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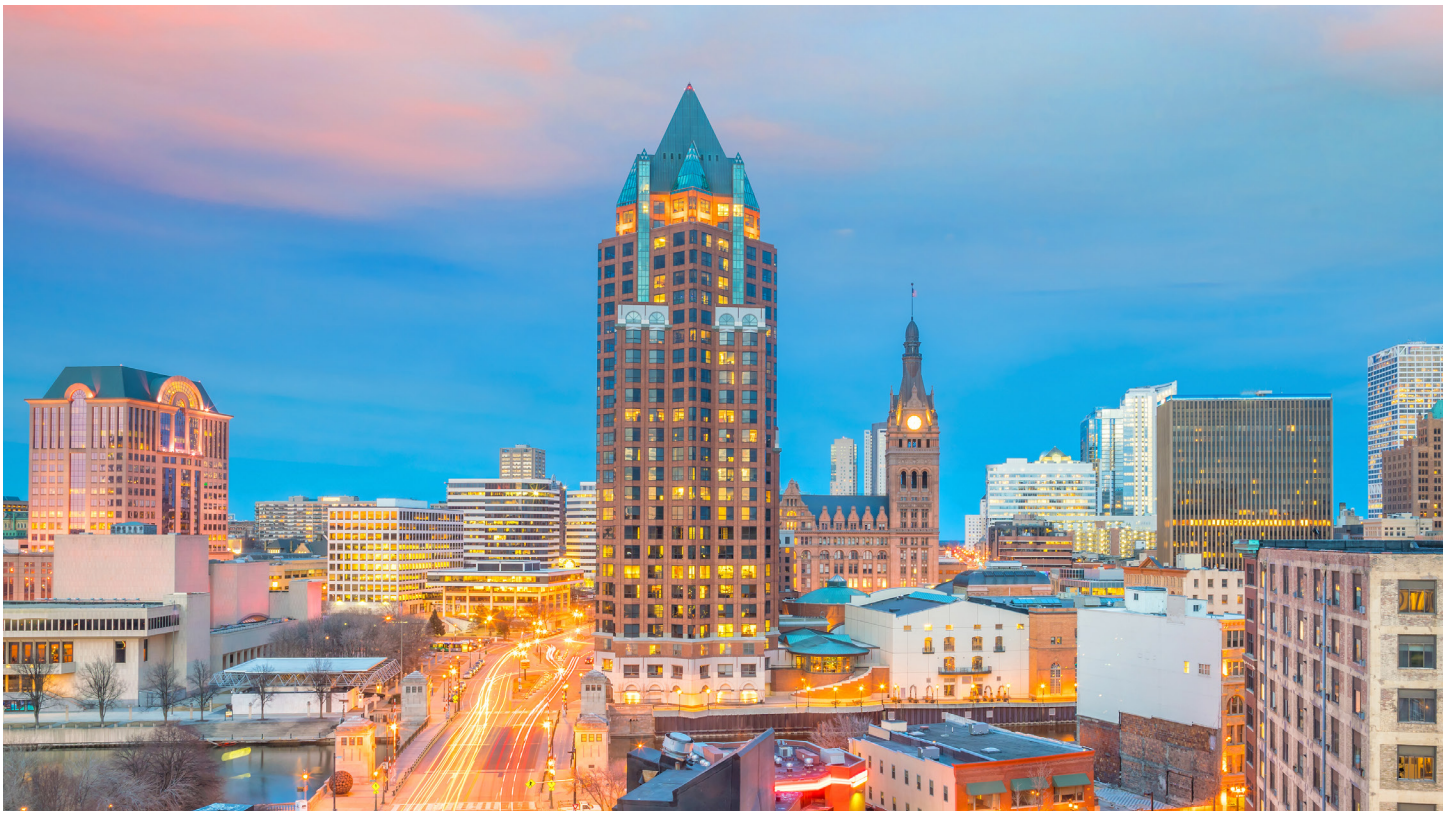

NAIC update: Spring 2018

State insurance regulators march ahead in Milwaukee

MILWAUKEE — Some things have not changed since the last time the National Association of Insurance Commissioners (NAIC) held its national meeting in Milwaukee in 1911. In that Wisconsin city, PBR, for example, still does not refer to principle-based reserving.

But much *has* changed. The NAIC meeting was held in the shadow of a ruling by the Fifth Circuit Court of Appeals apparently terminating the Department of Labor's fiduciary rule for retirement products. In Congress, work continued on a bipartisan if not bicameral effort to amend the Dodd-Frank Act.

Inside the Wisconsin Convention Center, state regulators were cognizant of the uncertainties caused by these changes. NAIC President Tennessee Commissioner Julie Mix McPeak observed in her opening statement, "In a variety of ways, the federal government

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has now endorsed the primacy of state regulation for insurance and identified areas where the federal government should more clearly defer to states. As they step back, the states must step forward to fill the voids."[1]

There was not necessarily agreement on what actions states should take in response. On issues such as a proposed "best interest" standard for annuity sales and possibly for life insurance sales, the apparent differences among states were inescapable.

There was agreement, however, on the future of the NAIC, with its three-year strategic plan, State Ahead—described as being driven by data and technological changes[2]—and its fiscal plan for 2018 investments consistent with that strategic plan unveiled and discussed.

In her opening statements, McPeak said the plan was an effort to "bring to bear the brightest talents, cutting-edge technologies, and our wealth of data to better serve state regulators in this brave new world we find ourselves in."[3]

With a recent Deloitte survey of state insurance regulators finding that budgets may represent the biggest obstacle to adopting the new technologies regulators seek,[4] the NAIC action may provide the resources necessary for all the organization's members to use new technologies to enhance their regulatory efforts.

Movement continued on other fronts. Issues addressed included long-term care insurance concerns, the reinsurance covered agreement, changes to the Affordable Care Act, and the ongoing work on the development of a group capital metric.

As is normal for the first meeting of the year, few final decisions were made, as regulators worked toward consensus and clarity. The fall meeting is usually where most changes are adopted, but given the importance and timeliness of issues such as the "best interest" standard and the necessity to adjust risk-based capital (RBC) to reflect tax law changes, the summer meeting in Boston may be livelier than most.

Photo courtesy of the NAIC

Scope, non-regulated entities, were the focus of the group capital calculation discussion

At the Group Capital Calculation (E) Working Group meeting, members discussed comments received on the proposed treatment of non-regulated entities in the group capital calculation and the potential scope of that calculation.

