

Date: 8/21/20

GROUP CAPITAL CALCULATION (E) WORKING GROUP

Thursday, August 27, 2020

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

WebEx Call-in

ROLL CALL

David Altmaier, Chair	Florida	Justin Schrader	Nebraska
Kathy Belfi, Vice Chair	Connecticut	Dave Wolf	New Jersey
Susan Bernard	California	Edward Kiffel	New York
Philip Barlow	District of Columbia	Jackie Obusek	North Carolina
Kevin Fry	Illinois	Dale Bruggeman	Ohio
Roy Eft	Indiana	Andrew R. Stolfi	Oregon
Carrie Mears	Iowa	Joe DiMemmo	Pennsylvania
Gary Anderson	Massachusetts	Trey Hancock/Rachel Jade-Rice	Tennessee
Judy Weaver	Michigan	Mike Boerner/Doug Slape	Texas
Kathleen Orth	Minnesota	David Smith/Doug Stolte	Virginia
John Rehagen/Karen Milster	Missouri	Amy Malm	Wisconsin

NAIC Support Staff: Dan Daveline/Lou Felice

AGENDA

1. Consider Adoption of its July 29 National Meeting Minutes Attachment 1
—*Commissioner David Altmaier (FL)*
2. Continue Discussion of Comments Received on an Exposed Revised Template & Instructions—*Lou Felice (NAIC)*
 - a. Summary of Comments Attachment 2
 - b. Combined comment Letters Attachment 3
3. Discuss Any Other Matters Brought Before the Working Group—*Commissioner David Altmaier (FL)*
4. Adjournment

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Attachment Five
Financial Condition (E) Committee
8/11/20

Draft: 8/4/20

Group Capital Calculation (E) Working Group
Virtual Summer National Meeting
July 29, 2020

The Group Capital Calculation (E) Working Group of the Financial Condition (E) Committee met via conference call July 29, 2020. The following Working Group members participated: David Altmaier, Chair (FL); Kathy Belfi, Vice Chair, (CT); Susan Bernard (CA); Philip Barlow (DC); Carrie Mears and Mike Yanacheak (IA); Kevin Fry (IL); Roy Eft (IN); John Turchi (MA); Judy Weaver (MI); Kathleen Orth (MN); John Rehagen (MO); Jackie Obusek (NC); Justin Schrader (NE); Dave Wolf and Diana Sherman (NJ); Victor Agbu (NY); Dale Bruggeman and Tim Biler (OH); Greg Lathrop (OR); Joe DiMemmo (PA); Trey Hancock (TN); Doug Slape (TX); Doug Stolte and David Smith (VA); and Amy Malm (WI).

1. Adopted its July 21, June 2 and May 19 Minutes

Commissioner Altmaier said the Working Group met July 21, June 2 and May 19. During its July 21 and June 2 meetings, the Working Group discussed proposed changes to the *Insurance Holding Company System Regulatory Act* (#440). During its May 19 meeting, the Working Group discussed the results of the Group Capital Calculation (GCC) field testing.

Ms. Belfi made a motion, seconded by Mr. Wolf, to adopt the Working Group's July 21 (Attachment Five-A), June 2 (Attachment Five-B) and May 19 (Attachment Five-C) minutes. The motion passed unanimously.

2. Considered Comments Received on Exposed Revised Template and Instructions

Commissioner Altmaier expressed his appreciation for the comments received (Attachment Five-D) on the previously exposed template and instructions, noting that they were extensive and thoughtful. He described how NAIC staff had divided the comments into 12 core issues (Attachment Five-E) and developed a recommended course of action, and the purpose of the meeting was for the Working Group to determine if it supported such a recommendation or preferred a different approach.

a. Use of the GCC

Mr. Felice described how this issue was related to some of the wording of how the analyst would use the GCC in a draft of the analyst guidance included in the June 2 conference call materials. He stated that the wording in that document is consistent with other tools with which you are trying to direct some action from the analyst under certain conditions, and he suggested that it was best that those issues be dealt with separately. Mariana Gomez-Vock (American Council of Life Insurers—ACLI) stated that the ACLI appreciated the inclusion of the interested parties developing the draft *Financial Analysis Handbook* guidance, and it seemed important and should be exposed for comment, particularly considering that it includes a threshold within it. Ms. Weaver stated that as chair of the NAIC group overseeing the *Financial Analysis Handbook*, if the guidance is exposed at this Working Group and any changes are made, we would have a shorter exposure at the group she chairs, but ultimately it will be exposed for comment.

Mr. Felice said the second part of this issue deals with the filing of the GCC. He stated that NAIC staff believed this was already being handled and the GCC would be filed in the changes to Model #440, where currently there will be strong confidentiality geared towards filing with the lead state regulator and sharing of some of the information in regulatory communication. Jim Braue (UnitedHealth Group—UHG) stated that it had two main points: 1) the GCC should be a tool for the lead state and can certainly share information with other domestic regulators within the group, but not more broadly; 2) emphasis on a tool, not a standard, and could take action using the GCC. Ms. Belfi stated that as they go through developing guidance for the *Financial Analysis Handbook*, they will make sure to sync that up with the instructions.

b. Calibration Level

Mr. Felice described how the calibration level determines the strength the GCC is set at, with it currently being set at 300% of Authorized Control Level (ACL) risk-based capital (RBC). Comments suggested that it be lowered to 200% ACL, and another suggested that it could go even lower. Mr. Felice noted that a number of other issues should be addressed first, such as how financials entities are defined and the definition of material risk for non-financial entities. However, he stated that NAIC staff

Draft Pending Adoption

Attachment Five
Financial Condition (E) Committee
8/11/20

supported the current proposed level from an analytical level as opposed to a lower threshold where action at the individual company level may be imminent. He stated that other comments suggested that the use of trend test terminology was an issue, for which staff does not oppose modifying. Ms. Gomez-Vock stated that the ACLI's concern was causing confusion since 200% ACL is what is referred to publicly, and she also noted its concern with unintended potential market perceptions. David Neve (Global Atlantic) stated that Global Atlantic is concerned about the confusion, and it prefers it to be consistent with the widely held use of 200% ACL. Mr. Braue stated that UHG had a few points, one of which is that the 300% calibration is in congruence with a group with its ultimate controlling person (UCP) an insurer; the filer would look fine for RBC, but yet fall below the threshold for the GCC, unless the suggestion is that RBC is not set at the appropriate level. He stated that from an analysis standpoint, looking at some level above that is reasonable; and he said such a level had already been developed for the *Financial Analysis Handbook* for the calibration of the ratio. The other point, discussed early on, is that a ratio equivalent to Company Action Level RBC is appropriate for a legal entity, and there is a lot of diversification benefit within a group; therefore, this should be taken into account, which has not been done. Ian Adamczyk (Prudential Financial) added that Prudential Financial's key point is the linkage that Ms. Belfi discussed. Mr. Bruggeman noted that he does not have a problem with a calibration different than 300%, but he thought the reason this was utilized was that was the first point when regulatory action could be triggered that puts the company in a situation where they have to do specified items. He emphasized that this does not mean any action would be taken; this is a tool, and for that reason, it is not a major deal. Therefore, he stated that he was confused by the interested parties' comments that it was not an action level when it is, along with other items. Ms. Belfi agreed with Mr. Bruggeman, but some of the comments seem to be suggesting that it is more punitive than if one was looking at an individual company. She stated that she was not sure if it was a potential something, but rather that it was a chance for the state insurance regulator to look at the risks of the group to cause the calibration level to hit that level. She stated that it was more of an awareness, and what risks are causing the drops needs to be determined. Mr. Rehagen stated that the Reinsurance (E) Task Force did a great deal of work with this, where 300% is utilized for comparison to other countries. He said for him, it is less confusing to use 300% RBC and not more confusing. Mr. Felice described what would happen if 300% was retained, which assists in a number of ways and can be messaged clearly, and an additional threshold above the 300% level might not be necessary in the *Financial Analysis Handbook* threshold.

c. Scope of Application

Mr. Felice described how some of the comments were focused on the ability to potentially exclude financial entities. He stated that NAIC staff believe that once financial entities are more clearly defined and agreeable to all, those entities should not be excluded, as they tend to have a little bit more risk. He stated that the original definition of financial entities was a bit more activities focused, and he would recommend improving the definition. He stated that other comments deal with the information required for entities from the calculation. Bob Ridgeway (America's Health Insurance Plans—AHIP) stated that the instructions should specifically exclude nonmaterial entities, regardless of being financial, noting that financial entities generally do not pose a risk. He stated that the staff recommendation to focus on activities was a good suggestion, and AHIP would be happy to work with staff to accomplish this. Stephen Broadie (American Property Casualty Insurance Association—APCIA) agreed with AHIP that changes to the definition of financial would be helpful, but he suggested the removal of nonmaterial entities. Chuck Finer (State Farm) suggested the elimination of information already provided to the lead state insurance regulator from the inventory tab, specifically noting how Schedule Y already contains information on all entities, and inclusion of information on each entity is duplicative. He questioned why the exclusion of non-financial entities should not apply to financial entities, including insurance companies.

d. Excluded Entities and Material Risk/Definition of Financial Entities/Treatment of Financial Entities

Mr. Felice described how he was hearing a number of related comments from issues four, six and seven, and he noted that he would discuss them together. The definition of material risk was an area in which NAIC staff was supportive of either principle-based or quantitative-based; although, the group has not been able to agree to such. Therefore, they would determine if the principle-based ideas could be considered in detail. Mr. Felice noted that there is also room for improvement on the definition of financial entities. Therefore, inclusion of some of the affiliates that are more related to the performance of the policy should be reconsidered in favor of a more activities-based definition. Mr. Felice stated that once an agreeable definition is developed, NAIC staff are not in favor of applying a diversification benefit or excluding it. Rather, past financial crisis suggests that a properly defined financial entity is subject to risks that are independent of the insurance company. Mr. Felice stated that NAIC staff also believe that quantitative data in the GCC is complimentary to other filings to state insurance regulators. He described comments on the charge for financial entities, and he said all financial entities should be treated the same. Currently, an

Draft Pending Adoption

Attachment Five
Financial Condition (E) Committee
8/11/20

operational risk type charge is applied to revenue. Mr. Felice state that the approaches considered now generally are consistent; although, one considers three years average revenue, while another considers just one year.

Mr. Felice described how the Working Group could make a referral back to the Capital Adequacy (E) Task Force in cases where the treatment of an entity type is different from RBC, but this should not be a prerequisite to finalizing the GCC. He described how if the Working Group sticks to the original 300% calibration, a 15% factor should be considered since that is what is considered internationally. Mr. Ridgeway stated that AHIP looked forward to working with NAIC staff, but it continues to consider how these are considered together, since the process should consider existing things already considered by state insurance regulators to determine materiality. He discussed how a number of issues being contemplated are already subject to regulatory review (affiliated transactions). He emphasized the need to look at the activity itself, and he hopes AHIP can work through this issue with state insurance regulators. Mr. Broadie agreed with working with staff on a better definition of financial entity, and he also noted the need for a high-level principle definition of materiality; he had made recommendations in this area. The APCIA has also proposed a list of criteria that a lead state and a company should look at, but it is happy to work with NAIC staff. Mr. Finer stated that he too looks forward to working on a definition. Mr. Braue stated that if financial entity is redefined to be more like banks and securities traders, it would eliminate UHG's concerns, noting that affiliates that provide services to the insurer are less risky and already subject to review by the state insurance regulator. Mr. Adamczyk stated that Prudential Financial was the party that recommended that a simple approach be taken, as it views the key goal of providing insight into the nonregulated entity, but it does not believe different factors will make a material difference. The APCIA believes that ultimately, the inventory approach will facilitate the conversation and serve as a point for further discussion by the state insurance regulator, as well as other tools beyond the GCC.

Having no further business, the Group Capital Calculation (E) Working Group adjourned.

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**Comment Summary - GCC Template and Instructions
July 29, 2020 (Revised August 27)**

Issue 1	Commenter	Essence of Comment	Primary Rationale
Use of the GCC	ACLI	Concerned that some aspects of the instructions and preliminary Draft Analysis Handbook infer a GCC that goes beyond its objective and would turn the GCC into a binding standard or constraint.	General comment but likely consistent with United HealthCare rationale
	United HealthCare	<p>key area of concern is the statement that “insurance companies may be subsidizing the operations of non-insurance entities, potentially undermining the insurance company’s financial condition.”</p> <p>Another concern arises from the statements in that the GCC “provides an additional early warning signal so regulators can begin working with a company to resolve any concerns” and will “allow them to make informed decisions on both the need for action.”</p> <p>Concern that the instructions as written may not make clear that the GCC is intended to be used solely by the lead state regulator.</p>	<p>The idea that non-insurance operations within the group pose a proximate risk to the solvency of the group’s insurers has little historical evidence to support it.</p> <p>It seems inappropriate to suggest that the GCC, in and of itself, would be grounds for regulatory action to protect policyholders; that is the function of a regulatory standard, not an analytical tool.</p> <p>The statement, “State insurance regulators already have broad authority to take action when an insurer is financially distressed, and the GCC is designed to “allow them to make informed decisions on both the need for action, and the type of action to take,” suggests that the GCC will be used by the domiciliary regulator of each insurer.</p>

Initial NAIC Staff Comments:
 Some of the Introductory wording could be revised and / or moved to the Analysis Guidance being drafted & reviewed by the drafting subgroup, particularly with reference to cross subsidization. Comments on other thresholds applied in the analysis guidance can be addressed there. Staff notes that industry representatives are assisting in revising and reviewing the analysis guidance.
 Although the GCC in totality can be viewed as an early warning vehicle, the GCC ratio itself is just one piece. This is similar to other analytical tools. Early warning is distinct from capital standard driving statutorily authorized regulator action. Although made clear throughout the GCC process that it will not be a capital standard, clarification of language to avoid any such inference will be considered.
 As a group rather than entity-based tool, the submission itself is limited to the lead-State regulator (s/b addressed in Model Holding Company Act), it seems logical that post review regulatory concerns may be shared with other involved regulators in collaborative forums. Staff will look at the suggested language.

Issue 2			
Calibration Level	ACLI Global Atlantic Prudential	Adopt a 200% ACL calibration level for the GCC. In addition, calibrations of other factors and regimes should be based on 200% ACL level RBC as well.	Inconsistent with RBC reporting and industry’s current reporting of two capital calibration levels, (100% ACL and 200% ACL) results in confusion and frequent misinterpretation of reported ratios; adding a third calibration level for the GCC of 300% ACL will compound the problem. This will lead to additional confusion and misunderstanding by users of financial information, including the regulatory, rating agency, and banking communities.
	United HealthCare	Lower 300% Calibration (consider lower than 200%) and / or add a diversification component	The calibration does not adequately consider the capital mitigation in diversified integrated holding company systems.

Initial NAIC Staff Comments:
 Staff recommends that a 300% calibration be retained for a group-wide analytical tool that compliments entity-based RBC. The working group should consider whether using CAL or lower could imply that some specified regulatory action is immanent, especially within the context recommended by some commenters that risk charges mirror entity RBC. Staff believes that would add confusion between RBC as a standard and GCC as an analytical tool. Using a level above CAL RBC is consistent with a regulator analytical tool and consistent with an RBC reference point (Trend Test). Further it applies a reference point that is agnostic to the structure of the group.
 A secondary issue is ability to be somewhat consistent with the AM – ICS being proposed by the NAIC in cooperation with other U.S. regulatory partners.
 Staff believes that issues related to calibration are better addressed via the working group decisions on the definition of a financial entities, level of post covariance charges to be applied to non-financial entities, and definition of material risk for purposes of potential exclusion of entities from the calculation.
 Staff agrees that there should be careful coordination between the GCC Template, and the analysis guidance as regards the level of the GCC ratio. Staff notes that industry representatives are assisting in revising and reviewing the analysis guidance.

