

PBR Reinsurance

This subgroup spent the entire call discussing how to calculate reserves before reinsurance ceded (gross), reserves after reinsurance ceded (net), and the reinsurance credit (credit). Although this might seem like a trivial problem (given $\text{gross} - \text{credit} = \text{net}$, compute any two of them, and solve directly for the third one), the logistics are not trivial.

There are a number of issues related to the calculations:

- Which two of the three are calculated independently, and which one is the “balancing” item?
- Would a company use the same scenarios for gross and net?
- What if the CTE level indicates different scenarios for gross and net?
- How does a company project investment returns for gross when it does not hold the assets on a gross basis?
- Which of the three items is the most significant?
- How do companies determine assumptions for gross and net? Who can rely upon whom, if at all, for such assumptions in a reinsurance transaction?

Industry supports placing the emphasis on the net calculation, since that is ultimately the determinant of surplus. However, many states refuse to minimize the gross calculation, stating that it serves as a key measure of exposure to reinsurance.

Industry proposed starting with the gross and net calculations and merely letting the credit equal the difference. The subgroup rejected that by overwhelmingly recommending determining the net, computing the credit by considering the reinsurance cash flows, and setting the gross equal to the net plus the credit.

The entire body of LHATF must now act on this recommendation at the next meeting in December.

The subgroup mentioned another outstanding issue but had no chance to discuss it, i.e. what happens if a company can meet the stochastic exclusion test on a net basis, but not on a gross basis (or vice versa)?

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