A representative of the American Council of Life Insurers (ACLI) focused on the treatment of asset managers and registered investment advisors in the proposal, saying the RBC charge should be applied to subsidiary asset managers and investment advisors.

The ACLI also recommended field testing for non-subsidiaries with the Basel standard being used as the basis. If there was a difference, then the working group should refer follow-up to the appropriate committee. The commenter said the group capital calculation should not undermine the existing state regulatory framework, and that the working group should not unilaterally change RBC.

A representative of America's Health Insurance Plans (AHIP) told the committee its primary concern was that the scope of the calculation may provide for the exclusion of smaller plans and holding companies with no international focus. The health market in the US is very different from life and property casualty, the representative said, so it was difficult to respond to internationally focused efforts on group calculation.

The representative of a US insurance company called for a rethinking of the working group's approach to group capital, voicing opposition to the scalar approach and support for the inventory approach. A representative of a coalition of industry stakeholders suggested that any calculation should use a legal entity basis framework, except where such a framework does not exist. This may include "sister entities," subsidiaries of holding companies.

"Any changes to the legal entity rule should only be made at the legal entity basis," the representative said.

Another US insurance company representative expressed concern about what he considered an overly broad view of the scope of the group included in the calculation, saying this may result in a false positive. With a big group with an insurance entity, he said, it may seem as if group capital was available to pay claims when it was not.

The representative suggested regulators use regulatory discretion in defining the scope of the group, and that group capital should focus on the "insurance group."

A representative of the National Association of Mutual Insurance Companies (NAMIC) said there was a need to keep any work aligned closely to the RBC process, referring to ICP 23, the international standard governing the treatment of mixed conglomerates. The representative suggested the group should use other group capital requirements such as the insurance capital standard to avoid multiple requirements for a group.

The Property Casualty Insurers Association of America (PCI) thinks a group capital calculation should focus on consumer protection and thus contagion risk, its representative said, adding that the scope of the group was an issue. He suggested it should be limited to the intermediate financial services holding company in large conglomerates.

Speakers from two large US insurance companies said they saw the group capital calculation as complementary to RBC, while the representative of a large health insurer said it was not necessary to sweep in health insurers because of the difference in structure.

Chair Florida Commissioner David Altmaier will ask NAIC staff to review the memo prepared by staff on the treatment of non-regulated entities in light of the comments received.

Speaking about the scope of the calculation, the representative of one US insurer called for a quick resolution of the issue, expressing concern that unfettered regulatory discretion could result in differing outcomes nationwide. He also pointed out what he saw as an inconsistency with the aggregation approach, in that the group capital calculation began with the ultimate controlling person, while aggregation worked from the ground up.

A memorandum on the scope of the group was exposed for a 45-day public comment period.

Photo courtesy of the NAIC

"Best interest" draft model for annuity sales is reopened for comment

The Annuity Suitability (A) Working Group met shortly after court decisions affecting the current core work of the group. A decision by the Tenth Circuit Court of Appeals rejected a challenge to the US Department of Labor's (DOL) fiduciary rule requiring certain retirement product providers to act in a fiduciary capacity.

However, a decision from the Fifth Circuit struck down the DOL rule. The working group had been considering its own best interest rule for annuity sales, and it continued this discussion in light of the court rulings.

Numerous speakers agreed that the NAIC could now take a leadership role in creating a new standard, working with the Securities and Exchange Commission (SEC). An ACLI representative told the working group the ACLI remained committed to "appropriately tailored rules for annuities" that require the best interest of consumers. He noted that there had been significant marketplace disruption with only partial implementation of the DOL rule, saying that an NAIC model was needed.

A representative of the Independent Insurance Agents and Brokers of America (Big I) welcomed the decision from the Fifth Circuit, asking what deficiencies regulators saw in the current model, and what producers should do that they are not now doing. NAIC consumer representative Birny Birnbaum told the group that saying there was no problem with the current regime was simply not credible.

Working Group Chair Idaho Commissioner Dean Cameron said he was reopening the comment period on the current chairman's draft and model act for 30 days, with the hope that there would be a face-to-face meeting after that, probably in May. He said this was so that the NAIC leadership could have a document ready to go into a meeting with the SEC, which is preparing its own rule on the subject.

Numerous speakers agreed that the NAIC could now take a leadership role in creating a new standard, working with the Securities and Exchange Commission.

"A" Committee ponders best interest rule

Evidence of regulatory disagreement over the future regulation of annuity sales first surfaced in the Annuity Suitability Working Group when a New York regulator expressed concern about the reopening of assumptions as well as the chairman's draft of the new "best interest" model. That disagreement resurfaced at the meeting of the Life Insurance and Annuities (A) Committee during the discussion of the adoption of the report of the working group.

New York Department of Financial Services Superintendent Maria Vullo asked for a discussion on the new comment period for the proposed model.

Working Group Chair Idaho Commissioner Dean Cameron advised Vullo the new comment period was opened because the direction in which the working group was headed was not necessarily the most appropriate given recent court rulings, and the working group wanted new stakeholder feedback. He said he had discussions with leadership, which supported a full review in light of the ruling from the Fifth Circuit Court of Appeals striking down the DOL fiduciary rule.

Vullo said the decision on an additional comment period was not made by the working group but by the chair, and that the minutes did not accurately reflect that. Cameron responded that the document provided to the committee was a report and not the minutes of the working group. He further said that while there had been no motion for the new comment period, there had also been no objection. The committee then adopted the working group's report.

New York has already proposed a new regulation mandating a "best interest" standard be used for life insurance and annuity sales in that state.

Adding travel insurance to MCAS is up in the air

The Market Regulation and Consumer Affairs (D) Committee refused to overrule one of its working groups and authorize the addition of a new line to the market conduct annual statement (MCAS).

Consumer representative Birny Birnbaum asked the committee to do what the Market Analysis Procedures (D) Working Group would not—add travel insurance to the MCAS. Working Group Chair Commissioner John Haworth of Washington told the committee that part of the issue was that a model law was still in the process of being drafted. That meant that travel insurance was still being defined and was the subject of ongoing deliberation.

New York Superintendent Maria Vullo made a motion to include travel insurance as a line of business on the MCAS. Committee Chair Commissioner Allen Kerr of Arkansas said that would set a bad precedent, and he would prefer to send the issue back to the working group for deliberations.

