

NAIC Update Summer 2014



Top stories

- NAIC adopts corporate governance model act and regulation
- Revised Rector Report adoption means new framework for XXX/AXXX captives
- Regulators air internal disagreements over NAIC governance
- Closing doors at the IAIS cause widespread grumbling
- Forum on capital hears many concerns about standards

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- NAIC actuarial update
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- NAIC health update

What's next

- October 20–25: IAIS Annual Conference; Amsterdam, The Netherlands
- November 16–19: NAIC Fall National Meeting; Washington, D.C.
- November 19–23: NCOIL Annual Meeting; San Francisco, CA

Louisville meeting marked by victories, competing visions

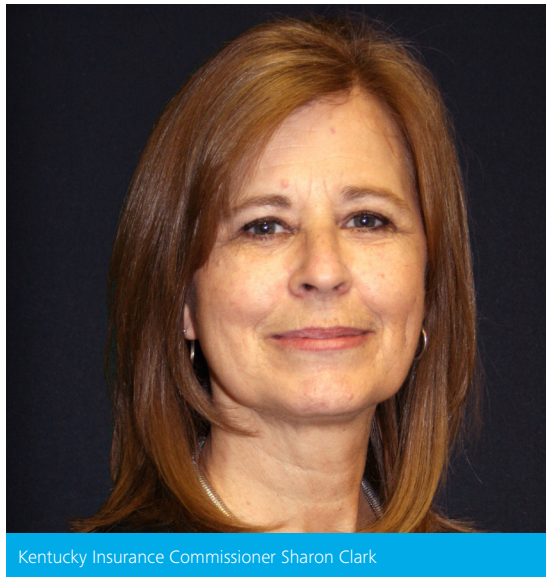
LOUISVILLE, KY – With the legendary Churchill Downs racetrack a mere stone’s throw down I-65, host Insurance Commissioner Kentucky’s Sharon Clark started the summer national meeting of the National Association of Insurance Commissioners (NAIC) with a blast, specifically a blast from the official bugler of the famed Kentucky Derby.

At times during the meeting, this seemed apropos. Against the odds, the working group chaired by Vermont Commissioner Susan Donegan managed with wit and grace not just the improbable—getting industry and regulators to agree on a draft Corporate Governance Model Act and Model Regulation and guiding them past the post—but the near impossible—making 8 a.m. Sunday morning meetings a cause for anticipation and not complaints.

But at other times, the meeting seemed to invoke another Louisville institution whose museum was also a short distance away—Muhammad Ali.

“Float like a butterfly, sting like a bee” was one of Ali’s most famous bits of doggerel. New York’s chief regulator, Benjamin Lawsky, landed a few punches before the meeting, attacking the NAIC’s position on principle-based reserving (PBR) for life insurers, and regulation of affiliated captives used by life insurers for reinsurance. Lawsky’s chief deputy, Robert Easton, continued the attack during the meeting as New York stood strongly against the NAIC’s adoption of the Rector Report containing the recommendations on the captives.





Photos courtesy of the NAIC

Consumers had their own concerns. Most notably, consumer representatives were disappointed by the NAIC's decision to include industry provided material in its report on the affordability and availability of auto insurance, while excluding material provided by consumers.

Regulators landed more than a few punches of their own. The International Association of Insurance Supervisors (IAIS) served as the designated punching bag, with its move toward a closed system for setting global insurance standards unifying regulators, consumers, and industry in opposition. If the enemy of my enemy is my friend, no matter their other concerns, U.S. stakeholders drank deeply of the wine of friendship whenever the topic was the Basel-headquartered IAIS.

Still, in the state whose motto is “United we stand, divided we fall,” one of the liveliest prizefights was within the NAIC itself. Like Lawsky, Connecticut Insurance Commissioner Thomas Leonard used the media to convey his disappointment. His concern was with the NAIC’s own moves toward governance reform, prompted by a letter he had written at the winter 2013 NAIC meeting. During this meeting, as altered plans to hire a consultant were discussed, some regulators openly vented their dismay with the actions of the leadership team headed by current NAIC President, North Dakota’s Adam Hamm, with one going so far as to suggest that NAIC leadership needed to be cognizant that at any time, any state could withdraw from the organization.

To some observers, though, this frank and open exchange of views—characterized by one consumer representative as a fight within the family—itself testified to the contrasting openness of the NAIC at a time when the IAIS is assuming increased influence over global insurance regulation while decreasing its openness to stakeholders.

Whether the topic was capital, group supervision, or corporate governance, that expanded international regulatory influence was clear, as was the determination of many U.S. stakeholders to maintain what they saw as the best in the U.S. system. State insurance legislators from the National Conference of Insurance Legislators (NCOIL) were there in force, by their very presence implicitly allying themselves with the NAIC in the battle to preserve state regulation.

Also present were reminders of the changes imposed by Dodd-Frank. Former Connecticut Insurance Commissioner Thomas Sullivan, now the senior insurance advisor for the Federal Reserve Bank (Fed), was notable by his presence, and his vigorous participation in the roundtable on capital.

The other major Dodd-Frank legacy, Federal Insurance Office (FIO) Director Michael T. McRaith, also a former state insurance commissioner, was much more difficult to find at this meeting. Unlike at earlier meetings where he was highly visible, McRaith’s presence seemed limited to his attendance at the commissioners’ roundtable. The third leg in the Dodd-Frank stool, the Financial Stability Oversight



Photo courtesy of New York Department of Financial Services

Council (FSOC), was represented by former Kansas Commissioner Roy Woodall.

McRaith, Sullivan, Woodall, and numerous NAIC Commissioners will no doubt see each other soon at the IAIS annual meeting in Amsterdam in October, where capital standards and group supervision will be hot topics, and again in November, when the NAIC holds its final meeting of Hamm’s term in Washington, D.C.

The fact that so much of what will be important at November’s NAIC meeting depends on what happens at October’s IAIS meeting is itself telling. But just as notable may be the simple fact that whatever happens in Amsterdam, the D.C. meeting will still determine the regulatory expectations for most U.S. insurers, at least for now.

The NAIC’s apparent unity in the face of international pressure, and the support of legislators and industry, means the next chapter in U.S. insurance regulation is still being written. Industry will have to wait a while longer to see who gets the power seats when the music stops.

Birth, death and corporate governance

Not often is putting yourself out of work considered cause for celebration these days, but the Corporate Governance Working Group seemed thrilled by its impending doom. Its fate was sealed by the adoption of the Corporate Governance Annual Disclosure Model Act and Model Regulation, an act repeatedly compared to the process of giving birth by working group members and observers.

The Act will require insurers to provide their lead state or domestic regulator with a detailed summary of the insurer or insurance group's corporate governance structure, policies and practices by June 1 of each year. The requirements of the Act are expected to be effective starting in 2016.

But like birth, this may be in some ways just a beginning. Noting that this was what he called an ongoing process and praising Vermont Commissioner Susan Donegan's leadership, Pennsylvania's Steve Johnson moved passage of the Model Act and the Regulation. After the unanimous adoption of the Act and Regulation, Commissioner Donegan exclaimed excitedly, "Guess what, it's twins!"

The Commissioner did not hand out cigars, however both industry groups and regulators seemed pleased by the outcome of the negotiating process.

Referring to concerns expressed in an interested parties duplication report about redundant regulatory information requests, one industry representative noted that 36 redundancies had already been referred to three different groups. The representative, who was speaking in support of the Act before its passage, called for the creation of a task force or working group to study all redundancies.

The representative also stressed industry appreciation of the confidentiality solution agreed to with the working group, but warned that the erosion of those confidentiality protections in states as the Model Act is being considered could erode industry support.

The working group heard and discussed comments received on proposed responses to the interested parties' duplication report, which outlined potential redundancies that may be created through the adoption of the annual corporate governance disclosure. Interested parties wanted the working group to suggest that an EX Working Group be established to address redundancies and duplication. Instead, the working group agreed to refer several potential redundancies to the Blanks (E) Working group and the Financial Examiners Handbook (E) Technical Group for consideration, as well as to refer the broader redundancy concerns to the Financial Condition (E) Committee. Commissioner Donegan also noted an ongoing partnership between NCOIL and industry devoted to reducing these redundancies.

