

*2009 Winter National Meeting
San Francisco, CA*

FINANCIAL REGULATION STANDARDS AND ACCREDITATION (F) COMMITTEE

Saturday, December 5, 2009

2:00 – 2:30 p.m.

Hilton San Francisco – Continental 6 – Ballroom Level

ROLL CALL

Joseph Torti, III, Chair	Rhode Island	Ralph S. Tyler, III	Maryland
Leslie Newman, Vice Chair	Tennessee	Mary Jo Hudson	Ohio
Linda S. Hall	Alaska	Kim Holland	Oklahoma
Thomas R. Sullivan	Connecticut	Scott H. Richardson	South Carolina
Gennet Purcell	District of Columbia	Kent Michie	Utah
Kevin M. McCarty	Florida	Alfred W. Gross	Virginia
Susan E. Voss	Iowa		

AGENDA

1. Discuss Company Licensing Implementation Guidance Attachment One
2. Discuss Referral from Risk Retention Group (E) Task Force Regarding Part B and Part C Accreditation Standards Attachment Two
3. Any Other Matters Brought Before the Committee

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National Association of Insurance Commissioners

To: Financial Regulation Standards and Accreditation (F) Committee
From: Julie Glaszczak, Staff Support, Risk Retention Group (E) Task Force
Date: October 15, 2009
Re: Referral on Part B and Part C Accreditation Standards for Risk Retention Groups

On Sept. 8, 2009, the Risk Retention Group (E) Task Force adopted recommendations regarding which (and to what extent) Part B and Part C accreditation standards should apply to risk retention groups (RRGs) chartered as captive insurers. Listed below are the Part B and Part C accreditation standards, the related Review Team Guidelines and the Task Force’s consensus on how each individual guideline should apply to RRGs.

PART B: REGULATORY PRACTICES AND PROCEDURES

1. Financial Analysis

a. Sufficient Qualified Staff and Resources

Standard: The Department should have the resources to review effectively on a period basis the financial condition of all domestic insurers.

General Guidance: Identified personnel who have the time and experience necessary to perform this function should be assigned to the analysis tasks, and the tasks should be satisfactorily completed in a timely manner.

Review Team Guideline	Task Force Consensus
<i>Qualification Guidelines</i>	
1) The Department should have analysts or qualified contractual resources with appropriate experience levels to perform necessary tasks. Such experience should match the sophistication of the domestic industry. For example, if the domestic industry consists of reinsurers, the analysis staff should have significant experience dealing with the impact of reinsurance on financial results and trends.	Applicable to captive RRGs.
2) Although not required, credentials such as Accredited Financial Examiner (AFE), Certified Financial Examiner (CFE), Certified Public Accountant (CPA), Chartered Property Casualty Underwriter (CPCU), Fellow of the Life Management Institute (FLMI), Associate in Insurance Accounting and Finance (AIAF), Associate of Reinsurance (ARe), Member, American Academy of Actuaries (MAAA) may demonstrate expertise in insurance and/or financial analysis.	Applicable to captive RRGs.
3) Staff should have an accounting, insurance, financial analysis or actuarial background. If their background is insurance, it should be financial in nature. College degrees should focus on accounting, insurance, finance or actuarial science.	Applicable to captive RRGs.

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<i>Timing Guidelines</i>	
<p>1) The Department should begin its analysis review of priority multi-state domestics very shortly after the annual statements arrive. The Department should be essentially finished with the analysis of the annual statements (both by the primary analyst and the analyst's supervisor) and the actuarial opinions of priority, multi-state domestics by the end of April. It is acceptable if a reasonable number of reviews of companies carry over into May. The Department should be essentially finished with its analysis of the annual statements and actuarial opinions of the rest of its multi-state domestics by the end of June. Once again, it is acceptable for the analysis to carry over into July, so long as the companies carried over are the lowest priority companies. The date by which the Department should finish its analysis of the annual statements depends in part upon the size and complexity of the domestic industry. For example, if the Department has only 5 multi-state companies to analyze, it will likely finish its review of all companies (priority and non-priority) within a few weeks. But if the Department has 300 multi-state domestic companies to analyze and many of these are large, complex entities, it may take the Department several months to finish its review of domestics, even though it starts right away and progresses very diligently.</p>	Applicable to captive RRGs.
<p>2) Analysis of other supplemental filings (MD&A, CPA Audit, Holding Company Filings, Quarterly Financial Statements, etc.) should be completed within 60 to 90 days from receipt. Again, highest priority multi-state domestics should be analyzed well before the 60- to 90-day time frame.</p>	Applicable to captive RRGs.

b. Communication of Relevant Information to/from Financial Analysis Staff

Standard: The Department should provide relevant information and data received by the Department which may assist in the financial analysis process to the financial analysis staff and ensure that findings of the financial analysis staff are communicated to the appropriate person(s).

Review Team Guidelines	Task Force Consensus
<p>1) Procedures should be established such that information material to the financial analysis process is communicated to the analysts. Examples would include significant complaint data, legal actions taken against the company, material rate changes, results of market conduct and financial condition examinations, significant changes in the company's agents, MGAs or reinsurance intermediaries, and regulatory actions taken by other states. Some information may be effectively analyzed in a summary fashion (e.g. summary analysis of a complaint register including all domestic insurers). <u>Because of the organizational structure of some state insurance departments, other sections within the department might not receive or have significant information related to captive insurers, as all business related to the captive occurs within the Captive unit. To the extent that sections outside of the Captive unit have information relevant to the financial analysis process of a captive, such information should be communicated to the captive financial analyst. To the extent that upper management in the Captive unit has significant information relevant to the financial analysis process of a captive, such</u></p>	<p>The Task Force noted that such interdepartmental communication might not be applicable to all Departments because relevant information regarding captive insurers is held within a Department's captive area, instead of within different sections of a Department (as is the case with traditional insurers). To address this, the Task Force developed additional language to be added to the guideline.</p>

