NAIC National Association of Insurance Commissioners

FINANCIAL EXAMINERS HANDBOOK (E) TECHNICAL GROUP
Virtual Meeting
Thursday, November 12, 2020
3:00 p.m. ET/ 2:00 p.m. CT

ROLL CALL

Susan Bernard, Chair	California	Justin Schrader	Nebraska
John Litweiler, Vice Chair	Wisconsin	Joel Bengo/Peter Rao	Nevada
Richard Ford	Alabama	Colin Wilkins	New Hampshire
William Arfanis	Connecticut	John Sirovetz	New Jersey
N. Kevin Brown	District of Columbia	Tracy Snow	Ohio
Cindy Andersen	Illinois	Eli Snowbarger	Oklahoma
Grace Kelly	Minnesota	Matt Milford	Pennsylvania
Shannon Schmoeger	Missouri	John Jacobson	Washington
NAIC Support Staff: Bailey Henning			

AGENDA

1. Consider Adoption of Financial Examiners Handbook (E) Technical Group October 5, 2020 Meeting Minutes—*Susan Bernard (CA)* — Attachment One

2. Consider Adoption of Handbook Guidance—*Susan Bernard (CA)*
   - Revisions to Incorporate Consideration of Reciprocal Jurisdiction Reinsurers — Attachment Two
   - Revisions to Incorporate Various Reserve-Related Guidance — Attachment Three
   - Comment Letters — Attachment Four

3. Consider Adoption of ORSA Revisions—*Susan Bernard (CA)* — Attachment Five

4. Discuss Any Other Matters Brought Before the Technical Group—*Susan Bernard (CA)*

5. Adjournment

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Draft: 10/14/20

Financial Examiners Handbook (E) Technical Group
Webex Meeting
October 5, 2020

The Financial Examiners Handbook (E) Technical Group of the Examination Oversight (E) Task Force met via Webex Oct. 5, 2020. The following Technical Group members participated: Susan Bernard, Chair (CA); John Litweiler, Vice Chair (WI); Richard Ford (AL); William Arfanis (CT); N. Kevin Brown (DC); Levi Nwasoria (MO); Justin Schrader (NE); Colin Wilkins (NH); John Sirovetz (NJ); Peter Rao (NV); Tracy Snow (OH); Eli Snowbarger (OK); John Jacobson (WA).

1. Exposed Handbook Guidance

a. Reinsurance Revisions

Ms. Bernard said the first set of revisions to consider for exposure relate to the reinsurance chapter in the *Financial Condition Examiners Handbook* (Handbook). The proposed revisions are intended to incorporate the concepts from the recently updated *Credit for Reinsurance Model Law* (#785) and *Credit for Reinsurance Model Regulation* (#786), which extend the ability for U.S. ceding insurers to obtain credit for reinsurance ceded to reinsurers from Reciprocal Jurisdictions with no collateral requirements. The proposed revisions add a definition for "reciprocal jurisdiction reinsurers" and describe the requirements for obtaining a credit for reinsurance in this circumstance.

b. Reserves Revisions

Ms. Bernard said the next set of revisions incorporate updates to various sections of Handbook guidance related to reserves and originated from several different workstreams. Bailey Henning (NAIC) began by providing an overview of the three workstreams and related revisions. She said the first workstream relates to the Technical Group's annual maintenance project to update examination repositories. The reserves examination repository updates began during 2019 and carried over into 2020. These updates were developed by a group of volunteers from the Technical Group, as well as through input received from members of the Actuarial Opinion (C) Working Group, the Life Actuarial (A) Task Force, and the Health Actuarial (B) Task Force. As part of this workstream, updates were developed for each of the three reserve-related examination repositories, as well as narrative guidance in Section 1, Part 6 of the Handbook related to life insurance reserves reviews. Ms. Henning said the proposed revisions to the examination repositories are intended to add clarity to select risk statements, possible controls, and possible test procedures, as appropriate, as well as add new risks and/or remove risks that are no longer deemed relevant. The proposed revisions to Section 1, Part 6 narrative guidance are intended to add references to the relevant sections of the NAIC *Valuation Manual*.

The second workstream, which resulted in proposed revisions, relates to updates to incorporate the consideration of long-term care insurance (LTCI). Ms. Henning stated that the Long-Term Care Insurance (EX) Task Force recently developed guidance for state insurance regulators to consider in monitoring insurers with this line of business, and the proposed updates to the Handbook build off of that guidance. Revisions related to this workstream include: 1) the addition of narrative background guidance added to Section 1, Part 6 of the Handbook; 2) a new risk and related procedures added to the reserves/claims handling – life examination repository related to assumptions utilized when calculating reserves for LTCI policies; 3) a new risk and related procedures added to the underwriting examination repository related to establishing appropriate rates for LTCI policies; and 4) additional questions added to the Chief Actuary interview template within Exhibit Y – Interviews.

The third workstream, which resulted in proposed revisions, relates to feedback received from the Casualty Actuarial and Statistical (C) Task Force and the Actuarial Opinion (C) Task Force. Revisions related to this workstream include: 1) revisions within the reserves/claims handling – property and casualty examination repository to add clarity to certain risk statements and procedures; and 2) updates to Exhibit M – Corporate Governance to add considerations when assessing the management overseeing the actuarial function.

The Technical Group agreed to expose the proposed revisions for a 30-day public comment period ending Nov. 4.

2. Discussed Other Matters

Ms. Bernard said the Risk-Focused Surveillance (E) Working Group and the Own Risk and Solvency Assessment (ORSA)

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Implementation (E) Subgroup recently exposed proposed revisions to ORSA guidance within the *Financial Analysis Handbook* and the *Financial Condition Examiners Handbook*. She said that the respective Handbook groups do not expect to conduct a separate exposure period; rather, the Handbook groups will receive a final recommendation from the Risk-Focused Surveillance (E) Working Group and the ORSA Implementation (E) Subgroup to consider for adoption once that work has been finalized. She said these groups expect to conduct a joint conference call in October to discuss comment letters received during the public exposure period; and Technical Group members, interested state insurance regulators, and interested parties are encouraged to participate.

Having no further business, the Financial Examiners Handbook (E) Technical Group adjourned.

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V. REINSURANCE REVIEW

This section of the Handbook addresses the following subjects:

A. Evaluation of Risk Transfer
B. Credit for Reinsurance Guidelines
C. Reinsurance Balances Recoverable
D. Termination of Reinsurance Agreements

--Detail Eliminated to Conserve Space---

B. Credit for Reinsurance Guidelines

Note: In ~~late 2011~~2019, the NAIC adopted revisions to the Credit for Reinsurance Model Law (#785) and the Credit for Reinsurance Model Regulation (#786). These revisions serve to extend the ability for U.S. ceding insurers to obtain credit for reinsurance for reinsurance ceded to reinsurers from Reciprocal Jurisdictions with no collateral requirements. ~~reduce reinsurance collateral requirements for reinsurers that have been "certified" by the domestic state of the ceding insurer. A number of states have adopted these revisions within their respective credit for reinsurance statute and/or regulation, and several additional states are considering similar proposals.~~ If your state has adopted these revisions, you should refer to the model or your state's updated statute for the most current guidance regarding credit for reinsurance as it pertains to "Reciprocal Jurisdictions".
~~"certified reinsurers."~~

Subject to the laws of the various states, credit for reinsurance may be allowed to the ceding company when the reinsurance contract includes a proper insolvency clause and the specific criteria for the appropriate category have been adequately met:

1. Reinsurer is Licensed in the Ceding Company's Domiciliary State

   Reinsurers who meet this classification must have obtained their licensure status at the time the statutory financial statement credit for reinsurance is claimed or when financial statements indicating the credit have been filed by the ceding company. The reinsurer then must continue to maintain compliance with the licensure status at all times after the credit has been taken. The licensure requirement is considered to be perpetual and not periodic; therefore, appropriate information is required to be included in the company's financial statements when reinsurers do not comply with the requirements.

2. Assuming Insurer Has Obtained Reinsurer Accreditation

   An assuming insurer must have obtained reinsurance accreditation in the domiciliary state of the ceding company at the time the financial statement credit is claimed in order for the domestic insurer to receive a credit for reinsurance. In order to obtain the status of an accredited reinsurer, the assuming company must file a Form AR-1 (Certificate of Assuming Insurer), which grants specific authority to the ceding company's domiciliary insurance commissioner (Part Two of Exhibit N – Reinsurance Review), as well as documentation of licensure to transact insurance or reinsurance and annual statements with the domiciliary insurance commissioner. In addition, the assuming insurer must demonstrate to the satisfaction of the commissioner that it has adequate financial capacity to meet its reinsurance obligations and is otherwise qualified to assume reinsurance from domestic insurers. An assuming insurer is deemed to meet this requirement as of the time of its application if it maintains a surplus as regards policyholders in an amount not less than $20 million and its accreditation has not been denied by the commissioner within ninety (90) days after submission of its application. The insurance commissioner is entitled to suspend or revoke reinsurer accreditation if the above conditions are not preserved.

3. Reinsurer is Domiciled in Another State

   The reinsurer must be domiciled (and licensed) in a substantially similar state that has adopted the NAIC *Credit for Reinsurance Model Law* (#785) or substantially similar law and, therefore, is subject to that state's credit for

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reinsurance standards at the time the financial statement credit for reinsurance is claimed. The reinsurer must also maintain a surplus of at least $20 million and file a Form AR-1 with the insurance commissioner.

4. Reinsurer Maintains Trust Funds

A credit for reinsurance ceded by domestic insurers is available to assuming insurers that maintain trust funds for a requisite amount in a qualified U.S. financial institution (actual amount is determined by the classification of the assuming insurer). The assuming insurer is required to annually report to the insurance commissioner for determination of the sufficiency of the trust fund. The classifications of assuming insurers are as follows:

a. Single Assuming Insurer – Trust funds must equal or exceed the assuming insurer's liabilities attributable to ceded reinsurance by U.S. domiciled insurers. In addition, the assuming insurer shall maintain trusteed surplus of at least $20 million. If the assuming insurer has permanently discontinued underwriting new business secured by the trust for at least three full years, the commissioner may authorize a reduced required trusteed surplus to an amount no lower than thirty percent (30%) of the assuming insurer's liabilities attributable to reinsurance ceded by the U.S. ceding insurers covered by the trust.

b. Incorporated and Unincorporated Group Underwriters – For reinsurance ceded under reinsurance agreements dated after January 1, 1992, trust funds must equal or exceed the group's liabilities for business ceded by U.S. domiciled ceding insurers. For reinsurance agreements dated before December 31, 1992, trust funds must at least equal the insurance and reinsurance liabilities attributable to business written in the United States. In addition to these trusts, the underwriters must maintain $100 million in surplus for the benefit of U.S.-domiciled ceding insurers. The incorporated members of the group are prohibited from engaging in auxiliary business, other than underwriting as a member of the group, and must be subject to the same regulation and control of the group as the unincorporated members. The group is also required to annually file either a certification of solvency for each underwriter member or independently prepared financial statements for each underwriter to the insurance commissioner.

A credit for reinsurance will not be granted for reinsurers who maintain trust funds, unless the insurance commissioner of the state where the trust is domiciled has approved the form of the trust. An insurance commissioner from another state may approve the trust if the commissioner has accepted responsibility for the regulatory oversight of the trust. The form of the trust is required to be filed with the insurance commissioner in every state the ceding insurer beneficiaries of the trust are domiciled.

5. Certified Reinsurers

An assuming reinsurer must have obtained certification by the commissioner of the domiciliary state of the ceding company at the time the financial statement credit is claimed in order for the domestic insurer to receive a credit for reinsurance. In order to obtain the status of certified reinsurer, the assuming reinsurer must be domiciled and licensed to transact insurance or reinsurance in a qualified jurisdiction, as determined by the commissioner. The assuming reinsurer must also maintain a surplus level of no less than $250 million and maintain financial strength ratings from two or more acceptable rating agencies.

The allowable credit for reinsurance ceded by a domestic insurer to an assuming reinsurer that has been certified as a reinsurer in the domestic insurer's state is based upon the security held by, or on behalf of, the ceding insurer (e.g., amount of funds held, letter of credit, etc.). The amount of security required to be held (e.g., level of collateral required) corresponds to the rating assigned to the certified reinsurer by the commissioner, which is based on various factors including, but not limited to, the certified reinsurer's business practices, regulatory actions against the certified reinsurer, financial strength and the report of the independent auditor.

6. Reciprocal Jurisdiction Reinsurers

Credit for reinsurance ceded by domestic insurers is available to an assuming insurer that is licensed to write reinusrance by, and has its head office or is domiciled in, a Reciprocal Jurisdiction. For reinsurance with

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Reciprocal Jurisdiction Reinsurers there are no collateral requirements if the reinsurers have met the minimum standards in the *Credit for Reinsurance Model Law* (#785) and the *Credit for Reinsurance Model Regulation* (#786). In order to be designiated a Reciprocal Jurisdiction by the Commissioner, a jurisdiction must meet one of the following requirements: 1) a non-U.S. jurisdiction that is subject to an in-force covered agreement with the United States, 2) meets the requirements for accreditation under the NAIC financial standards and accreditation program, or 3) a jurisdiction that has been designated by the commissioner as a qualified jurisdiction and which meets any additional requirements specified by the regulation. ~~qualified jurisdiction, as determined by the commissioner.~~ The assuming insurer must also maintain a surplus level of no less than $250 million and a minimum RBC ratio 300%, or amounts established by Model #785 and Model #786.

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VI. LIFE INSURANCE RESERVE REVIEW

This section covers procedures and considerations that are important when conducting financial condition examinations of life insurance reserves. The discussion here is divided as follows:

A. Life Insurance Reserve Overview
B. Formula Based Valuation Methodology
C. Principle-Based Valuation Methodology
D. Actuarial Opinion and Asset Adequacy Analysis
E. Actuarial Oversight and Internal Controls
~~E.~~ Long Term Care Insurance (LTCI) Reserves Overview

A. Life Insurance Reserve Overview

Life insurance reserves represent the liability established by the insurance company to pay future policy benefits such as death benefits upon the death of the insured, endowment benefits upon the maturity of a life insurance policy and cash surrender benefits upon the surrender of the life insurance policy. Historically, the company liability to pay future policy benefits has been determined by calculating a reserve based on a formula valuation methodology as described below. Life insurance products have evolved over time and today, such products may be quite complex offering multiple benefits and/or options to the policyowner or the insured or both the policyowner and the insured within a single contract such as death benefits, accelerated death benefits, secondary guarantees such as no lapse guarantees, policy loans, retirement income benefits such as guaranteed lifetime income benefits and long term care benefits. The value of some of these complex benefits depends upon the current and future market value of the underlying assets. Regulators have found it increasingly difficult to define or modify a formula based valuation methodology to value all the options and/or benefits in a single contract. This complexity of current insurance products along with the fact that the value of certain benefits depends upon the current and future market value of underlying assets has led to the development of a principle-based valuation methodology which incorporates the value of both asset and liability cash flows. The principle-based valuation methodology is described below.

In order to implement the principle-based valuation methodology, amendments to the Standard Valuation Law were adopted in 2009 and a Valuation Manual was developed. The Valuation Manual which is referred to in the amended Standard Valuation Law provides reserve requirements for life, health, and annuity products issued on and after the manual's operative date. Requirements include all of the details of the methodology for determining a principle-based reserve as well as any changes to the formula based valuation methodology that occurs on and after the operative date of the Valuation Manual. The operative date of the Valuation Manual is January 1, 2017. Unless a change in the Valuation Manual specifies a later effective date, changes to the Valuation Manual shall be effective January 1 following the date when the change to the Valuation Manual has been adopted by the NAIC by an affirmative vote of at least three-fourths (3/4) of the members of the NAIC voting but not less than a majority of the total membership and such members voting in the affirmative represent jurisdictions totaling greater than 75% of the direct premiums written as reported in the most recent life, accident and health annual statements, health annual statements, or fraternal annual statements. No state legislative adoption is needed to effect changes to the Valuation Manual.

The Valuation Manual defines the insurance contracts that are subject to a principle-based valuation (Section II). Unless otherwise specified in Section II of the Valuation Manual, the principle-based valuation methodology will apply to life insurance contracts issued on or after the operative date of the Valuation Manual, however a company may elect to defer the implementation of the principle-based valuation methodology to life insurance contracts issued during the first 3 years following the operative date of the Valuation Manual. Since elements of the Actuarial Method in AG 48 are based on VM-20, a company may "partially implement" the Valuation Manual during the deferral period even though for new business the company otherwise defers implementation.

Actuarial Guideline 48 (AG 48) was adopted December 16, 2014 with an effective date of January 1, 2015 and refers to the Actuarial Method which is also a principle based methodology that companies may use in evaluating level of primary assets held by captive insurers in support of reserves. If regulators determine that the insurer under examination has business subject to AG 48, they may also consider the involvement of a credentialed actuary and may apply the concepts

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discussed in evaluating PBR. Similar considerations apply if a state has adopted Model Regulation 787 which supersedes AG 48 and applies a principle-based methodology to those policies that AG 48 would have otherwise applied to.

A Valuation Analysis Working Group (VAWG) consisting of regulators with expertise in actuarial, financial analysis and examination experience reports to the Financial Condition (E) Committee and supports the states in the review of Principle-Based Reserves (PBR) to ensure consistent implementation and application of the methodology. VAWG will also suggest necessary changes to the Valuation Manual to enhance clarification and interpretation of application of the principle-based valuation methodology.

In addition, NAIC actuarial staff is available to provide expertise in modeling insurance cash flows to assist individual states and VAWG in conducting analyses and examinations to verify the PBR and exclusion test calculations performed by the company.

Due to the complexities of life insurance products, the involvement of a credentialed actuary is required on all examinations of life and health insurers with a substantial amount of interest-sensitive business or with a substantial amount of PBR calculations or subject to PBR exclusion tests See Section 1, Part III, E. Using the Work of a Specialist for further reference.

B. Formula Based Valuation Methodology

Theoretically, the formula based reserves represent the present value of future guaranteed benefits reduced by the present value of expected future net premiums. The insurance policy is a unilateral contract whereby the insured can cancel the agreement to pay premiums at any time. However, the insurer is "locked in" regardless of future experience and cannot forfeit on its guarantees as long as the premiums are paid. Life reserves are required in order to ensure that commitments made to policyholders and their beneficiaries will be met, even though the obligations may not be due for many years. Since the primary purpose of life reserves is to pay claims when they become due, life reserves must be adequate and the funds must be safely invested.

The Valuation Manual prescribes the minimum standards to be used in determining the formula based reserves as applicable in addition to principle-based reserves as discussed elsewhere in this document. Currently for most formula based reserves, the manual refers to requirements in the NAIC *Accounting Practices and Procedures Manual* (AP&P Manual). Insurers may establish life reserves, which equal or exceed these minimum standards. These minimum life reserve standards specify a: 1) valuation mortality table; 2) maximum valuation rate of interest; and 3) valuation method. The valuation method used to define minimum life reserves for statutory accounting purposes is referred to as the Commissioners Reserve Valuation Method (CRVM). The mortality assumptions are higher than what the insurer can expect to realize from medically underwritten insurance policies. The interest rate assumptions are intended to be significantly lower than current money and capital market yields. Thus, the life reserves developed are generally conservative.

There are three general valuation methods under a formula based valuation methodology used to value life reserves. The net level premium method does not provide for a first-year acquisition cost allowance in determining life reserves. Therefore, this method results in the most conservative, or highest, life reserve valuation of the three methods. The full preliminary term method does provide a first-year expense allowance and then assumes that the remaining premium stream is used to cover policy benefits. The Commissioners Reserve Valuation Method (CRVM) is a form of the full preliminary method. This method allows for a lower life reserve valuation than the net level premium method in the earlier years of the policy term. The modified preliminary term method is a variation of the two methods described above and results in a reserve valuation between the net level premium and preliminary term methods.

As described below, the type of life insurance policy dictates the amount of the life reserve that must be established and the duration for maintaining the reserve. In addition, special situations arise which require unique reserving techniques. The following summarizes the major types of life insurance policies, and the related reserving implications under a formula based valuation methodology:

1. Ordinary Life Reserves

   Under a whole life plan of insurance, the insurer is obligated to maintain a reserve until the death of the insured. Term

life insurance provides coverage only for the period that is specified in the policy. Under a term insurance plan, the insurer must maintain a reserve, which reduces to zero upon expiration of the term period. Similar to term insurance, endowment life insurance provides coverage for a period specified in the policies. Unlike term insurance, the proceeds of endowment insurance are payable if the insured lives to the end of the period. Policies, which permit flexible premium payments, are referred to as "universal life" policies and those with fixed premiums are referred to as "interest sensitive" policies. Universal life policies are accumulation type policies where the current account value is determined based upon the accumulation of premiums less mortality charges and expense charges, plus a current interest rate credit. The account value less surrender charges is the cash value. Because of the unique features of universal life and interest sensitive types of policies, unique reserving requirements are specified for them in Appendix A-585, Universal Life Insurance, of the AP&P Manual. The minimum standard for universal life reserves consider guarantees within the policy at the time of issue, present value of future guaranteed benefits, account value and cash value.

2. Group Life Reserves

   Most group life insurance is monthly renewable term insurance. For these policies, gross premiums are typically recalculated periodically, most often annually, using the age and sex census of the group along with experience adjustments. Therefore, the reserve is usually calculated as the unearned premiums or a percentage thereof to estimate the claim exposure. However, some group life insurance policies provide permanent or longer term benefits analogous to individual coverages. In these cases, the reserving methods are similar to those employed for individual insurance, using appropriate mortality tables. Appendix A-820 does not specify a mortality table for group life insurance but leaves that to the discretion and approval of the domiciliary state.

3. Industrial Life Reserves

   Industrial life insurance is unique in that it involves higher unit premiums, smaller face amount policies and higher mortality expectations. The minimum standards for reserves are the same as the traditional life insurance except that a unique mortality table is used.

4. Credit Life Reserves

   Credit life insurance policies are designed to discharge a debt upon the debtor's death. They are usually funded as a single premium. Reserve requirements vary among the states. Key considerations include claims reserves and policy reserves based on a state-specified combination of mortality reserves, unearned premium reserves, and potential refunds. Credit Life and Disability Reserves are addressed in Valuation Manual (VM)-26.

5. Life Reserves Relating to Riders

   Life insurance policies frequently include riders for additional benefits such as accidental death and disability and waiver of premium upon disability. The minimum valuation standards for reserves are the same as for the base life insurance except that specialized mortality and disability tables are used and the net level premium valuation method is required. Detailed guidance for requirements for life reserves relating to riders is found in Section II of the Valuation Manual.

6. Miscellaneous Life Reserves

   There are various other special situations involving life reserves. First, a deficiency reserve may be required in situations where the actual policy gross premium is less than the valuation net level premium. This situation occurs when pricing assumptions are used that are different from the minimum reserve valuation standards. This does not necessarily indicate that the policy is being sold at a loss by the insurer, but rather is a reflection of the highly conservative nature of the minimum reserve valuation standards. Second, there may be unusual situations where the cash surrender value of a life insurance policy is greater than the minimum reserve standard. In these situations, life reserves must be increased by the amount of this excess.

7. Minimum Aggregate Reserves

   In the aggregate, policy reserves for all life insurance policies valued under a formula based valuation methodology that are reported in the statutory financial statements must equal or exceed reserves calculated by using the assumption and methods that produce the minimum formula standard valuation.

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C. Principle-Based Valuation Methodology

In general, under a principle-based valuation methodology, all of the liability cash flows emanating from the contract benefits provided in the product are determined for each period and compared with all of the asset cash flows for each period determined from the assets the insurance company has purchased or plans to purchase or sell to fund the liability cash flows. The resulting differences between the asset and liability cash flows for each period are valued under a range of likely or plausible economic scenarios.

The principle-based valuation methodology developed for life insurance contracts defines 3 components of a principle-based reserve: 1) a net premium reserve (NPR); 2) a deterministic reserve (DR); and 3) a stochastic reserve (SR). The level of risk embedded in a life insurance contract will determine whether the principle-based reserve will consist of all 3 reserve components (NPR, DR, SR), or only 2 reserve components (NPR, DR); or only 1 reserve component (NPR). The principle-based valuation methodology defines a stochastic exclusion test and a deterministic exclusion test each of which are designed to measure the level of risk embedded in a life insurance contract. Life insurance contracts that pass an exclusion test are then exempt from the calculation of the associated principle-based reserve component. For example, all life insurance contracts that pass the stochastic exclusion test but fail the deterministic exclusion test, must calculate the NPR and DR components. Life insurance contracts that pass both the stochastic and deterministic exclusion tests need only calculate the NPR component. For groups of policies other than variable life or universal life with a secondary guarantee, a company may provide a certification by a qualified actuary that the group of policies is not subject to material interest rate risk or asset return volatility risk in lieu of performing the stochastic exclusion ratio test or stochastic exclusion demonstration test. In addition, a company is not required to compute stochastic reserves and deterministic reserves on any of its ordinary life policies if it meets the conditions of Section ~~2~~II of the Valuation Manual~~VM-20~~ under the requirements referred to as the~~ "companywide exemption"~~ "Life PBR Exemption". If the domestic commissioner does not reject a company's application for the Life PBR Exemption~~companywide exemption~~ pursuant to Section II of the Valuation Manual~~6 of VM-20~~, then the company will compute reserves for its ordinary life policies per applicable~~the~~ requirements provided in VM-A and VM-C of the Valuation Manual. Note the domestic commissioner may apply the PBR requirements of VM-20 to only a portion of the ordinary life policies that are requested for exemption under the Life PBR Exemption.

The stochastic reserve under a principle-based valuation methodology is determined as a function of the discounted value of the differences between the asset and liability cash flows for each period over the range of economic scenarios. Economic scenarios may consist of interest rates or market returns or both depending on the nature of the asset and liability cash flows. A single economic scenario represents multiple consecutive periods (such as 30 or 40 years) of movements in the underlying interest rate or market rate returns. The length of the scenario period is determined by the length of the liabilities being valued. The economic scenarios are stochastically (randomly) generated using a prescribed Economic Scenario Generator (ESG). The prescribed ESG can be found on the Society of Actuaries website. The objective is to determine if there is a reasonable likelihood that assets are insufficient to cover the obligations of the company, and by what amount they may be insufficient. Under economic scenarios where assets are insufficient, the principle-based methodology determines all the amounts of the insufficiencies and discounts them back to the valuation date. The largest discounted value is known as the Greatest Present Value of Accumulated Deficiencies, or "GPVAD", for that scenario. The stochastic reserves may be set at a CTE(70) level (conditional tail expectation at the 70% level). The function CTE(70) means the average of the 30% (100%-70%) worst (largest) GPVADs. So for example if a company randomly generates 1,000 economic scenarios, it would then determine the largest accumulated amount of deficiency for each of the 1,000 scenarios. The CTE(70) stochastic reserve level would be determined by taking the average of the 300 [1,000 x (100% - 70%)] worst GPVADs out of the 1,000 scenarios.

Note that some states incorporated a "companywide exemption" in the Standard Valuation Law that may override Section 2 of VM-20. In such cases the state's Standard Valuation Law will determine whether a company is not subject to computing the stochastic and deterministic reserves. Note also, the commissioner may exempt specific product forms or product lines of a domestic company that is licensed and doing business only in a single state as defined in Section 15 of the amended NAIC Model Standard Valuation Law.

As part of the calculation process, the principle-based valuation methodology allows companies to aggregate or group

policies with similar risk characteristics. For example, all term policies that provide only a death benefit and do not provide any cash surrender values may be grouped together by underwriting class. The exclusion tests are then applied on a group or aggregated basis and not a contract by contract basis. Also, the DR and the SR are calculated on the aggregated or group basis. However, the SR must be performed using aggregation subgroups that do not intermingle multiple product groups (Term, ULSG, Other). The NPR component is a fully prescribed formula based reserve and must be applied on a contract by contract basis.

The annual statement blank contains a VM-20 Supplement. This supplement breaks out the principle-based reserve into its various components of NPR, DR and SR. Regulators may request the assistance of NAIC modeling staff and or VAWG in verifying exclusion testing as well as various components of the principle-based reserve on a smaller sample set of company contracts.

D. 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.

E. Actuarial Oversight and Internal Controls

Appendix G of the Valuation Manual provides guidance that while not expanding the existing legal duties of a company's board of directors, senior management, and appointed actuary and/or qualified actuaries, provides guidance that focuses on their roles in the context of principle-based reserves. Some of the duties and expectations for the board of directors and senior management are provided below. If an actuarial specialist is involved in an examination, Appendix G includes additional requirements that should be considered during the review of the company's actuarial oversight and associated internal controls.

1. The Board of Directors should:

   a. Receive and reviews reports, including the certification of the effectiveness of internal controls with respect to the principle-based calculation, as provided in Section 12.B.(2) of the Standard Valuation Law.
   b. Understand the process undertaken by senior management to correct any material weaknesses in the internal controls with respect to a principle-based reserve valuation, if any is identified.
   c. Understand the infrastructure (consisting of policies, procedures, controls and resources) in place to implement and oversee principle-based reserve processes.
   d. Ensure the proper documentation of review and action undertaken by the board relating to the principle-based reserving function in the minutes of all of the board meetings where such function is discussed.

2. Senior Management should:

   a. Ensure that an adequate infrastructure (consisting of the risk tolerances, policies, procedures, controls, risk management strategies and resources) has been established to implement the principle-based reserving function.
   b. Review for reasonableness the principle-based reserving elements (consisting of the assumptions, methods and models used to determine principle-based reserves of the insurer company or group of insurance companies) that have been put in place.
   c. Review the principle-based reserving results for consistency with established risk tolerances of the insurance company or group of insurance companies in relation to the risks of the products of the insurance company or group of insurance companies offers, the various strategies used to mitigate such risks, and its emerging experience, in order to understand the general level of conservatism incorporated into principle-based reserves.

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d. Review and address any significant and/or unusual findings in light of the results of the principle-based reserve valuation processes and applicable sensitivity tests of the insurance company or group of insurance companies.

As examiners perform both the Corporate Governance assessment and the examination interviews, the topics above should be considered to ensure that the companies with transactions governed by PBR are adequately implementing the relevant portions of the Valuation Manual.

Additional procedures regarding the examiners' assessment of the insurer's PBR related risks, controls, and possible test procedures can be located in Section 3 Reserves/Claims Handling (Life) repository.

