



NATIONAL MEETING SUMMER 2021

Date: 7/15/21

Virtual Meeting

(in lieu of meeting at the 2021 Summer National Meeting)

ACCOUNTING PRACTICES AND PROCEDURES (E) TASK FORCE

Tuesday, July 27, 2021

12:00 – 1:00 p.m. ET / 11:00 a.m. – 12:00 p.m. CT / 10:00 – 11:00 a.m. MT / 9:00 – 10:00 a.m. PT

ROLL CALL

Doug Slape, Chair	Texas	Troy Downing	Montana
Trinidad Navarro, Vice Chair	Delaware	Eric Dunning	Nebraska
Jim L. Ridling	Alabama	Chris Nicolopoulos	New Hampshire
Lori K. Wing-Heier	Alaska	Marlene Caride	New Jersey
Peni Itula Sapini Teo	American Samoa	Russell Toal	New Mexico
Evan G. Daniels	Arizona	Linda A. Lacewell	New York
Alan McClain	Arkansas	Mike Causey	North Carolina
Ricardo Lara	California	Jon Godfread	North Dakota
Andrew N. Mais	Connecticut	Judith L. French	Ohio
Karima M. Woods	District of Columbia	Glen Mulready	Oklahoma
David Altmaier	Florida	Jessica K. Altman	Pennsylvania
Dean L. Cameron	Idaho	Elizabeth Kelleher Dwyer	Rhode Island
Amy L. Beard	Indiana	Raymond G. Farmer	South Carolina
Doug Ommen	Iowa	Larry D. Deiter	South Dakota
Vicki Schmidt	Kansas	Carter Lawrence	Tennessee
Sharon P. Clark	Kentucky	Jonathan T. Pike	Utah
James J. Donelon	Louisiana	Michael S. Pieciak	Vermont
Eric A. Cioppa	Maine	Scott A. White	Virginia
Gary D. Anderson	Massachusetts	Mike Kreidler	Washington
Anita G. Fox	Michigan	James A. Dodrill	West Virginia
Grace Arnold	Minnesota	Mark Afable	Wisconsin
Chloria Lindley-Myers	Missouri	Jeff Rude	Wyoming

NAIC Support Staff: Robin Marcotte

AGENDA

1. Consider Adoption of its Spring National Meeting Minutes
—*Jamie Walker (TX)* Attachment One
2. Consider Adoption of its Working Group Reports—*Jamie Walker (TX)*
 - a. Statutory Accounting Principles (E) Working Group
—*Dale Bruggeman (OH)* Attachment Two
 - b. Blanks (E) Working Group—*Jake Garn (UT)* Attachment Three
3. Consider Adoption of its 2022 Proposed Charges —*Jamie Walker (TX)* Attachment Four
4. Consider Adoption of Revisions to the Model Audit Rule Implementation Guide
—*Doug Stolte (VA)* Attachment Five



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5. Discuss Any Other Matters Brought Before the Task Force—*Jamie Walker (TX)*
6. Adjournment

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Draft: 3/29/21

Accounting Practices and Procedures (E) Task Force
Virtual Meeting (*in lieu of meeting at the 2021 Spring National Meeting*)
March 23, 2021

The Accounting Practices and Procedures (E) Task Force met March 23, 2021. The following Task Force members participated: Doug Slape, Chair, represented by Jamie Walker (TX); Trinidad Navarro, Vice Chair, represented by Rylynn Brown, Dave Lonchar and Tom Hudson (DE); Lori K. Wing-Heier and David Phifer (AK); Jim L. Ridling represented by Sheila Travis (AL); Evan G. Daniels represented by Kurt Regner (AZ); Alan McClain represented by Mel Anderson (AR); Ricardo Lara represented by Kim Hudson (CA); Andrew N. Mais represented by William Arfanis and Kathy Belfi (CT); Karima M. Woods represented by N. Kevin Brown (DC); David Altmaier represented by Carolyn Morgan and Virginia Christy (FL); Doug Ommen represented by Kevin Clark (IA); Dean L. Cameron represented by Eric Fletcher (ID); Stephen W. Robertson and Roy Eft (IN); Vicki Schmidt represented by Tish Becker (KS); Sharon P. Clark represented by Bill Clark (KY); James J. Donelon represented by Caroline Fletcher, Melissa Gibson and Denise Gardner (LA); Gary D. Anderson represented by John Turchi (MA); Eric A. Cioppa and Vanessa Sullivan (ME); Anita G. Fox represented by Judy Weaver (MI); Grace Arnold represented by Kathleen Orth (MN); Chlora Lindley-Myers represented by Shannon Schmoeger and John Rehagen (MO); Troy Downing (MT); Mike Causey represented by Jackie Obusek (NC); Jon Godfread represented by Colton Schulz (ND); Bruce R. Ramge represented by Lindsay Crawford and Justin Schrader (NE); Chris Nicolopoulos represented by Patricia Gosselin and Doug Bartlett (NH); Russell Toal represented by Leatrice Geckler (NM); Linda A. Lacewell represented by Bob Kasinow (NY); Judith L. French represented by Dale Bruggeman (OH); Glen Mulready represented by Eli Snowbarger (OK); Jessica K. Altman represented by Kimberly Rankin and Melissa Greiner (PA); Elizabeth Kelleher Dwyer represented by Jack Broccoli and John Tudino (RI); Raymond G. Farmer represented by Michael Shull (SC); Larry D. Deiter represented by Johanna Nickelson (SD); Carter Lawrence represented by Trey Hancock (TN); Jonathon T. Pike represented by Jake Garn (UT); Scott A. White represented by Doug Stolte and David Smith (VA); Michael S. Pieciak represented by Karen Ducharme (VT); Mike Kreidler represented by Steve Drutz (WA); Mark Afable represented by Amy Malm (WI); James A. Dodrill represented by Jamie Taylor (WV); and Jeff Rude, Linda Johnson and Doug Melvin (WY).

1. Adopted its 2020 Fall National Meeting Minutes

Ms. Walker directed the members to the Task Force's 2020 Fall National Meeting minutes. Ms. Walker also noted that the Task Force met March 16, 2021, in regulator-to-regulator session, pursuant to paragraph 3 (discussion of specific companies, entities or individuals) and paragraph 6 (consultations with NAIC staff related to NAIC technical guidance of the Accounting Practices and Procedures Manual) of the NAIC Policy Statement on Open Meetings. No actions were taken during this meeting, and the discussion was limited to the Spring National Meeting agenda.

Ms. Malm made a motion, seconded by Ms. Obusek, to adopt the Task Force's Nov. 19, 2020, minutes (*see NAIC Proceedings – Fall 2020, Accounting Practices and Procedures (E) Task Force*). The motion passed unanimously.

2. Adopted the Report of the Statutory Accounting Principles (E) Working Group

Mr. Bruggeman provided the report of the Statutory Accounting Principles (E) Working Group, which met March 15, except for 2019-24 related to leveled commissions which will be discussed separately. During this meeting, the Working Group adopted its Jan. 25, 2021; Jan. 6, 2021; Dec. 28, 2020; Dec. 18, 2020; Dec. 8, 2020; and Nov. 12, 2020, minutes. The interim minutes included the following adoptions to Appendix B—Interpretations (INTs) of statutory accounting principles (SAP):

- a. Extended *INT 20-03: Troubled Debt Restructuring Due to COVID-19* and *INT 20-07: Troubled Debt Restructuring for Certain Debt Instruments Due to COVID-19* through Jan. 1, 2022, or the date that is 60 days after the date on which the national emergency concerning the COVID-19 outbreak terminates.
- b. *INT 20-10: Reporting Nonconforming Credit Tenant Loans (CTLs)*: This INT allows nonconforming CTLs to continue to be reported on Schedule D Part 1 – Long-Term Bonds if filed with the NAIC Securities Valuation Office (SVO) by Feb. 15, 2021. The provisions within this INT and the ability to continue reporting nonconforming CTLs on Schedule D Part 1 with an SVO-assigned NAIC designation are limited time exceptions that extend only to Oct. 1, 2021.
- c. *INT 20-11: Extension of Ninety-Day Rule for the Impact of 2020 Hurricanes, California Wildfires and Iowa Windstorms*: This INT provides a 60-day extension from the 90-day rule for uncollected premium balances, bills

receivable and amounts due from agents and for policies directly affected by the noted events. This INT expires Feb. 28, 2021.

Mr. Bruggeman stated that the Working Group adopted the following nonsubstantive revisions to statutory accounting guidance:

- a. *Statement of Statutory Accounting Principles (SSAP) No. 5R—Liabilities, Contingencies and Impairments of Assets, SSAP No. 72—Surplus and Quasi-Reorganizations and SSAP No. 86—Derivatives: Revisions reject Accounting Standards Update (ASU) 2020-06, Debt—Debt with Conversion and Other Options (Subtopic 470-20) and Derivatives and Hedging—Contracts in Entity’s Own Equity (Subtopic 815-40), Accounting for Convertible Instruments and Contracts in an Entity’s Own Equity* for statutory accounting. (Ref #2020-41)
- b. *SSAP No. 25—Affiliates and Other Related Parties: Revisions clarify that an ownership greater than 10% in a reporting entity results in a related party designation, regardless of any disclaimer of control or affiliation. Additionally, the agenda item requires disclosure of such instances and identification of an insurer’s ultimate controlling party, as requested by the Group Solvency Issues (E) Working Group.* (Ref #2019-34)
- c. *SSAP No. 26R—Bonds:*
 - i. Revisions clarify that perpetual bonds are within the scope of SSAP No. 26R, and they are subject to the yield-to-worst concept. Additionally, perpetual bonds that possess a future call date will retain bond accounting—i.e., accounted for at amortized cost. However, if a perpetual bond does not possess a future call date, fair value accounting is required regardless of NAIC designation. (Ref #2020-22)
 - ii. Revisions expand the current called bond disclosures to also include bonds terminated early through a tender offer. (Ref #2020-32)
- d. *SSAP No. 32R—Preferred Stock and SSAP No. 86: Revisions direct that publicly traded preferred stock warrants are in the scope of SSAP No. 32R, and they shall be reported at fair value.* (Ref #2020-33)
- e. *SSAP No. 43R—Loan-Backed and Structured Securities: Revisions incorporate minor scope modifications to reflect recent changes to the Federal Home Loan Mortgage Corporation (Freddie Mac) Structured Agency Credit Risk (STACR) and Federal National Mortgage Association (Fannie Mae) Connecticut Avenue Securities (CAS) programs, which allow credit risk transfer securities from these programs to remain in the scope of SSAP No. 43R when issued through a real estate mortgage investment conduit (REMIC) structure.* (Ref #2020-34)
- f. *Appendix D—Nonapplicable GAAP Pronouncements: Revisions reject ASU 2020-07, Not-for-Profit Entities (Topic 958): Presentation and Disclosures by Not-for-Profit Entities for Contributed Nonfinancial Assets* as not applicable for statutory accounting. (Ref #2020-42)
- g. *Appendix F—Policy Statements: Revisions to the NAIC Policy Statement on Maintenance of Statutory Accounting Principles* clarify the existing process regarding the Working Group’s issuance and adoption of accounting interpretations. (Ref #2020-39)
- h. *Preamble: Revisions clarify that while any state in which a company is licensed can issue prescribed practices, the prescribed practices directed by the domiciliary state: 1) shall be reflected in the financial statements filed with the NAIC; and 2) are the financial statements subject to independent audit requirements.* (Ref #2020-40)

Mr. Bruggeman stated that the Working Group exposed the following nonsubstantive revisions to statutory accounting guidance:

- a. Exposed *INT 21-01T: Statutory Accounting Treatment for Cryptocurrencies*, which clarifies that cryptocurrencies do not meet the definition of cash, and they are nonadmitted assets for statutory accounting. The Working Group requested comments on the level of interest and ownership of cryptocurrencies. (Ref #2021-05)

- b. Revisions reject:
- i. ASU 2020-08, Codification Improvements to Subtopic 310-20, Receivables – Nonrefundable Fees and Other Costs for statutory accounting. (Ref #2021-02)
 - ii. ASU 2021-02, Franchisors – Revenue from Contracts with Customers (Subtopic 952-606): Practical Expedient. (Ref #2021-07).
 - iii. ASU 2020-11, Financial Services—Insurance (Topic 944): Effective Date and Early Application (Ref #2021-08).
- c. Exposed revisions to *INT 20-01: ASU 2020-04 – Reference Rate Reform*. INT 20-01 exposes a temporary (optional) expedient and exception guidance for *ASU 2021-01, Reference Rate Reform (Topic 848): Scope* with an expiration date of Dec. 31, 2022. The optional expedients would expand the current exceptions to allow for the continuation of the existing hedge relationship and thus not require hedge dedesignation for derivative instruments affected by changes to interest/reference rates due to reference rate reform, regardless of whether they reference the London Interbank Offered Rate [LIBOR] or another rate that is expected to be discontinued. The exception in INT 20-01 would apply for affected derivatives used for discounting, margining or contract price alignment. (Ref #2021-01)
- d. *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities*: Exposed this agenda item with the intent to dispose without statutory edits. NAIC staff note that the long-standing, required statutory adjustments to SSAP No. 97, paragraph 8.b.iv. – Foreign Insurance SCA Entities could result in negative equity valuation, as assets held in a foreign subsidiary should not be valued in a more favorable manner than had they been held directly by the insurer. Industry comments are requested regarding detailed instances of negative value subsidiary, controlled and affiliated entities (SCAs). (Ref #2021-04)
- e. *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*: Revisions propose data-captured templates for existing disclosures in SSAP No. 103R, which are currently only completed in narrative form. Data-capturing of such items will permit state insurance regulators to submit system inquiries to determine the extent to which reporting entities have transferred (sold), but still retain, a material participation with said assets. A blanks proposal will be concurrently exposed with the Working Group’s exposure. (Ref #2021-03)
- f. *SSAP No. 107—Risk-Sharing Provisions of the Affordable Care Act*: Revisions include state Affordable Care Act (ACA) reinsurance programs, which are using Section 1332 waivers in the scope of SSAP No. 107. The revisions continue to follow the hybrid accounting approach for the state ACA programs, as they operate in a similar manner. (Ref #2021-09)
- g. *SSAP No. 108—Derivatives Hedging Variable Annuity Guarantees*: Re-exposed this agenda item to provide additional time for interested parties to develop a proposal for establishing accounting and reporting guidance for derivatives hedging the growth in interest for fixed indexed products. (Ref #2020-36)

Mr. Bruggeman stated that the Working Group exposed the following blanks proposals:

- a. Re-exposed this agenda item for a concurrent exposure with the Blanks (E) Working Group. The Working Group is sponsoring blanks agenda item 2021-03BWG to modify the current General Interrogatory instructions and require that a distinct disaggregated product identifier be used for each product represented. The disaggregation will require that each separate account product filing or policy form be separately identified. The instructions will also indicate that companies may eliminate proprietary information. However, the elimination will still require the use of a unique reporting identifier. (Ref #2020-37)
- b. Re-exposed this agenda item for a concurrent exposure with the Blanks (E) Working Group. The Working Group is sponsoring blanks agenda item 2021-03BWG to clarify reporting by each separate product filing or policy form and add product identifiers, specifically for pension risk transfer (PRT) and registered index linked annuity (RILA) transactions in the Separate Account General Interrogatories. (Ref #2020-38)

Mr. Bruggeman stated that the Working Group exposed the following editorial revisions (Ref #2021-06EP):

- a. *SSAP No. 53—Property Casualty Contracts—Premiums*: Revisions retitle the statement to *SSAP No. 53—Property and Casualty Contracts—Premiums*.
- b. *SSAP No. 97*: Revisions correct grammatical errors in paragraph 54.
- c. *SSAP Glossary*: Revisions remove the footnote in the Glossary title and replace it as an opening paragraph with updated verbiage.