<u>information should be communicated to the captive financial analyst.</u>	
2) Analysts should comment in the analysis file with respect to significant information obtained from other units <u>or other individuals within the Captive unit, if applicable.</u>	Applicable to captive RRGs; however, because of various organizational structures of Departments related to captives, the Task Force agreed that additional language be added.
3) Evidence of communication (e.g., minutes of meetings, memos or notes to the file, printouts, etc.) when problems or concerns are identified should be included in the department's analysis files or binders. To a lesser extent, oral verification may provide such evidence.	Applicable to captive RRGs.
4) Financial solvency information, particularly adverse findings or significant unresolved issues, obtained as a result of the financial analysis procedures performed should be communicated to examiners, management and other Department staff as needed.	Applicable to captive RRGs.

c. Appropriate Supervisory Review

Standard: The Department's internal financial analysis process should provide for appropriate supervisory review and comment.

General Guidance: An analyst's conclusion and work files regarding the financial condition of any company should be reviewed by experienced personnel with supervisory review responsibility. Supervisory review may be conducted by the analyst's supervisor or a senior level analyst whose job functions include such review duties.

Review Team Guidelines	Task Force Consensus
1) At least one level of supervisory review should be performed on each company analysis.	Applicable to captive RRGs.
2) Evidence of such review should be documented via sign-off and dating by the reviewer.	Applicable to captive RRGs.
3) Supervisory review should be timely, usually within 2-3 weeks of completion of the original analysis.	Applicable to captive RRGs.
4) Supervisory review should include a review of all significant worksheets and evidence of the analysis performed. The supervisory review should also include at least some review of the source documents, the level of which should be based on the experience of the analysts. For very experienced analysts with a solid understanding of complex insurance issues including the accounting and reporting implications thereof, the supervisory review of the source documents may be more limited.	Applicable to captive RRGs.
5) The supervisory review should be an in-depth and challenging review of the analyst's findings. Some Departments may demonstrate in-depth and challenging supervisory review by maintaining supervisory review notes. Regardless of whether supervisory review notes are kept, however, the supervisory review shall be presumed to be sufficient if	Applicable to captive RRGs.

the analysis appears to be complete and no material matter remains unaddressed.	
6) The supervisory review should encompass any written responses received by the primary analyst from the company, which contain significant information.	Applicable to captive RRGs.

d. Priority-Based Analysis

Standard: The Department’s financial analysis procedures should be priority-based to ensure that potential problem companies are reviewed promptly. Such a prioritization scheme should utilize appropriate factors as guidelines to assist in the consistent determination of priority designations.

Review Team Guidelines	Task Force Consensus
1) General factors used to develop the priority system should be documented by the Department and consistently applied. The regulator should exercise reasonable judgment in the application of these factors to specific insurers.	Applicable to captive RRGs.
2) Domestic companies with the highest priority should be analyzed first. For example, if the Department rates companies from 1 to 4, with 1 being the highest priority, companies rated as 1's should generally be analyzed prior to analyzing lower priority companies. For states with few domestics, an informal prioritization system can be considered adequate.	Applicable to captive RRGs.
3) Justification for priority ranking and any change to the priority ranking should be included in the analysis file. For example, if a company has historically been a troubled company receiving high priority and shows signs of improvement in the current year with the analyst rating them as low priority, a proper discussion of why the rating is appropriate should accompany such rating.	Applicable to captive RRGs.
4) Any change to a priority ranking should be approved by the appropriate supervisor, and evidence of that approval should be apparent.	Applicable to captive RRGs.

e. Appropriate Depth of Review

Standard: The Department’s financial analysis procedures should ensure that domestic insurers receive an appropriate level or depth of review commensurate with their financial strength and position.

Review Team Guidelines	Task Force Consensus
1) Depth of the analysis will depend on the complexity and the financial strength of the insurer and the existing or potential issues and problems found during review of the financial statements. Those companies with the highest priority should receive the most in-depth review. For those companies with the lowest priority, a less detailed review can suffice. This review can be conducted cooperatively with other experts, such as actuaries, where necessary or indicated.	Applicable to captive RRGs.

<p>2) At a minimum, the following information should be analyzed, to at least some extent, by the Department for all domestic multi-state companies:</p> <ul style="list-style-type: none"> • Annual Statement • Actuarial Opinion • Management’s Discussion and Analysis • Annual Audited Financial Statements • Holding Company Filings • Quarterly Statements (key financial data) • Financial ratios such as IRIS, FAST or other similar ratios. <u>(Some ratios or financial analysis scoring tools may not be appropriate for captive RRGs, primarily because of the accounting method utilized. If it is found that some of the tools are not appropriate, the analyst should explain why.)</u> 	<p>The Task Force agreed that the analysis of most of this information is applicable to captive RRGs.</p> <p>However, some of the financial ratios currently utilized for traditional insurers might not be appropriate for captive RRGs. To address this, the Task Force agreed that language should be added to the last bullet.</p>
<p>3) Departments may wish to use checklists developed by the Department or obtained from the NAIC <i>Financial Analysis Handbook</i>, and these checklists may be tailored to the particular needs of the analyst and the insurer under review. When using the NAIC <i>Financial Analysis Handbook</i>, the Level 1 Procedures Checklist and significant areas included in the Annual Statement General Checklist should be completed. The remainder of the checklists may be used to the extent the complexity of the insurer’s operations warrants such use or to the extent that procedures in the checklists provide a practical learning tool for less experienced analysts. The use of the Department-developed checklists or those from the NAIC <i>Financial Analysis Handbook</i> for the supplemental filings (Actuarial Opinion, MD&A, CPA Audit, Form B Holding Company Filings, Quarterly Financial Statements) is encouraged, especially for those analysts who are less experienced.</p>	<p>Applicable to captive RRGs.</p>
<p>4) <u>For captive RRGs, the following procedures should also be performed and documented in the analysis file in conjunction with the review of the annual statement and/or the audited financial statement:</u></p> <ul style="list-style-type: none"> • <u>Review the business plan to ensure that it is unchanged from the prior year.</u> • <u>Ensure that all changes in the plan of operations have been approved.</u> • <u>Review the reconciliation in Note 1 and ensure that it appears accurate and can be relied upon by others.</u> • <u>Review question 13.1 (largest net amount insured) and ensure that the amount agrees with the approved plan of operations.</u> • <u>Ensure that the financial projections on file accurately reflect the operations as presently conducted</u> • <u>Ensure that the “Notes” relating to the operation of the company agree with the approved plan of operation.</u> 	<p>This is a new guideline developed by the Task Force that would be applicable to captive RRGs only.</p>

