EXAMINATION OVERSIGHT (E) TASK FORCE

Draft: 9/25/09

Examination Oversight (E) Task Force
Washington, DC
September 22, 2009

The Examination Oversight (E) Task Force met in Washington, DC, Sept. 22, 2009. The following Task Force members participated: Mary Jo Hudson, Chair, represented by Bill Harrington (OH); Ken Ross, Vice Chair, represented by Judy Weaver (MI); Jim L. Ridling represented by Richard Ford (AL); Jay Bradford represented by Mel Anderson (AR); Steve Poizner represented by Al Bottalico (CA); Thomas R. Sullivan represented by William Arfanis (CT); Gennet Purcell represented by Kevin Brown (DC); Karen Weldin Stewart represented by Linda Sizemore (DE); J.P. Schmidt represented by Dwight Hamamura (HI); Susan E. Voss represented by Jim Armstrong (IA); William W. Deal represented by Georgia Siehl (ID); Michael T. McRaith represented by Jim Hanson (IL); Carol Cutter represented by Connie Ridinger (IN); Sandy Praeger represented by Ken Abitz (KS); Sharon P. Clark represented by David Hurt (KY); Ralph S. Tyler, III, represented by Les Schott (MD); Glenn Wilson represented by Jaki Gardner (MN); John Huff represented by Fred Heese (MO); Wayne Goodwin represented by Tony Riddick (NC); Ann Frohman represented by Jim Nixon (NE); Roger A. Sevigny represented by Tom Burke (NH); Scott J. Kipper represented by Jackie Rambardo (NV); James J. Wrynn represented by Larry Levine (NY); Kim Holland represented by Chris Van Ess (OK); Teresa Miller represented by Russell Latham (OR); Joel Ario represented by Steve Johnson (PA); Leslie A. Newman represented by Mark Jaquish (TN); Alfred W. Gross represented by Doug Stolte (VA); Paulette Thabault represented by Pete Raymond (VT); Mike Kreidler represented by Patrick McNaughton (WA); Sean Dilweg represented by Roger Peterson (WI); and Ken Vines represented by Linda Johnson (WY).

1. Discuss Model #385 Survey Results

Mr. Harrington stated that in September 2008, the NAIC membership adopted revisions to the Model Regulation to Define Standards and Commissioner's Authority for Companies Deemed to be in Hazardous Financial Condition (#385). These revisions provide additional standards to determine whether the continued operation of any insurer might be deemed to be hazardous to its policyholders, creditors or the general public. In addition, the revisions give the commissioner additional authority to issue an order requiring companies deemed to be in hazardous financial condition to take corrective action. As requested by the Executive (EX) Committee, a survey is updated quarterly to track the states' progress in adopting the revisions. Bruce Jenson (NAIC) presented the results of the survey, stating that two states have adopted the revisions, 30 states plan to adopt the revisions, eight states plan to adopt the revisions with minor changes, three states do not plan to adopt the revisions, six states are undecided and two states did not provide a response. Of the states that plan to adopt the revisions, nine states plan to complete the adoption in 2009, 12 in 2010, four in 2011 and 19 do not yet have a timeline for adoption. No states have indicated that problems are anticipated in adopting the model revisions. NAIC staff will continue to update this survey on a quarterly basis, and the results will be discussed at each national meeting.

2. Adoption of Examiner Salaries for 2010

Mr. Harrington said that because Ohio bases much of its examiner compensation on the NAIC recommended rates, he has asked Mr. McNaughton to oversee the examiner salary recommendations to avoid any conflict of interest in this area. Mr. McNaughton said the Task Force is charged with recommending salary rate adjustments on an annual basis. This year, the Task Force asked NAIC staff to review changes in the Consumer Price Index (CPI) and report them to the Task Force for purposes of setting recommended rates for 2010. The Task Force reviewed a report prepared by NAIC staff on this topic and noted that the CPI had decreased from the previous year. Based on this information, Mr. McNaughton proposed no changes to the recommended examiners salaries for 2010. On a motion from Mr. Abitz, seconded by Mr. Johnson, the Task Force adopted no changes to the examiner salary recommendations for 2010.

3. Adoption of 2010 Charges

Mr. Harrington presented the proposed charges for the Task Force and its groups for 2010. The only changes for 2010 include the reorganization of charges related to the coordination of analysis and examination efforts of holding company groups. New charges have been added to the Financial Analysis Handbook Working Group and the Financial Examiners Coordination Working Group to emphasize the importance of coordinating work of holding company groups in these areas. In addition, the charge to oversee the Lead State Summary Report has been moved back up to the Task Force level to reflect the importance of this issue. On a motion from Mr. Peterson, seconded by Ms. Weaver, the Task Force adopted the proposed charges for 2010 (Attachment One).

4. Adoption of Working Group Reports

Mr. Harrington asked the Task Force members to review the written reports of the Financial Analysis Handbook Working Group (Attachment Two), Financial Analysis Research and Development Working Group, Financial Examiners Coordination Working Group (Attachment Three), Financial Examiners Handbook Technical Group (Attachment Four) and IT Examination Working Group (Attachment Five) that were included in the materials. On a motion from Mr. Johnson, seconded by Mr. Peterson, the Task Force adopted the reports of its working groups.

Having no further business, the Examination Oversight (E) Task Force adjourned.

W:\Sep09\TF\Examo\09-eotf.doc

2010 PROPOSED CHARGES
EXAMINATION OVERSIGHT (E) TASK FORCE

The mission of the Examination Oversight (E) Task Force is to monitor all aspects of the financial examination process and to identify, investigate and develop solutions to problems related to financial examinations; to monitor and refine the IRIS ratios and the Financial Analysis Solvency Tools, including Company Profiles*,* FAST ratio scoring system and the *Financial Analysis Handbook*; to oversee the Analyst Team Project; to review details of examination surveillance process; to monitor the development of tests for determining when a financial examination of an insurer is necessary; to establish procedures for flow of information between states about troubled companies; to enhance the quality and timeliness of financial examinations and monitor additions to the *Financial Condition Examiners Handbook* covering this area; and to monitor the examination schedules in various states and assist the states in developing methods to maintain current schedules.

Ongoing Support of NAIC Programs, Products or Services:

1. The Examination Oversight Task Force will:

- Provide ongoing maintenance and enhancements to the Form A Database, monitor the usage and encourage state participation.—*Essential*
- Provide input and comments to the International Association of Insurance Supervisors (IAIS) or other related groups on issues regarding international risk-management concepts; coordinate such comments with the International Solvency and Accounting Working Group.—*Important*
- Recommend salary rate adjustments for examiners.—*Essential*
- Provide ongoing maintenance and enhancements to the NAIC Lead State Summary Report tool and encourage coordination with solvency matters.—*Essential*

2. The Analyst Team System Oversight Working Group will:

- Monitor the work performed by the Analyst Team and the progress of any changes made to the Analyst Team Project.—*Essential*

3. The Financial Analysis Research and Development Working Group will:

- Provide ongoing maintenance and enhancements to the automated financial solvency tools developed to assist in monitoring the financial condition of insurance companies. Prioritize analysis and examination efforts to ensure the tools remain reliable and accurate.—*Essential*
- Review current financial analysis solvency tools for life insurance companies, for consideration of risk with reserve liabilities as affected by principle-based reserving standards; make appropriate enhancements as necessary.—*Important*

4. The Financial Analysis Handbook Working Group will:

- Provide ongoing maintenance and enhancements to the NAIC *Financial Analysis Handbook* and related applications for changes to the NAIC annual/quarterly statement blank, as well as coordinate and analyze input received from other state regulators.—*Essential*
- Continue incorporating the assessment of risk and risk management into the financial analysis oversight role.—*Essential*
- Review current guidance in the NAIC *Financial Analysis Handbook* regarding the analysis of reserve liabilities for life insurance companies and make appropriate revisions based on the finalized principle-based reserving standards.—*Important*
- Develop enhancements to the financial analysis process that encourage coordination of analysis activities between states with regard to holding company groups.—*Essential*

5. The Financial Examiners Coordination Working Group will:

- Develop enhancements to the financial examination process that encourage coordination of examination activities between states with regard to holding company groups.—*Essential*

- Provide ongoing maintenance and enhancements to the Examination Tracking System (ETS). The Working Group also will provide reports to the Examination Oversight Task Force regarding usage of ETS, including examination and coordination statistics.—*Essential*

6. The Financial Examiners Handbook Technical Group will:

- Continue incorporating the assessment of risk and risk management into the financial solvency oversight role.—*Essential*

- Continually review the NAIC *Financial Condition Examiners Handbook* and revise, as appropriate.—*Essential*

- Review annually the examination procedures included within the NAIC *Financial Condition Examiners Handbook* for updates in response to revisions to the NAIC *Accounting Practices and Procedures Manual.—Essential*

- Continually review the Annual Financial Reporting Model Regulation (#205) and revise the NAIC *Financial Condition Examiners Handbook*, as appropriate.—*Essential*

- Monitor the implementation of the revised risk-assessment process by receiving feedback, conducting training courses and performing ongoing maintenance — as well as developing additional guidance and exhibits within the NAIC *Financial Condition Examiners Handbook* as needed to assist examiners in completing financial condition examinations.—*Important*

- Review current guidance in the NAIC *Financial Condition Examiners Handbook* regarding the examination of reserve liabilities for life insurance companies and recommend appropriate revisions based on the finalized principle-based reserving standards.—*Important*

7. The IT Examination Working Group will:

- Monitor state usage of automated examination tools (ACL and TeamMate), technology changes and emerging issues in order to re-evaluate examination processes and keep states abreast of the latest tools, techniques and training.—*Essential*

- Enhance current training opportunities for auditing tools and techniques: IT Examination, Introductory ACL, Advanced ACL and TeamMate. Continue offering on-site training programs to states upon request.—*Important*

- Continually review and revise, as needed, the Examination of Computer-Based Operations and Exhibit C — Evaluation of Controls in Information Technology sections of the *NAIC Financial Condition Examiners Handbook.—Essential*

- Develop and maintain tools that will be part of the more complete IT examination process.—*Important*

W:\Sep09\TF\Examo\Attachment One.doc

Draft: 9/11/09

Financial Analysis Handbook (E) Working Group
Conference Call
Aug. 27, 2009

The Financial Analysis Handbook (E) Working Group of the Examination Oversight (E) Task Force met via conference call Aug. 27, 2009. The following Working Group members participated: Roger Peterson, Chair (WI); Steve Ostlund (AL); Kurt Regner (AZ); Louis Quan (CA); Dave Lonchar (DE); James Lawrence (DC); Tom Lurkins (IL); Neil Miller (MD); Judy Weaver (MI); Thomas Burke (NH); Russell Jones (NJ); Dennis Fernez (NY); Annette Boyce (OR); Will Smith (PA); and Jack Broccoli (RI). Also participating were: Janice Gordon (DC); Debbie Doggett (MO); and Kashik Patel (PA).

1. Consider Enhancements to the 2009 Edition of the NAIC *Financial Analysis Handbook*

Jane Koenigsman (NAIC) summarized a proposed enhancement to include text in the audit opinion chapter analyst reference guide of the NAIC *Financial Analysis Handbook* to highlight the upcoming changes related to the Annual Financial Reporting Model Regulation (#215) — commonly referred to as the Model Audit Rule — that are effective Jan. 1, 2010, and a new procedure to verify that the insurer has established an audit committee in compliance with state laws. Mr. Peterson asked what data point would be available in the annual statement blank for an analyst to confirm that an audit committee had been established, or whether the expectation would be that analysts would contact each insurer. Bruce Jenson (NAIC) said that no data point has been built into the annual statement or the audit report; instead, the requirement is built into the model. Mr. Burke said that the information should be in a general interrogatory, but that it appears to be an examination function. Mr. Lawrence said that he agrees it is an examination function; however, if analysts are to be responsible for ensuring compliance, it would be easier to include it in an interrogatory. Mr. Peterson agreed that an interrogatory would be the best approach. He said that this is a significant component of the Model Audit Rule, and the states would want to ensure that insurers are in compliance. Mr. Lawrence asked if there was a statement or certification that could be sent from the board of directors to the audit firm. Ms. Doggett said that this information is available to analysts in Missouri through the review of the insurer's bylaws and the articles of incorporation, if there is an audit committee authorized in the bylaws. Mr. Peterson said that, for most large insurers in Wisconsin, bylaws are not required to be filed. Ms. Boyce said that bylaws are not required to be filed in Oregon. Ms. Doggett said that bylaws are not required in Missouri, either, but there is an interrogatory that asks if there have been any changes to corporate documents. When the interrogatory is answered "yes," the analyst follows up with the insurer to ask them about the changes and to request a copy. Mr. Fernez said New York has a list of items to be filed with the annual statement; therefore, if the state wanted to get that question confirmed by the insurer, New York would add it to the list. He added that, because audit committees can be established at the holding company level and down, this checklist is an option to get the information instead of the analyst requesting it from the insurers. Mr. Jenson said that within the Model Audit Rule there is a notification requirement of the election by the insurer to choose its holding company audit committee to act as the legal entity's audit committee, but there is no notification requirement if they have their own audit committee established. Mr. Peterson said that asking the analyst to contact the company is a good thing to do and should not be discouraged; however, it would be easier to refer to a question the insurer answered. Mr. Peterson suggested adding "as necessary" to the question. Ms. Weaver suggested leaving the question as-is and proceeding with a blanks request for a general interrogatory. She said this would become an ongoing dialogue that analysts will have with their insurers in the risk-focused approach. Mr. Peterson agreed with her suggestion. Ms. Weaver suggested NAIC staff send out a reminder to the states. Mr. Peterson noted that this Working Group sponsors training each year on changes to the *Financial Analysis Handbook*, where this topic could be highlighted. A motion was made by Ms. Weaver to accept the proposal and to draft a request to the Blanks Working Group for a general interrogatory for information on the insurer's audit committee. The motion was seconded by Mr. Burke and unanimously adopted. Mr. Peterson added that the interrogatory should ask for the formation of the audit committee in compliance with the Model Audit Rule. Ms. Weaver suggested the question, "Has there been a change in the composition or structure of the audit committee?" Mr. Jensen asked, because the key part of the rule is to determine independence, whether the interrogatory should ask who the members are and which ones are independent. Ms. Weaver said insurers would likely resist that, as they would likely prefer that to be kept confidential. Mr. Peterson suggested the question be left general, such as, "Is the audit committee in compliance with the Model Audit Rule?" Mr. Jensen said with that suggestion, the verification of the audit committee independence is an examination function.