Regulators were supportive. Johnson noted the effect of the passage of the Model Act and Regulation on international perceptions. The draft questionnaire asked many questions that would be answered by this law, he said.

Donegan noted that the next steps for the working group would involve consideration of enhancements to the accreditation standards in relation to the Models and a recommendation to the Financial Regulation Standards and Accreditation (F) Committee on the recently adopted Act and on the Model Audit Rule. With that done, it would be time for the end of the working group and its 8 a.m. Sunday meetings.

The working group also heard a report on IAIS activities related to governance. Commissioner Donegan discussed the May 2014 IAIS Governance and Compliance Subcommittee meeting in Malaysia and the status of the draft IAIS Issues Paper on Approaches to Group Corporate Governance: Impact on Control Functions.

Affiliated captives issue dragged kicking and screaming to rest

Goldilocks might have felt right at home at the meeting of the Executive Committee, especially during the discussion around the regulation of life insurer-owned captives involving XXX/AXXX transactions.

This discussion followed the release of the Rector & Associates June 2014 report that proposed a modified framework from that outlined in the Rector & Associates February 2014 report. A comparison of the frameworks outlined in the two reports can be found on the NAIC website.¹

The framework adopted via the June report is not expected to change the statutory reserving requirements for these types of transactions. However, it is expected to change the types of assets and securities that are needed to be held by the direct/ceding company to support those statutory liabilities. The Framework would also require the direct/ceding company to disclose the assets and securities used to support the statutory reserves and to hold a risk-based capital (RBC) cushion if the assuming captive does not file RBC.

As expected, not all regulators found the revised Rector Report to their liking. North Carolina Insurance Commissioner Wayne Goodwin found it much too harsh, ultimately voting against adoption of its recommendations. New York, on the other hand, found it much too mild, also voting against adoption of the recommendations. In general, however, the committee found it just right, and its recommendations will form the basis of the NAIC's actions on the subject going forward.

"We had concerns with a modified Rector Report," Goodwin told the committee. Among other issues, he cited the possibility of a double RBC hit, and in some instances said there was no materiality threshold. He encouraged a delay in adoption, saying a proper discussion would require the airing of confidential work product from the NAIC that could not happen in open session.

Rhode Island Commissioner Joseph Torti disagreed.

Torti had previously expressed concerns over the use of life insurer-owned captives purposes, but said of the proposal, "This sets standards, does not inhibit transactions... a double RBC hit does not exist." He also noted that no moratorium would be imposed as a result of the Rector Report as had been called for previously by New York.

"The Rector Report has been fully vetted in lots of different forums," said Tennessee Commissioner Julie Mix McPeak in support.

New York disagreed.

"In hindsight, the February report seems to be light-years ahead of where we ended up," said New York's Robert Easton. "It had some teeth that has now been watered down if not downright neutered." Easton cited three categories of objections, including the removal of active coordination among commissioners in the new report, the removal of the hazardous financial condition statement in favor of what he called the equivalent of an actuarial note, and the timing.

"We'll be patting ourselves on the back for taking action

¹ "National Association of Insurance Commissioners. Update to February Report Executive Summary—June 13, 2014. http://www.naic.org/documents/committees_ex_pbr_implementation_tf_140613_rector_report.pdf.

while we've only put on a veneer," said Easton as he called for the discussion process to continue. "We as regulators need to do what we think is right. We, not industry, are responsible for setting the standards."

Commissioner Torti responded strongly.

"I've been reluctant to accept continuation of these captives," he said. "But these regulations are far from toothless. What's right is not necessarily what New York says is right." Torti said there would still be active coordination and cooperation among regulators, adding, "It is very difficult to assume hazardous financial condition."

Nobody wants a qualified statement, Torti said. Noting the new actuarial guidelines would go into effect in the

next few months, he said modifying the formulaic report as some would wish would stifle product development, not be quickly responsive, and could result in redundant or deficient regulation.

The Report's recommendations were adopted by voice vote. Following this adoption, the Principle-Based Reserving (PBR) Implementation (EX) Task Force along with other groups and committees will be charged with developing an action plan to create the Framework and propose changes to the insurer/captive regulations specific to XXX/AXXX transactions.

The recommendations in the Report will be applied prospectively.

International affairs of prime importance, but move to global secrecy decried

The importance of international regulatory influence on U.S. insurance regulation was clearly evidenced by the large crowd gathered in the Kentucky Convention Center, filling the room hosting the meeting of the International Insurance Relations (G) Committee.

If attendees had come to hear U.S. regulators and others pan the IAIS for its moves away from transparency, they were not disappointed. The IAIS, the international standard setter for insurance regulation, has moved to exclude observer participation in its deliberations, in favor of by invitation only consultations with stakeholders at defined points in the standard-setting process. The IAIS restructuring and reorganization would eliminate the observer membership category and limit stakeholder participation in most IAIS meetings. This approach is counter to the approach favored by the NAIC, which has been pushing for increased observer and stakeholder involvement and a transparent process.

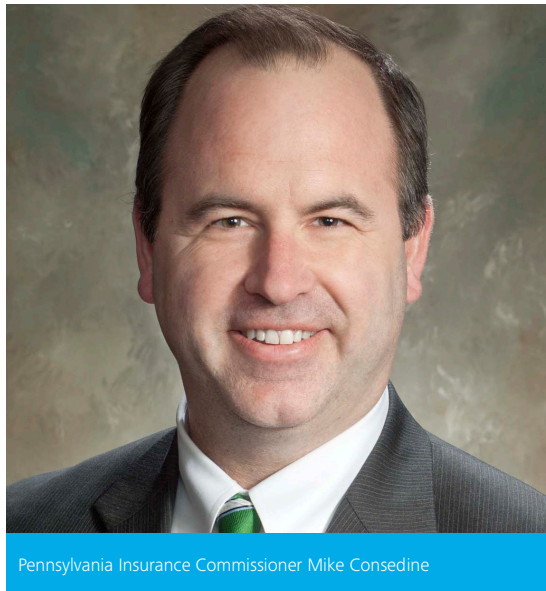
This exclusion is “a step in the wrong direction,” Florida Commissioner Kevin McCarty told the crowd. Connecticut Commissioner Tom Leonardi agreed, saying, “We have been very vocal in our opposition.”

Representatives of various trade organizations, including the Reinsurance Association of America (RAA), the American Council of Life Insurers (ACLI), the Property Casualty Insurers Association of America (PCI), and the American Insurance Association (AIA) all expressed support of the NAIC’s stance and disapproval of the moves by the IAIS.

Consumer representative Birny Birnbaum and another consumer representative also expressed support for the NAIC and its continued support of consumer participation at the IAIS. Other industry speakers also asked for more openness at the IAIS and supported the NAIC’s push.

On other issues, New Jersey Commissioner Ken Kobylowski reported that the Financial Stability Committee (FSC) of the IAIS is currently in the midst of its annual review of G-SII insurers and reinsurers. There is a November date for this determination. In addition to possible additions to the list, current G-SII insurers will be reviewed to see if they continue to meet the criteria to be so designated. Reinsurers may be named as G-SIIs for the first time. In addition, Kobylowski said the IAIS hopes to have a consultation on Higher Loss Absorbency (HLA) in December.

Florida Commissioner McCarty noted that the ComFrame document had been finalized in June with field testing in progress in stages. The IAIS Field Testing Task Force will begin qualitative field-testing on Module 2 in October 2014 and Module 3 in 2015. Module 1 field testing is complete.



Pennsylvania Insurance Commissioner Mike Consedine

Photos courtesy of the NAIC

Pennsylvania's Mike Consedine noted that the International Monetary Fund's (IMF) U.S. Financial Sector Assessment Program (FSAP) is in progress and is expected to be completed in 2015. U.S. adherence to the 26 IAIS Insurance Core Principles (ICP) will be evaluated by the IMF. The NAIC will be working with the Federal Reserve and Federal Insurance Office (FIO).