Mr. Bruggeman stated that the Working Group disposed agenda item 2020-35: *SSAP No. 97 – Audit Opinions without statutory revisions*, as the issue of nonadmittance due to the inability to quantify a departure from U.S. generally accepted accounting principles (GAAP) was not deemed prevalent. (Ref #2020-35)

Mr. Bruggeman stated that the Working Group received an update on the following projects and referrals:

- a. Received an update that NAIC staff, industry and key state insurance regulators have made significant progress on agenda item 2019-21: *SSAP No. 43R – Investment Classification Project*. While discussions remain ongoing, it is anticipated that a public exposure will occur via an interim meeting prior to the Summer National Meeting. The exposure will include additional principle concepts on which investments are eligible for reporting on Schedule D as a bond.
- b. Received an update that *INT 19-02: Freddie Mac Single Security Initiative* remains in full effect. The Freddie Mac Single Security Initiative remains an ongoing program, and it does not appear to be subject to termination in the foreseeable future.
- c. Received an update on agenda item 2019-49: *Retroactive Reinsurance Exception*. This agenda item addresses a referral from the Committee on Property and Liability Financial Reporting (COPLFR) of the American Academy of Actuaries (Academy), which noted diversity in reporting regarding companies applying the retroactive reinsurance exception, which allows certain contracts to be reported prospectively. NAIC staff have held preliminary discussion with Casualty Actuarial and Statistical (C) Task Force members, with a preliminary recommendation that the premium and losses transferred under such transactions should be allocated to the prior Schedule P calendar year premiums and the losses allocated to the prior accident year incurred losses.
- d. Received an update on the reporting and extinguishment of loans received from the Paycheck Protection Program (PPP). For statutory accounting, the authoritative guidance in *SSAP No. 15—Debt and Holding Company Obligations*, paragraph 11 provides that debt is recognized until extinguished, including formally being forgiven. In addition, per *SSAP No. 15*, paragraph 25 gains on termination of debt are recognized as capital gains.
- e. Received an update on the Valuation of Securities (E) Task Force discussion regarding revisions to the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* (P&P Manual) as coordination regarding the revisions to *SSAP No. 105R—Working Capital Finance Investments* adopted by the Working Group in May 2020 (agenda item 2019-25). At its Nov. 18, 2020, meeting, the Task Force directed a referral to the Working Group, which is still pending. NAIC staff anticipate addressing this referral when received.
- f. Received an update on current U.S. GAAP exposures/invitations to comment, noting that no comments by the Working Group are planned during the exposure periods.

Mr. Bruggeman stated that the public comment period for all exposed agenda items ends April 30.

Mr. Bruggeman made a motion, seconded by Ms. Rankin, to adopt the Working Group's report except for agenda item 2019-24 on levelized commission, which will have a separate vote (Attachment One). The motion passed unanimously.

3. Adopted Agenda Item 2019-24

Mr. Bruggeman provided an overview of Statutory Accounting Principles (E) Working Group agenda item 2019-24 regarding levelized commission, which affects *SSAP No. 71—Policy Acquisition Costs and Commissions*. He stated that the Working Group has been discussing this item since August 2019, when it was brought to the Working Group by a domiciliary state. Mr.

Bruggeman stated that after six public discussions, the nonsubstantive revisions that clarify the guidance in SSAP No. 71 regarding levelized commissions were adopted on March 15, 2021, with a Dec. 31, 2021, effective date. Thirteen Working Group members voted in favor of adoption, and one member was opposed. At the March 15 meeting, the Working Group affirmed the nonsubstantive classification of these revisions as consistent with the original intent of SSAP No. 71. In addition, the Working Group exposed a new annual statement general interrogatory to identify the use of a third party for the payment of commission expenses, which will be concurrently exposed with the Blanks (E) Working Group.

Mr. Bruggeman stated that both U.S. GAAP and SAP would calculate acquisition costs in a similar manner. However, one of the major financial reporting differences between SAP and GAAP is that GAAP capitalizes acquisition costs and expenses them over time to match revenue and expenses. SAP expenses policy acquisitions costs as incurred.

Mr. Bruggeman stated that at the heart of this issue is that a small number of reporting entities are using third parties to pay their sales commission costs and not recognizing the full liability of what is in essence a loan to repay the third parties as required under SSAP No. 71. He said that the Working Group has had extensive discussion on this topic and has noted that the revisions clarify the long-standing principles in SSAP No. 71, which have existed since even prior to codification. He stated that the revisions were classified as nonsubstantive because the revisions emphasize the original principles regarding funding agreements and the impact to a minor number of companies do not determine the classification of the revisions.

Mr. Bruggeman noted that state insurance regulators and consumer representative also voiced concerns about the illusory surplus and unlevel playing field such arrangements create. He stated that because of the unfair competitive advantages that are perceived, the Working Group was not in favor of grandfathering the practices. He noted that the Working Group did discuss that companies could have discussions with their domiciliary states regarding obtaining a permitted practice for phasing in the financial impact. He stated that a permitted practice approach was favored because the impact to the affected companies may vary.

Ms. Fletcher noted that Commissioner James J. Donelon could not attend the meeting, but he wanted his comments that this is a substantive change noted and also that he is in favor of a phase-in period. Mr. Snowbarger noted that Oklahoma also supports the comments from Louisiana.

Lynn Kelley (Delaware Life) stated that their position is also that the revisions are substantive and that they appreciate the time that the Working Group has spent discussing this issue even if not all of the edits they submitted were incorporated. She also stated support for an effective date at least as late as Dec. 31, 2021.

Elly Nettleton (Guggenheim Life and Annuity) highlighted two points from their prior comment letters: 1) levelized commissions are not a new concept and date back several decades. She noted that a 2010 U.S. Securities and Exchange Commission (SEC) complaint against another carrier identified levelized commissions as a common practice in the industry. She said Guggenheim is not aware that the accounting treatment was determined not to be in accordance with statutory accounting principles; and 2) traditional commissions such as those tied to policy persistency are carved out of the proposals. Ms. Nettleton said Guggenheim believes it is a dangerous precedent to remove persistency as a factor in the accrual of commissions as it is a key insurance element.

Mr. Bruggeman noted that similar comments as Ms. Nettleton's were made at the Working Group. He stated that the Working Group did hear the comments but did not agree with them.

Thomas Considine (National Council of Insurance Legislators—NCOIL) stated that NCOIL members feel strongly that the revisions are substantive but are willing to put that aside and do not feel the need to debate that classification again at this time. He stated that this is a practice that has been going on for decades. He stated that to implement this change during a period of great economic turmoil seems not only short-sighted, but also it is dangerous to require entities to make such a change in a period of a year. He stated that NCOIL recommends a significant phase-in period with a proposed effective date of Dec. 31, 2025. He noted prior Working Group discussions have recommended that reporting entities seeking a phase-in period should seek a permitted practice from their domiciliary regulators. He stated that a permitted practice does not reflect positively on the state granting the practice or the reporting entity receiving the practice. He stated that accreditation reviews note the permitted practices granted by a jurisdiction. He stated that the most fair and equitable solution and a way to avoid the debate of change classification is to add a four- or five-year phase-in.

Mr. Bruggeman stated that funding agreements to levelized commission costs are not prohibited. He said the issue is that the full liability for the funding agreement must be recognized for the inherent loan. In other words, it is a financing arrangement; it does not delay the timing of recognition of the acquisition costs. He stated that a permitted practice may not have a positive

perception. However, permitted practice disclosure requirements allow state insurance regulators to understand the surplus impact of the arrangement. He stated that a permitted practice provides transparency and noted that if there were any decisions to extend the effective date beyond Dec. 31, 2021, there would need to be a disclosure of the impact. Ms. Walker agreed, noting that consistency, meaning the ability to compare reporting entities' financial positions, is a fundamental concept that statutory accounting is based on. She noted its importance for solvency regulation.

Mr. Considine noted that to address Mr. Bruggeman's point about state insurance regulators' information, he is confident that if there were a four- or five-year phase-in, legislators would be supportive of a reasonably tailored data call. Mr. Rehagen asked if Mr. Considine envisioned a confidential data call or one that would be publicly produced. Mr. Considine indicated he assumed if it were for the state insurance regulators, then such a data call would be confidential. However, he said NCOIL would be open to discussion. Mr. Bruggeman stated his intent was for a disclosure to be part of the public statutory accounting filing.

Mr. Stolte stated that the Task Force is discussing noncompliant statutory accounting by a handful of companies. He stated that in 1991, Virginia had an insurance receivership of a large life insurance company that had a deferred commission funding arrangement. He said that the insurer had not booked the liability, but when the company was put into receivership, the funding entity/financier filed with the receivership a request for payment of \$16 million. He said that the reporting entity prior to the receivership was reporting \$120 million in surplus, but true surplus ended up being approximately \$4 million. He said he disagreed with the statement that what the handful of companies are doing is an acceptable SAP practice. He said it is noncompliance with statutory accounting in SSAP No. 71, and also with the statutory accounting guidance that existed even prior to codification. He said from a level playing field perspective, he does not want to be forced to approve such agreements for his companies to be able to compete with reporting entities employing this practice. He stated that not recording the full liability for the funding agreements creates illusory surplus. He stated that if a reporting entity needs more time to implement the revisions, a permitted practice is what should be employed. He noted that he received notification of more than 100 permitted practices in an average year. He stated that the permitted practices are designed to provide transparent disclosure for all state insurance regulators.

Mr. Considine stated that what Mr. Stolte is terming "noncompliance" has been accepted in the regulatory community for 20 years. He said if reporting entities have been doing so for 20 years, it seems unreasonable to require a change in one year. Mr. Stole said that in Virginia, they have not accepted such practices. He noted that there may be some that they were unaware of, but they do not view it as an acceptable practice. He stated that this has been noted as problematic in a formal examination report, and he respectfully disagrees with Mr. Considine's statement that it was an acceptable practice. Ms. Walker also noted that she has been a Texas state insurance regulator for 20 years and is not aware of any entities that are using funding agreements to defer the recognition of acquisition costs. She noted that she would also take exception to doing so if it were identified in an examination or other regulatory review.

Brendon Bridgeland (Center for Insurance Research—CIR) stated support for the proposal as adopted by the Working Group. He stated that one of the top priorities for state insurance regulators was ensuring that the insurers are solvent. He stated that part of that is also ensuring that there is a level playing field. He stated that in this case, there are a handful of companies using a technique that, by their own admission, is enhancing surplus. He noted that as a consumer advocate, he does not want to see insurers have illusory surplus.

Mr. Bruggeman made a motion, seconded by Mr. Stolte to adopt the nonsubstantive revisions to SSAP No. 71 with a Dec. 31, 2021, effective date as adopted by the Working Group (Attachment One-Q). The motion passed with 41 in favor and the states of Louisiana and Oklahoma opposed.

Ms. Walker stated that agenda item 2019-24 will next be discussed by the Financial Condition (E) Committee, which is scheduled to meet April 13.

4. Adopted the Report of the Blanks (E) Working Group

Mr. Garn provided the report of the Blanks (E) Working Group, which met March 16. He stated that the Working Group adopted its Dec. 16, 2020, minutes, which included the following action:

- a. Adopted four blanks proposals: 1) 2020-28BWG – remove Note 22; 2) 2020-29BWG – remove a line category from the investment schedules; 3) 2020-30BWG – move an interrogatory question from the annual blank to the quarterly blank; and 4) 2020-31BWG – changes to the Life, Health and Annuity Guaranty Association Model Act Assessment Base Reconciliation Exhibits.

- b. Exposed seven proposals for a 60-day public comment period ending Feb. 16.
- c. Adopted its editorial listings.

Mr. Garn stated that the Working Group adopted its editorial listing and the following seven proposals:

- a. 2020-32BWG – Add a new Health Care Receivables Supplement to the Life\Fraternal Annual Statement that adds Exhibit 3 and Exhibit 3A from the Health Annual Statement to the Life\Fraternal annual filings. Add a guidance document reference to Exhibit 3A of the Health Annual Statement.
- b. 2020-33BWG – Modify Annual Statement Lines (ASLs) used on Underwriting and Investment (U&I) Exhibits, State Page and Insurance Expense Exhibit (IEE). Change Health ASL categories used in Property to be consistent with other statement types. Update ASL references used in crosschecks. Update definitions used in the appendix for the Health ASLs.
- c. 2020-34BWG – Add definitions for the Occupational Accident, Fiduciary Liability, Premises and Operations (OL&T and M&C), Professional Errors and Omissions Liability, Kidnap & Ransom Liability and Tuition Reimbursement Plans products to the appropriate Line of Business in the appendix.
- d. 2020-35BWG – Expand the number of characters used from seven to 10 in the investment line categories for Schedules D, DA, DL and E excluding Schedule D, Part 6 (Sections 1 and 2) and Schedule E (Part 1 and 3). Add line categories for Unaffiliated Certificates of Deposit and Exchange Traded Funds (ETFs). Split the line categories for Mutual Funds, Investment Unit Trusts and Closed-End Funds into lines indicating if the fund has been assigned a designation by the SVO. Make changes to Summary Investment Schedule, Summary by Country and Schedule D, Part 1A (Section 1 and Section 2) to reflect the additional line categories.
- e. 2020-36BWG – Modify the General Schedules Investment Instructions and Schedule DB General Instructions to reflect treatment of publicly traded stock warrants as being in the scope of *SSAP No. 30R—Unaffiliated Common Stock* or *SSAP No. 32R* and reporting as common and preferred stock (SAPWG 2020-33).
- f. 2020-37BWG – Add a new Schedule Y, Part 3 to capture all entities with ownership greater than 10%, the ultimate controlling parties of those owners and other entities that the ultimate controlling party controls (SAPWG 2020-34).
- g. 2020-38BWG – Make changes to the Accident and Health Policy Experience Exhibit by adding new columns, removing lines distinguishing with and without contract reserves, adding some new product lines, eliminating summary tables, changing the date that the exhibit is due and having it reported by state.

Mr. Garn stated that the Working Group exposed five new proposals for a six-week public comment period ending April 27 and received a memorandum from the Valuation of Securities (E) Task Force regarding the addition of two new residential mortgage-backed securities (RMBS)/commercial mortgage-backed securities (CMBS) administrative codes.

Mr. Garn made a motion, seconded by Mr. Eft, to adopt the report of the Blanks (E) Working Group (Attachment Two). The motion passed unanimously.

Having no further business, the Accounting Practices and Procedures (E) Task Force adjourned.

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NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

Virtual Meeting

STATUTORY ACCOUNTING PRINCIPLES (E) WORKING GROUP

July 20, 2021 / July 12, 2021 / May 20, 2021 / April 20, 2021

Summary Report

The Statutory Accounting Principles (E) Working Group conducted e-votes that concluded July 20, 2021; July 12, 2021; and April 20, 2021; and met May 20, 2021.

1. During the July 20 e-vote, the Working Group exposed agenda item 2021-10: *SSAP No. 32R—Clarification of Effective Call Price* for a public comment period ending Aug. 6.
2. During the July 12 e-vote, the Working Group adopted its May 20, April 20, and Spring National Meeting minutes.
3. During the May 20 meeting, the Working Group:
 - a. Adopted the following nonsubstantive revisions to statutory accounting guidance:
 1. *Statement of Statutory Accounting Principles (SSAP) No. 26R—Bonds*: Revisions reject *Accounting Standards Update (ASU) 2020-08, Codification Improvements to Subtopic 310-20, Receivables – Nonrefundable Fees and Other Costs* for statutory accounting. (Ref #2021-02)
 2. *SSAP No. 47—Uninsured Plans*: Revisions reject *ASU 2021-02, Franchisors – Revenue from Contracts with Customers* for statutory accounting. (Ref #2021-08)
 3. *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*: Revisions incorporate disclosure elements and a data-capture template for where an entity has transferred assets but retains economic interest within the reporting entity, its related parties, or another member within the holding company group. (Ref #2021-03)
 4. Adopted agenda items supporting disaggregated product identifiers to be used for each separate account product reported in the general interrogatories. This adoption does not result in statutory revisions, but it is reflected in the Working Group recommendation to support blanks proposal 2021-03BWG. (Ref #2020-37 and Ref #2020-38)
5. *Appendix B—Interpretations of Statutory Accounting Principles*:
 - i. *Interpretation (INT) 20-01: ASU 2020-04 – Reference Rate Reform*: This interpretation provides optional guidance, allowing for the continuation of certain existing hedge relationships and thus does not require hedge dedesignation for derivative instruments affected by changes to interest/reference rates due to reference rate reform. This interpretation is all-encompassing for “any hedging relationships” within the scope of INT 20-01 and captures all hedging transaction types, regardless of if the transaction occurred bilaterally or through a central clearing party. (Ref #2021-01)



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- ii. *INT 21-01: Accounting for Cryptocurrencies*: This interpretation clarifies that directly held cryptocurrencies neither meet the definition of cash in *SSAP No. 2R—Cash, Cash Equivalents, Drafts and Short-Term Investments* nor when directly held, meet the definition of an admitted asset per *SSAP No. 4—Assets and Nonadmitted Assets*. (Ref #2021-05)
- 6. *Appendix D—Nonapplicable GAAP Pronouncements*: Revisions reject *ASU 2020-11, Financial Services – Insurance: Effective Date and Early Application* as not applicable for statutory accounting. (Ref #2021-07)
- b. Adopted the following editorial revisions (Ref #2021-06EP):
 - 1. *SSAP No. 53—Property Casualty Contracts—Premiums*: Revisions retitle to *SSAP No. 53—Property and Casualty Contracts—Premiums*.
 - 2. *SSAP No. 97—Investments in Subsidiary, Controlled and Affiliated Entities*: Revisions correct grammatical errors in paragraph 54.
 - 3. *SSAP Glossary*: Revisions remove the footnote in the Glossary title and replace it as an opening paragraph with updated verbiage.
- c. Exposed the substantive proposed bond definition to be used for all securities in determining whether they qualify for reporting on Schedule D, Part 1 – Long-Term Bonds. The definition intends to reflect principal concepts to ensure appropriate consideration on whether a structure qualifies as an issuer credit obligation or an asset-backed security (ABS) prior to reporting as a bond. The public comment period for this agenda item ends July 15. (Ref #2019-21)
- d. Exposed nonsubstantive revisions to *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies* and *SSAP No. 97* to indicate that the equity method valuation reference in *SSAP No. 97* can result in a negative equity valuation and to limit the statutory adjustments match in *SSAP No. 97*, paragraph 9. The exposure requests public comments on language suggested by interested parties that foreign insurance subsidiary, controlled and affiliated entities (SCAs) shall stop at zero (and thus not be subject to negative equity valuations) when applying paragraph 9 adjustments in cases where the foreign insurance subsidiary is not engaged in providing services to, or holding assets on behalf of, U.S. insurers. The public comment period for this agenda item ends July 15. (Ref #2021-04)
- e. Adopted a response to the Life Risk-Based Capital (E) Working Group on its referral request to consider accounting and reporting aspects of an American Council of Life Insurers (ACLI) proposal to modify the treatment of real estate in the life risk-based capital (RBC) formula. The adopted response identifies concerns on the reliability and consistency of fair value data to be considered before allowing reporting entities to reduce RBC through the reported fair value of real estate.
- f. Received an update on the following projects and referrals:
 - 1. The Working Group directed a referral to be sent to the Life Actuarial (A) Task Force seeking input regarding whether the Task Force would consider changes to the