With the working group close to creating a new model, the motion was modified to ask the working group to provide a summary of its deliberations and conclusion to the committee.

Birnbaum also asked the committee to release data collected for the Auto Insurance (C/D) Study Group's auto study to the public. He said this data was aggregated and there was no confidentiality issue. The chair declined to act on Birnbaum's request.

Photo courtesy of the NAIC

Reinsurance Task Force adapts to Covered Agreement

The Reinsurance (E) Task Force focused mainly on the effect of the US-EU Covered Agreement and next steps to be taken after the February 2018 public hearing on the agreement. Among other measures, the task force submitted a memorandum to the E Committee for a model law request and for several new charges.

Many parties recommended amendments to the credit for reinsurance models to allow for the same treatment for EU and non-EU qualified jurisdictions. The proposed model law would reflect this approach. Proposed additional charges to the Capital Adequacy Task force included a directive to review and possibly modify the life and health RBC formulas specific to reinsurance credit risk charges based on the financial strength of the reinsurer, consistent with the P-C RBC formula. The hope was that a draft would be available for the summer meeting with possible adoption by the fall meeting.

The task force also received a report on the status of the Revised Credit for Reinsurance Model Law (#785), the Revised Credit for Reinsurance Model Regulation (#786), and the Term and Universal Life Insurance Reserve Financing Model Regulation (#787). So far, 43 states passed the original models and 36 states have amended them based on 2011 changes.

Among the reports adopted by the task force were those of the Qualified Jurisdiction (E) Working Group and the Reinsurance Financial Analysis (E) Working Group (REFAWG). The first noted that it had received another request from an EU member state to be considered a qualified jurisdiction, and that the working group will need to reevaluate the status of qualified jurisdictions shortly. They were qualified in 2015 and qualifications last for five years.

REFAWG noted that it currently monitored 26 reinsurers, but that number could expand dramatically. It will consider changes in its current methods of monitoring certified reinsurers.

Groups call for actuarially justified LTC product pricing

Representatives of AHIP and the ACLI called on regulators at the Long-Term Care Insurance (B/E) Task Force to provide actuarially justified increases for long-term care (LTC) products so companies can stay financially healthy. This has been a troubled marketplace, with concerns over the status of some blocks of business.

LTC was developed and offered with the assumption that if experience developed adversely, rate increases would be approved, the representatives said, adding that LTC rate increases should be approved based on the actuarial analysis and not linked to an insurer's overall corporate health.

There has been inconsistent application of the above foundations across the states, they charged, and that had negative consequences for the industry. If a company is basically subsidizing across their lines of business, it weakens the company's overall financial health. They called for regulators and actuaries to work together to propose common tenets to apply to the LTC rate increase process nationally.

Utah suggested it had an idea on how states might be able to coordinate rate increases. There may be a conference call in the near future to review that proposal.

The task force also considered if its charge to "rigorously assess the financial solvency of LTC Insurance" had been completed. Consumer representative Birny Birnbaum said that based on recent news from one company needing to add significantly to reserves and speculation that it may be the tip of the iceberg, the task force could not say the charge had been completed.

The task force disagreed, voting to close the charge and noting that closing a charge does not mean they are finished with the subject.

Photo courtesy of the NAIC

In brief

RBC, reinsurance changes

The effects of tax law changes on RBC are being evaluated, and RBC changes are expected in response. However, the revised RBC may not be ready until 2019, Financial Condition (E) Committee Chair Florida Commissioner David Altmaier told his committee. The committee also set in process various measures required to align NAIC requirements with the Covered Agreement and extend Covered Agreement privileges to insurers from jurisdictions deemed qualified by the NAIC. These included asking the Executive Committee to open up the model law, determining if Schedule F needs to be revised, creating new charges for various groups and subgroups, and reaching out to qualified jurisdictions to determine their interest and willingness to conform to NAIC requirements.

Form F Implementation Guide gets the OK

Concerns about the proposed Form F Implementation Guide and the Form F/ ORSA Comparison Memorandum were the major discussion issue at the meeting of the Group Solvency Issues (E) Working Group. An ACLI representative suggested that the guidance examples be withdrawn and also said there was an issue with trade secret protections. The representative suggested a company should be able to use its 10K filing to fulfill the Form F requirements and thus avoid possible disclosure of trade secrets. A regulator responded that the implementation guide was simply guidance, and that no changes had been recommended in the guide. The working group chair added that if a company believes the 10K referenced everything required for disclosure, it could simply say that. The Form F implementation guide was adopted unanimously.

Health MCAS additions set for fall agenda

No comments have been received on the Market Analysis Review System (MARS) merger drafting document since the last call held by the Market Analysis Procedures (D) Working Group, but there were suggestions from consumer representative Birny Birnbaum to modify the Draft 2018 Lender-Placed Auto and Home MCAS Scorecard Ratios. The working group will attempt to incorporate the suggestions into a draft. Discussions were delayed on the addition of draft health questions to the MCAS in order to allow for more time to review. Any additions will be on the fall agenda for adoption.

One terrorism data call

Terrorism Insurance Implementation (C) Working Group Chair Martha Lees of New York told the working group that there would be a single main data call for terrorism risk insurance this year. Lees noted that the states had been working closely with the US Department of the Treasury's Federal Insurance Office (FIO) on that data call, and that the data would be due on May 18. FIO will hold webinars prior to the due date. State regulators will still need some additional information by the end of September.

One place to report data breaches?

Regulators and industry expressed strong support for the creation of a centralized online reporting tool for data breaches at the meeting of the Innovation and Technology (EX) Task Force. Rhode Island Insurance Superintendent Elizabeth Kelleher Dwyer raised the issue and will follow up with the NAIC.

Photo courtesy of the NAIC

Health care update

The Health Insurance and Managed Care (B) Committee and its task forces and working groups are working to respond to health care developments and plan for the future. This includes being well-informed and hearing from both industry and states as to how each is responding and working proactively with the federal Center for Consumer Information and Insurance Oversight (CCIIO).

The pharmaceutical industry continued to be the highlight of the B Committee meeting and in particular—cost. There were presentations from representatives of the Pharmaceutical Research and Manufacturers of America, the Pharmaceutical Care Management Association and states (Arkansas, California, and New Hampshire) focusing on cost drivers.

