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NAIC Meeting Notes

Global Insurance Industry Group, Americas

NAIC 2015 Spring National Meeting

The National Association of Insurance Commissioners held its Spring National Meeting in Phoenix March 28-31. This newsletter contains information on activities that occurred in some of the committees, task forces and working groups that met there, as well as summarizes conference calls before and shortly after the Spring National Meeting. For questions or comments concerning any of the items reported, please feel free to contact us at the address given on the last page.

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Executive Summary

- The Executive Committee and Plenary introduced 12 new commissioners and adopted revisions to several model regulations including AG 38.
- The Cybersecurity Task Force adopted twelve principles to guide the NAIC in its goal of protecting consumers and insurers from cyber attacks.
- The Financial Condition Committee formed a new working group to address issues related to variable annuity captive transactions and requested input on how to decrease permitted practices and increase consistency in the accounting for XXX/AXXX reinsurance transactions.
- The Statutory Accounting Principles Working Group adopted revisions to SSAP 69, Statement of Cash Flows, effective year-end 2015 and exposed for comment four documents as part of its Investment Classification Review project.
- The PBR Implementation Task Force adopted the 2015 XXX/AXXX Reinsurance Supplemental Proposal and the PBR Small Company Exemption Proposal.
- The Life RBC Working Group continued work on AG 48 RBC proposals and adopted two informational-only ACA tests for 2015 Life RBC filings.
- The Investment RBC Working Group outlined its priority topics for 2015, which include finalizing proposed corporate bond and real estate factors used in the Life RBC calculation.
- The Operational Risk Subgroup continued to make progress on the design and implementation of an operational risk charge by 2016; review of ORSA filings is expected to provide key insights into operational risk.
- The Property/Casualty RBC Working Group adopted the R3 reinsurance credit risk charge proposal on an informational-only basis, which reduces the reinsurance credit risk factor.
- The Catastrophe Risk Subgroup adopted three proposed changes to the 2015 informational-only catastrophe risk calculation, including the R6 and R7 contingent credit risk proposal and the catastrophe risk charge exemption proposal.
- The Health RBC Working Group adopted the investment affiliate risk proposal, which converts the calculation from a "look-through" treatment to a flat 30% RBC charge.
- The Valuation of Securities Task Force continued discussion of private letter ratings and the related Filing Exempt process, and referred the issue of catastrophe-linked bonds to the SAP Working Group.
- The Private Equity Working Group finalized its proposed revisions to the Financial Analysis Handbook to aid analysts in evaluating risks associated with a change in control of an insurer.
- The ComFrame Development and Analysis Working Group discussed the proposed IAIS global capital standard and its draft position papers on ComFrame and the Capital Standard. The working group hopes to have a revised U.S. Group Capital Methodology conceptual framework document before the Summer National Meeting.
- The Reinsurance Task Force heard updates on reinsurance modernization efforts and agreed with the recommendations of the Valuation of Securities Task Force related to qualified non-bank LOCs and which "SVO Listed Securities" should be acceptable collateral for reinsurance.
- The Unclaimed Life Insurance Benefits Working Group received approval to draft a model Unclaimed Life Insurance Benefits Act and appointed a subgroup to develop the model.
- The Life Actuarial Task Force discussed and later adopted a compromise proposal for an Actuarial Guideline for Indexed Universal Life policy illustrations. The task force also exposed the 2014 VBT Basic and Relative Risk Mortality Tables for comment. With respect to the Valuation Manual the task force exposed for comment a proposal for commercial mortgage assumptions and adopted the December 31, 2014 VM-20 spreads.
- The Emerging Actuarial Issues Working Group voted to re-expose an interpretation regarding the basis for determining the pre-funding ratio as defined in Section 8E of AG 38, and also exposed an alternative interpretation for the same issue.

- The Health Actuarial Task Force Long-Term Care Pricing Subgroup continued work on its draft *NAIC Guidance Manual for Rating Aspects of the Long-Term Care Insurance Model Regulation* to assist in implementation of changes to the *Long-Term Care Insurance Model Regulation* (#641) adopted in 2014.
- The Financial Regulation Standards and Accreditation Committee proposed narrowing the scope of its controversial "multi-state insurer" proposal to four specific types of entities.
- After several months of work, the Sharing Economy Working Group adopted its white paper *Transportation Network Company Insurance Principles for Legislators and Regulators* that provides guidance on insurance issues relative to TNC activities.
- The Casualty Actuarial and Statistical Task Force exposed its white paper on price optimization in rate filings; several states have recently required insurers to end this practice.
- The Risk-Focused Surveillance Working Group heard comments on proposed revisions to the Financial Condition Examiners Handbook and the Financial Analysis Handbook encouraging additional communication between the examiners and analysts.
- The Climate Change and Global Warming Working Group heard presentations from Munich Re on its climate strategy.
- As a result of the adoption by Congress of TRIA2015, the Terrorism Insurance Implementation Working Group updated its model bulletin describing reauthorization and filing procedures related to the Terrorism Risk Insurance Act.
- The Mortgage Guaranty Insurance Working Group discussed its February 2015 version of the proposed revised Mortgage Guaranty Insurance Model Act and the Wisconsin version of the Mortgage Guaranty Insurance Standards Manual. Industry requested additional time to comment.

Executive Committee and Plenary

Note: All documents referenced in this Newsletter can be found on the NAIC's website at naic.org.

New Commissioners

There were a lot of new faces in Phoenix at the Spring National Meeting; since the last National Meeting at least 12 commissioners have left office due to retirements, new jobs or changes in governors. High profile departures include former NAIC officers Sandy Praeger (KS), Michael Consedine (PA) and Thomas Leonardi (CT).

Final Adoptions

The Executive Committee and Plenary adopted the following items at the Spring National Meeting, which were the subject of public hearings and debate as they were considered by various groups of the NAIC:

- Adopted revisions to *Actuarial Guideline XXXVIII—The Application of the Valuation of Life Insurance Policies Model Regulation* (AG 38) related to the small company exemption
- Adopted amendments to the *Annuity Disclosure Model Regulation* (#245), the *Suitability in Annuity Transactions Model Regulation* (#275), the *Advertisement of Life Insurance and Annuities Model Regulation* (#570) and the *Life Insurance and Annuities Replacement Model Regulation* (#613)
- Adopted the *Transportation Network Company Insurance Principles for Legislators and Regulators* white paper drafted by the Sharing Economy Working Group
- Adopted the Compendium of Reports on the Pricing of Personal Automobile Insurance
- Adopted the model bulletin, policyholder disclosures and expedited SERFF filing document related to the federal Terrorism Risk Insurance Program Reauthorization Act of 2015
- Adopted the Health Reform Data Call and Definitions

- Adopted the *Model Risk Retention Act* (#705) as an additional Part A standard for accreditation purposes

Cybersecurity Task Force

Charges and Workplan
The Cybersecurity Task Force was created during the Fall National Meeting; the task force's charges include monitoring cybersecurity developments and coordinating activities among various NAIC committees regarding cybersecurity. At the Spring National Meeting, the chair discussed the task force's recent work, which includes creation of a cybersecurity supplement to the P/C Annual Statement, a survey of states to assess state insurance department "cyber vulnerabilities" to be distributed during the summer and developing a "Consumer Bill of Rights," outlining an insurer's role if a cybersecurity attack is suspected.

Anthem Data Breach
Representatives from Anthem presented an update on its data breach and remediation efforts to the task force. The company is working closely with the FBI investigation on how the attack occurred, which was expected to conclude in 30-60 days from the Spring National Meeting. It was noted the FBI monitors the "black market" for dissemination of information relating to the cyberattack, and nothing has been seen to date. They've been advised that typically such information would be sold to the black market within six to nine months of the breach. The breach at Anthem was described by the representatives as a sophisticated "advanced persistent threat," that disguised itself as users.

Anthem has also hired an outside firm with strengthening their data security, which is currently progressing five separate work streams surrounding cybersecurity. It has also completed its mailings to some 80 million policyholders, and an average of 5% of individuals signed up for the identity protection monitoring. To date, Anthem has not confirmed any claims by policyholders of fraud that is directly traced to the breach. When asked if they would have done anything differently, the representatives stated that they would have moved faster in elevating its level of cybersecurity.

Principles for Effective Cybersecurity Insurance Regulatory Guidance
Prior to its meeting in Phoenix, the task force exposed for comment a March 12 draft of eighteen proposed principles for effective cybersecurity, which had been derived from the Securities Industry and Financial Markets Association's "Principles for Effective Cybersecurity Regulatory Guidance." At the Spring National Meeting, the task force had a lengthy discussion of preliminary comments and extended the exposure until April 10; a total of 21 comment letters were received from insurers, trade associations, regulators, consumer representatives and security consultants. The task force then met via conference call on April 16, heard oral comments, and the principles were condensed down to 12.

During the call, interested parties were generally supportive of the task force's progress and efforts in drafting the principles and some additional edits were discussed. The task force concluded the call by adopting the 12 principles to guide the NAIC in its goal of protecting consumers and insurers from cyberattacks. Key aspects of the finalized cybersecurity principles include: securing personally identifiable information, consistent, risk-based regulatory guidance, cybersecurity knowledge sharing across the industry, and timely communication of cybersecurity breaches. The final document has been posted to the task force's webpage and is linked here Principles.

NYDFS Letter to Insurers on Cyber Securities
On March 26, the New York Department of Financial Services issued a letter to insurance company CEOs, CIOs and general counsels that the Department "intends to incorporate new questions and topics into the existing IT examination framework," including management of cyber security issues and resources devoted to information security and overall risk management. The letter directs insurers to respond in writing by April 27 to sixteen detailed questions on information technology and security processes, procedures and safeguards.

Property/Casualty Annual Statement
The Property and Casualty Insurance Committee drafted and exposed for comment during March a Cybersecurity Insurance Coverage Supplement. The committee received 8 comment letters from interested parties editing proposed terminology on the supplement, enhancing instruction on what should be included on the form and requests for more time to provide input.

Financial Condition Committee

In addition to receiving the reports of its various task forces and working groups, the committee discussed the following significant new projects at the Spring National Meeting.

Variable Annuities Issues Working Group
As Federal regulators continue to study the variable annuity market, the committee appointed a new group, the Variable Annuities Issues Working Group,

to "oversee the NAIC's efforts to study and address regulatory issues resulting from variable annuity captive reinsurance transactions." The working group will include members from nine lead states with variable annuity captives, and Iowa will chair. The Financial Analysis Working Group will collect information on cessions to variable annuity captives. The VA Issues Working Group will evaluate the use of captives for variable annuity products and is expected to make recommendations for changes to SSAPs, the Life RBC formula and reserving requirements, broadly developing a regulatory framework around variable annuity captives. A key issue is the hedge accounting requirements for derivatives purchased to manage the variable annuity risk.

Captive Reinsurance Transactions
The committee discussed at some length "how to address the dynamic of insurers asking for, and regulators approving, captive reinsurance transactions without the regulatory incentive first being directed to the E Committee." The chair, Superintendent Torti of RI, commented on the pervasiveness of "one-off issues" that receive permitted accounting practices relating to captive reinsurance transactions, and the difficulties created by "national issues being addressed by single state actions," including lack of transparency. He expressed his view that SAP may have to move closer to GAAP in the accounting for these types of transactions. Superintendent Torti also suggested that permitted practices at the ceding company level would be a better solution than permitted practices issued to captives. He then asked that regulators, trade associations and insurers provide feedback to identify issues that should be reviewed in terms of updating the solvency framework.

P/C Risk Transfer
During its December 12 conference call, the committee adopted a charge to "develop regulatory guidance on how to evaluate risk transfer as it pertains to contracts with risk limiting features and also evaluate how current actuarial/accounting practices used to monitor a company's financial strength need to be enhanced due to distortions from these contracts." To address this charge, the Risk-Limiting Contracts Working Group has been formed and will be chaired by Illinois; the working group expects to have its first meeting sometime in the second quarter.

Title Insurance Guaranty Fund Working Group
The committee adopted the working group's Title Insurance Consumer Protection Fund Guideline, which provides states with a mechanism for the continuation of coverage and payment of covered title insurance claims, in lieu of a title insurance guaranty fund.

Statutory Accounting Principles Working Group

The working group discussed the following projects at the Spring National Meeting.

(After each topic is a reference to the Statutory Accounting Principles Working Group's agenda item number.)

Adoption of Revisions to SSAPs

Statement of Cash Flows (2014-23) – After obtaining feedback from industry in 2014 that most insurance entities exclude non-cash transactions from the statement of cash flows, the working group proposed revisions to SSAP 69 to clarify that only items defined as cash, cash equivalents and short-term investments should be included in the cash flow statement. Disclosure of non-cash items affecting assets and liabilities will be expanded to include non-cash operating items in addition to financing and investing items. At the Spring National Meeting, the working group adopted the revisions with an effective date of year-end 2015. The working group also approved proposed revisions to the annual statement cash flow worksheets to be consistent with these changes, which were considered by the Blanks Task Force in Phoenix.

ASU 2014-15, *Presentation of Financial Statements-Going Concern* (2014-29) – The working group adopted proposed changes to SSAP 1 to include disclosure in the audited financial statements of the evaluation of substantial doubt of an entity's ability to continue as a going concern. The guidance would also amend SSAPs 48, 68 and 97 to nonadmit investments whose financial statements include "substantial doubt" going concern disclosures. The guidance is effective for year-end 2016 with early adoption permitted.

SSAP 11 Disclosures (ASU 2014-35) – The working group adopted revisions to SSAP 11 to delete disclosures that pertain to defined benefit and defined contribution plans from the postemployment benefits guidance, with a reference to complete the disclosures in SSAP 92 if the entity is providing special or contractual termination benefits.

ASU 2014-04 and ASU 2014-14, *Receivables, Troubled Debt Restructuring by Creditors* (2014-30) – The working group adopted the two ASUs with some modifications; the revisions provide guidance

on accounting and disclosures for foreclosed mortgage loans. The modifications to ASU 2104-04 broaden the scope to include all mortgage loan foreclosures and not just residential real estate with a consumer mortgage loan. The ASU 2014-04 guidance was modified to not allow a gain on foreclosure, which would require the real estate to be recorded at the lower of fair value or the outstanding mortgage loan balance. The new guidance will be effective prospectively (after March 28, 2015).

ASU 2014-16, *Derivatives and Hedging, Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share is More Akin to Debt or to Equity* (2014-37) The working group adopted a revision to SSAP 86 to reject ASU 2014-16 as not applicable to statutory accounting because SSAP 86 does not bifurcate an embedded derivative from the host contract.

Exposure of New Guidance and Discussion of New and On-going Projects

Comments on exposed items are due to NAIC staff by May 21 unless otherwise noted.

Investment Classification Review (2013-36) – In 2013, the working group agreed to a new comprehensive project to review the investment SSAPs and clarify definitions, scope, accounting methods and reporting guidance and has been working on identified issues since that time. At the Spring National Meeting, the working group exposed four discussion documents for comment "to assist with the consideration of revisions under the Investment Classification Project."