Committee Chair Commissioner Consedine provided an update on the Organization for Economic Cooperation and Development (OECD). Commissioner Monica Lindeen of Montana had attended the most recent OECD meeting where topics included: working on analytic tools, variable annuities and guarantees, disaster risk financing, and long-term investments for infrastructure development. Commissioner Jim Donelon of Louisiana had presented in a session regarding disaster risk financing during March 2014 in Tokyo.

Commissioner McCarty provided an update on the NAIC's International Capital Forum. He said the forum had a great turnout and state legislators were very involved. He asked that any specific proposals related to group capital be submitted to Ryan Workman of the NAIC staff. He said the ComFrame Development and Analysis Working group (C-DAWG) would meet soon to discuss proposals.

More evidence of the NAIC's international activities was presented. Commissioner Gordon Ito of Hawaii provided an update on International Regulatory Cooperation Activities. The International Regulatory Cooperation (G) Working group meets twice a year. Just before the NAIC meeting, some state regulators and NAIC staff were in Bangkok with 60 participants from various countries to discuss risk-focused examinations. The NAIC also attended a Chilean seminar on market conduct with Latin American supervisors. The NAIC will host 13 fellows from various countries for the NAIC International Fellows Program. Commissioner Consedine provided an update on the EU-U.S. Dialogue, which recently released an updated work plan, *The Way Forward*.



Montana Insurance Commissioner Monica Lindeen

Photos courtesy of the NAIC

The document raises the possibility of addressing group supervision and confidentiality issues through a bilateral agreement or part of an FIO covered agreement. NAIC is still exploring this, and has not made any decisions yet. The Way Forward document does not limit the NAIC to any one option, Consedine said. The NAIC has also not committed to using a covered agreement to address collateral issues, although the NAIC is discussing the approach with the U.S. Trade Representative and the Department of the Treasury.

NAIC CEO Ben Nelson said the EU is offering temporary (five year) equivalence rather than a permanent solution, which would require other major steps. One trade organization urged the NAIC to push for a solution prior to the January 1, 2016, effective date of Solvency II, to prevent U.S. insurers from being negatively impacted. An EU-U.S. Dialog hearing will take place in Amsterdam on October 25.

New York's Rob Easton provided an update on the Joint Forum. The Joint Forum was created in 1996 for the regulators of banking, securities and insurance to address cross-sectoral issues that are common among the three financial sectors. The Joint Forum comprises the Basel Committee on Banking Supervision (BCBS), the International Organization of Securities Commission (IOSCO), and the International Association of Insurance Supervisors (IAIS), each of whom have an equal number of senior supervisors representing each supervisory constituency. The Joint Forum is now at a crossroads and will consider winding down if supervisors don't endorse its work. Current work streams have involved financial innovation and cybercrime. Additionally, its asset encumbrance report is being reworked.

Hamm sets out his priorities



NAIC President and North Dakota Commissioner Adam Hamm

Photos courtesy of the NAIC

As he opened the middle national meeting of his term, NAIC President and North Dakota Insurance Commissioner Adam Hamm set out five key priorities:

- Principle-based reserving (PBR)
 - The NAIC’s work on PBR and the implementation plan continues. The adoption of changes to the model law and the valuation manual has been completed by 18 states. Several more are planning to adopt. There is a need to develop a regulatory review system for adoption. A PBR pilot will be held as was the ORSA pilot. Ultimately the NAIC is looking for consistency of adoption across the states.
- The implementation of the Affordable Care Act
 - States continue to face challenges in the adoption of the Affordable Care Act. The NAIC is seeking to maintain stable and accessible insurance markets. The NAIC continues its work concerning the regulation of the long-term insurance market.
- Federal issues and relationships
 - The NAIC believes that there continues to be a lack of understanding in Congress concerning the state based system of insurance regulation. To seek to address this, the NAIC has launched a Protecting the Future program to reinforce the strength and stability of the insurance market place. A video was shown during the opening session on the Protecting the Future Program. Ultimately the aim of the program is to shrink the perceived knowledge gap of key stakeholders (including federal and international agencies). He called on Congress to get the Terrorism Risk Insurance Act (TRIA) reauthorized as soon as possible.
- International activities and relationships
 - Insurance regulation is both domestic and international as globalization increases. So must the dialogue between the U.S. and the international community. The EU-U.S. dialogue project is one way to increase the dialogue and improve the understanding of the U.S. state-based system of regulation. He noted that the international capital standards forum was held the day before.
- Group supervision
 - The fifth major priority outlined was that of group supervision. The NAIC committed to review the Model Insurance Holding Company Act and Regulation. In the spring of this year the NAIC started to look at changes to these models. Example areas of focus included impacts of receivership and insolvency and the authority to act as a group wide supervisor of an IAIG. He noted that a number of states have adopted language to accommodate this.

Capital forum hears concerns about standards

With capital a key concern for U.S. insurance companies as the IAIS works to create various capital standards, the NAIC held a Capital Forum that showcased strongly held views on the issue.

"This is an issue that affects us all, from Wall Street down to Main Street," said Pennsylvania Commissioner Michael Consedine. After Florida Commissioner Kevin McCarty detailed the background of the IAIS's work on capital standards, Connecticut Commissioner Tom Leonardi noted the inherent conflict between protecting counterparties and protecting policyholders.

Responding to skeptical comments by an industry representative on the integral nature of the use of models in currently envisioned capital standards, the Fed's Tom Sullivan asked if capital computations today captured all the risk insurance companies face. He defended the use of models, saying, "Models...are a useful tool." The industry representative responded by cautioning against an overreliance on models.

Another representative of an industry trade group said that the insurance capital standards were written so broadly, "We need to take this issue of financial stability either out of the equation or lower the priority."

Consumer representative Birny Birnbaum called for an equal focus on products causing systemic risk. As examples, he cited products with guaranteed lifetime withdrawal benefits and contingent deferred annuities.

Yet another industry group representative called for clarity: "There really needs to be a clear agreement on what the goals of a global capital standard are," he said.

The representative of one insurer called the focus on a global capital standard misguided, while another industry representative warned currently proposed IAIS standards would restrict available capital and ultimately consumers would pay the price.

One industry representative said the United States needed a group capital standard of its own in order to have a more effective voice in the global discussion, conceding that the number one problem in the creation of such a U.S. standard is valuation.

Many participants expressed the desire for any standards to reflect the unique nature of the U.S. system, and not simply be a one-size-fits-all concoction into which U.S. insurers must be shoehorned.

What is direct holdco supervision?

How does one define direct holding company supervision? That question gained added importance at the meeting of the Group Solvency Issues (E) Working group as Rob Esson of the NAIC discussed with the group work by the IAIS on group supervision and capital standards.

The ICS are interlinked with group supervision authority, Esson told the working group. An IAIS working group is now working on the definition of holding company, direct supervision and other relevant items, he said.

There is a question as to whether direct holding company supervisory powers should be for all groups, or just for Internationally Active Insurance Groups (IAIGs) or Global Systemically Important Insurers (G-SIIs). The NAIC's position is that there is no current explanation of why these powers are needed. The response to that is that then there would be different effects on IAIG's, non-IAIG and G-SIIs, according to Esson.

Esson pointed out that the United States has more small groups than most jurisdictions, with the rest of the world by contrast primarily having larger groups. The concern is that rules meant for larger groups will have to be applied locally on very small group insurers, causing increased costs and regulatory complexity. Esson said added clarity should be coming from the next IAIS Insurance Groups Working Group meeting in Frankfurt.

One issue is whether much of the concern is largely a matter of semantic differences. The working group discussed a NAIC Legal Division memorandum titled *Comparative analysis of powers and authority with respect to group-wide supervision*. The Chair noted that state regulators appear to already have several of the IAIS key

elements related to direct group supervision, but need to be more careful in the future when describing the U.S. group supervision approach as "indirect".

