




International Solvency & Accounting

Objectives


- Understand the current status of the U.S. SEC consideration of International Financial Reporting Standards (IFRS)
- Describe the SMI Task Force timeline pertaining to policy positions regarding IFRS and possible choices for statutory accounting and reporting
- Understand monitoring and communication efforts to the International Accounting Standards Board and the U.S. FASB on key projects, including Insurance Contracts and Financial Instruments.



Julie Gann

NAIC Senior Accounting Policy Advisor

- Supports SAPWG and EAIWG
- Provides technical & advisory services in the areas of SAP, GAAP & IFRS
- Joined NAIC in February 2001. Prior Positions Include:
 - Financial Examination Manager
 - International Insurance Accountant
 - Public accountant and insurance examiner consultant
- CPA, FLMI, ARA and AIRC; Member of AICPA & MSCPA



History of International Accounting Standards Board

- IASB Formed in 2001 – Preceded by IASC
- IASC Formed in 1973 through agreement by:

Canada	France	Germany
Italy	Japan	UK
Netherlands	Spain	USA
- IFRS Foundation - Independent, not-for-profit private sector organization working in the public interest. The IASB is the independent standard-setting body of the IFRS Foundation.


International Accounting Standards Board

The IASB is an independent group of 15 experts with broad geographical diversity. (Membership will expand to 16 in 2012)

• Hans Hoogervorst (Chair) – Netherlands	• Prabhakar Kalavacherla – India
• Ian Macintosh (Vice-chair) – New Zealand	• Eric Kling – Germany
• Stephen Cooper – United Kingdom	• Patricia McConnell – United States
• Philippe Danjou – France	• Takatsugu Ochi – Japan
• Jan Ingemar – Sweden	• Paul Pacter – United States
• Patrick Finnegan – United States	• Darrel Scott – South Africa
• Almaro Luiz de Oliveira Gomes – Brazil	• John Smith – United States
	• Zhang Wei-Guo – China

Members as of Feb 2012 and their jurisdictions are noted above


Adoption of IFRS



Since 2005, several countries have adopted use of IFRS

The European Union (EU) and Australian Accounting Standards Board required listed companies to adopt IAS January 1, 2005

In adopting IFRS in 2005 the European Commission said that it regarded the IASB as the appropriate vehicle for harmonizing accounting within the European Union



IASB and IFRS Foundation – Key Objectives –

Key Objective:

To develop a single set of high quality, understandable, enforceable and globally accepted financial reporting standards based upon clearly articulated principles.

Additional Objectives

- to promote the use and rigorous application of those standards;
- to take account of the financial reporting needs of emerging economies and small and medium-sized entities (SMEs), and
- to bring about convergence of national accounting standards and IFRS to high quality solutions

Key Points on IFRS Adoption European Union

Adoption is "IFRS as adopted by the EU". Pursuant to this adoption, firms in the EU are not required to completely comply with IAS 39: Financial Instruments (IAS 39)

The ability of the EU to modify the adopted IFRS has generated discussions of political pressure on the IASB in developing standards, as well as generated debates on whether countries in the EU can certify that they comply with IFRS.

Key Points on IFRS Adoption Japan & Saudi Arabia

As of 2012, both of these countries have significantly altered their position. Japan permits some companies to use IFRS, with mandatory consideration expected in 2012, and Saudi Arabia requires IFRS for banks and insurance companies, with full convergence being considered.

In 2006 Japan and Saudi Arabia were identified as two countries with no intention of converging with IFRS.

Status of SEC Consideration of IFRS

2002 - Convergence Efforts Begin - "Norwalk Agreement"

2003 - SEC Action to Remove Reconciliation Requirement

2005 - IASB/FASB Reaffirm Commitment to Convergence

2009 - IASB/FASB Reaffirm Convergence Commitment, completion date for each major project by **June 2011**

2008 - Progress Report on Convergence identified 2011 completion date for priorities and milestones

Key Points on IFRS Adoption United States

In 2007, the SEC adopted rules allowing foreign private issuers who prepare their financial statements in accordance with IFRS, as issued by the IASB to file financial statements with the SEC without reconciliation to US GAAP. Financial statements prepared in compliance with a jurisdictional variation of IFRS that varies from what was issued by the IASB would not be acceptable.

Decision of the IFRS and US GAAP convergence was expected in 2011, however, as of February 2012, this decision has yet to occur.

SEC provisions for IFRS seemingly disqualified EU companies, since they follow IFRS as adopted by the EU. The SEC issued temporary transition relief for the EU companies available for impacted entities for their first two financial years ending after Nov. 15, 2007.

Status of SEC Consideration of IFRS

2010 - (February) - SEC issued statement in support of convergence and global accounting standards

2010 - (October) - SEC progress report including assessment of IASB funding and governance structure

2010 - (June) - IASB/FASB modifies convergence strategy

2010 - (December) - SEC "Contingent"

2011 - (May) - SEC exposure draft outlining possible approach for incorporation of IFRS into US financial reporting system

SEC Exposure Draft - Incorporate IFRS

Key principles from the exposure:

- Convergence** - US GAAP retained, but the FASB would incorporate IFRS over a defined period of time. At the end, objective would be full compliance with US GAAP would represent compliance with IFRS as issued by the IASB.
- Fiduciary** - FASB would participate in the development of accounting standards, rather than serving as the principle body responsible for developing new accounting standards under US GAAP. FASB should be in a position to readily endorse (incorporate directly into GAAP) vast majority of the IASB's modifications to IFRS. U.S. modifications would be subject to an established protocol. Protocol could entail the FASB determining whether the IASB's modification to IFRS met a predefined threshold - for example, incorporates the consideration of the public interest and the protection of investors. If the IASB's modification reaches the threshold, the FASB would incorporate fully the IASB's adopted standards into US GAAP.

2012 IASB Timeline Priority Projects

Classification & Measurement - Exposure 2nd half of 2012

Implementation - Re-exposure 2nd half of 2012

General Hedge Accounting - IFRS 9 IASB of 2012

Macro Hedge Accounting - Exposure 2nd half of 2012

Financial Instruments

Status of SEC Consideration of IFRS

2011 - (April) - IASB/FASB progress report, extending timetable for remaining priority MacG projects and insurance accounting beyond June 2011

2011 - (November) - FASB Comment Letter noting concerns and proposing modifications to the endorsement approach

2011 - (November) - SEC staff papers analyzing IFRS in practice and comparing US GAAP and IFRS

2011 (December) - SEC staff papers analyzing IFRS in practice and comparing US GAAP and IFRS

2012 - (Despite communication intent for a decision in 2011) SEC has yet to make a decision regarding incorporating IFRS into US GAAP.

2012 IASB Timeline Priority Projects

Revenue Recognition - Exposure - Comments due March 2012

Insurance - Review draft of re-exposure 2nd half of 2012

Leases - No exposure 2nd quarter of 2012

Solvency Modernization Initiative
- Task Force

Task Force - Expected to make policy positions regarding IFRS and its inclusion / exclusion from the framework of insurance solvency regulation.

- **Roadmap Updated Spring 2011** - Task Force will request recommendation from technical regulators - i.e. the IASB/FASB insurance contracts Project is completed and a decision is made by the SEC regarding IFRS.
- **Updated Timoframe for Policy Positions** - 2012

Primary Purpose of Regulator Accounting

Objective is to ensure legal obligations of each individual regulated entity to its policyholder, contract holders and other customers when they come due

Primary Questions

1. Can regulatory rules be addressed through other means?
2. Is conservatism necessary in accounting model?
3. Is individual entity reporting necessary?
4. Should model provide means to communicate with other regulators?
5. What methods could be employed to ensure comparability?
6. Is there a need for product specific rules?

SMI Task Force
- Primary Questions

Accounting and Financial Reporting Subgroup Charge

1. What should be the purpose of the regulatory accounting model?
2. As the IASB and major jurisdictions are advocating the use of IFRS (possibly with modifications) for regulatory purposes, should the NAIC continue to maintain an entire codification of statutory accounting?
3. Should regulatory financial statements be utilized for public purposes or should a separate public financial filing be required?

Other Related Points of Consideration - Purpose of Regulatory Accounting

1. Control over regulatory accounting requirements
2. Implications for non-GAAP firms
3. Ability for states to grant variations
4. Impact of current model laws
5. Impact of taxation bases
6. Impact on various regulatory tools
7. Non-regulatory use of statutory financial statements
8. Confidential statutory financial statements
9. Comparability of U.S. and Non-U.S. multi-national insurers
10. Impact to small and medium U.S. only insurers
11. Resource needs

Should NAIC Maintain Entire Codification of Statutory Accounting?

Possible Identified Choices (On a Continuum)

1. Freeze SAP without changes
2. U.S. GAAP with statutory adjustments / step-by-step review
3. IFRS with statutory adjustments
4. IFRS for public companies; IFRS/GAAP with SAP adjustments for nonpublic companies
5. IFRS without adjustments

Summary of Comments - Summer 2010

Two Most Significant Comments

1. Do not make decision until SEC makes a decision on IFRS and also until completion of IASB Insurance Contracts Project
2. Concern with giving up regulatory control

Should Regulatory Financial Statements be Utilized for Public Purposes?

Possible scenarios (On a Continuum)

1. **Current Process** - NAIC Blank is used for both regulatory reporting and public reporting purposes
2. **Middle of the Continuum** - Require NAIC Blank for public reporting purposes, and include specific statutory basis exhibits and schedules in the confidential RBC filing
3. **Most Changes** - Establish separate public reporting financial statement and utilize an entirely different confidential financial statement for regulators only

NAIC Monitoring and Communication Efforts - IASB and FASB


1. International Solvency and Accounting Standards Working Group
2. Statutory Accounting Principles Working Group
3. International Insurance Relations (G) Committee




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Corporate Governance

International Fellows Presentation


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What is Corporate Governance?

