



Date: 11/21/22

Virtual Meeting

**FINANCIAL ANALYSIS SOLVENCY TOOLS (E) WORKING GROUP**

Tuesday, December 6, 2022

12:00 p.m. – 1:00 p.m. PT / 1:00 p.m. – 2:00 p.m. MT / 2:00 p.m. – 3:00 p.m. CT / 3:00 p.m. – 4:00 p.m. ET

**ROLL CALL**

Judy Weaver, Chair	Michigan	Lynn Beckner	Maryland
Greg Chew, Vice Chair	Virginia	Debbie Doggett	Missouri
Sheila Travis	Alabama	Patricia Gosselin	New Hampshire
Kurt Regner/David Lee	Arizona	Olga Dixon	New Jersey
Michelle Lo	California	Victor Agbu	New York
Jack Broccoli	Connecticut	Dwight Radel/Tim Biler	Ohio
Nathaniel Kevin Brown	District of Columbia	Ryan Keeling	Oregon
Carolyn Morgan/Nicole Crockett	Florida	Liz Ammerman/Ted Hurley	Rhode Island
Eric Moser	Illinois	Amy Garcia	Texas
Julia Conrad	Indiana	Kristin Forsberg	Wisconsin

NAIC Support Staff: Ralph Villegas / Rodney Good / Bill Rivers

**AGENDA**

1. Consider Adoption of its Oct. 20 Meeting Minutes – *Judy Weaver (MI)* Attachment 1
  
2. Consider Adoption of Financial Analysis Handbook Guidance Related to the Following – *Judy Weaver (MI)*
  - a. Terrorism Risk Attachment 2
  - b. Agents Balances / Trust Accounts Attachment 3
  - c. Monitoring Startup Insurers Attachment 4
  - d. Redomestication Communication Attachment 5
  - e. Intercompany Pooling Arrangements Attachment 6
  - f. Form F and CGAD Guidance Attachment 7
  - g. Investments Involving Related Parties Attachment 8
  - h. Branded Risk Assessment Attachment 9
  - i. Health Insurers CMS Star Rating Attachment 10
  - j. Actuarial Guideline 53 Attachment 11
  - k. Prioritization Framework for Priority 4 Insurers Attachment 12
  - l. Quarterly Quantitative Assessment of Non-Troubled Insurers Attachment 13
  
3. Discuss Any Other Matters Brought Before the Working Group – *Judy Weaver (MI)*
  
4. Adjournment

Draft: 11/4/22

Financial Analysis Solvency Tools (E) Working Group  
Virtual Meeting  
October 20, 2022

The Financial Analysis Solvency Tools (E) Working Group of the Examination Oversight (E) Task Force met Oct. 20, 2022. The following Working Group members participated: Judy Weaver, Chair (MI); Greg Chew, Vice Chair (VA); Michelle Lo (CA); N. Kevin Brown (DC); Eric Moser (IL); Julia Conrad (IN); Lynn Beckner (MD); Debbie Doggett (MO); Pat Gosselin (NH); Victor Agbu (NY); Dwight Radel and Tim Biler (OH); Liz Ammerman (RI); and Kristin Forsberg (WI). Also participating was: Arthur Schwartz (LA).

1. Adopted Handbook Guidance

Weaver said revisions to various sections of the *Financial Analysis Handbook* (Handbook) related to the International Association of Insurance Supervisors' (IAIS's) Common Framework for the Supervision of Internationally Active Insurance Groups (ComFrame) were exposed for public comment by the Group Solvency Issues (E) Working Group and approved at the Summer National Meeting. She said because the guidance was previously exposed and because of the need to ensure consistency across functions, she recommends adopting the revisions as included.

Lo made a motion, seconded by Doggett, to adopt Handbook revisions related to the ComFrame (Attachment \_ - A). The motion passed unanimously.

2. Exposed Handbook Guidance

Weaver said the next item of business is to consider exposing revisions to the Handbook in response to referrals and recommendations received from the Financial Analysis (E) Working Group, the Ad Hoc (E/F) Subgroup, the Risk-Focused Surveillance (E) Working Group, and NAIC staff.

a. Terrorism Reinsurance, Affiliated Agents, Monitoring Startup Insurers, and Redomestication Communication

Weaver said the first set of proposed revisions related to terrorism reinsurance, affiliated agents, monitoring startup insurers, and redomestication communication is in response to a referral from the Financial Analysis (E) Working Group.

Rodney Good (NAIC) provided an overview of the proposed revisions:

- **Terrorism Reinsurance:** Good said the recommendation resulted from the Working Group removing the topic from the *Solvency Monitoring Risk Alert*, a regulator-only publication. He said the guidance that was previously included in the *Solvency Monitoring Risk Alert* was incorporated into the Pricing/Underwriting Risk Repository – Property/Casualty (P/C).
- **Affiliated Agents:** Good said the recommendation was based on troubled company situations where the agent's misappropriation of trust accounts contributed to the insurer's financial difficulties. He said the proposed revisions to the Credit Risk Repository include information about the fiduciary responsibility of agents and brokers for trust accounts, as well as procedures that the analyst could consider if there are concerns in this area.

- **Monitoring Startup Insurers:** Good said this recommendation was based on the Working Group's discussions of a recent trend of startup insurers that rely heavily on capital support from the parent company to support rapid growth and a trend of material underwriting and net losses. He said the Working Group's underlying concern was whether this was sustainable until the insurer achieved profitability. He said the proposed revisions to the Strategic Risk Repository include additional considerations for analysts, such as obtaining a five-year business plan and projections from the insurer and assessing future capital funding, growth expectations, and profitability.
  - **Redomestication Communication:** Good said the recommendation stemmed from recent troubled company situations where licensed states were not informed of plans to redomesticate a troubled insurer prior to the redomestication being finalized, as noted in the referral. He said the proposed revisions to the Introduction – Interstate Communication and Cooperation section of the Handbook are intended to encourage state insurance regulator communication before a priority insurer is approved for redomestication.
- b. Analysis Efficiencies Related to Intercompany Pooling Arrangements and Holding Company Analysis

Weaver said the next set of proposed revisions is in response to a recommendation and a separate referral from the Ad Hoc (E/F) Subgroup for analysis efficiency related to intercompany pooling arrangements and holding company analysis.

Good provided an overview of the proposed revisions related to intercompany pooling arrangements. He said states have the option to complete a combined risk assessment and/or insurer profile summary for intercompany pools, but only if all pool participants are domiciled in the same state. The Subgroup recommended expanding this to all pool participants, including those domiciled in other states. The work would be completed by the domestic state of the pool lead, at its discretion. Other states that intend to rely on the combined work will have 30 days to review and accept the work of the pool lead state as satisfying all requirements for conducting a legal entity analysis. Good stated that the proposed revisions of the Subgroup are included in the risk assessment.

Jane Koenigsman (NAIC) provided an overview of the proposed revisions related to holding company analysis. She said the Subgroup recommended that both the lead state and the non-lead state can gain efficiencies in the review of Form F and the Corporate Governance Annual Disclosure (CGAD), where it is filed on a group basis. She said the lead state would still be responsible for reviewing both group filings, but where the CGAD is filed on a legal entity basis, it would still be the responsibility of the domestic regulator. She said the change would no longer require a separate analysis worksheet or checklist. The takeaways and risks from either filing will be documented in the Enterprise Risk Management (ERM) and Corporate Governance sections of the Group Profile Summary (GPS). She said non-lead states could still contact the lead state for more information if the GPS indicates concerns, if necessary. She stated that Form F and the CGAD appear in more than 20 different sections of the Handbook, but some require only minor revisions.

c. Investments Involving Related Parties

Weaver said the next set of proposed revisions is related to investments involving related parties that resulted from a new disclosure column in the investment schedules.

Koenigsman provided an overview of the proposed revisions. She said NAIC staff are proposing a new procedure in the Credit, Market, Liquidity, and Operational Risk Repositories for identifying material exposure to investments involving related parties. She said the procedure also addresses concerns with material related

party exposure to investment management and advisory services. She said NAIC staff also propose qualitative procedures related to expertise, fee structures, and investment policies.

d. Branded Risk Assessment, Insurer Priority Rating, and Health Plan Star Ratings

Weaver said a referral was received from the Risk-Focused Surveillance (E) Working Group to enhance Handbook guidance related to branded risk assessment, insurer priority rating, and health plan star ratings.

Koenigsman provided an overview of the proposed revisions:

- **Branded Risk Assessment and Insurer Priority Rating:** Koenigsman stated that the proposed revisions to the risk assessment are designed to clarify guidance regarding how the three branded risk assessment levels—significant, moderate, and low—are defined. She said this was due to situations where the analyst may have assessed some risks too high because it was the insurer's highest risk compared to other risks, but it may not pose a significant risk to financial solvency.
- **Health Plan Star Ratings:** Koenigsman said the proposed change includes a new procedure in the Reputational Risk Repository for health insurers. She said this procedure is for assessing the impact of the rating or changes in the rating on the insurer's reputation and strategic plans going forward.

e. AG 53

Weaver said the next set of proposed revisions related to *Actuarial Guideline LIII—Application of the Valuation Manual for Testing the Adequacy of Life Insurer Reserves* (AG 53) resulted from a new guideline adopted by the NAIC at the Summer National Meeting.

Ralph Villegas (NAIC) provided an overview of the proposed revisions. He said NAIC staff recommend new guidance on complex assets in the Reserving Risk Repository – Life/Accident and Health (A&H)/Fraternal. He said NAIC staff also recommend new guidance in the Statement of Actuarial Opinion Worksheet – Life/A&H/Fraternal regarding assumptions and sensitivity testing, asset adequacy testing (AAT) on high-yielding complex assets, and whether concerns exist in meeting asset adequacy requirements. He said the proposed revisions also include a footnote explaining that additional guidance may be added in the future, as this is a new reporting requirement for annual 2022.

The Financial Analysis Solvency Tools (E) Working Group agreed to expose the proposed revisions to the Handbook related to: 1) Terrorism Reinsurance, Affiliated Agents, Monitoring Startup Insurers, and Redomestication Communication (Attachment \_-B); 2) Intercompany Pooling Arrangements (Attachment \_-C); 3) Holding Company Analysis (Attachment \_-D); 4) Investments Involving Related Parties (Attachment \_-E); 5) Branded Risk Assessment, Insurer Priority Rating, and Health Plan Star Ratings (Attachment \_-F); and 6) AG 53 (Attachment \_-G) for a 30-day public comment period ending Nov. 18.

3. Received Referral from the Climate and Resiliency (EX) Task Force

Weaver said the next item of business is to receive a referral from the Climate and Resiliency (EX) Task Force. She said the Task Force designated a Solvency Workstream to explore potential enhancements to existing solvency monitoring processes surrounding this topic. After the Workstream held a series of public panels on various climate solvency-related topics and solicited input on potential enhancements to existing regulatory tools, the Working Group was asked to consider enhancements to the Handbook. This includes procedures for utilizing the P/C catastrophe reporting data; any investment stress scenario results available from the NAIC



Capital Markets Bureau; and climate risk exposure survey results, if available, in conducting ongoing financial analysis.

Weaver said this is a referral (Attachment \_-H) that requires further consideration and work to develop the enhancements to the Handbook, and the work will extend into next year. She directed NAIC staff to proceed with drafting changes for 2023.

#### 4. Discussed Other Matters

Schwartz shared information about the work he has been doing on the Insurance Regulatory Information System (IRIS) ratios. He said this involves looking at the ratios in different formats and determining whether it may be necessary to eliminate some of the current ratios, as well as create new ones. He said he is also looking at the ceilings and floors for each ratio and replacing them with percentiles. He said he would make a formal recommendation to the Working Group as soon as the work is completed.

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

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## III.B.6.a. Pricing/Underwriting Risk Repository – P/C Annual

----- **DETAIL ELIMINATED TO CONSERVE SPACE** -----**Premium Production, Concentration and Writings Leverage**

2. Determine whether concerns exist regarding changes in the volume of premiums written, changes in the insurer's mix of business (lines of business and/or geographic location) and changes in writing leverage.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Change in gross premiums written		>25% or <-25%	[Data]	[Data]
b. Change in net premiums written		>25% or <-25%	[Data]	[Data]
c. Change in direct premiums written (DPW) for any line of business		>33% or <-33%	[Data]	[Data]
d. Ratio of DPW for any new lines to total DPW		>5%	[Data]	[Data]
e. Change in DPW in any one state when DPW is greater than 10% of total DPW in either the current or prior year-end		>50% or <-50%	[Data]	[Data]
f. Ratio of DPW in a new state to total DPW		>5%	[Data]	[Data]
g. Gross premiums written to surplus [IRIS #1]	ST*	>900%	[Data]	[Data]
h. Net premiums written to surplus [IRIS #2]	ST*	>300%	[Data]	[Data]
				<i>Other Risks</i>
i. If significant changes in premium volume are identified, consider the following procedures:				ST
i. Request and review additional information from the insurer (if necessary) to understand and evaluate the source(s) of significant changes in premium volume.				
ii. Evaluate the impact of the sources of changes on the underwriting/marketing strategy, profitability and solvency position of the insurer.				
j. Review, by line of business, premiums written by year in the Financial Profile Report for shifts in the mix of business between years and to gain an understanding of lines of business written.				ST
k. <a href="#">Determine whether the insurer has material exposure to losses resulting from acts of terrorism. If concerns are identified, consider the following procedures:</a>				<a href="#">ST</a>
i. <a href="#">Request additional data/information from the insurer to gain an understanding of its exposure to terrorism risk.</a>				
ii. <a href="#">If the insurer is subject to ORSA reporting, review information provided on terrorism exposure and risk assessment in the ORSA Summary Report or obtain the lead state's review (if applicable).</a>				
iii. <a href="#">Gain an understanding of the insurer's mitigation of terrorism risk through TRIA coverage.</a>				
iv. <a href="#">Assess the reasonableness of the ultimate exposure based on the insurer's business strategy and capital position.</a>				

## III.B.6.a. Pricing/Underwriting Risk Repository – P/C Annual

<p><u>v.</u> Consider the reasonableness of the insurer’s plan to limit exposures, such as policy limits, policy exclusions, location of risks, pricing modifications, non-renewal of certain policies, plans for diversification, or other risk mitigation strategies.</p>	
<p><del>k.l.</del> Review the Five-Year Historical Data of the Annual Financial Statement. Has there been a shift in the mix of gross premiums written or net premiums written from property lines to liability lines within the past five years? If so, evaluate the underwriting/marketing strategy of the insurer and its expertise in writing liability lines of business.</p>	
<p><del>l.m.</del> Review Annual Financial Statement, Schedule T for new direct business written in any state where the insurer is not licensed and verify that the insurer is authorized to write all lines of business written.</p>	LG
<p><del>m.n.</del> Review Annual Financial Statement, Schedule T and the writings section in the Financial Profile Report to evaluate the top states in terms of direct premiums and the percentage of total DPW in those states. Based on the lines of business written, determine whether large concentrations of premiums are written in areas prone to catastrophic events.</p>	ST
<p><del>n.o.</del> Is the company diversified in terms of product lines and geographical exposure? If not, request and review information from the insurer regarding mitigation strategies to limit exposure concentrations.</p>	ST
<p><del>o.p.</del> Review the insurer’s underwriting/marketing strategy included in its business plan.</p> <ol style="list-style-type: none"> <li>i. If 2.e is “yes,” evaluate the insurer’s marketing and expansion plans in that state.</li> <li>ii. Is the insurer planning expansion into new states or premium growth in the future?</li> <li>iii. Has the insurer applied for or received new licenses in other states?</li> <li>iv. Has the insurer reported that it has ceased writing new business, a line of business or writing in a certain geographical location?</li> <li>v. Does the insurer have closed block operations?</li> <li>vi. Does the insurer’s marketing strategy and projected premium growth match actual results reported in the current period? If materially different, evaluate the reasons why, or ask the insurer for an explanation.</li> </ol>	ST
<p><del>p.q.</del> Determine whether the insurer has expertise (e.g., distribution network, underwriting, claims, and reserving) in the lines of business written. Consider reviewing the insurer’s MD&amp;A, business plan and/or additional information from the insurer to determine the expertise in the lines of business written.</p>	
<p><del>q.r.</del> Review the insurer’s gross and net writings leverage positions to assist in evaluating risk exposure. Consider the following specific procedures in this area:</p> <ol style="list-style-type: none"> <li>i. Compare the gross writings leverage and net writings leverage ratios to the industry averages and determine any significant variances.</li> <li>ii. If the insurer is a member of a group, compute the gross premiums written to surplus ratio and the net premiums written to surplus ratio on a consolidated basis to determine if the group appears to be excessively leveraged.</li> <li>iii. Obtain an explanation from the insurer for unusual results for P/C IRIS ratios #1 and #2.</li> </ol>	ST

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## III.B.6.d. Pricing/Underwriting Risk Repository – Analyst Reference Guide

----- DETAIL ELIMINATED TO CONSERVE SPACE -----

**Discussion of Annual Procedures**

----- DETAIL ELIMINATED TO CONSERVE SPACE -----

**Quantitative and Qualitative Data and Procedures – Property & Casualty**

----- DETAIL ELIMINATED TO CONSERVE SPACE -----

**Premium Production, Concentration and Writings Leverage**

**PROCEDURE #2** assists analysts in determining whether concerns exist regarding changes in the volume of premiums written or changes in the insurer's mix of business. Significant increases or decreases in premiums written may indicate a lack of stability in the insurer's operations. In addition, a significant increase in premiums written may be an indication of the insurer's entrance into new lines of business or sales territories, which might result in financial problems if the insurer does not have expertise in these new lines of business or sales territories. Significant increases in premiums written might also be an indication that the insurer is engaging in cash flow underwriting. Cash flow underwriting is the practice of writing a significant amount of business in order to invest and earn a greater investment return than the costs associated with potentially underpriced business. Cash flow underwriting can be a serious concern if it is accompanied by a shift in business written from short-tail property lines of business to long-tail liability lines.

Analysts should consider reviewing premiums written by line of business to determine which lines increased or decreased significantly and whether any new lines of business are being written. Analysts should also consider verifying that the insurer is authorized to write all lines of business being written. If new lines of business are being written, or if premiums are being written in new states, analysts should consider determining whether the insurer has expertise in the new lines of business or new sales territories. This would include expertise in distribution, underwriting, claims, and reserving. There is no information in the Annual Financial Statement to assist analysts in making this determination. However, there may be helpful information in the insurer's Management's Discussion and Analysis (MD&A). Otherwise, information may be requested from the insurer. Analysts should also consider determining if, as a result of changes in the mix of business, the insurer's business is concentrated in specific geographic areas, which could result in the insurer being potentially exposed to catastrophic losses.

[Within several lines of business and policy types \(most notably commercial property\), property/casualty insurers may be exposed to losses resulting from acts of terrorism. Following the September 11, 2001 attacks on the New York World Trade Center and the U.S. Pentagon, terrorism coverage became prohibitively expensive, if offered at all. In response, the U.S. Congress passed the Terrorism Risk Insurance Act \(TRIA\) of 2002. TRIA was initially created as a temporary three-year federal program that required insurers to offer commercial policyholders with terrorism coverage, while allowing the Federal Government to share monetary losses with insurers on commercial property/casualty losses from a terrorist attack. Since then, it has been renewed four times and is due to expire on December 31, 2027. Before this backstop can be accessed, several stipulations and limits are applied, many of which have been adjusted under subsequent extensions of the Act to limit the support available to insurers. Analysts should assess the insurer's exposure to losses related to acts of terrorism and consider any mitigation by TRIA.](#)

Procedure #2 also assists analysts in determining whether the insurer is excessively leveraged due to the volume of premiums written. Surplus can be considered as underwriting capacity, and the ratios of gross and net writings leverage measure the extent to which that capacity is being utilized and the adequacy of the insurer's surplus cushion to absorb losses due to pricing errors and adverse underwriting results. A gross writings leverage ratio result greater than 900% may indicate that the insurer is excessively leveraged, and special attention should be given to the adequacy of the insurer's reinsurance protection and the quality of the reinsurers. A net writings

**III.B.6.d. Pricing/Underwriting Risk Repository – Analyst Reference Guide**

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leverage ratio greater than 300% may also indicate that the insurer is excessively leveraged and lacks sufficient surplus to finance the business currently being written. In evaluating these ratios, analysts should also consider the nature of the insurer's business. For example, an insurer that has historically written primarily short-tail property lines of business might not be considered excessively leveraged even though it has higher ratio results, because the risk of significant underpricing or adverse underwriting results is less than that of an insurer that writes primarily volatile long-tail liability lines of business such as medical professional liability.