Esson noted that some of what is referred to as indirect holding company power in the United States is regarded as direct elsewhere. As an example, he cited authority over a controlling person who lies to a regulator. U.S. regulators may regard this as routine and indirect, but it may well exceed the powers available in jurisdictions considered to have direct supervisory power over holding companies.

During the discussion, a few working group members, including Delaware and Iowa, noted that their respective states used the Pennsylvania statute language as a starting point for their model for group supervision with some modifications, but faced heavy industry opposition.

Concerns were expressed by an industry representative over the use of a Pennsylvania statute as a template. Under the Pennsylvania statute, group supervision is determined by the domicile of the holding company. Normal NAIC procedure is that the lead state is that state where the lead insurance company is domiciled.

The working group concluded the discussion by directing NAIC staff to draft proposed changes to the Insurance Holding Company System Model Act (#440) to provide state authority to act as a group-wide supervisor using the Pennsylvania language as a starting point. The Chair encouraged the industry to provide written comments to the working group on any concerns.

NAIC staff will continue work on the legal issue.

Internal governance review remains contentious at the NAIC



Connecticut Insurance Commissioner Tom Leonardi

Photos courtesy of the NAIC

There have been more vigorous disagreements in Kentucky: that little cross-border dispute between the McCoy's of Kentucky and the Hatfields of West Virginia springs to mind. But at a meeting of the Governance Review Task Force—which itself sprang back to life like a zombie from *The Walking Dead*, reinstated to the schedule after first being canceled—regulators dispensed with diplomatic bromides and vigorously shared often opposing views on the future of the NAIC.

This discussion had begun less than a year before when Connecticut Insurance Commissioner Tom Leonardi shared his concerns about the NAIC's governance with his fellow regulators. In response, the NAIC had decided to hire a consultant to review its governance, and a request for proposal issued by the NAIC to vendors had been done just days before. However, responsibility to choose the vendor had been shifted from the Task Force to an executive subcommittee.

Saying that he was encouraged by the response to the RFP and that the NAIC was making progress, immediate past president Louisiana Commissioner Jim Donelon said, "Some of us were anxious to have this meeting here today to keep the focus on what is being done."

"My concern deals very much again with the issues I raised in December," said Leonardi. These issues included transparency and good governance. Leonardi said control over the process had been removed from the Governance Review Task Force with no discussion and no ability to respond, and placed in the hands of a new group imposed by the leadership of the NAIC.

This group will choose a consultant, Leonardi said, but four of the five members of the new committee named from the Governance Review Task Force previously had voted against the need for a governance review.

Illinois Insurance Director Andrew Boron voiced his dismay. Referring to the famed Pogo cartoon in which Pogo met the enemy, Boron said, "That enemy is us."

Boron pointed out that any state may leave the NAIC at any time, and decisions should be made in a transparent fashion. I don't believe that is happening now, he said. Referencing George Orwell's *Animal Farm* where some animals were more equal than others, he said this organization cannot succeed if decisions are being made in secret by a few. He criticized what he called commissioners using questionable procedures to thwart the will of other regulators.

"I pray that there is not a person in this room who was not revolted by this decision," Boron said, demanding that the decision over the consultant be returned to the Governance Review Task Force.

Task Force Chair Director John Huff of Missouri said that while the executive committee named a subcommittee to make the vendor selection, the vendor will work with the Governance Review Task Force. Donelon noted that after concerns were raised by Leonardi and Boron, he requested NAIC leadership add Director Huff to the subcommittee. That request was denied.

Oklahoma Insurance Commissioner John Doak agreed with the criticisms. This process should be returned to the Task Force, he said. "There are meetings that are being held (between officers and staff) that commissioners are not being invited to... and are not noticed," he said.

The NAIC's President-elect, Montana Insurance Commissioner Monica Lindeen, denied people were being left out of the process. She implied that it was more a perception issue. "What we need to do is look at better ways to be better communicators," she said.

Interested parties joined in the discussion. One speaker suggested that the NAIC needed to define what it was—public or private. Until that is done, the speaker said, the organization will continue to have problems with governance.

One interested party asked if the new open meetings policy had allowed more meetings to be closed. A trade association representative said, "NAIC is now part of the process of state regulation... because of that it has a burden to do what you all do at home... that level of transparency." The representative suggested the NAIC do an analysis of open meetings to see if, after the implementation of the new standards, there had been fewer or more closed meetings.

North Carolina's Commissioner Wayne Goodwin made a motion to request that the Executive Committee rescind its subcommittee creation and return the process to the Governance Review Task Force. Director Huff said he was opposed because he did not want to slow down the process. Director Boron, quoting an earlier statement in another context by NAIC president Adam Hamm about doing it right, said delay should be secondary to doing it right.

Leonardi said that with the RFP just issued Friday, nothing had been done yet, so there would be no real slowdown. He said the issue was not membership but good governance, criticizing President Hamm's creation of the subcommittee. "We shouldn't have to have a discussion of what's good governance, but that ain't it," Leonardi said.

Donelon noted that during the subcommittee selection process, Commissioner Michael Consedine of Pennsylvania called it ill-advised because it was dominated by officers. Leonardi's concerns included the fact that a review of governance policies, partly focusing on what some considered the too strong role of president and past presidents of the NAIC, would be done by a group selected by the president and soon to be presidents and eventually past presidents of the NAIC.

"It's the appearance of what happened here that [the group] should take the time to back up," said Doak, adding that if he were an officer he would recuse himself and return it to Governance Review.

Despite the vigorous discussion, the motion eventually failed on a 6-3 roll call vote after a voice vote proved ambiguous.

State departments to get help from NAIC on PBR; VAWG on its way

NAIC staff or consultants and state insurance departments may well be working together on PBR reports, the PBR Review (EX) Working Group was told by Chairman Mike Boerner, Texas, as the working group discussed NAIC support for PBR reviews and state insurance department staffing.

While there will be further discussion on calls, Boerner said the idea was for NAIC resources to review PBR reports and asset adequacy analyses in tandem with state insurance department staff. NAIC resources would help provide consistency, since there would be lots of judgment involved, Boerner explained.

He also said there could be a role for the Valuation Analysis Working Group (VAWG) to work with the Life Actuarial Task Force (LATF) on interpreting the Valuation Manual (VM). The definition of the scope of the requirements is to be discussed on two conference calls before the next national meeting in Washington, D.C. In addition, the working group will seek to determine to whom VAWG should report.

The working group received a PBR Blanks Reporting (EX) Subgroup report from Larry Bruning (NAIC staff). It discussed and exposed the draft principle-based reserving (PBR) blanks changes, supplements and revised blanks instructions for 45 days. The Working group also discussed receiving a presentation from ACLI to discuss comments on some parts of the document.

The working group received a brief PBR Review Procedures (EX) Subgroup report from Pete Weber of Ohio. As several of the NAIC tools are confidential and regulatory only, the Subgroup met in closed session to brainstorm with NAIC staff. Bruning presented a draft supplemental data collection template for VM-31 to the working group, but stated it is not ready to be exposed for comment as more changes were needed.

Boerner said that VAWG Procedures Manual has been drafted for regulator review, but it is considered regulator-only because the document was modeled after the Manuals for FAWG, Re-FAWG, and R-FAWG, which are regulator-only documents. Mark Birdsall of Kansas requested a bullet to the materials to describe the ability of VAWG to provide feedback to a Company on how to reserve for new products.

In other matters, the working group received a status update from Bruning (NAIC staff) on the development of the PBR Statistical Agent Framework. Three comment letters were received and will be considered. The working group also received a status update on PBR company outreach. Fifty-three companies provided data, however, the Society of Actuaries is currently attempting to resolve inconsistencies in the data received. The results of the survey should be received by the end of the year.

FSOC looking at captives; the Fed wants partnership

Not surprisingly, issues beyond its direct purview dominated the discussion at the meeting of the Financial Stability (EX) Task Force. This began with the task force hearing an update from Chair Commissioner Ken Kobylowski of New Jersey on the implications of current IAIS financial stability initiatives. Elise Liebers of the NAIC remains the acting chair of the IAIS Financial Stability Committee (FSC).