The states focused on their efforts to control costs and improve transparency, such as California's medical price and quality transparency website (www.californiahealthcarecompare.org) and New Hampshire's HealthCost website (https://nhhealthcost.nh.gov).

The pharmaceutical benefit managers (PBMs) sector of the industry was of specific focus—regulators asked probing questions to understand cost trends to consumers. Certain states, such as Arkansas, have representatives who have recently enacted legislation establishing licensing and other requirements for PBMs. Regulators discussed how regulation of PBMs could impact costs and protect consumers.

Two other health care topics at the spring meeting were health care risk-based capital (RBC) and long-term care insurance. The Health RBC Working Group had a full agenda, focused on incorporating changes in the industry into the model—from the ACA provisions to Medicaid pass-through payments, which have increased in number and significance. The Senior Issues Task Force exposed for public comment the new Limited Long-Term Care Insurance Model Act.

It was clear that the efforts of regulators related to the pharmaceutical industry is something that will continue to be on the agenda for meetings to come. Regulator viewpoints and state regulatory actions will be something for all industry sectors, including PBMs, to be watching as the year unfolds.

This summary was prepared by Lynn Friedrichs. For comments or suggestions, you may contact her at lfriedrichs@deloitte.com

Photo courtesy of the NAIC

Actuarial update

Variable Annuities Issues (E) Working Group & C-3 Phase II/AG43 (E/A) Subgroup

At its December 2017 meeting, the Variable Annuities Issues (E) Working Group exposed for comment recommended changes to Actuarial Guideline 43 (AG43) and C-3 Phase II. There were 28 specific recommended changes, grouped into changes to: CTE Amount, Standard Scenario Amount, C-3 Charge, Disclosure Requirements, and Other Topics. The exposure period ran until March 2, 2018. Comments were received from five organizations, including the AG43/C3P2 Workgroup of the American Academy of Actuaries and the ACLI. The Variable Annuities Issues (E) Working Group and the C-3 Phase II/AG43 (E/A) Subgroup held a joint one-day meeting to discuss the comments received on the exposure materials.

The recommendations and the associated comments were discussed individually, with spirited debate among regulators, the consultants supporting the NAIC in its effort to revise AG43/C-3 Phase II, commenters, and other interested parties. The first group of recommendations addressed were those related to the CTE Amount, items 1–10 in the recommended changes exposed in December.

Remove the Working Reserve when calculating scenario GPVAD

In general, the commenters were in favor of this recommendation. There was support for the effect of removing noneconomic volatility from the reserve calculation.

Discount deficiencies at the Net Asset Earned Rate on Additional Assets

There was some discussion as to the intent, and how the discount rate would relate to the method of choosing the starting assets. It was clarified that the intent was that the discount rate for deficiencies would be based on the earned rate on additional assets available. If a company chose a pro-rata asset allocation for starting assets, then there may be sufficient additional assets available at the same net yield. On the other hand, if a company chose specific assets to allocate to the starting portfolio, the discount rate for deficiencies would be based on other assets available on the balance sheet. Finally, if no additional assets were available, the discount rate would assume cash at the beginning of the projection is then invested based on the modeled reinvestment strategy.

It was suggested that additional disclosures should be added to make it clear how the company is determining the discount rate, as well as support for a change in methodology.

Follow VM-20 guidance on general account asset projections, with additional constraints on borrowing cost

There was discussion around the amount of conservatism in the requirements, but it was decided that convergence with VM-20 makes sense and that the recommendation would be accepted. The issue of conservatism and the borrowing costs may be taken up at LATF in the future.

Permit immediate liquidation of currently held hedges and non-reflection of mark-to-market hedge gains and losses

One topic discussed was the question of whether a reserve framework should allow only a reduction in reserves for hedges. Many companies hedge economic risks, which often don't align with a statutory reserve framework. In rising equity markets, there may be a cost to the hedge program but no hedge gains, resulting in an increase in reserves. Some commenters observed that this recommendation might allow companies to omit hedges in the calculation when they result in a higher reserve.

Several issues were raised on the requirement of the use of a Clearly Defined Hedging Strategy (CDHS) when hedging is used in the reserve calculations:

- Does having a CDHS in place obligate a company to reflect hedges in the reserve calculation?
- Are some companies getting around increased reserves by simply failing to meet one of the criteria of a CDHS (such as designating one or more specific individuals as responsible for implementing the hedging strategy)?
- Should a company be permitted to switch between including and excluding hedges in the reserve calculation if the hedging strategy has not materially changed?

The current recommendation is that a company is not required to make a determination that a hedge program is a CDHS. It was suggested that the language be updated to make it clear that the recommendation is that liquidation is available in CTE Amount (adjusted) but not allowed in CTE Amount (best efforts).

Reduce minimum allowable CDHS "error factor," but require back-testing disclosure to support chosen "error factor"

The recommendation would allow the E-factor to be as low as 5 percent subject to back-testing of modeled hedge results against actual hedge strategy performance. This would apply to explicit as well as implicit modeling of dynamic hedge strategies. The ACLI expressed concern that a company making minor adjustments to its hedge strategy may then not have 12 months of history and would, therefore, be subject to a higher adjustment. The AAA Workgroup raised the question of whether the requirements of AG43 allow the "implicit" and "reinsurance cost" methods in the recommendation. In response, the NAIC consultant stated that the implicit methods are favored where appropriate, as they are simpler for both the company to model and the regulators to understand. Implicit modeling will require disclosures supporting reflection of the actual program and its cost.

The AAA Workgroup will draft language around the requirements of implicit methods, and the regulators will consider the use of implicit methods, as well as the proposed language.

Use VM-20 scenario generator for interest rate scenarios
The AAA Workgroup is in agreement with this recommendation as long as companies have the right to use proprietary generators that meet the minimum requirements, and the regulators were generally in agreement with this recommendation.

Use VM-20 scenario generator for separate account returns, but recalibrated based on data from 1926 to 2016
The consensus, though not unanimous, was to maintain the current generator and calibration period, while continuing to study through the ESG group.

Allow companies to use proprietary scenario generators if—and only if—they do not reduce the Total Asset Requirement
AG 43 and C-3 Phase II currently allow the use of proprietary generators, while VM-20 requires use of a prescribed generator. This recommendation would allow companies to continue use of a proprietary generator if it can be demonstrated that the Total Asset Requirement is not reduced due to the use of the proprietary generator.