A framework of rules and practices by which a board of directors ensures accountability, fairness and transparency in an insurer's relationship with all its stakeholders.


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Corporate Governance

- What is Corporate Governance?
- How is CG currently required of U.S. insurers outside of Insurance Regulation?
- How is CG currently reviewed by U.S. regulators in U.S. Insurance Regulation?
- What Changes are coming?


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What is Corporate Governance?

- Suitability
 - Owners
 - Financial stability
 - Directors
 - Background and Experience
 - Senior Management
 - Background and Experience


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What is Corporate Governance?


- Board of Directors
 - Duties
 - Care
 - Loyalty
 - Oversight
 - Structure
 - Independence
 - Committees



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How is CG currently required of U.S. insurers outside of Insurance Regulation?

General Corporate Law


- Generally at the State Level
 - Board structure
 - Duties
- Case Law
 - Generally at the State Level
 - Court rulings




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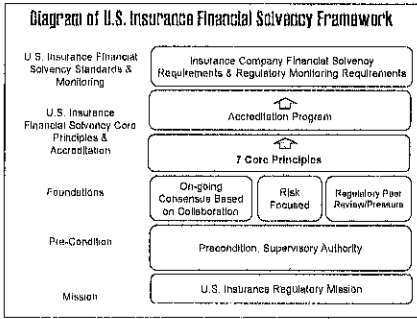
What is Corporate Governance?

- Senior Management
 - Duties
 - Financial Reporting
 - Risk Management
 - Internal Controls
 - Integrity/Code of Conduct


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How is CG currently required of U.S. insurers outside of Insurance Regulation?

- Requirements issued by the Securities and Exchange Commission (SEC) for publicly-held companies
 - Securities Exchange Act of 1934
 - Sarbanes-Oxley Act of 2002
 - Audit Committee independence
 - Attestation regarding internal control over financial reporting
- Other requirements
 - Remuneration
 - Risk Management



Principle 1:
Regulatory Reporting, Disclosure & Transparency

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A. Annual Statement Reporting
B. Annual Financial Reporting Model Regulation (NAIC Model #205)
C. Holding Company Reporting Requirements (NAIC Model #440)

U.S. Insurance Financial Solvency Core Principles

- 1 Regulatory Reporting, Disclosure & Transparency
- 2 Off-site Monitoring & Analysis
- 3 On-site Risk-focused Examinations
- 4 Reserves, Capital Adequacy and Solvency
- 5 Regulatory Control of Significant, Broad-based Risk-related Transactions
- 6 Preventive & Corrective Measures, including Enforcement
- 7 Exiting the Market & Receivership
- 8 Other Non-Solvency Related Processes

Principle 2:
Off-site Monitoring and Analysis

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Off-site solvency monitoring is used to assess:

- the financial condition of insurer's as of the valuation date
- to identify and assess current and prospective risks through risk-focused surveillance.

The results of the off-site analysis are included in an insurer profile for continual solvency monitoring

Principle 2

Principle 3:
On-site Risk-focused Examinations

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A. Background
B. Suitability
C. Corporate Governance Assessment
D. Risk Management & Internal Controls

Principle 3

Principle 5:
Regulatory Control of Significant, Broad-based Risk-related Transactions/Activities

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A. License Application Process
B. Holding Company Models (NAIC Model #440 & 450)
C. Model Investment Laws
D. Credit for Reinsurance
E. Outsourcing of Functions

Principle 4:
Reserves, Capital Adequacy and Solvency

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A. Reserves
B. Risk-Based Capital

Principle 6:
Preventive and Corrective Measures, including Enforcement

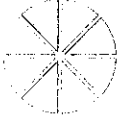
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A. NAIC Model # 385 - Hazardous Financial Condition Model
B. Other Powers of the Commissioner
C. Troubled Insurance Companies

**Principle 7:
Exiting the Market and Receivership**

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A. Receivership



**Corporate Governance (CG)
Working Group**


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- Part of a broader Solvency Modernization initiative
- Study of existing law relating to corporate governance
 - US Non- Insurance
 - US Insurance
 - IAS- ICPs

Other Non-Solvency Related Processes

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A. Market Conduct




What are current changes?

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- IAS redraft of principles relating to CG
 - ICP 5: Suitability
 - ICP 7: Corporate Governance
 - ICP 8: Risk Management & Internal Control

Questions

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Contact Information

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Reinsurance Overview

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Reinsurance

- Reinsurance allows for maximization of the principle of insurance, i.e., the spreading of risk
- In simplest terms, it is insurance for insurance companies
- Essentially, it is a contractual promise from one insurer to indemnify another insurer, which in many cases may not be presented for collection until long after the contractual obligations are created


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Objectives

- Discuss reinsurance and its importance in the context of financial solvency regulation
- Provide a basic overview of how reinsurance is regulated in the U.S.
- Review reinsurance-related statutory accounting, reporting and risk transfer requirements
- Review common issues with respect to the analysis of reinsurance programs and agreements
- Discuss recent developments and current issues in U.S. reinsurance regulation


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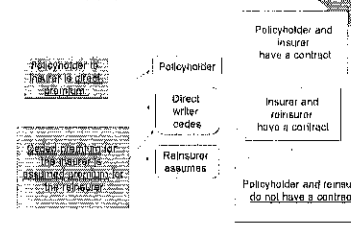
Elements of Reinsurance

- Reinsurance is a form of insurance.
- A reinsurance contract is an indemnity contract.
- There are only two parties to the reinsurance contract – the reinsurer and the reinsured – both of whom are insurers, i.e., entities empowered to insure.
- The subject matter of a reinsurance contract is the insurance liability of the reinsured undertaken by it under insurance policies issued to its own policyholders.

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Parties to the Reinsurance Contract



The diagram illustrates the following relationships:

- Reinsurer to Reinsured:** Reinsurer assumes the risk of the reinsured.
- Policyholder:** Policyholder and insurer have a contract.
- Insurer:** Insurer and reinsurer have a contract.
- Reinsured:** Policyholder and reinsurer do not have a contract.


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What Reinsurance Does Not Do

- Reinsurance is not banking
 - It is not the lending of money, though it can have the same effect
- Reinsurance is not a security.
- Reinsurance does not:
 - Convert an uninsurable risk into an insurable risk
 - Make loss either more or less likely to happen
 - Make a loss either greater or lesser in magnitude
 - Convert bad business into good business


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What Reinsurance Does

- Reinsurance redistributes the risk of loss incurred by the reinsured under its policies, according to its own business needs.
- Reinsurance redistributes the premiums received by the reinsured, which now belong to the reinsurer, according to its own business needs.

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Primary Purposes

- **Capacity** – allows ceding insurer to increase its capacity to write more insurance
- **Catastrophe protection** – protects ceding insurer from excessive losses due to catastrophic events
- **Stabilization** – provides more stable underwriting results for ceding insurer by avoiding widely fluctuating experience
- **Financing** – helps offset statutory accounting surplus strain from writing an increasing amount of new business

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Importance to Financial Solvency Regulation NAIC

- Reinsurance transactions significantly affect reported financial results, financial ratios and Risk Based Capital (RBC)
- Under statutory accounting requirements, accounting and reporting differs significantly depending on whether agreement is prospective or retroactive in nature, and whether there is an adequate transfer of insurance risk; transparency of reinsurance transactions is critical
- Ceding insurer maintains its obligation to primary policyholder regardless of whether reinsurer fulfills its obligation to indemnify the ceding insurer

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U.S. Reinsurance Regulation NAIC

- U.S. system takes a direct as well as an indirect approach to reinsurance regulation
- Direct** – U.S. domiciled assuming insurers
 - Subject to the same level of oversight, disclosure and solvency requirements as U.S. primary insurers
- Indirect** – use of reinsurance by U.S. ceding insurers
 - Credit for Reinsurance Model Law is the cornerstone of reinsurance regulation in the U.S.
 - Regulation of financial statement credit for reinsurance focuses on solvency of the ceding insurer and the impact of reinsurance on the ceding insurer's financial condition, and ultimately the financial impact on consumers of insurance products

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Importance to Financial Solvency Regulation NAIC

- Reinsurance frequently has been a key factor in troubled company situations
- Contracts can be complex, subject to misinterpretation between contracting parties
- Successful insurance company management generally requires high degree of reinsurance understanding
- Comprehensive analysis of a reinsurance program requires a thorough understanding of the rights and obligations of each party under the agreements

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U.S. Reinsurance Regulation NAIC

- Authorized Reinsurer:**
 - Licensed in the same state of domicile as the ceding company
 - Accredited by the domiciliary insurance department of the ceding company
 - Domiciled and licensed in a state with substantially similar credit for reinsurance laws as the ceding company's domicile
 - Maintains a multi-beneficiary trust in the U.S.
- If the reinsurer is not authorized, or is not otherwise approved, the reinsurance is "unauthorized"
- Historically, under the NAIC *Credit for Reinsurance Model Law*, a U.S. ceding company must hold collateral in order to take financial statement credit for reinsurance ceded to an unauthorized reinsurer
- Significant reforms adopted in 2011 will change this requirement under certain conditions

