

SOLVENCY MODERNIZATION INITIATIVE (EX) TASK FORCE

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SOLVENCY MODERNIZATION INITIATIVE (EX) TASK FORCE
2010 Charges

The mission of the Solvency Modernization Initiative (EX) Task Force is to coordinate all NAIC efforts to successfully accomplish the Solvency Modernization Initiative. The Task Force will utilize the technical expertise of other NAIC groups, particularly for the five focus areas of the Solvency Modernization Initiative:

- Capital Requirements, which will be coordinated with the Capital Adequacy (E) Task Force;
- International Accounting, which will be coordinated with the Statutory Accounting Principles (E) Working Group as well as the International Accounting Standards (EX) Working Group;
- Group Supervision, which will be addressed by the Group Solvency Issues (EX) Working Group;
- Valuation Issues in Insurance, which will be coordinated with the Principles-Based Reserving (EX) Working Group; and
- Reinsurance, which will be coordinated with the Reinsurance (E) Task Force.

Ongoing Maintenance of NAIC Programs, Products or Services:

1. Provide oversight to the International Solvency Working Group and its charges to do the following:

- Assist the Task Force with all focus areas in the Solvency Modernization Initiative.
- Critically review and provide input and drafting to the International Association of Insurance Supervisors (IAIS) Solvency and Actuarial Issues Subcommittee, and on other IAIS papers as assigned by the parent Task Force. From this work, identify future initiatives to improve our regulatory solvency system.
- Analyze other financial supervisory modernization initiatives, to the extent appropriate. Analysis should include the following:
 - The Basel II international capital framework for banks and implementation in the U.S.;
 - Solvency work by the International Association of Insurance Supervisors (IAIS);
 - Solvency proposals in place or under development in other jurisdictions, including Australia, Canada, Switzerland and the EU.
 - Solvency improvements in place or under development in U.S. states.
- Complete the analysis of the U.S. solvency system compared to the EU Solvency II proposed system upon final action by the EU, and identify areas for U.S. regulators to consider including in the current NAIC programs.

— *Essential*

2. Provide oversight to the International Accounting Standards Working Group and its charges to do the following:

- Assist the Task Force with the international accounting focus area in the Solvency Modernization Initiative.
- Critically review and provide input and drafting to the IAIS Insurance Contracts Subcommittee, and on other IAIS papers as assigned by the parent Task Force. From this work, identify future initiatives to improve our regulatory solvency system.
- Analyze other financial supervisory modernization initiatives, to the extent appropriate. Analysis should include the following:
 - Accounting standards being developed by the International Accounting Standards Board (IASB).
- Monitor and provide comments directly or to the IAIS on the developments of the International Accounting Standards Board (IASB) and on the IASB and Financial Accounting Standards Board (FASB) joint convergence projects related to insurance accounting issues. Coordinate with the Statutory Accounting Principles (E) Working Group to provide responses to the FASB on joint projects; and
- Report findings relative to these developing issues to the Accounting Practices and Procedures (E) Task Force.

— *Essential*

SOLVENCY MODERNIZATION INITIATIVE (EX) TASK FORCE
2010 Charges

3. Provide oversight to the Group Solvency Issues Working Group and its charges to do the following:

- Assist the Task Force with the group focus area in the Solvency Modernization Initiative.
- Study the need to modify the Holding Company Model Act by gathering input from all states regarding the use of the existing model and its effectiveness in addressing the issues that exist within insurer groups, particularly considering issues identified during this most recent economic downturn. At the conclusion of such study, provide a recommendation to the Financial Condition (E) Committee, including a request for model law development/change if the recommendation is for the NAIC to devote its resources to such an effort.
- Study the international solvency issues related to groups and the need to modify the Holding Company Model Act for any proposed changes in this area. This study should include consideration of the interaction between federal and state financial regulators and any changes that would be necessary to improve regulatory oversight provided by the Holding Company Model Act. At the conclusion of such study, provide a recommendation to the Financial Condition (E) Committee.
- Study the need to develop group-wide supervision, which may include group-wide capital requirements. The study should consider possible approaches to such capital requirements, including how capital for financial conglomerates and non-regulated entities is calculated.
- Recommend courses of action regarding supervisory colleges and/or other methods of communication and coordination among cross-border (including cross-state) and cross-sectoral supervisors.
- Critically review and provide input and drafting to the International Association of Insurance Supervisors Insurance Groups and Cross-Sectoral Issues Subcommittee or on other IAIS papers as assigned by the parent Task Force. From this work, identify future initiatives to improve our regulatory solvency system.

—*Essential*

4. Provide oversight to the Principles-Based Reserving Working Group and its charges to do the following:

- Serve as a coordinating body with all NAIC technical groups involved with projects related to a principle-based approach to regulation and assist the Task Force with the “insurance valuation” focus area in the Solvency Modernization Initiative.
- Consider policy and practice issues related to principle-based regulation for life insurance and thereafter property and casualty insurance, including but not limited to the impact on areas such as corporate governance, examination and analysis, as well as staff resources and other insurance department administrative concerns.
- Focus on balancing theoretical approaches with effective regulatory practices to achieve desired end-results in solvency monitoring efforts, and further coordinate with NAIC leadership to provide direction to NAIC technical groups, including whether and to what degree principle-based approaches should be pursued, setting timelines for such pursuit, and ensuring other issues are addressed prior to or concurrently with implementation of principle-based approaches by the technical groups.
- Report the status of its work to, and seek guidance from, the parent committee no less frequently than a quarterly basis.
- Evaluate necessary changes to existing state insurance laws, regulations or administrative policies to effectuate a principle-based regulatory framework
- Critically review and provide input and drafting on the International Association of Insurance Supervisors papers, as assigned by the parent Task Force. From this work, identify future initiatives to improve our regulatory solvency system.

—*Essential*

SOLVENCY MODERNIZATION INITIATIVE (EX) TASK FORCE
2010 Charges

5. Monitor solvency-related work products of the International Association of Insurance Supervisors (IAIS). Assign papers to working groups to submit comments to the IAIS. Additionally, the Working Groups should review the papers and recommend whether and/or how the ideas in those papers should be implemented in the U.S. regulatory solvency system. —
Essential
6. Communicate and coordinate with the International Insurance Relations (G) Committee and provide technical support to the Committee as needed. —*Essential*
7. Report the status of its work to the Executive Committee no less frequently than on a quarterly basis.
—*Essential*

New Objectives and Goals (*representing new NAIC programs, services or initiatives*):

None

Sponsors for Proposed 2010 Charges:

(Except as noted, I support all charges)

Commissioner/Director
State

Alfred Gross
VA

Staff Support: Kris DeFrain/George Brady/Todd Sells

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**Symposium on U.S.
Insurance Regulation**

What Have We Learned?

Where Do We Go?

July 13-14, 2009

Mary A. Weiss, Ph.D.

Participants

- Regulators
- Academics
- Industry CFOs and CROs
- Consumer Representatives
- Guaranty Fund Representatives



Purpose

Bring together well-informed participants:

**To deliberate on the lessons learned from
the current financial crisis
international developments**

**To conceptualize the future of insurance
solvency regulation**



Panel Discussion Topics

- I. Capital Adequacy Standards**
- II. Regulatory Processes/Intervention and Resources**
- III. Holding Company/ Group Supervision**



Capital Adequacy Standards

How useful is the RBC system?

When is the use of internal models
and/or standard models appropriate?

Should an insurer's ERM become part of
solvency surveillance?



How Useful is the RBC System?

- **RBC system works**
 - Solvency record
- **Dissenters**
 - Take advantage of improved technology
 - Possibility of systemic risk



When Is the Use of Internal and/or Standard Models Appropriate?

- **Use two-part system**
 - Baseline, floor model
 - Internal model
 - Multi-year
 - Small insurers
 - Regulatory resources



Should Insurer ERM Become Part of Solvency Surveillance?

- **ERM is important**
 - Insolvencies associated with management failures
- **Regulatory recognition ERM is insurer specific**
 - No cookie cutters!
- **ERM development within industry**
 - Some insurers further along



Regulatory Processes/Intervention and Resources

- How well overall has the regulatory system worked?
- What are the problems with the present regulatory system?
- How can the present system be improved upon?



How Well Overall Has the Regulatory System Worked?

- State-based system effective (vis a vis banking)
 - Efficiency Vs Natural Experiments
- Risk-focused exams important
 - Dialogue between examiner and management



What Are the Problems with the Present Regulatory System?

- Place more emphasis on evaluating management and corporate governance
- Regulatory authority limited in some cases
- More accountability needed
 - “post-mortem” on insolvent insurers
 - best practices for timing and type of intervention



How Can the Present System Be Improved Upon?

- Improved disclosure
 - Off B/S, remuneration systems
- More of ERM focus
 - Forward-looking
- Qualitative Assessments
 - Internal controls and corporate governance
- Stress testing



Holding Company/Group Supervision

- What are the challenges involved in supervising groups?
- What additional challenges exist in regulating multi-country groups?



What Are the Challenges Involved in Supervising Groups?

- Expertise needed to supervise *entire* group, so...
- Authority over unregulated group subs
- Group supervisory colleges good idea
- Regulation of group vs firm



What Additional Challenges Exist in Regulating Multi-country Groups?

- Fungibility of capital
 - Movement of “excess capital” among group
 - Allocation of capital if insolvency
- Regulatory arbitrage
 - Option to choose lead supervisor



Conclusion

Main ideas

- ERM
- Corporate Governance/Internal Control
- State regulation works!



Thank you!



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Draft: 9/29/09

International Accounting Standards (EX) Working Group
Washington, DC
September 22, 2009

The International Accounting Standards (EX) Working Group of the Solvency Modernization Initiative (EX) Task Force met in Washington, DC, Sept. 22, 2009. The following Working Group members participated: Mel Anderson, Chair (AR); Richard Ford (AL); Christina Urias represented by Steve Ferguson (AZ); Louis Quan (CA); Gennet Purcell represented by Philip Barlow (DC); Al Willis (FL); Jim Armstrong (IA); Jaki Gardner (MN); Ann Frohman (NE); Lou Felice and Joseph Fritsch (NY); Mary Miller (OH); Alfred W. Gross represented by David Smith (VA); and Peter Medley (WI).

1. Report on IASB, FASB, ICSC and FCAG matters

Rob Esson (NAIC) provided a set of reports on International Accounting Standards Board (IASB) and Financial Accounting Standards Board (FASB) decisions in the last quarter relating to the Insurance Contracts Project, the financial instruments replacement project, the exposure draft on fair value measurement, and the activities of the Financial Crisis Advisory Group (FCAG). He also reported on the meetings and work of the International Association of Insurance Supervisors' (IAIS) Insurance Contracts Subcommittee (ICSC) (Attachment Three-A). He also provided a report on the IASB roundtable on financial instrument classification (Attachment Three-B). As a result of these updates, Mr. Anderson encouraged the Working Group to provide input to the IAIS Insurance Contracts Subcommittee on the forthcoming exposure draft on insurance contracts and the future exposure drafts on financial instruments.

Mr. Esson gave a presentation that he had provided to a joint meeting of the IASB and FASB in July (Attachment Three-C).

Ed Stephenson (Group of North American Insurance Enterprises—GNAIE) noted that GNAIE did not agree with the IAIS position regarding the urgency of the insurance contracts project, stating that it was better to complete the project correctly rather than quickly.

Morag Fullilove (GNAIE) noted that GNAIE, along with other U.S. trade associations, would be providing input and comment to the International Accounting Standards Committee Foundation regarding the potential changes to its constitution, and specifically requesting that the IAIS be provided the same observer status as the Basel Committee on Banking Supervision.

2. Consideration of 2010 Charges

The Working Group considered the prior-year charges for any possible updates. After discussion, the Working Group decided to recommend to the Task Force that an additional charge should be added to "Coordinate responses to the FASB on joint projects with the Statutory Accounting Principles (E) Working Group" so that, for example, U.S. input into the responses from the ICSC would not diverge unnecessarily from U.S. responses on the same issues to the FASB.

Having no further business, the International Solvency and Accounting (EX) Working Group adjourned.

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MEMORANDUM

DATE: September 18, 2009
TO: International Accounting Standards (EX) Working Group
FROM: Rob Esson
RE: Update on IASB, FASB, ICSC and FCAG matters

This memo provides an update on the International Accounting Standards Board (IASB), Financial Accounting Standards Board (FASB), Insurance Contracts Subcommittee (ICSC) and Financial Crisis Advisory Group (FCAG) matters. The main areas for reporting since June are insurance contracts, fair value, financial instruments, liabilities, and the FCAG & the International Association of Insurance Supervisors (IAIS) Insurance Contracts Subcommittee.

Insurance contracts:

The latest timetable issued by the Board shows an Exposure Draft (ED) being issued in December with comments due by May 2010, and a final standard by June 2011.

Although the project was discussed at both the June and July meetings, the only decision of major importance was the decision to use an unearned premium approach to short duration contracts, although the details were left undefined.

At the Sept. 18, 2009 meeting, there was a narrow 8-7 decision in favor of the IAS 37 measurement approach (this would have a separate risk, service and residual margin, although how these would be calculated was unspecified). Given the narrowness of this majority, the IASB will present the alternative view of the fulfillment value. It is not clear from the discussion exactly how this will be presented, but the IAS 37 approach will be the primary approach represented. It was noted that the FASB has decided to go with a current fulfillment value (CFV) approach and will be putting out an ED on that basis.

Margin release—No decision was taken on the driver of margin release. More information on the Australian approach of releasing service margins in life contracts will be sought, as well as asking participants in field testing about the appropriate approach. On the question about the period over which the residual or composite margin should be released, the board chose the coverage period, again with a narrow margin of 8-7. There was a question as to what the relationship is between the residual margin under the IAS 37 approach (or composite margins under fulfillment value) and subsequent changes in estimates. Two approaches were presented: Approach A—The margin remains locked in at the amount determined at inception and is released over the remaining period of the contract so subsequent changes in estimates will appear in the income statement; Approach B—The margin is adjusted for subsequent changes in estimates (that is, it acts as a shock absorber). The board agreed to approach A, with 11 votes in favor.

Regarding discount rates, the board agreed to:

- Set as the objective a discount rate that reflects the characteristics of the liability and use this as a principle rather than setting a particular rate for reasons of comparability.
- Provide no specific guidance on how to estimate a discount rate for insurance liabilities, beyond providing a cross-reference to the guidance on fair value measurements.
- Seek input from practitioners about adjusting discount rates derived from highly liquid assets so that they can be applied to illiquid insurance liabilities.

At the end of this meeting, I requested further regulator-to-Board meetings, as I felt that it was particularly inappropriate that the current fulfillment approach had been presented as if it would not re-measure cash flows and margins, and that it would not use the three building blocks. As a result, I believe, some Board members voted against CFV on this erroneous basis.

Fair value:

Suggested reading: IASBFairValueSnapshot.pdf

Deep background reading: IASB_EDFairValueMeasurement.pdf

The IASB has issued an exposure draft of its fair value measurement standard for comment through Sept. 28. The ED is based upon FAS 157, and incorporates as additional sections the recent guidance (FSP 157-4) in U.S. GAAP. The deadline for comment is Sept. 28, and the IAIS Insurance Contracts Subcommittee will respond.

The IASB has also announced a set of roundtables on fair value measurement—Nov. 2 in Norwalk, Nov. 27 in Tokyo and Dec. 11 in London. I will likely be attending one of these on behalf of the IAIS. Input from Working Group members on this issue would be appreciated.

Financial Instruments:

IASB_Classn_and_Measurement_snapshot.pdf

FASB_Classn_and_Measurement_snapshot.pdf

Fin_Instr_FASB_IASB_comparison.pdf

090911 IAIS to D Tweedie re ED FI measurement and classification final.pdf

FinInstr_Comment_letter_analysis.pdf

Deep background reading: EDFinancialInstrumentsClassificationandMeasurement.pdf

The IASB issued its exposure draft on financial instruments classification and measurement in July with a comment deadline of Sept. 14. The IAIS Insurance Contracts Subcommittee, with U.S. input, provided a response to the IASB. The IASB ED proposed two main classifications: amortized cost and fair value. Fair value would be measured through P/L (with a limited exception for “strategic” equity investments through OCI). Amortized cost would be used for financial instruments with basic loan features managed on a contractual yield basis. The amortized cost basis would no longer be subject to tainting, but gain and loss on sale of instruments at amortized cost would need separate disclosure. A fair value option would be allowed on initial recognition.

The IAIS response supported an additional attribute of fair value through OCI (FVTOCI) with recycling. The response was also cognizant of the likely requirements of the Basel Committee so as to be inclusive of banking regulators’ needs while at the same time providing an insurance perspective.

The IASB intends to issue two more exposure drafts this year. In October it will issue an ED on impairment, and in December it will issue an ED on hedge accounting. It intends to issue the new IFRS as soon as it is able,

possibly early in the first quarter, but to allow (but not require) the final requirements on classification and measurement to be applied to year-end 2009 financial statements. The IASB aims to have replaced all of the requirements of IAS 39 during 2010.

At present, the Board intends that there will be only one impairment methodology, and it is under significant political pressure to ensure that this methodology is some form of expected cash flow approach.

The FASB, while apparently intending to endeavor to converge, is pursuing a different approach. It will issue only one exposure draft by the end of the year or in early 2010, covering measurement, classification, impairment and hedge accounting. The FASB does not agree at present with the IASB classification proposals, particularly on the amortized cost category, and wants to pursue a full fair value method in the balance sheet, with either measurement through net income or, for debt instruments not for trading, with interest less credit losses through income and the rest in OCI. How this difference will be reconciled with the IASB is open to question at present.

The IASB's Financial Instruments Working Group met in early September to discuss the IASB proposals. There was a great deal of opposition to the IASB's proposals, and many thought that an additional attribute of FVTOCI should be available.

In addition, there have been roundtables held in London and Norwalk. A separate report on the Norwalk roundtable, which had significant insurance sector participation, is supplied.

IAS 37 Liabilities standard replacement:

The Board intends to issue a new IFRS on liability measurement. Originally, it intended to update IAS 37, but the project has grown and become more complex. Regrettably, the Board's thinking has not necessarily become a great deal clearer. At its meeting on Sept. 16, Board members were split on whether uncertain liabilities needed a risk adjustment in addition to the expected cash flows, and if so, how the risk margin would be calculated. Nonetheless, a majority did agree that liabilities should be built up using the same three building blocks as insurance. It is clear, however, that considerably more discussion will be required before the Board can come to a common view on the details of measurement.

Financial Crisis Advisory Group:

Suggested reading: *Pages 18-21 of FCAGReport29July_LD.pdf*

The Financial Crisis Advisory Group (FCAG) was formed under the aegis of the IASB and FASB. The scope of the group included the following: "The advisory group will consider how improvements in financial reporting could help enhance investor confidence in financial markets. The advisory group also will help identify significant accounting issues that require urgent and immediate attention of the boards, as well as issues for longer-term consideration."

The group met six times in total. The IAIS had a seat and was represented by Commissioner Al Gross (VA) in his capacity as chair of the IAIS Technical Committee. I represented Commissioner Gross at the last four meetings.

The FCAG issued its report in July. The report focused on effective financial reporting, its limitations, convergence (especially IASB and FASB), and standard setter independence and accountability. Within the first item, a principle similar to that of the IAIS was espoused: "Where regulatory standards differ from accounting standards in ways that could have significant effects on financial reporting, the effects of those differences should be disclosed in a manner that does not compromise the transparency and integrity of financial reporting."

One recommendation in the report regarding convergence was: "To sustain momentum, we encourage all national governments that have not already done so to set a timetable that is both practicable and firm for adopting or converging with IFRS." This included the U.S., in that many FCAG members thought that it would be important for the U.S. to issue a timetable for convergence.

Insurance Contracts Subcommittee:

The IAIS Insurance Contracts Subcommittee met twice in the last quarter. It discussed the various IASB requests for information and exposure drafts, the IAIS presentation to the joint IASB/FASB meeting, and the work on the IAIS joint valuation working group.

As a result of this work, the Subcommittee issued three letters to the IASB on an expected loss approach for impairment, own credit standing for liabilities, and on classification and measurement for financial instruments (see above). The letters are attached to this memo.

Attachments: ICSC 090901 IAIS to D Tweedie re own credit risk final.pdf
ICSC 090901 IAIS to D Tweedie re rfc impairment expected loss final.pdf

In addition, it agreed in advance the content of a presentation that I made to the joint IASB/FASB meeting on July 23. This presentation covered timing of the insurance contracts project, acquisition costs, run-off of margins, and the importance of the financial instruments projects to insurers. The presentation is also attached to this memo. The presentation seemed well received by the Boards, and as a follow-up, I will represent the IAIS and Joe Fritsch (NY) will represent the NAIC at an education session before the FASB on Sept. 30. In particular, the FASB wishes to understand the issues surrounding acquisition costs and the evaluation of cash flows at the beginning of a policy period, especially where such cash flows evaluate as an asset.

Attachment: 090716 - Esson Presentation to Joint IASB-FASB July 09.ppt

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National Association of
Insurance Commissioners

M E M O R A N D U M

DATE: September 14, 2009
TO: International Accounting Standards (EX) Working Group
FROM: Rob Esson
RE: Norwalk Roundtable on Financial Instruments Classification and Measurement

I attended the IASB/FASB roundtable on Financial Instruments Classification and Measurement today at the FASB on behalf of the International Association of Insurance Supervisors (IAIS). The roundtable had significant insurance sector involvement: I represented insurance regulators, Brad Hunkler represented the American Council of Life Insurers (ACLI), Kevin Spataro represented the Group of North American Insurance Enterprises (GNAIE), and Craig Mense represented CNA. The following documents those parts of the conversations that I felt were noteworthy.

I made an opening statement about the importance of this project to the insurance sector: I said that insurers were either the largest or one of the largest purchasers of financial instruments in the world, that the measurement attribute for insurance contracts was still uncertain—yet asset/liability matching is extremely important to insurers—and that accounting does affect behavior, so there was the scope for significant and potentially macro-prudential and macro-economic unintended consequences unless the projects were carefully coordinated.

Matt Schroeder (Goldman Sachs) said that fair value through P&L focuses the mind significantly. Mr. Spataro replied that “through P&L” does not necessarily enable matching, and increases in equity may not be available for dividends or other distribution.

John Smith (IASB) asked John Gallagher (UBS) what cut the bankers would make. He replied that if cash flows are predictable, then amortized cost should be available. Bob Herz (Chairman, FASB) asked what information amortized cost provided. Mr. Mense replied that accounting should reflect what goes on in the business. For example, he said that CNA had approximately 95% of its assets as available for sale (AFS). He did not understand why AFS was no longer going to be allowed. During the fourth quarter, CNA had a \$2 billion decrease in invested assets value followed by a \$2 billion increase in the first half of 2009. He queried whether it was useful to have these movements through P&L.

Tony Sondhi (CFA Institute) asked what analyst does not focus on fair value. Tom Linsmeier (FASB) queried the appropriateness of a business model cut where the primacy is to hold assets for collection, noting that risks occur when you cannot hold to collection. He asked why one would concentrate on a model that assumes you can hold.

Tom Panther (American Bankers Association) said that they would prefer to look at cash flows rather than amortized cost per se or fair value per se. If banks hold for collection of the cash flows, then volatility in fair value was less relevant.

Scott Blackley (Fannie Mae) said that they have had \$25 billion swings in fair value based merely on investor sentiment, and it was difficult to say that this was appropriate to be reflected in the P&L. From a management perspective, they look at fair value daily. However, he said that he believed that both amortized cost and fair value

information was important. He thought that the fair value through other comprehensive income (OCI) was an elegant solution to a “religious war.”

Hal Schroeder (Carlson Capital) asserted that matching does not work and, consequently, one needed fair value. Mr. Hunkler replied that fair value has caused many bad decisions, especially in up markets—for example, people took cash out of their houses, and companies increased leverage purely on an unrealized fair value basis.

Alan Zimmerman (Fox-Pitt Kelton) said that he thought putting all the information (both fair value and amortized cost) on one statement would give users the information they needed. Mr. John Smith replied that dual disclosure may be useful. He asked about the concerns surrounding fair value through OCI. Craig Mense replied that the question was which is more important: the balance sheet or the profit and loss. Hal Schroeder stated that in his view, if one gets the balance sheet right, the P&L is a balancing item.

Bob Uhl (Deloitte) said that one needed both items in prominent display. He noted that not every regulator treats OCI the same way. He thought that fair value through OCI raises some complexity issues.

Mr. Schroeder recommended looking at the FAS107 disclosures and the quality of their marks (to market).

I said that I thought an unstated part of many peoples’ difficulties is that we have not dealt with dispersion of estimates and uncertainty in any systematic manner.

Mr. Spataro said that was one of the reasons why fair value through OCI with recycling should be allowed. Larry Smith (FASB) asked why it should not be through P&L, and Mr. Spataro replied that insurance liabilities are very long-term, and the volatility of the assets being reflected in the P&L was not particularly useful.

Vincent Daniel (FrontPoint Partners) said that there were potentially a number of different levels of equity portfolios that insurers might hold, and if these were all reflected through OCI, it may not be obvious that they were exposed to different risks. I replied that regulators would increase the capital requirements for insurers with large equity portfolios to reflect the volatility risk, and that this would be obvious. He replied that he had no confidence after the financial crisis in regulatory capital requirements. Mr. Herz jumped in at this stage and said that insurance regulation was different to banking regulation, noting that the accounting was not so joined at the hip.

Mr. Hunkler said that fair value through OCI was useful but if realizations were without recycling, the usefulness would decrease.

Mr. Zimmerman said that he believed the comprehensive income was more important than either OCI or P&L, although he admitted that this was his personal opinion. Mr. Spataro replied that he believed it was important to have both. He said that the entities do not pay claims, dividends, debt, etc., with unrealized gains.

Mr. John Smith said that fair value through OCI was not intended to be an election, merely an exception for strategic investments. However, the boards have been unable to define “strategic.” He asked whether those who wanted recycling would accept a lower of cost or market model, which would eliminate the requirement for a separate impairment model. Mr. Hunkler replied that he would be strongly opposed to a lower of cost and market model.

There was a brief discussion about embedded derivatives. Enrique Tejerina (KPMG) stated that he liked the IASB model.

The discussion then moved to convergence. I asked how this could be achieved politically, given that the IASB will be issuing a standard on classification and measurement before the end of 2009, whereas the FASB will not issue its standard until 2010. Unless the FASB simply accepts the IASB model, I queried how convergence could be achieved.

Larry Smith (FASB) said that the boards were trying to converge, but Jim Leisenring admitted that those requiring a standard to be in place by Dec. 31, 2009, may have to accept that for convergence there may be two standards in rapid succession. Mr. Herz stated that he was committed to convergence, but U.S. law also required the FASB to undertake certain actions which could not be done in time to enable immediate convergence.


Mr. Panther said that the biggest risk of the IASB's three-phase process is impairment.

Mr. Zimmerman recommended the IASB's alternate view (Steve Cooper's model) as an acceptable compromise between the Boards.

Mark Scoles (Grant Thornton) said that if convergence is the end goal, then the Boards have to draw the line between different measurement attributes at the same place using the same words. Mr. Hunkler replied that there are some parallels between the income statements in the two models proposed by the Boards, but the balance sheets have large differences. Carlo Pippolo (Ernst & Young) stated that it would have been preferable if the IASB could wait before issuance of its standards.


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IAIS presentation to joint IASB/FASB meeting



London, 23 July 2009

Rob Esson, Chair, Insurance Contracts Subcommittee




Agenda

Topics we will address today

- Timing of the Insurance Contracts project
- Acquisition costs
 - Long-term policies cash flow
 - Contract boundaries
- Day 2 / Day 366 – run-off of the margins
- Financial Instruments issues


July 2009
IAIS presentation to joint IASB/FASB meeting
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Timing of the Insurance Contracts Project

- The project has taken 10+ years ... and counting
- Today's timetable envisages a December ED and May 2011 standard
- Further delays are unacceptable – international consensus is beginning to break down as regions cannot wait
- IAIS aim is still to utilize IFRS/GAAP as input into insurance regulatory requirements


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Acquisition costs


- Pricing at time zero immediately before issuance is the same as cash flow expectations plus a composite margin
- Acquisition costs become payable on day 1
- Acquisition costs can exceed first year's premium for long-term contracts
- Generally expect profitable long-term contracts
- Subsequent cash flow expectations are presumably unchanged by payment of acquisition costs
- Hence the cash flows for profitable long-term contracts imply an asset at time zero (margin'd out), and a bigger asset after payment of acquisition costs

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 **Contract boundaries**


- IAIS recommendation to the Boards:
- “The relevant cash flows are bounded by the earlier of the following, if they exist:
 - the contractual termination date as extended by any unilateral option available to the policyholder, or
 - the insurer having a unilateral right to cancel or freely re-underwrite the policy, or
 - both the insurer and policyholder being jointly involved in making a bilateral decision regarding continuation of the policy.”

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 **Day 2 / Day 366**


- Run-off of margins almost entirely not discussed in the last 10 years
- It desperately needs to be solved before the ED
- The answer must be simple, understandable and auditable
- Following slides provide a deliberately simple example to illustrate the issues

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 **Margin run-off example**


- Non-life 1 year policy. Expected loss cash flows 80. Premium 100, therefore composite margin 20.
- If the first year is analogized to revenue recognition, the performance obligation is satisfied over the year. At the end of the year, there will be future expected losses
- Assume no claim payments have yet occurred and no reason to change the estimates of loss cash flows

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 **Margin run-off example continued**


- Day 366, building block one – expected probability weighted cash flows relating to claims incurred and IBNR are still 80.
- What is the margin?
- Is it still 20, as the future cash flows (and uncertainty) have not changed?
- Is it zero, as the risk underlying the policy has run-off, i.e. no further claims can in fact occur and it is merely loss estimation?
- Is it something in between?

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 **Margin run-off example continued**


- Do the margins run off based on release from risk – if so, and the risk is the underwriting risk, then this would argue for the 20 to run off in year one.
- Do the margins run off based on the expected cash flows, which could be analogized to FAS114 as a fixed percentage of the remaining cash flows relative to the originally assumed cash flows.
- Need the answers in time for the ED

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 **Financial Instruments**


- Two most significant parts of an insurer's balance sheet – insurance contracts and financial instruments
- Insurers are the largest purchasers of financial instruments in the world
- Need to have regard to consistency on asset and liability side of the balance sheet
- Asset/Liability management is vital to insurers

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 **Financial Instruments, continued**

- There needs to be coherence between asset and liability measures: timings of the projects problematical
- Fundamental institutional factors exist: banks and insurers are different, and while cross sectoral comparability is important, a bank solution may cause significant problems for insurers
- How will assumptions unlock and margins run off for liabilities – and will amortized cost “hedge” these liabilities?

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 **International Association of Insurance Supervisors (IAIS)**

Questions and Answers

www.iaisweb.org

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Draft: 9/28/09

International Solvency (EX) Working Group
Washington, DC
September 22, 2009

The International Solvency (EX) Working Group of the Solvency Modernization Initiative (EX) Task Force met in Washington, DC, Sept. 22, 2009. The following Working Group members participated: Christina Urias, Chair (AZ); Mel Anderson (AR); Louis Quan and Ronald Dalhquist (CA); Gennet Purcell and Philip Barlow (DC); Al Willis (FL); Jaki Gardner (MN); Ann Frohman (NE); Alan Seeley (NM); Lou Felice and Joseph Fritsch (NY); Mary Miller (OH); Alfred W. Gross represented by Doug Stolte and David Smith (VA); and Peter Medley (WI). Also participating was: Steve Ferguson (AZ).

