NAIC NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

Draft date: 9/28/26

Virtual Meeting

FINANCIAL ANALYSIS SOLVENCY TOOLS (E) WORKING GROUP
Monday, October 19, 2026
1:00 – 2:00 p.m. ET / 12:00 – 1:00 p.m. CT / 11:00 a.m. – 12:00 p.m. MT / 10:00 – 11:00 a.m. PT

ROLL CALL

Danielle Smith, Chair	Missouri	Kristin Hynes	Michigan
Amy Garcia, Vice Chair	Texas	Paul Lupo	New Jersey
Richard Russell/Todrick Burks	Alabama	Victor Agbu	New York
Dave Lathrop	Arizona	Tracy Snow/Mark Boston	Ohio
Michelle Lo	California	Ryan Rowe	Oklahoma
Jack Broccoli	Connecticut	Ryan Keeling	Oregon
N. Kevin Brown	District of Columbia	Liz Ammerman	Rhode Island
Carolyn Morgan/Shalice Rivers	Florida	Samantha Watkins	South Dakota
Amanda Denton	Indiana	Greg Chew	Virginia
Gregory Ricci	Maryland	Kristin Forsberg	Wisconsin

NAIC Committee Support: Rodney Good/Ralph Villegas/John Murray

AGENDA

1. Receive Comments and Consider Adoption of Proposed Revisions to the Financial Analysis Handbook—*Danielle Smith (MO)*
   a. Comment Letters — Attachment A
   b. Handbook Exposure with Edits — Attachment B

2. Consider Adoption of Handbook Revisions Referred from Life Actuarial (A) Task Force and Casualty Actuarial and Statistical (C) Task Force—*Danielle Smith (MO)* — Attachment C

3. Consider Adoption of Handbook Revisions Referred from the Actuarial Opinion (C) Working Group—*Danielle Smith (MO)* — Attachment D

4. Consider Adoption of a Referral to Financial Regulation Standards and Accreditation (F) Committee—*Danielle Smith (MO)* — Attachment E

5. Consider Adoption of proposed revisions to Life/A&H IRIS Ratio 7 (Total Affiliated Investments to Capital and Surplus)—*Danielle Smith (MO)* — Attachment F

6. Discuss Any Other Matters Brought Before the Working Group

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—Danielle Smith (MO)

7. Adjournment

ATTACHMENT B

Financial Analysis Handbook revisions including highlighted edits as a result of comments received and staff edits.

- Holding Company Analysis and Form A Procedures – Cybersecurity
- Credit Risk – Private Credit
- Market Risk – Private Credit
- Liquidity Risk – Private Credit
- Credit Risk – Unauthorized Reinsurance
- Form D – Unauthorized Reinsurance
- Supplemental Analysis – IBT & Corporate Divisions
- Risk Assessment Worksheet
- Framework – Artificial Intelligence
- Holding Company Analysis – GCC
- Holding Company Analysis – ORSA

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NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

ATTACHMENT A

COMMENT LETTERS

- Wisconsin
- ACLI
- APCIA
- Athene

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Wisconsin Office of the
COMMISSIONER OF INSURANCE
FINANCIAL REGULATION

Tony Evers, Governor of Wisconsin
Nathan Houdek, Commissioner of Insurance

August 3, 2026

Financial Analysis Solvency Working Group
Ms. Danielle Smith, Chair; Ms. Amy Garcia, Vice Chair

Re: Wisconsin OCI Comments on the Financial Analysis Solvency Tools (E) Working Group (FASTWG) Exposed Revisions to the 2026 Financial Analysis Handbook

Dear Members of the Financial Analysis Solvency Tools (E) Working Group:

The State of Wisconsin Office of the Commissioner of Insurance (WI OCI) appreciates the opportunity to provide feedback on the proposed 2026 revisions to the Financial Analysis Handbook. We greatly appreciate the time and effort that went into the proposed revisions.

After careful review, the WI OCI would like to propose the following revisions for the consideration of the Working Group:

1. Cybersecurity Considerations – Holding Company Reviews: Additional commentary explaining how vertical integration and third-party dependencies pose a potential risk to the insurer would be helpful.

   In addition, consider adding: If significant concerns are identified, the analyst should consider requesting additional information from the insurer regarding how the insurer is mitigating the cybersecurity concerns identified. [The analyst may wish to consult with the Department's IT examination team prior to contacting the insurer.]

2. Investment Exposures – Liquidity Risk (Private Equity/Private Credit Funding Commitments): With regards to private equity/private credit funding commitments, the WI OCI recommends adding a procedure to review the Schedule BA – Part 1 – column 19 total (Commitment for Additional Investment) in relation to Policyholders' Surplus, to assess the magnitude of the impact of unfunded commitments on the insurer's liquidity.

   [Private Equity and Private Credit LP agreements typically include a funding commitment, which can require the limited partners to reserve a significant amount of liquid assets to meet funding calls (failure to meet a funding call could result in severe penalties). This could significantly impair the insurer's liquidity (as any reserved funds would not be readily available to pay the insurer's other obligations).]

Please don't hesitate to contact me at (608) 266-9896 or kristin.forsberg@wisconsin.gov should you have any questions. Thank you for your consideration.

Sincerely,

Kristin L. Forsberg, CPA, CFE
Insurance Financial Examiner Chief
Division of Financial Regulation

September 10, 2026

Ms. Danielle Smith, Chair
Financial Analysis Solvency Tools (E) Working Group
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1000
Kansas City, MO 64106-2197

Re: Exposure of Proposed Revisions to the Financial Analysis Handbook

Submitted Electronically

Dear Chair Smith:

The American Council of Life Insurers (ACLI) appreciates the opportunity to comment on the proposed revisions to the Financial Analysis Handbook (Handbook) contained in Attachments 1 through 7 of the July 30, 2026, Financial Analysis Solvency Tools (E) Working Group (FASTWG) exposure. ACLI appreciates the significant work undertaken by the NAIC to identify emerging issues and trends that may warrant additional regulatory consideration and by FASTWG to revise the Handbook. ACLI supports FASTWG's objective of strengthening analytical guidance and recommends that any new Handbook procedures be tied to clearly identified supervisory needs, calibrated to complement existing solvency oversight tools, and implemented consistently across jurisdictions. The comments contained within this letter and our suggested redlines to the exposed Handbook revisions are intended to ensure the Handbook continues to provide practical principles-based guidance that supports effective solvency oversight without creating unintended supervisory expectations or duplicative review processes that go beyond oversight supported by appropriate due diligence.

Executive Summary

ACLI offers the following summary to assist FASTWG in evaluating how the proposed Handbook revisions can best support consistent, risk-focused financial analysis while preserving appropriate supervisory judgment.

- New Handbook procedures should be tied to clearly identified supervisory needs, calibrated to complement existing solvency oversight tools, and implemented consistently across jurisdictions.
- The guidance would be more useful to analysts if it distinguished among asset types and structures—such as private credit, traditional investment-grade private placements, PLR-backed securities, Level 3 assets, and collateral loans—based on specific risk characteristics rather than broad private-market labels or registration status.

The American Council of Life Insurers (ACLI) is the leading trade association driving public policy and advocacy on behalf of the life insurance industry. 90 million American families rely on the life insurance industry for financial protection and retirement security. ACLI's member companies are dedicated to protecting consumers' financial wellbeing through life insurance, annuities, retirement plans, long-term care insurance, disability income insurance, reinsurance, and dental, vision and other supplemental benefits. ACLI's 275 member companies represent 94 percent of industry assets in the United States.

- Clear definitions, objective risk indicators, and a principles-based materiality framework would promote consistent application while allowing regulators to focus review on exposures that present meaningful solvency considerations.
- The liquidity and Level 3 asset discussions should reflect the long-duration nature of life insurance liabilities, established asset-liability management practices, and the distinction between valuation classifications and credit or investment risk.
- The reinsurance guidance should remain analytical and principles-based, recognize practical limitations on information available from unaffiliated or non-U.S. reinsurers, and avoid inconsistencies or redundancies with existing regulatory reporting, audit, examination, and NAIC workstreams.

Taken together, these refinements would help ensure the Handbook continues to provide practical analytical guidance that supports effective solvency oversight without creating unintended supervisory expectations or duplicative review processes.

ACLI asks FASTWG to consider extending the discussion of changes to the Handbook in light of other NAIC activity that could have a material impact on its scope and interpretation, such as the Financial Condition (E) Committee exposure of Model Law #285 Disclosure of Material Transactions Model Act. In addition to helping ensure that commenters understand the context in which the Handbook will be interpreted, a longer discussion period would give industry and regulators time to calibrate on the issues and the underlying concerns, ensuring that changes are effective.

General Comments

Our comments focus primarily on the proposed guidance relating to private assets, liquidity analysis, private letter ratings (PLRs), Level 3 assets, collateral loans, and asset intensive reinsurance. ACLI generally supports providing analysts with additional information and tools to understand evolving investment and reinsurance markets. At the same time, several aspects of the proposal would benefit from further refinement to ensure that analytical procedures remain risk-focused, objective, and appropriately calibrated to the insurance business model. In particular, any data-gathering or analytical framework should be accompanied by clear definitions, objective risk indicators, and appropriate materiality thresholds so that registration status or private-market classification does not become a proxy for heightened risk where the underlying investment characteristics do not warrant that conclusion. More broadly, it is important to first assess if existing tools and resources can be utilized to achieve the desired regulatory objectives of the Handbook updates and any new measures should be targeted at clearly articulated gaps and implemented consistently across states.

Several aspects of the proposal would benefit from clarification to ensure that distinct asset classes, investment structures, and reporting attributes are evaluated based on the specific risks they present. In addition, portions of the reinsurance guidance may be read as moving beyond analytical considerations toward supervisory expectations that could be difficult to apply in all circumstances, particularly with respect to unaffiliated or non-U.S. reinsurers. Certain changes may also front run ongoing NAIC analysis of these topics, which could lead to misalignment. ACLI encourages FASTWG to preserve the Handbook's longstanding role as a principles-based source of analytical guidance that assists regulators in understanding and monitoring risk, while avoiding language that could be interpreted as creating implied standards or de facto requirements.

ACLI encourages FASTWG to consider whether certain proposed procedures could result in inconsistent analytical outcomes, duplicate existing review expectations, or impose burdens that are disproportionate to the supervisory benefit. Several proposed metrics, review procedures, and reporting expectations may overlap with reviews or analysis already performed through existing regulatory, audit, and financial reporting processes, particularly for insurers with significant reinsurance programs. In many cases, these existing tools may better capture potential risks because they are tailored towards providing insights into the related activities. They should be leveraged or refined instead of creating new and potentially conflicting procedures. ACLI encourages FASTWG to evaluate whether the proposed procedures are sufficiently targeted and risk-sensitive to justify the additional reporting and review burdens they may create. We also encourage FASTWG to consider whether certain proposed ratios, particularly those using capital and surplus as the denominator, produce meaningful comparisons across insurers with differing business models and reinsurance structures. Ratios based on total invested assets or other exposure-based measures may in some cases provide a more comparable and informative analytical framework.

ACLI also encourages FASTWG to consider how the proposed procedures would interact with other ongoing NAIC initiatives addressing private asset oversight, including work related to credit rating provider due diligence, RBC modernization, and enhanced reporting requirements. We believe these initiatives should be finalized and leveraged first to avoid duplication, unintended expansion beyond the Handbook's intended analytical purpose, and unnecessary strain on both regulator and insurer resources. To that end, Handbook revisions should clearly identify the specific analytical gap they are intended to address and be calibrated to complement, rather than overlap with, existing solvency oversight tools.

ACLI further recommends that FASTWG include a clearer materiality framework for applying the proposed review considerations. Several proposed procedures appear to apply when exposures are considered "material," but the exposure does not define materiality, identify who should make that determination, or provide objective factors analysts should consider. A principles-based materiality framework should allow analysts to consider an insurer's liability profile, liquidity needs, business model, investment strategy, reinsurance structure, total invested assets, exposure concentrations, risk management practices, and overall capital adequacy. Such a framework would promote consistent application across jurisdictions while preserving appropriate supervisory judgment and avoiding unnecessary review of exposures that do not present meaningful solvency risk.

We also note that since the Handbook was exposed, the NAIC's Financial Condition (E) Committee has asked regulators and interested parties to comment on the definition of materiality for reinsurance agreements. This highlights an important benefit of defining a materiality framework within the Handbook: it would ensure that the drafter and the reader have the same understanding, regardless of events since the Handbook was published. Reviewing proposed guidance is more difficult without it because it is unclear how changes will be applied. Again, it may be inappropriate to front run analysis recommendations without further study and consideration of projects already in flight.

The remainder of this letter provides feedback on specific topics.

Private Credit

ACLI appreciates FASTWG's efforts to provide guidance on private credit and related private market investments. However, we believe the proposed discussion would benefit from a more balanced and comprehensive description of private credit and greater differentiation among various private market asset classes. The discussion would also benefit from recognizing that private fixed-income investments can provide incremental yield, portfolio diversification, structural protections, enhanced covenant protections, and asset-liability matching benefits. Such investments are generally well suited to insurers' long-duration liabilities and investment horizons, and historical experience has demonstrated that certain segments of private credit have been a longstanding and effective component of insurer investment portfolios.

The narrative generally defines private credit using examples such as direct lending and middle-market lending, while many accompanying procedures appear to apply based on broader characteristics such as private placement status, registration status, PLRs, or Level 3 valuation classifications. As drafted, the guidance could cause analysts to treat the following categories as interchangeable even though they present different risk considerations:

- Private credit strategies involving newer or more complex structures;
- Traditional investment-grade private placements that have long been a core component of insurer portfolios; and
- Assets that may warrant additional valuation review due to the nature of available pricing inputs.

These categories do not necessarily represent the same risks and should not be treated interchangeably. Traditional investment-grade private placements have been used by life insurers for decades and have historically served as an important asset class for matching long-duration liabilities. Private fixed-income investments encompass a broad range of strategies and are not limited to lending to middle-market borrowers.

ACLI encourages FASTWG to distinguish more clearly between traditional private placements and newer private-market structures and to focus analytical procedures on specific risk characteristics such as complexity, credit quality, valuation uncertainty, leverage, or concentration risk rather than on registration status alone. We also recommend adding clarifying language to avoid unintentionally capturing longstanding traditional asset classes that do not present the concerns the proposal appears intended to address.

We further recommend that FASTWG provide additional context for several narrative statements that may read as broad characterizations of private credit. For example, private credit borrowers are not uniformly small middle-market companies, and they do not necessarily have higher leverage or greater sensitivity to economic downturns or rising interest rates than companies accessing other credit markets. Many companies that borrow in private credit markets present risk characteristics that overlap with issuers accessing broadly syndicated loan, high-yield, private placement, or other fixed-income markets. ACLI recommends that the Handbook avoid categorical statements suggesting that private credit, as a whole, presents distinct or elevated risk unless those statements are tied to clearly identified data or risk indicators.

In addition, if the Handbook includes quantitative statements regarding the size or composition of the private credit market, such as the relative share attributable to direct lending, ACLI recommends that FASTWG identify the source, methodology, and categories included in the measurement. Clear taxonomy is important because different definitions of "private credit" may encompass materially different asset types and investment strategies. Analytical conclusions may vary depending on whether the term is limited to direct lending or includes other private fixed-income, structured-credit, or alternative-credit strategies. ACLI recommends removing statistics that cannot be sourced.

The definition of "private assets" is particularly important if analysts are expected to evaluate private securities related ratios or undertake additional review procedures based on those ratios. A broad or imprecise definition could combine assets with materially different risk profiles, including traditional investment-grade private placements, direct lending strategies, structured assets, PLR-backed securities, and assets classified as Level 3 for valuation purposes. ACLI recommends that any analytical metric be tied to clearly defined exposure categories and specific risk characteristics rather than a broad private-market label that may obscure important distinctions among asset classes.

In addition, several proposed analytical ratios rely on capital and surplus as the denominator. While these measures may provide useful information in some circumstances, they may produce misleading outliers in others such as instances where the denominator does not reflect capital supporting business that has been reinsured but assets supporting the business remain on the cedant's balance sheet. ACLI encourages FASTWG to evaluate whether alternative exposure-based measures (i.e. assets) would produce more comparable and decision-useful results across insurers.

Liquidity Analysis

ACLI agrees that liquidity risk is an important component of insurer financial analysis. However, the proposed liquidity guidance would benefit from greater recognition of the long-duration nature of insurance liabilities and insurers' established asset-liability management practices.

Life insurers generally maintain predictable liability profiles and actively model future cash flows to ensure that sufficient liquidity is available to meet policyholder obligations. The ability to invest in less liquid assets is a structural feature of the insurance business model and allows insurers to earn an illiquidity premium while continuing to meet policyholder obligations. Accordingly, the presence of private assets or unfunded commitments should not, by itself, be viewed as indicative of elevated liquidity risk.

ACLI encourages FASTWG to calibrate the liquidity discussion to better reflect the distinction between assets used for immediate liquidity management and long-duration assets intended to support longer-term insurance obligations. The Handbook should also recognize that commitments and unfunded commitments are generally incorporated into insurers' portfolio construction, liquidity planning, and ongoing cash-flow management processes.

Level 3 Assets

ACLI recommends clarifying that Level 3 classification should not be viewed as a proxy for increased credit risk. Level 3 classifications reflect the nature of valuation inputs used in fair value measurements and are not measures of credit quality. As noted above, insurance liabilities are often uniquely long-duration and illiquid, so there can be an appropriate role for less liquid assets and more complex assets in insurer portfolios.

Many long-duration insurance assets may be classified as Level 3 because observable market inputs are limited even though the underlying investments may exhibit stable contractual cash flows and strong credit characteristics. In addition, the use of unobservable inputs does not necessarily indicate weak valuation practices; internal valuation models can be robust, and asset classifications may change as market information becomes available.

ACLI therefore recommends clarifying that Level 3 classifications are valuation classifications rather than risk classifications and should not be interpreted as evidence of elevated investment risk in isolation.

Private Letter Ratings

ACLI supports regulatory understanding of PLR-backed securities but believes the guidance should more clearly acknowledge that growth in PLRs largely reflects expanding private-market issuance rather than deterioration in credit quality.

We also recommend that any request for SVO support to review rating sources be tied to objective criteria indicating when additional review is warranted. As currently drafted, the language could create uncertainty regarding established rating processes without identifying specific risk indicators or thresholds that justify additional scrutiny.

The guidance should also recognize that many insurers supplement external ratings with robust internal underwriting, credit analysis, and ongoing surveillance processes that form an important component of investment risk management.

ACLI also recommends that any comparison of insurer internal ratings and PLRs be limited to circumstances where objective risk indicators warrant further review. Routine or broad-based comparison of internal ratings to PLRs could create substantial operational burden, particularly for smaller insurers, without necessarily producing meaningful additional solvency insight. The Handbook should recognize that internal ratings are often developed for risk-management, surveillance, and portfolio-monitoring purposes and may not be designed to serve as direct substitutes for, or comparison points against, external or private letter ratings.

Collateral Loans

ACLI recommends refining the characterization of collateral loans in the proposed credit-risk guidance. The draft states that collateral loans are subject to the same risks as their underlying collateral and may be riskier

due to their illiquid and less transparent nature. ACLI believes this characterization would benefit from additional context regarding the economic structure and contractual protections commonly associated with collateral loans.

Collateral loans are debt instruments secured by pledged collateral and often incorporate significant structural protections, including overcollateralization, diversification, lender remedies, cross-collateralization provisions, and other credit enhancements. Accordingly, collateral loans should not be viewed as economically equivalent to direct ownership of the underlying assets. Consistent with the discussions at the Life Risk-Based Capital Working Group which resulted in look-through C-1 factors adjusted based on the level of overcollateralization, ACLI recommends revising the discussion to recognize the structural protections commonly associated with collateral loans and their role in reducing economic risk relative to direct ownership of the collateral. Additionally, ACLI recommends removing the reference to private-equity owned insurers because it could be misconstrued as directing analysts to base their risk assessment of the asset on the ownership structure of the insurer. The NAIC has previously declined to define "private equity" and noted that regulatory considerations should be focused on activities rather than owners.