F. Long Term Care Insurance (LTCI) Reserves Overview

Per NAIC *Long-term Care Insurance Model Act* (#640), "Long-term care insurance" means any insurance policy or rider advertised, marketed, offered or designed to provide coverage for not less than twelve (12) consecutive months for each covered person on an expense incurred, indemnity, prepaid or other basis; for one or more necessary or medically necessary diagnostic, preventive, therapeutic, rehabilitative, maintenance or personal care services, provided in a setting other than an acute care unit of a hospital. ~~Long-Term Care Insurance (LTCI) provides coverage for the cost of long-term care services in the event that an insured becomes unable to perform a specified number of activities of daily living (ADL) (e.g. dressing, bathing, eating, etc.).~~ Historically, insurers that wrote LTCI encountered difficulties accurately projecting claims costs, lapse rates, investment returns and other factors associated with LTCI, and subsequently many writers have experienced unprofitability in older (legacy) blocks of LTCI business. This has led many companies to request significant rate increases, offer policyholders the option of modifying product benefits, or exit the product line altogether.

As many insurers continue to experience significant solvency challenges related to this line of business, state insurance regulators should continue to carefully evaluate and monitor the solvency position of all insurers with a material amount of LTCI business. As some insurers look for avenues to minimize or eliminate its risk from the LTCI block, they may look to new reinsurance opportunities and non-traditional buyers.

These same risks also affect reinsurers because the reinsurance contract ~~cannot~~ may not arbitrarily allow for ceded premium increases. Additionally, in order to effectuate a true transfer of risk, the reinsurer ~~does~~ may not have the ability to require the direct writer to request rate increases. The NAIC *Life and Health Reinsurance Agreements Model Regulation* (#791) provides additional guidance with respect to qualifying for risk transfer and reinsurance accounting within life and health reinsurance agreements.~~Furthermore, it would not qualify for reinsurance accounting.~~

In addition, periods of economic downturn and low interest rates increase the risk that LTCI writers will be challenged to generate sufficient returns to support this line. Declines in projected investment returns could also have a significant impact on LTCI reserve assumptions.

1. Actuarial Guideline 51—The Application of Asset Adequacy Testing to Long-Term Care Insurance Reserves (AG 51)

   Effective for reserves reported with the Dec. 31, 2017, financial statement, Actuarial Guideline 51—The Application of Asset Adequacy Testing to Long-Term Care Insurance Reserves (AG 51) now applies. The *Health Insurance Reserves Model Regulation* (#10) and the NAIC *Valuation Manual* VM-25, Health Insurance Reserves Minimum Reserve Requirements, contain requirements for the calculation of LTCI reserves. AG 51 is intended to provide uniform guidance and clarification of requirements for the appropriate support of certain assumptions for the asset adequacy testing applied to a company's LTCI block of contracts. AG 51 requires reporting to the department within the appointed actuary's actuarial memorandum required by VM-30, Actuarial Opinion and Memorandum Requirements, or in a special actuarial memorandum containing LTCI-specific information on the results of the analysis, assumptions on mortality, voluntary lapse, morbidity, investment returns and rate increase assumptions.

2. Reserve Increase Factors

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a. Background

Ever since asset adequacy testing became a requirement for life insurers in the 1980s, actuaries have been required to analyze reserve adequacy assumptions on an annual basis and make the assumptions more conservative when experience or expectations become more adverse. ~~If the more conservative assumptions resulted in inadequate reserves, companies were required to establish higher reserves to ensure future claims could be paid in the more adverse environment.~~ If reserves were found to be inadequate in light of the more conservative assumptions, companies were required to establish higher reserves to ensure that future claims could be paid in the more adverse environment.

In some cases, the chain of events is straightforward. For instance, for life insurance, if more people die at earlier ages than expected and the experience is highly credible, then the actuary increases mortality rates in the upcoming year-end filing. This leads to higher reserves being established.

In other cases, the chain of events is less straightforward. For instance, it is expected that cash surrenders on deferred annuity products will increase if interest rates rise. However, most deferred annuities have been sold during a period of decreasing interest rates. Actuarial and regulatory practice require reserves to be adequate in moderately adverse conditions, even if those conditions have not been recently experienced. There is typically judgment by the company actuary and another layer of judgment by regulators in play in this type of complex situation. The NAIC Standard Valuation Law Model 820 (SVL), NAIC Valuation Manual (VM), and the Actuarial Standards Board's Actuarial Standards of Practice (ASOPs) describe how these complex situations should be handled.

b. Long Term Care Insurance

LTCI blocks of business experiencing higher morbidity than expected will likely lead to changes in expectations on future morbidity for both the observed block and other blocks.

With LTCI, some factors are likely to play out in a straightforward manner. For instance, a combination of higher life expectancy and lower lapses will lead to more people than expected reaching prime LTCI claims ages of 80 and above. This leads to companies holding higher reserves than originally anticipated. Similarly, companies experiencing a decreasing interest rate environement will have lower-than-expected investment returns. This leads companies to hold higher reserves as the investment income relied upon to help pay claims is diminished.

~~It is important to note that mortality, lapse, and interest rate factors become observable and credible during the later premium-paying years.~~ Mortality, lapse, and interest rate factors become observable and can develop credibility during the premium-paying years prior to policy years when significant claims tend to occur.

c. Morbidity Assumptions

Morbidity, however, has tended to fall into the category of a complex factor. The three main aspects of LTCI morbidity are: (1) incidence, the percentage of people at a given age who start a claim; (2) average length of claim; and (3) utilization, which is less than 100 percent if, for example, the daily nursing home cost is lower than the maximum daily benefit in the insurance policy.

There has not been uniform experience development in morbidity, except that length of claim has tended to increase. This is likely because cognitive (e.g. dementia and Alzheimer's) claims tend to be longer than average and incidence has been higher than expected, which may be due to more people reaching the age when cognitive claims tend to occur.

Because of divergent experience among companies and because morbidity becomes observable and credible during the later claim-paying years, establishing and regulating LTCI morbidity assumptions has not been straightforward. However, as with other factors and other products, the handling of these situations is addressed in the SVL, VM, and ASOPs. Examples of these standards include:

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- SVL Section 12A(3)(a): "Assumptions shall, to the extent that company data is not available, relevant, or statistically credible, be established using other relevant, statistically credible experience."

- SVL Section 12A(4): "Provide margins for uncertainty … such that the greater uncertainty the larger the margin and resulting reserve."

- Actuarial Guideline 51 (providing guidance on VM-30) Section 4.B.: "The analysis shall comply with applicable Actuarial Standards of Practice, including standards regarding identification of key risks. Material assumptions associated with the LTCI business shall be determined testing moderately adverse deviations in actuarial assumptions."

- Acounting Practices and Procedures Manual, Appendix A-010 paragraph 48.e (referenced in VM-30): "The total contract reserve established shall incorporate provisions for moderately adverse deviations."

- Acounting Practices and Procedures Manual, Appendix A-010 paragraph 51 (referenced in VM-30): "Annually, an appropriate review shall be made of the insurer's prospective contract liabilities… and make appropriate increments… if such tests indicate that the basis of such reserves is no longer adequate."

The result is that whether credible experience exists or not, the company actuary needs to set assumptions underlying reserves, and the factors underlying the assumptions are often complex and frequently changing. Company and regulatory actuaries are experienced in working in this complex, changing environment with many life insurance products, such as variable annuities, indexed products, and LTCI having product features and factors underlying reserves that are complex and changing.

d. Rate Increases

A unique aspect of LTCI products is being a long-term product with rate increases that require review by states. Besides states with the largest insurance departments, the actuaries reviewing LTCI reserves are often the same staff reviewing LTCI rate increases. For larger states, there is typically coordination or training to ensure the reserve and rate teams are on the same page regarding developments in for example, life expectancy and morbidity. State insurance regulator experience in reviews of LTCI reserves and rate increase filings show that factors resulting in reserve increases and requests for rate increases are similar and include higher life expectancy, lower lapses, lower investment returns, and worsened morbidity.

There has been additional regulatory attention on ensuring that the companies asking for rate increases based on adversity of certain factors are holding reserves based on at least the same level of adversity in those factors. The questions used in many states' rate increase reviews require the company to explain the consistency between the rate increase filing assumptions and reserve adequacy assumptions.

To date, the most common complex, non-straightforward case is the applicability of a company's adverse morbidity experience of an older LTCI block to morbidity assumptions on a newer block. This complex dynamic comes into play when establishing reserve and rate increase assumptions.

The reserve assumption changes can occur with initiation by the company, through formal or informal agreement between regulators and ~~or~~ companies, or by relying on SVL Section 11.6., which allows a commissioner to require a company to change reserve assumptions and adjust reserves.

A typical example of a chain of events would first involve a block issued in 1995 to 1998 to policyholders with issue ages ranging from 52 to 62. By 2019, enough policyholders have reached prime LTCI claim ages of 80+, that experience driving reserve assumption changes has developed. As policyholders enter ages in the upper 80s and 90s, additional experience will develop that will help predict future LTCI costs and result in further changes in reserve assumptions. The development of older-age morbidity experience is expected to generate volatility in LTCI reserves. For some companies, the older-age morbidity experience will likely be unfavorable, with increased reserves needed.

For most other companies, the older-age morbidity experience will likely be as expected, leading to no significant, unforeseen reserve increases.

Companies will be expected to apply lessons learned from older blocks of business to their newer blocks of business. Those lessons will likely differ by situation. For example, to the extent underwriting is different, the newer and older blocks may experience different morbidity trends.

e. Rate Increase Factors

~~All of the above-mentioned reserve-related dynamics have occurred, are occurring, or will occur with rate increase requests. Historically, rate increases were based on higher life expectancy, lower lapses, and lower investment returns. As morbidity experience has developed, regulators have started receiving more morbidity-driven LTCI rate increase requests.~~

~~As the credibility of morbidity experience on older blocks increases, consideration is given to the applicability of the older-block data to newer blocks. This consideration is required with reserves and can drive substantial reserve increases in the industry. The same consideration can also drive rate increase requests, in some cases before prime claims years begin on the newer LTCI block.~~

~~To assist state insurance department staff performing reserve valuation analysis to gain an understanding of the rate review process, communication and coordination with the rate review staff may be necessary. The following example describes how lessons learned on an older block's morbidity experience and/or the need for more credible experience on the newer blocks may factor into a rate increase review.~~

- ~~Three potential approaches for regulatory consideration of such rate increases are, (1) disapprove the rate increase and force the new block to have credible experience before approving an increase, (2) allow partial consideration of the "lessons learned" on the older block and partially approve the rate increase, or (3) allow full consideration of the older-block lessons learned and fully approve the rate increase.~~

- ~~The downside of option (1) is that it will lead to higher rate increase requests in the future if newer block experience plays out similarly to older block experience. The downside of option (3) is that rates would end up being too high if experience plays out more favorably than expected.~~

- ~~After multiple, public, regulatory actuarial discussions on the topic, general (but not unanimous) consensus was that most rate approvals should land in a spot between options (2) and (3). To the extent the rate increase approval is towards option (3), the department should ensure the company has a mechanism to lower future premium rates if experience plays out more favorably than expected.~~

Factors impacting LTC reserves, including higher life expectancy, lower lapses, lower investment returns, and changes in morbidity, also potentially impact LTC rate increases.

If a company's reserve adequacy testing is dependent upon assumption of future LTC rate increases, the state insurance department staff performing reserve valuation should evaluate that assumption for reasonableness. The company's rate increase assumptions and documentation should be consistent with the requirements specified in Actuarial Guideline 51 related to rate increase plans. The state insurance department staff performing reserve valuation may wish to coordinate and communicate with the state's rate review staff to help evaluate the appropriateness and reasonableness of the company's future rate increase assumption.

f. Intra-Department Communication and Coordination of Actuarial Review Work

While every state insurance department may be structured differently, many state insurance departments have the same staff members perform work on both LTCI reserve valuation analysis and rate increase reviews. For state

insurance departments that have separate staff performing these functions, department staff should be aware of or coordinate the intra-department review work related to each function.

As examiners perform both the Corporate Governance assessment and the examination interviews, the topics discussed in this section should be considered. Exhibit Y – Examination Interviews includes several questions which may be considered as part of that process. Additionally, procedures regarding the examiners' assessment of the insurer's long-term care insurance related risks, controls, and possible test procedures can be located in Section 3 Reserves/Claims Handling (Life) repository and Underwriting repository.

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EXAMINATION REPOSITORY – RESERVES/CLAIMS HANDLING (HEALTH)

Annual Statement Blank Line Items

Listed below are the corresponding Annual Statement line items that are related to the identified risks contained in this exam repository:

Claims Unpaid (Less Reinsurance Ceded)
Accrued Medical Incentive Pool and Bonus Payments
Unpaid Claims Adjustment Expenses
Aggregate Health Policy Reserves
~~Premium Deficiency Reserves~~
Aggregate Life Policy Reserves
Property/Casualty Unearned Premium Reserves
~~Aggregate Claim Reserves~~
Aggregate Health Claim Reserves

Relevant Statements of Statutory Accounting Principles (SSAPs)

The relevant SSAPs related to the health insurance reserving process, regardless of whether or not the corresponding risks are included within this exam repository, are listed below:

~~No. 3 Accounting Changes and Corrections of Errors~~
No. 5R Liabilities, Contingencies and Impairments of Assets – Revised
~~No. 25 Affiliates and Other Related Parties~~
No. 50 Classifications of Insurance or Managed Care Contracts
No. 54R Individual and Group Accident and Health Contracts
No. 55 Unpaid Claims, Losses and Loss Adjustment Expenses
No. 61R Life, Deposit-Type and Accident and Health Reinsurance – Revised
No. 66 Retrospectively Rated Contracts
No. 107 Risk-Sharing Provisions of the Affordable Care Act

Identified Risk	Branded Risk	Exam Asrt.	Critical Risks	Possible Controls	Possible Test of Controls	Possible Detail Tests
Other Than Financial Reporting Risks						
The board of directors (or committee thereof) is not involved in establishing and/or reviewing the insurer's overall reserving practices.	OP ST RV	Other	RA	The insurer's board of directors (or committee thereof) has adopted and/or reviewed the insurer's overall reserving practices. The board of directors (or committee thereof) regularly discusses reserving issues and receives reports from the appointed actuary. The reports include an explanation of the reserving policy and methodology, as well as an analytical review of the insurer's reserves. The insurer monitors and revises its reserving practices as needed.	Verify that the insurer has established overall reserving practices that have been adopted and/or reviewed by the board of directors (or committee thereof). Review board of directors (or committee thereof) minutes to ensure discussion of reserving. Review meeting materials to determine if materials would properly facilitate BOD oversight. Obtain information on revisions made by the insurer to its reserving practices and verify whether they were appropriately reviewed and/or approved by the board of directors (or committee thereof).	Obtain information on the insurer's overall reserving practices, including meeting materials, and forward it to the insurance department actuary or an independent actuary for review. Discuss with members of the board of directors (or committee thereof) their level of involvement in the monitoring of reserving practices.
Financial Reporting Risks						
New claims are not entered into the claims management system.	RP LG	AC CT CO	RD	Segregation of duties exists between the claim notification and the input of claims data into the claims system. Control reports exist to	Observe that segregation of duties exists between the claim notification and the input of claims data into the claims system. Obtain the exception report	Select a sample of items from the exception reports and verify that the claim was appropriately accounted for.* Select a sample of claim

Identified Risk	Branded Risk	Exam Asrt.	Critical Risks	Possible Controls	Possible Test of Controls	Possible Detail Tests
				ensure all claims reported to the insurer electronically or manually have been entered into the claims system. Exceptions are identified and resolved timely. The insurer reviews the Type II SOC 1 reports and ensures compliance with user-control considerations for any outsourcing companies that enter claims on behalf of the insurer.	and ensure management review and resolution of any exceptions. Test the operating effectiveness of the automated claims posting process through reperformance and observation, which could include IT testing of batch totals to ensure completeness of transactions processed. Obtain documentation of management's review of the Type II SOC 1 reports.	and expense payments made subsequent to year-end to verify that claims were recorded in the proper period. Review Type II SOC 1 reports, including bridge letters, to ensure there are no significant control deficiencies or internal control weaknesses related to processing new claims into the claims system.
Claims data is incomplete or incorrectly entered into the claims management system.	OP LG	AC CT CO EX	RD	Claims data is subject to independent verification or quality assurance (QA) reviews. The claims system has automated controls that will not allow a claim to be entered without a valid in-force policy. The claims system has automated controls that will not permit continued	Obtain documentation of independent claim verification or QA review. Ensure reviews performed address the completeness and accuracy of underlying claims information entered into the system. Test the operating effectiveness of automated controls (i.e., edit checks) through reperformance and observation. Obtain the error report and ensure proper resolution of exceptions.	Perform data validation tests to verify the accuracy of claim information maintained in the claims system, such as coverage terms, demographic data, date of service, provider name, service description or code, insured name, claim number and coverage period by vouching the information to the claimant's insurance contract, claims form and any other underlying support.* Scan the database(s) for internal inconsistencies,

Identified Risk	Branded Risk	Exam Asrt.	Critical Risks	Possible Controls	Possible Test of Controls	Possible Detail Tests
				processing until all pertinent claim data has been entered. Entering a valid policy number will automatically populate select policy data. System edits will identify data that does not meet the predetermined criteria, resulting in inclusion on a system-generated exception report. Segregation of duties exists between individuals responsible for new claim set-up and those responsible for setting up new policies.	Test the operating effectiveness of authority restrictions through reperformance and observation. Obtain claims set-up and new policy set-up authorization listings and cross-reference the listings to ensure that there are no employees with conflicting authority.	such as missing claim amounts, unusually small amounts and claims misclassified by type (e.g., Medicare). In situations where adequate segregation of duties is not apparent, obtain data to determine whether any claims were set up by the same user who created the corresponding policy in the master file. If any instances are identified, investigate the claim to ensure the claim exists and is supported by underlying data.
The third-party administrators (TPAs), or managing general agents (MGAs), are not processing claims in accordance with the insurer's claims procedures as outlined in the TPA agreement.	LG OP RP	AC CM	RD	The insurer performs regular audits of its TPAs/MGAs to determine whether insurer claims handling standards and additional contract provisions are being consistently followed by the TPA. Management obtains a Type II SOC 1 report for all TPAs and reviews the report to verify whether the TPA has adequate controls and that the insurer is adhering to user control considerations. Management performs necessary reviews to comply with applicable	Review audit reports and other documentation to determine whether the insurer provides sufficient oversight of its TPAs/MGAs. Verify that the insurer has obtained and reviewed the TPA's Type II SOC 1 report, if available. Determine whether the insurer is adhering to user control considerations. Obtain evidence of management's review of compliance with applicable	Determine, by a review of selected claims, whether the insurer is settling its claims accurately and in accordance with the contract, based on information contained in the claim file.* Review the Type II SOC 1 report to determine whether the controls outlined in the report are adequate to ensure that claims are being processed in accordance with the TPA agreement. Test for compliance with applicable state MGA regulations.

Identified Risk	Branded Risk	Exam Asrt.	Critical Risks	Possible Controls	Possible Test of Controls	Possible Detail Tests
				state MGA regulations.	state MGA regulations.	
Claims are not being processed accurately and in accordance with insurer guidelines.	OP ST LG	AC CM CO	RD	The insurer has administrative policies and maintains a claims procedures manual that outlines the following requirements: • Maximum benefit to be paid based on procedure type. • Usual, customary and reasonable (UCR) limitations. • Proper application of deductibles. • Reserving and payment authority and approval levels. • File documentation and tracking. • Procedures for handling suspicious and/or fraudulent claims. • Compliance with applicable state fair claims practices laws and/or regulations. Automated controls are in place to ensure that paid losses are not to exceed policy limits, cover ineligible loss causes/types and/or apply to a policy period for which insurer is not contractually responsible. Any consideration to pay a loss must be processed in	Review the claims procedures manual to determine its appropriateness, including management approval. Test the operating effectiveness of system edit checks to ensure procedures are implemented through reperformance and observation. Review assessments of the claims handling process performed by internal/external auditors,	Perform tests to determine whether claims were accurately processed in accordance with the claims procedures manual, approved authority limits and administrative policies through review of the claimant's insurance contract, claims form and any other underlying support. Review policyholder complaints and investigate significant issues. Review a sample of denied claims to ensure compliance with contract provisions.*

Identified Risk	Branded Risk	Exam Asrt.	Critical Risks	Possible Controls	Possible Test of Controls	Possible Detail Tests
				accordance with the insurer's procedures. As part of the claims processing procedures, the insurer obtains adequate documentation and coverage of benefits before a claim is settled. Claims approval is subject to approved authority limits. A QA review is periodically performed for each claims processor to ensure compliance with the claims handling policies.	reinsurers and/or others for significant issues. Test the operating effectiveness of controls to ensure adequate documentation is obtained before payment is made. Test the controls in place to ensure that claims are approved in accordance with documented authority limits. Review documentation of QA reviews to determine that the QA function is being executed as outlined in the insurer's policies. On a sample basis, reperform the QA testing to ensure that the testing was completed accurately.	
The claims data utilized by the actuary to estimate reserves does not correspond to the data in the insurer's claims system and to the data in the insurer's accounting records.	OP RV	AC CO	RD	The insurer has established procedures to reconcile actuarial data to the insurer's claims system, the data in the insurer's accounting records and appropriate annual financial statement schedules and/or exhibits. Such reconciliations are reviewed by supervisory personnel. Inventories of reported and unpaid claims are maintained and periodically	Review the insurer's reconciliation reports of actuarial data to the insurer's claims system and the insurer's accounting records. Ensure evidence of supervisory review. Review the insurer's reconciliation of reported and unpaid claims to the	Test reconciling items within the reconciliations for appropriateness. Reconcile the insurer's actuarial report for claims paid and claims adjustment expenses (CAE) to supporting insurer reports, general ledger and annual financial statement schedules and exhibits as of the valuation date.

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Identified Risk	Branded Risk	Exam Asrt.	Critical Risks	Possible Controls	Possible Test of Controls	Possible Detail Tests
				reconciled to the general ledger.	general ledger.	
Reinsurance is not properly taken into account in accumulating claims data.	RV	AC CO	RD RRC	The insurer has established procedures to prepare the claims data for actuarial review in accordance with the insurer's reinsurance treaties.	Review the insurer's reconciliation reports of actuarial data to the insurer's claims system, reinsurance reports, and accounting records. Test the operating effectiveness of the insurer's established procedures to include claims data from assumed reinsurance treaties within the data for actuarial review.	Test reconciling items relating to reinsurance claims data for appropriateness. Verify assumed reinsurance claims data accumulated for actuarial review by comparing to the data provided by the ceding insurer for completeness.
Initial ~~case~~ claim reserves are not established or reviewed in accordance with insurer standards.	RV CR	AC VA CO	RA	The insurer has a ~~case~~ claim reserving philosophy and qualified actuaries are involved in establishing and reviewing the reserving policy. Initial reserves are made in accordance with the insurer's reserving philosophy and within a specified time frame. Claim adjusters/supervisors are required to review significant initial case reserves on a timely basis and make adjustments as necessary.	Obtain documentation supporting the insurer's reserving philosophy. Review reserving philosophy for actuary review and policy adequacy. For a sample of loss reserves, determine whether loss reserve reviews were performed and documented in accordance with insurer policy. Obtain periodic new claims reports and verify the insurer reviews significant initial case reserves and makes adjustments, if necessary, in a timely manner.	For a sample of reserves verify that the calculation is in accordance with the reserving philosophy and that reserves are calculated on a timely basis.* For a sample of reserves meeting the criteria to go to a claims committee, determine whether the reserves were referred to this committee.* Confirm a sample of unpaid claims with major providers.

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Identified Risk	Branded Risk	Exam Asrt.	Critical Risks	Possible Controls	Possible Test of Controls	Possible Detail Tests
				Committees are formed to evaluate and strategize claims involving serious injuries, complex claims law, and large or unusual loss reserve determinations or settlements.	Obtain minutes and other meeting materials from the meetings of the committee to determine whether the committee provided appropriate oversight.	
~~Case~~ Claim reserves (other than IBNR) are not updated accurately.	RV CR	CO VA	RA	The insurer has a policy requiring open claims to be reviewed regularly. When new information is received, case reserves are reviewed and adjusted, if necessary. The claims management system generates analyses of reserve increases and decreases, an outstanding reserve list, an outstanding reserve list by claim adjuster, and a reserve release report. These reports are reviewed/ monitored by the claims manager for reasonableness.	From a sample of ~~case~~ claim reserves (other than IBNR), determine whether the reserves are updated regularly and are appropriately updated when new information is received. Obtain copies of the reserve reports, noting management approval.	Select a sample of paid claims and compare the final overall claims settlement with the case reserve to determine whether the reserves are adequate and/or updated accurately. Verify that the information contained in the reports is accurate and determine whether the appropriate analyses are being used to evaluate the reserves.
The assumptions and methodologies used by the insurer for the health, long-term care and long-term disability business are not accurate and appropriate.	RV	VA AC PD	RA	The insurer uses consistent assumptions and methodologies that have been based on historical results (to the extent appropriate), adequately documented, approved by senior management and in accordance with statutory accounting principles, Actuarial Standards of Practice, and applicable state statutes and/or regulations.	Gain an understanding of the insurer's assumptions and methodologies and compare with prior periods. Verify that senior management signs off on assumptions and methodologies used by the insurer, including any changes. Verify senior management review of reports from	Review assumptions and methodologies for reasonableness, appropriateness and accuracy, with assistance from the insurance department actuary or an independent actuary. Verify that reserving assumptions are in accordance with the relevant SSAPs related to health reserving, as well as any applicable state statutes,

Identified Risk	Branded Risk	Exam Asrt.	Critical Risks	Possible Controls	Possible Test of Controls	Possible Detail Tests
				Senior management uses either internal or independent actuaries to conduct reserve analyses of all major lines of business on an annual basis. Actuarial analysis is subject to a peer review process. Management receives regular reports on loss ratios by line or class of business, as well as other key ratios, and reviews unusual fluctuations on a timely basis to review reserves for adequacy. The insurer utilizes a fully staffed, well-qualified actuarial department that is under the direction of a fellow of the Society of Actuaries (FSA) or member of the American Academy of Actuaries (MAAA) and is experienced in the lines of business written by the insurer. The reserving actuarial unit's responsibilities are segregated from the pricing actuarial unit, but there is regular communication between the two units.	actuaries and that reports include reserve analyses of all major lines of business. If performed in-house, review and test the actuarial peer review process and related sign-offs. Verify management review of reserve reporting and test the operating effectiveness of procedures in place. Review the credentials, background and responsibilities of the insurer's actuarial department (internal or external) for appropriateness. Request and review the insurer's organizational chart and job descriptions to determine whether the functions are separate and distinct. Interview the appointed actuary during the planning	regulations, actuarial guidelines, pronouncements and/or bulletins. Review prior history of claims development, as well as subsequent claims development data to analyze the reasonableness of assumptions and methodologies. Determine whether the appropriate disclosures have been made in the Notes to the Financial Statements for the changes in reserve methodologies. Review actuarial reports and compare reports to prior periods. Investigate significant variations. Utilize the insurance department actuary or an independent actuary to perform an independent calculation/estimate of the reserves. Review correspondence related to peer review for appropriate depth of review. Compare the opining actuary's assumptions and estimates with those in other available actuarial analyses.

Identified Risk	Branded Risk	Exam Asrt.	Critical Risks	Possible Controls	Possible Test of Controls	Possible Detail Tests
				The insurer's organizational structure limits the influence that management can have on the appointed actuary. The insurer has appropriately established procedures to include policy lapse rates when calculating the reserving estimates.	phase of the examination to determine whether the insurer's organizational structure is appropriate in this area. Review insurer processes in place to calculate the reserve calculations to ensure consideration is given to policy lapse rates.	Determine whether the Actuarial Opinion was changed by the appointed actuary after meeting with insurer management.
The claims unpaid, claims reserve, policy reserve and premium deficiency reserve computations are not performed correctly or the selected estimates are unreasonable.	OP RV	AC VA	RA	The insurer has an established process (although assumptions and methodologies may change) to estimate the claims unpaid, claim reserves, policy reserves and premium deficiency reserves on an annual basis. The insurer maintains a fully staffed, well-qualified actuarial department that is under the direction of a fellow of the Society of Actuaries (FSA) or member of the American Academy of Actuaries (MAAA) and is experienced in the lines of business written by the insurer. Senior management uses either internal or independent actuaries to conduct reserve analyses of all major lines on an annual	Review the process in place (which may include performance of a walkthrough) to estimate the claims unpaid, claim reserves, policy reserves and premium deficiency reserves. Review the credentials, background and responsibilities of the insurer's actuarial department staff for appropriateness. Obtain actuarial reports to verify insurer is using either independent or in-house actuaries to perform the reserve calculations on all	Utilize the insurance department actuary or an independent actuary to perform an independent estimate of the claims unpaid, claims reserve, policy reserve and premium deficiency reserves. Perform analytical procedures to review the reasonableness of reserve estimates.

Identified Risk	Branded Risk	Exam Asrt.	Critical Risks	Possible Controls	Possible Test of Controls	Possible Detail Tests
				basis. The actuarial calculations are subject to a peer review process. The insurer's board of directors (or committee thereof) receives an annual presentation on the actuarial analysis process. Management receives regular reports on claims ratios (including claims unpaid, claims reserve, policy reserve and premium deficiency reserve) by line or class of business for accident year and calendar year, as well as other key ratios, and reviews unusual fluctuations on a timely basis to review reserves for adequacy.	major lines of business annually and verify senior management review. If performed in-house, review and test the actuarial peer review process and related sign-offs. Review the board of directors (or committee thereof) minutes to verify that a presentation was given on the actuarial analysis process. Verify management review of reserve reporting and test the operating effectiveness of procedures in place.	
The claims adjustment expense (CAE) computations are not performed correctly.	OP RV	AC VA CO	RA	The insurer has established processes to estimate both the cost containment and other claim adjustment reserves on an annual basis. The insurer maintains a fully staffed, well-qualified actuarial department that is under the direction of a	Review the processes (which could include a walkthrough) in place to calculate both the cost containment and other claim adjustment reserves. Review the credentials, background and responsibilities of the insurer's actuarial	Utilize the insurance department actuary or an independent actuary to perform an independent calculation/estimate of the CAE. Perform analytical procedures to review the reasonableness of CAE calculations.