1. 2010 Working Group Charges

Director Urias said the former International Solvency and Accounting (EX) Working Group was split into two working groups: the International Solvency (EX) Working Group, which she would chair, and the International Accounting Standards (EX) Working Group, which Mr. Anderson would chair.

The Working Group reviewed the 2010 charges to be considered by its parent task force and had no changes to propose. Mr. Seeley asked whether there was cross-over between the working groups, because this Working Group is charged to work on all focus areas, while other groups also have individual focus areas as their main charge. Director Urias said there is need for significant coordination, explaining that this Working Group is charged with working on all focus areas, because of its involvement in creating a Solvency Modernization Initiative (SMI) roadmap, as well as performing studies of other systems.

2. Solvency Modernization Initiative (SMI) Roadmap

Director Urias said the Solvency Modernization Initiative Task Force asked the Working Group to develop a roadmap for the SMI. The first working draft of the SMI roadmap was developed based on the Working Group's adopted document titled, "Issues for Consideration in the Solvency Modernization Initiative." Ramon Calderon (NAIC) presented the draft roadmap. He said there are three processes related to the SMI: 1) look at ourselves; 2) look outside ourselves; and 3) make changes to the current system. Mr. Felice said that work on the SMI related to capital requirements began a year ago, so there is a question whether that work should stop or be included in the SMI roadmap. On a motion from Mr. Felice and second from Mr. Medley, the Working Group received the SMI Roadmap and will continue to use it as a working document (Attachment Four-A).

Brad Kadling (Association of Bermuda Insurers and Reinsurers—ABIR) said the ABIR is working on compliance with the European Union's Solvency II and the new Bermuda regulatory systems. He offered assistance to the Working Group.

As part of the studies of other solvency systems, the Working Group will have a regulator-to-regulator meeting with Swiss and Canadian regulators Oct. 5–6 in New York. Dr. Mary Weiss (NAIC) prepared a pre-meeting webinar on the Swiss Solvency Test so that regulators would be prepared for productive discussions. The webinar is also available to interested parties through the NAIC Education and Training Department.

3. IAIS Solvency Subcommittee Report

Kris DeFrain (NAIC) said the International Association of Insurance Supervisors (IAIS) Solvency Subcommittee met in July and September (Attachments Four-C and Four-B). The Subcommittee discussed the IAIS' expected modification to the Insurance Core Principles (ICPs). This work needs significant monitoring and input, because the result will be the new insurance supervisory standards under which each country is assessed in the Financial Sector Assessment Program (FSAP).

The Subcommittee will distribute numerous papers for comment over the next quarter (investment standards and guidance papers likely by the end of September), so the Working Group will have multiple conference calls. Also, the Subcommittee will modify many of the previously adopted IAIS solvency papers that providing for solo-entity supervision requirement to also apply to group supervision.

Ms. DeFrain said the U.S. submitted preliminary views on valuation to the IAIS and succeeded in getting the draft standard modified so that market-consistent valuation is not the only accepted approach to achieve an economic valuation (whereby amortized cost might be appropriate if matched to long-term liabilities). However, the European Commission is expected to approach this issue at the IAIS Technical Committee to try to impose market consistency as an IAIS requirement. Mr. Fritsch said the IAIS principles and standards should be flexible, especially regarding accounting and valuation issues. The IAIS' joint valuation drafting group (between IAIS Solvency and IAIS Insurance Contracts) will continue to work on valuation guidance; the United States needs a representative to participate on that joint group.

Mr. Fritsch continues to lead work on supervisory monitoring papers: one on supervisory review and one on supervisory reporting. The work will incorporate U.S. views on supervisory reporting, public disclosure, financial analysis and financial examination. Following the IAIS Solvency Subcommittee chair's request, the Subcommittee modified the paper to increase concentration more on the reporting and review for current IAIS standards to include, sections on internal models, enterprise risk management, capital, investments and valuation which, will likely lead to new reporting and review standards.

4. IAIS Technical Committee Roadmap

Director Urias said the IAIS Technical Committee is the parent committee to the IAIS subcommittees supported in the SMI and it will be adopting its annual IAIS roadmap soon. George Brady (NAIC) said the roadmap identifies strategic themes to pursue through standards and then charges the subcommittees to follow through with those plans. One such theme identified is financial stability concerns. For the IAIS Solvency Subcommittee, the general mandate is to review existing papers to account for lessons learned from the financial crisis. He said there is also a Common Assessment Framework Task Force for Solvency that was formed to analyze the issues of supervising internationally active groups, but not necessarily formed to create a framework. When asked by Director Urias, Mr. Brady said the roadmap is a responsibility for assigned U.S. representatives and the SMI Task Force, but any comments are welcome.

Having no further business, the International Solvency (EX) Working Group adjourned.

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----DRAFT Working Document----

Solvency Modernization Initiative Work Plan (Roadmap)

Solvency Modernization Initiative (SMI) Overview

The NAIC's Solvency Modernization Initiative (SMI) began in June 2008. The SMI is a critical self-examination of the United States' insurance solvency regulation framework and includes a review of international developments regarding insurance supervision, banking supervision, and international accounting standards and their potential use in U.S. insurance regulation. While U.S. insurance solvency regulation is updated on a continual basis, the SMI will focus on five key solvency areas: capital requirements, international accounting, insurance valuation, reinsurance, and group regulatory issues.

The initiative includes the following:

- Articulation of the U.S. solvency framework and principles.
- Study of other sectors' and other countries' solvency and accounting initiatives and the tools that are used and proposed.
- Creation of a new reinsurance regulatory framework.
- Movement to principle-based reserving for life insurance products.
- Enhancement of group supervision.
- Ultimately, implementation of new ideas to incorporate into the U.S. solvency system.

Issues for Consideration in the SMI

On June 14, 2009, the NAIC adopted a first draft of a working document titled "Issues for Consideration in the Solvency Modernization Initiative." That paper was designed to provide some initial ideas for consideration in the Solvency Modernization Initiative, albeit not an exhaustive list.

This document expands those initial ideas, adds timelines, and identifies sources of information, study, and research. Eventually, NAIC charges will be created from this work plan.

Work Plan

As a first step, the following identifies some key tasks, estimated target deadlines, and primary NAIC support. The timelines are defined as "Short-term" (less than 6 months), "Medium-term" (6-12 months), and "Long-term" (1-3 years).

- I. Articulate U.S. Solvency Framework and Principles *E Committee supported by CIPR, short-term*
- II. Study Other Solvency Systems *ISWG supported by CIPR, short-term*
 - a. IAIS relevant standards and ICP essential criteria
Comparison to IAIS (expanding beyond the analysis to ICP Principles done in FSAP)
 - b. U.S. banking supervision & Basel II
 - c. Develop questionnaire to solvency supervisors—what do we want to know about other insurance systems?
Utilize IAIS work to date.
 - d. EU Solvency II and comparison to U.S. solvency in more detail—update comparison document
 - e. Australia
 - f. Bermuda
 - g. Canada
 - h. Switzerland SST
 - i. UK ICAS

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----DRAFT Working Document----

Solvency Modernization Initiative
Work Plan (Roadmap)

III. Research and Make Recommendations

1. Capital Requirements

CADTF/ISWG, staff to develop exposure document to ask questions such as, "If you were creating RBC from scratch, what would you change?" and "What is the fundamental structure and conceptual framework in the U.S. and why should it be different from other sectors and countries?" and "What is the significance of market discipline?"

—Staff questions: short-term

—Expose for comment: medium-term

2. ERM/risk-focused surveillance

ISWG, staff to develop exposure document to ask questions such as, "What would you recommend be included in a U.S. ORSA?" and "What NAIC support is needed for risk-focused surveillance?" and "What stress testing is needed?" and "What governance or internal controls is needed beyond that needed for PBR?"

—Staff questions: short-term

—Expose for comment: medium-term

—NAIC/AICPA to be consulted regarding governance/auditing: long-term

3. International Accounting

a. Study of IASB/IFRS

IASWG referral to SAPWG, short-term

b. Assess impact to the future of statutory accounting

IASWG/SAPWG, long-term

4. Reinsurance Modernization

Reinsurance Task Force, long-term

a. Continue implementation of reinsurance modernization

b. Identify any additional reinsurance regulatory modernization

5. Insurance Valuation (PBR)

PBR Working Group, long-term

a. Continue implementation of PBR

- Standard Valuation Law
- Valuation Manual

6. Group Issues

Group Solvency Issues Working Group, long-term

a. Group Supervision

- Supervisory Colleges
- Unregulated or federally regulated entities
- Holding Company model act and regulation

b. Group Capital

c. IAIS Internationally Active Groups / Common Assessment Framework

7. Other potential issues

SMI TF, long-term

a. Other areas that are identified for further work through the analysis of IAIS core principles

b. Systemic Risk – measurement for regulators

- Impact of general economy on insurers
- Centralized review process

c. International Activities

- Determine improvements to or identify new international standards
- Continue to develop international relations regarding solvency-related issues (which extend beyond the IAIS Solvency Subcommittee)

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Solvency Modernization Initiative
Work Plan (Roadmap)

- IV. Overarching Implementation Issues *SMI Task Force, long-term*
- a. Charges to Cmte/TF/WG, *can be made over time and do not all need to be made at one time.*
 - b. Regulatory Forbearance
 - c. Legal and Regulatory Process for Implementation and Future Modification, Uniformity
 - d. Accreditation

- V. Finalize U.S. Solvency Framework and Principles *SMI Task Force, long term*

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**International Association of Insurance Supervisors
Solvency & Actuarial Issues Subcommittee**

Summary of the Madrid Meeting, Sept. 7-9, 2009

**Presented to the
NAIC's International Solvency (EX) Working Group**

Anne Kelly (NY), Kris DeFrain (NAIC), and Ramon Calderon (NAIC) represented the U.S. at the International Association of Insurance Supervisors' (IAIS) Solvency and Actuarial Issues Subcommittee (SSC) meeting in Madrid, Sept. 7-9. The following is an overview of the activities of the Subcommittee.

Insurance Core Principles (ICPs)

Kuni Kawasaki (IAIS Secretariat) said the Insurance Core Principle (ICP) coordination group met at the end of August in Basel, Switzerland. It developed a draft of a revised structure of the ICPs along with underlying standards and guidance papers. He said the SSC needs to determine an agreed structure for the new ICPs 14, 15 and 16; get initial ideas for the text draft for the ICPs; determine whether to retire old papers; make sure elements of the current ICP remain covered within the standards; and decide what to do with the old explanatory notes in the ICPs. A main decision made by the SSC was to separate the ERM ICP from the Investment ICP; while investment risk is a part of ERM, there are also quantitative limits and/or other restrictions established by regulators that are outside of ERM.

Chair Rob Curtis (UK) said the Subcommittee needs to develop a proposal that addresses modifications to ICPs and replacement of essential/advanced criteria in the ICPs with the standards' principles. One issue is whether standards should say "must" rather than "should." The U.S. commented that the word "must" could have much stronger implications, and perhaps the decision should rest with a higher committee in light of IAIS strategic planning, aims, and goals. The Subcommittee attempted to avoid using either "must" or "should,"

With elimination of "essential" and "advanced" criteria and their replacement with standards, "advanced" criteria may remain in guidance material rather than in standards.

Revisions to incorporate the standards into the ICPs are currently slated for 2011, but the chair would like to revise the SSC standards by 2010 so that the Technical Committee does not receive all Subcommittee changes all at once.

Valuation of Assets/Liabilities

The Subcommittee is still charged to have valuation papers completed for 2010 adoption, although Mr. Curtis said he would go to the Technical Committee and stress that this work be delayed until 2011 for adoption. Mr. Curtis commented that this work has been around for years and credibility is at stake soon, but there are resource issues. Many members of the joint valuation group (between the SSC and Insurance Contracts Subcommittees) are no longer members of the Subcommittees or can't currently dedicate time to the project. Mr. Curtis asked whether the SSC is interested in drafting the papers and then asking for input from Insurance Contracts, given that the joint working group is not active and Insurance Contracts has such a full agenda with IASB pronouncements. Mr. Curtis commented that this work is not proprietary, but he simply wants to move the work forward. Some members commented that they prefer to repopulate the joint group, and the U.S. again questioned the self-imposed urgency of this work.

In lieu of the joint valuation group, the UK drafted a revised valuation guidance paper using the valuation principles agreed on at the Edinburgh meeting. The guidance in the document was discussed in detail at the meeting, but the principles remained unchanged.

The European Commission voiced strong opposition to a principle that says valuation should be done on an economic basis without the phrase "market consistent" in that principle. The Subcommittee maintained that the guidance paper allow for economic valuation as market consistent, yet noting that it could also be appropriate to allow amortized value in circumstances where particular assets are matched to long-term liabilities. Canada agreed to draft some language to get this point across. Trevor Cooke (UK) said there should be some test to limit this. Mr. Curtis reminded the SSC that the papers

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need to accommodate different approaches in different jurisdictions. However, the European Commission plans to approach the Technical Committee at their next meeting in Rio about this issue.

Mr. Curtis said the IAIS is still operating from the position of being cognizant of the International Accounting Standards Board (IASB), yet some people are expressing a desire to divorce the IAIS deliberations from the IASB and simply develop separate IAIS standards. At present the IAIS valuation papers are not labeled as a standard, but again this is another issue that is expected to be brought up at Technical Committee by the European Commission.

Capital Resources Papers

The standard and guidance papers on capital resources were adopted via written procedure.

While this was just adopted, the standard on capital resources will be merged with the standard on capital requirements into one “capital adequacy” standard. Guidance papers on these two subjects will remain separate.

Group Supervision and Expansion of Solvency Papers from “Solo” to “Group”

The SSC is expanding its “solo entity” solvency papers to create solvency papers for groups. This process could be as simple as saying the solo entity paper applies to groups, it could require just a few additional points be inserted into the current solo papers, or it could be as detailed as creating a new paper applicable to groups. The SSC appears to be going in the direction of creating joint solo/group standards but having separate guidance papers for solo supervision vs. group supervision.

Regarding group solvency, a group supervisor would be charged with gathering information for individual entities of a group and disseminating that information to the supervisors in that group. The solvency information should be comprehensive enough to ascertain reputational/contagion risk.

There are definite concerns with regard to definitions of terms. A first step is to define “group.” Does it include insurance groups, unregulated entities, or financial conglomerates? The initial SSC reaction is to limit work to insurance groups, which could include unregulated entities. Another needed definition is one for “solo”—does the capital requirement for an insurance parent of insurance subsidiaries fall into the solo entity or group category?

For assessment of group capital as reflected in current IAIS principles, some are advocating having both an minimum capital requirement (MCR) and prescribed capital requirement (PCR) at the group level. There are many questions around this: What does group capital represent? What supervisory/legal actions can be taken if a group has capital levels lower than a PCR or MCR? Are the actions significantly different than what would be used by solo supervisors and, if so, should the IAIS then use different names for group capital levels to distinguish their different meanings/actions? Also, general reaction from the members was that unregulated entities would not have a capital requirement. But then there is the question about how one knows what the contagion/reputational risk is from those unregulated entities.

Since the IAIS is still deliberating the full extent and application of group supervision (including legal issues), the SSC’s pursuit of group supervision guidance seems ill-advised at this juncture. It’s an open question about process and raises the question if this is the best prioritization of workload at the IAIS.

Bernard Dupont (Canada) suggested that the standards could be modified to say, “These standards apply to whatever supervisory framework exists in the jurisdiction.” Then, if a jurisdiction doesn’t have group supervision, the particular standard would not apply to groups in that jurisdiction.

Investment, ERM & ALM – paper development and expansion to groups

Bernard Dupont (Canada) said the revised draft standard and guidance papers on investment eliminated the asset-liability management (ALM) discussion and that work has been incorporated into the enterprise risk management (ERM) papers.

In the investment paper, Carolyn Cobb (American Council of Life Insurers—ACLI) questioned the wording about location of an asset, and the decision was to discuss availability versus location. Mr. Calderon questioned the requirement that insurers could not invest in assets they could not assess or manage. He said insurers can invest in junk bonds in the U.S., although

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limited to a small percentage of invested assets, and he questioned the ability to “manage” these investments. The investment paper will be revised in a few weeks (Sept. 25) and will be put out by the SSC with comments due Nov. 2. The plan would be for the SSC to discuss the paper further in December and February and then send the paper for formal consultation of Technical Committee.

The ERM papers were revised to incorporate ALM, stress testing, the ICP essential criteria, and group issues. Morag Fullilove (Group of North American Insurance Enterprises—GNAIE) said the incorporation of ALM into the ERM paper puts too much emphasis on ALM without fuller exploration of other risks. These ERM papers will also be distributed on Sept. 25 for comment.

Internal Models – for Groups

To expand the solo requirements for internal models to groups, the IAIS needs to answer the question about whether the MCR applies and whether the group model is the same as what would be used by the solo entities.

Capital Requirements – for Groups

There is question whether the solo standards apply to groups—should there be a range of solvency action levels, a PCR, and an MCR at the group level? Requirements should not exclude a legal entity approach to group supervision. One idea was to create different names for the group capital requirements, as they might have entirely different meanings than the PCR and MCR, and it would be confusing to use the same name for different actions.

Supervisory Monitoring

David Vacca (NAIC) submitted revisions to the U.S. work by separating the document about supervisory reporting, financial examinations, and financial analysis into a paper on supervisory reporting and a paper on supervisory review. No discussion ensued due to lack of time.

Mr. Curtis said the supervisory review and reporting work spans across the IAIS into market conduct, governance, accounting, etc. He said he tentatively agreed that the secretariat would take both papers, likely for 2011 adoption. The SSC will continue to develop the solvency elements for consideration in these papers. Thomas Luder (Switzerland) suggested that the IAIS should consider letting the SSC develop its own paper and let the secretariat’s paper refer to that work.

SSC Process

Pauline de Chatillon (France) suggested that the SSC have more discussion based on a list of issues before commenting on drafting.

Next Meeting

The next meeting will be in San Francisco in December prior to the NAIC Winter National Meeting.

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July 2009

**International Association of Insurance Supervisors
Solvency & Actuarial Issues Subcommittee**

Summary of the Edinburgh Meeting, July 14-16, 2009

**Presented to the
NAIC's International Solvency and Accounting (EX) Working Group**

Lou Felice (NY) and Kris DeFrain (NAIC) represented the U.S. at the International Association of Insurance Supervisors' (IAIS) Solvency and Actuarial Issues Subcommittee (SSC) meeting in Edinburgh, July 14-16. The following is an overview of the activities of and reports to the Subcommittee:

Joint Meeting with IAIS Insurance Contracts Subcommittee: Valuation of Assets/Liabilities

The SSC met jointly with the IAIS Insurance Contracts Subcommittee on July 14 to discuss insurance valuation principles. Ramon Calderon (CA) and Rob Esson (NAIC) represented the U.S. on the Insurance Contracts Subcommittee. The following principles were agreed on by the end of the meeting, although there is likely to be continued debate, especially regarding whether to create an IAIS principle that valuation should be market-consistent:

1. The valuation, for solvency purposes, of assets and of liabilities should be undertaken on consistent bases.
2. Assets and liabilities should be valued in a reliable and transparent manner.
3. The valuation for solvency purposes of assets and liabilities should be an economic valuation.
4. An economic valuation of assets and liabilities should reflect the risk-adjusted present values of the cash flows arising from the assets or incurred under the liability.
5. The solvency regime should require the valuation of technical provisions to exceed the current estimate of the cost of meeting the insurance obligations (Current Estimate) by a margin to reflect the inherent uncertainty of those obligations (Margin over the Current Estimate, or MOCE).
6. The Current Estimate should reflect the expected present value of all relevant future cash flows that arise in fulfilling insurance contract obligations, using unbiased, current assumptions.
7. The MOCE should reflect the inherent uncertainty related to all relevant future cash flows that arise in fulfilling insurance contract obligations over the full time horizon thereof.
8. The valuation of technical provisions should allow for the time value of money. The solvency regime should establish criteria for the determination of appropriate interest rates to be used in the discounting of technical provisions.
9. The value of technical provisions should not reflect the insurer's own credit standing.
10. The solvency regime should require the valuation of technical provisions to make appropriate allowance for embedded options and guarantees.

Most discussion centered around the first three principles. It was noted that each of these principles would be discussed in greater detail within the guidance paper. The following describes some of the debate on the first three principles:

Principle 1. The consistency principle was agreed on but with reservation that exploration of details and implementation would likely result in some exceptions. Mr. Esson said "consistency" is not necessarily with the calculation but rather the matching of cash flows. He said "own credit standing" is an example of where the symmetry of asset and liability valuation does not hold. The IAIS believes the use of "own credit standing" to value insurance liabilities is inappropriate (with some exceptions of discount rates and particular types of loans); use of own credit standing to value liabilities would result in lower liabilities when companies get downgraded in their credit ratings, which seems counter-intuitive for solvency assessment. Nobu Sugimoto (Japan) said the IAIS should start with liability valuation and proceed into asset valuation.

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Principle 2. The U.S. advocated removal of the word “objective,” just as it had removed that word from its principle-based reserving principles. Some believed that objectivity should remain the aim, but with realization that much of what is done is subjective. At one point the principle was qualified by including “objective to the extent practicable,” but the principle was subsequently removed altogether. Rich Shaw (Bermuda) said actuaries have jobs because insurance valuation is not objective and judgment needs to be exercised. Trevor Cooke (UK) said he still believes in using the aim of “objective”; he said it doesn’t mean “no subjectivity” but rather means subjectivity should be kept in reasonable bounds. Thomas Luder (Switzerland) said the valuation should limit subjectivity to be as small as possible, and valuation should be “defendable in conversation with a knowledgeable person.” Olaf Ehrmert (Germany) said valuation should be carried out in an “objective manner,” which means in an “impartial manner” and not arbitrary. The U.S. also asked for “prudent” to be an aim; however, Guernsey said that is interpreted as “conservative” and they could not agree to that. Overall, the guidance paper will explain that the word “reliable” in the principle implies that there would not be too much subjectivity; professional judgment is often required; peer reviews are useful, etc.

Principle 3. The most extensive debate was around the third principle and whether the Subcommittee still agreed with the previously stated IAIS position that the valuation of assets and liabilities should be market-consistent. Australia (who wasn’t at the meeting), the EU and Switzerland are strongly in favor of maintaining this principle. Bermuda, Canada and the U.S. recognized that some countries would like to keep market-consistent as the aim, but believe they can still accomplish that, as the principle says valuation should be economic; a country can interpret “economic” to be market-consistent, but the principle would be broad enough for other approaches as well. For example, there could be justifiable exceptions, such as amortized asset valuation, when there is hedging against long-term liabilities or when a country chooses to utilize public (audited) financial reporting as the basis for capital requirements (with any “non-solvency valuation” adjusted in the capital requirements).

Stuart Wason (Canada), chair of the joint valuation working group, highlighted some areas that would result in countries having different views on valuation. He said countries currently have a variety of practices as to whether and how GAAP financial reports are used. Some use GAAP (audited) public financial reports directly to determine their final capital requirements. Some start with GAAP, require adjustments to develop a solvency balance sheet, and then determine capital requirements from the solvency balance sheet. Some utilize separate and distinct solvency accounting. In addition, differences in opinion exist between countries where the balance sheet that enters into the determination of capital requirements is public, and therefore some of the reasons why GAAP statements might deviate from pure market-consistency are also reasons that need to be considered by supervisors.

At one point in the debate, the principle included the idea that valuation should utilize relevant and credible market information and entity-specific information where appropriate. However, it was argued that the largest liability on the balance sheet for insurance companies can only be tied to the market on a limited basis because there is no deep and liquid market. So market valuation seems inappropriate as a principle because it is not achievable. Also, inclusion in a principle to use credible entity-specific information met significant resistance from EU participants and eventually led to elimination of market-consistency altogether from the principle as well.

Within this debate was discussion about the use of amortized cost when matched against long-term liabilities. Craig Swan (Bermuda) said the IAIS should focus on the outcome with the realization that different methods would achieve similar results. He said that if assets and liabilities move in the same direction and are perfectly matched, then the same outcome is achieved without market valuation. Trevor Cooke (UK) said that with principles to account for the time value of money and use of economic prospective valuation, then amortized cost is not consistent.

One missing principle that the U.S. supported was to have general purpose reporting as the basis for statutory accounting, and to make adjustments as needed from that as the starting point. This is supported by Bermuda and Canada as well; however, others believe it is not necessary to have a similar starting basis, and a completely separate accounting basis should be acceptable as the start. Some believe that the IAIS should, at a minimum, state that differences between the statutory and general purpose accounting should be identified and data should be reconcilable. Emmanuel Cortese (Belgium) said that when it comes to solvency purposes, the valuation should be comparable and consistent. While the exact same rules would not apply, they should be applied consistently. On one end are obligations, and on the other end are rights. Stuart Wason (Canada) said consideration should be given when a company goes insolvent and the supervisor has to explain the situation to a judge. If a GAAP statement shows the company to be solvent, yet the supervisor wants to prove insolvency, the supervisor

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will need to be able to tie their analysis to the GAAP statement and show why their analysis is a more accurate depiction. Japan agreed that comparability is needed. It was also noted that costs are minimized the more the IAIS can minimize differences between financial and solvency reporting.

Capital Resources Papers

The standard and guidance papers on capital resources were released for formal comment by the Technical Committee. The Committee asked the Subcommittee to review the comments received and recommend changes to the paper for their consideration. The Technical Committee approved an unusual process for adoption of these papers and will, along with Executive Committee, do approval by written procedure. In October the papers will be considered by the full membership.

There were three main comments. The first was to consider the styling of the paper in light of the potential replacement of Insurance Core Principles (ICPs) by standards. It was decided that until the decision is made to use the standard to replace ICPs, the current styling would be maintained. The second main comment was to consider overlap with the valuation work. It was decided to remove valuation aspects from the paper and to remove any definition of economic value. The third main comment was the proposal to eliminate the fourth standard requirement dealing with own risk and solvency assessment (ORSA). The principle was modified to eliminate reference to ORSA, and the guidance paper was adjusted accordingly. However, some reference to ORSA remains in the guidance.

Group Supervision and Expansion of Solvency Papers from “Solo” to “Group”

Mr. Sugimoto said the IAIS Executive Committee received a report from the New Issues Task Force and agreed that the IAIS should proceed with a common structure for insurance groups. Karen Doran said the IAIS Groups Issues and Cross-Sectoral Subcommittee was given endorsement to develop the group supervision framework. That subcommittee also has a supervisory college paper out for consultation with a plan for member approval in October; did a survey on the use of supervisory colleges to share the results with the Financial Stability Board for their broader work on the subject; are developing guidance papers on the treatment of non-regulated entities and on criteria for mutual recognition in a group context; and have a new work stream on crisis management.

Main drafters of the SSC’s solo papers introduced various approaches to expanding the SSC’s solo work to groups. The drafters were given some ideas for modification and will present new versions for the next meeting.

Investment & ALM Papers

Bernard Dupont (Canada) said the revised draft standard and guidance papers on investment eliminated the ALM discussion, with that work to be incorporated into the ERM papers.

Supervisory Monitoring

Mr. Felice presented a second draft document about supervisory reporting, financial examinations and financial analysis. The new version expands the work into reporting for solvency tools. The supervisory process for the solvency tools still needs to be drafted, such as how supervisors should review internal models. Rob Curtis (UK) suggested that the work could be split into separate papers for reporting and supervisory review.

Some redrafting ideas were as follows:

- Information should not be requested that won’t be used.
- Supervisors may not have capacity to do a lot of detailed testing and checking.
- “Factors for consideration” should be drafted to help supervisors know what they might need to ask.
- The paper should use similar headings as other papers.
- Supervisors should establish a relationship with the company.
- The paper should be flexible between on-site and off-site categorizations of duties.
- For reporting, identification should be given as to public or supervisory reporting.
- What financial data is needed, especially for valuation?

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IAA Update

Rolf Stolting (International Actuarial Association - IAA) said the IAA Solvency Subcommittee will publish an internal models paper soon and is working on stress testing. The IAA Regulation Committee is reviewing the role of the actuary worldwide to evaluate to what extent actuaries should be the risk managers. A risk manager needs actuarial expertise but also needs other expertise. A new working group was established to evaluate the extent to which insurance companies contribute to systemic risk.

Solvency Changes around the World

EU

Teresa Rubino (EU Commission) said agreement was reached on Solvency II's Level 1 directive after intensive debate; she called the final work "compromise text." Parliament adopted the directive in May. Level 2 adoption will need to be completed at the end of 2010. This means CEIOPS needs to provide their final advice to the Commission by January 2010. A fifth quantitative impact study (QIS) will be conducted as well. Level 3 work should be published in 2011. They are working to develop a centralized database to include both individual company as well as group data.

For mutual recognition, general criteria will be developed in 2010, and country assessments will be conducted in 2011.

Following the De Larosiere Report, the European Commission proposed reforms at the micro and macro level. At the macro level, a new body would be established to monitor risks such as systemic risk. At the micro level for individual firms, a system of financial supervisors would be created. A European agency would replace the Level 3 committees (CEIOPS for insurance, CESR for securities, and CEBS for banking). This would promote harmonization, create binding technical standards, and allow the Commission to intervene if there are disagreements of colleges. This Commission proposal will be negotiated in Council and Parliament.

U.S.

Mr. Felice reported on the Solvency Modernization Initiative (SMI) and the Obama Administration regulatory proposals.

Next Meeting

The next meeting will be in September in Madrid, back to back with the Insurance Groups and Cross-Sectoral Subcommittee's meeting.

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Draft: 10/1/09

Group Solvency Issues (EX) Working Group
Washington, DC
September 23, 2009

The Group Solvency Issues (EX) Working Group of the Solvency Modernization Initiative (EX) Task Force met in Washington, DC, Sept. 23, 2009. The following Working Group members participated: Ann Frohman, Co-Chair (NE); Danny Saenz, Co-Chair (TX); Louis Quan (CA); Kathy Belfi (CT) Linda Sizemore (DE); Ray Spudeck (FL); Jim Armstrong (IA); Jim Hanson (IL); Joseph Fritsch (NY); Steve Johnson (PA); and Roger Peterson (WI). Also participating were: William Arfanis (CT); Jim Mumford (IA); Jim Nixon (NE); James Everett (NY); Doug Slape (TX); and Alfred W. Gross (VA).

1. Discussed Matrix of Assignments

Director Frohman said the matrix of assignments (Attachment Five-A) is being utilized for two purposes. First, it is being used to track the items from the questionnaire relative to the Insurance Holding Company System Regulatory Act (#440) survey responses. Second, it is being used to track the larger national issues that were surveyed. The last page of the matrix contains a key of issues that have been grouped together. This will be the start of an outline for research topics. She said there are action items being drafted that are less controversial, based on the information received in the questionnaire, and there are preliminary drafts for those. This Working Group is to provide support and research to Solvency Modernization Initiative Task Force, and a number of the items in the matrix will be appropriate research topics for this Working Group to work on. She explained that these items will not be a deliverable, in the sense of providing a position to the industry; instead, this Working Group will refer these issues back to the Task Force. Some of the items are temporarily deferred, based on previous discussions, and the Working Group will come back to some of these. The Working Group has a starting point for discussion topics, will draft the first outline and then move into further research. Some of these items have been assigned to specific Working Group members. Regarding a deliverable date for changes to model #440, the Working Group will have a year to perform its work. She said she does not expect to have a full draft ready for public comment until the first part of November, because the information on supervisory colleges needs to be incorporated and it won't be ready until the end of October.