Asset Intensive Reinsurance

ACLI appreciates regulators' interest in enhancing analytical guidance related to asset intensive reinsurance. We support efforts to provide analysts with tools to better understand these arrangements and facilitate greater regulatory coordination and information sharing. We also support efforts by the NAIC and state regulators to engage with foreign supervisory authorities to better understand how their frameworks work and support shared objectives of ensuring policyholders are protected and consumers can access insurance and retirement solutions needed to address the protection gaps they face.

At the same time, ACLI believes several aspects of the proposed guidance would benefit from greater clarity and refinement. For example, the proposed Handbook revisions refer to "unauthorized jurisdictions", "unauthorized reinsurers", and "offshore unauthorized reinsurance". ACLI suggests clarifying the intended scope, in particular whether the guidance is focused on jurisdictions, categories of unauthorized reinsurers, or transaction structures. Additional clarity would help ensure a common understanding and promote consistent application over time.

ACLI is also concerned that several proposed procedures may duplicate reviews already performed through existing solvency oversight mechanisms. Assets supporting Modco and funds-withheld arrangements generally remain on the ceding insurer's balance sheet and are already subject to ongoing financial analysis, statutory reporting, examination procedures, and audit requirements. While additional review may be appropriate where specific concerns exist, ACLI recommends avoiding routine duplicative reviews that increase regulatory burden without a demonstrated supervisory benefit.

Further, ACLI encourages FASTWG to distinguish between guidance intended to help regulators understand and monitor risk and guidance that could be interpreted as establishing new substantive expectations for insurers or reinsurers. Several proposed procedures contemplate obtaining extensive reporting from reinsurers, including reporting based on U.S. accounting and capital frameworks that may not exist in foreign

jurisdictions and may not be available to ceding insurers, particularly in the context of unaffiliated transactions. Many non-U.S. reinsurers do not prepare financial statements on this basis, and developing such information could involve substantial cost and operational burden. ACLI recommends that the guidance recognize practical limitations on the availability of such information and avoid creating expectations that may not be achievable in practice. Working with insurers to first leverage the statements and tools that are already available will increase transparency by supporting more responsive engagement and better focusing resources when there are clearly demonstrated supervisory needs.

In addition, ACLI recommends that the proposed Form D guidance make clear that detailed examples are illustrative considerations rather than supervisory requirements or checklists. While examples can be useful, many of the cited provisions, including specific overcollateralization levels, dividend restrictions, recapture provisions, retrocession limitations, parental guarantees, and prescribed investment-management approaches, are transaction-specific considerations that may or may not be appropriate depending on the facts and circumstances of a particular arrangement. We encourage FASTWG to frame these concepts as illustrative considerations rather than preferred transaction structures. ACLI also recommends that FASTWG consider whether certain illustrative examples may be more stringent than requirements generally applicable to U.S.-domiciled insurers and reinsurers. For example, guidance suggesting minimum RBC thresholds applicable across an entire reinsurance structure, including non-U.S. entities, raises questions regarding consistency, appropriateness, and the relationship between such expectations and existing solvency standards. Similarly, requirements for extensive long-term stochastic business planning and reporting appear more expansive than current expectations and may not be justified solely because a transaction involves a non-U.S. jurisdiction.

Finally, ACLI encourages FASTWG to place greater emphasis on insurer governance frameworks and risk-management practices. Regulators should be able to evaluate whether insurers maintain effective processes for identifying, monitoring, and mitigating reinsurance risks, including counterparty, collateral, liquidity, reserving, and operational risks. A principles-based focus on governance and risk management would allow regulators to assess diverse reinsurance structures while avoiding unnecessarily burdensome reporting requirements that may not provide meaningful incremental supervisory value. A governance-focused approach would also better align with existing solvency oversight and avoid creating extensive reporting, valuation, and review processes that may duplicate information already available through statutory filings, examinations, annual audits, AG 55 reporting, or other established supervisory tools.

Conclusion

ACLI appreciates FASTWG's commitment to improving regulatory analytical tools and supports the objective of providing analysts with additional resources to understand evolving investment and reinsurance markets. We believe the revisions discussed above would better align the Handbook with a risk-focused supervisory framework by distinguishing among different asset classes, recognizing the unique characteristics of the insurance business model, avoiding duplicative review expectations, ensuring that analytical metrics remain informative across varying insurer structures, and maintaining reinsurance guidance that is practical, objective, and appropriately tailored to regulatory needs.

More generally, ACLI encourages FASTWG to maintain the Handbook's traditional role as a source of analytical guidance rather than a vehicle for establishing de facto supervisory requirements. Guidance should remain principles-based, flexible, and focused on helping regulators identify and understand risk while preserving appropriate discretion for both regulators and insurers. The Handbook is most effective when it promotes risk-focused analysis using objective measures, clearly defined materiality considerations, and supervisory expectations calibrated to demonstrated risk, while avoiding unnecessary duplication of existing regulatory processes and NAIC workstreams. We believe this approach will produce effective supervisory outcomes and facilitate consistent application across a broad range of insurer business models, investment strategies, capital structures, and reinsurance arrangements.

We have attached a red-lined version of the exposure reflecting specific drafting suggestions and would welcome any questions regarding these comments. Further, we would appreciate the opportunity to continue fine-tuning these procedures through a second exposure period after a better understanding of the issues FASTWG is trying to address.

Sincerely,



Hans Avery
Actuary
hansavery@acli.com
(202) 624-2012



Marc Altschull
Managing Director, Investment and Capital Markets Policy
marcaltschull@acli.com
(202) 624-2089

----------Detail Removed to Conserve Space----------

ANNUAL CREDIT RISK ASSESSMENT

----------Detail Removed to Conserve Space----------

Credit Quality~~, Adequacy~~ and Appropriateness of Asset Intensive Reinsurance~~s Held for~~Placed Through Modco or FWH Agreements (Life/A&H Insurers)

Modified Coinsurance and Funds Withheld Agreements

Concerns may exist regarding the quality, adequacy and appropriateness of assets held to support asset intensive reinsurance placed through Modified Coinsurance (Modco) or Funds Withheld (FWH) ~~reinsurance~~agreements, particularly as investments become increasingly complex. Concerns may include controls and governance over investment practices, valuation and ratings of assets, and if material amounts of assets involve related party transactions.

Where collateral held is related to Modco and FWH reinsurance, the analyst should review the information in Note to the Financials #5L(1), #5L(4) and #5L(5), and Schedule S—Part 8—Reinsurance Agreements with Funds Withheld and Modified Coinsurance, in conjunction with other credit, operational and strategic risk of the insurer's reinsurance program. Additionally, review the analysis considerations related reserve reporting required by AG 53 (complex assets) and AG 55 (assets supporting reinsurance) outlined in the Reserving Risk Assessment and SOA procedures and guidance.

Where the company is engaged in material Modco and FWH arrangements, the analyst can use the detail of collateral received and held under Note 5L(4) to identify the types of assets held by investment schedule, and gain an understanding of the materiality of aggregate BACV of the collateral received to the insurer's asset portfolio. Further, the Note #5L(5) disclosure identifies if securities held as collateral under Modco or FWH agreements are also pledged under other arrangements, in which case they would not be for the benefit of the reinsurer or available to fulfill the liabilities of the reinsurance contract. The analyst can use the information in Schedule S—Part 8 to identify any concerns with the types of assets and credit quality of assets held under ceded or assumed Modco or FWH agreements.

Procedures / Data

- Identify the types of reinsurance agreements and jurisdiction of the reinsurer [Annual Financial Statement, Schedule S – Part 3] and determine if concerns may exist over the adequacy and quality of assets held by reinsurers in support of ceded reserves that may require further analysis or inquiry to the insurer.
    - Compare the BACV of the collateral received and assets held under Modco/FWH Reinsurance Agreements to the recognized obligation for Modco and FWH assets. [Annual Financial Statement, Notes to the Financials #5L(4)(m and n)].
    - Identify if investments held under FWH agreements (including Modco) are related to the Modco/FWH reinsurer [Annual Financial Statement, Notes to the Financials 5L(5)(o-v)].
    - Identify if the insurer is engaged in ceding business under Modco and FWH agreements with offshore reinsurers.
        - Gain an understanding, through review of Schedule S - Part 3, of the types of insurance business ceded, the reinsurer's jurisdiction, if affiliated or non-affiliated, and applicable collateral requirements

by type of reinsurer (i.e. authorized, unauthorized, reciprocal jurisdiction, certified). See the following sections for additional procedures for assessing risk for offshore unauthorized reinsurance.

- Review Schedule S – Part 8 to determine if concerns exist regarding the types of assets held or the credit quality of assets held under Modco/FWH agreements. Consider if the aggregate of medium or lower quality assets held represent a material amount of the related Modco/FWH liabilities.
  - Review Schedule S – Part 8 in comparison to Life RBC (asset schedules) to ensure asset subtotals match. If differences exist, inquire of the insurer, as differences may have an impact on the RBC calculation.
- Determine if assets held under Modco or FWH agreements are also pledged under other agreements [Annual Financial Statement, Notes to the Financials #5L(5)].

Additional Review Considerations

- If concerns exist regarding the types of assets held or the credit quality of assets held under Modco or FWH agreements, or concerns over reinsurance reporting, inquire of the insurer to:
  - Identify the applicable reinsurers and reinsurance agreements. Annual Financial Statement, Schedule S – Part 3, Financial Profile, Reinsurance Dashboard]
  - Has the insurer entered into new offshore unaffiliated Modco or FWH agreements for which the agreement was not required to be reviewed by the Department?
  - If offshore reinsurance, gain an understanding of the types of business ceded and the insurer's business purpose for ceding the business offshore.
  - Gain an understanding of the collateral requirements for the type of reinsurance and jurisdiction.
  - Request a copy of the applicable Modco/FWH reinsurance agreements and assess if the investment requirements are in compliance with the terms of the agreement and the state's reinsurance statutes.
  - Gain an understanding of the insurer's investment practices, who is managing the investments supporting the reserves, governance policies and use of asset managers for reinsurance assets.
  - If the management of the assets withheld or placed in trust in support of the reinsurance agreement is transferred to the reinsurer or an asset manager:
    - Assess ~~whether~~ the degree to which the ceding company has provided ~~sufficient~~ direction and oversight to the reinsurer in terms of investment guidelines and limitations.
    - Closely monitor the assets in the funds withheld or trust account to verify they are in compliance with state laws and ceding company guidelines, and ~~are not overly concentrated~~ identify concentrations in complex or risky investments.
- If a material amount of assets held under Modco or FWH agreements are also pledged under other arrangements, inquire of the insurer to gain a better understanding of their use of collateral assets within their reinsurance program and to ensure the insurer is in compliance with collateral requirements.
- Refer significant concerns identified to the examiner for further review, if warranted.

Commented [HA1]: Suggesting language to make these points more objective

Reinsurance Ceded to Reinsurers in Unauthorized Offshore Jurisdictions

Additional concerns may exist when asset intensive reinsurance is placed in unauthorized offshore jurisdictions with varying regulatory requirements and oversight. In recent years, regulators have observed a rise in the use of offshore reinsurance transactions (both affiliated and unaffiliated) to reinsurers in unauthorized jurisdictions. An underlying concern is that this activity could result in reduced policyholder protection or regulatory arbitrage, and

rising reinsurance credit risk, if reinsurance reserves or the underlying collateral supporting those ceded reserves is not sufficient, all of which should be carefully assessed and monitored. Some additional considerations are provided below including an optional "reinsurance comparison worksheet" that can be used to compare different accounting, reserving and capital standards across jurisdictions. In certain international jurisdictions regulators have had difficulties determining if offshore reinsurance arrangements are affiliated or unaffiliated as information about the ownership of the reinsurer may not always be readily available or easily obtained, therefore it is important to have good communication with cedents and relevant foreign jurisdiction regulatory authorities.

A potential concern with utilizing unaffiliated third-party offshore unauthorized reinsurance is when management of the assets withheld or placed in trust in support of the agreement is transferred to the reinsurer or an asset management affiliate, which may be the case in some asset intensive reinsurance arrangements. In these situations, the reinsurer may have incentive to reallocate the portfolio into more complex assets to achieve a higher rate of return, including assets originated by or placed within its affiliated entities.

Finally, while historically more common in property/casualty insurance, there have been recent indications that more reinsurance sidecars are being formed in the life/annuity reinsurance industry. Sidecars are limited purpose reinsurance transactions where third-party investors infuse capital in exchange for dividends, and may also provide other services, such as asset management services in exchange for fees. The purpose is to offer alternative capital to reduce volatility in earnings and capital of the ceding insurers. Since sidecars arrangements may be formed with different strategies and interests in mind (infuse capital support, specialized asset management expertise, favorable offshore capital/tax treatment, reduce volatility, etc.), it is important to understand the structure of the sidecar deal, and whether the ceding insurance company has sufficient governance and controls over services provided by the sidecar.

Procedures / Data

- Identify the type(s) of reinsurance agreements, type(s) of business ceded, and jurisdiction(s) of the unauthorized offshore reinsurer(s). Determine if amounts ceded to unauthorized offshore reinsurers are material. [Annual Financial Statement, Schedule S – Part 3; Financial Profile; Reinsurance Dashboard]

Additional Review Considerations

- For material new reinsurance transactions placed with unauthorized offshore reinsurers, regulators should gain an understanding of ~~and assess the appropriateness of~~ the business purpose for the transaction.
- Monitor the reinsurer's credit and financial strength ratings.
- Consider utilizing the Reinsurance Comparison Worksheet developed by the Macroprudential (E) Working Group to assist in understanding and evaluating cross-border reinsurance treaties where different regulatory systems are involved.
- Gain an understanding of the regulatory requirements for assets held to support the reinsurance agreement.
- ~~Verify~~ Assess the credit quality and liquidity of the funds-withheld assets supporting the agreement, including assessing risks associated with complex assets backing the reinsurance agreements. [e.g. for Life/A&H: Review of Actuarial Guideline 55 filing, if required; Annual Statement Note 5; Schedule S, Part 8 for Life/A&H]. Refer to additional Modco/FWH procedures above.
- For assets managed by third-party reinsurers or asset managers (i.e., funds withheld or held in trust), closely review the assets to identify relationships with the reinsurer and ensure compliance with ceding company guidelines and state investment laws (i.e., single issuer limitations).

Commented [HA2]: Suggesting that this "appropriateness" phrase be removed as it is unclear what standard would be used. This also seems like it is guiding supervisory judgement rather than helping an analyst identify areas of focus to support a thorough examination.

Commented [HA3]: Suggesting "assess" as a replacement for verify because it was not clear what standard to verify against.

III.B.1 Credit Risk Assessment

- Consider engaging with foreign jurisdiction regulatory authorities to understand their applicable capital, investment, and reserving requirements as well as their understanding of the ownership structure of the reinsurer and the regulatory agency's supervisory plan for the reinsurer.
- Review information provided in the insurer's Actuarial Guideline 55 filing, if required, relating to asset adequacy analysis, reserves and assets supporting asset intensive reinsurance transactions, if applicable. (See additional guidance in the Life Reserve Risk chapter, III.B.8.b.ii)
  - Coordinate with the Valuation Analysis (E) Working Group, as appropriate, to access information from their targeted review of AG-55 filings and/or request additional support.
- Consider requesting information from the cedent, the reinsurer, or the reinsurer's domiciliary regulatory authority, for the Department's ongoing risk assessment. The level of detailed information requested may be dependent on the materiality and complexity of the transaction . For example:
  - ~~Require reporting~~Reporting on the reinsurer (noting that other jurisdictions may have disclosure limitations). Examples include:
    - Financial condition of the reinsurer ~~quarterly, which includes RBC calculations for the entity under the fully compliant U.S. statutory basis and foreign jurisdiction's approach~~under its domestic regulatory accounting requirements.
    - Audited financial statements of the reinsurer.
    - ~~Mid-year u~~Unaudited statements of the reinsurer~~. The financial statements audited are~~ (if possible, prepared under US GAAP and GAAS)~~,~~ and supplemental notes that provide detail on reserves/ capital, investments, and reinsurance activities.
    - Reinsurer's ~~annual~~ standalone cash flow testing results/memorandum, actuarial valuation report.
    - Assets supporting ~~that~~ the ceded business and asset adequacy testing that the reinsurer provides to their foreign regulatory authority.
    - ~~For~~The foreign regulatory authority's examination or inspection report of the reinsurer.
  - ~~Require reporting~~Reporting on the cedent in addition to statutory filing requirements (to the extent that it is not duplicative), such as:
    - Actuarial Opinion and the supporting Memorandum annually, as well as reporting of mortality and policyholder behavior experience development vs. pricing expectations
    - Regular summary reporting of all transactions, or other material blocks of business ceded (e.g. annual in conjunction with AG55 requirements).
  - ~~Require reporting~~Reporting on the transaction, specifically, noting that in unaffiliated transactions the cedant may not be aware of all of the aspects of the reinsurer's business plan or global risk management strategy and may not be able to compel their disclosure if they are not contractually required.
    - ~~Quarterly summary reporting of all transactions, or other material blocks of business ceded.~~
    - Operating results of the entire reinsurance structure (cedent, reinsurer/retrocessaire, unauthorized offshore reinsurer), noting constraints on availability referenced above
    - Confirm if the transaction is subject to AG55 reporting
    - Consider requesting projections of all material components of the reinsurance structure if not subject to AG55, with focus on impact to the cedant
    - ~~Updated business plan~~Confirm the business purpose ~~,~~and ~~-~~investment ~~policy~~guidelines associated with the reinsurance structure~~, and quarterly projections for operations of the entire reinsurance~~

Commented [HA4]: Addition to make the approach more risk-based.

Commented [HA5]: Rewording to prevent confusion about best practices vs requirements

Commented [HA6]: Additional considerations for the analyst in order to help with cost-benefit analysis.

Commented [HA7]: Removed references to specific timing throughout this section in order to encourage more discussion about frequency and timing.

Commented [HA8]: Realigning to leverage materials that are already prepared.

Commented [HA9]: Noting potential constraint on availability.

Commented [HA10]: Rewording to prevent confusion about best practices vs requirements

Commented [HA11]: Moved this from the transaction-specific section to the cedant section since it suggests reporting for multiple treaties.

Commented [HA12]: Rewording to prevent confusion about best practices vs requirements

Commented [HA13]: Noted limitations of disclosure requirements

Commented [HA14]: Moved this from the transaction-specific section to the cedant section since it suggests reporting for multiple treaties.

Commented [HA15]: Unclear what is being asked here, financial statements of the reinsurer?

Commented [HA16]: Noted that this is an item to confirm, not an additional requirement for transactions deemed out of scope.

Commented [HA17]: For transactions not subject to AG55, a more limited starting point may be justified

~~structure, including projection of all pertinent aspects of the business ceded from the perspectives of all entities in the reinsurance structure.~~

~~Three projections, each for twenty years, as the risk flows from entity to entity.~~

~~One is a level equity and interest projection to represent a baseline expectation.~~

~~Two projections from the 1000 stochastic projections developed as part of the quarterly reserve and capital calculation. The two projections represent the 15th and 5th worst ending surplus positions and are intended to approximate moderately adverse and minimum capital level projections.~~

~~The projections provide,~~

~~Broadly, product/treaty level detail as well as the aggregated cash flows. Annual projected amounts for reserves, capital, net after tax income, capital transfers among the entities within the system, and cedent RBC, among many other variables are provided for the system.~~

~~Present value of projected capital contributions from cedent to the reinsurers for each scenario.~~

- ~~Cedent's starting statutory reserve and details the ceded and assumed amounts throughout the system, giving insight into the amount of reserve and capital relief provided by the structure.~~

Commented [HA18]: Removing very specific language that raised questions about intent and whether it was too prescriptive. Could this be replaced with the references to AG55 analysis added above?