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reserve framework of fixed indexed annuity products, as its response will likely directly influence the accounting options for derivatives hedging these products. (Ref #2020-36)

2. *SSAP No. 107—Risk-Sharing Provisions of the Affordable Care Act*: The Working Group directed NAIC staff to develop additional revisions that expand the guidance to address the diversity in state Affordable Care Act (ACA) reinsurance programs identified in the industry comments. (Ref #2021-09)
3. *INT 20-10: Reporting Nonconforming Credit Tenant Loans*: Contingently exposed *nonsubstantive* revisions in anticipation of a Valuation of Securities (E) Task Force proposal to revise filing exempt (FE) requirements for credit tenant loans (CTLs). Subsequent to the Working Group meeting, on May 24, the Task Force did not expose the anticipated revisions. Instead, the Task Force exposed edits to clarify that the reference to mortgage loans in the CTL definition pertains to items in scope of *SSAP No. 37—Mortgage Loans*, and that the *Accounting Practices and Procedures Manual* determines investment accounting and reporting. With this Task Force action, the revisions to INT 20-10 were not exposed. It is anticipated that the Working Group will review INT 20-10 after the Task Force concludes actions after their exposure.
4. Received a response from the Valuation of Securities (E) Task Force regarding CTLs and information regarding Securities Valuation Office (SVO) filings received.
4. During the April 20 e-vote, the Working Group voted to update exposed agenda item 2021-03: SSAP No. 103R – Disclosures to reflect interested parties’ preliminary comments. While minor revisions were proposed to SSAP No. 103R disclosures, the primary changes from the original agenda item were reflected in the data capture template, which include instructions, updated capture fields, and column descriptions.

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Virtual Meeting

(in lieu of meeting at the 2021 Summer National Meeting)

BLANKS (E) WORKING GROUP

Thursday, July 22, 2021

10:30 – 11:30 a.m. ET / 9:30 – 10:30 a.m. CT / 8:30 – 9:30 a.m. MT / 7:30 – 8:30 a.m. PT

Meeting Summary Report

The Blanks (E) Working Group met July 22, 2021. During this meeting, the Working Group:

1. Adopted its May 26, 2021, minutes, which included the following action:
 - a. Adopted eight blanks proposals: 1) 2021-01 – add reference to health care receivables line in the Asset page; 2) 2021-02BWG – add questions to the General Interrogatories, Part 1 regarding depository institution holding companies as it pertains to the group capital calculation (GCC); 3) 2021-03BWG – add category lines to the Separate Accounts General Interrogatories for additional granularity; 4) 2021-04BWG – add a General Interrogatory to identify insurers that utilize third parties to pay agent commissions in which the amounts advanced by the third parties are not settled in full within 90 days; 5) 2021-05BWG – modify Note 17B(4) to reflect changes made by the Statutory Accounting Principles (E) Working Group reference number SAPWG 2021-03 regarding transferred assets; 6) 2021-06BWG – add crosschecks to the long-term care (LTC) reporting forms to gain consistency; 7) 2021-07BWG – add additional line categories to capture collateral type data for all residential mortgage-backed securities (RMBS), commercial mortgage-backed securities (CMBS), and loan-backed and structured securities (LBSS) regardless of reporting category; and 8) 2021-08BWG - add a new supplement Mortgage Guaranty insurance Exhibit to capture more information from mortgage guaranty insurers.
 - b. Adopted its editorial listing.
 - c. Exposed five proposals for public comment.
2. Adopted the following proposal:
 - a. 2021-10BWG – remove language in quarterly General Interrogatories Part 1, line 4.1 that requires filing of a quarterly merger/history form. The annual form shall still be required.
3. Adopted its editorial listing.
4. Adopted Health Actuarial Statement of Opinion Guidance for the 2021 Reporting Year.
5. Deferred four proposals for additional discussion for a 90-day public comment period ending Oct. 22.

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2022 PROPOSED CHARGES
ACCOUNTING PRACTICES AND PROCEDURES (E) TASK FORCE

The mission of the Accounting Practices and Procedures (E) Task Force is to identify, investigate and develop solutions to accounting problems with the ultimate goal of guiding insurers in properly accounting for various aspects of their operations; modify the *Accounting Practices and Procedures Manual* (AP&P Manual) to reflect changes necessitated by Task Force action; and study innovative insurer accounting practices that affect the ability of state insurance regulators to determine the true financial condition of insurers.

Ongoing Support of NAIC Programs, Products or Services

1. The **Accounting Practices and Procedures (E) Task Force** will:
 - A. Oversee the activities of the Blanks (E) Working Group and the Statutory Accounting Principles (E) Working Group.
2. The **Blanks (E) Working Group** will:
 - A. Consider improvements and revisions to the various annual/quarterly statement blanks to:
 1. Conform these blanks to changes made in other areas of the NAIC to promote uniformity in reporting of financial information by insurers.
 2. Develop reporting formats for other entities subject to the jurisdiction of state insurance departments.
 3. Conform the various NAIC blanks and instructions to adopted NAIC policy.
 4. Oversee the development of additional reporting formats within the existing annual financial statements as needs are identified.
 - B. Continue to monitor state filing checklists to maintain current filing requirements.
 - C. Continue to monitor and improve the quality of financial data filed by insurance companies by recommending improved or additional language for the *Annual Statement Instructions*.
 - D. Continue to monitor and review all proposals necessary for the implementation of statutory accounting guidance to ensure proper implementation of any action taken by the Accounting Practices and Procedures (E) Task Force affecting annual financial statements and/or instructions.
 - E. Continue to coordinate with other task forces of the NAIC to ensure proper implementation of reporting and instructions changes as proposed by these task forces.
 - F. Coordinate with the Life Actuarial (A) Task Force to use any special reports developed and avoid duplication of reporting.
 - G. Review requests for investment schedule blanks and instructions changes in connection with the work being performed by the Capital Adequacy (E) Task Force and its working groups.
 - H. Review changes requested by the Valuation of Securities (E) Task Force relating to its work on other invested assets reporting for technical consistency within the investment reporting schedules and instructions.
3. The **Statutory Accounting Principles (E) Working Group** will:
 - A. Maintain codified statutory accounting principles by providing periodic updates to the guidance that address new statutory issues and new generally accepted accounting principles (GAAP) pronouncements. Provide authoritative responses to questions of application and clarifications for existing statutory accounting principles. Report all actions and provide updates to the Accounting Practices and Procedures (E) Task Force.
 - B. At the discretion of the Working Group chair, develop comments on exposed GAAP and International Financial Reporting Standards (IFRS) pronouncements affecting financial accounting and reporting. Any comments are subject to review and approval by the chairs of the Accounting Practices and Procedures (E) Task Force and the Financial Condition (E) Committee.
 - C. Coordinate with the Life Actuarial (A) Task Force on changes to the AP&P Manual related to the *Valuation Manual* VM-A, Requirements, and VM-C, Actuarial Guidelines, as well as other *Valuation Manual* requirements. This process will include the receipt of periodic reports on changes to the *Valuation Manual* on items that require coordination.
 - D. Obtain, analyze and review information on permitted practices, prescribed practices or other accounting treatments suggesting that issues or trends occurring within the industry may compromise the consistency and uniformity of statutory accounting, including, but not limited to, activities conducted by insurers for which there is currently no statutory accounting guidance or where the states have prescribed statutory accounting that differs from the guidance issued by the NAIC. Use this information to consider possible changes to statutory accounting.

Appendix G

Implementation Guide (Guide)

for the

Annual Financial Reporting Model Regulation (Model)

Introduction

The new requirements within the Annual Financial Reporting Model Regulation related to auditor independence, corporate governance and internal control over financial reporting became effective in 2010. The Implementation Guide is being published to assist companies in planning and preparing for compliance with the new requirements.

The Implementation Guide (Guide) is intended to supplement the Model, not to create additional requirements, by providing interpretive guidance and clarifying the meaning of terms used in the Model. Such guidance is important to ensure common understanding between insurers and regulators and to memorialize the intent of the changes. Because issues and questions will occur from time-to-time, by placing the Guide outside of the Model, maintenance can be achieved in a cost effective way without reopening the Model especially when the issue under consideration is an interpretation of the requirements. The Guide should not be viewed as a requirement of complying with the *Accounting Practices and Procedures Manual*.

Maintaining the Guide

The responsibility of developing and maintaining the Guide resides with the NAIC/AICPA (E) Working Group with changes to the Guide following the NAIC regulatory due process. The Guide resides as an informational appendix to the NAIC *Accounting Practices & Procedures Manual* (AP&P Manual). The AP&P Manual was selected as the logical repository since the Guide provides instruction about compliance with the Model, which directly relates to financial reporting and statutory accounting.

The regulatory due process for modifying this Guide requires the NAIC/AICPA (E) Working Group to send adopted proposals to the Accounting Practices and Procedures (E) Task Force for adoption and inclusion in the AP&P Manual. If the Accounting Practices and Procedures (E) Task Force recommends substantive changes to the proposal received from the NAIC/AICPA (E) Working Group, the proposal should be returned to the NAIC/AICPA (E) Working Group for further deliberation.

Table of Contents

The Table of Contents for the Guide mirrors that of the Model. However, not all sections of the Model require interpretive guidance. Consequently, only those sections containing guidance are contained in the Guide. The presentation of the Guide is organized by the Section Title with the Section number of the Model appearing after the title.

Title	Section	Page
Definitions	3	2
General Requirements Related to Filing and Extensions for Filing of Annual Audited Financial Reports and Audit Committee Appointment	4	4
Qualifications of Independent Certified Public Accountant	7	4
Communication of Internal Control Related Matters Noted in an Audit	11	10
Requirements for Audit Committees	14	11
Management's Report of Internal Control over Financial Reporting	17	13
Exemptions and Effective Dates	18	18
Appendix 1	17	22

Definitions (Section 3)

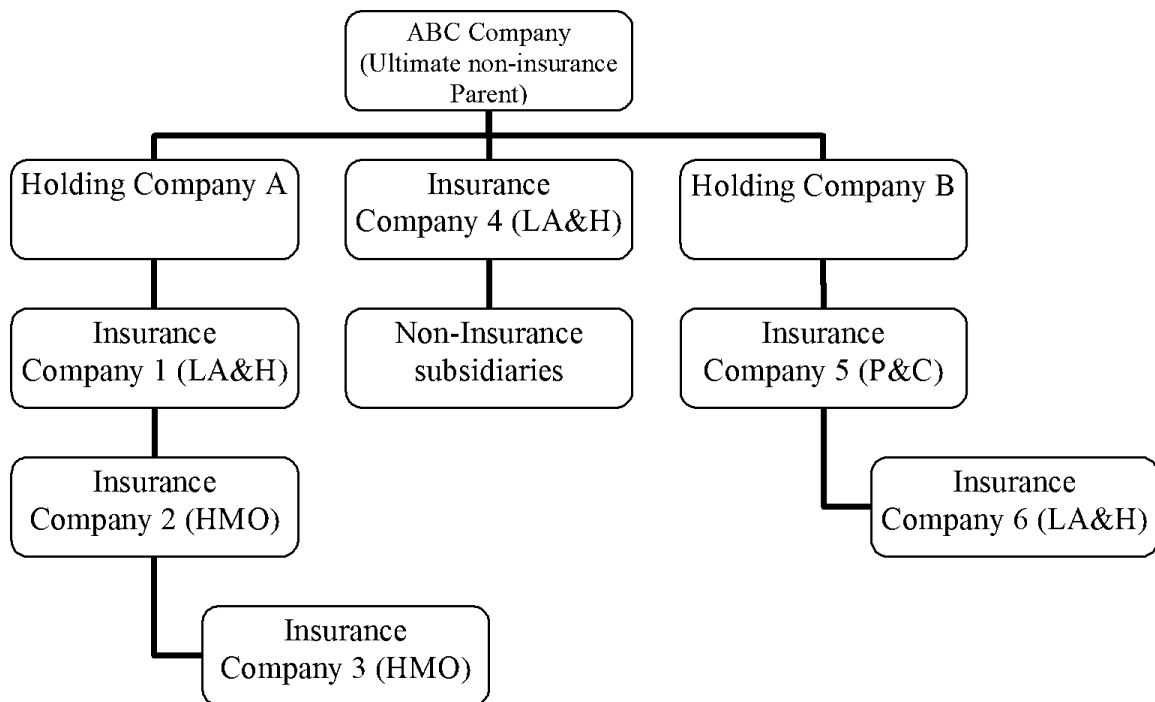
Certain terms and definitions contained in the Model need no further explanation. The Guide provides additional information for preparers and users for some definitions to facilitate their understanding.

“Audited financial report” (D), differs from the term “financial statements” in that the Audited financial report (see Section 5 of the Model) includes the financial statements plus the report of the independent certified public accountant. “Financial statements,” therefore, excludes the report of the independent certified public accountant.

“Group of insurers” (H), as intended for use in the Model is to recognize the variety of structures that may exist. Companies within a holding company structure, or other set of insurers identified by management, may often share common management, systems or processes. Consequently, when management asserts to the effectiveness of their internal controls, it is appropriate to make such an assertion for those companies based upon the organization management determines to be most relevant to meet the reporting requirements. Because holding company structures, and other groups of insurers, can be complex and organized to meet corporate objectives, that structure may not align with the organizations that are responsible for managing and preparing the financial statements of the insurer. The Model provides flexibility to insurers to identify a “Group of insurers” for purposes of evaluating the effectiveness of their internal control over financial reporting. In determining the appropriate scope and level of testing for systems that are shared by a group of insurers, management is not required to expand the scope or perform additional testing that would be redundant for each legal entity included within the group of insurers. To the extent that a specific internal control or system is unique to and has a material impact on the preparation of the audited statutory financial statements of a legal entity included in a group of insurers and the legal entity exceeds the premium thresholds contained in Section 17, that control or system is to be included in management's evaluation of internal controls.

A “Group of insurers” that has been granted approval to file audited statutory consolidated or combined financial statements of a group of insurers (as described in Section 8) may set the scope and level of testing for purposes of determining effectiveness of internal controls over financial reporting consistent with the basis on which the audited statutory financial statements for the Group are prepared (i.e., at the combined or consolidated level).

The following example is intended to illustrate various ways that a “Group of insurers” could be determined. The example is not intended to be limiting in any way. Rather, it is intended to show the flexibility to be in compliance with the Model. Insurers are encouraged to notify the Commissioner of its initial “Group of insurers” and any subsequent changes to such group.



1. “Group of insurers” could be established at the ultimate parent level, i.e., one report of the effectiveness of internal controls for all insurers in the group—insurance companies 1-6.
2. Two “Group of insurers” could be established at the holding company level, i.e., holding company A and B. In this case, a separate report would be required for holding company A, holding company B, and if it met the reporting threshold, insurance company 4 since it is not in either group.
3. Two “Group of insurers” could be established based upon the type of insurance company, i.e., LA&H companies 1, 4 and 6 could be one group and HMO companies 2 and 3 in the second group. In this case, a separate report would be required for the LA&H companies, the HMO companies and if it met the reporting threshold, insurance company 5 since it is not in either group.
4. Two “Group of insurers” could be established based upon the way the entities are managed. For example, companies, 1, 2, 3 and 5 have the same management while companies 4 and 6 have common management.

5. If management elects not to identify a “Group of insurers” for purposes of evaluating the effectiveness of internal control over financial reporting then each reporting entity meeting the reporting requirements of Section 17 would prepare such a report.