2. Discussed Draft Revisions to Model #440

Mr. Saenz said that some states have worked on draft revisions to model #440, but the Working Group has not reviewed these draft revisions until today. A conference call will be scheduled in October to discuss some of these specific items and continue revisions.

a. Nebraska Draft Revisions

Director Frohman said Nebraska addressed access to affiliates and the parent in the holding company system, upon acquisition and within the registration statement (Attachment Five-B). She said Nebraska saw this as an opportunity to enhance regulatory efforts and try to get a better picture of the group operations. With that in mind, Nebraska proposed being able to include consolidated financial statements in the registration process. That is, at the time the Form B is submitted, the commissioner could request information, depending on the nature of the group, to determine if the group has the wherewithal to be able to access that information on a regular basis. What Nebraska tried to accomplish with the provision on examination authority was to take the financial condition of the insurer — including the risks to the insurer within the group — and shore up that language so that regulators could say they are looking at the perspective of an insurance enterprise and protection of the capital of the insurance enterprise. Nebraska suggested some language, so that regulators have the ability to access information and be able to enhance what they are doing when they are looking at affiliates. Nebraska suggested the regulator first go to the insurer to obtain the information; then, if the insurer is not able to obtain it, the insurer must explain why they cannot provide the information. Nebraska proposed language to give authority and penalty information, if there is a lack of cooperation from the insurance company, but also if the insurance company is either being instructed to not provide the information and/or if it cannot get the information from its parent company. Given that regulators also are reviewing the filing process, Director Frohman suggested that the Working Group work on the Form B process and, later, the Form A process. Electronic capabilities are different than when the model #440 was first put into effect. The Working Group should use this opportunity to provide a centralized mechanism for filing in a way that does not interfere with the domiciliary regulator's ability to oversee the process or the domestic insurer, at registration or acquisition. Nebraska has drafted language that allows for the NAIC to be a repository on a confidential basis; however, the responsibility for enforcement would continue to be with the domestic regulator. It would be a "pass through" requirement, by which the electronic filing would

streamline the process of coordinating efforts. Nebraska also has a request to consider the ultimate controlling person in the processes where the ultimate controlling person is an individual, recognizing that individuals might or might not be able to provide capital. Language was provided that aims to capture what type of information should be provided if the ultimate controlling person is an individual. Nebraska tried to identify a way to access not only the background biographical information, but also the financials.

Director Frohman also said Nebraska wanted to take note of what transpired with American Internatioal Group (AIG). Regulators have moved in a coordinated fashion with the federal government in looking at AIG acquisitions and sales of entities. And, she said, the lessons learned from AIG seem to present a perfect opportunity to provide some uniformity in model #440 — and do so in a manner that balances unified coordination, with the independence needed for the review process. She said Nebraska tried to capture that concept with a request for hearing on a consolidated basis, as there might be a situation when a number of insurance companies are being acquired that are domiciled across multiple jurisdictions.

Mr. Johnson said that with regard to Form B filings databased at the NAIC, when confidential information is sent to the NAIC (as with the market filing data) the industry believes there is a reduced level of protection of that information — and, as such, that is a thorny issue that the Working Group could get caught up in for a long time. Mr. Saenz said he recognizes some of those issues and the Working Group will try to work them out as best it can. Mr. Johnson said that, at some point, the Working Group will need to make a decision about separating the controversial issues from the non-controversial issues, and then decide whether to move forward with the non-controversial items. Mr. Saenz said that, in looking at the matrix, there are short-term and long-term issues. The Working Group will move forward on issues that can be resolved quickly; other issues will be set aside and worked on in the long-term.

b. Illinois and Texas Department Draft Revisions

Mr. Slape summarized the Texas and Illinois suggested draft changes to model #440 (Attachment Five-C).

Mr. Peterson said that, with regard to charges of fees for services performed, Wisconsin suggests that the use of the current market rate be used only when the service provider actually provides services to third-party vendors, so the market rate can be established. Wisconsin's experience in getting a comparable quote on a contract is that it is difficult, and real application of it is challenging. Some small premium contracts (for example, catastrophic writers) could have a material impact; therefore, the Working Group should be cautious in this area. Mr. Saenz said there would be points and issues that we may need to clarify and work on further.

Steve Broadie (Property Casualty Insurers Association of America—PCI) asked whether the draft was getting too specific for the statute. He suggested that the Working Group should consider instead revising the Insurance Holding Company System Model Regulation (#450) or drafting some other type of guidance. Mr. Broadie stated that the Working Group could end up prescribing too many requirements when, down the road, things might change and regulators might need more flexibility.

c. Connecticut and Illinois Department Draft Revisions

Dan Shelp (NAIC) summarized Illinois' revisions to Section 1C relating to the definition of control and Section 3B relating to Form A filings (Attachment Five-D). He said that during the AIG Form A process, there was some confusion expressed by certain parties about whether the party acquiring control (or the party whose control was acquired) was required to file a Form A. Illinois suggested additional language to remove any ambiguity regarding whether the party acquiring control is required to file a Form A. Specific language was suggested to Section 4A, related to disclaimers of affiliation. With respect to matrix item #19, Illinois believed there needed to be significant changes to this area and suggested it would not be prudent for the Working Group to address the topic at this time. With respect to matrix item #25 related to Form A filing requirements, Illinois believed there were other ongoing discussions related to this issue and that, until those discussions proceeded further, it would not be prudent for the Working Group to address the topic at this time.

Ms. Belfi summarized Connecticut's comments (Attachment Five-E). She stated that Illinois and Connecticut have some work to do with certain sections; however, matrix item #39 was more easily conveyed as a best practice. Mr. Johnson said this is a good list that needs to be distributed to regulators in some form. Also, he said, having an understanding of obtaining a board seat is a good practice. Understanding why they want to make the investment, what the ultimate goal is and making sure that discussions are with the right person, the decision-maker vs. the businessperson, is a best practice that might be considered also. These things can become very controversial, so regulators need to assess what is happening from a business and economic standpoint.

d. Other Interested Regulator or Party Comments Received

Mr. Saenz said there are other reports and drafts under development. While the Working Group would appreciate oral comments, he asked interested parties to refrain from sending formal written comments, as the Working Group is still in the initial stages of development. The Working Group still needs to review and discuss these drafts at a future conference call. At a later date, drafts will be released to interested parties for comment.

3. Heard Report on Items Directed to NAIC Staff

David Vacca (NAIC) said matrix item #44 was regarding data repositories at the NAIC for International Financial Reporting Standards (IFRS) and GAAP financials. He said he spoke to Todd Sells (NAIC), who indicated that the NAIC does have the data-capture capability from insurers filing with the NAIC. The NAIC would have to explore further if the NAIC were asked to collect this data from other regulatory bodies. Regarding matrix item #60 related to standardized electronic reporting formats, such as eXtensible business reporting language (XBRL), NAIC staff needs more information to clarify the comment. In terms of receiving information from the U.S. Securities and Exchange Commission (SEC), there would have to be discussions on how to configure NAIC systems to receive information in that format. NAIC staff will contact some states to get their feedback and research the topic further. Regarding matrix item #43 to consider a project to compare and contrast the Part A Accreditation standards for laws and regulations with applicable, comparable international standards, Mr. Vacca said he spoke to Kris DeFrain (NAIC). Ms. DeFrain said the International Association of Insurance Supervisors (IAIS) has already done that type of comparison; however, there is so much change occurring that she recommended that the Working Group wait until the changes occur and then take up the issue at that time. Mr. Vacca said he would research existing IAIS documentation.

Director Frohman said that on the issue of federal preemption, there is no report today but there would be a report given on a future conference call.

4. Discussed Suggestions on International Research Efforts

Director Frohman said that, from a broader scope, the Working Group has a good idea of the topics that require further discussion and study. The Working Group will be asking for suggestions on these research efforts and what the approach should be; e.g., conduct surveys or engage speakers. She suggested keeping the Working Group together on these issues, as opposed to forming subgroups, and requesting topics on which to engage others to speak to the Working Group. Mr. Saenz asked if these presentations would occur at the Winter National Meeting or an interim meeting. Director Frohman said that presentation would likely occur in both forums. Mr. Spudeck said he agreed that Working Group should stay together to discuss these issues and not separate into subgroups. Director Frohman said NAIC Staff can provide the Working Group with the resources to stay briefed and up-to-date.

5. Received Report from Supervisory College Subgroup

Mr. Armstrong provided a report of the Subgroup on Supervisory Colleges and Methods of Cross-Border Communication. (Attachment Five-F) He said that on the last conference call, Florida raised an issue regarding the flow of information-sharing with federal regulators, in that it seems to be moving predominantly in one direction (i.e., from state to federal regulators). Mr. Spudeck suggested a federal bill to clarify the expectations regarding the flow of information. Mr. Armstrong asked for direction from the Working Group. Director Frohman asked whether — in addition to the supervisory college issue, which relates to the supervisory relationship in the global context — the states should have their own responsibilities relative to functional-regulator relationships under the federal Gramm-Leach-Bliley Act (GLBA). She added that this is another facet of cross-border communication that needs some sort of resolution. Mr. Spudeck stated that it can be frustrating to figure out how to get information on different issues. Director Frohman asked if this might be an issue for the Solvency Modernization Initiative Task Force to tackle. She said her understanding is that duties related to confidentiality were established separately from GLBA, and that the manner in which those confidentiality standards were established would require a significant legal research project.

Linda Duzick (U.S. Office of Thrift Supervision—OTS) said she would be available to answer the Working Group's questions, as well as provide history on the introduction of GLBA. She said that state insurance regulators should feel free to contact her anytime, and she would be happy to share the original MOU contract with the states to share information. She said the OTS has information-sharing agreements with all state insurance regulators. She said she is not aware of any situation in her 10 years at the OTS that they did not respond to a request from a state insurance regulator.

Director Frohman said she appreciates Ms. Duzick's comments, as regulators have had varying experiences on different transactions with many agencies. Ms. Duzick said that regarding supervisory colleges, the OTS has always invited international and state insurance regulators to those colleges, so there has been extensive participation of state insurance regulators in those meetings over the years. She said the OTS would be happy to work with the the Working Group to discuss the lessons learned.

Mr. Armstrong said they discussed possible processes in which U.S. regulators who participate in supervisory colleges could share their experiences (both pre- and post-supervisory colleges) with other relevant regulators, such as through the creation of a tracking system, whereby the NAIC would monitor attendance at supervisory colleges and create best practices for regulators to share information regarding pre- and post-supervisory college attendance.

Mr. Armstrong said the Subgroup discussed components of the IAIS MOU and subsequent actions for state review. He said the Subgroup would prepare summary a memorandum regarding the IAIS MOU for discussion at next meeting and discuss steps for disseminating this memorandum for discussion.

Mr. Armstrong also said the Subgroup discussed drafting amendments to model #440 and/or #450 to require state insurance regulators to share information with federal and international counterparties. The Subgroup will prepare general language amending model #440 and/or #450 to authorize the use of supervisory colleges, where appropriate, for further discussion and refinement at the next meeting. The Subgroup will prepare draft amendment to model #440 and/or #450 enabling the states to have all costs for attending supervisory colleges be borne by the insurer as part of the examination process. He said he is hoping to have these draft amendments for the Working Group in October.

Mr. Armstrong stated that the Working Group, as well as interested regulators and parties, should review the draft IAIS guidance paper on supervisory colleges, which is near adoption (Attachment Five-G). Mr. Johnson suggested that, as part of the NAIC's efforts with the supervisory college process, there should be best practices of the logistics of the actual meeting with the company. For example, he suggested that these best practices should outline whether the regulators should agree on the focus of the presentations by companies, as well as what should be done afterward. It shouldn't be just "show-and-tell," he said; regulators should come with issues, as this would make the meeting more information- and issue-focused. He said his second comment is that, if state regulators are to become world leaders in insurance, it is critical to have the necessary funds to go overseas. He asked how revenue sources could be maximized (including the NAIC budget) to fund the expenses for state insurance regulators to travel around the world to participate in these discussions. Mr. Saenz said that Working Group members, interested regulators and interested parties should provide comments on the IAIS guidance paper within 15 days, so that the Working Group can provide comments to the IAIS and/or inform the Solvency Modernization Initiative Task Force that the Working Group is generally comfortable with the guidance paper.

Upon a motion made by Mr. Armstrong, seconded by Mr. Spudeck, the Working Group voted unanimously to receive the report of the Subgroup on Supervisory Colleges and Methods of Cross-Border Communication.

6. Received Update on Related IAIS Activities

Mr. Spudeck summarized the activities at the recent IAIS Insurance Groups and Cross-Sectoral Issues Subcommittee meeting. Specifically, he mentioned efforts by the Subcommittee in the following areas: differentiated nature and scope of regulation work stream; Financial Stability Board work stream; activities of the Group of Twenty (G-20) Finance Ministers and Central Bank Governors; developments in groupwide supervision of other jurisdictions; guidance paper on the treatment of non-regulated entities; guidance paper on crisis management and supervisory resolution of cross-border entities; and guidance paper on supervisory recognition. He and Mr. Vacca have been attending IAIS meetings and actively participating in drafting the papers. He stated that the IAIS is an international standard-setter and, as such, its standards are taken into consideration by jurisdictions across the globe that are contemplating the review and revision of their insurance laws and regulations. Mr. Spudeck said that is why it is important for this Working Group to actively follow and participate in IAIS activities.

7. Discussed Coordination with Solvency Modernization Initiative Task Force

Director Frohman said that Ramon Calderon (NAIC) and one of the international working groups provided a presentation on the Solvency Modernization Initiative workplan. It is a preliminary draft. She suggested everyone be aware of it and keep it in mind.

8. Adopted Interim Conference Call Minutes

A motion was made by Mr. Johnson to adopt the minutes from the Aug. 12 and July 23 conference calls (Attachments Five-H and Five-I). The motion was seconded by Mr. Spudeck and unanimously adopted.

10. Heard Update on 2010 Proposed Charges

Mr. Vacca summarized the 2010 proposed charges. If the Working Group has any changes, please let NAIC staff know, so the chair can communicate those to Solvency Modernization Initiative Task Force.

Having no further business, the Group Solvency Issues (EX) Working Group adjourned.

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Comments from GSIWG - Insurance Holding Company System Regulatory Act Questionnaire					
Grouping for Discussion	Topic	Study Items and/or Recommendations	Working Group Action (Pass, Draft, Research Further, Refer)	Assignment of Task	Deliverables Tentative *T Final *F
1	A	Clearer access upstream and downstream on any information desired regarding the holding company, regardless of entity. This point could be addressed through a group supervision requirement to provide consolidated financial statements of the entire group when requested.	Draft	NE	*T Sept. 09
2	A	Suggest Adding: • Authority for the insurance department to review the books and records of the immediate and ultimate holding company of the insurer.	Draft	NE	*T Sept. 09
3	A	Section 6 – Examination The Examination section should be expanded to clarify that the power of the Commissioner extends to acquiring the books and records of any affiliate for the purpose of determining its possible effect on the holding company system and the insurer.	Draft	NE	*T Sept. 09
4	B	A review of a recent Form A filing by an Australian conglomerate that acquired a regional, multi-state insurance group disclosed some significant difficulty in obtaining information about the conglomerate from its domiciliary regulatory agency and from other official sources monitoring or regulating its affiliates. This situation should be addressed in revisions to the Model Act.	Further Research/Possible Draft	IA, CT (Possible assistance from NAIC Legal & Supervisory College and Methods of Cross-Border Communications Subgroup)	*T Nov 09
5	C	Stronger language is needed relative to cost sharing/management agreements among affiliates. Many affiliated "management" companies are merely organized to siphon funds. Although regulators can and do ask questions in an attempt to determine whether fees are reasonable, it is difficult without updated language/guidelines.	Draft	TX, IL	*T Sept. 09
6	C	Act should require an insurer to provide prior notice to the Department for the termination or amendment to affiliated agreements that originally required the Department's approval. The notice should include information regarding the reasons for the change and the financial impact on the domestic insurer.	Draft	TX, IL	*T Sept. 09
7	C	In addition to the points made above, recommend that the fair and reasonable standard for transactions between affiliates be strengthened by requiring that all services provided to the insurer be at actual cost.	Draft	TX, IL	*T Sept. 09
8	C	Recommend the "fair and reasonable" standard for transactions between affiliates be strengthened by requiring that all services provided to the insurer be at actual cost.	Draft	TX, IL	*T Sept. 09
9	A	Suggest Adding: • Authority to review the auditors work papers of the immediate and ultimate holding company, as deemed appropriate.	Draft	NE	*T Sept. 09
10		Expansion of the collateral examination authority to specifically include broader risk categories such as liquidity, reputation, and rating risks in the definition of "impact on the financial condition"	Pass		
11	B	A codified requirement, at least in federal law, for regular communication, information-sharing and collaboration between the functional regulators within a holding company system should be advocated	Further Research/Possible Draft	IA, CT (Possible assistance from NAIC Legal & Supervisory College and Methods of Cross-Border Communications Subgroup)	*T Nov 09

Comments from GSIWG - Insurance Holding Company System Regulatory Act Questionnaire						
Grouping for Discussion	Topic	Study Items and/or Recommendations	Working Group Action (Pass, Draft, Research Further, Refer)	Assignment of Task	Deliverables Tentative *T Final *F	
12	B	Communication of Functional Regulators As GLBA didn't require functional regulators to communicate with each other, should that requirement be placed into the model? Discussion point – Is this an issue? Do you find that functional regulators are not communicating with each other provided the appropriate confidentiality agreements are in place?	Further Research/Possible Draft	IA, CT (Possible assistance from NAIC Legal & Supervisory College and Methods of Cross-Border Communications Subgroup)	*T Nov. 09	
13	B	Confidentiality with non US regulators Examine confidentiality and other protections in current state laws and current state holding company laws for purposes of sharing information among state, federal and international regulators (i.e. international supervisory colleges).	Further Research/Possible Draft	IA, CT (Possible assistance from NAIC Legal & Supervisory College and Methods of Cross-Border Communications Subgroup)	*F Nov. 09	
14	D	Definition of Control Section 1 – Definitions There should be consideration given to adding the types of control to the definition of control that are currently found in SSAP No. 25 paragraph 4. The two currently not found in the Act are “(c) by contract for goods or non management services where the volume of activity results in a reliance relationship (d) by common management.” The model should be changed so that disclaimers of affiliation may be disallowed without a pre-disallowance hearing. Any hearing should come after the disapproval.	Draft	IL	*T Sept. 09	
15	D	Disclaimers of Affiliation Also, they may consider changing the model to clarify that when the 10% presumption applies, the party rebutting that presumption carries the risk of non-persuasion as well as the risk of non-production. Which means that if you've got at least 10% of the voting securities, you're going to have to produce affirmative and persuasive evidence that you don't in fact control the company rather than just pointing out that you have less than 50% of the voting securities.				
16	E	Enterprise-wide risk management Consideration should be given to requiring (based on materiality) documentation and reporting enterprise-wide risk management processes	Draft	IL GSIWG (W1 to clarify)	*T Sept. 09	
17	F	Entities or Transactions with Detrimental impact to insurer Over the years regulators have used aspects of the holding co act to investigate non-insurance activities of companies. If regulators believe other entities in a holding co system potentially impact the solvency of an insurer, regulators have authority to examine & require(?) the insurer to deal with it. What regulators don't have is the ability to directly require the other entities to do something.	Discussion Item			
18		Entities or Transactions with Detrimental impact to insurer Suggest Adding: • Authority to stay or require written approval any material financial transaction of the holding company and another non-affiliated, which appears to have a detrimental financial impact upon the insurer.	Discussion Item	GSIWG (NAIC Legal Assistance)		
19	D	Exemption vs. Disclaimer There is a wide interpretation of exemption versus disclaimer requests and many use them interchangeably. Ins holding co systems - clarify disclaimer vs. exemption - control vs. affiliation, insurance policy issuance require filing, clarify whether amendments to non-reinsurance agreements require filing, determination as to whether "minor" agreements require filing.	Pass			
			Draft	IL	*T Sept. 09	

Comments from GSIWG - Insurance Holding Company System Regulatory Act Questionnaire						
Grouping for Discussion	Topic	Study Items and/or Recommendations	Working Group Action (Pass, Draft, Research Further, Refer)	Assignment of Task	Deliverables Tentative *T Final *F	
20	D	Federal Preemption of the Holding Company Act	Health entities have indicated there is Federal Preemption of the Holding Company Act for reviewing affiliated service agreements under which CMS required services are provided. In these situations, since states are responsible for the solvency of these Medicare entities holding a license in our state, then the question arises whether a review of an affiliated service agreement should be considered part of our regulation of the entities' solvency (and therefore not preempted). Have encountered Federal Preemption of the Holding Company Act in regards to federal government's acquisition of Control of AIG and GMAC. Act should somehow address how this situation needs to be handled so that states can address it in a uniform manner.	Draft	TX, IL	*T Sept. 09
21	D	Federal Preemption of the Holding Company Act	Currently all affiliated reinsurance agreements need to be filed and there is a question as to whether that is necessary. Consider a change so that affiliated reinsurance agreements would have to involve more than 5% of GWP to require filing.	Draft	TX, IL	*T Sept. 09
22	C	Filing of affiliated reinsurance agreements	Regardless of administrative form, regulation should not result in any unfair, discriminatory treatment of foreign owned US insurance or insurance holding companies relative to similarly situated US owned insurers or insurance holding companies or disruption of home country regulation of non US companies affiliated with US insurers. The system should recognize those requirements applicable to the insurer's foreign or non-US parent which are broadly equivalent to US regulations.	Draft	TX, IL	*T Sept. 09
23	G	Equivalence	Act should be amended to more clearly state that a Form A filing or Form A Exemption filing must be submitted by the person acquiring ownership. Although regulators consider the Act to be clear on this issue, there are other states with the same law, which interpret and handle this situation differently. In the situation where the federal government acquired ownership of domestic insurance companies, an intermediate holding company filed a Form A Exemption requesting the Department to approve the acquisition by the federal government. However, such an intermediate holding company cannot have complete knowledge regarding the true intentions of the acquiring party and its plans for the insurers.	Monitor	GSIWG Chairs	
24	D	Form A filing and Form A Exemption filings	Uniform Form A filing requirements or, in the alternative, a uniform review process when insurers within a group are impacted. With the issues arising with AIG, it is apparent that a uniform Form A review process would be helpful in order to coordinate Form A reviews. Discussion points – Consider a lead state approach, a team of lead states, whether a hearing process is required, etc.	Draft	IL (Possible assistance from NAIC Legal)	*T Sept. 09
25	D	Form A filing requirements or review process	Add additional instructions to Form B filing information when the ultimate controlling person is an individual, as it is not possible to have biographical information of Officers and Directors for an individual and not many individuals have certified audited financial statements.	Draft	IL (Possible assistance from NAIC Staff)	*T Sept. 09
26	A	Form B filing instructions	Consider having all Form B filings for Insurance Group Holding Companies (i.e. have a group code) submitted confidentially to NAIC for easier regulator-to-regulator review.	Draft	NE	*T Sept. 09
27	A	Form B filings submitted to NAIC	The NE Legislature adopted a statute in 2008 regarding statutory authority to conduct group supervision, which granted the Department authority to adopt a regulation setting specific standards. Although the act references "financial conglomerate", it is more accurately an insurance group. Source: Laws 2008, LB855, § 50.	Draft	NE & NAIC Staff	*T Sept. 09
28	H	Groupwide Supervision/Group Supervision Authority	Consider adding similar provisions to the Model Holding Company Act or separate statutory section using the Nebraska statute as a starting point for drafting/refinement.	Draft	GSIWG	
29	A	Holding Company filings	Require registered Holding Companies to file financial data in a standard format to provide the capability to analyze their financial profiles in a prescribed format.	Draft	NE	*T Sept. 09
30	A	Holding Company filings	Require Holding Companies to also file their federal or national filings with state insurance departments.	Draft	NE	*T Sept. 09

Comments from GSIWG - Insurance Holding Company System Regulatory Act Questionnaire						
Grouping for Discussion	Topic	Study Items and/or Recommendations	Working Group Action (Pass, Draft, Research Further, Refer)	Assignment of Task	Deliverables Tentative *T Final *F	
31	E	Limited Liab Company Reference	Add limited liability company references wherever appropriate to clean up the model.	Draft	NAIC Staff	*F Sept. 09
32	C	Materiality Requirement of Revisions to agreement	If a reinsurance agreement meets the materiality requirement requiring a filing for prior notice, do all revisions need to be reported under the prior notification requirement or only modifications that meet the materiality requirements? Suggest Adding: • Authority to the insurance department to require the immediate and/or ultimate holding company of the insurer to maintain an RBC of 300% of the insurer.	Draft	TX, IL	*T Sept. 09
33	K	Combine with 56		Pass (Possibly Consider Later if appropriate related issues are discussed)		
34	A, E	Regulatory Authority over Holding companies	Require all Holding Companies to register or license with the States and the NAIC to enhance the regulatory powers of the Commissioners over those entities.	Defer until after discussions of access to information and ERM		
35		Holding Company Structure	Require all financial service related legal entities (non-insurance) to be downstream of the insurance legal entity or comprised neatly within one financial services holding company.	Pass		
36	B	Supervisory Colleges	Consider adding a new section to the Model Holding Company Act to mandate or allow supervisory colleges, add parameters/criteria for supervisory colleges in terms of what size of holding company group would warrant a supervisory college, add confidentiality provisions, if necessary, and add rule/regulation authority to further refine the process.	Further Research/Possible Draft	IA, CT (Possible assistance from NAIC Legal & Supervisory College and Methods of Cross-Border Communications Subgroup)	*T Nov 09
37	I	Systemic risk analysis or Form D	Strengthen current materiality thresholds with respect to analysis of systemic risk and provide an update to the list of activities for prior approval of holding company transactions and disclosure of specified events occurring within the holding company structure in addition to reporting requirements just measured against a percentage of assets.	Further Research - Clarify with NAIC staff - Discussion item if relates to Form D - Defer until we get direction from SMITF if relates to systemic risk	GSIWG	
38	I	Systemic risk factors	Develop systemic risk factors for holding companies and affiliates on a group basis.	Further Research/Monitor	GSIWG Chairs	
39	D	Control	Investment managers/advisors who hold proxies in a company/group for mutual funds may have more than 10% control. This may trigger Form A. This may require more monitoring.	Draft	IL/CT	

Comments from GSIWG - Insurance Holding Company System Regulatory Act Questionnaire					
Grouping for Discussion	Topic	Study Items and/or Recommendations	Working Group Action (Pass, Draft, Research Further, Refer)	Assignment of Task	Deliverables Tentative *T Final *F
Comments from GSIWG International - Questionnaire					
40	J	Group Support - Asset Protections Laws	Consider adopting an asset protection law forbidding insurance companies from encumbering any assets supporting the reserves of the company or have the holding company enter into a letter of credit or trust account for any shortfall when the market value of assets are less than the carrying value of assets of the insurer. It would be beneficial if alien regulators and U.S. regulators had more interaction regarding financial oversight of insurers, which has begun.	Discussion Item	GSIWG
41	B	Coordination/Communication with Non-US Regulators		Further Research	IA/CT (Supervisory College)
42	B	Coordination/Communication with Non-US Regulators	A) Consider the role of the Lead State concept to include functioning as an international contact for Holding Company parent companies that are domiciled in other countries. Non-Lead States should be able to rely on the Lead State for obtaining the necessary information regarding international holding companies. Lead states should take the initiative in promoting better communication with international entities and foreign regulators.	Further Research	IA/CT (Supervisory College)
43	B	Coordination/Communication with Non-US Regulators	C) Consider a project to compare and contrast the PART A Accreditation standards for laws and regulations (17) with applicable, comparable international standards for holding companies. This would help create a basis for a common dialogue when coordinating with foreign counterparts.	Further Research	NAIC Staff
44	K	Data Repositories at the NAIC	B) Consider new data repositories at the NAIC for the maintenance of financial information for IFRS or GAAP financials (or other accepted comprehensive bases of accounting) including audited financial statements for international holding companies. This would encourage uniformity of review.	Further Research	NAIC Staff
45		DTAs	Consider disallowing deferred tax assets for insurers because it has no marketable value. (Not holding company matter)	Pass	
46	A	Examinations of Holding Companies	E) Consider developing best practices for risk assessments of all holding companies and develop models to determine trigger points for conducting financial examinations of holding companies.	Defer until drafting of Access to Info and Legal review of Federal Pre-emption is completed	
47	H	Legal Entity	Changes that are inconsistent with or detract from legal entity level solvency and receivership laws will weaken, not strengthen, our solvency protections. Group-wide considerations should be subordinate and/or supplemental to entity level requirements	Discussion Item	GSIWG
48		Group Wide Considerations	Two pressing reasons to get group supervision right. First, the crisis has exposed a big gap (e.g., unregulated entities at AIG) which needs to be addressed. Second, the approach in Bermuda (which is similar to the US) is not going to get a 'pass mark' from the EU under Solvency 2, which could mean Bermuda firms will be denied market access, unless we change.	Pass	
49	H	Level Playing Field	Solvency treatment of policyholders must be equitable and fair across jurisdictions. This requires a 'level' playing field for insurance entities in regards to solvency requirements.	Discussion Item	GSIWG

Comments from GSIWG - Insurance Holding Company System Regulatory Act Questionnaire					
Grouping for Discussion	Topic	Study Items and/or Recommendations	Working Group Action (Pass, Draft, Research Further, Refer)	Assignment of Task	Deliverables Tentative *T Final *F
50	Awareness of Issues	Global Plan for Recovery which included the topics (summary of comment letter topics): - Restoring Growth and Jobs - Strengthening Financial Supervision and Regulation - Strengthening our Global Financial Institutions - Resisting protectionism and prompting global trade and investment - Ensuring a fair and sustainable recovery for all - Delivering our Commitments	Discussion Item	GSIWG	

Comments from GSIWG - Insurance Holding Company System Regulatory Act Questionnaire					
Grouping for Discussion	Topic	Study Items and/or Recommendations	Working Group Action (Pass, Draft, Research Further, Refer)	Assignment of Task	Deliverables Tentative *T Final *F
51	Accounting Standards	There should be a set of harmonized solvency and accounting standards globally.	Pass		
52	Equivalence	There should be a mechanism that permits equivalence among regulatory bodies, especially in light of the current Solvency II debate.	Get Direction from SMITF	GSIWG	
53	Intervention Points	A common structure for the calculation of the main supervisory intervention points should be adopted for group supervision.	Discussion Item	GSIWG	
54	Risk Management	A minimum level of risk management standards is necessary in order to ensure adequate policyholder protection.	Discussion Item	GSIWG	
55	Holding Company Audit Reports	Consider having the holding company file their audit report based on statutory accounting principles.	Defer until after discussions on Accounting and Legal		
56	Minimum Capital Requirements	Consider developing high level analysis tools or minimum capital requirements (corporate RBC) for holding companies.	Discussion Item	GSIWG	
57	Maintenance Agreements	To the extent that group-wide capital is relied upon to maintain minimum entity level capital, we recommend establishment of a statutory structure that prescribes the form of capital maintenance agreements and provides for improved enforceability.	Discussion Item	GSIWG	
58	Fungibility / Diversification Credits	The fungibility of capital must be clearly defined and appropriate parameters established. Diversification should be recognized to the full extent that can be adequately demonstrated.	Discussion Item	GSIWG	
59	NAIC assistance with Budget and Communication with non US regulators	NAIC budget should provide resources necessary to support communication and coordination between international and lead state regulators. While international travel is expected to be limited, some face-to-face meetings between the relevant regulators seems advisable and approvals for such expenses within state budget processes are likely to be difficult.	Discussion Items	GSIWG	
60	Reporting Formats	The NAIC could assist communications between state and international regulators by maintaining contact information on relevant foreign regulators and by providing assistance with technology improvements such as video conferencing. D) Consider standardized electronic reporting formats, such as XBRL which is on track for adoption as a standard by the SEC so regulators would have improved query capabilities and analysis for financial reviews.	Further Research	IA/CT (Supervisory College)	
61	Supervisory Colleges	There must be a functional structure for group supervision that is effective from the insurance supervisors view and efficient from the insurance entities view. A structure such as the College of Supervisors could be considered.	Further Research	NAIC Staff	
			Further Research	IA/CT (Supervisory College)	

KEY

- A - Access to information within holding co
- B - Information sharing, communication, regulatory interaction with non US regulators, including supervisory college
- C - Agreements and transactions within holding company system
- D - Influence and Control, or lack thereof, regarding insurers
- E - Enterprise Risk Management
- F - Entities or Transactions within holding company that may risk detrimental impact
- G - Recognition of non US regulatory regimes and vice versa
- H - Groupwide Supervision Issues
- I - Systemic Risk Analysis and Factors
- J - Group Capital
- K - Reporting Methodologies

NE DOI Suggested Revisions (Related to Items 1, 2, 3, 9, 26, 26, 27, 29, 30 & 31)

INSURANCE HOLDING COMPANY SYSTEM MODEL REGULATION WITH REPORTING FORMS AND
INSTRUCTIONS
NAIC 450-1

Section 4. Forms - General Requirements

A. Forms A, B, C, D, and E are intended to be guides in the preparation of the statements required by Sections 3, 3.1, 4, and 5 of the Act. They are not intended to be blank forms which are to be filled in. The statements filed shall contain the numbers and captions of all items, but the text of the items may be omitted provided the answers thereto are prepared in such a manner as to indicate clearly the scope and coverage of the items. All instructions, whether appearing under the items of the form or elsewhere therein, are to be omitted. Unless expressly provided otherwise, if any item is inapplicable or the answer thereto is in the negative, an appropriate statement to that effect shall be made.