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Risk Transfer NAIC

- Insurance risk transfer is the essential ingredient of a reinsurance contract
- Insurance risk includes both:
 - Underwriting risk** – uncertainties about the ultimate amount of net cash flows from premiums, commissions, claims and claim settlement expenses
 - Timing risk** – the timing of the receipt and payment of those cash flows
- Various analytical methods are utilized to evaluate contracts for risk transfer

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Statutory Accounting & Reporting NAIC

- Reinsurance Accounting (net of reinsurance basis)**
 - Agreement is prospective in nature (i.e., covers future events)
 - Agreement transfers an adequate amount of underwriting and timing risk to the reinsurer
 - Recoverable on paid losses recorded as an asset; reserves are reduced by reinsurance ceded; impact of transaction flows through underwriting results
- Retroactive Accounting**
 - Agreement is retroactive in nature (i.e., covers past events)
 - Agreement transfers a significant amount of underwriting and timing risk to the reinsurer
 - More restrictive than prospective accounting treatment; paid losses and reserves are reported gross of reinsurance; surplus restricted

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Risk Transfer NAIC

- Statutory financial statements include several disclosures to facilitate the identification of specific characteristics in reinsurance contracts that warrant further analysis as to whether risk transfer is sufficient
- There is no "bright-line" test in statutory accounting; requires case-by-case analysis
- CEO and CFO of the reporting company must specifically attest that reinsurance contracts are accounted for appropriately in the statutory financial statements

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Statutory Accounting & Reporting NAIC

- Deposit Accounting**
 - To the extent that a reinsurance agreement does not, despite its form, transfer both components of insurance risk, all or part of the agreement is accounted for and reported as a deposit
 - Applies whether the agreement is prospective or retroactive
 - All cash flows are processed through a deposit account
 - No reduction in reserves or liabilities
 - Any gain from the transaction is not recognized until termination

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Reinsurance Reporting NAIC

- Various annual/quarterly statement underwriting exhibits provide information with respect to the impact of reinsurance transactions on premium, losses and expenses
- Reinsurance schedules ("F" for Property/Casualty, "S" for Life, Accident & Health) disclose significant details about reinsurance transactions and balances by counterparty, and restate the Balance Sheet to a gross of reinsurance basis to identify the net credit for reinsurance in the financial statements
- Specific reinsurance disclosures provide details on reinsurance program and specific types of transactions

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Reinsurance Analysis NAIC

- Proper transparency / disclosure in the financial statements
 - Do the financial statements accurately reflect the reinsurance that is in place?
 - Do any contracts exist with characteristics that dictate the need for more detailed risk transfer analysis?
 - Are the amounts reported as recoverables likely to be collected?
 - Are the contracts legitimate reinsurance agreements?
 - Particular attention to commutations and Loss Portfolio Transfers

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Reinsurance Analysis NAIC

- Adequate reinsurance cover
 - Does the company have an appropriate reinsurance program with adequate/appropriate reinsurance cover in place?
- Quality / financial strength of reinsurers
 - Does the company appropriately manage its credit risk from reinsurance through using quality reinsurance, monitoring the condition of reinsurers?
 - Does the company obtain collateral when required or when appropriate, and is the reinsurance reliable?
- Affiliated reinsurance arrangements
 - Is there any unusual shifting of risk among affiliates?
- Diversification
 - It may be prudent for the ceding company to use a sufficient number of reinsurers to further distribute financial risk

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Reinsurance Analysis NAIC

- Fronting
 - Any abuses of this practice?
 - Quality of reinsurers behind any fronting programs?
- Reinsurance Intermediaries
 - Any unusual arrangements?
- Assumed reinsurance
 - Does the company have the appropriate expertise to analyze, underwrite, monitor and service the assumed business?

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U.S. Reinsurance Collateral Debate NAIC

- Over the past decade, non-U.S. reinsurers and regulators have called for the elimination of collateral requirements for financially strong reinsurers domiciled in well-regulated jurisdictions
- U.S. regulators have acknowledged the need to modernize reinsurance regulation
- International efforts continue toward facilitating the development of an effective and efficient global reinsurance supervisory framework based on mutual recognition of reinsurance supervision

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Federal Dodd-Frank Act NAIC

- Federal legislation signed into law on July 21, 2010
- Broad U.S. financial regulatory reform
- Did not include the NAIC's proposed federal reinsurance legislation
- Does include provisions that impact reinsurance
 - Nonadmitted and Reinsurance Reform Act (NIRRA)
 - Federal Insurance Office Act

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NAIC Reinsurance Regulatory Modernization Framework NAIC


- First step in an effort to facilitate cross border reinsurance transactions and enhance competition in the U.S. market while ensuring that U.S. insurers and policyholders are adequately protected against the risk of insolvency
- Based on the principles of single-state supervision for U.S. and non-U.S. insurers' U.S. reinsurance business, recognition of reinsurance supervision, and collateral reduction based on financial strength and business practices
- Adopted by NAIC in December 2008; NAIC proposed federal legislation to implement, but not enacted

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Nonadmitted and Reinsurance Reform Act NAIC


- Became effective on July 21, 2011
- Prohibits a state from denying credit for reinsurance if the domiciliary state of the ceding insurer recognizes such credit and is an NAIC-accredited state
- Reserves to a reinsurer's domestic state the sole responsibility for regulating the reinsurer's financial solvency, so long as it is an NAIC-accredited state
- Facilitates state-based approach to implementation of NAIC reinsurance reforms

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Federal Insurance Office 


- Under U.S. Department of the Treasury
- FIO is not a regulator or supervisor, but has authority to
 - Receive information on the insurance sector
 - Enter into binding "covered agreements" with international bodies
 - Preempt a state insurance measure under certain conditions
- FIO may preempt a state insurance measure to the extent that it:
 - results in less favorable treatment of a non-U.S. insurer domiciled in a foreign jurisdiction that is subject to a covered agreement than a U.S. insurer domiciled, licensed, admitted or otherwise authorized in that state, and
 - is inconsistent with such covered agreement

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NAIC Model Revisions 


- Major step in the NAIC reinsurance regulatory modernization efforts
- Certification and rating process for reinsurers
 - Financial strength
 - Business practices
 - Effectiveness of domestic supervision
 - State may certify reinsurers or defer to the certification/rating issued by another NAIC-accredited jurisdiction
- Evaluation process for determining Qualified Jurisdictions
 - NAIC list of recommended qualified jurisdictions
 - States must consider NAIC list in determining qualified jurisdictions, and thoroughly document justification if deviating from the list

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State and NAIC Reforms 


- In light of these developments, individual states began to express an interest in reforming state laws to reduce collateral requirements for eligible reinsurers
 - Florida (2007/2008)
 - New York (2010)
 - New Jersey and Indiana (2011)
 - Other states currently considering similar proposals
- NAIC incorporated key elements of the adopted Reinsurance Framework into its *Credit for Reinsurance Model Law* and *Credit for Reinsurance Model Regulation* to facilitate uniformity in state-based reinsurance reforms

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NAIC Model Revisions 


- Certification process for reinsurers – a certified reinsurer will be eligible for collateral reduction with respect to contracts entered into or renewed subsequent to certification
- Each state has authority to certify reinsurers, or may recognize the certification granted by another NAIC-accredited state
- A state will evaluate a reinsurer that applies for certification, and will assign a rating based on the evaluation; a certified reinsurer will be required to post collateral in an amount that corresponds with its assigned rating in order for a U.S. ceding insurer to be allowed full credit for reinsurance ceded

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NAIC Model Revisions 


- A list of recommended qualified jurisdictions will be published through the NAIC committee process
- States must consider this list in determining qualified jurisdictions, and thoroughly document justification for any deviation from the list.
- Qualified jurisdiction must agree to share information and cooperate with the commissioner with respect to all certified reinsurers doing business within the jurisdiction

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Next Steps 


- Accreditation standard key elements exposed for public comment with a comment deadline of April 6th
- Interim discussion to consider revised accreditation standard for adoption as recommendation to Financial Regulation Standards and Accreditation Committee
- Reinsurance Task Force drafting groups:
 - Develop process for evaluating non-U.S. jurisdictions
 - Develop process for Reinsurance FAWG
- Monitor progress on RTF web page: http://www.naic.org/committees/rtf_reinsurance.htm

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Implementation 

- Revise accreditation standards for reinsurance codes
 - Proposed Part A standards exposed for comment
 - Recommendations for Part B standards to be developed
 - Determine whether proposed revisions should be considered on an expedited basis
- Qualified Jurisdictions
 - Develop process for review and determination
 - Determine which jurisdictions will be initially reviewed
 - Develop a timeline for implementation
- Reinsurance FAWG
 - Establish new NAIC group to provide advisory support and assistance to the states in the review of reinsurance collateral reduction applications

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Questions?

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RBC Formulas

Risk Based Capital
Robin Marcotte



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Overview of RBC

RBC is used to identify a poorly capitalized insurer given its overall business operations in consideration of its size and risk profile.

- Accounts for a company's risk exposure
- Adjusts minimum capital and surplus
- Reflects unique risks inherent in operating an insurance company

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Agenda

- Risk Based Capital (RBC) purpose
- Major components in the formulas
- Overview of Industry results
- How this is applied in the U.S.

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Overview

- RBC formula creates minimum standard for capital & surplus before regulatory action
- RBC is one of the tools used in analysis related to reviewing the capital position
- RBC gives regulators legal authority to act
- Analyst must understand the insurer, its operations, and risks
- A good RBC ratio does not indicate a company is financially stable

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Risk Based Capital Goals

RBC was intended to provide a Capital Adequacy Standard that:

- Is uniform among the states.
- Provides regulatory authority for timely action.
- A calculation of minimum capital required and not a target or ideal level of capital.
- Reflects unique risks inherent in operating an insurance company.
- Is easy to understand and calculate.
- RBC data used can be verified to or pulled in directly from the statutory annual statement.