- If the agreement was approved by the Department, assess the compliance with the terms and conditions of any MOU, contractual agreement or conditions placed on the approval of the transaction.
- Conduct periodic in-depth meetings with the cedent's senior management where agenda items may include:
  - Financial/operating results for all material entities in the reinsurance structure on a U.S. statutory basis and pro-forma RBC, where relevant and available
  - ~~Company~~ Relevant initiatives and filings
  - Investment reporting on the assets supporting the agreement including investment income results, rebalancing, and monitoring
  - New sales reporting, and other supplemental information ~~depending on~~ that is relevant to the block of business ceded
  - Compliance with pre-approval conditions
- For the next scheduled examination, recommend the examiner verify the funds-held assets associated with foreign reinsurers to ensure existence, accuracy, and admissibility; and review of the reinsurance agreements for proper risk transfer.

Commented [HA19]: Noted materiality and potential constraints on availability (e.g. for established agreements that do not include provisions for this reporting)

Commented [HA20]: Added "relevant"

Commented [HA21]: Replacing "depending on" with "that is relevant to" in order to make it clear that this will often not be relevant (example: closed block transactions)

Special Notes:

The following procedures do not supersede state regulation but are merely additional guidance analysts may consider useful only if the state has adopted the *Insurance Holding Company System Model Regulation with Reporting Forms and Instructions*, (#450).

Form D – Prior Notice of a Transaction

Form D is transaction specific and is not part of the regular annual/quarterly analysis process. The review of these transactions may vary as some states may have regulations that differ for Form D.

----------Detail Removed to Conserve Space----------

Assessment of Form D – Unauthorized/Offshore Asset Intensive Reinsurance Transactions

Best Practices for Review of the Agreement:

Reinsurance transactions with reinsurers in foreign jurisdictions that are unauthorized and not reciprocal or certified, may be based on capital and reserving standards that vary materially from U.S. standards. Therefore, it is important when reviewing these unauthorized transactions to understand the foreign jurisdiction's regulatory framework and the financial impacts of the transaction.

In addition to the procedures described above for Form D review, consider the following best practices for review, and pre-/post-approval considerations, of ceded reinsurance transactions with unauthorized reinsurers in offshore jurisdictions.

Coordination with other regulatory agencies should be prioritized where possible to ensure consistent and risk-aware guidance from all regulators. The best practices listed below are context dependent. Input from the reinsurer's domestic regulator may be helpful in determining what guardrails are most prudent.

Requests for additional reporting and analysis should balance the potential for important insights with the expected investment of time and resources. Simple conceptual issues may be missed if focus is placed on complicated analysis. To support an effective and efficient review, regulators may consider focusing initially on the most relevant information and expanding the scope of analysis where preliminary findings suggest additional review would be beneficial.

Note: While some of the following best practices may be relevant and useful for any unauthorized offshore reinsurance agreement, the following are intended primarily for life asset intensive life reinsurance agreements.

Analytical Tools and Practices

1. Assess the companies' governance and controls to monitor and mitigate risks such as reinsurer credit risk; identify information that can be obtained from companies' existing processes as well as potential blind spots.
2. Request information to complete the review, such as:
    a. ~~A business plan~~The business purpose of the transaction, and projections including ~~a~~ three-year proforma financial statements and ~~RBC~~ capital ratios for the insurer and the reinsurer.
        i. For the reinsurer, recommend amounts be reported ~~not only~~ in the framework that will be reported to the reinsurer's foreign regulatory authority ~~but also request at a minimum~~. Also consider a best-efforts balance sheet and income statement for the reinsurer using U.S. GAAP presentation and U.S. Statutory presentation and an explanation of differences.
    b. All ~~licensing~~relevant transaction documents (e.g. master transaction agreement, reinsurance agreement, supplemental trust agreement, related investment management agreement, etc.)

Commented [HA1]: Adding language to identify downsides of some best practices below while also emphasizing that these are only suggestions, not requirements. Could this be a place to call out how limitations on the reinsurer's ability to pay dividends or retrocede risk also have the potential downside of limiting the reinsurer's ability to manage capital? Is there another better place to do that?

Commented [HA2]: Suggesting that reviewers leverage prior work where possible since this has time and resource advantages for both companies and regulators

Commented [HA3]: Changing RBC ratio to more general "capital ratio" throughout the document since analysts could pick different target ratios or have multiple ratios they track.

Commented [HA4]: Updates to reflect that these are ideas for analysts to consider, not requirements and that there is value in understanding how differences between frameworks apply to the business being reviewed.

Commented [HA5]: Suggesting alternate phrasing because the examples don't appear to be related to licensing.

c. Accounting narratives that fully explain the accounting of the transaction.
d. Company's risk transfer analysis

3. Utilize the Macroeconomic Working Group Reinsurance Worksheet, where appropriate. Note that Worksheet's may need to be modified and customized accordingly, for example, to work with funds withheld agreements, or where the U.S. state insurance regulator is imposing specific requirements~~.~~, in particular requirements based on US RBC ~~such as those based on fully compliant U.S. RBC~~.
4. Transactions should undergo review by both the analyst and supervisor and based on complexity, may also undergo an additional supervisory review.
5. Communication and Coordination with the entities during the review process, for example:
   a. ~~Require in-person~~ meetings with the Company for transaction walkthroughs and initial discussions
   b. Weekly standing meetings with both the Company and the actuarial or other specialists assisting on the review.
6. Communicate with the unauthorized reinsurer's regulatory authority to discuss the transaction, gain an understanding of the foreign jurisdiction regulator's oversight and any concerns with the reinsurer.
7. Retain an actuarial specialist and/or an investment specialist to assist in the review of the transaction.
8. Perform an independent review conducted by a senior analyst in conjunction with a separate review performed by the specialists.

Analysis Procedures, in addition to general Form D procedures outlined above:

9. Perform a detailed review of all legal agreements.
   a. Assess if the transaction ~~contains all required arms-length terms and provisions.~~meets the requirements of the state's Holding Company Systems statute.
   b. Does the transaction contain ~~all contractual protections as in 3rd party transactions in order to support the arms-length standard under the~~ appropriate contractual protections against counterparty credit risk including, for example, collateral and recapture terms~~state's Insurance Holding Company Systems statute, including terms around overcollateralization, recapture and dividend restrictions~~?
10. Review the investment guidelines.
    a. Do they define the asset classes eligible for the FWA/ the credit quality, duration, and concentration limits, with sub-limits by instrument and class?
    b. Confirm that the management of the assets supporting the transaction are aligned with the cedent's investment policies and guidelines. Where not, identify reasons for the difference and assess the materiality and potential impact.~~Confirmed that the assets supporting the transaction would be managed using the same investment policies and guidelines required for the cedent.~~
    c. Review the investment and custody rules. Does the investment management agreement subject the manager to the policies established without authority to withdraw or transfer the assets? For funds withheld and modified coinsurance agreements, ~~Do~~ do the custody and title remain exclusively with the cedent?
11. Confirm the analyst's understanding of the accounting framework being used by performing ~~Perform~~ a detailed actuarial review of material items:
    a. ~~Any alternative reserve~~The reserve methodology and any changes in the plan of operations of the reinsurer relevant to the transaction
    b. Pre-reinsurance vs post-reinsurance balance sheets, ceding commissions
    c. A comparison of the reserve and capital requirements for onshore vs offshore
    d. Recapture provisions
    e. Investment guidelines
    ~~Reinsurance collectability concerns~~
    f. Company's standalone cash flow testing

Commented [HA6]: Removed example that could be interpreted as being prescriptive.

Commented [HA7]: Wording as an option rather than a requirement.

Commented [HA8]: Rephrasing to clarify that this section is all related to the Holding Company Systems statute.

Commented [HA9]: Creating a separate item for contractual protections so that they are more clearly defined.

Commented [HA10]: Rephrasing to suggest clear paths for handling of materially similar investment strategies and differentiated strategies

Commented [HA11]: Clarifying where this would be expected.

Commented [HA12]: Establishing context to support more focused requests.

Commented [HA13]: Suggesting focus on changes in order to keep focus on current issues

Commented [HA14]: Striking because these aren't an item that can be requested like the others. They seem like a judgement for the supervisor to make after the analyst has collected data.

12. Perform a detailed review of the Company's risk transfer analysis to identify any terms that highlight concern or that could limit risk transfer. Determine if the agreement transfers risk.
13. Perform a limited-scope examination, if determined necessary, over standalone asset adequacy testing ~~for high-risk transactions~~
14. Assess the effectiveness of the cedent's counterparty risk mitigation, noting that different reinsurance structures may require different solutions (for example, if assets are in a trust or not), such as:
    a. Gain an understanding of the basis for managing the solvency of the reinsurer
    b. Examples of terms of the agreement that may mitigate financial risk of failure are:
        i. ~~100% Quota Share Coinsurance w/~~ Funds Withheld Coinsurance or Modified Coinsurance in place of ordinary coinsurance
        ii. Assets with Book Value equal to ~~100~~X% of U.S. Statutory Reserves retained on cedent's balance sheet.
        iii. Supplemental Trust with additional assets ~~equal to 4.5% of U.S. Statutory Reserves are required to be held in a supplemental trust~~ as overcollateralization with a US bank as Trustee.
        iv. Granular negotiated investment guidelines ~~subject to state insurance department approval~~ – i.e., failure to retain ~~RBC~~ capital ratio triggers more conservative investment guidelines.
        v. Market-to-Book Restrictions: Limitations or conditions on collateral assets when the market value of such assets is less than X% of the book value of those assets ~~Limit: the Market Value of assets may not be less than 85% of book value of the assets~~.
        vi. Excess collateral may not be withdrawn by reinsurer if ~~RBC~~capital ratio is less than ~~250~~X% ~~CAL (500% ACL), calculated on a fully compliant U.S. statutory basis~~, or if the Market Value of collateral assets is less than ~~90~~X% of book value.
        vii. Recapture permitted if the reinsurer's ~~Reinsurer cannot pay dividends if RBC~~ capital ratio is less than X% after a divided payment ~~250% CAL (500% ACL), calculated on a fully compliant U.S. statutory basis~~.
        viii. Parental Guarantee
        ix. Cedent can elect to recapture if the reinsurer's ~~RBC~~capital ratio falls below ~~200% CAL (400% ACL)~~ a threshold or if the reinsurer fails to pay any material amount due, including topping up the collateral accounts. ~~If collateral fell to a specified percentage, such as 105%, and the reinsurer fails to top off, the cedent can recapture with full access to all 105% of statutory reserves in collateral.~~
        x. Two-layers of collateral: The funds withheld ~~trust~~ account must be equivalent to ~~100~~X% of the required statutory ceded reserves, calculated monthly and the trust adds an additional ~~5~~X% over the required reserves.
15. Assess the ~~monthly settlement~~settlement mechanics. Is the settlement a cash settlement? Does it include a reconciliation of required reserves vs. the funds withheld asset balance with ~~monthly~~ scheduled top-off ~~by cedent~~, and top off of the Trust Account to a specified level?
16. Assess the termination and recapture triggers. Does the agreement provide~~s~~ for the cedent's right of recapture upon a reinsurer's insolvency event, ~~RBC~~capital Level, and provides for a notification trigger upon the ~~ACL RBC~~capital ratio falling below a specified level ~~, e.g. 300%~~.

Best Practices for Pre-Approval of the Transaction

Consider entering into a Memorandum of Understanding (MOU) or similar contractual agreement, or require conditions as part of the final approval of the transaction MOU~~-~~s. The terms of the MOU between the cedent and the insurance department or conditions for approval could include reporting, notification and capital requirements. For example:

Commented [HA15]: Suggest striking to eliminate unnecessary subjectivity and encourage decisions based on the characteristics of the transaction rather than a label.

Commented [HA16]: Noting for clarity that some of the points below will not apply in every situation.

Commented [HA17]: Striking since this seems duplicative as the investment guidelines are part of the Form D approval by the Department.

Commented [HA18]: Removed specific numbers but left generic examples that could be tailored to different transactions.

Commented [HA19]: Removing "by cedant" since presumably the reinsurer is funding the top-off.

Commented [HA20]: Suggesting "scheduled" rather than "monthly" because settlements are often quarterly.

Commented [HA21]: Removing specific thresholds that don't have context.

V.C. Domestic and/or Non-Lead State Analysis – Form D Procedures

1. For Modco and Funds Withheld agreements, ~~T~~the cedent retains at all times the legal title and custody of the assets ~~of the Funds Withheld Account~~. For collateral held in trust, the assets are held in the name of the trustee. ~~(or Trust account)~~
   - ~~Funds withheld assets are held in a Trust where cedent is grantor and reinsurer is beneficiary. All assets are held on cedent's balance sheet in a segregated custody account in US banks.~~
   - ~~Investments held in the Funds Withheld Account account shall be in the name of the cedent.~~
   - ~~Custody is operated through a qualified custodian.~~
2. Funds Withheld Account or Trust account is established at, for example, ~~5~~X% over the required statutory resources, where the Trust is voluntary contractual collateral, i.e. security, not for reinsurance credit.
3. ~~Require~~Consider basing the terms of the agreement ~~to be based~~ on fully compliant U.S. Statutory Reserves and RBC, irrespective of how the foreign regulatory authority monitors solvency.
4. ~~Require~~Consider restrictions on dividend and capital distributions without first obtaining Department approval.
   a. For example, ~~the~~ recapture is permitted if the reinsurer ~~cannot~~ pays dividends within its first year. Subsequently ~~it cannot~~ recapture is permitted if the reinsurers pays dividends that ~~will~~ cause ~~its RBC ratio~~ capital ratios to fall below a specified target~~, for example, 350% CAL RBC~~.
   b. For example, the cedant cannot pay dividends should ~~its CAL RBC ratio~~ target capital ratios fall below a sliding scale, for example, that starts at ~~400~~X% and ends at ~~350~~Y% over ~~8~~some number of years. Any ordinary or extraordinary dividends require Department approval for the first three years after the transaction closes.
5. Action item for the Analyst: flag for future Department awareness required notifications ~~Require notification~~ to the Department, such as for future or contemplated affiliated and non-affiliated reinsurance transactions, qualified financial contracts
6. ~~Require~~Consider parental guarantees or keep-well agreements assuring the parent will provide capital support to maintain a ~~certain RBC level~~ target capital ratios or to ensure claims payments.
7. Require AG-55 Reporting, or some subset thereof.
8. To the extent not already required by AG55, consider ~~To monitor mortality and policyholder behavior experience, actual vs. expected, r~~requiring~~e on an annual basis,~~ the cedent to perform annual Asset Adequacy Testing for the ceded policies, under the same requirements and moderately adverse scenarios and using the same assumptions it uses for Asset Adequacy Testing generally, but on a stand-alone basis for the business subject to reinsurance. The results of the stand-alone Asset Adequacy Testing, including a summary of the analysis, assumptions, and results, would be submitted to the department as a separate opinion of the Appointed Actuary, ~~To the extent that the funds withheld assets, exclusive of any Letters of Credit, are insufficient to satisfy all cash flows under such analysis, additional reserves will be established at the cedent accordingly. C~~concurrently with the filing of the annual Actuarial Opinion~~, the cedent will submit to the department a separate opinion of the Appointed Actuary, summarizing the analysis, assumptions, and results of the stand alone Asset Adequacy Testing~~. To the extent that the funds withheld assets, exclusive of any Letters of Credit, are insufficient to satisfy all cash flows under such analysis, the cedent could be required to establish additional reserves accordingly ~~will be established at the cedent accordingly~~.
   a. On an annual basis the cedent ~~will~~would report on mortality experience, including expected to actual, along with any changes in mortality assumptions used in establishing reserves.
   b. The Cedent ~~will~~ would make submissions to the Department for prior approval for additional cessions on an ongoing basis (other than newly issued policies as provided in the terms of the treaty).
   c. The Cedent ~~will~~would report a quarterly summary of transactions to date on a level of detail as requested by the Department.
   d. Targeted restrictions (for example, taking into consideration the location of the assets) on retrocessions without the prior approval of the department could be established to ensure that assets remain available to meet policyholder obligations, or for other purposes as specified by the

Commented [HA22]: Adding more detail to clarify different circumstances for Modco, FWH, and trusts.

Commented [HA23]: Striking detail because these may be mixing structures (FWH, custodial agreements, trusts…). Could they be addressed separately?

Commented [HA26]: Reframing as items for the analyst

Commented [HA27]: Moving this for clarity when read in context with other items, also acknowledging the possibility that full AG55 reporting is not necessary.

Commented [HA28]: Clarifying that this may already be addressed by AG55.

Commented [HA29]: Clarify that ongoing new business should not need prior review

Department. ~~The reinsurer is restricted from retroceding any of its assumed business without the prior approval of the Department.~~ Any violation of this restriction ~~will~~could result in the automatic retraction of the Department's approval.

e. Failure to comply with these conditions ~~will~~could result in retraction of the Department's approval.

9. Where there are material differences in regulatory standards and reasonable approximations can't be developed, consider ~~Require~~ ongoing reporting whereby the foreign reinsurer provides best-effort annual financial statements and ~~CAL RBC ratio~~ capital ratios with reserves and capital including asset adequacy testing and RBC, in accordance with U.S. Statutory accounting, and U.S. RBC standards.

~~Require AG-55 Reporting.~~

10. Quarterly reporting requirements for all entities in the reinsurance structure.
    a. "Reinsurance structure" in this best practice refers to the cedent, any reinsurer/retrocessionaire(s) in the middle, and the offshore unauthorized reinsurer, for a specific block of business.
    b. Capital ratio reporting for all entities in the reinsurance system, for example, X% capital ratio. This requirement is a minimum threshold set by the Department to act as a regulatory backstop to apply a consistent lens across the various regulatory regimes.
    c. This quarterly reporting is intended to allow the Department to proactively identify capital adequacy trends or declines in ~~RBC~~capital ratios, and take appropriate regulatory action, well before reaching the ~~300~~X% minimum. Consider requiring similar thresholds for recapture triggers or other risk-mitigating solutions in the reinsurance contract.

    ~~Minimum RBC requirement for all entities in the reinsurance system, for example, CAL RBC 300%. The RBC requirement is a minimum threshold set by the Department to act as a regulatory backstop to apply a consistent RBC lens across the various regulatory regimes.~~

11. In addition to quarterly financial statements and ~~RBC~~capital ratios of the reinsurer, request the cedent provide quarterly and annual information detailing various aspects of the treaties, including:
    a. Asset-liability management data
    b. Investment guidelines compliance report
    c. Reinsurer's actuarial report
    d. Reinsurer's audited financial statements
    e. Peer review report on the work of the appointed actuary
    f. Summary of settlement activity
    g. Internal capital calculations

Post-Transaction Ongoing Monitoring – Analysis or Examination

After closing the transaction and during future ongoing monitoring, the analysis should focus on assessing the financial solvency of the reinsurer as well as the cedent, compliance with any terms or conditions of the approval and assessing the ongoing reserve adequacy, credit quality of supporting assets, counterparty risk, and risk mitigating strategies. See guidance and procedures in the Credit Risk and Life Reserve Risk chapters III.B.1 and III.B.8.ii. for Credit Quality, Adequacy and Appropriateness of Assets Held for Modco or FWH Agreements and Actuarial Guideline-55 review.

Commented [HA30]: Reframing to make it more risk-focused and enable prudent risk management (for example, stop loss or YRT treaties to manage mortality risk)

Commented [HA31]: Edit to make this less prescriptive

Commented [HA32]: Edit to make this less prescriptive

Commented [HA33]: Suggest scoping this to situations where other solutions wouldn't be faster, easier, or more effective.