B. [Insert number] complete copies of each statement including exhibits and all other papers and documents filed as a part thereof, shall be filed with the Commissioner by personal delivery or mail addressed to: Insurance Commissioner of the State of [insert state and address], Attention: [insert name - title]. A copy of Form C shall be filed in each state in which an insurer is authorized to do business, if the Commissioner of that state has notified the insurer of its request in writing, in which case the insurer has [insert number] days from receipt of the notice to file such form. At least one of the copies shall be manually signed in the manner prescribed on the form. Unsigned copies shall be conformed. If the signature of any person is affixed pursuant to a power of attorney or other similar authority, a copy of the power of attorney or other authority shall also be filed with the statement.

C. A copy of Form B and Form C shall be filed with the National Association of Insurance Commissioners. A copy of Form B and Form C filed with the National Association of Insurance Commissioners shall be deemed to be filed in each state in which the insurer is authorized to do business. The filing shall be made within five days of the date the filing required in subsection B of this section. The National Association of Insurance Commissioners shall notify the commissioner of the receipt of the filing. The domestic commissioner may bring an action against the insurer for failure to file a complete or timely filing, which shall be a -----.

D. Statements should be prepared on paper 8 1/2" x 11" [or 8 1/2" x 14"] in size and preferably bound at the top or the top left hand corner. Exhibits and financial statements, unless specifically prepared for the filing, may be submitted in their original size. All copies of any statement, financial statements or exhibits shall be clear, electronically. Statements shall be easily readable and suitable for photocopying review and reproduction. Debits in credit categories and credits in debit categories shall be designated so as to be clearly distinguishable as such on photocopies. Statements shall be in the English language and monetary values shall be stated in United States currency. If any exhibit or other paper or document filed with the statement is in a foreign language, it shall be accompanied by a translation into the English language and any monetary value shown in a foreign currency normally shall be converted into United States currency.

Note: Section 4 may be omitted if it is included as instructions on Forms A, B, C, D and E.

Section 5. Forms - Incorporation by Reference, Summaries and Omissions

A. Information required by any item of Form A, Form B, Form D or Form E may be incorporated by reference in answer or partial answer to any other item. Information contained in any financial statement, annual report, proxy statement, statement filed with a governmental authority, or any other document may be incorporated by reference in answer or partial answer

to any item of Form A, Form B, Form D or Form E provided the document or paper is filed as an exhibit to the statement. Excerpts of documents may be filed as exhibits if the documents are extensive. Documents currently on file with the domestic Commissioner or the National Association of Insurance Commissioners which were filed within three (3) years need not be attached as exhibits. References to information contained in exhibits or in documents already on file shall clearly identify the material and shall specifically indicate that such material is to be incorporated by reference in answer to the item. Matter shall not be incorporated by reference in any case where the incorporation would render the statement incomplete, unclear or confusing.

B. Where an item requires a summary or outline of the provisions of any document, only a brief statement shall be made as to the pertinent provisions of the document. In addition to the statement, the summary or outline may incorporate by reference particular parts of any exhibit or document currently on file with the domestic Commissioner or the National Association of Insurance Commissioners which was filed within three (3) years and may be qualified in its entirety by such reference. In any case where two (2) or more documents required to be filed as exhibits are substantially identical in all material respects except as to the parties thereto, the dates of execution, or other details, a copy of only one of the documents need be filed with a schedule identifying the omitted documents and setting forth the material details in which the documents differ from the documents, a copy of which is filed.

Note: Section 5 may be omitted if it is included as instructions on Forms A, B, D, and E.

Section 6. Forms-Information Unknown or Unavailable and Extension of Time to Furnish

A. Information required need be given only insofar as it is known or reasonably available to the person filing the statement. If any required information is unknown and not reasonably available to the person filing, either because the obtaining thereof would involve unreasonable effort or expense, or because it rests peculiarly within the knowledge of another person not affiliated with the person filing, the information may be omitted, subject to the following conditions:

(1) The person filing shall give such information on the subject as it possesses or can acquire without unreasonable effort or expense, together with the sources thereof; and

(2) The person filing shall include a statement either showing that unreasonable effort or expense would be involved or indicating the absence of any affiliation with the person within whose knowledge the information rests and stating the result of a request made to that person for the information.

B. If it is impractical to furnish any required information, document or report at the time it is required to be filed, there may shall be filed with the Commissioner and the National Association of Insurance Commissioners a separate document:

(1) Identifying the information, document or report in question;

(2) Stating why the filing thereof at the time required is impractical; and

(3) Requesting an extension of time for filing the information, document or report to a specified date. The request for extension shall be deemed granted unless the Commissioner of the state of domicile within [insert number - probably 60] days after receipt thereof enters an order denying the request. An order of the Commissioner of the state of domicile shall be filed by such Commissioner with the National Association of Insurance Commissioners within five days of the entry of the order.

Note: Section 6 may be omitted if it is included as instruction on Forms A, B, C, D and E.

Section 15. Summary of Registration - Statement Filing

An insurer required to file an annual registration statement pursuant to Section 4 of the Act is also required to furnish information required on Form C, hereby made a part of these regulations. An insurer shall file a copy of Form C in each state in which the insurer is authorized to do business, if requested by the Commissioner of that state.

FORM B

INSURANCE HOLDING COMPANY SYSTEM ANNUAL REGISTRATION STATEMENT

Filed with the Insurance Department of the State of _____
By _____

Name of Registrant
On Behalf of Following Insurance Companies
Name Address

Date: _____, 19_____
Name, Title, Address and telephone number of Individual to Whom Notices and Correspondence
Concerning This Statement Should Be Addressed:

ITEM 1. IDENTITY AND CONTROL OF REGISTRANT

Furnish the exact name of each insurer registering or being registered (hereinafter called "the Registrant"), the home office address and principal executive offices of each; the date on which each registrant became part of the insurance holding company system; and the method(s) by which control of each registrant was acquired and is maintained.

ITEM 2. ORGANIZATIONAL CHART

Furnish a chart or listing clearly presenting the identities of and interrelationships among all affiliated persons within the insurance **holding company system**. No affiliate need be shown if its total assets are equal to less than 1/2 of 1% of the total assets of the ultimate controlling person within the insurance **holding company system** unless it has assets valued at or exceeding \$[insert amount]. The chart or listing should show the percentage of each class of voting securities of each affiliate which is owned, directly or indirectly, by another affiliate. If control of any person within the system is maintained other than by the ownership or control of voting securities, indicate the basis of control. As to each person specified in the chart or listing indicate the type of organization (e.g., - corporation, trust, partnership) and the state or other jurisdiction of domicile.

ITEM 3. THE ULTIMATE CONTROLLING PERSON

As to the ultimate controlling person in the insurance holding company system furnish the following information:

- (a) Name;
- (b) Home office address;
- (c) Principal executive office address;
- (d) The organizational structure of the person, i.e., corporation, partnership, individual, trust, etc.;
- (e) The principal business of the person;
- (f) The name and address of any person who holds or owns 10% or more of any class of voting security, the class of such security, the number of shares held of record or known to be beneficially owned, and the percentage of class so held or owned;
- (g) If court proceedings involving a reorganization or liquidation are pending, indicate the title and location of the court, the nature of proceedings and the date when commenced.

ITEM 4. BIOGRAPHICAL INFORMATION

Furnish If the ultimate controlling person is a corporation, an organization, a limited liability company, or other legal entity furnish the following information for the directors and executive

officers of the ultimate controlling person: the individual's name and address, his or her principal occupation and all offices and positions held during the past 5 years, and any conviction of crimes other than minor traffic violations during the past 10 years. If the ultimate controlling person is an individual, furnish the individual's name and address, his or her principal occupation and all offices and positions held during the past 5 years, and any conviction of crimes other than minor traffic violations during the past 10 years.

ITEM 5. TRANSACTIONS AND AGREEMENTS

Briefly describe the following agreements in force, and transactions currently outstanding or which have occurred during the last calendar year between the registrant and its affiliates:

- (a) Loans, other investments, or purchases, sales or exchanges of securities of the affiliates by the Registrant or of the Registrant by its affiliates;
- (b) Purchases, sales or exchanges of assets;
- (c) Transactions not in the ordinary course of business;
- (d) Guarantees or undertakings for the benefit of an affiliate which result in an actual contingent exposure of the Registrant's assets to liability, other than insurance contracts entered into in the ordinary course of the registrant's business;
- (e) All management agreements, service contracts and all cost-sharing arrangements;
- (f) Reinsurance agreements;
- (g) Dividends and other distributions to shareholders;
- (h) Consolidated tax allocation agreements; and
- (i) Any pledge of the registrant's stock and/or of the stock of any subsidiary or controlling affiliate, for a loan made to any member of the insurance holding company system.

No information need be disclosed if such information is not material for purposes of Section 4 of the Act.

Sales, purchases, exchanges, loans or extensions of credit, investments or guarantees involving one-half of 1% or less of the registrant's admitted assets as of the 31st day of December next preceding shall not be deemed material.

Note: Commissioner may by rule, regulation or order provide otherwise.

The description shall be in a manner as to permit the proper evaluation thereof by the Commissioner, and shall include at least the following: the nature and purpose of the transaction, the nature and amounts of any payments or transfers of assets between the parties, the identity of all parties to the transaction, and relationship of the affiliated parties to the registrant.

ITEM 6. LITIGATION OR ADMINISTRATIVE PROCEEDINGS

A brief description of any litigation or administrative proceedings of the following types, either then pending or concluded within the preceding fiscal year, to which the ultimate controlling person or any of its directors or executive officers was a party or of which the property of any such person is or was the subject; give the names of the parties and the court or agency in which the litigation or proceeding is or was pending:

- (a) Criminal prosecutions or administrative proceedings by any government agency or authority which may be relevant to the trustworthiness of any party thereto; and
- (b) Proceedings which may have a material effect upon the solvency or capital structure of the ultimate **holding company** including, but not necessarily limited to, bankruptcy, receivership or other corporate reorganizations.

ITEM 7. STATEMENT REGARDING PLAN OR SERIES OF TRANSACTIONS

The insurer shall furnish a statement that transactions entered into since the filing of the prior year's annual registration statement are not part of a plan or series of like transactions, the purpose of which is to avoid statutory threshold amounts and the review that might otherwise occur.

ITEM 8. FINANCIAL STATEMENTS AND EXHIBITS

- (a) Financial statements and exhibits should be attached to this statement as an appendix, but

list under this item the financial statements and exhibits so attached.

(b) The If the ultimate controlling person is a corporation, an organization, a limited liability company, or other legal entity, the financial statements shall include the annual financial statements of the ultimate controlling person in the insurance holding company system as of the end of the person's latest fiscal year.

If at the time of the initial registration, the annual financial statements for the latest fiscal year are not available, annual statements for the previous fiscal year may be filed and similar financial information shall be filed for any subsequent period to the extent such information is available. Such financial statements may be prepared on either an individual basis; or, unless the Commissioner otherwise requires, on a consolidated basis if consolidated statements are prepared in the usual course of business.

Such financial statement shall be filed in a standard form and format adopted by the National Association of Insurance Commissioners.

The financial statements shall include any filings made to federal or national regulatory agencies.

Unless the Commissioner otherwise permits, the annual financial statements shall be accompanied by the certificate of an independent public accountant to the effect that the statements present fairly the financial position of the ultimate controlling person and the results of its operations for the year then ended, in conformity with generally accepted accounting principles or with requirements of insurance or other accounting principles prescribed or permitted under law. If the ultimate controlling person is an insurer which is actively engaged in the business of insurance, the annual financial statements need not be certified, provided they are based on the Annual Statement of the ~~insurer filed with the insurance department of the insurer's domiciliary state~~ and are in accordance with requirements of insurance or other accounting principles prescribed or permitted under the law and regulations of that state. If the ultimate controlling person is an individual, the annual financial statements shall consist of a copy of the individual's most recently filed tax return and a personal statement of net worth including identification of types and amounts of material assets and liabilities, which shall at all times remain confidential. [Note: is this latter part necessary? No, these filings are confidential per Section 7 of the act, and while belts and suspenders are always good in these areas, it might cause some ambiguity to have two separate confidentiality provisions]

(c) Exhibits shall include copies of the latest annual reports to shareholders of the ultimate controlling person and proxy material used by the ultimate controlling person; and any additional documents or papers required by Form B or regulation Sections 4 and 6.

A-to-Z Index Terms

FORMS

HOLDING COMPANIES

HOLDING COMPANIES - Capital/financial requirements

HOLDING COMPANIES - Dividends

HOLDING COMPANIES - Filing requirements

HOLDING COMPANIES - Forms/schedules

HOLDING COMPANIES - Organizational structure

NAIC 450-1

NE DOI - Draft Date September 11, 2009 (Related to Items 25)

HOLDING COMPANIES
INSURANCE HOLDING COMPANY SYSTEM REGULATORY ACT
NAIC 440-1

Section 3. Acquisition of Control of or Merger with Domestic Insurer

D. Approval by Commissioner: Hearings.

(1) The commissioner shall approve any merger or other acquisition of control referred to in Subsection A unless, after a public hearing, the commissioner finds that:

(a) After the change of control, the domestic insurer referred to in Subsection A would not be able to satisfy the requirements for the issuance of a license to write the line or lines of insurance for which it is presently licensed;

(b) The effect of the merger or other acquisition of control would be substantially to lessen competition in insurance in this state or tend to create a monopoly. In applying the competitive standard in this subparagraph:

(i) The informational requirements of Section 3.1C(1) and the standards of Section 3.1D(2) shall apply;

(ii) The merger or other acquisition shall not be disapproved if the commissioner finds that any of the situations meeting the criteria provided by Section 3.1D(3) exist; and

(iii) The commissioner may condition the approval of the merger or other acquisition on the removal of the basis of disapproval within a specified period of time;

(c) The financial condition of any acquiring party is such as might jeopardize the financial stability of the insurer, or prejudice the interest of its policyholders;

(d) The plans or proposals which the acquiring party has to liquidate the insurer, sell its assets or consolidate or merge it with any person, or to make any other material change in its business or corporate structure or management, are unfair and unreasonable to policyholders of the insurer and not in the public interest;

(e) The competence, experience and integrity of those persons who would control the operation of the insurer are such that it would not be in the interest of policyholders of the insurer and of the public to permit the merger or other acquisition of control; or

(f) The acquisition is likely to be hazardous or prejudicial to the insurance-buying public.

(2) The public hearing referred to in Paragraph (1) shall be held within thirty (30) days after the statement required by Subsection A is filed, and at least twenty (20) days notice shall be given by the commissioner to the person filing the statement. Not less than seven (7) days notice of the public hearing shall be given by the person filing the statement to the insurer and to such other persons as may be designated by the commissioner. The commissioner shall make a determination within the sixty (60) day period preceding the effective date of the proposed transaction. At the hearing, the person filing the statement, the insurer, any person to whom notice of hearing was sent, and any other person whose interest may be affected shall have the right to present evidence, examine and cross-examine witnesses, and offer oral and written arguments and in connection therewith shall be entitled to conduct discovery proceedings in the same manner as is presently allowed in the [insert title] Court of this state. All discovery proceedings shall be concluded not later than three (3) days prior to the commencement of the public hearing.

(3) The public hearing referred to in Paragraph (2) may be held on a consolidated basis, at the request of the person filing the application. The commissioner may opt out of a consolidated hearing, and shall provide notice to the applicant of the opt out within ten days of the receipt of the application. A hearing conducted on a consolidated basis shall be a public hearing, held within the United States at which the domestic commissioners for the insurers shall hear and receive evidence. The commissioner may attend such hearing, in person or by telecommunication.

(4) In connection with a change of control of a domestic insurer, any determination by the commissioner that the person acquiring control of the insurer shall be required to maintain or restore the capital of the insurer to the level required by the laws and regulations of this state shall be made not later than sixty (60) days after the date of notification of the change in control submitted pursuant to Section 3A(2) of this Act.

(5) The commissioner may retain at the acquiring person's expense any attorneys, actuaries, accountants and other experts not otherwise a part of the commissioner's staff as may be reasonably necessary to assist the commissioner in reviewing the proposed acquisition of control.

E. Exemptions. The provisions of this section shall not apply to:

(1) [Any transaction which is subject to the provisions of Sections [insert applicable section] and [insert applicable section] of the laws of this state, dealing with the merger or consolidation of two or more insurers].

NE DOI - Draft Date September 10, 2009 (Related to Items 1, 2, 3, 9, 26, 26, 27, 29, 30 & 31)

INSURANCE HOLDING COMPANY SYSTEM REGULATORY ACT
NAIC 440-1

Section 4. Registration of Insurers

A. Registration. Every insurer which is authorized to do business in this state and which is a member of an insurance holding company system shall register with the commissioner, except a foreign insurer subject to registration requirements and standards adopted by statute or regulation in the jurisdiction of its domicile which are substantially similar to those contained in:

- (1) Section 4;
- (2) Section 5A(1), 5B, 5D; and
- (3) Either 5A(2) or a provision such as the following: Each registered insurer shall keep current the information required to be disclosed in its registration statement by reporting all material changes or additions within fifteen (15) days after the end of the month in which it learns of each change or addition.

Any insurer which is subject to registration under this section shall register within fifteen (15) days after it becomes subject to registration, and annually thereafter by [insert date] of each year for the previous calendar year, unless the commissioner for good cause shown extends the time for registration, and then within the extended time. The commissioner may require any insurer authorized to do business in the state which is a member of a holding company system, and which is not subject to registration under this section, to furnish a copy of the registration statement, the summary specified in Section 4C or other information filed by the insurance company with the insurance regulatory authority of its domiciliary jurisdiction.

B. Information and Form Required. Every insurer subject to registration shall file the registration statement on a **form and in a format** prescribed by the NAIC, which shall contain the following current information:

- (1) The capital structure, general financial condition, ownership and management of the insurer and any person controlling the insurer;
- (2) The identity and relationship of every member of the insurance holding company system;
- (3) The following agreements in force, and transactions currently outstanding or which have occurred during the last calendar year between the insurer and its affiliates:
 - (a) Loans, other investments, or purchases, sales or exchanges of securities of the affiliates by the insurer or of the insurer by its affiliates;
 - (b) Purchases, sales or exchange of assets;
 - (c) Transactions not in the ordinary course of business;
 - (d) Guarantees or undertakings for the benefit of an affiliate which result in an actual contingent exposure of the insurer's assets to liability, other than insurance contracts entered into in the ordinary course of the insurer's business;
 - (e) All management agreements, service contracts and all cost-sharing arrangements;
 - (f) Reinsurance agreements;
 - (g) Dividends and other distributions to shareholders; and
 - (h) Consolidated tax allocation agreements;
- (4) Any pledge of the insurer's stock, including stock of any subsidiary or controlling affiliate, for a loan made to any member of the insurance holding company system;

(5) If requested by the commissioner, the insurer shall include consolidated financial statements of a holding company system including all affiliates;

~~(5)~~ (6) Other matters concerning transactions between registered insurers and any affiliates as may be included from time to time in any registration forms adopted or approved by the commissioner.

C. Summary of Registration Statement. All registration statements shall contain a summary outlining all items in the current registration statement representing changes from the prior

registration statement.

D. Materiality. No information need be disclosed on the registration statement filed pursuant to Section 4B if the information is not material for the purposes of this section. Unless the commissioner by rule, regulation or order provides otherwise; sales, purchases, exchanges, loans or extensions of credit, investments, or guarantees involving one-half of one percent (.5%) or less of an insurer's admitted assets as of the 31st day of December next preceding shall not be deemed material for purposes of this section.

E. Reporting of Dividends to Shareholders. Subject to Section 5B, each registered insurer shall report to the commissioner all dividends and other distributions to shareholders within fifteen (15) business days following the declaration thereof.

F. Information of Insurers. Any person within an insurance holding company system subject to registration shall be required to provide complete and accurate information to an insurer, where the information is reasonably necessary to enable the insurer to comply with the provisions of this Act.

G. Termination of Registration. The commissioner shall terminate the registration of any insurer which demonstrates that it no longer is a member of an insurance holding company system.

H. Consolidated Filing. The commissioner may require or allow two (2) or more affiliated insurers subject to registration to file a consolidated registration statement.

I. Alternative Registration. The commissioner may allow an insurer which is authorized to do business in this state and which is part of an insurance holding company system to register on behalf of any affiliated insurer which is required to register under Subsection A and to file all information and material required to be filed under this section.

J. Exemptions. The provisions of this section shall not apply to any insurer, information or transaction if and to the extent that the commissioner by rule, regulation or order shall exempt the same from the provisions of this section.

K. Disclaimer. Any person may file with the commissioner a disclaimer of affiliation with any authorized insurer or a disclaimer may be filed by the insurer or any member of an insurance holding company system. The disclaimer shall fully disclose all material relationships and bases for affiliation between the person and the insurer as well as the basis for disclaiming the affiliation. After a disclaimer has been filed, the insurer shall be relieved of any duty to register or report under this section which may arise out of the insurer's relationship with the person unless and until the commissioner disallows the disclaimer. The commissioner shall disallow a disclaimer only after furnishing all parties in interest with notice and opportunity to be heard and after making specific findings of fact to support the disallowance.

L. Violations. The failure to file a registration statement or any summary of the registration statement required by this section within the time specified for filing shall be a violation of this section.

Section 6. Examination

A. Power of Commissioner. Subject to the limitation contained in this section and in addition to the powers which the commissioner has under Sections [insert applicable sections] relating to the examination of insurers, the commissioner shall ~~also~~ have the power to examine any insurer registered under Section 4 and its affiliates to ascertain the financial condition of the insurer, including the risk of financial contagion to the insurer by the ultimate controlling party, or by any entity or combination of entities within the holding system, or by the holding company system on a consolidated basis.

B. Access to Books and Records. (1) The commissioner may order any insurer registered under Section 4 to produce such records, books, or other information papers in the possession of the insurer or its affiliates as are reasonably necessary to ascertain the financial condition of the insurer or to determine compliance with this Chapter.

(2) The commissioner may order any insurer registered under Section 4 to produce information not in the possession of the insurer if the insurer can obtain access to such information pursuant to contractual relationships, statutory obligations, or other method. In the event the insurer

cannot obtain the information requested by the commissioner, the insurer shall provide the commissioner a detailed explanation of the reason that the insurer cannot obtain the information circumstances and the identity of the holder of information. Whenever it appears to the commissioner that the detailed explanation is without merit, the commissioner may require, after notice and hearing, the insurer to pay a penalty of \$[insert amount] for each days delay, or suspension or revocation of the insurer's license.

C. Compelling Production. In the event the insurer fails to comply with ~~the~~ **an** order, the commissioner shall have the power to examine the affiliates to obtain the information. **The** commissioner shall also have the power to issue subpoenas, to administer oaths, and to examine under oath any person for purposes of determining compliance with this section. Upon the failure or refusal of any person to obey a subpoena, the commissioner may petition a court of competent jurisdiction, and upon proper showing, the court may enter an order compelling the witness to appear and testify or produce documentary evidence. Failure to obey the court order shall be punishable as contempt of court. Every person shall be obliged to attend as a witness at the place specified in the subpoena, when subpoenaed, anywhere within the state. He or she shall be entitled to the same fees and mileage, if claimed, as a witness in the district court, which fees, mileage, and actual expense, if any, necessarily incurred in securing the attendance of witnesses, and their testimony, shall be itemized and charged against, and be paid by, the company being examined.

B. D. Use of Consultants. The commissioner may retain at the registered insurer's expense such attorneys, actuaries, accountants and other experts not otherwise a part of the commissioner's staff as shall be reasonably necessary to assist in the conduct of the examination under Subsection A above. Any persons so retained shall be under the direction and control of the commissioner and shall act in a purely advisory capacity.

~~C. E.~~ Expenses. Each registered insurer producing for examination records, books and papers pursuant to Subsection A above shall be liable for and shall pay the expense of examination in accordance with Section [insert applicable section].

NE DOI - Draft Date September 11, 2009 (Related to Items 25)

HOLDING COMPANIES
INSURANCE HOLDING COMPANY SYSTEM MODEL REGULATION WITH REPORTING FORMS AND
INSTRUCTIONS
NAIC 450-1

Section 4. Forms - General Requirements

A. Forms A, B, C, D, and E are intended to be guides in the preparation of the statements required by Sections 3, 3.1, 4, and 5 of the Act. They are not intended to be blank forms which are to be filled in. The statements filed shall contain the numbers and captions of all items, but the text of the items may be omitted provided the answers thereto are prepared in such a manner as to indicate clearly the scope and coverage of the items. All instructions, whether appearing under the items of the form or elsewhere therein, are to be omitted. Unless expressly provided otherwise, if any item is inapplicable or the answer thereto is in the negative, an appropriate statement to that effect shall be made.

B. [Insert number] complete copies of each statement including exhibits and all other papers and documents filed as a part thereof, shall be filed with the Commissioner by personal delivery or mail addressed to: Insurance Commissioner of the State of [insert state and address], Attention: [insert name - title]. A copy of Form C shall be filed in each state in which an insurer is authorized to do business, if the Commissioner of that state has notified the insurer of its request in writing, in which case the insurer has [insert number] days from receipt of the notice to file such form. At least one of the copies shall be manually signed in the manner prescribed on the form. Unsigned copies shall be conformed. If the signature of any person is affixed pursuant to a power of attorney or other similar authority, a copy of the power of attorney or other authority shall also be filed with the statement.

C. If the applicant requests a hearing on a consolidated basis under Section 3(D)(3) of the Act, in addition to filing the Form A filed with the commissioner, the applicant shall file a copy of Form A with the National Association of Insurance Commissioners in electronic form. The date of the filing of the Form A shall be the date on which the Form A is filed with the commissioner. The National Association of Insurance Commissioners shall notify the commissioner of the receipt of the filing.

D. A copy of Form B and Form C shall be filed with the National Association of Insurance Commissioners. A copy of Form B and Form C filed with the National Association of Insurance Commissioners shall be deemed to be filed in each state in which the insurer is authorized to do business. The filing shall be made within five days of the date the filing required in subsection B of this section. The National Association of Insurance Commissioners shall notify the commissioner of the receipt of the filing. The domestic commissioner may bring an action against the insurer for failure to file a complete or timely filing, which shall be a -----.