“Internal control over financial reporting” (I), as defined in the Model is intended to have the same meaning as understood in the public sector to comply with the requirements of the Sarbanes-Oxley Act of 2002. Because some terms might not be fully defined and to avoid misunderstanding, this Guide attempts to clarify such terms. For example, the word “reliability” used in the phrase “reliability of financial statements” has the same meaning as that contained in the generally accepted accounting principles (GAAP) framework, Statement of Financial Accounting Concepts Two. This Statement is referenced in the Preamble, Part III, paragraph 24 of the AP&P Manual.

General Requirements Related to Filing and Extensions for Filing of Annual Audited Financial Reports and Audit Committee Appointment (Section 4)

Section 4D stipulates that each insurer required to file an annual Audited financial report pursuant to the Model shall designate a group of individuals as constituting its Audit committee. Section 4D further states that the Audit committee of an entity that controls an insurer may be deemed to be the insurer’s Audit committee for purposes of this regulation at the election of the controlling person. The definition of Audit committee in Section 3 of the Model references Section 14E for exercising this election. However, a disclaimer within Section 14 of the Model indicates that the section shall not apply to SOX Compliant Entities or wholly-owned subsidiaries of SOX Compliant Entities. Regardless of the disclaimer, in order to comply with the second sentence in Section 4D, the Audit committee of any entity that controls an insurer (a SOX Compliant entity or a non-SOX Compliant Entity) may be deemed to be the insurer’s Audit committee at the election of the controlling person, and only if such election is completed in the manner outlined in Section 14E.

The responsibility of the Audit committee is defined in Section 14 of the Model. Section 14 states that each member of the Audit committee shall be a member of the Board of Directors and sets forth the requirements for the proportion of independent Audit committee members based on the insurer’s direct written and assumed premiums. The definition of an independent Audit committee member is outlined in Section 14.

Qualifications of Independent Certified Public Accountant (Section 7)

Lead Audit Partner Rotation Requirement (Section 7D)

Purpose

The purpose of this section is to provide companies and their independent accountants with guidance to enable an orderly transition in meeting the revised lead audit partner rotation requirements as set forth in Section 7.

Background

Section 7 provides certain limitations on the number of years an audit partner may serve in the capacity of lead audit partner for an insurance company audit. Previously, the lead audit partner was permitted to serve for seven consecutive years in that capacity with a two year break in service. Under the revised Model “...the lead ...audit partner (having primary responsibility for the audit) may not act in that capacity for more than five (5) consecutive years. The person shall be disqualified from acting in that or a similar capacity for the same company or its insurance subsidiaries or affiliates for a period of five (5) consecutive years.”

The new rotation requirements under Section 7 are effective beginning with audits of the 2010 financial statements. The rotation requirements of the Model and the interpretative guidance provided are applicable for statutory reporting and regulatory purposes. An insurer and its affiliates that are subject to the rotation requirements of the Securities and Exchange Commission (SEC) and Public Company Accounting Oversight Board (PCAOB) must also continue to comply with those rotation requirements.

Relief from the Lead Audit Partner Rotation Requirement (Section 7D)

The Model states:

An insurer may make application to the Commissioner for relief from the above rotation requirement on the basis of unusual circumstances. This application should be made at least thirty (30) days before the end of the calendar year. The Commissioner may consider the following factors in determining if the relief should be granted:

- (a) Number of partners, expertise of the partners or the number of insurance clients in the currently registered firm;
- (b) Premium volume of the insurer; or
- (c) Number of jurisdictions in which the insurer transacts business.

The following examples illustrate circumstances that the Commissioner may consider in determining if relief from the lead partner rotation requirement shall be granted:

1. No other partners in the firm's local office have the qualifications to serve as lead audit partner and the use of a qualified partner resident in another location could result in increased audit risk and higher audit fees.
2. Limited number of partners in the firm that have the qualifications to serve as the lead audit partner.
3. Switching firms could result in increased audit risk due to the new engagement team's lack of familiarity with the insurer.
4. Limited availability of other firms in a particular location with the requisite expertise.
5. The regulator believes that complex issues at an insurer make a particular partner best suited to continue as lead audit partner
6. Short-term relief due to the occurrence of an unforeseeable event that renders a partner unable to continue as the lead audit partner on the engagement.
7. Short-term relief due to unexpected delays in the state's licensing or admission process that prevent the "new" lead audit partner from assuming that role.

Also, the granting of transitional relief may be warranted when the non-insurance parent or ultimate parent of an insurance company is an SEC registrant and the current lead audit partner on the SEC registrant has completed his or her rotation as the lead audit partner on insurance subsidiaries prior to completing his or her five-year rotation as the lead partner on the audit of the GAAP financial statements of the SEC registrant. In this situation the relief would allow the lead audit partner to complete his or her rotation on the SEC registrant as long as he or she no longer acts in the capacity of lead audit partner for any insurance subsidiaries and/or any downstream affiliates of the insurance subsidiaries.

Frequently Asked Questions (Section 7D)

Following are a series of frequently asked questions to assist companies and their independent accountants in interpreting this guidance. Dates provided refer to the year of financial statements under audit.

In determining when the lead audit partner must rotate, consecutive time served in the capacity of lead audit partner prior to the effective date of these rules would be counted (i.e., the lead audit partner is not afforded a “fresh start”). If the lead audit partner completed the two year break in service required by the previous version of the Model prior to the effective date of these rules, the partner is eligible to resume service as a lead audit partner for a five year period and need not wait additional years to accomplish a five year break in service.

1. 2010 would be the fifth year that a partner would serve as lead audit partner of an insurance company. Would that partner be able to complete the 2010 year-end audit?

Yes. The partner would be able to complete the 2010 year-end audit; however, the partner would be required to rotate off the engagement after the 2010 year-end audit.

2. 2010 would be the sixth or seventh year that a partner would serve as the lead audit partner. Would that partner be able to serve in that capacity for the 2010 audit?

No. The partner would be required to rotate off for the 2010 year-end audit. In determining when the lead audit partner must rotate, consecutive time served in the capacity of lead audit partner since the most recent two year break in service prior to the effective date of these rules would be counted.

3. If a partner serves as the concurring partner from 2007 – 2010, can that partner serve as the lead audit partner in 2011? If so, for how many years?

Yes. The Model does not prohibit a partner that has served as the concurring partner from subsequently serving as the lead audit partner. The time served as concurring partner does not count towards the five year limitation. In the situation above, the partner would be permitted to serve as lead audit partner from the 2011 year-end audit through the 2015 year-end audit.

4. Can a lead audit partner serve as the concurring review partner during the required five year break in service?

Yes. The Model specifies that a partner may not act in “that or a similar capacity for the same company or its insurance subsidiaries or affiliates for a period of five (5) consecutive years” where “that” refers to the role of lead audit partner. Therefore, the Model does not prohibit that partner from serving as concurring partner during that partner’s five year break in service.

5. During the five-year break in service, can a partner serve as lead audit partner on an insurance company affiliate of that company?

No. The Model specifies a “person shall be disqualified from acting in that or a similar capacity for the same company or its insurance subsidiaries or affiliates for a period of five (5) consecutive years.” The phrase “insurance subsidiaries or affiliates” is interpreted to mean any subsidiaries and affiliates (whether insurance or non insurance).

6. If a lead audit partner serves for six years prior to the effective date of the revised Model (year-end audits from 2003 – 2008) then rotates off the engagement for two years (year-end audits 2009

– 2010), can that partner serve for five additional consecutive years (year-end audits from 2011 – 2015) as the lead audit partner?

No. The requirement for a break in service of five consecutive years becomes effective for the 2010 year-end audits. If the partner has not completed the two-year break in service prior to the effective date of the new requirement, the partner becomes subject to the new requirement and must complete a five-year break in service. However, if the lead audit partner completes the two year break in service by 2009 instead of 2010, that partner would be permitted to resume the lead audit partner role in 2010.

7. A partner that served seven years as lead audit partner has not worked on the engagement for two years. Assuming 2010 otherwise would be year three of the break in service, can that partner assume the lead audit partner role for the 2010 year-end audit?

Yes. The requirement for the five year break in service starts with engagement years beginning 2010. Prior to 2010, the rotation requirement is for a two year break in service.

8. If a lead audit partner served in that capacity for years 2007 – 2009 and was not on the engagement (or that of any subsidiary or affiliate) for 2010, would that partner have to complete a five year break in service before again serving as the lead audit partner?

No. However, the partner could only serve as the lead audit partner for two more years since the partner has already served three years on this engagement.

9. Can a former lead audit partner currently in a break in service continue to serve the client in a role other than the lead audit partner, for example concurring partner or auxiliary partner, such as tax review partner or other assisting role?

Yes. The Model auditor rotation rules apply only to the role of lead audit partner on the audit of the insurance company and its insurance subsidiaries or affiliates.

10. 2010 is the first year that a partner serves as the lead audit partner on an insurer. The partner serves as the lead audit partner on that insurer for year-end audits of 2010 – 2012; however, during 2013 – 2015 that partner does not serve as the lead audit partner on that insurer or any of its affiliates. If that partner again serves the insurer (or any of its insurance subsidiaries or affiliates) as the lead audit partner for 2016 year-end audit, when must that partner rotate off the engagement?

The partner is permitted to serve as the lead audit partner for the 2016 and 2017 year-end audits and must begin a five-year break in service with the year-end 2018 audit. The break in service during 2013 – 2015 would be for less than the five-year period required by the Model. In order for the partner to be permitted to begin a new five-year service period as lead audit partner on the insurer or any of its insurance subsidiaries or affiliates, a full five-year break in service is required to be completed by that partner.

11. How is service as the lead audit partner on the audit of the GAAP-basis financial statements of a separate account evaluated under the Model?

A separate account is not a legal entity, but an accounting entity with accounting records for variable contract assets, liabilities, income, and expenses segregated as a discrete operation within the insurance company. Therefore, the separate account is considered to be an insurance affiliate for purposes of applying the Model.

If the insurer is a part of a mutual fund complex, the mutual funds are considered to be non insurance affiliates even if held as investments in the insurer's separate accounts.

12. An insurer changes to a new independent accounting firm. At the same time, the lead audit partner for that insurer joins the new independent accounting firm. Would the lead audit partner's time at the previous accounting firm count toward the five year rule at the new accounting firm?

Yes. The rule specifically applies to the lead audit partner and not the independent accounting firm.

13. Some firms have individuals that are CPAs but not partners (i.e., nonequity participants such as directors or principals) that serve in the role of the lead audit partner. Can such a CPA serve in the role of the lead audit partner of an insurance company?

Yes. The Model defines the lead audit partner as the individual having "primary responsibility for the audit." Whether this capacity is served by a partner or other CPA with the equivalent qualifications is at the discretion of the independent accounting firm. As such, the individual would be subject to the rotation requirements of the lead audit partner under Section 7.

Questions 14 through 23 are based on the following hypothetical fact pattern and assume there are no public registrants in the group.

Neither insurance subsidiary A nor insurance subsidiary B has any investment in non insurance subsidiary C.

- Partner Smith served as the lead audit partner on non insurance holding company H for six years through the 2010 year-end audit.
- Partner Jones served as the lead audit partner on insurance subsidiary A for four years through the 2010 year-end audit.
- Partner Little served as the lead audit partner on insurance subsidiary B for three years through the 2010 year-end audit.
- Partner Brown served as the lead audit partner on non insurance subsidiary C for two years through the 2010 year-end audit.
- Partner Miller served as the lead audit partner on insurance subsidiary D for three years through the 2010 year-end audit.
- Partner King served as the lead audit partner on non insurance subsidiary E for seven years through the 2010 year-end audit.

14. Can Partner Smith rotate from serving as the lead audit partner on non insurance holding company H to serving as the lead audit partner on insurance subsidiary B for the 2011 year-end audit?

Yes. The limitation under Section 7 initiates with service as the lead audit partner of an *insurer*. Assuming Partner Smith has not previously served as the lead audit partner on an insurer, he or she can then serve as the lead audit partner on insurance subsidiary B or any of its affiliates for up to five years.

15. Can Partner King rotate from serving as the lead audit partner on non insurance subsidiary E to serving as the lead audit partner on insurance subsidiary B for the 2011 year-end audit?

Yes. The limitation initiates with service as the lead audit partner of an *insurer*. Assuming Partner King has not previously served as the lead audit partner on an insurer, he or she can then serve as the lead audit partner on insurance subsidiary B or any of its affiliates for up to five years.

16. Can Partner Brown rotate from serving as the lead audit partner on non insurance subsidiary C to serving as lead audit partner on insurance subsidiary B for the 2011 year-end audit?

Yes. The limitation initiates with service as the lead audit partner of an *insurer*. Assuming Partner Brown has not previously served as the lead audit partner on an insurer, he or she can then serve as the lead audit partner on insurance subsidiary B or any of its affiliates for up to five years. Therefore, Brown could serve insurance subsidiary B for five years beginning with the 2011 year-end audit.

17. Can Partner Brown rotate from serving as the lead audit partner on non insurance subsidiary C to serving as lead audit partner on Holding Company H for the 2011 year-end audit?

Yes. C is a non insurance subsidiary and H is a non insurance holding company; therefore, assuming Partner Brown has not previously served as the lead audit partner on an insurer, the partner rotation requirements of Section 7 are not applicable relative to non insurance subsidiary C and non insurance holding company H.

18. Can Partner Jones rotate from serving as the lead audit partner on insurance subsidiary A to serving as the lead audit partner for insurance subsidiary B for the 2011 year-end audit?

Yes. However, Jones can only serve for one year due to four years prior service as the lead audit partner on insurance subsidiary A (an insurance affiliate).

19. Can Partner Jones rotate from serving as the lead audit partner on insurance subsidiary A to serving as the lead audit partner on non insurance subsidiary C for the 2011 year-end audit?

Yes. However, Jones can only serve for one year due to four years prior service as the lead audit partner on insurance subsidiary A (an insurance affiliate). The limitation initiates with serving as the lead audit partner on an insurer.

20. Can Partner King rotate from serving as the lead audit partner on non insurance subsidiary E to serving as the lead audit partner on non insurance subsidiary C for the 2011 year-end audit?

Yes. E is a non insurance subsidiary and C is a non insurance subsidiary; therefore, assuming Partner King has not previously served as the lead audit partner on an insurer, the partner rotation requirements of Section 7 are not applicable relative to non insurance subsidiary E and non insurance subsidiary C.

21. Can Partner Jones rotate from serving as the lead audit partner on insurance subsidiary A to serving as the lead audit partner on non insurance subsidiary E for the 2011 year-end audit?

Yes. However, Jones can only serve for one year due to four years prior service as the lead audit partner on insurance subsidiary A (an insurance affiliate). The limitation initiates with serving as the lead audit partner on an insurer.

22. Can Partner Jones rotate from serving as the lead audit partner on insurance subsidiary A to serving as the lead audit partner on insurance subsidiary D for the 2011 year-end audit?

Yes. However, Jones can only serve for one year due to four years prior service as the lead audit partner on insurance subsidiary A (an insurance affiliate). The limitation initiates with serving as the lead audit partner on an insurer.

23. Can Partner Little rotate from serving as the lead audit partner on insurance subsidiary B to serving as the lead audit partner on non insurance subsidiary E for the 2011 year-end audit?

Yes. However, Little can only serve for two years due to three years prior service as the lead audit partner on insurance subsidiary B (an insurance affiliate). The limitation initiates with serving as the lead audit partner on an insurer.

Prohibited Services (Section 7 G)

The Model does not allow the Commissioner to accept an Audited financial report prepared by an accountant who provides the insurer, contemporaneously with the audit, non-audit services as outlined within the Model. One of the prohibited services outlined in the Model consists of bookkeeping or other services related to the accounting records or financial statements of the insurer. The prohibition in this area should include, but is not limited to, services related to the preparation of the Annual Statement to be submitted by the insurer. However, the drafting of the Audited financial report would not be prohibited, provided that the accountant does not assume decision-making authority (e.g., approval of journal entries) in compiling the draft report.

Communication of Internal Control Related Matters Noted in an Audit (Section 11)

In addition to the annual Audited financial report, each insurer must furnish the Commissioner with a written communication as to any unremediated material weakness in its internal control over financial reporting noted during the audit. The communication is prepared by the accountant within 60 days after the filing of the annual Audited financial report and is filed by the insurer. Recognizing it may not always be practical, insurers are encouraged to file the communication concurrently with the filing of the annual Audited financial report for those years in which the insurer is aware that a financial condition examination has been scheduled. The insurer is required to provide a description of remedial actions taken or proposed to correct unremediated material weaknesses, if the actions are not described in the accountant's communication.

The Model requires that the Commissioner be notified when unremediated material weaknesses in internal control over financial reporting were noted during the audit. Previous versions of the Model required such communication when any significant deficiencies in internal control over financial reporting were noted during the audit, whether remediated or not. This distinction is important because of the level of severity of the internal control deficiency that is applicable to each term. The terms "material weakness" and "significant deficiency" have the same meaning respectively as used in PCAOB or American Institute of Certified Public Accountants (AICPA) auditing literature - PCAOB Auditing Standard No. 5, An Audit of Internal Control over Financial Reporting That is Integrated With an Audit of Financial Statements or AICPA AU Section 325, Communicating Internal Control Matters Identified in an Audit (see Section 17E of this Guide for the definitions of material weakness and significant deficiency that are included in the auditing literature). However, the insurer is expected to maintain information about significant deficiencies that were communicated by its auditors and such information should be available for review during the financial condition examination.

