ISSUE: FX Treatment in Schedule P - possible additional changes due to RBC needs.

As background, the way of dealing with FX in Schedule P will be as follows:

* Only the Summary Parts 1 and 2 will be affected
* Summary Part 1 will have additional columns that are used to bring Net Earned Premium and Net Incurred Loss to current exchange rates
* Summary Part 2 will have adjusted 1 and 2 year development totals that reflect all development at current exchange rates

The potential distortions that existed in the old Schedule P structure and still exist in the line-specific detail are:
* Current reserves will be at current exchange rates, but paid losses and historical reserves will reflect exchange rates in effect at the time losses were paid and the historical reserves were established
* Net incurred losses in the line-specific sections of Part 1 will reflect a mix of historical and current exchange rates, with paid losses reflecting the exchange rates in effect at the time losses were paid and the current reserves reflecting current exchange rates
* Net earned premiums will also reflect a mix of historical and current exchange rates, depending upon when the premium was earned

Foreign exchange currently affects the following RBC calculations:
* R4: Company reserve development, as calculated from line-specific sections of Part 2, could be distorted by differences between current and historical exchange rates. This could cause actual reserve development to be masked or exacerbated by foreign exchange adjustments, depending upon direction in which foreign exchange adjustments caused the Part 2 values to move.
* R5: Company loss ratio experience, as calculated from line-specific sections of Part 1, could be distorted by differences between current and historical exchange rates.

The problem is that with current information, there is really no way to quantify how material any distortions might be. Therefore, the recommendation to not change current procedure can not rest on an exhaustive analysis of what impacts a recognition of FX might have on individual companies and on the industry as a whole. Instead, the recommendation is based on the following items:
* Not many companies within the industry have sizable amounts of international business that is affected by foreign exchange issues, relative to domestic business.
* The Risk-Based Capital committee can think of no historical situations that would lead one to expect a bias in the risk-based capital calculations of affected companies.

* It is the Risk-Based Capital Committee's understanding that companies with foreign exchange issues typically incorporate a strategy of maintaining assets in the same currencies as which they have liability exposure. This further serves to mitigate any foreign exchange risk that might otherwise exist for companies with foreign exchange issues.

As noted above, the committee's recommendation is that no changes be made to either the line-specific sections of Schedule P or the risk-based capital calculation itself. The Risk-Based Capital committee can not think of a reason to require all companies to perform a series of FX-adjustment calculations at the line of business level. Such calculations could potentially be costly to companies from a systems and recordkeeping standpoint, without a commensurate improvement in the calculated risk-based capital value.

There is no evidence that would lead us to believe that the FX disclosures in Schedule P that have not already been addressed in the current RBC formula

AAA P&C RBC Committee - FX subgroup (Gerry Kirschner, Mike McCarter)