The IAIS will be making annual determinations on G-SIFs in November 2014, which will include the assessment of large global reinsurers. Additionally, the first consultation of the Financial Stability Board's (FSB) Assessment Methodologies for Identifying Non-Bank, Non-Insurer (NBNI) Global Systemically Important Financial Institutions (G-SIFIs) ended on April 7. The FSB, in consultation with the International Organization of Securities Commissions (IOSCO), will issue a proposed assessment methodology for NBNI G-SIFIs by the end of 2014.

Missouri Director John Huff, a non-voting member of the U.S. Financial Stability Oversight Council (FSOC), provided the Task Force an update on the FSOC process. The FSOC is monitoring several areas related to insurance, including:

- Concerns with captive insurers related to regulatory arbitrage, added complexity, reduced transparency and resolvability;
- The low interest rate environment; and
- The transfer of pension plan exposure to insurance companies.

During the FSOC's annual evaluation of two previously designated non-bank SIFIs, it decided not to rescind the designations.

The Task Force engaged in a discussion with the Fed's Thomas Sullivan regarding insurance supervision and collaboration. During the discussion, it was noted that the Fed currently regulates about one-third of the U.S. premium through bank and savings and loan holding companies.

The term, "Team U.S.," was repeated on several occasions by state regulators, Sullivan and interested parties, primarily in the context of encouraging a common U.S. position regarding international matters. Not all was sweetness and light, however, with Connecticut Commissioner Tom Leonard complaining that state legislators had been marginalized and minimized at the IAIS and by the federal government over the past three years.

Differences between the Fed and state insurance regulators were discussed, such as the Fed's "going concern" considerations and its constraints related to the Collins Amendment. Regarding supervisory colleges, where applicable, the Fed expressed the desire to sit at the supervisory college table with state regulators and co-lead.

Private equity still being examined

The Private Equity Issues (E) Working Group will hold a conference call to discuss issues related to transactions between favored investors and insurance companies. Iowa's Jim Armstrong, Vice Chair of the working group, said, "We've noticed transactions where insurance companies have done transactions... with large investors in private equity companies."

The working group was given a presentation by A.M. Best on that company's view of private equity issues in insurance. Among other findings, an A.M. Best survey said there was no impact on insurers' strategies of the increased flow of private equity into the insurance industry.

Best found that start-ups faced challenges including the lack of a track record for their management team, capital raising, business model, need for scale, license, ALM and cash flow testing, transparency, risk management, short vs. long term view, and the complex structure of the business.

In rating new company formation, A.M. Best looks at factors including the five-year business plan, policy statements on underwriting, investments and risk management, products, risk adjusted capital above that of a mature company, strong management alignment of insurance and asset expertise, U.S. legal entity versus offshore status, and strong risk management.

Concerns about rated groups were different, including significant growth and whether that was organic or through M&A, high minimum guarantees, higher than average risk asset classes, disintermediation risk, change from reinsurance to direct, risk management, fee based businesses, a level playing field statutory accounting and permitted practices, fees, dividends and leverage, and unrated reinsurers.

Offsetting these concerns were factors including risk-based capital with limited adjustments, strong liquidity, U.S. based entities, management insurance expertise, mix of mortality risk, operating performance versus expectations, strong capital commitment, risk management capabilities, and quarterly and annual updates.

The working group also discussed proposed changes to the Financial Analysis Handbook affecting private equity. A representative of a company linked to private equity expressed appreciation for the staff's work, but noted some concerns with the proposal. Areas of concern include:

1. Requiring personal financial statements: While it is appropriate and to look at directors, the fear is that this is a complicated structure and there is a lot of information required and this might make it difficult to get qualified individuals to sit on the boards of holding companies, he said, calling it a mistake.
2. Focusing on return target: Return targets are not requirements, he said, investors do not have a guarantee. In addition, this is proprietary information.
3. Return levels and the relationship to risk: The returns might be higher but often the companies are picked up at a discounted price. Therefore the level of risk is not necessarily higher, he told the working group.

The working group has also asked the Securities and Exchange Commission (SEC) to come in and discuss expense issues they have raised. This discussion, the Group expects, will help provide insight into the necessary changes to the Handbook.

More states adopt PBR

Despite the opposition of some large states, principle-based reserving (PBR) adoption for life insurance companies continues, Tennessee's Commissioner Julie Mix McPeak told the PBR Implementation (EX) Task Force.

At last count, 18% of states representing 28% of premium have adopted the enabling legislation, with 12 more states adopting or introducing the legislation by 2015. If those states adopt the legislation, 30 states representing 60.3% of premium would have adopted PBR. To become effective, PBR must be adopted by 42 states representing 75% of premium.

McPeak said there was a chance for PBR to become operative in 2016, although a January 2017 date would be more realistic.

The Task Force also reviewed comments on the Statistical Agent Framework. Comments included:

- A single agent may not be ideal;
- Warehousing data collected is problematic because of confidentiality issues;

- There were also other confidentiality concerns expressed by industry;
- Varying suggestions for cost allocation; and
- A suggestion that direct NAIC collection as opposed to even three-state collection would be preferred.

The Task Force directed NAIC staff to revise the draft Framework. The Task Force also discussed the adopted Framework for captives from the Rector Report. Its author, Neil Rector, told the Task Force that "there would be serious and substantial disclosure as part of the 2014 annual statement." However, he did not anticipate that modified VM20 calculations would be included in the 2014 report, and was only cautiously optimistic that the revised schedule shown in his Report would be acceptable.



E Committee adopts governance changes

The closest the meeting of the Financial Condition (E) Committee potentially came to a moment of drama was when Florida's Danny Altmaier raised an objection to the adoption of the Corporate Governance Model Act because of its language regarding confidentiality. Florida regarded the language as too restrictive, citing provisions including the fact that filings would not be subject to subpoena. Committee Chair Superintendent Joseph Torti of Rhode Island said the language was similar to those in the exam laws, while Vermont Commissioner Susan Donegan added that the wording was based on the advice of NAIC counsel.

Drama over, the committee adopted the Corporate Governance Annual Disclosure Model Act and its attendant model regulation. The committee also agreed that a charge will be added to investigate and eliminate regulatory redundancy, with most to be addressed in the Risk-Focused Surveillance Working group. Pennsylvania's Steve Johnson encouraged states to do better training of staff and reviewing existing workpapers and databases before asking insurers for information.

The report of the Receivership and Insolvency (E) Task Force (RITF) was adopted. The report included an action that tabled a charge at this time to require large insurance groups to prepare resolution plans. The report also adopted a NAIC Model Guideline titled Guideline for Payment of Interest to Receiver on Overdue Reinsurance Recoverables.

The guideline is intended for use by receivers in instances where a reinsurer unjustifiably denies payment after such time as a claim under its reinsurance agreements has

been shown to be properly due and owed. It is not an amendment to the NAIC Receivership Model, but to be used by states seeking to permit a receiver to collect the payment of interest on overdue reinsurance recoverables and pre-empts any contract language that prohibits the payment of such interest.

The committee discussed a memorandum on recommendations regarding separate accounts. The committee agreed to work with NAIC staff and legal counsel to determine the best way forward. The committee also discussed a preliminary report on Examiner Salary Recommendations from NAIC staff.

The committee adopted the reports of all of its subsidiary task forces and working groups. The committee discussed and agreed to expose for a 30-day comment period the proposed modification to Actuarial Guideline 38 – The Application of the Valuation of Life Insurance Policies Model Regulation (Model #380), which will delete the existing requirement for companies to file annual reports with the Financial Analysis (E) Working Group while granting the working group the right to ask for such reports when appropriate.

Interested party comments on the exposed draft NAIC Group Code Assignment process were received, but due to time constraints, the NAIC will follow-up on the comment letters on another call.

Ridesharing to get further study

Cars and California have long seemed to go together, even if getting anywhere in a car in some California cities is enough to make some want to move east. The hassle of having one's own car may partly explain the rise of ridesharing services, so fittingly, California will lead a working group set up by the Property and Casualty (C) Insurance Committee to develop information and evaluate ridesharing practices, policies, and the insurance impact.