Issue 3	Commenter	Essence of Comment	Primary Rationale
Scope of Application	AHIP APCIA	GCC Instructions should explicitly state that non-material entities (including financial) within the Broader Group (but outside the Insurance Group) should be excluded from the Scope of Application.	<p>All entities that meet the broad definition of “financial” in the GCC Instructions do not necessarily pose material risk (as defined above) under all circumstances.</p> <p>The fact that an entity would be classified as “financial” should be weighed as a factor in the materiality analysis.</p>
	State Farm	Requests that excluded entities not be required to be on the Inventory Tab or, at least, the Lead State Regulator have the discretion to not require excluded entities on the Inventory Tab if requested by the preparer.	Gathering information under the GCC from entities that are excluded from the GCC seems counterintuitive and duplicative in certain situations.
		State Farm questions why the Draft Instructions do not allow exclusion of immaterial financial or insurance entities that are isolated from the group as are non-financial entities.	Acknowledging the isolation of financial and insurance entities fits within already existing regulatory arrangements as well as the GCC and acknowledges that capital is not freely fungible for use by the group or entities within the group.

Initial NAIC Staff Comments:

Staff believes that given prior problems (e.g. during the financial crisis) with financial entities, some that appeared immaterial at the time, all financial entities should initially be included in the calculation for both risk and consistency purposes. Staff does appreciate the comments on the breadth and targeting of defining certain affiliates as financial entities as that was one of several areas of the instructions where comments were specifically requested and agrees that revisions are appropriate. The prior and current versions of the instructions do identify some financial entities without regulatory capital requirements with closer reference to their activities, so the working group could consider revisions targeted more specificity related to activities of financial entities.

The instructions currently limit the amount of data that is required from entities that the lead-State regulator agrees should be excluded.

Issue 4	Commenter	Essence of Comment	• Primary Rationale
<p>Excluded entities / Material Risk</p>	<p>ACLI AHIP APCIA</p>	<p>GCC Instructions should provide a definition of “material risk” for purposes of the Scope of Application as follows “risk emanating from a non-insurance entity that is of a magnitude that would adversely impact a group’s insurance operations and its ability to pay policyholder claims.”</p> <p>GCC Instructions should provide a principles-based definition of “material risk” for purposes of the Scope of Application.</p> <p>Suggest that “material risk” should be defined as “risk emanating from a non-insurance entity that could adversely impact a group’s insurance operations and ability to pay policyholder claims.”</p> <p>APCIA recommends developing a list of factors related to whether an entity could adversely impact a group’s ability to pay policyholder claims. (List included in letter – Page 2). No single factor is determinative of materiality of risk, nor should these factors be used as a scorecard or checklist.</p>	<ul style="list-style-type: none"> • Follows the fundamental reason for state insurance regulation and the stated objective of the GCC: policyholder protection. • Is in accordance with international standards. For example, under ICP 23. • Given the diverse structures and business models of insurers, it would be impracticable to develop a one-size-fits-all checklist of guidelines that would be useful for materiality determinations across all groups. • Form B and D processes and Enterprise Risk Reports entail similar considerations and are already enshrined in the state regulatory process. <p>Insurers and regulators could then use these factors to undertake a materiality analysis based on the totality of the facts and circumstances by considering the factors and how they apply to the group’s business</p>
	<p>State Farm</p>	<p>Requests a baseline materiality definition be provided while maintaining Lead State Regulator discretion to determine if a higher or lower material threshold is appropriate.</p>	<p>There should be some consistency in application under these provisions and that materiality should be based on the group’s net worth given the GCC is measuring risk of the group and not a particular entity in the group.</p>
		<p>Suggests a group equity threshold for materiality with a drafting note suggesting 5% threshold subject to regulator discretion</p>	<p>Baseline for materiality while still allowing the Lead State Regulator and the preparer to use a higher or lower threshold given circumstances presented by the preparer.</p>
<p>Initial NAIC Staff Comments: Staff agrees that materiality of risk is important in deciding whether to exclude non-financial entities. Staff supports a definition to promote consistency in completion of the GCC. We are supportive of principles-based criteria being included in the instructions. We are also supportive of quantitative Criteria if preferred by the working group but recognize that there has not up until now been coalescence around a single quantitative benchmark. See staff comments above under Scope of Application (Issue #3) regarding financial entities.</p>			

Issue 5	Commenter	Essence of Comment	Primary Rationale
Grouping	Prudential	Supports flexibility of current grouping language, but state regulators should retain the option of requesting more granular information should they feel it is needed to obtain a sufficient view of risks within the group.	Self-Explanatory
Initial NAIC Staff Comments: Although staff believes this is implicit, we support adding explicit language.			

Issue 6	Commenter	Essence of Comment	Primary Rationale
Definition of Financial Entities	AHIP	Disagrees with the notion that certain affiliates are inherently riskier than others and more generally with the expanded definition of financial affiliates.	<ul style="list-style-type: none"> • There is a wide array of types of non-affiliated entities within insurance groups, and it is overly simplistic to conclude that all that are somehow associated with assisting the insurer with contract performance or policyholder services are inherently riskier than others.
	APCIA	Third-party administrators and pharmacy benefit managers, provider groups, and pharmacy benefit managers should not be considered financial entities.	<ul style="list-style-type: none"> • Form B and D processes recognize that transactions with affiliates may have risks.
		APCIA is concerned with the expanded definition of financial entity in the GCC.	
	United HealthCare	Base comments are similar to AHIP Comments. This is amplified by lack of diversification credit for the wide array of entities defined as “financial”	<ul style="list-style-type: none"> • Affiliates that merely provide contracted services to a carrier should not be defined as “financial”: they do not create any more financial risk to their affiliated insurers than do non-affiliates that provide the same services to other insurers. • Some of the examples given diversify risk for the insurance entity in the group, facilitating more access to capital by the insurance entity. The aim of the working group should not be to promote smaller, less integrated or diversified groups. • Greater regulatory oversight to certain currently defined entities and regulatory review of intercompany agreements should be considered to reduce the group’s risk.

Initial NAIC Staff Comments:

Staff appreciates the comments on the breadth and targeting of defining certain affiliates as financial entities as that was one of several areas of the instructions where comments were specifically requested. The issue of an appropriate definition of financial entities impacts other concerns identified in the comments including, calibration, scope of application, materiality of risk, and consistency across group structures. The instructions currently do identify some specific financial entities without regulatory capital requirements and some associated activities, so the working group could consider more specificity related to activities based on the activities of those identified entities. As intended, staff also believes that the quantitative aspects of the GCC in the context of a regulatory view, as well as the additional data supporting analytics does compliment rather than overlap the benefits of other regulatory filing requirements.

Issue 7	Commenter	Essence of Comment	Primary Rationale
Treatment / Charges Financial Entities	ACLI	To the extent that there are differences in the GCC and legal RBC treatment for subsidiaries that have been de-stacked and reported separately from their legal entity parent, then it seems desirable for the GCC and RBC treatment to align. To the extent that there are differences between the two, we recommend the Working Group explain the rationale for the difference (e.g., achieving substantial consistency in charges regardless of corporate organizational structure) and, if appropriate, refer the issue to the appropriate RBC working for further dialogue.	ACLI believes that the GCC should be consistent with the legal entity rules applied to insurance legal entities – including the subsidiaries of insurance legal entities. In the long run, we believe this approach will benefit regulators and the industry by promoting a more consistent and up-to-date risk framework.
	AHIP	Recommends applying the equity-based capital charge that is recommended for non-financial affiliates to all affiliates that are not subject to a regulatory capital requirement.	Subjecting these entities to a capital charge for financial entities (12% of 3-year average gross revenue – possibly to be increased to 15%) could result in a significant additional charge as compared to current RBC.
	APCIA	in the short term, use a capital charge that is roughly equivalent to the current post-covariance charge (presumably equity charge) for such affiliates in RBC.	Over the first few years of the GCC’s implementation, data can be collected and used to derive a more risk-sensitive charge that is pragmatic (e.g., a differentiated charge for entities of high/medium/low risk as determined by specified criteria).
	Prudential	Supports adopting a single approach for establishing a proxy capital measure for all financial entities that are not subject to a regulatory capital requirement. Supports a method that most closely aligns with how the AM - ICS will ultimately treat this item.	<ul style="list-style-type: none"> • Ensuring state regulators obtain adequate insight into the entities within the insurance group and risks associated with them is the key point of consideration for these entities and this is best accomplished through the inventory element of the GCC as opposed to an arbitrary proxy capital calculation. • To the extent a state regulator believes an entity poses material risk to the group, they have discretion to request additional information to understand the risks.

Initial NAIC Staff Comments:

Staff notes that as a complimentary group analytical tool covering entities other than those owned by RBC filer, total consistency with RBC is not entirely relevant, particularly for financial entities. Staff does agree that the Capital Adequacy Task Force should determine whether the treatment of financial entities in the GCC is relevant for U.S. Insurer entity-based RBC. This can be tasked to the current Ad Hoc Affiliates Subgroup or directly to the RBC Working Groups

Staff agrees that an overarching explanation of where differences exist is helpful.

Staff does not recommend using a post covariance charge for most financial entities that are not subject to a regulatory capital charge. Properly defined Financial entities can pose additional non-diversifiable risk. Staff agrees that a narrower more activities focused definition of such financial entities will address many stated concerns.

Staff recommends continuing a revenue-based / enhanced operational risk type charge. Up until this point there seems to have been more agreement around a revenue-based charge for these entities.

Staff has no issue with treating all financial entities that are not subject to a regulatory capital charge the same at least initially. The only current difference is whether to use a 3-year average revenue (currently used for asset managers) or current year revenue only (currently used for other financial entities that are not subject to a regulatory capital charge) as the base used to apply the charge.

Staff supports the 15% charge as reflective of a 300% calibration and consistency whether where international standards are headed but understands that the working group may consider a scaled version as a starting point for the near-term. Staff supports the proposal to consider refinements over time for financial entities not subject to a regulatory capital requirement in order to be more risk sensitive along the lines of the low / medium / high approach suggested by APCIA (e.g. lower risk entities could go with the post covariance non-financial entity charge / medium risk entities, a scaled revenue-based charge / and high risk entities, the full revenue based charge).

Issue 8	Commenter	Essence of Comment	Primary Rationale
Treatment / Charges - Non- Financial Entities (incl. material non-financial A / BA)	ACLI	ACLI was unable to discern how the proposed charges for “other non-insurance/non-financial entities” and “material Schedule A/BA entities” were created.	Further clarification on this issue is necessary, including an explanation of why the Working Group is recommending a novel approach that has not been subject to field testing.
	AHIP	Risk charges for non-financial entities should be equal or very similar to the current charge in the sectoral RBC formulas, i.e., 3% post-covariance charge in the case of health insurers.	<ul style="list-style-type: none"> • The GCCWG has not provided data to suggest that a more substantial risk charge is needed to protect policyholders. • Form B and D processes are already in place to ensure that the regulated legal entity is protected from the non-regulated, non-insurance entity.
	APCIA	During the first few years of the GCC’s implementation use 3% of 3-year average revenue. Once some experience is gained with the GCC, the Working Group should consider a simple variable risk charge (low / medium / high risk charge) that is more risk-sensitive based on industry and activity.	A period during which experience will be gained that can then be analyzed in more detail and across more groups than was possible in field testing.
	Prudential	Supports adopting a single approach for establishing a proxy capital measure for all non-financial entities	See rationale for financial entities.
	United HealthCare	Charge should be based on the group specific after covariance equity charge.	Using an average industry post covariance charge is not reflective of the proportion of insurance vs. non-insurance business within a group.
<p>Initial NAIC Staff Comments:</p> <p>Once materiality of risk has been established, Staff supports a post covariance equivalent equity-based charge that is broadly consistent with RBC treatment for non-financial entities that are “included” in the GCC. The current template uses a single average post covariance factor across all industry types, but Staff believes that an industry specific charge has merit. A group specific charge was previously tested and could be considered by the working group, but unlikely to have a significant impact on the GCC. However, NAIC Staff would be interested in information to the contrary by a group that has run the numbers given that the NAIC will not be receiving the GCC filings.</p> <p>Staff supports the suggestion to make future refinements based on continued collection of data but again notes that NAIC will not have access to the submissions.</p>			

Issue 9	Commenter	Essence of Comment	Primary Rationale
Allowance for Debt	ACLI Prudential United HealthCare	The current debt caps are too restrictive.	<ul style="list-style-type: none"> • Could have procyclical effects in times of stress, when available capital tends to contract and capital requirements tend to increase. • Could negatively impact a group’s ability to prudently manage capital and liquidity risks. • Tying the constraint to a percentage of the group’s available capital embeds an undesirable element of procyclicality into the GCC, because a company’s available capital is likely to decrease in times of stress, especially if markets crash. • The 30% factor for senior debt and 15% for hybrid debt are being applied to a more conservative base than rating agencies use for establishing limits • Adding a limit of 50% of total adjusted carrying value to the conservative 30% and 15% limits for senior and hybrid debt (relative to total adjusted carrying value + outstanding senior and hybrid debt) effectively lowers the 45% permitted (i.e., 30% + 15%) to approximately 33%.
	ACLI Prudential United HealthCare	Requirements for tracking the down-streaming of debt issuance proceeds to regulated entities should be eliminated.	<ul style="list-style-type: none"> • Interpretations related to how to support “tracking” will be difficult to verify and may lead to inconsistencies across groups. • Keeping funds at the holding company level is a prudent strategy that provides insurance groups flexibility to quickly and easily manage capital and liquidity needs across the group. • A tracking requirement could give rise to unintended consequences such as reducing the availability and fungibility of capital resources and forcing U.S. insurance groups to issue greater amounts of debt.
	ACLI	Remove the call option criteria, because the exercise of a call option is typically followed by refinance of the instrument which supports its permanence and structural subordination.	Relative to the 5-year term, the presence of call options should not prevent a capital instrument’s inclusion as a qualifying instrument. Call options are a common feature of U.S. issued capital instruments.

<p>Allowance for Debt</p>	<p>Global Atlantic</p>	<p>Eliminate downstream tracking logic and replace it with a simple comparison to paid-in capital and surplus.</p>	<ul style="list-style-type: none"> • Simpler, more efficient, and more reliable test • Avoids complications that could result from debt that has been refinanced by the parent as there would be no contribution of the debt amount issued. • Avoids complications of tracking upside transactions where debt is borrowed at one date and then down streamed at a different date. • Avoids complications of tracking the reverse: dividends which are up streamed. Are those upstream transactions to be netted against down streamed capital or not? • Avoids complications and questions related to M&A transactions – if a company is acquired, does the new parent company automatically assume the historical relationship of down streamed debt, so long as its debt at least equals the debt of the old parent company?
	<p>APCIA</p>	<p>The treatment of debt differs in some key respects from that which was adopted by the International Association of Insurance Supervisors (IAIS) in the Insurance Capital Standard (ICS) in 2019.</p>	<p>The GCC could be viewed as less credible by other jurisdictional supervisors including those who may be parties to a Covered Agreement. Comparability of the GCC with the ICS is a looming issue on the horizon, the resolution of which can impact the views of many IAIS member jurisdictions about the efficacy of state-based regulation over U.S.-based insurance groups.</p>
		<p>FED BBA is more closely aligned with the principles-based criteria in the ICS than with the approach taken in the exposed GCC Instructions</p>	
	<p>Working Group may need to supplement the GCC Instructions with definitions for each type of instrument. For example, “hybrid debt” is not defined in the Instructions</p>	<ul style="list-style-type: none"> • Rating agencies treat subordinated debt issued by a parent company as “hybrid debt” if it is long-dated and has provisions to defer interest payments for a period of time. This could give rise to variation in treatment of hybrid debt (e.g., it may be unclear to a group if it should classify it as “hybrid” or as “subordinated” debt) • Comparability with the ICS needs to be considered, and on this point it seems that the more important issue is not whether types of debt are called out by name or more generically by tier, but whether comparable criteria to the ICS are used. 	