1. Proposed amendments to SSAP 26, Bonds, to adopt the GAAP definition of a "security" used in ASC 320 and 860, and which is already included in SSAP 37, paragraph 2

2. A proposed amendment to require all SSAP 26 investments to have a "contractual amount of principle due"

3. An analysis of exchange-traded fund investments approved for reporting as bonds or preferred stocks as of year-end 2013, and the effect on insurer surplus if these investments, which have no contractual amount of principle due, would be reported at fair value/net asset value, as opposed to actual cost

4. Definitions for debt-like investments that would not meet the proposed new definition of a security in SSAP 26: loan participations, loan syndication, TBA securities, convertible securities and four types of hybrid securities

SSAP 97, Nonadmitted Assets and Application of the SAP Guidance (2015-08) – The working group discussed a significant new project to reconsider conclusions reached in SSAP 97 which could have a material effect on many insurers. The working group exposed for comment the following questions, requesting feedback from regulators and the industry with respect to investments in subsidiary, controlled and affiliated entities (SCAs).

- Nonadmitted Assets in Non-Insurance SCAs - Should guidance be considered to restrict the amount of assets held in an SCA that would not be admitted assets if held directly by the reporting entity? Should guidance be considered to restrict or eliminate the extent to which nonadmitted assets can be transferred to an SCA and included in the reported value of the SCA?

- Valuation of U.S. Insurance SCAs - The statutory equity reported by U.S. insurance SCAs may be affected by permitted or prescribed practices, which may not be disclosed in the parent insurance entity financial statements. Should guidance be considered to require that the value reported for these investments reflect statutory value as calculated per the APP Manual, and not the statutory value from the SCA's financial statements, which could include deviations from SAP through prescribed or permitted practices? Alternatively, should prescribed practices only be permitted in the valuation by the parent insurer with disclosure of any deviations? A third option could be to continue the current guidance, with disclosure of both prescribed and permitted practices of insurance SCAs in the parent company financial statements.

- Valuation of Non-Insurance SCAs Engaging in Insurance Activities and Foreign Insurance Entities - Should paragraph 9 of SSAP 97 be revised to require that the SCA entities captured within 8bii and 8biv be adjusted to a "full statutory accounting basis"? Or should paragraph 9 be revised to reflect additional SAP adjustments, i.e. more than the six adjustments currently required?

Wholly-Owned Real Estate and Mortgage Loan Encumbrances (2015-11) – As a result of adoption of revisions to SSAP 40R effective January 1, 2015 to allow certain wholly-owned real estate LLCs to be accounted for as real estate instead of using an equity method valuation under SSAP 48, the working group exposed a clarification that a "standard mortgage or encumbrance by an unrelated party is not considered a sharing of risks or rewards"

and would not otherwise prevent a wholly-owned LLC from being accounted for as real estate.

XXX/AXXX Reinsurance Disclosure (2014-31) – At the Fall National Meeting the working group exposed for comment a proposed new disclosure related to the adoption of Actuarial Guideline 48 which would require the audited financial statements of insurers ceding XXX/AXXX "Covered Policies" (i.e. ceded on or after January 1, 2015) to disclose information related to such transactions. At the request of the ACLI and the AICPA/NAIC Task Force, the proposed disclosure was revised to clarify the requirements and re-exposed for comment. The revised disclosure requires confirmation that funds for Primary Security and Other Security have been satisfied for all covered policies. If any shortfalls exist, the insurer would disclose additional detailed information.

Medicare Advantage and Medicare Part D Adjustment Premium Receivables and Payables (2014-27) – NAIC staff has received questions as to the appropriate annual statement lines to report Medicare risk adjustment receivables and payables. In 2015, staff met with working group and trade association representatives to develop recommendations. At the Spring National Meeting, the working group voted to expose a proposal to revise SSAP 54, paragraph 30 to record these premium adjustments through premiums receivable (increases) or reserve liabilities (decreases) with an offset to written premium, as opposed to adjustments to aggregate write- in lines and unearned premium reserves.

Short Sales (2015-02) – The working group asked for comments from regulators and industry on whether short sale transactions should be permitted by insurers; SSAP 86 on derivatives is silent on this topic, and some state investment laws explicitly prohibit insurers from entering into short sales. A representative from the NAIC's Capital Markets Bureau commented that it is not uncommon for insurers to do short sales, such as selling U.S. Treasuries short for hedging purposes.

Sale-Leasebacks of Non-Admitted Assets (2015-03) The working group discussed a new issue raised by NAIC staff as a result of questions they have received recently, which is whether the guidance in SSAP 22 was intended to allow the sale/leaseback of nonadmitted assets with unrelated parties. Paragraph 27(d) of SSAP 22 specifically refers to sale/leaseback transactions of nonadmitted assets with third parties, but the leasing guidance has been modified many times since 2001 and some have questioned, for example, whether software would meet the requirements for such a sale/leaseback. The SAP Working Group is asking for input from regulators and interested parties.

Prepayment Penalties and Amortization on Callable Bonds (2015-04) – As a result of numerous bonds being called in 2014 resulting in questions to NAIC staff, the working group voted to expose new guidance to require prepayment penalties and acceleration fees to be reported as realized capital gains, clarify the yield-to-worst concept for continuously callable bonds, and revise the guidance for bonds with make-whole call provisions. The exposure includes illustrative examples.

ASU 2014-01, *Accounting for Investments in Qualified Affordable Housing Projects* (2014-24) The working group re-exposed proposed amendments to SSAP 93 to adopt ASU 2014-01 with a significant modification that net income statement reporting would not be permitted. Revisions were suggested by interested parties to be more explicit that statutory accounting would use the "proportional amortized cost" method, which is essentially the same as optional GAAP method under ASU 2014-01.

Asbestos and Environmental Exception Reporting (2011-45 and 2014-28) – In 2012, the working group adopted accounting guidance for SSAP 62R related to the Schedule F penalty for asbestos and pollution contracts that have duplicate coverage. However, the regulators have been struggling for months to finalize the guidance and instructions for Schedule F. At the Fall National Meeting, the working group voted to expose for comment the more-detailed Option 1 for reporting, which is favored by the majority of the working group; Option 2 is favored by interested parties and some working group members. At the Spring National Meeting, after significant discussion, including a motion and vote on Option 2 which failed, the working group re-exposed Option 1 with modifications to paragraphs 66-68 of SSAP 62R. The comment period for this exposure ends April 30.

Holders of Surplus Notes (2014-25) – As a result of its discussion during 2014, the working group exposed for comment proposed changes to SSAP 41 which would require the following for holders of surplus notes: 1) NAIC 1 rated surplus notes would continue to be reported at amortized cost, 2) unrated surplus notes or those rated other than NAIC 1 would be valued at the lower of cost or fair value. This would eliminate the concept of reporting the notes at outstanding face value or a calculated amount based on a statement factor. Valuation changes would be reflected as changes in unrealized gain or loss.

ASU 2010-23, Health Care Entities, Measuring Charity Care (2015-01) – The working group exposed for comment a proposal to adopt the ASU definition of "charity care" as part of SSAP 54 and adopt, with modification, the disclosure required by the standard. The proposed disclosure provides less detail (compared to the GAAP disclosure guidance) on the types of techniques that may be used to estimate the cost of charity care.

SSAP 24, Discontinued Operations and Extraordinary Items – The working group exposed for comment a proposal to adopt with modification both ASU 2015-01, *Income Statement, Extraordinary and Unusual Items* (2015-06) and ASU 2014-08, *Reporting Discontinued Operations and Disclosures of Disposal of Components of an Entity*. The first ASU eliminates the concept of extraordinary items; the modifications proposed by the working group to ASU 2014-08 guidance would continue to disallow discontinued operations being shown separately from continuing operations in the income statement.

Update Appendix-821 for 2012 Individual Annuity Mortality Table (2015-12) – The working group exposed revisions to include the 2012 Individual Annuity Mortality Table in Appendix A-821, Annuity Mortality Table for Use in Determining Reserve Liabilities for Annuities, effective January 1, 2015. (2015-12)

SSAP 25 Disclosures (2014-36) – The working group re-exposed for comment proposed revisions to reject ASU 2013-06, *Not-for-Profit Entities; Services Received from Personnel of an Affiliate* and to require disclosure of the fair value of services received or transferred by the insurance entity with affiliated entities.

Technical Edits to APP Manual (2015-09) – The working group exposed for comment technical edits to the APP Manual to clarify intent. The most significant proposed change is to SSAP 106 for the ACA section 9010 disclosure. NAIC staff noted that in 2014 annual statement filings some reporting entities incorrectly reported an impact on Authorized Control Level RBC. The risk-based capital sensitivity test determines the effect on Total Adjusted Capital only.

Report of the Restricted Asset Subgroup
The subgroup met February 18 to discuss collateral requirements for repurchase and reverse repurchase agreements and consider ASU 2014-11, *Repurchase-to-Maturity Transactions, Repurchase Financings and Disclosures*. With respect to ASU 2014-11, the subgroup released a Discussion Points document, which recommends that the subgroup "consider diverging from the U.S. GAAP guidance and establishing new guidance that would remove transferred securities under repurchase agreements from the financial statements." Detailed comment letters from the ACLI and AIG disagreed with this proposal. At the SAP Working Group's meeting in Phoenix, the subgroup reported no revisions to SSAP 103 are being brought to the working group for consideration at this time. The subgroup has scheduled for May 13 an educational session on repos together with interested parties.

Based on a survey done with state insurance departments, the subgroup concluded that the prohibition of insurers investing in long-term repurchase agreements (i.e. longer than a year) should continue; therefore, the subgroup will not begin a project to consider such repos as admitted assets.

Principles-Based Reserving Implementation Task Force

The task force met via conference call in February and March and at the Spring National Meeting to discuss progress on its many PBR-related projects.

2015 XXX/AXXX Reinsurance Supplemental Proposal (2015-18BWG)
During its February conference call the task force exposed for comment the proposed 2015 reporting for XXX/AXXX reinsurance transactions, which reflects changes resulting from certain transactions now being subject to AG 48 and requirements considered for 2014 but deferred until 2015. Changes from 2014 include the following:

1. Part 1, All XXX and AXXX Cessions, has a new column "Special Exemption by Domestic Regulator" to highlight any transactions exempted by the NAIC's Financial Analysis Working Group or other designated regulators.

2. Part 2 has been separated into two subparts: Part 2A for "grandfathered or special exemptions," and Part 2B for "non-grandfathered" transactions. Part 2A replaces the Required Level of Primary Security disclosure with a column for "Economic Reserve Level."

3. Part 5 is new and has ten interrogatories with additional disclosure on letters of credit, pledges and related party guarantees.

The task force heard comments during its March 16 conference call including a request from the ACLI

and the AAA not to require reporting of "special exemptions" in parts 2 through 4; this change was not made. The task force did agree to a proposal to keep as confidential interrogatories 1.1 and 1.2 on the use of LOCs or similar instruments as collateral. The task force then voted to adopt the proposal for consideration by the Blanks Working Group, who exposed it for comment at the Spring National Meeting. A proposal to include the two confidential interrogatories in the Life RBC filing, as opposed to the Reinsurance Supplement, was exposed for comment during the Life RBC Working Group's April 8 conference call.

PBR Adoption by States and "Substantially Similar" Considerations

The task force reported that as of Spring National Meeting, 23 states have adopted the principles-based reserving requirements, which represents 37% of direct U.S. premium. Seventeen additional states have indicated they will introduce legislation in 2015 or 2016, which would bring the total to 79% of premium. This would exceed the 75% premium threshold requirement but would not meet the 42 required states for PBR implementation. The task force is still recommending the use of January 1, 2017 as the earliest probable PBR Valuation Manual effective date, which would require the 42 states to adopt PBR by July 1, 2016.

The above analysis assumes all states' adoptions of PBR will meet the "substantially similar" test, i.e. that the states have adopted all the sections of the Standard Valuation Law necessary for each law to be considered "substantially similar." At the Fall National Meeting, the task force had exposed for comment the same "substantially similar" components as were exposed for Accreditation purposes by F Committee in 2010 (but which has not yet been finalized); no comments were received during the comment period. At the Spring National Meeting the task force agreed they need to proceed quickly on this issue and adopted a motion to form a subgroup to perform the detailed work necessary, which will need significant input from insurance departments' attorneys. Tennessee and Washington volunteered for the subgroup but more members are needed.

Small Company Exemption

At the Fall National Meeting, the task force voted to expose the controversial PBR Small Company Exemption Proposal for comment until January 15. During its February 11 conference call, the task force discussed comments which were similar to those previously expressed, e.g. New York stated that there is no actuarial justification for an exemption based on premium and there are already exclusion tests included in the Valuation Manual; proponents viewed the exclusion tests as being too costly and time consuming to perform. After significant discussion, the task force voted to include a $300 million/$600 million exemption in the Valuation Manual with the following requirements:

- Premium threshold – A company's ordinary life premiums must be less than $300 million for the legal entity and less than $600 million for the holding company group. The small company exemption applies to the entire company, which differs from the product line exclusion tests.
- Risk-Based Capital threshold – A company's RBC must be at least 450%
- An unqualified actuarial opinion on reserves
- The company can have no material universal life with secondary guaranty business in force
- Exempted companies must use the Commissioners Reserve Valuation Methodology (CRVM) instead of the Net Premium Reserve (NPR).
- Statements of exemption must be filed with the company's domestic commissioner by July 1 of the reporting year, which the Commissioner may reject prior to September 1 of the reporting year.

This proposal was also adopted by the Executive Committee in Phoenix.

PBR Experience Reporting Framework

The task force heard a brief update on the Framework which addresses data collection and dissemination under PBR. In 2014, the task force had surveyed the states regarding legal authority, coordination, expense sharing of data collection and other issues. Thirty-five states responded to the survey and NAIC staff is considering options based on the responses; a proposal is expected in the next few months.

Status of Other Reinsurance Framework Charges

The task force briefly reviewed a written report on the status of its charges to eight working groups and committees to implement the XXX/AXXX Framework. The status of most of these charges is discussed in the summaries of the respective NAIC groups. Longer term projects not currently in process are only the following:

- The Life Actuarial Task Force will consider whether changes are needed to the *Actuarial Opinion and Memorandum Regulation* after

adoption of revisions to the *Credit for Reinsurance Models* and related Accreditation decisions.

- The Financial Condition Committee has a charge to "evaluate the risk transfer rules applicable to XXX/AXXX reserve financing transactions to make sure they appropriately apply to situations such as those where parental/affiliate guarantees are used, resulting in the risk effectively being kept within the holding company system even though the reinsurance arrangement involves an unrelated third party." There is no current activity on this charge as the committee is waiting to see if there are risk transfer concerns remaining after other proposals have been implemented.

Capital Adequacy Task Force

The task force met March 11 and adopted the working agendas for 2015 RBC projects for its five working groups and subgroup. The task force has scheduled a conference call for April 30 (11:30 EDT) to consider final adoption of the various proposals for 2015 RBC filings discussed in this Newsletter.

The task force and its working groups now index proposed changes to the formulas and instructions, similar to the Blanks Working Group. The proposal reference is shown after each topic below.