The AAA WG commented that the use of a proprietary generator should be based on the merits of that generator, rather than the impact on the Total Asset Requirement. The requirement that a proprietary generator may only be used if the Total Asset Requirement is not reduced may incent companies to use a standard generator, even though a proprietary generator may be more consistent with a company's risk management practices.

The regulators were generally in favor of allowing use of proprietary scenario generators (not unanimously), though the standard may be changed to requiring that the TAR be "not materially reduced."

Differentiate treatment of non-guaranteed revenue sharing income by affiliated funds vs. non-affiliated funds
Several suggestions were presented, but in the end no decision was made, and the topic will be taken up on a future call.

Align AG43 Standard Scenario calculations with CTE ("adjusted")
Following the discussion, the options for consideration were summarized as:

- Maintain a Standard Scenario as a floor
- Move the Standard Scenario to a disclosure item
- Create a list of scenarios for analysis
- Require sensitivity tests on key variables
- Take an approach similar to VM-20 and identify all key risks, create sensitivity tests that are used to derive a margin used in the stochastic runs that determine the CTE

The regulators will regroup with their own offices on the topic of the Standard Scenario and continue to move the issue forward in the near future to address in future calls and meetings.

Life Actuarial Task Force (LATF)

VM-22 Subgroup

Work continues on developing VM-22 reserve requirements for non-variable annuities. The current direction is that there will be some sort of exclusion test. If a product passes the test, AG33 methodology will continue to be used; otherwise, there will be a stochastic modeling approach. A summary is expected by the next meeting.

The AAA Standard Valuation Interest Rate Group is working on methodology for determining valuation interest rates for non-variable annuities (other than immediate annuities, for which the new VM-22 requirement was effective January 1, 2018). The products in scope are more complex than SPIAs, with interest rate guarantee periods, free withdrawal options, and market value adjustments. These features may have different adjustments to the valuation interest rates. The group is currently looking at a single rate, locked-in at issue, with rates updated quarterly. Rising, level, and falling interest rate scenarios are being considered. Updates will be provided at future meetings.

A redraft of VM-22 for SPIA interest rates was presented. After VM-22 went into effect January 1, 2018, for valuation interest rates for immediate annuities, the group received many questions, and it was apparent that clarification was needed in some areas. The proposed updates and clarifications address five key topics:

- The scope was expanded to include all products that were initially intended.
- "Premium Determination Date" was redefined
  - The previous language did not work well for all products that were in scope, such as when account value runs out.
  - The update now presents a set of decision rules.
- In "Premium Determination Date," there is reference to domestic commissioner approval
  - Intent has been expanded
  - Exemption from VM-22 is allowed for certain benefit streams and situations
- Concern with the definition of "Reference Period"
  - There was potential for manipulation by placing a non-life contingent payment far out in the future to obtain higher reference date.
  - The definition has been clarified to avoid this possibility.

Since the decision was made to publish rates, the guidance is now directed at how to select the rate rather than how to calculate the rate, but some parts were expanded for companies who want to calculate the rates themselves.

The group voted to expose for comment the updates to VM-22, "Statutory Maximum Valuation Interest Rates for Income Annuities," for 30 days.

Guaranteed Issue and Simplified Issue Mortality

Analysis of model results based on 11 companies' Guaranteed Issue mortality experience was presented, as a basis for a new Guaranteed Issue statutory mortality table. There is some urgency in this proposal, as companies will otherwise use 2017 CSO for GI business, which may not be appropriate. The group voted to expose for comment the GI loaded mortality tables for a period of 30 days.

For Simplified Issue mortality, the work to date that has been previously presented has been based on experience from 2005 to 2009. There have been significant changes in the market since that time, such as increasing face amounts. Also, prior studies did not include final expense, COLI/BOLI, and some group business. The group will schedule a call in the future to talk with LATF about how to proceed.

Accelerated Underwriting

LATF has exposed for comment the AAA VM-20 Accelerated Underwriting Question & Commentary document, regarding application of VM-20 mortality to business issued under an Accelerated Underwriting program. Also, there is currently underway a Delphi study focused on underwriting methodologies and their impact on mortality experience. Results are expected from the researcher by the end of May, and will be brought to LATF at the August meeting. The group will come back to LATF with a revised recommendation, either on a call or at the August meeting.

Valuation Manual Adjustments

Edits to VM-50, "Experience Reporting Requirements," and VM-51, "Experience Reporting Statistical Plans" were voted to be exposed for comment for 30 days. These edits include structural as well as content changes based on comments received. It is anticipated that this will go into effect January 1, 2020.

Amendment Proposal Form (APF) 2017-94 to revise VM-31

- Clarify the scope of VM-31, "PBR Actuarial Report Requirements for Business Subject to Principles-Based Valuation," to include VM-21 and VM-20 exclusion tests only
- Reword for consistency with VM-20
- Other minor edits
- The group voted to expose the edits for comment

APF 2017-89 to revise VM-20

The group voted to adopt these changes:

- Non-substantive, clarifying changes to VM-20 Sections 3.B.4.c and 6.B.5.e
- Language will be changed to clarify that gross premium includes any policy fee

APF 2017-66 Revision, to revise VM-26, "Credit Life and Disability Reserve Requirements"

- Changes will allow gender and smoker distinct mortality tables for certain credit life and disability products that are priced based on gender and smoking status.
- The proposal will be addressed on an LATF call later this year.

APF on Morality Credibility to revise VM-20

This APF addresses the degree to which mortality segments can be aggregated to determine credibility of a company's experience.

- For segments for which mortality was based on aggregate experience and then subdivided into segments
  - If all mortality segments to be aggregated were subject to the same or similar underwriting process.
  - If the segments were sold by similar distribution systems and in similar market segments.

Additional edits will be made based on the live discussion, and the group voted to expose for comment the edited APF for a period of 45 days.

Two additional topics for APFs were discussed:

- Indexed UL under PBR
  - The 2 percent growth rate proposed for the deterministic reserve was intended for variable products where returns could be positive or negative.
  - The Life Reserves Work Group presented analysis demonstrating that the 2 percent growth rate is not appropriate for Indexed UL.
  - The group will draft a specific proposal and APF for discussion in the future.
- APF 2018-02
  - This is a change to VM-01 proposed by the Role of the Actuary Subgroup of the PBR Governance Work Group of the AAA.
  - VM-20 contains definitions for "qualified actuary" and "actuarial opinion" that, together, might be interpreted to mean that, in order to carry out responsibilities assigned to a "qualified actuary" in the Valuation Manual, an actuary must meet the AAA qualification standards for signing the opinion of the appointed actuary regarding the adequacy of reserves and related actuarial items.
  - This APF proposes deleting the definition of "actuarial opinion" and adding definitions for "actuarial services" and "statement of actuarial opinion".
  - Following the comments and discussion, the group will go back and continue to work on the proposal.