Commented [HA34]: It isn't clear if there could be any reinsurers/retrocessionaires in the middle. It seems like the agreement being reviewed would have to be between affiliates because this guidance is for a Form D filing. Would it be possible to provide an example? If not, would propose deleting this entire "quarterly reporting for all entities in the reinsurance structure" item and incorporating any points about group capital elsewhere.

Commented [HA35]: Adding language to address the question of what happens if triggers are hit.

Commented [HA36]: Reordering these points and replacing 300% with X% to make it clear that the RBC percentage is only an example.

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

ANNUAL CREDIT RISK ASSESSMENT

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

Exposure to Private Credit Securities, Level 3 Securities, and Bonds with Private Letter Ratings

In recent years, the insurance industry has seen an ongoing increase in the amount and diversity of private fixed income investments held by U.S. domestic insurers. Private fixed income encompasses a broad range of asset types, including traditional investment-grade private placements, private structured assets, direct lending, and other credit-oriented investments. Many of these investments have been longstanding components of insurer portfolios and are generally well suited to insurers' long-duration liabilities and investment horizons.

The ability to invest in less liquid assets is a structural feature of the insurance business model and allows insurers to earn an illiquidity premium while continuing to meet policyholder obligations. While certain newer and more complex private credit structures may warrant enhanced regulatory attention, analysts should distinguish between traditional private placements and emerging private credit strategies when assessing credit risk exposures.

Potential areas of focus may include investments that involve heightened complexity, limited transparency, reliance on unobservable valuation inputs, private letter ratings, or nontraditional structures.
~~In recent years, the insurance industry has seen an ongoing increase in the amount of private assets held by U.S. domestic insurers, including securities with NAIC designations supported by private letter ratings and securities that are valued based on Level 3 (unobservable) inputs.~~

While this increase is generally consistent with the broader capital markets trend of increased issuance of private assets, their relative opacity versus other asset types ~~the potential lack of transparency related to private assets~~ can complicate the assessment of credit quality and reduce the liquidity of the portfolio.

Private credit generally refers to privately negotiated debt or debt-like investments that are not broadly syndicated or publicly traded. The asset class encompasses a wide range of investment strategies and structures, including traditional private placements, direct lending, private structured assets, asset-based finance, infrastructure debt, commercial real estate debt, and other privately originated credit investments. Asset-based finance encompasses a broad range of transactions secured by identifiable collateral and may exhibit substantially different risk characteristics depending on asset quality, structure, leverage, and credit enhancement features. Analysts should evaluate asset-based finance exposures based on underlying risk characteristics rather than treating all such investments as a single risk category.

Commented [MA2]: Current references to ABF could unintentionally capture large portions of high-quality insurer portfolios.

While some private credit strategies focus on middle-market corporate lending, the asset class is considerably broader and includes many investment-grade exposures that have long been utilized by insurance companies. Accordingly, analysts should avoid treating all private credit investments as having similar risk characteristics and

III.B.1 Credit Risk Assessment

should consider the underlying credit quality, structure, transparency, and valuation methodology of the investment.

~~Private credit generally refers to debt, or debt-like, securities that are not publicly issued or traded. Private credit is an evolving, alternative funding source. Non-bank lenders, including insurance companies, private debt funds, and business development companies, issue private loans directly to mostly small and middle-market companies that do not have—or have limited—access to the public corporate bond and loan markets. These small middle-market companies often have more debt than larger companies that access capital via leveraged loans and public bonds and, therefore, are more susceptible to economic downturns and the impact of rising interest rates.~~

~~Private credit has~~ "Private credit" describes a variety of strategies that include direct lending, distressed debt, venture debt, mezzanine finance, and special situations.

The largest investors in private credit are typically pension funds, insurance companies, and sovereign wealth funds. While direct lending to corporate issuers is the simplest and most common strategy, ~~type of private credit, it is evolving into~~ more complex investments like feeder fund structures, private credit CLOs, and asset-based financing (where loans are secured by collateral such as inventory, receivables, equipment, or property) are expanding.

Risks and mitigating factors include:

- Enhanced covenant protections and documentation relative to broadly syndicated lending markets.
- Greater ability for lenders to negotiate transaction-specific terms and monitor borrower performance.
- Diversification benefits through access to issuers and asset types not available in public markets.
- Structural protections, including collateralization, overcollateralization, cash flow controls, and other credit enhancements depending on the investment structure.
- Historical performance in certain private credit segments that has demonstrated recovery characteristics comparable to or stronger than similar public market exposures.
- Less liquidity: Private credit is generally issued directly by a non-bank lender or a small group of lenders, resulting in a relatively illiquid market where secondary trading is limited.
- Less transparency: The availability of information about a private credit security is often contractually restricted, which contributes to lower transparency compared to public securities.
- Less frequent pricing: Private credit may be subject to less frequent valuation and pricing; and it may rely on third-party valuations and/or modeling~~, which may be subjective~~.
- Assessment of credit quality:
  - While lack of transparency can make credit quality more difficult to assess, private credit lenders can often benefit from stronger control over documentation than lending through a syndicate of banks and are able to customize terms of the transaction given their direct relationship with borrowers. In the event of stress, lenders and investors should be able to work directly with the borrower to modify the transaction terms or add investor safeguards.
  - Private credit also has the potential to provide a broader pool of debt issuers that results in portfolio diversification.
- Future performance:
  - Private credit generally offers higher spreads and yields than public corporate bonds and loans to compensate investors for the relative market illiquidity (lack of a secondary market) and complexity depending on the transaction type.

Commented [MA3]: "alternative" to what? Suggests abnormality when it is not abnormal

Commented [MA4]: Current language largely equates private credit with direct lending to leveraged middle-market borrowers.

Commented [MA5]: Based on what data?

Commented [HA6]: Recommend striking unless there is a source that can be cited.

Commented [MA7]: Balance the discussion, which currently focuses almost exclusively on risks.

Commented [MA8]: Subjectivity exists in all pricing and valuation.

III.B.1 Credit Risk Assessment

~~As the nature of private credit evolves and expands, there is no assurance that current/historical performance trends (largely favorable) will continue. The solid historical performance of private lending may not be comparable performance as the market grows and as new entrants change focus to non-traditional alternative assets and more challenging and stressed credit environments occur, particularly higher interest rates.~~

Commented [HA9]: Suggesting removal since this is not unique to private credit.

Refer also to guidance published by the NAIC Capital Markets Bureau on private credit and its characteristics.

Note that the Annual Statement includes new disclosures and reporting requirements to improve the identification of different types of private placements. For year-end 2026, insurers will be required to disclose the SEC registration status for each investment: public, Rule 144A, private placements (defined to include Regulation D, Section 4(a)(2) exempt or other exclusion from SEC registration), or not applicable because the investment is not within the scope of the Securities Act of 1933. An aggregate disclosure in Note 5.T—Private Securities to capture key data by each grouping of investments by registration status to allow for ease of regulator review. The reporting will be provided in an electronic column in all investment reporting schedules (held, acquired, disposed) for short-term investments, cash equivalents, issuer credit obligations, asset-backed securities, common stock, preferred stock and other long-term investments.

Fair Value Measurement Hierarchy

An important element in evaluating risks associated with valuation of private investments (equity or credit) is the level of input available to determine fair value. To increase consistency and comparability in fair value measurements and related disclosures, the fair value hierarchy (see SSAP No. 100) prioritizes the inputs to valuation techniques used to measure fair value into three broad levels. The fair value hierarchy gives the highest priority to quoted prices (unadjusted) in active markets for identical assets (Level 1) and the lowest priority to unobservable inputs (Level 3).

- **Level 1** inputs are quoted prices (unadjusted) in active markets for identical assets that the reporting entity has the ability to access at the measurement date.

- **Level 2** inputs are inputs other than quoted prices included within Level 1 that are observable for the asset, either directly or indirectly. Level 2 inputs might include quoted prices for similar assets in active markets, quoted prices for identical or similar assets in inactive markets, or prices derived from inputs that are observable (e.g., interest rates and yield curves).

- **Level 3** inputs are unobservable inputs for the asset. Unobservable inputs are used to measure fair value to the extent that relevant observable inputs are not available. These inputs often involve significant judgment and estimation, including the use of internal models and assumptions.

Information associated with fair value measurement is provided in Note 20 (Fair Value Measurements) of the Annual Statement and can assist regulators in assessing the risks associated with an insurer's private investment holdings. In addition, information on fair value hierarchy reported in the investment schedules can be utilized to identify individual securities warranting additional review.

III.B.1 Credit Risk Assessment

Private Letter Ratings (PLRs)

Privately rated securities reported by U.S. insurance companies have become more prevalent in recent years. The greater use of PLRs is generally consistent with the overall increase in private credit investments by insurers, particularly life companies. PLRs provide proprietary details of investments and are only communicated to the issuer and a specified group of investors. Therefore, these investments do not benefit from the market validation that comes from market transparency (multiple investors, publicly viewable ratings, etc.) and often come as a single rating rather than multiple ratings. The NAIC has required insurance companies to submit PLRs for verification since 2018, whereby the NAIC's SVO reviews that the letter submitted is for the appropriate security and the current year. In addition, effective in 2022, insurers are required to file full rating rationale reports for PLR requests with the SVO, to partially mitigate concerns regarding the lack of transparency of PLRs.

Risk assessment procedures should be applied in a manner that distinguishes among:

1. Traditional private placements and other established private fixed income investments;
2. Emerging or nontraditional private credit strategies, including certain direct lending, feeder fund, private CLO, and asset-based finance structures; and
3. Investments characterized by elevated valuation uncertainty or limited transparency, including securities primarily reliant on private letter ratings or significant Level 3 valuation inputs.

The presence of a private placement designation alone should not be viewed as indicative of elevated risk. Analysts should prioritize review of investments exhibiting multiple risk characteristics, including lower credit quality, limited transparency, valuation complexity, concentrated exposures, or nontraditional structures.

Commented [MA10]: The guidelines should be more specific rather than conflating three different things: (1) private credit defined by new/complex/middle market), (2) private placements (largely IG traditional private placements), and (3) hard-to-value/opaque securities (Level 3, PLR-only). The narrative defines #1 but the procedures act on #2 and #3, which would capture many high-quality assets—not the intended goal of identifying risky concentrations.

Procedures / Data

Review Private Security Code details, Note 5.T disclosures, and available analytical tools to identify concentrations in:

- Nontraditional private credit structures;
- Securities backed by private letter ratings;
- Investments with significant Level 3 valuation inputs;
- Below-investment-grade or unrated private credit exposures; and
- Asset classes exhibiting elevated complexity, opacity, or valuation uncertainty.

When evaluating private placements, analysts should consider credit quality, diversification, and performance characteristics and avoid relying solely on registration status as an indicator of risk.

~~Review the Private Security Code details in the investment schedules, and aggregate private securities information in Note 5.T.; or utilize iSite+ tools, to identify a concentration in private securities.~~

~~Ratio of Private securities in aggregate and by security code category to capital and surplus plus AVR (Life/A&H) and to capital and surplus (Health).~~

Commented [MA11]: Current procedures focus heavily on registration status, PLRs, and Level 3 classifications.

- Review the SVO Administrative Symbols provided for the insurer's bond portfolio on Column 6 of Schedule D, or utilize iSite+ tools, to identify a concentration in securities backed by PLRs (i.e., symbols PL and PLGI).
  - Ratio of securities backed by PLRs to ~~capital and surplus~~total invested assets ~~plus AVR~~ (Life/A&H) and to capital and surplus (Health)
  - Change in securities backed by PLRs from the prior year
- Review information provided in Note 20C of the Annual Statement (Fair Value Measurement) or utilize iSite+ tools, to identify the extent investments (by type of financial instrument) have a fair value determined with unobservable inputs (i.e., Level 3 inputs).
  - Ratio of Level 3 securities to ~~capital and surplus plus AVR~~total invested assets (Life/A&H) and to capital and surplus (Health)
  - Change in Level 3 securities from the prior year

Additional Review Considerations

- For insurers with a concentration in bonds with Private Letter Ratings PLRs:
  - Request the support of the NAIC's Securities Valuation Office (SVO) to investigate the rating sources for the securities (with a focus on concentrations with any one rating agency and/or securities with only one rating) and consider the potential impact on the insurer's RBC charges and investment risk exposures.
  - Request details from the company on its own internal ratings for securities backed by PLRs where applicable and compare with rating agency rating for discrepancies.
- If private placements, private credit investments, Level 3 or 2D securities, or assets with PLRs are material, consider inquiring of the insurer its infrastructure and investment management policies and procedures (i.e. portfolio management and credit analyst expertise, including approach to making investment decisions) in place either internally, or via an affiliate, and/or outsourced investment manager, to manage these investments.
- ~~If necessary, consider utilizing an investment specialist to assist in asset valuation considerations.~~
- ~~If appropriate, consult with or request an Opinion from the NAIC's SVO or Structured Securities Group (SSG) on a specific investment holding or transaction. [A state insurance regulator can ask for SVO or SSG analytical assistance with respect to any investment related activity or in connection with an assessment of investment related aspects of a Regulatory Transaction (defined in the P&P Manual). The department can direct an insurance company to file relevant information with the SVO or SSG for the purpose of that analysis and the SVO or SSG will issue a report back to the department.]~~

~~Request a Preliminary Analysis from the NAIC's Capital Markets Bureau (CMB) to assess the insurer's overall portfolio investment risk exposures and suggest additional follow-up procedures that can be performed by the department to address overall portfolio issues identified. Request analytical assistance from the CMB to better understand and measure the investment risks related to a particular asset class, investment related activity, or market trend.~~

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

Inadequate Collateral for Mortgage Loan Risk

An important consideration in the analysis of mortgage loans is the adjusted loan-to-value and debt service coverage ratio for each property owned, which are used in the determination of the mortgage's Commercial

Commented [MA12]: Capital and surplus as the denominator results in significant outliers for companies that have a material reliance on reinsurance, as this ratio will not reflect any capital held by the reinsurer. Using total invested assets would result in a more comparable and informative statistic.

Commented [MA13]: Capital and surplus as the denominator results in significant outliers for companies that have a material reliance on reinsurance, as this ratio will not reflect any capital held by the reinsurer. Using total invested assets would result in a more comparable and informative statistic.

Commented [MA14]: Could significantly increase the time, effort, and cost, particularly for smaller companies

Mortgage Risk Category and are detailed in the RBC worksheet. Out-of-date appraisals may result in inaccurate valuation, resulting in an undervalued underlying collateral asset.

Procedures / Data

- Review information available in the RBC filing (LR004) and Schedule B detail to identify a concentration in loans with unfavorable debt service coverage (DSC) ratios and adjusted loan-to-values (LTV) (i.e., book value/recorded investment of each loan compared to the value of the land and buildings mortgaged) of the individual mortgage loans to determine whether the mortgage loans, or in office property types are adequately collateralized.

Additional Review Considerations

- For mortgage loans with interest overdue or in process of foreclosure, review the date of the last appraisal or valuation (Schedule B – Part 1) to determine whether updated appraisals should be obtained.
- If significant or concerning concentrations in mortgage loans with unfavorable DSC or LTV ratios or in office property types are identified, request additional information from the insurer to further assess their credit risk in this area and evaluate any risk mitigation strategies in place.

Traditional investment-grade private placements and mortgage-related investments that are addressed elsewhere in the Handbook generally should not be considered elevated-risk private credit exposures solely because they are privately originated, privately negotiated, or less liquid than comparable public securities. Additional scrutiny should focus on investments exhibiting heightened complexity, valuation uncertainty, lower credit quality, or nontraditional structures.

Commented [MA15]: ACLI is concerned that the current framework over-captures long-standing insurer assets while understating the distinction between traditional private placements and newer private credit strategies. It also better aligns the narrative with the actual regulatory objective of identifying concentrated exposures to complex, opaque, or difficult-to-value assets rather than all private assets.

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

Credit Quality of Assets Supporting Collateral Loans (Life/A&H Insurers)

The procedure assists analysts in determining whether concerns exist due to the level of investment in collateral loans. Collateral loans are unconditional obligations for the payment of money secured by the pledge of an investment. ~~They are subject to the same market and credit risks as their underlying collateral but are likely even riskier given their illiquid and less transparent nature.~~ Market conditions such as rising interest rates and market volatility can impact the value of the underlying collateral and, in turn, an insurer's ability to fulfill policyholder obligations. However, interest rates, while still relatively high, were lowered for the first time in almost a year, and collateral loans are not a core investment for U.S. insurance companies. ~~While collateral loans represent less than 1% of U.S. insurers' total cash and invested assets industry-wide, for private-equity-owned insurers, collateral loans are typically a larger proportion of their total cash and invested assets as compared to the overall U.S. insurance industry.~~ Analysts should review Annual Financial Statement, Schedule BA. In most states, collateral loans are required to be secured or collateralized by assets which have a value in excess of the amount of the loan and which are considered admitted assets for an insurer.

Commented [MA16]: ACLI is concerned that the highlighted sentence is not accurate and directly contradicts the thoughtful deliberation at LRBC. We would suggest that either this sentence should be deleted or revised with the following more accurate language:

While collateral loans are exposed to the market and credit performance of their underlying collateral, they are debt instruments that incorporate structural credit enhancements, including overcollateralization, diversification, cross-collateralization, and lender protections, which reduce economic risk relative to direct ownership of the underlying assets.

Commented [HA17]: Recommend removing the comment on ownership structure. A comment on the risk characteristics of a concentration in collateral loan investments may be appropriate.

Procedures / Data

- Review the following ratios to determine the level of concentration in collateral loans.
  - Ratio of collateral loans to total net admitted assets.
  - Ratio of collateral loans to capital and surplus plus AVR.

Additional Review Considerations

- Compare the fair value of the collateral to the amount loaned to determine whether the loan is adequately collateralized. In those instances where the underlying collateral is comprised of securities, analysts might consider verifying the rate used to obtain the fair value of the securities by referencing the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* (P&P Manual).
- Review Annual Financial Statement, Schedule BA – Other Invested Assets Owned and perform the following for each such loan:
  - Determine whether the collateral for the loan is invested in a quality asset.
  - Determine whether the collateral loan is to an officer, director, parent, subsidiary, or affiliate.

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

Impairment of Invested Assets Exposed to Climate Change and/or Transition Risk

Identify and assess the potential exposure of the insurer's investment portfolio to the impact of material climate change and/or energy transition risks. Transition risks refer to stresses on certain investment holdings arising from the shifts in policy, consumer and business sentiment, or technologies associated with the changes necessary to limit climate change. A few examples of investment holdings and sectors generally subject to greater levels of transition risk include oil/gas, transportation, heavy manufacturing, and agriculture. The insurer's investment portfolio is subject to prospective devaluation or impairment of the assets or changes in the asset return associated with its holdings of climate-affected assets.

Procedures / Data

- Review the information disclosed by the insurer in its responses to the NAIC's Climate Risk and Disclosure Survey (if available) on its exposure to material climate change/energy transition risk and related mitigation activity in this area.
- Review other relevant information provided in the Own Risk and Solvency Assessment (ORSA) Summary Report, and/or U.S. Securities and Exchange Commission (SEC) 10K or 10Q filings (if available) that discusses the insurer's exposure to material climate change/energy transition risk and related mitigation activity in this area.
- Review results of basic scenario analysis conducted by the NAIC using insurers' Annual Statement filings in the NAIC's U.S. Insurance Industry Climate Affected Investment Analysis to identify potential concentrations in insurer exposure.
- Review the Climate Affected Assets Dashboard to assess an insurer's exposure to assets that might be subject to transition risk in the coming years. The dashboard allows the user to view an individual insurer's investment portfolio as of year-end, which has been classified into buckets of climate affected assets (i.e., Fossil Fuel, Energy Intensive), with the ability to view those categories as a percentage of the overall portfolio. Companies that do not have assets subject to transition risk (i.e., Treasuries, Cash) will not be included.

Additional Review Considerations

- Review the insurer's investment policies and strategies to assess whether material climate change, transition and asset devaluation risk considerations have been appropriately implemented into the investment processes.