Andrew Daleo (NAIC) summarized a proposed enhancement requested by the Illinois Department of Insurance to include guidance on non-routine analysis in the Level 1 chapter analyst reference guide to highlight additional analysis that might be performed by state insurance departments. Mr. Peterson said he appreciated this contribution and that it is something that has been implicit in analysis responsibilities. Being explicit about the need for non-routine analysis is a good addition. Ms. Weaver suggested including, under the investment examples, a reference to the SVO Portfolio Analysis Memorandums or other resources that could assist in this process. Mr. Burke said that this text refers to a crisis situation, but a lot of these are procedures that analysts might do on a regular basis — and that limiting this to only situations where there is a crisis is too restrictive. Mr. Peterson said that this is not a checklist and not meant to encompass all the non-routine areas of analysis; these are examples of particular cases. And, he said, when the analyst is aware of risk factors that are outside the typical risks, they consider additional steps to assess those risks. He said that some broader statements about content and the need for non-routine analysis in general could be added to this text as additional language on the investment review, as Ms. Weaver suggested. The Working Group agreed to accept the recommendation with the edits proposed. Mr. Peterson said he would review the edits before the recommendation was released for comment.

Mr. Daleo summarized proposed edits to the Level 1 procedures related to the review of holding company filings that would document communication with other state insurance departments having domestics within the holding company group. In addition, edits were proposed to the holding company analysis procedures and analyst reference guide related to indentifying and communicating with other regulatory bodies that have authority over the group, where their insurer is part of a bank holding company. The Working Group agreed to accept the recommendation without any edits.

Ms. Koenigsman summarized proposed edits to the Level 1 chapter procedure related to review of changes in state statutes and regulations, as proposed by the Pennsylvania Insurance Department. Pennsylvania had recommended edits to the wording of the procedure, as well as a preferred alternative to include the question, "Has the insurer failed to adopt the changes made to the NAIC Annual or Quarterly Statement Instructions and/or the SSAP adopted during the period and/or failed to provide the required information?" Mr. Patel said the purpose of the alternative questions was to provide prompts to look for such changes, such as the new note disclosures on subprime in the past year. Mr. Burke said there are a lot of legal changes each year that might affect the financial statement or market conduct. As such, he said it seems too broad to say "state statutes or regulations." Mr. Peterson suggested adding a limitation in the language for those changes that "impact the insurer's financial reporting or position." He said, other than large changes, it might be difficult to tell if an insurer is following a SSAP change just by looking at the financial statement. Mr. Broccoli said that if he was an analyst, he would need a list of all of the changes to blanks and SSAPs in order to be able to sign off on whether the insurer complied or if it affects the company. He said it is too broad for an analyst to be able to sign off on all of it. As part of the analysis process, the analyst identifies unusual items and verifies that the insurer has reported those in accordance with SSAP and instructions. Ms. Boyce said she was in favor of the minor edits to the existing question, but not in favor of the preferred alternative because it is too broad and an analyst would spend too much time on this question with little significant results for most companies. Mr. Jones suggested the following alternative language: "does the insurer appear to have failed" or "are there indications that the insurer has failed to comply." Mr. Burke said his analysts do not feel they can analyze compliance on SSAPs each year, and this seems more likely an audit function. Mr. Broccoli said the question asks the analyst if they have become aware of all the changes in the annual statement instructions and SSAPs — and, if the answer is "yes," then there is no need for these questions, because the analyst would be looking at those in their normal analysis process. He said there is probably a better way to make the analysts aware of the changes in annual statement instructions and SSAPs. Mr. Peterson said there is a required amount of information and knowledge that analysts have to have in order to perform their duties, and these are probably not something the analyst is aware of routinely. There are many minor changes to instructions and SSAPs that might not have any impact on the insurer's reporting or position. Mr. Peterson said that adding the language, "impacts the insurer's financial position or reporting," would address materiality. A motion was made by Ms. Burke to accept the proposal for the limited textual changes, with Mr. Peterson's suggested edits. The motion was seconded by Mr. Broccoli and unanimously adopted.

Ms. Koenigsman summarized proposed edits to the automated I-SITE reports that would include indicators for permitted or prescribed practices, amended filings, mergers and acquisitions, and filing under a reporting basis other than SAP. A motion was made by Ms. Weaver to accept the proposal. The motion was seconded by Mr. Lawrence and unanimously adopted.

Mr. Daleo summarized a proposal from the Kansas Insurance Department requesting that when a "yes" response is triggered on an automated handbook procedure, directly below the question the report would display the historical amount for the past five years for the annual *Financial Analysis Handbook* or five quarters for the quarterly *Financial Analysis Handbook*. He said that if this were to be approved by the Working Group, it would need to be phased in over time due to resource constraints. David Vacca (NAIC) said that such large changes impact the resources necessary, not only for development, but also ongoing maintenance of the tool. He requested that if the Working Group were to approve the proposal, that NAIC staff be given time to research and assess the time and resource requirements. Mr. Peterson said there are already charges in this Working Group and the Financial Analysis Research and Development Working Group for the development of fraternal solvency monitoring tools. He said that, in his perspective, the fraternal tools were a higher priority than this proposal. Ms. Gordon said that it might not be necessary to have five years of data for every automated question. Ms. Weaver said that some states do most of their analytical work electronically and have to flip between screens. Ms. Weaver suggested the proposal be tabled for this year. Mr. Peterson directed NAIC staff to evaluate the scope of the request, including which handbook procedures the request would be applicable to, the resource requirements for development and maintenance, and provide him with a summary of staff’s assessment. Upon Mr. Peterson’s review of the assessment the Working Group could then re-address this proposal in possibly January or February 2010

Ms. Koenigsman summarized a proposal to include a procedure for the health RBC trend test in the level two RBC chapter. Mr. Peterson said that, even though the health RBC trend test has not been adopted by all states, it is a good analysis point and a comment to that regard could be included in the analyst reference guide. Mr. Fernez asked that the RBC trend test question also be added to the Level 1 procedures for all editions of the handbook. A motion was made by Mr. Fernez to accept this proposal. The motion was seconded by Mr. Burke and unanimously adopted.

Ms. Koenigsman summarized a referral received from the Accident and Health Working Group of the Life and Health Actuarial Task Force for revisions to the health actuarial opinion chapter, based on recent revisions to the Health Actuarial Opinion Annual Statement Instructions. A comment letter was received from Bill Weller (America’s Health Insurance Plans—AHIP). Mr. Peterson said that comment letters would be addressed on a conference call after all recommended revisions had been released for comment. A motion was made by Mr. Ostlund to receive the referral and release it for comment. The motion was seconded by Ms. Gordon and unanimously adopted.

Ms. Koenigsman said a referral received from the Financial Analysis Working Group to the NAIC officers requesting development of financial solvency tools for fraternal societies was approved by the officers July 29 to be referred to appropriate working groups, including the Financial Analysis Handbook Working Group. She summarized the NAIC staff’s recommendation to begin development with Level 1 chapter procedures and reference guide to be included in the life/A&H edition of the 2009 *Financial Analysis Handbook*. She said that due to resource constraints, automating the Level 1 chapter on I-SITE would not likely occur for annual 2009; however, the text could be included on I-SITE under the utilities function. Mr. Peterson said the intent of the referral was to move analysis tools on fraternal societies in line with what is provide on life insurers. A motion was made by Mr. Burke to receive the referral, accept the recommendation from NAIC staff and charge NAIC staff to begin development of automated Level 1 procedures and corresponding reference guide text. The motion was seconded by Mr. Jones and unanimously adopted.

A motion was made by Ms. Weaver to release for comment the recommendations received and accepted on this call. The motion was seconded by Mr. Burke and unanimously adopted. The exposure draft will be released Aug. 28 for a period of 30 days. Comments are due by Sept. 29.

Having no further business, the Financial Analysis Handbook (E) Working Group adjourned.

W:\Sep09\TF\Examo\Attachment Two.doc

2009 Fall National Meeting
Washington, DC

Financial Examiners Coordination (E) Working Group

Meeting Summary Report

The Financial Examiners Coordination (E) Working Group of the Examination Oversight (E) Task Force did not meet this quarter. However, each of the industry subgroups that report to the Working Group met twice via conference call.

During these meetings, the Health Coordination Subgroup (Attachments Three-A and Three-B), Life Coordination Subgroup (Attachments Three-C and Three-D) and P&C Coordination Subgroup (Attachments Three-E and Three-F):

- Requested feedback from industry members by asking three main questions:
    - How would you define a coordinated financial exam? Do you have any specific expectations from a coordinated financial exam?
    - What are some characteristics or traits of the health companies in your holding company group that might make coordinating exams difficult?
    - Please list the types of information you would expect to provide to a financial examiner to assist them in coordinating the companies in your holding company group and making the exam(s) more efficient. In other words, what company characteristics would you consider if you had to determine how to coordinate the exams for the companies in your holding company group?

  The Health Coordination Subgroup received three comment letters, the Life Coordination Subgroup received nine comment letters and the P&C Coordination Subgroup received seven comment letters.

- Referred a feedback summary document to the Financial Examiners Coordination Working Group for consideration in developing exam coordination guidance for the *Financial Condition Examiners Handbook.*

W:\Sep09\TF\Examo\Attachment Three.doc

Draft: 9/2/09

Health Coordination (E) Subgroup
Conference Call
August 27, 2009

The Health Coordination (E) Subgroup of the Financial Examiners Coordination (E) Working Group of the Examination Oversight (E) Task Force met via conference call Aug. 27, 2009. The following Subgroup members participated: Pat McNaughton, Chair (WA); David Palmer (MD); Fred Heese (MO); and Bill Harrington (OH).

1. Summary of Feedback Received

Mr. McNaughton asked NAIC staff to review the summary document that was created as a result of feedback from the industry. Mike Sindel (NAIC) provided a detailed review of the feedback received. Randi Reichel (America's Health Insurance Plans—AHIP) mentioned that interviews should begin at the legal-entity level and executives at the holding company level should only be interviewed if necessary.

Ms. Reichel mentioned that the feedback letter received from AHIP had additional information that was not included in the summary. Bruce Jenson (NAIC) stated that there was information in the feedback letters that, while important for conducting coordinated exams, was not vital information necessary to determine how examinations of companies in a holding company group should be coordinated. Additional verbiage was added into the feedback summary to explain this.

Joe Zolecki (Blue Cross and Blue Shield Association—BCBSA) stated that once the regulators had the necessary information to determine how to coordinate examinations of companies in holding groups, the regulators would need an efficient way to share the information with other states. He suggested utilizing I-SITE, if possible. He added that the states should share their exam schedules with each other when determining how to coordinate these examinations.

Upon a motion from Mr. Heese, seconded by Mr. Harrington, the Subgroup referred the summary of feedback received document to the Financial Examiners Coordination Working Group.

Having no further business, the Health Coordination (E) Subgroup adjourned.

W:\Sep09\TF\Examo\Attachment Three-A.doc

Draft: 8/19/09

Health Coordination (E) Subgroup
Conference Call
August 5, 2009

The Health Coordination (E) Subgroup of the Financial Examiners Coordination (E) Working Group of the Examination Oversight (E) Task Force met via conference call Aug. 5, 2009. The following Subgroup members participated: Pat McNaughton, Chair (WA); John Reagan (MO); and Dave Cook (OH).

1. Charges of the Subgroup

Mr. McNaughton discussed the three charges of the Subgroup: 1) Understand company expectations and perceptions of what coordinated exams are and should entail; 2) Identify exam coordination issues that are unique to insurers in a particular line of business; and 3) Provide recommendations and improvements to the Financial Examiners Coordination Working Group for additional guidance.

2. Discussion of Examination Coordination

Mr. McNaughton mentioned that coordination of insurers in holding company groups primarily writing health products has been limited in the past because of the single-state nature of these types of companies. He asked for input from industry members on their expectations of coordinating financial exams. Randi Reichel (America's Health Insurance Plans—AHIP) stated that health insurers are supportive of increasing coordination on their exams and that they are committed to the risk-focused process. She added that, although the risk-focused approach takes corporate governance into consideration, her expectations include interviews of corporate-level employees would be performed by one state and utilized by other states as appropriate. She also expects that testing of common functions within a group of insurers (such as a common IT platform) by one state can be utilized by multiple states, if appropriate. Mr. McNaughton mentioned that specific information must be obtained to determine where common functionality exists within holding company groups. Mr. McNaughton asked NAIC staff to develop a request for feedback that industry members could complete and send back to the Subgroup for consideration. The goal of this feedback would be a document that can be sent to a holding company group to assist in determining how coordination should occur. This information request might ask for information on the level of controls within the group, platforms or systems utilized by various entities within the group, or other similar information. Joe Zolecki (BlueCross and BlueShield Association—BCBSA) supported of the idea of an information request to holding company groups to obtain this information to help coordinate financial exams. He also recommended an electronic location for states to store information pertaining to a holding company group, which other regulators could utilize for their exams of insurers in that group. He added that communication between regulators of when exam are occurring is important.