Life Risk-Based Capital Working Group

The working group met via conference call three times in February and March and in person at the Spring National Meeting. There was also a call April 8 to continue discussion of the AG 48 RBC proposals as discussed below.

XXX/AXXX Reinsurance Framework Referrals
The working group had been asked to consider issues related to the Framework by the PBR Implementation Task Force and has spent nearly all of its time in 2015 discussing these proposals.

Qualified Actuarial Opinion (2014-33-L) – The PBR Implementation Task Force asked the working group to "determine whether the current RBC C-3 treatment of qualified actuarial opinions is adequate for the purpose of the risks of XXX/AXXX reinsurance transactions that receive qualified actuarial opinions." Because a qualified opinion would otherwise increase RBC factors for reserves subject to Interest Rate Risk and Market Risk, the working group has proposed revisions to LR027 to avoid impacting all lines of business of the ceding company "for a qualification of the Actuarial Opinion due solely to the direction provided in AG 48."

Primary Securities Shortfall/RBC Cushion (2014-35b-L) – This proposal would increase captive authorized control level RBC dollar for dollar by the amount of any shortfall of Primary Securities. Both the ACLI and the AAA had suggested that increasing total adjusted capital instead of ACL, but the working group did not agree to that change. The instructions state that this RBC adjustment would apply even if a state exempts an insurer from AG 48. This proposal was revised during the working group's April 8 conference call and re-exposed for comment until April 20.

Consolidated RBC Shortfall/RBC Cushion (2014-42-L) – This proposal would apply to the ceding company's RBC calculation and would add a new schedule to show the calculation of the RBC AG 48 shortfall for all captives with an adjustment to total adjusted capital. This proposal was revised during the working group's April 8 conference call and re-exposed for comment until April 20. The most significant change made was to set the benchmark RBC level at 300% of authorized control level for each captive. (The benchmark had previously not been set.)

The working group had also been asked to develop charges for the "other security" assets under the Framework/AG 48. At the Spring National Meeting, the working group decided to defer consideration of this proposal until 2016 RBC due to its complexity and lack of time given the other proposals.

It is expected that the three proposals above will be adopted during the April 22 call of the Life RBC Working Group and the subsequent April 30 call of the Capital Adequacy Task Force and will be effective for 2015 RBC filings.

ACA RBC Proposals (2014-36-L and 2014-39-L)
At the Spring National Meeting, the working group adopted two informational-only ACA tests for 2015 Life RBC filings, which had been exposed for comment in 2014. These two tests, the underwriting risk-experience fluctuation risk and risk adjustment and risk corridor sensitivity test had been adopted for the 2014 Health RBC formula. These proposals were also adopted by the Capital Adequacy Task Force in Phoenix.

Derivatives Collateral Proposal (2014-32-L)
The working group discussed the proposal, the goal of which is to implement consistent reporting of cash pledged as collateral for derivative transactions and

would eliminate the over-charging of risk for cash collateral. The proposal had been developed by the Investment RBC Working group in 2013 and would exclude cash collateral pledged for derivative transactions from a separate RBC charge and also proposes a new "centrally cleared" derivatives category for RBC and AVR (as a result of the Dodd Frank requirements), which would be assessed a 0.4% RBC charge. During its April 8 conference call, the working group made some minor changes to the proposal and exposed it for comment until April 20. The chair noted the related AVR changes won't be effective until 2016 at the earliest. If adopted by the working group on April 22 and April 30 by the Capital Adequacy Task Force, the derivatives collateral revisions will be effective for 2015 RBC.

Referral from the Operational Risk Subgroup
At the Spring National Meeting, the working group discussed a referral from the Operational Risk Subgroup (which had been suggested by the chair of the Life RBC Working Group) to "expand the granularity" of the proposed operational risk charge to better reflect the complexities of life and annuity products. The chair noted that the NAIC is under pressure from international regulators to complete an operational risk charge quickly, but a premium and reserve factor-based charge is too "superficial" for purposes of Life RBC. The working group agreed to take on this project, recognizing that they will likely need some educational sessions from third parties as they begin to address this complex issue.

Stress Testing Subgroup
The goal of the subgroup is to have stress testing requirements in place when PBR becomes effective, likely 2017. However, the subgroup has not met since the Fall National Meeting due to time spent on the AG 48 RBC proposals.

C-3 Phase II/AG43 (E/A) Subgroup Update
This joint subgroup is charged with evaluating the overall effectiveness of capital and reserve requirements for variable annuities and presenting recommendations to improve the effectiveness of those requirements. In 2014, the subgroup asked for additional resources so that the necessary in-depth analysis can be performed. At the Spring National Meeting, the chair reported that Connecticut will be assisting with a field test on different alternatives for C3P2. The NAIC plans to hire consultants to assist with the effort; no timetable for the project was discussed.

Investment Risk-Based Capital Working Group

The Investment RBC Working Group held three conference calls in January, February and March and met at the Spring National Meeting. The working group is focused on several priority topics to be addressed in 2015, which are discussed below.

Corporate Bonds
The AAA continues to recommend increased granularity in the base factors, by expanding the current 6 NAIC designations to 14 categories, utilizing "+" and "-" indicators to expand the number of designations for categories 1-4 (e.g., 1+, 1, 1-). However, under AAA's recommendation NAIC 6 and NAIC 5 designated bonds would not have +/- indications. The AAA's preliminary factors were presented at the 2014 Summer National Meeting, and are generally higher for investment grade bonds and generally lower for below investment grade bonds as compared to the current C-1 factors. The AAA is expected to present minor revisions to proposed base factors at the 2015 Summer National Meeting. The changes are intended to reduce cliffs and plateaus across the ratings categories by "smoothing" the C-1 factors; this is expected to reduce the potential for ratings arbitrage.

The AAA is still working to reconcile the current factors to the proposed factors, with the goal of explaining and quantifying how and why the factors have changed. The AAA is also finalizing its model validation procedures and completing documentation. The AAA anticipates completing its documentation and analysis by the Summer National Meeting.

The ACLI commented that some life insurers have started to analyze the effect of the preliminary factors on their RBC requirements, and have observed an increase of approximately 20% to more than 100% on page LR002 of the RBC calculation before tax, covariance and other adjustments. As a result, the ACLI believes a transition period to the new factors should be considered. NAIC staff supporting the working group noted that preliminary discussions with rating agencies has indicated their ratings processes would be impacted negligibly.

Real Estate
The working group continues to discuss what is expected be a significant reduction in the base factor for real estate. The initial proposal would was to reduce the current base factor of 15% to 8% for all real estate categories. While the recommended base

factor was developed using a price variation analysis of what is perceived to be reliable real estate industry data, concerns have been expressed by the working group that that the significance of the decrease in the base factor may incentivize insurers to increase their exposure to this less-liquid asset class. The working group had preliminarily concluded that the base factor should be adjusted to reflect variable property type risk (beta factor). However, after considering feedback from the ACLI on the implementation challenges of a beta factor on a relatively small investment class, the work group is expected to approve an increase in the proposed base factor to 8.5% rather than adding a variable beta factor. According to ACLI modeling results, an increase in the base factor from 8% to 8.5% would increase the confidence level from 95% to 97%. A revised proposal is expected to be considered by the working group at the Summer National Meeting.

Granularity
The working group discussed the level of granularity, or precision, necessary for RBC factors of each investment class. While the working group favors the perceived increased in accuracy that results from increased granularity, the regulators acknowledge that this comes with greater implementation costs. For example, the working group has decided not to add granularity, through a beta factor, to the real estate base factor, recognizing that this asset class represents approximately 1% of life insurer portfolios. However, the working group does favor increased granularity for more material asset classes. For example, the working group appears to supports the AAA's proposal to expand the corporate bond factors by increasing the NAIC designations from 6 to 14, because bonds are life insurers' most material asset class.

Derivatives
The Life Insurer RBC for Derivatives proposal developed by interested parties was approved by the working group in 2014 and has now been referred to the Life RBC Working Group for its consideration and possible adoption for 2015 RBC filings. See the Life RBC Working Group summary for further discussion.

Affiliated Investments
The task force is considering whether there should be a difference in RBC factors if an insurer invests in an affiliate-issued investment, including bonds, real estate and Schedule BA assets. The chair of the working group has observed that affiliated investments may pose a greater risk than those issued by third parties and perhaps should have a higher capital charge commensurate with their risk. The task force is aware that the Health and P/C RBC Working Groups are considering simplifying the RBC charge for investment affiliates.

Sovereign and Municipal Bonds
The working group's preliminary perspective is that sovereign and municipal bonds should carry the same RBC factor as corporate bonds. Based on discussions with the nationally recognized statistical rating organizations, those entities apply a global ratings methodology; thus the factors for sovereign, municipal and other non-corporate fixed income securities rated by the NRSROs are expected to be same as corporate debt ratings with comparable non-performance risk. The working group has requested that if NAIC members or interested parties want to make a case that these bonds should be treated differently from corporate bonds, a comprehensive argument, well-grounded with data, should be provided to the working group by the Summer National Meeting.

Concentration
The working group plans to analyze how the asset concentration factor currently works and determine whether it is still appropriate going forward. This topic is expected to be discussed following the Summer National Meeting.

Carrying Value
The working group exposed a proposal in 2013 to adjust the RBC factor for corporate bonds based on the carrying value of the investment; however no decision or conclusions were made. The AAA model assumes that bonds are held at par value. If bonds are held at a premium to par, some risks are not captured and the factors are understated; if bonds are held at a discount to par, the factors are overstated. The working group needs to consider whether the risks not captured are offsetting or if they are material to warrant further consideration. The working group plans to discuss this topic on an upcoming conference call.

Implementation
The implementation of new factors, particular those with increased granularity, as is being contemplated for bonds, will require significant discussion and coordination with several other NAIC groups, including the Valuation of Securities Task Force, Blanks Working Group, SAP Working Group, and Financial Regulation Standards and Accreditation Committee.

Other priority topics of discussion include potential adjustments to the AVR, Schedule BA assets, commercial mortgages, funds, and structured securities. The working group's 2015 priorities do

not specifically include any consideration of the impact of Life RBC factors on P/C and Health RBC. The timeline for implementing any new life RBC C-1 factors remains uncertain given the significance of the work that remains. Based on concerns raised by the industry with implementing expanded C-1 factors, 2017 Life RBC filings seems like the earliest date changes to the bond factors could be effective.

Operational Risk Subgroup

The subgroup met three times by conference call in January and March. During the conference calls, the subgroup discussed the following topics.

Life RBC Referral
As discussed in the Life RBC Working Group summary, the subgroup adopted a referral to the Life RBC Working Group to discuss and/or develop an alternative method for an operational risk charge in the Life RBC formula. It was clarified that any recommendations by the working group would be sent to the subgroup for consideration. The subgroup will continue to determine if all RBC blanks would remain uniform in their treatment of operational risk before a proposal is sent to the Capital Adequacy Task Force for exposure and consideration.

AAA Comment Letter
The subgroup reviewed AAA's response to two questions raised by the subgroup in its December 4 conference call. The first question is whether an industry survey on the amount of operational risk embedded in the current RBC factors would be valuable. The AAA believes that such a survey would have limited value in advancing the NAIC's goal of quantifying the explicit amount of operational risk captured in the RBC formulas (with the exception of the C-4 life RBC business risk component). Because individual companies are concerned with their specific exposures, insurers may not be up-to-date with the ongoing technical developments for the current RBC factors; as such, they would have very little insight on what is embedded in the current RBC formula for operational risk.

As a result of this and other discussions, the subgroup determined that the quantification of embedded operational risks other than growth risks is not feasible at this time, even though the subgroup has been advised that substantial amounts of operational risk exist in underwriting and insurance risk charges.

The second question relates to whether strategic or reputational risk should be included in the definition of operational risk. The AAA does not believe these two risks should be included in the definition. Strategic risk is the result of poor strategic decisions, such as entering a new market or choosing to offer (or not offer) a new product. Strategic risk is identified as a separate risk category in many risk taxonomies (e.g., Basel II) and is not included with operational risk, and the AAA does not see value in creating another risk taxonomy. Reputational risk is considered a second order risk; it is a consequence of a risk event. As such, AAA does not believe that it rises to the level of being considered within the definition of operational risk. A subgroup member noted agreement with AAA's conclusion. No action was taken by the subgroup on this matter.

Activity Status
The subgroup discussed the status of its activities:

Design of Operational Risk Charge - The design of a new operational risk charge is the subgroup's primary task. This includes whether to use a factor-based or a capital add-on approach, the specific proxies and factors to be used in a factor-based approach for life vs. non-life, and the inclusion of growth risk charges. To aid this effort, the subgroup implemented an informational-only reporting of an operational risk charge (without specifying factors) in 2014. The subgroup will use this information to determine an appropriate methodology that meets an overall (yet to be determined) target impact on RBC. To assist the subgroup, NAIC staff will test the outcome of using various factors in the informational-only filings. The premium and reserve data submitted for 2015 RBC filings will the same as for 2014.

Testing of Growth Risk Charges - NAIC staff is currently comparing the effects of the subgroup's proposed growth risk charges to the growth risk charges that are currently embedded in P/C and health underwriting risk charges.

Role of ORSAs – The subgroup anticipates that ORSAs will provide regulators with the best source of insight into companies' exposure to operational risk and intends to analyze ORSAs when they become available in early 2016.

Creation of an Operational Loss Database - The subgroup considered the merits and difficulties of creating such a database and decided to defer this matter until the subgroup has had a chance to analyze the operational risk content of ORSAs.

Role of Partial Internal Models of Operational Risk- Because the use of internal models would be heavily dependent on the use of a credible operational loss database, the subgroup does not intend to consider this issue further at this time.

Property/Casualty Risk-Based Capital Working Group

The working group met by conference call in December and February and in Phoenix to discuss the following projects.

Reinsurance Credit Risk Charge (2014-38-P)
At the Fall National Meeting, the working group re-exposed the revised RAA Reinsurance Credit Risk Charge proposal. During the December 22 conference call, the working group received an update on an analysis performed by Wisconsin based on data provided by the RAA and NAIC. Wisconsin reported that the proposal will likely benefit companies that cede significant amounts of business to unauthorized reinsurers. The chair suggested proceeding with the proposal for informational purposes only for one year to allow regulators an opportunity to analyze the potential impact to the RBC ratio and work out any unforeseen issues. Following the discussion, the working group exposed the informational-only proposal, which was adopted by the working group and its parent task force in Phoenix, and is effective for 2015 RBC filings.

ACA RBC Proposals (2014-30-P and 2014-31-P)
At the Spring National Meeting, the working group adopted two informational-only ACA tests for 2015 P/C RBC filings, which had been exposed for comment in 2014. These two tests, the risk adjustment and risk corridor sensitivity test and the underwriting risk-experience fluctuation risk had been adopted for the 2014 Health RBC formula. These proposals were also adopted by the Capital Adequacy Task Force in Phoenix.