Allowance for Debt	APCIA	Replace terminology “additional capital allowance” with “within supervisory limits”.	Focusing the Instructions’ text on "limits", rather than "allowance", will help in some respects with perceptions about comparability.
		Add criteria supporting structural subordination to “Tracked Down-streamed Debt” proceeds rather than eliminate that test.	<ul style="list-style-type: none"> • Team USA argued long and hard to support structural subordination in the ICS. • While down-streaming has raised many questions about how debt proceeds can be tracked and verified, the ICS criteria are workable and rely in large measure on each group and its group-wide supervisor to make that determination in light of the unique facts and circumstances. • The IAIS avoided prescribing detailed rules or criteria for tracking. APCIA believes the NAIC should do the same in the GCC, leaving the determination of the amount down streamed to the lead state working in conjunction with the group. • This would include criteria to support that the qualifying amount of debt to be treated as capital is actually subordinated (either contractually by the terms of the instrument, or structurally), and other principle-based criteria, as in the ICS, to support permanence, loss absorbency, etc. Some refinement of the ICS criteria may be necessary to address U.S.-specific nuances for the GCC.
		Another option to test structural subordination is to limit the amount of senior debt to qualify as capital to that which is in excess of the liquid assets in the holding company.	As a practical matter, the lender would have recourse only to the liquid assets that remain in the entity that issued the debt (i.e., the holding company in the case of senior debt). The unconsolidated balance sheet of the holding company (reflects a very large, illiquid investment in insurance subsidiaries, control over which is subject to regulatory oversight and approval.
		APCIA is open to the possibility of some allowance for other debt in the future.	Self-Explanatory
		It would seem appropriate that the overall limitation should apply to all debt, including surplus notes and	

	APCIA	foreign debt. That said, and as noted above, APCIA supports no limit on surplus notes of mutual insurers.	See Staff Comments
		we do not offer a view on the overall limit of 50%. However, the ICS comparability issue is also an important goal and encourage the Working Group to give due consideration in the context of the overall limit.	The comparability issue is also an important part of navigating the way forward with the GCC and encourage the Working Group to give due consideration in the context of the overall limit.

Initial NAIC Staff Comments:

Staff is open to eliminating the tracked down-streamed option as suggested by some commenters especially since current debt issued generally refinanced expiring or called debt which would have required tracking for debt issued potentially years ago. The arguments put forth by APCIA are relevant, however, structural subordination is strongly represented by insurer paid in capital and surplus which has the most rigorous regulatory control over distributions. If there is down-streaming on newer debt, it would most likely become part of paid in capital or surplus thus raising the amount allowed (subject to the limitations)

If an option for tracked down-streamed is retained criteria for tracking will need to be developed. Here are some suggested criteria:

- Evidence of infusion of proceeds
- Description of the method used for tracking the proceeds
- Explanation of excess over what is reported as paid-in and contributed capital and surplus
- Default is paid-in and contributed capital and surplus

Staff is sympathetic to the point that the proxy allowance for Senior Debt is applied to regulatory available capital rather than GAAP available capital and the 50% limit of otherwise available capital could be adjusted upward if the working group concurs. Staff would initially suggest no more than 75% in order to balance the point raised with recognizing that there is no tiering of capital in reference to the ICS and that the GCC applies the limits to the larger base of available capital rather than required capital.

Staff understands the issue of including Foreign Debt in the limit. However, fully including contractually subordinated debt already recognized by a regulatory authority as capital and included in the carrying values in Inventory B (e.g. U.S. surplus notes and contractually subordinated foreign debt) seems consistent from a regulatory perspective. Staff agrees that foreign senior and hybrid debt that is not included in the value of an entity In Inventory B should be included within the limit.

Staff has some concerns about the APCIA alternative methodology as it may provide too much of an allowance since large groups may rely on illiquid assets at the holding company level and the method would seem to result in including the entire book value of insurers in the group.

Staff supports the suggestion to continue to collect data on “Other Debt” for future refinements but notes that NAIC will not have access to the filings.

Staff will review language for clarity considering edits provided and definitions of debt instrument types.

Staff will follow-up on the issue of terminology “additional capital allowance” vs. “within supervisory limits” but notes that there is currently no GAAP or SAP allowance for subordinated debt other than surplus notes (so the supervisory limit is essentially zero per accounting requirements). The GCC provides an on top allowance that reflects a supportable proxy alternative for structural subordination.

Allowance for Debt as additional capital is an area of potential divergence between the GCC and AM- ICS.

Issue 10	Commenter	Essence of Comment	Primary Rationale
Scalars	ACLI Global Atlantic Prudential	Use the Excess Approach over the Pure Approach. Use the Excess Relative Ratio Approach for scaling non-U.S. capital ratios to U.S. RBC.	<ul style="list-style-type: none"> • This method utilizes two anchor points for scaling. • The Pure Relative Ratio lacks a mechanism to ensure that a non-U.S. firm at the regulatory intervention level within its respective country will be at the U.S. RBC intervention level once scaled. • The Pure Relative Ratio Approach fails to adequately account for key differences in insurance regimes (e.g., level of conservatism embedded in reserves versus required capital, different valuation and asset admissibility standards, etc.). • The decision would prejudice the Pure Relative Ratio Approach as the methodology that should be adopted for the AM and could undermine the ongoing work at the NAIC’s work at the global level to secure recognition of the AM
	Global Atlantic	Transparency of how the scalars are calculated will be critical, regardless of which scaling methodology is selected	<ul style="list-style-type: none"> • Consistency – scalars should be calculated and applied consistently across all non-U.S. regimes. • Specificity – scalars should be discretely computed and applied amongst life, property casualty and health insurance companies. • Stability – the results of applying scalars to Non-U.S. capital ratios should not be volatile; for example, converting to U.S. RBC should not yield a significant headwind in one year, and a significant tailwind in the following year

Initial NAIC Staff Comments:
 Scalars remains an open issue. The use of the Pure Relative Ratio appeared to strike a good balance between precision, simplicity and ease of explanation.

However, staff has no strong feelings between the two approaches and believes that the working group should be open additional approaches while maintaining a placeholder methodology.

Staff notes the argument put forth by Prudential that selection of a scalar methodology even as a placeholder at this juncture may send a stronger signal than anticipated relative to the AM – ICS. The suggestion to use 100% scalars as the placeholder pending further work on scalars is worth consideration by the Working Group.

The working group should be aware of ongoing work on the AM-ICS as scalar methodology is an area of potential convergence between the GCC and AM- ICS.

Issue 11	Commenter	Essence of Comment	Primary Rationale
Sensitivity Analysis	ACLI Prudential	Eliminate Sensitivity Analysis Tab altogether	<ul style="list-style-type: none"> • Narrowing the design of the GCC will ensure insurers, supervisors (domestic and foreign) and other stakeholders have a clear vision and understanding of what the GCC is (e.g., it would eliminate the need to distinguish between a “Base” view and alternative measures). • To the extent broader information on the insurance group is of interest to a state regulator, we believe it should be obtained through discretionary powers as opposed to embedding it in the GCC template.
	Coalition	Supports Eliminating the XXX/ AXXX analysis in favor of a referral.	<ul style="list-style-type: none"> • The need for the GCC to adhere fully to legal entity rules in support of the state-based legal entity solvency system

Initial NAIC Staff Comments:

Staff recommends against deleting the sensitivity analysis tab in its entirety. The XXX/ AXXX sensitivity test is in process of removal. The information contained in most other analysis points informs future decisions on capital charges, and more generally is consistent with the primary purpose of the template as an analytical tool and should be retained for a period of time for further assessment of its value.

Staff understands that some of the sensitivity analysis may fall away as more finalized decisions on treatment of financial entities not subject to regulatory capital requirement and for treatment of non-financial entities and perhaps on scalars are incorporated into the GCC template.

Staff believes that the data is more readily accumulated in the Sensitivity Tab from other parts of the template. Separating it would require additional work particularly for non-insurance entities.

Issue 12	Commenter	Essence of Comment	Primary Rationale
Other Information Collected	United HealthCare	Questions the rationale for collecting information on intangible assets (such as deferred acquisition costs, provider contracts, customer lists, and goodwill).	<ul style="list-style-type: none"> • The focus on intangible assets, to the exclusion of other types of assets, seems unwarranted. • Regardless of their availability for sale, intangible assets do produce a stream of income to the group; otherwise, GAAP accounting would require that they be written down in value or written off entirely. • As businesses rely more and more on digital assets and intellectual property as the basis for their operations, and less and less on fixed assets, there is more scrutiny of the value of those assets, and there should be less concern about whether the stated values are appropriate. We • Both business trends and accounting changes have made the differentiation of “intangible” assets increasingly less relevant.
<p>Initial NAIC Staff Comments: Staff notes that the GCC represents a regulatory view of group available capital. It is not intended that the value of intangibles allowed under GAAP, SAP or another accounting basis should be excluded. However, staff believes that there is some value in quantifying the extent that group capital is comprised of illiquid non-physical assets. This can provide good regulatory information in addition to the views of rating agencies or other group stakeholders.</p> <p>Staff is comfortable with assessment of the value of the data collected in the Tab by the Analytics Guidance Drafting Group and making any adjustments accordingly.</p>			
Issue 13	Commenter		
Other Technical Comments, Language Edits, Clarification requests and Second Tier Concerns	AHIP, APCIA, UHG		
<p>Initial NAIC Staff Comments: These items will be reviewed and accepted, adjusted or rejected after this meeting based on the direction taken in response to the comments discussed today.</p>			



July 20, 2020

Commissioner David Altmaier, Chair
Group Capital Calculation (E) Working Group
National Association of Insurance Commissioners

Via e-mail to Lou Felice: lfelice@naic.org

Re: Exposure of Proposed Group Capital Calculation Instructions and Template

Dear Commissioner Altmaier:

America's Health Insurance Plans (AHIP) appreciates the opportunity to comment on the changes that have been proposed by the NAIC's Group Capital Calculation (E) Working Group to the Group Capital Calculation (GCC) Draft Instructions and Template, as well as the related FAQ Document, and PowerPoint.

AHIP appreciates the hard work of the GCCWG and of NAIC staff in developing the GCC under tight timeframes as well as in suboptimal working conditions that persist with the ongoing pandemic. In a separate letter submitted on July 15, we stated our appreciation to the working group for recognizing appropriate exemptions and expedited treatments for filing of the GCC. We have some comments below regarding the GCC Instructions that we hope will be seen as constructive. But we first want to call out what we see as clear "positives" in the revised draft GCC and acknowledge the efforts of you and your working group to bring these to bear:

- The overall approach maintains that the GCC is an analytical tool for use by the lead state that will not, in and of itself, dictate capital requirements.
- Appropriate exemptions and expedited treatments from filing all or part of the GCC template have been provided and which provide, in certain instances, for the Lead State Commissioner to use discretion to allow filing only of Schedule 1, i.e., as an analytical construct it could be a sufficient supervisory measure without aggregation to a single group-wide measure.
- Groups could exclude certain non-financial entities from the Scope of Application and large, decentralized groups could request up front a reduction in the scope.

- Determination of materiality of risk posed to the insurance group by non-insurance entities in the broader group will be a qualitative determination (the Financial Analysis Handbook Drafting Group is to consider appropriate criteria).
- Modified instructions for the GCC template are less onerous (than in field testing), i.e., with more grouping and less de-stacking.
- Senior and hybrid debt criteria and limits will accommodate a large majority of debt held by insurance groups to be recognized in group capital.

With that, AHIP would like to provide the following suggestions relative to the GCC Instructions.

I. Scope of Application

Determination of Material Risk

AHIP believes the GCC Instructions could improve the readability of the principle-based guidance for establishing the Scope of Application of the GCC. Currently, some of the principles are included in the section on “definitions” which follows other text where both an understanding of those definitions and the principles therein would be useful for the reader. As well, sections which would appear by the heading to be about principles are more focused on instructions for completing parts of the template.

The section of the GCC instructions on scope of application is intended to help the holding company and its lead state to reach an understanding as to whether a non-insurance entity within the Broader Group poses material risk to the Insurance Group. It should provide principles-based guidance for companies and their lead-state regulators to identify such entities that do not pose material risk and therefore can be excluded from the Scope of Application.

As a threshold matter, the GCC Instructions should provide a definition of “material risk” for purposes of the Scope of Application. In this context, we believe “material risk” should be defined as “risk emanating from a non-insurance entity that is of a magnitude that would adversely impact a group’s insurance operations and its ability to pay policyholder claims.” Likewise, the GCC Instructions should explicitly state that non-material entities within the Broader Group but outside the Insurance Group (as both terms are defined in the GCC instructions) should be excluded from the Scope of Application.

These points naturally follow from the fundamental reason for state insurance regulation and the stated objective of the GCC: policyholder protection. Indeed, paragraph 13 of the GCC Instructions already makes clear that “the overall purpose of this assessment is to better understand the risks that could adversely impact the ability...to pay policyholder claims”.

This reasoning is also in accordance with international standards. For example, under ICP 23, the fact that a non-insurance entity poses risk is not, alone, determinative of whether that entity should be in or out of the scope of group supervision; rather, to be considered included in scope, there also must be some means by which the non-insurance entity could actually transmit that risk to the group's insurance operations, as well as a lack of adequate safeguards that would mitigate that risk of transmission. We believe that the GCC instructions currently embrace those concepts. However, terms such as "cross support mechanisms," and "safeguards" are not defined and it is unclear how they are intended to apply in the context of the scope of application.

For effectuating the materiality analysis for purposes of the Scope of Application, AHIP believes it is necessary for holding companies and lead states to consider the facts and circumstances of a particular entity within a group in a holistic manner. Given the diverse structures and business models of insurers, it would be impracticable to develop a one-size-fits-all checklist of guidelines that would be useful for materiality determinations across all groups. Strict or formulaic quantitative measures are likewise an insufficient proxy for materiality. Instead, the materiality analysis must be assessed in the manner it has been historically – by considering the unique circumstances of the relevant entity and group. We believe that to be the intent of what has evolved through field testing, i.e., an interactive process whereby the group brings forward its suggestions as to entities that should be excluded from the scope of application for a discussion with the lead state, ultimately culminating in an agreement on the scope.

We are not suggesting to somehow upset that interactive process or discussion between the group and its lead state. Rather, AHIP simply recommends facilitating it with definitions for "cross support mechanisms" as well as "safeguards" over the possible transmission of risk between the subject entities of that discussion.

We note that the Form B and D processes entail similar considerations and are already enshrined in the state regulatory process. For example, a detailed review is made of inter-company transactions and agreements that could, depending upon their terms and other pertinent information, fall into the category of "cross support mechanisms" as contemplated by the GCC instructions. Examples could (depending on the facts and circumstances) include certain loans, transactions not in the ordinary course of business; guarantees or other undertakings for the benefit of an affiliate, management agreements, service contracts, cost-sharing arrangements, reinsurance agreements; tax allocation agreements, and more. These agreements are already filed and approved with states. States can leverage these processes already in existence for visibility into cross support mechanisms that may be able to transfer material risk.

As well, Enterprise Risk Reports filed with the lead state already provide information as to the existence of "enterprise risk" defined as "any activity, circumstance, event or series of events involving one or more affiliates of an insurer that, if not remedied promptly, is likely to have a material adverse effect upon the financial condition or liquidity of the insurer or its insurance holding company system as a whole..."

Taken together, Forms B and D and Enterprise Risk Reports establish examples of “cross support mechanisms” as well as whether there is risk that could have a material impact to the insurers in the group (presumably via transfer through at least one such mechanism). It stands to reason that in the GCC, only such risks of non-insurance non-financial entities outside the insurance group that are already identified through those processes could therefore have a material impact and for which the subject entity(ies) that are the source of that risk would therefore be included in the scope of the GCC.