Having no further business, the Health Coordination (E) Subgroup adjourned.

W:\Sep09\TF\Examo\Attachment Three-B.doc

Draft: 8/26/09

Life Coordination (E) Subgroup
Conference Call
August 24, 2009

The Life Coordination (E) Subgroup of the Financial Examiners Coordination (E) Working Group of the Examination Oversight (E) Task Force met via conference call Aug. 24, 2009. The following Subgroup members participated: Bill Harrington, Chair (OH); Jim Hattaway (AL); and Bob Lamberjack (MI). Also participating was: Dave DelBiondo (PA).

1. Summary of Feedback Received

Mr. Harrington asked NAIC staff to review the summary document that was created as a result of feedback from the industry. Mike Sindel (NAIC) provided a detailed review of the feedback received. Susan Lee (ING) asked what happens if holding company groups have multiple lead states. Mr. Harrington and Mr. DelBiondo responded that the majority of groups will have only one lead state. However, there might be certain circumstances in some holding company groups where multiple lead states would make sense, such as with more complex companies. They added that it is a case-by-case basis and if a group has multiple lead states, they might need to work together to determine the exam work for the group. Mr. Harrington mentioned that he would expect a rationale if multiple lead states are necessary.

One of the comments received discussed the five-year exam period that is required by statute in most states. The comment recommended that, in order to facilitate coordinated examinations and align exam scheduling, a one-time exemption of these states' mandatory five-year exam period should be granted to allow the states the ability to get on the same examination schedules as the other domestic states. Bruce Jenson (NAIC) mentioned that a similar recommendation was previously presented to the Financial Regulation Standards and Accreditation (F) Committee, but was ultimately rejected. The Committee recommended, in such an instance, that the state should perform an exam early to coordinate with other states, rather than violate the statutory five year exam period.

Upon a motion from Mr. Lamberjack, seconded by Mr. Hattaway, the Subgroup referred the summary of feedback received document to the Financial Examiners Coordination Working Group.

Having no further business, the Life Coordination (E) Subgroup adjourned.

W:\Sep09\TF\Examo\Attachment Three-C.doc

Draft: 8/5/09

Life Coordination (E) Subgroup
Conference Call
August 3, 2009

The Life Coordination (E) Subgroup of the Financial Examiners Coordination (E) Working Group of the Examination Oversight (E) Task Force met via conference call Aug. 3, 2009. The following Subgroup members participated: Bill Harrington, Chair (OH); Jim Hattaway (AL); Bob Lamberjack (MI); and Russell Jones (NJ).

1. Subgroup Charges

Mr. Harrington discussed the three charges of the Subgroup, which include 1) Understanding company expectations and perceptions of what coordinated exams are and would entail; 2) Identifying exam coordination issues that are unique to insurers in a particular line of business; and 3) Providing recommendations and improvements back to the Financial Examiner Coordination Working Group for additional guidance.

2. Discussion of Examination Coordination

Mr. Harrington mentioned the importance of determining industry expectations of what constitutes a coordinated exam. He added that the Subgroup wants to make sure everyone's understanding of this concept is consistent to make sure the expectations are in line with what is appropriate and possible given the current exam resources.

Mr. Harrington stated that companies that write different lines of business might have unique characteristics or traits that make it challenging to coordinate exams for those companies. He added that the goal of a coordinated exam is to make financial exams more efficient. Mr. Hattaway discussed that companies might utilize the same IT platforms or have similar management; therefore, it might make sense to examine these companies with a coordinated exam.

Michele Trampe (Genworth Financial) mentioned that Genworth typically has several exams being conducted at any one point in time. She added that her previous experiences working for a property/casualty company that pooled business amongst multiple entities showed her the value of working with regulators to organize a coordinated exam instead of many separate exams. She mentioned that it would be helpful to reduce duplication of several different state examiners performing exams in different years on the same internal controls and processes. Sandy Morris (MetLife) supported Ms. Trampe's comments by stating that MetLife is often examined by multiple states in a given year and much of the work performed on each examination appears to be duplicative. Mr. Harrington requested that interested parties provide information to NAIC staff with the goal of creating a document that can be sent to a holding company group to assist in determining how coordination should occur. This information request might ask for information on the level of controls within the group, platforms or systems utilized by various entities within the group, or other similar information.

Having no further business, the Life Coordination (E) Subgroup adjourned.

W:\Sep09\TF\Examo\Attachment Three-D.doc

Draft: 9/2/09

P&C Coordination (E) Subgroup
Conference Call
August 26, 2009

The P&C Coordination (E) Subgroup of the Financial Examiners Coordination (E) Working Group of the Examination Oversight (E) Task Force met via conference call Aug. 26, 2009. The following Subgroup members participated: David Palmer, Chair (MD); Peter Foley (MN); and Bill Harrington (OH).

1. Summary of Feedback Received

Mr. Palmer asked NAIC staff to review the summary document that was created as a result of feedback from the industry. Mike Sindel (NAIC) provided a detailed review of the feedback received. Margaret Dodson (Progressive) recommended that NAIC staff work with those states that are utilizing different information requests to incorporate additional questions or information into the existing planning questionnaire found in the *Financial Condition Examiners Handbook*. Cheryl Davis (Nationwide) clarified that interviews performed by the lead state should be with the executives at the holding company level, to avoid duplication of efforts.

One of the comments discussed the five-year exam period that is required by statute in most states. The comment recommended that, in order to facilitate coordinated examinations and align exam scheduling, a one-time exemption of these states' mandatory five-year exam period should be granted to allow the states the ability to get on the same examination schedules as the other domestic states. Bruce Jenson (NAIC) mentioned that a similar recommendation was previously presented to the Financial Regulation Standards and Accreditation (F) Committee, but was ultimately rejected. The Committee recommended, in such an instance, that the state should perform an exam early to coordinate with other states, rather than violate the statutory five-year exam period.

Bill Sergeant (State Farm) recommended that examiners perform work off-site and share the work performed by utilizing technology whenever possible. Ms. Dodson agreed and asked that all information requests, including logistical requirements for the coordinated examination, be communicated to company personnel well in advance of on-site examination activities.

Upon a motion from Mr. Harrington, seconded by Mr. Foley, the Subgroup referred the summary of feedback received document to the Financial Examiners Coordination Working Group.

Having no further business, the P&C Coordination (E) Subgroup adjourned.

W:\Sep09\TF\Examo\Attachment Three-E.doc

Draft: 8/19/09

P&C Coordination (E) Subgroup
Conference Call
August 4, 2009

The P&C Coordination (E) Subgroup of the Financial Examiners Coordination (E) Working Group of the Examination Oversight (E) Task Force met via conference call Aug. 4, 2009. The following Subgroup members participated: David Palmer, Chair (MD); Peter Foley (MN); and Jeff Ebert (OH).

1. Charges of the Subgroup

Mr. Palmer discussed the three charges of the Subgroup: 1) Understand company expectations and perceptions of what coordinated exams are and should entail; 2) Identify exam-coordination issues that are unique to insurers in a particular line of business; and 3) Provide recommendations and improvements to the Financial Examiners Coordination Working Group for additional guidance.

2. Discussion of Examination Coordination

Mr. Palmer asked interested parties about their expectations of coordinating financial examinations. Bill Boyd (National Association of Mutual Insurance Companies—NAMIC) mentioned that efficiency was an important goal. Bill Sergeant (State Farm) stated that regulators should always attempt to have a coordinated exam of a holding company group and there should be valid reasons why exams are not coordinated. Enya Carter (W.R. Berkley Corp.) added that cost savings, consistency in exams and timing of exams are some expectations of coordination.

Mr. Palmer discussed challenges in coordinating exams for companies primarily writing property/casualty insurance products. Cheryl Davis (Nationwide) mentioned that timing of exams has been an issue with their companies, because not all of the regulators would be prepared to examine the companies at the same time. Mike Sindel (NAIC) added that receiving specific information from insurer personnel can help determine the best way to coordinate financial exams in a holding company group. Therefore, Mr. Palmer asked NAIC staff to develop a request for feedback that industry members could complete and send back to the Subgroup for consideration. The goal of this feedback would be a document that can be sent to a holding company group to assist in determining how coordination should occur. This information request might ask for information on the level of controls within the group, platforms or systems utilized by various entities within the group, or other similar information.

Having no further business, the P&C Coordination (E) Subgroup adjourned.

W:\Sep09\TF\Examo\Attachment Three-F.doc

Drafted: 9/10/09

Financial Examiners Handbook (E) Technical Group
Conference Call
September 10, 2009

The Financial Examiners Handbook (E) Technical Group of the Examination Oversight (E) Task Force met via conference call Sept. 10, 2009. The following Technical Group members participated: Al Bottalico, Chair (CA); Jim Hattaway (AL); Sean O'Donnell (DC); Peter Foley (MN); Jim Nixon (NE); Steve Kerner (NJ); Bill Harrington (OH); Pat McNaughton (WA); and Peter Medley (WI). Also participating was: Fred Thornton (WI).

1. Adoption of Minutes from Aug. 25 Conference Call

Mr. Bottalico mentioned that the Technical Group held a conference call Aug. 25 to discuss a referral from the Credit Default Swap Working Group regarding the current economic crisis. He added that the Technical Group asked NAIC staff to draft guidance on several topics including liquidity risk, fair value and impairment of investments, and accounting estimates for the Technical Group to review.

On a motion from Mr. McNaughton, seconded by Mr. Nixon, the Technical Group adopted the minutes from the Aug. 25 conference call (Attachment Four-A).

2. Referral from the Risk Assessment Implementation Subgroup

Mr. Bottalico explained that the Technical Group received a referral from the Risk Assessment Implementation Subgroup. He stated that, as a result of the survey conducted by the Subgroup that was sent to all chief examiners, there were some concerns regarding exam interviews that warranted a review of the existing guidance in the *Financial Condition Examiners Handbook*. The Subgroup developed additional narrative guidance about information an examiner would like to receive from performing interviews with company personnel. The Subgroup also modified *Exhibit Y – Examination Interviews* to ask clearer and more concise questions that might be of greater benefit to examiners. Larry Lentini (INS Services) provided several minor editorial revisions, which the Technical Group accepted.

On a motion from Mr. Hattaway, seconded by Mr. Kerner, the Technical Group agreed to expose the items, as amended, for a 45-day comment period.

3. RRG Subgroup Update

Mr. McNaughton provided a status report on the RRG Subgroup, which held two conference calls during the past quarter. He said the Subgroup reviewed some of the areas of a risk-focused exam believed to need specific guidance related to risk retention groups (RRG). The main areas considered were exam coordination; corporate governance, including guidance for interviews; consideration of information technology risks; identification and testing of controls; and GAAP/SAP differences — as well as other RRG-specific nuances. The RRG Subgroup asked NAIC staff to create narrative guidance based on the discussion, along with an RRG-specific exam repository.

On a motion from Mr. McNaughton, seconded by Mr. O'Donnell, the Technical Group received the report of the RRG Subgroup.

4. Exposure of Revised Exhibits

Mr. Bottalico mentioned that several exhibits were exposed on the Technical Group's last quarterly conference call. Some of the major changes proposed include combining Exhibits L and N into one exhibit and removing Exhibit O due to duplication with the new exam repositories. Only one comment letter was received during the exposure period. Mr. Bottalico asked Mr. Lentini to present his comment letter to the Technical Group. The Technical Group agreed to several changes to *Exhibit T – Sample Letter of Representation* based on Mr. Lentini's comments.

On a motion from Mr. Harrington, seconded by Mr. Hattaway, the Technical Group adopted several items for inclusion in the Handbook and removed *Exhibit O – Examples of Other Than Financial Reporting Risks*. The items adopted by the Technical Group included *Exhibit B – Examination Planning Questionnaire, Exhibit F – Analytical Review Procedures, Exhibit G –*

Consideration of Fraud, Exhibit H – Insurer Profile Summary, and *Exhibit L – Assessment of Controls* (Attachment Four-B). *Exhibit N – Branded Risk Classifications and Common Activities and Sub-Activities* was combined with Exhibit L.

On a motion from Mr. Nixon, seconded by Mr. Kerner, the Technical Group agreed to expose *Exhibit T – Sample Letter of Representation* for a 45-day comment period.

5. Guidance on Prospective Risks

Mr. Bottalico stated that *Exhibit V – Prospective Risk Assessment* was exposed on the Technical Group's last quarterly conference call, with the original intent of removing this exhibit from the Handbook because the majority of the risks in the exhibit were placed into the examination repositories. Upon additional review, NAIC staff recommended updating the exhibit with general prospective risks that do not necessarily fit into one of the key activities for which the exam repositories were created. NAIC staff proposed an updated exhibit that provides a way to document these general prospective risks and some common areas or categories to consider when identifying prospective risks.

In addition to revamping the exhibit, NAIC staff also revised the narrative guidance on prospective risks in Part 5 of Phase 1 of the risk-focused process. The major changes included clarifying how to document prospective risks and referencing the newly proposed Exhibit V.

On a motion from Mr. Kerner, seconded by Mr. Harrington, the Technical Group agreed to expose the items for a 45-day comment period.

6. New Examination Repository

Mr. Bottalico mentioned that the Risk Assessment Implementation Subgroup referred to the Technical Group an examination repository on the key activity of other liabilities and surplus. He added that the goal for all the exam repositories is to include them in the 2010 Handbook when they are completed and have been exposed and adopted by the Technical Group. Until the repositories are adopted, an electronic version of each completed exam repository is posted on StateNet, to allow examiners access to utilize these new tools.

On a motion from Mr. McNaughton, seconded by Mr. Harrington, the Technical Group agreed to expose the examination repository for a 45-day comment period.

On a motion from Mr. Kerner, seconded by Mr. Hattaway, the Technical Group agreed to include the examination repository online for examiner access.