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Identified Risk	Branded Risk	Exam Asrt.	Critical Risks	Possible Controls	Possible Test of Controls	Possible Detail Tests
				fellow of the Society of Actuaries (FSA) or member of the American Academy of Actuaries (MAAA) and is experienced in the lines of business written by the insurer.	department staff for appropriateness. Obtain actuarial reports to verify the insurer is using either independent or in-house actuaries to perform separate cost containment and other claim adjustment reserve analyses on an annual basis.	
				Senior management uses either internal or independent actuaries to conduct separate cost containment and other claim adjustment reserve analysis of all major lines on an annual basis.	Verify senior management review of reports from actuaries.	
				The actuarial analyses are subject to a peer review process.	If the analyses are performed in-house, review and test the actuarial peer review process and related sign-offs.	
				The insurer's board of directors (or committee thereof) receives an annual presentation on the actuarial analysis process.	Review the board of directors' (or committee thereof) meeting minutes to verify whether a presentation was given on the actuarial analysis process.	
				Management receives regular reports on loss ratios by line or class of business, as well as other key ratios, and reviews unusual	Verify management review of reserve reporting and test the operating effectiveness of procedures in place.	

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Identified Risk	Branded Risk	Exam Asrt.	Critical Risks	Possible Controls	Possible Test of Controls	Possible Detail Tests
				fluctuations on a timely basis to review reserves for adequacy.		
Changes in the legal environment or changes in the insurer's underwriting, reserving or claims handling processes are not appropriately considered within the insurer's reserving assumptions and methodologies.	OP RV ST	VA PD AC	RA	The insurer has procedures in place for its legal department to monitor and communicate changes in the legal environment (e.g., changes in case law, award amounts, trends in the number of claims being litigated) are being taken into consideration by the reserving unit in a timely manner. The insurer has procedures in place for the underwriting, case reserving and claims handling units to communicate changes in their processes to the reserving unit in a timely manner.	Review the insurer's process to monitor changes in the legal environment that may affect the reserving process. Review evidence of communication between the reserving unit and other relevant insurer units.	Through a review of the actuarial reports, determine whether changes in the legal environment and/or changes in the insurer's internal processes have been properly incorporated in the insurer's reserving assumptions and methodologies.
The computations of reinsurance credits within the reserves are not performed correctly. (See also Examination Repository – Reinsurance Ceding Insurer)	CR RV	AC VA CO	RA RRC	The reserving actuary calculates the reserve on a gross basis and determines the net basis by estimating the reinsurance credits and applying them to the gross reserve. The insurer applies reinsurance credits to reserves by reviewing reinsurance treaties in place at the insurer, as well as historical results.	Test the operating effectiveness of the insurer's process for reviewing the reserve analysis to determine whether reserves have been estimated on a gross basis, including management approval and sign-off. Test the operating effectiveness of the insurer's process to estimate reinsurance credits for reserves, including management approval and	Compare the annual financial statement net and gross incurred and paid loss presentation for consistency with reinsurance treaties in place at the insurer. Consider the reasonableness of reinsurance credits taken, based on a review of the insurer's reinsurance program and treaties in place.

Identified Risk	Branded Risk	Exam Asrt.	Critical Risks	Possible Controls	Possible Test of Controls	Possible Detail Tests
					sign-off.	
The insurer is not properly recording case reserves (assumed or ceded) for contracts subject to reinsurance.	RV CR LG	CO VA AC	RA RRC	The insurer has policies in place to verify that case reserves subject to reinsurance are valid and accurate (within contract time frame, covered under the contract, etc.).	Review insurer policies to determine appropriateness, noting management approval. Review documentation of insurer's review of claim validity.	Utilize the NAIC Examination Jumpstart report to determine whether case reserves recorded by the insurer agree with the case reserves of the assuming (ceding) insurer.
Management books reserves that are materially different than the actuary's best estimate.	OP ST LG	VA PD	RA	The insurer has a process in place to ensure that reserves are recorded based on the actuary's best estimate, or documents an appropriate reason for any deviations. The board of directors (or committee thereof) reviews management's best estimate of booked reserves and challenges such estimates based on reports received, including the actuarial report from the appointed actuary. The insurer's organizational structure limits the influence that management can have on the appointed actuary.	Review management guidelines regarding the recording of actuarially determined reserves. Verify that deviations from the actuary's best estimate are properly documented, if applicable. Review the board of directors (or committee thereof) meeting minutes ~~to~~ for evidence of a presentation and review of information supporting management's best estimate of the booked reserves (i.e., the actuarial report). Interview the appointed actuary during the planning phase of the examination to determine whether the insurer's organizational structure is appropriate in this area.	Review the actuarial report, as well as the annual financial statements and other appropriate documentation, to determine whether the insurer has booked the actuary's best estimate. Review the documentation supporting a deviation from the actuary's best estimate for reasonableness, if applicable.
The insurer does not maintain an adequate premium deficiency reserve.	RV ~~RQ~~LQ OP	VA CO CM	RA	The insurer has a process in place to review for premium deficiencies on an annual basis in accordance with SSAP No. 54.	Review the process in place and verify key controls surrounding the calculation of premium deficiency reserves.	Perform an analytical review of loss ratios. If necessary, utilize the insurance department actuary or an independent

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Identified Risk	Branded Risk	Exam Asrt.	Critical Risks	Possible Controls	Possible Test of Controls	Possible Detail Tests
~~Note: It may also be appropriate to consider reserves for insufficient administrative fees for self-insured contracts.~~				Independent actuaries review and sign off on premium deficiency reserve calculations.	Obtain the actuarial opinion and verify approval of premium deficiency reserve calculations.	actuary to perform a detailed review or an independent calculation/estimate of the premium deficiency reserves.

EXAMINATION REPOSITORY – RESERVES/CLAIMS HANDLING (LIFE)

Annual Statement Blank Line Items

Listed below are the corresponding Annual Statement line items that are related to the identified risks contained in this exam repository:

Aggregate Reserve for Life Contracts
Aggregate Reserve for Accident and Health Contracts
Liability for Deposit-Type Contracts
Contract Claims

Relevant Statements of Statutory Accounting Principles (SSAPs)

All of the relevant SSAPs related to the life insurance reserving process, regardless of whether or not the corresponding risks are included within this exam repository, are listed below:

No. 5R Liabilities, Contingencies and Impairments of Assets – Revised
No. 50 Classifications of Insurance or Managed Care Contracts
No. 51R Life Contracts
No. 52 Deposit-Type Contracts
No. 54R Individual and Group Accident and Health Contracts
No. 55 Unpaid Claims, Losses and Loss Adjustment Expenses
No. 61R Life, Deposit-Type and Accident and Health Reinsurance – Revised
No. 63 Underwriting Pools
~~No. 70 Allocation of Expenses~~

Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
Other Than Financial Reporting Risk						
The board of directors (or committee thereof) is not involved in establishing and/or reviewing the insurer's overall reserving ~~practices~~policy.	ST RV	Other	RA	The insurer's board of directors (or committee thereof) has adopted and/or reviewed the insurer's overall reserving policy~~practices~~. The board of directors (or committee thereof) regularly discusses reserving issues and receives reports from the appointed actuary. The reports include an explanation of the reserving policy and methodology, as well as an analytical review of the insurer's reserves. The insurer monitors and revises its reserving policy~~practices~~ as needed.	Verify that the insurer has established overall reserving policy ~~practices~~ that have been adopted and/or reviewed by the board of directors (or committee thereof). Review board of directors (or committee thereof) minutes to ensure discussion of reserving. Review meeting materials to determine if materials would properly facilitate BOD oversight. ~~Review board of directors (or committee thereof) minutes to ensure regular discussion of reserving issues including reports (at least annually) from the appointed actuary.~~ Obtain information on revisions made by the insurer to its reserving practices and verify the revisions were appropriately reviewed and/or approved by the board of directors (or committee thereof).	Obtain information on the insurer's overall reserving policy ~~practices~~ and forward it to the insurance department actuary or an independent actuary for review. Discuss with members of the board of directors (or committee thereof) their level of involvement in monitoring the implementation of reserving policy~~practices~~.
The insurer has not taken appropriate steps to prepare for the implementation of Principle-Based Reserving (PBR).	RV ST	Other	RA RD	The insurer has a PBR implementation plan that includes consideration of staffing needs and appropriate expertise in current and/or future	Verify that budgets and/or strategic plans contain consideration of PBR implementation needs including qualified staff.	Review the insurer's PBR implementation plan for reasonableness. Review actuarial department staff

Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
Note: Under the requirements of the Valuation Manual, companies have until 1/1/2020 to implement PBR requirements. See Section 1, VI, ~~6~~ for further information on the implementation of PBR.				budgets and strategic plans. The insurer has a process to monitor the progress and ongoing needs of PBR implementation. Process includes consideration of exempted products. Data reporting and system needs are reviewed by management on a periodic basis in preparation for PBR implementation.	Determine if the company has adequate suitability requirements in place for the actuarial department that requires the actuarial staff to be qualified to implement and practice a PBR methodology. Review the insurer's procedures to determine if pending PBR implementation needs are continuously monitored by company personnel. Consider if certain products have been exempted and the appropriateness of that determination. Verify that management reviews data reporting and system needs.	qualifications to determine if suitability requirements are met and/or determine if actuarial staff has adequate training available for implementation of PBR. Consider involving an IT specialist in a review of system capabilities necessary for PBR implementation.
Financial Reporting Risks						
In-force data is not complete or accurate nor consistent with accounting records	OP RV	CO AC	RD	The insurer has established appropriate internal controls over the input and maintenance of in-force data as outlined in the Examination Repository – Underwriting. The in-force data is tested periodically by the insurer's quality assurance (QA) function for completeness and accuracy.	Perform tests to verify the operating effectiveness of policy in-force controls as outlined in the Examination Repository – Underwriting. Review the QA reports relating to the testing of in-force data to verify the operating effectiveness of the controls.	Obtain a copy of the listing detailing in-force insurance contracts provided to the insurer's actuary. Perform procedures to verify the completeness of this listing by tracing to the database a sample of contracts selected from sources outside the reserve system (e.g., premium cash collections). Use control totals for face amount, benefits, and policy count in order to detect use

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Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
				The insurer's system is programmed to issue insurance contracts utilizing sequential policy numbers. In-force database is reconciled to accounting records on a periodic basis.	Verify through observation and/or reperformance that system parameters prohibit the issuance of non-sequential policy numbers. Ensure management review of exceptions. Test reconciliation process for supervisory review, appropriateness and operating effectiveness.	of incorrect files.* In conjunction with the testing performed in the Examination Underwriting Repository, select a sample of in-force insurance contracts to verify that the system data reflects the actual insurance contract provisions.* Review complaint logs for misapplied payments, missing policy documentation and investigate the status of the complaint. Reconcile data elements to AS reporting.
The data utilized in the company's PBR model is not representative and consistent with the company's in-force data.	OP RV	AC CO	RD	The insurer maintains a model validation process to confirm that model cells represent actual inforce data.	Review documentation associated with the model validation process performed by the company to ensure agreement between the insurer's model and aggregated in-force data for attributes such as: *Issue age *Gender *Policy counts *Face amounts *Fund values *Annualized premium	Compare in-force aggregation and statistics for products under scope of PBR to model output reports at period zero for attributes such as: *Average issue age *Gender distribution *Total policy counts *Total face amounts *Total fund values *Total annualized premium
In-force data is not appropriately restricted and protected to maintain	OP	AC CO EX	RA RD	The insurer maintains logical access controls, including password protection and active	Test the operating effectiveness of logical access controls by reviewing documentation	Select a sample of in-force policy data at the examination as of date for accuracy and completeness

Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
accurate and complete data.				directories, to properly restrict access to in-force data. The insurer has appropriately segregated its duties to ensure that individuals with the ability to update in-force data do not have conflicting responsibilities. The insurer has established policies and procedures for making accurate, timely changes to policies. The insurer has established a QA process to review changes to policies to ensure compliance with the insurer's policies and procedures on a sample basis.	relating to requests for access and by attempting to have unauthorized individuals access the in force data. Test the operating effectiveness of segregation controls by attempting to have individuals authorized to access in-force data access claims processing or other systems. Perform a walkthrough to gain an understanding of the insurer's process to make changes to in-force policies. Test a sample of changes to policies reviewed by the QA function for proper implementation of the insurer's policies and procedures.	testing. * Test a sample of changes made to in-force policies during the year by reviewing supporting documentation.*
Reinsurance is not properly taken into account in accumulating in-force data. (See also Examination Repository – Reinsurance Assuming Insurer.)	RV	AC CO	RD RRC	The insurer has established procedures to prepare the in-force data for actuarial review in accordance with the insurer's reinsurance treaties.	Review the insurer's reconciliation reports of actuarial data to the insurer's in-force system, reinsurance reports, and accounting records. Test the operating effectiveness of the insurer's established procedures to include in-force data from assumed reinsurance treaties within the data for actuarial	Test reconciling items relating to reinsurance in-force data for appropriateness. Verify the assumed reinsurance in-force data accumulated for actuarial review by comparing to the data provided by the ceding insurer for completeness. Utilize the NAIC Examination Jumpstart report to compare in-force

Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
					review.	amounts reported by the assuming insurer to those amounts reported by the ceding insurer.
The insurer does not properly monitor XXX/AXXX reserve development related to its ceded reinsurance transactions. Note: The Financial Analysis Handbook (V.C. Domestic and/or Non-Lead State Analysis) has several procedures that may be relevant in the evaluation of captive reinsurance transactions and the related reserves.	RV	AC VA	RA RRC	The insurer monitors actual experience on ceded reinsurance relative to the initial or most recent projections and monitors underlying assumptions to evaluate asset adequacy and report any material adverse deviations to management.	Review the insurer's process to monitor experience on ceded reinsurance transactions and verify that material adverse deviations are reviewed by management.	Determine whether the insurer's ceded reinsurance transactions are tracking appropriately relative to the initial or most recent projections and underlying assumptions. For example, compare actual deaths under the reinsurance transaction with expected deaths assumed in the reserve under the reinsurance transaction. Consider utilizing an actuarial specialist to assist in this determination.
The assumptions and methodologies used by the insurer for determining the reserves for life, A&H and deposit-type contracts are not accurate or appropriate.	RV	VA AC PD	RA	The insurer uses consistent assumptions and methodologies that have been based on guidelines outlined in the *Valuation Manual (VM)* and Appendix A and Appendix C of the NAIC *Accounting Practices and Procedures Manual* (to the extent appropriate), adequately documented, approved by senior management, and in accordance with statutory accounting principles (SAP) and applicable state statutes and/or regulations.	Gain an understanding of the insurer's assumptions and methodologies and compare with prior periods. Verify that senior management signs off on assumptions and methodologies used by the insurer, including any changes. Verify senior management review of reports from actuaries and that reports include reserve analyses of all major lines of business.	Review assumptions and methodologies for reasonableness, appropriateness, accuracy, and compliance with the *Valuation Manual* and Appendix A and Appendix C of the NAIC *Accounting Practices and Procedures Manual*, with assistance from the insurance department actuary or an independent actuary. Compare actual investment, mortality, morbidity, lapse, interest crediting strategy and expense experience to assumptions, by line of

Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
				Senior management uses internal or independent actuaries to conduct reserve analyses of all major lines of business on an annual basis. The insurer maintains a fully staffed, well-qualified actuarial department Actuarial analysis is subject to a peer review process. Management receives regular reports on claim liabilities (including IBNR) by line or class of business, as well as other key ratios, and reviews unusual fluctuations on a timely basis to review claim liabilities for adequacy.	Review the credentials, background and responsibilities of the insurer's actuarial department staff or independent actuaries. If performed in-house, review and test the actuarial peer review process and related sign-offs. Verify management review of contract claim liabilities reporting, including analysis of fluctuations, and test the operating effectiveness of procedures in place.	business and to prior-period assumptions. Verify whether the assumptions surrounding contract claim liabilities are in accordance with the relevant SSAPs, as well as applicable statutes, regulations, pronouncements and/or bulletins. Utilize the insurance department actuary or an independent actuary to perform an independent calculation/estimate of the life reserves and incurred but not reported (IBNR) contract claims liability. Determine whether the appropriate disclosures have been made in the Notes to the Financial Statements for any changes in reserve methodologies. Review actuarial reports and compare reports to prior periods. Investigate significant variations. Review correspondence related to any peer reviews performed for appropriate depth of review.
The assumptions used by the insurer to calculate reserves for	RV	VA AC PD	RA	The company utilizes the prescribed valuation assumptions of the	Utilize a Department actuary, independent actuary or NAIC Actuarial	Utilize a Department actuary, independent actuary or NAIC Actuarial

Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
policies subject to Principle-Based Reserving are not accurate or appropriate.				Valuation Manual to calculate PBR reserves. The company has established a process for determining appropriate margins. The company maintains credible experience data to support all assumptions utilized in PBR reserving, including: • Lapse • Mortality • Morbidity • ~~Interest rate~~ • Premium Persistency • Etc.	Modeling support staff to review company documentation that provides support for assumptions and evidence that they are developed in accordance with the requirements of PBR as published in the Valuation Manual.	Modeling support staff to verify and validate that the company has followed the requirements of PBR as prescribed in the Valuation Manual in developing assumptions.
The assumptions used by the insurer to calculate reserves for long-term care insurance (LTCI) policies are not accurate or appropriate to meet reserve adequacy requirements.	RV	VA AC	RA	The company maintains credible experience data to support all assumptions utilized in calculating reserves for LTCI policies, including: • Lapse • Mortality • Morbidity • Interest rate • Etc. The company utilizes an independent actuarial firm (other than its appointed actuary) to periodically review its LTCI reserving assumptions.	Select a sample from experience studies to verify support for and consistency with assumptions used by the company. Review any third-party actuarial work to verify and substantiate the appropriateness of company assumptions.	Utilize the insurance department actuary or an independent actuary to review assumptions and methodologies for reasonableness, appropriateness, accuracy, and compliance with the *Valuation Manual*. Compare actual investment, mortality, morbidity, and lapse experience to assumptions. Compare reserving assumptions to rate increase assumptions, (for example

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Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
						review the AG51 filing and compare against rate increase requests) to ensure that assumptions used for pricing and reserving do not materially conflict. ~~are similar in nature~~. Review the company's AG51 filing and compare assumptions utilized by the company in LTCI reserving against industry standards and those of its competitors. Review the company's AG51 reporting to identify assumptions underlying the asset adequacy testing memorandum that appear to be an outlier and compare against a subsequent rate increase filing. Coordinate with the Valuation Analysis Working Group of the NAIC regarding any reviews it has performed on the company's AG 51 filings. Utilize the insurance department actuary or an independent actuary to evaluate the impact that a change in assumptions could have on the company's LTCI reserves and the company's solvency

Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
						position by reperforming reserve calculations using more conservative assumptions.
Policies with supplemental or accelerated benefits have not been properly separated and reserved for in accordance with SAP.	OP RV	AC	RA RD	The insurer has a process in which supplemental and accelerated benefits are properly identified and reserved.	Test the process surrounding the identification and reserving of supplemental and accelerated benefits.	Utilize the insurance department actuary or an independent actuary to perform an independent calculation of the reserves of supplemental and accelerated benefits. Verify that reserves are in accordance with SAP.
Policies subject to Principle-Based Reserving are not properly identified or exclusion testing is not appropriately conducted.	RV	VA AC PD	RA	Company conducts and reviews exclusion testing in accordance with Valuation Manual instructions.	Review company support and supervisory sign-off for exclusion testing.	Utilize a Department actuary, independent actuary or NAIC Actuarial Modeling support staff to conduct or reperform exclusion testing.
The life, A&H and deposit-type reserve and IBNR contract claim liability computations are not performed correctly or the selected estimates are unreasonable.	OP RV	AC VA	RA	The insurer has an established process that is consistent with the method adopted by the NAIC to calculate the life reserves on an annual basis. The insurer maintains a fully staffed, well-qualified actuarial department. Senior management uses internal or independent actuaries to conduct reserve analyses of all major lines on an annual basis.	Review the process in place (which may include performance of a walkthrough) to estimate the life reserves. Review the credentials, background and responsibilities of the insurer's actuarial department staff. Obtain actuarial reports to verify whether the insurer is using independent or in-house actuaries to perform the reserve calculations on all major lines of business	Utilize the insurance department actuary or an independent actuary to perform an independent estimate of the life reserves and IBNR contract claims liability. Perform analytical procedures to review the reasonableness of reserve calculations.

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Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
					annually and verify senior management review of reports from actuaries.	
				The actuarial calculations are subject to a peer review process**.**	If performed in-house, review and test the actuarial peer review process and related sign-offs**.**	
				The insurer's board of directors (or committee thereof) receives an annual presentation on the actuarial analysis process.	Review the meeting minutes of the board of directors (or committee thereof) to verify whether a presentation was given on the actuarial calculation process.	
				Management receives regular reports on key ratios and reviews unusual fluctuations on a timely basis to review reserves for adequacy.	Verify management review of reserve reporting and test the operating effectiveness of procedures in place.	
The methodologies utilized in PBR are not appropriate or the reserve computations are not performed correctly.	OP RV	AC VA	RA	The company has a formal process in place to develop and validate a model for use in PBR. Governance of the actuarial model includes consideration of: • Security Process • Software Change Process • Parameter Setting Process • Validation Process • Oversight of Overall Model Processes	Review evidence that the company followed its process in developing and validating its model for use in PBR. Review the credentials, background and responsibilities of the insurer's actuarial department staff in developing and validating the model used in PBR.	Utilize a Department actuary, independent actuary or NAIC Actuarial Modeling support staff to review and evaluate results (e.g. compare results of the standard portfolio, reasonableness in comparison with prior periods, etc.) of the insurer's modeling computations. Utilize a Department actuary, independent actuary or NAIC Actuarial Modeling support staff to recalculate reserves on

Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
				Model results have undergone peer review and are subject to reasonableness tests, such as: • The insurer manually calculates Net Premium Reserve (NPR) on selected policies. • The insurer does movement analysis ~~compares~~ comparing reserves per 1000 of face amount with prior periods. • The insurer performs sensitivity testing on key non-prescribed assumptions.	Ensure that company peer review process is in place and operating effectively.	selected policies.
The computation of reinsurance credits within life, A&H and deposit-type reserves are not performed correctly. (See also Examination Repository – Reinsurance Ceding Insurer.)	CR RV	AC VA CO	RA RRC	The reserving actuary calculates the reserve on a gross basis and determines the net basis by estimating the reinsurance credits and applying them to the gross reserve. The insurer applies reinsurance credits to life reserves by reviewing	Test the operating effectiveness of the insurer's process for reviewing the reserve analysis to determine whether life reserves have been estimated on a gross basis, including management approval and sign-off. Test the operating effectiveness of the insurer's process to estimate	Compare the annual financial statement net and gross incurred for consistency with reinsurance treaties in place at the insurer. Consider the reasonableness of reinsurance credits taken, based on a review of the

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Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
				reinsurance treaties in place at the insurer, as well as historical results.	reinsurance credits for life reserves, including management approval and sign-off.	insurer's reinsurance program and treaties in place. Compare the corresponding reserve held by the reinsurer with the credit taken by the insurer and identify all reasons for differences.
The insurer does not properly adjust the terminal reserve computation back to the reporting date.	OP RV	AC VA	RA	The insurer has a process in place whereby reserve computations are adjusted back to the reporting date.	Test the key controls surrounding the process by which reserve computations are adjusted back to the reporting date.	Utilize the insurance department actuary or an independent actuary to perform an independent estimate of the reserve adjustment back to the reporting date.
The initial reserves calculated by the actuary do not adequately reflect reserve liabilities.	OP RV	AC VA	RA	The insurer has a process in place by which it computes an asset adequacy test on the calculated life reserves. The insurer has a process in place to ensure that the correct assumptions and methodologies are used to estimate the adequacy of the life reserves. Management reviews the asset adequacy test for reasonableness of the reserve amount.	Test the key controls surrounding the process by which the reserve adequacy test is calculated. Test the key controls surrounding the assumptions and methodologies used to estimate reserve adequacy. Verify management review of asset adequacy test.	Utilize the insurance department actuary or an independent actuary to perform an independent estimation of the reserve adequacy test to determine whether the overall reserve liability is adequate.
Management books reserves that are materially different than the actuary's best estimate.	OP ST LG	VA ~~PD~~ AC	RA	The insurer has a process in place to ensure that reserves are recorded based on the actuary's best estimate, or documents an appropriate reason for any deviations.	Review management's guidelines regarding the recording of actuarially determined reserves. Verify that deviations from the actuary's best estimate are properly documented, if applicable.	Review the actuarial report, as well as the annual financial statement and other appropriate documentation, to determine whether the insurer has booked the actuary's best estimate.

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Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
				The board of directors (or committee thereof) compares the booked reserves to the amounts included in the actuarial report by receiving a report from the appointed actuary. The insurer's organizational structure limits the influence that management can have on the appointed actuary.	Review meeting minutes of the board of directors (or committee thereof) for evidence of a presentation and review of the actuarial report. Interview the appointed actuary during the planning phase of the examination to determine whether the insurer's organizational structure is appropriate in this area.	Review the documentation supporting a deviation from the actuary's best estimate for reasonableness, if applicable.
The insurer is not properly accounting for cash surrender value (CSV) on life (including annuities) contracts.	OP LG	OB/OW ~~PD~~ VA	RA	The insurer has policies in place to ensure the reporting of CSV on life (including annuities) contracts in accordance with SSAP No. 51.	Ensure the policies for the process used to report CSVs on life (including annuities) contracts is periodically reviewed and approved by management.	For a sample of life (including annuities) contracts with cash surrenders, determine whether the CSV is being properly reported.
Contract claim liabilities are not established or reviewed in accordance with the insurer's standards and applicable statutory guidelines.	RV OP ~~CR~~ LG	AC VA CO	RA	The insurer has a policy for recording contract claim liabilities and actuaries are involved in establishing and reviewing the policy. Contract claim liabilities are recorded in accordance with the insurer's policy, applicable statutory guidelines and within a specified time frame. Committees evaluate and strategize claim liabilities involving large or unusual	Obtain documentation supporting the insurer's contract claim liability policy to ensure actuary review and policy adequacy. For a sample of contract claim liabilities, determine whether contract claim reviews were performed and documented in accordance with the insurer's policy and applicable statutory guidelines. Obtain minutes and other meeting materials from the meetings of the committee	For a sample of contract claim liabilities, verify that the calculation is in accordance with the insurer's policy, applicable statutory guidelines, and are calculated on a timely basis. From the sample selected above, identify any claims included on the detail for which the liability recorded is not consistent with the contract terms. Identify claims that appear to have not been paid in a reasonable or fair time frame. Investigate the status

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Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
				loss contract claim determinations and/or settlements.	to determine whether the committee provided appropriate oversight.	of these claims/benefits with the insurer's management.* Verify that the claims/benefits liability is complete and properly recorded at year-end. Obtain a detail of resisted claims and claims closed without payment. Perform procedures to verify the grounds for the resisted claims. For a sample of contract claim liabilities meeting the criteria to go to a loss/benefits committee, determine whether the liabilities were referred to this committee.*
The insurer does not maintain an adequate ~~premium~~ deficiency reserve.	RV ~~RQ~~ OP	VA CO CM	RA	The insurer has a process in place to review for premium deficiencies on an annual basis in accordance with SSAP No. 54. Independent actuaries review and sign off on deficiency reserve calculations.	Review the process in place and verify key controls surrounding the calculation of premium deficiency reserves. Obtain the actuarial opinion and verify approval of deficiency reserve calculations.	Perform an analytical review of loss ratios. If necessary, utilize the insurance department actuary or an independent actuary to perform a detailed review or an independent calculation/estimate of the premium deficiency reserves.