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RBC is NOT:

- An Early Warning Device
- Designed to Prevent Insolvency
- Designed to Detect Fraud/Mismanagement
- A Stand-Alone Tool for Solvency Monitoring
- Designed to Fit Every Scenario and Capture Every Possible Risk
- Public Information (RBC Filing Itself)
- A Rating Mechanism

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RBC is just one part of the NAIC solvency framework:

- RBC
- Financial Analysis and Reporting
- Examinations
- Statutory Accounting
- Reserve Requirements
- Regulatory Control of Transactions/Activities
- Governance / Risk Assessment



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RBC

- Ratio is not a target regulatory capital.
- It is a minimum that must be maintained to avoid regulatory action
- 96-98% of US Companies are well above their minimum RBC ratios

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Reporting of NAIC RBC

2 Public Results are published in the Five Year Historical Data Page of the Statutory Financial Statement:

- Total Adjusted Capital
(a calculation of the total actual capital held)
- Authorized Control Level RBC
(a calculation of the minimum capital that should be held to avoid regulatory control)

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Total Adjusted Capital - Numerator

Capital and Surplus is taken from the Annual Statement Filing Capital and surplus is then adjusted for:

- Life
 - Asset Valuation Reserve: is counted as capital for purposes of the RBC formula although it represents a liability and is not usable against general contingencies
 - 50% of Dividend Liabilities: the annual statement provision for future dividends can provide a general cushion against potentially adverse future experience; to reflect this possible cushion, 50% of the dividend liability is included.
 - Affiliated amounts (life affiliates AVR etc., P/C affiliates non-tabular discount)

Sensitivity Test for deferred taxes does not affect the RBC calculated

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RBC Ratio

- The Company's actual capital held (Total Adjusted Capital) is compared the minimum level of capital (Authorized Control Level):

$$\frac{\text{Total Adjusted Capital}}{\text{Authorized Control Level}} = \text{RBC Ratio}$$

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Total Adjusted Capital - Numerator

Capital and Surplus is taken from the Annual Statement Filing Capital and surplus is then adjusted for:

- P/C - (PR026)
 - Non-tabular discount
 - Affiliated amounts (life affiliates AVR etc., P/C affiliates non-tabular discount)

Sensitivity Test for deferred taxes does not affect the RBC calculated

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Authorized Control Level – Denominator

- The NAIC RBC formula focuses on key risks:
 - Asset Risk
 - Underwriting Risk/ Insurance Risk
 - Business Risk (Life & Health)
 - Interest Rate Risk and Market Risk (Life)

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Levels of action that a company RBC Ratio can trigger:

	RBC Ratio
No Action- RBC Ratio is greater than 200-300% (depending on RBC Trend Test.)	< 200% - 300%
Company Action Level	150-200%
Regulatory Action Level	100% - 150%
Authorized Control Level	70% - 100%
Mandatory Control Level	Below 70%

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Generic Risk Components

- Authorized Control Level RBC:
 - Asset Risk – Affiliated Investment Risk
 - Asset Risk – Credit Risk
 - Asset Risk – Other
 - Underwriting/Insurance Risk
 - Other Types of Risk (Varies by Formula)
 - Business Risk (Life & Health)
 - Interest Rate and Market Risk (Life)

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Trend Test

- A company action level RBC can also be triggered because of the trend test
- Life triggered if:
 - RBC% between 200% and 250%
 - Negative RBC trend for 3 years
- P/C triggered if:
 - RBC% between 200% and 300%
 - Combined ratio greater than 120%
- Health triggered if:
 - 200% and 300%
 - Combined ratio greater than 105%

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Company action level 150-200%

- What happens when a company RBC ratio is between 150-200%?
- State would start requiring the company to take actions to increase its RBC.

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Regulatory Action Level 100% - 150%

- Regulator would take actions
 - Would typically require more frequent reporting.
 - Recommend ways of raising capital etc.

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RBC Corrective Action Plan

- Conditions that contributed to the Company Action Level Event
- Proposals of corrective actions expected to result in the elimination of the Company Action Level Event
- Projections of the insurer's financial results for the current year and succeeding years
- Key assumptions impacting the insurer's projections
- Quality of and problems associated with the insurer's business

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Authorized Control Level 70% -100% Mandatory Control Level Below 70%

- State is authorized to take over control of the company at the Authorized control level
- State is required to take over control of the company at the mandatory control level

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Four RBC formulas

- Life RBC formula finalized in 1993
- P/C RBC formula finalized in 1994
- RBC standards for health organizations were implemented in 1998

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2011 STATISTICS

	Life RBC	P&C RBC	Health RBC
No Action	761	2499	761
Company (Life Trend Test)	3	13	11
Regulatory	1	14	8
Authorized	3	16	4
Mandatory	6	21	7
Total	772	2560	784

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STATISTICS

	2006	2007	2008	2009
No. of Insurers	4,194	4,195	4,148	4,118
Companies	36	40	63	53
Regulatory	26	28	27	22
Authorized	5	12	36	11
Mandatory	4	2	2	1
Total	4,318	4,317	4,304	4,251
No. of Actions	98.6	98.51	97.17	97.68

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STATISTICS

	2006	2007	2008	2009
Life No. of Insurers	97.17%	97.79%	98.26%	98.58%
P&C No. of Insurers	96.74%	97.42%	97.66%	97.62%
Health No. of Insurers	94.78%	94.24%	95.58%	96.56%

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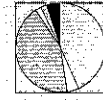
Industry Averages on RBC Ratio

	2009	2010	2011
Life	989%	1047%	1050%
Property and Casualty	1047%	1037%	1041%
Health	537%	606%	608%

Life Risk Components

Life Formula

- C-1 - Asset Risk - Mortality
- C-1a - Asset Risk - Common Stock
- C-1b - Asset Risk - Other
- C-2 - Insurance Risk
- C-3a - Interest Rate Risk
- C-3b - Health/Credit Risk
- C-4 - Business Risk
- C-4a - Business Risk - Admin Expenses



- Assets
- Interest
- Insurance
- Health
- Business

Property and Casualty Risk Components

Property/Casualty Formula

- R0 - Asset Risk - Affiliated
- R1 - Asset Risk - Fixed Income
- R2 - Asset Risk - Equity
- R3 - Asset Risk - Credit
- R4 - Underwriting Risk - Reserves



- Assets
- Reserves
- Business

Risk Based Capital Key Risks

- Risks that the Company is exposed to:
- Asset risk - affiliate
 - Risk of default for affiliated investments
 - Risk of default of debt assets and loss in market Value for Equity assets (Bonds, Stocks, Real estate, etc.)
- Underwriting Risk
 - Insurance Risk
- Business Risk

Asset Risk - Overview

- The risk that asset values turn out to be lower than expected, such as a bond default or by decreases in the market value of common stock.
- An insurer that has a portfolio containing high quality bonds has more stability in its investment earnings over time than an insurer who holds junk bonds or derivative securities. (Ex: CDO's, swaps, etc.)
- Insurers that have higher quality bonds typically have lower RBC requirements for this component.

Asset Risk - Affiliated

- Off-Balance Sheet Items include:
 - Non-controlled Assets: Not under the "exclusive control" of the company to dispose of the asset at will
 - Securities lending agreements
 - Guarantees for affiliates
 - Contingent Liabilities
- Annual Statement General Interrogatories and the Notes to Financial Statement

Asset Risk - Affiliated

- Insurer is charged based on affiliate's RBC.
- Calculated on a "see-through" basis.
- Advantage to this approach is that where there is a choice of whether to have ownership of an asset in either the parent or the subsidiary, RBC results are unlikely to affect the decision.



Asset Risk - Fixed Income

- Bonds
- Securities lending off-balance sheet collateral
- Cash, short-term, cash equivalents, money market funds

Asset Risk – Fixed Income

- Mortgage Loans -- Life – Currently LR004 Mortgage Experience Adjustment calculation for certain mortgages
- Replications & Mandatorily Convertible Securities
- Asset Concentration
- Separate Accounts



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Asset Risk – Other Long-Term

- Real estate :
 - Life RBC Charge for real estate and encumbrances combined is limited to the book/adj. carry
- Other Long Term Assets
 - Examples: Loan to Agent, Artwork, Pineapple, Rare Properties
 - P/C has on fixed factor
 - Life has different categories based on the "underlying characteristics"
 - Life fixed income BA assets must be rated



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Asset Risk - Equity

- Unaffiliated Preferred Stock and Hybrid securities
- Unaffiliated Common Stock
- RBC charge is based on the class of the security

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Asset Risk - Credit

- Reinsurance Recoverables – Schedule F, Part 3
 - Reinsurance balances receivable on reinsurance ceded to non-affiliated companies (excluding certain pools)
 - Paid and Unpaid, unearned premiums, and contingent commissions
 - Credit for provision for overdue authorized reinsurance, as well as, total unauthorized reinsurance, as reported on the liability page
 - Miscellaneous Recoverables from the Asset page
- Health Credit Risk – U & I, Part 1B
 - Reporting entity writes 5% or more of its net premiums in A & H lines in 2007, 2008 or 2009
 - Capitations to Intermediaries
 - ASC/ASC Business

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Underwriting Risk – P/C Companies Insurance Risk – Life Companies

- Same type of risk
- Surplus needed to provide for excess claims over the expected claims
 - From Random Fluctuations
 - Inaccurate Pricing
- Reserve Adequacy



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Insurance Risk

- Life Insurance
 - Looks at the amount of equity life, industrial life, group life and credit life insurance is in force and reduces it by the amount of reserves held
 - In force amount from Exhibit of Life Insurance less reserves from Exhibit 5
- Health Insurance
 - Includes health premiums, reserves and premiums stabilization reserves
 - Calculation is based on premiums and claims



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Underwriting Risk

- Largest Risk for P/C Companies
- Two Categories
 - Loss Reserve Risk *Underwriting Risk - Reserves*
 - Premium Risk *Underwriting Risk - Retention Premiums*
- Calculated by lines of business shown in Schedule P



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Other Types of Risk

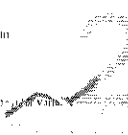
- Interest Rate Risk - Life
 - The risk of losses due to changes in interest rate levels
- Excessive Growth Risk – Property/Casualty
 - This is the risk that a company may grow too rapidly and have reserve deficiencies
- Business Risk – Life
 - Based on premium income, annuity considerations and separate account liabilities. Other general business risk exposures were also considered, such as litigation costs.