7. Detailed Review of Examination Repositories

Mr. Bottalico mentioned that, as the Technical Group is nearing the deadline for including guidance in the 2010 Handbook, they need to determine how to review and adopt the examination repositories. He stated that it would be beneficial to conduct an additional detailed review of the repositories prior to adopting them into the 2010 Handbook, because there have not been many comments during the exposure periods. He added that, because these will be replacing the existing repositories, the Technical Group wants to make sure they have received the appropriate attention. Therefore, Mr. Bottalico and NAIC staff discussed several options to complete this review — to include holding a special call or an interim meeting to review the repositories in detail. Unfortunately, the call would have to be quite long to allow enough time to review each of the repositories and, due to budget restrictions, it was thought that an interim meeting would not be the best option either. Mr. Bottalico decided to delegate each of the exam repositories to three members of the Technical Group to perform a detailed review and report back to the Technical Group. The Technical Group will then hold a conference call in October to discuss each of the repositories and what was found during the detailed reviews. Mr. Bottalico suggested that each member utilize their respective department resources to complete the review. He delegated each state three repositories to review and requested that feedback be sent to NAIC staff no later than Oct. 16.

8. Reorganization of Handbook

Mr. Bottalico mentioned that on the last quarterly call, the Technical Group discussed rearranging the Handbook to improve the flow and ease of use. He stated that the reorganization was completed and asked NAIC staff to provide a review of the proposed changes. Jodi Bachelor (NAIC) provided a quick overview of the Handbook reorganization.

On a motion from Mr. Harrington, seconded by Mr. Hattaway, the Technical Group agreed to expose the revisions for a 45-day comment period.

9. Proposed Revisions to Guidance on Affiliated Transactions

Mr. Bottalico mentioned that the section on reviewing affiliated transactions was revised due to the new exam repositories being prepared. Some of the information in this section is repetitive with the related party repository. He added that NAIC staff had recommended removing it from this section.

On a motion from Mr. Kerner, seconded by Mr. Nixon, the Technical Group agreed to expose the item for a 45-day comment period.

Having no further business, the Financial Examiners Handbook (E) Technical Group adjourned.

W:\Sep09\TF\Examo\Attachment Four.doc

Drafted: 8/26/09

Financial Examiners Handbook (E) Technical Group
Conference Call
August 25, 2009

The Financial Examiners Handbook (E) Technical Group of the Examination Oversight (E) Task Force met via conference call Aug. 3, 2009. The following Technical Group members participated: Al Bottalico, Chair (CA); Jim Hattaway (AL); Kevin Brown (DC); Ginny Godek (IL); Connie Ridinger (IN); David Palmer (MD); Peter Foley (MN); Jim Nixon (NE); Jeff Ebert (OH); Pat McNaughton (WA); and Peter Medley (WI).

1. Current Economic Crisis

Mr. Bottalico discussed a referral received from the Credit Default Swap Working Group. The referral included a charge to provide suggestions as to areas where financial regulation could be fortified in response to the current economic crisis. Mr. Bottalico mentioned a document that was created by NAIC staff to review topics related to the economic crisis and whether guidance was currently included in the *Financial Condition Examiners Handbook* (Handbook). Bruce Jenson (NAIC) provided a detailed review of the document, which included topics such as liquidity risks; securities lending; fair value and impairment of investments; fraud risks; enterprise risk management; holding company issues; accounting estimates, including loss reserves; financial reporting; and rating agency issues. As each topic was discussed, the group determined whether guidance should be created for inclusion in the Handbook, an Exam Risk Alert, or neither. Mr. Bottalico asked NAIC staff to create guidance related to these topics for the Technical Group's consideration. Mr. Bottalico clarified that an Exam Risk Alert would be temporary guidance for examiners to utilize based on current issues and would be provided online through StateNet.

Having no further business, the Financial Examiners Handbook (E) Technical Group adjourned.

W:\Sep09\TF\Examo\Attachment Four-A.doc

EXHIBIT B - EXAMINATION PLANNING QUESTIONNAIRE

The Examination Planning Questionnaire contains procedures and questions that are designed to assist the examiner in gathering necessary planning information and obtaining an understanding of the insurer's organization. The examiner or company personnel should complete this questionnaire as early in exam planning as practical. If company personnel complete this exhibit, identification of who completed each request as well as supporting documentation should be provided to the examination team and the responses to this questionnaire should be critically evaluated by the examiner. The substance of the information collected during the completion of this questionnaire should be incorporated into the Examination Planning Memorandum. The questionnaire responses should be considered when identifying the inherent risks of the insurer. They should also impact the planned examination approach, and the nature, timing and extent of examination procedures performed.

All questions should be completely addressed, using additional sheets if necessary.

	COMPLETED BY	SUPPORTING DOCUMENTATION
I. OWNERSHIP AND MANAGEMENT INFLUENCES		
A. Concentration of Ownership 1. Provide documentation explaining.		
a. The concentration of ownership.		
b. The approximate number of shareholders.		
c. Any significant shareholders.		
d. Changes in ownership.		
e. Whether shares are actively traded.		
f. Extent of management's ownership interest.		
B. Board of Directors 1. Provide documentation describing the makeup of the board of directors, including number of directors, affiliations of outside directors, relationship of each director to the organization and number of years as a director. If biographical summaries are available for the directors, these should also be included. Include information on board members who served at any time during the period under examination.		
C. Audit Committee 1. Provide information on the audit committee. This information should include:		

	COMPLETED BY	SUPPORTING DOCUMENTATION
a. The number of members that serve on the committee.		
b. The names of the members of the audit committee that could qualify as a financial expert in that they hold an accounting certification (CPA, CFE, etc) and have previously been employed in a financial oversight role.		
c. The number of members that are not part of company management and do not have business relationships with the company.		
d. How often the committee meets.		
e. Whether each member of the audit committee is a member of the board of directors and considered independent. Independent members are individuals who are not part of company management and who do not have business relationships with the company.		
f. Whether the audit committee has an established charter. If so, provide a copy.		
g. Whether minutes of meetings are prepared and retained.		
D. Duties of the Board and Its Committees 1. Provide the excerpt from the articles of incorporation and bylaws that provides a description of the duties assigned and performed by the board of directors, its audit committee and any other committees of the board. Include a current list of committees and the members as of the examination date.		
2. Provide an inventory of policies promulgated (and in effect as of 12-31-XX) by the board and its committees for oversight of the insurer and describe how compliance with these policies is reported on by management.		
3. Describe the following board activities and provide supporting documentation:		
a. How does the board monitor professional ethics and independence from issuers of audit reports?		

	COMPLETED BY	SUPPORTING DOCUMENTATION
b. How does the board consult with external auditing firms on accounting and auditing questions?		
c. How does the board supervise audit work (internal and external)?		
d. How is the board involved with the oversight of the hiring, professional development and advancement of personnel?		
e. To what extent is the board responsible for the acceptance and continuation of audit engagements?		
4. Describe the following audit committee activities and provide supporting documentation:		
a. To what extent is the committee responsible for approving all auditing services and non-audit services provided by the company's issuer of audit reports?		
b. To what extent is the committee responsible for establishing procedures for the receipt, retention, and treatment of complaints received by the company regarding accounting, internal controls, or auditing matters?		
c. To what extent is the committee responsible for establishing procedures for the confidential, anonymous submission by employees of concerns regarding questionable accounting or auditing matters?		
d. Which member(s) of the committee is a financial expert?		
E. Corporate Planning 1. Advise whether the company has developed a long-term strategic plan. Summarize the company's business strategy, if applicable and provide the following information:		
a. How often is the strategic plan and business plan reviewed and updated?		

	COMPLETED BY	SUPPORTING DOCUMENTATION
b. How does management obtain and use information to stay abreast of changes in the competitive, technological and regulatory environments? If so, what resources are used?		
c. What is the scope of the established compliance and ethics program and how does it integrate with your overall business strategy?		
F. Use of Specialists 1. List any key consultants whose services were used during the examination period. State the specialist's relationship, if any, to the company.		
G. Culture 1. Provide the company's formal mission statement, noting the elements regarding compliance, ethics and values.		
2. How does the board and management set the "tone at the top" and communicate compliance, ethics, values, mission and vision?		
3. Discuss how employees and other stakeholders understand that the organization is serious about its compliance and ethics responsibility.		
II. ORGANIZATION AND PERSONNEL PRACTICES		
A. Organization 1. Provide details of the company structure, including:		
a. Corporate structure chart (by legal/business unit);		
b. Personnel organization chart;		
c. Organizational chart detailing the structure of key business activities that include the individuals responsible for each activity, areas of responsibility and lines of reporting and communication; and		
d. List of critical management and operating committees and their members.		

	COMPLETED BY	SUPPORTING DOCUMENTATION
2. Provide formal position descriptions for administrative and financial personnel.		
3. Provide a copy of the formal conflict of interest policy. Provide information on the following elements regarding the conflict of interest policy:		
a. Does the conflict of interest policy require periodic declarations by officers, directors and key employees?		
b. Describe the system used to monitor compliance with the conflict of interest policy.		
c. What position in the organization provides oversight and leadership in the compliance/ethics function, and where does this position fall in the organization chart?		
4. Does the company have a written corporate governance framework? If so, describe how the corporate governance framework is:		
a. Approved and overseen by involved board of directors.		
b. Implemented and monitored by executive management.		
c. Aimed at the identification and fulfillment of sound ethical, strategic and financial objectives.		
d. Supported by business planning and resource allocation.		
e. Built by reliable business planning and proactive resource allocation.		
f. Reinforced by firm adherence to sound principles of segregation of duties.		
g. Independent in the assessment of these programs. Is the assessment of these programs performed by the internal audit and/or by the independent certified public accountants?		
h. Objective in reporting of findings to the board or appropriate committees thereof.		

	COMPLETED BY	SUPPORTING DOCUMENTATION
B. Personnel		
1. Describe the investigation of backgrounds and references during the recruitment and selection process for new employees in the administrative and financial areas.		
2. Describe any significant turnover in management.		
3. For each member of the company's key management, please provide:		
a. The member's length of service with the company as well as service in his/her current position.		
b. The member's specific industry experience.		
c. The member's biographical information.		
4. List any officers that have been associated with a company that has become insolvent or placed in receivership, suffered a revocation of license, or ordered to cease and desist from violations of insurance law or regulations.		
a. If applicable, have the officers describe their roles in the insolvency, receivership, etc.		
5. How are personnel policies, including hiring, evaluation and termination, documented and communicated to employees?		
6. Are employees who handle cash, securities, and other valuable assets bonded? List those covered, the amount of coverage and deductible.		
7. Are any related persons employed within the company? If yes, provide their names, job titles and relationship.		
8. To what extent is rotation of duties enforced by mandatory vacations? Explain.		
9. To what extent is job performance periodically evaluated and reviewed with each employee?		
10. To what extent are there formal training programs for administrative and financial personnel? Provide		

	COMPLETED BY	SUPPORTING DOCUMENTATION
documentation describing the training provided.		
11. Describe the organization structure of your compliance and ethics management team.		
12. How often, and by what methods, does management communicate the mission and vision of the compliance and ethics program to employees and other stakeholders?		
III. INTERNAL AUDIT ACTIVITIES AND INTERNAL CONTROLS		
A. Use of Internal Audit Departments 1. To what extent are internal audit departments used?		
2. Is the scope of internal audit activities planned in advance with senior management, the board of directors or the audit committee? If so, which? If activities are planned with senior management, describe how the internal audit department remains independent.		
3. To what extent do internal auditors prepare and follow written audit programs? How do these programs:		
a. Provide objective, independent reviews and evaluations of insurer activities, internal controls, and management information systems (MIS)?		
b. Help maintain or improve the effectiveness of insurer risk management processes, controls and corporate governance?		
c. Provide reasonable assurance about the accuracy and timeliness with which transactions are recorded and the accuracy and completeness of financial regulatory reports?		
4. Provide documentation describing the normal duties of the internal auditors including the extent of financial audits and operational audits. Include the following information:		
a. Size and organization of the staff (including ratio of supervisors to staff);		

	COMPLETED BY	SUPPORTING DOCUMENTATION
b. Prior experience of staff members;		
c. Number of CPAs and CIAs; and		
d. Scope restrictions. If any, consider internal audit's independence from management.		
5. Do internal auditors have direct access to:		
a. Senior management?		
b. Board of directors?		
c. Audit committee?		
d. Appropriate executives?		
6. How are responses to internal audit recommendations communicated and documented?		
7. How is the implementation of internal audit recommendations monitored?		
8. Are there training programs for internal auditors? Describe the training programs available for internal auditors as well as any established continuing educational requirements.		
9. Are any internal auditors or members of their families related to other employees? If so, explain.		
IV. MONITORING PROCEDURES		
A. Budgets 1. Does management develop an annual budget and financial plan based on corporate goals and objectives? If so, please provide.		
2. How are budget expectations communicated to those affected?		
3. Are estimates included in financial data and statements reviewed by knowledgeable persons independent of the estimation process? If yes, who performs this review?		
a. Are the entries supported by explanation and/or		

	COMPLETED BY	SUPPORTING DOCUMENTATION
documentation?		
4. How is financial performance and the status of the company's financial condition periodically reviewed and/or compared to the budget and prior year?		
a. Are variances between budget and actual results explained by management?		
b. Are variances between prior and current year explained by management?		
c. How often are these analyses performed?		
5. To what extent do budgeting procedures cover all subsidiaries and departments?		
6. Do budgets and forecasts cover:		
a. Premium income by line of insurance?		
b. Policy benefits by line of insurance?		
c. General expenses?		
d. Investments (allocation of investable funds, and income and expenses)?		
e. Statutory surplus?		
f. Federal income taxes?		
g. Cash flow?		
B. Financial Planning and Reporting 1. Provide documentation summarizing the qualifications of key employees responsible for preparation and issuance of financial statements. Include names, titles, job responsibilities, background and number of years in present position.		
2. How and with what frequency are financial statements submitted to:		
a. Operating management?		
b. Board of directors?		