f. Documented Analysis Procedures

Standard: The Department should have documented financial analysis procedures and/or guidelines to provide for consistency and continuity in the process and to ensure that appropriate analysis procedures are being performed on each domestic insurer.

General Guidance: The Department should develop an analysis manual or otherwise document its analysis process to provide a reference guide and training tool for the analysts. The use of the NAIC *Financial Analysis Handbook* or sections thereof is considered acceptable.

Review Team Guidelines	Task Force Consensus
1) All analysis work performed should include initials of the preparer and the dates of completion.	Applicable to captive RRGs.
2) Worksheets designed to document the analysis process should be properly completed as set forth by the Department's procedures.	Applicable to captive RRGs.
3) Procedures and worksheets should be of sufficient detail to uncover potential concerns addressing all material areas of the financial filing being analyzed. For example, financial analysis procedures, which ignore reinsurance transactions, would not be considered sufficient.	Applicable to captive RRGs.
4) Any unusual item, fluctuation from established norms, or other issue raised during the analysis of a company, should be properly addressed and documented in the analysis file. For example, if the Department establishes a premiums to surplus ratio of 3 to 1 and the company being analyzed is writing 6 to 1, the issue should be addressed in the analysis file, as to why it is acceptable, or if not, what action the Department will require the company to take to remedy it. Also, if an analyst indicates that a fluctuation or ratio result is unusual, there should be evidence of follow-up and a conclusion as to whether the analyst considers the unusual fluctuation or ratio result to be a concern and why. <u>Some ratios or fluctuations from established norms may not be appropriate for captive RRGs, primarily because of the accounting method utilized. If this is the case, the analyst should explain why the ratio or fluctuation is not applicable.</u>	This is applicable to captive RRGs; however, some of the financial ratios currently utilized for traditional insurers may not be appropriate for captive RRGs. To address this, the Task Force agreed that language should be added to the end of the guideline, as noted.
5) Any follow-up (e.g., memo to the file, letter to the company, etc.) should be properly documented. Any letter received from a company should show proper analysis by the Department, signing off and concluding that the response is adequate. For example, if the Department discovers that a company is not filing its securities with the SVO and sends a letter to the company requesting that such filings be made, a copy of the Department's letter and a copy of the company's response, including evidence that the analyst has determined that the company's final response is adequate, should be in the analysis file.	Applicable to captive RRGs.
6) The financial analysis process should include a summary discussion of the analysis findings, including a general discussion of the company's strengths and weaknesses.	Applicable to captive RRGs.

7) Conclusions should be reached as to whether any action should be considered as a result of the analysis. For example, the worksheets could have a write-in section at the end, which would enable the analyst and supervisor to comment and make recommendations for action, monitoring and plans for follow-up.	Applicable to captive RRGs.
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g. Reporting of Material Adverse Findings

Standard: The Department’s procedures should require that all material adverse findings be promptly presented to the commissioner or an appropriate designee for determination and implementation of appropriate regulatory action.

General Guidance: A material adverse finding is defined as a finding made by a Department with respect to an event, trend, transaction or series of transactions, fluctuation, agreement, arrangement, operating results or violation of law, which either has, or reasonably could have, a significant negative impact on a company’s financial position.

Review Team Guidelines	Task Force Consensus
1) The Department should have a policy or procedure to require that all material adverse findings be promptly presented to the commissioner or an appropriate designee. This policy or procedure should be in written form and should be formally communicated to individuals capable of taking appropriate regulatory action via inclusion in the Department Handbook or through some other formal communication channel such as department bulletin, memo, etc. The policy or procedure should define a material adverse finding and to whom the finding should be communicated, as described in Guideline (3), and require findings to be promptly reported.	Applicable to captive RRGs
2) Financial analysis files should contain evidence that material findings were promptly presented to the commissioner or appropriate designee.	Applicable to captive RRGs
3) Material adverse findings should be reported to individuals who are capable of taking appropriate regulatory action. For example, if as a result of the material adverse finding the company need only be contacted to get further information on the finding, then reporting to the analyst’s immediate supervisor would be considered adequate. However, if as a result of the material adverse finding the company needs to be placed in liquidation, contact at the highest levels of the Department is expected.	Applicable to captive RRGs.

h. Action on Material Adverse Findings

Standard: Upon reporting of any material adverse findings from the financial analysis staff, the Department should take timely action in response to such findings or adequately demonstrate the determination that no action was required.