Analysts should consider reviewing the net premiums written by line to determine which lines of business are being written. An insurer that writes primarily short-tail property lines may be able to write at higher levels of premiums to surplus than an insurer that writes primarily long-tail liability lines, because the risk of underpricing and significant adverse underwriting results is less with the short-tail property lines of business. Analysts should also consider comparing the ratios of gross and net writings leverage to industry averages to help evaluate the insurer's leverage. If the insurer is a member of an affiliated group of insurers, analysts might want to compute the net and gross writings leverage ratios on a consolidated basis to help evaluate whether the affiliated group of insurers is excessively leveraged. If the net and gross writings leverage ratios results are high, analysts should consider determining whether the insurer has adequate reinsurance protection against large losses and catastrophes and that the reinsurers are of high quality.

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## III.B.1.a. Credit Risk Repository – P/C Annual

----- **DETAIL ELIMINATED TO CONSERVE SPACE** -----

**NOTE – THE SAME CHANGES BELOW WOULD BE APPLIED TO THE LIFE/HEALTH AND HEALTH REPOSITORIES (III.B.1.b and III.B.1.c)**

### Uncollected Premium and Agents' Balances

#### 12. Review and assess uncollected premiums and agents' balances for potential collectability issues.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of uncollected premiums and agents' balances to surplus [IRIS ratio #10]	LQ	>40%	[Data]	[Data]
b. Change in uncollected premiums and agents' balances from the prior year		>25% or <-25%	[Data]	[Data]
c. Ratio of uncollected premiums to net premium income	LQ	>5%	[Data]	[Data]
d. Ratio of non-admitted uncollected premiums to total uncollected premiums	LQ	>10%	[Data]	[Data]
e. Net agents' balances and premium balances charged off and recovered to total uncollected agents' balances and premium balances		>5%	[Data]	[Data]
				<i>Other Risks</i>
f. Review amounts non-admitted and compare to prior years.				
g. With respect to agents' balances, verify the creditworthiness of the agent.				

#### ***Additional Analysis and Follow-up Procedures***

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##### **Uncollected Premium and Agents' Balances:**

- Explanation for the significant balance
- Listing of balances of subscribers, which individually account for 10% or more of the premiums uncollected and compare to a similar list from prior years
- Amounts of any uncollectable balances that have been written off in the current period. Compare the write-offs to those of the prior reporting period, if any
- Written procedures for monitoring and collecting uncollected premiums, including amounts already written off
- If the insurer has factored or sold its uncollected premium balances to a third party, note whether the receivables were discounted in the transaction
- Concerns over uncollected agents' balances warrants further investigation to ensure that adequate controls are in place and that trust accounts are properly managed. An increase or trend of material non-admitted agents' balances or write-offs may be a sign of mismanagement or misappropriation of premium

**III.B.1.a. Credit Risk Repository – P/C Annual**

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trust accounts by the agency. If there are concerns in this area, consider the following:

- Request additional data/information from the insurer to identify the source(s) of the balances and the reason(s) for the non-admitted or charged-off amounts.
- Request the insurer to provide a summary of the controls in place over agencies and ensure proper management and oversight of trust accounts.
- Request monthly reports from the insurer.
- Discuss concerns with the exam team, including whether a targeted exam is necessary.

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## III.B.1.d. Credit Risk Repository – Analyst Reference Guide

----- DETAIL ELIMINATED TO CONSERVE SPACE -----

**Discussion of Annual Procedures**

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**Other Receivables**

<i>Property/Casualty #</i>	<i>Life/A&amp;H/Fraternal #</i>	<i>Health #</i>
<b>11, 12</b>	<b>N/A</b>	<b>8, 9, 10</b>

The procedures assist analysts in reviewing receivable assets of an insurer that may have limited collectability.

**Uncollected Premiums and Agents' Balances**

The asset for uncollected premiums and agents' balances [in the course of collection](#) includes amounts receivable that have been billed, but have not yet been collected.

[Agencies and brokers receive premium payments from insureds in a fiduciary capacity. Most states have laws that require the agent or producer to maintain trust accounts for the premiums they collect, which must be kept separate from their business operating funds. The premiums, net of commissions, are then remitted to the insurer or general agents from the accounts, leaving an audit trail.](#)

Although agents are used by health entities, they are generally used more extensively with P/C insurers or even life insurers. Agents' balances are admitted to the extent that the assets conform to the requirements of SSAP No. 6—*Uncollected Premium Balances, Bills Receivable for Premiums, and Amounts due from Agents and Brokers*, which also requires that premiums owed by agents should be reported net of commissions and are non-admitted under a 90-day rule. Remaining amounts that are determined to be uncollectable must be written off. Generally, if a contract with an agent permits offsetting, amounts payable to an agent may be offset against a receivable from that agent. Agents' balances carry credit risk and can have a material impact on the net income and capital and surplus of an insurer if the balances are significant. Significant or growing balances can also lead to liquidity problems if the insurer is unable to convert the receivables into cash to be used to pay claims.

Irrespective of the type of business written, inadequate systems and controls over the collection process can lead to uncollectable premiums. Uncollected premium balances on non-government business that are over 90 days due are non-admitted under SSAP No. 6. On all business, an evaluation of any remaining asset balance is required to determine any impairment. Amounts deemed uncollectable are required to be written off against income in the period the determination is made. These accounting requirements are designed to limit the total impact that collectability issues can have on an insurer at a given point in time.

Despite the efforts to mitigate the impact of uncollected premiums and agents' balances, write-offs and non-admitted unpaid premium assets can still have a material impact on the net income and capital and surplus of an insurer. These issues can lead to liquidity problems if the insurer is unable to convert the receivable into cash to be used to pay claims. Analysts should monitor the level of this asset as well as the change in the balance to help identify potential collection problems that can ultimately lead to significant decreases in surplus.

[A material amount of uncollected agents' balances warrants further investigation to ensure that adequate controls are in place and that trust accounts are properly managed. An increase or trend of material non-admitted balances or write-offs may be a sign of mismanagement or misappropriation of trust accounts by the agency and should be investigated. Although this could occur at any agency, the risk is greater at affiliated agencies for the following reasons:](#)

- [The same owner controls both sides of the transaction](#)
- [There is a lack of internal controls in relation to management overrides](#)
- [Affiliated agency balances are often more material to small or medium-sized insurers](#)



**III.B.1.d. Credit Risk Repository – Analyst Reference Guide**

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- Affiliated agencies may not be subject to the same level of oversight as unaffiliated agencies
- In the event of financial stress to the insurer or the agency, there may be an inherent conflict of interest

If the analyst has concerns about the timely collection of agents' balances, the additional procedures related to premium trust accounts in the repository should be considered.

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## III.B.9.a. Strategic Risk Repository – Annual (All Statement Types)

----- **DETAIL ELIMINATED TO CONSERVE SPACE** -----**Business Plans****5. Evaluate the effectiveness of the insurer's business/strategic planning process and whether the current plan adequately addresses the significant solvency risks facing the insurer.**

	<i>Other Risks</i>
<p>a. Review previous business plans and financial projections filed with the state insurance department, and determine the following:</p> <ol style="list-style-type: none"> <li>i. Have significant changes in business plan or philosophy occurred? If "yes," explain.</li> <li>ii. Assess if initiatives outlined in the business plan have been accomplished.</li> <li>iii. Compare actual with projected financial results. Are actual results consistent with management's expectations? If not, explain.</li> <li>iv. Request an explanation for the variance including an explanation of whether management believes it has achieved its goals for the period and if any noted risks or challenges were not considered in the business plan.</li> <li>v. Request a revised business plan.</li> <li>vi. Describe any events, transactions, market conditions and/or strategic management decisions that have occurred (or are planned) that may cause a significant positive or negative variance from projections, including new product development or enhancements, changes in sales volume, product mix, or geographical locations.</li> <li>vii. Are there internal and/or external prospective risks that have the potential to impact the overall business plan?</li> </ol>	OP
<p>b. If necessary, request and review an updated strategic business plan, note any areas of concern and if necessary, request additional explanations from the insurer.</p> <ol style="list-style-type: none"> <li>i. Does the new business plan reflect significant changes in the strategic goals or philosophies compared to the prior plan? If "yes," explain.</li> <li>ii. Describe the insurer's strategic and annual planning process.</li> <li>iii. Describe the board of directors' involvement in developing and implementing the business plan.</li> <li>iv. Assess the insurer's ability to attain the expectations of the business plan and projections. Does the business plan reflect changes that appear unrealistic for the current market environment, financial position of the insurer or other circumstances? If "yes," explain. <ul style="list-style-type: none"> <li>• Reasonableness of underwriting assumptions</li> <li>• Current and anticipated interest rate and economic environment</li> <li>• Growth objectives</li> <li>• Stability of capital and ability to access additional capital, if needed</li> <li>• Quality and sources of earnings (trends and stability)</li> <li>• Dividends and dividend payout policy</li> </ul> </li> </ol>	OP
<p><u>c. For startup insurers that project rapid growth and material losses, consider the following:</u></p>	<u>OP</u>

**III.B.9.a. Strategic Risk Repository – Annual (All Statement Types)**

- |   |  |
|---|--|
| <ul style="list-style-type: none"><li>i. <u>Obtain a five-year business plan and assess the insurer’s current and projected capital adequacy relative to its growth plans.</u></li><li>ii. <u>If future growth is to be funded by capital contributions from the parent, assess the parent’s ability to meet future funding expectations.</u></li><li>iii. <u>Determine whether growth and capital financing expectations are sustainable until the insurer becomes profitable.</u></li></ul> |  |
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III.B.9.b. Strategic Risk Repository – Analyst Reference Guide

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### Discussion of Annual Procedures

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### Quantitative and Qualitative Data and Procedures

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#### Business Plans

**PROCEDURE #5** directs analysts to evaluate the effectiveness of the insurer’s business/strategic planning process and whether the current plan adequately addresses the significant solvency risks facing the insurer. After obtaining and reviewing a current business plan from the insurer, analysts should determine whether any changes have been made in the business goals or philosophies. Analysts should consider the overall planning process (e.g., who is involved, how frequently it occurs, etc.) and how the overall initiatives are determined. In addition, analysts may consider discussing with the insurer any assumptions used in establishing the goals. Analysts should assess whether the current management team has the expertise to attain the goals of the business plan. Through communication with the insurer, analysts should document any detailed explanations regarding variances in projected financial results and the insurer’s intended plan to address variances. If analysts determine the goals of the business plan are not attainable and/or projections are unreasonable, a revised business plan may be requested.

Special consideration should be given to startup insurers that project rapid growth and significant underwriting and net losses. In many cases, startups rely heavily on the parent company’s capital contributions to finance operations until the insurer can achieve profitability. The analyst should evaluate the reasonableness of the insurer’s business plan and projections and determine whether the plan is attainable.

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**I. Introduction B. Interstate Communication and Cooperation**

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**Redomestication and Acquisition—Communication of Regulatory Actions and Analysis**

Communication between states in situations where a company has redomesticated or is being acquired by a party that owns other insurers since the last annual analysis is an important step in conducting effective solvency oversight. In addition to the review of the application for redomestication or Form A, the state insurance regulator should engage the domestic state insurance regulator of the former state in the case of redomestication or the lead state or domestic state(s) of other insurers in the new group in the case of Form A in communication to request the Insurer Profile Summary (IPS), supervisory plan and other relevant solvency monitoring information to effectively incorporate insights from the other domestic state's supervisory plan into the current analysis. In these situations, it is imperative that state insurance regulator concerns and supervisory plans be appropriately transitioned to avoid losing regulatory insights accumulated over years of oversight. Communication should include (but not be limited to) such items as:

- IPS and supervisory plan, including analysis detail for significant risks
- History of regulatory actions
- History of communication with the insurer/group
- Assessment of senior management, board of directors and corporate governance
- Findings (i.e., Summary Review Memorandum (SRM), exam report and management letter) from the most recent financial and market conduct examinations, including the status of the resolution to issues identified
- Assessment of Enterprise Risk Management (ERM)
- Group Profile Summary (GPS) and Supervisory Plan from the holding company analysis, including detail on any significant risks obtained from the lead state
- Assessment of Own Risk and Solvency Assessment (ORSA) Summary Report, if applicable, and Form F

[In situations where the company seeking redomestication is considered a priority company \(i.e., NAIC 1 or 2\) by the current domestic state, the department should communicate the company's intent to redomesticate with all licensed states prior to approval. This type of communication will ensure that all licensed states are informed of the company's plan and encourage an open dialogue between all interested regulators as part of the approval process.](#)

### III.A.4. Risk Assessment (All Statement Types) – Analyst Reference Guide

## Discussion of Analysis for Intercompany Pooling Arrangements

Intercompany pooling arrangements involve the establishment of a quota share reinsurance agreement under which pooled business is ceded to a lead entity and then retroceded back to pool participants in accordance with stipulated shares (if any). This generally results in pool participants sharing exposure to the various insurance risks ceded into the pool. Because of this structure, financial analysts may be able to gain efficiencies by conducting and documenting the analysis of insurance risks associated with the pooled business on a combined basis and then leveraging the results of that work to complete legal entity analysis. For example, in situations where the majority of the group's writings are ceded into the intercompany pool and there are few unique legal entity risks, analysts may choose to create and maintain a combined risk assessment and/or IPS for all of the legal entities participating in the pool ~~(if domiciled in the same state)~~. In other situations, it may be more appropriate to maintain separate risk assessment worksheets and/or IPSs for each legal entity, but to reference work completed in the pool lead's documentation or include substantially similar information in each legal entity's risk assessment worksheet and IPS.

While insurers participating in intercompany pooling arrangements often share exposure to pooled insurance risks, differences in the overall risk exposure of participants may arise due to a number of factors including, but not limited to, the following:

- Surplus/RBC levels
- Balance sheet composition
- Pool participation percentages
- The timing of pool participation
- Premiums not ceded to the pool
- Reinsurance arrangements outside of the pool (e.g., facultative placement prior to cessions to the pool lead)
- Current or legacy risks (e.g., asbestos exposure) disclosed within the financial statement

Regardless of the method utilized to assess and document the analysis of the pool, the financial analyst should ensure that all significant, unique exposures of each pool participant are separately assessed and addressed within analysis documentation.

If pool participants are domiciled in various states, communication and coordination across states is ~~strongly encouraged~~needed to achieve efficiencies in analysis. For example, ~~it might be appropriate for~~ the domestic state of the pool lead would generally be expected to indicate to the analysts of the other insurers in the pool that if it intends to complete a combined risk assessment and IPS and specifically when both will be provided to the other domestic states for their review. This will complete the analysis of the pooled insurance risks early in the analysis cycle to enable other states with domestics in the pool to leverage the completed work. To allow sufficient time for this coordination to take place, domestic states that intend to place reliance on the work of the pool lead state will have 30-days from the receipt of completed analysis work from the pool lead to complete the analysis of their legal entity or until the end of the prescribed analysis timeline, if longer. During this 30-day review period, prior to accepting the risk assessment and the IPS from the pool lead as satisfying all legal entity analysis requirements, each domestic state should consider and document the following:

- The extent to which they are satisfied with the quality of work performed by the pool lead state and willing to be judged on that work from an NAIC Accreditation perspective (if relevant);
- The extent to which the work performed by the pool lead addresses all relevant and material solvency risks of the individual legal entity, including common differences in the risk exposure of pool participants noted above; and

**III.A.4. Risk Assessment (All Statement Types) – Analyst Reference Guide**

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- [The completion of any supplemental, state specific analysis procedures \(compliance or otherwise\) that are necessary to finalize the legal entity analysis.](#)

In situations where an insurer cedes business to an intercompany pool but does not participate in retrocession, the analysis of the pooled business should be obtained/reviewed to evaluate reinsurance credit risk. If the pool is troubled or potentially troubled, this may require more in-depth analysis to evaluate the potential impact of claims associated with the insurer's direct writings not being covered by the pool.

**I. Introduction B. Interstate Communication and Cooperation**

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**Redomestication and Acquisition—Communication of Regulatory Actions and Analysis**

Communication between states in situations where a company has redomesticated or is being acquired by a party that owns other insurers since the last annual analysis is an important step in conducting effective solvency oversight. In addition to the review of the application for redomestication or Form A, the state insurance regulator should engage the domestic state insurance regulator of the former state in the case of redomestication or the lead state or domestic state(s) of other insurers in the new group in the case of Form A in communication to request the Insurer Profile Summary (IPS), supervisory plan and other relevant solvency monitoring information to effectively incorporate insights from the other domestic state's supervisory plan into the current analysis. In these situations, it is imperative that state insurance regulator concerns and supervisory plans be appropriately transitioned to avoid losing regulatory insights accumulated over years of oversight. Communication should include (but not be limited to) such items as:

- IPS and supervisory plan, including analysis detail for significant risks
- History of regulatory actions
- History of communication with the insurer/group
- Assessment of senior management, board of directors and corporate governance
- Findings (i.e., Summary Review Memorandum (SRM), exam report and management letter) from the most recent financial and market conduct examinations, including the status of the resolution to issues identified
- Assessment of Enterprise Risk Management (ERM), [including risks from Form F that are provided in the GPS or provided by the lead state](#)
- Group Profile Summary (GPS) and Supervisory Plan from the holding company analysis, including detail on any significant risks obtained from the lead state
- Assessment of Own Risk and Solvency Assessment (ORSA) Summary Report, if applicable, ~~and Form F~~



## II. Risk-Focused Financial Analysis Framework

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### Group-Wide Supervision

The Group-Wide Supervision procedures establish guidance for lead state use in the analysis of insurance company holding systems. This includes a risk-focused approach to group regulation where specific risks that are relevant to insurance holding company structures are addressed.

- **INSURANCE HOLDING COMPANY SYSTEM ANALYSIS DOCUMENTED IN THE GROUP PROFILE SUMMARY (GPS) (LEAD STATE):**

- Understanding the insurance holding company system (lead state)
- Addressing lead state analysis considerations
- Evaluating the overall financial condition of the holding company system by completing a detailed analysis through the group's exposure to each of the nine branded risk classifications
- Assessing corporate governance and enterprise risk management
- Documenting material concerns or conditions in the group that affect the lead state's domestic companies
- Performing additional procedures on key risk areas, as needed
- Sharing the results of the analysis, through the GPS, with other impacted regulators on a timely basis

- **CORPORATE GOVERNANCE DISCLOSURE PROCEDURES**

The *Corporate Governance Annual Disclosure Model Act* (#305) and *Corporate Governance Annual Disclosure Model Regulation* (#306) require an insurer, or an insurance group, to file a summary of an insurer or insurance group's corporate governance structure, policies and practices with the commissioner by June 1 of each calendar year. [The Lead State should take primary responsibility for reviewing the CGAD filing, if it is filed on a group basis, and should incorporate any takeaways or concerns into the GPS. Any concerns relevant only to a specific insurance entity in the group should be communicated to the domestic state in a timely manner.](#) ~~As of the date of this publication, most states had not adopted such legislation. These procedures are applicable to only those states that have adopted such legislation.~~

- **OWN RISK AND SOLVENCY ASSESSMENT (ORSA) PROCEDURES**

The *Risk Management and Own Risk and Solvency Assessment Model Act* (#505) requires insurers above a specified premium threshold, and subject to further discretion, to submit a confidential annual ORSA Summary Report.

- **FORM F PROCEDURES**

[The Form F is filed with the lead state commissioner of the insurance holding company system for every insurer subject to registration under the \*Insurance Holding Company System Regulatory Act\* \(#440\). The Form F review is to be completed by the lead state in conjunction with the review of Form B. The lead state analyst should identify the material risks within the insurance holding company system that could pose enterprise risk to the insurers in the group. Takeaways and concerns from the review should be documented in the GPS. Any concerns relevant only to a specific insurance entity in the group should be communicated to the domestic state in a timely manner.](#) ~~The Form F is filed with the lead state commissioner of the insurance holding company system for every insurer subject to registration under the *Insurance Holding Company System Regulatory Act* (#440).~~

- **PERIODIC MEETING WITH THE GROUP PROCEDURES**

These procedures are intended to demonstrate the type of potential questions a lead state may want to consider when it conducts a periodic meeting with the group.

## II. Risk-Focused Financial Analysis Framework

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- **TARGETED EXAMINATION PROCEDURES**

The targeted examination procedures provide examples of potential risk areas where the lead state may want to perform certain limited examination procedures as part of the continual risk assessment process.

### **LEAD STATE REPORT**

The Lead State Report is located in iSite+, within Summary Reports, and is designed to improve communication and coordination between state insurance regulators. It provides a list all insurance groups and the companies within each group, which can be sorted in various ways. The report also contains current contact information for the state's assigned insurance company analyst and the state's chief analyst, which is maintained by state insurance department staff.

## III.B.2.a. Legal Risk Repository – Annual (All Statement Types)

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

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## Fraud

### 3. Assess if any material fraudulent activity has been identified and evaluate the financial impact of such activity.