	COMPLETED BY	SUPPORTING DOCUMENTATION
c. Audit committee?		
3. Describe the review and approval process including who reviews and approves financial information for public distribution (e.g., press releases, filings with regulatory bodies and policyholders' or shareholders' reports)?		
4. To what extent does management assess the effectiveness of the company's internal control over financial reporting?		
a. Did management assess the internal controls over financial reporting as effective? Please provide management's assessment		
b. Did the company's external auditor issue an unqualified opinion as to management's assessment? Please provide the auditor's opinion.		
C. Operations 1. Describe how operating policies are periodically reviewed. Does this documentation include up-to-date accounting policies and procedures? Provide a chart describing the nature of each account.		
D. Operating Analyses 1. In multi-line insurance organizations, describe how reports on operating results and key financial data provided by major lines of business and/or subsidiary to the home office are completed and how often.		
a. Describe the principal operating analyses used (e.g., line of business analyses, loss ratios, in-force and reserve amounts, investment yields). Describe contents and indicate frequency of preparation. Sample analyses may be attached instead of a schedule.		
E. Investments 1. Provide a copy of the company's investment policy and answer the following questions:		
a. How often is the policy reviewed and updated?		
b. How is investment performance periodically		

	COMPLETED BY	SUPPORTING DOCUMENTATION
reviewed by management?		
c. How are investment activities approved by the board of directors?		
2. Describe the policy regarding treatment of securities. Include whether securities are kept::		
a. On hand?		
b. With a non-discretionary custodian?		
c. With a discretionary custodian? If kept with a discretionary custodian, advise if there is an approved list of investments.		
3. Describe the company's exposure to the following derivative risks:		
a. Those included on Schedule DB of the Annual Statement.		
b. Those not included on Schedule DB of the Annual Statement.		
F. Third-Party Administrators 1. How are the services of third-party administrators used? Please provide a list of all TPAs used and answer the following:		
a. Are detail records reconciled? If yes, how and with what frequency?		
b. Are internal audits performed? If yes, how and with what frequency?		
G. Reconciliations		
1. For the following assets, indicate how often they are reconciled to the accounting records and the person performing the reconciliation:		
a. Bonds;		
b. Stocks;		
c. Mortgage loans on real estate;		

	COMPLETED BY	SUPPORTING DOCUMENTATION
d. Collateral loans;		
e. Real estate;		
f. Policy loans;		
g. Certificates of deposit;		
h. Cash;		
i. Office equipment; and		
j. Other significant assets not already discussed above.		
2. How often are the following detail and control accounts reconciled and who performs the reconciliation?		
a. Financial values in master policy file;		
b. Suspense accounts;		
c. Reinsurance assumed;		
d. Investment in bonds;		
e. Stocks;		
f. Mortgage loans on real estate;		
g. Collateral loans;		
h. Policy loans;		
i. Certificates of deposit;		
j. Accrued investment income;		
k. Office equipment;		
l. Income tax asset/liability;		
m. Debt;		
n. Equity; and		
o. Other significant accounts not already discussed		

	COMPLETED BY	SUPPORTING DOCUMENTATION
above.		
3. Please indicate how often the following are reconciled and who performs the reconciliation:		
a. Information files or registers for agreement of the information base premium, commission and cash receipts registers;		
b. Premium billing and in-force files; and		
c. Reserve valuation and master file.		
4. Explain any differences in accounting and closing practices followed at interim dates compared to year-end?		
5. Are current year statements prepared on the same basis (i.e., key accounting principles, actuarial and pricing assumptions) as used in prior years? Explain any differences.		
6. How do you ensure that statements are prepared in accordance with state statutes and regulations?		
7. To what extent are general journal entries (other than standard entries) required to be authorized by a responsible official not involved with the origination of entries?		
8. How is access to accounting and financial records restricted to authorized personnel?		
9. To what extent are internal control procedures written and current to safeguard the company's assets?		
H. Reinsurance 1. Do reinsurance agreements require formal review and approval, prior to execution, by officers? Explain which officers complete this review and approval. Also note whether the board of directors also review and approve.		
2. How is regulatory approval (where applicable) of reinsurance agreements documented?		
3. Does the documentation include projections of the expected economic results and the accounting for the		

	COMPLETED BY	SUPPORTING DOCUMENTATION
transactions?		
4. Explain whether all amendments and changes to reinsurance agreements are supported by written documentation?		
5. Discuss any major changes in terms (e.g., commission, percent participation, limits or retentions) or conditions of contracts with significant management companies, agents or on reinsurance layers. Document in detail significant specific arrangements with agents, MGAs or others.		
I. Assumed Reinsurance 1. Are ceding companies required to submit appropriate periodic reports on the reinsured business? Indicate the extent and frequency of these reports.		
2. Are such periodic reports compared to projections made at the date of the agreement?		
a. If yes, how are material deviations investigated?		
3. To what extent does your company review or inspect ceding company records and changes therein (premiums, terminations, benefits or claims)?		
a. Are these reviews performed as of the assumption date?		
b. Are these reviews performed periodically after the assumption date? How often?		
J. Ceded Reinsurance 1. Describe how the financial stability of assuming companies is reviewed to ascertain whether such companies are solvent and have the ability to meet liabilities assumed under the reinsurance agreement?		
2. Describe how the results of reinsurance agreements are monitored to permit timely recapture of ceded premium or cancellation of assumed reinsurance?		
3. Who reviews and approves the decision to recapture or cancel the treaties?		
4. To what extent and how often does company management report on the reinsurance plan and		

	COMPLETED BY	SUPPORTING DOCUMENTATION
communicate an evaluation of the plan's effectiveness to the board of directors?		
V. LEGAL AND REGULATORY REQUIREMENTS		
1. Where are current copies of insurance company and/or insurance holding company laws, Internal Revenue Service tax laws and other regulations maintained?		
2. Describe the procedures to ensure that management is informed of changes in laws.		
3. Are the following specific areas of company activities regularly reviewed for compliance with regulatory requirements? If yes, how often? Describe the documentation procedures and indicate who is responsible.		
a. Capital requirements and dividend restrictions?		
b. Transactions with employees, directors, and officers?		
c. Permitted ratios of categories of qualified investments to statutory capital and/or surplus?		
d. Prohibitions or restrictions as to particular kinds of investments?		
e. Prescribed loan-to-value ratios for mortgage loans and similar credit-type investments?		
f. Policy form approval?		
g. Treatment of policyholders in benefit settlement matters?		
h. Disposal of real estate acquired by foreclosure?		
i. Permitted non-insurance activities?		
j. Foreign operations?		
k. Reporting?		
l. Others not already discussed above?		

	COMPLETED BY	SUPPORTING DOCUMENTATION
4. State any government restrictions or regulatory requirements that pertain specifically to the company including any permitted practices.		
5. Provide copies of any limited scope examinations and audits by regulatory or other government agencies. Discuss any IRS revenue agents' reports, deficiency assessments and developments in IRS examinations in progress.		
6. Has the company complied with all debt covenants and other agreements?		
7. Describe whether there are any material contingent liabilities or commitments.		
VI. CODE OF CONDUCT		
1. Does the company have an established Code of Conduct? If so, provide a copy and advise what the Code addresses and who receives it.		
2. Do you distribute the Code of Conduct and confirm that employees both receive and understand the Code and other policies? If so, please describe this process.		
3. Do you have a process for updating policies and procedures? Please describe this process.		
4. Can any requirements established by the Code of Conduct and other policies be waived or overridden? If so, please describe this process.		
5. Under the Code of Conduct, can employees, agents, and other stakeholders raise issues regarding compliance and ethics-related matters? If so, please describe this process.		
6. Does the Code have an established procedure to address compliance and ethics issues that arise? If so, please describe the procedures for this process and how the company scrutinizes the source of compliance failures.		
7. Does the Code provide guidance to take action against violators of the Code? If so, please describe how consistently this has been applied or whether other provisions are in place to address this issue.		

	COMPLETED BY	SUPPORTING DOCUMENTATION
8. Is there a process for determining which issues are escalated to the board and for informing the board when issues are resolved? If so, please describe this process.		
9. Are there ongoing processes in place to monitor the effectiveness of the compliance and ethics program? If so, please describe.		
10. Does the organization engage an external law firm or consultant to audit compliance and ethics program elements? If so, please list the firm or consultant?		
11. Is the company a member of the Insurance Marketplace Standards Association and/or other best practices organizations? If so, please list.		

EXHIBIT F – ANALYTICAL REVIEW PROCEDURES

Performing an analytical review involves the study and comparison of relationships among data at a point in time and the trend in those relationships over periods of time. Based on an understanding of a company's business, the examiner develops certain expectations about important financial and operating relationships. Analytical review results that support these expectations increase the level of confidence and may lead to examination efficiencies by changing the nature of tests or by reducing the extent of other procedures. Conversely, analytical review results that differ from expectations should increase overall skepticism and may require additional procedures to explain significant variations from expectations.

Overall analytical review is used during initial planning to help understand the impact of changes in environmental factors, and to provide a preliminary indication of the company's overall financial condition, including areas that might require emphasis. Detail analytical review may be performed after key activities are identified to gain more information about individual accounts or classes of transactions affected by specific examination assertions. In Phase 5, analytical review procedures can be the primary substantive test of an account balance or class of transactions, or can be used in combination with other substantive tests to support the reasonableness of annual statement amounts. The extent to which these analytical review procedures can be substituted for or can reduce other procedures will depend on the quality of the evidence (i.e., persuasive, corroborative, or minimal) obtained from the analytical review procedures.

Prior to conducting their own analytical assessments, examiners should utilize analytical procedures conducted by the insurance department's financial analysts. The financial analysts perform analytical procedures on a quarterly and annual basis from the information obtained within the company's periodic report filings. These procedures are outlined in the *Financial Analysis Handbook* according to the company's line of business (i.e., Life, Health or Property/Casualty).

In addition, examiners should obtain and review analytical assessments from company management, internal and external auditors, and other industry reports. These sources may assist the examiner in identifying unusual relationships and reducing the extent of analytical or detail testing procedures that the examiner expects to perform.

Types of Analytical Review Procedures

A. Comparisons to Prior Periods

Analysis of a company's financial characteristics and operating results over a period of time provides information useful in evaluating operating performance and assessing expected current-year financial condition and results of operations. Two-year comparisons (e.g., a comparative analysis of current and prior-year operating expenses) may be sufficient to identify changes requiring follow-up with the company. However, comparisons over a number of years (i.e., trend analysis) often can be more informative. Many factors can affect comparisons. For example, changes in price levels or the overall industry trend (growth or decline) may distort comparisons between periods. Therefore, annual statement comparisons should include both dollar amounts and percentage of total assets and income statement classifications as a percentage of total premiums. Financial statements presenting only percentage relationships (sometimes called "common-size statements") can provide a quick indication of fluctuations and trends that may require further investigation or explanation.

When making comparisons over a period of years, trends may be distorted by significant non-recurring events or transactions. Some factors that may affect inter-period comparability include:

1. Changes in product design, customers, marketing strategy or capitalization;

2. Disposal or acquisition of a line of business;

3. Accounting changes or account reclassifications;

4. Unusual charges or credits to operations;

5. Significant reinsurance transactions.

The examiner should understand the effects of such events in performing and evaluating trend analysis and in developing expectations about the company's financial data.

B. Comparisons to Budgets or Forecasts

Comparisons of actual operating results to budget or forecasted amounts often can provide important analytical review evidence. However, before making budget or forecast comparisons and investigating variances, the examiner should understand the company's budget or forecast preparation process and the significant underlying assumptions. For example, if the budgetary process includes a study of both present and past operating experience of the company and of general and industry economic conditions, and if past budgets have proven to be realistic, comparison to budgeted amounts can be useful. But if budgets are simply motivational tools (i.e., "stretch goals" rather than management's best estimates) or historically have been prepared inadequately, they may be subject to large variances. In these cases, examiners should be aware that the usefulness of comparisons with budgets for analytical review purposes may be limited.

Certain components of the annual statement lend themselves more readily to budget comparisons (e.g. investment income and general and administrative expenses). Other financial information, such as benefits and claims are influenced by factors difficult to quantify when preparing a budget.

When budgets or forecasts are used in performing analytical review procedures, the examiner should (1) compare them to prior years' operating results and to the current year's financial information, and (2) analyze major revisions made to them during the year.

C. Comparisons to Industry and Competitor Data

Comparisons of annual statement amounts and relationships for the company or its segments to competitor or industry statistics can facilitate an understanding of the company's business environment by showing the impact on the company of emerging trends or structural changes in the industry. By highlighting the company's financial performance relative to the industry, these comparisons also help to identify areas requiring additional attention. Comparisons can be performed by identifying peer groups of companies with similar characteristics and comparing the company's performance to the group, or by comparing the company's results to industry averages.

An industry average is not a "magic number" indicating ideal or even acceptable performance. However, industry statistics can serve as effective benchmarks for evaluating a company's operations. Therefore, significant variances from industry norms may indicate problems and should be further evaluated and understood. Industry comparisons can identify possible examination problems or management concerns.

While comparisons to industry statistics can provide useful information, the data must be comparable. Meaningful comparisons can be difficult for a variety of reasons, including the fact that each company has unique characteristics, such as product design, target customers, location, corporate structure and capitalization. The variability of industry data does not mean that comparisons with industry norms will not be useful. On the contrary, their principal value may be the questions they raise. However, the examiner should always use judgment in selecting industry data for analytical review purposes and in evaluating the comparisons. In using peer group comparisons, it is important to select insurance companies that are comparable in size, financial structure, locality and market emphasis (e.g., lines of business), because those factors will affect performance indicators. While caution should be used, comparisons between peer companies may be useful in determining the aggressiveness or conservatism of the company's investment policies, tax practices and pricing strategies.