At least seven other states will join California on the panel, including Alaska, a state where not just many towns, but the state capital Juneau is unreachable by road. Among other issues, the panel will compile state by state activities, including loss data.

The committee also heard a presentation on a car rating model based solely on the vehicle history and not consumer data. Among the information such a model would be able to incorporate would be the difference between reported and actual miles driven per year.



ComFrame field testing not showing capital strain

The ComFrame Development and Analysis (G) working group heard an update from Ramon Calderon of the NAIC staff on the field testing process currently being undertaken by the IAIS for ComFrame. Calderon stated that quantitative testing of 33 volunteers had not revealed any adverse findings related to the current definition of capital resources.

Commissioner Ken Kobylowski of New Jersey provided an update to the working group on the IAIS's Basic Capital Requirements (BCR) and Higher Loss Absorbency (HLA). Comments received in the consultation on BCR will be discussed at a closed IAIS meeting. The IAIS still intends to maintain an accelerated schedule that would allow a final BCR proposal to be endorsed by the G20 during November 2014.

Tennessee's Commissioner Julie Mix McPeak provided an update to the working group on the Insurance Capital Standard. Industry representatives expressed concerns regarding transparency and the accelerated timeframe for developing these group capital proposals. Commissioner Kevin McCarty of Florida stated that the NAIC has cautioned the IAIS Executive Committee on the matter, but the response was that the IAIS's credibility was at stake as a standard setter.



Actuaries discuss catastrophe risk charge

The Catastrophe Risk (E) Subgroup discussed the aggregate (AEP) basis versus occurrence (OEP) basis for catastrophe risk modeling. Interested parties suggested that while AEP is more comprehensive and considers frequency and severity, OEP was the standard and preferable.

For example, most rating agencies use OEP, except for S&P which uses AEP. Additionally, most insurers manage hurricane and earthquake risk on an OEP basis. Lastly, AEP can introduce volatility at the one in 100 year level because retentions and reinsurance limits could be different. No conclusion was reached, but the subgroup will continue discussing the topic on a future conference call.

The subgroup then discussed two methods raised by industry for calculating the R6 and R7 within the new RBC catastrophe risk charge that were exposed on the July 22, 2014 conference call. An interested party suggested that the option 2 was invalid because it calculates from two different curves. The Chair stated that the option would need a third curve in order to be consistent with assumptions. The Chair had initially posed a question of whether to let a company use whatever method it uses to sort modeled loss curves gross and net of reinsurance, however, the use of an invalid method above illustrates the risk with that approach.

The subgroup discussed exemption criteria for PR026, Calculation of Catastrophe Risk charge R6 and R7, since some companies don't model such risks. The National Association of Mutual Insurance Companies (NAMIC) requested the subgroup reconsider premium volume exception criteria. Instead, the subgroup requested industry to propose some exemption criteria for companies with minimal catastrophe exposure for consideration. The subgroup also requested NAMIC to address the issues it previously cited with its proposal.

The subgroup discussed the contingent credit risk charge for the R6 and R7 components. Some interested parties believe the 10% credit risk charge is onerous. The subgroup requested solutions.

The Chair stated that catastrophe risk data was being collected by the states and that the NAIC would be compiling the results into a summary analysis.

Task force hears CDAs may be covered by guaranty funds

The Receivership and Insolvency Task Force adopted the Model Guideline for Payment of Interest to Receiver on Overdue Reinsurance Recoverables. The guideline is intended for use by receivers in instances where a reinsurer unjustifiably denies payment after such time as a claim under its reinsurance agreements has been shown to be properly due and owed. It is not an amendment to the NAIC Receivership Model, but to be used by states seeking to permit a receiver to collect the payment of interest on overdue reinsurance recoverables and pre-empts any contract language that prohibits the payment of such interest.

The task force also adopted the Guidance on Separate Accounts for the NAIC Receivership Handbook for Insurance Company Insolvencies, Chapter 9: Legal Considerations. The guidance, which was drafted by the Receivership Separate Accounts (E) Working Group, includes considerations for handling separate accounts, such as: applicable federal and state statutes and rules, case law, example rehabilitation orders, SEC Registered Products considerations, Federal Securities Laws, etc.

Working group reports were received with little discussion. Regarding points of interest, the Receivership Model Law (E) Working group is in the process of evaluating the Insurer Receivership Model Act, the Life and Health Insurance Guaranty Association Model Act and the Property and Casualty Insurance Guaranty Association Model Act to assess the provisions of the existing acts that should be uniform across states.

The Task Force adopted the report of the Receivership Reinsurance Recoverable Working group that approved recommended benchmarks for reinsurance recoverables in the Global Receivership Information Database (GRID).

The National Organization of Life & Health Insurance Guaranty Associations (NOLHGA) made a presentation on Contingent Deferred Annuity (CDA) definition and related guaranty association coverage. NOLHGA stated that the CDA was classified under state law as an annuity. The coverage summary was that CDA certificates issued to individual consumers appear to be eligible for guaranty association coverage, subject to guaranty association coverage limitations and partial exclusions that may limit guaranty coverage, just like any other annuities.

A professional services firm presented on Resolution Planning. The presentation noted that the Federal Reserve and Federal Deposit Insurance Corporation (FDIC) recently released statements discussing shortcomings with bank resolution plans. After the presentation, the task force tabled at this time the charge to evaluate the benefits and costs associated with requiring resolution plans for large insurance groups.

The Task Force discussed the FIO report recommendations regarding receivership and assigned some related research duties to an existing working group. The task force will continue discussions on the FIO report at a future time.

Mortgage guaranty capital modeling project still in development

The Mortgage Guaranty Insurance (E) working group heard a presentation from mortgage guaranty representatives on the status of the Oliver Wyman capital modeling project. The model is still in the development stages. During September 2014, the insurers working on the project together will review preliminary specifications and back test results to the working group using company data.

A representative stated that the group is considering numerous items, including: cyclical nature of housing markets, life of loan commitment, adequacy of claims paying resources, use of loan-level models, countercyclical stresses, seasoning factors, loss severity, etc. However, there are limitations with the loan models because they only consider first-lien, 1–4 family residential loans.

The mortgage insurers also requested that future meetings on the project be conducted in closed session, since some of the entities are publicly traded and the companies will be using company data. A consumer representative strongly disagreed with the request, stating that the insurers could utilize a generic data set to conduct the review and that a closed meeting would represent antitrust issues. Lastly, mortgage insurers who withdrew from Phase 1 asked to be included in the confidential discussions.

The working group heard an update on federal developments in housing finance and mortgage guarantee matters. Tony Cotto of the NAIC provided a view point that legislation on these issues is likely dead for 2014, but GSE reform could become a priority item in the 2015 Congress, as members of the House want government out of the mortgage market, and have gone as far to label it a wealth redistribution scheme. The Chair asked members and NAIC Staff whether it should be more proactive than reactive with Congress on a federal solution. NAIC staff advised that it could be challenging for states to take a forward position.

The working group discussed comments on the draft revised Mortgage Guaranty Insurance Model Act (Model 630), which included six key issues. Regarding Section 10 on reinsurance, the working group agreed with many of the RAA's comments and would consider incorporating into the next draft of the model. However, the reinsurance section is on hold, since some provisions of the section are dependent on the completion of the capital modeling project.

Regarding Section 8C, the Working group agreed to run numbers to see if the wording created circular issues.

The working group also agreed to accept revisions to Section 8D Premium Deficiency Reserve proposed by Arizona, which mostly followed SSAP 58 language. Steve Junior of Wisconsin stated he withdrew his comments on Section 9—Investment Restrictions and will support an industry proposal plus a permitted practice requirement. Lastly, there was healthy debate among members regarding the inclusion of the draft Section 11 Underwriting Standards. California stated it would be difficult to get through the legislature. North Carolina stated it was too much detail. Steve Johnson of Pennsylvania strongly believed the language was needed to illustrate companies broke the law. The working group left the language intact, but changed “shall be written” to “may be written.”