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TX & IL DOI - Draft Date September 15, 2009 (Related to Items 5, 6, 7, 8, 20, 21, 22, 32)

INSURANCE HOLDING COMPANY SYSTEM REGULATORY ACT

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Section 5. Standards and Management of an Insurer Within a Holding Company System

A. Transactions Within a Holding Company System

(1) Transactions within a holding company system to which an insurer subject to registration is a party shall be subject to the following standards:

(a) The terms shall be fair and reasonable;

(I) Any agreement for cost sharing, services, and management must contain the following:

(i) who is providing services and what those services are;

(ii) definition of the methods of allocation of costs;

(iii) provision for the monthly settlement between parties;

(iv) provision which prohibits advancement of funds by the insurer to the affiliate

(v) provision that the insurer will maintain oversight and responsibility for functions provided by affiliate and insurer will monitor services annually for quality assurance;

(vi) provision that the insurer will maintain oversight and responsibility for proper internal control procedures;

(vii) provision that the books and records of the insurer include all books and records developed or maintained under or related to the agreement;

(viii) provision that any right of the non-insurer party to the agreement to access any books or records does not affect the status of those books and records as "books and records of the insurer"

(ix) provision that all books and records of the insurer -are and remain the property of the insurer and are subject to control of insurer;

(x) provision that all books and records of the insurer and copies thereof are made available to insurer upon request of insurer;

(xi) provision that all funds and invested assets of the insurer are the exclusive property of the insurer, held for the benefit of the insurer and are subject to the control of the insurer;

(xii) provision that insurer is allowed to unilaterally terminate the agreement without cause at any time upon notice;

(xiii) provision that insurer may unilaterally terminate the agreement with cause immediately;

- (xiv) provision that the insurer shall be indemnified in the event of gross negligence or willful misconduct on the part of the affiliate providing the services;
 - (xv) provision that requires the affiliate to post bond to cover damages resulting from errors and omissions or misconduct;
 - (xvi) provision that, pursuant to [Chapter 443 in TX OR insert reference to state receivership act] all of the rights of the insurer under the agreement extend to a receiver appointed under that Chapter, or to the Commissioner acting under a Seizure Order pursuant to that Chapter;
 - (xvii) provision that, if the insurer is placed in receivership under [insert reference to state receivership act] all books and records will immediately be made available to the receiver, and will be turned over to the receiver within seven days upon the receiver's request;
 - (xviii) [insert if state has adopted NAIC model receivership act] provision that if the insurer is seized by the Commissioner pursuant to [insert reference to state receivership act], all books and records will immediately be made available to the Commissioner, and will be turned over to the Commissioner within seven days upon the Commissioner's request;
 - (xix) provision stating that the affiliate has no automatic right to terminate the agreement if the insurer is placed in receivership pursuant to [insert reference to state receivership act];
 - (xx) provision that, if the insurer is placed in receivership pursuant to [insert reference to state receivership act], for any systems, programs, or other infrastructure which the affiliate made available to the insurer pre-receivership or maintained for purposes related to the agreement, the affiliate will continue to maintain those systems, programs, or other infrastructure and will make them available to the receiver;
 - (xxi) provision that the affiliate shall give the insurer thirty days notice of its intent to file bankruptcy; and
 - (xxii) provision that if the affiliate is placed in bankruptcy, none of the insurer's rights to access or take possession of records shall be abridged.
- (b) Charges or fees for services performed shall be reasonable;
- (i) cost or current market rate may be used, however, if cost is used, charges must be equal to or less than the current market rate;
 - (ii) evidence of current market rate must be provided;
 - (iii) the maximum term of the agreement may only be 10 years;
 - (iv) the agreement must contain a provision for an annual evaluation to ensure that charges are the lower of cost or current market value.
- (c) Expenses incurred and payment received shall be allocated to the insurer in conformity with customary insurance accounting practices consistently applied;

- (d) The books, accounts and records of each party to all such transactions shall be so maintained as to clearly and accurately disclose the nature and details of the transactions including such accounting information as is necessary to support the reasonableness of the charges or fees to the respective parties; and
 - (e) The insurer's surplus as regards policyholders following any dividends or distributions to shareholder affiliates shall be reasonable in relation to the insurer's outstanding liabilities and adequate to meet its financial needs.
- (2) The following transactions involving a domestic insurer and any person in its holding company system may not be entered into unless the insurer has notified the commissioner in writing of its intention to enter into the transaction at least thirty (30) days prior thereto, or such shorter period as the commissioner may permit, and the commissioner has not disapproved it within that period. Any amendments, modifications or termination of previously approved affiliated agreement require at least 30 days prior notice to the Commissioner. The notice should include information regarding the reasons for the change and the financial impact on the domestic insurer.
- (a) Sales, purchases, exchanges, loans, extensions of credit, or investments, provided the transactions are equal to or exceed:
 - (i) With respect to nonlife insurers, the lesser of three percent (3%) of the insurer's admitted assets or twenty-five percent (25%) of surplus as regards policyholders as of the 31st day of December next preceding;
 - (ii) With respect to life insurers, three percent (3%) of the insurer's admitted assets as of the 31st day of December next preceding;
 - (b) Loans or extensions of credit to any person who is not an affiliate, where the insurer makes loans or extensions of credit with the agreement or understanding that the proceeds of the transactions, in whole or in substantial part, are to be used to make loans or extensions of credit to, to purchase assets of, or to make investments in, any affiliate of the insurer making the loans or extensions of credit provided the transactions are equal to or exceed:
 - (i) With respect to nonlife insurers, the lesser of three percent (3%) of the insurer's admitted assets or twenty-five percent (25%) of surplus as regards policyholders as of the 31st day of December next preceding;
 - (ii) With respect to life insurers, three percent (3%) of the insurer's admitted assets as of the 31st day of December next preceding;
 - (c) Reinsurance agreements or modifications ~~thereto thereto in which the reinsurance premium or a change in the insurer's liabilities equals or exceeds five percent (5%) of the insurer's surplus as regards~~

~~policyholders, as of the 31st day of December next preceding,~~
including those agreements which may require as consideration the transfer of assets from an insurer to a non-affiliate, if an agreement or understanding exists between the insurer and non-affiliate that any portion of the assets will be transferred to one or more affiliates of the insurer;

- (d) All management agreements, service contracts, guarantees and all cost-sharing arrangements;
- (e) Guarantees when made by a domestic insurer; provided, however, that a guarantee which is quantifiable as to amount is not subject to the notice requirements of this paragraph unless it exceeds the lesser of one-half of one percent (.5%) of the insurer's admitted assets or ten percent (10%) of surplus as regards policyholders as of the 31st day of December next preceding. Further, all guarantees which are not quantifiable as to amount are subject to the notice requirements of this paragraph;
- (f) Direct or indirect acquisitions or investments in a person that controls the insurer or in an affiliate of the insurer in an amount which, together with its present holdings in such investments, exceeds two and one-half percent (2.5%) of the insurer's surplus to policyholders. Direct or indirect acquisitions or investments in subsidiaries acquired pursuant to Section 2 of this Act (or authorized under any other section of this Chapter), or in non-subsidiary insurance affiliates that are subject to the provisions of this Act, are exempt from this requirement; and

Drafting Note: When reviewing the notification required to be submitted pursuant to Section 5A(2)(f), the commissioner should examine prior and existing investments of this type to establish that these investments separately or together with other transactions, are not being made to contravene the dividend limitations set forth in Section 5B. However, an investment in a controlling person or in an affiliate shall not be considered a dividend or distribution to shareholders when applying Section 5B of this Act.

- (g) Any material transactions, specified by regulation, which the commissioner determines may adversely affect the interests of the insurer's policyholders.

Nothing in this paragraph shall be deemed to authorize or permit any transactions which, in the case of an insurer not a member of the same holding company system, would be otherwise contrary to law.

- (3) A domestic insurer may not enter into transactions which are part of a plan or series of like transactions with persons within the holding company system if the purpose of those separate transactions is to avoid the statutory threshold amount and thus avoid the review that would occur otherwise. If the commissioner determines that separate transactions were entered into over any twelve-month period for that purpose, the commissioner may exercise his or her authority under Section 10.
- (4) The commissioner, in reviewing transactions pursuant to Subsection A(2), shall consider whether the transactions comply with the standards set forth in Subsection A(1) and whether they may adversely affect the interests of policyholders.

- (5) The commissioner shall be notified within thirty (30) days of any investment of the domestic insurer in any one corporation if the total investment in the corporation by the insurance holding company system exceeds ten percent (10%) of the corporation's voting securities.

B. Dividends and other Distributions

No domestic insurer shall pay any extraordinary dividend or make any other extraordinary distribution to its shareholders until thirty (30) days after the commissioner has received notice of the declaration thereof and has not within that period disapproved the payment, or until the commissioner has approved the payment within the thirty-day period.

For purposes of this section, an extraordinary dividend or distribution includes any dividend or distribution of cash or other property, whose fair market value together with that of other dividends or distributions made within the preceding twelve (12) months exceeds the lesser of:

- (1) Ten percent (10%) of the insurer's surplus as regards policyholders as of the 31st day of December next preceding; or
- (2) The net gain from operations of the insurer, if the insurer is a life insurer, or the net income, if the insurer is not a life insurer, not including realized capital gains, for the twelve-month period ending the 31st day of December next preceding, but shall not include pro rata distributions of any class of the insurer's own securities.

In determining whether a dividend or distribution is extraordinary, an insurer other than a life insurer may carry forward net income from the previous two (2) calendar years that has not already been paid out as dividends. This carry-forward shall be computed by taking the net income from the second and third preceding calendar years, not including realized capital gains, less dividends paid in the second and immediate preceding calendar years.

Notwithstanding any other provision of law, an insurer may declare an extraordinary dividend or distribution which is conditional upon the commissioner's approval, and the declaration shall confer no rights upon shareholders until (1) the commissioner has approved the payment of the dividend or distribution or (2) the commissioner has not disapproved payment within the thirty-day period referred to above.

Drafting Note: The following Subsection C entitled "Management of Domestic Insurers Subject to Registration" is optional and is to be adopted according to the needs of the individual jurisdiction.

[C. Management of Domestic Insurers Subject To Registration.

- (1) Notwithstanding the control of a domestic insurer by any person, the officers and directors of the insurer shall not thereby be relieved of any obligation or liability to which they would otherwise be subject by law, and the insurer shall be managed so as to assure its separate operating identity consistent with this Act.
- (2) Nothing in this section shall preclude a domestic insurer from having or sharing a common management or cooperative or joint use of personnel,

property or services with one or more other persons under arrangements meeting the standards of Section 5A(1).

- (3) Not less than one-third of the directors of a domestic insurer, and not less than one-third of the members of each committee of the board of directors of any domestic insurer shall be persons who are not officers or employees of the insurer or of any entity controlling, controlled by, or under common control with the insurer and who are not beneficial owners of a controlling interest in the voting stock of the insurer or entity. At least one such person must be included in any quorum for the transaction of business at any meeting of the board of directors or any committee thereof.

- (4) The board of directors of a domestic insurer shall establish one or more committees comprised solely of directors who are not officers or employees of the insurer or of any entity controlling, controlled by, or under common control with the insurer and who are not beneficial owners of a controlling interest in the voting stock of the insurer or any such entity. The committee or committees shall have responsibility for recommending the selection of independent certified public accountants, reviewing the insurer's financial condition, the scope and results of the independent audit and any internal audit, nominating candidates for director for election by shareholders or policyholders, evaluating the performance of officers deemed to be principal officers of the insurer and recommending to the board of directors the selection and compensation of the principal officers.
 - (5) The provisions of Subsections C(3) and C(4) of this section shall not apply to a domestic insurer if the person controlling the insurer is an insurer having a board of directors and committees thereof that meet the requirements of Subsections C(3) and C(4)].
- D. Adequacy of Surplus. For purposes of this Act, in determining whether an insurer's surplus as regards policyholders is reasonable in relation to the insurer's outstanding liabilities and adequate to meet its financial needs, the following factors, among others, shall be considered:
- (1) The size of the insurer as measured by its assets, capital and surplus, reserves, premium writings, insurance in force and other appropriate criteria;
 - (2) The extent to which the insurer's business is diversified among several lines of insurance;
 - (3) The number and size of risks insured in each line of business;
 - (4) The extent of the geographical dispersion of the insurer's insured risks;
 - (5) The nature and extent of the insurer's reinsurance program;
 - (6) The quality, diversification and liquidity of the insurer's investment portfolio;
 - (7) The recent past and projected future trend in the size of the insurer's investment portfolio;
 - (8) The surplus as regards policyholders maintained by other comparable insurers;
 - (9) The adequacy of the insurer's reserves; and
 - (10) The quality and liquidity of investments in affiliates. The commissioner may treat any such investment as a disallowed asset for purposes of determining the adequacy of surplus as regards policyholders whenever in the judgment of the commissioner the investment so warrants.

Model Regulation Service— November 2001

**APPENDIX
ALTERNATE PROVISIONS**

Alternative Section 1. Findings

- A. It is hereby found and declared that it may not be inconsistent with the public interest and the interest of policyholders and shareholders to permit insurers to:
- (1) Engage in activities which would enable them to make better use of management skills and facilities;
 - (2) Diversify into new lines of business through acquisition or organization of subsidiaries;
 - (3) Have free access to capital markets which could provide funds for insurers to use in diversification programs;
 - (4) Implement sound tax planning conclusions; and
 - (5) Serve the changing needs of the public and adapt to changing conditions of the social, economic and political environment, so that insurers are able to compete effectively and to meet the growing public demand for institutions capable of providing a comprehensive range of financial services.
- B. It is further found and declared that the public interest and the interests of policyholders and shareholders are or may be adversely affected when:
- (1) Control of an insurer is sought by persons who would utilize such control adversely to the interests of policyholders or shareholders;
 - (2) Acquisition of control of an insurer would substantially lessen competition or create a monopoly in the insurance business in this state;

Model Regulation Service—January 2004

- (3) An insurer which is part of a holding company system is caused to enter into transactions or relationships with affiliated companies on terms which are not fair and reasonable; or
 - (4) An insurer pays dividends to shareholders which jeopardize the financial condition of such insurers.
- C. It is hereby declared that the policies and purposes of this Act are to promote the public interest by:
- (1) Facilitating the achievement of the objectives enumerated in Subsection A;
 - (2) Requiring disclosure of pertinent information relating to changes in control of an insurer;
 - (3) Requiring disclosure by an insurer of material transactions and relationships between the insurer and its affiliates, including certain dividends to shareholders paid by the insurer; and
 - (4) Providing standards governing material transactions between the insurer and its affiliates.
- D. It is further declared that it is desirable to prevent unnecessary multiple and conflicting regulation of insurers. Therefore, this state shall exercise regulatory authority over domestic insurers and unless otherwise provided in this Act, not over nondomestic insurers, with respect to the matters contained herein.

Alternative Section 2. Subsidiaries of Insurers

- A. Authorization. Any domestic insurer, either by itself or in cooperation with one or more persons, may organize or acquire one or more subsidiaries engaged in the following kinds of business:
- (1) Any kind of insurance business authorized by the jurisdiction in which it is incorporated;
 - (2) Acting as an insurance broker or as an insurance agent for its parent or for any of its parent's insurer subsidiaries;
 - (3) Investing, reinvesting or trading in securities for its own account, that of its parent, a subsidiary of its parent, or an affiliate or subsidiary;
 - (4) Management of an investment company subject to or registered pursuant to the Investment Company Act of 1940, as amended, including related sales and services;
 - (5) Acting as a broker-dealer subject to or registered pursuant to the Securities Exchange Act of 1934, as amended;
 - (6) Rendering investment advice to governments, government agencies, corporations or other organizations or groups;

Holding Company Act

- (7) Rendering other services related to the operations of an insurance business, such as actuarial, loss prevention, safety engineering, data processing, accounting, claims, appraisal and collection services;
- ~~(8)~~ Rendering services through Centers for Medicare & Medicaid Services, ("CMS"). Services rendered between affiliates for Centers for Medicare & Medicaid Services, ("CMS"), are required to be filed for approval (although services and fees for services are prescribed by federal government and are therefore preempted). The agreement must be filed.
- ~~(9)~~ Ownership and management of assets which the parent corporation could itself own or manage;

Drafting Note: The aggregate investment by the insurer and its subsidiaries acquired or organized pursuant to this paragraph should not exceed the limitations applicable to such investments by the insurer.

- ~~(10)~~ Acting as administrative agent for a governmental instrumentality that is performing an insurance function;
- ~~(11)~~ Financing of insurance premiums, agents and other forms of consumer financing;
- ~~(12)~~ Any other business activity determined by the commissioner to be reasonably ancillary to an insurance business; and
- ~~(13)~~ Owning a corporation or corporations engaged or organized to engage exclusively in one or more of the businesses specified in this section.

Legislative History (all references are to the Proceedings of the NAIC).

1969 Proc. II 736, 737, 738-751, 756 (adopted).
1972 Proc. I 14, 16, 443, 449 (corrected).
1980 Proc. II 22, 26, 29, 42-46 (amended, added Section 3.1).
1983 Proc. I 6, 37, 96, 99 (amended).
1985 Proc. I 19, 37, 178, 183-200 (amended and reprinted).
1985 Proc. II 11, 24-25, 74, 75-92 (amended and reprinted).
1986 Proc. I 10, 25, 72 (amended).
1986 Proc. II 12, 19-20, 93-94, 94-109 (amended and reprinted).
1993 Proc. 4th Quarter 16, 31, 57, 61-62 (amended).
1995 Proc. 4th Quarter 11, 33, 307, 310, 312-328 (amended and reprinted).
1996 Proc. 1st Quarter 124, 270, 272-275 (amendments adopted later printed here).
1997 Proc. 4th Quarter 11 (amendments adopted).
1999 Proc. 4th Quarter 15, 364, 369, 379-380 (amended).
2001 Proc. 2nd Quarter 11, 14, 319, 339, 342-348 (amended).

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IL DOI Suggested Revisions

Section 1C (Items 14 and 15)

“Control.” The term “control” (including the terms “controlling,” “controlled By” and “under common control with”) means the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract other than a ~~commercial~~ contract for goods or nonmanagement services, by contract for goods or nonmanagement services where the volume of activity from such contract results in a reliance relationship between the parties, by common management, or otherwise, unless the power is the result of an official position with or corporate office held by the person. Control shall be presumed to exist if any person, directly or indirectly, owns, controls, holds with the power to vote, or holds proxies representing, ten percent (10%) or more of the voting securities of any other person. This presumption may be rebutted by a person’s showing the commissioner, made in the manner provided by Section 4K, -where such person has the burden of proof, that control does not exist in fact. The commissioner may determine, after furnishing all persons in interest notice and opportunity to be heard and making specific findings of fact to support the determination, that control exists in fact, notwithstanding the absence of a presumption to that effect.

Section 3B (Item 24)

Content of Statement. The statement to be filed with the commissioner shall be made under oath or affirmation of the person or officer of such person acquiring ~~of the person or officer of such person acquiring~~ ownership and shall contain the following information:

Section 4K (Item 15)

Disclaimer. Any person may file with the commissioner a disclaimer of affiliation with any authorized insurer or a disclaimer may be filed by the insurer or any member of an insurance holding company system. The disclaimer shall fully disclose all material relationships and bases for affiliation between the person and the insurer as well as the basis for disclaiming the affiliation. After a disclaimer has been filed, the insurer shall be relieved of any duty to register or report under this section which may arise out of the insurer’s relationship with the person unless and until the commissioner disallows the disclaimer. The commissioner ~~shall may~~ disallow a disclaimer. Upon such disallowance, an administrative hearing shall be granted upon the petition of the disclaiming party. only after furnishing all parties in interest with notice and opportunity to be heard and after making specific findings of fact to support the disallowance.

(Item 19)

In regard to item 19 on disclaimers of control and affiliation, it seems that may take significant time to review all pertinent sections and formulate clarifications.

(Item 25)

In regard to item 25, it appears this is in discussion stage within the Working Group so it seems too soon for language suggestions.

CT DOI – Item #39

<u>Category</u>	<u>Cause of Trouble/Risk</u>	<u>Comments</u>
REPUTATIONAL	Market disruption	<p>An investor with a large % of Holding Company stock may be entitled to divest significant shares, therefore driving the stock price down. This may lead investor's and policyholder's confidence levels to decrease. This may also lead to ratings downgrades (if in combination with other issues).</p> <p>BEST PRACTICES: Upon request for an exemption from change in control, notify the insurer to obtain board of directors "no objection" to one investor holding a material amount of stock. Some Holding Company structures have a limitation on % of stock ownership allowed for investment purposes.</p> <p>Statement from the investor- investment buying and selling policy</p>
OPERATIONAL	The ability to influence Management and Policy decisions	<p>An investor with a large % of Holding Company stock may inherently have the ability to influence management and policy.</p> <p>BEST PRACTICES: Upon reviewing the exemption from change in control, inquire not only about the ability to obtain a board seat, but even being a "non voting observer" on the board. Holding Company board controls should be firmly in place to assure that "influencing policy and management decisions" cannot occur.</p> <p>Board member internal controls should be</p>

Attachment Two-c

reviewed upon exam.

FINANCIAL	The Financial Condition of Holding Company and Insurer deteriorates	Due to the risks mentioned above, both Reputational and Operational, can lead to financial risks. BEST PRACTICES: Annual attestation from the investor, stating that there are no changes in investing philosophy. (As approved in the exemption from change in control)
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*2009 Fall National Meeting
Washington, DC*

**Subgroup on Supervisory Colleges
and Methods of Cross-Border Communication
of the Group Solvency Issues (EX) Working Group
September 23, 2009**

Meeting Summary Report

The Subgroup on Supervisory Colleges and Methods of Cross-Border Communication of the Group Solvency Issues (EX) Working Group met via conference call on Aug. 27, 2009.

During this call, the Subgroup:

- Discussed the one-sided nature of conversations with federal regulators and proposed solutions.
 - Subgroup will explore the framework for proposing regulations to federal authorities requiring information sharing between different regulators and will research which federal entities would be involved for discussion at next meeting.
- Discussed possible processes in which U.S. regulators who participate in supervisory colleges can share experiences pre- and post-supervisory colleges with other relevant regulators, such as through the creation of a tracking system whereby the NAIC would monitor attendance at supervisory colleges and create best practices for regulators to share information pre- and post-supervisory college attendance.
- Discussed components of IAIS MMOU and subsequent actions for state review and possible future state accession to this cooperation and information sharing mechanism.
 - Subgroup will prepare summary memorandum of IAIS MMOU for discussion at next meeting and discuss next steps for disseminating such memorandum for discussion at state level.
- Discussed drafting amendments to Model Holding Company Act or Regulation regarding authorizing supervisory colleges and enabling the sharing of information by state regulators with federal and international regulators for discussion at next meeting.
 - Subgroup will prepare draft amendment to Model Holding Company Act or Regulation requiring state insurance regulators to share information with federal and international counterparts.
 - Subgroup will prepare general language amending Model Holding Company Act or Regulation to authorize the use of supervisory colleges where appropriate for further discussion and refinement at next meeting.
 - Subgroup will prepare draft amendment to Model Holding Company Act or Regulation enabling states to have all costs for attending supervisory colleges be borne by the insurer as part of the examination process.

W:\Sep09\TF\SMI\Group Solvency wg\Att 5f 3a - Subgroup Report to Working Group for September meeting (2) (3).doc

INTERNATIONAL ASSOCIATION OF INSURANCE SUPERVISORS



GUIDANCE PAPER ON THE USE OF SUPERVISORY COLLEGES IN GROUP-WIDE SUPERVISION

DRAFT, 14 SEPTEMBER 2009

This document was prepared by the Insurance Groups and Cross-sectoral Issues Subcommittee in consultation with IAIS members and observers.

This publication is available on the IAIS website (www.iaisweb.org).

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Preamble

The IAIS Insurance Core Principles (ICPs) establish the fundamental requirement for supervision on a group-wide basis: “the supervisory authority supervises its insurers on a solo and a group-wide basis” (ICP 17). The Principles on group-wide supervision elaborate on the requirements of ICP 17, with the purpose of establishing an internationally acceptable framework that contributes to ensuring appropriate streamlining, consistency, effectiveness and efficiency of supervision on a group-wide basis.

This Guidance paper is part of a first stage in the IAIS’s work on the development of global standards and guidance on group-wide supervision and complements the IAIS Guidance paper on the role and responsibilities of a group-wide supervisor.

These papers are necessarily evolutionary in their approach. In light of the current financial crisis it is recognised that timely development of enhanced communication and cooperation among supervisors involved in the supervision of a group on a group-wide basis is critical. Papers focussing on such coordination initiatives – the role of a group-wide supervisor and supervisory colleges –are therefore important foundation pieces. This work will also support the IAIS implementation of the Financial Stability Forum (FSF)¹ recommendations and the IAIS response to the G20 declarations.

For reasons of cross-sectoral consistency and supervisory convergence, close coordination with approaches chosen in other financial services sectors (in particular banking) is essential. However, it is equally important that all participating sectoral supervisors recognize and acknowledge the differences inherent in the business models for banking and insurance.

Following the approval of the Issues Paper on group-wide solvency assessment in March 2009 - developed jointly by the Insurance Groups and Cross-sectoral Issues Subcommittee and the Solvency and Actuarial Issues Subcommittee - the agenda of the IAIS on group-wide supervision has developed. In particular, over the period 2009-2011, standards setting work will progress on aspects of solvency assessment on a group-wide basis as well as on issues of treatment of non regulated entities and establishing criteria for equivalence assessment.

As the IAIS takes forward this agenda, there are many complex issues and challenges to be considered, including :

- balancing the needs and views of its 140 member jurisdictions, recognising the diversity of regulatory and supervisory approaches and frameworks*
- acknowledging that some aspects of regulation - contract, insolvency and consumer protection legislation - may extend beyond the direct control of the insurance supervisor or the IAIS.*

¹ Now renamed the Financial Stability Board (FSB)
IAIS Guidance paper on the use of supervisory colleges in group-wide supervision
Draft, 14 September 2009

Guidance paper on the use of supervisory colleges in group-wide supervision

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1. Introduction

IAIS developments on group issues

1. Since its inception in 1994, the IAIS has developed a number of principles, standards and guidance papers to help promote the development, globally, of well-regulated insurance markets, consistent with one of its objectives under the IAIS By-laws. A further objective of the IAIS under the By-laws is to contribute to broader stability of the financial system.

2. The IAIS Insurance Core Principles (ICPs) establish the fundamental requirement for supervision on a group-wide basis. ICP 17 states that “the supervisory authority supervises its insurers on a solo and a group-wide basis”. Essential criteria (d) of ICP 17 indicates minimum aspects of supervision to be covered by group-wide supervision, “as a supplement to solo supervision”. Essential criteria (b) of ICP 17 goes on to require that supervisors, in meeting this fundamental requirement, “cooperate to avoid unnecessary duplication”.

3. The IAIS *Principles on group-wide supervision* (the Principles) elaborate on the requirements of ICP 17, with the purpose of establishing an internationally acceptable framework that contributes to ensuring appropriate streamlining, consistency, effectiveness and efficiency² of supervision on a group-wide basis.

4. The IAIS *Multilateral Memorandum of Understanding on Cooperation and Information Exchange* (IAIS MMoU) establishes a formal basis for cross-border cooperation and information exchange among supervisors, and hence covers the circumstances of supervision at group level.

² Where the concepts of effectiveness and efficiency of supervision are used, it is intended to mean effectiveness and efficiency in achieving the objectives of prudential supervision. In this context, effectiveness of supervision would take primacy over issues of efficiency alone, albeit the dual objectives may be achievable simultaneously.

5. The IAIS *Guidance paper on the role and responsibilities of a group-wide supervisor* supports the Principles, and provides guidance on one possible element of an international framework for group-wide supervision – the designation of a group-wide supervisor to promote efficient and coordinated group-wide supervision – while also referring to the use of supervisory colleges as another element.

6. The IAIS *Issues Paper on group-wide solvency assessment and supervision* (March 2009) is an exploration of the issues associated with developing a framework for group-wide supervision and has contributed to defining the forward agenda of the IAIS in this area. In particular, standard-setting work will progress on aspects of solvency assessment on a group-wide basis as well as on the issue of treatment of non regulated entities (including non operating holding companies) and on establishing criteria for equivalence assessment of supervisory regimes.

7. This guidance paper further complements this suite of papers on group-wide supervision. It provides guidance on the use of a supervisory college as a further element of an international framework for group-wide supervision – as a mechanism to facilitate cooperation and exchange of information among involved supervisors³ and coordination of supervisory activities on a group-wide basis in normal and crisis situations.

Developments in the Insurance Industry

8. Most internationally active insurers are organised in the form of groups with insurers within the group incorporated according to the legal framework in their respective local jurisdiction. The financial position, risk profile and governance (including risk management and control) of an insurer may be affected by its belonging to a group, with the possibility of both positive and negative effects⁴ on the prudential situation of the individual entities and the group as a whole.

9. In groups, risk management and control functions are often established at group level. Significant strategic and policy decisions are generally taken at the head of the group. Taking this into account, it is important to consider the management and governance structure of the group and the quality of risk management and internal controls on a group-wide basis.

10. It is, therefore, important for supervisors of insurers within a group to be able to form a comprehensive view of the business strategy, financial position, legal and regulatory position, risk exposure and risk management and governance processes of the insurance group as a whole, and to assess (and react to, as necessary) the prudential situation and solvency of the respective insurers within the group. Where the insurance business of the group is carried out in a number of jurisdictions and a number of different supervisors are involved, this makes the task of supervising on a group-wide basis more challenging and the coordination of supervisory activities more important.

11. The IAIS recognises that effective group-wide supervision can contribute to sound insurance markets, improved management of group-wide risk and capital and enhanced policyholder protection. At the same time, solo supervision will remain integral as the legal obligation to policyholders is established at the legal entity level. Therefore, to be effective and efficient, supervision of a group should be undertaken in a manner which recognises the respective requirements for solo and group-wide supervision, establishes common understanding and coordination among supervisors and avoids unnecessary duplication of supervision.

³ The determination of the involved supervisors will depend on the circumstances of the particular group and jurisdictions in which it operates, but could be all supervisors involved in the supervision of insurers within the group. Refer to section 6.2 on the Form and operational structure of a supervisory college.

⁴ The positive and negative effects are detailed in the *Issues paper on group-wide supervision* (Mar 2009)

12. The growing internationalisation of insurance business makes it appropriate and timely to explore mechanisms to achieve more effective and coordinated supervision on a group-wide basis, as a supplement to the solo supervision of each insurer within the group.

International developments in relation to financial stability issues

13. In the light of the financial market crisis which commenced in mid 2007, there has been an increased focus on issues of financial stability, and the risks associated with large financial organisations operating on a cross-border and/or cross-sector basis.

14. In the recommendations of the Financial Stability Forum (FSF) in April 2008 and the statements of the G20 (November 2008⁵) – there has been particular reference to the important role of supervisory colleges in enhancing supervisory cooperation and coordination of internationally active groups and as one mechanism for crisis management⁶. Protocols for the establishment of supervisory colleges for the major global financial institutions have been developed by a subgroup of the FSF working group on market and institutional resilience. The London summit of the G20 reinforced this work by demanding the FSB⁷ “set guidelines for, and support the establishment, functioning of, and participation in, supervisory colleges”⁸.

15. In developing this guidance, due regard has been had for these recent developments and recommendations in respect of supervisory colleges. As a member of the FSB, the IAIS provides this guidance paper as the basis of its initial input to the development of guidelines for supervisory colleges.

16. Consideration has also been given to the important work of the Joint Forum in the supervision of financial conglomerates – in particular, the Coordinator Paper and the Framework for Supervisory Information Exchange Paper. The experience of the banking sector in the establishment and use of global supervisory colleges has also been considered.

17. It is recognised that there is established experience within the insurance sector in the use of supervisory colleges, including in the European concept of coordinating committees and the US process for supervisory cooperation across its state based regulation system. The IAIS has undertaken a survey among members to gather information on their experiences with supervisory colleges in practice – the information gathered from that survey was used to inform the development of this paper and the results confirm and reinforce the guidance provided.

⁵ The G20 declaration from November 2008 states: “Supervisors should collaborate to establish supervisory colleges for all major cross-border financial institutions, as part of efforts to strengthen the surveillance of cross-border firms.”

⁶ The November declaration further states that: “Regulators should take all steps necessary to strengthen cross-border crisis management arrangements, including on cooperation and communication with each other and with appropriate authorities, and develop comprehensive contact lists and conduct simulation exercises as appropriate.”

⁷ One of the outcomes from the April 2009 London Summit, was the expansion of the scope and responsibilities of the FSF – now named the Financial Stability Board (FSB).

⁸ From the “Declaration on strengthening the financial system – London, 2 April 2009”.

2. Scope and purpose

2.1 Scope of the paper

18. Consistent with the identified scope of the Principles, the groups covered by this paper are those whose main activity is insurance, including reinsurance groups and an insurance subgroup within a financial conglomerate⁹. The guidance is intended to apply to insurance groups operating in multiple jurisdictions.

19. The Principles do not establish a detailed supervisory regime for group-wide supervision, but rather establish a framework within which group-wide supervision can be undertaken in an effective and efficient manner. The Principles acknowledge that there may be different approaches to group-wide supervision. Similarly, this guidance paper presents the use of a supervisory college as one mechanism for facilitating cooperation and exchange of information and effective coordination and communication among involved supervisors. While recognising the need for flexibility, the paper discusses factors to consider in the implementation of a supervisory college framework, the role and range of functions of a supervisory college, the establishment and operational activity of a supervisory college, including its form and membership and the interrelationship between the supervisory college and a designated group-wide supervisor.

20. In providing guidance on the use of a supervisory college in group-wide supervision, it is not the intention of this paper to lessen the importance of solo supervision or to replace the role of the solo supervisor in respect of insurers within its jurisdiction.

21. This guidance paper does not modify or supersede any legal or regulatory requirements in force in, or applying to, the respective jurisdictions of involved supervisors.

2.2 Purpose of the paper

22. As mentioned, this paper provides guidance on an international framework that contributes to ensuring appropriate consistency, effectiveness and efficiency of group-wide supervision and a streamlining of supervisory activities on a group-wide basis.