Finally, the GCC Instructions currently contemplate excluding only non-material, non-financial entities from the Scope of Application. However, the Working Group should also consider allowing non-material financial entities within the Broader Group (but outside the Insurance Group) to be excluded from the Scope of Application. We understand that the Working Group views financial entities, in general, to be of greater risk than other affiliates. Even so, all entities that meet the broad definition of “financial” in the GCC Instructions do not necessarily pose material risk (as defined above) under all circumstances. The fact that an entity would be classified as “financial” for purposes of the GCC should be weighed as a factor in the materiality analysis described above, but that alone should not be determinative of materiality.

II. Risk Charges for Material Non-Insurance Entities

Non-Financial Entities

AHIP’s view is that risk charges for non-financial entities should be equal or very similar to the current charge in the sectoral RBC formulas, i.e., 3% in the case of health insurers. The GCCWG has not provided data to suggest that a more substantial risk charge is needed to protect policyholders. In addition, existing regulatory processes, such as the Form B and D processes, are already in place to ensure that the regulated legal entity is protected from the non-regulated, non-insurance entity. Adding an additional risk charge is unwarranted in light of existing regulatory requirements.

Further, the GCCWG has not provided data indicating that policyholders are any more at risk in a diversified insurance holding company than in a non-diversified group. If that is a concern, and if it is desired to consider changes to underlying RBC levels, that should be handled through the appropriate (e.g., Health) RBC Working Group.

Financial Entities

On a related matter, AHIP is concerned with the breadth of the expanded definition of “financial entity” in the GCC Instructions. If the Working Group maintains this expanded definition of “financial entity”, we recommend using a capital charge that is roughly equivalent to an entity’s current post-covariance RBC charge. If it is desired to consider changes to underlying RBC levels, that should be handled through the appropriate (e.g., Health) RBC Working Group.

The exposed GCC Instructions provide that certain non-insurance affiliates of an insurer be deemed as financial. We understand that the Working Group views such affiliates to be of greater risk relative to other types of affiliates, and by deeming them to be financial, they would be listed separately for analytical purposes as well as subjected to a higher capital charge. Specifically, the exposed GCC Instructions add the following to the definition of “financial entity”:

“Affiliates that are integral to the performance of the insurance contract or the provision of insurance or financial products or services to policyholders, members or depositors [Examples include: agents, reinsurance intermediaries, claims adjusters or processors, third party administrators, pharmacy and other benefit managers, provider groups or entities that provide more than X percent of the policy benefits under policies issued by insurers within the group, and] will be treated as financial entities.”

AHIP fundamentally disagrees with the notion that certain affiliates are inherently riskier than others, as based on the language cited above which would effectively deem some affiliates to be considered financial, including third-party administrators and pharmacy benefit managers, provider groups, and pharmacy benefit managers. There is a wide array of types of non-affiliated entities within insurance groups, and it is overly simplistic to conclude that all that are somehow associated with assisting the insurer with contract performance or policyholder services are inherently riskier than others. Indeed, the Form B and D processes recognize that transactions with affiliates may have risks, and that a determination of such risk is very fact-specific to the subject entities and underlying transactions or agreements.

Further, subjecting these entities to a capital charge for financial entities (12% of 3-year average gross revenue – possibly to be increased to 15%) could result in a significant additional charge as compared to current RBC for several reasons:

- The base of the entity’s charge would be changed from BACV to gross revenue.
- The factor applied to the base would increase from 7% BACV to 12% of gross revenue.
- Removing the charge from the insurer’s RBC—where it is subject to the covariance adjustment—to a separate line item for the affiliate itself, where the capital charge is aggregated without a similar covariance calculation or other recognition of risk diversification.

In addition, AHIP has concerns about the reference to “entities that derive a majority of their gross revenue from services that are integral to the performance of the insurance contracts within the group or from the provision of other financial services to policyholders within the group will be considered a Financial Entity without a regulatory capital requirement” in the definition of “Financial Entity.” The GCCWG has not provided evidence to suggest that services performed by such affiliates add risk to the group. In our view, because of greater regulatory oversight

through the Form B and D and other regulatory processes, these arrangements actually reduce the group's risk.

Therefore, AHIP recommends using an equity-based capital charge that is roughly equivalent to the current post-covariance charge for such affiliates in RBC.

III. Treatment of Debt as Qualifying Capital

AHIP very much appreciates that the GCC will, in large measure, recognize certain senior and hybrid debt as capital. Debt is a critical capital resource for many of our members. The capital markets are well-established and have proven to be a reliable resource for the funding of debt instruments, even during the 2008-2009 financial crisis. Experience has shown time and again that the debt markets can be tapped quickly and utilized to enhance policyholder protection in a flexible and cost-efficient manner. Moreover, in periods of macroeconomic stress such as the financial crisis, the use of debt can be a more attractive alternative to the issuance of stock in depressed markets while also avoiding dilution of shareholder interests.

IV: Other Comments

In the attachment, AHIP has provided other comments and questions of a technical nature that were provided by our members.

* * * * *

Again, AHIP appreciates the opportunity to offer comments on the GCC Instructions and Template.

Sincerely,

Bob Ridgeway
Senior Government Relations Counsel

Attachment to Comment Letter of AHIP on the GCC Instructions and Template

1. We note that there are many areas within the template that are labeled “further work needed” or “technical discussions needed.” For example, “Summary Group Alternative 4” is blank. Also, in Summary 2 – Top Level: No formulas appear in the sensitivity section. When will companies have a completed template to review and test, and what other opportunities will there be to provide input on the template based on their review?
2. “Summary Alternative 5 – Organizational Option” is missing from both the template and the instructions. This option is intended to allow the reporting entity to present a summary of the results to assist regulators with understanding the submission.
3. Schedule 1D –Reporting “net dividends paid/(received)” is more practical and meaningful, because many entities act as “pass-through” for moving dividends up the corporate structure. In that context, “dividends received and not retained” becomes unnecessary.
4. I.A.2 in the instructions suggests that another consequence of “subsidization” may be “upward pressure on premiums to the detriment of insurance policyholders.” This implies that the GCC might somehow be a factor in regulating insurance premium rates, which we believe to be an inappropriate use of the GCC based on our understanding of its objectives.
5. I.A.2 in the instructions states that the GCC “provides an additional early warning signal to regulators so they can begin working with a company to resolve any concerns in a manner that will ensure that policyholders will be protected” and will “allow them to make informed decisions on both the need for action, and the type of action to take.” As stated, this is an overly ambitious aspiration for the GCC. In particular, at least in early years of implementation, the GCC will produce a ratio that would require much reliance on other existing regulatory tools to interpret – not the other way around. We understand that the Financial Analysis Handbook Drafting Group is working on guidance for regulators as to how the GCC would be utilized as part of financial analysis and in developing the Group Profile Summary. We recommend deleting the cited phrases in the instructions and await to comment on the work of the Drafting Group in that regard.
6. II.E.20. of the instructions discusses an annual redetermination of scope. This raises concerns about the meaningfulness of year-to-year trends in the GCC should the scope change. And if companies automate processes to produce the GCC, revisions would have to be made on an annual basis.

7. AHIP is unclear as to why the NAIC is proposing to collect data on intangible assets, which is not an element that is necessary to calculate the GCC.



July 20, 2020

Commissioner David Altmaier, Chair
Group Capital Calculation (E) Working Group
National Association of Insurance Commissioners

Re: Proposed Revisions to the Group Capital Calculation Instructions

Dear Commissioner Altmaier:

The American Property Casualty Insurance Association (APCIA) appreciates the opportunity to comment on the Group Capital Calculation (E) Working Group's revised draft Group Capital Calculation (GCC) Instructions. 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.

APCIA reiterates our appreciation that the NAIC is moving with the appropriate speed to develop the GCC and help incorporate it into state law. We likewise thank the Working Group and NAIC staff for their continued efforts to advance this important project. We offer these comments on the revised GCC Instructions for the following three topics: (1) Scope of Application, (2) risk charges for material non-insurance entities, and (3) treatment of capital instruments and debt.

I. Scope of Application

A. Determination of Material Risk

APCIA believes the GCC Instructions should include more detailed and principle-based guidance for establishing the Scope of Application of the GCC. In particular, guidance is needed for determining whether a non-insurance entity within the Broader Group poses material risk to the Insurance Group. This will allow companies and their lead-state regulators to identify such entities that do not pose material risk and therefore can be excluded from the Scope of Application, with as much consistency as possible across groups and states.

As a threshold matter, the GCC Instructions should provide a definition of “material risk” for purposes of the Scope of Application. In this context, we believe “material risk” should be defined as “risk emanating from a non-insurance entity that could adversely impact a group’s insurance operations and ability to pay policyholder claims.” Likewise, the GCC Instructions should explicitly state that non-material entities within the Broader Group (but outside the Insurance Group) should be excluded from the Scope of Application.

These points naturally follow from the fundamental reason for state insurance regulation and the stated objective of the GCC: policyholder protection. Indeed, paragraph 13 of the GCC Instructions already makes clear that “the overall purpose of this assessment is to better understand the risks that could adversely impact the ability . . . to pay policyholder claims”. This reasoning is also in accordance with international standards. For example, under ICP 23, the fact that a non-insurance entity poses risk is not, alone, determinative of whether that entity should be in or out of the scope of group supervision; rather, to be considered included in scope, there also must be some means by which the non-insurance entity could transmit that risk to the group’s insurance operations. In sum, there is more than sufficient justification for the GCC Instructions to make clear that the crux of the materiality analysis is whether an entity could adversely impact a group’s ability to pay policyholder claims, and that non-material entities (as determined using the definition of “material risk” in the preceding paragraph) should be excluded from the Scope of Application.

For effectuating the materiality analysis for purposes of the Scope of Application, APCI believes it is necessary to consider the totality of the facts and circumstances of a particular entity within a group. Given the diverse structures and business models of insurers, it would be impracticable to develop a one-size-fits-all checklist of guidelines that would be useful for materiality determinations across all groups. Strict or formulaic quantitative measures are likewise an insufficient proxy for materiality. Instead, the materiality analysis must consider the unique circumstances of the relevant entity and group.

To that end, APCI recommends developing a list of factors related to whether an entity could adversely impact a group’s ability to pay policyholder claims. Insurers and regulators could then use these factors to undertake a materiality analysis based on the totality of the facts and circumstances by considering the factors and how they apply to the group’s business. After this analysis, a determination can be made as to whether an entity is material. To be clear, no single factor is determinative of materiality of risk, nor should these factors be used as a scorecard or checklist. Below we offer examples of factors that should be considered when determining materiality of risk:

- The nature of the subject entity and specific activity(ies) that give rise to the risk.
- The means by which risk can be transmitted, or prevented from being transmitted, from the entity to the group’s insurance operations.
- The means applied for risk mitigation or transfer to third parties and the extent to which risk is reduced or transformed (e.g., to credit risk).
- Past experience (i.e., the extent to which risk from the entity has impacted the Insurance Group over prior years/cycles).
- The existence of cross-support mechanisms between the entity and the Insurance Group (e.g., guarantees).
- The location of the entity within the Broader Group and how direct or indirect the linkage may be.
- The existence and relative strength or effectiveness of structural safeguards that could minimize the transmission of risk to the Insurance Group (e.g., whether the corporate shell can be broken).

- The existence of sufficient capital within the entity itself to absorb losses under stress and/or if adequate capital is designated elsewhere in the Broader Group for that purpose.
- The extent to which there is risk diversification (e.g., where risks of one or more entities outside the Insurance Group are potentially offset (or exacerbated) by risks of other entities) and whether the corporate structure or agreements allow for the benefits of such diversification to protect the Insurance Group.
- The degree to which capital management across the Broader Group has historically relied on funding by the Insurance Group to cover losses of the subject entity.
- The degree of risk correlation between the subject entity and the Insurance Group.

The GCC Instructions currently contemplate excluding only non-material, non-financial entities from the Scope of Application. However, the Working Group should also consider allowing non-material financial entities within the Broader Group (but outside the Insurance Group) to be excluded from the Scope of Application. We understand that the Working Group views financial entities, in general, to be of greater risk than other affiliates. Even so, all entities that meet the broad definition of “financial” in the GCC Instructions do not necessarily pose material risk (as defined above) under all circumstances. The fact that an entity would be classified as “financial” for purposes of the GCC should be weighed as a factor in the materiality analysis described above, but that alone should not be determinative of materiality.

B. Scope of Application Starting Point

APCIA supports the new starting point proposed in the revised GCC Instructions that would allow large decentralized groups a reduction in Scope of Application up front in some cases. Likewise, we agree with NAIC staff’s suggestion that regulatory evaluation of an up-front reduction in Scope of Application should be based on established guidance that can be applied consistently across states. For this purpose, the GCC Instructions should provide guidance that is similar to the materiality test detailed in the preceding section. We believe utilizing similar guidance would be appropriate since the underlying purpose of excluding entities from the Scope of Application is the same, regardless of whether entities are first listed on Schedule 1 or excluded up front.

II. Risk Charges for Material Non-Insurance Entities

A. Non-Financial Entities

In the short term, risk charges for non-financial entities should be 3% of 3-year average revenue. By “short term” we mean during the first few years of the GCC’s implementation, a period during which experience will be gained that can then be analyzed in more detail and across more groups than was possible in field testing. In the meantime, APCIA recommends using average revenue over a 3-year period as the base for the risk charge in order to minimize volatility.

Once some experience is gained with the GCC, the Working Group should consider a variable risk charge that would be more risk-sensitive based on the industry or activity(ies) in which the subject non-financial entity participates. APCIA does not believe that the variable charge needs to be developed in an overall complex fashion, especially since the published field-test results show this charge had a fairly minor impact overall (e.g., as compared to the inclusion of debt as qualifying capital or the use of scalars). Rather, a future variable charge could be as simple as a

construct based on an assigned risk category (e.g., high/medium/low) with a differentiated charge for each.

B. Financial Entities

APCIA is concerned with the breadth of the expanded definition of “financial entity” in the GCC Instructions. If the Working Group maintains this expanded definition of “financial entity”, we recommend using, in the short term, a capital charge that is roughly equivalent to an entity’s current post-covariance RBC charge, while also developing a high/medium/low-risk construct with differentiated charges for the long term.

The exposed GCC Instructions provide that certain non-insurance affiliates of an insurer are deemed as financial. We understand the Working Group views such affiliates to be of greater risk relative to other types of affiliates, and by deeming them to be financial, they would be listed separately for analytical purposes as well as subjected to a higher capital charge. Specifically, the exposed GCC Instructions add the following to the definition of “financial entity”:

“Affiliates that are integral to the performance of the insurance contract or the provision of insurance or financial products or services to policyholders, members or depositors [Examples include: agents, reinsurance intermediaries, claims adjusters or processors, third party administrators, pharmacy and other benefit managers, provider groups or entities that provide more than X percent of the policy benefits under policies issued by insurers within the group, and] will be treated as financial entities.”

We have some concerns about the language cited above, which would effectively deem some affiliates to be considered financial. There is a wide array of types of non-affiliated entities within insurance groups, and it seems overly simplistic to conclude that all that are somehow associated with assisting the insurer with contract performance or policyholder services are inherently riskier than others. Subjecting these entities to a capital charge for financial entities (12% of 3-year average gross revenue – possibly to be increased to 15%) could result in a significant additional charge as compared to current RBC, for several reasons:

- The base of the entity’s charge would be changed from BACV to gross revenue.
- The factor applied to the base would increase from 7% BACV to 12% of gross revenue.
- Removing the charge from the insurer’s RBC—where it is subject to the covariance adjustment—to a separate line item for the affiliate itself, where the capital charge is aggregated without a similar covariance calculation or other recognition of risk diversification.

Therefore, in the short term, APCIA recommends using a capital charge that is roughly equivalent to the current post-covariance charge for such affiliates in RBC. Over the first few years of the GCC’s implementation, data can be collected and used to derive a more risk-sensitive charge, but also one that is pragmatic to develop and implement (e.g., a differentiated charge for entities of high/medium/low risk as determined by specified criteria).