Investment Affiliates (2014-29-P)
The working group discussed the proposal exposed at the Fall National Meeting, which goal is to simplify the RBC charge for the ownership of investment affiliates to be a fixed factor times the carrying value of the common stock, preferred stock and bonds. The current RBC charge for the ownership of an investment affiliate is a "look-through" approach based on the RBC of the underlying assets and prorated for the degree of ownership. Because investment affiliates do not submit RBC filings, the RBC charge for the investment affiliate cannot be easily determined and is a challenge to verify. Two industry comment letters opposing the proposal were received noting that the fixed factor appears to contradict the principle that the RBC charge should be the same as if the assets were held directly, thus resulting in less accurate reporting which would not improve the ability of regulators in identifying weakly capitalized companies. No action was taken by the working group in Phoenix, but the chair committed to working with NAIC staff to explore alternatives, such as retaining the current treatment with additional worksheets for verification purposes.

WCFI and LIHTC (2015-07-P)
The working group discussed a proposal to move the NAIC02 Working Capital Finance Investments and Low Income Housing Tax Credit Lines from the Other Long-Term Assets Page PR008 to the Fixed Income Section in the Asset Concentration Page PR011. The proposal will address the issue of these line items that are included in the R1 part of the formula that are not handled consistently in PR011. Following the discussion, the working group exposed the proposal for comment until April 12.

Catastrophe Risk Subgroup

The subgroup met by conference call on February 17, held an e-vote in March and met at the Spring National Meeting to discuss its projects in process.

Timeline
The subgroup discussed its 2015 working agenda which is focused on the development of RBC formula revisions to include a risk charge based on catastrophe model output. The subgroup confirmed that the catastrophe risk charge will be reported on an information-only basis in 2015 with a plan to go-live by year-end 2016.

Contingent Credit Risk Proposal (2014-27-CR)
The subgroup discussed a previously exposed proposal to revise the catastrophe contingent credit risk charge for modeled reinsurance recoverable in R6 and R7 from 10% to 4.8%. The change applies a more appropriate factor for modeled reinsurance recoverables that reflects the underlying credit risk associated with highly rated reinsurers plus a margin for other than credit risk and is consistent with the methodology utilized to derive the R3 credit risk charge. The RAA commented that using the aggregate exceedance probability as the standard could be a challenge for smaller companies that do not have in-house expertise to perform the calculation. Comments raised by others include adding a "ceded amount recoverable" column to be consistent with the net amount; sorting the gross and net probable maximum losses separately and having the ceded amount be the subtraction of the gross and the net; allowing flexibility on reporting requirements and soliciting information from the filers as an alternative for addressing the issues. Following the discussion, the subgroup adopted the proposal to adopt the 4.8% contingent credit risk factors for R6 and R7, noting that the associated

issues will be resolved later. The Capital Adequacy Task Force adopted the proposal in Phoenix.

Catastrophe Risk Charge Exemption (2014-37-CR)
The subgroup discussed a previously exposed proposal that provides an exemption from completing PR026 by providing interrogatories to determine whether there is "substantive earthquake and hurricane risk exposure" based on minimum coverage exposure and surplus percentages of property insured value in catastrophe-prone areas. No comment letters were received. The subgroup and its parent task force adopted the proposal in Phoenix.

Aggregate Exceedance Probability vs. Occurrence Exceedance Probability (2015-04CR)
The subgroup continued its discussion on an industry concern regarding the use of an AEP curve to model catastrophe losses as opposed to an OEP curve. On March 6, the subgroup held an e-vote and exposed a proposal that changes the form and instructions for PR026 to clarify issues related to EP curve sorting, calculation of the catastrophe contingent credit risk charge for reinsurance recoverables, and use of AEP and OEP model output. The revisions provide needed flexibility to companies by allowing them to employ catastrophe models for RBC in a manner that is consistent with the way the company internally evaluates and manages its modeled net catastrophe risk. Three comment letters were received in support of the proposal including comments to clarify and enhance the instructions. Following the discussion, the subgroup adopted the proposal which was later adopted by its parent task force in Phoenix.

Attestation Revision (2014-40-CR)
The subgroup discussed a proposal that would add a new question to PR002 to have companies indicate which of the methodologies was used to sort the net and gross probable maximum losses so regulators can collect data on how companies are deriving their modeled catastrophe losses. The subgroup exposed the proposal for comment until April 12.

Health Risk-Based Capital Working Group

The working group met by conference call on January 13 and February 12, held an e-vote on February 24 and met in Phoenix to discuss the following issues.

Affiliated Risk (2015-01-H and 2015-02-H)
The working group discussed the affiliated risk proposal to simplify the RBC charge for the ownership of investment affiliates to be a fixed factor times the carrying value of the common stock and preferred stock. The investment affiliate proposal applies a 30% factor charge to affiliate type 5 and changes the name "investment subsidiaries" to "investment affiliates" to be consistent with the terminology used in the other formulas. The proposals were exposed for comment until March 12 and were adopted by the working group and its parent task force at the Spring National Meeting, making it effective for 2015 RBC filings. (Note that interested parties objected to this same change for the P/C RBC formula so it is still under discussion by the P/C RBC Working Group.)

Underwriting Risk Instructions (2015-06-H)
The working group discussed an issue in which the Health RBC instructions do not currently address where a company should report life and property and casualty premiums in the health RBC formula. The working group discussed a proposal to modify the "Other Health Coverages" instructions for page XR012 & XR012A to "Other Coverages." In Phoenix, the working group exposed the proposal for comment until April 15.

AAA Annual Statement Revisions
The working group heard a proposal by the AAA on changes to the Underwriting and Investment Part 2 annual statement instructions that provide cross checks to the healthcare receivable amounts. Following the discussion, the working group exposed the proposal for comment, and subsequently adopted a referral to the Blanks Working Group for consideration in the 2015 annual statement instructions.

Excessive Growth Charge
The working group continued its discussion on excessive growth charge for start-up companies. A retired regulator from the Connecticut Insurance Department had previously performed a study which revealed that only 6% to 8% of reporting companies have an excessive growth charge greater than zero. Additional analysis in 2105 confirmed these findings. As a result it would appear that the excessive growth charge has not been a significant factor in causing a company (start-up or not) to be subject to regulatory consequences. The working group is deferring further discussion of this matter until the Operational Risk Subgroup has completed its review of the excessive growth charge and has made its recommendation.

Medicaid Pass-Through Payment Survey
The working group heard an update on the results of the Medicaid pass-through payment survey. The survey was conducted as an opportunity for the working group to provide guidance on how to treat the payments from an RBC perspective and not

necessarily from an accounting perspective. Twenty-three states responded to the survey demonstrating that there is diversity in practice as to whether the payments are considered premium for premium tax or statutory accounting purposes or are not recorded at all in the financial statements

Consistent with the survey results, there are currently some companies that incur a higher RBC charge because the pass-through payments are treated as premiums and are flowing through to the underwriting risk in the RBC calculation. However, the payments are not underwriting-related premiums and are not related to any specific health claim. The chair believes there should likely be a business risk charge for the pass-through payments. The working group plans to discuss the survey responses in greater detail during its April 21 conference call.

Valuation of Securities Task Force

The task force held a joint conference call in February with the Reinsurance Task Force and met in Phoenix, taking the following actions. Unless otherwise noted, exposed items have a comment period ending May 14.

NAIC Bank List
See discussion in the Reinsurance Task Force summary of the conclusion that the P&P Manual should be amended to allow letters of credit issued by qualified non-banks as acceptable collateral under the *Credit for Reinsurance Models*.

Securities Listed by SVO
The task force has been working with the Reinsurance Task Force to develop a consistent interpretation of the phrase "securities listed by the Securities Valuation Office," as that term is used in the *Credit for Reinsurance Models* to establish investments which are acceptable forms of collateral for reinsurance obligations. See the Reinsurance Task Force summary for discussion of proposed amendments to the P&P Manual to clarify this issue.

Private Rating Letters
At the 2014 Summer National meeting, SVO expressed concerns with the volume of securities designated as FE by insurers, but for which the SVO was not able t0o confirm with its data sources that the filing exempt classification was appropriate. These exceptions appear on the state examiners Jump-Start report, and are routinely investigated during the financial examination process. With the growing volume of exceptions, the SVO considered possible options to reduce the number of exceptions appearing on the Jump-Start reports. The SVO initially attributed the discrepancies as likely the result of private letter ratings obtained from CRPs by insurers, and proposed that insurers file copies of all private letter ratings with the SVO when the security is not in NAIC systems. The industry strongly objected to the SVO proposal and agreed to work with the SVO to develop a compromise solution.

Following further investigation, it was noted that a significant portion of the holdings classified as FE were not subject to private letter ratings, including U.S. government securities, CDs, pre-refunded securities, syndicated securities and lottery securities. These exceptions were termed "false positives." However, private letter ratings still comprise a meaningful portion of the industry's FE holdings. The SVO continues to recommend that the task force consider a requirement that insurers submit private letter ratings as an administrative process so that they can be recorded in NAIC systems and reduce Jump-Start exceptions going forward.

The SVO indicated that it will review the 2014 filings to determine if a large volume of FE exceptions continues to be present in the current filing year. The SVO also announced that it is adding new data feeds to address reduce the number of FE exceptions. A task force sponsored proposal has also been submitted to the Blanks Working Group (2015-14BWG) to add other identifier numbers, specifically the ISIN and SEDOL numbers, which is expected to further reduce the number of false positives in 2015 filings. Additionally, at least one CRP has indicated that it plans to file all private letter ratings with the SVO on a go forward basis, despite there being no official requirement to do so.

The chair of the task force commented on the importance of this project as it is desirable to reduce the amount of time examiners spend on these issues so that they can focus their efforts on items of greater significance. The task force requested the SVO to continue working with industry on this issue and to report back at the Summer National Meeting.

UK GAAP Considerations
The Purposes and Procedures Manual currently permits the submission of financial statements prepared in accordance with UK national GAAP without reconciliation to U.S. GAAP for SVO analysis purposes. However, changes have been adopted to UK GAAP, effective in 2015, which may require an amendment to instructions in the Purposes and Procedures Manual to preserve the U.S. GAAP reconciliation exemption. The SVO is working with

the ACLI to study the impact of changes in UK GAAP. Based on their analysis thus far, most of the changes have been made in order to align with IFRS and to eliminate redundant disclosures. The SVO and ACLI are expected to submit any proposed changes to the Manual for exposure at the Summer National Meeting.

RMBS & CMBS Modeling

SSG staff reported on the 2014 year-end RMBS and CMBS modeling results, indicating that the process was relatively uneventful. Approximately 18,000 RMBS and 4,000 CMBS held by insurers were modeled. SSG staff also noted that, as a result of NAIC governance requirements, an RFP process was initiated in February for the 2015 financial modeling of RMBS and CMBS holdings. Several vendors have submitted proposals; and those proposals are currently being assessed. The final recommendation of vendors is expected in June.

Derivative Instrument Model Regulation

No comments were received on a previously exposed report from the SVO regarding its review of the *Derivative Instruments Model Regulation* against the NAIC's Model Law criteria. The SVO's report was in response to a request from the Financial Condition Committee to consider whether the model should be retained, amended, converted to a guideline or archived. The SVO noted that since the most recent revision by the NAIC in 2009, only one state has adopted the revised model. Nine other states have adopted some other legislation related to the regulation of derivative instruments, including the pre-2009 model law. Despite these low adoption rates, the SVO noted that derivative regulation is an important issue that the NAIC should have a position on.

The task force directed NAIC Investment Analysis Office (the SVO and the SSG) to coordinate with interested parties in assembling a panel of industry experts who can inform the task force as to how the derivatives market and related regulation has changed since 2009. The task force will then in be in a position to recommend a course of action in response to the Financial Condition Committee request.

Catastrophe-Linked Bonds Regulatory Framework

At the Fall National Meeting, the task force received a presentation from the North American CRO Council, which proposed a review of the regulatory framework that applies to catastrophe-linked bonds. The CRO Council noted that the current framework creates a disincentive for life insurers to invest in catastrophe-linked bonds, as the C-1 (credit risk) factor of the Life RBC formula creates an RBC charge that is disproportionate to the risks of this asset class. Catastrophe-linked bonds, which are not commonly rated by a CRP, are subject to the 5*/6* treatment, receiving the highest C-1 charge despite having little credit risk per the Council. As a result life insurers do not typically participate in the catastrophe bond market. The Council suggested that the Life RBC formula should instead view these bonds based on their predominant risk, as insurance, and apply a C-2 insurance risk factor. P/C insurers would benefit from this change by providing access to additional capital base, leading to better pricing. Life insurers would benefit from the portfolio diversification and obtain a higher risk-adjusted return. The task force exposed the presentation for comment until January 18.

In Phoenix, the task force noted that one comment letter had been received from the California Earthquake Authority in support of the proposal. Additionally, the chair of the task force indicated that he had reconsidered his initial perspective that the proposal should be referred to the Capital Adequacy Task Force; instead, having discussed the matter with the chairs of the relevant working groups, there was a consensus that the topic should be referred to SAP Working Group. SAPWG will consider whether a new statutory accounting principle should be developed specific to catastrophe-linked bonds. The task for also requested that ACLI poll its membership regarding the potential demand for these investments. ACLI expects to report back to the task force and SAPWG in April.

Non-Recourse Loans

The SVO reported that that it had assessed the credit quality of at least 51 non-recourse notes in error. The issuer of non-recourse notes has no legal obligation to repay the notes as the loans are made based on the basis of charitable criteria, thus their viability as a financial asset is questionable. As a result, the SVO has concluded that the P&P Manual does not grant the SVO the authority to assess these loans. The SVO removed 13 non-recourse loans from the VOS database during the 2014 annual review process and another 38 loans have been identified for deletion, while several other notes are being assessed. The SVO also observed that non-recourse notes may not meet the definition of an admitted asset under statutory accounting principles. The task force exposed the SVO report for comment.

Definition of Structured Securities
As a result of the recent addition of Part Seven to the Purposes and Procedures Manual, there was confusion during the 2014 filing process regarding the meaning of "structured securities." Specifically, some insurers have concluded that the special reporting provisions referred to as 5*/6* are applicable to structured finance securitizations. The SVO staff presented a report which explained that the 5*/6* process is intended to apply only to a group of complex corporate securities, and not to securitizations. The SVO recommends adding further clarification to the Purposes and Procedures Manual to remove this confusion. The task force exposed the SVO's recommendation for comment.

Filing Process Modernization
The SVO informed the task force that it is currently evaluating its computer systems needs and related processes to improve its ability to provide high-quality and timely credit and valuation assessments to the industry. This undertaking has prompted the need to revisit the filing process rules defined in the Purposes and Procedures Manual, as there is a desire to build these rules into new systems. The SVO staff noted that the current filing rules were developed approximately 20 years ago at a time when computer systems were far less advanced; thus there are substantial requirements for paper documentation in the filing process. The current rules place stress on SVO analysts at year-end to produce quick results, while underutilizing SVO resources in the first half of the year. The SVO recommends these filing procedures be reviewed and updated for a digital-based framework to enable better management of the workload throughout the year. The task force exposed the SVO document for comment period May 14 and directed the SVO to work with the North American Securities Valuation Association, ACLI and other industry representatives on the project. The goal is to develop proposed alternative filing frameworks that can then be presented to the task force and other NAIC groups for consideration.