Model 805 Drafting – Update
The group was charged with drafting a preliminary version of a new actuarial guideline to address application of Section 6 of the model 805 (usually referred to as the "Prospective Test") to the variety of the product features that were not contemplated at the time the deferred annuity Standard Nonforfeiture Law was drafted. The model law addresses Cash Surrender Value benefits payable at surrender, which reflect actual contract performance from the time of issue to the time of surrender, as well as future guarantees (for the period from surrender to the maturity date). Items addressed in the guideline include: maturity date and the issue of optional maturity dates, maturity value, and the treatment of bonuses. The group voted to expose the draft actuarial guideline for comment for a period of 60 days.

C-3 Phase II/AG 43 (E/A) Subgroup
Recommended changes to AG43 and C-3 Phase II were exposed for comment in December. Highlights from the meeting included the following topics:

- After discussion, the decision was made to maintain the current equity calibration criteria.
- No decision was made on revenue sharing.
- Standard scenario as either a disclosure or still as a specific floor—there are still differences of opinion on this topic.

This Subgroup is not making a determination or decision on a framework and, therefore, doesn't expect to have any calls to discuss those items until the work on the framework is complete and decisions are made.

VM-20 Supplement Edits submitted to the Blanks (E) Working Group
There are some edits that have been proposed to the VM-20 Reserves Supplement. These include:

- Update to Part 3 to reflect amendments made to the Valuation Manual (replacing "companywide exemption" with "Life PBR Exemption")
- A new supplement, Part 4, for reporting of other exclusions from Life PBR
- Instructions for the VM-20 Reserve Supplement to be updated for the new Part 4
- Exhibit 5 instructions need to be updated to reflect reporting of valuation bases for annuity contracts subject to VM-22

The proposed changes will be exposed for comment at a future date.

This summary was prepared by David Armstrong. He may be reached at daarmstrong@deloitte.com.

Photo courtesy of the NAIC

Accounting update

This section of the NAIC Update focuses on accounting and reporting changes discussed, adopted, and exposed by the Statutory Accounting Principles (E) Working Group, the Accounting Practices and Procedures (E) Task Force, and the Financial Condition (E) Committee during the 2018 Spring Meeting and interim conference calls. Substantive changes finalized during these meetings have explicit effective dates as documented below. All nonsubstantive changes finalized during these meetings are effective upon adoption unless otherwise noted.

Statutory Accounting Principles Working Group

Current developments:
The SAPWG did not adopt any **substantive** items as final during the 2018 Spring Meeting and interim conference call held February 8, 2018. The SAPWG adopted the following **nonsubstantive** items as final during the 2018 Spring Meeting and interim conference call held February 8, 2018:

Ref#	Title	Sec.	Amendments adopted	F/S impact	Disclosure	Effect. date
2017-21	SSAP No. 41R—Surplus Notes SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities	P&C Life Health	Revisions clarify that surplus notes issued and held (directly or indirectly) between insurance reporting entities and subsidiary, controlled, and affiliated entities (SCAs) requires adjustment to prevent double-counting of surplus notes as reflected by the following: • For any SCA that has issued a surplus note, which has been acquired by the parent reporting entity, the parent reporting entity must eliminate the value of the surplus note from the total equity investment in the SCA. [current guidance] • Any parent reporting entity that has issued a surplus note, which has been acquired by an SCA (held directly or indirectly) must adjust the investment in the SCA to eliminate the issued surplus note to prevent double-counting of the surplus note at the parent reporting entity. – The surplus note shall also be eliminated for instances in which the SCA acquires any portion of outstanding surplus notes issued by the parent through any means (e.g., directly acquired from the parent, acquired through a third-party broker, or via the market).	Y	N	2018
2017-37 2016-19	SSAP No. 47—Uninsured Plans	P&C Life Health	Revisions reject US-GAAP related to revenue recognition included in the following: • *ASU No. 2014-09, Revenue from Contracts with Customers;* • *ASU 2015-14, Revenue from Contracts with Customers, Deferral of the Effective Date;* • *ASU 2016-08, Revenue from Contracts with Customers, Principal versus Agent Considerations;* • *ASU No. 2016-10, Revenue from Contracts with Customers, Identifying Performance Obligations and Licensing; and* • *ASU No. 2016-12, Revenue from Contracts with Customers, Narrow-Scope Improvements and Practical Expedients.*	N	N	NA
2017-18	SSAP No. 68—Business Combinations and Goodwill	P&C Life Health	Revisions require additional disclosure to identify the amount of admitted goodwill and the percentage of admitted goodwill to total equity (including admitted goodwill) in the subsidiary, controlled, or affiliated entity.	N	Y	2018