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Interest Rate & Market Risk

- Life Insurance Charge currently based on Exhibit 5 Reserves
- Annuity Reserves
 - Factor based calculation categories by low, medium and high risk.
 - C-1 Phase I RBC testing for products that are cash flow tested.
 - C-3 Phase II Stochastic modeling (random variation) - use of Monte Carlo simulation with generalized benefits.




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Covariance Formula

- What is the covariance adjustment?
 - Reduces aggregate amount of RBC - Authorized Control Level recognizing that the risk is remote that the surplus will be simultaneously impaired by reductions in all risk.
- The calculations:

$$\text{Life} = C_{10} + C_{15} + \sqrt{C_{10}^2 + C_{15}^2} + (C_{10}^2 + C_{15}^2) + (C_{20}^2 + C_{25}^2)$$

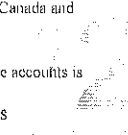
$$\text{Property/Casualty} = R_0 + \sqrt{R_0^2 + (R_1)^2} + (R_1)^2 + (R_2)^2 + (R_3)^2 + (R_4)^2 + (R_5)^2$$
- The Covariance adjustment is used to discount the total RBC before Covariance because the RBC amounts for the individual components when simply added together, overstate the true risk. It is assumed that not all events for which RBC is required would occur at the same time.



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Business Risk

- Premiums (Schedule T)
 - Total Premiums less Territories, Canada and Other Alien
- Separate Account Liabilities
 - Much of the exposure for separate accounts is reserve based
- Health Administrative Expenses



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Future of RBC


- Comparison to formulas used by other regulators is constantly being considered.
- Future view of RBC is still being discussed.
- Solvency Modernization/
- IAIS
- Group solvency issues

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Questions ??




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Insurance Regulation and Supervision in the U.S.

Financial Examinations




Training Objectives:

- Understand the purposes of financial examinations
- Identify the key points of the Model Law on Financial Condition Examinations
- Recall the types of Financial Condition Exams
- Understand what is included in the Report of Financial Condition Exams
- Describe the key examination participants
- Describe the Risk-Focused Surveillance examination approach method




Sherry L. Flippo, CPA, FLMI

- Financial Education Program Manager
- Joined NAIC in Jan. 2006
- Previously Manager in Internal Audit at Assurant, Inc.
- Previous experience in public accounting
- Primary responsibilities:
 - NAIC Financial Summit
 - Teaching Financial Courses
 - Updating Training Materials




What is a Financial Examination?

- A financial condition exam is an on-site regulatory review of an insurer's key processes with the primary goal of assessing financial solvency of the company.
 - An exam is risk-focused because the examiner focuses on areas of higher risk of an insurance company.




Why Conduct Financial Exams?

- To detect insurers with potential financial trouble (financial solvency of insurers)
- To identify noncompliance with statutes/regulations
- To compile information for timely, appropriate regulatory action
- Compliance with state laws.




Model Law on Examinations

- The NAIC Model Law and Accreditation guidelines specifically require state departments to conduct examinations in accordance with policies and procedures included in the NAIC *Financial Condition Examiners Handbook*. Variations to the methods and scope of exams are permitted to the extent that the variations reflect the financial strength and position of the insurer.




Why Conduct Financial Exams?

- To assess residual risk in insurer's activities and translate it into exam procedures
- To assess risk management processes such as corporate governance in addition to reviewing financial statement information
- To utilize exam findings to establish or revise the company's priority score




Model Law on Examinations

- Exams must be conducted on each licensed insurer at least once every 5 years
 - Some state statutes require more frequent exams
- A state may accept an examination report on a company prepared by another state if:
 - The state department performing the exam was accredited at the time of the exam: or
 - The exam was performed under the supervision of an accredited insurance department or by at least one examiner who is employed by an accredited department.




Examination Classifications

- Insurer Type
 - **Single-state insurer:** A company that does not meet the definition of a multi-state insurer such as a Health Maintenance Organization.
 - **Multi-state insurer:** A company that is domiciled or chartered in one state and licensed, registered, qualified or accredited, eligible or operating in at least one other state.




Examination Classifications

- Examination Type
 - **Individual exam:** A financial exam over one insurer.
 - **Group exam:** A financial exam over more than one insurer. This type of exam is typically conducted when multiple companies in a holding company group have similar key processes, systems and/or management.
- Exams can also be coordinated between regulators from multiple states.




Examination Classifications

- Exam Scope:
 - **Full-scope:** An examination in which the scope of the control and substantive procedures to be performed during the examination is based on the implementation and documentation of the risk assessment procedures required under the NAIC *Financial Condition Examiners Handbook*.
 - Review all areas of exam and focus on high-risk areas.
 - **Limited-scope:** An examination which is limited to a review or examination of specific financial statement line items or particular risk areas.




Key Examination Participants

- The following individuals from a state insurance department are the key participants that conduct and oversee the examinations of domestic insurance companies.
 - **Chief Examiner (or designee):** Schedule examinations, assign staff, coordinate with other state and zone examiners, and approve exam plan.
 - **Examiner-in-charge:** Coordinate review of company and examination testwork. Coordinate meetings with company and personnel.
 - **Staff Examiner:** Conduct examination testwork and become knowledgeable of company operations.
 - **Financial Analysts:** Interpret key financial and operational ratios, provide examiners with insight on company management, operating results, current events, etc.




Risk-Focused Exam Approach

- Examination methodology included within the NAIC Handbook is a 'risk-focused' approach.
- Required by Accreditation Standards.
- Under this approach, examination fieldwork will emphasize the review of an insurer's current or prospective solvency risk areas and the fair presentation of surplus.
- Examiner will focus work and resources on identified risk areas and focus less on areas with less risk.




Risk-Focused Surveillance

- In accordance with the risk-focused surveillance guidance, examination work will shift so that more time is spent during the planning and risk assessment processes of the examination.
- Efficiencies should be gained as examiners utilize knowledge from prior exams as well as information provided through on-going monitoring by analysts to stay aware of risks within insurer operations.



Risk-Focused Surveillance

- The risk-focused surveillance process requires examiners to prospectively consider the company's financial condition by assessing whether the company's current processes provide indications of future solvency concerns. Examples of items considered for prospective assessments include:
 - Corporate Governance
 - Future Business Plans
 - Rate of Company Growth
 - Liquidity of Assets



Risk-Focused Exam Approach

- Seven Phase Process:
 1. Understand the Company and Identify Key Functional Activities to be Reviewed
 2. Identify and Assess Inherent Risk in Activities
 3. Identify and Evaluate Risk Mitigation Strategies (Controls)
 4. Determine Residual Risk
 5. Establish/Conduct Detail Examination Procedures
 6. Update Prioritization and Supervisory Plan
 7. Draft Examination Report and Management Letter

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National Association of
Insurance Commissioners

Risk-Focused Exam Approach

Phase 1 – Understand the Company and Identify Key Functional Activities

- Key activities/sub-activities are identified using background information gathered on the company from various sources.

Phase 2 – Identify and Assess Inherent Risk

- Inherent risks are identified for each key activity selected in Phase 1. Inherent risks are the risks that exist before considering internal controls
 - Use examination repositories for assistance
- The examiner assesses each inherent risk based on the magnitude of impact and likelihood of occurrence.

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Risk-Focused Exam Approach

Phase 5 – Establish/Conduct Detail Exam Procedures

- Nature and extent of examination procedures should be commensurate with residual risk assessments.

Phase 6 – Update Prioritization and Supervisory Plan

- Relevant and material findings should be utilized and incorporated into determining or validating the priority of the insurer. The supervisory plan should outline the type of surveillance planned, resources dedicated to oversight, and coordination with other states

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Risk-Focused Exam Approach

Phase 3 – Identify/Evaluate Risk Mitigation Strategies

- Internal controls should be assessed by how well they mitigate each inherent risk. Risk mitigation strategies are assessed as strong, moderate, or weak.

Phase 4 – Determine Residual Risk

- How much risk is remaining after controls are considered? Once this is determined, the examiner can determine what detail tests should be performed.

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Risk-Focused Exam Approach

Phase 7 – Draft Exam Report and Management Letter

- Examination Report – A report documenting the examiner's assessment of financial condition and the identification of any material adverse findings noted during the examination.
- Management Letter – Optional tool to present results and observations of the exam that are not needed in the public report.

Examination reports are provided to other states in which the company is licensed.