III. Treatment of Debt as Qualifying Capital

APCIA very much appreciates that the GCC will, in large measure, recognize certain senior and hybrid debt as capital. Debt is a critical capital resource for many of our members. The capital markets are well established and have proven to be a reliable resource for the funding of debt instruments, even during the 2008-2009 financial crisis. Experience has shown time and again that the debt markets can be tapped quickly and utilized to enhance policyholder protection in a flexible and cost-efficient manner. Moreover, in periods of macroeconomic stress such as the financial crisis, the use of debt can be a more attractive alternative to the issuance of stock in depressed markets while also avoiding dilution of shareholder interests.

There is, however, an overarching issue that is presented by the way debt is treated in the proposed GCC Instructions. The treatment of debt differs in some key aspects from that which was adopted by the International Association of Insurance Supervisors (IAIS) in the Insurance Capital Standard (ICS) in 2019—which was the culmination of a long and hard negotiation process with U.S. interests supported by the NAIC, Federal Reserve Board (FED), and Federal Insurance Office (“Team USA”). As a result, and given the nature of the differences, the GCC could be viewed as less credible by other jurisdictional supervisors including those who may be parties to a Covered Agreement. Comparability of the GCC with the ICS is a looming issue on the horizon, the resolution of which can impact the views of many IAIS member jurisdictions about the efficacy of state-based regulation over U.S.-based insurance groups.

At the same time, the FED is working to complete its Building Block Approach (BBA) applicable to insurance groups under its supervision (i.e., savings and loan holding companies). The currently proposed approach in the BBA is more closely aligned with the principles-based criteria in the ICS than with the approach taken in the exposed GCC Instructions. While the proposed BBA approach would disallow debt except for grandfathered surplus notes, in some respects that is due to the unique mandate of the FED. For example, a criterion in the proposed BBA is that financial instruments be “subordinated to depositors and general creditors of the building block parent”, thus reflecting the FED’s mandate to protect the depository institution within the group.

With those high-level comments as an introduction, the following comments are intended as constructive suggestions to address some technical points in the GCC Instructions and template regarding debt. In addition, we offer some thoughts that may be helpful in addressing international perceptions.

A. Qualifying Instruments

APCIA recommends using criteria, rather than defined terms, to identify qualifying capital instruments. The GCC takes the approach of testing whether certain types of debt qualify as capital—specifically, senior debt, hybrid debt, surplus notes and “similar” instruments, and “other debt”. This contrasts with the approach taken by the IAIS in its ICS V.2.0 for the Monitoring Period, and by the FED in its proposed BBA. Both the ICS and the FED focus on criteria (e.g., permanence, loss absorbency, etc.) that are agnostic as to the title or name of a particular instrument.

There are two implications that we see. First, should the GCC go forward as currently proposed, the Working Group may need to supplement the GCC Instructions with definitions for each type of instrument. For example, “hybrid debt” is not defined in the Instructions. We understand that rating agencies treat subordinated debt issued by a parent company as “hybrid debt” as long as it is long-dated and has provisions to defer interest payments for a period of time. This could give rise to variation in treatment of hybrid debt (e.g., it may be unclear to a group if it should classify it as “hybrid” or as “subordinated” debt). On another level, comparability with the ICS needs to be considered, and on this point it seems that the more important issue is not whether types of debt are called out by name or more generically by tier, but whether comparable criteria to the ICS are used.

B. Treatment of Senior and Hybrid Debt

Using the calculation described below, the Instructions provide for an “additional capital allowance”. We first note this terminology has a potential connotation of an amount that is granted, in this case, to qualify as capital. We do not believe that to be the true nature of the calculation. Rather, for instruments that qualify for capital treatment based on specified criteria, it is a calculation to determine whether the aggregate dollar value of those instruments is within supervisory limits, and if not, the excess amount that would then disqualify. APCA believes that focusing the Instructions’ text on “limits”, rather than “allowance”, will help in some respects with perceptions about comparability.

For subordinated senior and hybrid debt instruments meeting specified criteria, the GCC Instructions are detailed and have certain options remaining for consideration by the Working Group. In brief, the amount that would qualify would be determined based on the following inputs:

- (1) Tracked down-streamed proceeds.
- (2) Total paid-in capital and surplus of U.S. insurers.
- (3) A proxy value, i.e., for senior debt, 30% of available group capital pre-debt plus outstanding senior and hybrid debt (15% in the case of hybrid debt).

The amount that would qualify for treatment as capital in the GCC would be the larger of (3) over the larger of (1) or (2), subject to two caps:

- The total amount of outstanding senior and hybrid debt.
- The amount of senior debt and hybrid instruments allowed in group capital cannot exceed 50% of group capital before such debt.

While APCA is of course not privy to the confidential, company-specific results of GCC field testing, it appears based on the wording in the GCC Instructions alone that in the vast majority of cases the amount of paid-in capital and surplus will exceed tracked down-streamed proceeds and, possibly, the proxy values as well. (The NAIC reported that field-test results showed only a handful of groups that were impacted by the limit, and only half of those resulted in a “haircut” greater than 10% of reported debt). This, in part, is because the calculation includes the paid-in capital and surplus of all U.S. insurance entities in the group, regardless of the source of that capital (whether from debt proceeds or otherwise).

The GCC Must Test for Subordination to Policyholders. There are indications in the exposed GCC Instructions that consideration is being given to simplifying the process by eliminating the down-streaming criterion altogether such that qualified debt would be the greater of (3) over (2), above, subject to the caps. If so, there would in effect be no explicit test to support that the debt is structurally subordinated. Recognizing that U.S. senior debt is not contractually subordinated, this could raise issues about international perceptions about the GCC. Team USA argued long and hard to support structural subordination in the ICS, finally achieving victory in Abu Dhabi last November. While use of structural subordination in the ICS is termed by the IAIS as a “national discretion”, it is an option nonetheless in the ICS that is now recognized by the IAIS and its key member jurisdictions on the IAIS Executive Committee who voted to adopt ICS 2.0. Therefore, we have concerns with the notion of deleting the down-streaming criteria without any other criteria to support subordination, as explained in the following paragraphs.

At a time when comparability with the ICS is an issue that is quickly coming to the forefront, it is not clear why the GCC would now take a very different route with respect to the treatment of debt. While down-streaming has raised many questions about how debt proceeds can be tracked and verified, the ICS criteria are workable and rely in large measure on each group and its group-wide supervisor to make that determination in light of the unique facts and circumstances surrounding each respective group. The IAIS avoided prescribing detailed rules or criteria for tracking. APCA believes the NAIC should do the same in the GCC, leaving the determination of the amount down-streamed to the lead state working in conjunction with the group.

APCIA believes a similar approach (to the ICS) can be just as workable in the GCC—focusing on criteria that are agnostic to the type or name of any particular financial instrument. This would include criteria to support that the qualifying amount of debt to be treated as capital is actually subordinated (either contractually by the terms of the instrument, or structurally), and other principle-based criteria, as in the ICS, to support permanence, loss absorbency, etc. Some refinement of the ICS criteria may be necessary to address U.S.-specific nuances for the GCC. Indeed, structural subordination is an example of such a nuance for which Team USA successfully negotiated before the IAIS to accommodate U.S. practices in the ICS. This would avoid a comparability issue with respect to which capital instruments qualify as capital resources. That said, one area where there could be explainable and appropriate differences with the ICS involves limits on the amount of those qualifying capital resources (such as described below with respect to surplus notes, which in our view, and as argued by Team USA before the IAIS in the case of the ICS, should have no limit) given some of the unique features of state-based regulation in the United States.

Therefore, to the questions posed by the exposed GCC Instructions as to whether the down-streaming / tracking test should be maintained and, if so, what criteria should be in place, APCA recommends keeping the test and using the criteria (with any U.S.-specific refinements necessary) that have been approved in ICS 2.0 for the Monitoring Period. That is, structurally subordinated debt should increase available capital to the extent the group and its lead state have determined such amount supports the insurance operations and is insulated from recourse by the lender, through tracking of down-streamed proceeds of the instruments into insurance subsidiaries.

There is, however, one other criterion for down-streaming that the Working Group could consider as an option to tracking down-streaming. Fundamentally, jurisdictional supervisors who permit subordinated debt to be treated for regulatory purposes as capital do so because policyholders remain protected; whether structurally subordinated or by the terms of the instrument, legally enforced restrictions and safeguards prevent the lender from “pulling the rug out from under” policyholders such that the debt is considered sufficiently permanent and loss absorbing. The issue becomes, to what assets and how much of those assets would the lender nonetheless have recourse?

As a practical matter, the lender would have recourse only to the liquid assets that remain in the entity that issued the debt (i.e., the holding company in the case of senior debt). For many groups, the unconsolidated balance sheet of the holding company (for public companies, the separate financial statements of the registrant are publicly reported in Form 10-K filed annually with the SEC) reflects a very large, illiquid investment in insurance subsidiaries, control over which is subject to regulatory oversight and approval. The amount of other, liquid assets in the holding company is typically much smaller. So, another option to test structural subordination is to limit the amount of senior debt to qualify as capital to that which is in excess of the liquid assets in the holding company. This would be easier to determine and to verify and may produce a value that would satisfy the group. If not, the group could revert to the tracking of down-streaming criterion.

C. Other Debt

Debt other than senior and hybrid debt is not allowed as capital pursuant to the exposed GCC Instructions. However, we understand that data will be collected in the GCC template for purposes of facilitating a sensitivity test based on a 15% allowance (of available group capital pre-debt plus outstanding senior and hybrid debt). We understand that the Working Group may later consider allowing limited amounts of other debt as capital if criteria can be determined. APCA is open to the possibility of some allowance for other debt in the future. However, we believe that consideration should also be given to comparability with the ICS and adherence to the principle of subordination.

D. Surplus Notes

APCIA agrees surplus notes should be treated as capital in the GCC and with no limit, as proposed in the Instructions. We understand that Team USA argued before the IAIS for a similar outcome in the ICS, especially for mutual insurance companies. The IAIS ultimately decided to make some accommodations for mutual-company surplus notes (included in Tier 2 instruments) but retained limits, albeit limits that are slightly higher than those applied to non-mutuals. Nonetheless, APCA supports the GCC treatment with no limit, given the well-established supervisory requirements and safeguards that surround all aspects of the issuance, maintenance, and repayment of surplus notes in the U.S.

E. Foreign Debt

APCIA likewise supports the GCC’s treatment of foreign debt. For debt issued by foreign entities, the GCC respects the treatment afforded by the local supervisor while also holding to the principle of subordination, whether that be achieved structurally or through the terms of the

instrument. If subordination is in place and if approved by the local supervisor as capital, the debt would qualify as capital in the GCC, a position with which APCIA agrees.

F. Overall Limitations on Debt as Capital

The exposed GCC Instructions have an overall limit on the use of debt as capital (i.e., senior debt and hybrid instruments allowed in group capital cannot exceed 50% of group capital before such debt). It is unclear if “group capital” as used for this test would include full value for surplus notes and qualifying foreign debt. Given that there is a separate limit applied to senior and hybrid debt – no more than 100% of such debt can qualify – it would seem appropriate that the overall limitation should apply to all debt, including surplus notes and foreign debt. That said, and as noted above, APCIA supports no limit on surplus notes of mutual insurers. It is important that all insurers be able to include unlimited amounts of capital from at least one organic source and one external source. In the case of stock companies, those would be retained earnings and common stock, respectively. In the case of mutuals and similar companies that cannot issue common stock, those would be retained earnings and surplus notes.

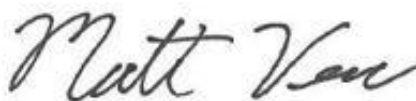
We observe that there are members of NAIC staff who participate in the development of the GCC as well as field testing of the ICS through their role on the IAIS Capital and Solvency Field Testing Working Group. Only they would be in a position to assess how the impact of the proposed limits in the GCC compare to those in the ICS for groups that have participated in both the GCC and ICS field testing exercises. Because APCIA is not in the same position, we do not offer a view on the overall limit of 50%. However, we do recognize that the comparability issue is also an important part of navigating the way forward with the GCC and encourage the Working Group to give due consideration in the context of the overall limit.

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

Sincerely,



Stephen W. Broadie
Vice President, Financial & Counsel



Matthew B. Vece
Manager & Tax Counsel

July 20, 2020

Commissioner David Altmaier
Florida Office of Insurance Regulation
Chair, NAIC Group Capital Calculation (E) Working Group
via e-mail to ddaveline@naic.org and lfelice@naic.org

Re: GCC Working Group Exposures

Dear Commissioner Altmaier:

A coalition of fourteen companies (Brighthouse Financial, CNO Financial, Genworth Financial, Global Atlantic Financial Group, Hannover Life Reassurance Company of America, Jackson National Life Insurance, Lincoln Financial Group, National Life Group, Principal Financial Group, Protective Life, Reinsurance Group of America, Sammons Financial Group, Standard Insurance Company/StanCorp Financial Group, and Transamerica) (collectively, the “Coalition”) appreciates the opportunity to comment on the exposure of the: a) Staff Group Capital Calculation (GCC) PowerPoint (the “PowerPoint”); b) revised draft instructions; c) revised GCC template; and d) FAQs relating to these documents.

The Coalition’s primary area of advocacy has been the need for the GCC to adhere fully to legal entity rules in support of the state-based legal entity solvency system. Accordingly, we welcome significant improvements within the exposed materials that eliminate several proposed “on top adjustments.” In this letter, we specifically want to indicate our support for the proposed treatment of XXX/AXXX captives.

In particular, we understand the revised instructions to include no “on top adjustments” for captives or permitted/prescribed practices. Furthermore, slide 11 of the PowerPoint indicates that a proposed sensitivity analysis for XXX/AXXX captives will be excluded from the GCC template “upon referral to an E Committee Group or Subgroup for Further Risk Assessment.” Once this occurs, we understand that further analysis would be separate from the GCC itself. Assuming our understanding is correct, the Coalition fully supports the proposed treatment and looks forward to working with the relevant group of regulators.

We thank you, the Working Group, and NAIC staff for your attention to this letter and prior Coalition correspondence. We look forward to continuing to work with you and your team as the NAIC moves towards finalization of the GCC.

Sincerely,

Brighthouse Financial
CNO Financial
Genworth Financial
Global Atlantic Financial Group
Hannover Life Reassurance Company of America
Jackson National Life Insurance

Lincoln Financial Group
National Life Group
Principal Financial Group
Protective Life
Reinsurance Group of America
Sammons Financial Group
Standard Insurance Company/StanCorp Financial Group
Transamerica



July 20, 2020

Lou Felice
Solvency and Capital Policy Advisor
National Association of Insurance Commissioners

Dear Mr. Felice,

Global Atlantic appreciates the opportunity to comment on the exposure draft of the revised GCC instructions and the revised GCC template. Our comments address concerns with the following:

- Capital calibration
- Downstream tracking of debt
- Scalar methodology
- Scalar governance

We also seek guidance on whether GAAP equity values should include or exclude OCI when GAAP is used as the accounting method to determine the carrying value of an entity.

Capital Calibration

We have concerns with the current proposed approach of using the trend test level of 300% ACL as the capital calibration level. First of all, 300% ACL is inconsistent with the 200% ACL (= 100% CAL) calibration level widely used in the insurance industry for RBC. We believe this will lead to confusion and misunderstandings when comparing RBC to GCC, potentially undermining the current RBC standard. RBC ratios are typically in the 350% to 450% range, but the GCC ratio will be much lower. For example, if the underlying RBC ratios of the companies in the group average 450% RBC, the resulting group capital ratio will be ~300%.

In addition, we believe the insurance industry's current reporting of two capital calibration levels, (100% ACL and 200% ACL) results in confusion and frequent misinterpretation of reported ratios; adding a third calibration level for the GCC of 300% ACL will compound the problem. We believe this will lead to additional confusion and misunderstanding by users of financial information, including the regulatory, rating agency, and banking communities.

We strongly request that the NAIC adopt a 200% ACL calibration level for the GCC.