In Brief

CDAs get the spotlight

Contingent Deferred Annuity (A) Working Group Chair Commissioner Ted Nickel of Wisconsin told the working group that Model Act 805, the Standard Nonforfeiture Law for Individual Deferred Annuities, was not the appropriate place to address nonforfeiture benefits for contingent deferred annuities (CDAs). Consumer representative Birny Birnbaum had highlighted what his group saw as the lack of appropriate protection for consumers, most especially with nonforfeiture benefits, as a major concern with CDAs. On a related matter, the working group reached a consensus to revise the Annuity Disclosure Model Regulation (#245), the Suitability in Annuity Transactions Model Regulation (#275), Advertisements of Life Insurance and Annuities Model Regulation (#570), and Life Insurance and Annuities Regulations Replacement Model Regulation (#613) to specifically mention CDAs. CDAs were recently defined by the NAIC as annuities, with some regulators and insurers objecting to that action. The instruments are designed to protect a portfolio and ensure continued income.

Unclaimed benefits

Discussion on what to do about unclaimed life insurance benefits will continue, partly due to new federal government restrictions on the use of the Social Security Death Master File (DMF). Insurers were supposed to compare their files against the DMF to uncover covered deceased, but the federal government imposed new limits on the use of the file, requiring all with access to be licensed. The NAIC's Brooke Stringer told the Life Insurance and Annuities (A) Committee that the Department of Commerce who had issued an interim final rule allowing a temporary certification program for those persons needing to obtain access to the DMF. A final rule was to be issued this summer, but may be delayed.

Reinsurance rolling along

Twenty-three states have passed legislation to implement the Revised Credit for Reinsurance Model Act, representing almost two-thirds of written premium, the Reinsurance (E) Task Force was told.

Actuarial Update

Life Actuarial Task Force (LATF)

LATF is still pushing through additional amendments to the PBR Valuation Manual. Although a 1/1/2016 operative date is unlikely (based on the pace of legislative activity, a 1/1/2017 date is the current “best estimate”), LATF is moving its agenda forward as if a 1/1/2016 operative date is still a possibility. Other activities include further work on new life mortality tables, principles based annuity reserving standards, a new Life Reinsurance guideline (Actuarial Guideline 48), and nonforfeiture modernization. Following are highlights from LATF from the Summer 2014 NAIC Meeting:

New Actuarial Guideline 48

LATF exposed a draft Actuarial Guideline 48 on which address XXX/AXXX reserves ceded to a reinsurer, including captive reinsurers. The guideline is in response to Rector Report recommendations and subsequent NAIC discussion of the report. Under the proposed guideline, ceding insurers will need to calculate minimum reserves and such reserves will need to be secured by “hard” invested assets instead of “softer” assets such as letters of credit (LOCs). The proposed minimum reserves for term are 85% of the NPR (per the latest draft of VM-20). For universal life with secondary guarantees (ULSG), the proposed minimum reserve is the minimum of deterministic, stochastic, or 85% of NPR (again, per VM-20). The effective date for the guideline will be 1/1/15 for new policies or for inforce policies under new reinsurance agreement entered into on 1/1/15 or later. The proposed AG 48 was exposed for comments for 30 days, and a revised version will be discussed at the Fall NAIC meeting.

New Mortality Tables

The American Academy of Actuaries (AAA) gave another update of the mortality work being performed by the Society of Actuaries (SOA) and AAA toward developing the 2014 VBT/CSO mortality tables and tables for PreNeed and Simplified Issue products.

Regarding the 2014 VBT (industry experience) tables, LATF voted to expose the AAA presentation and tables for a 60 day comment period. Following the comment period, the AAA anticipates a testing phase with volunteers from the NAIC and industry, plus consulting assistance performing the testing over the fall and winter months with a spring 2015 target completion date. Work on the 2014 CSO table will follow with a target adoption date in August 2015 and a 1/1/2016 operative date. Work will continue concurrently on the PreNeed and Simplified Issue tables, with a spring 2015 completion date targeted.

Life PBR (VM-20)

Work continues on refinements to the Life portion of the Valuation Manual. However, the pace of proposed amendments has slowed compared to prior meetings. Proposed amendments to VM-20 included the following:

- The ACLI proposed changes to exempt small companies from PBR that do not have complex products (such as secondary guarantee UL). LATF voted to expose the changes for comments for 21 days. Following that, comments will be discussed on LATF conference calls.
- The ACLI also proposed to exempt UL products with “non-material” guarantees from stochastic testing. LATF voted to expose the change for comments for 30 days.
- The ACLI also proposed an amendment to defer the mortality credibility process under Actuarial Guideline 38 to 1/1/2017, the expected operative date of PBR. LATF voted to expose the change for comments for 30 days.

General Account Annuity PBR (VM-22) Subgroup

The VM-22 Subgroup provided another update on activities from LATF and from the AAA. LATF is now compiling results from additional Kansas field tests, this time testing VM-22 parameters across products for two sample companies, including an aggregate margin methodology. The Kansas Department Chief Actuary Mark Birdsall discussed preliminary results from one company (the other company had not completed testing) including patterns in PBR reserves by product and relative to CARVM reserves. Next steps are to compile results from the other company. In addition, LATF expects to have a draft of VM-22 ready for exposure by the Fall meeting.

Post Level Term Lapse Experience

The Society of Actuaries (SOA) provided a summary of results from a recently released experience study on post level term lapses. There has been increased focus on this topic recently as many large blocks of inforce term policies sold in the 1990s and 2000s have been entering post-level premium duration. The study indicated varying results for the “shock lapse” at the end of the level premium period, depending on the “jump” in premium in the first non-level duration. While not immediately applicable to statutory reserving methodology, the study should be of interest for cash flow testing purposes in the near term and for PBR in the long term.

The actuarial update was prepared by Russell Menze. For your comments and suggestions please contact the author – rmenze@deloitte.com.

Health Care Update

The mission of the Health Insurance and Managed Care (B) Committee is to consider issues relating to all aspects of health insurance and work related to the implementation of the Affordable Care Act (ACA) continued to dominate the agenda in August. The focus is more than just implementation of the programs, but how it is enacted across the states and focusing on the impact to consumers.

The committee heard an update from the Center for Health Insurance Reforms (CHIR) on its work related to the ACA through the State Health Reform Assistance Network. The committee wanted to learn—what are they hearing out in the marketplace. CHIR is based at Georgetown University's Health Policy Institute and works to improve access to affordable and adequate health insurance by providing balanced, evidenced-based research, analysis and strategic advice. CHIR representatives discussed a recently released issue brief titled, "Specialty Tier Pharmacy Benefit Designs in Commercial Insurance Policies: Issues and Considerations" and a recently released white paper related to qualified health plan (QHP) renewals for plan year 2015 titled "Addressing the Financial Impact of Renewals: Why Many Enrollees Could Benefit from Shopping."

The brief discusses the use of pharmacy benefit designs as one of the few remaining mechanisms for health insurers to control costs given the changes due to the ACA reforms including eliminating underwriting and imposing a federal minimum loss ratio limited administrative and other non-healthcare spending, which may impact the affordability of prescription drug therapies. The white paper discusses the importance of evaluating premium increases by looking at the after-subsidy and tax liability implications. Marketplaces are using auto-renewals and rolling over Advanced Premium Tax Credits to make the renewal process as smooth as possible for consumers; however, this approach may be detrimental to some consumers, depending upon changes to factors such as income, premium or changes in the benchmark plan. Consumers in evaluating premium increases need to consider the impact of premium increases after consideration of the subsidies. Further information on the briefs is available at www.state.network.org.

The consumer was a focus at the meeting of the committee and its subgroups and task forces. The Consumer Information (B) Subgroup discussed its current task of revising the Frequently Asked Questions about Health Care Reform document, including technical updates and new sections to be added. The Subgroup had queried state regulators about the usefulness of the of the FAQ document and comments received indicated that the document is useful, so the Subgroup is proceeded with the revisions and discussed how states are using the FAQ document on its website and providing linkage to additional consumer materials. The Subgroup also received comments about addressing questions from consumers and noted the importance of education and improving consumer literacy.