Purposes & Procedures Manual Publication Schedule
The IAO staff reported that the NAIC Publications Department plans to make the Purposes and Procedures Manual available for download electronically to AVS+ subscribers. A hard copy of the Manual will continue to be available for purchase; however, going forward it will be published on an annual basis rather than twice a year. Interim changes to the Manual will be available on the NAIC website throughout the year.

Group Solvency Issues Working Group

ORSA Pilot Project and Regulator Training
As a result of the ORSA Subgroup being disbanded, this working group will take on the charges of that subgroup. To that end, the working group received an update regarding the results of the 2014 ORSA pilot: 27 companies and 26 states participated in the pilot in 2014. Several of the most common areas for improvement based on the pilot are as follows: continued alignment of risks and business strategies, quantifying risk appetite statements, and support for why a company selected its solvency capital method. In addition, states continue to receive trainings in how to review ORSA reports. Steve Johnson (PA) reiterated his comments from other meetings that ORSA is a "regulatory game changer." He even went as far as to say he didn't think "we'll see another large insolvency" as a result of the improvements initiated by the ORSA processes.

2014 Revisions to the *Insurance Holding Company System Regulatory Act* (#440)
The working group then discussed the changes to the holding company model that were adopted in December relating to the ability of the regulator to act as group-wide supervisor for internationally active insurance groups. Pennsylvania and Florida have already adopted the guidance, and New Jersey plans to adopt later in 2015. Other working group member states plan to adopt in 2016 or 2017.

Changes to the Financial Analysis Handbook
During a February 13 conference call, the working group exposed for comment proposed holding company analysis changes to the Financial Analysis Handbook. A number of comments were received; edits discussed during the Spring National Meeting included updates to the confidentiality wording regarding information collected from insurers, revisions to the guidance for potential requests for unaudited consolidating financial statements, to instead first leverage the ORSA report, and clarifications to potential additional detail by legal entity. Ultimately the changes were adopted and forwarded to the Financial Analysis Handbook Working Group for its consideration.

The comments relating to the changes proposed to the supervisory college section of the Financial Analysis Handbook were more substantive, and ultimately the working group directed the staff to propose additional changes based on the feedback. Industry group members agreed to work with staff to

draft new wording in light of the comments provided. Subsequent to this process, the changes will be re-exposed at a future date.

Private Equity Issues Working Group

The working group met via conference call on February 17, and voted to expose for comment through March 11 its proposed changes to the Financial Analysis Handbook, which represents guidance in reviewing Form A applications. This change would create a new section of the Handbook to aid analysts in evaluating risks associated with a change in control. While discussions in previous meetings by this working group focused on private equity acquirers, the risks are more broadly applicable, and therefore the section would not be restricted solely to private equity acquirers. The section provides guidance in considering nine risks in evaluating a change in control: credit, market, pricing/underwriting, reserving, liquidity, operational, legal, strategic and reputational.

At the Spring Meeting, the working group discussed the one comment letter received, which supported the exposure with some minor editing. The working group voted unanimously to adopt the proposed amendments to the Handbook, and refer them to the Financial Analysis Handbook Working Group.

International Insurance Relations Committee

IAIS Draft Insurance Capital Standard
The committee met via conference call on February 13 to discuss their draft comments to the exposed IAIS 169 questions associated with its proposed insurance capital standard. During the call, the committee approved the submission of its comments to the IAIS. Key issues highlighted in the consultation document include: 1) testing of "GAAP plus adjustments" valuation, for which the NAIC, Federal Reserve and FIO will assist the IAIS with developing a suitable methodology; 2) ability of capital requirements to address most material risks with appropriate charges; and 3) definitions and tiering of capital, which the U.S. broadly opposes. The NAIC responded to 66 of the 169 questions in its 18 page comment letter.

IAIS Stakeholder Meeting
On February 5 in Rome, the IAIS held its first stakeholder meeting after changing its approach to limiting the meetings to which stakeholders could participate—a move that has been criticized by the NAIC and many interested parties as a step in the wrong direction. Regulator and interested party reaction to the IAIS meeting reflected a lukewarm response, as many expressed desire for more transparency and interaction. Several noted that the meeting was focused on extracting stakeholder reaction for specific agenda topics, rather than having an open discussion on ICS.

Many interested parties as well as regulators voiced their concern over the lack of transparency to an IAIS representative at the meeting. The committee reiterated its position voiced in previous national meetings and urged the IAIS to commit to open meeting structures, similar to that of the NAIC.

Update on the Joint Forum
The committee heard an update on the Joint Forum, which was dissolved following its final meeting in Basel, Switzerland March 31-April 1. Superintendent Lawsky expressed his view, shared with other Joint Forum members that he did not think the forum should wind down as it facilitated useful cross-sector discussion.

ComFrame Development and Analysis Working Group

The working group met December 30 and at the Spring National Meeting. They also held regulator to regulator sessions in January and March.

ComFrame
The IAIS has been developing ComFrame with the goal of creating an integrated framework for group-wide supervision of IAIGs. The working group received an update on the field testing of ComFrame. Qualitative field testing is underway, and the first round of questionnaires, focusing on group structure and corporate governance, were received from 14 IAIG volunteers and group supervisors. A high level summary of the responses was provided, noting ComFrame environments are largely in place for the respondents. The next phase of qualitative testing, focusing on group-wide risk management, is in process with a mid-April due date. The second round of quantitative testing is due by the end of April. Quantitative testing will begin in April and be due in June.

International Capital Standard
The working group heard an update on the field testing process of the IAIS's proposed International Capital Standard for IAIGs, which is on a very compressed timeline. The first deliverable of the capital requirements is a factor-based model entitled the Basic Capital Requirement (BCR), which was endorsed by the G-20 in 2014. Refinements are expected to be made to the model based on the

results of field testing being performed through June. The second component of the capital standard relates to the Higher Loss Absorbency (HLA) requirement. The HLA is expected to be completed by year end 2015, and will be subject to a similar quantitative testing process that the BCR is currently undergoing. Quantitative testing is expected to be performed through 2016. Overall the IAIS has set steps to finalizing the ICS in incremental timeframes, which indicates a slower pace than initially planned. It is expected ICS would replace BCR and HLA, for globally systemically important insurers. The comment period for the ICS consultation document ended February 16; refer to the International Insurance Relations Committee for further discussion.

NAIC position statements on ComFrame and Capital
The NAIC's draft position statement on ComFrame has two over-arching messages: the NAIC would support ComFrame if it enhances supervision of IAIGs; however it would oppose ComFrame if requirements are duplicative of those that exist in the U.S. or the existing IAIS ICPs. Flexibility, rather than a prescriptive approach, in allowing an IAIG to develop its corporate governance, ERM and ORSA is stressed throughout. It also references some of the positions in the ICS paper, discussed in the next paragraph.

The draft position statement paper on ICS was shared at the Spring National Meeting, and the NAIC has committed to working alongside the IAIS to evaluate the cost/benefit and compatibility of this group-wide capital requirement with the existing U.S. legal entity capital requirements, i.e. RBC. The paper points to the flaws in producing a single uniform capital standard, similar to the methodology pursued with the banking industry, as the business models of the two industries are significantly different. It stresses ICS will be in addition to the RBC requirements that currently exist, as the development and application of ICS will not substitute RBC, as the former applies group-wide and the latter at a legal entity level. It also raised concerns on the proposed timeline in developing the global group capital standard, and states the "GAAP plus adjustments" valuation approach should be explored for ICS. The position paper specifically would not support the market adjusted approach as the sole approach for ICS valuation. Lastly, it notes the HLA should not be applied to insurers not designated as systemically important.

Interested parties asked, and the working group approved, a short exposure period on the position statements. Comments from interested parties have now been received subsequent to the Spring National Meeting and the working group is planning to have a call by the end of April to discuss.

Development of a Domestic Group Capital Standard
During its December 30 conference call, the working group heard a summary of 10 comment letters received from interested parties regarding the development of a U.S. Group Capital Methodology that had been exposed for comment at the Fall National Meeting. The comments included preferences between a factor-based, cash flow or hybrid approach, capital resources and the ongoing need for collaboration with the Federal Reserve and FIO. The approaches discussed were the "RBC Plus" methodology, the Cash Flow methodology, and a hybrid approach of the two. During the Fall National Meeting, reactions from interested parties had been mixed, with non-life interested parties broadly supportive of the RBC Plus approach and life interested parties supportive of the Cash Flow approach.

With the first ICS consultation complete, the working group will now be focusing again on the NAIC conceptual framework proposal and hopes to have a revised document for discussion before the Summer National Meeting.

Financial Stability Task Force

The chair opened the meeting with an update of the current developments of the IAIS. The next round of G-SII data collection is expected to be launched in April, to which 15 of the 50 insurers subject to this testing are from the U.S., including AIG, MetLife and Prudential Financial.

FSOC
Commissioner Hamm provided the Financial Stability Oversight Council update. FSOC, a council within the Department of the Treasury, is charged with identifying risks and responding to emerging threats to financial stability, and Commissioner Hamm serves in a non-voting, advisory capacity to the council. He noted that MetLife has contested, both written and orally, FSOC's consideration to be designated a financially systemic institution; however FSOC voted 9 to 1 in favor of the designation. The one who opposed was Roy Woodall, who is the independent member with insurance expertise. Commissioner Hamm noted his opposition to the designation during the FSOC meeting as well. He elaborated during the Spring National Meeting that he believes there to be confusion by FSOC members in the following areas: an understanding of the NAIC regulatory requirements, the regulatory intervention associated with liquidity requirements and insolvency, lack of

qualitative assessments associated with the G-SIFI designation (i.e. size is most important requirement), and impossible burden of proof relating to plausibility of events that could cause an insolvency. He also expressed his concerns that FSOC has not provided insight as to how a company would be de-designated as financially systemic. He stated FSOC should provide the company with guidance as to what the risks are and how they could be mitigated.

IAIS Resolution Working Group
The task force received an update on the discussions held by the IAIS Resolution Working Group (ReWG) and its applicability to insurers. The total loss-absorbing capacity (TLAC) was discussed, specifically with respect to the concept of retaining additional capital somewhere in the holding company structure. The concept is somewhat of a "bail-in," whereby this excess capital within the structure would be redeployed to an aspect of the organization in need. Questions remain in ReWG as to where to house the additional capital and what is the appropriate amount. While TLAC will be applicable to systemically important banks and discussions focus on this, the differences associated with its application to systemically important insurers are still being assessed. During the meeting, members of the task force reiterated the differences between banks and insurers, and interested parties expressed interest in when the IAIS will expose TLAC for comment.

Reinsurance Task Force

The task force met in February and at the Spring National Meeting and discussed the following projects in process.

Reinsurance Modernization Implementation
The task force received an update on the adoption of the revised Credit for Reinsurance Models by the states, noting that 26 states have passed the legislation, which represents more than 60% of U.S. direct premium, with two additional pending signatures by the respective governors. Eleven additional states have confirmed that they plan to adopt the models in 2015, which would bring the total to 93% of U.S. direct premium. With respect to the certification of reinsurers, the chair reported that more than 30 reinsurers remain certified by various states. Whether these revisions should be accreditation standards was discussed again by the Financial Regulation Standards and Accreditation Committee at the Spring National Meeting; see that summary for further details.

Covered Agreements
During the Spring National Meeting, several interested parties spoke in support of covered agreements. A covered agreement is between U.S. and a foreign jurisidiction that would establish a level of protection to insurers and reinsurers that would be substantially equivalent to state law, and could preempt state law under certain circumstances. The agreement could be negotiated by the FIO and the U.S. Trade Association with foreign regulators. Speakers noted current barriers to entry in Poland and the Netherlands, and expect further barriers in other European nations once Solvency II is adopted on January 1, 2016. However, the NAIC previously published an Issue Brief on its website outlining additional concerns and questions regarding the need for such agreements, and is therefore not convinced they are necessary.

Report of Reinsurance FAWG
During its December 30th regulator-to-regulator conference call, the Reinsurance Financial Analysis Working Group approved the renewal of five certified reinsurers, approved one new certified reinsurer and withdrew certification of another.

During the Spring National Meeting, the chair commented that in his view the passporting process (the ability for a certified reinsurer to passport into other states based on its initial certification) is not being applied as consistency as he had hoped, which is an issue he wants to explore in 2015. He also encouraged all states to apply the passporting process consistently to avoid the need for a covered agreement with the EU.

Report of the XXX/AXXX Captive Reinsurance Regulation Drafting Group
The group met twice in March in regulator to regulator sessions to discuss a first draft of the XXX/AXXX Model Regulation, which it hopes to expose for comment by the Summer National Meeting. The proposed model will establish reinsurance requirements for transactions subject to AG 48.

NAIC Bank List
The SVO was asked to assess whether non-banks, in addition to banks, should be considered qualified U.S. financial institutions, per the Credit for Reinsurance Models. In the SVO referral paper discussed at the Spring National Meeting, the SVO concluded that the non-banks are regulated at an equivalent level as banks. As a result, the task force adopted a recommendation asking the SVO to expand the NAIC Bank List to include non-banks as qualified U.S. financial institutions, when the specified requirements are met. This will allow LOCs issued by qualified non-bank institutions to be an

accepted form of reinsurance collateral. The task force recommended that the SVO develop criteria on LOC issuer applications to allow for the inclusion of qualified non-banks.

SVO Listed Securities
At the request of the task force, the SVO did exhaustive research to determine the intent of the phrase "Securities Listed by the SVO," which allows those securities to be used as collateral in the Credit for Reinsurance Models. At the Spring National Meeting the SVO proposed, and the task force recommended moving forward with amendments to the Purposes and Procedures Manual of the NAIC Investment Analysis Office to expand the definition and delineate between an investment security, and a "regulatory transaction," or a funding solution to a company/state-specific regulatory issue. These regulatory transaction securities have been discussed in previous conference calls as "bespoke" securities (custom structured securities, often affiliated) that have state practices that differ from NAIC practices. The recommendation would allow investment securities to be listed as acceptable collateral, while regulatory transactions would not.

The task force also discussed amending the definition of a security to include sub-listings that would "permit the identification of populations of securities deemed eligible for use as collateral in reinsurance transactions beyond the population of insurer owned securities the SVO compiles and publishes." In turn, these securities may therefore be acceptable for the Credit for Reinsurance Models. The task force recommended the Valuation of Securities Task Force to move forward with these amendments.

Response to FIO
NAIC leadership received a letter from the FIO requesting them to describe "the impact of Part II of the federal Nonadmitted and Reinsurance Reform Act of 2010 on their ability to access reinsurance information for regulated companies in their jurisdictions." The NAIC received comments from its members and is preparing a response.

Blanks Working Group

At the Spring National Meeting, the working group adopted two blanks proposals as final. The adopted proposals, 2014-19BWG and 2014-20BWG, clarify terminology and correct inconsistencies and are not considered material changes. The proposals are effective for 2015 annual statement reporting. Eighteen blanks proposals were exposed for a public comment period which ends May 29. These proposals will be considered for adoption on a conference call to be scheduled in June. The more significant proposals, which would be effective for 2015 annual statements, include the following and would:

- Modify the Supplemental Health Care Exhibit and instructions to eliminate the Aggregate 2% Rule Column for Parts 1 and 2 and replace it with a column to capture Medicare Advantage Part C Plans and Medicare Part D Stand Alone Plans, which are no longer excluded by statute (2015-02BWG).