- Review the most recent examination report and summary review memorandum (SRM) for any findings regarding climate change/energy transition risks.
- If concerns exist, consider requesting information from the insurer regarding its management of exposure to material climate change/energy transition risk, including how it identifies and estimates current and prospective exposures and the limits (if any) in place to avoid concentrations.

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

Credit Quality, Adequacy and Appropriateness of Assets Held for Modco or FWH Agreements (Life/A&H Insurers)

Concerns may exist regarding the quality, adequacy and appropriateness of assets held to support Modified Coinsurance (Modco) or Funds Withheld (FWH) reinsurance, particularly as investments become increasingly complex. Concerns may include controls and governance over investment practices, valuation and ratings of assets, and if material amounts of assets involve related party transactions.

Where collateral held is related to Modco and FWH reinsurance, the analyst should review the information in Note to the Financials #5L(1), #5L(4) and #5L(5), and Schedule S—Part 8—Reinsurance Agreements with Funds Withheld and Modified Coinsurance, in conjunction with other credit, operational and strategic risk of the insurer's reinsurance program. Additionally, review the analysis considerations related reserve reporting required by AG 53 (complex assets) and AG 55 (assets supporting reinsurance) outlined in the Reserving Risk Assessment and SOA procedures and guidance.

Where the company is engaged in material Modco and FWH arrangements, the analyst can use the detail of collateral received and held under Note 5L(4) to identify the types of assets held by investment schedule, and gain an understanding of the materiality of aggregate BACV of the collateral received to the insurer's asset portfolio. Further, the Note #5L(5) disclosure identifies if securities held as collateral under Modco or FWH agreements are also pledged under other arrangements, in which case they would not be for the benefit of the reinsurer or available to fulfill the liabilities of the reinsurance contract. The analyst can use the information in Schedule S—Part 8 to identify any concerns with the types of assets and credit quality of assets held under ceded or assumed Modco or FWH agreements.

Procedures / Data

- Identify the types of reinsurance agreements and jurisdiction of the reinsurer [Annual Financial Statement, Schedule S – Part 3] and determine if concerns may exist over the adequacy and quality of assets held by reinsurers in support of ceded reserves that may require further analysis or inquiry to the insurer.
- Compare the BACV of the collateral received and assets held under Modco/FWH Reinsurance Agreements to the recognized obligation for Modco and FWH assets. [Annual Financial Statement, Notes to the Financials #5L(4)(m and n)].
- Identify if investments held under FWH agreements (including Modco) are related to the Modco/FWH reinsurer [Annual Financial Statement, Notes to the Financials 5L(5)(o-v)].
- Identify if the insurer is engaged in ceding business under Modco and FWH agreements with offshore reinsurers.
    - Gain an understanding, through review of Schedule S - Part 3, of the types of insurance business ceded, the reinsurer's jurisdiction, if affiliated or non-affiliated, and applicable collateral requirements by type of reinsurer (i.e. authorized, unauthorized, reciprocal jurisdiction, certified)

- Review Schedule S – Part 8 to determine if concerns exist regarding the types of assets held or the credit quality of assets held under Modco/FWH agreements. Consider if the aggregate of medium or lower quality assets held represent a material amount of the related Modco/FWH liabilities.
    - Review Schedule S – Part 8 in comparison to Life RBC (asset schedules) to ensure asset subtotals match. If differences exist, inquire of the insurer, as differences may have an impact on the RBC calculation.
- Determine if assets held under Modco or FWH agreements are also pledged under other agreements [Annual Financial Statement, Notes to the Financials #5L(5)].

- Determine if assets held under Modco or FWH agreements contain a material amount of private credit assets or related party investments (or related to the reinsurer managing the portfolio). If so, consider additional procedures in the Private Credit section above and/or Related Party section below.

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

Collectability or Default of Investments Involving Related Parties

Determine related party exposure in the investment portfolio and assess any related credit risk.

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

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

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

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

1. Direct loan or direct investment (excluding securitizations) in a related party, for which the related party represents a direct credit exposure.
2. Securitization or similar investment vehicles such as mutual funds, limited partnerships and limited liability companies involving a relationship with a related party as sponsor, originator, manager, servicer, or other similar influential role and for which 50% or more of the underlying collateral represents investments in or direct credit exposure to related parties.
3. Securitization or similar investment vehicles such as mutual funds, limited partnerships and limited liability companies involving a relationship with a related party as sponsor, originator, manager, servicer, or other

similar influential role and for which less than 50% (including 0%) of the underlying collateral represents investments in or direct credit exposure to related parties.

4. Securitization or similar investment vehicles such as mutual funds, limited partnerships, and limited liability companies in which the structure reflects an in-substance related party transaction but does not involve a relationship with a related party as sponsor, originator, manager, servicer, or another similar influential role.
5. The investment is identified as a related party, but the role of the related party represents a different arrangement than the options provided in choices 1-4.
6. The investment does not involve a related party.

Procedures / Data

- Review the Annual Financial Statement investment schedules, as disclosed in the column "Investments Involving Related Parties" and utilizing iSite+ tools, determine if the insurer has material related party exposures in its investment portfolio. This disclosure is included in:
  - Schedule B – Part 2
  - Schedule BA – Part 2
  - Schedule D – Part 1, Sections 1 and 2
  - Schedule DA – Part 1
  - Schedule DB – Part A Section 1
  - Schedule DL – Part 1 and 2
  - Schedule E, Part 2

  Consider exposure by asset class and in aggregate, and by the role of the related party in the investment as designed by the "Investments Involving Related Parties" disclosure.
- If concerns exist regarding a material related party exposure in the investment portfolio, assess the credit quality of those investments and assess any historical default experience.
- Determine if related party investments include a material amount of private credit assets (e.g. related investment manager or related reinsurer managing the Modco/FWH reinsurance assets). If so, consider additional procedures in the Private Credit or Modco/FWH sections above.

LIQUIDITY RISK: Inability to meet contractual obligations as they become due because of an inability to liquidate assets or obtain adequate funding without incurring unacceptable losses.

The Liquidity Risk Assessment is focused primarily on overall liquidity, liquidity of investments, receivables, and cash flow from operations. In analyzing liquidity risk, analysts may analyze specific types of investments and receivables held by insurers. An analyst's risk-focused assessment of liquidity risk should take into consideration the following areas (but not be limited to):

- Liquidity ratios/metrics
- Liquidity of certain investments with shallow markets and limited public information, such as: private credit securities, including private placement bonds~~:~~; ~~and~~ common stock~~,~~; highly structured investments~~,~~; investments on Schedule BA~~,~~; and affiliated investments
- Liquidity of certain receivables, including health care receivables and special deposits
- Cash flow from operations
- Stockholder dividends
- Surrender and withdrawal activity for life insurers

Commented [HA1]: Adding more explanation to help focus this guidance on the risk presented by illiquid assets rather than the structure of particular assets. Statistics could be helpful in this section, if there are any that NAIC can provide.

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

Impact of Market Volatility on the Liquidity of the Aggregate Investment Portfolio

An important consideration when markets experience significant volatility and strains is the potential negative impact may not be on just one or a small number of investments held by insurers. Rather, market strains can have a significant impact on an entire asset class, several asset classes, or the entire investment portfolio. Particularly vulnerable are asset classes that represent smaller markets that are typically less liquid, are more complex or are assets that would be considered less traditional for insurers. Therefore, state insurance regulators should consider the potential impact of significant market challenges on different asset classes in the investment portfolios of insurers.

Procedures

- Review and monitor material asset classes for significant changes in fair value and/or significant changes in relative liquidity. Utilize data in the Annual Statement, Financial Profile, Snapshot Investment Summary and investment dashboards. Also refer to specific liquidity guidance in this chapter on asset groups such as bonds, BA assets and mortgage loans. Do not limit considerations to one asset class, but also consider the aggregate of all such vulnerable asset classes. Examples of asset groupings that may represent notable exposures in insurer portfolios and that should be considered are:
  - Below investment grade bonds.
  - Weaker investment grade ("BBB" rated) bonds.
  - Commercial mortgage loans, particularly office properties.
  - Mezzanine loans.
  - Real estate equity.

- Structured securities, especially collateralized loan obligation (CLO) tranches (including CLO Combo Notes and Middle Market CLOs).
- Residential mortgage-backed securities (RMBS), specifically as to cash flow variability.
- Emerging markets investments.
- Hedge funds.
- Private equity funds.
- Private credit, including private placements (specifically non-144A) and private letter ratings.
- Derivatives transactions.
- Concentrations in exposure to the auto, technology, consumer products and retail sectors (due to the potential impact of tariffs).

The significance of these exposures should be evaluated in the context of the insurer's overall risk profile, including applicable NAIC capital requirements associated with the assets. Different situations may call for different standards, so it is important to be able to explain the standard used.

Commented [HA2]: Since there is no single standard of materiality, stating the standard being used will be helpful for focusing the review.

When evaluating the liquidity of less liquid assets, analysts should consider the insurer's broader asset-liability management framework. Insurers generally have long investment horizons due to the long-duration and generally predictable nature of their liabilities. Accordingly, insurers actively model asset and liability cash flows to ensure sufficient liquidity is available to meet policyholder obligations as they come due. Less liquid assets, including private equity, hedge funds, private credit, and commercial mortgage loans, generally are not used for day-to-day liquidity management. Rather, the ability to allocate a portion of the portfolio to such assets is a structural feature of the insurance business model and can provide additional investment return while remaining consistent with prudent liquidity management.

Commented [MA3]: Insurers have long investment horizons and model cash flows to meet these liabilities
- Insurers have long investment horizons due to the long-duration nature of their liabilities and actively model asset and liability cash flows to ensure sufficient liquidity is available when obligations come due.
- Insurance liability cash flows are generally predictable and have limited exposure to short-term market sensitivity.
- Insurers do not rely on many of the assets listed in this section for day-to-day liquidity management (i.e., PE, Hedge funds, private credit, commercial mortgage loans, etc.).
- The ability to invest in less liquid assets is a structural feature of the insurance business model and allows insurers to earn a premium while continuing to meet policyholder obligations.

- Refer to the Procedures for review of Actuarial Guideline 53 and Actuarial Guideline 55 in the Reserve Risk Chapter for additional related investment liquidity review.

Additional Review Considerations

i. For the identified asset classes above, where there is not a readily available or exchange traded market, verify pricing and valuation sources and methods. Close attention should be given to asset classes like private equity and real estate that usually report on a 3-month lag, as well as private credit whose valuations may be subjective.

ii. Inquire as to how the insurer is managing the potential risk of rating migration. Inquire as to how they may apply a credit rating transition matrix and calculate the resulting increased RBC charges.

iii. Inquire as to how the insurer is managing the above-mentioned challenges and other potential challenges in the investment marketplace. For example, consider the following questions:
   a. How is the insurer managing its liquidity needs given the changes in investment markets, especially given historically liquid assets may not be as liquid?
      1. How is the insurer managing changes in cash-flow expectations from prepayments, both generally and specifically associated with mortgage-backed securities?
   b. How is the insurer managing significant changes in fair value of portfolio assets, especially for longer dated investments?
      1. Are other-than-temporary- impairments (OTTI) appropriate?

2. If there is an ongoing risk, should the insurer consider shortening the duration of future investments?

iv. Review the insurer's Liquidity Stress Test submission (if applicable) to evaluate results and assess the insurer's stress testing process and assumptions.

v. Inquire as to how changes in the investment profile (particularly duration) may impact asset/liability matching, asset adequacy analysis and cash-flow testing.

vi. Request an Opinion from the NAIC's Securities Valuation Office (SVO) or Structured Securities Group (SSG) on a specific investment holding or transaction. A state insurance regulator can ask for SVO or SSG analytical assistance with respect to any investment related activity or in connection with an assessment of investment-related aspects of a Regulatory Transaction (defined in the P&P Manual). The department can direct an insurance company to file relevant information with the SVO or SSG for the purpose of that analysis and the SVO or SSG will issue a report back to the department.

vii. Request a Preliminary Analysis from the NAIC's Capital Markets Bureau (CMB) to assess the insurer's overall portfolio of investment risk exposures and obtain additional follow-up procedures that can be performed by the department to address any overall portfolio issues identified. Request analytical assistance from the CMB to better understand and measure the investment risks related to a particular asset class, investment-related activity, or market trend.

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

Exposure to Private Credit Securities, Level 3 Securities, Bonds with Private Letter Ratings and Unfunded Commitments

In recent years, the insurance industry has seen an ongoing increase in the amount of private assets held by U.S. domestic insurers, including securities with NAIC designations supported by private letter ratings and securities that are valued based on Level 3 (unobservable) inputs. While this increase is generally consistent with the broader capital markets trend of increased issuance of private assets, the potential lack of transparency related to private assets can complicate the assessment of credit quality and increase the liquidity risk of the portfolio.

Private credit generally refers to debt, or debt-like, securities that are not publicly issued or traded. Private credit is an evolving, alternative funding source. Non-bank lenders, including insurance companies, private debt funds, and business development companies, issue private loans directly to mostly small and middle-market companies that do not have—or have limited— access to the public corporate bond and loan markets. These small middle-market companies often have more debt than larger companies that access capital via leveraged loans and public bonds and, therefore, they are more susceptible to economic downturns and the impact of rising interest rates.

Private credit has a variety of strategies that include direct lending, distressed debt, venture debt, mezzanine finance, and special situations. Direct lending is the largest segment and accounts for about 40% of the U.S. private credit market. The largest investors in private credit are typically pension funds, insurance companies, and sovereign wealth funds. While direct lending to corporate issuers is the simplest and most common type of private

credit, it is evolving into more complex investments like feeder fund structures, private credit CLOs, and asset-based financing (where loans are secured by collateral such as inventory, receivables, equipment, or property).

Risks and mitigating factors include:

- Less liquidity: Private credit is generally issued directly by a non-bank lender or a small group of lenders, resulting in a relatively illiquid market where secondary trading is limited.
- Less transparency: The availability of information about a private credit security is often contractually restricted, which contributes to lower transparency compared to public securities.
- Less frequent pricing: Private credit may be subject to less frequent valuation and pricing; and it may rely on third-party valuations and/or modeling, which may be subjective.
- Assessment of credit quality:
    - While lack of transparency can make credit quality more difficult to assess,private credit lenders can often benefit from stronger control over documentation, as compared to a syndicate of lenders, and are able to customize terms of the transaction given their direct relationship with borrowers. In the event of stress, lenders and investors should be able to work directly with the borrower to modify the transaction terms or add investor safeguards.
    - Private credit also has the potential to provide a broader pool of debt issuers that results in portfolio diversification.
- Future performance:
    - Private credit generally offers higher spreads and yields than public corporate bonds and loans to compensate investors for the relative market illiquidity (lack of a secondary market) and complexity depending on the transaction type.
    - As the nature of private credit evolves and expands, there is no assurance that current/historical performance trends (largely favorable) will continue. The solid historical performance of private lending may not be comparable performance as the market grows and as new entrants change focus to non-traditional alternative assets and more challenging and stressed credit environments occur, particularly higher interest rates.

Refer also to guidance published by the NAIC Capital Markets Bureau on private credit and its characteristics.

Note that the Annual Statement includes new disclosures and reporting requirements to improve the identification of different types of private placements. For year-end 2026, insurers will be required to disclose the SEC registration status for each investment: public, Rule 144A, private placements (defined to include Regulation D, Section 4(a)(2) exempt or other exclusion from SEC registration), or not applicable because the investment is not within the scope of the Securities Act of 1933. An aggregate disclosure in Note 5.T—Private Securities to capture key data by each grouping of investments by registration status to allow for ease of regulator review. The reporting will be provided in an electronic column in all investment reporting schedules (held, acquired, disposed) for short-term investments, cash equivalents, issuer credit obligations, asset-backed securities, common stock, preferred stock and other long-term investments.

Fair Value Measurement Hierarchy

An important element in evaluating risks associated with valuation of private investments (equity or credit) is the level of input available to determine fair value. To increase consistency and comparability in fair value measurements and related disclosures, the fair value hierarchy (see SSAP No. 100) prioritizes the inputs to

valuation techniques used to measure fair value into three broad levels. The fair value hierarchy gives the highest priority to quoted prices (unadjusted) in active markets for identical assets (Level 1) and the lowest priority to unobservable inputs (Level 3).

- **Level 1** inputs are quoted prices (unadjusted) in active markets for identical assets that the reporting entity has the ability to access at the measurement date.

- **Level 2** inputs are inputs other than quoted prices included within Level 1 that are observable for the asset, either directly or indirectly. Level 2 inputs might include quoted prices for similar assets in active markets, quoted prices for identical or similar assets in inactive markets, or prices derived from inputs that are observable (e.g., interest rates and yield curves). Level 2D reflects use of internal models.

- **Level 3** inputs are unobservable inputs for the asset. Unobservable inputs are used to measure fair value to the extent that relevant observable inputs are not available. These inputs often involve significant judgment and estimation, including the use of internal models and assumptions.

When reviewing Level 3 assets, analysts should distinguish valuation classification from credit risk assessment. The fair value hierarchy is intended to identify the nature of inputs used to measure fair value, not to assign a credit risk classification. Therefore, a Level 3 classification reflects the use of significant unobservable inputs and should not be interpreted, on its own, as evidence of elevated credit risk. Certain long-duration insurance assets may have limited observable market inputs but still exhibit stable contractual cash flows and strong credit characteristics. In addition, some assets may be classified as Level 3 because observable valuation inputs are not available at the measurement date, and those assets may subsequently migrate to Level 2 once observable inputs become available.

Commented [MA4]: Clarifies that Level 3 is a valuation-input classification, not a credit-risk classification, and explains why certain long-duration insurance assets may be Level 3 despite stable cash flows and strong credit characteristics.

Information associated with fair value measurement is provided in Note 20 (Fair Value Measurements) of the Annual Statement and can assist regulators in assessing the risks associated with an insurer's private investment holdings. In addition, information on fair value hierarchy reported in the investment schedules can be utilized to identify individual securities warranting additional review.

Private Letter Ratings (PLRs)

Privately rated securities reported by U.S. insurance companies have become more prevalent in recent years. The greater use of PLRs is generally consistent with the overall increase in private credit investments by insurers, particularly life companies. PLRs provide proprietary details of investments and are only communicated to the issuer and a specified group of investors. Therefore, these investments do not benefit from the market validation that comes from market transparency (multiple investors, publicly viewable ratings, etc.) and often come as a single rating rather than multiple ratings. The NAIC has required insurance companies to submit PLRs for verification since 2018, whereby the NAIC's SVO reviews that the letter submitted is for the appropriate security and the current year. In addition, effective in 2022, insurers are required to file full rating rationale reports for PLR requests with the SVO, to partially mitigate concerns regarding the lack of transparency of PLRs.

When reviewing securities supported by PLRs, analysts should consider that the growth in PLRs is largely a reflection of increased private market issuance and the continued evolution of private credit markets, rather than, by itself, an indication of deteriorating credit quality. As market activity shifts toward newer private credit asset

classes, the use of PLRs may increase because these assets are often issued in private markets and may not be broadly rated or publicly disseminated. Analysts should also consider the insurer's broader credit assessment framework, including internal underwriting, investment committee review, and ongoing surveillance, as investments in private assets generally do not rely solely on agency ratings for credit evaluation.

Commented [MA5]: Explains that PLR growth should be viewed in the context of expanding private markets and newer private credit asset classes, while also emphasizing insurers' internal underwriting, investment committee review, and ongoing surveillance as part of the credit assessment framework.

Unfunded Private Equity Commitments

Insurers have continued to expand their allocations to private equity, as evidenced by the increase in unfunded commitment (liability) levels in recent years. These funding commitments—contractual obligations to contribute capital to private equity funds over time—have grown along with insurers' appetite for higher-yielding, long-duration assets amid heightened market volatility. This trend underscores a strategic shift toward private markets, although it also introduces additional considerations around liquidity management and possible valuation uncertainty. Unfunded commitments may be commitments to private credit funds, but can also include commitments to private equity, hedge funds and real estate limited partnerships.