	Other Risks
a. Were any fraud concerns disclosed during the review of the Annual Financial Statement, including the Notes to Financial Statements, Audited Financial Statement, and Examination findings (i.e., Exhibit G)?	
b. Contact the state insurance department's Fraud Unit (if applicable). Has the state insurance department concluded any fraud investigations involving the insurer? If so, identify the following: <ul style="list-style-type: none"> <li>• Nature and scope of the investigation and its findings</li> <li>• Regulatory and/or corrective actions required of the insurer</li> <li>• Insurer's plan to address the fraudulent activity</li> <li>• Financial impact of the investigation and corrective actions</li> </ul>	
c. Do any news and media reports, information from the insurer or other information available to the analyst indicate the insurer is under investigation by any regulatory body other than the state insurance department? If so, identify the nature and scope of the investigation and impact on the insurer to determine if further information should be requested from the other regulatory body.	RP
d. Review Regulatory Actions (Regulatory Information Retrieval System—RIRS) on iSite+. Were any regulatory actions taken by other states identified as fraud? If so, and if not communicated to the state insurance department, contact the reporting state insurance department to obtain information regarding the regulatory action.	
e. Contact other regulatory agencies that have regulatory authority over the business of the insurer (e.g., federal agencies where the insurer is engaged in government contracts). Have any regulatory authorities concluded any fraud investigations involving the insurer? If so, request the following information: <ul style="list-style-type: none"> <li>• Nature and scope of the investigation and its findings</li> <li>• Regulatory and/or corrective actions required of the insurer</li> <li>• Insurer's plan to address fraudulent activity</li> <li>• Financial impact of the investigation and corrective actions</li> </ul>	RP
f. Review <a href="#">the GPS and any other information provided by the lead state for any legal risks of the group or the insurance entity (e.g., from the Form F - Enterprise Risk Report)</a> <del>filed with the lead state</del> . Were any investigations, regulatory activities or litigations that may impact the insurer or holding company reported?	
g. If the above analysis indicates concerns related to current or prior fraud, inquire of the	

## III.B.2.a. Legal Risk Repository – Annual (All Statement Types)

insurer regarding its internal processes and controls for preventing fraud.

**Compliance with Code of Ethics Standards****4. Assess the insurer's compliance with code of ethics standards.**

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Identify if senior officers are subject to code of ethics standards [Annual Financial Statement, General Interrogatories, Part 1, #14.1 and #14.11]		=NO	[Data]	[Data]
b. Identify if the code of ethics has been amended [Annual Financial Statement, General Interrogatories, Part 1, #14.2 and #14.21]		=YES	[Data]	[Data]
c. Identify if the code of ethics has been waived [Annual Financial Statement, General Interrogatories, Part 1, #14.3 and #14.31]		=YES	[Data]	[Data]
				<i>Other Risks</i>
d. Determine if the responses provided in 4.a, 4.b, or 4.c identify any concerns with the insurer's compliance with code of ethics.				
<b>e. <u>Corporate Governance Annual Disclosure (CGAD):</u></b> i. <u>If filed on an insurance entity basis available</u> , does the information provided in the <del>Corporate Governance Annual Disclosure</del> <u>CGAD</u> filing on ethics policies identify any concerns with the insurer's ethics standards or conflict with information reported in Annual Financial Statement, General Interrogatories, Part 1, #14?				
ii. <u>If filed on a group basis, does the information provided in the GPS or provided by the lead state identify any concerns with the insurer's ethics standards or conflict with information reported in the Annual Financial Statement, General Interrogatories, Part 1, #14?</u>				

**Audit Committee**

Every insurer is required to have designated an Audit Committee, a percentage of whose members should be independent from the insurer depending upon premium volumes.

**14. Assess compliance with audit committee requirements.**

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Did the insurer fail to establish an Audit Committee in compliance with the domiciliary state insurance laws? If "yes," review information for an explanation. [Annual Financial Statement, General Interrogatories, Part 1, #10.5 and #10.6]		=YES	[Data]	[Data]
b. Has the insurer been granted any exemptions under Sections 7H, or 18A of the NAIC <i>Annual Financial</i>		=YES	[Data]	[Data]

**III.B.2.a. Legal Risk Repository – Annual (All Statement Types)**

<p><i>Reporting Model Regulation?</i> If “yes,” review information about the exemption. [Annual Financial Statement, General Interrogatories, Part 1, #10.1, #10.2, #10.3 and #10.4]</p>				
				<i>Other Risks</i>
<p>c. Does the Audit Committee membership meet independence requirements of the domiciliary state insurance laws?</p>				
<p><u>a. Corporate Governance Annual Disclosure (CGAD):</u></p> <p><u>i. If filed on an insurance entity basis, does the information provided in the CGAD <del>if available, does the information provided in the Corporate Governance Annual Disclosure filing</del> on auditor independence identify any concerns or conflict with information reported in the Annual Financial Statement, General Interrogatories, Part 1, #10?</u></p> <p><u>ii. If filed on a group basis, does the information provided in the GPS or provided by the lead state identify any concerns with the insurer’s ethics standards or conflict with information reported in the Annual Financial Statement, General Interrogatories, Part 1, #14?</u></p>				

## III.B.2.a. Legal Risk Repository – Quarterly (All Statement Types)

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**Compliance with Code of Ethics Standards****4. Assess the insurer's compliance with code of ethics standards.**

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Identify if senior officers are subject to code of ethics standards. [Quarterly Financial Statement, General Interrogatories, Part 1, #9.1]		=NO	[Data]	[Data]
b. Identify if the code of ethics has been amended. [Quarterly Financial Statement, General Interrogatories, Part 1, #9.2]		=YES	[Data]	[Data]
c. Identify if the code of ethics has been waived. [Quarterly Financial Statement, General Interrogatories, Part 1, #9.3]		=YES	[Data]	[Data]
				<i>Other Risks</i>
d. Determine if the responses provided in 4.a, 4.b, or 4.c identify any concerns with the insurer's compliance with the code of ethics.				
<b>e. <u>Corporate Governance Annual Disclosure (CGAD):</u></b> i. <u>If filed on an insurance entity basis, does the information provided in the CGAD filing on ethics policies identify any concerns with the insurer's ethics standards or conflict with information reported in Annual Financial Statement, General Interrogatories, #9?</u> ii. <u>If filed on a group basis, does the information provided in the GPS or provided by the lead state identify any concerns with the insurer's ethics standards or conflict with information reported in the Annual Financial Statement, General Interrogatories, #9?</u> <del>if available, does the information provided in the Corporate Governance Annual Disclosure filing on ethics policies identify any concerns with the insurer's ethics standards or conflict with information reported in General Interrogatory #9?</del>				

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## III.B.2.d. Legal Risk Repository – Analyst Reference Guide

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**Legal Risk Assessment**

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**Quantitative and Qualitative Data and Procedures**

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**Compliance with Code of Ethics Standards**

**PROCEDURE #4** directs the analyst to identify and evaluate risks related to the insurer's compliance with code of ethics standards. This procedure references information provided in the General Interrogatories of the Annual Statement related to the code of ethics. The analyst is encouraged to use this information, as well as information provided in the Corporate Governance Annual Disclosure (CGAD) (if [filed on an insurance entity basis](#) ~~available~~), to identify and assess risks in this area. [If the CGAD is filed on a group basis, rely on the information provided in the GPS for group risks or provided by the lead state if risks apply to the insurance entity.](#) If concerns regarding an insurer's failure to implement or abide by a code of ethics are identified, the analyst should correspond with the company to address these concerns and/or identify other compensating controls in place.

**Audit Committee**

**PROCEDURE #14** directs the analyst to assess compliance with audit committee requirements. As mandated by the *Annual Financial Reporting Model Regulation*, every insurer required to file an audited financial report is also required to have an audit committee that is directly responsible for the appointment, oversight and compensation of the auditor. Insurers with less than \$500 million in direct and assumed premium may apply for a waiver from this requirement based on hardship. Based on various premium thresholds, a certain percentage of the audit committee members must be independent from the insurer. However, if domiciliary law requires board participation by otherwise non-independent members, such law shall prevail and such members may participate in the audit committee. This procedure references information provided in the General Interrogatories of the Annual Statement related to whether the insurer has established an audit committee in accordance with state insurance laws and requires the insurer to report if it has been granted any exemptions in this area. In assessing compliance with these requirements, the analyst is encouraged to compare other information received on the corporate governance practices of the insurer, including the CGAD (if [filed on an insurance entity basis](#) ~~available~~), to information provided in the interrogatories. [Note, if the CGAD is filed on a group basis, the analyst should rely on the information provided in the GPS or provided by the lead state if material risks are only relevant to specific insurance entities.](#)

## III.B.5.a. Operational Risk Repository – P/C Annual

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NOTE – THE SAME CHANGES BELOW WOULD BE APPLIED TO THE LIFE/HEALTH AND HEALTH REPOSITORIES (III.B.5.b and III.B.5.c)

## Corporate Governance

2. Determine whether the corporate governance practices of the insurer provide effective oversight of operations.

	<i>Other Risks</i>
a. If the Corporate Governance Annual Disclosure (CGAD) is filed to your state as either the domestic state of a legal entity (not part of a group) or the lead state of a group, review and assess information on the insurer's or insurance group's corporate governance practices as provided in the CGAD to identify and follow up on any issues noted that could affect the insurer's <u>or the group's</u> ability to adequately oversee operations. <u>If your state is the lead state, document information and risk from the CGAD in the Group Profile Summary (GPS), and if materials risks relate only to an insurance entity, contact the domestic state in a timely manner.</u>	
b. If your state is not the lead state and the CGAD is filed to the lead state, review the corporate governance assessment included in the lead state's <del>Group Profile Summary (GPS)</del> and contact the lead state with any questions, concerns or follow-ups. <u>Upon the receipt of any additional information, the non-lead state should document any material concerns regarding corporate governance that could impact the financial condition (e.g., operations, policyholder surplus or capital position) of the domestic insurer.</u>	
c. Review and follow up on any issues noted in the department's documentation of corporate governance in the most recent examination reports, other examination documentation or summaries, communication with the examiner-in-charge, or the most recent communication with the insurer. Note any observations or follow-up analysis performed.	
d. Obtain a copy of and review the most recent board of directors' meeting minutes (i.e., may refer to last quarterly, monthly, etc., depending on the frequency of the meetings). Has the board of directors taken any significant actions that may result in changes in operations, business structure, or management that may result in a material financial impact on the insurer?	
e. Based on the above procedures, does the board of directors and management provide a sufficient level of oversight and support? Explain.	

### ***Additional Analysis and Follow-Up Procedures***

#### **Corporate Governance:**

If the CGAD is filed to your state as either the domestic state of a legal entity (not part of a group) or the lead state of a group and if concerns related to the corporate governance practices of the insurer or insurer group are identified:

- Consider reviewing internal resources on file related to the following, and if not on file, request the following information from the insurer:
  - For the board of directors and each committee established by the board of directors request a copy of



**III.B.5.a. Operational Risk Repository – P/C Annual**

- the charter/policy, the business ethic policy, code of conduct policy, and conflict of interest policy
- The most recent conflict of interest statement, or its equivalent, for each member of the board of directors and committees established by the board of directors including an explanation of any conflicts reported
  - Financial expertise or statutory accounting principles expertise of the audit committee
  - Reporting structure of the internal audit function
  - Copy of the company's by-laws currently in effect
  - If part of a holding company system, discussion on the level of oversight the parent company maintains over the insurer
  - Discussion of compliance with corporate governance statutes
  - Discussion of compensation policies, bonus/incentive programs, and management performance and assessment programs
  - Discussion of the board of directors' and management's responsibilities and authority
- If your state is not the lead state and the CGAD is filed to the lead state, [review the information provided in the GPS or other information provided by the lead state.](#) ~~e~~Contact the lead state with any questions, concerns or follow-ups. [Upon the receipt of any additional information, the non-lead state should document any material concerns regarding corporate governance that could impact the financial condition \(e.g., operations, policyholder surplus or capital position\) of the domestic insurer.](#)

## III.B.5.d. Operational Risk Repository – Analyst Reference Guide

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**Operational Risk Assessment**

**Operational Risk: The risk of financial loss resulting from inadequate or failed internal processes, personnel and systems, as well as unforeseen external events.**

The objective of Operational Risk Assessment analysis is to focus on risks inherent in the company's daily operations. As such, although operational risk encompasses overall profitability, other risks in this area may not be identified through traditional financial statement review. Therefore, analysts may require additional investigation and information requests to understand and assess the potential impact of these risks. For example, analysts may need additional information to assess the insurer's exposure to cybersecurity risks. In addition, information presented in the Enterprise Risk Report (Form F) and Own Risk and Solvency Assessment (ORSA) Summary Report (if available), [which are reviewed and risks documented by the lead state](#), may assist analysts in identifying and assessing the insurer's exposure to operational risks.

**Discussion of Annual Procedures****Corporate Governance**

<i>Property/Casualty #</i>	<i>Life/A&amp;H/Fraternal #</i>	<i>Health #</i>
<b>2, 3</b>	<b>2, 3</b>	<b>2, 3</b>

**PROCEDURE #2** assists analysts in determining whether concerns exist regarding the insurer's corporate governance practices. Analysts are asked to review the Corporate Governance Annual Disclosure (CGAD) filing (if [filed on an insurance entity basis available](#)) to identify and assess the governance practices in place at the insurer. [If the CGAD is filed on a group basis, the analyst should rely on the information provided in the GPS or provided by the lead state if material risks are only relevant to specific insurance entities.](#) In addition, analysts are encouraged to review the results of the corporate governance assessment conducted during the last on-site examination to identify issues or concerns to be considered or addressed. If concerns are identified, analysts may elect to request a copy of recent board minutes to review and/or contact the insurer regarding actions taken to address the concerns identified.

**Additional Analysis and Follow-Up Procedures**

**CORPORATE GOVERNANCE** directs analysts to use the CGAD and/or request additional information from the insurer [\(if filed on an insurance entity basis or your state is the lead state\)](#) to review and evaluate relevant policies and processes such as board/committee charters, code of conduct policy, conflict of interest policy, bylaws, compensation policies, etc. [If your state is not the lead state, rely on information provided in the GPS or provided by the lead state.](#)

## III.B.8.a. Reserving Risk Repository – P/C Annual

----- *DETAIL HAS BEEN ELIMINATED TO CONSERVE SPACE* -----

NOTE – THE SAME CHANGES BELOW WOULD BE APPLIED TO THE LIFE/HEALTH AND HEALTH REPOSITORIES (III.B.8.b and III.B.8.c)

### ***Additional Analysis and Follow-Up Procedures***

#### **Inquire of the Insurer:**

If concerns exist, consider requesting information from the insurer regarding:

- Request a copy of the qualified actuary’s actuarial report and review the actuary’s comments regarding the analysis performed and conclusions reached.
  - If additional questions or concerns are noted after reviewing the report, contact the appointed actuary to discuss the nature and scope of the reserve valuation procedures performed.
- Request a copy of the insurer’s business plan, and review the insurer’s plans to assess and mitigate reserve risks.
- Request information regarding any significant changes in reserve methodologies and assumptions, underwriting practices, case reserving, or claims handling practices with the potential to affect reserve setting.
- Request information on who ultimately determines the insurer’s carried reserves and the Board of Director’s role in overseeing the reserving process.
- If [filed on an insurance entity basis or if your state is the lead state](#) ~~available~~, review the insurer’s Corporate Governance Annual Disclosure (CGAD) filing to understand and assess the board of director’s role in overseeing the reserving process. [If your state is not the lead state, rely on the information provided in the Group Profile Summary \(GPS\) or provided by the lead state.](#)

### III.B.9.b. Strategic Risk Repository – Analyst Reference Guide

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----- *DETAIL HAS BEEN ELIMINATED TO CONSERVE SPACE* -----

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## Strategic Risk Assessment

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

The objective of Strategic Risk Assessment analysis is to focus on risks inherent in the company's business strategy and plans. As such, risks in this area are often prospective in nature and may require additional investigation and information requests to understand and assess their potential impact. For example, analysts may require an up-to-date business plan from the insurer to assess emerging risk exposures and prospective risks that could prevent the insurer from meeting its strategic goals. In addition, information presented in the Enterprise Risk Report (Form F) and Own Risk and Solvency Assessment (ORSA) Summary Report (if available) which the lead state reviews and documents risks, may assist analysts in identifying and assessing the insurer's exposure to strategic risks.

## III.A.4. Risk Assessment (All Statement Types) – Analyst Reference Guide

----- DETAIL HAS BEEN ELIMINATED TO CONSERVE SPACE -----

## Corporate Governance

As part of the risk-focused surveillance approach, analysts should work with the examination staff to assess the quality and reliability of corporate governance in order to identify, assess and manage the risk environment facing the insurer. This assessment will assist in identifying current or prospective solvency risk areas. Corporate Governance Disclosures ~~(if required in your state)~~ will assist in assessing corporate governance of the insurer or the insurer group. (See section VI.D. Corporate Governance Disclosure Procedures). By understanding the corporate governance structure and assessing the “tone at the top,” analysts will obtain information on the quality of guidance and oversight provided by the board of directors and the effectiveness of management, including the code of conduct established in cooperation with the board. To assist in this assessment, analysts may utilize:

- Board and audit committee minutes
- List of critical management and operating committees, the members and meeting frequencies
- Examination findings related to the insurer’s risk assessment and risk management activities
- Sarbanes-Oxley filings and similar filings through the NAIC Model Audit Rule, as applicable

## Discussion of Annual Procedures

**INFORMATION REQUEST PROCEDURE #11:** In order to effectively enhance risk-focused financial analysis, state insurance regulators may need to gain a greater understanding of the insurer’s strategies, risk exposures and business operations. While a general understanding of the insurer can be obtained through a review of regulatory filings and publicly available information, additional information may be needed on certain strategies, risk exposures and business operations before the insurer can be fully understood and evaluated.

State insurance regulators should first review existing sources of information available to the department (e.g., annual and quarterly statement Notes to Financial Statements and General Interrogatories, MD&A, filed business plans, recent examination results, etc.). Additionally, if the insurer is part of a holding company group and the department is not the lead state, if not already provided by the lead state, the ~~state insurance regulator~~non-lead state should contact the lead state to obtain analysis already prepared by the lead state for additional holding company group information ~~(e.g., i.e., the Group Profile Summary Holding Company Analysis, and ORSA Summary Report analysis, Form F, and Corporate Governance Annual Disclosure (CGAD) analysis).~~ For Corporate Governance Annual Disclosure (CGAD) filed on a group basis and the Enterprise Risk Report (Form F), the non-lead states should rely on the information provided in the GPS or other information provided by the lead state on material risk relevant to the insurance entity. Contacting the lead state first will help eliminate the duplicate requests for holding company group level information.

If it is determined that additional information is still needed, state insurance regulators may choose to conduct in-person meetings with the insurer, hold conference calls, submit written information requests or take other steps necessary to obtain a sufficient understanding of the insurer. If meetings or conference calls are scheduled with the insurer to gather additional information, state insurance regulators should give consideration to the level at which the meetings should be conducted (i.e., legal entity, intermediate holding company, or ultimate controlling parent) and involve the lead state and other affected state insurance regulators in the process as appropriate. If a meeting is conducted at the group level, lead states may also wish to consider topics and questions outlined in V.H. Periodic Meeting with Group.

The following table highlights topics where the information available through regulatory filings may not be sufficient to provide an adequate understanding of the insurer.

## III.A.5. Risk Assessment (All Statement Types) – IPS Example

**XX DEPARTMENT OF INSURANCE**  
**INSURER PROFILE SUMMARY**  
**COMPANY NAME**  
**As of 12/31/20XX**  
**Updated as of XX/XX/20XX**

**BUSINESS SUMMARY**

Provide a summary of the business operations and lines of business of the insurer.

ABC is an independently owned property and casualty insurance organization based in state X that specializes primarily in writing private passenger automobile insurance coverage. Through its subsidiaries, DEF Insurance Company, GHI Insurance Company, JKL Underwriters, and MNO Premium Finance Company, the group offers a variety of insurance related services including premium finance and claims processing.

**REGULATORY ACTIONS**

Discuss any significant actions taken against the company, permitted practices, issues of non-compliance, results from the most recent financial examination, etc.

In 20XX, ABC was required to file a corrective action plan with the department to address its breach of the RBC Company Action Level. Since that time, ABC received a capital infusion from its parent and has raised its RBC to an acceptable level. The company has been granted a permitted practice relating to its SCA investment in JKL Underwriters. The permitted practice allows ABC to admit its investment in JKL (\$2 million at 12/31/XX) without requiring an independent financial statement audit.