Ref#	Title	Sec.	Amendments adopted	F/S impact	Disclosure	Effect. date
2016-48	SSAP No. 86—Derivatives	P&C Life Health	Some insurance companies enter into purchased options whereby the premiums under the contracts are scheduled in the future and paid at multiple points throughout the term of the contracts or at expiration.	N	Y	2018
2017-30	SSAP No. 92—Postretirement Benefits Other Than Pensions SSAP No. 102—Pensions	P&C Life Health	Revisions remove the disclosure requirement to reconcile level 3 fair value information for plan assets.	N	Y	2018
2017-31	SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities	P&C Life Health	Revised the wash sale disclosure requirements, as follows: • Exclude all cash equivalents, derivative instruments, as well as short-term investments with credit assessments equivalent to an NAIC 1-2 designation from the wash sale disclosure; and • Clarifies that the disclosure is included in the financial statements in the period the investment is initially sold.	N	Y	2018
2017-36	Appendix B—Interpretations of Statutory Accounting Principles: INT 02-22—Accounting for the U.S. Terrorism Risk Insurance Program Appendix H—Superseded SSAPs and Nullified Interpretations—INT 09-08—Accounting for Loans Received under the Federal TALF Program	P&C Life Health	Revisions update the interpretation to remove the expiration date and note that the interpretation is in effect as long as the federal Terrorism Risk Insurance Act (TRIA) program is in effect. In addition, the revision updates and nullifies INT 09-08, as there are no longer any loans outstanding under the Federal Reserve's Term Asset-Backed Securities Loan Facility program.	Y	N	2018
2017-03	Appendix D – GAAP Cross-Reference to SAP	P&C Life Health	Revisions reject *ASU 2017-06: Defined Benefit Pension Plans, Defined Contribution Pension Plans and Health and Welfare Benefit Plans – Master Trust Reporting*, as not applicable to statutory accounting.	N	N	NA
2018-02	Appendix B—Interpretations of Statutory Accounting Principles: INT 18-01: Updated Tax Estimates under the Tax Cuts and Jobs Act	P&C Life Health	In February of this year, an interpretation of SSAP No. 101 was adopted that provided guidance on the following items: **Issue 1:** Reporting and updating estimates. Addresses accounting for analysis that is complete, incomplete, and changes to estimates before and after the annual statement filing deadline. If estimates change after the filing deadline, this shall not reflect the changes as a type 1, subsequent event but reflect as a change in estimate with applicable disclosure. **Issue 2:** Reporting changes to deferred tax assets and liabilities. Clarifies that existing reporting instructions should be applied. **Issue 3:** Completion of Note 9c. Clarifies reporting requirements for the Table.	Y	Y	2017

The SAPWG exposed the following items for written comments (due by May 18, 2018, unless otherwise noted) by interested parties:

Ref#	Title	Sec.	Amendments exposed	F/S impact	Disclosure	Effect. date
2017-33	SSAP No. 86—Derivatives	P&C Life Health	**Substantive** – Exposed an issue paper to consider that statutory response for *ASU 2017-12, Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities*. The issue paper considers whether there is a reason to differ from US GAAP and whether current inconsistencies will be continued. Comment period ending: June 22, 2018	TBD	TBD	TBD
2016-03	New SSAP and Issue Paper	P&C Life Health	**Substantive** – This item relates to the work performed by the Variable Annuity Issues (E) Working Group and the charge from that group to the SAPWG to consider "hedge accounting treatment" for certain limited derivatives (macro hedges) that do not meet hedge effectiveness requirements related to variable annuity products and associated guarantees. Exposed an issue paper to allow special accounting treatment for limited derivatives hedging variable annuity guarantee benefits subject to fluctuations as a result of interest rate sensitivity.	Y	Y	TBD
2016-20	Various SSAPs	P&C Life Health	**Substantive** – Exposed a concept paper considering adoption of the US GAAP guidance included in *ASU 2016-13: Credit Losses.* • Considers replacing the "incurred loss model" with an "expected credit loss" concept. • It should be noted that other statutory elements already consider credit risk (e.g., Risk-Based Capital and the Asset Valuation Reserve).	TBD	TBD	TBD
2018-05	SASP No. 1—Accounting Policies, Risks & Uncertainties, and Other Disclosures; SSAP No. 32—Preferred Stock	P&C Life Health	**Nonsubstantive** – Exposed revisions to incorporate modifications to reporting requirements adopted by the Valuation of Securities (E) Task Force and currently exposed by the Blanks (E) Working Group related to NAIC designations and other reporting symbols.	N	N	TBD
2018-06	SSAP No. 4— Assets and Nonadmitted Assets	P&C Life Health	**Nonsubstantive** – Exposed revisions that propose items acquired as part of "regulatory transactions," as defined in the *Purposes and Procedures Manual of the Investment Analysis Office* that meet the definition of an asset: • Shall only be admitted with approval of the domestic state insurance department as a prescribed or permitted practice; and • Such items will also be identified in the investment schedules with the symbol (RT).	Y	N	TBD
2018-04	SSAP No. 26R—Bonds	P&C Life Health	**Nonsubstantive** – Exposed proposed response to the Valuation of Securities (E) Task Force on its draft guidance for bank loans. This response suggests revisions to indicate that investments shall follow the guidance in the Accounting Practices and Procedures Manual (AP&P Manual), which would classify borrowing base loans and debtor in possession (DIP) financings as collateral loans.	TBD	TBD	TBD

Ref#	Title	Sec.	Amendments exposed	F/S impact	Disclosure	Effect. date
2018-12	SSAP No. 26R—Bonds; SSAP No. 30—Unaffiliated Common Stock; SSAP No. 32—Preferred Stock; SSAP No. 43R—Loan-Backed and Structured Securities; and SSAP No. 100R—Fair Value	P&C Life Health	**Nonsubstantive** – Exposed proposed rejection of *ASU 2018-03, Recognition and Measurement of Financial Assets and Financial Liabilities,* which relates to technical corrections within the guidance.	NA	NA	NA
2018-07	SSAP No. 41R—Surplus Notes	P&C Life Health	**Nonsubstantive** – Exposed revisions to clarify: • Surplus notes linked to other structures are not subordinate and do not qualify for reporting as statutory equity by the issuer. • Assets linked to issued surplus notes are not available for policyholder claims and shall be nonadmitted.	Y	TBD	TBD
2018-03	SSAP No. 43R—Loan-Backed and Structured Securities	P&C Life Health	**Nonsubstantive** – Exposed revisions to clarify that if a loan-backed or structured security has different NAIC designations by lot, then • The reporting entity shall either report the entire investment on a single reporting line with the lowest applicable NAIC designation; or • Report separately by purchase lot.	TBD	TBD	TBD
2017-35	SSAP No. 49—Policy Loans	P&C Life Health	**Nonsubstantive** – Exposed revisions to require that all policy loans related to separate account policies shall be "funded" in order to be admitted. In addition, the exposure contemplates suggesting removal of the "contract loan" line from the Separate Account blank.	TBD	TBD	TBD
2018-08	SSAP No. 56—Separate Accounts	Life	**Nonsubstantive** – Exposed proposed revisions to capture information on the insurer issuance of private placement life insurance and private placement variable annuities. The working group intends for this disclosure to be effective for year-end 2018. The exposure also requests comments from industry on characteristics differentiating private placement products that are investment-focused and the traditional life products intended to be captured under *SSAP No. 21—Other Admitted Assets* when the insurer holds the product as owner and beneficiary.	TBD	Y	2018
2018-09	SSAP No. 97—Subsidiary, Controlled and Affiliated Entities	P&C Life Health	**Nonsubstantive** – Exposed revisions to clarify guidance when a company's share of losses exceeds its investment and adds a loss-tracking disclosure. The working group intends for this disclosure to be effective for year-end 2018.	TBD	Y	2018

