

Property & Casualty Industry RBC Results for 2008

by NAIC Staff

As of July 30, 2009, approximately 2,650 Property & Casualty Risk-Based Capital (RBC) filings have been received and uploaded to the NAIC database for calendar year 2008. This article summarizes the industry results and discusses some of the trends noted in the 2008 filings.

The NAIC RBC formula generates the regulatory minimum amount of capital that a company is required to maintain to avoid regulatory action. There are five levels of action that a company can trigger under the formula. The base action level is the Authorized Control Level. If a company's actual capital dips below its Authorized Control Level Risk-Based Capital, the state insurance regulator has the authority to place the company under regulatory control. Therefore, the Authorized Control Level (ACL) is used as the base level, and the other regulatory intervention levels are defined relative to the ACL. The five action levels are:

- 1) No Action, which means that a company's total adjusted capital (TAC) is at least twice its ACL;
- 2) Company Action Level, which means that a company's TAC is at least 1.5 times its ACL but less than twice its ACL;
- 3) Regulatory Action Level, which means that the company's TAC is at least equal to its ACL but less than 1.5 times its ACL;
- 4) Authorized Control Level, which means that a company's TAC is at least 0.70 times its ACL but less than its ACL; and
- 5) Mandatory Control Level, which means that the company's TAC is less than 0.70 times its Authorized Control Level RBC.

Most companies fall into the "No Action" level. This level does not necessarily mean that the company is in strong financial condition. It simply means that the company has not triggered one of the regulatory intervention levels. A company can be in weak condition and still pass the RBC test.

Distribution of Companies by Action Level

As can be seen in Table 1, the number of companies triggering one of the regulatory intervention levels is relatively small. Typically, around 97 percent of all P&C insurers filing with the NAIC fall into the "No Action" level. That number has been fairly constant throughout the fourteen years that the NAIC's Property & Casualty RBC system has been in place.

Table 2 shows the disposition of insurers filing in data years 2007 and/or 2008. There is an increase of 58 new filers in 2008, which is offset by a decrease of 48 companies that filed in 2007 but did not file in 2008. Some of these companies have not filed because they have merged or otherwise gone out of business, and some have not filed because they were exempted by state regulators.

Of the 2,592 companies that filed in both 2007 and in 2008, 69 companies triggered one of the action levels in 2007. Twenty-seven percent of those companies that triggered an action level in 2007 were able to move to the "No Action" level in 2008, while 73 percent (50 out of 69 companies) remain in one of the action levels.

Aggregate Industry Results

The RBC ratio is the ratio of a company's TAC to its ACL RBC. Table 3 shows the median RBC ratio by asset size for data years 2004 through 2008. The "average" RBC ratio is a function of size. Larger insurers tend to operate with lower capital margins (the ratio of capital to assets). The RBC ratios reflect this difference and emphasize the inappropriateness of comparing RBC ratios between insurers. Although larger insurers tend to have lower RBC ratios, on average, the larger insurers also tend to have more stability in their operating results.

Another word of caution is in order with respect to time series analysis of RBC ratios. The ratios for years prior to 1998 are not exactly comparable to the ratios for later years because of phase-out aspects of the RBC formula. Companies were allowed to count 80 percent of reserve discounts

as part of TAC in 1994, 60 percent in 1995, 40 percent in 1996, and 20 percent in 1997. In 1998, all reserve discounts were phased out of the calculation of TAC. Though relatively few companies employ reserve discounting, this phase-out must still be considered.

Table 4 shows the relative risk factors by year for the two major underwriting risk components: reserve risk and premium risk. The total amount of RBC attributable to premiums and reserves has typically grown over time, as would be expected due to inflation, but the totals fell in 2008. The effective rate for premiums is increased up to

2007 with a decrease in 2008, while the reserves effective rate remains relatively stable after a decrease in 2007.

Table 5 shows the aggregate RBC by major covariance elements for 2004 through 2008. The RBC after covariance for each year is calculated using that year's respective covariance formula.

Overall, aggregate TAC fell nearly 10 percent from 2007 to 2008, with a net TAC increase of 19 percent over the past five years. Total RBC fell 6 percent in the past year and increased 5 percent over the past five years.