**FINANCIAL SNAPSHOT (SUMMARY DATA) – OPTIONAL****Assets and Liabilities**

<b>Years Ended December 31 (Dollars in millions)</b>	<b>20XX</b>	<b>20XX</b>
Total Invested Assets	219	253
Other Assets	111	131
<b>TOTAL ASSETS</b>	<b>330</b>	<b>384</b>

**LIABILITIES**

Insurance reserves	97	95
Other liabilities	169	193
<b>TOTAL LIABILITIES</b>	<b>266</b>	<b>288</b>
Capital and Surplus	64	96
<b>TOTAL LIABILITIES AND C&amp;S</b>	<b>330</b>	<b>384</b>

**Operations**

	<b>20XX</b>	<b>20XX</b>
Premiums	218	233
Investment income (net of gains/losses)	1	8
Other income	0	0
<b>Total revenues</b>	<b>219</b>	<b>241</b>

**LOSSES, BENEFITS AND EXPENSES**

Policyholder Benefits	177	157
Expenses	77	80
<b>Total losses, benefits and expenses</b>	<b>254</b>	<b>237</b>
Other	0	2
<b>NET INCOME</b>	<b>(35)</b>	<b>2</b>

**Insurer's Group Number**

List here

**Lead State/Groupwide Supervisor**

List here

**State Prioritization**

List X out of X

**RBC Ratio**

List % here as calculated in the 5 year history by the Company

**Insurer's Financial Strength/Credit Ratings**

List here

**Contact at Insurer**

List name here

List phone here

List e-mail here

**Key Personnel**

List name here – CEO

List name here – CFO

List name here – CRO

List name here – Other

**CPA Firm**

List here

**Appointed Actuary**

List here

**Analyst**

List here

**Date of Last Exam**

List here

**Examiner In Charge**

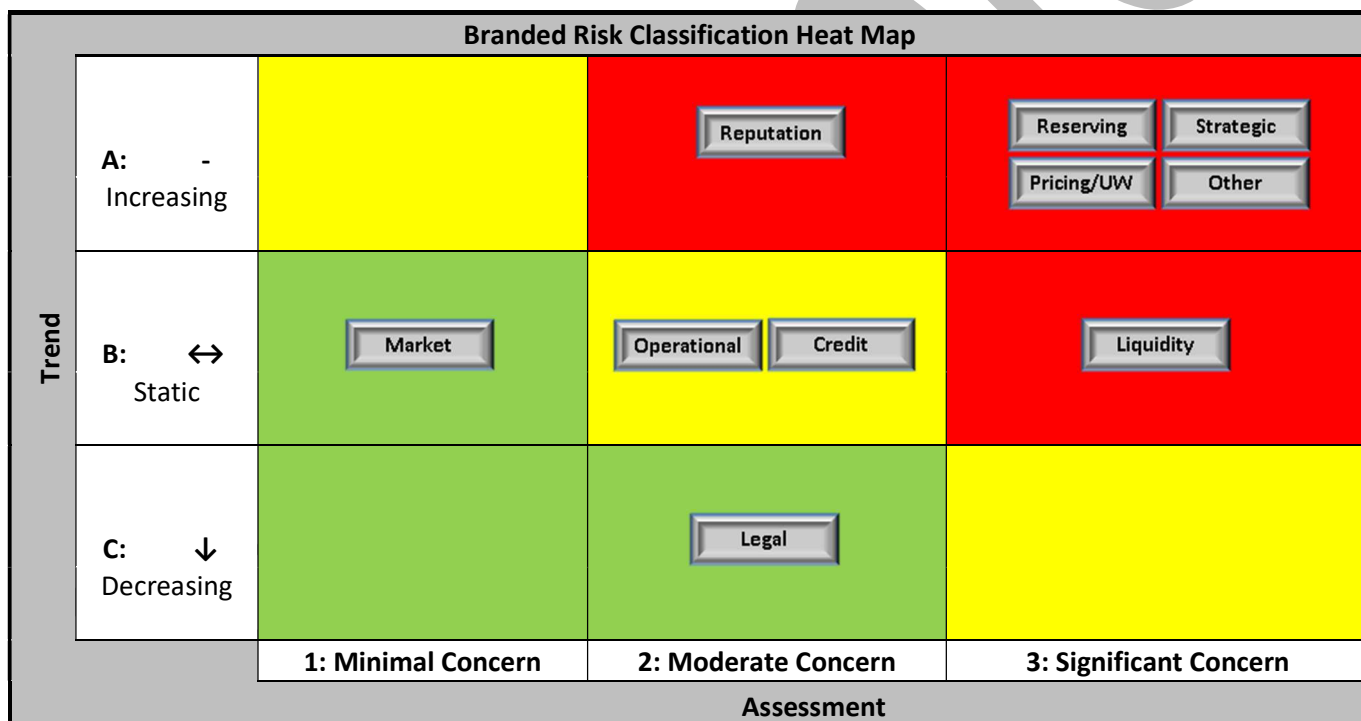
List here

III.A.5. Risk Assessment (All Statement Types) – IPS Example

**BRANDED RISK ASSESSMENTS**

Summarize your assessment of the branded risk classifications for the insurer based upon both quantitative (e.g., 5 year trending of key ratios) and qualitative information. An assessment of each significant individual risk component (including prospective risks) relevant to the classification should be provided by indicating either “minimal concern,” “moderate concern” or “significant concern” as well as the direction in which the risk is trending. If no significant individual risk components are identified for a branded risk classification, documentation should be provided to support this conclusion. Consider the materiality and/or significance of each individual risk component in aggregating the overall assessment and overall trend for each branded risk classification. Update the Branded Risk Classification Heat Map to illustrate your conclusions.

The following is an interactive map. Click and drag the risk classification to the appropriate section of the risk classification heat map after assessing the trend in each individual category.



## III.A.5. Risk Assessment (All Statement Types) – IPS Example

**Credit:** This risk is considered moderate, driven primarily by a fairly conservative investment mix (96.4% of bonds are NAIC 1 with 28% US government, 14% US states, most of the rest high quality corporates) and limited exposure to equities, offset by a relatively high amount of real estate (\$33 million), growing agent balances (\$99 million) and significant reinsurance recoverables (paid and unpaid) of \$81 million. However, the reinsurance recoverables are diversified across a number of highly rated reinsurers.

Minimal Concern	Moderate Concern	Significant Concern	Trend
Bonds			↑
Reinsurance Recoverable			↑
	Real Estate-Home Office		↔
		Agent Balances and Uncoll Prem	↑
<b>Overall Credit Assessment: Moderate Concern</b>		<b>Overall Trend:</b>	↑

**Legal:** The Company has a vested interest in the outcome of the case of GEI v. Virtual Imaging which is before the State Supreme Court. This case pertains to a change in statutes, effective January 1, 2008, that affected the manner in which insurers, including the Company, have paid claims. Subsequent to the statutory change, cases have been brought and trial courts have concurred that the statutes and resulting payments are ambiguities in the statutes. These cases are collectively known as the “Fee Schedule” matter. The Company began receiving lawsuits on this matter in May 2010, some of which were closed at high cost. Since that time, the Company has modified its strategy for handling these cases and has received multiple trial victories from juries that ruled no further payments were owed to the plaintiffs. Exam results indicate that the Company’s legal team tracks and monitors outstanding lawsuits and involves experienced external counsel in representing the Company in these matters.

Minimal Concern	Moderate Concern	Significant Concern	Trend
Effectiveness of legal counsel			↔
	Fee Schedule lawsuits		↓
<b>Overall Legal Assessment: Moderate Concern</b>		<b>Overall Trend:</b>	↓

**Liquidity:** The Company is subject to high liquidity risk due to the lines of business written and the corresponding need to meet short-term obligations. The Company’s high exposure to the volatile PIP market and related losses has reversed the trend of improved liquidity in recent years. Trends in the Company’s five-year liquidity ratio are shown in the following chart, which was indicating improvements before a negative shift in the current year:

	CY	PY	PY1	PY2	PY3
<b>Liquidity Ratio</b>	108.5%	98.3%	101.4%	107.1%	113.0%

Minimal Concern	Moderate Concern	Significant Concern	Trend
		Exposure to PIP Market	↔
		Liquidity Ratio	↔
<b>Overall Liquidity Assessment: Moderate Concern</b>		<b>Overall Trend:</b>	↔

**Market:** Market risk includes equity risks, changes in credit spreads, and also interest rate risks. Most of these risks are not inherently significant to the Company due to its relatively conservative investment portfolio and relatively short-term policies (typically 6 months or 1 year), which allow the Company to reprice fairly easily to align with shifts in the market. However, as shown during the financial crisis, some of the Company’s products are more sensitive to general economic downturns, which can impact the Company’s performance.

Minimal Concern	Moderate Concern	Significant Concern	Trend
Equity			↔



## III.A.5. Risk Assessment (All Statement Types) – IPS Example

Changes in Credit Spreads			↔
	Economic Downturn		↑
<b>Overall Market Assessment: Moderate Concern</b>		<b>Overall Trend:</b>	↔

**Operational:** The results of the last exam indicated that the Company has a reliable IT environment and effective internal controls in most areas. However, concerns were raised regarding segregation of duty issues relating to the handling of claims and cash disbursements during the last exam. In addition, a recent news report indicated that one of the Company's independent agents has been charged with committing fraudulent activities. Due to the Company's heavy reliance on independent agents to generate business and manage policyholder relations, even though the report might be an isolated incident it represents a moderate concern in this category.

Minimal Concern	Moderate Concern	Significant Concern	Trend
IT Environment			↔
	Segregation of Duties		↔
	Agent Fraud		↑
<b>Overall Operational Assessment: Moderate Concern</b>		<b>Overall Trend:</b>	↔

**Pricing/Underwriting:** Although the Company is primarily engaged in short-term products (6 months or 1 year), it is subject to highly competitive price pressure and has shown historically weak underwriting results. Underwriting results have shown a negative trend over the past 6 periods as losses incurred continue to rise, a sign that pricing pressures are influencing the bottom line. The Company appears to be utilizing cash flow underwriting as a way to bolster earnings through investment income, which leads to a concern regarding the adequacy/appropriateness of rates used by the Company. In addition, the last financial exam noted a lack of documented underwriting guidelines at the Company, which is in the process of being corrected. However, the lack of documented, detailed underwriting guidelines represents a moderate concern in this area. Overall, this risk category represents a significant ongoing concern for the Company.

Minimal Concern	Moderate Concern	Significant Concern	Trend
	Underwriting Guidelines		↔
		Rate Adequacy	↑
<b>Overall Pricing/Underwriting Assessment: Moderate Concern</b>		<b>Overall Trend:</b>	↑

**Reputation:** The Company's business is not rating sensitive, but the Company is highly dependent upon business produced by agents. As noted above, a recent concern has been identified regarding potential fraud committed by one of the Company's agents. In addition, findings of a recent market conduct examination lead to numerous violations. These violations related to claims handling issues, such as failure to comply with timely payments and denial of legitimate claims. Although the Company has disputed these findings, gross writings continue to suffer as several agents have stopped writing on behalf of the Company.

Minimal Concern	Moderate Concern	Significant Concern	Trend
	Agent Fraud		↑
	Market Conduct Findings		↑
<b>Overall Reputation Assessment: Moderate Concern</b>		<b>Overall Trend:</b>	↑

**Reserving:** The Company is subject to high reserving risk, as shown in the following reserve trending of information. The Company historically has been overly optimistic in the forecasting of future liabilities and reserving, where actual reported results have failed to meet projections. The types of business written and geographic regions in which coverage is provided leave the Company vulnerable to high losses and a greater than industry average risk for adverse reserve development.

## III.A.5. Risk Assessment (All Statement Types) – IPS Example

	CY	PY	PY1	PY2	PY3	
<b>Two Year Develop Loss &amp; LAE/C&amp;S</b>	53.4%	8.0%	-20.3%	25.7%	100.1%	
	204.1%	132.3%	168.0%	235.2%	496.9%	
Minimal Concern	Moderate Concern			Significant Concern		Trend
				Lines of Business		↔
				Loss Development		↑
<b>Overall Reserving Assessment: Moderate Concern</b>				<b>Overall Trend:</b>		↑

**Strategic:** The following issues have been identified relating to the Company's strategy:

- As discussed above, the Company has experienced weak underwriting, which has resulted in material losses and material reductions in capital. Underwriting losses have been reported in each of the past five years. Consequently, profitability and capital are considered weak as investment activity has been used to prop-up the bottom line, in addition to capital contributions from the Company's parent. The Company has not yet finalized and presented an updated business plan to demonstrate how it will address these strategic issues going forward.
- The Company indicated in its Form F that it was changing its mix of business in states other than State X and Y. This could create a risk as the Company has only been writing in the other states for a few years; therefore there is limited historical development available for these states. This should be considered in the context of the targeted examination.

Minimal Concern	Moderate Concern	Significant Concern	Trend
	Expansion in new jurisdictions		↑
		Profitability/capital concerns	↑
<b>Overall Strategic Assessment: Significant Concern</b>		<b>Overall Trend:</b>	↑

**Other:** The following other issues have been identified that don't clearly fit into one of the branded risk classifications highlighted above:

- The company has consistently been out of compliance with one or more laws, regulations or requirements of the Department and other states.

Minimal Concern	Moderate Concern	Significant Concern	Trend
	Incorrect statutory financial statements		↑
		Lack of knowledge or laws	↑
<b>Overall Reserving Assessment: Moderate Concern</b>		<b>Overall Trend:</b>	↑

**IMPACT OF HOLDING COMPANY ON INSURER**

Summarize the evaluation of the impact of the holding company system on the domestic insurer. [See Domestic and/or Non-Lead State Analysis Holding Company Procedures for further discussion.](#)

**EXAMPLE:**

[The holding company's UCP, has provided capital to the insurer when it has been required. The presence of many agreements involving the insurer and its affiliates indicate that the holding company is highly interconnected with entities being dependent on one another. The insurer provides services to, as well as receives services from affiliates. This is accomplished via a Risk Share Agreement which superseded previous agreements the insurers had with the affiliated entities. The insurer provides TPA services for certain members of the group. The insurer also has service agreements with affiliates for shared operational and management services, and investment management.](#)

**III.A.5. Risk Assessment (All Statement Types) – IPS Example**

Overall, the operations of the holding company are profitable and able to maintain the ability for the holding company to infuse capital into the three insurers when needed. The holding company has requested distributions from the insurer from time to time to help fund capital deficiencies in two affiliates, but there is no concern with the insurer’s financial condition or independent ability to provide this support at the present time. In evaluating whether the holding company has the ability to provide necessary financial support to its insurers, it is noted that the holding company has equity of \$X billion as of its most recent audited financial statements and has positive net operating income over the past several years. In addition, the holding company has bond ratings from Moody’s of Aa3 and from Standard & Poors of AA. These strong ratings coupled with a strong balance sheet provide evidence that holding company has the ability to continue to assist the insurer by means of capital infusions should the needs arise.

The group is highly dependent upon cash flows from the various entities, including ABC, to make payments on the holding company debt used to help finance past transactions associated with the growth of the group. The Form F provides more specific information on necessary cash flows expected in the near term. Others risk from the non-insurers is not significant. See Domestic and/or Non-Lead State Analysis Holding Company Procedures for further discussion.

**OVERALL CONCLUSION AND PRIORITY RATING**

This section should include an overall conclusion as to the Company’s financial condition, discuss strengths that potentially mitigate the risks assessed above, and highlight weaknesses and any concerns with the Company’s operations going forward. Include any actions that may have been taken (e.g., significant holding company transactions, prior or planned meetings with management, and referrals to/from other divisions, etc.). Recommend the priority that should be assigned to the Company and explain the rationale.

**EXAMPLE:**

Based on the branded risk assessments provided above as well as the Company’s poor financial results reported in recent periods, the Company appears to be potentially troubled. The Company has triggered more than five of the department’s prioritization criteria and is a multi-state insurer; therefore, the Company has been assigned our highest priority rating of 1, which is unchanged from the prior year. Some of the most significant issues facing the Company include rate adequacy, reserve sufficiency and overall cash flow and liquidity issues. However, these weaknesses are somewhat offset by Company strengths including a conservative investment portfolio, brand recognition and a strong historical reputation. The department has scheduled a meeting with senior management for the 3<sup>rd</sup> Quarter to discuss the Company’s poor financial performance and ongoing business plan. During the meeting, the department plans to share its concerns and inform the Company of steps planned to more closely monitor the company’s operations, as described below.

**SUPERVISORY PLAN**

List any specifically identified items that require further monitoring by the analyst or specific testing by the examiner. In addition, indicate if the Company is or should be subject to any enhanced monitoring, such as monthly reporting, a targeted examination, or a more frequent exam cycle.

**EXAMPLE:****Analysis Follow Up**

- Obtain further detail regarding the impact of proposed rate increases and monitor through monthly financial reporting.
- Obtain further detail regarding the insurer’s liquidity strategy.
- Assess the reasonableness of the Company’s business plan as soon as it is received, given the inability to execute the most recent strategy. Consider attending board meetings to reflect the concern regarding the future viability of the Company.

**III.A.5. Risk Assessment (All Statement Types) – IPS Example**

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**Examination Follow-Up**

- During the next regularly scheduled examination, audit the specific risks associated with the Company's agents balances and uncollected premiums to determine if further concerns exist.
- Follow-up on segregation of duties issues noted in the last examination.
- Perform a targeted examination of the reserves, pricing and claims management. Consider in the reserve study any pricing review, information related to the changing legal environment, as well as the mix of business in states outside of X and Y.

Example

### III.A.6. Template for Planning Meeting with Financial Examiner

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----- *DETAIL HAS BEEN ELIMINATED TO CONSERVE SPACE* -----

#### **Planning Meeting Between the Financial Analyst and Financial Examiner – Agenda Items**

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1. **Business Summary** – Discuss a summary of the business operations and lines of business of the insurer.
  - a. Discuss whether the department has received a recent business plan from the company and has identified any significant changes in strategy/operations.
  - b. Discuss any recent meetings with the company and their potential impact on the examination.
  - c. Discuss the corporate governance in place at the company and any recent changes or concerns identified.
2. **Regulatory Actions** – Discuss any significant recent steps taken in supervising the company, including, but not limited to:
  - a. Granting of permitted practices
  - b. Identification of issues of non-compliance
  - c. Follow-up on items from the last financial examination
  - d. Review of items filed with the department for approval
3. **Financial Snapshot/Overview of Financial Position** – Discuss the company’s recent financial results, including, but not limited to:
  - a. Changes in profitability trends.
  - b. Deterioration in asset quality, liquidity or capital adequacy.
  - c. Changes in investment holdings and strategy.
  - d. Changes in key annual statement balances.
  - e. Changes in reinsurance balances and program structure.
  - f. Significant results noted in financial analysis solvency tools.
4. **Branded Risk Assessments** – Discuss individual branded risk assessments with a focus on moderate and significant areas of concern. For example:
  - a. Discuss a summary of detailed analysis work performed to address key issues.
  - b. Discuss the status of any outstanding inquiries or requests for the company.
  - c. Discuss any management representations to the department that should be verified or corroborated during the exam.
  - d. Discuss any recommended exam procedures and/or follow-up on key issues.
5. **Impact of Holding Company on Insurer** – Discuss the impact of the holding company system on the domestic insurer. For example:
  - a. Discuss and obtain the Group Profile Summary and non-lead state holding company analysis work as necessary.
  - b. If the lead state, discuss whether the analyst’s review of the group’s Corporate Governance Annual Disclosure (CGAD), if applicable, Own Risk and Solvency Assessment (ORSA) Summary Report and/or Form F reporting indicate a need for additional follow-up and review during the exam.
  - c. If not the lead state, discuss whether your state’s review of the following indicate a need for additional follow-up and review during the exam.

### III.A.6. Template for Planning Meeting with Financial Examiner

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- i. As applicable, either the insurance entity's CGAD, or the lead state's review of the group's CGAD provided in the GPS and other information provided by the lead state
  - ii. The lead state's analysis of Own Risk and Solvency Assessment (ORSA) Summary Report
  - iii. The lead state's analysis of the Form F provided in the GPS or other information provided by the lead state
- ~~b-d.~~ Discuss any developments or follow-up items resulting from recent supervisory college sessions.
6. **Overall Conclusion and Priority Rating** – Discuss the analyst's overall conclusion on the company's financial condition, strengths, weaknesses, and priority rating assigned to the company.
7. **Supervisory Plan** – Discuss the analyst's plans for the ongoing supervision of the company, including any specific examination procedures identified.
8. **Access to Work Papers and Company Documents** – Discuss the best way that the analyst's work can be reviewed/obtained. As the number of files that examiners wish to review and obtain increases, they may consider obtaining access to the analyst's workpapers and receiving specific locations (i.e., workpaper references) for all requested documents.
9. **Input from Other Areas of the Department** – Discuss whether the analyst has received recent communications from other areas of the insurance department regarding issues that could affect the financial examination including, but not limited to, units in charge of:
  - a. Approving rates and forms filings
  - b. Legal and administrative matters
  - c. Market conduct examinations/filings
10. **General Observations** – Depending on the information already provided, determine whether there are any additional topics relevant for discussion, such as:
  - a. If you were going on-site to examine this company, where would you focus your time?
  - b. What are your biggest concerns in terms of things that could go wrong at this company to result in a solvency concern?
  - c. Are you aware of any fraud allegations or concerns at the company? Are there any fraud risk factors that the exam team should be aware of?