23. Such a framework will assist supervisors to collaborate at an international level in supervising the cross-border activities of a group: this in turn will contribute to the protection of policyholders and to overall financial market stability.

24. This paper considers the situation of establishing a supervisory college to facilitate cooperation and exchange of information, communication and coordination of supervisory activities on a group-wide basis as a supplement to the solo level supervision of the entities within the group.

25. The effective operation of a supervisory college is based on mutual trust and confidence among the involved supervisors. Group-wide supervision will be most effective where all involved supervisors act with a common understanding and commitment to cooperation and appropriate information exchange based on generally accepted and agreed supervisory principles and practices.

26. Mechanisms for enhanced cooperation and information exchange based on such mutual trust and common understanding can further contribute to the long-term objectives of convergence, equivalence assessment and recognition of supervisory practices within the insurance sector as well as cross-sectoral supervisory convergence. All involved supervisors share the ultimate aim of ensuring optimal, effective and efficient

⁹ While not directly within the scope of this paper, the IAIS acknowledges the relevance of financial conglomerates and the importance of considering mechanisms for supervisory communication and coordination on a cross-sectoral basis.

group-wide supervision and hence enhancing and making more effective solo supervision.

27. Supervisory colleges also provide an important mechanism for enhanced communication among involved supervisors and the insurer, giving supervisors a valuable opportunity to discuss relevant issues with top management of the group.

28. A benefit of establishing a supervisory college lies in promoting coordination of supervisory activities among involved supervisors, which assists in avoiding unnecessary overlaps and duplication of work and maintains necessary levels of protection for policyholders and stability of financial markets overall. The effective operation of a supervisory college may also avoid unnecessary supervisory burden for industry.

29. The establishment of a supervisory college does not remove the need for effective regular communication between supervisors involved in the supervision of a group, including the possibility of establishing other mechanisms to facilitate such communication (such as bilateral agreements, MoUs etc.)

3. Summary of Key Features in the use of Supervisory Colleges

30. This section identifies twelve key features in relation to the use of a supervisory college in group-wide supervision. These key features have been extracted from the sections which follow, as a summary of that more detailed guidance material. The key features are:

1. Appropriate flexibility in the establishment of a supervisory college - both when to establish and the form of its establishment - to reflect its particular role and functions is important.
2. Where established, a supervisory college should be organised in accordance with the nature, scale and complexity of the group; its form should be commensurate with the legal and organisational structure and business activities of the group.
3. A supervisory college has no legal or binding authority as a decision making body, nevertheless it should promote common understanding and agreement on supervisory activities in relation to group-wide issues.
4. Where a supervisory college is established, to be most effective it should generally be established as a permanent, integral part of the group-wide supervision process.
5. The effective operation of a supervisory college is based on mutual trust and confidence among the involved supervisors.
6. The key functions of a supervisory college should be defined, and may include assessment, on a group-wide basis, of risk exposures, capital adequacy and governance including risk management and internal controls.
7. It is vital that appropriate information sharing agreements are in place between the members of the supervisory college to ensure that confidential information can be shared in a secure environment.
8. The group-wide supervisor is expected to take the responsibility for initiating a supervisory college and to act as the key coordinator or chairman of the supervisory college, to the extent practicable.

9. The roles and functions of the supervisory college and the respective roles of the involved supervisors should be agreed and clearly defined to avoid unnecessary duplication of supervision.
10. A supervisory college is expected to meet on a regular basis, appropriate to the nature, scale and complexity of the group. In the case of a group which is relevant to overall financial stability the supervisory college should meet at least annually to be most effective.
11. The supervisory college provides involved supervisors an opportunity for discussion of issues with management at the group level.
12. Regular assessment of the effectiveness of a supervisory college in achieving its role and functions should be conducted. Where supervisory colleges at subgroup level are established regular assessment of the effectiveness of the coordination between the various supervisory colleges for the group should be conducted.
13. A supervisory college also has an important role in facilitating crisis management.

4. Interrelationship between Group-wide Supervisor and Supervisory College

31. The operational effectiveness of a group-wide supervisor may be enhanced considerably through the establishment of a supervisory college¹⁰ as a mechanism for enhancing cooperation and information exchange among involved supervisors. Also, effectiveness and efficiency of the supervisory college may be improved further through an awareness and understanding of the quality of relationship possible between the group-wide supervisor and other members.

32. This paper identifies a number of areas in respect of the operation of a supervisory college where the group-wide supervisor is expected to take an important role. These can be summarised as follows:

- initiating the establishment of a supervisory college
- clarifying the membership/participation of involved supervisors in the supervisory college, including considering the establishment of subgroup colleges to enhance the overall effectiveness of the college
- clarifying the functions of the supervisory college and the role of involved supervisors, including of the group-wide supervisor, which may be formalised in a terms of reference
- coordinating the ongoing activities of the supervisory college, including planning meetings, supervisory activities, processes of information exchange
- establishing a crisis management plan

33. In all of these areas, while the group-wide supervisor would be expected to take the initiative as the coordinator or chair of the supervisory college, the group-wide supervisor must necessarily work in collaboration with involved supervisors and seek, to

¹⁰ As noted in the *Guidance paper on the role and responsibilities of a group-wide supervisor*, "The benefits of designation of a group-wide supervisor can be further enhanced through mechanisms such asestablishment of a "college" of involved supervisors".

the extent possible, agreement among involved supervisors. In this respect, establishing early agreement and clarity of understanding on the operational aspects of the college will contribute to establishing good relationships among the involved supervisors from the commencement.

34. An important role of the group-wide supervisor will be the continued management of these relationships with and among supervisory college members. The group-wide supervisor should be mindful of the expectations of involved supervisors from the supervisory college, and their expectations of the role of the group-wide supervisor. Awareness of these expectations could play a pivotal role, especially in times of a crisis. This awareness should also include legal and internationally relevant facts and relationships, which may be critical to the supervisory actions taken in particular circumstances including crisis.

35. An efficient and harmonious relationship may only be possible when a mutual respect and trust is established and observed among involved supervisors. The group-wide supervisor should regularly consider opportunities to improve relationships and to reinforce mutual trust.

36. Access to relevant information for involved supervisors will be one important measure of the effectiveness of the supervisory college. While the group-wide supervisor will have a clear role in the gathering of relevant information, an equally important consideration will be the appropriate and timely dissemination of that information consistent with applicable confidentiality requirements. Interim information that has been received and may be of importance to the supervisory work of the other involved supervisors, should be made available to those supervisors. This will encourage mutual trust, sharing of information, and further collaboration and cooperation among all involved supervisors.

37. While the management of internal relationships is important, the group-wide supervisor should also play a role in establishing appropriate contacts with other associated participants who may be of assistance to the supervisory college, for example other sector participants in the case of a financial conglomerate. When identifying such participants the group-wide supervisor should take into consideration the impact and/or influence that they may have on the existing relationship between college members and should weigh these issues against the value of information and wealth of experience these additional members may be able to provide.

5. Role of a Supervisory College

5.1 General rationale

38. A supervisory college is generally established for the fundamental purpose of facilitating the effectiveness of supervision of entities which belong to a group; both facilitating supervision of the group as a whole on a group-wide basis and improving the solo supervision of the entities within the group¹¹. A supervisory college serves this purpose by providing a permanent forum for cooperation and communication between the involved supervisors. Through the sharing of information and discussion of supervisory issues, involved supervisors gain an improved mutual understanding of supervisory practices, which may contribute to enhanced convergence of supervisory practice on a global basis.

¹¹ Where reference is made to the entities within a group throughout this paper, consideration should be given to the circumstances of subsidiaries and/or branches, reflecting the inherent differences in their nature, to the extent appropriate.

39. The form, membership and operations of a particular supervisory college can be expected to vary according to the circumstances of the group and of the jurisdictions in which it operates. Appropriate flexibility in the establishment of a supervisory college, and the determination of its functions and operational structure, to reflect its particular circumstances is therefore important. A supervisory college should be organised in accordance with the nature, scale and complexity of the group; its form should be commensurate with the legal and organisational structure and business activities of the group¹².

40. Although a supervisory college has no legal or binding authority as a decision making body, in establishing the role and functions of a supervisory college, consideration should be given to the facilitation of coordinated supervisory activities. To the extent agreed among involved supervisors, and to the extent possible given any legal constraints in particular jurisdictions, this could include the delegation of tasks (but not legal responsibilities) and, where necessary, consistent and coordinated supervisory interventions. Ultimately any supervisory activity (including delegation of tasks) and coordinated supervisory interventions undertaken by a supervisory college will rely on cooperation among involved supervisors and does not override the various individual jurisdictions' legal responsibilities or existing supervisory relationships.

To facilitate group supervision

41. A supervisory college contributes to the coordinated supervision of the group and facilitates discussion and action on a collaborative approach to supervising a group, subject to any restrictions or requirements under each jurisdiction's legal framework.

42. A supervisory college supports the role of a group-wide supervisor, where designated, and assists the group-wide supervisor in undertaking its functions. A supervisory college facilitates information collection and analysis at the group level, including compiling and analysing information available on risk exposures, financial soundness and governance of group entities. With access to such aggregated information, a supervisory college may also enhance supervisory assessment of systemic risks.

To improve solo supervision

43. Through information collection and sharing, analysis and discussion, a supervisory college facilitates the transfer of knowledge and expertise among involved supervisors, and hence can contribute to improved supervision of the individual entities within the group. For example, effective cooperation may provide additional knowledge of the intra-group risks affecting an entity as a result of being a member of the group and may precipitate pre-emptive supervisory activities at the solo level.

As a permanent forum for cooperation

44. Where a supervisory college is established, to be most effective it should generally be established as a permanent, integral part of the group-wide supervision process. A supervisory college would generally be an ongoing mechanism, contributing to the ongoing protection of policyholders interests. As such, an effectively operating supervisory college should contribute to the prevention of financial loss or crisis (as well as being an important mechanism to foster better crisis management in the circumstances of financial crisis – refer to section 5.3).

45. A supervisory college provides a formal and effective permanent forum for supervisors to build relationships and engender greater cohesiveness in cooperating with

¹² Refer to recommendation V6 of the FSF Recommendations, April 2008

each other and coordinating supervisory activities in relation to the group and the entities within the group both on a going-concern basis and in situations of crisis management.

To facilitate improved understanding of supervisory practices and effectiveness of supervision

46. There may be significant variances in supervisory practices across jurisdictions, caused by the diversity of market environments and the specific features of a market which are better understood by the local supervisor. As supervisors work together through a supervisory college, they gain a greater understanding of the nature of the group and its risks. A supervisory college facilitates the transfer of knowledge and expertise to other supervisors allowing involved supervisors to become aware of different supervisory tools and approaches.

47. An important consequence of improving the understanding of supervisory practices among involved supervisors is the potential for enhanced supervisory convergence on a global basis. Also more effective and efficient group-wide supervision should result, with enhanced policyholder protection and a possible consequence of minimising regulatory burden on the industry.

5.2 The range of functions of a supervisory college

48. There is a range of functions which a supervisory college may undertake, depending on its role and the reasons for its establishment. The circumstances of the particular group and the legal and supervisory structures in the involved jurisdictions can also influence the range of functions of a supervisory college.

49. Ultimately, the involved supervisors should establish among themselves the appropriate functions of the supervisory college given its role, and the allocation of those functions among the involved supervisors. Where there is a designated group-wide supervisor for the group, that group-wide supervisor would be expected to play an integral and transparent role in the establishment and ongoing operation of the supervisory college, including taking the initiative in establishing and coordinating the functions of the supervisory college, in consensus with other involved supervisors. (Refer to section 4 on the interaction between the group-wide supervisor and the operations of a supervisory college).

50. The roles and functions of the supervisory college and the respective roles of the involved supervisors should be clearly defined to avoid unnecessary duplication of supervisory tasks and to ensure no gaps exist in the supervision of the group. For example, at its establishment the functions of a supervisory college may be set out in its terms of reference (refer to section 6.2) and the ongoing operations and activities of the supervisory college detailed in a supervisory plan. Where agreed among involved supervisors, delegation of supervisory tasks can be an appropriate means to increase efficiency of the work of a supervisory college.

51. In establishing the functions of a supervisory college, some of the key activities which should be considered include:

- Information sharing
- Assessment of risk exposures, financial soundness and capital adequacy and group governance, including risk management and internal control
- Coordinated supervisory activities (for example, joint inspections)
- Specialisation, special focus teams
- Liaison with insurer management
- Regular assessment of effectiveness.

*Information sharing*¹³

52. A main function of a supervisory college will be to facilitate enhanced supervision of the group and the legal entities within the group by providing greater access for involved supervisors to information and knowledge about the group and the environment in which it operates. Adequate information sharing arrangements are intended to provide supervisors with a vehicle to achieving a comprehensive understanding of the group and its risks while also protecting confidential information so that the group can be appropriately supervised.

53. As noted, effective group-wide supervision requires trust among supervisors. This is particularly the case in terms of sharing and exchanging information. As information is shared and exchanged in a secure and controlled environment, it both requires and encourages mutual trust. The supervisory college facilitates this relationship ultimately leading to greater cooperation.

54. The ability of each supervisor to share information must be determined to ensure that information remains confidential. The need to establish information sharing agreements¹⁴ should be considered to ensure confidentiality and define the parameters in which the information can be used. Supervisors are encouraged to initiate dialogue among themselves in order to identify ways in which they can foster an environment of cooperation and trust. Establishment of MoUs among involved supervisors could enhance the effectiveness of the supervisory college. Jurisdictions that are part of the IAIS MMoU will have had their legislative regimes assessed to ensure strict confidentiality requirements are met as a precondition for effective cooperation and coordination of joint supervisory activity.

Assessment of risks exposures, financial soundness and group governance

55. As described in section 4.2 of the *Guidance paper on the role and responsibilities of a group-wide supervisor*, the range of functions of a group-wide supervisor could include consideration of the following issues on a group-wide basis: risk analysis and capital adequacy assessment (including the sufficiency and adequacy of allocation of capital), fit and proper requirements and corporate governance and internal controls. As a mechanism for cooperation and coordination among involved supervisors and a forum for information exchange, an effective supervisory college may allow involved supervisors to gain an enhanced understanding of the group, its inherent risks, financial position and its business activities.

56. In the case where the group operates as a single economic entity, with management decisions being taken at the head of the group, and ERM frameworks and internal models being established and operated on a group basis, it is important for the involved supervisors to have a group-wide understanding of these aspects to complement their supervision of the entities within the group. The supervisory college provides a forum for involved supervisors to focus on risk assessment and capital management from a group-wide perspective.

57. A group-wide review and assessment of risks to which the group and its entities are or might be exposed can ensure a prospective focus of supervision and foster early warning of major risks to the extent possible. It can facilitate consideration of the impact of a group on the insurance industry, on other sectors of an economy, and any systemic risks which a group may present.

¹³ For further details on information sharing refer also to the Joint forum paper 'Framework for Supervisory Information Exchange' (1999) and the IAIS *Standard on the exchange of information*. (Jan 2002)

¹⁴ Information sharing agreements, such as MoUs, are mechanisms to share information, engender cooperation and trust, and ensure confidentiality.

Coordinated supervisory activities

58. Through a supervisory college, joint activities among involved supervisors may be organised and coordinated where appropriate and as agreed on a voluntary basis between the involved supervisors, subject to any legislative requirements/restrictions. An example of a joint supervisory activity may be joint inspections of one or more group entities, or joint inspection of a particular aspect of the groups functions such as internal audit, actuarial function or risk management processes. Through joint activities, all involved supervisors can benefit from the shared information and expertise, and use this to enhance the supervision of their local insurer. The undertaking of joint activities should not be taken to imply joint decision making or any delegation of an individual supervisor's responsibilities.

Specialisation, special focus teams

59. A supervisory college may facilitate the formation of special focus teams to evaluate areas of particular concern or importance to the supervisors, or to bring together the requisite expertise to examine a specialised aspect of the group's operations. As an example, a specialised focus team may be established through the supervisory college to assess a group's internal model and to share that information with all involved supervisors.

Liaison with insurer management

60. The supervisory college provides a forum for the supervisors and the insurer to engage in face-to-face dialogue. The insurer is afforded the opportunity to provide clarity with respect to its operations and its business strategies at a group-wide level. For the supervisors, the opportunity to discuss issues with management at the group level, and with a group-wide focus is valuable.

Regular assessment of effectiveness

61. Where a supervisory college is established, regular assessment of the effectiveness of the supervisory college in achieving its agreed role and functions should be conducted. Where a group-wide supervisor is designated, it would be expected that the group-wide supervisor would organise the assessment, ensuring input from all involved supervisors as well as considering the benefit of seeking input from the supervised insurers, to the extent appropriate.

5.3 The role of a supervisory college in crisis management

62. Supervisory colleges can be an effective tool in reducing the likelihood of crises and averting them. In fact, they are a tool for crisis prevention that contributes to the safeguarding of overall financial stability. While, there may be circumstances where a supervisory college is established purely or exclusively as a vehicle for crisis management this would be expected to be the exception in practice (refer to paragraphs 44 and 45). Nevertheless, a high level of cooperation between supervisors is necessary for good crisis management which could be facilitated by the establishment of a supervisory college.

63. Since a supervisory college is a forum to engender cooperation and mutual trust among supervisors, an effectively operating supervisory college would result in

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established relationships which would be beneficial particularly in times of financial distress or a crisis. Regular cooperation and communication can, in fact, facilitate efficient action in times of crisis. Where a crisis situation arises, an existing supervisory college could function, and should be well positioned, to contribute to the management of that situation and to finding coordinated and agreed solutions.

64. It is important to be flexible in the use of a supervisory college with regards to crisis management. In fact the approach chosen needs to be able to adapt to the particular and individual situation. Other mechanisms of coordination might also be considered or needed.

65. To be effective in crisis management, it is essential for a supervisory college to provide mechanisms to exchange and communicate important information effectively and efficiently. The timely exchange of information is crucial, while always preserving confidentiality requirements. This may mean that, under very exceptional circumstances, highly sensitive information is only exchanged on a "need to know" basis. In addition, requirements to consult widely on supervisory actions which may be appropriate in normal times may need to be limited in crisis situations to ensure necessary timely responses.

66. A supervisory college can also be used for the sharing of experiences and lessons learnt about crisis management i.e. more from the retrospective view. This way it can provide members with examples of good practices of crisis management.

Infrastructure in case of emergency/crisis management

67. While it is not expected to be the ultimate focus of a supervisory college, a crisis management plan should be discussed. In establishing the role and functions of any supervisory college it is important to consider the scenario of a crisis and the expected role of the college in that situation.

68. A supervisory college should consider, in advance, the due process of cooperation and coordination during emergency situations in order to benefit from well established information and cooperation channels and procedures once the crisis occurs (refer to paragraph 66 of the *Guidance paper on the role and responsibilities of a group-wide supervisor*). The channels for communication with the head of the group as well as other parts of the group should be clearly established in case a crisis emerges. The group-wide supervisor, where designated, should establish close liaison channels with group management and the board of directors as well as the owners of the group.

69. The supervisory college should have procedures in place which help involved supervisors to provide and receive all necessary information in a timely manner to facilitate well informed decisions within their own jurisdictions. Furthermore, there should be mechanisms in place related to the sharing of information on a voluntary basis.

70. The supervisory college may assist in performing and sharing crisis assessments as well as contribute to the management of a crisis. Therefore, comprehensive and up-to-date contact lists as well as realistic simulation exercises should be developed to increase crisis-resilience.

71. The approach to a crisis situation should appropriately reflect the nature, size and complexity of the group and the particular crisis situation. It may be the supervisory college, as a whole, which responds to a crisis or a crisis management team. Alternatively, the supervisory college may establish a subgroup whose focus would be on crisis management aspects and, therefore, may be better capable to assess systemic risks.

72. The supervisory college should remain aware of the important role it will play in supporting the group-wide supervisor, especially in times of financial stress or crisis. Also the benefit of such a holistic approach is to provide the supervisory college with solutions

73. A supervisory college could also be a means for involved supervisors to coordinate on the timing and content of information that could be disclosed to/communicated with third parties (such as local supervisory/regulatory bodies, international organisations or the public where appropriate) and the insurance group, both on an ongoing basis and/or in a crisis situation and in particular where systemic risks exist taking into account confidentiality requirements. The supervisory college should identify any potential areas where the interests of third parties, in a crisis situation, may be in conflict with the relevant objectives of the college. As an example, confidentiality rules which determine the ability of individual authorities to communicate firm specific information may be a conflict.

6. Establishment of a Supervisory College

6.1 Whether and when to establish a supervisory college

74. There is a high level of divergence in the insurance industry regarding the nature of organisations, the nature of regulation and supervision, and the development of markets and supervisory regimes in different jurisdictions. While enhanced convergence of supervisory practice is expected over time, there is currently a need for flexibility in the considerations of both whether and when to establish a supervisory college.

75. As a general premise, the establishment of a supervisory college should be considered where it is necessary to improve the effectiveness and efficiency of supervision – for example, when significant cross-border activities and/or intra-group transactions are conducted; where effective group-wide supervision is essential to the protection of policyholders; and/or where effective group-wide supervision is essential to the financial stability of the financial market as a whole.

76. Consideration should be given to the circumstances and/or other factors that could be considered in determining whether and when to establish a supervisory college. Also the principle of materiality and proportionality should be applied in this determination. Further a jurisdiction may determine that there are particular circumstances or minimum criteria which suggest that the establishment of a supervisory college should be a requirement.

77. The factors which are relevant in this context include the following (it is noted that these factors are also relevant to considerations on the form and operational structure of a supervisory college, addressed in section 6.2) :

- Relevance of the group to overall financial stability
 - where effective group-wide supervision of a particular insurance group is relevant to overall financial stability, the establishment of a supervisory college is expected.
 - the relevance of a group to overall financial stability would be highly dependant on the nature, scale and complexity of the cross-border activities and/or intra-group transactions and associated risks of the group.
- The nature and complexity of the business undertaken by the group
 - where the cross-border activities of the group are highly complex - through intra-group transactions etc - the effectiveness of pure solo supervision can be limited without appropriate cooperation and information exchange

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with related supervisors. Therefore, the establishment of a supervisory college is expected.

- Relevance of the group in specific insurance market
 - where a particular group has significant market share in one or more specific jurisdictions, the establishment of a supervisory college may be expected.
- Similarity of supervisory practices (such as risk and capital assessment, governance assessment and other key supervisory practices) among the involved supervisors
 - where the group operates mainly in jurisdictions with similar supervisory frameworks and practices (e.g. the EEA), the establishment of a supervisory college would be more practicable, and therefore may be expected.
- The operational and management approach of the group:
 - where the group functions - risk management, capital management, corporate governance and internal controls - are centralised, the establishment of a supervisory college should be encouraged to facilitate dialogue between the involved supervisors and management of the group.
- Legal constraints limiting the effectiveness of supervisory college in the involved jurisdictions
 - Ensuring professional secrecy and confidentiality are vital elements in allowing supervisors to share and exchange relevant information. Where, there are legal constraints to information exchange, the effectiveness of a supervisory college would be limited. In such a case, in considering the establishment of a supervisory college, supervisors should be encouraged to address any such legal constraints.

78. As a general point, where a supervisory college already exists in practice, but may not be comprehensive in its coverage (e.g. a regional college), that college may be adapted to meet the needs of the wider number of involved supervisors to the extent practicable. Involved supervisors should seek to avoid establishing duplicate supervisory colleges.

6.2 Form and Operational Structure of a Supervisory College

79. The criteria discussed in section 6.1 are important considerations not only in determining whether and when to establish a supervisory college, but also where a college is established, in informing the definition of the form and operational structure of that college, its membership and the focus of its work.

Overall approach

80. The legal and regulatory frameworks that exist in the jurisdictions where the group operates may vary considerably. This will place limitations on how each supervisor carries out its supervision of solo entities and the scope of its authority. This in turn will have an impact on any work that a supervisory college agrees to carry out. In particular, a supervisory college will need to ensure that any work planned does not go beyond the authority of a supervisor or exceed the legal framework that exists in a jurisdiction.

81. The resources and capabilities of each supervisor involved in a supervisory college may vary considerably. As such the supervisory college will need to ensure that the activities agreed to are appropriate and realistic for all of the involved supervisors. This may require that:

- any tasks allocated are achievable for the supervisor carrying out the work; and
- the supervisory college focuses on the areas of greatest risk.

82. Supervisory approaches may differ by jurisdiction, for example some have adopted a risk-based/principles approach to supervision while others use a rules based approach. These differences will need to be considered and appropriately reflected in the form and operations of a supervisory college.

83. As already stated, supervisory colleges would generally be expected to be established on a permanent basis. However, there may be circumstances where a supervisory college is established on an ad-hoc basis in order to coordinate a particular issue with regard to the group in question (e.g. crisis management).

*Membership of, and participation in, a supervisory college*¹⁵

84. The membership of a supervisory college would be expected to comprise representatives of each of the supervisors responsible for the day-to-day supervision of the insurers which are part of the group. While participation in a supervisory college is generally voluntary, broad involvement by the supervisors of the more significant entities is critical to the effective operation of that college.

85. To facilitate effectiveness and efficiency, careful consideration should be given as to how to approach the participation of members at meetings and in other activities of the supervisory college. There is a need to balance the desire for an inclusive membership approach with the need to maintain manageable operational structures and to avoid the supervisory college becoming unwieldy and unworkable.

86. The basis of participation should, to the extent possible, be agreed among involved supervisors having due regard for the particular circumstances of the group. However, pragmatic solutions should be found to facilitate the operational functioning of the supervisory college in an effective and efficient manner.

87. In the case of a large group with entities operating in many jurisdictions, the number of involved supervisors may make it impracticable to involve all members in supervisory college meetings. A structured approach to participation could be considered where for example, participation in the supervisory college meeting is on the basis of regional representatives, where that representative is responsible for communication to and from other regional supervisors. Another option may be to adopt a multiple tier structure of supervisory colleges, with subgroups of members identified and meetings organised to facilitate discussions at the subgroup levels (refer to below section on supervisory colleges at subgroup level).

88. Where participation in supervisory college meetings is limited, it is vital that other mechanisms such as secure members-only website be adopted to ensure the flow of information to and from all involved supervisors.

89. Further, clear criteria should be established for defining the basis of participation. Issues which should be considered in establishing these criteria include:

- the relative size and/or materiality of the entities relative to the group as a whole

¹⁵ The terms membership and participation should be interpreted in the context of these sections and in terms of every day usage. It is recognised that within the regulatory regimes of certain jurisdictions the terms may be defined for particular purposes and so take different meanings.

- the relative size or materiality of the entity relative to its local market
- the level of risk in a particular entity
- the role of the supervisory college and its relevance to the particular entity.

90. Regardless of the approach to participation in a supervisory college, each involved supervisor is expected to make every reasonable effort to cooperate and coordinate in a spirit of mutual trust, to ensure the protection of confidential information shared and to avoid unwarranted supervisory duplication and unnecessary supervisory burden for both the insurers and supervisors involved.

91. The membership and participation approach of a supervisory college should be reviewed on a regular basis, to reflect changing circumstances in the group and the effectiveness of the operational structures.

Supervisory colleges at subgroup level

92. Within a group, it is recognised that subgroups may be, or are required to be, identified to reflect various structural, operational or supervisory objectives. Such subgroups may exist within a jurisdiction or on a cross-border basis.

93. There may be circumstances where it is appropriate to establish a supervisory college at the level of such a subgroup (for example on a regional basis or sectoral basis, as in the case of an insurance group within a financial conglomerate). In the case of large groups, with many involved supervisors, such an approach may bring benefits in facilitating the involvement of all supervisors at an appropriate level (as described in paragraphs 84 – 91).

94. When it is considered necessary to establish colleges at a subgroup level, supervisors should carefully consider the appropriate form and operational structure of the subgroup college, having regard to the circumstances of the group and supervisory structure, to facilitate its effective operation. In particular, supervisors may consider the following practical aspects of implementation:

- whether the subgroup college is established on a temporary or a permanent basis
- the interrelationships between the various supervisory colleges for a group, as well as the interrelationship with a designated group-wide supervisor
- mechanisms to facilitate effective and efficient information sharing and coordination between the various colleges
- ensuring the best dialogue with the industry without unnecessarily duplicating regulatory intervention (e.g. a dialogue at subgroup level)

95. Further, in these considerations supervisors should be aware of establishing mechanisms or processes to avoid the potential inefficiencies that may arise in a structure of subgroup colleges, such as:

- withholding material information at the subgroup level,
- insufficient coordinated action/interventions at the subgroup level,
- potential conflicts of interest between the subgroup and whole group,
- duplication of supervision, by adding another layer.

96. Where supervisory colleges at subgroup level are implemented, regular assessment of their effectiveness and, in particular, the effectiveness of coordination between the various supervisory colleges for the group should be conducted.

Coordination and chairmanship

97. There may be various circumstances in which the establishment of a supervisory college is initiated, and depending on purpose and membership, various ways in which the roles of involved supervisors - including chairmanship – are determined. In general, the group-wide supervisor, where designated, would be expected to take the responsibility for initiating a supervisory college and to act as the key coordinator or chairman of the supervisory college, to the extent practicable.¹⁶

98. The chairman should ensure the prerequisites for the effective operation of a supervisory college exist, such as coordinating meeting schedules; confidentiality agreements etc. A supervisory college would be expected to meet on a regular basis appropriate to the nature, scale and complexity of the group. In the case of a group which is relevant to overall financial stability, it would be expected that the supervisory college should meet at least annually to be most effective.

99. The chairman should propose the agenda for supervisory college meetings, but should incorporate the views and opinions of other members. The agenda may be set to discuss specific issues, or wide ranging issues depending on what is happening globally and/or in respect of a particular group.

100. Supervisory college meetings should be planned with clarity of the outcomes that are being sought and, based on this, should clearly record the outcomes that are achieved, including :

- action points arising from any meeting(s);
- the individual(s) to whom a task has been assigned; and
- the deadline when an action should be complete.

It will be the responsibility of the supervisory college to track individual items to make sure that the necessary action has been carried out.

Mechanisms to facilitate information sharing and co-operation within a supervisory college

101. The importance of mutual trust and confidence, in particular with respect to the exchange of sensitive supervisory information, to establishing successful cooperation within a supervisory college has been noted. Further the need to ensure the protection of confidential information has been established.

102. There is no global law or regulation on confidential information; it is the responsibility of each supervisor within the supervisory college to ensure the safe handling of confidential information. Each member of the supervisory college must consider carefully the consequences of unintentional divulgence of information. Therefore, it is vital that appropriate information sharing agreements are in place between the members of the supervisory college to ensure that information can be shared in a secure environment.

103. There are two principle methods with which this could be achieved:

- Each authority involved in the supervisory college establishes a memorandum of understanding (MoU) on a bilateral basis with the other members of a supervisory college. It is feasible that in many instances such MoUs already exist so this may not be as onerous as it first appears.

¹⁶ Refer to the IAIS *Guidance paper on the role & responsibilities of a group-wide supervisor* (Oct 2008).

- The members of the supervisory college sign up to the IAIS MMoU which requires the compatibility and the commitment to a strict confidentiality regime.

Where confidential information, shared within a supervisory college, is also communicated to other supervisory authorities there also needs to be a formal mechanism in place with these supervisors to ensure the protection of the confidential information. Mechanisms could be included in MoU's or via direct arrangement by the supervisory college members.