Table 1
Industry Results By Action Level, 2004-2008

| | 2004 | 2005 | 2006 | 2007 | 2008 |
|---------------------------------|-------|-------|-------|-------|-------|
| No Action | 2,410 | 2,471 | 2,523 | 2,567 | 2,566 |
| Company Action Level | 30 | 28 | 23 | 22 | 29 |
| Regulatory Action Level | 28 | 17 | 15 | 16 | 16 |
| Authorized Control Level | 8 | 6 | 5 | 8 | 10 |
| Mandatory Control Level | 41 | 37 | 33 | 27 | 29 |
| Total | 2,517 | 2559 | 2599 | 2640 | 2650 |
| Percent At 'No Action' Level | 95.8% | 96.6% | 97.1% | 97.2% | 96.8% |

Table 2
2008 Disposition of 2007 RBC Filers By Action Level

| | | 2008 Action | | | | | |
|--------------------|--------------------------|-------------|----------------------|---------------------|-----------------------|-------------------------|-----------------|
| | | NO ACTION | COMPANY ACTION LEVEL | REGUL. ACTION LEVEL | AUTHOR. CONTROL LEVEL | MANDATORY CONTROL LEVEL | NOT ON DATABASE |
| 2007 Action | NO ACTION | 2,493 | 20 | 4 | 0 | 6 | 44 |
| | COMPANY ACTION LEVEL | 11 | 5 | 5 | 1 | 0 | 0 |
| | REGULATORY ACTION LEVEL | 3 | 3 | 4 | 2 | 1 | 3 |
| | AUTHORIZED CONTROL LEVEL | 0 | 0 | 1 | 4 | 3 | 0 |
| | MANDATORY CONTROL LEVEL | 5 | 0 | 1 | 3 | 17 | 1 |
| | NOT ON DATABASE | 54 | 1 | 1 | 0 | 2 | 0 |

Table 3
Median RBC Ratios By Asset Size, 2004-2008

| Asset Size | 2008 Surplus to Asset Ratio | 2004 | 2005 | 2006 | 2007 | 2008 |
|--------------------------------|-----------------------------------|-------|-------|-------|-------|-------|
| Less than \$10 million | 0.714 | 1885% | 1722% | 1536% | 1924% | 1605% |
| \$10 million to \$25 million | 0.572 | 1056% | 1326% | 1389% | 1559% | 1595% |
| \$25 million to \$100 million | 0.442 | 879% | 924% | 983% | 985% | 1039% |
| \$100 million to \$250 million | 0.393 | 698% | 766% | 803% | 896% | 870% |
| \$250 million to \$500 million | 0.361 | 653% | 716% | 796% | 862% | 861% |
| \$500 million to \$1 billion | 0.353 | 605% | 648% | 722% | 744% | 773% |
| \$1 billion to \$10 billion | 0.344 | 545% | 610% | 690% | 681% | 667% |
| More than \$10 billion | 0.322 | 416% | 422% | 480% | 539% | 474% |
| All Companies | 0.454 | 828% | 877% | 935% | 977% | 992% |

Table 4
Average Underwriting Risk Factors, 2004-2008

| Year | Aggregate Reserve Base (000) | Aggregate Reserve Base RBC (000) | Average Effective Factor | Aggregate Premium Base (000) | Aggregate Premium Base RBC (000) | Average Effective Factor |
|------|------------------------------|----------------------------------|--------------------------|------------------------------|----------------------------------|--------------------------|
| 2004 | 441,180,424 | 79,510,895 | 0.180 | 421,688,879 | 48,120,617 | 0.114 |
| 2005 | 492,746,672 | 86,709,164 | 0.176 | 420,892,665 | 49,539,011 | 0.118 |
| 2006 | 498,386,189 | 90,883,219 | 0.182 | 441,514,956 | 53,926,560 | 0.122 |
| 2007 | 553,508,233 | 92,254,735 | 0.167 | 437,408,945 | 57,208,353 | 0.131 |
| 2008 | 543,265,335 | 91,358,674 | 0.168 | 428,270,742 | 55,376,189 | 0.129 |