EXAMINATION REPOSITORY – RESERVES/CLAIMS HANDLING (P&C)

Annual Statement Blank Line Items

Listed below are the corresponding Annual Statement line items that are related to the identified risks contained in this exam repository:

Losses
Loss Adjustment Expenses
Ceded Reinsurance Case Loss and Loss Adjustment Expense Reserves
Supplemental Reserve (*Title Companies*)

Relevant Statements of Statutory Accounting Principles (SSAPs)

All of the relevant SSAPs related to the property and casualty insurance reserving process, regardless of whether or not the corresponding risks are included within this exam repository, are listed below:

No. 5R Liabilities, Contingencies and Impairments of Assets – Revised
No. 54R Individual and Group Accident and Health Contracts
No. 55 Unpaid Claims, Losses and Loss Adjustment Expenses
No. 57 Title Insurance
No. 62R Property and Casualty Reinsurance – Revised
No. 63 Underwriting Pools
No. 65 Property and Casualty Contracts
No. 70 Allocation of Expenses

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Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
Other Than Financial Reporting Risks						
The board of directors (or committee thereof) is not involved in establishing and/or reviewing the insurer's overall reserving ~~practices~~policy.	OP RV ST	Other	RA	The insurer's board of directors (or committee thereof) has adopted and/or reviewed the insurer's overall reserving ~~practices~~policy. The board of directors (or committee thereof) regularly discusses reserving issues/levels and receives reports from the ~~appointed~~ Appointed ~~actuary~~Actuary. ~~The reports include an explanation of the reserving policy and methodology, as well as an analytical review of the insurer's reserves.~~ The insurer monitors and revises its reserving ~~practices~~ policy as needed.	Verify that the insurer has established an overall reserving ~~practices~~ policy that ~~have~~ has been adopted and/or reviewed by the board of directors (or committee thereof). Review board of directors (or committee thereof) minutes to ensure discussion of reserving. Verify that the minutes indicate that the Appointed Actuary reported to the board (or committee thereof) on the items within the scope of the actuarial opinion an identifies the manner of presentation. Obtain information on revisions made by the insurer to its reserving ~~practices~~ policy and verify the revisions were appropriately reviewed and/or approved by the board of directors (or committee thereof). ~~Verify that the insurer's reserving process was reviewed and/or approved by the board of directors (or committee thereof).~~	Obtain information on the insurer's overall reserving ~~practices~~ policy and forward it to the insurance department actuary or an independent actuary for review. Discuss with members of the board of directors (or committee thereof) their level of involvement in the monitoring of reserving ~~practices~~ policy.
Financial Reporting Risks						
New claims are not entered into the claims	RP LG	AC CT	RD	Segregation of duties exists between the claim	Observe that segregation of duties exists between the	Select a sample of items from the exception reports

Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
management system.		CO		notification and the input of claims data into the claims system. Control reports exist to ensure all claims reported to the insurer electronically or manually have been entered into the claims system. Exceptions are identified and resolved timely. The insurer reviews the Type II SOC 1 report and ensures compliance with user control considerations for any outsourcing companies that enter claims on behalf of the insurer.	claim notification and the input of claims data into the claims system. Obtain the exception report and ensure management review and exception resolution. Test the operating effectiveness of the automated claims posting process through reperformance and observation, which could include IT testing of batch totals to ensure completeness of transactions processed. Obtain documentation of the management's review of the Type II SOC 1 report.	and verify that the claim was appropriately accounted for.* Select a sample of claim and expense payments made subsequent to year-end to verify that claims were recorded in the proper period. Review the Type II SOC 1 report, including any bridge letters, to ensure there are no significant control deficiencies or internal control weaknesses related to processing new claims into the claims system.
Claims data is incomplete or incorrectly entered into the claims management system.	OP LG	AC CT CO EX	RD	Claims data is subject to independent verification or quality assurance (QA) reviews. The claims system has automated controls that will not allow a claim to be entered without a valid in-	Obtain documentation of independent claim verification or QA review. Ensure reviews performed address the completeness and accuracy of underlying claims information entered into the claims system. Test the operating effectiveness of automated controls (i.e., edit checks) through reperformance and	Perform data validation tests to verify the accuracy of claim information maintained in the claims system — such as coverage terms, demographic data, loss occurrence and/or loss report date, date of service, insured name, claim number and coverage period — by vouching the information to the claimant's insurance contract, claims form and

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Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
				force policy. The claims system has automated controls that will not permit continued processing until all pertinent claim data has been entered. Entering a valid active policy number will automatically populate select policy data. System edits will identify data that does not meet the predetermined criteria resulting in inclusion on a system generated exception report. Segregation of duties exists between individuals responsible for new claim set-up and those responsible for setting up new policies.	observation. Obtain the error report and ensure proper exception resolution. Test the operating effectiveness of authority restrictions through reperformance and observation. Obtain claims set-up and new policy set-up authorization listings and cross-reference the listings to ensure that there are no employees with conflicting authority.	any other underlying support. Scan the database(s) for internal inconsistencies, such as missing claim amounts, unusually small amounts and claims misclassified by type. In situations where adequate segregation of duties is not apparent, obtain data to determine whether any claims were set up by the same user who created the corresponding policy in the master file. If any instances are identified, investigate the claim to ensure the claim exists and is supported by underlying data.
The third-party administrators (TPAs) or managing general agents (MGAs) are not processing claims in accordance with the insurer's claims procedures as outlined in the TPA agreement.	LG OP RP	AC CM	RD	The insurer performs regular audits of its TPAs/MGAs to determine whether the insurer's claims-handling standards and additional contract provisions are being consistently followed by the TPA. Management obtains a Type II SOC 1 report for all TPAs and reviews the report to verify the TPA has adequate controls and that the insurer	Review audit reports and other documentation to determine whether the insurer provides sufficient oversight of its TPAs/MGAs. Verify that the insurer has obtained and reviewed each TPA's Type II SOC 1 report, if available. Determine whether the	Determine, by a review of selected claims, whether the insurer is settling its claims accurately and in accordance with the contract, based on information contained in the claim file. Review the Type II SOC 1 report to determine whether the controls outlined in the report are adequate to ensure that claims are being processed in accordance

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				is adhering to user control considerations. Management performs necessary reviews to comply with applicable state MGA regulations.	insurer is adhering to user control considerations. Obtain evidence of management's review of compliance with applicable state MGA regulations.	with the TPA agreement. Test for compliance with applicable state MGA regulations.
Claims are not being processed accurately and in accordance with the insurer's guidelines.	OP ST LG	AC CM CO	RD	The insurer has administrative policies and maintains a claims procedures manual that outlines the following requirements: • Proper application of deductibles. • Reserving and payment authority and approval levels. • File documentation and tracking. • Procedures for handling suspicious or fraudulent claims. • Compliance with the domiciliary state's fair claims practices laws and regulations. Paid losses are not to exceed policy limits, cover ineligible loss causes/types and/or apply to a policy period for which the insurer is not contractually responsible. Any consideration to pay a	Review the insurer's claims manual to determine appropriateness including management approval. Test the operating effectiveness of system edit checks to ensure procedures are implemented through reperformance and observation. Review assessments of the claims-handling process	Perform tests to determine whether claims were accurately processed in accordance with the claims procedures manual, approved authority limits and administrative policies, through review of the claimant's insurance contract, claims form and any other underlying support.* Review policyholder complaints and investigate significant issues. Review a sample of denied claims to ensure compliance with contract and timeliness provisions.

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Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
				loss that meets one or more of the aforementioned categories must be processed in accordance with the insurer's procedures. As part of the claims processing procedures, the insurer obtains adequate documentation before a claim is settled. Claims approval is subject to approved authority limits. A QA review is periodically performed for each claims processor to ensure compliance with the claims-handling policies.	performed by internal/external auditors, reinsurers and/or others for significant issues. Test the operating effectiveness of controls to ensure adequate documentation is obtained before payment is made. Test the controls in place to ensure that claims are approved in accordance with documented authority limits. Review documentation of QA reviews to determine whether the QA function is being executed as outlined in the insurer's policies. On a sample basis, reperform the QA testing to ensure that the testing was completed accurately.	
Claims under claims-made liability policies are improperly accepted (or rejected) by the claims adjusters.	RP RV OP ST	AC CM	RD	The insurer has a policy in place whereby coverage is automatically triggered under claims-made liability policies when a claim is first made during the policy period (as long as it did not occur prior to the retroactive policy date specified). A QA review is periodically	Perform a walkthrough to verify that the adjuster properly applies tail coverage to the claim and reallocates the claim to the correct policy year. Review documentation of	Perform data validation testing to ensure that claims under claims-made liability policies are being properly administered.

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Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
				performed for each claims processor to ensure compliance with claims-handling policies	QA reviews to determine whether the QA function is being executed as outlined in the insurer's policies. On a sample basis, reperform the QA review to ensure the testing was accurately completed.	
The claims data utilized by the actuary to estimate reserves does not correspond to the data in the insurer's claims system and to the data in the insurer's accounting records.	OP RV	AC CO	RD	The insurer has established procedures to reconcile actuarial data to the insurer's claims system, the data in the insurer's accounting records and appropriate annual financial statement schedules and/or exhibits. Such reconciliations are reviewed by supervisory personnel. Inventories of reported and unpaid claims are maintained and periodically reconciled to the general ledger. The company's internal Appointed Actuary reconciles the claims data used in the analysis to Schedule P. The insurer has established procedures to prepare complete and accurate data for actuarial review.	Review the insurer's reconciliation reports of actuarial data to the insurer's claims system and the insurer's accounting records. Ensure evidence of supervisory review. Review the insurer's reconciliation of reported and unpaid claims to the general ledger. Review the company's internal Appointed Actuary's reconciliation of the claims data used in the analysis to Schedule P. Test the operating effectiveness of the insurer's established procedures to prepare the claims data for actuarial review.	Test reconciling items within the reconciliations for appropriateness. Reconcile the insurer's actuarial report for losses and loss adjustment expenses to supporting insurer reports, general ledger, and annual financial statement schedules and exhibits as of the valuation date. Independently reconcile the actuarial data to Schedule P.

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Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
Reinsurance is not properly taken into account in accumulating claims data. (See also Examination Repository – Reinsurance Ceding Insurer)	RV	AC CO	RD	The insurer has established procedures to prepare the claims data for actuarial review in accordance with the insurer's reinsurance treaties.	Review the insurer's reconciliation reports of actuarial data to the insurer's claims system, reinsurance reports, and accounting records. Test the operating effectiveness of the insurer's established procedures to include loss data from assumed reinsurance treaties within the claims data for actuarial review.	Test reconciling items relating to reinsurance loss data for appropriateness. Verify assumed reinsurance loss data accumulated for actuarial review by comparing to the data provided by the ceding insurer for completeness.
Initial case reserves are not established or reviewed in accordance with the insurer's standards.	RV CR	AC VA CO	RA	The insurer has a case reserving philosophy, and qualified actuaries are involved in establishing and reviewing the reserving policy. Initial reserves are made in accordance with the insurer's reserving philosophy and within a specified time frame. Claims adjusters/ supervisors are required to review significant initial case reserves on a timely basis and make adjustments as necessary. The insurer verifies that the TPAs that process claims follow the insurer's	Obtain documentation supporting the insurer's reserving philosophy. Review the reserving philosophy for actuarial review and policy adequacy. For a sample of loss reserves, determine whether loss reserve reviews were performed and documented in accordance with the insurer's policy. Obtain periodic new claims reports and verify the insurer reviews significant initial case reserves and makes adjustments, if necessary, in a timely manner.	For a sample of reserves, verify that the calculation is in accordance with the reserving philosophy and that reserves are calculated on a timely basis. For a sample of reserves meeting the criteria to go to a claims committee, determine whether the reserves were referred to this committee.*

Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
				guidelines for setting case reserves on reported claims. Committees are formed to evaluate and strategize claims involving serious injuries, complex claims law, and large or unusual loss reserve determinations or settlements.	 Obtain minutes and other meeting materials from the meetings of the committee to determine whether the committee provided appropriate oversight.	
Case reserves are not updated accurately.	RV CR	CO VA	RA	The insurer has a policy requiring open claims to be reviewed regularly. When new information is received, case reserves are reviewed and adjusted, if necessary. The claims management system generates analyses or reports that identify reserve increases and decreases, an outstanding reserve list, an outstanding reserve list by claims adjuster and a reserve release report. These reports are reviewed/ monitored by the claims manager for reasonableness.	From a sample of case reserves, determine whether the reserves are updated regularly and are appropriately updated when new information is received. Obtain copies of the reserve reports, noting management approval.	Select a sample of paid claims and compare the final overall claims settlement with the case reserve to determine whether the reserves are adequate and/or updated accurately.* Verify that the information contained in management reserve reports is accurate and complete and determine whether the appropriate analysis is being used to evaluate the reserves.
The insurer is not properly recording case reserves (assumed or ceded) for contracts subject to reinsurance.	RV CR LG	CO VA AC	RA	The insurer has policies in place to verify that case reserves subject to reinsurance are valid and accurate (within contract time frame, covered under the contract, etc.).	Review the insurer's policies to determine appropriateness, noting management approval. Review documentation of the insurer's review of claim validity.	Utilize NAIC Examination Jumpstart reports to determine whether case reserves recorded by the insurer agree with the case reserves of the assuming (ceding) insurer.
~~The assumptions and methodologies used~~ Actuarial analyses	RV	VA AC PD	RA	The insurer's actuarial analyses use~~s consistent assumptions and~~	Gain an understanding of the ~~insurer's assumptions and methodologies~~ methods	Review the actuarial analyses' methodologies for appropriateness and

Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
relied upon by the insurer's management in determining carried reserves are not based on~~accurate and~~ appropriate methods and/or reasonable assumptions.				~~methodologies~~ appropriate methods and reasonable assumptions that have been based on historical results (to the extent appropriate), adequately documented, approved by senior management (where appropriate) and in accordance with statutory accounting principles and applicable state statutes and/or regulations. ~~Senior management uses internal or independent actuaries to conduct reserve analyses of all major lines of business on an annual basis.~~ Actuarial analys~~i~~es relied upon by management in determining carried reserves ~~is~~ are subject to a peer review process. Management receives regular reports on loss/LAE reserve levels, loss/LAE ratios (including incurred but not reported (IBNR)) by line or class of business grouped by accident year and calendar year, as well as other key ratios, and reviews unusual fluctuations on a timely basis to review	and assumptions used in the analyses ~~and~~ compared with prior periods. ~~Verify that senior management signs off on assumptions and methodologies used by the insurer, including any changes.~~ ~~Verify senior management review of reports from actuaries and that reports include reserve analyses of all major lines of business.~~ If performed in-house, review and test the actuarial peer review process and related sign-offs. Verify management review of loss/LAE reserve reporting and test the operating effectiveness of procedures in place. Review the credentials, background and responsibilities of the insurer's actuarial function	assumptions ~~and methodologies~~ for reasonableness, ~~appropriateness and accuracy~~ with assistance from the insurance department actuary or an independent actuary. Verify that reserving methodologies and assumptions are in accordance with the relevant SSAPs related to P&C reserving, as well as applicable statutes, regulations, pronouncements and/or bulletins. Review prior history of loss development, as well as subsequent loss development data to analyze the appropriateness of methodologies and reasonableness of assumptions ~~and methodologies~~. Determine whether the appropriate disclosures have been made in the Notes to the Financial Statements for the changes in the insurer's reserve methodologies. Review actuarial reports and compare reports to prior periods. Investigate

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Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
				reserves for adequacy. The insurer utilizes a fully staffed, well-qualified actuarial function that is under the direction of an actuary that has an Accepted Actuarial Designation, as defined in the NAIC Statement of Actuarial Opinion Instructions, ~~fellow (or associate) of the Casualty Actuary Society (FCAS)~~ and is experienced in the lines of business written by the insurer. The reserving actuarial unit's responsibilities are segregated from the pricing actuarial unit, but there is regular communication between the two units. The insurer's ~~organizational structure limits the influence that~~ management ~~can have on~~ does not inappropriately influence the methods, assumptions, or conclusions of the ~~appointed actuary~~Appointed Actuary.	(internal or external) for appropriateness. Request and review the insurer's organizational chart and job descriptions to determine whether the functions are separate and distinct. Interview the ~~appointed actuary~~Appointed Actuary during the planning phase of the examination to ~~determine whether the insurer's organizational structure is appropriate in this area~~ascertain the degree of influence the insurer's management has on the Appointed Actuary's work.	significant variations. Utilize the insurance department actuary or an independent actuary to perform an independent calculation/estimate of the loss/LAE reserves for significant reserve segments with volatility if necessary. Review the external auditor's reserve level calculations when available and Appointed Actuary's report; independent tests should only be conducted if other tests are not conclusive. Review correspondence related to peer review for appropriate depth of review. Compare the ~~opining actuary's~~ Appointed Actuary's assumptions and estimates with those in other available actuarial analyses. Determine whether the Actuarial Opinion was materially changed by the ~~appointed actuary~~Appointed Actuary after meeting with insurer management.
Catastrophe-type (CAT) claims or large or significant exposure type claims data are not separately	OP RV	AC VA	RD RA	The insurer has established procedures to prepare the claims data for actuarial review by extracting CAT claims or large or	Test the operating effectiveness of the insurer's established procedures to prepare the claims data for actuarial	Obtain a detailed download of all claim transactions during the examination period. Utilize audit software to verify that

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Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
identified and evaluated from other claims.				significant exposure type claims, for a separate reserve analysis.	review. Review the insurer's actuarial reserve analysis for incorporation of a separate review of CAT claims or large or significant exposure type claims.	claims data appropriately distinguishes CAT claims or large or significant exposure type claims and that these claims have been extracted from the general claims data and presented separately to the actuary.
Changes in the legal environment or changes in the insurer's underwriting, case reserving or claims-handling processes are not appropriately considered within the insurer's reserving assumptions and methodologies.	OP RV ST	VA PD AC	RA	The insurer has procedures in place ~~for its legal department~~ to monitor and communicate changes in the legal environment (e.g., changes in case law, award amounts, trends in the number of claims being litigated) are being taken into consideration by ~~the reserving unit~~ management in a timely manner. The insurer has procedures in place for the underwriting, case reserving and claims-handling units to communicate changes in their processes to the reserving unit in a timely manner.	Review the insurer's process to monitor changes in the legal environment that may affect the reserving process and to reflect changes appropriately in management's determination of carried reserves. Review evidence of communication between the reserving unit and other relevant insurer units.	Through a review of ~~the actuarial reports~~documentation supporting management's carried reserves, determine whether changes in the legal environment or changes in the insurer's internal processes have been properly incorporated ~~in the insurer's reserving assumptions and methodologies~~.
The loss and loss adjustment expense (LAE) reserve computations are not performed correctly or the selected estimates are unreasonable.	OP RV	AC VA	RA	The insurer has an established process (although assumptions and methodologies may change) to estimate the loss reserves on an annual basis. The insurer has established processes to estimate the defense and cost	Review the process in place (which may include performance of a walkthrough) to estimate the loss reserves. Review the processes (which may include a walkthrough) in place to	Utilize the insurance department actuary or an independent actuary to perform an independent estimate of the loss reserves. Utilize the insurance department actuary or an independent actuary to

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				containment (DCC) and the adjusting and other (AO) loss adjustment expense reserves on an annual basis. The insurer maintains a fully staffed, well-qualified actuarial department that is under the direction of a fellow (or associate) of the Casualty Actuary Society (FCAS) and is experienced in the lines of business written by the insurer. Senior management uses either internal or independent actuaries to conduct reserve analyses of all major lines on an annual basis. The actuarial calculations are subject to a peer review process. The insurer's board of directors (or committee thereof) receives an annual presentation on the actuarial analysis process. Management receives regular reports on loss ratios (including IBNR) by line or	estimate both the DCC and AO loss adjustment expense reserves. Review the credentials, background and responsibilities of the insurer's actuarial department staff for appropriateness. Obtain actuarial reports to verify insurer is using either independent or in-house actuaries to perform the reserve calculations on all major lines of business annually and verify senior management review of reports from actuaries. If performed in-house, review and test the actuarial peer review process and related sign-offs. Review meeting minutes of the board of directors (or committee thereof) to verify that a presentation was given on the actuarial analysis process. Verify management review of loss reserve reporting and test the operating	prepare an independent estimate of LAE. Perform analytical procedures to review the reasonableness of loss reserve estimates.

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Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
				class of business for accident year and calendar year, as well as other key ratios, and reviews unusual fluctuations on a timely basis to review reserves for adequacy.	effectiveness of procedures in place.	
~~The computation of reinsurance credits within loss reserves are not performed correctly.~~ ~~(See also Examination Repository – Reinsurance Ceding Insurer.)~~	~~CR~~ ~~RV~~	~~AC~~ ~~VA~~ ~~CO~~	~~RA~~	~~The reserving actuary calculates the reserve on a gross basis and determines the net basis by estimating the reinsurance credits and applying them to the gross reserve.~~ ~~The insurer applies reinsurance credits to loss reserves by reviewing reinsurance treaties in place at the insurer, as well as historical results.~~	~~Test the operating effectiveness of the insurer's process for reviewing the reserve analysis to determine whether loss reserves have been estimated on a gross basis, including management approval and sign-off.~~ ~~Test the operating effectiveness of the insurer's process to estimate reinsurance credits for loss reserves, including management approval and sign-off.~~	~~Compare the annual financial statement's net and gross incurred and paid loss presentation for consistency with reinsurance treaties in place at the insurer.~~ ~~Consider the reasonableness of reinsurance credits taken, based on a review of the insurer's reinsurance program and treaties in place.~~ ~~Utilize the insurance department actuary or an independent actuary to review the reasonableness of the ceded reinsurance estimates contained in the opining actuary's report.~~
~~Management books reserves that are materially different than the actuary's best estimate.~~ Management does not have reasonable support for its carried reserves.	OP ST LG	VA PD	RA	The insurer has a process in place~~to ensure that reserves are recorded based on the actuary's best estimate, or documents an appropriate reason for any deviations~~ for determining carried reserves, and management is able to explain its selection.	Review management's guidelines regarding the ~~recording of actuarially determined loss~~determination of carried reserves. Verify that any material changes from the prior year's reserves and any material ~~deviations~~ differences between ~~from~~ carried reserves and the	~~Review the actuarial report, as well as the annual financial statement and other appropriate documentation, to determine whether the insurer has booked the actuary's best estimate.~~ Review the documentation supporting management's

Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
				The board of directors (or committee thereof) reviews management's best estimate of ~~booked~~ reserves and challenges such estimates based upon reports received, including the actuarial report from the ~~appointed actuary~~Appointed Actuary. ~~The insurer's organizational structure limits the influence that management can have on the appointed actuary.~~	~~actuary~~Appointed Actuary's ~~best~~ point estimate are properly documented~~, if applicable~~. Review meeting minutes of the board of directors (or committee thereof) minutes for evidence of a presentation and review of information supporting management's best estimate of the booked reserves (~~i.e.~~ e.g., the actuarial report). ~~Interview the appointed actuary during the planning phase of the examination to determine whether the insurer's organizational structure is appropriate in this area.~~	carried reserves, including management's analysis of the reasonableness of the reserve estimates. ~~a deviation from the actuary's best estimate for reasonableness, if applicable.~~
The insurer does not maintain an adequate premium deficiency reserve.	RV RQ OP	VA CO CM	RA	The insurer has a process in place to review for premium deficiencies on an annual basis in accordance with SSAP No. 5~~4~~3. ~~Independent actuaries~~ Qualified personnel perform, review, and sign off on premium deficiency reserve calculations.	Review the process in place and verify key controls surrounding the calculation of premium deficiency reserves. Obtain the ~~actuarial opinion and verify approval of~~premium deficiency reserve calculations, and verify approval and sign-off.	Perform an analytical review of loss ratios. If necessary, utilize the insurance department actuary or an independent actuary to perform a detailed review or an independent calculation/estimate of the premium deficiency reserves.

EXAMINATION REPOSITORY – UNDERWRITING

Annual Statement Blank Line Items

There are no Annual Statement line items directly related to the underwriting process; however, policies underwritten and rate calculations may impact line items associated with areas such as premiums and reserves.

Relevant Statements of Statutory Accounting Principles (SSAPs)

All of the relevant SSAPs related to the underwriting process, regardless of whether or not the corresponding risks are included within this exam repository, are listed below:

No. 6 Uncollected Premium Balances, Bills Receivable for Premiums, and Amounts Due from Agents and Brokers (*All Lines*)
No. 51R Life Contracts (*Life Companies*)
No. 53 Property Casualty Contracts – Premiums (*P&C Companies*)
No. 54R Individual and Group Accident and Health Contracts (*Health Companies*)
No. 65 Property and Casualty Contracts (*P&C Companies*)

--Detailed Eliminated to Conserve Space--

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Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
Other Than Financial Reporting Risks						
The company has not established appropriate rates for its long-term care insurance (LTCI) policies	ST PR/UW	Other	UPSQ	The insurer utilizes a fully staffed, well-qualified actuarial pricing function that has significant experience and expertise in LTCI. The company conducts experience studies and utilizes credible data as the basis for its rate assumptions. The company files accurate and complete rate increase requests with all departments in a timely manner.	Review the credentials, background and responsibilities of the insurer's actuarial pricing function for appropriateness. Select a sample from experience studies to verify support for and consistency with rate assumptions used by the company. Communicate with department staff in charge of LTCI rate review requests (in multiple states if appropriate) to assess the quality and timeliness of the insurer's rate requests.	Perform analytical procedures to review the insurer's profitability and history of indicated rates vs. selected/filed rates to evaluate the sufficiency of premium rates. Compare the premium rates utilized by the insurer to industry averages and those of competitors (if known) for reasonableness. If rates have been subject to insurance department approval, consider whether reliance can be placed on this work. If deemed necessary, utilize the insurance department actuary or an independent actuary to perform a review or independent calculation of premium rates. Compare rate increase assumptions to reserve assumptions, (for example review the rate requests and compare against AG51 filings) to ensure that assumptions used for pricing and reserving do not materially conflict. ~~are similar in nature~~ . Track the progress of the

Identified Risk	Branded Risk	Exam Asrt.	Critical Risk	Possible Controls	Possible Test of Controls	Possible Detail Tests
						company in achieving its rate increase goals by comparing rate increases received against those requested. If necessary, evaluate the potential impact of rate request denials on the future solvency position of the insurer.

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EXHIBIT M
UNDERSTANDING THE CORPORATE GOVERNANCE STRUCTURE

---**Detail Eliminated to Conserve Space**--

Management should provide effective oversight of the insurer's actuarial function in evaluating and providing advice to the insurer in respect to technical provisions, premium, pricing, and reserving activities, and compliance with related statutory and regulatory requirements. While various components of an actuarial function can be provided internally or outsourced to an external third party, the following elements should be considered in understanding and assessing the insurer's governance practices in this area:

1. Are individuals within the insurer's actuarial function suitable for their respective roles? Do they possess the necessary competence and integrity for their positions?
   a. Does the insurer's appointed actuary maintain current an Accepted Actuarial Designation (Property/Casualty) or actuarial credentials with an appropriate professional organization (e.g., ~~FCAS,~~ MAAA, etc.)and otherwise meet the definition of a Qualified Actuary, as stated in the NAIC Statement of Actuarial Opinion Instructions?
   ~~b. Does the appointed actuary have experience in the lines of business written by the company?~~
   ~~c. Do others within the company's actuarial function have the appropriate knowledge, experience and background to function in the roles assigned to them?~~
   b. If the company has an internal actuarial function, is it appropriate for the company's size, complexity, and lines of business written?
      i. Do those within the company's actuarial function have the appropriate knowledge, experience, and background to function in the roles assigned ot them?
      ii. Does the organizational chart indicate appropriate lines of reporting for the actuarial function?
   c. If the company outsources any part of its actuarial function, is it appropriate for the company's size, complexity, and lines of business written?
      i. Has management determined that the actuary has the appropriate knowledge, experience, and background to function in the assigned role?
      ii. What oversight is the company performing, and who at the company is responsible for this task?

2. Does the insurer's actuarial function provide advice on actuarial matters to management as appropriate based on the size and complexity of the entity? Key components include:
   a. The insurer's actuarial and financial risks.
   b. The insurer's current and prospective solvency position.
   c. Risk-assessment and risk-management policies and controls relevant to actuarial matters or the financial condition of the insurer.
   d. Distribution of policy dividend or other benefits.
   e. Underwriting policies.
   f. Reinsurance arrangements.
   g. Product development and design, including the terms and conditions of insurance contracts.
   h. The sufficiency and quality of data used in the calculation of technical provisions.
   i. Risk modeling and use of internal models in risk management.

3. Does the insurer have appropriate segregation of duties between its actuarial function and executive management to ensure that:
   a. ~~Recorded reserves reflect an appropriate actuarial estimate (P&C and Health).~~Actuarial analysis is considered by management in determining carried reserves.
   ~~b. The company books the actuary's best estimate each year (P&C).~~
   ~~c.~~b. If the company's recorded reserves differ significantly from the actuary's ~~best~~ point estimate, the rationale for such deviation is appropriately documented and presented to the board of directors (P&C).

~~d.~~c. The company's appointed actuary has submitted a report to the Board of Directors on reserve adequacy (All Lines)?

Sample Interview Questions for the Chief Actuary

Experience and Background
- How has your professional experience and background prepared you to be the Chief Actuary for this company?

Duties and Responsibilities
- Briefly describe your duties and responsibilities.
- How does management establish objectives, and how is the achievement of those objectives monitored?
- How is your performance evaluated? Is it based on the performance of the company?

Reporting Structure
- Describe the reporting structure of the actuarial function, including to whom you report, as well as those reporting to you.
- Is there a reserving committee?
  - How is it organized and who are its members?
  - How are differences resolved?
- Describe your interaction with the CFO/CEO/BOD.
  - Do you provide them with any specific reports?
- Do the board/audit committee members demonstrate an understanding of the variability inherent in the reserves?
- How does the board/committee oversee the application of Principle Based Reserving (if applicable)?

Ethics
- Does the company have a code of conduct/ethics in place? Is it enforced? Approved?
- Explain management's commitment to ethics and explain how that commitment is conveyed to employees.
- Do you have any knowledge or suspicion of fraud within the company?

Risk Areas
- How are key legal and regulatory risks faced by the company identified and monitored?
  - What are the key prospective risks the company faces?
  - How are these risks communicated to senior management and throughout the company?
- Have there been changes in the appointed actuary in recent years and, if so, how often have such changes occurred and why?
- What is the current reinsurance program? Describe any changes over the past five years.
- Describe the company's process to establish Principle Based Reserves.
  - Does the company have credible experience or experience studies to substantiate the model assumptions?
  - Does the company use a vendor supplied or internally developed Cash Flow Model?

Risk Mitigation Strategies (Internal Controls)
- What is the formal procedure for reporting on risk management to senior management and the board.
- What controls are in place to ensure reserving guidelines are followed?
- Who determines which reserves will be booked in the financial statements quarterly and/or annually?
  - ~~Does the company book to the actuary's point estimate, or is there a monitored gap?~~
- How often are full reserve analyses performed?
- Does the company book to the actuary's point estimate, or is there a monitored gap?
- Is the actuarial opinion signed by a company actuary or a consultant?
- Does the company use commercial software or "homegrown" spreadsheets? What controls are in place to check for errors?
- How are pricing and underwriting monitoring integrated into the reserving process?
- Is there a peer review of the reserving actuary's work? If so, who performs it?
- How much reliance does the appointed actuary place on the work of others?
- Describe the controls in place over the PBR processes.
- Has the company instituted any new controls as a result of the implementation of Principle Based Reserving (if applicable)?

- Describe the modeling controls in place supporting the Principle Based Reserving processes (e.g. model validation, changes in modeling assumptions, etc.).
- If the company writes long-term care insurance, consider the following questions:
  - Describe how applicable actuarial guidelines (e.g., Actuarial Guideline 51) impact the company's rates and reserves.
  - Describe the relationship between the actuarial assumptions used in rate filings versus those used for annual statement reporting. Explain any difference in assumptions, if applicable.
  - Describe the relationship between the actuarial assumptions underlying projections versus those used in asset adequacy analysis. Explain any difference in assumptions, if applicable.
  - Describe plans for future rate increase requests and/or the status of current rate requests.

Corporate Strategy

- Give a general description of the company's reserving philosophy.
- Explain what types of tools or reports you utilize to evaluate actuarial decisions.

Other Topics

- What is the quality of the actuarial report, with respect to completeness and clarity of documentation?
- What actions have been taken to apply PBR methodologies? (*Life Insurers Only*)
  - How are system capabilities considered in preparation for PBR implementation?
  - What system changes were made to apply PBR?
  - How are staffing needs, appropriate expertise and availability of effective training evaluated in preparation for PBR implementation?
  - What changes to staffing and training were made to apply PBR?
  - Discuss management's commitment to successful implementation of PBR.