**V.A. Domestic and/or Non-Lead State Analysis – Holding Company Procedures (Non-Lead State)**

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----- [DETAIL HAS BEEN ELIMINATED TO CONSERVE SPACE](#) -----

**Assess the Impact of the Holding Company Group on the Domestic Insurer**

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**Assessment of Group Profile Summary from the Lead State**

5. Obtain a copy of the lead state's Group Profile Summary (GPS).
6. Consider the GPS's branded risk assessment in determining the impact of the holding company on the domestic insurer.
7. Review the conclusion and supervisory plan of the GPS. Did the lead state identify any holding company risks impacting the domestic insurers' in the group and/or supervisory plans that impact your state's domestic insurer?
8. Consider the nature of the domestic insurer(s)' interdependence on the holding company group or affiliated entities for business operations or financial stability (e.g., employees, services provided, reinsurance and/or capital support in the near term). (OP, CR, ST)
9. Consider the level of reputational risk that the holding company (as a group) poses to the domestic insurer(s). (RP)
10. Determine if income of the domestic insurer(s) is being used to service holding company debt or other corporate initiatives (e.g., acquisitions). (OP, ST)
11. Review the information provided in the GPS regarding the Corporate Governance Annual Disclosure (CGAD) and other related corporate governance information provided by the lead state. Does it identify any risk or concerns that require questions or follow-up to the lead state? Does it highlight any issues that are only relevant to your state's domestic insurance entity? Do any material concerns exist regarding corporate governance that could impact the domestic insurer's financial condition (e.g., operations, policyholder surplus or capital position)?
12. Review the information provided in the GPS regarding risks or concerns noted in the Enterprise Risk Report (Form F) or any other related information provided by the lead state. Does it identify any risk or concerns that require questions or follow-up to the lead state? Do any material concerns regarding enterprise risk have the potential to impact the financial condition of the domestic insurer risks or pose an immediate material risk to the domestic insurer's policyholder surplus or risk- based capital position, insurance operations (e.g., changes in writings, licensure, and organizational structure), balance sheet, leverage, or liquidity?

**Assessment of Form B (and C)**

- ~~14~~3. Based upon a review of the registration statement, were any significant and/or unusual items noted, such as, but not limited to, the following?
  - a. Person(s) holding 10% or more of any class of voting security who also have a history of transacting business of any kind directly or indirectly with the insurer. (OP, ST)
  - b. Biographical information about directors or officers, which may elevate concerns such as convictions of crimes. (OP, ST)
  - c. Any litigation or administrative proceeding involving the ultimate controlling entity or any of its directors and officers, such as criminal prosecutions or proceedings which may have a material effect upon the solvency or capital structure of the ultimate holding company, such as bankruptcy, receivership, or other corporate reorganization. (LG)

**V.A. Domestic and/or Non-Lead State Analysis – Holding Company Procedures (Non-Lead State)**

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- d. The absence of an affirmative statement that transactions entered into since the filing of the prior year's annual registration statement are not part of a plan or series of like transactions to avoid statutory threshold amounts. (OP, ST)

**Assessment of Affiliated Risks on the Domestic Insurer**

~~12-~~ 14. Were any material deficiencies or risks noted during the annual review of the domestic insurer's Notes to Financial Statements, Interrogatories, Schedule Y – Part 2, Holding Company Forms B & C, or recent examination reports with respect to affiliated transactions? (CR, LQ, OP, ST)

- a. Management agreements
- b. Third-party administrative agreements
- c. Managing general agent agreements
- d. Investment management pools
- e. Reinsurance agreements and pools
- f. Consolidated tax sharing agreements
- g. Other

~~13-~~ 15. If any of the following forms have been filed with the domestic regulator since the last review, indicate if risks or concerns were noted in any of the reviews of these forms.

- a. Form A (Acquisition of Control or Merger)
- b. Form D (Prior Notice of a Transaction)
- c. Form E (Pre-Acquisition Notification) or Other Required Information
- d. Extraordinary Dividend/Distribution

**Assessment of Form F – Enterprise Risk Statement**

~~14. Obtain either the Form F from the lead state, if available, and/or the lead state's analysis of the Form F if it addresses the impact of the holding company on your state's domestic insurer(s).~~

~~15. Based on the analyst's review of Form F and/or the lead state's analysis of the Form F, and any additional information related to enterprise risk available (e.g., Form B, other filings), document any material concerns regarding enterprise risk that could impact the financial condition of the domestic insurer.~~

~~16. Do any of the risks identified pose an immediate material risk to the insurer's policyholder surplus or risk-based capital position, insurance operations (e.g., changes in writings, licensure, and organizational structure), balance sheet, leverage or liquidity?~~



**V.A. Domestic and/or Non-Lead State Analysis – Holding Company Procedures (Non-Lead State)**

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**Assessment of Own Risk and Solvency Assessment (ORSA), if applicable**

~~17.~~ 16. Obtain the lead state's analysis of the ORSA Summary Report (See section VI.F-Own Risk and Solvency Assessment Procedures.)

~~18.~~ 17. Did the lead state document in its analysis any risks or concerns that in its opinion have an impact on the overall financial condition of the insurance holding company system? If so, do any of the risks or concerns identified pose a material risk to the domestic insurer?

**Assessment of Corporate Governance Annual Disclosure (CGAD), if applicable**

~~19.~~ Obtain the lead state's analysis of the CGAD and determine if it addresses corporate governance policies and practices of the group applicable to your state's domestic insurer(s).

~~a.~~ If the CGAD analysis does not address corporate governance policies and practices of the group applicable to the non-lead states' domestic insurer, request the CGAD from the insurer.

~~20.~~ Based on the analyst's review of the CGAD or the lead state's analysis of the CGAD, and any additional available information related to corporate governance, document any material concerns regarding corporate governance impacting the domestic insurer.

~~21.~~ Do any of the concerns identified pose an immediate material risk to the domestic insurer's financial condition (e.g., operations, policyholder surplus or capital position)?

**Communication & Follow-Up with the Lead State**

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- Notify the lead state of any additional material events or concerns applicable to the domestic insurer, or the group as a whole, that the lead state may not otherwise be aware of, and that should be considered in the evaluation of the overall financial condition of the holding company system.
- If any material risks or events were identified during your holding company analysis that were not discussed in the lead state's holding company analysis, communicate those findings to the lead state.

**Update the Insurer Profile Summary**

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Update the Insurer Profile Summary of the domestic insurer with the summary and conclusion of the impact of the holding company system on the domestic insurer based on the above analysis performed.

Analyst:	Date:
Supervisor Review:	Date:
Supervisor Comments:	

----- [DETAIL HAS BEEN ELIMINATED TO CONSERVE SPACE](#) -----

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## Form A – Statement of Acquisition of Control of or Merger with a Domestic Insurer

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### Ultimate Controlling Person/Parent (UCP), Officers, and Directors

6. Perform additional review considerations as necessary to analyze and identify potential risks concerning the UCP, Officers, and Directors which may include but not limited to the following:
  - a. Perform a query of the NAIC Form A database on the name of the UCP, directors, executive officers, or owners of 10 percent or more of the voting securities of the applicant and perform the following step(s):
    - i. Assess the feasibility of the acquiring person's holding company structure including location and control (direct/indirect) of the target company post acquisition.
    - ii. Carefully scrutinize and understand complex organization and ownership structures.
  - b. Review other external sources to gain a better understanding of the acquiring persons, its affiliates, and the UCP.
  - c. Identify and review all relevant parties to the proposed acquisition and the nature of other filings made in other states by similar individuals.
  - d. Consider suitability of UCP through background review and regulatory review of the prospective new owners, using UCAA biographical affidavits and third-party background reviews by NAIC listed independent third-party reviewing companies or fingerprinting criminal checks if applicable and note any risks or concerns regarding competence, experience, and integrity of the applicant, as well as the results of any background investigation.
  - e. Does the Form A provide adequate background information (e.g., biographical affidavits including third-party background checks) on the applicant (if an individual) or all persons who are directors, executive officers, or owners of 10% or more of the voting securities of the applicant (if the applicant is not an individual)?
  - f. Review the lead state's assessment of the acquiring UCP's most recent ORSA Summary Report and [information in the Group Profiles Summary \(GPS\) regarding](#) Form F, if applicable; to better understand the impact on risk assessment, risk appetite and tolerances, and prospective solvency (capital and liquidity).
  - g. Cross check the UCP with source of funds and consider debt funding sources.
  - h. Consider acceptability of SEC disclosures by board members of publicly traded UCPs in suitability review.

## Non-Lead State Holding Company System Analysis Procedures

**PROCEDURES #5-17** assist analysts in assessing the impact of the holding company system on the domestic insurer. This includes five primary segments of the analysis as follows.

- **#5-120 ASSESSMENT OF THE GROUP PROFILE SUMMARY (GPS) FROM THE LEAD STATE:** If the Lead State is not your state, the Lead State should provide a GPS to the non-lead states in the group by Oct. 31. Using the GPS consider the risks identified and assessed by the Lead State to determine any material impacts on the branded risks of the domestic insurer, the interdependence of the holding company and its affiliated entities, including the domestic insurer, dividend obligations of the domestic insurer to service holding company debt or fund other holding company initiatives, ~~and~~ the holding company's reputation, [enterprise risk management and corporate governance](#).
- **#131 ASSESSMENT OF FORM B (AND C):** Model #440 defines insurance holding companies and the related registration, disclosure, and approval requirements. Form B is the insurance holding company system annual registration statement. Model #440 requires every insurer, which is a member of an insurance holding company system, to register by filing a Form B within 15 days after it becomes subject to registration, and annually thereafter. Any non-domiciliary state may require any insurer that is authorized to do business in the state, which is a member of a holding company system, and which is not subject to registration in its state of domicile, to furnish a copy of the registration statement.

An insurance holding company system consists of two or more affiliated individuals, one or more of which is an insurer. An affiliate is an entity that directly or indirectly, through one or more intermediaries, controls, is controlled by, or is under common control with, another entity. Control is presumed to exist when an entity or person, directly or indirectly, owns, controls, holds with the power to vote, or holds proxies, representing 10 percent or more of the voting securities.

- **#124-135 ASSESSMENT OF AFFILIATED RISKS ON THE DOMESTIC INSURER:** Affiliated risks may exist due to interdependence of the holding company and its affiliated entities through affiliated transactions. Consider also the guidance included in section III.B.5.d Operational Risk Repository – Analyst Reference Guide as well as guidance in this section regarding supplemental form filings for review of affiliated agreements.
- ~~**#14-16 ASSESSMENT OF FORM F – ENTERPRISE RISK STATEMENT:** The purpose of the Form F is to identify if there is any contagion risk within the group, and domestic states should not be discouraged from reviewing such information because ultimately they are required to relate the financial condition of the group to their domestic state. The Form F must be reviewed by the lead state but other domestic states are also expected to review it. To the extent the Lead State's analysis of Form F assesses the impact of any contagion risk of the group on the non-lead state's domestic insurer, that analysis may be leveraged by the non-lead state to reduce the analysis work of the non-lead state. If the Lead State's analysis of Form F does not assess the impact of the group on the non-lead state's domestic insurer, consider a review as noted in Procedure #15 and #16, or similar to the procedures in section VI.G. Group-Wide Supervision – Form F – Enterprise Risk Report Procedures for reviewing Form F.~~
- **#16-1717-18 ASSESSMENT OF OWN RISK AND SOLVENCY ASSESSMENT (ORSA):** If the Holding Company files an ORSA Summary Report, it is the responsibility of the Lead State to review and perform analysis of the report. At the completion of this review, the lead state should prepare a thorough summary of its review, which would include an initial assessment of each of the three sections. The lead state should also consider and include key information to share with other domestic states that are expected to place significant reliance on the lead state's review. Non-lead states are not expected to perform an in-depth review of the ORSA, but instead rely on the review completed by the lead state. The non-lead state's review of the lead state's ORSA review should be performed only for the purpose of having a general understanding of the work performed by the lead state, and to understand the risks identified and monitored at the group-level so the non-lead state may better monitor and communicate to the lead state when its legal entity could

**V.F. Domestic and/or Non-Lead State Analysis – Analyst Reference Guide**

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affect the group. Any concerns or questions related to information in the ORSA or group risks should be directed to the lead state.

- ~~● **#19-21 ASSESSMENT OF CORPORATE GOVERNANCE ANNUAL DISCLOSURE (CGAD):** Analysis of CGAD only applies where states have enacted such legislation as that in the *Corporate Governance Annual Disclosure Model Act* (#305) and *Corporate Governance Annual Disclosure Model Regulation* (#306). The purpose of the CGAD is to provide a summary of an insurer or insurance group's corporate governance structure, policies and practices to permit the regulator to gain and maintain an understanding of the insurer's corporate governance framework. The CGAD must be filed to the lead state if on a group basis or the domestic state if on a legal entity basis, but other domestic states may request the filing. To the extent the Lead State's analysis of a group CGAD assess the impact of corporate governance practices and procedures of the group on the non-lead state's domestic insurer, the analysis may be leveraged by the non-lead state to reduce the analysis work of the non-lead state. If the Lead State's analysis of CGAD does not assess the impact of the group on the non-lead state's domestic insurer, review the filing to identify and assess any material concerns and determine if any material immediate risks impact the domestic insurer's financial condition.~~

**VI.C. Group-Wide Supervision – Insurance Holding Company System Analysis Guidance (Lead State)**

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----- *DETAIL HAS BEEN ELIMINATED TO CONSERVE SPACE* -----

**Responsibilities of Each Domestic State**

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**Evaluation of the Impact of Holding Company System**

The domestic state is responsible for completing an evaluation of the impact of the insurance holding company system on the domestic insurer. In doing so, the domestic state is responsible for identifying and understanding the affiliated risks within the insurance holding company system. This information and understanding can be obtained from several sources, including the supplemental filings (i.e., Form A, Form B, Form D, [and Form E](#), ~~and Form F~~). The Form B, Form C and any other holding company filings should be analyzed, to at least some extent, by December 31<sup>st</sup> for analysis conducted by the domestic state (See also chapter V.A. and V.F. for possible Form B and C compliance and assessment procedures and guidance.) Additionally, the domestic state should obtain a GPS from the lead state containing the risk assessment of the group that is necessary to evaluate the impact that the insurance holding company system could have on the domestic insurer. The domestic state is responsible for summarizing a conclusion regarding this evaluation. This should be included in either the annual or quarterly financial analysis work papers and summarized in the Insurer Profile Summary (IPS) of the respective domestic insurer on a yearly basis.

**Lead State Holding Company Analysis – Process and Procedures**

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**Specific Procedures for Completing the Insurance Holding Company Analysis**

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The following procedures are intended to assist analysts completing a holding company analysis documented in the GPS. The following procedures do not represent additional documentation requirements.

**Understand the Insurance Holding Company System**

1. Evaluate and document an understanding of the insurance holding company system. Consider using the following if available and/or applicable: statutory Schedule Y, Form B Registration Statement, [Enterprise Risk Report \(Form F\)](#), [Corporate Governance Annual Disclosure \(CGAD\)](#), ORSA Summary Report, and financial filings of the insurance holding company system and/or person. Summarize the understanding of the holding company in the GPS. If necessary, analysts may also document further details below.

**Conduct Detailed Analysis of the Insurance Holding Company System**

Conduct detailed analysis by evaluating the overall financial condition of the holding company system through an assessment of the group's exposure to each of the nine branded risk classifications. Consider both the financial review of insurance and non-insurance entities within the insurance holding company system. In certain cases, the review of non-insurance entities may be mitigated by the lack of interdependence of the entities. Conduct the assessment by using quantitative and qualitative information. Consider utilizing the following, if available and/or applicable: legal entity IPSs; Form B and Form F; [CGAD](#); ORSA; shareholders' report; combined financial statements; quarterly and annual SEC filings; International Financial Reporting Standards (IFRS) filings; personal net worth statements; audited financial statements; management's assessment of internal controls; auditor's assessment of management's assessment of internal controls; press releases; confidential information from other regulatory/supervisory bodies; and any other available sources.

**Contents of the Group Profile Summary (GPS)**

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The following analysis work should be documented in the GPS:

**VI.C. Group-Wide Supervision – Insurance Holding Company System Analysis Guidance (Lead State)**

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- **Holding Company System Summary** – Include an understanding the holding company system by discussing the structure and business operations, including any significant recent events, changes in structure, key business segments, international activity, rating organization changes/actions and key entities/persons within the insurance holding company system. Include discussion of new and material affiliated transactions/relationships, management and third-party agreements and non-insurance agreements as well as the impact of these agreements to the group/insurers.
- **Corporate Governance Summary** – Present a summary of the group’s overall corporate governance structure, [including a review of the Corporate Governance Annual Disclosure—CGAD \(if filed on a group basis\)](#) and an overall assessment for the holding company system.
- **Enterprise Risk Management Summary** – Present a summary and assessment of the enterprise risk management function in place at the holding company system, as well as a discussion of ORSA Summary Report filing/review status (if applicable).
- **Branded Risk Assessments** – Include a summary assessment of the group’s exposure to branded risk classifications, including prospective risks, the financial strength of the insurance holding company system, including financial position, liquidity, leverage, and profitability. Such documentation should include summarizing key risks noted within the IPSs from respective domestic regulators within the group.
- **Overall Conclusion** – Present an overall conclusion as to the group’s financial condition, including key strengths and weaknesses or material concerns that regulators may have with the group’s operations going forward.
- **Supervisory Plan** – Present any specifically identified items that require further action and/or monitoring by analysts or specific testing by the examiner.
- **Other Functional Financial Regulators/Supervisors** – Where appropriate, it may be necessary to document an understanding of other functional financial regulators/supervisors involved with legal entities within the insurance holding company system, including international regulators/supervisors and U.S. federal banking regulators.

## VI.D. Group-Wide Supervision – Corporate Governance Disclosure Procedures

**Special Note:** The following procedures do not supersede state regulation but are merely additional guidance an analyst may consider useful.

The *Corporate Governance Annual Disclosure Model Act (#305)* and *Corporate Governance Annual Disclosure Model Regulation (#306)* provide a summary of an insurer or insurance group's corporate governance structure, policies and practices to permit the Commissioner to gain and maintain an understanding of the insurer's corporate governance framework.

States should also consider completion of applicable questions within the Operational and Strategic risk repositories of this Handbook based upon the level of concern an analyst may have with management performance and the driving forces behind operations. The risk repositories may also be used by an analyst of a state that has obtained the disclosure for an insurer or insurance group subject to the aforementioned corporate governance disclosure. However, analysts should avoid duplicate information requests.

## Introduction

Models #305 and #306 requires an insurer, or an insurance group, to file a summary of an insurer or insurance group's corporate governance structure, policies and practices with the commissioner by June 1 of each calendar year. Model #305 allows the information to be at the ultimate controlling parent level, an intermediate holding company level and/or the individual legal entity level, depending upon how the insurer or insurance group has structured its system of corporate governance. Because most corporate governance is driven at a controlling or intermediate holding company level, this guidance is contained within this section dealing with group supervision. Although by inclusion in this section, reviewing the corporate governance disclosure of a group is a responsibility of the lead state, the approach on this is different from that taken with the Own Risk Solvency and Analysis (ORSA). This is because it's common for most groups to have different layers of governance that is important in achieving the objectives of the group. More specifically, most groups have some level of governance at the individual legal entity level. However, because it is common for legal entity governance to be a less significant aspect of the governance objectives, even those companies that incorporate governance at the individual legal entity level are likely to include materially less documentation on such, may instead summarize such processes and list those entities for which they exist.

### Non-Lead State Reliance on the Lead State Analysis of Corporate Governance Annual Disclosure:

Model #305 requires the filing to be made with the lead state; however, non-lead domestic states may request the CGAD filing from the insurer. Because the filing may be made on a group basis or legal entity basis, it may contain group information that applies to all insurers within the group or it may contain information applicable to a specific legal entity.