- Move the definitions for all property and casualty lines of business to the Appendix of the property rather than defining them within the instructions for specific schedules. It would also add definitions for lines of business included in the Property Product Matrix but not currently included in the property instructions (2015-03BWG).

- Revise instructions to clarify the reporting of Health Care Receivables within the Underwriting and Investment Expense Exhibit (2015-05BWG).

- Modify the instructions for Schedule A, Part 1 to reflect the reporting of real estate owned by an LLC on Schedule A if it meets the requirements set forth in SSAP 40R, Real Estate Investments (2015-07BWG).

- Modify the Cash Flow instructions to include cash transactions to reflect changes adopted by SAPWG for SSAP 69, Statement of Cash Flows (2015-08BWG).

- Add a new supplement to collect data on cybersecurity insurance coverage to assist the Cybersecurity Task Force in its charge. (2015-13BWG).

- Modify instructions to Schedule D to enable additional security identifiers (SEDOL code and ISIN Identification) to be included (2015-14BWG).

- Add a new supplement to include details about reinsurers aggregated on Schedule F. This proposal reflects a compromise adopted by SAPG that will allow companies to aggregate asbestos and pollution reinsurers on Schedule F if certain criteria identified in paragraphs SSAP 62R are met. The new supplement will be a public document (2015-16BWG).

- Split the Supplemental XXX/AXXX Reinsurance Exhibit, Part 2 into to two new parts (2015-18BWG). See further discussion in the PBR Implementation Task Force summary.

The working group discussed comments received from interested parties on a previously exposed Corporate Governance Working Group memo requesting a review of possible reporting redundancies between the Corporate Governance annual filing and the annual statement filing. Interested parties requested that the memo be referred to the Risk-Focused Surveillance Working Group for further consideration as that group has recently taken on a new charge to identify and eliminate redundant efforts in collecting and reviewing insurer information related to financial analysis and examination activities for solvency monitoring purposes. The working group agreed with the interested party recommendation and referred the matter to the Risk-Focused Surveillance Working Group.

The task force also received comments that the NAIC Supplemental Health Care Exhibit is not in the identical format as the U.S. Department of Health and Human Services medical loss ratio (MLR) reporting form used to calculate the actual MLR rebates to be paid. It was observed that there are significant reporting differences between the two forms and that they serve different purposes so consistency should not be expected. During its April 17 conference call, the Health Care Solvency Impact Subgroup exposed for comment a "cautionary statement" documenting that the SHCE is "not meant to represent or replicate the MLR calculated by HHS/CMS in its MLR reporting form for actual rebate purposes."

Investment Reporting Subgroup
The subgroup last met via conference call on December 9. This subgroup's objective to reduce the number of Schedule BA categories has been deferred pending the SAP Working Group's consideration of items reported on Schedule BA within the larger investment classification review project.

Governance Review Task Force

Subsequent to the Fall National Meeting, the National Association of Corporate Directors was appointed the consultant to review the NAIC's governing documents, organizational structure, management and decision-making processes and recommend improvements to enhance the NAIC's ability to support and improve state regulation. NACD provided an update of their process, which to date has focused on surveying and interviewing members of the NAIC. The NACD expects to issue a draft report to the working group in the next 4-6 weeks, which will be discussed during the Summer National Meeting if not sooner.

Unclaimed Life Insurance Benefits Working Group

At the Spring National Meeting the working group received approval from Executive Committee and Plenary to proceed with a model Unclaimed Life Insurance Benefits Act, which would "require all authorized insurers regulated by the state's insurance department to undertake good faith efforts, as to be specified in the Act, to locate and pay beneficiaries proceeds under unclaimed life insurance policies, annuity contracts, and retained asset accounts issued in the state or remit such proceeds as unclaimed property to the appropriate jurisdiction if the beneficiaries are unable to be located or paid."

The working group held a public hearing in Phoenix to hear comments from stakeholders on whether the National Conference of Insurance Legislators' (NCOIL) Model Unclaimed Life Insurance Benefits Act should be used as a starting point for developing the NAIC model. The working group heard comments from industry and insurers who expressed a strong need for a model; they also raised issues, such as requiring the use of the Social Security Death Master File, discussed at length during 2013-2014, as the NAIC debated whether to develop a model. The chair noted that some have suggested that the starting point for a model should be the Illinois version of the Unclaimed Life Insurance Benefits Act introduced into the Illinois Senate in 2014 (but not yet adopted), as opposed to the NCOIL model. No policy conclusions were reached in Phoenix, but the working group did appoint a subgroup to develop the model. The following states have already committed to participate in the subgroup: CA, FL, LA, NE, NY and WI. A conference call is expected to be scheduled shortly.

At the Fall National Meeting, the working group had approved sending a comment letter to the Uniform Law Commission's Drafting Committee to Revise the Uniform Unclaimed Property Act (which is part of the National Commission on Uniform State Law) to inform the Committee of its recommendation to develop a NAIC model and to ask that the Committee not revise the *Uniform Unclaimed Property Act* because it would create the dual regulation of life insurers. The letter was not sent last fall as the NAIC thought the deadline for

commenting had passed; an interested party asked whether that was really the case. NAIC staff will follow up to determine whether comments are still being accepted.

Life Insurance and Annuities Committee

Life Insurance Buyer's Guide
The committee met in Phoenix and discussed its 2015 charge to revise the Life Insurance Buyer's Guide, which was last updated in 2005. The chair asked whether the drafters might be "better off starting from scratch since the current guide is so outdated." The committee voted to form a working group to take on the project; Florida and Iowa volunteered as the first two members.

Life Actuarial Task Force

During the day and a half dedicated to the LATF meeting, once again the lengthiest discussion and the most well attended was that regarding development of an actuarial guideline for Indexed Universal Life Illustrations. This topic and other highlights from discussions since the Fall National Meeting are summarized below.

Indexed UL Illustration Guidance
IUL products are not included in the current Illustration Model Regulation and regulators and some industry representatives are concerned that a few companies are illustrating these products with extremely favorable investment returns. Over the past year there has been much discussion by LATF and other industry groups regarding illustrations for IUL products, including consideration of different actuarial guidelines proposed by the ACLI, the "Coalition" of companies supporting an alternative guideline to that proposed by the ACLI, and input from other industry groups and interested parties. During the Spring National Meeting, LATF members, ACLI representatives, "Coalition" company representatives and other interested parties discussed the proposed "compromise" actuarial guideline for application of the *Life Insurance Illustrations Model Regulation* to indexed universal life contract illustrations. The current draft guideline is a compromise between proposals submitted by three industry groups. The draft guideline was previously exposed during the interim period. In Phoenix, the task force and interested parties discussed edits in response to comments on the previously exposed draft and made further edits, culminating in the exposure of the current draft for public comment through April 14 and subsequent adoption on April 16.
The draft guideline defines the crediting rates to be used in the illustrations, the earned rates for the disciplined current scale, the exhibits to be included in the illustrations, and also limits the loan leverage that can be shown in an illustration. Additional consumer information (side-by-side illustration and additional disclosures) prescribed by this guideline is intended to aid in consumer understanding of the range of results inherent in indexed products.

The guidance limiting the Illustrated Scale crediting rate and the Disciplined Scale earned rate would be effective for all new business and in-force life insurance illustrations on policies sold on or after September 1, 2015, and the guidance limiting the illustrated rate credited to the loan balance and requiring additional exhibits and disclosures would be effective for all new business and in-force life insurance illustrations on policies sold on or after March 1, 2016. The delayed effective date for including the additional information and disclosures allows time for companies to revise illustrations and consider new product designs.

Comments during the April 16 call on the re-exposed draft focused on language added during the Spring National Meeting, which some regulators, the ACLI, the AAA, and other interested parties thought was confusing and subject to misinterpretation. In particular, language intended to clarify the requirements for illustrated account charges and for a table showing actual historic index changes and corresponding hypothetical credited interest rates was omitted from the adopted draft. For purposes of expediency, LATF opted to adopt the draft guideline without further clarifications and these issues will be addressed at a later date. A section on professional responsibility was also omitted from the adopted draft, considering that professionalism is addressed in other applicable guidance and has broader application than one actuarial guideline. Regulators from NY and CT opposed the adoption. The guideline must also be approved by the Life Insurance and Annuities Committee and then Executive Committee and Plenary for final adoption.

As of the publication date of this Newsletter, the newly adopted guideline has not yet been posted to the LATF webpage, but should be available shortly.

PBR Valuation Manual and Related Matters

Small Company Exemption

See the PBR Implementation Task Force summary for discussion of the small company exemption, which was adopted by the NAIC in Phoenix.

Commercial Mortgage Asset Ratings

Asset modeling in VM-20 is predicated on the use of an asset rating to determine default assumptions. Commercial mortgages are currently not included in the rating categories defined for modeling in VM-20; however the Life RBC instructions contain a method to assign commercial mortgages to risk classes. The ACLI presented a proposal allowing commercial mortgages to be used in VM-20 modeling with PBR risk classes assigned based upon the relationship between NAIC commercial mortgage rating categories and current AVR and RBC factors. LATF voted to expose the proposal until April 28.

VM "Top 10" Items

LATF discussed other items that must be completed for incorporation into the Valuation Manual before the operative date, also known as the "VM Top 10" list. Items discussed include the need for a smoothing mechanism to address reserve volatility, and VM-31 documentation requirements, and the definitions of products subject to the VM-20 Net Premium Reserve calculation. Discussion included input from the ACLI recommending changes to the VM-31 actuarial report requirements and emphasizing the need for a reserve smoothing mechanism. No specific action was taken on these items and considering that the earliest possible operative date is now assumed to be January 1, 2017, it appears completion of these items may extend beyond spring 2015.

VM-20 Spread Tables

At the 2014 Fall National Meeting, LATF discussed and exposed for comment the recommended VM-20 current and long-term investment spread tables as of September 30, 2014. Under this framework separate spreads are provided for investment costs and default costs based on source data from vendors J.P. Morgan and Bank of America; default costs will be updated annually while investment spread costs will be updated quarterly. During the interim period LATF adopted the exposed spread tables and also exposed spread tables updated as of December 31, 2014. During the Spring National Meeting LATF adopted the VM-20 spread tables as of December 31, 2014. Because PBR is not yet effective, the VM-20 spread tables currently apply only to testing under Actuarial Guideline 38.

Academy Council on Professionalism

LATF received an update from the American Academy of Actuaries Council on Professionalism. The chair of the Academy Committee on Qualifications, discussed the Academy's recommendations regarding qualification standards and statements of opinion for actuaries pertaining to principles-based reserves. The standard on statements of actuarial opinion addresses basic credentialing requirements. The standard would be modified if the NAIC requires that the opinion be signed by an FSA. The Council does not intend to create a specific standard for the qualification of an actuary to sign a PBR statement of opinion as the existing standards sufficiently cover PBR requirements. Statements of opinion regarding principles-based reserves will be incorporated into the broader statement of actuarial opinion for the annual statement.

LATF also heard a report from Patricia Matson, Chairperson of the Actuarial Standards Board (ASB). Ms. Matson reported that many comments were received on the Modeling Actuarial Standard of Practice (ASOP) for which the second draft was exposed through March 1. This standard will be broad reaching in the profession. The ASB will discuss this standard further this summer. ASOP 21, *Responding to or Assisting Auditors or Examiners in Connection with Financial Statements for All Practice Areas,* is being updated to reflect NAIC changes, especially those pertaining to risk-focused exams. The comment period for the second draft of the ASOP on PBR for Life Products closed in December 2014 and the final ASOP will be forthcoming. Ms. Matson also announced that the ASB launched a new website and mobile app enabling easier viewing of ASOPs. Attention at the meeting was immediately interrupted as attendees rushed to download the app.

Actuarial Guideline XXXIII (AG 33)

LATF continues to work on changes to the proposed AG 33 language, targeting implementation by year-end 2015. Just prior to the Spring National Meeting, LATF re-exposed proposed changes to AG 33 with ACLI edits included. The proposed changes address the incidence rates to be used in determining the greatest present value of integrated benefit streams for annuities with elective and non-elective benefits. In particular, incidence rates for other than mortality-based non-elective benefits are restricted where financial incentives exist for contractholders to forego non-elective benefits in favor of higher elective benefits. However, it is unclear how financial incentives would be determined.

The original effective date of AG 33 was December 31, 1998 and industry concern regarding retrospective application back to 1998 of the proposed changes was expressed with a belief that asset adequacy testing is sufficient to cover concerns associated with reserve levels for existing policies. In addition, industry concern was expressed that the new changes require period by period comparison of benefits which was not contemplated by the original AG 33 drafting. In its current form, significant valuation system changes would be required if the amendments are adopted. The changes will have an impact on product pricing as well. No motion was made pertaining to the re-exposed guideline. A follow-up call will be scheduled prior to the Summer National Meeting.

VM-22 Fixed Annuity PBR

LATF received a report from the VM-22 Subgroup on work related to development of PBR methodology for non-variable annuities. Three potential reserving methods were proposed: a) replicate VM-20, b) representative scenario method (RSM), and c) modernized Standard Valuation Law formulas. The subgroup presented pros and cons of each method along with "scoring" of each method. The RSM involves generating scenarios for each key risk driver and assigning probability weights to each scenario. The Kansas Field Test surrounding the feasibility of the RSM approach has been completed and will be shared at a future VM-22 Subgroup call. The field test results are consistent with the Academy work on this matter. Higher reserves emerge under scenarios reflecting greater risk. Potential changes to the SVL formulas focus on stable value funds, fixed annuities with guaranteed living benefits, and improvement in the SVL valuation interest rate formulas. Next steps are to validate the RSM, seek public input on the feasible options, and identify and propose solutions to weaknesses in the current SVL. No timeframe was provided for completion of these tasks.

Aggregate Margins

The Aggregate Margins Subgroup reported on activity during the interim period. This subgroup's work parallels that of the Academy's Aggregate Margin Task Force. The subgroup is interested in right-sizing margins in order to achieve right sizing of reserves, with a focus on implicit versus explicit margins. The subgroup has narrowed its focus from seven methods down to two methods – a cost of capital method and the percentile margin method. The cost of capital method is generally favored. With data now available to analyse, the subgroup looked at how aggregate margins developed for term insurance and the run-off of reserves. Their report included comparisons of 10, 20, and 30 year term insurance reserves modeled under several different methods varying in terms of margins reflected, lapse assumptions, reflection of mortality improvement, and capitalization of deferred acquisition expenses.

Valuation Mortality Tables

LATF received a status report from the Society of Actuaries & Academy Joint Project Oversight Group on the development of the 2014 Valuation Basic Table (VBT) and the 2017 CSO valuation mortality tables. Following the 2014 Summer National Meeting the 2014 VBT primary tables were exposed for comment. The revised 2014 VBT tables reflect comments received, monotonicity checks, and finalized preferred wear-off patterns consistent with the 2008 VBT. The Relative Risk tables are also ready for exposure and reflect the range of expected mortality from super preferred to residual standard risk classes. LATF voted to expose the 2014 VBT, projected forward to 2015, and the associated relative risk tables for 45 days. The 2015 VBT tables could possibly be used for AG 38 by year-end if adopted at the Summer National Meeting in August.