Downstream Tracking of Debt

The current instructions rely on downstream tracking in order to count debt proceeds as part of available capital. In practice, our company borrows externally in order to downstream it to the insurance companies; however, we have not found it necessary to track downstream transactions and question whether a tracking system would simply introduce complexity without providing a benefit.

We are in favor of a proposal to eliminate downstream tracking logic and replace it with a simple comparison to paid-in capital and surplus, for the following reasons:

- Simpler, more efficient, and more reliable test
- Avoids complications that could result from debt that has been refinanced by the parent as there would be no contribution of the debt amount issued.
- Avoids complications of tracking upsize transactions where debt is borrowed at one date and then down streamed at a different date.
- Avoids complications of tracking the reverse: dividends which are up streamed. Are those upstream transactions to be netted against down streamed capital or not?
- Avoids complications and questions related to M&A transactions – if a company is acquired, does the new parent company automatically assume the historical relationship of down streamed debt, so long as its debt at least equals the debt of the old parent company?

If the downstream tracking approach is maintained, once layers of transactions of the type described above are introduced, a comprehensive downstream tracking system will need to be developed, communicated, applied and reported across the industry in a way which is comparable and reliable. Our view is that industry and regulator efforts to track down streaming will not add value. In our case, the resulting capital adjustment will be the same whether we develop a downstream tracking process or whether we run a simple test ensuring that paid in capital at least exceeds the capital adjustment amount.

Scalar Methodology

We support the Excess Relative Ratio Approach for scaling non-U.S. capital ratios to U.S. RBC. This method utilizes two anchor points for scaling:

1. The respective industry average capital ratio
2. The regulatory intervention level.

The alternative scaling approach, the Pure Relative Ratio, relies solely on the industry average capital ratio to translate a non-U.S. capital ratio to U.S. RBC. It does not take in to account the regulatory intervention level. Since the Pure Relative Ratio approach adjusts required capital only, available capital is not adjusted, resulting in excess capital being distorted. Since the Excess Relative Ratio approach adjusts both available capital and require captial, excess capital is not affected.

Thus, the Pure Relative Ratio lacks a mechanism to ensure that a non-U.S. firm at the regulatory intervention level within it's respective country will be at the U.S. RBC intervention level once scaled. This is a material fault. Again, we support the Excess Relative Ratio Approach, and its ability to align regulatory intervention levels across jurisdictions.

Scalar Formulation

Transparency of how the scalars are calculated will be critical, regardless of which scaling methodology is selected. In order to appropriately manage capital under the group framework, firms must have a thorough understanding of how scalars behave. Many non-U.S. countries rely on market-

value based capital ratios, which have potential to behave differently than the book-value based RBC measure.

We believe the following themes should define the scalars:

Consistency – scalars should be calculated and applied consistently across all non-U.S. regimes.

Specificity – scalars should be discretely computed and applied amongst life, property casualty and health insurance companies.

Stability – the results of applying scalars to Non-U.S. capital ratios should not be volatile; for example, converting to U.S. RBC should not yield a significant headwind in one year, and a significant tailwind in the following year.

Additionally, we believe answers to the following questions are critical for firms to understand the impact of the scalars:

1. How is the country average computed? Is the concept of country average based on equal weighting each firm? Alternatively, is it size weighted, such that a large provider in Country Y may dominate the average of Country Y?
2. How frequently will the scalars be updated?
3. Will scalars derived from Year 20XX be applied to 20XX actual results, or will timing of filings and data availability create a lag?
4. Will scalars take in to consideration only a single year, or alternatively, will a rolling average mechanism be utilized?

GAAP Equity

The GCC instructions are silent on whether OCI should be included or excluded when GAAP equity is used as the carrying value of an entity. Companies typically report GAAP equity excluding OCI to lessen the amount of volatility that can arise when including market value adjustments of assets. Excluding OCI is also consistent with statutory accounting rules that generally do not reflect the market value of assets. We suggest that the GCC instructions include guidance on whether OCI should be included or excluded when reporting GAAP equity. Otherwise there could be inconsistencies in how companies report GAAP equity amounts.

Again, thanks for allowing us to provide our comments on the revised GCC instructions.

Sincerely,



Lauren Scott
Head of Regulatory and Government Affairs
Global Atlantic Financial Group



Ann Kappler

Senior Vice President, Deputy General Counsel and
Head of External Affairs

Prudential Financial, Inc.

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Tel 973 802-9133

Ann.Kappler@prudential.com

July 20, 2020

Via Electronic Delivery

Commissioner David Altmaier
Florida Office of Insurance Regulation
Chairman, NAIC Group Capital Calculation (E) Working Group
Via email to Lou Felice (lfelice@naic.org)

Re: The National Association of Insurance Commissioners (“NAIC’s”) Draft Group Capital Calculation (“GCC”) Instructions and Template

Dear Commissioner Altmaier:

Prudential Financial, Inc. (“we”) thank the Group Capital Calculation Working Group (“Working Group”) for continuing to seek input on key elements of the GCC. We support the development of supervisory tools, such as the GCC, that will enhance state regulators’ ability to protect policyholders and insurance markets. Further, we believe the GCC framework – through its employment of an inventory approach to obtain insight into all entities within the group and the location and sources of capital – can achieve the NAIC’s stated objective of providing state regulators a *“panoramic, transparent view of the interconnectedness, business activities, and underlying capital support for an insurance group.”*

While the foundation of the GCC framework is strong, we believe appropriate outcomes for a number of key design elements is essential to ensure the final version provides state regulators appropriate insight into risks while minimizing the potential for unintended consequences. In the pages that follow, we identify the approaches that we believe would best position the GCC to accomplish these objectives.

We again thank the Working Group for seeking stakeholder input on key elements of the GCC and would welcome the opportunity to discuss the information included in this response should the Working Group or NAIC staff engaged in the GCC project wish to do so.

Sincerely,

A handwritten signature in blue ink, appearing to read "Ann Kappler", with a long horizontal flourish extending to the right.

Ann Kappler

Senior Vice President, Deputy General Counsel and Head of External Affairs
Prudential Financial, Inc.

Overview

We strongly support the Working Group's decision to employ an aggregation based approach in order to *"build on existing legal entity capital requirements where they exist rather than developing replacement / additional standards."* As the Working Group has rightfully noted, such an approach strikes an ideal balance of *"satisfying regulatory needs while at the same time having the advantages of being less burdensome and costly to regulators and industry and respecting other jurisdictions' existing capital regimes."*

As the Working Group takes steps to finalize the GCC, we encourage it to pursue approaches that are aligned with the objective of providing regulators transparency into risks while avoiding the creation of additional standards that are unnecessary and may be burdensome and costly. Further, we also encourage the Working Group to consider the impact the various design choices may have on the ability of the GCC to provide appropriate insight into risks (e.g., avoid false positives and negatives) and how they could affect the ability of supervisors and / or insurers to navigate periods of stress.

Limitations on the Recognition of Senior and Hybrid Debt Should be Removed

We believe the proposed limitations on the recognition of senior and hybrid debt are inconsistent with the NAIC's stated intent for the GCC to serve as tool for obtaining insight into insurance groups rather than a binding constraint and further, could discourage the prudent use of debt instruments as an effective capital and liquidity management tool – particularly during times of stress. We therefore believe the Working Group should eliminate the proposed limits on the degree to which senior and hybrid debt qualify as available capital.

Insurers weigh a number of critical elements when establishing and managing their capital structures such as rating agency targets, cost, tax implications, etc. In practice, these considerations serve as effective guardrails against behavior that may be detrimental to the insurer or policyholders. Similar to the Working Group's decision to leverage the strength of existing solvency regimes rather than developing replacement / additional standards, we believe the GCC should leverage existing market forces that promote sound capital management practices across the sector. The May 19 NAIC Group Capital Calculation Post Field Testing Staff Input presentation highlighted that under the current GCC proposal, 25% of the volunteer companies from the 2019 field test that reported senior and / or hybrid debt would not receive full credit for the capital instruments they have issued. We believe this percent could increase significantly during economic downturns as an insurer's available capital declines and required capital increases, which would further limit the recognition of these resources and inappropriately discourage their use. Eliminating the proposed limits on the recognition of senior and hybrid debt would avoid the potential for the GCC to trigger such procyclicality.

Should the Working Group insist on maintaining limitations, we request the following changes to better acknowledge the presence of existing market guardrails and reduce the potential for the GCC to inhibit an insurer's ability to manage its capital structure in a manner it feels is most appropriate and have procyclical effects during economic downturns. Further, the purpose of any imposed limitations that are retained should be explained in light of the stated intent for the GCC to serve as tool to obtain insight into risks as opposed to a binding constraint.

- The cap of the allowance at 50% of total adjusted carrying value in Inventory B should be eliminated given that the underlying allowances, which are modeled largely after rating agency approaches, already have conservatism embedded in them.
 - Specifically, the 30% factor for senior debt and 15% for hybrid debt are being applied to a more conservative base than rating agencies use for establishing limits – i.e., the GCC intends to apply the factors to the sum of total adjusted carrying value + outstanding senior and hybrid debt while rating agencies typically base their assessment on the group’s total consolidated U.S. GAAP equity.
 - Adding a limit of 50% of total adjusted carrying value to the conservative 30% and 15% limits for senior and hybrid debt (relative to total adjusted carrying value + outstanding senior and hybrid debt) effectively lowers the 45% permitted (i.e., 30% + 15%) to approximately 33%.
- More broadly, the different objectives of the GCC versus rating agency frameworks must also be considered. For example, S&P’s capital model is calibrated to much higher confidence levels (e.g., 97.2% for “BBB”) and views 20% to 40% financial leverage, based on a group’s total consolidated U.S. GAAP equity, plus outstanding debt, as “neutral”.
- Requirements for tracking the down-streaming of debt issuance proceeds to regulated entities should be eliminated. Keeping funds at the holding company level is a prudent strategy that provides insurance groups flexibility to quickly and easily manage capital and liquidity needs across the group. We believe a tracking requirement could give rise to unintended consequences such as reducing the availability and fungibility of capital resources and forcing U.S. insurance groups to issue greater amounts of debt.

The Base GCC Should Use the Excess Capital Ratio Scalar Approach

Prudential disagrees with the suggested change to apply the Pure Relative Ratio option at 300% RBC Calibration in the Base GCC. We believe that a total balance sheet approach to scalars – as embodied in the Excess Capital Ratio Approach – is necessary to adequately account for key differences across insurance regimes, such as the level of conservatism embedded in reserves versus required capital, different valuation and asset admissibility standards, etc. and avoid distorting the measure of required, available, and excess capital. Further, we believe embedding a scalar methodology with shortcomings (i.e., the Pure Relative Ratio Approach) in the Base GCC could undermine the NAIC’s ongoing work at the global level to secure recognition of the Aggregation Method (“AM”). Therefore, while we believe the Excess Capital Ratio Approach is an appropriate method for including in the Base GCC we would also support using a scalar of 100% (i.e., not scaling foreign insurance regimes) until there is greater clarity on what scaling approach will ultimately be included in the AM.

Through its simplistic approach of only focusing on required capital, the Pure Relative Ratio Approach fails to adequately account for key differences in insurance regimes (e.g., level of conservatism embedded in reserves versus required capital, different valuation and asset admissibility standards, etc.). While the limited analysis to date may suggest the two approaches yield similar results, we believe they would diverge in cases where individual insurer or industry capitalization levels change and that the conceptual shortcomings of the Pure Relative Ratio Approach could result in false positives or negatives.

More broadly, we are concerned that adopting the Pure Relative Ratio Approach for purposes of the Base GCC would undermine the ongoing work at the NAIC's work at the global level to secure recognition of the AM as comparable to the reference method version of the Risk-based Global Insurance Capital Standard ("ICS"). Specifically, we believe that the decision would prejudice the Pure Relative Ratio Approach as the methodology that should be adopted for the AM. Further, we believe it will be essential for the comparability assessment work to take a holistic approach to accounting for the different tools and methods supervisors employ to ensure insurers hold adequate loss absorbing resources to protect policyholders; of the two approaches the Working Group has considered, the Excess Capital Ratio Approach – with its total balance sheet approach – is the only one of the two that would accomplish this.

In the May 19 NAIC Group Capital Calculation Post Field Testing Staff Input presentation, NAIC staff noted the need to continue to explore the topic of scaling in conjunction with similar work for ICS – AM. We support this recommendation and believe it highlights the importance of keeping the GCC and AM in step with each other and taking time to consider the appropriateness of the methodology relative to a suite of criteria, including the reasonableness of the assumptions, ease of implementation, and stability of the parameterization. That said, while we strongly believe the Excess Capital Ratio Approach should be used in the Base GCC (and the Base AM), an alternative path that should be considered is to use a scalar of 100% for the Base GCC until there is greater clarity on what scaling approach will ultimately be included in the AM. Such an approach would avoid prejudging that the AM should employ the Pure Relative Ratio Approach and avoid the potential need to modify the Base GCC in the future if a different scaling methodology is embraced for the AM.

The Calibration of the Base GCC and Scalars for Foreign Insurance Regimes Should be 200% ACL RBC

Prudential disagrees with the suggestion to calibrate the Base GCC ratio or scalars for foreign insurance regimes at 300% authorized control level ("ACL") RBC – i.e., the Trend Test level. Instead, we believe they should be calibrated to 200% ACL RBC – i.e., Company Action Level ("CAL") as it has long been common practice for insurers to communicate and stakeholder to assess financial strength on this basis. We believe using 300% as the calibration would unnecessarily interrupt well-established market norms and introduce unwarranted confusion for insurers and stakeholders without any discernable benefit. Further, we believe calibrating to a 300% ACL RBC level could create confusion over, or trigger an unwarranted reset of, how the NAIC's time tested ladders of intervention approach to the supervision of capital adequacy works in practice.

We recognize a relationship has been established between the 300% ACL RBC level and 100% Solvency Capital Requirement ("SCR") for Solvency II in the U.S.-EU and U.S.-UK Covered Agreements and further, that the NAIC's Evaluations of Reciprocal Jurisdictions have similarly established relationships between the 300% ACL RBC level and intervention points under the solvency regimes of Bermuda, Japan, and Switzerland. However, we do not believe these developments justify upending years of industry norms, and the likely confusion that would result from calibrating the Base GCC or scalars of foreign insurance regimes at a 300% ACL RBC level. While we speculate that international considerations may be contributing to the interest in using the 300% ACL RBC level for calibration purposes, we believe it is incumbent on the Working Group to confirm its rationale so a more informed debate could be held with interested parties before a final decision is made.

The Sensitivity Analysis Tab Should Be Removed from the GCC Template

Prudential believes the GCC template should be limited to reporting of the Base GCC (and the required inputs thereto) and that the Sensitivity Analysis tab should be deleted. Narrowing the design of the GCC will ensure insurers, supervisors (domestic and foreign) and other stakeholders have a clear vision and understanding of what the GCC is (e.g., it would eliminate the need to distinguish between a “Base” view and alternative measures). Notwithstanding the comments above regarding scalar methodology, we believe clarity in the design of the GCC is critical as insurers and supervisors move to introduce the GCC as an additional metric to monitor and manage and would provide a stronger foundation for the NAIC’s ongoing efforts to advance the AM at the global level.

To the extent broader information on the insurance group is of interest to a state regulator, we believe it should be obtained through discretionary powers as opposed to embedding it in the GCC template. We believe “Input 6 – Questions” should be transitioned to a Microsoft Word document as it is more user friendly format (note that the NAIC employs such an approach for its work on the AM at the global level). A word based file could serve as a more flexible vehicle for insurers and state regulators, including potential instances where the regulator wishes to receive information beyond that which is included in the GCC template (note a fillable PDF could also be used).

Grouping of Similar Non-insurance Entities and / or Relaxing De-stacking Requirements for Non-Insurance Entities Should Be Permitted

Prudential appreciates the Working Group’s consideration of permitting grouping of similar non-insurance entities and / or relaxing the requirement for de-stacking as we believe such flexibility would reduce the burden of completing the GCC template. While we support such flexibility, we believe state regulators should retain the option of requesting more granular information should they feel it is needed to obtain a sufficient view of risks within the group.