From: Milford, Matthew
To: Henning, Bailey
Subject: RE: [External] FW: FEHTG Exposures - Comments Due 11/4/20
Date: Friday, October 30, 2020 2:06:27 PM

CAUTION: This email originated from outside of the organization. Do not click links or open attachments unless you recognize the sender and know the content is safe.

Good afternoon Bailey,

We have one comment on the documents you provided:

The only comment we have relates to the following P&C risk statement:

The claims data utilized by the actuary to estimate reserves does not correspond to the data in the insurer's claims system and to the data in the insurer's accounting records.

An Appointed Actuary can be internal or external…we think this would be an appropriate control when appointed actuary is a company employee, but not appropriate when the actuary is external. As currently written, we fear that examiners can overlook this difference.

We offer a suggestion to revise the wording for the control to clarify, as follows:

"The company's internal Appointed Actuary reconciles the claims data used in the analysis to Schedule P."

Thank you for your consideration.

Matthew Milford, CFE | Acting Director
Bureau of Financial Examinations
Pennsylvania Insurance Department
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November 4, 2020

Ms. Susan Bernard (CA)
Financial Examiners Handbook (E) Technical Group
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

Via e-mail: bhenning@naic.org

Re: Financial Examiners Handbook (E) Technical Group Exposure of Changes to Financial Examiners Handbook (10/5/20)

Dear Ms. Bernard:

On behalf of America's Health Insurance Plans (AHIP),[1] I appreciate the opportunity to provide comments regarding updates to the Financial Examiners Handbook, which were exposed by the National Association of Insurance Commissioners (NAIC) Financial Examiners Handbook (E) Technical Group (FEHTG) during its Oct. 5 call.

AHIP and their member companies appreciate the general intent of the updates and exposure that was discussed by FEHTG. However, AHIP would like to suggest some modifications to select language, specifically language added as Subsection F in the exposed document:

Section titled "F. Long-Term Care Insurance (LTCI) Reserves Overview" (beginning on page 58):

- The first sentence of the section provides a definition of LTCI that appears to be limiting by saying LTCI is coverage providing assistance with activities of daily living. We recommend using a definition for LTCI that is more consistent with the NAIC's Long-Term Care Insurance Model Act.

  The NAIC Model Act uses the following definition: "Long-term care insurance" means any insurance policy or rider advertised, marketed, offered or designed to provide coverage for not less than twelve (12) consecutive months for each covered person on an expense incurred, indemnity, prepaid or other basis; for one or more necessary or medically necessary diagnostic, preventive, therapeutic, rehabilitative, maintenance or personal care services, provided in a setting other than an acute care unit of a hospital.

- The third paragraph of this section address reinsurance and in a couple of places makes the statement that reinsurers/contracts cannot drive rate increases. While this is often the case, this is not an absolute. We suggest revising the paragraph as follows:

[1] AHIP is the national association whose members provide coverage for health care and related services to hundreds of millions of Americans every day. Through these offerings, we improve and protect the health and financial security of consumers, families, businesses, communities, and the nation. We are committed to market-based solutions and public-private partnerships that improve affordability, value, access, and well-being for consumers. Visit www.ahip.org for more information.

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> *"These same risks also affect reinsurers because the reinsurance contract may not arbitrarily allow for ceded premium increases. Additionally, in order to effectuate a true transfer of risk, the reinsurer may not have the ability to require the direct writer to request rate increases."*

Sub-Section F. 2. b. titled "b. Long-Term Care Insurance" (beginning on page 59):

- The last sentence of this section notes that "mortality, lapse, and interest rate factors become observable and credible during the early premium-paying years." We do not believe this to necessarily be correct. For example, ultimate lapse and mortality assumptions may not become evident for many LTC blocks for several years, after the impacts of underwriting wear off. In addition, while early year interest rate factors are observable, these factors are not necessarily reflective of the long-term interest rate factors that a block of insurance will experience. We would suggest removing this sentence.

Sub-Section Titled F. 2. e. "e. Rate Increase Factors" (beginning on page 60):

- We have significant concerns with this section as written – in particular with the example used that seems to indicate that it is reasonable for states to not approve rate increases that are based upon credible experience of a carrier's other LTC blocks. We believe that the intent of this section is to help provide the state examiner/analyst with guidance needed to evaluate the appropriateness of a company's rate increase assumptions if the company's LTC reserve adequacy is dependent upon such rate increases. As such, we would suggest that the current wording in the exposure draft for this sub-section be deleted and replaced with something along the following lines:

> *"If a company's reserve adequacy testing is dependent upon upcoming LTC rate increases, the state insurance department staff performing reserve valuation will want to evaluate the company's assumptions for reasonableness. The company's rate increase assumptions and documentation should be consistent with the requirements specified in Actuarial Guideline 51 related to rate increase plans. The state insurance department staff performing reserve valuation may wish to coordinate and communicate with the state's rate review staff to help evaluate the appropriateness and reasonableness of the company's assumptions."*

Lastly, there is language listing current Sections A through E at the top of page 53 of the pdf. We presume that the intention would be to add the new section "F. Long Term Care Insurance (LTCI) Reserve Reviews" to this list.

It appears that the proposed Subsection F language is virtually identical to recently proposed language additions exposed by the Financial Analysis Solvency Tools (E) Working Group for inclusion in the Financial Analysis Handbook. Please note that AHIP has submitted similar comments on that draft as well. We recommend that the two handbooks be consistent regarding any changes to this additional language.

We thank you for your consideration of these comments and would be happy to address any questions the Technical Group may have.

Sincerely,

Ray Nelson, Consultant
America's Health Insurance Plans

cc: Heather Jerbi - AHIP

November 4, 2020

Susan Bernard
California Department of Insurance
Chair, Financial Examiners Handbook (E) Technical Group
National Association of Insurance Commissioners

Re: Financial Examiners Handbook (E) Technical Group Exposure Drafts

Dear Ms. Bernard:

The American Property Casualty Insurance Association (APCIA)[1] appreciates the opportunity to comment on these proposed revisions to the NAIC's Financial Condition Examiners Handbook. Our comments address two portions of the exposed drafts, the Reinsurance Revisions and the P&C Reserves Repository.

Reciprocal and Qualified Jurisdictions

We appreciate the addition of paragraph 6, which addresses the 2019 revisions to the *Credit for Reinsurance Model Law (#785) and the Credit for Reinsurance Model Regulation (#786)* which extend the ability for U.S. ceding reinsurers to receive credit for reinsurance ceded to reinsurers from Reciprocal Jurisdictions without collateral requirements. Our comments apply to the following language: "(3) a qualified jurisdiction as determined by the commissioner." We are concerned that this language does not include reference to the additional requirements specified in the Model Law and Model Regulation that are needed for a qualified jurisdiction to be designated as a Reciprocal Jurisdiction. We suggest that the paragraph be amended to state: "(3) a jurisdiction that has been designated by the commissioner as a qualified jurisdiction and having met any additional requirements specified by regulation."

P&C Reserves Repository

We have the following comments on the Repository:

- In the Possible Test of Controls column on page 21, we would argue that an insurer's Board should not be reviewing the reserving "process". That is a technical detail that the Board should not be involved in. The Board should be relying on the Appointed Actuary for that control, as the actuarial opinion requires the actuary to evaluate whether the reserves are reasonable, and potentially to include a review of how they are set.

[1] APCIA is the primary national trade association for home, auto, and business insurers. APCIA promotes and protects the viability of private competition for the benefit of consumers and insurers, with a legacy dating back 150 years. APCIA members represent all sizes, structures, and regions—protecting families, communities, and businesses in the U.S. and across the globe.

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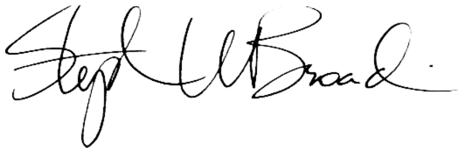
- On the top of page 29 the "Possible Controls" columns contains language that says the actuarial analysis uses "appropriate methods and reasonable assumptions that have been … approved by senior management …". This phrase is ambiguous. One of our members' actuaries commented that "I can see management approving some of the assumptions, but the methods and some of the assumptions are probably outside the expertise of senior management." We do not have language to propose here, but caution against applying that language too literally and broadly.
- At the bottom of page 30 in the "Possible Detail Tests" column, we suggest amending the language to read "Determine whether the Actuarial Opinion was changed materially by the Appointed Actuary after meeting with insurer management."

We look forward to discussing our comments with you and the Working Group.

Sincerely,



Stephen W. Broadie
Vice President, Financial & Counsel

DRAFT

November 4, 2020

Ms. Susan Bernard, Chair
Financial Condition Examiners Handbook (E) Technical Group
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

Attn: Ms. Bailey Henning, NAIC Examination Coordinator via electronic mail filing

RE: October 5, 2020, Financial Handbook Exposures

Dear Ms. Bernard:

We appreciate the opportunity to provide comments in response to the Financial Condition Examiners Handbook ("Handbook") that were exposed during the recent conference call held on October 5, 2020. Our comments will be given by identifying the subject heading and page of the exposure materials that were distributed by NAIC staff on October 8, 2020.

HEALTH RESERVES REPOSITORY

- Page 5, "Annual Statement Blank Line Items": "Premium Deficiency Reserves" ("PDRs") is not actually a separate line item. On Page 3 (Liabilities, Capital and Surplus), PDRs are included as part of Line 4, "aggregate health policy reserves"; and on Underwriting and Investment Exhibit Part 2D, which gives the details of the policy reserves, PDRs are included in Line 2, "additional policy reserves." There is a footnote on the latter exhibit that discloses the amount of any PDR, but that is not what anyone would normally think of as a line item. The PDRs are already included in the fourth line item listed, "Aggregate Health Policy Reserves." Listing them as a separate line item is misleading.
- Page 5, "Annual Statement Blank Line Items": The seventh line item listed, "Unearned Premium Reserves," should be "Property/Casualty Unearned Premium Reserves," which is the label for Line 6 on Page 3 of the Annual Statement. Health unearned premium reserves are included in the aggregate health policy reserves (Page 3 Line 4), and life unearned premium reserves are included in the aggregate life policy reserves (Page 3 Line 5).
- Page 12: The change in the Identified Risk from "Case reserves ..." to "Claim reserves ..." is a little confusing, as the two are not the same. While some of the Possible Controls, Possible Tests of Controls, and Possible Detail Tests are applicable to both, some are specific to case reserves. It seems that it would be

better to address case reserves as in the past, and create a new item for claim reserves more generally.

- Page 19: There is a note under "Identified Risk" that says, "It may also be appropriate to consider reserves for insufficient administrative fees for self-insured contracts." We do not believe this is actually a statutory accounting requirement, at least explicitly; and if the requirement is considered to stem from GAAP, it would not necessarily be comparable to the statutory PDR requirement. It is not clear what the result of the "consideration" is expected to be. We suggest removing the note.

LIFE RESERVES REPOSITORY

- Page 35: The Annual Statement Blank Line Items include the Liability for Deposit-Type Contracts. Therefore, the Relevant Statements of Statutory Accounting Principles should include SSAP No. 52, "Deposit-Type Contracts."
- Page 43: The Possible Detail Test at the top of the page (which starts on the previous page) directs the examiner to "ensure that assumptions used for [LTC] pricing and reserving are similar in nature." The use of the word "similar" is troubling. The reserving assumptions should include significant conservatism; presumably, the pricing assumptions should include relatively little conservatism. Directing the examiner to ensure that they're "similar" could be misleading. Perhaps a term such as "reconcilable" would be more appropriate; or perhaps a longer explanation of how the two sets of assumptions should relate to each other is required. See, for example, page 60, the second paragraph under "d. Rate Increases."

UNDERWRITING REPOSITORY

- Page 51: The fifth Possible Detail Test on the page again requires that the reserving and pricing assumptions be "similar." We have the same comment as for the "Life Reserves Repository," page 43, above.
- Pages 51-52: The focus is on addressing the risk that the company has not established appropriate rates for it's LTC policies, and the controls for that risk are based on the Company's Actuarial function (well trained, good data, and files for rate increases, etc.). However, it does not provide a clear path for the examiner when legitimate requests for LTC rate increases are denied by states – the detail tests (when controls are lacking) at the bottom right of page 51 point to the state examiner "tracking the progress ... by comparing rate increases received against those requested". We believe that test should go on to say:
    - *Any rate increase requests by the Company denied by states should be tabulated by the examiner and assessed by the state actuary for potential solvency issues. When the examiner determines the lack of approvals to*

be material the examiner should document the reason(s) for denial by the state actuary.

We feel that even when a well controlled and actuarially sound rate request is denied that the denial or lack of approval should still formally documented as part of the examination.

SECTION 1-6

- Page 58, "F. Long Term Care Insurance (LTCI) Reserves Overview": The third paragraph could be written more clearly. It says that the reinsurer "cannot" do certain things, and that, "Furthermore, it [the reinsurance arrangement] would not qualify for reinsurance accounting." What we believe it means is that if either of the provisions described is included in the reinsurance contract, then it will not qualify for reinsurance accounting. A possible rewording would be:
    - *These same risks also affect reinsurers because, in order for a reinsurance arrangement to qualify for reinsurance accounting, the arrangement cannot allow for arbitrary premium increases by the reinsurer. Nor can it allow the reinsurer to require the direct writer to request rate increases on the direct business.*

- Page 58, "2. Reserve Increase Factors, a. Background": The last sentence of the first paragraph begins, "If the more conservative assumptions resulted in inadequate reserves ..." Saying that the conservative assumptions result in inadequate reserves implies that reserves calculated based on those assumptions would be inadequate. What is really meant is that the tabular reserves appear inadequate in light of the more conservative assumptions. A better phrasing might be:
    - *If reserves were found to be inadequate in light of the more conservative assumptions, companies were required to establish higher reserves to ensure that future claims could be paid in the more adverse environment.*

- Page 60, "d. Rate Increases": In the fourth paragraph, we believe that "agreement between regulators or companies" should be "agreement between regulators and companies"; that is, the agreement is between a regulator and a company, not between two regulators and excluding the company, and not between two companies and excluding the regulator.

EXHIBIT M

- Page 62, "Exhibit M": Item 1.a refers to "an Accepted Actuarial Designation." That is a term that is relevant specifically to P/C. We believe the NAIC has not adopted that terminology for either life or health actuaries.

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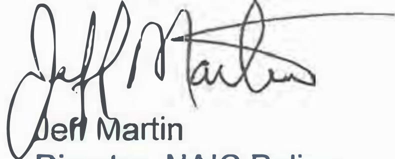
EXHIBIT Y

- Page 63, "Risk Mitigation Strategies (Internal Controls)": The sub-bullet under the third bullet appears identical to the fifth bullet. One of the two should be deleted.

Thank you for your consideration of these suggested revisions. Should you or members of the Technical Group have questions or comments, I would be glad to address them.

Sincerely,



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XI. REVIEWING AND UTILIZING THE RESULTS OF AN OWN RISK AND SOLVENCY ASSESSMENT

This section of the Handbook provides general guidance for use in reviewing, assessing and utilizing the results of an insurer's confidential Own Risk and Solvency Assessment (ORSA) in conducting risk-focused examinations. Therefore, this guidance may be used in support of the risk management assessments outlined in other sections of the Handbook (e.g., Phase 1, Part Two: Understanding the Corporate Governance Structure, Exhibit M – Understanding the Corporate Governance Structure) at the discretion of Lead State examiners.

A Background Information
B General Summary of Guidance for Each Section
C Review of Background Information
~~C~~D Review of Section I – Description of the Insurer's Risk Management Framework
~~D~~E Review of Section II – Insurer's Assessment of Risk Exposure
~~E~~F Review of Section III – Group Assessment of Risk Capital
~~F~~G ORSA Review Documentation ~~Template~~
~~G~~H Utilization of ORSA Results in the Remaining Phases of the Examination

A. Background Information

The NAIC's *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. The model gives the insurer and insurance group ~~(hereinafter referred to as "insurer" or "insurers" throughout the remainder of this guidance)~~ discretion as to whether the report is submitted by each individual insurer within the group or by the insurer group as a whole. (See the *NAIC ORSA Guidance Manual* for further discussion.) Throughout the remainder of this chapter, the term "insurer" is used to refer to both a single insurer for those situations where the report is prepared by the legal entity, as well as to refer to an insurance group when prepared at that level. However, in some cases, the term group is used to reinforce the importance of the group-wide view.

As stated in the *NAIC ORSA Guidance Manual* (Guidance Manual), the ORSA has two primary goals:

1. To foster an effective level of ERM for all insurers, through which each insurer identifies, assesses, monitors, prioritizes and reports on its material and relevant risks identified by the insurer, using techniques appropriate to the nature, scale and complexity of the insurer's risks, in a manner adequate to support risk and capital decisions.

2. To provide a group-level perspective on risk and capital, as a supplement to the existing legal entity view.

The ORSA is the company's "own" process. For insurance regulators, it is a tool to supplement the analyst's ongoing reviews of company/group data and flings, and to document key aspects of the company's /group's ERM. Regulators are expected to assess the ORSA and what it suggests about the state of ERM at the levels of the company/group and group-wide risks. While there are reporting requirements in the ORSA Manual, the necessary process and calculations remain the responsibility of management.

The Guidance Manual states that regulators should obtain a high-level understanding of the insurer's ORSA framework, and discusses how the ORSA Summary Report may assist in determining the scope, depth and minimum timing of risk-focused analysis and examination procedures.

These determinations can be documented as part of each insurer's ongoing supervisory plan. However, the Guidance Manual also states that each insurer's ORSA will be unique, reflecting the insurer's business model, strategic planning and overall approach to ERM. As regulators review ORSA Summary Reports, they should understand that the level of sophistication for each group's ERM program will vary depending upon size, scope and nature of business operations. Understandably, less complex organizations may not require intricate processes to possess a sound ERM program. Therefore, regulators

should use caution before using the results of an ORSA review to modify ongoing supervisory plans, as a variety of practices may be appropriate depending upon the nature, scale and complexity of each insurer.

There is no expectation with respect to specific information or specific action that the Lead State regulator is to take as a result of reviewing the ORSA Summary Report. Rather, each situation is expected to result in a unique ongoing dialogue between the insurer and the Lead State regulator focused on the key risks of the group. For this reason, as well as others, the Lead State analyst may want to consider including the Lead State examiner or any other individual acting under the authority of the commissioner or designated by the commissioner with special skills and subject to confidentiality that may be of assistance in their initial review of the ORSA Summary Report in possible dialogue with the insurer since the same team will be part of the ongoing monitoring of the insurer and an ORSA Summary Report is expected to be at the center of the regulatory processes. A joint review such as this prior to the Lead State analyst documenting his or her summary of the ORSA report may be appropriate.

In completing a review of the ORSA Summary Report, the lead state analyst should direct the lead state examiner to those areas where such additional support is necessary to address unresolved questions or issues that may have arisen from the analysts review of the ORSA through on-site inquiries and interviews, observation and, where necessary, testing. These items can be accumulated by the analyst on Appendix B of the template in the Financial Analysis Handbook for follow-up and communication. If there are specific reports, information and/or control processes addressed in the ORSA Summary Report that the lead state analyst feels should be subject to such additional procedures by the examination team, the lead state analyst is expected to provide direction as to its findings of specific items and/or recommended testing and such amounts should be listed in the template by the lead state analyst. During planning for a financial examination, the lead state examiner and lead state analyst should work together to develop a plan for additional testing and follow-up where necessary. The plan should consider that the lead state examiner may need to expand work to address areas of inquiry that may not be identifiable by the lead state analyst.

In addition to this specific expectation, during each coordinated financial condition examination, the exam team as directed by the lead state examiner and with input from the lead state analyst will be expected to review and assess the insurer's risk management function through utilization of the most current ORSA Summary Report received from the insurer. The lead state will direct the examination team to take steps to verify information included in the report and test the operating effectiveness of various risk management processes on a sample basis (e.g., reviewing certain supporting documentation from Section I; testing the reasonableness of certain inputs into stress testing from Section II; and reviewing certain inputs, assumptions and outputs from internal capital models).

~~After participating in the initial review of information provided in the ORSA Summary Report, the Lead State examiner is expected to incorporate a review of ORSA information into ongoing on-site examination activities.~~ Examiners are reminded that ORSA information is highly sensitive, proprietary and confidential, and examiners should exercise caution to ensure that no ORSA or ORSA-related materials are inadvertently made public in any way, including in any Exam Report. Depending upon the examination schedule or cycle, the Lead State examiner may consider performing a limited-scope exam to conduct on-site examination activities related to ORSA information on a timely basis. In incorporating a review of ERM/ORSA information into financial exam activities, the Lead State examiner should seek to utilize existing resources to avoid duplication of efforts and provide exam efficiencies.

In cases where one insurer provides an ORSA Summary Report, the domestic state is responsible for verifying, assessing and utilizing the information received to facilitate and gain efficiencies in conducting on-site examinations. In cases where a group of insurers provides an ORSA Summary Report (or multiple legal entities within an insurance group provide separate ORSA Summary Reports), the Lead State is expected to coordinate the review, assessment and utilization of the information received to facilitate and gain efficiencies in conducting coordinated examinations in accordance with Section 1, Part I of the Handbook. To the extent that an insurance group is organized into subgroups for examination purposes, the review, assessment and utilization of various aspects of the insurance group's ORSA Summary Report may require delegation of responsibilities to an Exam Facilitator. However, in all cases, examination teams should seek to avoid duplication and utilize existing work in reviewing, assessing and utilizing the ORSA Summary Report to conduct examinations of entities that are part of an insurance group. Throughout the remainder of this document, the term "Lead

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State" is used before the term "examiner" or "regulator" with the understanding that in most situations, the ORSA Summary Report will be prepared on a group basis, and, therefore, primarily reviewed by the Lead State. However, this does not remove the requirement for the domestic state to perform these responsibilities in the event of a single-entity ORSA Summary Report.

For additional guidance for sharing the ORSA Summary Report and/or the Lead State's analysis of the ORSA Summary Report with other regulators and/or other third parties, refer to the ORSA Information Sharing Best Practices found on the ORSA Implementation (E) Subgroup webpage.

~~As stated in the *NAIC ORSA Guidance Manual* (Guidance Manual), the ORSA has two primary goals:~~

1. ~~To foster an effective level of ERM for all insurers, through which each insurer identifies, assesses, monitors, prioritizes and reports on its material and relevant risks identified by the insurer, using techniques appropriate to the nature, scale and complexity of the insurer's risks, in a manner adequate to support risk and capital decisions.~~

2. ~~To provide a group-level perspective on risk and capital, as a supplement to the existing legal entity view.~~

~~The Guidance Manual states that regulators should obtain a high-level understanding of the insurer's ORSA framework, and discusses how the ORSA Summary Report may assist in determining the scope, depth and minimum timing of risk-focused analysis and examination procedures.~~

~~These determinations can be documented as part of each insurer's ongoing supervisory plan. However, the Guidance Manual also states that each insurer's ORSA will be unique, reflecting the insurer's business model, strategic planning and overall approach to ERM. As regulators review ORSA Summary Reports, they should understand that the level of sophistication for each group's ERM program will vary depending upon size, scope and nature of business operations. Understandably, less complex organizations may not require intricate processes to possess a sound ERM program. Therefore, regulators should use caution before using the results of an ORSA review to modify ongoing supervisory plans, as a variety of practices may be appropriate depending upon the nature, scale and complexity of each insurer.~~

~~Collectively, the goals above are the basis upon which the guidance is established. However, the ORSA Summary Report will not serve this function or have this direct impact until the Lead State becomes fairly familiar with and comfortable with evaluating each insurer's report and its processes. This could take more than a couple of years to occur in practice since the Lead State would likely need to review at least one or two ORSA Summary Reports to fully understand certain aspects of the processes used to develop the report.~~

B. General Summary of Guidance for Each Section

This section is designed to assist the examiner through general guidance regarding how each section of the ORSA Summary Report is expected to be reviewed and assessed during a financial examination. This guidance is expected to evolve over the years, with the first couple of years focused on developing a general understanding of ORSA and ERM. Each of the sections of the ORSA Summary Report requires distinct consideration to be adequately understood and assessed. However, each of the sections can supplement the understanding and assessment of the other sections. For example, Section II provides an insurer the opportunity to demonstrate the robustness of its process by including a detailed description of the reasonably foreseeable and relevant material risks it faces and their potential impact to the insurer. This can allow the Lead State regulator to gain a better understanding and increased appreciation for the insurer's processes to identify and prioritize reasonably foreseeable and relevant material risks described in Section I. Alternately, the Lead State regulator may assess stresses applied to individual risks in Section II as appropriate, but may not feel stresses are appropriately aggregated to determine an adequate group capital assessment in Section III. Therefore, the review and assessment of each section requires a full understanding of each of the other sections, and the Lead State regulator should exercise caution in the allocation of review responsibilities in this area.

Further, regulators do not believe there is a standard set of stress conditions each insurer should test. The Lead State examiner should never specify the stresses to be performed, nor what should be included in the insurer's ORSA Summary Report, as this would eliminate the "Own" aspect of the ORSA and defeat its purpose, which is to permit the Lead State

regulator to better understand the risk from the perspective of the insurer. This is not to suggest that the Lead State examiner should not consider asking questions about the extent to which the insurer considers particular risks, as these questions may provide the insurer an opportunity to discuss the robustness of its processes and considerations, either in specifically identified stresses or the inclusion of similar risks within a stochastic economic capital model for a particular risk.

Possible test procedures are provided for each section of the ORSA Summary Report as procedures that could be performed to address unresolved questions or issues that may have arisen from the analysts review of the ORSA. They are not intended to imply that procedures are necessary in every area or that all (or any) procedures are necessary for a given area. Instead, such procedures are intended to be applied in accordance with the examination budget, based on the judgment and discretion of the Lead State analyst and examination team, and in accordance with the concept of proportionality.

In applying the concept of proportionality, regulators should recognize that ORSAs of various insurers/ groups will inherently vary based on a multitude of factors including their size, geographic /international scope, lines of business, the nature and degree to which risks are assumed and mitigated, and managerial/professional and board judgement involving ERM and risk appetite. The scope of examination procedures to be applied with respect to the ORSA should therefore consider proportionality in application in all respects. For example, in assessing implementation, regulators should consider whether the design of ERM/ORSA practices appropriately reflects the nature, scale and complexity of the insurer.

Background Information

Background information procedures are provided to assist the regulator in gaining an overall understanding of the ORSA Summary Report and assessing compliance with ORSA Guidance Manual reporting requirements ~~in several critical areas~~ (i.e. attestation, entities in scope).

Section I

The guidance in Section I is designed to assist the Lead State examiner in performing procedures to verify and validate relevant information and assess~~reaching an assessment of~~ the risk management framework of the insurer. The Lead State examiner's assessment should utilize existing assessments of the insurer's risk management framework performed by the Lead State financial analyst through a review of the ORSA Summary Report, but should supplement the Lead State analyst's assessment with additional on-site verification and testing to reach a final conclusion.

The Section I procedures are focused on ~~determining the insurer's maturity level in regards to its~~the overall risk management framework of the insurer/group. . The procedures are presented as considerations to be taken into account when reviewing and assessing an insurer's implementation of each of the risk management principles highlighted in the NAIC's ORSA Guidance Manual. ~~The maturity level may be assessed through several ways, one of which is the incorporation of concepts developed within the Risk and Insurance Management Society's (RIMS) Risk Maturity Model (RMM). While insurers or insurance groups may utilize various frameworks in developing, implementing and reporting on their ORSA processes (e.g. COSO Integrated Framework, ISO 31000, IAIS ICP 16, other regulatory frameworks, etc.), elements of the RMM have been incorporated into this guidance to provide a framework for use in reviewing and assessing ERM/ORSA practices. However, as various frameworks may be utilized to support effective ERM/ORSA practices, Lead State regulators should be mindful of differences in frameworks and allow flexibility in assessing maturity levels. The RMM, which is only one of several processes that may be used to determine maturity levels, provides a scale of six maturity levels upon which an insurer can be assessed. The six maturity levels can generally be defined as follows:~~

~~Level 5: Risk management is embedded in strategic planning, capital allocation and other business processes, and is used in daily decision making. Risk limits and early warning systems are in place to identify breaches and require corrective action from the board of directors or committee thereof (hereafter referred to as "board") and management.~~

~~Level 4: Risk management activities are coordinated across business areas, and tools and processes are actively utilized. Enterprise-wide risk identification, monitoring, measurement and reporting are in place.~~

~~Level 3: The insurer has risk management processes in place designed and operated in a timely, consistent and sustained way. The insurer takes action to address issues related to high priority risks.~~

~~Level 2: The insurer has implemented risk management processes, but the processes may not be operating consistently and effectively. Certain risks are defined and managed in silos, rather than consistently throughout the organization.~~

~~Level 1: The insurer has not developed or documented standardized risk management processes and is relying on the individual efforts of staff to identify, monitor and manage risks.~~

~~Level 0: The insurer has not recognized a need for risk management, and risks are not directly identified, monitored or managed.~~

~~The guidance developed for use in this Handbook integrates the concepts of the RMM with the general principles and elements outlined in Section I of the Guidance Manual to assist Lead State regulators in reaching an overall assessment of the maturity of an insurer's risk management framework. The design of ERM/ORSA practices should appropriately reflect the nature, scale and complexity of the company. Lead State regulators should understand the level of maturity that is appropriate for the company based on its unique characteristics. Attainment of Level 5 maturity for ERM/ORSA practices is not appropriate, nor should be expected, for all companies or for all components of the framework.~~

Section II

The guidance for use in reviewing Section II is primarily focused on assisting the Lead State examiner in gaining an understanding of management's assessment of its reasonably foreseeable and relevant material risks. In addition, the guidance assists the Lead State examiner in understanding the potential impact of reasonably foreseeable and relevant material risks by considering the stress scenarios and stress testing presented by the insurer. Finally, information in Section II can inform or support the assessment of key principles reached during a review of Section I.