Effective for audits as of 12/31/21 and thereafter, the information required in Section 12 of the MAR required to be communicated by the accountant should be supplemented by providing both the name of the current lead audit partner and the year at which he or she began serving in that capacity. For the purpose of maintaining confidentiality, this information will not be included in the annual letter of

qualifications, but instead shall be included in the internal control communication required in Section 11 of the MAR by the accountant as a footer or under the firm signature as follows:

The engagement partner, [name], has served in that capacity with respect to the Company since [year that current term started].

Consistent with the Drafting Note¹ to Section 11 of the MAR, the information provided on the engagement partner shall remain confidential.

The following is an example of the type of communication that an insurer should prepare to communicate the remedial actions taken or proposed to correct a material weakness in its internal control over financial reporting noted during an audit.

Communication of Internal Control Related Matter Noted in an Audit - Sample

Honorable Commissioner
State of Domicile Insurance Department
State of Domicile

Dear Honorable Commissioner:

During the audit completed for the year ended December 31, 20XX, for XYZ Holding Company Inc (“XYZ”), a material weakness was noted in XYZ’s internal control over financial reporting related to the calculation of insurance reserves. Due to the manner in which the data for homeowners policies are captured by the systems used in its Southeastern US regional office, changes in XYZ’s estimate of insurance reserves for certain policies are not reviewed by XYZ’s Actuarial Department prior to being recorded in the company’s accounting records.

A material weakness is a deficiency or a combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the entity’s financial statements will not be prevented, or detected and corrected on a timely basis. In connection with the weakness noted above, XYZ’s management has taken remedial actions to change its procedures for coding policies issued in the states affected so that all homeowners’ policy data are included in the Actuarial Department review of estimate of insurance reserves. This change was effective on July 1, 20XX.

Should you have any questions regarding this matter, please do not hesitate to contact me at the number noted above.

Regards,

XYZ Holding Company, Inc.

Requirements for Audit Committees (Section 14)

A disclaimer within Section 14 of the Model indicates that the section shall not apply to SOX Compliant Entities or wholly-owned subsidiaries of SOX Compliant Entities. This disclaimer was placed within the Model to avoid conflicts between the independence requirements of the Model and those required of public companies under Section 301 of the Sarbanes Oxley Act of 2002. The expectation of regulators in

¹ The insurer is expected to maintain information about significant deficiencies communicated by the independent certified public accountant. Such information should be made available to the examiner conducting a financial condition examination for review and kept in such a manner as to remain confidential.

developing this disclaimer was that the same independent Audit committee required of public companies under Section 301 would be deemed to be the insurer's Audit committee for purposes of this regulation (pursuant to Section 4D of the Model) or would participate in the oversight of the insurers within the group. Therefore, if material weaknesses, significant deficiencies and/or significant solvency concerns are identified at the legal entity level, the independent Audit committee should be involved in addressing these issues, regardless of their materiality at the consolidated, parent company level.

Independence of an Audit Committee Member (Section 14C)

A policyholder would be considered "independent" unless they receive direct compensation from the insurer for other unrelated services.

A person who is otherwise considered independent and also serves on the Board of Directors of a contracting entity (e.g., medical provider, vendors, banks, etc.) is considered independent.

An otherwise non-independent member of the Board of Directors is considered independent for Audit committee purposes if state law requires participation on the Board (e.g., Medical providers) as long as the member is not an officer or employee of the insurer or one of its affiliates.

Notification letter (Section 14E)

In accordance with Section 14E, upon the initial election by the insurer to designate the Audit committee of an entity that controls the insurer as its Audit committee, the insurer shall provide written notification to the Commissioner of the affected insurer. This notification shall identify the controlling entity and the basis for the election. This election remains in effect for perpetuity, until rescinded, at which time written notification would need to be provided to the Commissioner of the insurer. The notification letter should be timely filed with the Commissioner by the ultimate controlling person prior to the issuance of the statutory Audited financial report. However, each of the affected insurers (i.e. those that will have an Audit committee designated by its ultimate controlling person) that is subject to the provisions of Section 14 shall ensure that the notification letter is filed with the Commissioner. Absence such filing, each of the affected insurers would be individually responsible for complying with Section 14. For example, referring to the "Group of insurers" chart in Section 3, if the ABC Company is the ultimate controlling person and elects to have its Audit committee serve as the Audit committee for insurance company 5, then ABC Company would file the notification letter (insurance company 5 would have to ensure that the notification letter is filed or comply with Section 14 as a single entity). Once submitted, the election remains in effect until rescinded. The following example illustrates the reporting requirement.

The XYZ insurance company (e.g., insurance company 5) is an indirect subsidiary of and controlled by ABC Company. ABC Company has an independent Audit committee comprised of directors of ABC Company. XYZ insurance Company has elected to designate the Audit committee of ABC Company as the Audit committee of XYZ insurance Company for purposes of complying with Audit committee requirements of the Annual Financial Reporting Model Regulation.

(Signed) _____ (Date) _____
 (XYZ Insurance Company Chief Executive Officer)

(Signed) _____ (Date) _____
 (ABC Company Chief Executive Officer)

Transitional Guidance (Section 14G)

Once a company exceeds the requisite thresholds for Audit committee requirements contained in Section 14 of the Model, it is required to comply with the Audit committee requirements by January 1 following one (1) complete calendar year. The following are examples of transitional period requirements.

A: Company surpasses \$300 million threshold:

ABC Insurance Company has reached the \$300 million requisite threshold in its December 31, 2011 audited statutory statement and therefore will be required to meet “majority (50% or more) member independence” Audit committee requirements by January 1, 2013, providing the company necessary time for recruitment and approvals.

B: Company surpasses \$500 million threshold:

ABC Insurance Company has subsequently reached the \$500 million requisite threshold in its December 31, 2014 audited statutory statement and therefore will be required to meet the “Supermajority (75% or more) member independence” Audit committee requirements by January 1, 2016.

C: Company drops below threshold amount:

If ABC Insurance Company has penetrated the requisite \$500 million threshold and has been in compliance with the requirements but subsequently drops below the \$500 million threshold, e.g., \$450 million in its December 31, 2018 audited statutory statements, the company would be subject to the “majority (50% or more) member independence” requirement and could reduce the Audit committee independence in 2019. Companies, however, are encouraged to structure their Audit committees with at least a supermajority of independent Audit committee members.

Hardship Waiver (Section 14H)

An insurer may make application to the Commissioner for a waiver from the Section 14 requirements based upon hardship. Examples may include, but are not limited to, requests based on the business type of the entity, the availability of qualified board members, or the ownership (e.g., entities owned by non-profit health systems) or organizational structure of the entity. If the application for a waiver is approved, the insurer would file, with its annual statement filing, the approval for relief from Section 14 with the states that it is licensed in or doing business in and the NAIC. If the nondomestic state accepts electronic filing with the NAIC, the insurer would file the approval in an electronic format acceptable to the NAIC.

Management’s Report of Internal Control over Financial Reporting (Section 17)

Premium Threshold (Section 17A)

The term “direct written premium” is frequently associated with the property/casualty business. While the Model continues to use the term, it raises the question for other businesses, e.g., life and fraternal, what is the appropriate measure for assessing compliance? The following examples have been developed to illustrate the computation since the starting point is the audited financial statements of the reporting entity, and it is possible that the amount reported may not be consistent with written premium as reported in the regulatory reporting blank.

The annual direct written and assumed premium:

- ◆ will be derived from the annual Audited financial report of an individual insurer, as of December 31 immediately preceding
- ◆ are generally reported in the Statement of Operations of the Audited Financial Report on an ‘earned’ and a ‘net of reinsurance ceded’ basis
- ◆ will be computed by making the following adjustments:

P/C, Health and Title entities:

	\$
Premiums earned (Statement of Income in Audited financial report)	A
Add/Deduct: Change in unearned premium	B
Add: Reinsurance ceded	C
Direct written and assumed premium *	D=A+B+C

*Note: Direct written and assumed premium would be reduced by any premiums reinsured with the Federal Crop Insurance Corporation and Federal Flood Program

- A - Premiums earned per the Statement of Income will generally equal the Annual Statement, Page 4.
- B - Change in unearned premium is the difference between the current period amount and the prior year-end amount reported in the liabilities section of the balance sheet. The amount may also be derived from other company prepared exhibits.
- C - Reinsurance ceded may be derived from the notes to the Audited financial report, if disclosed, or other company prepared exhibits or schedules. If the Statement of Income or Statement of Operations separately presents reinsurance ceded, an adjustment is not required.
- D - Must be equal to, or greater than, \$500 million in order to be subject to Section 17 reporting.

Life and Fraternal entities:

	\$
Premiums earned (Statement of Operations in Audited financial report)	A
Add: Reinsurance ceded	B
Direct written and assumed premium	C=A+B

- A - Premiums earned per the Statement of Operations will generally equal the Annual Statement, Page 4.
- B - Reinsurance ceded may be derived from the notes to the Audited financial report, if disclosed, or other company prepared exhibits or schedules. If the Statement of Operations separately presents reinsurance ceded, an adjustment is not required.
- C - Must be equal to, or greater than, \$500 million in order to be subject to Section 17 reporting.

Companies in an RBC Level Event or in Hazardous Financial Condition (Section 17B)

For purposes of this subsection, the phrase “RBC level event” refers to any of the regulatory action levels described in the Risk-Based Capital requirements or the trend test. For example, if the reporting entity’s total adjusted capital is equal to or less than 200% of the required risk-based capital, the result would trigger regulatory action.

Management’s Report of Internal Control over Financial Reporting (Sections 17C & 17D)

Management must annually provide their domiciliary insurance department with a report on internal controls over the statutory financial statement process. Recognizing it may not always be practical,

insurers are encouraged to file the report concurrently with the filing of the annual Audited financial report for those years in which the insurer is aware that a financial condition examination has been scheduled. The elements to be included in the report are outlined in 17D.

As outlined in Section 17C, an addendum is required for all reports that rely on a Section 404 Report (Sarbanes-Oxley). The Model states that the Section 404 Report means management's report on internal control over financial reporting as defined by the SEC and the related attestation report of the independent certified public accountant. However, in 2010, the Dodd-Frank Act exempted non-accelerated SEC filers (those reporting companies that do not meet the definition of either an "accelerated filer" or a "large accelerated filer" under Exchange Act Rule 12b-2.) from the requirement to obtain the related attestation report of the independent certified public accountant. As such, non-accelerated SEC filers may file a Section 404 Report that does not include an attestation report of the independent certified public accountant, along with the appropriate addendum, to fulfill requirements in this area.

Alternately, insurers may utilize a report received as a result of work performed in accordance with Statement of Standards in Attestation Engagements (SSAE) No. 15 in a similar fashion to a Section 404 Report. As such, there are two main types of reports that can be provided:

- Reports from entities that have complied with all required elements of Section 404 of the Sarbanes-Oxley Act (or have received an SSAE No. 15 report) either as a requirement or on a voluntary basis.
- Reports from entities that have not complied with Section 404 of the Sarbanes-Oxley Act (or have not received an SSAE No. 15 report).

Appendix 1 of this guide provides examples of Management's Report of Internal Controls over Financial Reporting utilizing various facts and circumstances.

Section 17D(2): Management must make an assertion regarding the effectiveness of the insurer's Internal control over financial reporting to the best of its knowledge and belief after diligent inquiry. For purposes of filing the report, "diligent inquiry" means conducting a search and thorough review of relevant documents which are reasonably likely to contain significant information with regards to Internal control over financial reporting and making reasonable inquiries of current employees and agents whose duties include responsibility for Internal control over financial reporting.

Section 17D(5): The report must disclose any unremediated material weaknesses in Internal control over financial reporting that exist as of the balance sheet date. If the insurer or Group of insurers has identified an unremediated material weakness, management is not permitted to conclude that its Internal control over financial reporting is effective and it must include a description of the nature of any unremediated material weakness in the report. December 31 is used as the measurement date to whether a material control weakness is unremediated for purposes of reporting under this section of the Model.

Section 17D(6): Users of the report should be aware of the inherent limitations in Internal control over financial reporting. PCAOB Auditing Standard No. 5, An Audit of Internal Control over Financial Reporting That is Integrated With an Audit of Financial Statements provides the following description of such inherent limitations:

Internal control over financial reporting has inherent limitations. Internal control over financial reporting is a process that involves human diligence and compliance and is subject to lapses in judgment and breakdowns resulting from human failures. Internal control over financial reporting also can be circumvented by collusion or improper management override. Because of such limitations, there is a risk that material misstatements will not be prevented or detected on a timely basis by internal control over

financial reporting. However, these inherent limitations are known features of the financial reporting process. Therefore, it is possible to design into the process safeguards to reduce, though not eliminate, this risk.

Additionally, readers of the report should be aware that projecting management's assertion regarding the effectiveness of Internal control over financial reporting to future periods is subject to the risk that controls may become inadequate because of changes in conditions, or the degree of compliance with policies or procedures may deteriorate.

Section 17D(7): The report must include signatures of the chief executive officer and chief financial officer (or the equivalent position/title). If a report is being filed on behalf of a Group of insurers, management should identify the officeholders (i.e., the CEO and CFO of Company ABC) that have the authority to sign the report on behalf of the all of the legal entities being reported upon within the Group of insurers.

Basis for Management's Review and Assertions (Section 17E)

One of the primary reasons for the new Section 17 of the Model is to bring additional focus and attention to internal control over financial reporting. Financial reporting is the underpinning of many of the solvency oversight activities of insurance regulators. Section 17 of the Model identifies management's responsibilities for internal control over financial reporting and provides regulators additional assurances of the effectiveness of internal control practices in a cost effective manner.

The basis for Management's Report of Internal Control over Financial Reporting shall be subject to insurance departments' financial condition examinations. Because of this and other solvency tools available to regulators, there is no requirement that the independent certified public accountant be engaged to perform an examination of the effectiveness of internal control over financial reporting. However, Section 9 requires the independent public accountant to consider (as that term is defined in AICPA Statement on Auditing Standards (SAS) No. 102, Defining Professional Requirements in Statements on Auditing Standards, or its replacement) the most recently available Management's Report of Internal Control over Financial Reporting in planning and performing the audit of the statutory financial statements. SAS No. 102, paragraph 4 states, "If a SAS provides that a procedure or action is one that the auditor "should consider," the consideration of the procedure or action is presumptively required, whereas carrying out the procedure or action is not." AU Section 319 of the Professional Standards of the AICPA, Consideration of Internal Control in a Financial Statement Audit, requires that the auditor obtain an understanding of internal control sufficient to plan and execute the audit. It is in this context that the auditor is required to "consider" management's report. There is no requirement that the auditor test or otherwise use management's report.

The Model does not mandate a specific framework for management's review and evaluation of internal controls. SEC registrants typically (but are not required to) use the COSO Internal Control-Integrated Framework in assessing the effectiveness of internal control over financial reporting. The COSO-sponsored "Enterprise Risk Management-Integrated Framework" and the PCAOB Guidance for Smaller Public Companies Reporting on Internal Control over Financial Reporting are other examples of relevant literature companies may want to consider in applying such a framework. Under the Model, however, management, when making its assessment and preparing its report, has discretion as to the nature of the internal control framework used. Insurers shall have flexibility as to the frequency and scope of testing activities and the documentation provided upon examination to support the assertions. Management should assess and select an appropriate framework or approach based upon its business risks and objectives.

Management's assertions about the effectiveness of internal controls enhance oversight and understanding of insurer solvency by allowing regulators to have greater confidence in the accuracy of financial reporting, which also provides a benefit to policyholders and creditors. An expected benefit of this enhancement, where internal controls are effective, is that financial examinations will become more efficient and risk-focused.

Management's Report of Internal Control over Financial Reporting may span more than one legal entity. Because internal controls are primarily about processes and these processes are often applied across multiple legal entities within an organization, (e.g., investment systems, premium and loss/benefit systems, and financial reporting processes), management may consider common processes and the associated controls when determining the Group of insurers for reporting purposes.