Similar to other solvency regulation models, Model #305 contemplates both off-site and on-site examination of the CGAD information, therefore, it may be necessary or acceptable for the lead state to share its work papers with another state during an exam, related to such filing, provided such information is shared in accordance with the confidentiality provisions of Model #305. ~~This is because similar to other solvency regulation models, Model #305 contemplates both off-site and on-site examination of such information.~~

The lead state should take primary responsibility for reviewing the CGAD filing, if it is filed on a group basis, and should incorporate any takeaways or concerns into the Group Profile Summary (GPS). Takeaways should be incorporated into the corporate governance summary in the GPS and/or the discussion of various branded risks, as deemed appropriate. There is no requirement or expectation for the analyst to create a separate CGAD checklist or create additional review documentation for sharing with another state or for internal documentation purposes.

If the CGAD highlights any issues that are only relevant to a particular insurance entity in the group, the lead state should notify the domestic state of this issue and share the relevant information from the CGAD with that state in a timely manner. ~~The Lead State can share the analysis of the filing through NAIC tools (i.e., iSite+~~



**VI.D. Group-Wide Supervision – Corporate Governance Disclosure Procedures**

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~~Regulator File Sharing System) or other means deemed appropriate. Before a non-lead state requests the CGAD filing or conducts a full review of CGAD to determine its impact on their domestic insurers, non-lead domestic states should consider obtaining and reviewing the Lead State's analysis of CGAD to reduce duplication of analysis efforts.~~

~~To the extent the Lead State's analysis of the Corporate Governance Annual Disclosure (CGAD) addresses policies and practices of the group applicable to the non-lead state's domestic insurer, that analysis may be leveraged by the non-lead state to reduce the analysis work of the non-lead state. If the Lead State's analysis of CGAD does not assess the impact on the non-lead state's domestic insurer or the CGAD is on a legal entity basis, the non-lead domestic state should consider a review of CGAD. Analysis steps are included in the non-lead state analysis procedures.~~

**PROCEDURES #1 - 2** ~~assist~~ [provides a guide to assist](#) analysts in reviewing the Corporate Governance disclosure for completeness and help guide analysts through each of the major items of information required by Model #306. [As noted above, concerns should be documented in the GPS, as there is no requirement or expectation for the analyst to create a separate CGAD checklist or create additional review documentation.](#)

**PROCEDURES #3 - 5** [provides a guide to](#) assist analysts in summarizing any concerns relative to the insurer or insurance group's corporate governance and its impact. [Risks and concerns should be documented in the GPS.](#)

**Compliance with Corporate Governance Disclosure Requirements**

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[The following procedures are intended to guide the analyst through a review of the CGAD. These procedures do not represent a documentation requirement.](#)

1. Does the disclosure provide information regarding the following areas as required by Model #306?
  - a. The insurer's or insurance group's corporate governance framework and structure including consideration of the following.
    - i. The Board and various committees thereof ultimately responsible for overseeing the insurer or insurance group and the level(s) at which that oversight occurs (e.g., ultimate control level, intermediate holding company, legal entity, etc.). The insurer or insurance group shall describe and discuss the rationale for the current Board size and structure; and
    - ii. The duties of the Board and each of its significant committees and how they are governed (e.g., bylaws, charters, informal mandates, etc.), as well as how the Board's leadership is structured, including a discussion of the roles of Chief Executive Officer (CEO) and Chair of the Board within the organization.
  - b. The policies and practices of the most senior governing entity and significant committees thereof, including a discussion of the following factors:
    - i. How the qualifications, expertise and experience of each Board member meet the needs of the insurer or insurance group.
    - ii. How an appropriate amount of independence is maintained on the Board and its significant committees.
    - iii. The number of meetings held by the Board and its significant committees over the past year as well as information on director attendance.
    - iv. How the insurer or insurance group identifies, nominates and elects members to the Board and its committees. The discussion should include, for example:
      1. Whether a nomination committee is in place to identify and select individuals for consideration.
      2. Whether term limits are placed on directors.



**VI.D. Group-Wide Supervision – Corporate Governance Disclosure Procedures**

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3. How the election and re-election processes function.
4. Whether a Board diversity policy is in place and if so, how it functions.
- v. The processes in place for the Board to evaluate its performance and the performance of its committees, as well as any recent measures taken to improve performance (including any Board or committee training programs that have been put in place).
- c. The policies and practices for directing senior management, including a description of the following factors:
  - i. Any processes or practices (i.e., suitability standards) to determine whether officers and key persons in control functions have the appropriate background, experience and integrity to fulfill their prospective roles, including:
    1. Identification of the specific positions for which suitability standards have been developed and a description of the standards employed.
    2. Any changes in an officer's or key person's suitability as outlined by the insurer's or insurance group's standards and procedures to monitor and evaluate such changes.
  - ii. The insurer's or insurance group's code of business conduct and ethics, the discussion of which considers, for example:
    1. Compliance with laws, rules, and regulations.
    2. Proactive reporting of any illegal or unethical behavior.
  - iii. The insurer's or insurance group's processes for performance evaluation, compensation and corrective action to ensure effective senior management throughout the organization, including a description of the general objectives of significant compensation programs and what the programs are designed to reward. The description shall include sufficient detail to allow the Commissioner to understand how the organization ensures that compensation programs do not encourage and/or reward excessive risk-taking. Elements to be discussed may include, for example:
    1. The Board's role in overseeing management compensation programs and practices.
    2. The various elements of compensation awarded in the insurer's or insurance group's compensation programs and how the insurer or insurance group determines and calculates the amount of each element of compensation paid.
    3. How compensation programs are related to both company and individual performance over time.
    4. Whether compensation programs include risk adjustments and how those adjustments are incorporated into the programs for employees at different levels.
    5. Any "clawback" provisions built into the programs to recover awards or payments if the performance measures upon which they are based are restated or otherwise adjusted.
    6. Any other factors relevant in understanding how the insurer or insurance group monitors its compensation policies to determine whether its risk- management objectives are met by incentivizing its employees.
  - iv. The insurer's or insurance group's plans for CEO and senior management succession.
- d. The insurer or insurance group shall describe the processes by which the Board, its committees and senior management ensure an appropriate amount of oversight to the critical risk areas impacting the insurer's business activities, including a discussion of:

**VI.D. Group-Wide Supervision – Corporate Governance Disclosure Procedures**

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- i. How oversight and management responsibilities are delegated between the Board, its committees and senior management;
  - ii. How the Board is kept informed of the insurer’s strategic plans, the associated risks, and steps that senior management is taking to monitor and manage those risks;
  - iii. How reporting responsibilities are organized for each critical risk area. The description should allow the commissioner to understand the frequency at which information on each critical risk area is reported to and reviewed by senior management and the Board. This description may include, for example, the following critical risk areas of the insurer:
    1. Risk management processes (an ORSA Summary Report filer may refer to its ORSA Summary Report pursuant to the *Risk Management and Own Risk and Solvency Assessment Model Act (Model #505)*);
    2. Actuarial function
    3. Investment decision-making processes
    4. Reinsurance decision-making processes
    5. Business strategy/finance decision-making processes
    6. Compliance function
    7. Financial reporting/internal auditing
    8. Market conduct decision-making processes
2. If the insurer or insurance group has not disclosed specific information listed in Procedure 1 above, was other information included that adequately describes why such information was not included?

**Assessment of Corporate Governance Disclosure**

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3. Is the analyst aware of any significant and material corporate governance information not reported in the disclosure? If “yes,” refer to the Management Considerations section of IV.A. Financial Analysis and Reporting Considerations for additional guidance.
- ~~4. Based on the analyst’s review of Corporate Governance disclosure and any additional information related to the corporate governance of the insurer or insurance group, document any material concerns regarding corporate governance of the insurer or insurance group.~~
- 5.4. Do any of the concerns pose an immediate risk to the insurer’s or insurance group’s operations, policyholder surplus or capital position?

**For the U.S. lead state:**

- Analysts should update the Group Profile Summary and Supervisory Plan with any [risks, concerns, and](#) material information.
- [Analysts should notify the domestic state of any issues that are only relevant to a particular insurance entity in the group and share the relevant information from the CGAD with that state in a timely manner.](#)
- Analysts should communicate to the examiner-in-charge (EIC) any prospective risks identified in the review of [the](#) corporate governance [annual](#) disclosure that affects the domestic insurer.

**Recommendations for further action, if any, based on the overall conclusion above:**

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For the U.S. lead state that is also the group-wide supervisor:

**VI.D. Group-Wide Supervision – Corporate Governance Disclosure Procedures**

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- ❑ Contact the holding company seeking explanations or additional information
- ❑ Meet with the holding company management
- ❑ Pursue, as appropriate, within an international supervisory college
- ❑ Other (explain)

For the U.S. lead state that is not the group-wide supervisor:

- ❑ Contact the group-wide supervisor, seeking explanations or additional information
- ❑ Pursue, if applicable and as appropriate, within an international supervisory college
- ❑ Other (explain)

For a non-lead state:

- ❑ Contact the lead state, seeking explanations or additional information [if questions exist about information noted in the GPS](#)
- ❑ Pursue, if applicable and as appropriate, within an international supervisory college (if applicable)

**VI.D. Group-Wide Supervision – Corporate Governance Disclosure Procedures**

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<b>Analyst:</b>	<b>Date:</b>
<b>Supervisor Review:</b>	<b>Date:</b>
<b>Supervisor Comments:</b>	

## VI.E. Group-Wide Supervision – Enterprise Risk Management Process Risks Guidance

----- DETAIL HAS BEEN ELIMINATED TO CONSERVE SPACE -----

**Form F - Enterprise Risk Report**

The 2010 revisions to Model #440 and *Insurance Holding Company System Model Regulation with Reporting Forms and Instructions* (#450) introduced a new filing requirement for a Form F. The Form F requires the ultimate controlling person to identify the material risks within the insurance holding company system that could pose enterprise risk to the insurer. The Form F may be completed using information contained in the financial statement, annual report, proxy statement, statement filed with a governmental authority, or other documents if such information meets the disclosure requirements. Form F is focused on disclosing the enterprise risk associated with the entire insurance holding company system including non-regulated entities. The Form F is filed with the lead state commissioner of the insurance holding company system for every insurer subject to registration under Model #440. Adoption of the applicable Form F and related confidentiality provisions outlined in the 2010 revisions to Model #440 is required for a state to be designated the lead state for Form F filings. Lead states and other domestic states receiving and sharing the Form F must have in place confidentiality agreements as prescribed in #Model 440.

**Lead State Responsibility for Analysis of Form F**

The Lead State should take primary responsibility for reviewing the Form F filing and should incorporate any takeaways, risks or concerns into the GPS. Takeaways, risks and concerns should be incorporated into the ERM summary in the GPS and/or the discussion of various branded risks, as deemed appropriate. There is no requirement or expectation to create a separate Form F checklist or create additional review documentation for sharing with another state or for internal documentation purposes.

If the Form F highlights any issues or risks that are only relevant to a particular insurance entity in the group, the Lead State should notify the domestic state of the issue and share the relevant information from the Form F with that state in a timely manner.

**~~Non-Lead State Reliance on the Lead State Analysis of Form F~~**

~~Although by inclusion in this section, reviewing the group Form F report is a responsibility of the lead state, the approach on this is different from that taken with the ORSA. Generally speaking, a non-lead state should not review the ORSA with the same level of depth as the lead state. However, that same approach is not encouraged with respect to the Form F. The entire purpose of the Form F is to identify if there is any contagion risk within the group, and domestic states should not be discouraged from reviewing such information because ultimately, they are required to relate the financial condition of the group to their domestic state. Most believe that the ORSA is much more detailed and less related to contagion as it is the group's actual risk management processes used to mitigate risk.~~

~~The Form F must be reviewed by the lead state and significant findings incorporated into the GPS. However, other domestic states are also expected to review the Form F in order to assess the impact of the group on their domestic insurer. One exception for non-lead states should be noted. **To the extent the lead state's analysis of Form F assesses the impact of any contagion risk of the group on the non-lead state's domestic insurer, that analysis may be leveraged by the non-lead state to reduce the analysis work of the non-lead state.** If the lead state's analysis of Form F does not assess the impact of the group on the non-lead state's domestic insurer, the non-lead domestic state should review Form F. The Lead State can share the Form F and its analysis through NAIC tools (Form F Sharing Tool for the filings and the iSite+ Regulator File Sharing System for the analysis). Analysis steps are included in the non-lead state analysis procedures with that in mind. To reduce duplication, domestic states should consider obtaining and reviewing the lead state's analysis of Form F before determining if a full review of the filing is necessary to determine its impact on their domestic insurers.~~

**Non-Lead State Reliance on the Lead State Analysis of Form F**

## VI.E. Group-Wide Supervision – Enterprise Risk Management Process Risks Guidance

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The Form F must be reviewed by the lead state and significant findings incorporated into the GPS. The non-lead state is encouraged to review the ERM summary and other information provided by the lead state in the GPS to access relevant information shared through Form F. There is no expectation of additional information shared by the lead state in this area, unless Form F highlights issues or risks that are only relevant to a particular insurance entity in the group. In that case, the non-lead state(s) should rely on the Lead State to proactively provide this information in a timely manner.

If there are material concerns noted in the GPS and additional information is needed, the non-lead state should request additional information from the lead state or company, if available. Such information could include additional information from the Form F filing, if relevant.

Upon the receipt of any additional information, the non-lead state should document any material concerns regarding enterprise risk that could impact the financial condition of the domestic insurer and conclude whether any of the risks identified pose an immediate material risk to the insurer's policyholder surplus or risk-based capital position, insurance operations (e.g., changes in writings, licensure, and organizational structure), balance sheet, leverage, or liquidity.

### **NAIC Enterprise Risk Report (Form F) Implementation Guide**

In March 2018, the Group Solvency Issues (E) Working Group adopted *the NAIC Enterprise Risk Report (Form F) Implementation Guide*, which is located at:

[https://www.naic.org/documents/committees\\_e\\_isftf\\_group\\_solvency\\_related\\_form\\_f\\_guide.pdf?97](https://www.naic.org/documents/committees_e_isftf_group_solvency_related_form_f_guide.pdf?97)

As outlined in the Guide, it is intended to assist insurers and regulators in maximizing the usefulness of the Form F by proposing best practices for consideration in preparing and reviewing filings. Therefore, while the Guide does not constitute authoritative guidance for information to be included in a Form F filing, filers are requested to consider the best practices outlined within the Guide when preparing their Form F filing. By adhering to the best practices outlined within the Guide, registrants will be able to reduce the extent of regulator follow-up and correspondence necessary to utilize the information provided, which should lead to a more effective and efficient process. The regulators' goal in developing this document was to provide some consistency and uniformity across states in reviewing and utilizing information obtained through the Form F. Therefore, it is recommended that states utilize the best practices outlined in the Guide to support their review and feedback process.

**PROCEDURES #1 - 2** provides a guide to assist analysts in reviewing the Form F filing for completeness and help guide analysts through each of the major items of information required by Form F. Analysts should review Form F in conjunction with a review of Form B and should document any nondisclosure of information. As noted above, concerns should be documented in the GPS, as there is no requirement or expectation for the analyst to create a separate Form F checklist or create additional review documentation.

**PROCEDURES #3 - 7** provides a guide to assist analysts in evaluating the risks described within Form F. Analysts should consider whether any enterprise risks not reported in Form F exist, and for all risks identified both within Form F and by analysts, analysts should review information available and document any concerns. Analysts should also evaluate whether the risks identified result in an impact to the insurer's financial condition (e.g., surplus, RBC, insurance operations, balance sheet, leverage and liquidity). Risks and concerns should be documented in the GPS.

**VI.G. Group-Wide Supervision – Form F – Enterprise Risk Report Procedures**

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**Special Note: The following procedures do not supersede state regulation but are merely additional guidance an analyst may consider useful.**

*The following procedures are intended to guide the analyst through a review of the Form F. These procedures do not represent a documentation requirement.*

**Compliance with Reporting Requirements**

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1. Does Form F provide information regarding the following areas that could pose enterprise risk [provided such information is not disclosed in Form B – Insurance Holding Company System Annual Registration Statement]?
  - a. Material developments regarding strategy, compliance or risk management affecting the insurance holding company system, or internal audit findings.
  - b. Acquisition/disposition of insurance entities and/or reallocation of existing financial or insurance entities within the insurance holding company system.
  - c. A change in shareholders of the insurance holding company system that exceed (10% or more of voting securities).
  - d. Development in investigations, regulatory activities or litigation that may have a significant bearing or impact on the insurance holding company system.
  - e. A business plan of the insurance holding company system and summarized strategies for the next 12 months.
  - f. Identify material concerns of the insurance holding company system raised by the supervisory college.
  - g. Identify capital resources and material distribution patterns of the insurance holding company system.
  - h. Identify any negative movement, or discussions with rating agencies that may have caused, or may cause, potential negative movement in credit ratings and insurer financial strength ratings assessment of the insurance holding company system (including both the rating score and outlook).
  - i. Corporate or parental guarantees throughout the insurance holding company system and the expected source of liquidity should such guarantees be called upon.
  - j. Identify any material activity or development that, in the opinion of senior management, could adversely affect the insurance holding company system.
2. If the registrant/applicant has not disclosed information listed in procedure 1 above, did the registrant/applicant include a statement that, to the best of his or her knowledge and belief, he or she has not identified enterprise risk subject to disclosure?

**Assessment of Form F – Enterprise Risk Report**

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3. Is the analyst aware of any enterprise risk to the insurer not reported in Form F?
4. Based on the analyst's review of Form F and any additional information related to enterprise risk available (e.g., Form B, other filings), document any material concerns regarding enterprise risk to the group.
5. Do any of the risks identified pose an immediate risk to ~~the insurer's~~ policyholder surplus or risk-based capital position of insurers in the group?
6. Do any of the risks identified result in material impact to the insurance operations of the group? (e.g., changes in writings, licensure, and organizational structure)?
7. Do any of the risks identified result in material impact to the group's balance sheet, leverage or liquidity?

**VI.G. Group-Wide Supervision – Form F – Enterprise Risk Report Procedures**

**For the U.S. lead state:**

- Analysts should update the ~~Holding Company System Analysis~~[Group Profile Summary](#); ~~Branded Risk Assessments~~ and Supervisory Plan ~~in the Group Profile Summary~~ with the risks identified and results from the Form F review.
- [Analysts should notify the domestic state of any issues that are only relevant to a particular insurance entity in the group and share the relevant information from the Form F with that state in a timely manner.](#)
- Analysts should communicate to the examiner-in-charge (EIC) any prospective risks identified in the review of Form F that affects the domestic insurer.

**Recommendations for further action, if any, based on the overall conclusion above**

For the U.S. lead state that is also the group-wide supervisor

- Contact the holding company seeking explanations or additional information
- Meet with the holding company management
- Pursue, as appropriate, within an international supervisory college
- Other (explain)

For the U.S. lead state that is not the group-wide supervisor

- Contact the group-wide supervisor, seeking explanations or additional information
- Contact the holding company directly if deemed appropriate by the group-wide supervisor given the Form F is a U.S. only filing
- Pursue, if applicable and as appropriate, within an international supervisory college
- Other (explain)

For a non-lead state

- Contact the lead state, seeking explanations or additional information [if questions exist about information noted in the GPS](#)
- Pursue, if applicable and as appropriate, within an international supervisory college (if applicable)

<del>Analyst:</del>	<del>Date:</del>
<del>Supervisor Review:</del>	<del>Date:</del>
<del>Supervisor Comments:</del>	



III.B.1.a. Credit Risk Repository – P/C Annual

----- DETAIL ELIMINATED TO CONSERVE SPACE -----

NOTE – THE SAME CHANGES BELOW WOULD BE APPLIED TO THE LIFE/HEALTH AND HEALTH REPOSITORIES (III.B.1.b and III.B.1.c) AS WELL AS REPOSITORIES FOR MARKET RISK, LIQUIDITY RISK AND OPERATIONAL RISK.

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Related Party Exposure in the Investment Portfolio

#13. Assess related party exposure in the investment portfolio.