A considerable amount of time was spent discussing development of the 2017 CSO mortality table margins and preferred risk structures. The presentation included comparisons of reserves under the 2001 CSO, 2017 unloaded CSO, and the loaded CSO tables for different issue ages, gender, and risk class. Mortality improvement is reflected to 2017 (vs. 2014) so that the mortality rates coincide with the expected PBR effective date. The proposed tables reflect LATF guidance for margins to cover 70%-79% of claims experience from contributing companies, and this equates to a margin of approximately 15%.

With the preferred risk mortality table structure created, the SOA is conducting an impact study of the margins in the 2014 VBT and 2017 CSO tables on VM-20 statutory reserves, tax reserves, non-forfeiture values, and Internal Revenue Code section 7702 requirements. Eleven companies have volunteered to participate. A range of products including IUL, UL, Term, ULSG, and IUL with secondary guarantees are being tested. Results are expected to be ready for the SOA Life & Annuity Symposium in early May with a completed report expected by mid-May. The Joint Project Oversight Group would like to see results of the impact study before recommending variations in the margins for the three preferred classes and before exposing the CSO tables, to avoid re-exposure. A LATF call will be scheduled to provide the Joint Project Oversight

Group with conceptual feedback on the structure of the 2017 CSO mortality table loading, the approach to development of preferred structure tables (basic and loaded), and the timing for exposure.
The proposed VBT and CSO tables are available for review on the SOA website.

Synthetic GIC Model Regulation
At the 2014 Fall National Meeting the Deposit Fund Subgroup of the Academy Annuity Reserves Work Group presented proposed revisions to the *Synthetic Guaranteed Investment Contracts Model Regulation* (#695) to address a mismatch between asset and liability valuations with these products which creates unnecessary volatility in statutory financial results, particularly in low interest environments. The proposed changes were exposed for comment at that time and subsequently adopted by LATF during an interim conference call. The adopted changes include a discount rate methodology that is responsive to all economic environments, strengthening of pooled fund contracts, additional requirements in the Actuarial Memorandum and increased transparency in the Plan of Operation.

Contingent Deferred Annuity Subgroup
The CDA Subgroup presented recommended changes to the *Standard Nonforfeiture Law for Individual Deferred Annuities* (Model #805) to exempt CDAs from sections 3-8 while granting Commissioners authority prospectively to require nonforfeiture benefits for CDAs. LATF voted to expose the proposed changes until May 13. The subgroup also exposed for comment proposed changes to the *Synthetic Guaranteed Investment Contracts Model Regulation* (#695) until April 28 to clarify that CDAs are not within the scope of the synthetic GIC model.

Emerging Actuarial Issues Working Group

The working group was formed by the NAIC to address implementation issues resulting from the revisions to AG 38 for universal life products with secondary guarantees.

At the Spring National Meeting, the working group voted to re-expose an interpretation regarding the basis for determining the pre-funding ratio as defined in Section 8E, and also exposed an alternative interpretation for the same matter. The interpretations are intended to address challenges in determining the pre-funding ratio when multiple sets of charges and credits apply to the policies. The substance of both responses is essentially the same, but the re-exposed interpretation, if adopted, would apply to policies issued July 1, 2015 and later while the alternative interpretation would apply to policies issued January 1, 2016 and later. The interpretations were exposed until April 20.

During the interim period the working group adopted an interpretation related to the applicability of Section 8D to reinsurance assumed and the use of hypothetical portfolios for testing the gross reserves. The interpretation directs that Section 8D does apply to reinsurance assumed on risks in scope, and provides guidance regarding use of hypothetical portfolios for testing AG 38-8D business ceded under a direct coinsurance arrangement. The interpretation also provides linkage between AG 38 and VM-20, noting that the ceding company, in calculating the pre-reinsurance ceded reserve or gross reserve required by AG 38 Section 8D, must assure that such modeling and assumptions are appropriate as provided by VM-20 Section 8.D.2.

Submitted questions, exposed responses and adopted interpretations are available on the working group's webpage.

PBR Review Working Group

At the 2014 Summer National Meeting, proposed revisions to the Blanks and instructions pertaining to VM-20 (i.e. the VM-20 Supplement) were exposed for public comment. At this meeting the PBR Blanks Reporting Subgroup presented a revised version of the proposed changes which incorporates public comments. The PBR Implementation Review Working Group voted to expose the subgroup's recommended changes to the VM-20 Supplement until May 29.

The PBR Company Outreach Group provided a status report on their work on the three projects that are underway. First, the group is finalizing the results of a 38 company survey completed in 2014 regarding PBR readiness. A final report summarizing the survey results is expected to be released this June. Second, the outreach group is working with the SOA and four subject matter experts to develop PBR durable education components, which will be housed on the Society of Actuaries website and available for anyone to access at any time. A Net Premium Reserve education deck will be ready by June. These education materials are considered durable in that they will always be kept up to date. Third, the outreach group plans to kick off a project

to gather information from volunteer companies and volunteer regulators pertaining to the PBR implementation process, as opposed to the PBR reserve impact which has been studied previously. This project is scheduled to kick off in June 2015 and last approximately one year.

The PBR Implementation Review Working Group is seeking vendors to provide software models to assist states on PBR financial exam reviews. The working group anticipates having a vendor selected by the end of 2015 with the software in place at the end of 2016.

Health Actuarial Task Force

Long-Term Care
The Society of Actuaries reported progress on its study of LTC claims terminations, incidence and utilization. The study covers exposures in years 2000-2011 and the goal of the study is to develop experience-based tables that reflect a variety of differences in policyholder and benefit characteristics. The research group also plans to develop a database of LTC experience data to facilitate user access of specific data for individual company modeling needs and analysis. Predictive modeling is being used to develop expected incidence rates based on a variety of "predictors," such as age, elimination period, etc. The experience tables, including Excel based models, and the companion report are expected to be completed by the end of April.

The LTC Actuarial Working Group received a progress report from the Long Term Care Pricing Subgroup on changes to the *NAIC Guidance Manual for Rating Aspects of the Long-Term Care Insurance Model Regulation* (the "Manual") to assist in implementation of changes to the *Long-Term Care Insurance Model Regulation* (#641) that were adopted in 2014. The subgroup held fourteen conference calls during the interim period to discuss changes to the Manual, culminating in exposure of draft changes on February 24, with comments accepted through March 24.

The changes include an assumption template intended to create uniform reporting of rating assumptions used in long-term care insurance initial rate filings and rate increase filings, a checklist of items for inclusion in all actuarial memoranda for LTC policies, sample actuarial certifications for initial and rate increase filings, and expanded or modified Question and Answer items. Changes to the draft manual also include a placeholder to incorporate content related to consumer disclosures. Confidentiality of the information in the assumption template generated some controversy in the interim calls; language was added to the draft noting responsibilities of both the company and regulatory actuaries to ensure confidentiality when warranted. The subgroup will address comments on the draft during the coming weeks.

Health Reform Solvency Impact Subgroup

The subgroup met April 6 and April 17 to discuss ACA projects in process.

SHCE 3Rs Disclosure
During its April 17 conference call the subgroup exposed for comment proposed changes to the Supplemental Health Care Exhibit to add a table to capture 3R receivables, payables and receipts by state for individual and small group plans. Amounts reported in the exhibit are expected to be consistent with the related annual statement Note 24F. The comment period ends May 15 and the subgroup hopes to make the changes effective for 2015 SHCE reporting.

SCHE Part 2
During its April 17 conference call the subgroup exposed for comment instructions to the Supplemental Health Care Exhibit Part 2 to clarify the reporting for retrospectively rated contracts. The comment period ends May 15 and the subgroup hopes to make these changes effective for 2015.

Risk Corridor Receivables
During its April 6 conference call, the chair of the Blanks Working Group commented that for 2014 year-end financial statements there have been questions as to whether large risk corridor receivables would be recoverable. He also noted that regulators will likely see variances in accounting and reporting for the risk corridor.

Contingent Deferred Annuity Working Group

The CDA Working Group continues its consideration of several projects with respect to the regulation of contingent deferred annuities. At the Spring National Meeting, the working group reviewed a March 24 draft *Guidance for the Financial Solvency and Market Conduct Regulation of Insurers Who Offer Contingent Deferred Annuities*. The guidance

document is intended to serve as a reference for states interested in modifying their annuity laws to clarify their applicability to CDAs. It sets forth what consumer protection and financial solvency model laws and regulations should be applied to CDAs. The working group is waiting for other NAIC groups to develop a risk management checklist, reserve requirements, and capital requirements for CDAs. Once these items have been completed, the guidance document will be updated further and re-expose for an additional public comment period.

In response to concerns raised by the Center for Economic Justice at the previous meetings, the working group continues to consider whether a nonforfeiture benefit should be applicable to CDAs. At the Fall National Meeting, the working group noted a clear consensus that it favors some form of nonforfeiture benefit, and requested that industry propose some options. In Phoenix, the working group heard a presentation from IRI and ACLI which discussed several potential alternatives that might be appropriate in the event that a CDA is cancelled by either the policyholder or the insurer. These alternatives include replacing the CDA with another annuity (such as Single Premium Deferred Annuity or a Deferred Income Annuity) or providing a lump sum distribution determined as the present value of future guaranteed income. IRI and ACLI representatives encouraged the working group to allow flexibility in the market rather than being overly prescriptive to allow some continued product innovation. No conclusions were reached by the working group with respect to any specific nonforfeiture or cancelation benefit.

Financial Regulation Standards and Accreditation Committee

The committee met in Phoenix and took the following actions. Comments are due on exposed items by May 4.

Definition of Multi-State Insurer
At the 2014 Spring National Meeting, the committee exposed proposed changes to Part A and Part B of the accreditation standards definition of "multi-state insurer" which has been a very controversial issue. Under the proposed definition, a multi-state reinsurer is an insurer assuming business that is directly written in more than one state and/or in any state other than its state of domicile. Captive insurers owned by non-insurance entities for the management of their own risk would continue to be exempted. Under the original proposal, all other captive insurers, special purpose vehicles and other entities assuming business in states other than their state of domicile would be subject to the accreditation standards under this proposal. Since that time, the committee has received 85 comment letters over two exposure periods strongly opposing the proposal due to the overly broad nature of the proposed revisions and the potential unintended consequences. As discussed at the Fall National Meeting, the revised approach is for NAIC staff to draft new versions of the Part A and Part B Preambles which would include in the scope of the Accreditation Program only four types of entities: captive insurers and special purpose vehicles that assume business written in accordance with 1) Regulation XXX, 2) Regulation AXXX, 3) variable annuities valued under *Actuarial Guidelines XLIII—CARVM for Variable Annuities* (AG 43), and 4) long-term care insurance valued under the *Health Insurance Reserves Model Regulation*. The NAIC is in the process of hiring people with expertise in these areas and is hoping to expose recommendations "quickly."

The committee has scheduled a conference call for May 26 to discuss proposed amendments to the Preamble to scope in these four types of entities. The proposed revisions are expected to be exposed for comment by April 24.

The ACLI expressed concerns related to the proposal to scope in variable annuity captives and the related complexities of those transactions; they recommended that existing VA captives be grandfathered. Superintendent Torti noted that the Financial Condition (E) Committee is also looking at VA and LTC captives; a regulator from Delaware suggested that F Committee defer a final decision until E Committee concludes its work. See the Financial Condition Committee summary for further discussion of VA captives.

Exposure of Possible Additions to Part A Standards
The committee voted to expose for comment three possible additions to the Part A Accreditations Standards:

- The newly adopted *Corporate Governance Annual Disclosure Model Act* (#305) and the *Corporate Governance Annual Disclosure Model Regulation* (#306)
- 2014 revisions to the *Annual Financial Reporting Model Regulation* (#205) related to internal audit function requirements
- 2014 revisions to the *Insurance Holding Company System Regulatory Act* (#440) related to group-wide supervision of internationally active insurance groups.

2010 Holding Company Model Revisions
The committee heard an update on the adoption of the 2010 revisions to the *Insurance Holding Company System Model Act* (#440) and *Regulation* (#450). As of March 1, forty-two jurisdictions have enacted the revisions to the model act in full or in part, with seven more states in the process of adoption. The 2010 revisions are required for accreditation purposes as of January 1, 2016, so the remaining accredited jurisdictions will need to adopt the revisions during 2015.

ORSA Model Act
At the 2013 Summer National Meeting, the committee exposed for a one year comment period a proposal to include the Risk Management and ORSA Model Act as an addition to the Part A Accreditation Standards. Prior to the 2015 Spring National Meeting, the committee received a comment letter from seven major trade associations highlighting an issue related to confidentiality of company information included in the ORSA filings that has arisen as states have begun to adopt the new model act. The committee heard comments that five states have adopted the ORSA model with weakened confidentiality provisions and an additional 5-6 states have introduced similar legislation. The trade associations are requesting that the committee replace the substantially similar confidentiality provisions included in April 7, 2013 referral memo with 11 "protections" of company information which should be considered significant elements. The goal of the trade associations' request is to require states to adopt confidentiality language that provides the same level of protection as provided in Section 8 of the ORSA Model Act. The committee will consider this issue further at the Summer National Meeting.

Referral from FAWG
The committee adopted, effective immediately, a referral from Financial Analysis Working Group to add Review Team Guidelines to the Part B Accreditation Standards that require states to perform analysis procedures for domestic insurers which cede to captive insurers or special purpose vehicles business written in accordance with Regulations XXX and AXXX.

States' Adoptions of Certified Reinsurer Revisions
The committee discussed the Credit for Reinsurance revisions related to certified reinsurers, which are currently optional for accreditation purposes. Industry representatives again raised the issue of problems with non-conformity, i.e. if one state doesn't adopt the certified reinsurer provisions, then an insurer is required to obtain full collateral for all business when those policies are ceded to a pool which includes the state not adopting the changes. Superintendent Joseph Torti of RI noted that he has changed his mind on this issue and agrees including the certified reinsurer provisions as a requirement for accreditation "makes a lot of sense." The committee agreed to discuss the issue at future meetings.

Sharing Economy Working Group

TNC White Paper
Since the Fall National Meeting, the Sharing Economy Working Group has been busy working on its white paper *Transportation Network Company (TNC) Insurance Principles for Legislators and Regulators*. The purpose of the white paper is to outline insurance principles that would be a guide for state and local policymakers when adopting laws or regulations regarding these services. TNCs are organizations that arrange transportation for a fee using a technology platform such as mobile application or website. The three most widely used TNCs are UberX, Lyft and Sidecar.