NAIC consumer representatives provided an update to the committee and to the Regulatory Framework Task Force about network adequacy issues. While public scrutiny focuses on the availability of certain physicians or hospitals in its network, the consumer representatives are focused on the overall availability and quality of the network. This dynamic of the individual viewpoint versus the broader adequacy and quality of the overall network presents challenges and a significant need for consumer education. Consumer literacy and education was something both the consumer representatives and the NAIC representatives agreed was of importance. The challenge is developing accuracy information on a timely basis and distributing out to the marketplace for consumers to utilize. Consumer representatives noted that surveys had been sent to all of the state insurance departments related to network adequacy issues and encouraged all states to fully engage in responding to the survey to engage and provide feedback.

The health update was prepared by Lynn Friedrichs. For your comments and suggestions please contact the author – lfriedrichs@deloitte.com.

NAIC Accounting Update

This section of the NAIC Update focuses on accounting and reporting changes discussed, adopted, and exposed during the 2014 Summer Meeting.

Statutory Accounting Principles Working group

Current Developments: The SAPWG adopted the following amendments as final during the 2014 Summer Meeting:

Ref#	Title	Sec.	Amendments Adopted as Final	F/S Impact	Disclosure	Effect. Date
2014-11	SSAP No. 86—Accounting for Derivative Instruments, Hedging, etc.	P&C Life Health	Nonsubstantive Change—Revisions to clarify the reporting of derivatives between Schedule DB and the balance sheet in order to allow the amounts to be traceable between the two schedules.	N	N	2015

The SAPWG exposed the following items for written comments (due by October 17, 2014, except Ref # 2014-28 which is due September 16, 2014) by interested parties—two proposals are substantive (see Ref # 2013-36 and 2014-23 below) and all other proposals are categorized as nonsubstantive:

Ref#	Title	Sec.	Amendments Exposed	F/S Impact	Disclosure	Effect. Date
2013-36	Various SSAPs related to investments	P&C Life Health	Substantive Change—Investment Classification Review: Proposed discussion topics, and their suggested prioritization for a comprehensive project to review “investment SSAPs” with suggestions to clarify definitions, scope and the accounting method/related reporting.	Y	Y	2015
2014-06	SSAP No. 57—Title Insurance	P&C	Nonsubstantive Change—Exposed revisions to delete the disclosure for premium revenue reported on the Gross-All-Inclusive and Gross-Risk-Rate premium basis, with corresponding revisions to the guidance.	N	Y	2014
2014-14 2014-26	Rejected GAAP Pronouncements	P&C Life Health	Rejected the following GAAP Pronouncements as not applicable: <ul style="list-style-type: none"> ASU 2014-10: Development Stage Entities, and INT 99-00: Compilation of Rejected EITFs Into Issue Paper No. 99 	N/A	N/A	N/A
2014-16	SSAPs Nos. 1 and 4—Disc. of Acct. Policies and Assets and Non-Admitted Assets	P&C Life Health	Nonsubstantive Change—Exposed revisions to clarify the difference between “restricted assets” and “admitted assets” as well as clarification of the reporting requirements for “restricted assets” (the goal is assure all “restricted assets” are included in the required disclosures).	N	Y	2014
2014-17	SSAP No. 104R—Share-Based Payments	P&C Life Health	Nonsubstantive Change—Exposed revisions to adopt ASU 2014-12: Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could be Achieved after the Requisite Service Period with an effective date of January 1, 2016 (with early adoption permitted).	Y	Y	2016
2014-18	SSAP No. 51—Life Contracts and SSAP No. 56—Separate Accounts	P&C Life Health	Nonsubstantive Change—Exposed revisions to enhance and clarify the disclosure currently captured in Note 34 related to contracts withdrawal characteristics. This action also included a proposal to the Blanks Working group to reflect a minor language revision to Notes 32 in order to make them consistent (effective in the 2015 Annual Statement Blank).	N	Y	2015

Ref#	Title	Sec.	Amendments Exposed	F/S Impact	Disclosure	Effect. Date
2014-19	SSAP No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses	P&C Life Health	Nonsubstantive Change—Exposed revisions to clarify that claims related losses for extra contractual obligations and bad faith lawsuits are to be included in losses.	N	N	2014
2014-20	SSAP No. 101—Accounting for Income Taxes	P&C Life Health	Nonsubstantive Change—Exposed revisions to clarify that the RBC authorized control level used in the annual realization threshold table for the DTA calculation should be using the RBC ratio for the current reporting period annual statement (i.e., in the process of being filed). For interim periods, the authorized control level RBC filed as of the most recent calendar year should be used.	N	Y	2014
2014-21 2014-22	Appendices A and C—Updates to allow the 2012 Group Long-Term Disability Table and Actuarial Guideline XLVII	P&C Life Health	Nonsubstantive Change—Exposed revisions to incorporate changes to Appendix A-010 adopted by the Health Actuarial Task Force and the related actuarial guideline, with preference for a January 1, 2016 effective date (with early adoption permitted).	Y	N	2016
2014-23	SSAP No. 69—Statement of Cash Flow	P&C Life Health	Substantive Change—Exposed agenda item requests information on the cash and non-cash transactions currently reflected in cash flow statements and preferences for what should be included/excluded (for example, non-cash intercompany exchanges, investments transferred as part of payment for operations, securities exchanged in reinsurance transactions, reconciliation to net income, etc.).	N/A	N/A	N/A
2014-25	SSAP No. 41—Surplus Notes	P&C Life Health	Nonsubstantive Change—Exposed agenda item requests comments on the need to clarify existing guidance (mostly within paragraph 10; using amortized cost or a “lessor of value”) and whether to revise the thresholds used when applying a statement factor for surplus note valuation.	N/A	N/A	N/A
2014-27	SSAP No. 54—Individual and Group Accident and Health Contracts	P&C Life Health	Nonsubstantive Change—Exposure requests information on the reporting for contract redetermination amounts resulting from Medicare Part D and Medicare Advantage, and whether guidance in SSAP No. 54 and SSAP No. 66 –Retrospectively Rated Contracts—should be applied.	N/A	N/A	N/A
2014-28	SSAP No. 62R—Property and Casualty Reinsurance	P&C Life Health	Nonsubstantive Change—Exposed revisions and requested the preferred reporting between two options for when asbestos and pollution exceptions are granted by state (comments due September 16).	N	N	2014

The SAPWG discussed, or received an update, on the following outstanding agenda items:

Ref#	Title	
2013-17	SSAP No. 40—Real Estate Investments	Single-Member and Single-Asset Limited Liability Corporations (LLCs) – Underlying Asset is Real Estate: Considered comments from the Capital Adequacy Task Force and directed NAIC staff to draft guidance to move assets into SSAP No. 40.
2014-12	New Issue Paper—Accounting for the Risk Sharing Provisions of the ACA	Affordable Care Act—Risk-Sharing Provisions: Directed NAIC staff to redraft the exposed issue paper to address a number of issues for the risk adjustment and risk corridors programs, including, but not limited to: 1) replacing the nonadmission guidance with criteria that incorporates conservatism and sufficiency of data; 2) removing the exposed 90-day guidance and adding language to be consistent with other government receivables; and 3) removing a reference to HHS guidance that has been superseded.
2014-15	Review of ASU 2014-11	ASU 2014-11: Repurchase-to-Maturity Transactions, Repurchase Financings and Disclosures: Moved to substantive active listing and referred consideration to the Restricted Asset Subgroup.
2014-24	Review of ASU 2014-01	ASU 2014-01: Accounting for Investments in Qualified Affordable Housing Projects: Directed NAIC staff to prepare revisions to SSAP No. 93 – Accounting for Low Income Housing Tax Credit Property Investments—to continue modified amortized cost methodology and gross presentation in investment income.

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