When reviewing unfunded commitments, analysts should consider how these obligations fit within the insurer's broader portfolio construction and liquidity planning framework. Funded and unfunded commitments are generally made as part of the portfolio construction process and are sized with consideration of expected liquidity needs, anticipated capital call timing, future reinvestment activity, and liability cash-flow generation. The existence of unfunded commitments, by itself, should not necessarily be viewed as indicative of elevated liquidity risk; rather, analysts should evaluate whether the insurer has incorporated those commitments into its liquidity planning, cash-flow forecasting, and overall asset-liability management process.

Commented [MA6]: Frames funded and unfunded commitments as part of insurers' broader portfolio construction, liquidity planning, cash-flow forecasting, and asset-liability management processes, while clarifying that the existence of unfunded commitments alone should not necessarily indicate elevated liquidity risk.

Procedures / Data

- Ratio of private-placement bonds owned to policyholder surplus (P/C), to capital and surplus plus AVR (Life/A&H) and to capital and surplus (Health)
- Increase in private placement bonds from the prior year
- Review the Private Security Code details in the investment schedules, and aggregate private securities information in Note 5.T.; or utilize iSite+ tools, to identify a concentration in private securities.
  - Ratio of Private credit securities in aggregate, by asset type, and by security code category to capital and surplus plus AVR (Life/A&H) and to capital and surplus (Health)
- Review the SVO Administrative Symbols provided for the insurer's bond portfolio on Column 6 of Schedule D, or utilize iSite+ tools, to identify a concentration in securities backed by PLRs (i.e., symbols PL and PLGI).
  - Ratio of securities backed by PLRs to capital and surplus plus AVR (Life/A&H) and to capital and surplus (Health)
  - Change in securities backed by PLRs from the prior year, in aggregate and by asset type
- Review information provided in Note 20C of the Annual Statement (Fair Value Measurement) or utilize iSite+ tools, to identify the extent investments (by type of financial instrument) have a fair value determined with unobservable inputs (i.e., Level 3 inputs).
  - Ratio of Level 3 or Level 2D securities in aggregate and by asset type, to capital and surplus plus AVR (Life/A&H) and to capital and surplus (Health)
  - Change in Level 3 or Level 2D securities from the prior year, in aggregate and by asset type
- Review Note 14A1 to identify if the insurer has a material exposure to contingent commitments.
  - Change in contingent commitments (liabilities) since the prior year, in aggregate.

Additional Review Considerations

- Review Note 14 – Liabilities, Contingencies, and Assessments, to assess the insurer's exposure to unfunded commitments to private credit funds.
- If exposure to unfunded commitments is significant, consider whether the insurer's management and board have a clear understanding of differences in liquidity and market value drivers, as well as the reasons for different yield and cash-flow characteristics, as unfunded commitments contractually obligate the insurer to contribute capital to private equity funds over a designated period of time.
- Review Annual Financial Statement, Schedule D – Part 1A to determine the amount, issue type, NAIC designations, maturity distribution of privately-placed bonds owned, and the amount of privately placed bonds that are freely tradeable under U.S. Securities and Exchange Commission (SEC) Rule 144 or qualified for resale under SEC Rule 144A.
- For insurers with a concentration in bonds with Private Letter Ratings (PLRs):
  - Request the support of the NAIC's Securities Valuation Office (SVO) to ~~investigate~~identify the rating sources for the securities (with a focus on concentrations with any one rating agency and/or securities with only one rating) and consider the potential impact on the insurer's RBC charges and investment risk exposures.
  - Request details from the company on its own internal ratings for securities backed by PLRs where applicable and compare with rating agency rating for discrepancies.
- For insurers with a significant concentration in Level 3 or Level 2D securities, consider reviewing the investment schedule detail to identify whether the investments with Level 3 or Level 2D fair values are private, whether a private letter rating is the source of the NAIC designation for these items, and the extent the investments have aggregate deferred interest or paid-in-kind (PIK) interest.
- Utilize information on fair value hierarchy reported in the investment schedules to identify individual securities warranting additional review.
- If private placements, private credit investments, Level 3 or 2D securities, or assets with PLRs are material, consider inquiring of the insurer its infrastructure and investment management policies and procedures (i.e. portfolio management and credit analyst expertise, including approach to making investment decisions) in place either internally, or via an affiliate, and/or outsourced investment manager, to manage these investments.
- Consider requesting additional information on the ongoing performance of these assets and/or the pricing assumptions and methodologies used in fair value measurement.
- If necessary, consider utilizing an investment specialist to assist in asset valuation considerations.
- If appropriate, consult with or request an Opinion from the NAIC's SVO or Structured Securities Group (SSG) on a specific investment holding or transaction. [A state insurance regulator can ask for SVO or SSG analytical assistance with respect to any investment related activity or in connection with an assessment of investment-related aspects of a Regulatory Transaction (defined in the P&P Manual). The department can direct an insurance company to file relevant information with the SVO or SSG for the purpose of that analysis and the SVO or SSG will issue a report back to the department.]
- Request a Preliminary Analysis from the NAIC's Capital Markets Bureau (CMB) to assess the insurer's overall portfolio investment risk exposures and suggest additional follow-up procedures that can be performed by the department to address overall portfolio issues identified. Request analytical assistance from the CMB to better understand and measure the investment risks related to a particular asset class, investment-related activity, or market trend.

Commented [HA7]: Suggest changing "investigate" to "identify" since the focus seems to be on identifying concentrations with one agency. In reviewing the proposed changes, it was noted that the word "investigate" might be interpreted to mean reviewing and evaluating the PLRs, which seems redundant.

Commented [MA8]: What are the metrics they should be considering? Seems subjective and substituting SVO's judgment for the rating sources.

~~Exposure to Private Placement Bonds~~

~~Significant investments in privately placed bonds may cause concerns regarding the insurer's liquidity because some of these investments cannot be resold, while those that can be resold have restrictions on whom they can be sold to, including restrictions under securities laws. There is no structured market for privately placed bonds like there is for publicly traded bonds. Therefore, even if the privately placed bonds can be sold, it may be difficult to find a willing buyer.~~

~~Procedures / Data~~

- ~~Ratio of private placement bonds owned to policyholder surplus (P/C), to capital and surplus plus AVR (Life/A&H) and to capital and surplus (Health)~~
- ~~Increase in private placement bonds from the prior year~~

~~Additional Review Considerations~~

- ~~Review Annual Financial Statement, Schedule D – Part 1A to determine the amount, issue type, NAIC designations, maturity distribution of privately placed bonds owned, and the amount of privately placed bonds that are freely tradeable under U.S. Securities and Exchange Commission (SEC) Rule 144 or qualified for resale under SEC Rule 144A.~~
- ~~For significant privately placed bonds rated by a chief revenue officer, review the issuer's rating or request the Securities Valuation Office's assessment of the designation to evaluate the issuer's financial position and ability to repay its debt.~~

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

Invested Asset Exposure to Climate Change, Transition and Asset Devaluation Risk

Identify and assess the potential exposure of the insurer's investment portfolio to the impact of material climate change and/or energy transition risks and asset devaluation risk. The insurer's investment portfolio is subject to prospective devaluation of the assets/changes in the asset return associated with its holdings of climate-affected assets. Transition risks refer to stresses on certain investment holdings arising from the shifts in policy, consumer and business sentiment, or technologies associated with the changes necessary to limit climate change. A few examples of investment holdings and sectors generally subject to greater levels of transition risk include, oil/gas, transportation, heavy manufacturing, and agriculture. In assessing an insurer's exposure to these risks, the analyst is encouraged to review information disclosed by the insurer in its responses to the NAIC's Climate Risk Disclosure Survey, U.S. Securities and Exchange Commission (SEC) filings, and/or the Own Risk and Solvency Assessment (ORSA) Summary Report filings. In addition, the analyst is encouraged to review the results of basic scenario analysis conducted by the NAIC using insurers' Annual Statement filings (U.S. Insurance Industry Climate Affected Investment Analysis) to identify potential concentrations in exposure.

Procedures

- Review information provided in the insurer's response to the NAIC's Climate Risk and Disclosure Survey (if available) on its exposure to material climate change/energy transition risk and related mitigation activity in this area.
- Review relevant information provided in the Own Risk and Solvency Assessment (ORSA) Summary Report, and/or U.S. Securities and Exchange Commission (SEC) 10-K or 10-Q filings (if available) that discusses the insurer's exposure to material climate change/energy transition risk and related mitigation activity in this area.
- Review information provided in the NAIC's U.S. Insurance Industry Climate Affected Investment Analysis to identify potential concentrations in insurer exposure.

- Review the Climate Affected Assets Dashboard to assess an insurer's exposure to assets that might be subject to transition risk in the coming years. The dashboard allows the user to view an individual insurer's investment portfolio as of year-end, which has been classified into buckets of climate affected assets (i.e., Fossil Fuel, Energy Intensive), with the ability to view those categories as a percentage of the overall portfolio. Companies that do not have assets subject to transition risk (i.e., Treasuries, Cash) will not be included.

American Property Casualty Insurance Association
INSURING AMERICA apci.org

September 10, 2026

Danielle Smith, Chair
Financial Analysis Solvency Tools (E) Working Group
National Association of Insurance Commissioners

Re: Proposed Revisions to the Financial Analysis Handbook

Dear Ms. Smith:

The American Property Casualty Insurance Association (APCIA)[1] appreciates the opportunity to comment on the proposed revisions to the Financial Analysis Handbook on the use of artificial intelligence tools in financial analysis work.

APCIA supports the majority of the proposed additions to the Handbook related to AI, including the recognition that financial analysis information is confidential, non-public, personally identifiable, or proprietary and thus not appropriate to be input into external public-facing AI platforms. We also support the additions to the Handbook stating that AI outputs should be reviewed and validated for accuracy, and that the proposed expectations apply equally to state insurance department analysts as well as any contract analysts or vendors a department may use in the course of analysis work.

However, APCIA recommends deleting the sentence in the second new paragraph stating: "If a secure AI tool is not available, analysts must ensure that any data is fully anonymized to remove any non-public or sensitive information."

Analysts should not be permitted – and especially not encouraged – to enter a company's non-public data, even when anonymized, into unsecured AI tools. Given the amount of confidential data that would need to be anonymized and entered in the unsecured AI tools, the risk of a company's confidential, non-public, personally identifiable, or proprietary information being inappropriately accessed or re-identified is relatively high. Allowing this information to be input into unsecure AI tools could also undermine confidence that proprietary materials will be handled only within secure systems. For these reasons, this sentence should be removed from the proposal, and the Handbook should instead make clear that financial analysts should not input company information in unsecure AI tools.

APCIA further recommends that the Working Group coordinate the development of proper governance and safeguards regarding analysts' and examiners' use of AI among the working

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

groups reporting to the Examination Oversight (E) Task Force to ensure the protection of companies' confidential, non-public, personally identifiable, or proprietary information is consistently applied.

Finally, regarding an unrelated topic, we note the exposure contains references to several NAIC dashboards, such as the Climate Affected Assets Dashboard. As the NAIC develops additional dashboards in the future and references them in the Handbook, any such references should make clear the purpose of the dashboard and how it is maintained to help stakeholders understand how various dashboards are used and developed.

Thank you for considering the points addressed in this letter, and please do not hesitate to contact us if you have any questions.

Sincerely,



Matthew Vece
Sr. Director, Financial & Tax Counsel

ATHENE

September 10, 2026

Danielle Smith
Chair, Financial Analysis Solvency Tools (E) Working Group
National Association of Insurance Commissioners
1100 Walnut Street
Suite 1500
Kansas City, MO 64106-2197

Via email: RGood@naic.org; RVillegas@naic.org; JMurray@naic.org

Re: Response to Financial Analysis Solvency Tools (E) Working Group Exposure Drafts — Private Asset Exposures and Unauthorized Reinsurance

Dear Chair Smith and Members of the Working Group,

Athene Holding Ltd. (Athene) appreciates the opportunity to comment on the Financial Analysis Solvency Tools (E) Working Group's proposed revisions to the Financial Analysis Handbook (Handbook.

Athene is a leading retirement services company that issues and reinsures annuity products, helping millions of Americans secure their retirement. We engage constructively with the NAIC and state regulators to support a solvency framework that is transparent, analytically grounded, and calibrated to protect policyholders.

Private Credit/Private Assets

Athene is generally supportive of the Working Group's efforts to update the Handbook to address "Private Assets Exposures" and endorses ACLI's comments and suggested revisions. We would add one definitional point. 'Private credit' and 'private assets' are convenient shorthand, not risk categories – the terms sweep together everything from seasoned investment-grade private placements to complex, less liquid structures with materially different risk profiles. The Handbook's procedures should follow the characteristics of the asset, not the label attached to it. The NAIC's own data makes the case: as the NAIC has observed with respect to insurer CLO holdings:

> [T]he overall credit profile of insurer CLO holdings has remained relatively strong, with about 80 percent rated investment grade or higher, including 39 percent rated AAA. These figures help explain why regulators are not treating CLOs or private credit as inherently inappropriate for insurance portfolios. The focus instead is on whether transparency, valuation, capital treatment, and

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supervisory tools are keeping pace with increasingly complex structures and growing concentrations."

We encourage examiners to apply that same discipline under the revised Handbook – looking through the label to the asset itself, rather than treating a generic classification as a proxy for risk.

Asset Intensive Reinsurance

Athene also supports the proposed guidance on "reinsurance ceded to reinsurers in unauthorized offshore jurisdictions." The expansion of asset-intensive reinsurance into less mature, less transparent regulatory regimes poses a genuine and growing risk to policyholders, market stability, and the integrity of the U.S. solvency framework.

We recommend that the revisions consistently refer to reinsurance ceded to reinsurers in unauthorized jurisdictions, and avoid the term "unauthorized offshore reinsurers," which can be read to include reinsurers in reciprocal jurisdictions such as Bermuda or the UK that have not applied to be "reciprocal jurisdiction reinsurers" in order to eliminate collateral, but are still regulated the same way as those reciprocal-jurisdiction reinsurers. The Financial Condition (E) Committee's own July 27, 2026 referral to the Life Risk-Based Capital (E) Working Group on reinsurance recapture and counterparty risk draws this same distinction, directing a new RBC recapture factor to apply to reinsurance "located outside of reciprocal jurisdictions" rather than to offshore or unauthorized reinsurance without regard to jurisdictional maturity. The Handbook should adopt the same convention.

The proposed best practices for Form D review and the enhanced monitoring procedures close a real gap in U.S. oversight of counterparty credit risk. We particularly welcome the recommendation that reinsurers in unauthorized jurisdictions report not only under their home-jurisdiction framework but also on a U.S. GAAP and U.S. Statutory basis, which will materially sharpen regulators' view of the risk.

A reinsurer whose home capital and solvency framework differs materially from U.S. standards may still assume U.S. liabilities once collateral requirements are met, with no separate finding that it holds capital protections comparable to those the U.S. framework expects. That invites regulatory arbitrage: lower reserving or capital standards create an apparent economic benefit without commensurate loss-absorbing protection beyond the required collateral. The concern is greatest where limited transparency, permissive reserving, and low capital requirements coincide.

We therefore support the Working Group's recognition that scrutiny should reflect the maturity, transparency, and demonstrated solvency equivalence of the assuming

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jurisdiction. This is not a hypothetical concern: preliminary findings from the NAIC's own Valuation Analysis (E) Working Group, cited in the Financial Condition (E) Committee's July 27, 2026 referral on reinsurance recapture and counterparty risk, indicate that business ceded to reinsures in unauthorized jurisdictions generally originates with newer, relatively small annuity writers offering aggressive crediting rates, and produces larger reductions in total asset requirements than comparable business ceded to Bermuda. The NAIC's own preliminary analysis confirms the dynamic this letter flags.

We likewise support the emphasis on international cooperation and data sharing. The guidance appropriately contemplates communication with foreign regulators, and we encourage strengthening those channels so U.S. regulators can obtain timely, reliable information on offshore reinsurers' financial condition and regulatory compliance.

We appreciate the opportunity to comment and would welcome the chance to discuss these views as the Working Group's deliberations continue.

Respectfully submitted,



Michael Consedine
Executive Vice President, Global Head of Government and Regulatory Affairs
Athene Holding Ltd.

Special Notes: The following procedures do not supersede state regulation but are merely additional guidance analysts may consider useful. The procedures may be completed in part, or in total, at the discretion of the analysts depending on the level of concern, and the area in which the risk was identified.

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

Model Act and Database Procedures

Form A is transaction-specific and is not part of the regular annual/quarterly analysis process. Every Form A review should be tailored to the risks associated with the proposed acquisition, including the target company, acquiring entity, and the complexity of the transaction. The review of these transactions may vary, as some states might have regulations that differ for Form A.

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

Compliance Assessment and Review

Transaction Details

3. Review details provided on the transaction for compliance with application filing requirements by determining whether the Form A application provides the required content, which may include the following:
   a. Provides a brief description of how control is to be acquired.
   b. Contains the following information:
      - Name and address (legal residence for an individual or street address if not an individual) of the applicant.
      - States the nature of the applicant's business operations for the past five years, if the applicant is not an individual.
      - Describes the business to be performed by the applicant and its subsidiaries.
      - Identifies and states the relationship of every member of the insurance holding company system on the organizational chart.
   c. Contains the required signature and certification, and include copies of all tender offers for, requests or invitations for, tenders of, exchange offers for, and agreements to acquire or exchange any voting securities of the insurer and of additional soliciting material relating thereto.
   d. Contains any proposed employment, consultation, advisory or management contracts concerning the insurer, annual reports to the stockholders of the insurer and the applicant for the last two fiscal years, and any additional documents or papers required by the Form A.
   e. Contains an agreement to provide the information required by Form F – Enterprise Risk Report within the required timeframe.
   f. Includes the number of each class of shares of the insurer's voting securities that the applicant, its affiliates, and any person that plans to acquire; 2) the terms of the offer, request, invitation, agreement, or acquisition; and 3) the method by which the fairness of the proposal was determined.

g. States the amount of each class of any voting security of the insurer that is beneficially owned or concerning that there is a right to acquire beneficial ownership by the applicant, its affiliates, or any person.

h. Gives a full description of any contracts, arrangements, or understandings with respect to any voting security of the insurer in which the applicant, its affiliates, or any person is involved. Discussion includes, but is not limited to, the transfer of any of the securities, joint ventures, loan or option agreements, puts or calls, guarantees of loans, guarantees against loss or guarantees of profits, division of losses or profits, or the giving or withholding of proxies.