Simple Approaches Should be Adopted for Financial Entities and Non-financial Entities Without Regulatory Capital Requirements

For simplicity, Prudential supports adopting a single approach for establishing a proxy capital measure for all financial entities that are not subject to a regulatory capital requirement. Further, we believe it would be beneficial for the Working Group to select the method it believes most aligns with how the AM will ultimately treat this item. Per our comments above, we support grouping of similar entities and thus support the netting of non-operating holding companies. We similarly support adopting a single approach for establishing a proxy capital measure for all non-financial entities that are not subject to a regulatory capital requirement.

We believe ensuring state regulators obtain adequate insight into the entities within the insurance group and risks associated with them is the key point of consideration for these entities and this is best accomplished through the inventory element of the GCC as opposed to an arbitrary proxy capital calculation. To the extent a state regulator believes a non-regulated entity poses material risk to the group, they have discretion to request additional information to understand the risks. Further, such situations would be better addressed through in-depth analysis on a case-by-case basis as a formula driven proxy capital calculation would likely fail to reflect the underlying risk exposures. That said, we believe further consideration of approaches is unwarranted and the Working Group should narrow the

GCC template to single approach for each respective category of entities rather than continuing to test multiple approaches.

The Draft Financial Analysis Handbook Guidance Should Be Exposed for Comment

Materials for the May 19 public meeting of the Working Group included an Attachment C – “Draft Regulatory Guidance on GCC”, which was not part of the materials recently exposed for comment. We request that the Working Group provide interested parties an opportunity to provide input on this material before it is finalized.

Below are some initial thoughts on the draft version that was included in the May 19 meeting materials.

- Establishing a minimum threshold that must be maintained to avoid triggering a more in depth supervisor review and/or the need to develop a plan to reduce risks would be inconsistent with the NAIC’s stated intent for the GCC to serve as a tool rather than a binding standard.
- The detailed nature of the guidance seems premature given the range of design elements that have yet to be finalized, which could have a material impact on GCC ratios, and ongoing consideration of which insurers will be exempt from having to file the GCC.



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Via Electronic Delivery

Commissioner David Altmaier
Florida Office of Insurance Regulation
Attention: Mr. Lou Felice
J. Edwin Larson Building
200 E. Gaines Street, Room 101A
Tallahassee, Florida 32399

RE: Draft Instructions from the Chair of the Group Capital Calculation (E) Working Group
to the Chair of the Group Solvency Issues (E) Working Group

Commissioner Altmaier:

State Farm Mutual® Automobile Insurance Company and its affiliates ("State Farm"), appreciate the opportunity to submit these comments concerning the Draft Instructions from the Group Capital Calculation (E) Working Group (the "Working Group"). As you know State Farm participated as a volunteer group and provided feedback as to the Group Capital Calculation ("GCC") and its supporting informational elements during its development. State Farm understands that the GCC provides an evaluation tool for domestic regulators to consider along with various other risk information already being provided by groups, such as the Own Risk Solvency Assessment ("ORSA") Report filing.

State Farm urges the Working Group to consider the entirety of the regulatory structure when evaluating whether to include additional measures through the Draft Instructions on insurers or the holding company of those insurers that are not entirely exempted, especially when the group structure is simplistic, focused on insurance operations and when such parent of the holding company is a regulated insurer.

As a volunteer participant State Farm benefitted from the effort and transparency the Working Group has utilized all along in developing the GCC and appreciates that the Draft Instructions incorporates many of the industry's clarifications and suggested additions. However, State Farm suggests a few more amendments to the Draft Instructions to recognize today's overall financial regulatory scheme and limit duplication as much as possible for regulators and those being regulated when such groups are not exempted from GCC and are substantially an insurance group.

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Scope

State Farm requests that the same isolation method of excluding non-financial entities be available for other entities in a group.

State Farm supports the Draft Instructions statement in paragraph 12 that recognizes there are groups that have material diverse non-financial activities that are isolated from the financial/insurance group and that could lead to a narrowing of the scope of the GCC in agreement with the Lead State Regulator. However, State Farm questions why the Draft Instructions do not similarly recognize financial or insurance entities that are also similarly isolated from the group. The purpose of the GCC is to evaluate a group's solvency soundness through a numerical calculation to ensure the primary regulated insurance entities within the group remain sound. Acknowledging the isolation of financial and insurance entities fits within already existing regulatory arrangements as well as the GCC, and acknowledges that capital is not freely fungible for use by the group or entities within the group. Since the same mechanisms recognized by the Draft Instructions to isolate the non-financial entities can be and are being used to isolate financial or insurance entities, the Draft Instructions should recognize the isolation no matter the entity type.

The GCC should not ignore the other existing provisions of the Holding Company Act or solvency provisions applicable to the individual insurance member of the group, such as the Risk Based Capital (RBC) calculation that provides a similar numerical calculation of soundness, financial statements and other applicable regulatory requirements. These provisions, commonly referred to as the windows and walls regulatory scheme, protect the capital of that insurance entity such that capital is not freely available for the use by the group or any other entity within the group. Similar to the recognized ability of non-financial entities to be isolated from the rest of the group, the windows and walls approach isolates the insurance entities from material transaction with affiliates and in a sense isolates the entities. Expanding the acknowledgement of the ability to isolate financial and insurance entities is not radical and fits within the overall goal of the current windows and walls regulatory approach as well as the GCC, to protect the solvency of the insurance members of a group. Just as a non-financial entity may be isolated and pose no risk to an insurance entity in the group, if a financial entity is isolated from the group, it does not pose a solvency risk to the insurance entity. Finally, an argument could also be made that if the insurance entity is isolated from the group in a similar fashion, the group does not pose a risk to the isolated insurance entity. For these reasons, State Farm requests that groups be allowed to present a narrower scope for entities that are otherwise isolated to the Lead State Regulator who would have discretion to accept such narrowing of the scope for that group's GCC.

State Farm requests that excluded entities not be required to be included on the Inventory Tab or discretion be provided to the Lead State Regulator to exclude, especially when the information is otherwise provided.

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In paragraph 14, the third bullet provides that “All entities, whether to be included in or excluded from the Scope of Application are to be reported in the Inventory Tab of the template.” Presumably, this includes the non-financial entities that are isolated and excluded under paragraph 12 or paragraph 30 and financial/insurance entities that are excluded under paragraph 10 and 18. If this is accurate, preparers will be required to provide the required information on entities that are excluded from the scope of the GCC. While there may be certain situations when such information would not otherwise be provided to the Lead State Regulator, in an insurer parent lead group this information is already provided through other required regulatory submissions including but not limited to, financial statements and RBC calculations of the parent insurer or the insurance entities. Gathering information under the GCC from entities that are excluded from the GCC seems counterintuitive and duplicative in certain situations. State Farm requests that excluded entities not be required to be on the Inventory Tab or, at least, the Lead State Regulator have the discretion to not require excluded entities on the Inventory Tab if requested by the preparer.

State Farm requests a baseline materiality definition be provided while maintaining Lead State Regulator discretion to determine if a higher or lower material threshold is appropriate.

The Draft Instructions use the term “material” in discussion whether an entity can be excluded or is to be included in the GCC. State Farm believes discretion should remain with the Lead State Regulator, however, it is important to have a clear understanding of what is meant by “material” and to create some consistency in application. For paragraphs 10 and 18 there is no guidance, but for paragraph 30, which addresses determining what is an “affiliate” to be included in the GCC, it states in part:

For purposes of the GCC, affiliates will NOT include those affiliates reported on Schedule A or Schedule BA, EXCEPT in cases where there are financial entities reported as or owned indirectly through Schedule A or Schedule BA affiliates or where a non-financial, non-insurance Schedule A or Schedule BA affiliate represents greater than X percent of an insurance entity’s adjusted available capital.

The paragraph provides a Drafting Note providing guidance to regulators:

DRAFTING NOTE: Initial suggestion is to set “X” threshold for material non-financial entities no higher than 5%.

State Farm suggests adding to the Draft Instructions, additional Drafting Notes in the paragraphs using the term “material”, a baseline for materiality of 5% of the group’s net worth while still allowing the Lead State Regulator and the preparer to use a higher or lower threshold given the particular circumstances presented by the preparer.

State Farm believes that there should be some consistency in application under these provisions and that materiality should be based on the group’s net worth given the GCC is measuring risk of the group and not a particular entity in the group. RBC calculation along with other regulatory



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requirements provides the Lead State Regulator the information necessary to evaluate the solvency risk of an individual insurance entity and the GCC should be focused on information that a Lead State Regulator doesn't already receive and be focused on the impacts to the group. Including a Drafting Note provides guidance, allows the Lead State Regulator and the preparer to utilize a different value for unique situations, and allows the focus of the GCC on those matters that truly impact a particular group.

State Farm offers these comments on the Draft Instructions to help streamline the process for those groups required to conduct the GCC. The intent of the comments is to help the focus of the preparer and Lead State Regulator to be on the insurers of that group and the material impacts of other members of the group that may have on the solvency of the insurance members.

Thank you for your time and consideration in this project and to our comments. If there are any questions concerning the comments, please contact me.

Sincerely,

A handwritten signature in blue ink, appearing to read "Charles M. Fein", written over a horizontal line.

Chuck Feinen
State Farm Mutual Automobile Insurance Company

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July 20, 2020

Hon. David Altmaier
Commissioner
Florida Office of Insurance Regulation
Chair, Group Capital Calculation Working Group
The Larson Building
200 East Gaines Street
Tallahassee, FL 32399-0305

Via electronic mail to Lou Felice

Re: Comments on GCC Instructions and Template

Dear Commissioner Altmaier:

We write today on behalf of UnitedHealth Group, one of the nation's largest managed care and healthcare services companies, which, through its UnitedHealthcare business platform, administers and provides healthcare benefits to more than 45 million individuals in all fifty states and the District of Columbia. UnitedHealth Group's Optum business segments provide health services, including pharmacy services, health care delivery, population health management, collaborative care delivery, information technology, and health care financial services to 115 million individuals and more than 100,000 physicians, practices, and other health care facilities nationwide. We thank you for the opportunity to provide comments on the recently released draft Group Capital Calculation ("GCC") template and instructions.

We appreciate the simultaneous disclosure of the template, instructions, confidentiality provisions and the handbook draft. This is helpful context for understanding the working group's intent for this initiative.

Comments on the Instructions

The GCC Instructions address not only the mechanics of filling in the template, but also many considerations that regulators are supposed to apply when using the template. We have comments about both aspects of the Instructions. We have divided our comments on the instructions into two sections – our key concerns, and additional concerns that do not rise to the level of a key concern but nevertheless are important to consider as these instructions are finalized.

Our comments in both sections are labeled according to the paragraph labels in the GCC Instructions.

Instructions Comments – Key Concerns

Key Concern #1: Calibration Level

V.A.40: As we have explained previously, with supporting numerical examples, the method being used to produce the “scalars” [sic] for alien insurers is incorrect, as it takes into account only differences in the average capital being held, and not the relative conservatism of reserves. While there are other conceptual problems with the concept of scalars as being employed here, this particular error should be corrected; we had previously offered a suggestion as to how to make the correction.

VI.57 and VI.58: For entities that file an RBC report, the requirement is to report “entity required capital” at 150% of Company Action Level (CAL). There is no justification for this. Reference is made to the trend test in the RBC formula, which may result in an action level event for entities with Total Adjusted Capital below 150% of CAL; however, that can only occur if certain other, relatively unusual conditions exist, and those other conditions are not tested for in the GCC. Consider the illogical result this would produce for a group where the ultimate controlling person was an RBC filer with Total Adjusted Capital equal to 130% of CAL: the entity would be considered well capitalized from an RBC standpoint, and yet would fall below the 100% level in the GCC. This seems especially misguided given that early drafts of the Financial Analysis Handbook procedures suggest further scrutiny of a group when the GCC ratio is below 175%—i.e., is below 262.5% of CAL.

Furthermore, 100% of CAL may itself be excessive. Early in the development of the GCC, the question was raised as to how the diversification benefit of large, heterogeneous groups would be reflected. Clearly, such a group is less risky than its individual components standing alone would be. The NAIC’s decision at that time was not to have an explicit diversification adjustment (like the covariance adjustment in RBC) built into the GCC, but instead to take diversification into account when interpreting the results. Accordingly, a diversified group should have a capital benchmark that is less than the corresponding benchmark for an individual entity—which in the case of an RBC filer would be CAL. From that standpoint, calibrating the GCC even to 100% of CAL would be conservative; using 150% of CAL is unjustifiably conservative. The mere addition of legal entity capital and capital requirement, without any provision for diversification should is not be interpreted as group risk-based capital regulation.

These concerns about calibration are heightened by the language in paragraph I.A.2 (discussed above) indicating that the GCC will be a basis for regulators to take actions with respect to a group. Even if the GCC will be used solely as an analytical tool, the analysis should be based on an appropriate calibration, to avoid unnecessary follow-up questions and prolonged discussions. However, if the GCC will, in and of itself, be grounds for regulatory action (as suggested by some of the language in the instructions), it is absolutely critical that the calibration not misstate the riskiness of the group.

Key Concern #2: Definition of “Financial Entity”

IV.22: We believe that the definition of “Financial Entity” is far too broad, in that it sweeps in “Affiliates that are integral to the performance of the insurance contract or the provision of insurance or financial products or services to policyholders, members or depositors,” such as “claims adjusters or processors, third party administrators, pharmacy, medical provider groups, and other benefit managers,” etc., even when those entities are not material to the group or calculation as a whole. Affiliates that merely provide contracted services to a carrier should not be defined as “financial”: they do not create any more financial

risk to their affiliated insurers than do non-affiliates that provide the same services to other insurers. In fact, given that regulators have oversight over inter-affiliate service agreements, we suggest that affiliated service providers present less risk than do non-affiliates. In the case of health groups, some of the examples given actually diversify risk for the insurance entity in the group, facilitating more access to capital by the insurance entity. The aim of the working group should not be to promote smaller, less integrated or diversified groups.

VI.61: We again object to the notion that “entities that derive a majority of their gross revenue from services that are integral to the performance of the insurance contracts within the group or from the provision of other financial services to policyholders within the group will be considered a Financial Entity without a regulatory capital requirement” [emphasis added]. As noted in our comments on paragraph IV.22, the fact that those services are being performed by an affiliate does not add risk to the group, but in fact because of greater regulatory oversight should be considered to reduce the group’s risk. We also point out that the “Financial Entity” designation is being applied only to such entities that provide services primarily to affiliates; clearly, therefore, it is not the activities of those service entities that are considered risky, since if they provide those services primarily to non-affiliates they are not considered “Financial Entities.” Again, the working group should not want the GCC to limit the scale, diversification, integration or efficiency of groups, given historical evidence of the benefit of size, diversification, and efficiency to group credit standing, as evidenced in public credit ratings.

Key Concern #3: Intangible Assets

VI.83: We question the rationale for collecting information on intangible assets (such as deferred acquisition costs, provider contracts, customer lists, and goodwill). The focus on intangible assets, to the exclusion of other types of assets, seems unwarranted. While it may not always be possible to sell intangibles quickly for cash equal to their reported value, that is true of a wide variety of tangible assets (such as real estate, plant and equipment, and airplanes) that are not being singled out. Furthermore, regardless of their availability for sale, intangible assets do produce a stream of income to the group; otherwise, GAAP accounting would require that they be written down in value or written off entirely. As businesses rely more and more on digital assets and intellectual property as the basis for their operations, and less and less on fixed assets, there is more scrutiny of the value of those assets, and there should be less concern about whether the stated values are appropriate. We believe that any focus on intangible assets—which has not previously been discussed by the working group—is unwarranted, and there is no valid reason to collect information in the GCC or otherwise differentiate this specific category of assets.