Terms of reference of a supervisory college

104. When a supervisory college is first established the involved supervisors may seek to underpin its establishment with a formal document - terms of reference - which sets out the agreed terms of operation of the supervisory college. While recognising the need to allow for flexibility in the operation of a supervisory college, the terms of reference could generally cover the following matters (this is not an exhaustive list):

- The membership of the supervisory college – including the approach to participation of members in the college
- The process for appointing a supervisor for chairing the college. (This would typically but not necessarily be the group-wide supervisor, where designated.)
- Roles and functions of the supervisory college and of the members of the supervisory college, including expectations of the chair/designated group-wide supervisor¹⁷.
- Frequency and locations of meetings – The supervisory college should agree locations that are likely to ensure the participation of as many of the members as possible. Where it is not feasible for supervisors to be present at a meeting, best endeavours should be made with the arrangements, so that where possible, people can participate by other means – for example by a conference call or electronic means.
- Scope of the activities of the supervisory college – It is likely that the supervisory college will focus on the following issues at a group level:
 - the solvency and financial stability of the insurance group;
 - the assessment of intra-group transactions and exposures;
 - internal control and risk management within the insurance group; and
 - appropriate actions to mitigate risks identified.

To be most effective in considering these issues, the supervisory college may develop a shared view of risk.

- The regular information collected by the supervisory college and any notifications that should be made to it (from both supervisors and the group). The supervisory college should agree the frequency at which information is provided. This should be coordinated in a way so as to avoid duplicative requests and to reduce the burden on a group. The supervisory college should have an overview of an insurance group's strategic plans.
- Procedures for dealing with emergencies (including breaches of solvency positions or the crystallising of risk).
- Procedures for facilitating crisis management.

¹⁷ Further information can be found in the IAIS *Guidance Paper on the role and responsibilities of a group-wide supervisor* (Oct 2008).

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Group Solvency Issues (EX) Working Group
Conference Call
August 12, 2009

The Group Solvency Issues (EX) Working Group of the Solvency Modernization Initiative (EX) Task Force met via conference call Aug. 12, 2009. The following Working Group members participated: Ann Frohman, Co-Chair (NE); Danny Saenz, Co-Chair (TX); Kim Hudson (CA); Kathy Belfi (CT); Linda Sizemore (DE); Al Willis (FL); Alan Harder (IA); Jim Hanson (IL); Dave DelBiondo (PA); and Roger Peterson (WI). Also participating was: Jim Nixon (NE).

1. Review Topics Requiring Future Study/Research

Director Frohman said there are two focuses with regard to the topics received from various states and interested parties: short-term vs. long-term. She said that the discussion on the previous call addressed the short-term items related to enhancements to the Insurance Holding Company System Model Act (#430), and this call is focused on determining actions for the long-term issues. The Working Group discussed and grouped the various issues received in the comment letters into similar topics and assigned an action item to each issue, as outlined in the matrix (Attachment Five-A).

Mr. Hanson asked that a new issue be added to the list of model enhancement topics for research and drafting. The issue is regarding control by investment managers that hold proxies for their mutual fund clients who own shares of the company and these managers vote those shares for the mutual fund. Ms. Belfi said the situation exists that, while no individual fund holds more than 10%, the investment manager may control by proxy more of the holding company. Mr. Saenz said that Texas reviews these situations on a case-by-case basis and might require a Form A. Ms. Belfi volunteered to assist Mr. Hanson in reviewing and drafting this issue, item #39.

Regarding item #10, collateral examination authority, Mr. Peterson explained that this topic related to the need to understand how groups managed risk on a broader level. Therefore, he said, the language should be broader, so that when the examination authority kicks in, it encompasses specific risks and the impact on the condition of the insurer. Director Frohman recommended no action on this topic.

Director Frohman said that item #16, enterprise risk management, might already be addressed by the risk-focused examination process. In addition, she noted that item #54 also addresses enterprise risk management. Morag Fullilove (Group of North American Insurance Enterprises—GNAIE) said that she agrees this topic should be included as an issue for further discussion. Steve Broadie (Property Casualty Insurers Association of America—PCI) said the Working Group's direction on this issue might depend on the Solvency Modernization Initiative Task Force's direction on enterprise risk management. Mr. Peterson said Wisconsin would clarify its interest in this topic. Director Frohman said this topic would be included for further discussion. Mr. Broadie asked what this Working Group's interaction would be with the Task Force. Director Frohman said the Working Group would work closely with the Task Force, as the Task Force will be looking for feedback and the Working Group will be providing technical research.

Director Frohman said that items #17 and #18 appear related, as both are transactions detrimental to the insurer. She said item #18 relates to non-affiliated entities, which is not necessarily issues within the group; however, it is a materiality issue with entities that can impact the financial condition of the insurance enterprise or group. Mr. Saenz said he would not look at this from a non-affiliated focus, but more as part of the state's regular oversight of the insurer and the impact to the insurer. From a group solvency perspective, he said he views it as how the insurer is impacted by other portions of the holding company structure. Mr. Peterson said he agreed with Mr. Saenz's comments, and that regulators need to evaluate the holding company's impact on the insurance company. He said that the suggestion in item #18, requiring the holding company to take action with a non-insurance entity, is an area that would be hard to identify where to draw the line. When states have authority, they have responsibility to act. Other than trying to assess the impact on the insurer, his concern is with the state's responsibility and authority to make non-insurance companies desist from some other practice that regulators believe is risky. Mr. Hanson said he agreed and said the model was started to protect the policyholders from outside interests and that the Working Group should keep the primary purpose in mind. Director Frohman said she was looking at this item from a literal perspective; i.e., an entity outside the holding company group. However, she said that the way the concept is structured is not necessarily non-affiliates, but affiliates that are not regulated. Mr. Saenz said he looks at the issue from the perspective of being able to have greater transparency and the ability to gather information about other non-insurance affiliated entities and how those entities might be impacting the insurance entity. Mr. Peterson said his comments are related to item #17, which he

interprets as affiliated non-insurance, while item #18 is non-affiliated — and, therefore, not within the scope of this Working Group’s charge. He said the states have laws regarding material transactions that would address risks of this type. Director Frohman said the Working Group should not look at non-affiliates, but should look instead at affiliated non-regulated entities that — whether through reputational, ratings or liquidity issues — could, in essence, bring down the whole group. Director Frohman asked if legal assistance might be needed on this topic. Dan Schelp (NAIC) said that NAIC legal staff can research and provide their assistance on this issue. He said that another related issue may be federal preemption. Director Frohman said the recommendation could involve federal authority and, perhaps, dovetail with systemic risk regulation. She said item #17 would remain on the list for further research and NAIC legal staff assistance and no action would be taken on item #18 , as it is not within the scope of the Working Group.

Director Frohman said that item #23 is a matter of recognition, equivalence and having confidence in foreign supervisors. She suggested two tracks: 1) what is needed for a group structure; and 2) what regulators recognize from foreign jurisdictions. Ms. Fullilove said this is an important issue, but that it is difficult to assess the equivalence issue without looking at the overall issue of group supervision. She said that other jurisdictions are moving forward and looking at equivalence. As part of that, she said, in terms of Europe specifically, is determining if other jurisdictions have a form of group supervision. Director Frohman said the Working Group should seek clarification and direction from the Solvency Modernization Initiative Task Force, in terms of how far they want the Working Group to go on this issue, and whether it is for the purpose of group supervision development or a separate track on equivalency.

Director Frohman said item #33, RBC, is related to the capital requirement issue. Director Frohman said the Working Group is not ready for the legal work on this issue, as we need to frame what we are interested in terms of if there should be a group requirement. Mr. Broadie said the comment asks for a higher minimum capital for insurers in holding companies than insurers are required to maintain as sole entities, which he thinks raises some issues. Mr. Peterson said that his interpretation is that the language would allow each jurisdiction to establish this requirement based on the facts and circumstances related to a specific insurer. He said that the argument would have to be made that for a particular insurer that the RBC standard is not sufficient and that it would be necessary and prudent to require a higher level of capital. For example, he said, there are situations where the state seeks the cooperation of the holding company to get a target RBC at a higher range, rather than running the company at very near the 200% level. He suggested that the Working Group consider in what context regulators would want this authority and how it would be utilized. Mr. Broadie said the Working Group might also want to review recent changes in the Model Regulation to Define Standards and Commissioner’s Authority for Companies Deemed to be in Hazardous Financial Condition (#385). Director Frohman said the Working Group should defer item #33 and possibly come back to it later.

Director Frohman said item #34 relates to authority over holding companies. Mr. Peterson said that the need to license or register a holding company has more to do with achieving some other goals, such as getting information on enterprise-risk management and access to information or transactions. As such, he said, licensing and registration requirements might be a way to achieve these other goals. He suggested the Working Group defer this issue until the Working Group has a better sense of what those underlying goals are. Director Frohman agreed to defer item #34.

Director Frohman said item #35 relates to requiring all financial services-related legal entities (non-insurance) to be downstream of the insurance legal entity. She said that, in her opinion, it is a disservice to have a structure for regulators to dictate the business operational location of enterprises. It might be a way to organize companies for oversight, but it might not be practical. Mr. Saenz said it might be ideal if all regulators would require to be owned is other insurance and financial entities; however, insurers might want to invest in unrelated entities that regulators would not want insurance companies to own. Unless regulators are trying to prohibit those types of things, regulators might run into other U.S. capitalist issues. Mr. Slape said these proposals are ways to try to get transparency and get access to information so that regulators can see the contagion before it impacts the insurance company. He said this proposal would bury the contagion in the insurance company and make them directly at risk. Mr. Peterson said one positive aspect regarding this proposal is that having affiliated transactions with subsidiaries of the subject insurer helps simplify that process, because if there is excess compensation to those affiliates it is still within the insurance company. However, he said, the proposal as written goes too far to meet an objective like that. Director Frohman said the Working Group would take no action on item #35. If an issue comes up later in another fashion, then this item could be reconsidered.

Director Frohman said that items #37 and #38 relate to systemic-risk analysis. She said systemic risk has to first be defined. She suggested segregating this issue from the group-supervision issue. She said the Working Group would need assistance from Ray Spudeck (FL) to understand the directive for the Working Group on systemic issues. She said she does not sense that systemic risks will be resolved through group supervision. There are steps that can be taken in the group supervision

structure to enhance and promote the companies' well-being so to minimize exposure to systemic risk. She said this might be a subset or an overlapping component, but not mutually inclusive or exclusive of group supervision. Mr. Peterson suggested that it is a separate issue, because what constitutes systemic risk or which entities might be systemically significant is not for this Working Group to opine upon. Once those definitions are established, there might be separate procedures or communication with other regulators on those types of companies that might help address the issues related to systemic risk. Other parties have to be allowed to define systemic risk and provide some direction. Director Frohman suggested referring this issue to the Solvency Modernization Initiative Task Force. Mr. Peterson agreed that more guidance from the Task Force was needed. Mr. Nixon said the goal of this item appears to be strengthening the requirements for the Form D filings, changing the parameters and getting more information filed. Director Frohman said that item #37 is one we can get some background on from NAIC staff and, to the extent this is something less than systemic risk, the Working Group would discuss it as possibly a Form D item; however, if it is a systemic risk issue outside the enterprise, the Working Group would place it on hold until the Task Force addresses the topic. The Working Group agreed that item #38 should be sent to the Task Force to address.

Director Frohman said that item #40, regarding asset protection laws, should be left as a discussion item and included with group support issues.

Director Frohman said that item #41 is commentary on communication and coordination with non-regulators and does not include an action item. This item should be included under supervisory colleges.

Director Frohman said that item #42 is a filtering issue that comes out of supervisory colleges. If a state participates in a supervisory college and gains information from the college, and there other states in which the group does business, the question is how to get that information to the next tier. It suggests using the lead state concept for getting access to the international holding companies. She suggested this be put under the supervisory college.

Director Frohman said that item #43, related to comparisons to accreditation standards, and item #52, related to equivalence, should be referred to the Task Force as an action item on equivalence.

Director Frohman said that item #44, related to data repositories at the NAIC, is a topic for NAIC staff to address and provide advice to the Working Group.

Director Frohman said that item #45, related to deferred-tax assets, does not fall within the Working Group's charge and, therefore, the Working Group will pass on this item.

Director Frohman said that item #46 relates to the examination of holding companies. Mr. Schelp said the NAIC legal staff would look at the federal preemption issues. Mr. Slape said this is parallel to the drafting that Nebraska was doing on access to information. Director Frohman said this issue should be deferred until drafting of access to information and the legal review of federal preemption is completed.

Director Frohman said item #47 relates to groupwide supervision and is a discussion item. She said the threshold question would be whether the Working Group is looking to create a group supervisory structure that supplants or is supplemental to the solo legal supervisory regime. Mr. Saenz said he considers it more supplemental, rather than subordinate; i.e., the overall issue is for regulators to get access to information to be able to determine the financial condition of the entity being regulated. He said he does not necessarily want oversight of the holding company, or even every entity in the group, but rather to gather information and have transparency enough to evaluate if any issues are impacting the insurance companies, so the state can take the action necessary to protect the insurance entities. Director Frohman suggested that this question be the first agenda item for starting this topic discussion. Mr. Saenz agreed and repeated Mr. Peterson's comments about not necessarily wanting to have too much authority or responsibility for non-insurance entities, but wanting to understand how these other entities are impacting the insurance companies. Mr. Peterson said he believes that regulators will agree that the focus is at the entity level and the groupwide supervision is to supplement the entity-level work. He said the question needs to be given appropriate discussion and should clarify regulators' position on the issue before going to the international community to say this is one point where U.S. regulators are going to retain their current and different approach. Director Frohman said this is an important issue that will be kept as an action item, with the ultimate goal being a recommendation to the Solvency Modernization Initiative Task Force that would require vetting and, perhaps, a hearing. Ms. Fullilove said GNAIE recognizes the concerns Wisconsin has regarding the legal entities, but stresses the importance of moving forward with consideration of this issue. She stressed that competitiveness on a global basis is important, as is the efficiency and effectiveness of regulation.

Director Frohman said item #48 (related to equivalency, competitive issues and unregulated entities) appears to be just commentary and has no action item. The Working Group passed on this item.

Director Frohman said item #49 was related to the equitable treatment of policyholders across jurisdictions. She said the European Union recognizes that policyholders should be treated equitably, in the event of an insolvent enterprise with more than one insurance company — and this brings up issues in the United States regarding receivership priorities, distribution and timing. Without group capital support, she said, the U.S. regime treats entities as a solo legal enterprise; i.e., policyholders are treated equally by class within the insurance company, but not across all insures within one holding company system. This concept would be new to the U.S. regulatory system, but she said it would be worth further discussion and understanding in terms of feasibility and implications on equivalency. She said it should be a discussion item. Ms. Fullilove said the broader issue of the “level playing field” is one that all of the industry participants have addressed in their comments at the last meeting. While recognizing the inherent complications it presents, Ms. Fullilove agreed that this item should be kept on the list, as it is a central tenet of many international regulatory developments. Director Frohman said it goes beyond equivalency, as it is a practical issue. She said the Working Group should weigh in on this issue and how to address policyholders in a system with a jurisdiction outside the United States.

Director Frohman said item #50 relates to the competitive issue and internationally ensuring the U.S. insurance industry is a vital player in the international environment and that there are not regulatory barriers created under U.S. group supervision that inhibits growth in the U.S. industry. She said this should be a discussion item.

Director Frohman said item #51 relates to accounting standards. She said this would be an important issue and the Working Group should be sensitive to the ongoing discussions in other groups. There is no action item; therefore, the Working Group did not take any action on this issue and will, instead, follow the issue globally and through the NAIC.

Director Frohman said items #53, #56, #57 and #58 relate to solvency capital. This is a discussion item.

Director Frohman said item #55 relates to holding company audit reports based on statutory accounting principles. Ms. Fullilove said she thinks this item relates to the difficulty in reviewing the portions of the holding company that are not filed on a statutory basis. Ms. Fullilove said this ties into the broader context of how regulators are looking at the holding companies and the information available. It relates more to the tools that may be resolved in the long run if there are any changes in the NAIC’s accounting standards. Director Frohman said this item should be deferred until further direction is given on accounting and legal issues.

Director Frohman said item #59 relates to supervisory colleges. The issue is whether the states have the resources to meet at the supervisory level and have those types of discussions. She said that, initially, she viewed this item within the examination authority and, if there are issues there, then those reviewing supervisory colleges can flesh those out and advise the Working Group accordingly. This item will be included with the item on supervisory colleges.

Director Frohman said item #60 relates to the financial data repository and asked NAIC staff to address and advise on this issue.

Director Frohman said item #61 relates to supervisory colleges and would be included with that topic group.

Director Frohman said item #28 relates to groupwide supervision and should be a discussion item.

Having no further business, the Group Solvency Issues (EX) Working Group adjourned.

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Group Solvency Issues (EX) Working Group
Conference Call
July 23, 2009

The Group Solvency Issues (EX) Working Group of the Solvency Modernization Initiative (EX) Task Force met via conference call July 23, 2009. The following Working Group members participated: Ann Frohman, Co-Chair (NE); Danny Saenz, Co-Chair (TX); Kim Hudson (CA); Kathy Belfi (CT); Linda Sizemore (DE); Al Willis (FL); Kim Cross (IA); Jim Hanson (IL); and Steve Johnson (PA). Also participating was: Doug Slape (TX).

1. Review Comments Regarding Insurance Holding Company System Regulatory Act

Director Frohman said there are two focuses with regard to the comments received from various states and interested parties, short-term vs. long-term. The discussion on this call is focused on delegating short-term issues for enhancements to the Insurance Holding Company System Model Act (#440) and its corresponding model regulation (#450), and approving a request for model law development. She said the long-term issues — such as group supervision, capital benchmarks and international issues — will be discussed on the Aug. 12 conference call.

The Working Group discussed and grouped the various issues received via comment letters into similar topics and assigned an action to each issue as outlined in the matrix (Attachment Five-A).

Director Frohman stated that, with regard to issues regarding access to information, there is a need to access greater information than what is permitted in the model. Even though the model indicates that regulators can get information as needed to ascertain the financial condition of the insurer, regulators are looking at information that takes regulators beyond what the financial condition of the insurer is presently to looking at affiliates, holding companies and entities within the structure that can create financial contagion that could impact the entire financial enterprise. She volunteered to review and draft items #1, #2, #3, #9, #26, #27 and #30. With regard to item #27 related to filing confidential Form B to the NAIC, David Vacca (NAIC) said the model would need to specifically state that the filings are confidential and are to be filed with the NAIC in order to give insurers confidence that the NAIC could keep the data confidential.

Director Frohman said item #4 is related to information-sharing among regulators and is a supervisory college issue. Ms. Belfi said Connecticut would assist Iowa on drafting for supervisory colleges.

Director Frohman said that items regarding affiliated agreements suggest there are concerns with determining reasonable transactions with affiliates. She said a related issue is federal preemption and affiliated reinsurance agreements. Mr. Saenz suggested including item #18, related to transactions detrimental to the insurer, in this grouping. Director Frohman suggested that item #18 be discussed on the next call. Mr. Hanson and Mr. Saenz volunteered to address the issues related to affiliated agreements and federal preemption, which includes items #5, #6, #7, #8, #20, #21, #22 and #32.

Director Frohman said that item #11 is related to supervisory colleges. She said that regulators have information-sharing laws, but what regulators do not have is a mandate requiring information-sharing. She asked if, in a group setting, information-sharing should be required. Ms. Belfi said this topic is something that would be appropriate to include with the topic of supervisory colleges. Director Frohman suggested that item #13, related to confidentiality, be included with the supervisory college topic. Mr. Vacca suggested having NAIC legal staff assist in reviewing the confidentiality issue. Director Frohman said items #11, #12, #13 and #36 would be grouped with supervisory colleges, and she assigned to Iowa and Connecticut to draft these items.

Director Frohman said items #14, #15, #19, #24 and #25 (regarding acquisition of insurers, definition of control and disclaimers of affiliation) are related and should be grouped together. She suggested that item #25, related to coordinated review processes within the state, could also be included in this group. Mr. Slape said number #25 fits in with the Form A process and, if the Working Group is looking at revisions to the Form A process and standardization, it ties in with bringing about a more uniform process between states. Mr. Hanson volunteered to review and draft.

Director Frohman said the following items would be appropriate for discussion on the next conference call: item #10, regarding collateral examination authority; items #16, #17 and #18, related to enterprise-wide risk management and financial contagion; item #23, related to foreign-owned U.S. insurers; item #28, related to groupwide supervision; item #33, related to

RBC; item #34, related to regulatory authority of holding companies; item #35, related to holding company structure; and items #37 and #38, related to systemic risk.

Director Frohman said that item #29 is related to holding company financial data. Mr. Vacca said this item might be related to how regulators receive data and asked whether it needs to change to provide more clarity. Director Frohman said the standard format could be addressed with item #27, but this item would be more appropriate to discuss on the next conference call. She said that Nebraska could streamline it, but the substantive discussion should occur on the next call.

Director Frohman said that item number #31 is related to limited-liability companies. Mr. Vacca volunteered to address this item.

2. Adopt Request for Model Law Development

Director Frohman summarized a request for model law development for enhancements for the Insurance Holding Company System Model Act (#440) and its corresponding model regulation (#450). (Attachment Five-I1)

Robert Neill (American Council of Life Insurers—ACLI) said that he has reviewed many of the items that were submitted and has submitted a comment letter in response (Attachment Five-I2). He suggested the regulators look to see if the authority already exists and how that could be applied and if an amendment is needed. He said that with regard to item #9, the ACLI referenced the ongoing regulatory reform efforts and specifically systemic risk. He said the ACLI would continue to be a resource to the Working Group. Director Frohman asked the Working Group to review the ACLI comments. Regulators do have ability to do a lot of things but those can be improved upon. The solution might also be in good business and regulatory practices to make sure regulators are doing everything that can be done under the authority that the states already have.

A motion was made by Mr. Hanson to adopt a request for model law development for the Insurance Holding Company System Model Act and its corresponding model regulation. The motion was seconded by Ms. Belfi and unanimously adopted.

Having no further business, the Group Solvency Issues (EX) Working Group adjourned.

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REQUEST FOR MODEL LAW DEVELOPMENT

This form is intended to gather information to support the development of a new model law or amendment to an existing model law. Prior to development of a new or amended model law, approval of the respective Parent Committee and the NAIC's Executive Committee is required. The NAIC's Executive Committee will consider whether the request fits the criteria for model law development. Please complete all questions and provide as much detail as necessary to help in this determination.

Please circle whether this is _____ New Model Law _____ Amendment to Existing Model

1. Name of group to be responsible for drafting the model:

Group Solvency Issues (EX) Working Group

2. NAIC staff support contact information:

David Vacca
816-783-8134
dvacca@naic.org

3. Please provide a description and proposed title of the new model law. If an existing law, please provide the title, attach a current version to this form and reference the section(s) proposed to be amended.

Model 440 – Insurance Holding Company System Regulatory Act (copy attached)
Model 450 – Insurance Holding Company System Model Regulation with Reporting Forms and Instructions (copy attached)

There is intent to consider changes to the entire models, if necessary, to make it as effective as possible.

4. Does the model law meet the Model Law Criteria? Yes or No (Circle one) (If answering no to any of these questions, please reevaluate charge and proceed accordingly to address issues).

a. Does the subject of the model law necessitate a national standard and require uniformity amongst all states? Yes or No (Circle one)

If yes, please explain why

The models set standards for regulating transactions between insurance legal entities and other affiliated entities. The models currently represent a Part A: Laws and Regulations standard as part of the NAIC Financial Regulation and Accreditation Program; therefore sections of the model are uniformly adopted and represent a national standard. These models

assure sufficient authority to regulate the solvency of insurers who are part of a holding company system.

b. Does Committee believe NAIC members should devote significant regulator and Association resources to educate, communicate and support this model law?

Yes or **No** (Circle one)

NAIC Staff has conducted informal surveys with Chief Financial Regulators with the majority of states responding in favor of devoting significant resources to support the revisions of these models.

5. What is the likelihood that your Committee will be able to draft and adopt the model law within one year from the date of Executive Committee approval?

1 2 3 4 5 (Circle one)

High Likelihood

Low Likelihood

Explanation, if necessary:

Although the Working Group has identified several areas for revision and the time to draft and expose the revisions should be well within a year, the Working Group recognizes such changes could be highly controversial with interested parties and require involved discussions as the revised models pass up through the committee structure.

6. What is the likelihood that a minimum two-thirds majority of NAIC members would ultimately vote to adopt the proposed model law?

1 2 3 4 5 (Circle one)

High Likelihood

Low Likelihood

Explanation, if necessary:

Based on results of a questionnaire and discussions held during Working Group meetings and conference calls, the Chief Financial Regulators appear to support revisions to these Models.

7. What is the likelihood that state legislature will adopt the model law in a uniform manner within three years of adoption by the NAIC?

1 2 3 4 5 (Circle one)

High Likelihood

Low Likelihood

Explanation, if necessary:

Considering the recent risks highlighted during this most recent economic crisis, and the fact a version of the models have already been adopted by all states (but has yet to be updated since 2001), legislators should recognize the importance of updating states regulatory authority regarding holding companies.

8. Is this model law referenced in the Accreditation Standards? If so, does the standard require the model law to be adopted in a substantially similar manner?

Yes. The Part A standards references #6 – Holding Company Systems, which explains that state law should contain the NAIC Model Insurance Holding Company System Regulatory Act or an Act substantially similar, and the Department should have adopted the NAIC’s model regulation relating to this law. Currently, the F Committee only requires the 1986 version of Model 440 and 1986 or 1993 of Model 450. However, upon completion of the revised models, the F Committee would review and determine if revisions should be required elements and substantially similar.

9. Is this model law in response to or impacted by federal laws or regulations? If yes, please explain.

The model law is impacted by the federal Gramm-Leach-Bliley Act of 1999 (GLBA) with regard to the with the functional regulatory structure set forth in GLBA and related federal regulations.

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July 22, 2009

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Assistant Director
Insurance Analysis and Information Services Department
NAIC Regulatory Services Division
2301 McGee Street, Suite 800
Kansas City, MO 64108-2604

E-mail: dvacca@naic.org

Dear David,

In our June 10 letter responding to the Group Solvency Issues Working Group's holding company questionnaire, the ACLI urged the Working Group to explore efficiency and uniformity of current holding company financial filings and to examine existing regulatory powers under the Insurance Holding Company System Model Regulatory Act (Holding Company Act), to foster more effective use of the Act in its current form. To aid in this review, this letter outlines existing authority under the Act, offers comments on revisions to the Act recommended by regulators during the June NAIC meeting, and provides suggestions for improving efficiency and uniformity in any contemplated revisions to the Act. At this time ACLI has not developed a comprehensive response to each comment on the holding company questionnaire distributed on July 21 or the overall effort; however, the attached spreadsheet provides the general direction of ACLI concerns as we continue to review the recommendations.

ACLI observed that a number of the recommendations do not lend themselves to an immediate modification to the Act. Recommendations relating to systemic risk, holding company RBC requirements, supervisory college authority, and perhaps others will require ongoing coordination with other NAIC, federal and international initiatives. Pertinent group-wide issues that must also be considered include the following:

- There should be a set of harmonized solvency and accounting standards globally.
- Solvency treatment of policyholders must be equitable and fair across jurisdictions. This requires a 'level' playing field for insurance entities in regards to solvency requirements.
- A common structure for the calculation of the main supervisory intervention points should be adopted for group supervision.
- There should be a mechanism that permits equivalence among regulatory bodies, especially in light of the current Solvency II debate.
- There must be a functional structure for group supervision that is effective from the insurance supervisors view and efficient from the insurance entities view. A structure such as the College of Supervisors could be considered.
- The fungibility of capital must be clearly defined and appropriate parameters established. Diversification should be recognized to the full extent that can be adequately demonstrated.
- Risk management standards are necessary in order to ensure adequate

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policyholder protection.

As you know, the U.S. Department of the Treasury has also embarked on a comprehensive financial regulatory reform plan including significant changes to financial holding company supervision at the federal level, and the final impacts of these reforms are unclear at this time. As Congress continues to debate financial services regulatory reform, ACLI believes it is critically important to carefully consider details of federal legislative initiatives impacting holding company oversight as well as ongoing efforts to streamline group supervision and international solvency requirements as modifications to the Holding Company Act are discussed to avoid conflicting or duplicative federal and state regulatory requirements.

Existing Insurance Holding Company System Model Regulatory Act Authority

The current NAIC Holding Company Act grants extensive powers to the state insurance regulator. Such powers include the authority to order production of books, records or other information in possession of the insurer or its affiliates; review change of control; require specific financial reporting; regulate dividends, and enforcement authority. The Holding Company Act also authorizes the sharing of information with other regulators, including federal regulators.

Inspection of Books and Records:

The state insurance regulator has the power to order the insurer to produce records, books, or other information papers in its possession or in its affiliates (including the insurance holding company) possession as are reasonably necessary to ascertain the financial condition of the insurer or to determine compliance with the holding company law. If the insurer fails to comply with the order, the state insurance regulator has the power to examine the affiliates to obtain the information.

Enforcement Power:

The domestic state insurance regulator has the authority to take a number of enforcement actions against a person seeking to acquire control of a domestic insurer or the domestic insurer itself for violations of the insurance holding company law including the following:

- Injunction,
- Injunction from voting securities acquired in violation of law,
- Sequestration of voting securities acquired in violation of law,
- Monetary penalties,
- Cease and desist order,
- Criminal proceedings for willful violations,
- Placing the domestic insurer into receivership,
- Recovery of certain dividends in a domestic insurer receivership, and
- Revocation, suspension or nonrenewal of the domestic insurer's license.

Regulatory Review of Change of Control:

The Holding Company Act requires that any person that seeks to acquire control of a domestic insurer or any person controlling a domestic insurer file a statement (Form A) with the state insurance regulator and obtain the prior consent of the state insurance regulator. Control is presumed at ownership of 10% or more of voting securities, and specific grounds for disapproval are included.

Financial Reporting:

Financial Statement Filings – The insurer must file an annual holding company registration statement (Form B) including annual audited financial statement of the ultimate controlling person (e.g. the insurance holding company).

Inter-company Transaction Reports – A 30-day prior notice (Form D) to the state insurance regulator is required for certain material affiliate transactions including sales, purchases, exchanges, loans, extensions of credit, investments, reinsurance agreements, management agreements, service contracts, guarantees and cost-sharing arrangements. The regulator can also disapprove of the transaction within the 30-day period.

Other affiliate transactions are to be reported annually in Form B with material changes or additions to be reported within 15 days after the end of the month in which the insurer learns of each change or addition. Standards for affiliate transactions are also included in the Act.

Other Reports- Annual Form B filings relating to the holding company must include the following:

- Organizational chart,
- Information regarding the holding company, its principal business, its 10% owners, certain court proceedings, its directors and executive officers, information about certain litigation or administrative proceedings, and
- Holding company latest annual report to shareholders and proxy material.

Material changes or additions to be reported within 15 days after the end of the month in which the insurer learns of each change or addition.

Dividend Regulation:

Requires 30-day prior notice to the state insurance regulator of an “extraordinary dividend”¹ by the insurer to its parent, and the regulator can disapprove of the dividend within the 30-day

Protocols for Dealing with Other Regulators:

The domestic state insurance regulator is authorized to share information with, receive information from, and enter into information sharing agreements with other regulators, including federal regulators.