In addition to conducting their own analyses, examiners may quickly benefit from the work of external industry analysts' reports. An abundance of statistical information exists for the insurance industry. Several industry publications, most notably *Best's Insurance Management Reports* and *Best's Review*, provide certain comparative and pooled statistics. Some external industry analysts' reports are prepared to address overall industry issues, while other reports may focus on analysis of a specific entity. Various credit and equity analysts prepare reports including: A.M. Best Company, Conning & Company, DeutscheBank, Fitch, J.P. Morgan, Moody's Investors Service, Morgan Stanley and Sanford Bernstein. Review of such reports may help the examination team to develop an independent point-of-view of the company and its risks and to provide a preliminary foundation for discussions with company management.

Use of Analytical Review in Risk Assessment

While the overall analytical review procedures emphasize general financial condition and trends, the detail analytical review procedures are directed to specific accounts and transactions. The primary purpose is to obtain some assurance as to the company's financial information and ratios in relation to the examiner's understanding of the company's operations and evaluation of the accounting system. These procedures usually are performed in Phase 1 when obtaining an understanding of the company. To determine the reasons for unexpected fluctuations, it may be necessary to investigate the details of specific transactions that constitute an account balance.

The performance of detail analytical review procedures after key activities have been selected may confirm and quantify expected problems (e.g., as a result of certain environmental considerations or inadequate controls noted), or they may indicate that problems are not as significant as expected. Thus, the results of detailed analytical review procedures may assist in identifying inherent risks which could increase or decrease the amount of work necessary to gain enough assurance related to the key activity. The results of this analytical review should be incorporated in the Risk Assessment Matrix (or similar document) and considered in accordance with the examiner's assessment of risks.

The difference in focus between overall and detail analytical review is in (1) the nature of the information used, (2) the extent of comparisons, and (3) the period covered by those comparisons, as illustrated in the following table:

	Overall	Detail
Information	"Top-level" interim financial statements and overall financial and operating ratios	Various levels of detail (line of business)
Extent of Comparisons	Comparisons of annual statement line items	Details of annual statement line items (e.g., Annual Statement Expense Exhibits)
Period Covered	Year-to-year comparisons and trends over a three to five year period	Quarter-to-quarter and/or month-to-month comparisons of current and prior year activity

For many examinations, the difference between overall and detail analytical review is not always clear-cut. As a practical matter, overall and detail analytical review often are performed at the same time. For example, various ratios are analyzed during initial planning to make a preliminary assessment of the company's financial condition (i.e., overall analytical review evidence). Because those ratios also apply to specific accounts, observations about fluctuations or trends may assist the examiner in identifying specific inherent risks of the company.

Judgment should be used in selecting detail analytical review relationships; some procedures will not be helpful. Each detail analytical review procedure may provide useful evidence that will help identify and assess inherent risks for a particular examination area.

Analytical Review Procedures as Substantive Tests

Substantive tests fall into three categories – (1) analytical review procedures, (2) tests of key items, and (3) tests of representative samples. Judgment is used to determine the most effective and efficient combination of those tests responsive to the assessment of residual risk. This section discusses analytical review procedures as substantive tests, and provides guidance on the level of persuasiveness and the need to test the underlying data.

Analytical review procedures may be used (1) as primary substantive tests of balances, (2) as corroborative tests in combination with other procedures, or (3) to provide at least some minimal level of support for conclusions. Analytical review procedures may provide an efficient alternative to detail tests of account balances and may allow the examiner to consider whether the company's financial information is in line with expectations. In some cases, typically in low and some moderate residual risk accounts, analytical review procedures may effectively be used as the only tests.

During planning, the examiner should consider what analytical review procedures are available. The extent to which analytical review procedures can be substituted for or can reduce other procedures will depend on the evidence provided by the analytical review procedures.

Analytical review procedures can be the primary substantive test, i.e., the primary basis for conclusions, if they provide sufficient evidence. That would be the case if the procedures generate an amount believed to be a reasonable estimate of the account balance and is consistent with expectations.

Analytical review procedures can also be effective as a check on general reasonableness of accounts even when not used to estimate the account balance. Analytical procedures often uncover unreasonable relationships or business trends that detail testing might not detect. Some good examples of situations where analytical review procedures can be effective and insightful include: detection of material accounting errors through analytical review and evaluating the reasonableness of interest income and/or commission expense.

Analytical review procedures provide corroborative evidence if they (1) confirm findings from other tests and (2) support management's representations, or otherwise decrease the level of skepticism. Analytical review procedures that provide only limited corroborative evidence contribute only minimal support for conclusions. In deciding whether a particular analytical review procedure or combination of procedures provides corroborative evidence or only minimal support for conclusions, the examiner should evaluate both the extent of analytical review procedures and the quality of the evidence expected to be obtained. For example, if the examiner simply compares a current year overall balance (e.g., reserves) to the prior-year balance, and does not supplement that comparison with any other analytical review procedures (e.g., lapses, cash surrenders, new issues, loss ratios, premium volume), the examiner would obtain only minimal support for a conclusion.

Examiners are encouraged to utilize software tools, such as ACL, to analyze significant amounts of data and increase the effectiveness and reliability of analytical tests.

Evaluating Analytical Review Results

An understanding of the company's business may identify likely fluctuations in the financial data. These fluctuations may be caused by (1) trends – general changes in business conditions; (2) seasonal patterns – changes in business activity caused by weather or other seasonal changes; (3) cyclical patterns – changes in overall economic activity; or (4) dependent relationships – changes related to movements in other financial data.

Fluctuations that cannot be explained from knowledge of the company's business or by known relationships with other financial data may result from non-recurring transactions, erroneous accounting procedures or practices, or other factors. When unexpected significant fluctuations in amounts or key relationships occur, or when expected fluctuations do not occur, the examiner should find out why. Initial follow-up procedures should include discussions with operating executives and financial management. Management may have already determined the cause of the variations, or if not, may save time by pursuing these matters. The examiner should challenge the reasonableness of management explanations in view of the examiner's understanding of the business and the examiner's expectations.

The examiner should consider how the company's ability to respond to reasonable analytical inquiry would impact the evaluation of the competency of management. Well-managed companies will often be able to answer questions about key relationships or will pursue the root cause of unexpected fluctuations.

Regulatory Analytical Reviews

The state insurance department's financial analysts perform analytical procedures on the Quarterly and Annual Statement Filings, in addition to other supplemental filings of an insurer. The examiner should utilize the in-depth analytical reviews prior to conducting any analytical assessments. In the event a specific concern is raised and further analytical review work is deemed necessary, there are examples of analytical review procedures posted on the NAIC Financial Condition Examiner's Handbook Updates page.

The Financial Analysis Working Group has developed prioritization and analytical tools to assist regulators with identifying insurers that could require immediate attention and aid regulators with identification of potential risk areas where enhanced analysis and review might be placed. Documentation is available for regulators that describes these prioritization and analytical tools.

Testing Underlying Data Used In Analytical Review

When should the examiner test the underlying data used in analytical review procedures? It is not necessary to test the data used in overall and detail analytical reviews during initial planning and program development. These reviews are only to increase the examiner's understanding of the company's business, provide a basis for developing examination scope, and identify areas that require further investigation.

If analytical review procedures are used to corroborate the results of other procedures, judgment should be used in determining the need for, or the extent of, tests of the underlying data. Operating data generated independently of the accounting system may not need to be tested as extensively as data generated by the accounting system. The examiner also should keep in mind that computer generated data used in corroborative analytical review procedures may need to be tested to avoid unwarranted reliance on the computer.

EXHIBIT G - CONSIDERATION OF FRAUD

COMPANY NAME ______________________________

PERIOD OF EXAMINATION______________________________

EXAMINER-IN-CHARGE ______________________________

In accordance with the Risk-Focused Surveillance Framework, the consideration of fraud in financial condition examinations should occur throughout all phases of the examination. The examiner needs to consider fraud risk factors and develop examination procedures in order to adequately obtain reasonable assurance that material misstatements due to fraud are not included in the financial statements. The manner in which the insurer's management identifies, considers and mitigates the risk of fraud should factor heavily into the examiner's understanding of the company and assessment of management. The external auditors are required by Statement on Auditing Standards (SAS) No. 99 *Consideration of Fraud in a Financial Statement Audit* to perform specific procedures to ensure that the audit has been responsibly planned and performed and to obtain reasonable assurance that the financial statements are free of material misstatement. In accordance with AICPA guidance, documentation of the auditor's consideration of fraud should be included in the external audit workpapers. The examiner should review the work performed by the auditor and consider the auditor's documentation and findings. The examiner should obtain and review this information in accordance with the review of the external audit workpapers. Although the examiner should utilize the external audit workpaper documentation to the extent deemed reasonable, reliance on the external audit workpapers does not preclude the examiner from identifying and inquiring about fraud risk factors noted during the examination or interviewing company management regarding the possibility of fraud, or known fraud occurrences.

The consideration of fraud is primarily completed through the identification and examination of fraud risk factors. Fraud risk factors are conditions that may indicate the occurrence of fraud. Some examples include the insufficient review of controls, failure to respond to known accounting irregularities, extraordinary growth or profitability, threat of regulatory action, and missing accounting documentation. This exhibit includes a detailed checklist of fraud risk factors identified in previously detected fraudulent incidences to assist the examiner in determining applicable fraud risk factors. Utilization of the Risk Assessment Matrix (Exhibit K) may be beneficial to identify and assess inherent risks, assess controls, determine residual risks and identify test procedures for applicable fraud risk factors. By properly considering and attesting to fraud risk factors, the examiner is able to obtain reasonable assurance that the financial statements are free from material misstatement due to fraud. Completion and approval of this document does not indicate that fraud has not been perpetrated on or within the company nor does it provide absolute assurance that committed frauds have been detected. It is possible to complete a properly planned and performed examination and not discover occurrences of perpetrated fraudulent activity. See for additional guidance relating to fraud considerations.

Note: Any examiner may complete the consideration of fraud during the examination, but the examiner-in-charge is required to review and sign-off the prepared workpapers.

CONSIDERATION OF FRAUD - PLANNING

Note: The following section should be completed in accordance with the consideration of fraud while planning the examination. The examiner should provide documentation of the actual review during the planning process as indicated throughout this exhibit.

PLANNING PROCEDURES	COMPLETED BY	DATE
1. Obtain and review the external audit workpapers detailing the fraud consideration documentation. Identify any fraud risk factors or other items noted, in the attached "Fraud Risk Factors" checklist below, that might be indicative of fraudulent activity by either fraudulent financial reporting, the misappropriation of assets, or through fraudulent claims. (Note: If the external auditor has performed a fraud risk assessment at the holding company level rather than the insurance company entity level, the external audit workpapers may not provide enough information to warrant a thorough review as outlined in the steps below. In this instance, the examiner may choose not to rely on the external auditor's consideration of fraud and should document the rationale in the workpapers. The examiner may continue the consideration of fraud in Part B – Review Company Operations and Identify Fraud Risk Factors.)		
a. Document any fraud risk factors noted and procedures performed by the external auditor to mitigate fraud risk.		
b. Document the results of communications amongst the external auditors, company officials, or others with respect to the risk of fraud in the entity and known fraudulent activity perpetrated on or within the company.		
c. Review and evaluate the other information documented by the external auditor with respect to their consideration of fraud and utilize this information, if applicable, to develop and further enhance the planned examination procedures.		
2. Review the company's operations, both financial and operative, to identify any additional fraud risk factors. Review and adjust the planned examination procedures according to the noted risk factors. Use the external audit workpapers to facilitate this review.		
a. Document the fraud risk factors identified and the examination procedures designed to mitigate the fraud risk. (Note: These procedures typically entail inquiry of management and others about the risk or occurrence of fraud, performing an evaluation of analytical procedures, considering fraud risk factors, and considering other information considered pertinent for the determination of fraud.		
b. Summarize the auditor's consideration of management's ability to override controls. Evaluate and document the auditor's determination		

to perform (or not perform) additional procedures to address the risk of control deviations due to management overrides.		
c. Document other risks or conditions noted by the auditor that resulted in the auditor completing additional auditing procedures or documenting added responses.		
d. Document any communications the external auditor had regarding fraud, or the risk of fraud, with the company's management, audit committee, or other individuals. The examiner should consider the level of management informed for all known fraudulent acts.		
e. For those fraud risk factors identified, document the examination procedures or steps the examiner will perform to mitigate fraud risk.		
3. Meet with company management to discuss the risk of material misstatement due to fraud in the entity and to inquire whether management is aware of any fraudulent activity that has been conducted on or within the company and if the company is maintaining compliance with federal anti-money laundering requirements. Determine that the company has established antifraud initiatives reasonably calculated to detect, prosecute and prevent fraudulent insurance acts.		
a. Identify the company managers utilized for this discussion and summarize the dialogue results. Include the discussion results in a memorandum for inclusion in the workpapers.		

CONSIDERATION OF FRAUD - TESTING

Note: The following section should be completed in accordance with the consideration of fraud during testing of the examination. The examiner should provide documentation of the actual review during testing as indicated throughout this exhibit.