General Guidance: Material adverse finding is defined in the guidelines in g. above. The review team will accept the ultimate action of the regulator as appropriate as long as the logic of the decision is clearly documented and the decision is reasonable based upon what other regulators would commonly understand to be appropriate in that scenario and given the information available at that time.

Review Team Guidelines	Task Force Consensus
1) The Department should have a policy or procedure to take timely action in response to material adverse findings or adequately demonstrate and document that no action was required.	Applicable to captive RRGs.
2) Department files should contain evidence that timely action was taken on material adverse findings or adequately demonstrate and document that no action was required.	Applicable to captive RRGs.

2. Financial Examinations

a. Sufficient Qualified Staff and Resources

Standard: The Department should have the resources to effectively examine all domestic insurers on a periodic basis, which is commensurate with the financial strength and position of each insurer.

General Guidance: Identified personnel who have the time and experience necessary to perform this function should be assigned to the examination tasks, and the tasks should be satisfactorily completed in a timely manner.

Review Team Guidelines	Task Force Consensus
<i>Timing Guidelines</i>	
1) Conduct a full-scope examination on each domestic company in accordance with the respective state law regarding the frequency of examinations or at least once every five years, whichever is less. Companies that redomesticate should be examined by the new domestic within five years of their last examination. Rare exceptions to the requirement to examine such redomesticated companies are permitted if adequately documented and communicated to all states in which the company is licensed <u>or registered</u> , but in no case shall the examination of a redomesticated company exceed six years. Domestic companies under court-ordered supervision, rehabilitation and receivership are excluded from this examination requirement. Companies classified as under administrative supervision, supervision, dormant, in run-off, or other similar designations are not excluded. Efforts to coordinate examinations with other states are not considered an acceptable allowance for non-compliance with this examination frequency requirement. The Department should be current with its statutory examination timetable.	Applicable to captive RRGs. Note: The Task Force recommends that the phrase “or registered” be included, as noted to the left.

2) The Department should have sufficient staff to perform necessary target and limited scope exams.	Applicable to captive RRGs.
<i>Qualifications Guidelines</i>	
1) The Department should have examiners or qualified contractual resources with appropriate experience levels to perform necessary tasks. Such experience should match the sophistication of the domestic industry. For example, if the domestic industry consists of reinsurers, the examination staff should have significant experience dealing with the impact of reinsurance on financial results.	Applicable to captive RRGs.
2) Although not required, credentials such as Accredited Financial Examiner (AFE), Certified Financial Examiner (CFE), Certified Public Accountant (CPA), Chartered Property Casualty Underwriter (CPCU), Fellow of the Life Management Institute (FLMI), Associate in Insurance Accounting and Finance (AIAF), Associate of Reinsurance (ARe), Member, American Academy of Actuaries (MAAA) may demonstrate expertise in insurance and/or financial examinations.	Applicable to captive RRGs.
3) Staff should have an accounting, insurance, financial analysis, financial examination or actuarial background. If their background is insurance, it should be financial in nature. College degrees should focus on accounting, insurance, finance or actuarial science.	Applicable to captive RRGs.

b. Communication of Relevant Information to/from Examination Staff

Standard: The Department should provide relevant information and data received by the Department, which may assist in the examination process to the examination staff and ensure that findings of the examination staff are communicated to the appropriate person(s).

Review Team Guidelines	Task Force Consensus
1) Procedures should be established such that information material to the financial examination process is communicated to the examiner-in-charge (EIC). Examples would include results of the financial analysis process, significant complaints data, legal actions taken against the company, material rate and form changes, results of market conduct examinations, significant changes in the company’s agents, MGAs or reinsurance intermediaries, and regulatory actions taken by other states. <u>Because of the organizational structure of some state insurance departments, other sections within the Department may not receive or have significant information related to captive insurers as all business related to the captive occurs within the Captive unit. To the extent that sections outside of the Captive unit have information relevant to the financial analysis process of a captive, such information should be communicated to the captive financial examiner. To the extent that upper management in the Captive unit has significant information relevant to the financial examination of a captive, such information should be communicated to the captive financial examiner.</u>	The Task Force noted that such interdepartmental communication might not be applicable to all departments, because relevant information regarding captive insurers is held within a Department’s captive area, instead of within different sections of a Department (as is the case with traditional insurers). To address this, the Task Force developed additional language to be added to the guideline.

2) The EIC, or other appropriate examination staff member, should comment in the examination file with respect to significant information obtained from other units <u>or other individuals within the Captive unit, if applicable.</u>	Applicable to captive RRGs; however, because of various organizational structures of state insurance departments related to captives, the Task Force recommends adding additional language, as noted.
3) Evidence of communication (e.g. biweekly reports, memos or notes to the examination files, examination reports, etc.) when problems or concerns are identified, as part of the examination process should be included in the examination files. To a lesser extent, oral verification may provide such evidence.	Applicable to captive RRGs.
4) Financial solvency information, particularly adverse findings, obtained as a result of the financial examination procedures performed should be communicated to the EIC, chief examiner, Department management and other Department staff as needed.	Applicable to captive RRGs.

c. Use of Specialists

Standard: The Department’s examination staff should include specialists with appropriate training and/or experience or otherwise have available qualified specialists, which will permit the Department to effectively examine any insurer. These specialists should be utilized where appropriate given the complexity of the examination or identified financial concerns.

General Guidance: The Department should have on staff or be able to contract the requisite expertise to examine effectively any insurer. The requisite expertise should be determined by the character and nature of the domestic industry and may include, but is not limited to, computer audit, reinsurance, actuarial and investment expertise. The Department should demonstrate that its use of specialists is appropriate.