Ref#	Title	Sec.	Amendments exposed	F/S impact	Disclosure	Effect. date
2018-01	SSAP No. 101—Income Taxes	P&C Life Health	**Nonsubstantive** – Exposed revisions proposing edits related to the federal Tax Cuts and Jobs Act. • Reflect guidance from adopted interpretation that addressed how the impact of reform should be reported. See description of interpretation noted in nonsubstantive adoptions (Ref #2018-02). • Clarifies differences in carry-back provisions between life and non-life entities. • Requests comments regarding scheduling requirements and known reversal patterns. • Updates the implementation guide to reflect impact of changes resulting from tax reform. Comment period ended: April 23, 2018.	TBD	TBD	TBD
2018-10	INT 18-02—ACA Section 9010 Assessment Moratoriums	Health	**Nonsubstantive** – Exposed revisions to provide guidance for the 2019 moratorium and future moratoriums for the federal Affordable Care Act (ACA) Section 9010 fee. In addition, the proposal removes the reference to 2019 fee accruals payable from INT 16-01—ACA Section 9010 Assessment 2017 Moratorium and proposes Dec. 31 nullification of INT 16-01.	TBD	TBD	TBD
2018-14	INT 05-05: Accounting for Revenues under Medicare Part D Coverage	Health	**Nonsubstantive** – Exposed revisions to add a description of the Coverage Gap Discount Program, amend existing guidance on program payments, and update definitions	TBD	TBD	TBD
2018-11	Appendix D – GAAP Cross-Reference to SAP	P&C Life Health	**Nonsubstantive** – Exposed revisions to reject *ASU 2017-15, U.S. Steamship Entities, Elimination of Topic 995*, as not applicable to statutory accounting.	NA	NA	NA

The SAPWG also took the following actions, received updates, and provided direction to NAIC staff on the following items:

Ref#	Title	Sec.	Description	F/S impact	Disclosure	Effect. date
2016-02	SSAP No. 22—Leases	P&C Life Health	**Nonsubstantive** – Received an update on the review of the proposed guidance for leases in accordance with the industry comments to determine further revisions for consideration. The existing modifications to US GAAP guidance in current statutory accounting (e.g., operating lease concept) continue to be retained. Updated materials will be presented for exposure consideration at the 2018 Summer National Meeting.	TBD	TBD	TBD
2017-32	SSAP No. 30—Unaffiliated Common Stock	P&C Life Health	**Substantive** – Directed the drafting of an issue paper proposing substantive revisions to: 1) improve the common stock definition; 2) include closed-end funds and unit-investment trusts within scope; and 3) incorporate enhancements to capture NAIC designations on Schedule D-2-2—Common Stocks.	Y	N	TBD
2017-12	SSAP No. 41R—Surplus Notes	P&C Life Health	**Substantive** – Directed continued development of guidance related to the issuance of a surplus note at a discount or zero coupon to consider comments received.	TBD	TBD	TBD
2017-28	SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance SSAP No. 62R—Property and Casualty Reinsurance Appendix A-791—Life and Health Reinsurance Agreements	P&C Life Health	**Substantive** – This item relates to regulator concerns for reinsurance contracts that include risk-limiting features related to short-duration contracts and the appropriate amount of reinsurance reserve credit that should be taken by ceding entities. The working group directed continued work with industry representatives, with informal drafting calls, to refine the proposed guidance for future consideration. It is expected to incorporate US GAAP language related to this issue.	TBD	TBD	TBD
2017-12	SSAP No. 41R—Surplus Notes	P&C Life Health	**Substantive** – Directed continued development of guidance related to the issuance of a surplus note at a discount or zero coupon to consider comments received.	TBD	TBD	TBD

This summary was prepared by John Tittle, Lynn Friedrichs, Diane Craanen, and Ed Wilkins. For your comments and suggestions, please contact the authors – johntittle@deloitte.com, lfriedrichs@deloitte.com, dcraanen@deloitte.com, or ewilkins@deloitte.com.

Contacts

Gary Shaw
Vice Chairman
US Insurance Leader
Deloitte LLP
+1 973 602 6659
gashaw@deloitte.com

Howard Mills
Managing Director
Global Insurance
Regulatory Leader
Deloitte Services LP
+1 212 436 6752
howmills@deloitte.com

Richard Godfrey
Principal
US Insurance Risk & Financial
Advisory Leader
Deloitte & Touche LLP
+1 973 602 6270
rgodfrey@deloitte.com

Rick Sojkowski
Partner
Insurance Professional Practice
Director
Deloitte & Touche LLP
+1 860 725 3094
rsojkowski@deloitte.com

George Hanley
Managing Director
Deloitte & Touche LLP
+1 973 602 4928
ghanley@deloitte.com

Lynn Friedrichs
Partner
Deloitte & Touche LLP
+1 813 273 8342
lfriedrichs@deloitte.com

Contributors

Ed Wilkins
Partner
Deloitte & Touche LLP
+1 402 444 1810
ewilkins@deloitte.com

Bryan Berkowitz
Senior Manager
Deloitte & Touche LLP
+1 973 602 4578
bberkowitz@deloitte.com

Diane Craanen
Managing Director
Deloitte & Touche LLP
+1 312 486 3625
dcraanen@deloitte.com

John Tittle
Senior Manager
Deloitte & Touche LLP
+1 312 486 5486
johntittle@deloitte.com

David Armstrong
Senior Manager
Deloitte Consulting LLP
+1 804 343 8569
daarmstrong@deloitte.com

Senior editor

Andrew N. Mais
Senior Manager
Deloitte Center for Financial Services
Deloitte Services LP
+1 203 761 3649
amais@deloitte.com

Endnotes

[1] The Honorable Julie Mix McPeak, "Opening session: states marching ahead," National Association of Insurance Commissioners, March 25, 2018, http://www.naic.org/meetings1803/dn_opening_session.htm.

[2] Ibid.

[3] Ibid.

[4] Andrew N. Mais, Nikhil Gokhale, and Alexander LePore, Jr., "Insurance regulators in an era of advanced technologies: Challenges and opportunities in oversight," Deloitte Insights, February 2018.