In order for the Lead State examiner to understand and utilize the information on reasonably foreseeable and relevant material risks provided in Section II, the Lead State examiner must obtain a minimum level of confidence regarding the reasonability of the information presented. ~~Much of the~~ Section II guidance has been developed around reviewing key risks assessed by the insurer and classifying them within the nine branded risk classifications outlined in Exhibit L of this Handbook, which are used as a common language in the risk-focused surveillance process. However, examiners should not expect or require insurers to organize or present their risks in a particular manner (i.e. by branded risk classification). Rather, the guidance should be used in a way to allow the lead state to better understand, assess and document the information presented, as well as a way to verify or validate the summary review and assessment prepared by the financial analyst (if available). ~~The primary reason for this approach is that insurers may utilize similar risk classifications in their ORSA Summary Reports. However, Lead State regulators should not restrict their focus to only the nine branded risk classifications as such an approach may not encourage independent judgment in understanding the risk profile of the insurer. Therefore, the use of the nine branded risk classifications provides a framework to organize the Lead State's summary, but should not discourage regulators from documenting other risks or excluding branded risk categories that aren't relevant. From this standpoint, Section II will also provide regulators with information to better understand current insurance market risks, changes in those risks as well as macroeconomic changes, and the impact they have on insurers' risk identification and risk management processes.~~

As part of evaluating the information presented on reasonably foreseeable and relevant material risks, the Lead State examiner may document how the insurer determines the appropriateness of its stress scenarios identified and stress testing performed by the insurer. However, regulators do not believe there is a standard set of stress conditions each insurer should test. Consistent with the language in the Guidance Manual, the Lead State examiner should not specify the stresses to be performed (other than in rare situations deemed necessary by the commissioner), nor what should be included in the ~~company~~insurer's ORSA Summary Report beyond the basic framework necessary to understand the work performed. Therefore, guidance has been provided to assist the Lead State examiner in considering the reasonableness of the assumptions and methodologies used in conducting stress scenarios/testing and to facilitate discussion with the insurer.

Section III

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The guidance for reviewing Section III of the ORSA Summary Report is intended to assist the Lead State examiner in understanding and assessing the estimated amount of capital the insurer determines is ~~reasonable~~ needed to sustain its current ~~business model~~risk profile, as well as its prospective solvency position on an ongoing basis. This determination typically utilizes internally developed capital models that estimate the distribution of potential losses and associated probabilities. Other insurers might base their determination on rating agency or regulatory capital models to determine the amount of capital needed to support a particular rating or to quantify the amount of capital at risk in case of extreme shocks. ~~and/or aggregates the outputs of Section II (i.e., stress testing) to calculate the amount of capital required to support ongoing business operations for a wide range of potential outcomes.~~ All of these approaches require the insurer to establish a capital quantification methodology and select supporting assumptions. Therefore, much of the guidance in this section relates back to how the insurer determines the reasonableness of the ~~assumptions and~~capital quantification methodolog~~ies~~y and assumptions, as well as the process undertaken by the insurer to validate the inputs, calculations and outputs.~~utilized to calculate and allocate capital to the reasonably foreseeable and relevant material risks it faces. Often, this calculation may be wholly or partially based on internal models developed by the insurer for this purpose. Therefore, the guidance also directs the Lead State examiner to consider and evaluate the insurer's processes to validate the suitability, reasonability and reliability of its internal models.~~

C. Review of Background Information

The ORSA Guidance Manual encourages discussion and disclosure of key pieces of information to assist regulators in reviewing and understanding the ORSA Summary Report. As such, the following considerations are provided to assist the Lead State examiner in reviewing and assessing the information provided in these areas.

Consideration	Description	Possible Test Procedure(s)
Attestation	The report includes an attestation signed by the Chief Risk Officer (or other executive responsible for ERM) indicating that the information presented is accurate and consistent with ERM reporting shared with the Board of Directors (or committee thereof).	• Consider the results of review/test procedures performed in Sections I - III to evaluate the accuracy of information in the ORSA Summary Report to verify this attestation • Obtain and review BOD (or appropriate committee) minutes or packets to verify that ORSA Summary Report (or similar ERM documentation) is subject to an appropriate level of review and oversight
Entities in Scope	The scope of the report is clearly explained and identifies all insurers covered. The scope of a group report also indicates whether material non-insurance operations have been covered.	• Compare insurance entities covered in ORSA report to Schedule Y, Lead State report and holding company filings to ~~identify any missing entities~~review which entities are accounted for in the filing for discussion with the ~~company~~insurer • Obtain and review information provided in Form F to get an understanding of whether non-insurance entities pose a risk to the insurance entities • If necessary, obtain and review the non-U.S. ORSA report(s) to get a full understanding of the group's risk capital o Review the home jurisdiction's ORSA requirements and compare against the NAIC ORSA Guidance Manual to understand differences
Accounting Basis	The report clearly indicates the accounting basis used to present financial information in the report, as well as the primary valuation date(s).	• Compare valuation date and accounting basis utilized across various sections of the report to ensure consistency • If multiple accounting bases are used, gain an understanding of which basis is used to manage capital
Key Business Goals	The report provides an overview of the insurer's/group's key business goals in order to demonstrate alignment with the relevant and material risks presented within the report.	• Compare the key business goals summarized in the report against other insurer filings and documents (e.g., MD&A, Holding Company Filings, submitted business plans, etc.) other regulatory documents (i.e. IPS/GPS) and the regulator's understanding of the insurer o If inconsistencies are noted, discuss with the insurer to determine if any key risks are excluded from assessment within the ORSA

Changes from Prior Filing(s)	The report clearly discusses significant changes from the prior year filing(s) to highlight areas of focus in the current year review including changes to the ERM framework, risks assessed, stress scenarios, overall capital position, modeling assumptions, etc.	• Focus test procedures in Section I, II and III on significant changes from prior filings • Verify appropriate governance over changes by requesting supporting documentation and approvals for a sample of changes made • After completing a review of other sections of the ORSA, consider whether all significant changes from the PY filing were appropriately summarized and disclosed
~~Planned ERM Enhancements~~	~~The report provides information on planned enhancements for improving the effectiveness of the insurer's/group's ERM practices to demonstrate ongoing development and a functioning feedback loop.~~	• ~~Perform procedures to understand and evaluate the current status of planned enhancements to verify information reported and assess the adequacy of governance over planned enhancements~~

D. Review of Section I - Description of the Insurer's Risk Management Framework

The Guidance Manual requires the insurer to discuss five key principles of an effective risk management framework in Section I of the ORSA Summary Report. Therefore, the Lead State examiner is required to review and assess the insurer's risk management framework by considering and evaluating each of the key principles. Upon receipt of the ORSA Summary Report, the Lead State financial analyst should perform an initial, high-level assessment of each of the key principles. During an on-site examination, the Lead State examiner is expected to supplement this initial assessment with additional procedures to verify the reported information and test the operating effectiveness of the insurer's risk management processes and practices. Upon conclusion of these procedures, the Lead State examiner should reach his or her own assessment regarding each of the five principles. This should be utilized to adjust the scope of the risk-focused examination and communicated back to the Lead State financial analyst for ongoing monitoring and adjustment of the supervisory plan.

Guidance is provided to assist the Lead State examiner in ~~developing review procedures and to give examples of attributes that may indicate the insurer is more or less mature in its handling of the individual~~assessing the effectiveness of the insurer's key risk management principles. ~~These attributes are meant to assist the Lead State examiner in reaching an assessment of the insurer's maturity level for each key principle.~~

Key Principles

1. Risk Culture and Governance
2. Risk Identification and Prioritization
3. Risk Appetite, Tolerances and Limits
4. Risk Management and Controls
5. Risk Reporting and Communication

Considerations When Reviewing and Testing Key Principles

When reviewing processes described in the ORSA Summary Report, the Lead State examiner should consider the extent to which the above principles are integrated into the ~~organization~~insurer. To do so, the Lead State examiner may need to review processes and practices beyond those documented within the ORSA Summary Report. In addition, the Lead State examiner may need to review and consider changes made to risk management processes since the filing of the last ORSA Summary Report. ~~In so doing, the Lead State examiner may consider information beyond what is included in the ORSA Summary Report to reach an assessment of the insurer's maturity level for each key principle.~~

In reviewing these key principles, examples of various ~~attributes/traits associated with various maturity levels~~considerations and possible test procedures for each key principle are provided. However, these ~~attributes~~ considerations and procedures only ~~demonstrate common currently known practices associated with each of the various maturity levels,~~ address certain elements associated with the key principles and practices of individual insurers may vary significantly. ~~from the examples provided. It is possible that the insurer has mature practices in place, even if those practices differ from the example attributes provided.~~ Therefore, the Lead State examiner should exercise professional judgment in determining the appropriate

maturity level to selectconsideratios and procedures to be performed when assessing each of the key risk management principles.

The following table provides example test procedures that may be performed by the Lead State examiner to verify information on risk management processes included in the ORSA Summary Report or to test the operating effectiveness of such practices. Several of these procedures may be performed in conjunction with other risk-focused examination processes, and Lead State examiners should attempt to gain efficiencies by coordinating testing and review efforts wherever possible. Lead State examiners should use professional judgment in selecting or tailoring procedures to assist in the assessment of each of the five risk management principles for the insurer. In addition, the Lead State examiner should incorporate any specific verification or testing recommendations made by the Lead State financial analyst into the planned examination procedures for Section I and consider the extent to which additional procedures should be utilized to test the changes that have been made to the insurer's ERM framework since the last on-site examination.

1. **Risk Culture and Governance**

It's important to note some organizationinsurers view risk culture and governance as the cornerstone to managing risk. The Guidance Manual defines this item to include a structure that clearly defines and articulates roles, responsibilities and accountabilities, as well as a risk culture that supports accountability in risk-based decision making. Therefore, the objective is to have a structure in place within the organizationinsurer that manages reasonably foreseeable and relevant material risk in a way that is continuously improved. Key considerations and possible test procedures for use in reviewing and assessing risk culture and governance might include, but aren't limited to:

Consideration	**Description**	**Possible Test Procedure(s)**
Roles & Responsibilities	Roles and responsibilities of key stakeholders in ERM are clearly defined and documented, including members of the board (or committee thereof), officers and senior executives, risk owners, etc.	• Review documentation to determine whether key stakeholders are identified and roles are clearly defined within the ERM framework • Consider the results of review/test procedures performed across Sections I-III to determine whether roles are effectively implemented
Board or Committee Involvement	The Board of Directors or appropriate committee thereof demonstrates active involvement in andthe oversight of ERM activities through receiving regular updates from management on ERM monitoring, reporting and recommendations	• Obtain and review management, board or committee minutes/packets for the director group responsible for ERM oversight and evaluate the level of oversight provided • Interview board member(s) with responsibilities for risk management oversight to determine level of knowledge and involvement of directors in risk oversight activities
Strategic Decisions	Directors, officers and other members of senior management utilize information generated through ERM processes in making strategic decisions	• Interview management or board member(s) to determine how risk management processes and results are utilized in strategic decision making • Evaluate the consistency between the insurer's business strategy and its risk management processes • Evaluate whether the insurer utilizes ERM to identify strategic opportunities, as opposed to focusing only on limiting exposures
Staff Availability & Education	The insurer/group maintains suitable staffing (e.g. sufficient number, educational background, experience) to support its ERM framework and deliver on its risk strategy	• Obtain and review information on the staffing and activity of key ERM functions (e.g. ERM group, Internal Audit, etc.) to evaluate their level of activity and involvement • Select a sample of key individuals to review job descriptions and biographical information for appropriateness and suitability • Interview a sample of key individuals to assess their suitability and verify their involvement in the operation of the ERM framework • Obtain and review evidence of formalized risk training programs for staff and consider whether the training matches the risk profile of the insurer/group

Leadership	The Chief Risk Officer (or equivalent position) possesses an appropriate level of knowledge and experience related to ERM and receives an appropriate level of authority to effectively fulfill responsibilities	• Obtain and review information necessary (i.e. biographical affidavit or equivalent) to evaluate the suitability of the Chief Risk Officer (or equivalent position) • Obtain and review information necessary to evaluate the authority and resources provided to the CRO to fulfill responsibilities • Review BOD/committee minutes to verify CRO access and reporting to the BOD/committee on a regular basis and assess the CRO's response to BOD recommendations
Compensation	The insurer/group demonstrates that incentives, compensation and performance management criteria have been appropriately aligned with ERM processes and do not encourage excessive risk taking given the capital position of the insurer/group	• Obtain and review information on the insurer's compensation plans to determine that risk management decision-making is not undermined by compensation structure • Obtain and review job descriptions or performance review criteria for select management positions to determine whether risk management elements are incorporated • Interview a member(s) of the BOD (or appropriate committee thereof) to discuss oversight of compensation and understand if there are concerns about excessive risk taking
Integration	The insurer/group integrates and coordinates ERM processes across functional areas of the insurer including HR, IT, internal audit, compliance, business units, etc.	• Interview selected executives from different functional areas to get a feel for the "tone at the top" of the insurer and the level of consistency in applying risk management processes across departments
Assessment	The insurer's ERM framework is subject to regular review and assessment, with updates made to the framework as deemed necessary	• Gain an understanding of the insurer's process to review and update its ERM framework to ensure involvement of appropriate stakeholders • Perform procedures to verify the insurer is reviewing and updating its framework on a regular basis

Level 5
Risk culture is analyzed and reported as a systematic view of evaluating risk. Executive sponsorship is strong, and the tone from the top has sewn an ERM framework into the corporate culture. Management establishes the framework and the risk culture, and the board reviews the risk appetite statement in collaboration with the chief executive officer (CEO), chief risk officer (CRO) where applicable and chief financial officer (CFO). Those officers translate the expectations into targets through various practices embedded throughout the organization. Risk management is embedded in each material business function. Internal audit, information technology, compliance, controls and risk management processes are integrated, and coordinate and report risk issues. Material business functions use risk-based best practices. The risk management life cycle for business process areas are routinely evaluated and improved (when necessary).

Level 4
The insurer's ERM processes are self-governed with shared ethics and trust. Management is held accountable. Risk management issues are understood and risk plans are conducted in material business process areas. The board, CEO, CRO (if applicable) and CFO expect a risk management plan to include a qualitative risk assessment for reasonably foreseeable and relevant material risks with reporting to management or the board on priorities, as appropriate. Relevant areas use the ERM framework to enhance their functions, communicating on risk issues as appropriate. Process owners incorporate managing their risks and opportunities within regular planning cycles. The insurer creates and evaluates scenarios consistent with its planning horizon and product timelines, and follow-up activities occur accordingly.

Level 3
ERM risk plans are understood by management. Senior management expects that a risk management plan captures reasonably foreseeable and relevant material risks in a qualitative manner. Most areas use the ERM framework and

report on risk issues. Process owners take responsibility for managing their risks and opportunities. Risk management creates and evaluates scenarios consistent with the business planning horizon.

Level 2
Risk culture is enforced by policies interpreted primarily as compliance in nature. An executive champions ERM management to develop an ERM framework. One area has used the ERM framework, as shown by the department head and documented team activities. Business processes are identified, and ownership is defined. Risk management is used to consider risks in line with the insurer's business planning horizon.

Level 1
Corporate culture has little risk management accountability. Risk management is not interpreted consistently. Policies and activities are improvised. Programs for compliance, internal audit, process improvement and IT operate independently and have no common framework, causing overlapping risk assessment activities and inconsistencies. Controls are based on departments and finances. Business processes and process owners are not well defined or communicated. Risk management focuses on past events. Qualitative risk assessments are unused or informal. Risk management is considered a quantitative analysis exercise.

Level 0
There is no recognized need for an ERM process and no formal responsibility for ERM. Internal audit, risk management, compliance and financial activities might exist, but they aren't integrated. Business processes and risk ownership are not well defined.

2. **Risk Identification and Prioritization**

The Guidance Manual defines this as key to the organizationinsurer, and responsibility for this activity should be clear. The risk management function is responsible for ensuring the processes are appropriate and functioning properly. Therefore, an approach for risk identification and prioritization may be to have a process in place that identifies risk and prioritizes such risks in a way that potential reasonably foreseeable and relevant material risks are addressed in the framework. Key considerations and possible test procedures for use in reviewing and assessing risk identification and prioritization might include, but aren't limited to:

Consideration	Description	Possible Test Procedure(s)
Resources	The insurer/group utilizes appropriate resources and tools (e.g. questionnaires, external risk listings, brainstorming meetings, regular calls, etc.) to assist in the risk identification process that are appropriate for its nature, size and structure	• Obtain and review information and tools associated with the risk identification and prioritization process for appropriateness • Determine whether appropriate external sources have been used to assist in risk identification (e.g. rating agency information, emerging risk listings, competitor 10K filings, etc.) where applicable • Obtain and review lists of key risks (or risk register) at different dates to identify which risks have been added/removed to understand and assess the process
Stakeholder Involvement	All key stakeholders (i.e. directors, officers, senior management, business unit leaders, risk owners, etc.) are involved in risk identification and prioritization at an appropriate level	• Interview select process owners/business unit leaders to verify their role in risk identification and prioritization • Interview risk management staff to understand and evaluate how risks are identified and aggregated across the insurer
Prioritization Factors	Appropriate factors and considerations are utilized to assess and prioritize risks (e.g. likelihood of occurrence, magnitude of impact, controllability, speed of onset, etc.)	• Assess the insurer's process and scale by which it prioritizes the key risks identified • Review the approach for, and results of, the insurer's likelihood, severity and speed of onset risk assessments, if applicable
Process Output	Risk registers, key risk listings and risk ratings are maintained, reviewed and updated on a regular basis	• Obtain and review a current copy of the insurer's risk register • Verify that the insurer's risk register is updated/reviewed on a regular basis by requesting copies at various dates

Emerging Risks	The insurer has developed and maintained a formalized process for the identification and tracking of emerging risks	• Obtain and review tools and reports utilized to identify and evaluate emerging risks to determine whether appropriate stakeholders and resources are utilized in this process

Level 5
Information from internal and external sources on reasonably foreseeable and relevant material risks, including relevant business units and functions, is systematically gathered and maintained. A routine, timely reporting structure directs risks and opportunities to senior management. The ERM framework promotes frontline employees' participation and documents risk issues' or opportunities' significance. Process owners periodically review and recommend risk indicators that best measure their areas' risks. The results of internal adverse event planning are considered a strategic opportunity.

Level 4
Process owners manage an evolving list of reasonably foreseeable and relevant material risks locally to create context for risk assessment activities as a foundation of the ERM framework. Risk indicators deemed critical to their areas are regularly reviewed in collaboration with the ERM team. Measures ensure downside and upside outcomes of risks and opportunities are managed. Standardized evaluation criteria of impact, likelihood and controls' effectiveness are used to prioritize risk for follow-up activity. Risk mitigation is integrated with assessments to monitor effective use.

Level 3
An ERM team manages an evolving list of reasonably foreseeable and relevant material risks, creating context for risk assessment as a foundation of the ERM framework. Risk indicator lists are collected by most process owners. Upside and downside outcomes of risk are understood and managed. Standardized evaluation criteria of impact, likelihood and controls' effectiveness are used, prioritizing risk for follow-ups. Enterprise-level information on risks and opportunities are shared. Risk mitigation is integrated with assessments to monitor effective use.

Level 2
Formal lists of reasonably foreseeable and relevant material risks exist for each relevant business unit or function, and discussions of risk are part of the ERM process. Corporate risk indicators are collected centrally, based on past events. Relevant business units or functions might maintain their own informal risk checklists that affect their areas, leading to potential inconsistency, inapplicability and lack of sharing or under-reporting.

Level 1
Risk is owned by specialists, centrally or within a business unit or function. Risk information provided to risk managers is probably incomplete, dated or circumstantial, so there is a high risk of misinformed decisions, with potentially severe consequences. Further mitigation, supposedly completed, is probably inadequate or invalid.

Level 0
There might be a belief that reasonably foreseeable and relevant material risks are known, although there is probably little documentation.

3. **Risk Appetite, Tolerances and Limits**

The Guidance Manual states that a formal risk appetite statement, and associated risk tolerances and limits, are foundational elements of a risk management framework for an insurer. While risk appetites, tolerances and limits can be defined and used in different ways across different insurers, this guidance is provided to assist the regulator in understanding and evaluating the insurer's practices in this area. Risk appetite can be defined as the amount of specific and aggregate risk that an insurer chooses to take during a defined time period in pursuit of its business objectives. Understanding Articulation of the risk appetite statement ensures alignment with of the risk strategy with the business strategy set by senior management and reviewed and evaluated by the board. Not included in the Guidance Manual, but widely considered, is that risk appetite statements should be easy to communicate, understood and closely tied to the organizationinsurer's strategy.

After the overall risk appetite for the organizationinsurer is determined, the underlying risk tolerances and limits can be selected and applied to business units and specific key risks identified by areas as the companyinsurer deems appropriate.

Risk tolerance can be defined as the aggregate risk-taking capacity of an insurer. Risk limits can be defined as thresholds used to monitor the actual exposure of a specific risk or activity unit of the insurer to ensure that the level of actual risk remains within the risk tolerance. The companyinsurer may apply appropriate quantitative limits and qualitative statements to help establish boundaries and expectations for risks that are hard to measure. These boundaries may be expressed in terms of earnings, capital or other metrics, such as growth and volatility. The risk tolerances/limits provide direction outlining the insurer's tolerance for taking on certain risks, which may be established and communicated in the form of the maximum amount of such risk the entity is willing to take. However, in many cases, these will be coupled with more specific and detailed limits or guidelines the insurer uses.

Due to the varying level of detail and specificity different organizationinsurers incorporate into their risk appetites, tolerances and limits, Lead State regulators should consider these elements collectively to reach an overall assessment in this area and should seek to understand the insurer's approach through follow-up discussions and dialogue. Key considerations and possible test procedures for use in reviewing and assessing risk appetite, tolerance and limits might include, but aren't limited to:

Consideration	Description	Possible Test Procedure(s)
Risk Appetite Statement	The insurer/group has adopteddeveloped an overall risk appetite statement consistent with its business plans and operations that is updated on a regular basis and approved by the board of directors (or committee thereof)subject to appropriate governance oversight	• Determine whether the insurer considers legal entity regulations and capital requirements in setting its overall risk appetite (if applicable) • Consider whether the insurer appropriately considers both qualitative and quantitave measures of risk appetite • Evaluate the appropriateness of the risk appetite statement and its consistency with the insurer's business strategy • Review board/committee minutes or supporting materials to verify that the insurer's risk appetite is reviewed, updated and approved as appropriate
Risk Tolerances/Limits	Tolerances and limits are developed for key risks in accordance with the overall risk appetite statement	• Select a sample of key risks to verify that specific tolerances and limits have been put in place • Gain an understanding of the checks and balances (i.e. supervisory review) in place to ensure that tolerances and limits are in accordance with the risk appetite • Review and evaluate the consistency between the insurer's risk appetite, tolerances and limits, as well as their appropriateness in light of the business strategy
Risk Owners	Key risks are assigned to risk owners with responsibility for monitoring and reporting on risk tolerances and limits, including actions to address any breaches	• Verify, as applicable, that all key risks are assigned appropriate risk owners • Interview select risk owners to get an understanding of and assess their roles and responsibilities in setting/updating tolerances and limits

Level 5
A risk appetite statement has been developed to establish clear boundaries and expectations for the organization to follow. A process for delegating authority to accept risk levels in accordance with the risk appetite statements is communicated throughout the organization. The management team and risk management committee, if applicable, may define tolerance levels and limits on a quantitative and/or qualitative basis for relevant business units and functions in accordance with the defined risk appetite. As part of its risk management framework, the company may compare and report actual assessed risk versus risk tolerances/limits. Management prioritizes resource allocation based on the gap between risk appetite and assessed risk and opportunity. The established risk appetite is examined periodically.

Level 4
Risk appetite is considered throughout the ERM framework. Resource allocation decisions consider the evaluation criteria of business areas. The organization forecasts planned mitigation's potential effects versus risk tolerance as part of the ERM framework. The insurer's risk appetite is updated as appropriate and risk tolerances are evaluated from various perspectives as appropriate. Risk is managed by process owners. Risk tolerance is evaluated as a

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~~decision to increase performance and measure results. Risk-reward tradeoffs within the business are understood and guide actions.~~

~~Level 3~~
~~Risk assumptions within management decisions are clearly communicated. There's a structure for evaluating risk on an enterprise-wide basis and for gauging risk tolerance. Risks and opportunities are routinely identified, evaluated and executed in alignment with risk tolerances. The ERM framework quantifies gaps between actual and target tolerances. The insurer's risk appetite is periodically reviewed and updated as deemed appropriate by the company, and risk tolerances are evaluated from various perspectives as appropriate.~~

~~Level 2~~
~~Risk assumptions are only implied within management decisions and are not understood outside senior leadership with direct responsibility. There is no ERM framework for resource allocation. Defining different views of business units or functions from a risk perspective cannot be easily created and compared.~~

~~Level 1~~
~~Risk management might lack a portfolio view of risk. Risk management might be viewed as risk avoidance and meeting compliance requirements or transferring risk through insurance. Risk management might be a quantitative approach focused on the analysis of high-volume and mission-critical areas.~~

~~Level 0~~
~~The need for formalizing risk tolerance and appetite is not understood.~~

4. **Risk Management and Controls**

The Guidance Manual stresses managing risk is an ongoing ERM activity, operating at many levels within the ~~organization~~insurer. This principle is discussed within the governance section above from the standpoint that a key aspect of managing and controlling the reasonably foreseeable and relevant material risks of the ~~organization~~insurer is the risk governance process put in place. For many companies, the day-to-day governance starts with the relevant business units. Those units put mechanisms in place to identify, quantify and monitor risks, which are reported up to the next level based upon the risk reporting triggers and risk limits put in place. In addition, controls are also put in place on the back end, by either the ERM function or the internal audit team ~~or an independent consultant~~, which are designed to ensure compliance and a continual enhancement approach. Therefore, one approach may be to put controls in place to ensure the ~~organization~~insurer is abiding by its limits. Key considerations and possible test procedures for use in reviewing and assessing risk management and controls might include, but aren't limited to:

Consideration	**Description**	**Possible Test Procedure(s)**
Lines of ~~Defense~~Accountability	Multiple lines of ~~defense~~accountability (i.e. business unit or risk owners, ERM function, internal audit) are put in place to ensure that control processes are effectively implemented and maintained	• Gain an understanding of business unit involvement in risk management and control processes to assess appropriateness • Review, verify and evaluate the role of ERM staff in setting and enforcing risk management processes and controls • Obtain a listing of internal audit reports to determine whether risk management processes are subject to periodic review. • Perform procedures to verify and evaluate segregation of duties between business units, ERM staff and the internal audit department in carrying out risk management responsibilities.
Control Processes	Specific control activities and processes are put in place to manage, mitigate and monitor all key risks	• Obtain minutes of internal risk management committee (or equivalent management group) meetings to review frequency and extent of oversight activities.