Review Team Guidelines	Task Force Consensus
<i>Computer Audit Expertise Guidelines</i>	
1) The Department should have access to a person with expertise to conduct computer audits.	Applicable to captive RRGs.
2) The Department should be utilizing software, such as ACL, which enables the Department to test and understand company data. For those companies where use of such software is not feasible, the Department should document proper testing “around the computer.”	Applicable to captive RRGs.
3) To determine if reliance upon an insurer’s Information Systems (IS) control system is appropriate, the Department may utilize such things as the IS Control Questionnaire from the NAIC <i>Financial Condition Examiners Handbook</i> , CPA Workpapers, etc.	Applicable to captive RRGs.
4) Determination to rely or not to rely upon an insurer’s IS controls should be made by an appropriate department representative consistent with the Department’s procedures.	Applicable to captive RRGs.
<i>Reinsurance Expertise Guidelines</i>	

<p>1) Reinsurance contracts should be reviewed to address requirements contained in state law and to determine proper accounting treatment as set forth in the NAIC <i>Accounting Practices and Procedures Manual</i>, utilizing the version effective January 1, 2001 and all subsequent revisions adopted by FRSAC and the NAIC <i>Financial Condition Examiners Handbook</i>, including, but not limited to, transfer of risk. <u>For those captive RRGs filing under GAAP, the reinsurance contracts should be reviewed to determine proper accounting treatment under GAAP.</u></p>	<p>This is applicable to captive RRGs filing under statutory accounting principles. For those captive RRGs filing under GAAP, the reinsurance contracts should be reviewed to determine proper accounting treatment under GAAP. The Task Force added a sentence to the guideline to indicate this.</p>
<p>2) Complex and sophisticated reinsurance contracts may require review by persons with greater reinsurance experience or expertise. This experience or expertise may be provided by persons on staff, under contract, or as otherwise available to the Department, e.g., through consultation with the NAIC reinsurance specialist.</p>	<p>Applicable to captive RRGs.</p>
<p><i>Actuarial Expertise Guidance</i></p>	
<p>1) Persons with appropriate experience to evaluate reserves should be involved on all examinations.</p>	<p>Applicable to captive RRGs.</p>
<p>2) Credentialed actuaries should be involved on all life and health company examinations where the company has a substantial amount of interest-sensitive business and on all property/casualty company examinations where the company has a substantial amount of long-tail lines of business. The Department may demonstrate that non-credentialed actuaries have appropriate actuarial expertise to perform an evaluation of these types of reserves.</p> <p>For purposes of the above guideline, it should be noted that long-tail property/casualty lines of business have no definitive classification system. Certain lines are generally considered to be long-tail in nature, e.g., workers' compensation, medical malpractice, commercial general liability, and some other types of liability coverage; however, due to the historic development pattern in any particular case, a line often considered to be long-tail may in such case be medium- or short-tail, or vice-versa. As one example, losses for a long-tail line of business would not generally reach 95% of the ultimate loss development until after five years from incurral date. Other relevant factors may be considered in the determination of long-tail lines of business.</p>	<p>Applicable to captive RRGs.</p>
<p>3) Coordination between examiners and actuaries should be evidenced in the examination files, especially in the planning file. For example, this would include identifying underlying data testing to be performed by the examiner and the methodologies to be used for determining reserve adequacy by the actuary.</p>	<p>Applicable to captive RRGs.</p>
<p>4) Appropriate documentation should support actuarial findings.</p>	<p>Applicable to captive RRGs.</p>
<p>5) The actuarial workpapers should be kept in the Department's files or otherwise be made available for review.</p>	<p>Applicable to captive RRGs.</p>

<i>Investment Expertise Guidelines</i>	
<p>1) Investment policies and investment holdings should be reviewed to address requirements contained in state law and to determine proper accounting treatment as set forth in the NAIC <i>Accounting Practices and Procedures Manual</i>, utilizing the version effective January 1, 2001 and all subsequent revisions adopted by FRSAC. <u>For those captive RRGs filing under GAAP or in accordance with state prescribed methods, the investment holdings should be reviewed to determine proper accounting treatment under the method utilized.</u></p>	<p>This is applicable to captive RRGs filing under statutory accounting principles. For those captive RRGs filing under GAAP or some other method, the investment holdings should be reviewed to determine proper accounting treatment under the method utilized. The Task Force added a sentence to the guideline to indicate this.</p>
<p>2) Complex and sophisticated investment policies and holdings that are material may require review by persons with appropriate investment experience or expertise. This experience or expertise may be provided by persons on staff, under contract or as otherwise available to the Department.</p> <p>For purposes of the above guideline, some examples of when an investment specialist may be necessary include: the insurer has a sophisticated derivatives program, material holdings of collateralized mortgage obligations with high flux scores, unusual real estate or limited partnership holdings, high or unusual portfolio turnover, material asset movements between related parties or unusual securities lending activities.</p> <p>If the Department does not have on staff persons with appropriate investment expertise, this investment expertise may be provided by persons associated with actuarial firms, commercial rating agencies, CPA firms, federal and state securities agencies, investment banking firms, investment brokerage firms, portfolio managers, the SVO, or other professionals experienced in analyzing investment activities.</p>	<p>Applicable to captive RRGs.</p>

d. Appropriate Supervisory Review

Standard: The Department's procedures for examinations should provide for supervisory review of examination workpapers and reports to ensure that the examination procedures and findings are appropriate and complete and that the examination was conducted in an efficient and timely manner.