	Other Risks
<p>a. <u>Review the Annual Financial Statement investment schedules, as disclosed in the column “Investments Involving Related Parties” and utilizing iSite+ tools, determine if the insurer has material related party exposures in its investment portfolio.</u></p> <p><u>This disclosure is included in:</u></p> <ul style="list-style-type: none"> <li>• <u>Schedule B</u></li> <li>• <u>Schedule BA</u></li> <li>• <u>Schedule D</u></li> <li>• <u>Schedule DA</u></li> <li>• <u>Schedule DB</u></li> <li>• <u>Schedule DL</u></li> <li>• <u>Schedule E, Part 2</u></li> </ul> <p><u>Consider exposure by asset class and in aggregate, and by the role of the related party in the investment as designed by the “Investments Involving Related Parties” disclosure.</u></p>	LQ, MK
<p><del>a.</del>b. <u>If concerns exist regarding a material related party exposure in the investment portfolio, assess the credit quality of those investments involving related parties by reviewing designations, assessing historical default experience, etc.</u></p>	LQ, MK

## III.B.1.a. Credit Risk Repository – P/C Annual

<p><u>c. If concerns exist regarding a material related party exposure in investment management or advisory services, consider the following:</u></p> <p><u>i. Review the procedures in the “Additional Procedures” section below regarding Third Party Investment Advisors and consider their application to related party advisors in that role.</u></p> <p><u>ii. In addition to the additional analysis procedures regarding third party investment advisors, consider the following:</u></p> <ol style="list-style-type: none"> <li><u>1. Review the insurer’s investment policy guidelines and determine whether the related party investments follow the guidelines and are in compliance with regulatory requirements.</u></li> <li><u>2. Review whether the fee structure for asset management is fair, reasonable, and appropriately recognized as investment expenses.</u></li> <li><u>3. If the related party asset manager also originates/securitizes investments held by the insurer, consider requesting additional information from the insurer to determine the following:</u> <ol style="list-style-type: none"> <li><u>a. Whether the asset manager has adequate experience and knowledge in originating and managing the types of investments;</u></li> <li><u>b. Whether the asset manager follows appropriate underwriting practices and applicable regulatory requirements in originating investments; and</u></li> <li><u>c. Whether the fee structures embedded in securities (if applicable) are fair, reasonable, and appropriately account for potential duplication of fees or conflicts of interest.</u></li> </ol> </li> </ol>	OP
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**Additional Analysis and Follow-up Procedures****Third Party Investment Advisors:**

Assess and determine if any concerns exist regarding third party investment advisors and associated contractual arrangements.

- Review Annual Financial Statement, General Interrogatories, Part 1, #28.05. Does the insurer utilize third party investment advisors, broker/dealer or individuals acting on behalf of the insurer with access to their investment accounts?

If “yes,” consider the following procedures:

- Review the results of the most recent financial examination work papers, follow-up and prospective risk information and the summary review memorandum provided by the examiners. Did the examination identify any issues with regard to investment advisors and associated contractual arrangements that require follow-up analysis or communication with the insurer? If “yes,” document the follow-up work performed.
- Compare Annual Financial Statement, General Interrogatories, Part 1, #28.05 for the current year to the prior year to determine if there have been any changes in advisors. If “yes,”
  - Consider obtaining an explanation for the change from the insurer
  - Consider obtaining a copy of the new investment advisor agreement and review it for appropriate provisions

**III.B.1.a. Credit Risk Repository – P/C Annual**

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- Using the information reported in Annual Financial Statement, General Interrogatories, Part 1, #28.05, obtain and review SEC Form ADV (if available), to determine if the investment advisor is in good standing with the SEC. If not in good standing, contact the insurer to request an explanation.
- If agreements with third party investment advisers are affiliated, have the appropriate Form D – Prior Notice of Transactions been filed and approved by the department? Were any concerns noted or follow-up monitoring recommended?
- Request information from the insurer regarding the background and expertise in structured securities of its investment advisors (in-house and/or contractual) and its analytical system capabilities. Determine whether the advisors and systems are adequate to allow the insurer to continuously monitor its structured securities investments.
- If the insurer uses an external asset manager, consider if investments on the Annual Financial Statement, Schedule BA are invested in funds that are affiliated with the asset manager or are managed by that asset manager. Consider the following issues:
  - If any conflicts of interest exist
  - If the investment is appropriate for the insurer’s portfolio and arm’s-length
  - If the insurer is paying double fees

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## III.B.1.d. Credit Risk Repository – Analyst Reference Guide

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**NOTE – THE SAME CHANGES BELOW WOULD BE APPLIED TO THE LIFE/HEALTH AND HEALTH REPOSITORIES (III.B.1.b and III.B.1.c) AS WELL AS REPOSITORIES FOR MARKET RISK, LIQUIDITY RISK AND OPERATIONAL RISK.**

**PROCEDURE #13 INVESTMENTS INVOLVING RELATED PARTIES** assist analysts in determining related party exposure in the investment portfolio and assessing any related credit [market, liquidity, operational] risk.

Related parties are entities that have common interests as a result of ownership, control, affiliation or by contract as defined in *SSAP No. 25—Affiliates and Other Related Parties* (SSAP No. 25). Refer to the *Insurance Holding Company System Model Act* (Model #440) and SSAP No. 25 for a broader definition of "affiliate," "related party" and "control".

Related party transactions are subject to abuse because reporting entities may be induced to enter transactions that may not reflect economic realities or may not be fair and reasonable to the reporting entity or its policyholders. As such, related party transactions require specialized accounting rules and increased regulatory scrutiny.

The analyst should utilize the tools available in iSite+ to identify if the insurer has a material exposure to investments involving related parties, either on an asset category basis or in aggregate, and by the related party designation noted below. If a material exposure exists, further assessment of the [credit, market, liquidity] risk may be warranted. For example, what is the NAIC designation of investments involving related parties? Analysts may also consider the extent to which related parties are involved in securitizing or originating business for the insurer, and what differences may exist in how investments involving related parties are valued. If the role of the related party is that of a third-party advisor, factors to consider may include for example, the expertise of the related party advisor, any potential conflicts of interest, and if related parties are originating investments only for the insurer or also to the public, the latter being subject to SEC requirements. The analyst may consider utilizing suggested procedures in the "Additional Procedures" section of the repository on third-party advisors, if applicable.

Within the Annual Financial Statement investment Schedules B, BA, D, DA, DB, DL, and E (Part 2), all investments involving related parties must include disclosure to ensure full transparency. This disclosure is in the column "Investments Involving Related Parties". It designates investments by the following roles:

1. Direct loan or direct investment (excluding securitizations) in a related party, for which the related party represents a direct credit exposure.
2. Securitization or similar investment vehicles such as mutual funds, limited partnerships and limited liability companies involving a relationship with a related party as sponsor, originator, manager, servicer, or other similar influential role and for which 50% or more of the underlying collateral represents investments in or direct credit exposure to related parties.
3. Securitization or similar investment vehicles such as mutual funds, limited partnerships and limited liability companies involving a relationship with a related party as sponsor, originator, manager, servicer or other similar influential role and for which less than 50% (including 0%) of the underlying collateral represents investments in or direct credit exposure to related parties.
4. Securitization or similar investment vehicles such as mutual funds, limited partnerships and limited liability companies in which the structure reflects an in-substance related party transaction but does not involve a relationship with a related party as sponsor, originator, manager, servicer or other similar influential role.
5. The investment is identified as related party, but the role of the related party represents a different arrangement than the options provided in choices 1-4.
6. The investment does not involve a related party.

### III.A.4. Risk Assessment (All Statement Types) – Analyst Reference Guide

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#### **Risk Assessment Levels and Trends**

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The financial analysis process assigns each risk component within the branded risk classification an assessment level commensurate with the nature, complexity and severity of the risk of either Minimal, Moderate or Significant. Additionally, analysts also assign a trend level to indicate the direction the risk is moving, either decreasing, static or increasing. Although risk assessment levels and trends are based on the judgement of the analyst and supervisor, they should factor in both quantitative and qualitative elements, as well as both current and prospective considerations. Note that within each of the three assessment levels, there may be appropriate grading of the severity of the risk.

[With regard to setting individual risk assessments, the level of concern and trend of a risk is not defined relative to other risks facing the insurer. Risks should be assessed individually on each's factors and circumstances. Analysts should not automatically assess the "top" risks of an insurer as Significant, Moderate or Increasing, if the factors don't meet the criteria for those assessment levels and trend. An insurer may have none, one, or multiple Significant risks, depending upon individual facts and circumstances. Failing to follow this guidance may result in an inappropriately high risk assessment for the individual risk component, but also for the branded risk category and the overall assessment of the insurer.](#)

## III.B.7.a. Reputational Risk Repository – Annual (All Statement Types)

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Note the same change would be applied to the quarterly reputational risk repository #2.

(Chapter III.B.7.a)

## Ratings

### 2. Determine if concerns exist regarding the insurer or insurance group's ratings.

	Other Risks
a. Review the most recent report from a credit rating provider (e.g., A.M. Best, Moody's, Standard & Poor's, Fitch, and Weiss) for the current financial strength and credit ratings and outlook, as well as an explanation of any change in the ratings.	PR/UW, ST
b. If concerns exist regarding a poor financial strength or credit rating, a negative outlook, or a rating change for the insurer or the insurance holding company, review the most recent report from the credit rating provider (CRP) to determine if the rating is at a level that may impact the insurer's ability to continue to write new business or that may impact other business functions (e.g., terms of debt covenants, ability to attract financing, ability to place reinsurance, etc.).	PR/UW, ST
<u>c. Health Insurers Only: Obtain and review the most recent information about CMS's Star Rating of the insurer, as well as an explanation of any change in the rating, to determine if concerns exist regarding the impact to the insurer's reputation, pricing and underwriting, and/or future strategic plans. Also note whether if the insurer has received a Star Rating of 4 or more and in turn received annual bonus payments from CMS to be spent on extra benefits for its members. Assess the reliance on bonus payments and the possible impact should the insurer no longer receive them.</u>	PR/UW, ST

### Example Prospective Risk Considerations

Risk Components for IPS		Explanation of Risk Components
1	Reputational impact of [other branded risks]	The risk that other concerns, primarily associated with other branded risk classifications, may damage the insurer's reputation.
2	Negative publicity related to [name of event]	Negative publicity for the insurer or its affiliates could affect the insurer's ability to write new business or retain its current business.
3	Financial strength rating downgrade by [name of rating agency]	A rating decline or a poor rating could negatively affect the insurer's ability to write new business, or it may affect other business operations. For example, debt covenants often include requirements to maintain ratings above a certain level.
4	Poor financial strength rating by [name of rating agency] [sustained or new]	Same as above.
5	<u>Poor Star Rating (Health only)</u>	<u>Star ratings issued by the Centers for Medicare &amp; Medicaid Services (CMS) reflect performance and members satisfaction and certain Medicare plans, which may impact the insurer's reputation, pricing and underwriting, and future strategic plans.</u>
5	Poor PSA [financial strength or credit] rating	Poor ratings by a PSA may have an indirect impact on the insurer.

**III.B.7.a. Reputational Risk Repository – Annual (All Statement Types)**

6	Market conduct examination [specify findings, corrective actions, etc.]	Material findings or corrective actions, including large fines, settlements or required remediation (e.g., re-reviewing denied claims), may have a current or prospective financial impact on the insurer. (E.g., if corrective actions extend into future years and result in future costs or changes in operating practices)
7	Material market conduct violations/concerns [related to ...]	Identified from communications or other iSite+ data.
8	Financial impact of remediation of market conduct violations	Identifies the financial impact both currently and prospectively in terms of either dollars or operation/process changes.

## Reputational Risk Assessment

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### Ratings

**PROCEDURE #2** directs analysts to determine if concerns exist regarding the insurer or insurance group's ratings. Ratings received from a rating agency, as well as changes in the ratings and company/industry outlooks, can have a significant impact on the insurer or insurance group's reputation. Therefore, analysts are strongly encouraged to monitor agency ratings and outlooks when assessing an insurer's exposure to reputational risk. The primary agencies that issue ratings to insurers include A.M. Best, Fitch Ratings, Moody's Investors Service, Standard & Poor's and Weiss Financial Group. For more information on these agencies and their ratings processes, see I. Introduction C. External Information. In reviewing agency ratings, reports and outlooks, analysts should consider and assess the reputational impact of any negative movements or trends with the potential to impact the insurer, as such trends may limit the insurer's ability to write new business or otherwise affect ongoing operations.

[Procedure 2.c. applies only to health insurers and instructs the analyst to obtain and review the most recent information about Centers for Medicare and Medicaid Services \(CMS\)'s Star Rating of the insurer, as well as an explanation of any change in the rating. Star ratings are calculated by CMS based on the insurer's performance and member satisfaction data for Medicare plans including Medicare Advantage and Medicare Part D prescription drug plans. The ratings measure various factors and assign ratings on a scale from 1 to 5 stars, where 5 is the best. Star ratings help consumers compare the quality of Medicare plans. -Performance data including Star ratings are available on the following CMS website:](#)

<https://www.cms.gov/Medicare/Prescription-Drug-Coverage/PrescriptionDrugCovGenIn/PerformanceData>

[A low or lowering of the Star rating may result in concerns regarding the insurer's reputation leading to loss of membership, decrease in underwriting results, and changes in future strategic plans. Where concerns exist, the analyst should consider gaining an understanding of the reasons for the low or lowering of the Star rating from the insurer, and how it impacts membership and future operations.](#)

[Also noteworthy is that insurers with Star ratings of 4 or higher receive annual bonus payments from CMS, which is required to be spent on extra benefits for members, which benefits consumers. Plans that receive at least four out of five stars have their benchmark increased. Total Spending on Medicare Advantage plan bonus payments have risen every year. The growth in spending on bonus payments has coincided with the increase in Medicare Advantage enrollment. Annual bonus payments from the federal government to Medicare insurers have reached an all-time high at a time when the Medicare program is facing growing fiscal pressures. -The analyst should consider the amount of the bonus payments relative to the overall profit/loss and assess the reliance on those bonus payments and the possible impact should the insurer no longer receive them.](#)



III.B.8.b. Reserving Risk Repository – Life/A&H/Fraternal Annual

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

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**Adequacy of Life Reserves**

5. Determine whether the insurer’s underlying assets are adequate to support the future obligations of its life insurance policies.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Net interest spread on life reserves (net investment income, less tabular interest, divided by average life reserves)	MK, OP	< 2%	[Data]	[Data]
b. Change in Asset Mix (IRIS Ratio 11)	OP, ST	> 5%	[Data]	[Data]
				<i>Other Risks</i>
c. If the insurer filed a Statement of Actuarial Opinion based on an asset adequacy analysis, review the results of the Actuarial Opinion Repository and note any concerns regarding the adequacy of the insurer’s underlying assets to support future life insurance policy obligations.				
d. Pursuant to the review of the Regulatory Asset Adequacy Issues Summary (RAAIS) in the Actuarial Opinion Repository, note whether the responses to the questions were satisfactory.				
e. If concerns still exist upon review of the asset adequacy analysis, discuss with the appointed actuary and the company and request any additional information or work to be performed to address these concerns. If the insurance commissioner determines that the supporting actuarial memorandum fails to meet the standards prescribed by the Valuation Manual or is otherwise unacceptable to the insurance commissioner, the insurance commissioner may engage a qualified actuary at the expense of the company to review the opinion and basis for the opinion and prepare the supporting actuarial memorandum required by the insurance commissioner. See the state’s equivalent authority to NAIC Model #820, Section 3B(3)(b). This also is noted in the Actuarial Opinion Repository.				
f. <a href="#">Review the Actuarial Guideline 53 reporting <del>in the regarding</del> relating to assumptions and sensitivity testing for <b>reinvested</b> high-yielding complex assets within the asset adequacy analysis, if applicable. Determine whether concerns exist in meeting asset adequacy requirements. See further guidance in the AOMR procedures and reference guide.</a>				

## III.B.8.b.i. Statement of Actuarial Opinion Worksheet – Life/A&amp;H/Fraternal Annual

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**Actuarial Memorandum****4. Consider the following procedures for reviewing the Actuarial Memorandum.**

	<i>Comments</i>
a. Did the qualified actuary conduct an asset adequacy test on the insurer's total reserves?	
b. For any reserve or other liability reported as not analyzed, did the qualified actuary indicate that such reserve or other liability was immaterial?	
c. Based upon the judgment of the analyst and after reviewing the SAO and RAAIS and discussing with the department actuary, determine if the actuarial memorandum should be requested from the insurer. <i>If "yes", the department actuary should perform the review of the Actuarial Memorandum. If no, skip the remaining procedures in this sub-section.</i>	
d. If the company does not have or provide an Actuarial Memorandum or in the review of the Actuarial Memorandum it is determined that the memorandum fails to meet the standards prescribed by the <i>Valuation Manual</i> or is otherwise unacceptable to the insurance commissioner, the insurance commissioner may engage a qualified actuary at the expense of the company to review the opinion and basis for the opinion and prepare the supporting Actuarial Memorandum required by the insurance commissioner. See the state's equivalent authority to the NAIC <i>Standard Valuation Law</i> (#820), Section 3B(3)(b).	
e. Does the Actuarial Memorandum include an asset adequacy analysis for the following? <i>(Note that the items required to be included may vary from state to state.)</i>	
i. For reserves: <ul style="list-style-type: none"> <li>• Product descriptions.</li> <li>• Source of liability in-force.</li> <li>• Reserve method and basis.</li> <li>• Investment reserves.</li> <li>• Reinsurance arrangements.</li> <li>• Persistency of in-force business.</li> <li>• Identification of any guarantees made by the separate account in support of benefits provided through a separate account.</li> <li>• Discussion of assumptions to test reserves.</li> </ul>	
ii. For assets: <ul style="list-style-type: none"> <li>• Portfolio descriptions.</li> <li>• Investment and disinvestment assumptions.</li> <li>• Source of asset data.</li> <li>• Asset valuation bases.</li> <li>• Documentation of assumptions made.</li> </ul>	
iii. For the analysis basis: <ul style="list-style-type: none"> <li>• Methodology.</li> </ul>	

**III.B.8.b.i. Statement of Actuarial Opinion Worksheet – Life/A&H/Fraternal Annual**

<ul style="list-style-type: none"> <li>• Rationale for inclusion or exclusion of different blocks of business and how pertinent risks were analyzed.</li> <li>• Rationale for degree of rigor in analyzing different blocks of business.</li> <li>• Criteria for determining asset adequacy.</li> <li>• Effect of federal income taxes and method of treating reinsurance in the asset adequacy analysis.</li> </ul>	
iv. Summary of material changes.	
v. Summary of results.	
vi. Conclusions.	
vii. A statement that the actuarial methods, considerations and analyses used in the preparation of this memorandum conform to the appropriate Actuarial Standards of Practice as promulgated by the Actuarial Standards Boards, which standards form the basis for the memorandum.	
viii. Method for aggregating reserves and assets.	
ix. Method for selecting and/or allocating assets supporting the Asset Valuation Reserve.	
x. Analysis of the effect of required interest rate scenarios.	
f. <a href="#"><u>If required within the scope of Actuarial Guidelines 53 (AG-53) and as required under VM-30, did the AOMR include a separate section documenting the assumptions and sensitivity testing for <b>reinvested</b> high-yielding complex assets?</u></a>	

**5. Identify any concerns from the review of the Actuarial Memorandum including, but not limited to, the areas of assets, liabilities, scenario results, actuarial assumptions, sensitivity tests and the general overall adequacy of the asset adequacy analysis.**

	<i>Comments</i>
If additional concerns are noted based on the review of the RAAIS and/or Actuarial Memorandum, consider performing the following additional procedures [Note: Procedures “a” through “d” are applicable to insurers utilizing the New York 7 actuarial interest rate scenario tests. Procedure “e” is applicable to other cash flow scenario testing.]	
a. Request from the company’s appointed actuary the year-by-year cash flow testing results from the five worst scenarios tested.	
b. Review the five worst year-by-year scenario test results and determine the largest cash flow deficiency.	
c. Assess the materiality of the largest deficiency(ies).	
d. If the worst scenario were to play out, determine the impact on the current RBC ratio.	
e. In the review of interim year-by-year scenario test results, review appropriateness of assumptions to fund negative cash flow, for example:	

**III.B.8.b.i. Statement of Actuarial Opinion Worksheet – Life/A&H/Fraternal Annual**

<ul style="list-style-type: none"> <li>i. Review explanations provided for how the insurer will fund negative cash flows.</li> <li>ii. Request borrowing agreements from the insurer and assess the insurer’s borrowing capacity and ability to execute a borrowing strategy. Compare cash flow requirements to the borrowing capacity.</li> <li>iii. If borrowing capacity is insufficient, what are the alternative options within the cash flow model to fund cash flow shortfalls (e.g., selling assets)?</li> <li>iv. Assess the insurer’s asset selling strategy.</li> </ul>	
<p><u>f. Review the AG-53 reporting in the AOMR regarding assumptions and sensitivity testing for high-yielding complex assets within the asset adequacy analysis, if within scope of AG-53. Determine whether concerns exist in meeting asset adequacy requirements, such as:</u></p> <ul style="list-style-type: none"> <li><u>i. the adequacy of assumptions utilized</u></li> <li><u>ii. the sensitivity testing and attributions analysis performed and its results</u></li> <li><u>ii. the determination of fair value of high-yielding assets originated by the company</u></li> </ul>	

----- **DETAIL ELIMINATED TO CONSERVE SPACE** -----**Discussion of Actuarial Opinion Assessment Procedures**

In most instances, proper review and analysis of the SAO will require a greater in-depth knowledge of actuarial science. In order to achieve this as a part of the financial review process, most opinions will be reviewed in detail by the Department's actuarial staff members. The review should encompass procedures discussed in the next section covering the Actuarial Opinion Assessment for the SAO. Although the analysis of the SAO, Actuarial Memorandum and RAAIS are often performed by the actuarial staff, analysts should have a basic understanding of interest rate risk and should consider reviewing the RAAIS and the New York 7, if available (see below for further discussion), or other stochastic testing results and discussing such results with the Department's actuary. When risks are identified in the RAAIS or actuarial memorandum, the analysts, examiners and regulatory actuaries should communicate with each other the risk identified so that an overall understanding of the current and prospective risks of the insurer are documented and considered in the overall prioritization and profile of the insurer.