The working group met by conference call in December, January and March to review the white paper outline and drafts and heard presentations from industry groups and state regulators from California, Rhode Island and Colorado. On January 21, the working group exposed its draft white paper. Twelve comment letters comprising 84 comments were reviewed in detail by the chair and NAIC staff. A second draft of the white paper and a detailed spreadsheet summarizing all comments received, whether accepted, rejected or modified, were circulated to the working group and discussed on March 5. A majority of the comments received were incorporated into the second draft. Following the March 5 conference call, the white paper was revised to include a state requirement for TNCs and TNC drivers to notify the drivers' personal auto insurers when they sign up to be a TNC driver. The white paper was adopted at the Spring National Meeting by the working group with a few additional revisions. One significant revision was to acknowledge the TNC Insurance Model Bill. Refer below for a summary of the model bill.

Traditional ride-sharing, also known as carpooling, is covered by most personal auto policies (PAPs); however, transporting passengers for a fee that exceeds the simple sharing of expenses is excluded in most PAPs. Personal auto insurers are concerned that they are experiencing losses from additional exposures because their policyholders do not inform them that they drive for TNCs.

The white paper addresses common exclusions used by personal auto insurers, identifies the various insurance options to fill any gaps in coverage, discusses the coverages carried by the largest TNCs and emphasizes the importance for cooperation in claims handling between multiple insurers. Additionally, it explains the elements of disclosure necessary to inform consumers and the general population about the fundamental risks of TNC activities and the insurance coverage options available to insure against those risks. The appendix to the white paper contains a compendium of city ordinances and state legislation enacted to establish insurance requirements for TNCs. California, Colorado, District of Columbia, Illinois, and Virginia have enacted TNC legislation and the remaining states are in various stages of legislative activity.

Following the adoption by the working group, the white paper was adopted by the Property and Casualty Insurance Committee and the Executive Committee and Plenary in Phoenix and is posted to the working group's webpage.

TNC Model Bill

As state regulators focused on the white paper, a group of TNCs, personal auto insurers and trade organizations worked to develop the TNC Insurance Compromise Model Bill in support of their commitment to eliminate consumer confusion, provide a framework for safe transportation options and support continued marketplace innovation. The document is not an NAIC Model, but it is hoped that it will bring clarity and consistency to TNC insurance laws. The model is similar to the bill passed in Colorado and the pending compromise bill in New Mexico. The bill permits personal auto policies to exclude coverage for TNC activities and mandates certain coverage levels similar to those enacted in states that have passed TNC laws. The bill requires TNC drivers to carry proof of TNC insurance coverage and TNCs must disclose to their drivers that their current personal auto policy may not provide any coverage for TNC-related driving. The bill grants a statutory right of contribution against TNCs for claims insurers may have erroneously paid. The bill was issued on March 26 and additional revisions will be considered this spring and summer.

Workers' Compensation Issues

The working group heard a presentation by a trade organization on workers' compensation issues related to TNC activities. One key issue is the classification of the drivers as employees versus independent contractors. The primary factor in determining whether the individual is an employee or independent contractor is the measure of control the company has over the individual and the product or service he or she provides. Taxi drivers are typically classified as employees when the taxi company provides the vehicle. Alaska, Massachusetts and Virginia specifically exclude taxi drivers from workers' compensation laws. There are still many questions regarding the difference between taxi drivers and TNC drivers, as well as the appropriate classification codes for TNC drivers. No action was taken by the working group on this issue.

Casualty Actuarial and Statistical Task Force

The task force met by conference call on January 13 and March 14, and met in Phoenix to discuss the following issues.

Price Optimization

On January 13, the task force discussed a draft outline of the price optimization white paper prepared by NAIC staff based upon regulatory discussions, presentations and materials from the NAIC's Auto Insurance Study Group. The task force discussed a distinction between predictive modeling, to get indicated rating factors, and prescriptive modeling, to seek to maximize profit and prescribe certain constraints. It was noted that the distinction might be helpful to limit the scope of the paper. One distinction is that price optimization focuses on the final or selected rating factors, whereas predictive modeling focuses on determination of the indication.

Price optimization is part of a complex modeling process. The chair noted ratemaking is the actuarial exercise to determine the best estimate (including development of loss costs and associated expenses, rating plan, discounts, etc.). The sometimes separate exercise of what price the company should charge has become more sophisticated using price optimization models. The task force discussed whether a distinction can be made between the two processes since price optimization is being used for ratemaking. A task force member responded that ratemaking and price optimization can be separated, although it will be difficult to divorce the two into ratemaking and price optimization processes; the reason being an actuary has always been allowed a certain level of judgment in the proposed rates. It was further noted that an actuary should not be turned into a robot and the task force needs to allow some judgment. The problem is how to define what aspects of price optimization are acceptable to regulators and which are not.

In Phoenix, the task force reviewed the draft white paper. The paper notes that a 2013 Earnix survey of 78 major insurers found that 45% of large insurance companies (with gross written premiums over $1 billion) in North America currently use price

optimization techniques, with an additional 29% of all companies reporting they plan to adopt this technique in the future. The paper discusses recent activity by state regulators in regulating price optimization, noting that Maryland, Ohio and California have recently issued guidance defining price optimization and requiring insurers to end such practices. The New York Department of Financial Services sent a letter to property/casualty insurers defining and declaring such practices as inconsistent with traditional cost-based rating approaches and could be unfairly discriminatory. The Department is seeking to determine whether insurers use price optimization in New York and required insurers to answer the Department's specific rating questions by April 15.

The paper includes seven options for regulatory responses as identified by the task force:

1) Don't allow price optimization or a particular component of price optimization.
2) Modify or add specificity to what is required to be included in rate filings.
3) In a rate regulatory review, ensure all rating factors are disclosed and filed.
4) Define appropriate constraints on the price optimization process and outcomes.
5) Identify potential changes to market conduct exams.
6) Regulators should be sufficiently familiar with how a particular insurer's model works and the accuracy and appropriateness of input data in order to make an informed determination regarding the key issues of excessive, inadequate or unfairly discriminatory rates.
7) Allow price optimization to the extent allowed by law.

Undrafted sections in the paper include best practices/principles identified by the task force and recommendations and next steps. Following the discussion in Phoenix, the task force exposed the white paper for comment; the comment period ended April 16.

ASB Ratemaking Standard
In September 2014, the Actuarial Standards Board exposed the proposed Actuarial Standard of Practice, Property/Casualty Ratemaking for public comment. On January 13, the task force discussed a draft response letter compiled based on comments submitted by its members. The letter noted that it is not clear how the ASOP would apply to regulatory actuaries in their review of rate filings submitted by insurers for insurance department review and approval. Other comments included suggestions on the ratemaking process. Following the discussion, the task force adopted the letter for submission to ASB.

SOA General Insurance Educational Track
The task force continued discussion of its charge to evaluate the Society of Actuaries' new general insurance educational track and whether actuaries meeting those requirements should be permitted to sign actuarial opinions for NAIC property/casualty annual statements. On March 14, the task force discussed the way forward for an independent study of the educational track. The chair provided an outline of the roles and responsibilities for the coordinator, content reviewer and exam reviewer. All individuals involved in the review process will be unbiased and independent of the SOA and the task force. The review will be funded by the SOA and the task force will oversee the review activities. Concerns were raised that the process as documented in the outline needs to be more independent. Thus, the draft will be revised. The chair stated that he does not expect the independent review to be completed by July 1 and may consider asking for more time from the parent committee. The chair will work on drafting a recommendation which will be circulated in the next call.

Risk-Focused Surveillance Working Group

The working group met by conference call on February 17, held an e-vote on March 10 and met in Phoenix to discuss the following topics.

Handbook Redundancy Revisions
In 2014, the working group had requested public comments on areas of redundancy within the U.S. solvency monitoring system. Comments were discussed during a December 16 conference call as summarized in the PwC NAIC Fall 2014 Newsletter. Many of the comments were related to redundancies that occur when financial examiners and analysts request information from a company that the state insurance department already has available. The NAIC staff was asked to develop some proposed revisions to the Financial Condition Examiners Handbook and the Financial Analysis Handbook encouraging additional communication between the two functions to discourage the submission of redundant information requests. Proposed revisions were discussed on February 17 and the working group exposed the revisions for comment through March 19.

In Phoenix, the working group discussed four comment letters received from Indiana, Wisconsin and two industry groups. Wisconsin raised concerns that the proposed guidance, in particular the

proposed change to the time when the examiners and analysts should meet and coordinate, may result in regulators needing to make substantial changes in current processes. In their view, these changes, when compared to current processes, may result in regulatory inefficiencies and cause delays in the examination process. After comments were heard, the working group requested that NAIC staff modify the proposed revisions reflecting comments from both regulators and interested parties. The working group will continue its discussion in a future meeting.

Accreditation Part B Revisions
The working group had spent a considerable amount of time and effort in 2014 to develop revisions to the Insurer Profile Summary template and related guidance for the purpose of improving the communication between the analysis and examination functions and between the states in relation to solvency risks and concerns facing insurers. As a result of the revisions, regulators are required to incorporate branded risk assessments into their Insurer Profile Summary documents this year. Throughout January, the working group oversaw the presentation of four webinar sessions to train regulators on the proper use of the new Insurer Profile Summary template and related guidance. However, the NAIC has not yet adopted revisions to the accreditation review team guidelines to explain how compliance with the new guidance will be reviewed and enforced. As such, the NAIC staff was asked to develop proposed revisions to the Part B accreditation standards to incorporate the new Insurer Profile Summary Guidance.

On February 17, the working group received an update on the revisions which attempt to provide consistency between the guidelines required for financial analysis and financial examination functions in sharing, receiving and utilizing information from each other. In addition, the revisions clarify the content required to be included in the Insurer Profile Summary. Following the discussion, the working group exposed the revisions for comment, which were adopted March 10 as a referral to the Financial Regulation Standards and Accreditation Committee recommending revisions to the Part B Accreditation Standards.

Group Profile Summary
In Phoenix, the working group discussed proposed changes to the Holding Company Analysis Checklist resulting from the incorporation of the Group Profile Summary template. The working group then exposed the template and related guidance for a comment period ending May 29.

Insurance Department Qualifications Project
The working group received an update on progress made on developing job descriptions encompassing the qualifications and skills necessary for financial analysts and examiners to be successful in performing risk-focused surveillance. Steve Johnson (PA) responded with candid comments that obtaining this expertise will be one of the biggest challenges the state-based system will face because the "skill set versus salary imbalance will catch up with us" alluding to the fact that sufficient state resources are difficult to obtain due to budget cuts and other pressures.

Climate Change and Global Warming Working Group

In Phoenix, the working group heard a presentation from Munich Re America on its multifaceted climate strategy and recent mitigation activities. As a supporter of climate change study, Munich Re founded two organizations: 1) Geo Risks Research was established in 1974 to collect events and loss data on natural hazards worldwide, and 2) NatCatSERVICE focuses on loss events with property and/or personal damages. Approximately 800 to 1,000 loss events are analyzed each year with a focus on economic, insured, humanitarian losses and their regional breakdown. There are currently more than 35,000 events stored in the database which is the basis for internal risk assessment in addition to providing detailed information to different stakeholders and in support of scientific research. Munich Re's position on climate change is that it is real; drivers include both natural (i.e. cyclic) and anthropogenic (increasing greenhouse gas emissions). The presentation included detail on Munich Re's projections for North America in the following areas: specific climate stresses, agriculture and food security, wildfire risk, tree mortality and forest infestation, human health risks, effects on transportation, and construction and housing.

The working group also heard a presentation from Ceres on briefing materials it has developed to educate financial examiners on how climate risks and opportunities affect insurer solvency. The focus on climate change for examiners began in 2013 when the NAIC revised the Financial Condition Examiners Handbook by incorporating three risk mitigation/ control strategies directly tied to climate change. The risk considerations included within underwriting and investing, are that the insurer has not established and maintained appropriate risk exposure limits, has not established sufficient pricing practices, resulting in inadequate or excessive premium rates in relation to its assumed risks and expense structure and/or the insurer's

investment portfolio and strategy are not appropriately structured to support its on-going business plan.

Pilot training sessions, instructed by Ceres, were held in February and March in Los Angeles and Seattle. Participant feedback on the training was positive with participants confirming they found the training valuable. Upcoming training by Ceres will be held at the NAIC Financial Summit Leadership Initiatives in May and at the Society of Financial Examiners Career Development Seminar in July.

Mortgage Guaranty Insurance Working Group

The working group held a conference call March 10 and met in Phoenix to discuss progress on its three main projects as discussed below.

Model Act and Standards Manual
Since the Fall National Meeting, the working group has continued making revisions to the M*ortgage Guaranty Insurance Model Act* (#630) and exposed the fourth version of the proposed model in February. A second draft of the 61-page Mortgage Guaranty Insurance Standards Manual, which will be referenced in the model act, was also exposed for comment. In Phoenix, a trade association noted it needs more time to accumulate and submit comments to the working group. As a result, the working group agreed to post the model act and manual on its website and will continue accepting comments until April 30. The working group also discussed that additional edits are needed for the reinsurance section which may result in changes to other sections of the model act and manual. In terms of timeline, the working group discussed an ambitious goal of finalizing the model act and manual by the Summer National Meeting, which the chair noted "may not be likely."

Capital Model
The working group heard a presentation from Oliver Wyman on the mortgage guaranty capital model, including details on the loan-level model results, development approach and proposed grids, RBC results and next steps. Wisconsin reported that it is conducting an inquiry concerning the development and design of the capital model and met with several states on February 27 to establish a set of questions regarding the capital model. The working group intends to hold a public meeting during each development phase of the capital model to facilitate public comment and the capital model will be made available for testing by interested party prior to its adoption.

Terrorism Insurance Implementation Working Group

The working group met via conference call six times during December and January as it monitored federal efforts to extend the Terrorism Risk Insurance Act (TRIA). Congress failed to pass a new bill before TRIA expired on December 31, 2014; however, the House and Senate ultimately passed extensions on January 7 and January 8, respectively. The bill (TRIA2015) was signed into law by President Obama on January 12. With the passage of TRIA2015, the working group shifted its attention to updating the model bulletin that describes the reauthorization and filing procedures. The bulletin was distributed to all states at the end of January.

In Phoenix, the working group discussed provisions related to data collection requirements contained within TRIA2015. The working group agreed to seek industry opinion on the data elements and meet via conference call to discuss the matter further.

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The next National Meeting of the NAIC will be held in Chicago August 14-17. We welcome your comments regarding issues raised in this newsletter. Please provide your comments or email address changes to your PricewaterhouseCoopers LLP engagement team, or directly to the NAIC Meeting Notes editor at jean.connolly@us.pwc.com.

Disclaimer

Since a variety of viewpoints and issues are discussed at task force and committee meetings taking place at the NAIC meetings, and because not all task forces and committees provide copies of agenda material to industry observers at the meetings, it is often difficult to characterize all of the conclusions reached. The items included in this Newsletter may differ from the formal task force or committee meeting minutes.

In addition, the NAIC operates through a hierarchy of subcommittees, task forces and committees. Decisions of a task force may be modified or overturned at a later meeting of the appropriate higher-level committee. Although we make every effort to accurately report the results of meetings we observe and to follow issues through to their conclusion at senior committee level, no assurance can be given that the items reported on in this Newsletter represent the ultimate decisions of the NAIC. Final actions of the NAIC are taken only by the entire membership of the NAIC meeting in Plenary session.

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