4. Perform analysis review considerations, in addition to the compliance review in #3 as necessary, to analyze the details of the transaction, which may include, but is not limited to the following:

   a. Document any risks or concerns by carefully reviewing transactional documents (e.g., merger, stock purchase, stock exchange).

      i. Consider disposition of all classes of target shares, including addressment of any beneficial owners.

      ii. Ascertain propriety of disposition of minority interests and concerns, if applicable.

   b. Consider any affiliate or employee benefit as appropriate.

   c. Has the applicant included information on the assignment of specialized personnel (such as an attorney, actuary, or CPA) to the transaction?

   d. Determine how any ancillary regulatory reviews or other interim procedural steps will be completed, including Form E – Pre-Acquisition Notification Form, for other licensed states.

   e. Obtain copies of shareholder communications or sole shareholder consent.

   f. Consider obtaining copies of fairness and other contractually required opinions, if available.

   g. Review relevant portions of board resolutions, power points and related board minutes pertinent to the Form A transaction, using care to keep documents confidential.

   h. Determine if after the change of control:

      i. The insurer will be able to satisfy the requirements for the issuance of a license to write the classes of insurance for which it is presently licensed.

      ii. The insurer's surplus will be reasonable in relation to its outstanding liabilities and adequate for its financial needs.

   i. Review financial projections for the applicant and the insurer to ensure that they are consistent with the description of the intended business plan of the insurer and other assertions and representations made in the Form A filing. Determine whether the projections are based on reasonable expectations.

      i. Determine the target's estimated post-acquisition financial condition and stability.

   j. If not included in the Form A filing, request copies of all contracts between the applicant (or other entities for which it exhibits control) and the insurer. Review these contracts to ensure that the terms are at arm's-length, fair, and reasonable to the insurer.

   k. Will the proposed merger or acquisition comply with the various provisions of the state's General Administrative Amendments or Business Corporation Law (e.g., board resolutions, plans of merger, draft articles of merger, etc.)?

l. Does the Form A describe any plans or proposals for which the applicant might have to declare an extraordinary dividend, to liquidate the insurer, to enter into material agreements (including affiliated agreements), to sell the insurer's assets, to merge the insurer with any person or persons, or to make any other material change in the insurer's business operations, corporate structure, or management?

m. Consider suitability of any new affiliated and non-affiliated material agreements, including managing general agents, third party administrators, any professional organizations and reinsurance arrangements.

n. ~~Consider plans for technological interfacing with new affiliates and any potential adverse impact on operations including claims.~~Review the applicant's plans for integrating IT systems, data, and platforms to identify potential operational disruptions or increased exposure to cybersecurity threats.

i. Confirm the applicant has a defined timeline and strategy for migrating data and systems, including ensuring that data and systems to be migrated are evaluated for compliance with the group's cybersecurity risk management framework prior to integration.

ii. Verify that the costs associated with system integration, software licensing, and cybersecurity upgrades are explicitly factored into financial projections.

iii. Confirm that the applicant has a plan to maintain normal policyholder service and claims handling during the technology transition period.

iv. Identify if the integration relies on third-party service providers (e.g., cloud services, TPAs, MGAs, or other vendors) for core insurance operations and ensure the applicant has formal contracts or service agreements to govern relationships, including ~~.~~ diligence processes, ongoing contractual oversight, and concentration risks.

v. Assess the group's cybersecurity risk management framework, including identification, mitigation, and monitoring of exposures specifically related to system integration. Identify any potential concerns such as vague risk disclosures, recurring cyber incidents, limited evidence of security testing, or lack of clear corporate oversight of cybersecurity exposure.

~~i.~~vi. Consider how vertical integration (e.g., internal technology, shared data management, or centralized administrative services) may create concentrated risks, such as single points of failure, increased internal attack surfaces, legacy system vulnerabilities, or complex data flows across affiliates.

~~n.~~o. Require Form D filings for any affiliated material transactions, post-acquisition; consider including language in the approval order.

~~o.~~p. Consider with disfavor any plans to liquidate the target or sell its assets, consolidate or merge, that may be unfair, unreasonable, or hazardous to policyholders.

~~p.~~q. Review required statutory deposits and authorized lines of business.

~~q.~~r. Has the insurance department identified any reasons or circumstances surrounding the transaction to warrant the hiring of outside experts or consultants?

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

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

SPECIFIC PROCEDURES FOR COMPLETING THE INSURANCE HOLDING COMPANY ANALYSIS

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

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

Additional Procedures on Key Risk Areas – Insurance Holding Company System

The following are available procedures that the lead state may consider performing in analyzing the financial condition of the holding company in part or in total to address current or prospective risks at the discretion of analysts, depending on the level of concern, the area in which the risk was identified, and the degree of interdependence within the holding company entities.

Analysts should use his or her judgment in determining if any of the following procedures should be applied to the group analysis, where the primary input for determining what is appropriate would depend on sophistication, complexity and overall financial position of the insurance holding company system. Documentation of the results of holding company analysis is in the GPS. After each additional procedure, examples of the branded risk classification(s) that may be associated with the procedure have been referenced in parentheses for use in mapping the procedures to branded risk classifications in the GPS.

1. Review the distribution of the insurance holding company's invested assets in order to assess the overall asset quality and note any shift in the mix. (CR, MK, LQ, ST)
2. Is the insurer(s) the only member(s) or the primary member(s) of the insurance holding company system that holds cash and invested assets? (CR, MK, LQ, ST)
3. If there are significant investments in non-investment grade bonds, unlisted stocks, mortgages, real estate or other invested assets, review the supporting schedules in greater detail to determine exposure to default, credit, and liquidity risk. (CR, MK, LQ, ST)
4. Review the distribution of the non-invested assets, and assess the overall collectability risk. (CR, LQ)
5. Review the level of goodwill and intangible assets. Determine the level of goodwill and intangible assets relative to the value of equity. (LQ, OP) If significant, summarize the following:
    a. Nature of intangible assets
    b. Change or trend in goodwill
    c. Source of goodwill
    d. Impairment of goodwill

6. Assess whether the insurance holding company system is reliant on the insurance operations for any of the following (LQ, ST):
    a. Service debt
    b. Provide financing
    c. Provide revenue streams
    d. Provide services and/or facilities/equipment
    e. Provide guarantees for the benefits of its affiliates
    f. Pledge assets for the benefit of its affiliates
    g. Contingently liable on behalf of its affiliates
7. Has debt shown an increasing pattern? If “yes,” explain any unusual changes. (ST)
8. Determine the level of insurance holding company debt and its relative value-to-equity. (ST, LQ) If significant, summarize the following:
    a. Type of debt
    b. Terms of the debt covenants
    c. Maturity schedules
    d. Interest payment schedules
    e. Ability to meet payments (e.g., principal and interest)
    f. Business purpose
9. Review the insurance holding company system’s commitments and contingent liabilities.
    a. Has the insurance holding company been subject to substantial complaints, class action lawsuits or other litigation or investigations? If "yes”, document the nature and outcome of those matters. (RP, LG)
    b. Are any contingencies expected to have a material impact on the financial condition of the insurance holding company? If so, document whether the holding company estimated the potential costs and established a reserve liability. (RV, LG)

10. Gain an understanding of and document the use of collateral across the holding company system. (ST, LQ).

11. Evaluate the group-wide cybersecurity exposures including the potential impact of vertical integration and third-party dependencies on the group's exposures (utilizing available group disclosures such as ORSA, Form F, and CGAD).

    a. Assess the group's cybersecurity risk management framework, including identification, mitigation, and monitoring of exposures. Identify any potential concerns such as vague risk disclosures, recurring cyber incidents, limited evidence of security testing, or lack of clear corporate oversight of cybersecurity exposure.

    b. Consider how vertical integration (e.g., internal technology, shared data management, or centralized administrative services) may create concentrated risks, such as single points of failure, increased internal attack surfaces, legacy system vulnerabilities, or complex data flows across affiliates.

    c. Evaluate the group's reliance on third-party service providers (e.g., cloud services, TPAs, MGAs, or other vendors that may be affiliated or non-affiliated) for core insurance operations, including due diligence processes, ongoing contractual oversight, and concentration risks.

    ~~c.~~

Financial Position

~~10.~~12. Review the insurance holding company's statement of shareholders' equity. (ST, OP)

a. Has equity decreased from the prior year or deteriorated over the past three years? If "yes," describe the reason(s) for the decline.

b. Does the net worth of the insurer(s) represent the total net worth or the majority of the net worth of the insurance holding company system?

c. Is the net worth of the insurance holding company system less than the net worth of the insurer(s)?

~~11.~~13. If publicly traded, review the changes in the insurance holding company's outstanding common stock. Document and understand the nature and business purpose of the following: new stock issuance; stock repurchase, stock split, short sales, or change in major exchange listings. (ST)

~~12.~~14. Have any insurer(s) of the insurance holding company paid extraordinary dividends upstream? If "yes":

a. Assess the nature of the dividends and the amount of dividends paid in relation to prior year surplus to determine the materiality of the insurance company dividends. (OP, ST)

b. Compare current year extraordinary dividends to prior year dividends to identify any excessive trends in payments. (ST)

~~13.~~15. Review the revenue of the group.

a. Identify each business segment as identified on the 10K, and review the net income from each. Discuss any notable changes in performance. Are there any business segments that are troubled or pose unusual risks to the insurance holding company system? (PR/UW, ST)

    i. Is the insurer(s) the only or primary revenue producer within the insurance holding company system?

    ii. If affiliates produce net income independently of the insurer(s), what percentage of total net income is produced independently of the insurer(s)?

b. Has the insurance holding company entered into any new lines of business or types of non-insurance business or discontinued any business? (ST, OP)

c. Has the volume of business increased or decreased significantly over the prior year? If "yes," explain the reason for the change. (ST, OP)

~~14.~~16. If the insurance holding company group places a significant amount of gross business with reinsurers, assess the following regarding reinsurance agreements:

a. Risk transfer (CR)

b. Collateralization to unauthorized reinsurance (CR)

c. Recent reinsurance transactions (CR, ST)

d. Credit quality of the reinsurer (CR)

e. Collectability of recoverables (CR)

f. Level of surplus aid (ST)

~~15.~~17. The annual group capital calculation (GCC) is a new analytical tool. To gain an understanding of the framework and results provided in the filing:

a. Follow the five procedure steps as outlined in VI.H. Group-Wide Supervision – Group Capital Calculation (Lead State) Procedures to review and document the results of the GCC.

b. Review the background information and context concerning the issues/considerations an analyst should consider when using the GCC for an insurance holding company group that completed the GCC where required as provided in VI.I. Group-Wide Supervision – Group Capital Calculation (Lead State) Analyst Reference Guide.

Profitability

~~16.~~18. Review investment income and realized capital gains and losses.

a. Has net investment income increased or decreased significantly over the prior year? If "yes," explain the reason for the change. (ST, MK)

b. Document the amount of investment income by sector that is attributed to dividends received from insurance subsidiaries. (ST)

c. Document the annual investment yield. Has the yield decreased materially over the prior year? If "yes," explain the reason(s) for the change. (ST, CR, MK)

d. Review the components of investment income. Has investment income from any asset category changed significantly over the prior year? If "yes," explain the reason for the change. (ST, CR, MK)

e. Did the insurance holding company report material realized capital gains/losses? If "yes," identify the cause of the loss. (ST, CR, MK)

~~17.~~19. Review all other sources of revenue, and note any material changes or weaknesses. (PR/UW, ST)

~~18.~~20. Review expenses.

a. Have losses increased or decreased substantially over the prior year? If "yes," explain the reason for the change. (RV)

b. Have administrative and other expenses increased significantly over the prior year? If "yes," explain the reason for the change. (OP)

c. Summarize the loss and expense ratios by line of business for material insurance lines and review the trend. (OP, RV, PR/UW)

~~19.~~21. Has the insurance holding company reported any non-recurring revenues or expenses that materially inflate or reduce earnings? If "yes," describe the reason for the revenue or expense. (ST, OP)

~~20.~~22. Did the insurance holding company report income or losses from discontinued operations? If "yes," summarize the nature of those operations and evaluate the earnings from those operations. (ST, OP)

~~21.~~23. Examine cash flow and document if there has been a negative trend in operating, investing, or financing activities over the past year or the past three years. (LQ)

~~22.~~24. Evaluate any downstream payments and explain the reason(s) for the downstream contributions. (LQ)

PROCEDURES #1 - 3 assist analysts in reviewing the invested assets of the group, noting any significant increases or decreases from the prior reporting period. Identify the most significant concentration of assets, and review the quality distribution of the asset portfolio. Assess the group's asset risk including credit, default, sector, and/or concentration risk. Include a review of affiliated ownership and any upstream holdings.

PROCEDURES #4 - 5 assist analysts in reviewing the non-invested assets of the group, noting any significant increases or decreases from the prior reporting period. Assess the group's exposure to risk related to high recoverable and receivables and miscellaneous balances. Also, assess the risk related to any miscellaneous assets such as goodwill or other intangible assets.

PROCEDURES #6 - 10 assists analysts in reviewing the liabilities of the group, noting any significant increases or decreases from the prior reporting period. Determine if debt exists at the holding company level that may be material and could affect the insurance companies. Debt includes not only long-term debt financed through the issuance of bonds, but also includes other long-term debt granted by a financial institution, as well as short-term vehicles such as commercial paper, repurchase agreements or bank credit facilities. Consider all types of debt arrangements when determining the amount and timing of cash flow payments.

PROCEDURE #11 assists analysts in evaluating group-wide cybersecurity exposure and operational resilience of the holding company system. Specifically, the procedure provides guidance to assess the maturity of the group's technology risk governance, identify concentrated risks stemming from vertical integration ~~(e.g., single points of failure across integrated affiliates or non-affiliates), and evaluate the group's reliance on~~or third-party service providers ~~for core insurance operations~~.

- **Vertical Integration**—When an insurance group brings core operations such as distribution, claims processing, or IT infrastructure in-house under shared affiliate structures, it creates single point of failure risks. A cyber incident at one affiliate can simultaneously disrupt operations across all operating insurers in the group. Shared active directories and centralized data flows increase the internal attack surface, allowing threats to move laterally into core financial and policyholder systems.
- **Third-Party Service Providers**—Heavy reliance on cloud service providers, MGAs, TPAs, or specialized software introduces supply chain risk. Outages or breaches at critical service providers can disrupt premium collection and claims processing, which in turn can create operational stress on the insurer, even if the insurer's own systems remain secure.

PROCEDURES #~~11~~ 12 - ~~13~~ 14 assist analysts in reviewing the holding company's overall financial position. Holding company equity is usually reported on a GAAP consolidated basis and represents the retained earnings of the holding company and its ownership share of the equity of its subsidiaries.

The initial focus of insurance holding company analysis centers on the current level of equity. The amount of equity is primary in evaluating the organization's capacity to write business and its ability to cover unanticipated loss payments and expenses, uncollectible premiums and receivables, and capital losses to invested assets. Analysts should take note of the trend over past reporting periods and the factors that have significantly influenced an increase or decline.

PROCEDURES #~~14~~ 15 - ~~15~~ 16 assist analysts in reviewing the operations of the group. A required component of certain holding company filings, including SEC filings, is the reporting of premium or other non-insurance business segments. The segment disclosure is fairly broad, including information for each segment on net income, total revenue, and total assets. This information is helpful because it provides analysts with information that management considers in evaluating the results of the entire organization. Reporting segments may include:

- **Operational**—This segment reports the holding company results by categories such as property/casualty, life, bank, non-insurance, or financing and may describe the major operational divisions.
- **Special Sectors**—This segment may identify writing categories or specific lines of business in which an organization specializes. Examples include program business such as artisan contractors.
- **Geographic Concentrations**—Some organizations report their results according to the geographic areas in which the insurance coverage is written or the location of the controlling branch office. This is a fairly common type of reporting for international organizations.
- **Managing General Agents (MGA) and Third-Party Administrators (TPA)**—This segment identifies business produced by MGAs or TPAs. For additional information regarding MGAs and TPAs, refer to Part III. Analyst Reference Guide—Operational Risk.

Analysts should focus on the overall profitability of the segments as well as the stability of earnings over a period of time. To the extent that the segment has reported inconsistent earnings or has reported any losses, analysts may wish to obtain a greater understanding of the causes.

Review the insurer's overall plan of operations, including mission statement, business plan, financial projections, marketing strategies, investment policy and management's philosophy.

- **Mission Statement**—Overall focus and philosophy is clearly stated.
- **Business Plan/Financial Projections**—Determine whether the group has a current business plan that includes details on its primary lines of business and growth strategies, geographic focus, and a plan of operation that contains the group's annual financial and marketing goals. Determine that the group has projected future financial results that appear reasonable based on the variances between plan versus actual results.
- **Marketing Strategies**—Determine whether the group has in place a viable marketing plan that outlines the methods of marketing its products and services, (e.g., direct marketing, agent force, managing general agents, projected sales growth, geographic strategies, and the development and sales of new products).
- **Investment Policy**—Determine the methodology of investment practice, (e.g., investment pool, investment manager, and investment consultants). Ensure that the domestic insurer is in compliance with state investment laws. Evaluate management's philosophy on high-risk securities, affiliated investments (both insurance and non-insurance), and asset and liability matching.
- **Management's Philosophy**—Gain an understanding of the group's culture, management's expertise, and management's future vision of the group.

Determine whether the reinsurance programs in place support the overall risk profile of the group. Determine whether significant errors exist relating to the accounting for reinsurance. Review reinsurance recoverables for materiality and collectability. Identify whether reinsurance between affiliates within the group involve any unusual shifting of risk from one affiliate to another. Determine whether any of the companies within the group are using reinsurance for fronting purposes, and if so, whether any potential problems exist.

PROCEDURE #~~16~~ 17 assist analysts in gaining insight into the background, context, and framework of the GCC analytical tool. The procedure primarily instructs the analyst to refer to the specific procedures provided in VI.H.

Group-Wide Supervision – Group Capital Calculation (Lead State) Procedures in reviewing and documenting the results of the GCC. However, before proceeding with these steps, it is recommended the analyst follow the background information outlined in VI.I. Group-Wide Supervision – Group Capital Calculation (Lead State) Analyst Reference Guide.

PROCEDURES #~~17~~ 18 - ~~21~~ 22 assist analysts in evaluating the profitability of a holding company, which is measured by its ability to generate earnings and reported on a consolidated basis as net earnings (loss). The earnings statement includes revenues and expenses and the contributing factors to net income. Attention should be focused on special reporting items such as earnings or expenses from discontinued operations. Losses from discontinued operations may represent a significant source of drain on the holding company's earnings. These operations should be investigated thoroughly to identify the types of operations involved, expected durations, and their impact on holding company earnings.

PROCEDURES #~~22~~ 23 - ~~23~~ 24 assist analysts in reviewing a group's cash flow. The three primary sections within a holding company cash flow statement include cash from operating, investing, and financing. These categories detail the cash inflows and the expenses associated with the activities of the holding company.

A positive cash flow from operations is essential to the continued financial stability of a holding company. A negative cash flow from operations or a negative cash flow trend could present a drain on assets.

Analysts should assess the level of liquid assets to current liabilities to determine the proper matching of assets to claims obligations. Analysts should also assess the material risk associated with low-quality assets and understated reserves.

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

Yellow Highlights – Changes recommended by Commentors that Staff supports accepting.
Grey Highlights – Edits recommended by Staff.

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

ANNUAL CREDIT RISK ASSESSMENT

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

Exposure to Private Credit Securities, Level 3 Securities, and Bonds with Private Letter Ratings

In recent years, the insurance industry has seen an ongoing increase in the amount and diversity of private fixed income investments held by U.S. domestic insurers. Private fixed income encompasses a broad range of asset types, including traditional investment-grade private placements, private structured assets, direct lending, and other credit-oriented investments. Many of these investments have been longstanding components of insurer portfolios and are generally well suited to insurers' long-duration liabilities and investment horizons.

The ability to invest in less liquid assets is a structural feature of the insurance business model and allows insurers to earn an illiquidity premium while continuing to meet policyholder obligations. While certain newer and more complex private credit structures may warrant enhanced regulatory attention, analysts should distinguish between ~~traditional~~ private placements and emerging private credit strategies when assessing credit risk exposures.

Potential areas of focus may include investments that involve heightened complexity, limited transparency, reliance on unobservable valuation inputs, private letter ratings, or nontraditional structures.
~~In recent years, the insurance industry has seen an ongoing increase in the amount of private assets held by U.S. domestic insurers, including securities with NAIC designations supported by private letter ratings and securities that are valued based on Level 3 (unobservable) inputs.~~

While this increase is generally consistent with the broader capital markets trend of increased issuance of private assets, their relative opacity versus other asset types ~~the potential lack of transparency related to private assets~~ can complicate the assessment of credit quality and reduce the liquidity of the portfolio.