However, if the Annual Financial Statement is received, a cursory review of the opinion should be performed to identify if any extraordinary item is detailed in the opinion. The primary goal of the Actuarial Opinion Assessment Procedures for the SAO is to determine if a SAO was to be filed and, if so, was it received and available for later review.

Every life insurer must file a SAO including an asset adequacy analysis unless granted exemption of such analysis based on doing business only in one state.

An actuarial memorandum, which supports the findings expressed in the SAO, is available upon request by the regulator. The insurer will also file with the commissioner by March 15 a confidential RAAIS.

If the insurer presently issues or has in-force policies that contain non-guaranteed elements, then a Non-guaranteed Elements Actuarial Opinion must also be filed. Other opinions may be required. For example, for business subject to an actuarial guideline—such as *Actuarial Guideline XXXV—The Application of the Commissioners Annuity Reserve Method to Equity Indexed Annuities* (AG 35) or XXXVI, which includes an opinion requirement, a compliant actuarial opinion must also be filed. The domestic insurance regulator should be familiar with all of the opinions each life insurer is required to submit. Reviewing the previous year checklist is useful, but the state insurance regulator should be aware of new policy forms issued during the year that may add additional opinion requirements.

**Asset Adequacy Analysis**

Asset adequacy analysis is a process the appointed actuary uses to ascertain that the assets supporting a block of liabilities, along with future premium payments and investment income, are adequate under moderately adverse conditions to pay future expenses and policy obligations. This analysis may include cash flow testing, gross premium valuations, demonstrations of extreme conservatism, risk theory techniques, or loss ratio methods. Prior to 2001, requirements similar to the AOMR specified seven scenarios for cash flow testing (commonly referred to as the New York 7). Amendments adopted in 2001 removed those required scenarios and allowed the appointed actuary to determine the scenarios to use for cash flow testing.

The asset adequacy analysis is testing the adequacy of the reserves on a block of business as of a valuation date, not the solvency of the company. Typically, cash flow testing includes assets approximately equal to the reserves and therefore does not include assets equal to the surplus. In addition, future new business is not included in the cash flow testing.

The asset adequacy analysis typically includes approximately 95% of the total of life insurance reserves, annuity reserves and reserves for deposit-type contracts. This 95% threshold is included in *procedure #4*, but it is a recommendation, and the standard of materiality may vary among actuaries and among state regulators.

**III.B.8.b.ii. Reserving Risk Repository – Life/A&H/Fraternal Analyst Reference Guide****Actuarial Guideline 53:**

Beginning with annual 2022, certain insurers will be required to document support for asset adequacy analysis for high-yielding complex assets pursuant to Actuarial Guideline 53 – Application of the Valuation Manual for Testing of Adequacy of Life Insurer Reserves (AG-53).

As noted in AG-53, "regulators have observed a lack of uniform practice in the implementation of asset adequacy analysis. The variety of practice in incorporating the risk of complex assets into testing does not provide regulators comfort as to reserve adequacy. Examples of complex assets are structured securities, including asset-backed securities and collateralized loan obligations, as well as assets originated by the company or an affiliated or contracted entity. An initial increase of this activity has been noted in support of general account annuity blocks; however, recent activity was noted in other life insurer blocks. AG-53 is intended to provide uniform guidance and clarification of requirements for the appropriate support of certain assumptions for asset adequacy analysis performed by life insurers."

This Guideline applies to a limited scope of life insurers, specifically those with:

- A. Over \$5 billion of general account actuarial reserves (from Exhibits 5, 6, 7, and 8 of the Annual Statement) and non-unitized separate account assets; or,
- B. Over \$100 million of general account actuarial reserves (from Exhibits 5, 6, 7, and 8 of the Annual Statement) and non-unitized separate account assets and over 5% of supporting assets (selected for asset adequacy analysis) in the category of Projected High Net Yield Assets, as defined in Section 3.F. of the AG-53.

The NAIC Life Actuarial (A) Task Force has developed a template for reporting of AG-53 documentation. The templates include reporting by asset classes, affiliated vs. non-affiliated, and initial assets vs. reinvestment assets. The template along with a narrative are submitted for the filing.<sup>1</sup>

The NAIC Valuation Analysis Working Group (VAWG) anticipates conducting reviews of AG-53 filings and can serve as a resource for state insurance departments for their own AG-53 reviews.

**Discussion of Actuarial Opinion Risk Assessment Procedures**

*The following Reference Guide text refers to Chapter III.B.8.b.i.- Statement of Actuarial Opinion Worksheet – Life/A&H/Fraternal Annual*

**RAAIS and Actuarial Memorandum**

**PROCEDURE #4** assists the analyst in reviewing the actuarial memorandum that supports the SAO. The actuarial memorandum is a comprehensive document that provides an understanding of the insurer's reserves, the assets available to support the reserves, and the projected impact on the insurer's financial condition of varying economic and interest rate projection scenarios. It is not automatically filed with the Annual Financial Statement but is provided to the regulator only upon request. The decision as to whether to request the actuarial memorandum is an important one. The actuarial memorandum should be requested for insurers with known financial problems, significant changes in product mix or investment strategy, or significant growth in a particular product line.

The RAAIS is filed with the Annual Financial Statement and is designed to assist the regulatory actuary in determining whether to request the actuarial memorandum. The RAAIS includes the eight data requests shown below. Note that some items, such as 1), 2) and 5) specifically refer to cash flow testing results.

<sup>1</sup> Given this is a new reporting requirement in 2022, additional analysis guidance in this area may be added to the Handbook in the future.

**III.B.8.b.ii. Reserving Risk Repository – Life/A&H/Fraternal Analyst Reference Guide**

- 1) The number of additional interest rate scenarios that were tested identifying separately the number of deterministic scenarios and stochastic scenarios. Also identify the number of such scenarios which produced ending negative surplus values on market value basis.
- 2) If sensitivity testing was performed, identify the assumptions tested and describe the variation in ending surplus values on a market value basis from the base case values.
- 3) If negative ending surplus results under certain tests in the aggregate, the amount of additional reserve which, if held, would eliminate the aggregate negative ending surplus values.
- 4) The extent to which the appointed actuary uses assumptions in the asset adequacy analysis which are materially different than the assumptions used in the previous asset adequacy analysis.
- 5) The amount of reserves and the identity of the product lines which have been subject to asset adequacy analysis in the prior opinion but were not subject to such analysis for the current opinion.
- 6) Comments should be provided on any interim results that may be of significant concern to the appointed actuary.
- 7) The methods used by the actuary to recognize the impact of reinsurance on the company's cash flows, including both assets and liabilities, under each of the scenarios tested.
- 8) Whether the actuary has verified that all options embedded in fixed income securities and equity-like features in any investments have been appropriately considered in the asset adequacy analysis.

While most states do not require the New York 7 actuarial interest rate scenario tests, states do require other stochastic scenario tests for life insurers and many life insurers, even though not required, still run the New York 7 interest rate scenario tests. The New York 7 interest rate scenario test which is an immediate decrease of 3% and then level would highlight the impact of prolonged low interest rates given the current interest rate environment. Also, the stochastically generated interest rate scenarios will also likely contain an interest rate scenario that represents a prolonged low interest rate environment.

The Department actuary and analyst should understand each scenario in the insurer's scenario testing and its limitations and assess the likelihood of each scenario in the current economic environment. For example, the New York 7 interest rate scenarios consist of the following scenarios:

- Level with no deviation.
- Uniformity increasing over 10 years at 0.5% per year and then level.
- Uniformity increasing at 1% per year over five years and then uniformly decreasing at 1% per year to the original level at the end of the 10 years and then level.
- An immediate increase of 3% and then level.
- Uniformly decreasing over 10 years at 0.5% per year and then level.
- Uniformly decreasing at 1% per year over five years and then uniformly increasing at 1% per year to the original level at the end of 10 years and then level.
- An immediate decrease of 3% and then level.

[Procedures 4.f. asks the analyst if an insurer that is within the scope of AG-53 has filed the required reporting within the AOMR. Further guidance on that reporting is provided below in procedure #5.](#)

**PROCEDURE #5** asks the analyst to document any concerns based on the review of the actuarial memorandum. Additional procedures the analyst may consider performing are provided if additional concerns exist based on the review of the RAAIS, the actuarial memorandum and the asset adequacy testing performed. The procedures should be used to help identify how the insurer will fund a negative cash flow. Procedures 5.a. through 5.d. are

**III.B.8.b.ii. Reserving Risk Repository – Life/A&H/Fraternal Analyst Reference Guide**

applicable to insurers utilizing the New York 7 actuarial interest rate scenario tests. Procedure 5.e. is applicable to other cash flow scenario testing. Explanations of negative cash flow provided by the appointed actuary should explain how the insurer will: 1) sell marketable assets and which type; or 2) borrow, with an explanation of any existing agreements to include security, duration and notice period required. If the appointed actuary wrote in his/her report that the insurer expects to sell assets, the modeling should be consistent for the sale of assets. Likewise, if the appointed actuary wrote that the insurer expects to borrow, then the modeling should be consistent with borrowing. If the insurer expects to borrow, the analyst should consider asking the insurer if a formal Lending Agreement is in place.

[Procedure 5.f. is applicable to AG-53 reporting on high-yield complex assets. Refer to the guidance above regarding the scope of which insurers are included in this reporting requirement. In line with the goals of AG-53 to provide uniform guidance and clarification of requirements for the appropriate support of certain assumptions for asset adequacy analysis performed by life insurers, the analyst or reviewing state actuary, should consider if the reporting identifies any concerns, including the following examples that may warrant further investigation or follow-up with the insurer.](#)

- [1. Reserve adequacy and claims-paying ability in moderately adverse conditions, including conditions negatively impacting cash flows from complex assets;](#)
- [2. Rationale supporting changes in assumptions, year-over-year;](#)
- [3. Expected gross returns and related risks \(including default rates\);](#)
- [4. Factors supporting margins on asset-related assumptions;](#)
- [5. That assumptions fit reasonably within the risk-return spectrum;](#)
- [6. The extent to which high-yielding assets are supporting major product categories;](#)
- [7. Sensitivity testing results regarding \*\*reinvested\*\* complex assets supporting life insurer business;](#)
- [8. Identifies expectations in practice regarding the valuation of complex assets within asset adequacy analysis; and,](#)
- [9. Investment fee income relationships with affiliated entities or entities close to the company.](#)

## **Actuarial Opinion and Asset Adequacy Analysis**

Due to the complexity in determining life reserves, insurers must rely on actuaries to assist with valuation of these reserves. Insurers are required to annually obtain an opinion regarding the reasonableness of the reserves by a qualified actuary who is appointed by the company. The actuarial opinion requirements are provided in VM-30 of the *Valuation Manual*. These requirements also include requirements for asset adequacy analysis. As a result of the asset adequacy analysis conducted by the appointed actuary, the actuary may conclude that the insurer's assets are not adequate to cover future liabilities as valued by the calculated reserves. When this occurs, reserves must be increased by the estimated deficiency resulting from asset adequacy testing. Additional procedures regarding the SAO are found in Section III.B.8.b.ii.

## **Quantitative and Qualitative Data and Procedures**

*The following Reference Guide text refers to Chapter III.B.8.b.i.- Statement of Actuarial Opinion Worksheet – Life/A&H/Fraternal Annual*

### **Adequacy of Life Reserves**

**PROCEDURE #5** assists the analyst in determining whether the insurer's underlying assets are adequate to support the future obligations of its life insurance policies. If the insurer filed an SAO based on an asset adequacy analysis,



**III.B.8.b.ii. Reserving Risk Repository – Life/A&H/Fraternal Analyst Reference Guide**

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then the SAO itself, and the supporting actuarial memorandum, if requested, can provide the analyst with comfort in this regard. If a SAO that does not include an asset adequacy analysis is filed, the analyst can review net interest spread ratios for insights regarding the relationship of investment income with tabular interest. Insurance Regulatory Information System (IRIS) ratio #11 is included in the procedures as a test of reserve consistency between the current year and the prior year.

The analyst may also consider performing a review of the actuarial memorandum, if available. This will provide the analyst with substantial analyses with regard to asset adequacy. If an actuarial memorandum is not available, the analyst should consider the need to have an independent asset adequacy analysis conducted. Additional procedures regarding the SAO are found in Section III.B.8.b.ii. [Additional guidance for new reporting requirements for AG-53 regarding high-yielding complex assets is found above.](#)

## I. Introduction F. Prioritization of Work

**Prioritization Framework**

The financial analysis process should be priority-based to ensure that insurers are reviewed promptly and at a level commensurate with the nature of their risks, complexity, and solvency position. To facilitate priority-based analysis, state insurance departments should utilize the following general framework to prioritize or classify insurance companies according to each insurer's relative stability and the perceived need for enhanced analysis:

- **Priority 1 (Troubled)** – The highest priority insurers from a solvency monitoring perspective, based on significant financial solvency risks. Insurers prioritized at this level are considered troubled and subject to comprehensive annual and quarterly analysis procedures, detailed considerations outlined with the *Troubled Insurance Company Handbook*, and a significantly elevated level of ongoing regulatory monitoring and oversight. Upon designating an insurer as a Priority 1, the domestic state should follow required procedures for troubled companies in communicating with other state insurance regulators. Insurers prioritized at this level would also be considered priority insurers for accreditation timeliness purposes and should generally be analyzed ahead of Priority 2, Priority 3, and Priority 4 insurers.
- **Priority 2 (Priority)** – High-priority insurers that are not yet considered troubled, but may become so if recent trends or unfavorable metrics are not addressed. High-priority insurers may also include those subject to heightened monitoring for reasons other than financial solvency risks, as determined by the department. Insurers prioritized at this level may be subject to full quarterly analysis procedures and are subject to comprehensive annual analysis and an elevated level of ongoing regulatory monitoring and oversight. Insurers prioritized at this level would also be considered priority insurers for accreditation timeliness purposes and should generally be analyzed ahead of Priority 3 and Priority 4 insurers.
- **Priority 3 (Non-Priority)** – Moderate priority insurers that indicate some need for additional monitoring. Insurers prioritized at this level should be subject to comprehensive annual analysis procedures, should generally be analyzed ahead of Priority 4 insurers, and may be subject to an enhanced level of ongoing regulatory monitoring and oversight.
- **Priority 4 (Non-Priority)** – Lower priority insurers that [are fundamentally sound, not overly complex and/or nationally significant<sup>1</sup>, and](#) do not currently indicate a need for additional monitoring [as no material regulatory concerns have been identified and their solvency risk is viewed as remote. Such insurers demonstrate a track record of stable operations, strong capitalization, and effective corporate governance. In addition, such insurers are not subject to significant business fluctuations or major changes to their core operations and strategies.](#) These insurers should be subject to a basic level of regulatory monitoring and oversight, including annual analysis.

The prioritization framework outlined above is primarily intended for use in communicating the prioritization of insurers on a uniform basis across state insurance departments. Therefore, state insurance regulators should present the prioritization of its insurers in accordance with the NAIC framework above when preparing and sharing information on insurers (i.e. Insurer Profile Summary) with other regulators. However, each state insurance department may adjust, enhance and/or develop an alternate prioritization framework and scale for its own internal purposes, as long as the framework outlined above is used in external communication with other regulators.

An insurer's priority level should be reconsidered as the result of each review performed to determine whether the designation is still appropriate and rationale for changes in priority ratings should be clearly documented within analysis files. However, changes in priority levels should only be made after approval by senior insurance department personnel.

<sup>1</sup> [The use of the term "nationally significant" is not intended to reference the nationally significant monitoring criteria utilized by the NAIC's Financial Analysis \(E\) Working Group. Regulators may use judgment in evaluating the significance of an individual insurer to the national insurance market to determine which domestic insurers qualify for low priority treatment.](#)

## I. Introduction F. Prioritization of Work

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### Prioritization Factors

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Although prioritization is, to a large extent, subjective, a state insurance department should establish guidelines to assist in the consistent assignment of priority designations to its insurers. These guidelines may consist of both quantitative and qualitative considerations. Factors that may be given consideration in the state insurance department's prioritization system include, but are not limited to, the following:

- Results of the most recently completed risk-focused analysis, including branded risk exposures and assessments (based on analysis of the Annual Financial Statement, Quarterly Financial Statements, supplemental filings, holding company analysis and any other documents reviewed by the analyst)
- Level of capitalization and identification of unfavorable trends
- Negative trends in profitability and/or cash flow from operations
- Insurance Regulatory Information System (IRIS) ratio results
- Annual and Quarterly Scoring System ratio results
- Changes in the insurer's officers or board of directors
- Changes in the insurer's business strategy or operations
- Summary of results of the automated quantitative data and benchmarks in the *Financial Analysis Handbook* risk repositories
- Issues/questions identified by the NAIC Financial Analysis (E) Working Group
- Examination findings and recommendations (financial condition and market conduct)
- Information from other divisions or areas within the insurance department
- Independent organization ratings and reports
- Information obtained from other regulatory agencies (including federal)
- RBC and RBC Trend Test results
- Impact on the public of an insurer's insolvency (policyholders and jurisdictions potentially affected)
- Structure and complexity of the insurer or insurance group
- Current or pending regulatory actions
- Standing of insurer in relation to statutes that impact financial solvency (e.g., hazardous financial condition)

As a general rule financial statements and other materials pertaining to those insurers that are deemed higher in priority should be reviewed before those materials pertaining to lower priority insurers. In addition, the review of higher priority insurers should typically be more in-depth than the review of lower priority insurers.

## III.A.3. Risk Assessment (All Statement Types) – Quarterly Quantitative Assessment of Non-Troubled Insurers

**Quantitative Risk Assessment**

- A. Non-troubled insurers will receive the following automated review each quarter. Troubled insurers will receive a full risk assessment analysis each quarter.

Each quarter, non-troubled insurers should be assessed based on the results of the following automated system. Based on the results of the automated system, you may need to proceed with a full risk assessment analysis. **Also consider any other information that may not be reflected in the quarterly statement but may be known or noted in the analysis file or Insurer Profile Summary (IPS), which could impact the company on a prospective basis prior to relying solely on an automated review.**

- B. If any of the following criteria is met, the insurer may be assigned a full quarterly risk assessment analysis:
1. The insurer is a troubled insurer
  2. Prior year risk-based capital (RBC) is less than 250% (*excluding title insurers*) (ST)
  3. Prior year triggered the RBC Trend Test (*excluding title insurers*) (ST)
  4. Scoring System result greater than or equal to (excluding title insurers):
    - 450 for property/casualty (P/C) insurers
    - ~~350~~ 250 for life ~~or fraternal~~ insurers
    - ~~300~~ 200 for accidental and health (A&H) insurers
    - 325 for health entities
- C. Based on the results of the automated system calculations, a full quarterly risk assessment analysis may be completed if the insurer has the following number of “yes” responses from the automated calculations:
1. Four or more for P/C insurers, title insurers and health entities or
  2. Three or more for life/A&H/fraternal insurers

Special Notes: Any automated results in D where the denominator is 0 return a “yes” response.

A default “no” response will be returned for insurers with no net retention for automated results #8 and #9.

For companies that have not filed a prior year-end or quarterly statement (e.g., either a new start-up insurer or exempt from filing), all responses in section D will default to a “yes.” In this scenario, it is recommended the analyst perform a full quarterly risk assessment analysis.

- D. Automated system calculations:
1. Are unassigned funds negative? (ST)
  2. Has surplus/capital and surplus (based on business type) increased  $\geq$  12.5% (for first quarter), 25% (for second quarter), or 37.5% (for third quarter)? (ST)
  3. Has surplus/capital and surplus (based on business type) decreased  $\geq$  5% (for first quarter), 10% (for second quarter), or 15% (for third quarter)? (ST)
  4. Has any individual asset category that is greater than 5% of surplus/capital and surplus (based on business type) changed by more than +/- 10% from the prior year-end? (CR, MK, LQ)

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