We note that securities in a “tangible” investment portfolio are valued on the net present value of expected cash flows to the investor in the private and public markets—despite the tangible nature of the issuers’ assets or capital producing these cash flows. Just over one-third of the S&P 500, which is well represented in corporate debt and equity investment asset classes, have negative tangible net worth. The differential treatment of “tangible” financial investments and physical assets versus income-producing intangible assets is inconsistent.

We note also that the increasingly digital economy is based on software and information assets. Under GAAP, the capitalization of software assets is narrow, and amortization relatively short, compared to traditional fixed assets. Furthermore, changes made to GAAP in 2001 eliminated both the “pooling of interests” accounting in acquisitions and the amortization of goodwill. Accordingly, both business trends and accounting changes have made the differentiation of “intangible” assets increasingly less relevant.

Key concern #4: Use of the GCC

I.A.2.: We suggest several revisions to this paragraph.

One key area of concern is the statement that “insurance companies may be subsidizing the operations of non-insurance entities, potentially undermining the insurance company’s financial condition.” Whether or not all or any of the insurance companies in a group are “subsidizing” other operations within the group is not relevant to the insurance company’s financial condition. Insurance regulators are already empowered to monitor and restrict the flow of capital out of the insurance entities, by means of restrictions on dividends, oversight of transactions with affiliates, and application of the statutory provisions regarding hazardous financial condition, among other methods. If the outflows from insurers to other members of the group are endangering the solvency of the insurers, that points to a regulatory failure that cannot be solved by the GCC. The GCC was never, in our understanding, intended to be a tool for each legal entity regulator to use for legal entity solvency monitoring. That is a function of U.S. risk-based capital (RBC) and state-based insurance regulation, not group-level supervision.

That same sentence in paragraph I.A.2 suggests that another consequence of “subsidization” may be “upward pressure on premiums to the detriment of insurance policyholders.” The GCC was never intended to be a tool for the regulation of insurance premium rates, and we find it highly concerning that this consideration is being introduced in this fashion.

The idea that non-insurance operations within the group pose a proximate risk to the solvency of the group’s insurers has little historical evidence to support it. The real lessons of the financial crisis of 2008 proved that even when an insurer belonged to a group with significant financial risk in other areas of operations, its policyholders were not subjected to significant risk, because the legal entity structure in the United States effectively protected them, especially relative to other group-oriented insurance regulatory regimes. It is clearly not the case that risk within a complex, diversified holding company system necessarily translates to risk to the individually regulated insurance entities or to their policyholders. Each state is responsible for reviewing the financial condition of the legal entities within its jurisdiction, and for decades, including the financial crisis of 2008, that first line of review has proved to be the most effective system worldwide. The GCC may identify “risk” in the larger holding company system, but that will not necessarily translate to better identification of risks to any insurer within that system. We suggest that the Financial Analysis Handbook is the more appropriate location for commentary about how to interpret the risks identified by the GCC.

Another concern arises from the statements in paragraph I.A.2 that the GCC “provides an additional early warning signal to regulators so they can begin working with a company to resolve any concerns in a manner that will ensure that policyholders will be protected” and will “allow them to make informed decisions on both the need for action, and the type of action to take.” It seems inappropriate to suggest that the GCC, in and of itself, would be grounds for regulatory action to protect policyholders; that is the function of a regulatory standard, not an analytical tool. The ratio produced by the GCC as well as the additional information provided in the GCC template may provide grounds for a regulator to have discussions with a group about its risks, but they would not be grounds for inferring that policyholders must be “protected” so that the regulator must “take action” by requiring the group to “resolve concerns.”

We also have a concern that the instructions as written may not make clear that the GCC is intended to be used solely by the lead state regulator. In the statement that the GCC “provides an additional early warning signal to regulators so they can begin working with a company to resolve any concerns,” the use

of the word “company,” rather than “group,” could be taken to suggest that the GCC is intended to be a tool for any regulator responsible for any legal entity within a group. Likewise, the statement, “State insurance regulators already have broad authority to take action when an insurer is financially distressed, and the GCC is designed to ... allow them to make informed decisions on both the need for action, and the type of action to take,” suggests that the GCC will be used by the domiciliary regulator of each insurer. We do not believe that is intended to be the function of the GCC.

In accordance with the foregoing comments, we propose revising paragraph I.A.2 as follows.

2. More specifically, the GCC and related reporting provides more transparency to insurance regulators regarding the insurance group and make risks more identifiable and more easily quantified. In this regard, the tool assists regulators in holistically understanding the financial condition of non-insurance entities, how capital is distributed across an entire group, and whether and to what degree insurance companies may be subsidizing the operations of non-insurance entities, ~~potentially undermining the insurance company's financial condition and/or placing upward pressure on premiums to the detriment of insurance policyholders.~~ This calculation provides an additional early warning signal to regulators so they can begin working with a company to resolve any concerns in a manner that will ensure that policyholders will be protected. The GCC is an additional reporting requirement but with important confidentiality protections built into the legal authority. State insurance regulators already have broad authority to take action when an insurer is financially distressed, ~~and~~ ~~the~~ GCC is designed to provide lead state regulators with further insights into the risks of the group as a whole, to allow them to reach make informed conclusions decisions about on the financial condition of the group both the need for action, and the type of action to take.

I.A.3. This paragraph contains a statement indicating that the GCC could be used “in conjunction with group-specific risks and stresses identified in the Own Risk and Solvency Assessment (ORSA) Summary Report as well as risks identified in Form F filings that may not be captured in legal entity RBC filings.”

While the GCC, the ORSA, and Form F are all intended to evaluate the risks of the group, we think it likely will be misleading to financial analysts to suggest that the GCC can be used together with the other two. They lack comparability to each other, for several reasons.

- The ORSA report and Form F reflect a company’s own internal risk analysis, whereas the GCC depends largely on rules prescribed by the regulators.
- The ORSA is forward-looking, and typically considers multiple future years. The GCC relies on historical data, mostly from the single most recent year.
- The “capital” that is considered for purposes of ORSA may be defined differently than the “capital” identified by the GCC.

The last sentence of the paragraph states, “Finally, it’s important to understand that regulators believed that a group capital calculation would be another valuable tool to complement the states’ legal entity focused solvency assessments.” Again, we are concerned that this statement could be construed to encourage use of the GCC by individual state regulators other than the lead state. The stated purpose of the GCC has always been to provide a tool to allow *the lead state* to better understand the risks to the group as a whole.

In light of those two concerns, we recommend that the paragraph be revised as follows.

3. State insurance regulators currently perform group analysis on all U.S. insurance groups, including assessing the risks and financial position of the insurance holding company system based on currently available information; however, they do not have the benefit of a consolidated statutory accounting system

and financial statements to assist them in these efforts. It was noted prior to development that a consistent method of calculating group capital for typical group risks would provide a very useful tool for state financial regulators to utilize in their group assessment work. It was also noted that a group capital calculation could serve as a baseline quantitative measure to be used by regulators, ~~to supplement in conjunction with the view of~~ group-specific risks and stresses ~~provided by identified in~~ the Own Risk and Solvency Assessment (ORSA) Summary Report filings ~~and as well as risks identified in Form F filings that may not be captured in legal entity RBC filings. Finally, it's important to understand that regulators believed that a group capital calculation would be another valuable tool to complement the states' legal entity focused solvency assessments.~~

II.E.20.: We are concerned about the potential for an annual redetermination of scope. If the scope of application were revised frequently, then year-over-year trends in the GCC would not be meaningful. There should be a materiality standard developed to determine when and if a group's scope is reconsidered; e.g., something based on the cumulative increase in the amount of the group's capital that is out-of-scope. To reduce burden on the group, such redetermination should be based upon material changes in the group, not changes in the reviewer.

V.A.33: This paragraph refers to "the lead state regulator and template reviewer." We question whether this is intended to suggest that the template reviewer can be someone other than the lead state regulator. If not, we suggest removing the phrase "and template reviewer" as it appears to be redundant and confusing. If there are intended to be multiple reviewers, we renew our concerns about the use of this tool by any party other than the lead state regulator.

V.A.37: Given that the GCC analytical procedures in the Financial Analysis Handbook are still undergoing development, it is not possible to speak in any but the broadest way about analytics. Probably, the description should be limited to the statement, "This tab includes or draws from entity-category-level inputs reported in the Tab or elsewhere in the GCC template to be used in GCC analytics."

Instructions Comments – Additional Concerns

We provide the following as some additional considerations for revisions to the instructions.

I.A.7. In the third sentence of this paragraph, the phrase "similar such as" appears to be an editing error. We suggest revising the sentence as follows.

The GCC instructions and template are intended to be modified, improved and maintained by the NAIC in the future, ~~similar such as~~ are existing tools such as the *Accounting Practices and Procedures Manual*, the *Annual Statement Instructions* and *Risk-Based Capital formula and Instructions*.

Also, we suggest deleting the final sentence of the paragraph. While "additional items, such as stress testing" may still be considered open, they are not relevant to the instructions for the current version of the GCC.

II.C.12: It is not clear exactly what is meant to be included in "cross support mechanisms." We would ask the work group to consider the following when working to define "cross support mechanisms":

- Is this limited to formal, legally enforceable financial guarantees among members of the group?
- Does it matter whether such guarantees can only result in payment to insurers, not from insurers?

- Can the definition of “cross support mechanisms” ever result in the ultimate controlling person being out of scope?
- If the ultimate controlling person is always in scope, would all of its subsidiaries of material size automatically be in scope, since they could have a material impact on the ultimate controlling person?

II.C. 13.: The last sentence of this paragraph says, “Consistent with sound regulation, the benefits of the quantitative analysis facilitated by the GCC should exceed the cost of implementation.” We question why this is referenced as part of the instructions. We do not believe there has been an attempt to quantify the benefit of the GCC; and, in fact, the procedures for how the GCC will be used in practice are only now being developed. Until we know how the GCC will be employed, it seems to be premature to include an assertion about its benefits here. We also suggest that any attempt at determining the “cost of implementation” needs to take into consideration other tools regulators are mandating that carriers complete, such as the ORSA and Form F, and the legal entity grid, all of which were similarly described as tools to assist in group supervision.

II.E.17.: Early in the development of the GCC, the NAIC stated that one of the fundamental principles underlying the calculation was that it would ignore group structure; an entity would be treated essentially the same, regardless of where it was positioned in the group. That principle was relaxed somewhat for subsidiaries of insurers, to try to maintain consistency with RBC as much as possible. Now it seems to have been abandoned altogether, since a non-financial entity that is not part of the “Insurance Group” may be excluded from the scope of the GCC, whereas an otherwise identical entity that is part of the “Insurance Group” must be included. In the current draft, it appears that even the ultimate controlling entity may be excluded from group scope, despite clear influence in the group on corporate governance and capital allocation. Given the definition of “Insurance Group” (paragraph IV.23), this could lead to the inclusion of a non-financial subsidiary that has no connection to the insurance operations other than being owned by the same holding company as the insurers in the group. The rationale for this disparate treatment is not at all clear. Overall, the working group should not create a GCC that leads to preferential group organizational structure.

II.E.18.: This paragraph introduces the concept of exclusion being justified by the determination that the entities excluded “do not pose material risk to its [i.e., the group’s] insurance operations.” This seems eminently reasonable. It is not clear why that same concept should not be adopted to resolve the problem noted in the comment above on paragraph II.E.17.

Section III: There is no Section III. We assume this is merely a tabulation error and not an entire section that has been omitted.

IV.23: With regard to the definition of “Insurance Group,” please see our comment above on paragraph II.E.17. As currently defined, the “Insurance Group” is not limited to the insurers within a group and their own subsidiaries. Merely being owned by the same intermediate holding company that happens to own the insurers in the group is enough to make a non-financial entity part of the insurance group. This does not seem reasonable. The “Insurance Group” should be defined to exclude any non-financial entities that are not actually owned by the insurers.

IV.28: The “Ultimate Controlling Person” is defined to be, “As used in the NAIC’s Insurance Holding Company System Regulatory Act (Model #440).” Model #440 does indeed use the term, but while it defines “control” and “person,” “ultimate controlling person” itself is never defined—that is, there is no

explanation of what “ultimate” means. This seems an important concept that should be defined more precisely, especially since the “head of the Insurance Group” may be distinct from the “Ultimate Controlling Person.”

IV.30: The definition of “Affiliate” applies an inappropriate threshold for materiality to Schedule A and Schedule BA assets, based on the capital of the insurance entity that owns the asset. The GCC is intended to be a measure of the group’s capital, and any materiality threshold should be set relative to the entire group (insofar as it is in scope), and not relative to any individual entity within the group. Note, in fact, that paragraph VI.51 states a materiality criterion for Schedule A and Schedule BA assets based on the capital of the group, not the entity that owns them.

VI.54: The instructions call for the reporting of all dividends paid within the group. This is significant—and, in the context of a balance-sheet-oriented calculation, unnecessary—additional burden. We note that in many cases, a dividend may pass through one or more holding companies before it reaches its final destination (e.g., from insurer to intermediate holding company to ultimate controlling person). Seeing the same dividend being recorded multiple times is very likely to create confusion. We suggest it would be more useful to show, for each entity, only the net of dividends paid and dividends received. In that case, the columns for Dividends Paid and Dividends Received could be collapsed into a single column. Also, it is not clear that the Yes/No response in the Dividends Received and Not Retained column is useful, as it relies on what is “expected” rather than what is certain; a better approach might be to include dividends declared but unpaid in the column for dividends.

Also with regard to paragraph VI.54, we question how meaningful it is to designate some capital contributions as being funded from debt proceeds. There may be a lag between when debt proceeds are received by the debt issuer and when capital is contributed to a downstream entity; how long may the lag be before the capital contribution is no longer considered to be “from debt proceeds”? Also, if a parent makes a capital contribution when needed, and then subsequently replenishes its own capital through debt issuance, shouldn’t that be deemed to be essentially the same as receiving the debt proceeds and then infusing them into the subsidiary? Furthermore, debt-funded capital injections may well survive the maturity of the debt. Because cash is fungible, it does not seem to be a worthwhile effort to try to determine the particular source from which a capital contribution was funded. We recommend that if holding company debt is to be included in capital, then the limitation should be the insurance entities’ total paid-in capital.

VI.56: We point out that intra-group guarantees, solvency reinsurance, and capital maintenance agreements typically do not have notional values. Moreover, triggering of these arrangements has historically been very unlikely. In an earlier communication from the NAIC on this subject, the estimated notional value was weighted by expected utilization. This weighted approach should be used here.

Comments on the Template

Although we understand the need to have a tool that quantitatively calculates group results, we suggest it is inappropriate to use the tool as a way to simply gather information about unregulated entities that do not impact the results of the GCC calculation itself, especially as most of this information is available to regulators from other filings. The following are examples of the information being collected that does not impact the results of the calculation:

- a significant amount of information related to trend analytics, which - on the legal entity basis- are not meaningful to the calculation;
- Reinsurance Assumed from Affiliates and Reinsurance Ceded to Affiliates. We question the relevance of the information to the calculation and note that this information is readily available in the annual statements;
- the notional values of both Intercompany Guarantees and Capital Maintenance Agreements, because 1) most, like insolvency reinsurance, have no stated value or have values that are based upon a calculation and not a fixed amount; and 2) in practice, these have extremely low probability of triggering guarantor action (earlier versions of this analysis weighted any notional amount by currently expected use);
- the value of intangible assets;
- descriptions related to intragroup assets; the values of some intragroup assets are also asked for on the Questions tab;
- descriptions related to reported adjustments;
- dividends paid and received;
- how downstream debt proceeds are tracked; and
- a listing of Schedule A and BA assets, which can easily be found in the NAIC financial statements.

Thank you for the opportunity to provide our input. We believe that addressing the issues we raise above will lead to the GCC being a more useful tool for regulators.

Sincerely,



James R. Braue
Director, Actuarial Services
UnitedHealth Group

cc: Kathryn Belfi, Vice-Chair, Group Capital Calculation Working Group
Dan Daveline, NAIC
Randi Reichel, UnitedHealth Group