The Model provides flexibility in meeting the requirements of Section 17D and E. The controls included in the scope of management's report should only include those controls deemed significant or critical by management. The following examples represent aspects and components of internal control that insurers may want to consider when making the assertions and determining relevant documentary evidence. These are not intended to serve as, and should not be considered, requirements:

- The internal control environment including oversight provided by the Audit committee of the Board of Directors. Insurers may want to consider how they can demonstrate "Tone at the Top." The insurer's compliance programs, code of conduct and the processes for reporting policy exceptions and overrides of controls may also be appropriate to consider.
- The risk assessment process utilized and identification of the areas of potential material internal control risk related to the financial statement. Risk areas that one might typically find for an insurance enterprise include:
 - Investments (including capital expenditures)
 - Policy and Claim Reserves
 - Benefit Payments
 - Premiums / Agent's Balances
 - Reinsurance
 - Related Party (Affiliate) Transactions
 - Operating Expenses/Taxes
- The control activities in place including procedures over financial reporting, which in management's judgment are appropriate under the circumstances. These might include the daily or monthly controls management relies upon in the normal course of its activities. They would also include any SAS 70 reports received from vendors upon which management relies. General information systems and technology controls might also be considered.
- The monitoring and testing processes used in the normal course of business to ascertain that the internal controls are in place and are working as intended. Insurers may want to consider describing the purpose, function or role of an internal audit department and/or describe other self-audit and analysis activities.
- The information and communication processes, including the frequency of reporting and monitoring activities and communication of internal control responsibilities.

Section 17D(5) of the Model indicates that if one or more unremediated material weaknesses in Internal control over financial reporting exists as of the balance sheet date, then management is not permitted to conclude that internal control over financial reporting is effective and it must include a description of the

nature of any unremediated material weaknesses in the report. For purposes of this determination, material weakness has the same meaning as used in PCAOB or AICPA auditing literature – PCAOB Auditing Standard No. 5, An Audit of Internal Control over Financial Reporting That is Integrated With an Audit of Financial Statements or AICPA AU Section 325, Communicating Internal Control Related Matters Identified in an Audit. Such guidance provides the following definitions:

Significant Deficiency – A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Material Weakness – A material weakness is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Insurers filing Management's Report of Internal Control over Financial Reporting as a Group of insurers may want to also consider identifying or documenting common systems and controls used by multiple companies within an insurance holding company system and how such information was used in the development of the Group of insurers for reporting purposes.

To allow insurers to comply with Section 17 in a cost effective manner, management may base its assertions, in part, upon its review, monitoring and testing processes performed in the normal course of its activities. Management may also consider diligent inquiry of key process owners throughout the organization to provide additional assurance as to the operating effectiveness of its internal control over financial reporting. For purposes of filing the report, "diligent inquiry" means conducting a search and thorough review of relevant documents which are reasonably likely to contain significant information with regards to Internal control over financial reporting and making reasonable inquiries of current employees and agents whose duties include responsibility for Internal control over financial reporting.

Exemptions and Effective Dates (Section 18)

Hardship Waivers (Section 18A)

Notwithstanding any other provision of the Model, an insurer may make written application to the Commissioner for waiver from any or all provisions of the Model based upon financial or organizational hardship. For example, the Commissioner could under this section grant a waiver of the Section 14B audit committee independence requirements to a company exceeding the \$500 million premium threshold, even though the Section 14H waiver would not apply. This exemption is granted at the discretion of the Commissioner, and may be granted at any time for a specified period or periods.

Specific Effective Dates (Section 18F)

An insurer will be required to file a Section 17 report if the insurer exceeds the premium threshold (as defined in Section 17A.)

1. Assume the insurer reports premiums as follows (note that the direct written and assumed premium in these examples would be reduced by any premiums reinsured with the Federal Crop Insurance Corporation and Federal Flood Program) :

\$ millions	201x	201x+1	201x+2	201x+3	201x+4
Net (written) premiums, per Statement of Operations in Audited financial report	350.3	390.8	410.5	425.7	450.8

Add: Reinsurance ceded	100.5	115.7	115.8	120.1	127.2
Gross direct written and assumed premium	450.8	506.5	526.3	545.8	578.0

In the above example, the insurer has reached the requisite threshold in 201x+1 and therefore will file its first Section 17 report effective December 31, 201x+3.

2. Assume the insurer reports premiums as follows:

\$ millions	201x	201x+1	201x+2	201x+3	201x+4
Net (written) premiums, per Statement of Operations in Audited financial report	350.3	380.5	390.8	410.5	425.7
Add: Reinsurance ceded	100.5	110.7	115.7	115.8	120.1
Gross direct written and assumed premium	450.8	491.2	506.5	526.3	545.8

In the above example, the insurer has reached the requisite threshold in 201x+2 and therefore will file its first Section 17 report effective December 31, 201x+4.

3. Assume the insurer reports premiums as follows:

\$ millions	201x	201x+1	201x+2	201x+3	201x+4
Net (written) premiums, per Statement of Operations in Audited financial report	350.3	390.8	380.5	410.5	425.7
Add: Reinsurance ceded	100.5	115.7	110.7	115.8	120.1
Gross direct written and assumed premium	450.8	506.5	491.2	526.3	545.8

In the above example, the insurer has reached the requisite threshold in 201x+1 and therefore will file its first Section 17 report effective December 31, 201x+3. Because the insurer dropped below the threshold in 201x+2, the insurer is not required to file a Section 17 report and thus, the reporting period starts over. The insurer reaches the threshold in 201x+3 and therefore, required to file the Section 17 report effective December 31, 201x+5. The insurer may choose to begin voluntarily filing the Section 17 report beginning with 201x+3 especially if the insurer has done the work to prepare the report.

Business Combination

A business combination is defined as acquisition of insurance/reinsurance business through:

- A. a stock acquisition,
- B. inforce reinsurance assumption, or
- C. a merger of insurers in a Group of insurers

A. Stock Acquisitions

Assume Company A, which has premiums of \$500m or more, buys Company B and retains Company B as a separate legal entity.

If Company B has premiums of less than \$500m (as derived from Section 17A), no Section 17 report is required.

If Company B has premiums of \$500m or more (as derived from Section 17A), a Section 17 report is required.

1. Assume Company B is acquired effective January 1, 201x and subsequently reports premiums as follows. Assume further that Company A and B elect to file separate Section 17 reports:

\$ millions	201x	201x+1	201x+2	201x+3	201x+4
Net (written) premiums, per Statement of Operations in Audited financial report	350.3	390.8	410.5	425.7	450.8
Add: Reinsurance ceded	100.5	115.7	115.8	120.1	127.2
Gross direct written and assumed premium	450.8	506.5	526.3	545.8	578.0

In the above example, Company B has reached the requisite threshold in 201x+1 and therefore will file its first Section 17 report effective December 31, 201x+3.

1. Assume Company B is acquired June 30, 201x+2 by Company A and Company B has premiums as follows. Assume further that Company A elects to file a single Section 17 report with the Group of insurers consisting of Company A and B:

\$ millions	201x	201x+1	201x+2	201x+3	201x+4
Net (written) premiums, per Statement of Operations in Audited financial report	350.3	390.8	410.5	425.7	450.8
Add: Reinsurance ceded	100.5	115.7	115.8	120.1	127.2
Gross direct written and assumed premium	450.8	506.5	526.3	545.8	578.0

In the above example, Company B has reached the requisite threshold in 201x+1 and therefore will file its first Section 17 report effective December 31, 201x+3. However due to the acquisition in 201x+2, the first combined Section 17 report, i.e., Group of insurers, would be effective December 31, 201x+4, two years subsequent to acquisition.

B. Inforce Reinsurance Assumption

For the purposes of determining premiums pursuant to Section 17A, assumed premiums from the assumption of an inforce reinsurance transaction will be excluded from the measurement of premiums, for two calendar years subsequent to acquisition.

Assume the insurer assumed an inforce transaction effective June 30, 201x+2 and reports premiums as follows:

\$ millions	201x	201x+1	201x+2	201x+3	201x+4
Net (written) premiums, per Statement of Operations in Audited financial report	350.3	390.8	610.5	850.7	875.8
Add: Reinsurance ceded	100.5	115.7	115.8	120.1	127.2
Gross direct written and assumed premium	450.8	506.5	726.3	970.8	1,003.0

Less: Gross assumed premium resulting from a business combination	0	0	200.0	425.0	425.0
Gross direct written and assumed premium, subject to Section 17	450.8	506.5	526.3	545.8	578.0

In the above example, the insurer has reached the requisite threshold in 201x+1 and therefore will file its first Section 17 report effective December 31, 201x+3, however only for business inforce in 201x+1 and still inforce in 201x+3. The business assumed at June 30, 201x+2 will be subject to a Section 17 report effective December 31, 201x+4, two calendar years after acquisition.

C. Mergers of Insurers in a Group of Insurers

If the merged insurer has premiums of less than \$500m (as derived from Section 17A), a Section 17 report is not required.

If the merged insurer has premiums of \$500m or more (as derived from Section 17A), a Section 17 report is required.

1. Assume that Insurer A and Insurer B have Gross direct written and assumed premiums as follows, and agree to merge effective January 1, 201x+1, with Insurer A as the surviving entity:

\$ millions	201x	201x+1	201x+2	201x+3	201x+4
Gross direct written and assumed premium – Insurer A	450.3	460.8	510.5	n/a	n/a
Gross direct written and assumed premium – Insurer B	100.5	115.7	115.8	n/a	n/a
Less: Intercompany transactions – gross	-	65.3	62.2	n/a	n/a
Combined gross direct written and assumed premiums Insurer A	-	511.2	564.1	n/a	n/a

In the above example, the merged entity (insurer A) has reached the requisite threshold in 201x+1, and will file its first Section 17 report effective December 31, 201x+3.

2. Assume that Insurer A and Insurer B have Gross direct written and assumed premiums as follows, and agree to merge effective January 1, 201x+2, with Insurer A as the surviving entity:

\$ millions	201x	201x+1	201x+2	201x+3	201x+4
Gross direct written and assumed premium – Insurer A	450.3	460.8	510.5	n/a	n/a
Gross direct written and assumed premium – Insurer B	100.5	115.7	115.8	n/a	n/a
Less: Intercompany transactions – gross	-	-	62.2	n/a	n/a
Combined gross direct written and assumed premiums Insurer A	-	-	564.1	n/a	n/a

In the above example, the merged entity (insurer A) has reached the requisite threshold in 201x+2, and will file its first Section 17 report effective December 31, 201x+4, two years subsequent to merger.

APPENDIX 1

Illustrative Examples of Management’s Report of Internal Control over Financial Reporting

The following are examples of Management’s Report of Internal Controls over Financial Reporting utilizing different facts and circumstances. These are only examples and individual company facts and circumstances will dictate the contents of their report. However, there are common elements that should be included in all reports as discussed in Sections 17C and 17D of the Model.

Example A: An SEC registrant or a member of a holding company system whose parent is an SEC registrant that had all material control processes over statutory financial reporting addressed in its Section 404 report.....Page 23

Example B: An SEC registrant or a member of a holding company system who is a SEC registrant and is a non-accelerated filer that had all material control processes over statutory financial reporting addressed in its Section 404 report. For these non-accelerated filers, the Section 404 report does not require the report of independent registered public accounting firm on internal control over financial reportingPage 25

Example C: An SEC registrant or a member of a holding company system whose parent is an SEC registrant that did not have all material control processes over statutory financial reporting addressed in its Section 404 reportPage 27

Example D: An SEC registrant or a member of a holding company system who is a SEC registrant and is a non-accelerated filer that did not have all material control processes over statutory financial reporting addressed in its Section 404 report. For these non-accelerated filers, the Section 404 report does not require the report of independent registered public accounting firm on internal control over financial reporting.....Page 30

Example E: A non-SEC registrant or a member of a holding company system that voluntarily complied with Section 404 of the Sarbanes-Oxley Act and produced a report on internal controls which included an auditor’s opinionPage 33

Example F: A company [or “group of insurers”] that is not subject to Section 404 and utilized their own framework to evaluate controlsPage 35

Example G: An SEC registrant or a member of a holding company system whose parent is an SEC registrant that had all material control processes addressed in their Section 404 report and had an unremediated material weaknessPage 37

Example H: An SEC registrant or member of a holding company system whose parent is an SEC registrant that did not include all material processes over statutory financial reporting addressed in its Section 404 report and had an unremediated material weakness noted.....Page 39

Example I: An SEC registrant or member of a holding company system whose parent is an SEC registrant that had all material processes over statutory financial reporting addressed in its Section 404 report. However, they recently acquired another insurer that is not included in their assessment.....Page 42

EXAMPLE A: AN SEC REGISTRANT OR A MEMBER OF A HOLDING COMPANY SYSTEM WHOSE PARENT IS AN SEC REGISTRANT THAT HAD ALL MATERIAL CONTROL PROCESSES OVER STATUTORY FINANCIAL REPORTING ADDRESSED IN ITS SECTION 404 REPORT

Management’s Report of Internal Control over Financial Reporting

XYZ Holding Company Inc (“XYZ”) is required to file annual reports on Form 10-K/20-F with the U.S. Securities and Exchange Commission. Each of the insurance companies listed on Attachment B is a wholly owned subsidiary of XYZ. For the purpose of XYZ’s Management’s Report of Internal Control over Financial Reporting, management has identified its “Group of insurers,” as that term is defined in [relevant state statute or Section 3H of the Model], as the insurance companies listed on Attachment B.

Management of XYZ is responsible for establishing and maintaining adequate internal control over statutory financial reporting. XYZ’s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements in accordance with statutory accounting principles. Management conducted an assessment of the effectiveness, as of December 31, 201X, of the Group of insurers’ internal control over statutory financial reporting, based on the framework established in *Internal Control—Integrated Framework Issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO)*. Based on our assessment under that framework, management concluded that the Group of insurers’ internal control over statutory financial reporting is effective to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements as of December 31, 201X.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are also subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In satisfaction of the Group of insurers’ obligation to deliver Management’s Report of Internal Control over Financial Reporting for the fiscal year ended December 31, 201X, as permitted by [relevant state statute or Section 17C of the Model], XYZ is hereby providing the Insurance Commissioner of [domiciliary state] copies of Management’s Report of Internal Control over Financial Reporting and the report of independent registered public accounting firm on internal control over financial reporting for XYZ included in XYZ’s Form 10-K/20-F for the fiscal year ended December 31, 201X (or alternatively the Annual Report to Stockholders). In addition, an Addendum (Attachment A) is included to this report which identifies the material processes that were not included in the Section 404 Report (as defined in Attachment A).

Based on management review of internal controls, there were no unremediated material weaknesses as of December 31, 201X identified as part of the Group of insurers’ internal control structure over the statutory financial statements for the year ended December 31, 201X.

(Signed) _____ (Date) _____
(Chief Executive Officer)

(Signed) _____ (Date) _____
(Chief Financial Officer)

ATTACHMENT A**XYZ Holding Company, Inc.****Addendum to Management's Report of Internal Control over Financial Reporting
For the Year Ended December 31, 201X**

For purposes of this addendum, the "Section 404 Report" means Management's Report on Internal Control over Financial Reporting and the report of independent registered public accounting firm on internal control over financial reporting contained in or incorporated by reference in the Form 10-K/20-F. Accordingly, as required by [relevant state statute or Section 17C of the Model], management of XYZ hereby affirms that there are no material processes with respect to the preparation of the audited statutory financial statements of the Group of insurers that were excluded from the Section 404 Report.

ATTACHMENT B**XYZ Holding Company, Inc.****Management's Report of Internal Control over Financial Reporting
List of Companies that are part of the Group of insurers
Pursuant to [relevant state statute or Section 17 of the Model]**

<u>Name</u>	<u>NAIC No</u>
ABC Insurance Subsidiary	12345
DEF Insurance Subsidiary	12346
GHI Insurance Subsidiary	12347
JKL Insurance Subsidiary	12348
MNO Insurance Subsidiary	12349

EXAMPLE B: AN SEC REGISTRANT OR A MEMBER OF A HOLDING COMPANY SYSTEM WHO IS A SEC REGISTRANT AND IS A NON-ACCELERATED FILER THAT HAD ALL MATERIAL CONTROL PROCESSES OVER STATUTORY REPORTING ADDRESSED IN ITS SECTION 404 REPORT. FOR THIS NON-ACCELERATED FILER, THE SECTION 404 REPORT DOES NOT REQUIRE THE REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM ON INTERNAL CONTROL OVER FINANCIAL REPORTING.

Management’s Report of Internal Control over Financial Reporting

XYZ Holding Company, Inc. (“XYZ”) is required to file annual reports on Form 10-K/20-F with the U.S. Securities and Exchange Commission. Each of the insurance companies listed on Attachment B is a wholly owned subsidiary of XYZ. For the purpose of XYZ’s Management’s Report of Internal Control over Financial Reporting, management has identified its “Group of insurers,” as that term is defined in [relevant state statute or Section 3H of the Model] as the insurance companies listed on Attachment B.

Management of XYZ is responsible for establishing and maintaining adequate internal control over statutory financial reporting. XYZ’s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements in accordance with statutory accounting principles. Management conducted an assessment of the effectiveness, as of December 31, 201X, of the Group of insurers’ internal control over statutory financial reporting, based on the framework established in Internal Control—Integrated Framework Issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on our assessment under that framework, management concluded that the Group of insurers’ internal control over statutory financial reporting is effective to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements as of December 31, 201X.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are also subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In satisfaction of the Group of insurers’ obligation to deliver Management’s Report of Internal Control over Financial Reporting for the fiscal year ended December 31, 201X, as permitted by [relevant state statute or Section 17 of the Model], XYZ is hereby providing the Insurance Commissioner of [domiciliary state] copies of Management’s Report of Internal Control over Financial Reporting included in XYZ’s Form 10-K/20-F for the fiscal year ended December 31, 201X (or alternatively the Annual Report to Stockholders). This does not include a report of independent registered public accounting firm on internal control over financial reporting for XYZ, as it is not required for non-accelerated filers. In addition, an Addendum (Attachment A) is included to this report which identifies the material processes that were not included in the Section 404 Report (as defined in Attachment A).