TESTING PROCEDURES	COMPLETED BY	DATE
1. Continue to identify fraud risk factors during the examination process. Adapt the planned examination procedures as necessary to mitigate fraud risk.		
a. Review the planned examination approach to determine if modification is necessary in accordance with the additional identified fraud risk factors.		
b. Evaluate the assessed materiality levels as well as the overall risk assessment to adequately reflect the discovery of additional fraud risk factors.		
c. Document any changes to the planned examination approach, materiality levels, or the overall risk assessments in a memorandum for inclusion in the examination workpapers.		
2. Review the fraud initiatives established by the company to advertise, identify, investigate and report fraudulent acts.		
a. Verify the established fraud program is advertised and promoted to the company's insured.		
i. Determine whether claim forms and applications indicate that any person who knowingly presents a false or fraudulent claim for payment of a loss or benefit or knowingly presents false information in an application for insurance is guilty of a crime and may be subject to fines and confinement in prison.		
b. Verify that the company has established a procedure to report fraudulent insurance acts to the commissioner in the manner prescribed by the commissioner.		
3. If applicable, verify that the company has established and maintains a written anti-money laundering program thas has been approved by senior management and contains the following elements: i) an assessment of money-laundering and terrorist financing risks associated with its covered products; ii) the appointment of an anti-money laundering compliance officer; iii) an anti-money laundering training program; iv) independent testing on a periodic basis. If the examiner determines that the company has not established or is not maintaining such an anti-money laundering program, then it may be appropriate for the domestic regulator to refer this information to the appropriate federal regulator. See detail guidance regarding anti-money laundering programs in Section 3.		

TESTING PROCEDURES	COMPLETED BY	DATE
4. Document the investigation of any potential fraudulent activity noted during the examination process. *(Note: This does not refer to additional fraud risk factors identified.)*		
a. If, after completing the review of fraud risk factors and examination procedures, the examiner identifies a potential fraud situation, the examiner and examiner-in-charge, depending on state guidelines, should either inform the appropriate state insurance department division responsible for investigating potential fraudulent activity, or perform procedures to further investigate the potential fraudulent activity. If the examiner is investigating the potential fraud, the examiner should:		
i. Discuss the nature and effect of the fraudulent activity with the appropriate level of management.		
ii. Attempt to obtain additional evidential matter regarding the fraudulent activity to determine the overall effect on the financial statements and the company operations.		
b. Verify that necessary information regarding the knowledge or reasonable belief that a fraudulent act has been, will be, or is being committed has been communicated to the commissioner as required. (Note: If the state has adopted the Insurance Fraud Prevention Model Act, information obtained by the commissioner in an investigation of a suspected or known fraudulent act is confidential by law and is not subject to subpoena. Additionally, the commissioner or individual gathering the information on behalf of the commissioner is not permitted or required to testify in a private civil action with regards to the confidential documents.)		

CONSIDERATION OF FRAUD - WRAP-UP

Note: The following section should be completed in accordance with the consideration of fraud during the completion of the examination. The examiner should provide documentation of the actual review during the wrap-up procedures as indicated throughout this exhibit.

WRAP-UP PROCEDURES	COMPLETED BY	DATE
1. Review the fraud risk factors identified throughout the examination and the examination procedures completed to verify that the noted fraud risk factors have been adequately considered throughout the examination process.		
2. Although the focus of the examination is not to detect fraud, verify that the examination has been conducted in a manner to alleviate the risk of fraud through the consideration of fraud risk factors.		
3. Verify that the report of examination properly presents the financial condition of the company with regards to any known instances of fraud perpetrated on or within the company.		

Review Company Operations and Identify Fraud Risk Factors

Review the company's operations, both financial and operative, to identify fraud risk factors. Common fraud risk factors are indicated in the following chart. The fraud risk factors are categorized according to the three conditions typically present when fraud occurs:

Incentives/pressures to commit fraud

Opportunities exist to perpetrate fraud

Attitudes/rationalizations that fraud is ethical or acceptable

FRAUD RISK FACTORS	COMPANY APPLICABILITY			
	Y	N	N/A	COMMENTS
Misstatements From Fraudulent Financial Reporting				
Incentives / Pressures				
1. Are any of the following conditions present that may indicate a personal incentive for management to engage in fraudulent financial reporting?				
a. Are compensatory management bonuses and incentives derived from the company's ability to accomplish aggressive operating or performance results?				
b. Do any other conditions exist that may indicate a motivation for management to engage in fraudulent financial reporting?				
c. Are unduly aggressive financial targets and expectations for operating personnel established by management?				
d. Is management or the board of directors' personal financial situation threatened by the individual's financial interests in the entity?				
2. Is the financial stability or profitability of the company threatened by economic, industry or entity operating conditions?				
a. Is the company subject to new accounting, statutory or regulatory pronouncements that could hinder the company's profitability or financial stability?				
b. Is the company encountering a significant competition or market saturation and declining margins?				
c. Is the insurance industry experiencing an increase in the number of insolvencies?				
d. Is the industry experiencing rapid changes in technology?				

FRAUD RISK FACTORS	COMPANY APPLICABILITY			
	Y	N	N/A	COMMENTS
e. Is the holding company's ability to meet its debt service requirements contingent upon increased profits and/or dividends from the insurance subsidiaries?				
f. Has the company experienced unusually rapid growth or profitability when compared with other companies in the same industry?				
3. Does company management have substantial pressure to acquire additional operating capital?				
4. Is management subject to excessive pressure to meet expectations or requirements of third parties?				
a. Is the company highly vulnerable to changes in interest rates?				
b. Does the company need to obtain debt financing or does the company have a marginal ability to meet debt repayment requirements? Are the debt covenants difficult to maintain?				
c. Could the company face adverse consequences on a significant pending transaction (such as a business combination, financing arrangement, or contract award) if poor financial results are reported?				
5. Has the company set unrealistically aggressive sales or profitability incentive programs?				
6. Is the company facing the threat of insolvency?				
Opportunities				
1. Do the company's operations provide opportunities to engage in fraudulent activity:				
a. Does the company engage in significant related-party transactions that are not considered to be in the ordinary course of business or with companies not subject to the examination process or audited by an independent accounting firm?				
b. Are the company's financial statements subject to significant estimates that were determined by subjective judgments or uncertainties, or that can adversely impact the financials if changed?				

FRAUD RISK FACTORS	COMPANY APPLICABILITY Y	N	N/A	COMMENTS
c. Does the company have unusual or highly complex transactions (particularly those close to year-end) that are difficult to assess for substance over form?				
d. Does the company have significant bank accounts or subsidiary or branch operations in tax-haven jurisdictions for which there appears to be no clear business justification?				
2. Does the company have appropriate monitoring controls over management?				
a. Is the overall management of the company dominated by a single person or small group without compensating controls (i.e., appropriate oversight by the board of directors or audit committee)?				
b. Is the board of directors actively involved in the oversight of the financial reporting process and internal control?				
3. Does the company have a complex or unstable organizational structure?				
a. Is it difficult to determine the organization or individual(s) that control(s) the entity?				
b. Does the company have an overly complex organizational structure involving numerous or unusual legal entities or managerial lines of authority?				
c. Is there a high turnover within senior management, the audit committee, board members or legal counsel?				
4. Does the company have suffient internal controls and are they operating properly?				
a. Has the company been observed to employ an ineffective accounting, internal auditing or information technology staff?				
b. Is there a high turnover rate in accounting, internal audit , or information technology staff?				
Attitudes				
1. Does company management convey an improper attitude regarding internal controls and the financial reporting process?				
a. Does management neglect to effectively communicate and encourage the company’s values or ethics?				

FRAUD RISK FACTORS	COMPANY APPLICABILITY Y	N	N/A	COMMENTS
b. Does management have an excessive interest in preserving or increasing the earning's trend through the use of aggressive accounting practices?				
c. Does management have an interest in engaging inappropriate methods to diminish reported earnings on a tax-motivated basis?				
d. Are there instances of management failing to correct known reportable conditions within an appropriate time frame?				
e. Does management illustrate a substantial disregard for regulatory authorities?				
2. Are management and employees employed in a non-financial department utilized to determine (or demonstrate an interest in) the accounting practices and financial estimates?				
3. Do related or competing businesses consider the management to have a poor reputation?				
4. Have any of the following situations occurred illustrating a strained relationship with either the current or predecessor auditor?				
a. Are there frequent disputes regarding accounting, auditing, or reporting matters?				
b. Is the auditor limited to specific individuals or sources of information while conducting the audit?				
c. Are auditor communications with the board of directors or the audit committee restricted?				
d. Does management attempt to influence the auditor, and/or the scope of the auditor's work?				
5. Are there any instances of fraud claims against the company or management or any recognized violations of security laws?				
Misstatements from Misappropriation of Assets				
Incentives / Pressures				
1. Are personal financial obligations of management or employees with access to cash and other assets creating pressure to misappropriate assets?				

FRAUD RISK FACTORS	COMPANY APPLICABILITY Y	N	N/A	COMMENTS
2. Do adverse relationships exist between the company and employees (i.e., anticipated lay-offs, compensation issues) that may motivate an employee to misappropriate assets?				
Opportunities				
1. Does the company maintain or process large amounts of cash?				
2. Does the company have fixed assets that are easily susceptible to misappropriation (i.e., small size, portability, marketability, lack of ownership identification, etc.)?				
3. Is the company susceptible to fraudulent, unauthorized disbursements (i.e., claim payments or payroll disbursements) being made in amounts that are material to the financial statements?				
4. Do any of the conditions listed below, that may indicate possible deficiencies in the company's internal controls over assets susceptible to misappropriation, exist?				
a. Is there a lack of appropriate management oversight of assets that are susceptible for misappropriation (for example, inadequate supervision or monitoring of remote locations)?				
b. Is there inadequate record-keeping with respect to assets susceptible to misappropriation?				
c. Is there a lack of appropriate segregation of duties or independent checks not mitigated by other factors?				
d. Does the company lack an appropriate system of authorization and approval of transactions (i.e., benefit or loss payments)?				
e. Are there inadequate physical safeguards over cash, investments, inventory, or fixed assets?				
f. Is there a lack of timely and appropriate documentation for transactions affecting assets susceptible for misappropriation (i.e., rejected claims, benefit payments, etc.)?				
g. Has the company failed to require mandatory vacations for employees in key control functions?				
h. Does management have an inadequate understanding of information technology, which enables IT employees to misappropriate assets?				

FRAUD RISK FACTORS	COMPANY APPLICABILITY			
	Y	N	N/A	COMMENTS
i. Are there adequate access controls over automated records including control over and review of computer systems event logs?				
Attitudes / Rationalizations				
1. Does management display a disregard for internal controls by overriding controls or failing to correct control deficiencies?				
2. Is there disregard for the need to monitor and reduce risks relating to the misappropriation of assets?				
3. Has there been any behavioral or lifestyle changes for management or employees that may indicate that assets have been misappropriated?				
4. Has there been behavior indicating displeasure or dissatisfaction with the company or its treatment of employees?				
Fraudulent Claims				
Note: The following risk factors indicate possible warning signs for fraudulent claims. Although the examiner should not evaluate all submitted claims for fraud, the examiner should verify that the company has established control procedures to mitigate related risk factors. If the company has experienced a significant number of fraudulent claims, the examiner should perform additional procedures to determine the company's actions to prevent and detect fraudulent claims.				
1. Does the company have several claims within the first six months of a coverage period or during the policy's contestable period?				
2. Does the company typically accept photocopied claim forms?				
3. Does the company usually write insurance policies with excessive coverage limits for the type of risk insured?				
4. Does the company fail to adequately review submitted claims and therefore inadvertently process claims with the following characteristics?				
a. Write-outs, type-overs, and erasures;				
b. Misspelled medical terms, and terms inconsistent with the diagnosis or treatment;				
c. Suspiciously detailed or extremely vague information concerning the claim;				

FRAUD RISK FACTORS	COMPANY APPLICABILITY			
	Y	N	N/A	COMMENTS
d. Stamped or photocopied physician/lawyer approval;				
e. Claimant address is a post office box;				
f. Subjective diagnosis or general statement of diagnosis rather than actual records;				
g. Omitted or different personal information on the claim form;				
h. Claim indicates physicians, attorneys, or employers who are outside the claimant's geographical area, or who have been included on other questionable claims.				

EXHIBIT H– INSURER PROFILE SUMMARY TEMPLATE

An Insurer Profile Summary should be developed by the domestic state for each domestic insurer and updated as needed throughout the year. The Insurer Profile Summary should be concise and should contain information obtained from each of the five identified functions of the regulatory Risk-Focused Surveillance Cycle. A template of an Insurer Profile Summary is provided below; however, the actual form and content should be determined by each respective state. In addition, each state should determine how it will allocate its resources to create and maintain the Insurer Profile Summary document. Regardless of who creates and maintains the document, a current version should be available for the review of all internal departments upon request.

Company Name:
Address:
City, State, Zip:
Website:
NAIC CoCode #:
State of Domicile:
Type of Insurer:
Date of last Full-Scope Examination:
Next Scheduled Full- Scope Examination Date:
Limited-Scope Examinations (if applicable):

Business Summary: (This section should include a description of the business, such as types of products and markets.)

	Current Year	**Prior Year**
Rating Agency		
AM Best		
S&P		
Moody's		
Other Information		
RBC Ratio		
NAIC Score		
Department Priority		

Key Financial Strengths / Weaknesses: This section should include financial strengths / weaknesses based upon review of financial statements and from work performed by the financial analysts on key ratios of the company.

Strengths:

Weaknesses:

State Regulatory Information: This section should include a summary of the work performed by the state insurance department.

State Regulatory Concerns:

Findings from last examination:

Other State Regulatory Actions:

Other Regulatory Information: This section should include information obtained from the most recent 10-K, external audit opinion and Sarbanes-Oxley documentation. In addition, a summary of any significant findings can either be included in the space provided below or in a separate document.

SEC filings (if applicable):

External Audit Opinions:

Sarbanes-Oxley Documentation (if applicable):

Holding Company & Insurance Company Summaries

Holding Company Summary: [This section should provide the reader with critical information on the Insurance Company's holding company. This will include the profitability of the holding company, any guarantees the holding company may have on the insurance company and any reputational issues that the holding company may have.]