Review Team Guidelines	Task Force Consensus
<i>Guidelines for Supervisory Review of Workpapers</i>	
<p>1) All workpapers, including work performed by the EIC, should receive at least one level of supervisory review. In addition, work of specialists should be reviewed by the EIC for familiarity and understanding. The reviewer should be looking to see that the specialists' reports and, if necessary, workpapers evidence all procedures that are expected to be performed. In addition, the workpapers should be consistent with the examiner's conclusions and the examination report.</p>	<p>Applicable to captive RRGs.</p>

2) Supervisory review should be evidenced by sign off and dating by the reviewer. Supervisory sign-off and dates on every single workpaper is not required.	Applicable to captive RRGs.
3) Supervisory review should be timely in nature. <ul style="list-style-type: none"> • Planning should be reviewed before significant fieldwork begins. • Supervisory review of workpapers should occur within a reasonable period after completion of the item being examined (generally 2–4 weeks). 	Applicable to captive RRGs.
4) Supervisory review should ascertain whether the form of examination workpapers is consistent with Department standards.	Applicable to captive RRGs.
5) Supervisory review should be an in-depth and challenging review of the examiner’s findings. The occurrence and sufficiency of supervisory review may be verified through discussions with department staff, including but not limited to, the EICs. The Department may demonstrate in-depth and challenging review by maintaining supervisory review notes. Regardless of whether supervisory review notes are kept, however, the supervisory review shall be presumed sufficient if the examination procedures appear to be complete and no material matter remains unaddressed.	Applicable to captive RRGs.
<i>Guidelines for Supervisory Review of Examination Reports</i>	
1) The examination report should be reviewed by at least one person other than the preparer. The commissioner or the commissioner’s designee should approve the report prior to final issuance.	Applicable to captive RRGs.

e. Use of Appropriate Guidelines and Procedures

Standard: The Department’s policies and procedures for the conduct of examinations should generally follow those set forth in the NAIC *Financial Condition Examiners Handbook*. Appropriate variations in methods and scope should be commensurate with the financial strength and position of the insurer.

General Guidance: The Department should demonstrate that examinations have been generally conducted in accordance with the NAIC *Financial Condition Examiners Handbook*. Examination procedures should produce reports of examination, which provide information needed by regulatory personnel involved in the admission and regulation of companies as well as specific information needed for any disciplinary or other regulatory action.

Review Team Guidelines	Task Force Consensus
1) The Specific Risk Analysis (SRA) approach should be utilized in establishing priority of accounts or operational areas. Such approach should include completion of the SRA workpapers and internal control questionnaires. On those examinations where the SRA approach is not utilized, planning documentation should include rationale for not utilizing such approach and evidence that the cycles identified in the SRA approach have otherwise been considered and properly addressed in the exam work.	Applicable to captive RRGs.
2) A memorandum should be prepared that summarizes the examination	Applicable to captive RRGs. Note

<p>planning process. The memorandum should adequately discuss, but is not limited to, the following:</p> <ul style="list-style-type: none"> • Results of SRA or alternative analysis • Reliance on work completed by accredited states <u>(if applicable)</u> • Review of independent auditor’s workpapers and reports • Staffing and Time Budgets • Management assessment • Analytical review results • Materiality assessment 	<p>that the Task Force added “if applicable” to the second bullet for clarification purposes. The “if applicable” would apply to both RRGs and traditional insurers.</p>
<p>3) Examination work programs should be utilized to document work performed. Such work programs should encompass steps identified in the NAIC <i>Financial Condition Examiners Handbook</i>. All work performed should be properly referenced from the work program to the workpaper(s) where the examination and analysis were performed. Such workpapers should fully document work performed and should include the initials and date of the preparer. Where work of the independent auditor is used or relied upon to supplement the work of the examiners, such reliance should be documented and limited re-testing of the CPAs work should be performed where appropriate.</p>	<p>Applicable to captive RRGs.</p>
<p>4) States electing to rely on examination work completed by another state should review the planning memorandum of the testing state related to the area of planned reliance, review the related examination program prepared by the testing state, and communicate any concerns with the testing state about the examination approach. Additionally, the relying state should review the testing state’s conclusions after the examination work and a detailed review has been completed by the testing state. The relying state may also review additional working papers at the sole discretion of the relying state. For example, the relying state may choose to review working papers related to significant findings and material adjustments. A memorandum shall be included within the workpapers of the relying state describing the communication between the testing state and the relying state, information on the relying state’s actual review of the workpapers and how this review and reliance will impact the relying state’s examination. The relying state should also have a copy of the pertinent workpapers completed by the testing state within their examination file.</p> <p>a. If relying on the work of a state that was accredited at the time of the review/reliance, the accreditation review team will not review the examination workpapers completed by the accredited testing state, but will review the memorandum documenting the review and reliance to determine compliance with this accreditation guideline. If a significant portion of the examination work was completed through reliance on another state’s workpapers, the accreditation review team may choose to select another examination to supplement the overall accreditation score on examinations.</p> <p>b. If relying on the work of a state that was not accredited at the time of review/reliance, the relying state must assume ownership of the</p>	<p>Typically, RRGs are not part of coordinated examinations and non-domestic states will not have a role in examinations of RRGs. However, if work of another state is used during the examination, this guideline would be applicable. The federal Liability Risk Retention Act of 1986 (LRRRA) does allow for the coordination of examinations to avoid unjustified duplication and repetition.</p>