Based on management review of internal controls, there were no unremediated material weaknesses as of December 31, 201X identified as part of the Group of insurers’ internal control structure over the statutory financial statements for the year ended December 31, 201X.

(Signed) _____ (Date) _____
(Chief Executive Officer)

(Signed) _____ (Date) _____
(Chief Financial Officer)

ATTACHMENT A**XYZ Holding Company, Inc.****Addendum to Management's Report of Internal Control over Financial Reporting
For the Year Ended December 31, 201X**

For purposes of this filing, the "Section 404 Report" means Management's Report of Internal Control over Financial Reporting only contained in or incorporated by reference in the Company's Form 10-K/20-F. This does not include a report of independent registered public accounting firm on internal control over financial reporting, as it is not required for non-accelerated filers. Accordingly, as required by [relevant state statute or Section 17 of the Model], management of XYZ hereby affirms that there are no material processes with respect to the preparation of the audited statutory financial statements of the Group of insurers that were excluded from the Section 404 Report.

ATTACHMENT B**XYZ Holding Company, Inc.****Management's Report of Internal Control over Financial Reporting
List of Companies that are part of the Group of insurers
Pursuant to [relevant state statute or Section 17 of the Model]**

<u>Name</u>	<u>NAIC No</u>
ABC Insurance Subsidiary	12345
DEF Insurance Subsidiary	12346
GHI Insurance Subsidiary	12347
JKL Insurance Subsidiary	12348
MNO Insurance Subsidiary	12349

EXAMPLE C: AN SEC REGISTRANT OR A MEMBER OF A HOLDING COMPANY SYSTEM WHOSE PARENT IS AN SEC REGISTRANT THAT DID NOT HAVE ALL MATERIAL CONTROL PROCESSES OVER STATUTORY FINANCIAL REPORTING ADDRESSED IN ITS SECTION 404 REPORT

Management’s Report of Internal Control over Financial Reporting

XYZ Holding Company, Inc. (“XYZ”) is required to file annual reports on Form 10-K/20-F with the U.S. Securities and Exchange Commission. Each of the insurance companies listed on Attachment B is a wholly owned subsidiary of XYZ. For the purpose of XYZ’s Management’s Report of Internal Control over Financial Reporting, management has identified its “Group of insurers,” as that term is defined in [relevant state statute or Section 3H of the Model] as the insurance companies listed on Attachment B.

Management of XYZ is responsible for establishing and maintaining adequate internal control over statutory financial reporting. XYZ’s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements in accordance with statutory accounting principles. Management conducted an assessment of the effectiveness, as of December 31, 201X, of the Group of insurers’ internal control over statutory financial reporting, based on the framework established in *Internal Control—Integrated Framework Issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO)*. Based on our assessment under that framework, management concluded that the Group of insurers’ internal control over statutory financial reporting is effective to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements as of December 31, 201X.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are also subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In satisfaction of the Group of insurers’ obligation to deliver Management’s Report of Internal Control over Financial Reporting for the fiscal year ended December 31, 201X, as permitted by [relevant state statute or Section 17C of the Model], XYZ is hereby providing the Insurance Commissioner of [domiciliary state] copies of Management’s Report of Internal Control over Financial Reporting and the report of independent registered public accounting firm on internal control over financial reporting for XYZ included in XYZ’s Form 10-K/20-F for the fiscal year ended December 31, 201X (or alternatively the Annual Report to Stockholders). In addition, an Addendum (Attachment A) is included to this report which identifies the material processes that were not included in the Section 404 Report (as defined in Attachment A).

Based on management review of internal controls, there were no unremediated material weaknesses as of December 31, 201X identified as part of the Group of insurers’ internal control structure over the statutory financial statements for the year ended December 31, 201X.

(Signed) _____ (Date) _____
(Chief Executive Officer)

(Signed) _____ (Date) _____
(Chief Financial Officer)

ATTACHMENT A**XYZ Holding Company, Inc.****Addendum to Management's Report of Internal Control over Financial Reporting
For the Year Ended December 31, 201X**

For purposes of this filing, the "Section 404 Report" means Management's Report of Internal Control over Financial Reporting and the report of independent registered public accounting firm on internal control over financial reporting contained in or incorporated by reference in the Company's Form 10-K/20-F. Accordingly, as required by [relevant state statute or Section 17C of the Model], management of XYZ hereby affirms that the only material processes with respect to the preparation of the audited statutory financial statements of the Group of insurers that were excluded from the Section 404 Report are the processes discussed below. Management of XYZ hereby affirms that all other material processes with respect to the preparation of the audited statutory financial statements of the Group of insurers were included in the Section 404 Report. The following statutory financial reporting processes were reviewed separately from the internal controls reported by the Group of insurers in its Section 404 report:

Significant Control Processes not tested due to Group Materiality Considerations

The Section 404 report excludes certain control processes deemed material to individual insurance legal entities included within the Group of insurers. This exclusion was due to group materiality decisions made at the parent company level. These processes, and the legal entities within the Group of insurers impacted, are listed as follows:

Workers' Compensation Claims Processing – The HIJ claims processing system is utilized to process workers' compensation claims material to ABC Insurance Subsidiary and DEF Insurance Subsidiary.

Related Party Transactions Eliminated through Consolidation

The Section 404 report does not consider controls surrounding related party transactions as the effects of those transactions are eliminated through consolidation at the holding company financial statement level. Significant related party transactions, and the legal entities within the Group of insurers impacted, are listed as follows:

Affiliate reinsurance agreements – A significant amount of reinsurance coverage is obtained by ABC Insurance Subsidiary and DEF Insurance Subsidiary through contracts with XYZ Parent Company.

Management service agreements – ABC Insurance Subsidiary receives all of its management services through an agreement with XYZ Parent Company.

Tax allocation agreements – ABC Insurance Subsidiary and DEF Insurance Subsidiary are subject to an intercompany tax allocation agreement with XYZ Parent Company.

Deferred Income Taxes

Federal income taxes are provided for XYZ's estimated current and deferred liability. Deferred taxes are provided for differences between the financial statement and tax bases of assets and liabilities. Pursuant to *SSAP No. 101—Income Taxes, A Replacement of SSAP No. 10R and SSAP No. 10*, changes in deferred tax assets and liabilities are recognized as a separate component of gains and losses in statutory surplus, while under GAAP/IFRS, these changes are included in income tax expense or benefit. Gross deferred tax assets not meeting the realization criteria outlined in SSAP No. 101 are not admitted.

Nonadmitted Assets

Certain XYZ assets (principally furniture, equipment, prepaid expenses, agents' balances, and certain deferred tax assets) have been designated as nonadmitted assets under statutory accounting guidance (primarily in *SSAP No. 4—Assets and Nonadmitted Assets* and *SSAP No. 20—Nonadmitted Assets*). Such nonadmitted assets are excluded from assets by a charge to statutory surplus. Under GAAP/IFRS, such amounts are carried at amortized cost with an appropriate valuation allowance, as necessary.

Asset Valuation Reserve (“AVR”)

The AVR represents a statutory contingency reserve for life and health insurers for credit related risk on most invested assets, and is charged to surplus pursuant to *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve*. No such reserve is required under GAAP/IFRS accounting.

Interest Maintenance Reserve (“IMR”)

The IMR represents the deferral of interest-related realized gains and losses, net of tax, on primarily fixed maturity investments, amortized into income over the remaining life of the investment sold pursuant to *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve*. No such reserve is required under GAAP/IFRS accounting.

Management of XYZ conducted an assessment of the internal controls over these processes and concluded that they were effective with respect to the audited statutory financial statements.

(Please note that this is not intended to be an all-inclusive list. It should only include material process that were not covered in the Section 404 Report. The facts and circumstances of each situation will determine the items to be included.)

ATTACHMENT B**XYZ Holding Company, Inc.****Management’s Report of Internal Control over Financial Reporting****List of Companies that are part of the Group of insurers****Pursuant to [relevant state statute or Section 17 of the Model]**

<u>Name</u>	<u>NAIC No</u>
ABC Insurance Subsidiary	12345
DEF Insurance Subsidiary	12346
GHI Insurance Subsidiary	12347
JKL Insurance Subsidiary	12348
MNO Insurance Subsidiary	12349

EXAMPLE D: AN SEC REGISTRANT OR A MEMBER OF A HOLDING COMPANY SYSTEM WHO IS A SEC REGISTRANT AND IS A NON-ACCELERATED FILER THAT DID NOT HAVE ALL MATERIAL CONTROL PROCESSES OVER STATUTORY FINANCIAL REPORTING ADDRESSED IN ITS SECTION 404 REPORT. FOR THESE NON-ACCELERATED FILERS, THE SECTION 404 REPORT DOES NOT REQUIRE THE REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM ON INTERNAL CONTROL OVER FINANCIAL REPORTING.

Management’s Report of Internal Control over Financial Reporting

XYZ Holding Company, Inc. (“XYZ”) is required to file annual reports on Form 10-K/20-F with the U.S. Securities and Exchange Commission. Each of the insurance companies listed on Attachment B is a wholly owned subsidiary of XYZ. For the purpose of XYZ’s Management’s Report of Internal Control over Financial Reporting, management has identified its “Group of insurers,” as that term is defined in [relevant state statute or Section 3H of the Model] as the insurance companies listed on Attachment B.

Management of XYZ is responsible for establishing and maintaining adequate internal control over statutory financial reporting. XYZ’s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements in accordance with statutory accounting principles. Management conducted an assessment of the effectiveness, as of December 31, 201X, of the Group of insurers’ internal control over statutory financial reporting, based on the framework established in Internal Control—Integrated Framework Issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on our assessment under that framework, management concluded that the Group of insurers’ internal control over statutory financial reporting is effective to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements as of December 31, 201X.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are also subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In satisfaction of the Group of insurers’ obligation to deliver Management’s Report of Internal Control over Financial Reporting for the fiscal year ended December 31, 201X, as permitted by [relevant state statute or Section 17 of the Model], XYZ is hereby providing the Insurance Commissioner of [domiciliary state] copies of Management’s Report of Internal Control over Financial Reporting included in XYZ’s Form 10-K/20-F for the fiscal year ended December 31, 201X (or alternatively the Annual Report to Stockholders). This does not include a report of independent registered public accounting firm on internal control over financial reporting for XYZ, as it is not required for non-accelerated filers. In addition, an Addendum (Attachment A) is included to this report which identifies the material processes that were not included in the Section 404 Report (as defined in Attachment A).

Based on management review of internal controls, there were no unremediated material weaknesses as of December 31, 201X identified as part of the Group of insurers’ internal control structure over the statutory financial statements for the year ended December 31, 201X.

(Signed) _____ (Date) _____
(Chief Executive Officer)

(Signed) _____ (Date) _____
(Chief Financial Officer)

ATTACHMENT A**XYZ Holding Company, Inc.****Addendum to Management's Report of Internal Control over Financial Reporting
For the Year Ended December 31, 201X**

For purposes of this filing, the "Section 404 Report" means Management's Report of Internal Control over Financial Reporting only contained in or incorporated by reference in the Company's Form 10-K/20-F. This does not include a report of independent registered public accounting firm on internal control over financial reporting, as it is not required for non-accelerated filers. Accordingly, as required by [relevant state statute or Section 17 of the Model], management of XYZ hereby affirms that the only material processes with respect to the preparation of the audited statutory financial statements of the Group of insurers that were excluded from the Section 404 Report are the processes discussed below. Management of XYZ hereby affirms that all other material processes with respect to the preparation of the audited statutory financial statements of the Group of insurers were included in the Section 404 Report.

Significant Control Processes not tested due to Group Materiality Considerations

The Section 404 report excludes certain control processes deemed material to individual insurance legal entities included within the Group of insurers. This exclusion was due to group materiality decisions made at the parent company level. These processes, and the legal entities within the Group of insurers impacted, are listed as follows:

Workers' Compensation Claims Processing – The HIJ claims processing system is utilized to process workers' compensation claims material to ABC Insurance Subsidiary and DEF Insurance Subsidiary.

Related Party Transactions Eliminated through Consolidation

The Section 404 report does not consider controls surrounding related party transactions as the effects of those transactions are eliminated through consolidation at the holding company financial statement level. Significant related party transactions, and the legal entities within the Group of insurers impacted, are listed as follows:

Affiliate reinsurance agreements – A significant amount of reinsurance coverage is obtained by ABC Insurance Subsidiary and DEF Insurance Subsidiary through contracts with XYZ Parent Company.

Management service agreements – ABC Insurance Subsidiary receives all of its management services through an agreement with XYZ Parent Company.

Tax allocation agreements – ABC Insurance Subsidiary and DEF Insurance Subsidiary are subject to an intercompany tax allocation agreement with XYZ Parent Company.

Deferred Income Taxes

Federal income taxes are provided for XYZ's estimated current and deferred liability. Deferred taxes are provided for differences between the financial statement and tax bases of assets and liabilities. Pursuant to *SSAP No. 101—Income Taxes, A Replacement of SSAP No. 10R and SSAP No. 10*, changes in deferred tax assets and liabilities are recognized as a separate component of gains and losses in statutory surplus, while under GAAP/IFRS, these changes are included in income tax expense or benefit. Gross deferred tax assets not meeting the realization criteria outlined in SSAP No. 101 are not admitted.

Nonadmitted Assets

Certain XYZ assets (principally furniture, equipment, prepaid expenses, agents' balances, and certain deferred tax assets) have been designated as nonadmitted assets under statutory accounting guidance (primarily in *SSAP No. 4—Assets and Nonadmitted Assets* and *SSAP No. 20—Nonadmitted Assets*). Such nonadmitted assets are excluded from assets by a charge to statutory surplus. Under GAAP/IFRS, such amounts are carried at amortized cost with an appropriate valuation allowance, as necessary.

Asset Valuation Reserve (“AVR”)

The AVR represents a statutory contingency reserve for life and health insurers for credit related risk on most invested assets, and is charged to surplus pursuant to *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve*. No such reserve is required under GAAP/IFRS accounting.

Interest Maintenance Reserve (“IMR”)

The IMR represents the deferral of interest-related realized gains and losses, net of tax, on primarily fixed maturity investments, amortized into income over the remaining life of the investment sold pursuant to *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve*. No such reserve is required under GAAP/IFRS accounting.

Management of XYZ conducted an assessment of the internal controls over these processes and concluded that they were effective with respect to the audited statutory financial statements.

(Please note that this is not intended to be an all-inclusive list. It should only include material process that were not covered in the Section 404 Report. The facts and circumstances of each situation will determine the items to be included.)

ATTACHMENT B**XYZ Holding Company, Inc.****Management’s Report of Internal Control over Financial Reporting****List of Companies that are part of the Group of insurers****Pursuant to [relevant state statute or Section 17 of the Model]**

<u>Name</u>	<u>NAIC No</u>
ABC Insurance Subsidiary	12345
DEF Insurance Subsidiary	12346
GHI Insurance Subsidiary	12347
JKL Insurance Subsidiary	12348
MNO Insurance Subsidiary	12349

ATTACHMENT A**XYZ Holding Company, Inc.****Addendum to Management's Report of Internal Control over Financial Reporting
For the Year Ended December 31, 201X**

For purposes of this addendum, the "Section 404 Report" means Management's Report of Internal Control over Financial Reporting and the report of independent registered public accounting firm on internal control over financial reporting contained in or incorporated by reference in the Annual Report to Stockholders. Accordingly, as required by [relevant state statute or Section 17C of the Model], management of XYZ hereby affirms that there are no material processes with respect to the preparation of the audited statutory financial statements of the Group of insurers that were excluded from the Section 404 Report.

ATTACHMENT B**XYZ Holding Company, Inc.****Management's Report of Internal Control over Financial Reporting
List of Companies that are part of the Group of insurers
Pursuant to [relevant state statute or Section 17 of the Model]**

<u>Name</u>	<u>NAIC No</u>
ABC Insurance Subsidiary	12345
DEF Insurance Subsidiary	12346
GHI Insurance Subsidiary	12347
JKL Insurance Subsidiary	12348
MNO Insurance Subsidiary	12349

EXAMPLE F: A COMPANY [OR “GROUP OF INSURERS”] THAT IS NOT SUBJECT TO SECTION 404 AND UTILIZED THEIR OWN FRAMEWORK TO EVALUATE CONTROLS**Management’s Report of Internal Control over Financial Reporting**

[As a non-SEC registrant, XYZ Holding Company, Inc. (“XYZ”) is not required to prepare or file with the U.S. Securities and Exchange Commission a Sarbanes-Oxley Act Section 404 report on internal control over financial reporting. Each of the insurance companies listed on Attachment A is a wholly owned subsidiary of XYZ. For the purpose of XYZ’s Management’s Report of Internal Control over Financial Reporting, management has identified its “Group of insurers,” as that term is defined in [relevant state statute or Section 3H of the Model], as the insurance companies listed on Attachment A.]