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The Examination Report

Includes

- Table of contents
- Salutation
- Scope of the examination
- Body of report
 - Summary of significant findings
 - Significant subsequent events
 - Company history
 - Corporate governance
 - Company's financial statements
 - Summary of recommendations
 - Any other important regulatory information disclosed by the exam.

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Questions?



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Post Examination Procedures

The following activities should be performed after the examination report is issued and prior to the next examination:


- Follow up on examination findings
- Communication with financial analyst between examination dates
- Supervisory Report

The goal is to continually monitor the companies under examination, rather than to only perform examinations.



Data Collection Methodology & Procedures


Matt Minnich
Technical Projects Manager
Financial Regulatory Services Division



Data Storage

NAIC Financial Database Repository (FDR)


- Relational Database, Oracle 10g
- One of the World's largest insurance databases
- Over 400 million records (including applications, contracts, and other data) submitted to the NAIC
- 400 million records considering retention period (10 yrs)



Financial Database Repository (FDR)


The Oracle relational database used to receive, process, and store company financial data submitted to the NAIC by insurance entities

We (NAIC) often use FDR as a catch all term to include everything related to this database: front-end applications, back-end applications, data, metadata, processes, etc.




Databases and Structure

- Online Transaction Processing (OLTP)
- Decision Support System (DSS) - Optional
- Primarily utilized by i-Site and external users
- OLTP / DSS separation may yield better performance
- Static data through the course of a day
- Caveats...




View Oracle Data

- SQL+ (Structured Query Language, least user friendly, but least room for error)
- Internal Applications (CAAT)
- SQL+ (proprietary, internally maintained)



FDR Database Financial Tables

- Table is a database structure used to store data
- Tables are made up of columns and rows
- The intersection of a column and a row is a data field (or data element)
- FDR is Metadata driven using proprietary specs



Blanks translated in to electronic data elements

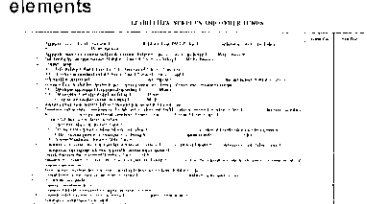





Table Metadata (Blanks Metadata)

- Data about the financial data
- Line (row) detail and Column detail
- "Line code" tagging
- Improves overall system efficiency
- Reduces hard or exception coding; yields flexibility



Specification Generator (SpecGen)

User friendly front end application

Develop and maintain financial table metadata (Metadata)

Copy Forward Years

Produce Vendor Specification Files

Raw Data File (.TXT)

2008 Life - Liabilities Database Table

SQL > desc L2008LIAB

Name	Null?	Type
COCCDF	NOT NULL	NUMBER(10)
LNCODE	NOT NULL	NUMBER(7)
LINE_NO	NOT NULL	VARCHAR2(7 CHAR)
ORDR	NOT NULL	NUMBER(10)
LAST_UPDATE	NOT NULL	DATE
ACTIVE_ROW	NOT NULL	VARCHAR2(1 CHAR)
YEAR	NOT NULL	NUMBER(4)
CURRENT_YEAR	NOT NULL	NUMBER(14)
PRGR_YEAR	NOT NULL	NUMBER(14)
INSIDE_AMT_1		NUMBER(14)
INSIDE_AMT_2		NUMBER(14)
INSIDE_AMT_3		NUMBER(14)

Table in Oracle

Instructions are translated in to electronic validations

Validation Rule Types

- Submission (allow/overrides)
- Completeness (expected files (PDF), filing sets (groups of tables), missing lines)
- Minimum Standard Failures (critical crosschecks)

FDR - Instructions are Translated into Electronic Validations

Validation Rule Types

- Submission (allow/overrides)
- Completeness (expected files (PDF), filing sets (groups of tables), missing lines)
- Minimum Standard Failures (critical crosschecks)

Formula Maintenance (FM)

User friendly Front-end application

Develop and maintain validation rules (Formula Metadata)

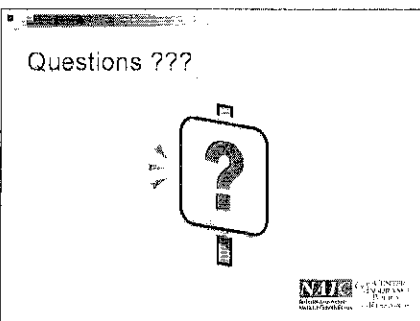
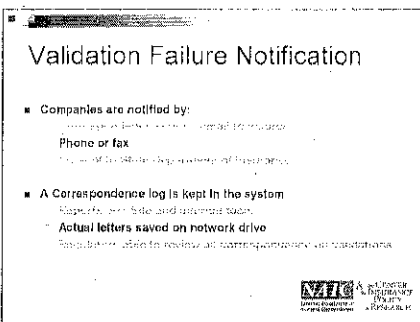
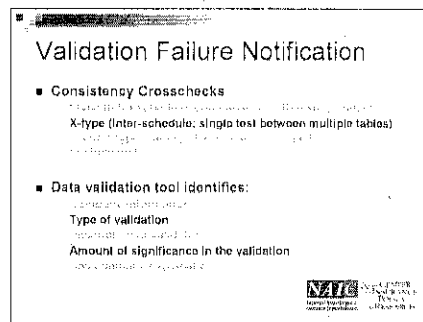
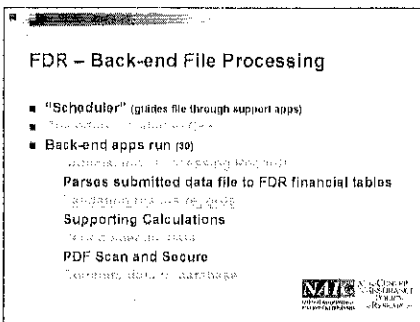
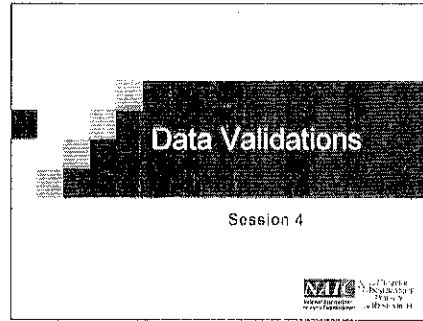
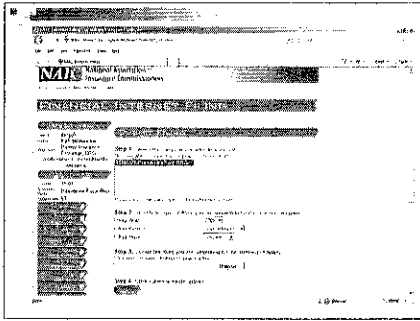
Copy Forward Years

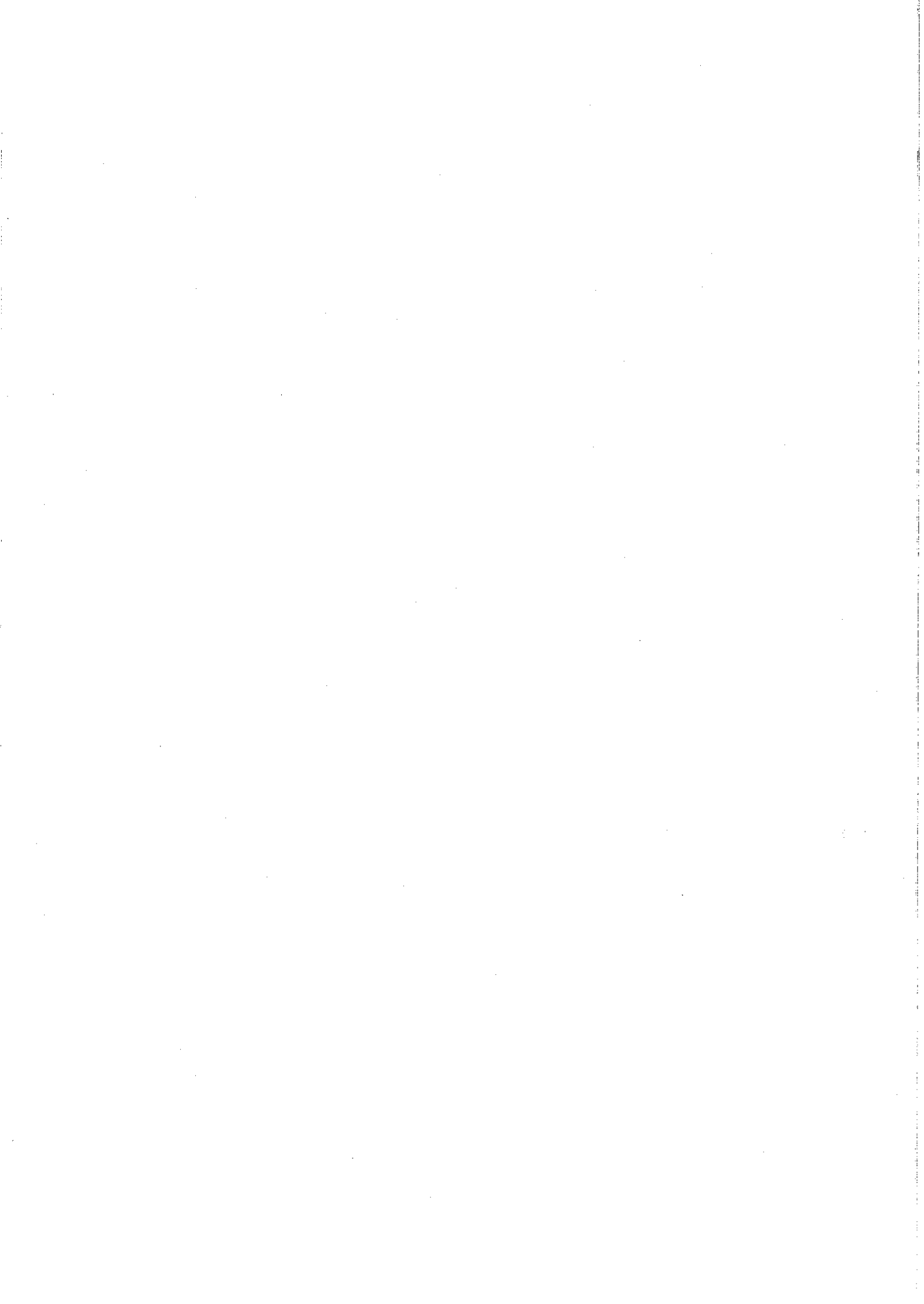
Simplify and complex validations

Supporting Gates

FDR - Blanks and Validation Metadata provided to External Software Vendors

- External Software Vendors (6 primary vendors)
- Insurers purchase software package
- Local desktop application or online entry
- Software Package is used to enter Annual to Quarterly financial data and produce FDR Submission file
- File submitted to NAIC via Internet Filing site





