extent any changes in reporting, solvency and regulatory standards will provide opportunities or challenges to our business over time. For instance, some types of business may look more attractive when reported under a particular solvency regime. That doesn't necessarily mean there will be significant movements of one type of risk into a particular reinsurance market, as there are a number of aspects considered by a primary life company in assessing options. They include, among other things, underlying business strategy and counterparty risk appetite. However, changes in solvency standards such as those that are a part of Solvency II typically do create opportunities for reinsurers, and RGA will be quite active in offering support where there seems to be a fit. Aside

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from these market dynamics, we don't think Solvency II will significantly affect RGA's reporting structure or the way it does business.

There has been friction between the federal government and the National Association of Insurance Commissioners (NAIC) over regulation of the insurance industry. Do you believe the public would be better served if insurers were regulated by a federal agency rather than a standard-setting body of state regulators?

This is a tricky issue, as one can argue the public and the industry have been well served over time by the state insurance regulators. However, one drawback in the state system is that the use of 51 different insurance departments can sometimes lead to inconsistent regulation. Additionally, it is my understanding that the state insurance departments cannot individually enter into agreements with foreign countries. For a global insurer or reinsurer, there is considerable value in having a single body vested with regulatory authority over the U.S. industry. My view is that a federal regulatory body may ultimately be more effective and efficient going forward for these reasons. I think regulators in various international markets would likely have more confidence in their ability to work with a single federal regulatory agency in the United States.

In the U.S. market, what is RGA doing in response to declining cession rates?

While RGA continues to maintain a leading position in the U.S. reinsurance market, there is no question that primary companies are ceding mortality risk at a significantly lower rate than was the case a decade ago. We have broadened our business in the United States to include group and various health reinsurance services, as well as asset-intensive reinsurance solutions associated with annuity portfolios. These actions have mitigated, to some extent, the effect of declining cession rates associated with traditional life reinsurance in the United States.

How has the increased consolidation in the U.S. life reinsurance market affected RGA?

The continued consolidation of the U.S. life reinsurance market has allowed RGA as well as the other remaining reinsurers to benefit from gains in market share. Reinsurance programs in the United States are typically split among a number of reinsurers, so the consolidation of the market generally benefits those reinsurers who remain active in the market.

Do you see any avenues of growth in the U.S. market for life reinsurers?

There are still opportunities for growth in the U.S. market, although the rate of growth will certainly be lower than what was typical in the recent past. Some of the growth opportunities are outside of traditional mortality reinsurance. Those include various forms of group and health-related reinsurance, as well as financial reinsurance.

There are also a considerable number of opportunities associated with companies wanting to reinsure blocks of in-force business or sell existing businesses or companies. Those sale transactions can be significantly supported, in whole or in part, by reinsurance structures.

RGA is a leader in providing financial reinsurance to insurers, and other reinsurers have also expressed interest in providing more capital relief transactions. Why do you believe reinsurers are a better choice to provide this service than investment banks or other financial institutions?

The structuring and modeling of financial reinsurance transactions are what reinsurers typically do well. While other institutions, such as investment banks, are skilled in the structuring aspects of such a transaction, the understanding and modeling of the expected product cash flows are of primary importance in any such transaction. There is a strong argument that reinsurers have the experience and capabilities to best determine the appropriateness of underlying assumptions driving any business valuation models. RGA has been involved in this part of the industry for years, and has a deep understanding of how to effectively structure a transaction that works for all parties involved.

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With the growing longevity reinsurance market, do you believe that current mortality improvement rates capture the speed of future health care advances?

The longevity reinsurance opportunities are expansive, and we have seen a number of such transactions in recent years, particularly in some of the international markets. It's hard to say whether any particular assumptions used will turn out to be appropriate over the long run, but all indications are that the parties accepting the longevity risk have prudently assessed the various possibilities, including the expected rate of health care advances over time.

Do you foresee any major changes to our industry over the next 30 years?

The life and health insurance industry will continually evolve, and address the challenges that it currently faces. Those include revitalization of the distribution force and the need to more effectively serve the middle market. It remains to be seen how effective the industry will be with respect to these issues, but it is highly likely the business will be transacted differently in the future. In particular, automated underwriting systems will likely play a broader role in risk selection. And, I believe distribution through electronic sources will play an increasing role in reaching the underserved middle market.

What are your priorities now? What are your plans for the future?

My priorities relate to addressing the increasingly complex nature of running RGA's finances. The rate of change in our industry, in terms of both domestic and international reporting and solvency requirements, is somewhat daunting. The needs of the capital markets, where we finance our ongoing operations, grow each year. Fortunately, we have a very strong team here to address those challenges as they arise.

As for my future, I enjoy what I do, and plan to leave an effective finance operation behind whenever I determine it's time to transition to something else. ■