<p>work completed by the non-accredited testing state. This requires the relying state to conduct a review of the examination work performed by the non-accredited testing state. The relying state should use professional judgment in determining the extent of the review to be performed. However, since the relying state assumes ownership of the work, the accreditation review team will review the examination workpapers completed by the non-accredited testing state as if they had been completed by the relying state. If the relying state does not have the workpapers from the non-accredited testing state, this will result in an interpretation that the examination procedures were not completed. The accreditation review team is encouraged not to select other examination files to review if the documentation within a file in which reliance on a non-accredited testing state was lacking.</p>	
<p>5) Data supplied by the company or an outside source (such as the insurer's independent auditor) on which material reliance is placed, should be tested for both accuracy and completeness. As stated in the NAIC <i>Financial Condition Examiners Handbook</i>, such tests may be substantive and/or compliance in nature.</p>	<p>Applicable to captive RRGs.</p>
<p>6) Sampling techniques used should conform to guidance set forth in the NAIC <i>Financial Condition Examiners Handbook</i> or other appropriate authoritative guidance. These techniques should conform to the Department's policy, be clearly documented, and be consistently applied on all examinations.</p>	<p>Applicable to captive RRGs.</p>
<p>7) The Department should utilize qualified examiners-in-charge (EICs). The NAIC <i>Financial Condition Examiners Handbook</i> provides guidance on the authority, responsibilities and credentials for a qualified EIC.</p>	<p>Applicable to captive RRGs.</p>
<p>8) If a Department elects to utilize contract examiners the Department should demonstrate significant involvement of appropriate Department personnel during the course of the examination to assure that the examination is generally conducted in accordance with the NAIC <i>Financial Condition Examiners Handbook</i> and the Department's policies and procedures.</p>	<p>Applicable to captive RRGs.</p>

f. Scheduling of Examinations

In scheduling financial examinations, the Department should follow procedures such as those set forth in the NAIC *Financial Condition Examiners Handbook* that provide for the periodic examination of all domestic companies on a timely basis. This system should accord priority to companies, which exhibit adverse financial trends or otherwise demonstrate a need for examination.

Review Team Guidelines	Task Force Consensus
1) The Department should prepare a flexible yearly examination schedule identifying the company being examined, priority of the company, projected period of the examination and the EIC scheduled to perform the exam.	Applicable to captive RRGs.
2) The criteria used to establish the examination schedule should encompass the criteria found in the NAIC <i>Financial Condition Examiners Handbook</i> . Any additional criteria used should be properly documented in the Department’s policies and procedures and should be consistently applied.	Applicable to captive RRGs.
3) The Department should be utilizing the NAIC Examination Tracking System for calling association -examinations, <u>as directed by the NAIC <i>Financial Condition Examiners Handbook</i></u> .	<p>The use of the NAIC Examination Tracking System (ETS) for calling examinations is applicable to captive RRGs if the language to the left is utilized. The following supplemental information should be noted:</p> <p>Examinations of captive RRGs are not considered “association examinations,” as the LRRRA does not specifically require other states’ participation. However, the LRRRA does allow for coordination of examinations in specific situations, although it does not require that the domestic regulator coordinate an examination if it has already begun or initiated an examination. This guideline merely requires that captive RRG examinations be called on ETS. It does not require the domestic regulator to allow other states to participate on the examination. A referral was sent to the Financial Examiners Handbook (E) Technical Group recommending that the Handbook and the ETS e-mail be updated to indicate that the calling of RRG examinations is simply a notification — and not an invitation to participate.</p>

g. Examination Reports

Standard: The Department’s reports of examination should be prepared in accordance with the format adopted by the NAIC and should be sent to other states in which the insurer transacts business in a timely fashion.

Review Team Guidelines	Task Force Consensus
<p>1) The Department should demonstrate that reports of examination have been prepared in accordance with a format outlined in the NAIC <i>Financial Condition Examiners Handbook</i>.</p>	<p>Applicable to captive RRGs.</p>
<p>2) Reports should be prepared and distributed in a timely manner as set forth in statute. Exceptions to these timing requirements should be properly documented. As a general rule, examination reports should be issued no more than 18 months after the “as of date”; however, exceptions to the general rule are possible as noted in the guidance included in the Accreditation Interlineations. Exceptions are permissible provided contemporaneous documentation highlights mitigating circumstances, which balance timeliness issues or provides reasonable justification for delays due to unforeseen circumstances. The documentation should indicate the nature of the exception, such as staffing constraints, lack of cooperation on the part of the insurer, complexity and size of the insurer, awaiting completion of actuarial support, and due process issues. Documentation should identify both the cause of the exception and the regulatory response; for example, the steps taken by the Department to keep other States informed concerning the financial condition of the insurer. Ultimately, all timeliness exceptions should be considered in the aggregate to determine whether the Department is administering its Examination Authority to ensure examination reports are useful in describing the insurer’s financial condition.</p>	<p>Applicable to captive RRGs.</p>
<p>3) Examination reports may be mailed in hard copy form to the other states, may be sent in an electronic format, or may be posted to the Internet. If the Department has the company mail out the reports to other states in which it does business, the Department should have an established procedure to obtain evidence from the company that such reports were mailed. If the report is posted to the Internet, the state must proactively communicate the availability of the report to the other state insurance departments. If a state requests a hardcopy of the examination report, such must be sent to the state in a timely manner. <u>Some state laws or regulations may require that examination reports are confidential documents, but this does not preempt the examining state from sharing examination reports with other states. The examining state may request confirmation from other states that they have the ability to maintain the confidentiality of the report.</u></p>	<p>Applicable to captive RRGs. Note: the Task Force added language regarding confidentiality of examination reports.</p>

h. Reporting of Material Adverse Findings

Standard: The Department’s procedures should require that all material adverse findings be promptly presented to the commissioner or an appropriate designee for determination and implementation of appropriate regulatory action.

General Guidance: A material adverse finding is defined as a finding made by a Department with respect to an event, trend, transaction or series of transactions, fluctuation, agreement, arrangement, operating results or violation of law, which either has, or reasonably could have, a significant negative impact on a company’s financial position.