ACLI Comments on Specific Revisions to the Holding Company Act Recommended by Regulators:

The attached spreadsheet offers ACLI comments on specific changes to the Holding Company Act suggested by regulators at the June Group Solvency Issues Work Group meeting. The spreadsheet references corresponding statutory citations to existing authority where appropriate. As we review additional comments ACLI will offer a more comprehensive response.

Recommendations to Enhance the Insurance Holding Company System Model Regulatory Act

ACLI recommends that the Working Group carefully consider the following changes to improve efficiency and effectiveness of the Holding Company Act:

- Examine confidentiality and other protections in current state laws and current state holding company laws for purposes of sharing information among state, federal and international regulators (i.e. international supervisory colleges).
- Regardless of administrative form, regulation should not result in any unfair, discriminatory treatment of foreign owned US insurance or insurance holding companies relative to similarly situated US owned insurers or insurance holding companies or disruption of home country regulation of non US companies affiliated with US insurers. The system should recognize those

¹ “Extraordinary dividend” is defined to mean a dividend that, together with other dividends made within the preceding 12 months, exceeds the lesser of: (i) 10% of the insurer’s surplus as of the prior December 31, or (ii) the net gain from operations of the insurer, if the insurer is a life insurer, or the net income, if the insurer is not a life insurer, not including realized capital gains, or the 12 month period ending the prior December 31.

requirements applicable to the insurer's foreign or non-US parent which are broadly equivalent to U.S. regulations.

- Review the scope and substance of the existing filing requirements to ensure that required information is necessary, appropriate and useful. Insurance holding companies currently expend significant time and resources filing significant amounts of required information with their regulators.
- Enhance uniformity among the states in required form filings under the Act.
- Enhance uniformity in accounting standards.
- Include a mechanism permitting equivalence among regulatory bodies in light of Solvency II.

ACLI continues to carefully review new recommended revisions to the Holding Company Act. We look forward to working with the Working Group to respond to specific recommendations and devise a comprehensive approach to addressing concerns with the Act taking into account all state, NAIC, federal and international initiatives that will impact this review. Do not hesitate to contact me with any questions.

Sincerely,



Robert H. Neill, Jr.

cc: Ms. Ann M. Frohman
Director
Nebraska Department of Insurance

Mr. Danny Saenz
Sr. Associate Commissioner
Texas Department of Insurance

**ACLI Analysis of Recommendations to Modify
 the NAIC Insurance Holding Company System Regulatory Act**

	Topic	Interested Party Recommendations	By	Comments*
1 [†]	Access to Information	Enforceable access upstream and downstream on any information desired regarding the holding company, regardless of entity.	NE / VA	<p>See § 6.A (Examination) – “[T]he commissioner shall also have the power to order any insurer...to produce such records, books, or other information papers in the possession of the insurer or its affiliates as are reasonably necessary to ascertain the financial condition of the insurer...”</p> <p>See also § 3 (Acquisition of Control of or Merger with Domestic Insurer) – Requires filing with, and prior approval of, the insurance commissioner for any merger or other acquisition of control of a domestic insurer.</p> <p>See also § 5.A(1)(d) (Standards and Management of an Insurer Within a Holding Company System) – “The books, accounts and records of each party to all [transactions within a holding company system to which an insurer subject to registration is a party] shall be so maintained as to clearly and accurately disclose the nature and details of the transactions...”</p> <p>See also § 4.F (Registration of Insurers) – “Any person within an insurance holding company system subject to registration shall be required to provide complete and accurate information to an insurer, where the information is reasonably necessary to enable the insurer to comply with the provisions of this Act.”</p> <p>Regarding enforceability, see §§ 10 (Sanctions) and 13 (Revocation, Suspension, or Nonrenewal of Insurer’s License)</p> <p>Insurance Departments currently has the statutory authority to do this.</p>

* All section references are to the NAIC Insurance Holding Company System Regulatory Act.

† Numbers mirror numeration in the July 21 NAIC document “Comments from GSIWG Insurance Holding Company System Regulatory Act Questionnaire.”

Topic	Interested Party Recommendations	By	Comments*
5 Affiliated Agreements	Consider stronger language re cost sharing/management agreements and reasonableness of fee arrangements.	WA	<p>See § 5 (Standards and Management of an Insurer Within a Holding Company System)</p> <ul style="list-style-type: none"> • Subsection A(1) establishes standards for “[t]ransactions within a holding company system to which an insurer subject to registration is a party.” • Subsection A(2) identifies transactions that require pre-filing with the insurance commissioner and gives the commissioner authority to disapprove of any such transaction within 30 days of such filing. • This list of transactions includes, under subsection A(2)(g), “[a]ll management agreements, service contracts, guarantees and all cost-sharing arrangements.” • Under Subsection A(4), “[t]he commissioner shall, in reviewing [such] transactions..., consider whether the transactions comply with the standards set forth in Subsection A(1) and whether they may adversely affect the interests of policyholders.” <p>See also § 10.C (Sanctions) – “Whenever it appears to the commissioner that any insurer subject to this Act or any director, officer, employee or agent thereof has engaged in any transaction or entered in to a contract which is subject to Section 5 of this Act and which would not have been approved had the approval been requested, the commissioner may order the insurer to cease and desist immediately any further activity under that transaction or contract.”</p> <p>See also § 13 (Revocation, Suspension, or Nonrenewal of Insurer’s License)</p> <p>States currently have the ability to issue bulletins to clarify the Department’s position on all of these matters under the general authority of the Commissioner/Director/Superintendent.</p>

	Topic	Interested Party Recommendations	By	Comments*
8	Affiliated Transactions	Consider strengthening fair and reasonable standard for transactions between affiliates.	WI	<p>See § 5 (Standards and Management of an Insurer Within a Holding Company System)</p> <ul style="list-style-type: none"> • Subsection A(1) establishes standards for “[t]ransactions within a holding company system to which an insurer subject to registration is a party”, including, in paragraph (a), that “[t]he terms shall be fair and reasonable.” • Subsection A(2) identifies transactions that require pre-filing with the insurance commissioner and gives the commissioner authority to disapprove of any such transaction within 30 days of such filing. • This list of transactions includes, under subsection A(2)(g), “[a]ll management agreements, service contracts, guarantees and all cost-sharing arrangements.” • Under Subsection A(4), “[t]he commissioner shall, in reviewing [such] transactions..., consider whether the transactions comply with the standards set forth in Subsection A(1) and whether they may adversely affect the interests of policyholders.” <p>See also § 10.C (Sanctions) – “Whenever it appears to the commissioner that any insurer subject to this Act or any director, officer, employee or agent thereof has engaged in any transaction or entered in to a contract which is subject to Section 5 of this Act and which would not have been approved had the approval been requested, the commissioner may order the insurer to cease and desist immediately any further activity under that transaction or contract.”</p> <p>See also § 13 (Revocation, Suspension, or Nonrenewal of Insurer’s License)</p> <p>States currently have the ability to issue bulletins to clarify the Department’s position on all of these matters under the general authority of the Commissioner/Director/Superintendent.</p>

	Topic	Interested Party Recommendations	By	Comments*
9	Audit work papers of holding company	Authority to review the auditors work papers of the immediate and ultimate holding company, as deemed appropriate.	KS	See § 6.A (Examination) – “[T]he commissioner shall also have the power to order any insurer...to produce such records, books, or other information papers in the possession of the insurer or its affiliates as are reasonably necessary to ascertain the financial condition of the insurer...” Regarding enforceability, see §§ 10 (Sanctions) and 13 (Revocation, Suspension, or Nonrenewal of Insurer’s License) Insurance Departments currently have the general statutory authority to do this
10	Collateral examination authority	Expansion of the collateral examination authority to specifically include broader risk categories such as liquidity, reputation, and ratings risks in the definition of “impact on the financial condition”.	WI	See § 6.A (Examination) – “[T]he commissioner shall also have the power to order any insurer...to produce such records, books, or other information papers in the possession of the insurer or its affiliates as are reasonably necessary to ascertain the financial condition of the insurer...” Regarding enforceability, see §§ 10 (Sanctions) and 13 (Revocation, Suspension, or Nonrenewal of Insurer’s License) Insurance Departments, in conjunction with the NAIC, currently have the statutory authority to do this under the general authority of the Commissioner/Director/Superintendent. Should not be a reduced to a list of items in a statute or regulation, but should be fluid, contained in a bulletin.
11	Communication and information sharing	Consider codified requirement for regular communication/coordination between functional regulators.	NE / WI	States currently have the ability to do this, e.g. group examinations, FAWG, MA WG, etc. Most states have authority to enter into confidentiality agreements with other states that have similar statutes for this purpose.

	Topic	Interested Party Recommendations	By	Comments*
14	Definition of Control	Consider expanding definition of control to reflect SSAP No. 25 paragraph 4 to include "(c) by contract for goods or non management services where the volume of activity results in a reliance relationship (d) by common management."	WA	<p>See § Section 1 (Definitions)</p> <ul style="list-style-type: none"> Subsection C establishes the definition of "Control" which includes, "by contract other than a commercial contract for goods or nonmanagement services, or otherwise, unless the power is the result of an official position with or corporate office held by the person." <p>States currently have the ability to issue bulletins to clarify the Department's position on all of these matters under the general authority of the Commissioner/Director/Superintendent.</p>
17	Entities or Transactions with Detrimental impact to insurer	Address authority to examine & require other holding company entities besides insurer to deal with noninsurance activities potentially impacting solvency.	IL	<p>See § 6.A (Examination) – "[T]he commissioner shall also have the power to order any insurer...to produce such records, books, or other information papers in the possession of the insurer or its affiliates as are reasonably necessary to ascertain the financial condition of the insurer..."</p> <p>See also § 5.A(1)(d) (Standards and Management of an Insurer Within a Holding Company System) – "The books, accounts and records of each party to all [transactions within a holding company system to which an insurer subject to registration is a party] shall be so maintained as to clearly and accurately disclose the nature and details of the transactions..."</p> <p>See also § 4.F (Registration of Insurers) – "Any person within an insurance holding company system subject to registration shall be required to provide complete and accurate information to an insurer, where the information is reasonably necessary to enable the insurer to comply with the provisions of this Act."</p> <p>Regarding enforceability, see §§ 10 (Sanctions) and 13 (Revocation, Suspension, or Nonrenewal of Insurer's License).</p>

	Topic	Interested Party Recommendations	By	Comments*
18	Entities of Transactions with Detrimental impact to insurer	Authority to stay or require written approval of any material financial transaction of the holding company and another non-affiliated company, which appears to have a detrimental financial impact upon the insurer.	KS	See § 6.A (Examination) – “[T]he commissioner shall also have the power to order any insurer...to produce such records, books, or other information papers in the possession of the insurer or its affiliates as are reasonably necessary to ascertain the financial condition of the insurer...” States currently have the right to question any transaction reported in the HC annual filing or in any SEC, audited statement or other document in the HC filing by the parent.
19	Exemption vs. Disclaimer	Ins holding co systems - clarify disclaimer vs. exemption - control vs. affiliation, insurance policy issuance require filing, clarify whether amendments to non-reinsurance agreements require filing, determination as to whether "minor" agreements require filing.	IL	See also § 5. (Standards and Management of an Insurer Within a Holding Company System) Insurance Departments currently have statutory authority to issue bulletins to clarify the Department’s position on all of these matters under the general authority of the Commissioner/Director/Superintendent.
21	Federal Preemption of the Holding Company Act	Federal preemption of the Holding Company Act in regards to the federal government’s acquisition of control of AIG and GMAC has been addressed by states in different ways. HC Act could suggest uniform way to address this going forward.	NC	See Section 10 (Acquisition of Control – Statement Filing) – A change in control requires a filing with the Domestic Insurance regulator. Whether or not such person is the federal government or governmental entity or any other foreign government. Insurance Departments currently have the statutory authority to do this.
29	Holding Company filings	Require registered holding companies to file financial data in a standard format to provide the capability to analyze their financial profiles in a prescribed format.	WA	See § 4.B (Registration of Insurers) – “Every insurer subject to registration shall file the registration statement on a form prescribed by the NAIC...” All holding companies are required to file the following annually: 10K or 20F and annual statement of the holding company, which includes the independent auditor’s opinion, as part of the Form B filing.

	Topic	Interested Party Recommendations	By	Comments*
30	Holding Company filings	Require holding companies to also file their federal or national filings with state insurance departments.	WA	<p>See § 6.A (Examination) – “[T]he commissioner shall also have the power to order any insurer...to produce such records, books, or other information papers in the possession of the insurer or its affiliates as are reasonably necessary to ascertain the financial condition of the insurer...”</p> <p>All holding companies are required to file the following annually: 10K, 20F and annual statement of the holding company, which includes the independent auditor’s opinion, as part of the Form B filing.</p> <p>Many filings are public (e.g. SEC filings) and are currently available for review by any state insurance department.</p>
33	RBC	Consider authority to require immediate and/or ultimate holding company of the insurer to maintain an RBC of 300% of the insurer.	KS	<p>Insurance Departments currently have the statutory authority to do this.</p> <p>Would establish a two-tier RBC requirement, those with holding companies and those without.</p> <p>Each state currently has the authority to require surplus maintenance agreements of holding companies to maintain the RBC level above the Company Action Level.</p> <p>This discussion should take place in a broader context than revision to the Holding Company Act and needs to be studied by other impacted groups.</p>
34	Regulatory Authority over Holding companies	Require all holding companies to register or license with the States and the NAIC to enhance the regulatory powers of the Commissioners over those entities.	WA	<p>See § 4.A (Registration of Insurers) – “Every insurer which is authorized to do business in this state and which is a member of an insurance holding company system shall register with the commissioner...”</p> <p>NAIC currently issues, in addition to the NAIC number, Group numbers identify members of the Holding Company</p>
36	Supervisory Colleges	Consider adding a new section to the HC Act or separate statutory section to mandate or allow supervisory colleges, add parameters/criteria in terms of what size of holding company group would warrant a supervisory college, add confidentiality provisions, if necessary, and add rule/regulation authority to further refine the process.	NE	<p>Insurance Departments currently have the general statutory authority to do this, e.g. group examinations, FAWG, MAWG, etc. Most states have authority to enter into confidentiality agreements with other states that have similar statutes.</p> <p>Most HC statutes require confidentiality of all filings (Section 7).</p>

Topic	Interested Party Recommendations	By	Comments*
37 Systemic risk analysis	Strengthen current materiality thresholds with respect to analysis of systemic risk and provide an update to the list of activities for prior approval of holding company transactions and disclosure of specified events occurring within the holding company structure in addition to reporting requirements just measured against a percentage of assets.	WA	<p>See § 5 (Standards and Management of an Insurer Within a Holding Company System)</p> <ul style="list-style-type: none"> • Subsection A(1) establishes standards for “[t]ransactions within a holding company system to which an insurer subject to registration is a party.” • Subsection A(2) identifies transactions that require pre-filing with the insurance commissioner and gives the commissioner authority to disapprove of any such transaction within 30 days of such filing. • This list of transactions includes, under subsection A(2)(g), “[a]ny material transactions, specified by regulation, which the commissioner determines may adversely affect the interests of the insurer’s policyholders.” • Under Subsection A(4), “[t]he commissioner shall, in reviewing [such] transactions..., consider whether the transactions comply with the standards set forth in Subsection A(1) and whether they may adversely affect the interests of policyholders.” <p>See also § 10.C (Sanctions) – “Whenever it appears to the commissioner that any insurer subject to this Act or any director, officer, employee or agent thereof has engaged in an y transaction or entered in to a contract which is subject to Section 5 of this Act and which would not have been approved had the approval been requested, the commissioner may order the insurer to cease and desist immediately any further activity under that transaction or contract.”</p> <p>See also § 13 (Revocation, Suspension, or Nonrenewal of Insurer’s License)</p> <p>States currently have the ability to issue bulletins to clarify the Department’s position on all of these matters under the general authority of the Commissioner/Director/Superintendent.</p>
38 Systemic risk factors	Develop systemic risk factors for holding companies and affiliates on a group basis.	WA	<p>Insurance Departments, in conjunction with the NAIC, currently has the statutory authority to do this.</p> <p>If these risk factors are needed, develop and update the Financial Condition Examiners Handbook of the NAIC.</p>

Draft: 9/29/09

Principles-Based Reserving (EX) Working Group
Washington, DC
September 21, 2009

The Principles-Based Reserving (EX) Working Group of the Solvency Modernization Initiative (EX) Task Force met in Washington, DC, Sept. 21, 2009. The following Working Group members participated: Adam Hamm, Chair (ND); Susan E. Voss, Vice Chair, represented by Jim Armstrong (IA); Linda S. Hall represented by Gloria Glover (AK); Jay Bradford represented by Mel Anderson (AR); Steve Poizner represented by Perry Kupferman (CA); Thomas R. Sullivan (CT); Gennet Purcell and Philip Barlow (DC); Kevin McCarty represented by Al Willis (FL); Sandy Praeger represented by Larry Bruning (KS); Ann Frohman (NE); Roger A. Sevigny represented by John Rink (NH); James J. Wrynn represented by Lou Felice and Fred Anderson (NY); Mary Jo Hudson represented by Mary Miller and Peter Weber (OH); Teresa Miller represented by Rae Taylor (OR); Joel Ario represented by Dave DelBiondo (PA); Kent Michie represented by Jake Garn (UT); and Alfred W. Gross (VA).

1. Status Reports

Commissioner Hamm asked for a status report on the Valuation Manual and what it would take to get this first edition completed by the end of the year. Mr. Bruning said the Valuation of Securities (E) Task Force had completed the requirements of principle-based reserving for variable annuities and the requirements for life insurance was nearing completion, but the Task Force was still waiting on the American Council of Life Insurers (ACLI) to complete their proposed net premium floor in order to deal with the possible deductibility issue. He noted that they met their deadline for completing the net premium. Mr. Bruning said completing the net premium floor was the only real bottleneck to getting the work done by the end of the year. He said most states were already working on their 2010 agendas. He said that at the Task Force meeting, he indicated that he did not suggest introducing the changes to the standard valuation law in 2010 in Kansas. He noted that other states on the Task Force responded similarly. He said that at the latest, the Task Force should be able to complete the Manual by the 2010 Spring National Meeting, which allows the membership to adopt by the summer of 2010, and thus be introduced in legislatures in the fall of 2010.

2. Corporate Governance

Commissioner Hamm stated that it was his understanding that corporate governance was a very controversial topic for this Working Group at one time. He noted that a great deal of work was put in by Mr. Felice, the Corporate Governance Subgroup, and the Working Group to get this corporate governance document into its current version, as well as a great deal of compromise by all parties. Commissioner Hamm suggested that since only one minor comment letter was received on this draft (Attachment Six-A), it seemed appropriate for the Working Group to consider adoption of the corporate governance document as final. Upon a motion by Mr. Felice, and second by Mr. Armstrong, the corporate governance requirements (Attachment Six-B) were unanimously adopted.

3. Draft Memorandum to Membership

Commissioner Hamm discussed a memorandum prepared by former Working Group chair Thomas Hampton. He indicated that he wanted to expose this document for two reasons: 1) to spark discussion at the Working Group level on the use of statistical agent, and the NAIC's role in that; and 2) to ultimately relay those views up to the membership once they are determined. Commissioner Hamm noted that he didn't have any strong feelings on the NAIC being the statistical agent used for principle-based reserving, but that he understands others may have such feelings. He said he believed it did make sense for the NAIC to be the repository for the information obtained from the statistical agents, and to get that information to the regulators. He stated that he knew the Life and Health Actuarial Task Force had done a great deal of work already in this area, and may have some views.

Mr. Bruning said he was in favor of exposing the document. He said the data should be warehoused at the NAIC, and he reminded the Working Group that there would need to be a financing mechanism in order to obtain this data. Mr. Anderson said Life and Health Actuarial Task Force hoped to discuss some of these issues. He noted that a good portion of the work for a statistical agent was being able to handle a great deal of detail data and to be able to scrub that data. He indicated that he wasn't sure the NAIC had the capacity to be that agent, but having the NAIC as the repository was appropriate.

Commissioner Hamm noted that those comments were helpful, and demonstrate the need to expose the document. A motion was made by Mr. Bruning to expose the document. The motion was seconded by Mr. Rink and passed unanimously.

4. Draft Fiscal Impact Study

Commissioner Hamm indicated this document was prepared by NAIC staff at the request of the former chair. He noted that NAIC staff had indicated that there is a Life and Health Actuarial Task Force group that has begun to put together some ideas on a possible training program. He suggested that this document be referred to that group, and for that group to modify the structure of the program as they see fit for state actuaries. He noted that if the states want the NAIC to pay for this, the project needs to be approved by the Internal Administration (EX1) Subcommittee. Mr. Bruning responded the Life and Health Actuarial Task Force held a conference call to begin discussion on some of these issues. He noted that the Task Force was working with the American Academy of Actuaries to help to determine what was appropriate. He said referral to the Task Force was appropriate. A motion was made by Mr. Willis to refer the document to the Life and Health Actuarial Task Force. The motion was seconded by Commissioner Gross and passed unanimously.

5. Other Matters

Mr. Felice said now that the work on corporate governance for principle-based reserving was complete, it may be appropriate for the Executive Committee to consider redefining the next steps for addressing corporate governance. He noted that the Corporate Governance Subgroup has some remaining issues to address that are examination-related, but had always indicated that once the work for principle-based reserving was complete, it was probably appropriate to take a broader look at the issue. He asked that this point be included in the report to the Solvency Modernization Initiative (EX) Task Force so they could make a decision on the appropriate direction for this matter.

Having no further business, the Principles-Based Reserving (EX) Working Group adjourned.

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Scott Harrison
Executive Director

August 13, 2009

Thomas E. Hampton, Commissioner
D.C. Department of Insurance, Securities and Banking
810 First St., NW
Suite 701
Washington, DC 20002

Re: Principles Based Reserves Working Group Exposure Draft – Valuation Manual
Governance Requirements

Commissioner Hampton:

This letter responds to the Principles Based Reserves Working Group's request for comments on the July 14, 2009 Exposure Draft regarding Corporate Guidance for Principles Based Reserves – VM-G.

We appreciate the hard work and effort that has gone into developing the current Exposure Draft, which we believe accomplishes for the most part the objective of a limited corporate governance framework for Principles Based Reserving. Given that significant portions of the Valuation Manual still remain to be completed, however, we believe it likely that certain aspects of VM-G will need to be reviewed and updated to ensure consistency with other provisions of the Valuation Manual.

Thank you for the opportunity to provide our comments to the Exposure Draft.

Cordially,

A rectangular box containing a handwritten signature in black ink. The signature is cursive and appears to read "Scott R. Harrison".

Scott R. Harrison
Executive Director

cc: Dan Daveline, NAIC

As Adopted and Finalized Sept 21, 2009

Corporate Governance Guidance for Principle-Based Reserves – VM-G

I. INTRODUCTION AND SCOPE

1. A principle-based approach to the calculation of reserves places the responsibility for actuarial and financial assumptions with respect to the determination of sufficient reserves on individual companies, as compared with reserves determined strictly according to formulas prescribed by regulators. This responsibility requires that sufficient measures are established for oversight of the function related to principle-based reserves.
2. For the purposes of this section:
 - i. The term “group of insurance companies” means a set of insurance companies in a holding company system (for purposes of applicable insurance holding company system acts) that is designated as a group of insurance companies by the senior management of any holding company that is a holding company of all the insurance companies in such set of insurance companies;
 - ii. The terms “board” and “board of directors” mean (a) the board of an insurance company that has not been designated to be part of a group of insurance companies, or (b) the board of a single company within a group of insurance companies that is designated by the senior management of any holding company of all the insurance companies in such group of insurance companies, or a committee of such board, consisting of members of such board, duly appointed by such board and authorized by such board to perform functions substantially similar to those described in this section; and
 - iii. The term “senior management” includes the highest ranking officers of an insurance company or group of insurance companies with responsibilities for operating results, risk assessment, and financial reporting (e.g., the chief executive officer, chief financial officer, chief actuary, and chief risk officer) and such other senior officers as may be designated by the insurance company or group of insurance companies.

This section, while not expanding the existing legal duties of a company’s board of directors, senior management and appointed actuary and/or qualified actuaries, provides guidance that focuses on their roles in the context of principle-based reserves.

3. While existing governance standards encompass adequate and appropriate standards for oversight of principle-based reserves, the following describes guidance for the roles of the board of directors, senior management and the appointed actuary and/or other qualified actuaries, in light of their existing duties as applied in the context of principle-based reserves. It is not intended to create new duties but rather to emphasize and clarify how their duties apply to the principle-based reserves actuarial valuation function of an insurance company or group of insurance companies. To the extent that any law or regulation conflicts with the guidance described herein, such other law or regulation shall prevail, and the conflicting parts of this section shall not apply.

II. GUIDANCE FOR THE BOARD

4. Consistent with its oversight role, the board is responsible for establishing a process whereby the board: receives and reviews reports, including the certification of the effectiveness of internal controls with respect to the principle-based calculation, as provided in section 12.B.(2) of the Standard Valuation Law; interacts with senior management to resolve questions and collect additional information as needed; and determines what additional steps or direction, if any, are necessary to rely on the principle-based reserving and valuation functions established by senior management. Commensurate with the materiality of principle-based reserves in relationship to the overall risks borne by the insurance company, this process should result in general oversight of the principle-based reserves actuarial function that includes:
 - i. The process undertaken by senior management to correct any material weakness in the internal controls of the insurance company or group of insurance companies with respect to a principle-based reserve valuation if any material weakness in such internal controls is identified;

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Corporate Governance Guidance for Principle-Based Reserves – VM-G

- ii. The infrastructure (consisting of policies, procedures, controls and resources) in place to implement and oversee principle-based reserve processes; and
- iii. The documentation of review and action undertaken by the board, relating to the principle-based reserving function, in the minutes of all board meetings where such function is discussed.

III. GUIDANCE FOR SENIOR MANAGEMENT

- 5. Senior management is responsible for the oversight of the principle-based actuarial valuation function. Oversight includes a process for senior management to perform the following functions:
 - i. Ensuring that an adequate infrastructure (consisting of the risk tolerances, policies, procedures, controls, risk management strategies, and resources) has been established to implement the principle-based reserving function;
 - ii. Reviewing the principle-based reserve elements (consisting of the assumptions, methods, and models used to determine principle-based reserves of the insurance company or group of insurance companies) that have been put in place, and whether these principle-based reserve elements appear to be consistent with, but not necessarily identical to, those for other company risk assessment processes, while recognizing potential differences in financial reporting structures and any prescribed assumptions or methods;
 - iii. Reviewing principle-based reserving results for consistency with established risk tolerances of the insurance company or group of insurance companies in relation to the risks of the products the insurance company or group of insurance companies offers, the various strategies used to mitigate such risks, and its emerging experience, in order to understand the general level of conservatism incorporated into principle-based reserves; and
 - iv. Reviewing and addressing any significant and unusual issues and/or findings in light of the results of the principle-based reserve valuation processes and applicable sensitivity tests of the insurance company or group of insurance companies.
- 6. Senior management is responsible for adopting internal controls with respect to the principle-based reserve valuations of the insurance company or group of insurance companies that are designed to provide reasonable assurance that all material risks inherent in the liabilities and assets subject to such valuations are included, and that such valuations are made in accordance with the Valuation Manual and regulatory requirements and actuarial standards. Senior management is responsible for ensuring that an annual evaluation is made of such internal controls and for communicating the results of that evaluation to the board of directors.
- 7. Senior management's responsibilities with respect to principle-based reserve valuations include determining that:
 - i. Resources are adequate to carry out the modeling function with skill and competence;
 - ii. A process exists that ensures that models and procedures produce appropriate results relative to principle-based valuation objectives (such process to provide reasonable assurance that the principle-based modeling does not produce a bias toward underestimation of such reserves, and that principle-based reserves are reasonable and adequate under the circumstances);
 - iii. A process exists that validates data for determination of model input assumptions, other than input assumptions that are prescribed in law, regulation, or the Valuation Manual for use in determining principle-based reserves;
 - iv. A process exists that is appropriately designed to ensure that model input is appropriate given the experience of the insurance company or group of insurance companies, other than model inputs that are prescribed in law, regulation, or the Valuation Manual for use in determining principle-based reserves;
 - v. A process exists that reviews principle-based reserve valuations to find and limit material errors and material weaknesses (such process (a) to provide a credible ongoing effort to improve model performance where material errors and weaknesses exist, and (b) to include a regular cycle of model validation that includes monitoring of model performance and stability, review of model relationships and testing of model outputs against outcomes); and

As Adopted and Finalized Sept 21, 2009

Corporate Governance Guidance for Principle-Based Reserves – VM-G

- vi. A review procedure and basis for reliance on principle-based reserve valuation processes has been established that includes consideration of reporting on the adequacy of principle-based reserves, the implementation of policies, reporting and internal controls, and the work of the appointed actuary.
8. Senior management is responsible for facilitating the board's oversight duties by reporting to the board, no less frequently than annually, regarding such matters as:
- i. The infrastructure (consisting of the risk tolerances, policies, procedures, controls, risk management strategies and resources) that senior management has established to support the principle-based reserves actuarial valuation function;
 - ii. The critical risk elements of the valuation as applicable, related to the assumptions, methods, and models; and their relationship to those for other risk assessment processes, noting differences in financial reporting structures and any prescribed assumptions or methods;
 - iii. The summary results of principle-based reserve valuations, including the general level of conservatism and the materiality of principle-based reserves in relationship to the total liabilities of the insurance company or group of insurance companies;
 - iv. The level of knowledge and experience of senior management personnel responsible for monitoring, controlling and auditing principle-based reserves; and
 - v. Reports related to governance of principle-based reserves, including the certification of the effectiveness of internal controls with respect to the principle-based valuation, as provided in section 12.B.(2) of the Standard Valuation Law.

IV. GUIDANCE FOR QUALIFIED ACTUARIES, INCLUDING THE APPOINTED ACTUARY

9. One or more qualified actuary(ies) is (are) responsible for overseeing the calculation of principle-based reserves.
10. One of more qualified actuary(ies) is (are) responsible for reviewing and approving assumptions, methods, and models that are used in determining principle-based reserves, as well as for reviewing and approving internal standards for actuarial valuation processes, internal controls, and documentation used for such reserves. The qualified actuary(ies) does (do) not review or approve assumptions or methods that are prescribed in law, regulation, or the Valuation Manual for use in determining principle-based reserves but does (do) confirm that the prescribed assumptions and methods are being used as required.
11. With regard to principle-based reserves, the qualified actuary(ies) is (are) responsible for providing a summary report to the board and to senior management on the valuation processes used to determine and test principle-based reserves to assist their understanding of principle-based reserve valuation results, the general level of conservatism incorporated into the company's principle-based reserves, the materiality of principle-based reserves in relationship to the overall liabilities of the company, and significant and unusual issues and/or findings.
12. The appointed actuary is responsible for providing an opinion on the adequacy of company statutory reserves, both those developed using principle-based approaches and those developed using other approaches, as part of his/her annual Statement of Actuarial Opinion.
13. The qualified actuary(ies) is (are) responsible for cooperating with the company's internal and external auditors and regulators and is (are) responsible for working with the external auditors, regulators, and company senior management to resolve significant issues regarding the company's principle-based reserves. This includes, but is not limited to, disclosing to such external auditors and regulators any significant unresolved issues regarding the company's principle-based reserves.

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