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BUREAU
RESEARCH

International Fellows Training April 12, 2012

Tim Mullen
NAIC Director of Market Regulation

NAIC
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Why Market Regulation?

The basic tenet of market regulation is to protect consumers by identifying and correcting insurer operating practices that are in conflict with contract provisions, state laws, rules, regulations, or orders of the Commissioner.

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Overview

- Why Market Regulation?
- Areas of Market Regulation
- NAIC Market Regulation Model Acts
- Standards for Company Conduct

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Areas of Market Regulation

- o Consumer Assistance
- o Education
- o Rate and Form Review
- o Producer Licensing
- o Investigations
- o Market Analysis
- o Examinations
- o Enforcement

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NAIC Market Regulation Model Acts

- Unfair Trade Practices Act
- Unfair Claims Settlement Practices Act
- Improper Termination Practices Act
- Producer Licensing Model Act
- Model Exam Law
- Market Conduct Surveillance Model Act

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Company Operations

- Licensed for the lines of business being written
- Audit program, antifraud plan and disaster recovery plan
- Monitor the activities of MGAs, GAs, TPAs and independent adjusters
- Records comply with state record retention requirements

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Standards for Company Conduct

- Company Operations/Management
- Marketing & Sales
- Underwriting & Rating
- Policyholder Service
- Claim Handling
- Complaints
- Producer Licensing

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INSURANCE
EXAMINERS
BUREAU
RESEARCH

Marketing and Sales

- All advertisements must be truthful and not misleading in fact or by implication
- Company communications to producers comply with applicable statutes and rules
- Internal producer training materials must comply with applicable rules

Underwriting and Rating

- The company underwriting practices are not unfairly discriminatory.
- Rates charged for the policy coverage are in accordance with filed rates (if applicable) or the company rating plan
- Company does not permit illegal rebating, commission cutting, or inducements.
- Rescissions are not made for non-material misrepresentation

Policyholder Service

- Policy issuance and insured-requested cancellations are timely
- All correspondence directed to the company is answered in a timely and responsive manner
- Company makes reasonable attempts to locate missing policyholders and beneficiaries

Underwriting and Rating, (cont)

- Applications are underwritten according to the company's underwriting guidelines
- All forms and endorsements are listed on the declarations page and filed with the department
- Cancellations/non-renewal notices comply with policy provisions and state laws

Claims Handling

- Timely investigations
- Claims handled in accordance with policy provisions
- Claims handled in accordance with applicable statutes, rules, and regulations
- Claim files adequately documented

Complaint Handling

- The company records complaints in the required format on the company complaint register
- The company takes adequate steps to finalize and dispose of the complaint
- The company responds to complaints in a timely fashion

Questions/Comments

Tim Mullen
NAIC Director of Market Regulation
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Producer Licensing

- Producers are properly licensed and appointed (if required)
- Appointments and terminations of producers does not result in unfair discrimination against policyholders
- Records of terminated producers adequately documented reasons for terminations

International Fellows Training

April 12, 2012

Fred Welker
NAIC - Market Regulation Specialist

The Basics

- Producer
- License and Renewal
- Agents and Broker License Programs
- Contract and Policy Approval
- Product Approval
- License Types
 - Individual
 - Business Entity
 - Renewal and Non-Renewal
- Lines of Authority
 - Variable Lines (Annuity, Accident & Health, Property)
 - Limited
 - Permitted Lines
 - Limited Lines

Presentation Overview

- The Basics - Agents/Brokers
- Licensing Process
- Continuation of Licenses
- Coordination Among States

Licensing Process

- Pre-Licensing Education
- Examination
- Background Check
 - Application Questions
 - Fingerprints
- Appointment

Continuation of Licenses

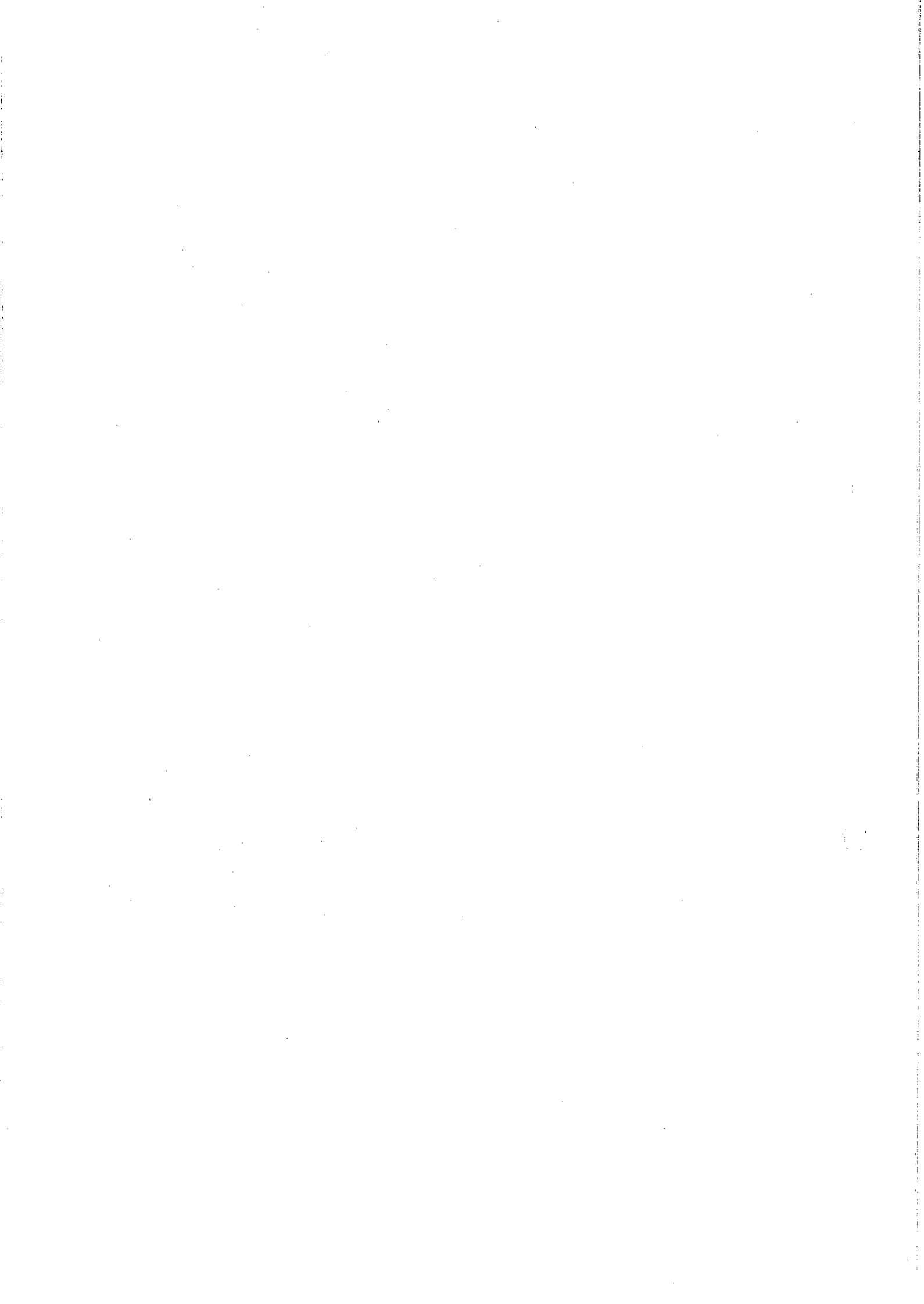
- Reporting of Actions
- Renewal - Two Year Cycle
- Continuing Education Requirement
- Suspensions and Revocations
- Reinstatements

Questions/Comments

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Coordination Among States

- Uniform License Applications
- State Producer License Database (SPLD) is a database of all producers across the United States. The following information is maintained in the SPLD:
 - Date of license when first issued to all producers, with name and address
 - License information such as license number, license number, license type, license status
 - Appointed agents, such as contract assignments, desired rate, commission, license, and renewal fees
 - Regulatory actions (if any)

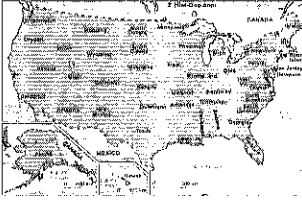


Regulating Life Insurance & Annuity Sales

International Fellows Training
Lois E. Alexander, FLMI, HIA, ACP
Market Regulation Manager