Insurance Company Summary: (This section will allow for comments based on all of the preceding information. Comments might address any of the following: company profitability, adequacy of loss reserves, reinsurance, intercompany transactions and significant issues surrounding corporate governance. This section gives the reader a sense of the company's financial condition and operations.]

EXHIBIT L – BRANDED RISK CLASSIFICATIONS

In order to assist examiners in categorizing identified risks, this exhibit links common risk areas and risk management controls to the branded risk classifications. This exhibit has been provided as a guide to the examiner and does not represent an all inclusive list of risk areas or risk management controls that will be identified when obtaining an understanding of the insurer's operations. Additionally, it should not be considered to be an exhaustive or definitive guide in determining the type of risk classification that would apply to each risk area, as each situation must be considered individually in the context of the insurer's environment in order to determine the appropriate branded risk classification. The nine risk classifications are to be identified in the Risk Assessment Matrix for each key activity being examined. More than one of the nine risk types may be applicable to a particular activity; as such, more than one risk type may be listed in the Risk Assessment Matrix. The following guidance is designed to help examiners think critically about the correlation between the nine risk classifications and various areas of the financial statements.

1. **Credit Risk -** Amounts actually collected or collectible are less than those contractually due.

   Risk Areas to consider:
   - Level and trend of non-investment grade, problem, restructured, delinquent and non-performing earning assets.
   - Existence of asset concentrations to include reinsurance recoverables and/or intercompany receivables.
   - Strength of affiliates involved in reinsurance pooling or asset participation arrangements.
   - Custodial arrangements.
   - Materiality of agents' balances.
   - Use of derivative or off-balance sheet transactions to mitigate credit risk (counter-party risk).
   - Premium and other receivables (i.e. Commissions, Refunds, etc.).

   Evaluating Credit Risk Management Controls (i.e., Effectiveness):
   - Policies established by management and the board are comprehensive and define risk tolerances, asset allocations, and accountabilities.
   - Underwriting standards and risk identification processes are in place, audited for compliance.
   - Exceptions (particularly management overrides) to policies and/or processes are reported to the board.
   - Through utilization of risk monitoring processes, problem assets (including agents' balances and affiliate receivables) are identified timely and collection steps initiated quickly.
   - Custodial arrangements are reviewed periodically and compliance to investment laws and regulations is monitored and reported to management and the board.
   - Reinsurers are evaluated regularly for financial strength.
   - Information systems are accurate, dependable, and validated.

2. **Market Risk -** Movement in market rates or prices, such as interest rates, foreign exchange rates, or equity prices adversely affect the reported and/or market value of investments.

   Risk areas to consider:
   - Income on investments.

- Composition and level of primary asset classes that are disposed to changes in value (e.g. derivative instruments, policy, mortgage and collateral loans) due to changes in:
  - stock markets;
  - interest rates;
  - currency exchange rates;
  - inflation;
  - industry sectors; and
  - global/national/regional economic conditions.

Evaluating Market Risk Management Controls (i.e., Effectiveness):

- Policies established by management and the board reflect an understanding of managing this risk (management overrides are prohibited).
- The process of managing this risk is effective and proactive (e.g., scenario impact modeling).
- Information systems are accurate, dependable, and validated.

3. **Pricing and Underwriting Risk -** Pricing and underwriting practices are inadequate to provide for risks assumed.

Risk Areas to consider:

- Composition and amount of growth in primary lines of direct, ceded, and assumed business by state/territory/distribution channel.
- New and/or discontinued products.
- Primary challenges to success.
- Reliance on asset returns to cover underwriting losses.
- Use of managing general agents or other concentration of writings.
- Underwriting performance of agents, brokers and sales personnel.
- Utilization of reinsurance to generate writing capacity.
- Catastrophe reinsurance program.
- Claim assessments and projections.

Evaluating Pricing and Underwriting Risk Management Controls (i.e., Effectiveness):

- Management and the board establish realistic and comprehensive goals/objectives and evaluate results.
- Changes in product pricing/underwriting are justified and reviewed by senior management for adherence to profitability/growth plans and objectives.
- Processes that include underwriting, pricing actuary and claims staff are in place to evaluate new product performance on a timely basis and report findings to management.
- Management overrides to pricing or underwriting limits/decisions/policies are reported to appropriate committee.
- Staff is competent and has appropriate level of experience.
- Utilization of credits and/or discounts is effectively monitored and reported upon.
- There is an active and thorough audit function for the detection of errors, overrides, and fraud.
- The plan of reinsurance and its effectiveness is evaluated and reported to the board.

- The risk of catastrophic loss is modeled and assessed periodically and appropriately included in pricing.
- Management compensation is tied to profitable performance.
- Informational systems are accurate, dependable, and validated.

4. **Reserving Risk -** Actual losses or other contractual payments reflected in reported reserves or other liabilities will be greater than estimated.

Risk areas to consider:

- Lines of business that generate significant reserves including methods and assumptions.
- Relevance of pooling as well as external third party ceded/assumed reinsurance.
- Use of internal versus external adjusting staff and claim processing procedures.
- Use of current technology and software.
- Loss adjustment expenses.

Evaluating Reserving Risk Management Controls (i.e., Effectiveness):

- Policies established by management and the board reflect a conservative approach toward reserving and reserving practices (management's ability to override the actuary's reserve estimate is limited and reported to the board/responsible committee).
- Historically, reserve levels have developed favorably.
- Staff responsible for recommending financial statement reserve levels is competent and experienced.
- Processes are in place to reliably, accurately, and timely evaluate prior and current period reserve levels (direct and net of reinsurance basis) for adequacy and report findings/recommendations to senior management.
- Reinsurance ceded/assumed is considered as a separate component of the reserve.
- Claims adjudication processes are well-documented, internal controls and limits of authority are clear and present, and there is an active audit function for the detection of errors, overrides, and fraud.
- Reserving actuary obtains relevant insight from pricing actuary, claims, and underwriting staff regarding emerging trends and product dynamics.
- Information systems are accurate, dependable, and validated.

5. **Liquidity Risk -** Inability to meet contractual obligations as they become due because of an inability to liquidate assets or obtain adequate funding without incurring unacceptable losses.

Risk areas to consider:

- Volume and growth of earning assets that are not publicly traded or do not lend themselves to securitization.
- Assessment of impaired securities (bonds, stocks, etc.).
- Investments in derivatives, securities lending and real estate.
- Sources of liquidity that are external to the insurer (particularly those available for emergencies).
- Extent of illiquid investments in affiliates (to include in working capital) including joint ventures, partnerships and limited liability companies.
- Policyholder dividends.
- Results of actuarial cash flow testing.

Evaluating Liquidity Risk Management Controls (i.e., Effectiveness):

- Policies (to include investment policy) established by management and the board reflect an understanding of managing this risk.
- Asset liability matching (ALM) analysis (i.e., scenario testing) is performed regularly for trends and reported upon to senior management and the board.
- Access to outside sources of liquidity (including affiliates) is adequate and available, particularly in emergencies.
- Liquidity considerations are factored into product design.
- All levels of management (i.e., short term cash, product actuaries, product and portfolio managers) are aware of the business activities that can trigger an adverse liquidity condition.

6. **Operational Risk -** Operational problems, such as inadequate information systems, breaches in internal controls, lack of internal controls over financial reporting, fraud, or unforeseen catastrophes will result in a disruption in business and financial loss.

Risk areas to consider:

- Incorporation of the internal audit function and program.
- Monitoring and evaluation of both financial and administrative internal controls as well as operational risks.
- Volume and complexity of transactions in relation to systems and hardware capacity and development.
- Internal controls to safeguard human, facility, and financial assets including antifraud initiatives and compliance with anti-money laundering requirements.
- Status of disaster recovery and business continuity programs.

Evaluating Operational Risk Management Controls (i.e., Effectiveness):

- Policy established by the board and/or senior management reflects an understanding of this risk.
- Programs are in place to identify, monitor, and evaluate operational risk.
- The audit function is qualified and possesses (or can obtain) the resources to accomplish its charter and implement the audit plan.
- Internal financial and administrative controls are monitored for effectiveness and completeness.
- The disaster recovery plan has been tested.

7. **Legal Risk -** Non-conformance with laws, rules, regulations, prescribed practices or ethical standards in any jurisdiction in which the entity operates will result in a disruption in business and financial loss.

Risk areas to consider:

- A process with assigned responsibilities is in place at the direction of senior management and the board of directors.
- Current litigation and or investigation.
- Sanctions or fines ongoing or over the past three years regarding compliance with either state or federal laws and/or regulations (including holding company considerations).
- Compliance with:
    - Company directives for insurance contracts, underwriting and investment decisions

- NAIC Statutory Accounting Principles and tax treatments
- State prescribed practices

Evaluating Legal Risk Management Controls (i.e., Effectiveness):

- Reporting of compliance exceptions to management and the board.
- Communication of compliance expectations (e.g., Code of Conduct, Conflicts of Interest) throughout the organization and distribution channels.
- Involvement of legal counsel with changes to products and new product development.
- Process and reporting of changes to regulatory requirements, litigation not in the normal course of claims-paying activities (includes disputes with reinsurers).

8. **Strategic Risk -** Inability to implement appropriate business plan, to make decisions, to allocate resources or to adapt to changes in the business environment will adversely affect competitive position and financial condition.

Risk areas to consider:

- Marketplace.
- Competition and benchmarking as well as financial projections and economic forecasts.
- Growth and mix of business.
- Experience level of management and the board of directors.
- New and or discontinued products/territories/distribution channels.
- Use of technology.
- Regulatory climate.
- Insurance holding company considerations.

Evaluating Strategic Risk Management Controls (i.e., Effectiveness):

- Historical and current success/failure in accomplishing stated strategic goals and operating/financial plans.
- Strategic goals (and the plans to implement them) and corporate culture are effectively communicated and applied throughout the organization.
- Initiatives and plans are well conceived, risks involved are well understood, and deliberated upon by management and the board.
- Risk management systems/processes are in place to evaluate results in relation to plan expectations.
- Access to capital, particularly in emergency situations.
- Assignment of responsibilities is clear and compensation is tied to achievement.

9. **Reputation Risk -** Negative publicity, whether true or not, causes a decline in the customer base, costly litigation, and/or revenue reductions.

Risk areas to consider:

- Customer service, current negative publicity and market conduct compliance.
- Antifraud initiatives and disaster recovery.
- Stability of financial strength ratings.
- Highly visible litigation and occurrence of same over the past three years.
- Marketing approach toward creating a positive brand relationship with the public and distribution force.
- Procedures used for claim processing.

Evaluating Reputation Risk Management Controls (i.e., Effectiveness):

- Establishment of policies/procedures by management and the board to respond to adverse publicity (include history of performance).
- Relationship with community (include distribution force).
- Contingency plans to mitigate risk in the event of a crisis.
- Process of disclosing financial performance to the public and distribution force.

W:\Sept09\Tf\Examo\Attachment Four-B.pdf

Draft: 9/29/09

IT Examination (E) Working Group
Conference Call
September 11, 2009

The IT Examination (E) Working Group of the Examination Oversight (E) Task Force met via conference call Sept. 11, 2009. The following Working Group members participated: Randy Milquet, Chair (WI); Jim Hattaway (AL); Earl Norton (AR); Howard Wong (CA); Cindy Revere (LA); Don Crowley (MD); Timothy Carroll (MO); Ke Xu (NC); Lisa Peterson (NE); Floyd Meeks (OH); Jerry Link (PA); and Pat McNaughton (WA).

1. Update on TeamMate and the Citrix Server

Mr. Milquet said 49 states are currently using TeamMate, and Tier 32 was finalized July 15, with 26 new licenses purchased. He said there are currently 33 states with examiners using the NAIC Citrix server, with a total of 97 examinations on the server and 344 user identifications currently in use. There has been a maximum of 87 concurrent users on the server at any given time, leading to some capacity issues that have recently been identified by the NAIC. At the current time, there is a waiting list to put an examination on the server, and the NAIC is not accepting new applications for single-state examinations. The Working Group plans to discuss a long-term solution to the Citrix server issues in future meetings.

2. Update on ACL and TeamMate Training

Mr. Milquet stated that there have been no updates to the NAIC ACL and TeamMate training schedules. He directed members to the NAIC Web site with further questions on the training programs.

3. Discussion of New Exhibit C within TeamMate

Mr. Milquet referred the Working Group to materials provided for information regarding the implementation of the recently adopted IT Review process and revised Exhibit C into the TeamMate TeamStore located on the NAIC Web site and on StateNet. Bruce Jenson (NAIC) explained the intent and structure of the new TeamStore. On a motion from Mr. Meeks, seconded by Mr. Hattaway, the Working Group approved the posting of the new TeamStore to the NAIC Web site and to StateNet for examiner use.

4. Planning/Summary Memos Going Forward

Mr. Milquet referred the Working Group to the current versions of the IT Planning and IT Summary Memos. He said both documents will need to be revised, based on the newly adopted IT Review process. He requested suggested changes be submitted to NAIC staff by Nov. 2.

5. Any Other Matters Brought Before the Working Group

Mr. Milquet stated that the TeamMate User Conference was held in August. There was a brief discussion held on the issues encountered as a result of the TeamMate upgrade to version 9.0.

There was a brief discussion on the state and NAIC guidance on obtaining holding company information on an examination. NAIC staff were asked to contact the Group Solvency Issues Working Group regarding the difficulties IT examiners had experienced in obtaining IT control documentation from non-insurance holding companies.

Mr. Milquet said there is a COBiT framework titled Quickstart that is designed for smaller companies. Mr. Meeks offered to review the guidance and provide feedback to the Working Group at a future meeting.

Having no further business, the IT Examination (E) Working Group adjourned.

W:\Sep09\TF\Examo\Attachment Five.doc