		• Review and evaluate how specific controls are mapped to legal entities (as appropriate if mapping is relevant to understanding of control). • Select a sample of key risks to verify that risk controls and mitigation activities are identified and implemented
Implementation of Tolerances /Limits	Risk tolerances and limits are translated into operational guidance and policies around key risks through all levels of the insurer	• Select a sample of key risks to verify that operational guidance and policies at mutliple levels/areas of the insurer are in place and consistent with risk limits identified through ORSA process • Identify and test the operating effectiveness of preventive controls in select areas to determine how risk tolerances/limits are enforced.
Indicators/Metrics	Key risk indicators or performance metrics are put in place to monitor exposures, provide early warnings and measure adherence to risk tolerances/limits	• Select a sample of key risks to verify that risk metrics have been identified to monitor exposures, provide early warnings and measure adherence to tolerances/limits • Perform procedures to verify that risk metrics are measured and monitored accurately and on a regular basis • Review and evaluate escalation process and remediation efforts when limits on key risks are breached

~~Level 5~~
~~ERM, as a management tool, is embedded in material business processes and strategies. Roles and responsibilities are process-driven, with teams collaborating across material central and field positions. Risk and performance assumptions within qualitative assessments are routinely revisited and updated. The organization uses an ERM process of sequential steps that strive to improve decision-making and performance. A collaborative, enterprise-wide approach is in place to establish a risk management committee staffed by qualified management. Accountability for risk management is woven into all material processes, support functions, business lines and geographies as a way to achieve goals. To evaluate and review the effectiveness of ERM efforts and related controls, the organization has implemented a "Three Lines of Defense" model or similar system of checks and balances that is effective and integrated into the insurer's material business processes. The first line of defense may consist of business unit owners and other front-line employees applying internal controls and risk responses in their areas of responsibility. The second line of defense may consist of risk management, compliance and legal staff providing oversight to the first line of defense and establishing framework requirements to ensure reasonably foreseeable and relevant material risks are actively and appropriately managed. The third line of defense may consist of auditors performing independent reviews of the efforts of the first two lines of defense to report back independently to senior management or the board, as appropriate.~~

~~Level 4~~
~~Risk management is clearly defined and enforced at relevant levels. A risk management framework articulates management's responsibility for risk management, according to established risk management processes. Management develops and reviews risk plans through involvement of relevant stakeholders. The ERM framework is coordinated with managers' active participation. Opportunities associated with reasonably foreseeable and relevant material risks are part of the risk plans' expected outcome. Authentication, audit trail, integrity and accessibility promote roll-up information and information sharing. Periodic reports measure ERM progress on all reasonably foreseeable and relevant material risks for stakeholders, including senior management or the board, as appropriate. The organization has implemented a "Three Lines of Defense" model to review and assess its control effectiveness, but those processes may not yet be fully integrated or optimized.~~

~~Level 3~~
~~The ERM framework supports material business units' and functions' needs. ERM is a process of steps to identify, assess, evaluate, mitigate and monitor reasonably foreseeable and relevant material risks. ERM frameworks include the management of opportunities. Senior management actively reviews risk plans. The ERM process is collaborative and directs important issues to senior management. The "Three Lines of Defense" are generally in place but are not yet performing at an effective level.~~

~~Level 2~~
~~Management recognizes a need for an ERM framework. Agreement exists on a framework, which describes roles and responsibilities. Evaluation criteria are accepted. Risk mitigation activities are sometimes identified but not often executed. Qualitative assessment methods are used first in all material risk areas and inform what needs deeper quantitative methods, analysis, tools and models. The "Three Lines of Defense" are not yet fully established, although some efforts have been made to put these processes in place.~~

~~Level 1~~
~~Management is reactive, and ERM might not yet be seen as a process and management tool. Few processes and controls are standardized and are instead improvised. There are no standard risk assessment criteria. Risk management is involved in business initiatives only in later stages or centrally. Risk roles and responsibilities are informal. Risk assessment is improvised. Standard collection and assessment processes are not identified.~~

~~Level 0~~
~~There is little recognition of the ERM framework's importance or controls in place to ensure its effectiveness.~~

5. **Risk Reporting and Communication**
The Guidance Manual indicates risk reporting and communication provides key constituents with transparency into the risk-management processes and facilitates active, informal decisions on risk-taking and management. The transparency is generally available because of reporting that can be made available to management, the board or compliance departments, as appropriate. However, most important is how the reports are being utilized to identify and manage reasonably foreseeable and relevant material risks at either the group, business unit or other level within the ~~organization~~insurer where decisions are made. Therefore, one approach may be to have reporting in place that allows decisions to be made throughout the ~~organization~~insurer by appropriately authorized people, with ultimate ownership by senior management or the board, as appropriate. Key considerations and possible test procedures for use in reviewing and assessing risk reporting and communication might include, but aren't limited to:

Consideration	Description	Possible Test Procedure(s)
Training	The importance of ERM processes and changes to the risk strategy are clearly communicated to all impacted areas and business units through ongoing training	• Obtain and review formal ERM training materials provided by the insurer to relevant employees and directors • Review records of recent training sessions to verify sessions are regular and ongoing and attended by all key stakeholders involved in the design, oversight and operation of the ERM framework
Key Risk Indicator Reporting	Summary reports on risk exposures (i.e. key risk indicators) and compliance with tolerances/limits are maintained and updated on a regular basis	• Obtain a current copy of the insurer's risk dashboard (or equivalent report) to verify that tracking for key risks is appropriate and to obtain a more current view of risks since the last ORSA valuation date • Verify the frequency with which risk information is accumulated and reported by selecting a sample of historical risk dashboards (or equivalent reports) to review • Test the reasonableness of key risk indicator information included on the risk dashboard (or equivalent report) on a sample basis
Oversight	Summary reports are reviewed and discussed by the appropriate members of management, and when appropriate, directors~~, officers and other members of senior management~~ on a regular basis	• Review meeting minutes and packets to determine whether risk reporting information is evaluated by the board and used by senior management for strategy and planning purposes • Gain an understanding of and evaluate the BOD's (or committee thereof) role in ~~overseeing,~~ reviewing and ~~approving~~discussing the ORSA process and resulting Summary Report

		• Select a sample of ERM information reported to the BOD for comparison against the ORSA Summary Report to validate accuracy and consistency in reporting
Breach Management	Breaches of limits and dashboard warning indicators are addressed in a timely manner through required action by management and, when appropriate, directors ~~and officers~~	• Select a sample of breaches from recent dashboard reports to determine whether Senior Management and/or the BOD take an active role in addressing breaches and/or significant changes in risk exposure • For the sample selected, review and evaluate the timeliness with which breaches in risk limits are reported and communicated to the appropriate authority
Feeback Loop	A feedback loop is embedded into ERM processes to ensure that results of monitoring and review discussions on key risks by senior management and the board are incorporated by business unit leaders and risk owners into ongoing risk-taking activities and risk management processes	• Discuss with ERM staff how input and feedback from BOD/committee or Senior Management review of summary reports is incorporated into risk management processes • Review relevant BOD/committee minutes and select a sample of decisions made on ERM to verify that they were appropriately incorporated into ongoing processes

~~Level 5~~
~~The ERM framework is an important element in strategy and planning. Evaluation and measurement of performance improvement is part of the risk culture. Measures for risk management include process and efficiency improvement. The organization measures the effectiveness of managing uncertainties and seizing risky opportunities. Deviations from plans or expectations are also measured against goals. A clear, concise and effective approach to monitor progress toward strategic goals is communicated regularly with relevant business units or functional areas. Individual, management, departmental, divisional and corporate strategic goals are linked with standard measurements. The results of key measurements and indicators are reviewed and discussed by senior management and the board, as appropriate, on a regular basis and as frequently as necessary to address breaches in risk tolerances or limits in a timely manner.~~

~~Level 4~~
~~The ERM framework is an integrated part of strategy and planning. Risks are considered as part of strategic planning. Risk management is a formal part of strategic goal setting and achievement. Investment decisions for resource allocation examine the criteria for evaluating opportunity impact, timing and assurance. The organization forecasts planned mitigation's potential effect on performance impact, timing and assurance prior to use. Employees at all relevant levels use a risk-based approach to achieve strategic goals. The results of key measurements and indicators are shared with senior management and the board, as appropriate, on a regular basis.~~

~~Level 3~~
~~The ERM framework contributes to strategy and planning. Strategic goals have performance measures. While compliance might trigger reviews, other factors are integrated, including process improvement and efficiency. The organization indexes opportunities qualitatively and quantitatively, with consistent criteria. Employees understand how a risk-based approach helps them achieve goals. Accountability toward goals and risk's implications are understood and are articulated in ways frontline personnel understand. The results of key measurements and indicators are shared with senior management and the board, as appropriate.~~

~~Level 2~~
~~The ERM framework is separate from strategy and planning. A need for an effective process to collect information on opportunities and provide strategic direction is recognized. Motivation for management to adopt a risk-based approach is lacking.~~

~~Level 1~~
~~Not all strategic goals have measures. Strategic goals aren't articulated in terms the frontline management understands. Compliance focuses on policy and is geared toward satisfying external oversight bodies. Process~~

improvements are separate from compliance activities. Decisions to act on risks might not be systematically tracked and monitored. Monitoring is done, and metrics are chosen individually. Monitoring is reactive.

Level 0
No formal framework of indicators and measures for reporting on achievement of strategic goals exists.

Examination Procedures for Section I

The following table provides example test procedures that may be performed by the Lead State examiner to verify information on risk management processes included in the ORSA Summary Report or to test the operating effectiveness of such practices. Several of these procedures may be performed in conjunction with other risk-focused examination processes, and Lead State examiners should attempt to gain efficiencies by coordinating testing and review efforts wherever possible. Lead State examiners should use professional judgment in selecting or tailoring procedures to assist in the assessment of each of the five risk management principles for the insurer. In addition, the Lead State examiner should incorporate any specific verification or testing recommendations made by the Lead State financial analyst into the planned examination procedures for Section I and consider the extent to which additional procedures should be utilized to test the changes that have been made to the insurer's ERM framework since the last on-site examination.

Principle	Possible Test Procedures
Risk Culture and Governance	• Obtain and review management, board or committee minutes/packets for the director group responsible for ERM oversight and evaluate the level of oversight provided. • Obtain and review formal ERM training materials provided by the insurer to relevant employees and directors. • Interview management or board member(s) with responsibilities for risk management oversight to determine level of knowledge and involvement of management or directors in risk management processes. • Interview insurer executives to get a feel for the "tone at the top" of the organization and the level of consistency in applying risk management processes across departments. • Obtain and review information on the insurer's compensation plans to determine that risk management decision-making is not undermined by compensation structure. • Obtain and review job descriptions or performance review criteria for select management positions to determine whether risk management elements are incorporated.
Risk Identification and Prioritization	• Obtain a current copy of the organization's risk listing/universe. • Determine whether appropriate external sources have been used to assist in risk identification (e.g. rating agency information, competitor 10K filings, etc.) where applicable. • Verify that the organization's risk listing/universe is updated/reviewed on a regular basis by requesting copies at various dates. • Assess the insurer's process and scale by which it prioritizes the key risks identified. • Review the approach for and results of the insurer's likelihood, severity and speed of onset risk assessments, if applicable. • Interview select process owners/business unit leaders to verify their role in risk identification and prioritization. • Interview risk management staff to understand and evaluate how risks are identified and aggregated across the organization.

~~Principle~~	~~Possible Test Procedures~~
~~Risk Appetite, Tolerances and Limits~~	• ~~Review the management committee's or board's supporting materials to verify that the organization's risk appetite is reviewed as appropriate.~~ • ~~Review and evaluate how risk appetite, tolerances and limits are set for the insurer.~~ • ~~Determine whether the insurer considers legal entity regulations and capital requirements in setting its overall risk appetite (if applicable).~~ • ~~Review and evaluate steps taken to address breaches in risk limits on a sample basis (if applicable).~~ • ~~Verify, as applicable, whether reasonably forseeable material and relevant risks are assigned risk owners to monitor risks and oversee mitigation plans.~~ • ~~Interview select risk owners to get an understanding of how risk limits are set and updated.~~ • ~~Verify that checks and balances (i.e., supervisory review) are in place to ensure that risk limits are set in accordance with the organization's overall risk appetite.~~
~~Risk Management and Controls~~	• ~~Obtain minutes of internal risk management committee (or equivalent management group) meetings to review frequency and extent of oversight activities.~~ • ~~Obtain a listing of internal audit reports to determine whether risk management processes are subject to periodic review.~~ • ~~Identify and test the operating effectiveness of preventive controls in select areas to determine how risk limits are enforced.~~ • ~~Review and evaluate how specific controls are mapped to legal entities (as appropriate if mapping is relevant to understanding of control).~~
~~Risk Reporting and Communication~~	• ~~Obtain a current copy of the organization's risk dashboard (or equivalent report) to verify that tracking for reasonably foreseeable material and relevant risk areas exists.~~ • ~~Verify the frequency with which risk information is accumulated and reported by selecting a sample of historical risk dashboards (or equivalent reports) to review.~~ • ~~Test the reasonableness of information included on the risk dashboard (or equivalent report) on a sample basis.~~ • ~~Determine whether risk reporting information is evaluated by the board and used by senior management for strategy and planning purposes.~~ • ~~Review and evaluate the timeliness with which breaches in risk limits are reported and communicated to the appropriate authority.~~

~~**Documentation for Section I**~~

~~The Lead State examiner should prepare documentation summarizing the results of the risk management framework assessment by addressing each of the five principles set forth in the Guidance Manual using the template at the end of this section. Each assessment should first provide a summary of the Lead State analyst's initial assessment, followed by a summary of the results of exam procedures, leading to a final exam assessment for each principle. The summary of exam results should provide rationale for any deviation from the Lead State analyst's initial assessment of the principle.~~

~~D~~E. Review of Section II - Insurer's Assessment of Risk Exposure

Section II of the ORSA Summary Report is required to provide a high-level summary of the insurer's quantitative and/or qualitative assessments of its exposure to reasonably foreseeable and relevant material risks. There may be a great deal of variation in how this information is displayed from one insurer to the next, but in most cases, insurers tend to organize this information around the reasonably foreseeable and relevant material risks of the insurer. The Guidance Manual does give

possible examples of relevant material risk categories (credit, market, liquidity, underwriting, and operational risks). In reviewing the information provided in this section of the ORSA, Lead State regulators may need to pay particular attention to risks and exposures that may be emerging or significantly increasing over time.

Lead State examiners may find the information regarding reasonably foreseeable and relevant material risk exposures the most beneficial aspect of the ORSA Summary Report, as this information may be useful in identifying risks and controls for use in the remaining phases of a risk-focused examination. This may be attributed to the fact that Section II provides risk information on the insurance group that may be grouped in categories similar to the NAIC's nine branded risk classifications (see Exhibit L). However, the grouping of risk information in the report is entirely up to the insurer, and the Lead State examiner should not expect each of the nine branded risk classifications to be directly addressed within Section II.

Stress Testing

In addition to providing background information on reasonably foreseeable and relevant material risks the insurer is facing, Section II anticipates the risk exposures to be analyzed under both normal and stressed environments. Therefore, as part of evaluating the information presented, the Lead State examiner is expected to consider the stress scenarios identified and assessment techniques performed by the insurer to quantify the financial impact of risks. In so doing, the Lead State examiner should note the assumptions and methodologies used by the insurer in conducting stress scenarios/testing. The Lead State examiner should obtain information from the Lead State analyst to determine the extent to which the state has already been provided information on the assumptions and methodologies.

The Lead State examiner should consider the assessment techniques the insurer has utilized to evaluate the impact that reasonably foreseeable and relevant material risks could have on its ongoing operations. In reviewing the insurer's efforts in this area, the Lead State examiner's focus would be on considering if additional information and support for the stress testing of individual risks or groups of risks are available in order to test the effectiveness of such processes. In reviewing the insurer's assessment techniques for ~~each of the nine branded risk classifications (if applicable) and other relevant risks~~its material and relevant (key) risks, the Lead State examiner should consider ~~each of~~ the following elements and possible test procedures:

Note: Possible test procedures that could duplicate or overlap with procedures listed in Section I or Section III are marked with an asterisk.

Consideration	**Description**	**Possible Test Procedure(s)**
Risks Assessed	Key risks assessed are consistent with the insurer's risk identification and prioritization process, its business strategy and the regulator's understanding of exposures	• Evaluate the effectiveness of risk presentation and classification ○ If necessary, prepare feedback to the financial analyst related to the mapping of the insurer's key risks to branded risk classifications • Compare risks discussed in Section II to the insurer's risk register and prioritization documentation to ensure that all significant risks have been assessed • Consider the completeness of the key risks identified by considering the insurer's business operations and strategy, as well as information presented in Form F, SEC reports and other filings • Compare risks identified by the insurer to those tracked by regulators on the IPS/GPS and risk-focused examinations • If key risks appear missing, consider discussing/addressing with the insurer
Presentation and Design of ERM Controls	Mitigation strategies and controls to address exposures are accurately presented and effectively designed for all key risks	• Verify that mitigation strategies and controls are clearly presented for all key risks identified in the summary report* • Request and review additional information on mitigation strategies/controls that aren't clearly presented in the report • Determine whether relevant metrics are in place to monitor risk exposures on a regular basis by selecting and reviewing a sample of key reports for review*

Consideration	Description	Possible Test Procedure(s)
		• In conjunction with work performed in Ph. 3 of a risk-focused examination, perform procedures to test the design effectiveness of mitigation strategies/controls for the insurer's key risks
Operating Effectiveness of ERM Controls	Mitigation strategies and controls are operating effectively in addressing the insurer's key risks	• Determine whether risk measurement metrics are compared against tolerances and risk limits by selecting a sample of key risks for review and testing* • Select a sample of risks that have breached tolerances/limits to review and assess the steps taken by the insurer to escalate, remediate and address issues* • In conjunction with work performed in Ph. 3 of a risk-focused examination, perform procedures to test the operating effectiveness of mitigation strategies/controls for the insurer's key risks
Rationale for Assessment Techniques	Assessment techniques and underlying assumptions are appropriately described and supported	• Verify that all significant risks are clearly assessed and presented in Section II of the ORSA Summary Report • Review the descriptions of and rationale for assessment techniques utilized in the ORSA Summary Report for appropriateness • Review the process used to select and document rationale for assumptions used in risk assessment and select a sample of risks to verify documented support for the assumptions used • Request and review additional information on assessment techniques not clearly presented in the report
Effectiveness of Assessment Tecnniques	Assessment techniques and underlying assumptions appear reasonable and in accordance with insurer standards and industry best practices	• Evaluate whether risks have been subjected to quantitative and qualitative analysis in accordance with their underlying characteristics o For those risks only subject to qualitative assessment, determine why they have not been quantitatively assessed (e.g. lack of data, lack of methodology) and consider its appropriateness • Evaluate the reasonableness of assumptions used and scenario/stress testing used by the insurer to assess risks by comparing to historical results and industry best practices and/or consulting with a specialist • Review scenario analysis and stress testing performed to verify that both capital adequacy and liquidity are addressed for all relevant key risks* • Assess whether the time horizons used to measure key risks are appropriate given their nature
Impact of Assessments	Results of assessments indicate that key risks have been effectively mitigated	• Review the results of stress testing and scenario analysis to assess the sufficiency of the insurer's capital/liquidity resources in the event of adverse situations* • If concerns are identified related to scenario results, inquire regarding the insurer's remediation plans and evaluate their adequacy

- ~~Was each of the most significant solvency risks facing the insurer identified and subjected to assessment techniques?~~
- ~~If scenarios were utilized to evaluate/stress the impact of such risks, were they appropriately described and justified?~~
- ~~Were techniques utilized to assess reasonably forseeable material and relevant risks in accordance with insurer standards and industry best practices?~~
    - ~~Did the time horizon or duration of the risks identified have an impact on the nature and extent of the assessment techniques selected?~~

- ~~Did the results of the assessment techniques indicate that the insurer had appropriately mitigated the impact that the risk might have on the insurer?~~
- ~~Do the assessment techniques utilized address issues from both a capital and liquidity perspective?~~

~~**Documentation for Section II**~~

~~Upon the conclusion of the Lead State examiner's review and testing of the information provided in Section II and related processes, documentation should be prepared to discuss whether the insurer included an appropriate discussion of reasonably foreseeable and relevant material risks. The nine branded risk classifications may be discussed within this summary, as well as any additional risk categories that the Lead State examiner deems relevant. In addition, the Lead State examiner should provide an assessment of the corresponding stress assumptions and test results presented for each of the risk categories discussed, keeping in mind that a company is not required to solely focus on the nine branded risk classifications.~~

~~E~~F. Review of Section III - Group Assessment of Risk Capital

~~Section III of the ORSA is unique in that it is required to be completed at the insurance group level, as opposed to the other sections, which may be completed at a legal entity level. However, in many cases, insurers will choose to also complete Sections I and II at the group level. The requirement to complete Section III at the group level is important because it provides the means for Lead State insurance regulators to assess the reasonableness of capital of the entire insurance group based upon its existing business plan.~~ The focus of financial analysis in reviewing Section III will be to understand the insurer's assessment of the ~~reasonableness of~~risk capital of the entire group to withstand potential unexpected losses and detrimental events, as well as the prospective outlook of the insurer's solvency position. The focus of the Lead State examiner in reviewing Section III should be on understanding the process the insurer used to ~~accumulate and present the information provided~~determine its capital needs. To perform this review, the Lead State examiner may need to request additional detail supporting the group capital calculations that the insurer performed.

Insurance groups will use different approaches to group capital calculation~~means to measure estimated risk (required) capital,~~ and they will use different accounting and valuation frameworks. For example, they may determine the amount of capital they need to fulfil regulatory and rating agencies' requirements, but also determine the amount of risk capital they need to absorb unexpected losses that are not accounted for in the reserves. While the insurer is free to select whichever approach or combination of approaches are appropriate to meet its needs, the Lead State examiner should consider whether the approach selected is consistent with the nature, size and extent of risks that the group faces.The Lead State examiner, in conjunction with the Lead State analyst, may need to request that management ~~to~~ discuss their overall approach to capital management and the reasons and details of the approach so that they can be considered in evaluating the estimation of group risk capital~~both the accounting and valuation frameworks, as well as the reasons and details for each. A different accounting basis can result in a significant difference in perceived risk exposures and capital needs.~~

The ORSA Summary Report should summarize the insurer's process for model validation to support the quantification methodology and assumptions chosen to determine the risk capital. The Lead State examiner should evaluate the work that the insurer performed to validate the reasonableness of the quantification methodology and assumptions used. If the ORSA Summary Report does not provide a summary of the model validation process, the Lead State examiner should request copy of the validation report prepared by the insurer.

Many insurers use internally developed capital models to quantify the risk capital. In these cases, ~~T~~the ORSA Summary Report should summarize the insurer's process for model validation to support the quantification methodology and assumptions chosen to de~~termine risk capital., including factors considered an~~d model calibration. The Lead State examiner should evaluate the work that the insurer performed to validate the reasonableness of the quantification methodology and assumptions used. If the ORSA Summary Report does not provide a summary of the model validation process, the Lead State examiner should request copy of the validation report prepared by the insurer. With regard to the determination of ~~the~~ risk capital under stressed conditions, ~~B~~because the risk profile of each insurer is unique, there is no standard set of stress conditions that each insurer should run. However, the Lead State regulator should be prepared to dialogue with management about the selected stress scenarios if there is concern with the rigor of the scenario. In discussions with management, the Lead State regulator should gain an understanding of the modeling methods used to project available and risk capital over

the duration of the insurer's business plan as well as the potential changes to the risk profile of the insurer over this time horizon (i.e. changes to the list of key risks) based on the business plan~~(e.g., stochastic vs. deterministic) and be prepared to dialogue about and understand the material assumptions that affected the model output, such as prospective views on risks~~. Th~~e~~is ~~aforementioned~~ dialogue may occur during either the financial analysis process and/or the financial examination process.

~~In focusing on the insurer's process to calculate and assess its group risk capital, the Lead State examiner will need to consider the source of the group's internal capital assessment. Some insurers may develop a group capital assessment based upon external models developed by third-party vendors, regulators or rating agencies, while other insurers may also consider and assess the results of an internal capital model. While the insurer is free to select whichever approach or combination of approaches are appropriate to meet its needs, the Lead State examiner should consider whether the approach selected is consistent with the nature, size and extent of risks that the group faces. In addition, the Lead State examiner should evaluate the work that the insurer performed to validate the approach and model utilized.~~

Internal Capital Models

The Guidance Manual states the analysis of an insurer's group assessment of risk capital requirements and associated capital adequacy description should be accompanied by a description of the approach used in conducting the analysis. This should include model design decisions, key methodologies, assumptions and considerations used in quantifying available capital and risk capital. Examples of information to be provided in Section III describing an insurer's processes in this area are provided in the Guidance Manual, and Lead State examiners should become familiar with these elements in order to assess an insurer's processes in this area.

In some situations, the insurer might purchase or license economic capital modeling software tools developed by third-party vendors that can be customized and tailored to by the insurer to operate as an internal capital model. Regardless of whether the internal capital model is developed in-house or licensed from a third-party vendor~~In reviewing an insurer's use of internal models~~, the Lead State examiner should gain an understanding of the work that the insurer performed to validate its own models, whether completed by internal audit, a third-party consultant or some other party. The importance of reviewing the insurer's self-validation process is not only to gain comfort on the information provided in Section III of the report, but also due to the fact that the insurer may be making business decisions based on the results of its modeling. This is an important step because the Lead State examiner is encouraged to look to the insurer's own process by which it assesses the accuracy and robustness of its models, as well as how it governs model changes and parameter or assumption setting, and limits Lead State examiner validation of reports to more targeted instances where conditions warrant additional analysis.

Depending upon the strength of the insurer's internal model validation processes, Lead State examiners may need to perform some level of independent testing to review and evaluate the controls over internal model(s) utilized by the insurer for its group economic capital calculation. This is largely due to the challenges inherent in developing, implementing and maintaining an effective internal capital model. In instances where independent testing is deemed necessary, this testing may consist of procedures to evaluate the appropriateness of assumptions and methodologies used in stochastic/deterministic modeling scenarios for individual risks or in estimating the amount of diversification benefit realized. In so doing, the Lead State examiner may need to select a sample of individual risks for review and consideration and involve an actuary to assist in the evaluation. When involving an actuary, the primary focus of this review would be on evaluating the reasonableness of the inputs and outputs of the models. An actuary may be able to provide input on the reasonableness of the inputs, while the outputs may be most easily tested by performing a walkthrough in which the inputs are modified, and the Lead State examiner or actuary evaluates and discusses with the insurer the impact that the change has on the outputs. There is no one set of assumptions or methodologies that fits every ~~company~~insurer. ~~The Lead State examiner may consider asking questions about the modeling approach that the company uses, as such questions may provide the company an opportunity to elaborate on information provided in the ORSA Summary Report and further the Lead State examiner's understanding.~~

External Capital Models

~~For some insurers, the group capital assessment may be based upon~~Many insurers utilize the output of external ~~capital~~ models (e.g., cat models, economic scenario generators) as an input into their internally developed capital models. These models are typically developed by third-party vendors and made available to the insurer through either a licensing or outsourced service agreement. In other instances, the insurer may use an external capital model developed for rating agency

or regulatory purposes to assist in quantifying its own capital needs. ~~If an insurer presents its standing in relation to external capital models, the insurer may provide information showing its potential standing after considering the impact of stresses. This information may be beneficial as it can demonstrate what types of events an insurer could withstand before potentially losing its rating or violating regulatory capital requirements. While some of this information may be presented in Section II of the report, the impact of stresses on external capital models, while not required, should be considered in an assessment of Section III. There are several ways this can be demonstrated, including the rigor the insurer applies to its stress scenarios.~~

If an insurer bases its group capital assessment ~~largely~~ on third-party vendor tools, rating agency capital calculations or regulatory capital requirements, the Lead State examiner should consider what validation efforts have been conducted to allow reliance to be placed on external models~~the appropriateness of such reliance based upon the nature, scale and complexity of the insurer's reasonably foreseeable and relevant material risks~~. In addition, the Lead State examiner should consider whether the insurer ~~has applied~~applies a reasonable range of stress scenarios to the outputs of these ~~its available capital to determine its prospective standing in relation to external capital~~ models under a wide range of different scenarios.

Prospective Solvency Assessment
The Guidance Manual requires the insurer to consider the prospective solvency of the group. Many companies will include information developed as part of their strategic planning, including pro forma financial information displaying possible outcomes as well as projected capital adequacy in those future periods based on the insurer's defined capital adequacy standard. However, the Lead State examiner should review the information provided to understand the impact such an exercise has on the ongoing business plans of the group. For example, to the extent such an exercise suggests that at the insurer's particular capital adequacy under expected outcomes, the group capital position will weaken, or recent trends may result in certain internal limits being breached, the Lead State examiner should understand what actions the insurer/group expects to take as a result of such an assessment (e.g., reduce certain risk exposure, raise additional capital, etc.). In addition, the Lead State examiner should consider how any planned changes in risk exposure or strategy may affect both the insurer's short- and long-term solvency positions. Finally, the Lead State examiner should consider whether the assumptions and methodologies used in preparing the prospective solvency assessment are consistent with the insurer's business strategy and should assess whether these assumptions and methodology are reasonable.~~industry best practices~~. However, there is no one set of assumptions or methodologies that fit every insurer. Regulators must use professional judgment to assess the reasonability and plausibility of capital model inputs and outputs. ~~This is not to suggest that the Lead State examiner should not consider asking questions about the modeling approach used by the insurer, as such questions may provide the insurer an opportunity to elaborate on information provided in the ORSA Summary Report and further the Lead State examiner's understanding.~~

In conducting examination procedures to verify and evaluate the insurer's processes for calculating group risk capital and a prospective solvency assessment, the Lead State examiner should consider the following elements and possible test procedures:

Topic	**Considerations**	**Possible Test Procedure(s)**
Capital Metric(s) Used	The capital metric(s) utilized to assess the group's overall capital target are clearly presented and described.	• Review and validate information presented on capital measurement tools for completeness and accuracy • Gain an understanding of and evaluate the scope and purpose of each of the capital models used by the group (internal and external)
	The capital metric(s) selected address all key risks of the group.	• Gain an understanding of the risks assessed through the capital metric(s) used and determine whether all key risks of the group are included in the quantification of risk capital • For external capital metrics, evaluate the appropriateness of their use considering the risk profile of the insurer/group o If necessary, involve a specialist in this evaluation
	Individual risk components are subject to reasonable/appropriate modeling scenarios.	• Gain an understanding and evaluate the use of stochastic/deterministic scenarios in modeling the group's exposure to key risks • If necessary, involve a specialist in evaluating the appropriateness of scenarios, assumptions and

		methodologies used to calculate and allocate capital to individual risk components • Gain an understanding of and evaluate the insurer's/group's processes for addressing key risks not directly quantified in its capital metrics into the risk capital process
	Model results are calibrated to an appropriate security standard	• Gain an understanding of the risk capital metric (e.g. Value at Risk, Tail Value at Risk) and security standard ~~(e.g. 99.5%)~~ used in the capital model and evaluate their appropriateness considering the insurer's risk profile and exposure to tail risk
Group Risk Capital (GRC)	Group risk capital is clearly presented and described on both an aggregate and per risk basis.	• Verify that the group risk capital presented in the ORSA Summary Report appropriately reconciles to modeled results and investigate any significant differences • Identify and review significant changes in group risk capital (individual components and in aggregate) from the prior filing
Impact of Diversificiation Benefit	Diversification benefit is calculated based on correlations in key risk components that are reasonable/appropriate	• Obtain and review information on the risk aggregation process used by the insurer (i.e. correlation matrixes or copulas) to address risk correlations and review the process and the overall diversification benefit taken for reasonableness • If necessary, involve a specialist in reviewing and testing the aggregation process and diversification benefit calculation
Available Capital	The group's capital is of high quality and sufficient to meet its business needs	• Provide information on and discuss the amount of capital available to absorb losses across the group, recognizing that there may be fungibility issues relating to capital trapped within various legal entities and jurisdictions for which regulatory restrictions and supervisory oversight constrain the extent and timing of capital movement across the group. • Describe management's strategy to obtain/deploy additional capital across the group should the need arise. Determine if there is any double counting of capital through the stacking of legal entities.~~Consider whether the group's capital is freely available to absorb losses and is permanent and fungible (i.e. available to be distributed as needed) in form~~ • Assess the quality of group capital by determining whether it includes items such as double counting/stacking of capital and/or excessive amounts of goodwill, intangible assets or deferred tax assets, etc.
Excess Capital	Results of capital metrics demonstrate the group has sufficient capital to meet its obligations over a wide range of expected outcomes	• Compare methods utilized and overall results to those from prior periods to assess consistency and identify/evaluate significant changes. • If concerns are identified over the level of excess capital available, perform procedures to determine whether sufficient additional sources of capital are available to the group and whether there are plans to access these additional sources of capital • Review the results of stress testing and scenario analysis to assess the sufficiency of the insurer's capital/liquidity resources in the event of adverse situations
Impact of Stresses on GRC	The results of external capital models are subject to consideration under a wide range of stress scenarios	• Assess how the insurer has determined the number of scenarios to run under a stochastic modeling approach (if utilized) • Assess whether the insurer has applied reasonable unfavorable stress scenarios in determining an appropriate level of risk capital and liquidity through use of a deterministic modeling approach, particularly if relying primarily on external capital metrics

		○ Evaluate whether rating downgrades or regulatory intervention could impact the insurer's ability to achieve its business strategy under certain scenarios
Governance and Validation	Capital models and metrics utilized are subject to a sufficient level of governance, oversight and ongoing validation.	• Obtain and review the model governance policy to understand and evaluate the role of the BOD and Senior Management in overseeing internal capital models • Obtain and review the model change authority policy to understand who is authorized to make changes to the capital model • Verify the operating effectiveness of oversight responsibilities by reviewing supporting documentation on a sample basis. • Select a sample of significant changes in the internal capital model to verify appropriate levels of change authority and supervisory review and approval. • Assess the level of oversight in place over the selection and application of the risk capital metric and security standard used in the internal capital model. • Obtain and review the data quality policy (if available) and review work performed by the insurer to validate data inputs for completeness and accuracy
Prospective Solvency Assessment	Prospective solvency is projected and evaluated in accordance with the group's ongoing business strategy/plans	• Evaluate whether the assessment covers an appropriate time horizon, considering the insurer's business plan and strategy. • Evaluate the methodologies to project available and risk capital over the time horizon and whether these methodologies take into account future new business. • Evaluate whether the expected changes in risk profile are consistent with the business strategy and plans presented by the group and how these changes have been incorporated into the capital projections • If concerns are identified through a review of the prospective solvency assessment, discuss with the insurer and perform additional procedures as necessary.