Management of ABC Insurance Company [or XYZ] is responsible for establishing and maintaining adequate internal control over statutory financial reporting. The Company has established an internal control system designed to provide reasonable assurance regarding the fair presentation of statutory financial reporting. The Company developed its own internal framework for evaluating the effectiveness of internal control over statutory financial reporting. The Company’s framework includes the identification and evaluation of the company’s internal control environment and areas of potential material internal control risk, documentation of existing internal controls, monitoring and testing of those key controls, documentation of remedial actions planned or taken, if any, and communication of the findings of the evaluation by the Company’s senior management to the Audit committee of the Board of Directors.

Management conducted an assessment of the effectiveness, as of December 31, 201X, of the Company’s internal control over statutory financial reporting, which included identifying, reviewing, monitoring and testing significant internal controls over statutory financial reporting. Based on our assessment under the above described approach and through diligent inquiry, management has concluded that the Company’s internal control over statutory financial reporting is effective to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements as of December 31, 201X.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are also subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Based on management review of internal controls, there were no unremediated material weaknesses as of December 31, 201X identified as part of the Company’s internal control structure over the statutory financial statements for the year ended December 31, 201X.

(Signed) _____ (Date) _____
(Chief Executive Officer)

(Signed) _____ (Date) _____
(Chief Financial Officer)

ATTACHMENT A**XYZ Holding Company, Inc.****Management's Report of Internal Control over Financial Reporting****List of Companies that are part of the Group of Insurers****Pursuant to [relevant state statute or Section 17 of the Model]**

<u>Name</u>	<u>NAIC No</u>
ABC Insurance Subsidiary	12345
DEF Insurance Subsidiary	12346
GHI Insurance Subsidiary	12347
JKL Insurance Subsidiary	12348
MNO Insurance Subsidiary	12349

EXAMPLE G: AN SEC REGISTRANT OR A MEMBER OF A HOLDING COMPANY SYSTEM WHOSE PARENT IS AN SEC REGISTRANT THAT HAD ALL MATERIAL CONTROL PROCESSES ADDRESSED IN THEIR SECTION 404 REPORT AND HAD AN UNREMIEDIATED MATERIAL WEAKNESS

Management’s Report of Internal Control over Financial Reporting

XYZ Holding Company, Inc. (“XYZ”) is required to file annual reports on Form 10-K/20-F with the U.S. Securities and Exchange Commission. Each of the insurance companies listed on Attachment B is a wholly-owned subsidiary of XYZ. For the purpose of XYZ’s Management’s Report of Internal Control over Financial Reporting, management has identified its “Group of insurers,” as that term is defined in [relevant state statute or Section 3H of the Model], as the insurance companies listed on Attachment B.

Management of XYZ is responsible for establishing and maintaining adequate internal control over statutory financial reporting. XYZ’s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements in accordance with statutory accounting principles.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are also subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management conducted an assessment of the effectiveness, as of December 31, 201X, of the Group of insurers’ internal control over statutory financial reporting, based on the framework established in *Internal Control—Integrated Framework Issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO)*.

A material weakness was noted in XYZ’s internal control over financial reporting related to the calculation of insurance reserves. Due to the manner in which the data for homeowners policies are captured by the systems used in its Southeastern US regional office, changes in XYZ’s estimate of insurance reserves for certain policies are not reviewed by XYZ’s Actuarial Department prior to being recorded in the company’s accounting records.

A material weakness is a deficiency or a combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the company’s financial statements will not be prevented, or detected and corrected on a timely basis. In connection with the weakness noted above, XYZ’s management has taken remedial actions to change its procedures for coding policies issued in the states affected so that all homeowners policy data are included in the Actuarial Department review of estimate of insurance reserves. This change was effective on July 1, 20XX.

As a result of the unremediated material weakness described above, XYZ management has concluded that, as of December 31, 201X, XYZ’s internal control over statutory financial reporting was not effective.

In satisfaction of the Group of insurers’ obligation to deliver Management’s Report of Internal Control over Financial Reporting for the fiscal year ended December 31, 201X, as permitted by [relevant state statute or Section 17C of the Model], XYZ is hereby providing the Insurance Commissioner of [domiciliary state] copies of Management’s Report of Internal Control over Financial Reporting and the report of independent registered public accounting firm on internal control over financial reporting for XYZ included in XYZ’s Form 10-K/20-F for the fiscal year ended December 31, 201X (or alternatively the Annual Report to Stockholders). In addition, an Addendum (Attachment A) is included to this report

which identifies the material processes that were not included in the Section 404 Report (as defined in Attachment A).

(Signed) _____ (Date) _____
(Chief Executive Officer)

(Signed) _____ (Date) _____
(Chief Financial Officer)

ATTACHMENT A

**XYZ Holding Company, Inc.
Addendum to Management's Report of Internal Control over Financial Reporting
For the Year Ended December 31, 201X**

For purposes of this addendum, the "Section 404 Report" means Management's Report of Internal Control over Financial Reporting and the report of independent registered public accounting firm on internal control over financial reporting contained in or incorporated by reference in the Form 10-K/20-F. Accordingly, as required by [relevant state statute or Section 17C of the Model], management of XYZ hereby affirms that there are no material processes with respect to the preparation of the audited statutory financial statements of the Group of insurers that were excluded from the Section 404 Report.

ATTACHMENT B

**XYZ Holding Company Inc.
Management's Report of Internal Control over Financial Reporting
List of Companies that are part of the Group of insurers
Pursuant to [relevant state statute or Section 17 of the Model]**

<u>Name</u>	<u>NAIC No</u>
ABC Insurance Subsidiary	12345
DEF Insurance Subsidiary	12346
GHI Insurance Subsidiary	12347
JKL Insurance Subsidiary	12348
MNO Insurance Subsidiary	12349

EXAMPLE H: AN SEC REGISTRANT OR MEMBER OF A HOLDING COMPANY SYSTEM WHOSE PARENT IS AN SEC REGISTRANT THAT DID NOT INCLUDE ALL MATERIAL PROCESSES OVER STATUTORY FINANCIAL REPORTING ADDRESSED IN ITS SECTION 404 REPORT AND HAD AN UNREMIEDIATED MATERIAL WEAKNESS NOTED

Management’s Report of Internal Control over Financial Reporting

XYZ Holding Company, Inc. (“XYZ”) is required to file annual reports on Form 10-K/20-F with the U.S. Securities and Exchange Commission. Each of the insurance companies listed on Attachment B is a wholly-owned subsidiary of XYZ. For the purpose of XYZ’s Management’s Report of Internal Control over Financial Reporting, management has identified its “Group of insurers,” as that term is defined in [relevant state statute or Section 3H of the Model], as the insurance companies listed on Attachment B.

Management of XYZ is responsible for establishing and maintaining adequate internal control over statutory financial reporting. XYZ’s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements in accordance with statutory accounting principles. Management conducted an assessment of the effectiveness, as of December 31, 201X, of the Group of insurers’ internal control over statutory financial reporting, based on the framework established in *Internal Control—Integrated Framework Issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO)*.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are also subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

A material weakness was noted in XYZ’s internal control over financial reporting related to the calculation of insurance reserves. Due to the manner in which the data for homeowners policies are captured by the systems used in its Southeastern US regional office, changes in XYZ’s estimate of insurance reserves for certain policies are not reviewed by XYZ’s Actuarial Department prior to being recorded in the company’s accounting records.

A material weakness is a deficiency or a combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the company’s financial statements will not be prevented, or detected and corrected on a timely basis. In connection with the assessment above, XYZ’s management identified a material weakness as of December 31, 201X in the controls over the calculation of insurance reserves.

As a result of the unremediated material weakness described above, XYZ management has concluded that, as of December 31, 201X, XYZ’s internal control over statutory financial reporting was not effective.

In satisfaction of the Group of insurers’ obligation to deliver Management’s Report of Internal Control over Financial Reporting for the fiscal year ended December 31, 201X, as permitted by [relevant state statute or Section 17C of the Model], XYZ is hereby providing the Insurance Commissioner of [domiciliary state] copies of Management’s Report of Internal Control over Financial Reporting and the report of independent registered public accounting firm on internal control over financial reporting for XYZ included in XYZ’s Form 10-K for the fiscal year ended December 31, 201X (or alternatively the Annual Report to Stockholders). In addition, an Addendum (Attachment A) is included to this report which identifies the material processes that were not included in the Section 404 Report (as defined in Attachment A).

(Signed) _____ (Date) _____
 (Chief Executive Officer)

(Signed) _____ (Date) _____
 (Chief Financial Officer)

ATTACHMENT A

XYZ Holding Company, Inc.

Addendum to Management's Report of Internal Control over Financial Reporting For the Year Ended December 31, 201X

For purposes of this filing, the "Section 404 Report" means Management's Report of Internal Control over Financial Reporting and the report of independent registered public accounting firm on internal control over financial reporting contained in or incorporated by reference in the Company's Form 10-K/20-F. Accordingly, as required by [relevant state statute or Section 17C of the Model], management of XYZ hereby affirms that the only material processes with respect to the preparation of the audited statutory financial statements of the Group of insurers that were excluded from the Section 404 Report are the processes discussed below. Management of XYZ hereby affirms that all other material processes with respect to the preparation of the audited statutory financial statements of the Group of insurers were included in the Section 404 Report. The following statutory financial reporting processes were reviewed separately from the internal controls reported by the Group of insurers in its Section 404 report:

Significant Control Processes not tested due to Group Materiality Considerations

The Section 404 report excludes certain control processes deemed material to individual insurance legal entities included within the Group of insurers. This exclusion was due to group materiality decisions made at the parent company level. These processes, and the legal entities within the Group of insurers impacted, are listed as follows:

Workers' Compensation Claims Processing – The HIJ claims processing system is utilized to process workers' compensation claims material to ABC Insurance Subsidiary and DEF Insurance Subsidiary.

Related Party Transactions Eliminated through Consolidation

The Section 404 report does not consider controls surrounding related party transactions as the effects of those transactions are eliminated through consolidation at the holding company financial statement level. Significant related party transactions, and the legal entities within the Group of insurers impacted, are listed as follows:

Affiliate reinsurance agreements – A significant amount of reinsurance coverage is obtained by ABC Insurance Subsidiary and DEF Insurance Subsidiary through contracts with XYZ Parent Company.

Management service agreements – ABC Insurance Subsidiary receives all of its management services through an agreement with XYZ Parent Company.

Tax allocation agreements – ABC Insurance Subsidiary and DEF Insurance Subsidiary are subject to an intercompany tax allocation agreement with XYZ Parent Company.

Deferred Income Taxes

Federal income taxes are provided for XYZ's estimated current and deferred liability. Deferred taxes are provided for differences between the financial statement and tax bases of assets and liabilities. Pursuant to *SSAP No. 101—Income Taxes, A Replacement of SSAP No. 10R and SSAP No. 10*, changes in deferred tax assets and liabilities are recognized as a separate component of gains and losses in statutory surplus, while under GAAP/IFRS, these changes are included in income tax expense or benefit. Gross deferred tax assets not meeting the realization criteria outlined in SSAP No. 101 are not admitted.

Nonadmitted Assets

Certain XYZ assets (principally furniture, equipment, prepaid expenses, agents' balances, and certain deferred tax assets) have been designated as nonadmitted assets under statutory accounting guidance (primarily in *SSAP No. 4—Assets and Nonadmitted Assets* and *SSAP No. 20—Nonadmitted Assets*). Such nonadmitted assets are excluded from assets by a charge to statutory surplus. Under GAAP/IFRS, such amounts are carried at amortized cost with an appropriate valuation allowance, as necessary.

Asset Valuation Reserve (“AVR”)

The AVR represents a statutory contingency reserve for life and health insurers for credit related risk on most invested assets, and is charged to surplus pursuant to *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve*. No such reserve is required under GAAP/IFRS accounting.

Interest Maintenance Reserve (“IMR”)

The IMR represents the deferral of interest-related realized gains and losses, net of tax, on primarily fixed maturity investments, amortized into income over the remaining life of the investment sold pursuant to *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve*. No such reserve is required under GAAP/IFRS accounting.

Management of XYZ conducted an assessment of the internal controls over these processes and concluded that they were effective with respect to the audited statutory financial statements.

(Please note that this is not intended to be an all-inclusive list. It should only include material processes that were not covered in the Section 404 Report. The facts and circumstances of each situation will determine the items to be included.)

ATTACHMENT B

XYZ Holding Company, Inc.

Management's Report of Internal Control over Financial Reporting

List of Companies that are part of the Group of insurers

Pursuant to [relevant state statute or Section 17 of the Model]

<u>Name</u>	<u>NAIC No</u>
ABC Insurance Subsidiary	12345
DEF Insurance Subsidiary	12346
GHI Insurance Subsidiary	12347
JKL Insurance Subsidiary	12348
MNO Insurance Subsidiary	12349

EXAMPLE I: AN SEC REGISTRANT OR MEMBER OF A HOLDING COMPANY SYSTEM WHOSE PARENT IS AN SEC REGISTRANT THAT HAD ALL MATERIAL PROCESSES OVER STATUTORY FINANCIAL REPORTING ADDRESSED IN ITS SECTION 404 REPORT. HOWEVER, THEY RECENTLY ACQUIRED ANOTHER INSURER THAT IS NOT INCLUDED IN THEIR ASSESSMENT

Management’s Report of Internal Control over Financial Reporting

XYZ Holding Company, Inc. (“XYZ”) is required to file annual reports on Form 10-K/20-F with the U.S. Securities and Exchange Commission. Each of the insurance companies listed on Attachment B is a wholly owned subsidiary of XYZ. For the purpose of XYZ’s Management’s Report of Internal Control over Financial Reporting, management has identified its “Group of insurers,” as that term is defined in [relevant state statute or Section 3H of the Model], as the insurance companies listed on Attachment B.

Management of XYZ is responsible for establishing and maintaining adequate internal control over statutory financial reporting. XYZ’s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements in accordance with statutory accounting principles. Management conducted an assessment of the effectiveness, as of December 31, 201X, of the Group of insurers’ internal control over statutory financial reporting, based on the framework established in *Internal Control—Integrated Framework Issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO)*. This assessment excluded an evaluation of internal controls over financial reporting for RST Insurance Company which was recently acquired. Based on our assessment under that framework, management concluded that the Group of insurers’ internal control over statutory financial reporting is effective to provide reasonable assurance regarding the reliability of financial reporting and the preparation of statutory financial statements as of December 31, 201X.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are also subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In satisfaction of the Group of insurers’ obligation to deliver Management’s Report of Internal Control over Financial Reporting for the fiscal year ended December 31, 201X, as permitted by [relevant state statute or Section 17C of the Model], XYZ is hereby providing the Insurance Commissioner of [domiciliary state] copies of Management’s Report of Internal Control over Financial Reporting and the report of independent registered public accounting firm on internal control over financial reporting for XYZ included in XYZ’s Form 10-K/20-F for the fiscal year ended December 31, 201X (or alternatively the Annual Report to Stockholders). In addition, an Addendum (Attachment A) is included to this report which identifies the material processes that were not included in the Section 404 Report (as defined in Attachment A).

Based on management review of internal controls, there were no unremediated material weaknesses as of December 31, 201X identified as part of the Group of insurers’ internal control structure over the statutory financial statements for the year ended December 31, 201X.

(Signed) _____ (Date) _____
(Chief Executive Officer)

(Signed) _____ (Date) _____
(Chief Financial Officer)

ATTACHMENT A**XYZ Holding Company, Inc.****Addendum to Management’s Report of Internal Control over Financial Reporting
For the Year Ended December 31, 201X**

For purposes of this addendum, the “Section 404 Report” means Management’s Report of Internal Control over Financial Reporting and the report of independent registered public accounting firm on internal control over financial reporting contained in or incorporated by reference in the Form 10-K. Accordingly, as required by [relevant state statute or Section 17C of the Model], management of XYZ hereby affirms that there are no material processes with respect to the preparation of the audited statutory financial statements of the Group of insurers that were excluded from the Section 404 Report.

ATTACHMENT B**XYZ Holding Company, Inc.****Management’s Report of Internal Control over Financial Reporting****List of Companies that are part of the Group of insurers****Pursuant to [relevant state statute or Section 17 of the Model]**

<u>Name</u>	<u>NAIC No</u>
ABC Insurance Subsidiary	12345
DEF Insurance Subsidiary	12346
GHI Insurance Subsidiary	12347
JKL Insurance Subsidiary	12348
MNO Insurance Subsidiary	12349