Regulating Life Insurance & Annuity Sales

MODEL LAWS



Regulating Life Insurance & Annuity Sales

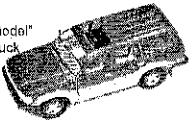
Learning Goals

1. Describe NAIC model law process (a best practice)
2. Recall two current problems discussed in class
3. Explain how one of these problems is the same or different in your country

Regulating Life Insurance & Annuity Sales

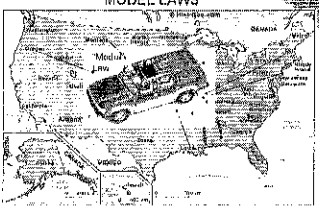
MODEL LAWS

"Model" Truck



Regulating Life Insurance & Annuity Sales

MODEL LAWS

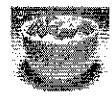


Regulating Life Insurance & Annuity Sales

Past Problems & Model Laws

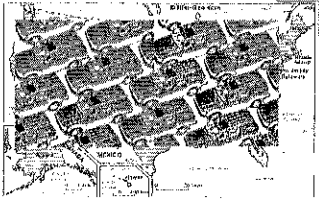
Annuities/variable annuities

- ♦ Suitability



Regulating Life Insurance & Annuity Sales

MODEL LAWS




Regulating Life Insurance & Annuity Sales

Past Problems & Model Laws

Annuities/variable annuities

- ♦ Suitability
- ♦ Disclosure




Regulating Life Insurance & Annuity Sales

Past Problems & Model Laws

Annuities/variable annuities

- ◆ Suitability
- ◆ Disclosure
- ◆ Replacement

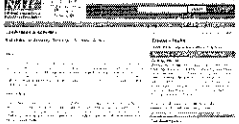


Regulating Life Insurance & Annuity Sales

Past Problems & Model Laws

Annuities/variable annuities

- ◆ Suitability
- ◆ Disclosure
- ◆ Replacement



Regulating Life Insurance & Annuity Sales

Past Problems & Model Laws
Best Practice Solution

- ◆ Annuity Suitability > Suitability in Annuity Transactions Model
- ◆ Annuity Disclosure >
- ◆ Annuity Replacement >

Regulating Life Insurance & Annuity Sales

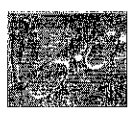
Past Problems & Model Laws
Best Practice Solution

- ◆ Annuity Suitability > Suitability in Annuity Transactions Model
- ◆ Annuity Disclosure > Annuity Disclosure Model
- ◆ Annuity Replacement > Life Insurance and Annuities Replacement

Regulating Life Insurance & Annuity Sales

Ongoing Problems


1. Annuity disclosure



Regulating Life Insurance & Annuity Sales

Ongoing Problems


2. Producers and Sales:
 - ◆ Licensing
 - ◆ Appointment



Regulating Life Insurance & Annuity Sales

Ongoing Problems


2. Producers and Sales:
 - ◆ Licensing



Regulating Life Insurance & Annuity Sales

Ongoing Problems

2. Producers and Sales:
 - ◆ Licensing
 - ◆ Appointment
 - ◆ Training




Regulating Life Insurance & Annuity Sales

Ongoing Problems

3. Insurers:

- ◆ Not admitted to state
- ◆ Failed to file rates and forms

> Model law?





Regulating Life Insurance & Annuity Sales

Ongoing Problems

4. Life Settlements

- ◆ Winners
- ◆ Losers






Regulating Life Insurance & Annuity Sales

Ongoing Problems

4. Life Settlements

- ◆ Winners






Regulating Life Insurance & Annuity Sales

Ongoing Problems

4. Life Settlements:


- ◆ Winners
- ◆ Losers
- ◆ Suitability

Regulating Life Insurance & Annuity Sales



Future Problems (?)

- ◆ Social Media and insurance sales
- ◆ Underwriting shortcuts:
 - ◆ ("jet" underwriting)
 - ◆ tele-underwriting



Questions?


Law: alexander.kalexander@naic.org

Regulating Life Insurance & Annuity Sales

Learning Goals

1. Describe NAIC model law process
2. Name two problems in regulating the sale of life insurance and annuities
3. Explain how one of these problems is the same or different in your country





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Product Filing Review Handbook

How to Use This Valuable Tool

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History of Rate and Form Regulation

- Philadelphia Contributionship - 1752
 - First fire insurance company by Benjamin Franklin.



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Objectives of this Session

- To acquaint stakeholders in the rate & form filing process with the use of *The Product Filing Review Handbook*.
- To provide stakeholders with a broad overview of the rate and form review process.
- To provide stakeholders with an overview of the System for Electronic Rate and Form Filing (SERFF)

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History of Rate and Form Regulation

- McCarran-Ferguson Act -1945
 - "The Congress hereby declares that the continued regulation and taxation by the states of the business of insurance is in the public interest... No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any state for the purpose of regulating the business of insurance..."

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History of Rate and Form Regulation

- Today:
 - States have retained the authority to regulate the insurance industry.
 - Federal Insurance Office created by the Dodd-Frank Bill.

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The Filing Process

The Filing The Filer The Reviewer Rating Level Rate Standards Filing Date

- The party making the filing such as the insurance company, advisory organization, or a third-party is referred to as the "filer."

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The Filing Process

The Filing The Filer The Reviewer Rating Level Rate Standards Filing Date

- A mechanism for an entity to use in seeking to meet certain requirements of a regulatory authority to obtain eligibility, or some other form of status or approval.
- Check with your state's definition.

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The Filing Process

The Filing The Filer The Reviewer Rating Level Rate Standards Filing Date

- The reviewer analyzes the filing for completeness, compliance with laws and regulations, and any other factors applicable for the type of insurance.

P&C Rate Regulation Basics

The P&C The File The Review Rating Laws Rate Standards Filing Date

- Rating Laws
 - Prior Approval
 - File and Use
 - Use and File
 - No File (Open competition)
 - Flex Rating

Filing Data

The P&C The File The Review Rating Laws Rate Standards Filing Data

- Time Frame (Accident Year, Policy Year, Report Year)
- Earned Premiums
- Incurred Losses

P&C Rate Regulation Basics

The P&C The File The Review Rating Laws Rate Standards Filing Date

- Rate Standards
 - Excessive
 - Inadequate
 - Unfairly discriminatory

Filing Data

The P&C The File The Review Rating Laws Rate Standards Filing Data

- Incurred Loss Adjustment Expense
- Other Expenses Incurred
- Claims Counts
- Exposures

Regulator Questions

- Data:
 - Enough for regulatory review?
 - Is number of years of experience appropriate?
 - How good is the quality of the data?
- Support & Justification:
 - Are supporting documents reasonable and acceptable?
 - Are assumptions used to develop the rates appropriate?

Life and Annuity Regulation

- Many States do not regulate life Insurance premium rates.
- They rely on competition and market forces.
- These states review contract provisions and non-forfeiture language.

Glossary of Terms

- Do you speak "actuarial?"

Chapter Three - Basics

Following are the definitions of terms used in this chapter. The definitions are intended to be consistent with the definitions used in the Act and the Regulations. The definitions are not intended to be exhaustive. The definitions are not intended to be interpreted as a limitation on the scope of the Act or the Regulations. The definitions are not intended to be interpreted as a limitation on the scope of the Act or the Regulations.

Health Rate Regulation

- Three types of Health Insurance

Disability
Income

Long Term
Care

Comprehensive
(Major Medical)

Comprehensive Medical Insurance

- Government-sponsored
- Employer –sponsored
- Commercial insurance

Review Questions for Policy Form Filings

- Is the consideration paid by policyholder clearly spelled out?
- Does the policy contain clear definitions?
- Are coverage agreements and limits of liability clearly spelled out?

Review Questions for Policy Form Filings

- Is the policy form an insurance contract?
- Is the policy form for a legal purpose?
- Does the policy form contain an acceptable risk transfer?
- Is the offer made by the filer to the policyholder clear?

Review Questions for Policy Form Filings

- Are duties of filer and policy or claimant clearly spelled out?
- Are coverage limitations or exclusions clearly spelled out?
- Any unreasonable or deceptive transfers?
- Are mandated provisions or conditions included?

Review Questions for Policy Form Filings

- Are any prohibited conditions or clauses included?
- Have readability requirements been met?
- Are form and contractual language consistent with pricing?
- Is advertising material consistent with the policy form?

SERFF Features and Functionality

- My Workfolder
- General Instructions
- Submission Requirements
- Filing Correspondence
- Objections and Responses
- Status Options
- Quick Text
- PDF Pipeline
- Electronic Funds Transfer
- Dispositions
- Public Access
- Paper filing Tracking and Disaster Recovery Plans
- Training/Tutorials

Speed To Market Tools

- Uniform Review Standards Checklists
- Product Requirements Locator
- Uniform Transmittal Documents
- Uniform Product Coding Matrices
- SERFF
- IIPRC

Regulatory Data Resources

- Financial Data Collection
 - Financial Annual Statements (Resources)
 - I-Site
 - Market Share Reports
 - Report on Profitability by Line and By State
 - Competition Database Report

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You Be The Judge

- Has this tool helped you understand how the rate and form approval process works?
- Do you have a better understanding of tools that are available to make form and filing reviews easier to complete?

NAIC

Ideas?

- Do you have ideas of ways you can speed insurance products to the market?
- If so, contact
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