| | | | | | | | | | | | | |
|--|------------|------------|------------|------------|------------|--------|--------|--------|--------|--------|--------|--------|
| Asset Concentration (Fixed) | 301,864 | 294,295 | 279,368 | 296,393 | 525,787 | 0.11% | 0.10% | 0.10% | 0.10% | 0.10% | 0.10% | 0.27% |
| Total R1 | 4,853,017 | 4,960,115 | 4,757,455 | 5,152,372 | 6,019,789 | 1.85% | 1.70% | 1.78% | 1.78% | 1.78% | 1.78% | 3.11% |
| R2 - Asset Risk - Equity | | | | | | | | | | | | |
| Common - Affiliated Investment Subs. | 46,616 | 89,363 | 43,749 | 191,617 | 106,809 | 0.03% | 0.02% | 0.07% | 0.07% | 0.07% | 0.07% | 0.06% |
| Common - Holding Company | 1,456,845 | 1,416,621 | 1,427,009 | 1,964,159 | 2,132,444 | 0.53% | 0.51% | 0.68% | 0.68% | 0.68% | 0.68% | 1.10% |
| Common - Parents | 70,252 | 92,090 | 109,060 | 98,226 | 69,171 | 0.03% | 0.04% | 0.03% | 0.03% | 0.03% | 0.03% | 0.04% |
| Common - PC Not Subject | 62,608 | 59,486 | 18,753 | 62,103 | 94,050 | 0.02% | 0.01% | 0.02% | 0.02% | 0.02% | 0.02% | 0.05% |
| Common - Life Not Subject | 1,860 | 1,870 | 1,107 | 1,128 | 1,475 | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% |
| Common - Health Not Subject | 1,926 | 359 | 4,444 | 0 | 0 | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% |
| Common - Non-Insurer | 2,536,013 | 2,579,414 | 2,557,389 | 2,360,484 | 4,148,937 | 0.96% | 0.92% | 0.81% | 0.81% | 0.81% | 0.81% | 2.15% |
| Preferred - Affiliated Investment Subs. | 0 | 0 | 0 | 0 | 0 | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% |
| Preferred - Holding Company | 0 | 0 | 0 | 3,596 | 147,015 | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% | 0.08% |
| Preferred - Parents | 0 | 0 | 0 | 0 | 374 | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% |
| Preferred - PC Not Subject | 0 | 0 | 0 | 0 | 5,059 | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% |
| Preferred - Life Not Subject | 0 | 0 | 0 | 0 | 0 | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% |
| Preferred - Health Not Subject | 0 | 0 | 0 | 0 | 0 | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% |
| Preferred - Non-Insurer | 458,064 | 460,145 | 562,026 | 547,793 | 681,041 | 0.17% | 0.20% | 0.19% | 0.19% | 0.19% | 0.19% | 0.35% |
| Unaffiliated Preferred | 99,312 | 92,436 | 107,151 | 148,225 | 139,334 | 0.03% | 0.04% | 0.05% | 0.05% | 0.05% | 0.05% | 0.07% |
| Unaffiliated Common | 21,534,688 | 23,297,869 | 26,856,613 | 27,127,325 | 18,660,310 | 8.67% | 9.62% | 9.35% | 9.35% | 9.35% | 9.35% | 9.65% |
| Real Estate | 944,460 | 948,819 | 999,341 | 1,052,561 | 1,096,874 | 0.35% | 0.36% | 0.36% | 0.36% | 0.36% | 0.36% | 0.57% |
| Schedule BA Assets | 7,033,564 | 7,924,085 | 10,579,772 | 15,357,049 | 11,923,225 | 2.95% | 3.79% | 5.29% | 5.29% | 5.29% | 5.29% | 6.17% |
| Receivables for Securities | 70,105 | 205,739 | 108,841 | 89,686 | 128,562 | 0.08% | 0.04% | 0.03% | 0.03% | 0.03% | 0.03% | 0.07% |
| Aggregate Write-ins for Invested Assets | 116,377 | 14,675 | 112,953 | 203,872 | 145,623 | 0.01% | 0.04% | 0.07% | 0.07% | 0.07% | 0.07% | 0.08% |
| Replication - Synthetic Asset: One Half | 3,812 | 2,896 | 8,534 | 14,438 | 4,620 | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% |
| Asset Concentration (Equity) | 12,058,527 | 13,281,066 | 16,361,398 | 18,305,541 | 12,971,776 | 4.94% | 5.86% | 6.31% | 6.31% | 6.31% | 6.31% | 6.71% |
| Total R2 | 46,495,028 | 50,594,935 | 59,858,120 | 67,527,803 | 52,456,701 | 18.83% | 21.45% | 23.28% | 23.28% | 23.28% | 23.28% | 27.13% |
| R3 - Asset Risk - Credit | | | | | | | | | | | | |
| Other Credit RBC | 6,169,864 | 6,810,725 | 6,179,719 | 2,713,236 | 3,310,690 | 2.53% | 2.21% | 0.94% | 0.94% | 0.94% | 0.94% | 1.71% |
| One Half of Rein Recoverables | 11,403,567 | 12,384,001 | 11,464,017 | 10,703,079 | 10,870,321 | 4.61% | 4.11% | 3.69% | 3.69% | 3.69% | 3.69% | 5.62% |
| Other Half of Rein Recoverables | 2,947,839 | 3,943,377 | 3,289,586 | 2,553,875 | 3,066,407 | 1.47% | 1.18% | 0.88% | 0.88% | 0.88% | 0.88% | 1.59% |
| Health Credit Risk | 671 | 650 | 0 | 0 | 0 | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% | 0.00% |
| Total R3 | 20,521,939 | 23,138,752 | 20,933,322 | 15,970,190 | 17,247,418 | 8.61% | 7.50% | 5.51% | 5.51% | 5.51% | 5.51% | 8.92% |
| R4 - Underwriting Risk - Reserves | | | | | | | | | | | | |
| One Half of Reinsurance RBC | 8,455,728 | 8,440,623 | 8,174,432 | 8,149,204 | 7,803,914 | 3.14% | 2.93% | 2.81% | 2.81% | 2.81% | 2.81% | 4.04% |