~~**Documentation for Section III**~~

~~The Lead State examiner should summarize exam conclusions regarding the insurer's assessment of group risk capital by describing the method used (e.g., internal, external, combination) by the insurer to assess its overall group capital target and its basis for such a decision.~~

~~If internal capital models are utilized in the process to assess group risk capital, a discussion of material assumptions and methodologies utilized in calculating capital allocated to individual risk components should be provided. In addition, material assumptions and methodologies utilized in calculating a diversification credit should be discussed. Finally, controls over model validation and/or results of independent testing performed in this area should be discussed.~~

~~If external capital models are utilized in the process to assess group risk capital, the Lead State examiner should describe the external capital models utilized and their importance to the insurance group. In addition, a discussion of the stress scenarios and testing applied to the external capital model to account for a wide range of potential events should be provided.~~

~~The Lead State examiner should also summarize exam conclusions regarding the prospective solvency assessment provided by the insurance group. This summary should discuss the group's prospective solvency projections and projected changes in risk exposures. For example, the Lead State examiner should discuss the material assumptions and methodologies that the insurer used in performing a prospective solvency assessment and whether the assumptions are consistent with the insurer's overall business plan and strategy. Finally, the Lead State examiner should discuss any material changes in individual risk exposures outlined by the insurer and whether any of the information provided presents concerns to be addressed in the remaining phases of the examination.~~

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Overall Assessment of ORSA/ERM Function

After conducting procedures to verify, validate and assess the processes and information reported on the insurer's ERM function in each section of the ORSA Summary Report, the Lead State examiner should reach an overall conclusion regarding the maturity and reliability of the function. In so doing, the Lead State examiner should consider both processes covered in the ORSA and verified during the onsite exam, as well as ERM processes that may not have been covered in the ORSA Summary Report but were identified and tested during the exam. In reaching an overall assessment, the Lead State examiner can consider the use of Handbook guidance, examiner judgment and/or the use of third-party tools such as the Risk and Insurance Management Society's (RIMS) Risk Maturity Model (RMM).

Insurers or insurance groups may utilize various frameworks in developing, implementing and reporting on their ORSA processes (e.g. COSO Integrated Framework, ISO 31000, IAIS ICP 16, other regulatory frameworks, etc.). Elements of the RMM have been outlined in this guidance to provide a reference for use in reviewing and assessing ERM/ORSA practices. However, as various frameworks may be utilized to support effective ERM/ORSA practices, Lead State regulators should be mindful of differences in frameworks and allow flexibility in assessing ERM. The RMM provides a scale of five maturity levels upon which an insurer can be assessed. The five maturity levels can generally be defined as follows:

- Leadership: Risk management is embedded in strategic planning, capital allocation and other business processes, and is used in daily decision-making. Risk limits and early warning systems are in place to identify breaches and require corrective action from management and, where appropriate, the board of directors or committee thereof ~~(hereafter referred to as "board") and management~~.

- Managed: Risk management activities are coordinated across business areas, and tools and processes are actively utilized. Enterprise-wide risk identification, monitoring, measurement and reporting are in place.

- Repeatable: The insurer has risk management processes in place designed and operated in a timely, consistent and sustained way. The insurer takes action to address issues related to high priority risks.

- Initial: The insurer has implemented risk management processes, but the processes may not be operating consistently and effectively. Certain risks are defined and managed in silos, rather than consistently throughout the insurer.

- Ad hoc: The insurer has not developed or documented standardized risk management processes and is relying on the individual efforts of staff to identify, monitor and manage risks.

The design of ERM/ORSA practices should appropriately reflect the nature, scale and complexity of the insurer. In assessing the effectiveness of an insurer's ERM program, Lead State regulators should understand the level of maturity that is appropriate for the insurer based on its unique characteristics. Attainment of "Leadership" or "Managed" levels of maturity for ERM/ORSA practices may not be appropriate, nor should it be expected, for all companies. Additionally, it would be expected that the level of testing performed in an examination to verify or validate ERM maturity would be commensurate with the level of maturity assessed. For example, ERM programs assessed at a "Leadership" or "Managed" level of maturity would typically be subject to more of the suggested exam procedures highlighted above than those programs assessed at a lower level of maturity.

~~F~~G. ORSA Review Documentation ~~Template~~

As outlined above, the Lead State examiner is expected to incorporate a review of ORSA information into ongoing on-site examination activities, including workpaper documentation. This includes documenting the work completed to verify and validate information presented in the three sections of the ORSA Summary Report, as well as assessing the effectiveness and maturity of the insurer's ERM processes. The results of such work can be documented in various areas of the examination file (e.g. Phase 1 documentation, Exhibit M, various risk matri~~x~~ces, etc.), as deemed appropriate.

The Lead State examiner is also expected to summarize the results and key findings/assessments in the Summary Review Memorandum (SRM) for communication to others within the department. See Exhibit AA – Summary Review Memorandum for additional guidance on relevant information to be included in the SRM on the ORSA/ERM function.

ORSA Summary Report Examination Results
Insurer XYZ 12/31/XX Examination
Using ORSA Summary Reported Dated XX/XX/XXXX

Section I

Prepare documentation summarizing the results of the risk management framework assessment by addressing each of the five principles set forth in the Guidance Manual. Each assessment should first provide a summary of the Lead State analyst's initial assessment, followed by a summary of the results of Lead State exam procedures, leading to a final exam assessment for each principle. The final Lead State exam assessment should provide adequate rationale for any deviation from the Lead State analyst's initial assessment of the principle.

A **Risk Culture and Governance** – Governance structure that clearly defines and articulates roles, responsibilities and accountabilities, and a risk culture that supports accountability in risk-based decision making.

Initial Lead State Analyst Assessment:

Summary of Lead State Exam Results:

Final Lead State Exam Assessment:

☐5 ☐4 ☐3 ☐2 ☐1 ☐0

B **Risk Identification and Prioritization** – Risk identification and prioritization processes are key to the organization. Responsibility for this activity is clear. The risk management function is responsible for ensuring the process is appropriate and functioning properly.

Initial Lead State Analyst Assessment:

Summary of Lead State Exam Results:

Final Lead State Exam Assessment:

☐5 ☐4 ☐3 ☐2 ☐1 ☐0

C **Risk Appetite, Tolerances and Limits** – A formal risk appetite statement, associated risk tolerances and limits are foundational elements of risk management for an insurer. Understanding of the risk appetite statement ensures alignment with risk strategy set by senior management and reviewed and evaluated by the board.

Initial Lead State Analyst Assessment:

Summary of Lead State Exam Results:

Final Lead State Exam Assessment:

☐5 ☐4 ☐3 ☐2 ☐1 ☐0

~~D **Risk Management and Controls** – Managing risk is an ongoing ERM activity, operating at many levels within the organization.~~

~~Initial Lead State Analyst Assessment:~~

~~Summary of Lead State Exam Results:~~

~~Final Lead State Exam Assessment:~~

~~☐5 ☐4 ☐3 ☐2 ☐1 ☐0~~

~~E **Risk Reporting and Communication** – Provides key constituents with transparency into the risk-management processes and facilitates active, informal decisions on risk-taking and management.~~

~~Initial Lead State Analyst Assessment:~~

~~Summary of Lead State Exam Results:~~

~~Final Lead State Exam Assessment:~~

~~☐5 ☐4 ☐3 ☐2 ☐1 ☐0~~

~~**Overall Section I Assessment**~~
~~After considering the assessment of each of the five previously identified principles and taking into account any additional factors that the examiner identified during the review of the ERM framework, develop an overall assessment of the insurer's risk management framework using the same risk maturity model. The assessment, along with findings from Section II and Section III, will assist the examination team in determining the extent of reliance to be placed on the insurer's ORSA/ERM processes throughout the remaining phases of a full-scope examination and through modifications to the ongoing supervisory plan. Results should also be provided to the analyst at the conclusion of the examination.~~

~~Overall Lead State Assessment Rationale:~~

~~☐5 ☐4 ☐3 ☐2 ☐1 ☐0~~

~~**Section II**~~

~~Prepare documentation summarizing a review and assessment of information that the insurer provided on its reasonably foreseeable and relevant material risks, and corresponding stress assumptions and test results.~~

~~A Based on your knowledge of the group, did the insurer include in its ORSA a discussion of risks and related stresses that you consider appropriate for the group? **Note whether the following are applicable or not.**~~

~~A **Credit** – Amounts actually collected or collectible are less than those contractually due or when payments are not remitted on a timely basis.~~

~~Lead State Examiner Summary of Risks and Stress Testing:~~

~~B **Legal** – Nonconformance 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.~~

~~Lead State Examiner Summary of Risks and Stress Testing:~~

C **Liquidity** – This is the inability to meet contractual obligations as they become due because of an inability to liquidate assets or obtain adequate funding without incurring unacceptable losses.

Lead State Examiner Summary of Risks and Stress Testing:

D **Market** – Movement in market rates or prices (such as interest rates, foreign exchange rates or equity prices) adversely affects the reported and/or market value of investments.

Lead State Examiner Summary of Risks and Stress Testing:

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

Lead State Examiner Summary of Risks and Stress Testing:

F **Pricing/Underwriting** – Pricing and underwriting practices are inadequate to provide for risks assumed.

Lead State Examiner Summary of Risks and Stress Testing:

G **Reputation** – Negative publicity, whether true or not, causes a decline in the customer base, costly litigation and/or revenue reductions.

Lead State Examiner Summary of Risks and Stress Testing:

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

Lead State Examiner Summary of Risks and Stress Testing:

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

Lead State Examiner Summary of Risks and Stress Testing:

J **Other** – Discuss any other reasonably foreseeable and relevant material risks facing the insurer that do not fit into one of the nine branded risk classifications identified above.

Lead State Examiner Summary of Risks and Stress Testing:

Overall Risk Assessment Summary
After considering the various risks that the insurer identified, as well as an analysis of such risks, develop an overall risk assessment summary of possible concerns that may exist.

Section III

Prepare documentation summarizing a review of the group capital assessment and prospective solvency assessment provided by the group as follows:

A Summarize exam conclusions regarding the insurer’s assessment of group risk capital by addressing each of the following elements:

1. **Overall Method of Capital Measurement**: Discuss the method(s) (e.g., internal, external, combination) that the insurer used in assessing its overall group capital target and its basis for such a decision.

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~~Lead State Examiner Summary:~~

~~2. **Internal Capital Models**: If internal capital models are utilized in the process to assess group risk capital, discuss each of the following items:~~

~~1. Material assumptions and methodologies utilized in calculating capital to be allocated to individual risk components.~~

~~Lead State Examiner Summary:~~

~~2. Stress scenarios and testing applied to individual risk components.~~

~~Lead State Examiner Summary:~~

~~3. Material assumptions and methodologies utilized in calculating a diversification credit based on the correlation between risk components.~~

~~Lead State Examiner Summary:~~

~~4. Controls over model validation and/or results of independent testing performed in this area.~~

~~Lead State Examiner Summary:~~

~~3. **External Capital Models**: If external capital models are utilized in the process to assess group risk capital, discuss each of the following items:~~

~~1. External capital models utilized and their importance to the insurance group.~~

~~Lead State Examiner Summary:~~

~~2. Stress scenarios and testing applied to the external capital model to account for a wide range of potential events.~~

~~Lead State Examiner Summary:~~

~~B Summarize exam conclusions regarding the prospective solvency assessment that the insurance group provided by discussing each of the following elements:~~

~~1. **Prospective Solvency Projections**: Discuss the material assumptions and methodologies that the insurer utilized in performing a prospective solvency assessment. Are assumptions consistent with the insurer's overall business plan and strategy?~~

~~Lead State Examiner Summary:~~

~~2. **Changes in Risk Exposure**: Discuss material changes in individual risk exposures that the insurer outlined. Document whether any of the following information provided present concerns to be addressed in the remaining phases of the examination.~~

~~Lead State Examiner Summary:~~

~~G~~H. Utilization of ORSA Results in the Remaining Phases of the Examination

The review and assessment of the insurer's ORSA/ERM processes during an on-site examination is meant to provide input and feedback to the Lead State financial analyst for updating the insurer's ongoing supervisory plan and in reaching a final assessment regarding the maturity of the insurer's ERM framework. A maturity assessment should consider the results of work performed to verify, validate, and assess ERM/ORSA processes as described in the previous sections above. In

addition, a maturity assessment should consider the size and complexity of the insurer/group, as well as the concept of proportionality in reaching the overall assessment.

However, tThe knowledge that the Lead State examiner gains in performing this review and assessment should also be utilized to gain efficiencies, if appropriate, in the seven-phase risk-focused examination process.

The extent to which the Lead State examination team utilizes information from the insurer's ORSA/ERM processes to create efficiencies should depend upon the overall assessment of the insurer's ERM framework as follows:

Maturity Level	Resulting Examination Impact
5 Leadership	The Lead State examination team may place a high degree of reliance on the insurer's general ERM framework and related controls and may utilize ORSA conclusions to substantially reduce and focus the scope of remaining examination activities. For example, in examining insurers with ERM functions at a "Leadership" level, most (if not all) other than financial reporting risks reviewed during the exam would be expected to come from risks assessed within Section II of the ORSA Summary Report, with corresponding mitigation strategies and controls sourced from ERM/ORSA functions.
4 Managed	The Lead State examination team may place a moderate-high degree of reliance on the insurer's general ERM framework and related controls, while considering additional testing for significant individual controls/strategies. ORSA conclusions may be utilized to reduce and focus the scope of remaining examination activities. For example, in examining insurers with ERM functions at a "Managed" level, many other than financial reporting risks reviewed during the exam would be expected to come from risks assessed within Section II of the ORSA Summary Report, with corresponding mitigation strategies and controls sourced from ERM/ORSA functions.
3 Repeatable	The Lead State examination team may place a moderate degree of reliance on the insurer's general ERM framework and related controls, but significant individual controls/strategies should be subject to testing. ORSA information should be considered in limiting and focusing the scope of remaining examination activities. For example, in examining insurers with ERM functions at a "Repeatable" level, some other than financial reporting risks reviewed during the exam would be expected to come from risks assessed within Section II of the ORSA Summary Report.
2 Initial	The Lead State examination team may place a low degree of reliance on the insurer's general ERM framework and related controls. Individual controls/strategies should be subject to examination testing. ORSA information should be considered in focusing the scope of remaining examination activities.
1 Ad hoc	The Lead State examination team should not place reliance on the insurer's ERM framework and related controls without performing testing on individual controls/processes. ORSA information can be considered in scoping examination activities, but it should be supplemented by additional tools and resources.
0	The Lead State examination team should not place any reliance on nor consider the results of the insurer's ERM/ORSA framework in scoping examination activities.

While this guidance is developed with ORSA-compliant insurers in mind, the concepts may also be applied to non-ORSA companies that have implemented risk management functions. Therefore, the Lead State examination team should customize the consideration of ERM processes during each examination to meet the needs of the insurer being reviewed.

While the results of the ERM maturity assessment can be broadly utilized in customizing risk-focused examination activities, additional guidance has been prepared to provide examples of specific information obtained through the

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ERM/ORSA review process that may be utilized to reduce or facilitate the remaining phases of the financial examination. The Lead State examination team may be able to utilize information obtained through a review of ERM/ORSA processes to gain exam efficiencies as outlined in the following table:

ERM/ORSA Information	Related Examination Process(es)	Explanation
Section I – Description of the Insurer's Risk Management Framework	Phase 1, Part Two: Understanding the Corporate Governance Structure	The Lead State examiner's work to review and assess the insurer's ERM framework (as reported in the ORSA) may be used to satisfy the requirement to review the insurer's risk management practices as part of the Phase 1 corporate governance review. The overall assessment of ORSA/ERM ~~maturity level assessment~~framework discussed above should be completed during the planning stage of an exam.
Section I – Risk Identification & Prioritization; Section II – Insurer's Assessment of Risk Exposure	Phase 1, Part Five: Prospective Risk Assessment; Exhibit V – Overarching Prospective Risk Assessment; Phase 2: Identifying and Assessing Inherent Risks	The risks described, prioritized and quantified through the insurer's ERM/ORSA processes should assist the Lead State examiner in identifying and assessing reasonably foreseeable and relevant material risks to be reviewed during the exam.
Section I – Risk Appetites Tolerances and Limits; Section II – Insurer's Assessment of Risk Exposure	Phase 3 – Identify and Evaluate Risk Mitigation Strategies/ Controls; Exhibit V – Overarching Prospective Risk Assessment	Risk tolerances and limits that the insurer set may represent strategies/controls that can be relied upon to mitigate reasonably foreseeable and relevant material risks in Phase 3 of the examination process or to address overarching prospective reasonably foreseeable and relevant material risks.
Section II – Insurer's Assessment of Risk Exposure; Section III – Group Assessment of Risk Capital	Phase 5 – Establish/ Conduct Detail Test Procedures	The results of stress testing that the insurer performed, as well as the amount of capital allocated to individual risk components, may assist the Lead State examiner in determining the ultimate impact of unmitigated residual risks on the insurer. To the extent that the insurer accepts certain residual risks and capital is allocated to the risk under a wide range of potential outcomes, the Lead State examiner may choose to document this fact in Phase 5 ~~and~~ to avoid documenting a finding or ongoing concern in this area. However, the documentation should discuss reasonably foreseeable and relevant material risks, capital and liquidity in sufficient detail to address future solvency concerns in these areas.
Section III – Group Assessment of Risk Capital	Exhibit DD – Critical Risk Categories (Capital Management)	The overall results of the group risk capital assessment, as well as the prospective solvency assessment that the insurer performed, should provide evidence of whether the insurer's capital management ~~plans are~~is adequate. This information may be used to address reasonably foreseeable and relevant material risks related to capital management required to be considered by Exhibit DD – Critical Risk Categories.

Section III – Prospective Solvency Assessment	Phase 6 – Update Prioritization & Supervisory Plan; Phase 7 – Draft Exam Report & Management Letter	Information provided in the insurer's prospective solvency assessment should address the insurer's ongoing strategy and business outlook. This information may be useful in reaching overall exam conclusions and determining steps for future monitoring efforts required to be documented in Phases 6 and 7 of the examination and communicated to financial analysis through the SRM.

EXHIBIT M
UNDERSTANDING THE CORPORATE GOVERNANCE STRUCTURE

The purpose of this exhibit is to assist the examiner in documenting the understanding and assessment of an insurer's corporate governance policies and practices, including its ERM function. As insurers are expected to demonstrate different corporate governance practices in accordance with the nature and extent of their operations, examiners should not expect the practices of each individual insurer to specifically match the guidance provided in this exhibit. Therefore, the focus of an examination team's considerations in this area should be to determine whether the practices implemented by the insurer are reasonable and effective.

The examination team should first attempt to utilize information obtained through Exhibit B – Examination Planning Questionnaire, Exhibit Y – Examination Interviews and other planning sources (including information provided to the financial analyst and any other information available to the examiner) before requesting any additional information that may be necessary to gain an understanding and perform an assessment of corporate governance. A favorable overall assessment of governance does not, by itself, serve to reduce the scope or extent of examination procedures; rather, specific governance controls need to be assessed for their adequacy of the management of specific risks, in conjunction with other controls designed to manage the same.

In conducting examinations of insurers that are part of a holding company group, the work to gain an understanding and assess corporate governance should focus on the level at which insurance operations are directly overseen (e.g., ultimate parent company level, insurance holding company level, legal entity level, etc.). However, in certain areas, it may be necessary to review governance activities occurring at a level above or below the primary level of focus. Many critical aspects of governance usually occur at the holding company level. The exam team should seek to coordinate the review and assessment of group corporate governance in accordance with the exam coordination framework and lead state approach outlined in Section 1 of this Handbook. Where possible, in a coordinated examination, the lead state's work on the corporate governance assessment should be utilized to prevent duplication of effort and to leverage examination efficiencies. Additionally, the examiner should utilize the Corporate Governance Annual Disclosure (CGAD), which is required to be filed with the Department of Insurance (DOI) annually in accordance with the *Corporate Governance Annual Disclosure Model Act* (#305) and *Corporate Governance Annual Disclosure Model Regulation* (#306). The CGAD provides a narrative description of the insurer's or insurance group's corporate governance framework and structure and may enhance examination efficiencies when leveraged. Examiners should also ensure they understand/leverage the Holding Company Analysis work performed by the lead state's financial analyst, as well as the Lead State's review of the ORSA filing, to understand and assess the company's corporate governance, as well as the filings noted above.

Detail Eliminated to Conserve Space

E. REVIEWING THE RISK MANAGEMENT FUNCTION

A review of the entity's risk management function should be conducted through discussions with senior management and the board of directors and through gaining an understanding of the risk management function including inspection of relevant risk management documentation.~~. For companies subject to the Own Risk and Solvency Assessment (ORSA),~~ The ORSA guidance outlined in Section 1, Part X of this Handbook includes procedures which may assist the examiner in conducting a robust review of the company's risk management practices and policies. ~~a review of the ORSA summary report – including completion of the ORSA Documentation Template in Section 1, Part X of this Handbook – may be used in place of completing this section. For companies that do not submit an ORSA summary report, the ORSA guidance contained in this Handbook may still be a helpful tool in assessing the maturity of an insurer's risk-management framework, which should include an assessment of each of five key principles.~~ While each of the key principles can be applicable to all insurers, it is important to consider variations in size and complexity and alter expectations appropriately. As a general guideline, the following areas should be considered in conducting a review of the risk-management function:

1. Risk Culture and Governance

   a. What kind of risk-management culture is demonstrated throughout the organization? What does the culture indicate regarding the importance of risk management to the organization?

2. Risk Identification and Prioritization
   a. How are existing risks identified, monitored, evaluated and responded to? Does risk assessment take probability, potential impact and time duration into account?
   b. How are emerging and/or prospective risks identified, monitored, evaluated and responded to?

3. Risk Appetite, Tolerances and Limits
   a. How are risk tolerances, appetites and limits defined and communicated throughout the organization? Does the insurer maintain appropriate policies outlining specific obligations of employees in dealing with risk?
   b. How does the organization use the risk information it gathers to determine its capital needs?

4. Risk Management and Controls
   a. How are responsibilities for risk-management functions delegated and monitored within the organization?

5. Risk Reporting and Communication
   a. What is the involvement of the board of directors in the risk-management function of the organization?

An effective risk-management function is essential in providing effective corporate governance over financial solvency. During the latter phases of the risk-focused examination, the examiner will document a review of the entity's individual risk-management functions within the system. However, during a review of the entity's corporate governance, the examiner should document the review of the entity's risk-management function as a whole, as well as its place and importance in the entity's corporate governance structure. For ORSA companies, the knowledge gained in performing a review and assessment of enterprise risk management (ERM) may also be utilized to gain efficiencies, if appropriate, in accordance with the insurer's assessed maturity level, in the latter phases of the risk-focused examination as described in Section 1, Part X of this Handbook.

F. DOCUMENTATION

The examination team should document its understanding and assessment of the entity's governance, as well as its assessment on the related impact on the examination. This summary should include a description of any unique examination procedures, including special inquiries that are considered necessary to any significant risks identified as a result of the assessment.

The Risk Assessment Matrix, as the central documentation tool, should be utilized for the identification and assessment of individual solvency risks requiring review through the risk assessment process. However, documentation on the understanding and assessment of corporate governance is at the discretion of the examiner and would not typically be presented in a Risk Assessment Matrix. For most companies, a memorandum and/or corresponding documentation in the electronic workpapers addressing the items presented in this exhibit should provide sufficient documentation. For example, the documentation could summarize the attributes and techniques supporting the examiner's overall evaluation, any resulting examination scope implications, and the approach used to validate the more significant attributes and techniques. For smaller companies, documentation of the examination's consideration of corporate governance may be provided in the appropriate section of Exhibit I – Examination Planning Memorandum.

Specific findings or concerns related to an insurer's corporate governance practices should be accumulated for inclusion in a management letter (or similar document) to provide feedback and recommendations to the insurer. In addition, the examination should utilize Exhibit AA – Summary Review Memorandum (or similar document) to summarize its understanding and assessment of the insurer's overall corporate governance framework, as well as the maturity and reliability of its ERM function, to ensure appropriate communication back to the financial analyst. ~~it may be necessary for the examination to document information on the corporate governance assessment for communication back to the financial analyst through the use of Exhibit AA – Summary Review Memorandum (or similar document).~~

EXHIBIT AA
SUMMARY REVIEW MEMORANDUM

The following is an illustration of how a summary review memorandum (SRM) may be set up to assist examiners in documenting the key issues and results of a risk-focused examination that should be shared with the Chief Examiner and the assigned analyst. The illustration also includes a high-level overview of the insurer's holding company structure (if applicable) and how that structure affected exam coordination with other states. Additionally, the SRM includes discussion of the insurer's governance and risk management practices, and a summary, by branded risk classification, of significant exam findings and/or concerns warranting communication. These findings may include overarching solvency concerns, examination adjustments, other examination findings, management letter comments, subsequent events and other residual risks or concerns the examiner may want to communicate to department personnel. The final sections, prioritization level and changes to the supervisory plan, provide discussion of the examiner's overall conclusions regarding ongoing monitoring, including specific follow-up recommended to the analyst .

This exhibit provides an example template, which is not intended to be all-inclusive and should be tailored to each examination. Reference to each branded risk classification is necessary and should be included in the examination's SRM; however, it is not necessary to address each of the supporting areas and points discussed herein. Therefore, the examiner-in-charge should use his or her judgment in determining which sections of this illustration are applicable and document any other relevant information deemed necessary. The purpose of the SRM is to provide interpretative analyses relative to significant examination areas and to provide a basis for communicating examination findings and recommendations to department personnel. In so doing, the SRM will provide input into the Insurer Profile Summary (IPS) and the supervisory plan. In fulfilling this purpose, the SRM should not merely repeat comments made in the examination report or management letter, but instead provide a comprehensive summary of examination conclusions both objective and subjective in nature. Conclusions should provide information necessary for ongoing supervision of the insurer that includes areas of concern as well as areas that support a positive outlook for the insurer.

COMPANY NAME: **EXAMINATION DATE:**

EXAMINATION BACKGROUND

The purpose of this section of the memorandum is to document at a high level what, if any, group the insurer belongs to, if the insurer was part of a coordinated exam and how the coordinated exam was conducted. Additional information regarding the timing of the exam, staffing resources utilized—including what specialists were used—or other background information necessary to understand the results presented in the memo should also be included.

CORPORATE GOVERNANCE ~~AND RISK MANAGEMENT~~

The purpose of this section of the memorandum is to summarize an understanding and assessment of the ~~an~~ insurer's corporate governance including its board of directors, senior management and organizational structure.~~, as well as the results of the review of the enterprise risk management (ERM) function of the insurer.~~ This assessment should include information obtained during both the planning and the completion stages of the examination. Therefore, consideration of information gathered during C-level interviews, completion of Exhibit M and review of the insurer's Own Risk and Solvency Assessment (ORSA), if applicable, should be combined with information obtained during detail testwork to reach a concise final assessment that focuses on communicating significant areas of strength or weakness within the overall corporate governance structure ~~and ERM functions~~ of the insurer. When the insurer is part of a holding company, documentation should reference the level at which conclusions are reached. Additional assessment may be necessary at the individual entity level, but the primary focus of the assessment will commonly be at the holding company level in a coordinated examination.

RISK MANAGEMENT

The purpose of this section of the memorandum is to summarize an understanding and assessment of the insurer's enterprise risk management (ERM) function of the insurer. This assessment should include information obtained during ~~both~~ the planning, fieldwork, and ~~the~~ completion stages of the examination. ~~Therefore, consideration of information gathered during~~

C level interviews, completion of Exhibit M and review of the insurer's Own Risk and Solvency Assessment (ORSA), if applicable, should be combined with information obtained during detail testwork to reach a concise final assessment.In documenting the regulator's assessment, regulators may consider using the maturity terminology established within the Risk Maturity Model (i.e. Leadership, Managed, Repeatable, Initial, and Ad hoc). that focuses on communicating significant areas of strength or weakness within the overall ERM functions of the insurerIn documenting the key points for the regulator's assessment of the maturity and reliability of the insurer's company's ERM's functionmaturity and reliability, consideration should be given to the following areas, if applicable:

- Information on key entity level ERM controls that were validated during the examination
- Summary assessment of significant areas of strength and weaknesses within the ERM framework
- Work performed to review the company's capital modeling processes
- Work performed to review the company's stress testing framework
- Evaluation of the company's key risks, risk appetites, tolerances and limits
- Evaluation of the company's capital and surplus (i.e. quality of capital, availibility of capital, etc.)
- Evaluation of the company's prospective risk assessment and capital position
- Recommendations to be made to the company based on ERM work performed

When the insurer is part of a holding company, documentation should reference the level at which conclusions are reached. Additional assessment may be necessary at the individual entity level, but the primary focus of the assessment will commonly be at the holding company level in a coordinated examination. Documentation should clearly indicate the exam's utilization and reliance on the company's ORSA/ERM processes to assist in the identification of key risks and/or controls.

It may also be appropriate to provide additional risk specific commentary related to ERM/ORSA review within the Branded Risk Assessments. Documentation should provide summary level information for key risks, with reference to examination workpapers for additional detail, when necessary. on Risk specific commentary should include consideration the following areas, if applicable:

- New risks for the analyst to consider in its ongoing financial surveillance
- Risk specific controls/risk mitigation strategies that were validated during the examination
- Evaluation of risk assessment techniques, including appropriateness of stress scenarios and underlying quantification techniques and assumptions
- Risks that may require further ongoing surveillance or recommended follow--up by the Department
- Other sources of information to evaluate key risks not referenced in the ORSA (e.g. key risk indicators, presentations to the BOD, project plans, etc.)

Detail Eliminated to Conserve Space

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