Review Team Guidelines	Task Force Consensus
1) The Department should have a policy or procedure to require that all material adverse findings be promptly presented to the commissioner or an appropriate designee. This policy or procedure should be in written form and should be formally communicated to individuals capable of taking appropriate regulatory action via inclusion in the Department Handbook or through some other formal communication channel such as department bulletin, memo, etc. The policy or procedure should define a material adverse finding and to whom the finding should be communicated, as described in Guideline (3), and require findings to be promptly reported.	Applicable to captive RRGs.
2) Examination workpapers should contain evidence that material findings were promptly presented to the commissioner or appropriate designee.	Applicable to captive RRGs.
3) Material adverse findings should be reported to individuals who are capable of taking appropriate regulatory action. For example, if as a result of the material adverse finding the company need only be contacted to get further information on the finding, then reporting to the examiner’s immediate supervisor would be considered adequate. However, if as a result of the material adverse finding the company needs to be placed in liquidation, contact at the highest levels of the Department is expected.	Applicable to captive RRGs.

i. Action on Material Adverse Findings

Standard: Upon the reporting of any material adverse findings from the examination staff, the Department should take timely action in response to such findings or adequately demonstrate the determination that no action was required.

General Guidance: Material adverse finding is defined in the guidelines in h. above. The review team will accept the ultimate action of the regulator as appropriate as long as the logic of the decision is clearly documented and the decision is reasonable based upon what other regulators would commonly understand to be appropriate in that scenario and given the information available at that time.

Review Team Guidelines	Task Force Consensus
1) The Department should have a policy or procedure to take timely action in response to material adverse findings or adequately demonstrate and document that no action was required.	Applicable to captive RRGs.
2) Department files, examination workpapers and examination reports should contain evidence that timely action was taken on material adverse findings or adequately demonstrate and document that no action was required.	Applicable to captive RRGs.

3. Information Sharing and Procedures for Troubled Companies

a. Information Sharing

Standard: States should allow for the sharing of otherwise confidential documents, materials, information, administrative or judicial orders, or other actions with the regulatory officials of any state, federal agency or foreign countries providing that the recipients are required, under their law, to maintain its confidentiality. States also should allow for the sharing of otherwise confidential documents, materials, information, administrative or judicial orders, or other actions with the NAIC providing that the NAIC demonstrates by written statement the intent to maintain its confidentiality. The Department should have a documented policy to cooperate and share information with respect to domestic companies with regulatory officials of any state, federal agency or foreign countries and the NAIC directly and also indirectly through committees established by the NAIC which may be reviewing and coordinating regulatory oversight and activities. This policy should also include cooperation and sharing information with respect to domestic companies subject to delinquency proceedings.

Review Team Guidelines	Task Force Consensus
1) The Department should demonstrate that it is authorized to share confidential documents, materials, information, administrative or judicial orders, or other actions with the regulatory officials of any state, federal agency or foreign countries and the NAIC provided that the recipients are required to maintain its confidentiality.	Applicable to captive RRGs.
2) The Department should demonstrate that it is authorized to keep confidential documents, materials, and information provided by the regulatory officials of any state, federal agency or foreign countries and the NAIC, which is considered confidential in their jurisdiction.	Applicable to captive RRGs.

3) The Department should have a documented policy to cooperate and share documents, materials, and information on domestic companies with the regulatory officials of any state, federal agency or foreign countries and the NAIC. For example, the Department’s policy could be to share critical information on a financially troubled company with the regulatory officials of any state, federal agency or foreign countries when requested as long as confidentiality is maintained.	Applicable to captive RRGs.
4) The Department should make reasonable efforts to respond to inquiries from the NAIC Analyst Team, the Financial Analysis Working Group, and any other appropriate NAIC body.	Applicable to captive RRGs.

b. Procedures for Troubled Companies

Standard: The Department should generally follow and observe procedures set forth in the NAIC *Troubled Insurance Company Handbook*. Appropriate variations in application of procedures and regulatory requirements should be commensurate with the identified financial concerns and operational problems of the insurer.

Review Team Guidelines	Task Force Consensus
1) Once the Department has identified an insurance company as troubled or potentially troubled, the Department should take steps such as those set forth in the NAIC <i>Troubled Insurance Company Handbook</i> to address the identified concerns. This shall apply from the point the Department identifies the insurance company as troubled, or potentially troubled, to the point the company has been placed into receivership.	Applicable to captive RRGs.
2) In most instances, examinations of those insurance companies that the Department has identified as troubled or potentially troubled should occur more frequently than once every five years as outlined in the NAIC Model Law on Examinations (#390). Limited scope examinations are acceptable in meeting this guideline; however; the Department is still required to complete a full-scope examination in compliance with statutory requirements.	Applicable to captive RRGs.
3) Once the Department has identified an insurance company as troubled or potentially troubled, the Department should, within a reasonable amount of time, make efforts to communicate proactively with other state insurance regulators where the insurance company has a significant amount of written, assumed or ceded insurance business and with states in which affiliates of the troubled company are domiciled or those states where the troubled company has significant market share. Department files should contain written evidence of such communication(s). To a lesser extent, oral verification may provide such evidence.	Applicable to captive RRGs.

PART C: ORGANIZATIONAL AND PERSONNEL PRACTICES

1. Professional Development

Standard	Task Force Consensus
The Department should have a policy that encourages the professional development of staff involved with financial surveillance and regulation through job-related college courses, professional programs and/or other training programs.	Applicable to captive RRGs.

2. Minimum Educational and Experience Requirements

Standard	Task Force Consensus
The Department should establish minimum educational and experience requirements for all professional employees and contractual staff positions in the financial regulation and surveillance area, which are commensurate with the duties and responsibilities of the position.	Applicable to captive RRGs.

3. Retention of Personnel

Standard	Task Force Consensus
The Department should have the ability to attract and retain qualified personnel for the positions involved with financial surveillance and regulation.	Applicable to captive RRGs.