| | | | | | | | | | | |
|--|-------------|-------------|-------------|-------------|-------------|---------|---------|---------|---------|---------|
| Unpaid Loss/Expense Reserve | 79,510,757 | 86,708,961 | 90,883,104 | 92,254,735 | 91,358,674 | 32.27% | 32.56% | 31.80% | 31.80% | 47.24% |
| Excess Growth – Loss/Expense Reserve | 9,163,784 | 4,441,808 | 1,346,463 | 898,700 | 688,114 | 1.65% | 0.48% | 0.31% | 0.31% | 0.35% |
| A&H Claims Reserves | 148,635 | 143,638 | 113,738 | 108,820 | 106,873 | 0.05% | 0.04% | 0.04% | 0.04% | 0.06% |
| Total R4 | 97,278,903 | 99,735,029 | 100,517,737 | 101,411,459 | 99,937,576 | 37.12% | 36.02% | 34.96% | 34.96% | 51.68% |
| R5 - Underwriting Risk - Written Premiums | | | | | | | | | | |
| NWP RBC | 48,120,592 | 49,539,011 | 53,926,575 | 57,208,353 | 55,376,189 | 18.44% | 19.32% | 19.72% | 19.72% | 28.64% |
| Excess Growth - Premiums | 4,122,515 | 1,907,343 | 654,028 | 540,365 | 483,979 | 0.71% | 0.23% | 0.19% | 0.19% | 0.25% |
| Net Health Premium RBC | 485,085 | 356,609 | 195,326 | 318,625 | 295,513 | 0.13% | 0.07% | 0.11% | 0.11% | 0.15% |
| Health Stabilization Reserves | -18,599 | -23,931 | -2,002 | -1,433 | -1,342 | -0.01% | 0.00% | 0.00% | 0.00% | 0.00% |
| Total R5 | 52,709,593 | 51,779,032 | 54,733,927 | 58,065,911 | 56,154,339 | 19.27% | 19.61% | 20.02% | 20.02% | 29.04% |
| Total RBC | 260,036,255 | 268,679,613 | 279,088,272 | 290,068,141 | 273,772,362 | 100.00% | 100.00% | 100.00% | 100.00% | 141.57% |
| RBC After Covariance | 186,151,113 | 190,003,749 | 197,427,592 | 205,803,118 | 193,386,033 | 70.72% | 70.74% | 70.95% | 70.95% | 100.00% |
| Total Adjusted Capital | 487,740,391 | 526,803,361 | 598,836,593 | 640,380,204 | 578,401,613 | 196.07% | 214.57% | 220.77% | 220.77% | 299.09% |