Private credit generally refers to privately negotiated debt or debt-like investments that are not ~~broadly syndicated or~~ publicly traded. The asset class encompasses a wide range of investment strategies and structures, including ~~traditional~~ private placements, direct lending, private structured assets, asset-based finance, infrastructure debt, commercial real estate debt, and other privately originated credit investments. Asset-based finance encompasses a broad range of transactions secured by identifiable collateral and may exhibit substantially different risk characteristics depending on asset quality, structure, leverage, and credit enhancement features. Therefore, ~~A~~analysts should evaluate asset-based finance exposures based on underlying risk characteristics ~~rather than treating all such investments as a single risk category~~.

While some private credit strategies focus on middle-market corporate lending, the asset class is considerably broader and includes many investment-grade exposures that have long been utilized by insurance companies. Accordingly, analysts should avoid treating all private credit investments as having similar risk characteristics and should consider the underlying credit quality, structure, transparency, and valuation methodology of the investment.

~~Private credit generally refers to debt, or debt-like, securities that are not publicly issued or traded. Private credit is an evolving, alternative funding source. Non-bank lenders, including insurance companies, private debt funds, and business development companies, issue private loans directly to mostly small and middle-market companies that do not have—or have limited—access to the public corporate bond and loan markets. These small middle-market companies often have more debt than larger companies that access capital via leveraged loans and public bonds and, therefore, are more susceptible to economic downturns and the impact of rising interest rates.~~

~~Private credit has~~ "Private credit" describes a variety of strategies that include direct lending, distressed debt, venture debt, mezzanine finance, and special situations. ~~Direct~~According to Morgran Stanley Investment Management~~ ~~~~, direct lending comprised 52%[1] ~~is the largest segment and accounts for about 40%~~ of the U.S. private credit market as of Sept. 30, 2025. The largest investors in private credit are typically pension funds, insurance companies, and sovereign wealth funds. While direct lending to corporate issuers is the simplest and most common strategy, ~~type of private credit, it is evolving into~~ more complex investments like feeder fund structures, ~~private credit~~ middle market CLOs with private letter ratings, and asset-based financing (where loans are secured by collateral such as inventory, receivables, equipment, or property) are expanding.

Risks and mitigating factors include:

- Less liquidity: Private credit is generally issued directly by a non-bank lender or a small group of lenders, resulting in a relatively illiquid market where secondary trading is limited.
- Less transparency: The availability of information about a private credit security is often contractually restricted, which contributes to lower transparency compared to public securities and can make it more difficult to assess credit risk and determine appropriate valuation.
- Less frequent pricing: Private credit may be subject to less frequent valuation and pricing; and it may rely on third-party valuations and/or modeling~~, which may be subjective~~.
- ~~Assessment of credit quality:~~
    - ~~While lack of transparency can make credit quality more difficult to assess, private credit lenders can often benefit from stronger control over documentation than lending through a syndicate of banks and are able to customize terms of the transaction given their direct relationship with borrowers. In the event of stress, lenders and investors should be able to work directly with the borrower to modify the transaction terms or add investor safeguards.~~
    - ~~Private credit also has the potential to provide a broader pool of debt issuers that results in portfolio diversification.~~
- ~~Future performance~~Risk/Reward Optimization:
    - Private credit generally offers higher spreads and yields than public corporate bonds and loans to compensate investors for the relative market illiquidity (lack of a secondary market) and complexity depending on the transaction type.

[1] 52% as of September 2026 per Morgan Stanley Investment Management

- ~~As the nature of private credit evolves and expands, there is no assurance that current/historical performance trends (largely favorable) will continue. The solid historical performance of private lending may not be comparable performance as the market grows and as new entrants change focus to non-traditional alternative assets and more challenging and stressed credit environments occur, particularly higher interest rates.~~
- Enhanced covenant protections and documentation relative to broadly syndicated lending markets.
- Greater ability for lenders to negotiate transaction-specific terms and monitor borrower performance.
- Diversification benefits through access to issuers and asset types not available in public markets.
- Structural protections, including collateralization, overcollateralization, cash flow controls, and other credit enhancements depending on the investment structure.
- Historical performance in certain private credit segments that has demonstrated recovery characteristics comparable to or stronger than similar public market exposures.

Refer also to guidance published by the NAIC Capital Markets Bureau on private credit and its characteristics.

Note that the Annual Statement includes new disclosures and reporting requirements to improve the identification of different types of private placements. For year-end 2026, insurers will be required to disclose the SEC registration status for each investment: public, Rule 144A, private placements (defined to include Regulation D, Section 4(a)(2) exempt or other exclusion from SEC registration), or not applicable because the investment is not within the scope of the Securities Act of 1933. An aggregate disclosure in Note 5.T—Private Securities to capture key data by each grouping of investments by registration status to allow for ease of regulator review. The reporting will be provided in an electronic column in all investment reporting schedules (held, acquired, disposed) for short-term investments, cash equivalents, issuer credit obligations, asset-backed securities, common stock, preferred stock and other long-term investments.

Fair Value Measurement Hierarchy

An important element in evaluating risks associated with valuation of private investments (equity or credit) is the level of input available to determine fair value. To increase consistency and comparability in fair value measurements and related disclosures, the fair value hierarchy (see SSAP No. 100) prioritizes the inputs to valuation techniques used to measure fair value into three broad levels. The fair value hierarchy gives the highest priority to quoted prices (unadjusted) in active markets for identical assets (Level 1) and the lowest priority to unobservable inputs (Level 3).

- **Level 1** inputs are quoted prices (unadjusted) in active markets for identical assets that the reporting entity has the ability to access at the measurement date.

- **Level 2** inputs are inputs other than quoted prices included within Level 1 that are observable for the asset, either directly or indirectly. Level 2 inputs might include quoted prices for similar assets in active markets, quoted prices for identical or similar assets in inactive markets, or prices derived from inputs that are observable (e.g., interest rates and yield curves).

- **Level 3** inputs are unobservable inputs for the asset. Unobservable inputs are used to measure fair value to the extent that relevant observable inputs are not available. These inputs often involve significant judgment and estimation, including the use of internal models and assumptions.

Information associated with fair value measurement is provided in Note 20 (Fair Value Measurements) of the Annual Statement and can assist regulators in assessing the risks associated with an insurer's private investment holdings. In addition, information on fair value hierarchy reported in the investment schedules can be utilized to identify individual securities warranting additional review.

Private Letter Ratings (PLRs)

Privately rated securities reported by U.S. insurance companies have become more prevalent in recent years. The greater use of PLRs is generally consistent with the overall increase in private credit investments by insurers, particularly life companies. PLRs provide proprietary details of investments and are only communicated to the issuer and a specified group of investors. Therefore, these investments do not benefit from the market validation that comes from market transparency (multiple investors, publicly viewable ratings, etc.) and often come as a single rating rather than multiple ratings. The NAIC has required insurance companies to submit PLRs for verification since 2018, whereby the NAIC's SVO reviews that the letter submitted is for the appropriate security and the current year. In addition, effective in 2022, insurers are required to file full rating rationale reports for PLR requests with the SVO, to partially mitigate concerns regarding the lack of transparency of PLRs.

Risk assessment procedures should be applied in a manner that distinguishes among:

1. ~~Traditional p~~Private placements and other established private fixed income investments;
2. Emerging or ~~nontraditional~~ more complex private credit strategies, including certain direct lending, feeder funds, privately-rated CLO, and asset-based finance structures; and
3. Investments characterized by ~~elevated~~ valuation uncertainty or limited transparency, including securities primarily reliant on private letter ratings or significant Level 3 valuation inputs.

The presence of a private letter ~~placement~~ designation rating alone should not be viewed as indicative of elevated risk. Analysts should prioritize review of investments exhibiting multiple risk characteristics, including lower credit quality, limited transparency, valuation complexity, concentrated exposures, or ~~nontraditional~~ complex structures.

Procedures / Data

- Review Private Security Code details, Note 5.T disclosures, and available analytical tools to identify concentrations in:
  - Complex private credit structures;
  - Securities backed by private letter ratings;
  - Investments with significant Level 3 valuation inputs;
  - Below-investment-grade or unrated private credit exposures; and

- Asset classes exhibiting elevated complexity, opacity, or valuation uncertainty.

- When evaluating private placements, analysts should consider credit quality, diversification, and performance characteristics and avoid relying solely on registration status as an indicator of risk.

~~Review the Private Security Code details in the investment schedules, and aggregate private securities information in Note 5.T.; or utilize iSite+ tools, to identify a concentration in private securities.~~

- Ratio of private securities in aggregate, by asset type, and by security code category to total invested assets
- Ratio of private securities in aggregate, by asset type, and by security code category to capital and surplus plus AVR (Life/A&H), to capital and surplus (Health) , and to policyholder surplus (P&C)
- Change in private securities from the prior year

- Review the SVO Administrative Symbols provided for the insurer's bond portfolio on Column 6 of Schedule D, or utilize iSite+ tools, to identify a concentration in securities backed by PLRs (i.e., symbols PL and PLGI).
  - Ratio of securities with PLRs to total invested assets
  - Ratio of securities ~~backed by~~ with PLRs to capital and surplus plus AVR (Life/A&H), to capital and surplus (Health), and to policyholder surplus (P&C)
  - Change in securities with ~~backed by~~ PLRs from the prior year
- Review information provided in Note 20C of the Annual Statement (Fair Value Measurement) or utilize iSite+ tools, to identify the extent investments (by type of financial instrument) have a fair value determined with unobservable inputs (i.e., Level 3 inputs).
  - Ratio of Level 3 securities to total invested assets
  - Ratio of Level 3 securities to capital and surplus plus AVR (Life/A&H), to capital and surplus (Health), and to policyholder surplus (P&C)
  - Change in Level 3 securities from the prior year

Additional Review Considerations

- For insurers with a concentration in bonds with Private Letter Ratings PLRs:
  - ~~Request the support of the NAIC's Securities Valuation Office (SVO) to investigate the rating sources for the securities (with a focus on concentrations with any one rating agency and/or securities with only one rating) and consider the potential impact on the insurer's RBC charges and investment risk exposures.~~
  - Request details from the company on its own internal ratings for securities with ~~backed by~~ PLRs where applicable and compare with rating agency rating for discrepancies.
- If private placements, private credit investments, Level 3 or 2D securities, or assets with PLRs are material, consider inquiring of the insurer its infrastructure and investment management policies and procedures (i.e. portfolio management and credit analyst expertise, including approach to making investment decisions) in place either internally, or via an affiliate, and/or outsourced investment manager, to manage these investments.
- If necessary, consider utilizing an investment specialist to assist in asset valuation considerations.
- ~~If appropriate, consult with or request an Opinion from the NAIC's SVO or Structured Securities Group (SSG) on a specific investment holding or transaction. [A state insurance regulator can ask for SVO or SSG analytical~~

~~assistance with respect to any investment related activity or in connection with an assessment of investment-related aspects of a Regulatory Transaction (defined in the P&P Manual). The department can direct an insurance company to file relevant information with the SVO or SSG for the purpose of that analysis and the SVO or SSG will issue a report back to the department.]~~

- Request a Preliminary Analysis from the NAIC's Capital Markets Bureau (CMB) to assess the insurer's overall portfolio investment risk exposures and suggest additional follow-up procedures that can be performed by the department to address overall portfolio issues identified. Request analytical assistance from the CMB to better understand and measure the investment risks related to a particular asset class, investment-related activity, or market trend.

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

Inadequate Collateral for Mortgage Loan Risk

An important consideration in the analysis of mortgage loans is the adjusted loan-to-value and debt service coverage ratio for each property owned, which are used in the determination of the mortgage's Commercial Mortgage Risk Category and are detailed in the RBC worksheet. Out-of-date appraisals may result in inaccurate valuation, resulting in an undervalued underlying collateral asset.

Procedures / Data

- Review information available in the RBC filing (LR004) and Schedule B detail to identify a concentration in loans with unfavorable debt service coverage (DSC) ratios and adjusted loan-to-values (LTV) (i.e., book value/recorded investment of each loan compared to the value of the land and buildings mortgaged) of the individual mortgage loans to determine whether the mortgage loans, and ~~or~~ in particular office property types (as of 2026) are adequately collateralized.

Additional Review Considerations

- For mortgage loans with interest overdue or in process of foreclosure, review the date of the last appraisal or valuation (Schedule B – Part 1) to determine whether updated appraisals should be obtained.
- If significant or concerning concentrations in mortgage loans with unfavorable DSC or LTV ratios or ~~in~~ office property types are identified, request additional information from the insurer to further assess their credit risk in this area and evaluate any risk mitigation strategies in place.

Traditional investment-grade private placements and mortgage-related investments that are addressed elsewhere in the Handbook generally should not be considered elevated-risk private credit exposures solely because they are privately originated, privately negotiated, or less liquid than comparable public securities. Additional scrutiny should focus on investments exhibiting heightened complexity, valuation uncertainty, lower credit quality, or nontraditional structures.

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

Credit Quality of Assets Supporting Collateral Loans (Life/A&H Insurers)

The procedure assists analysts in determining whether concerns exist due to the level of investment in collateral loans. Collateral loans are unconditional obligations for the payment of money secured by the pledge of an investment. ~~They are subject to the same market and credit risks as their underlying collateral but are likely even~~

~~riskier given their illiquid and less transparent nature.~~ While collateral loans are exposed to the market and credit performance of their underlying collateral, they are debt instruments that incorporate structural credit enhancements, including overcollateralization, diversification, cross-collateralization, and lender protections, which reduce economic risk relative to direct ownership of the underlying assets. Market conditions such as rising interest rates and market volatility can impact the value of the underlying collateral and, in turn, an insurer's ability to fulfill policyholder obligations. However, interest rates, while still relatively high (as of 2026), were lowered for the first time in almost a year, and collateral loans are not a core investment for U.S. insurance companies. While collateral loans are exposed to the market and credit performance of their underlying collateral, they are debt instruments that incorporate structural credit enhancements, including overcollateralization, diversification, cross-collateralization, and lender protections, which reduce economic risk relative to direct ownership of the underlying assets. ~~While collateral loans represent less than 1% of U.S. insurers' total cash and invested assets industry-wide, for private-equity-owned insurers, collateral loans are typically a larger proportion of their total cash and invested assets as compared to the overall U.S. insurance industry.~~ Analysts should review Annual Financial Statement, Schedule BA. In most states, collateral loans are required to be secured or collateralized by assets which have a value in excess of the amount of the loan and which are considered admitted assets for an insurer.

Procedures / Data

- Review the following ratios to determine the level of concentration in collateral loans.
  - Ratio of collateral loans to total net admitted assets.
  - Ratio of collateral loans to capital and surplus plus AVR.

Additional Review Considerations

- Compare the fair value of the collateral to the amount loaned to determine whether the loan is adequately collateralized. In those instances where the underlying collateral is comprised of securities, analysts might consider verifying the rate used to obtain the fair value of the securities by referencing the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* (P&P Manual).
- Review Annual Financial Statement, Schedule BA – Other Invested Assets Owned and perform the following for each such loan:
  - Determine whether the collateral for the loan is invested in a quality asset.
  - Determine whether the collateral loan is to an officer, director, parent, subsidiary, or affiliate.

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

Impairment of Invested Assets Exposed to Climate Change and/or Transition Risk

Identify and assess the potential exposure of the insurer's investment portfolio to the impact of material climate change and/or energy transition risks. Transition risks refer to stresses on certain investment holdings arising from the shifts in policy, consumer and business sentiment, or technologies associated with the changes necessary to limit climate change. A few examples of investment holdings and sectors generally subject to greater levels of transition risk include oil/gas, transportation, heavy manufacturing, and agriculture. The insurer's investment portfolio is subject to prospective devaluation or impairment of the assets or changes in the asset return associated with its holdings of climate-affected assets.

Procedures / Data

- Review the information disclosed by the insurer in its responses to the NAIC's Climate Risk and Disclosure Survey (if available) on its exposure to material climate change/energy transition risk and related mitigation activity in this area.
- Review other relevant information provided in the Own Risk and Solvency Assessment (ORSA) Summary Report, and/or U.S. Securities and Exchange Commission (SEC) 10K or 10Q filings (if available) that discusses the insurer's exposure to material climate change/energy transition risk and related mitigation activity in this area.
- Review results of basic scenario analysis conducted by the NAIC using insurers' Annual Statement filings in the NAIC's U.S. Insurance Industry Climate Affected Investment Analysis to identify potential concentrations in insurer exposure.
- Review the Climate Affected Assets Dashboard to assess an insurer's exposure to assets that might be subject to transition risk in the coming years. The dashboard allows the user to view an individual insurer's investment portfolio as of year-end, which has been classified into buckets of climate affected assets (i.e., Fossil Fuel, Energy Intensive), with the ability to view those categories as a percentage of the overall portfolio. Companies that do not have assets subject to transition risk (i.e., Treasuries, Cash) will not be included.

Additional Review Considerations

- Review the insurer's investment policies and strategies to assess whether material climate change, transition and asset devaluation risk considerations have been appropriately implemented into the investment processes.
- Review the most recent examination report and summary review memorandum (SRM) for any findings regarding climate change/energy transition risks.
- If concerns exist, consider requesting information from the insurer regarding its management of exposure to material climate change/energy transition risk, including how it identifies and estimates current and prospective exposures and the limits (if any) in place to avoid concentrations.

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

Credit Quality, Adequacy and Appropriateness of Assets Held for Modco or FWH Agreements (Life/A&H Insurers)

Concerns may exist regarding the quality, adequacy and appropriateness of assets held to support Modified Coinsurance (Modco) or Funds Withheld (FWH) reinsurance, particularly as investments become increasingly complex. Concerns may include controls and governance over investment practices, valuation and ratings of assets, and if material amounts of assets involve related party transactions.

Where collateral held is related to Modco and FWH reinsurance, the analyst should review the information in Note to the Financials #5L(1), #5L(4) and #5L(5), and Schedule S—Part 8—Reinsurance Agreements with Funds Withheld and Modified Coinsurance, in conjunction with other credit, operational and strategic risk of the insurer's reinsurance program. Additionally, review the analysis considerations related reserve reporting required by AG 53 (complex assets) and AG 55 (assets supporting reinsurance) outlined in the Reserving Risk Assessment and SOA procedures and guidance.

Where the company is engaged in material Modco and FWH arrangements, the analyst can use the detail of collateral received and held under Note 5L(4) to identify the types of assets held by investment schedule, and gain an understanding of the materiality of aggregate BACV of the collateral received to the insurer's asset portfolio. Further, the Note #5L(5) disclosure identifies if securities held as collateral under Modco or FWH agreements are also pledged under other arrangements, in which case they would not be for the benefit of the reinsurer or available to fulfill the liabilities of the reinsurance contract. The analyst can use the information in Schedule S—Part 8 to identify any concerns with the types of assets and credit quality of assets held under ceded or assumed Modco or FWH agreements.

Procedures / Data

- Identify the types of reinsurance agreements and jurisdiction of the reinsurer [Annual Financial Statement, Schedule S – Part 3] and determine if concerns may exist over the adequacy and quality of assets held by reinsurers in support of ceded reserves that may require further analysis or inquiry to the insurer.
- Compare the BACV of the collateral received and assets held under Modco/FWH Reinsurance Agreements to the recognized obligation for Modco and FWH assets. [Annual Financial Statement, Notes to the Financials #5L(4)(m and n)].
- Identify if investments held under FWH agreements (including Modco) are related to the Modco/FWH reinsurer [Annual Financial Statement, Notes to the Financials 5L(5)(o-v)].
- Identify if the insurer is engaged in ceding business under Modco and FWH agreements with offshore reinsurers.
    - Gain an understanding, through review of Schedule S - Part 3, of the types of insurance business ceded, the reinsurer's jurisdiction, if affiliated or non-affiliated, and applicable collateral requirements by type of reinsurer (i.e. authorized, unauthorized, reciprocal jurisdiction, certified)
- Review Schedule S – Part 8 to determine if concerns exist regarding the types of assets held or the credit quality of assets held under Modco/FWH agreements. Consider if the aggregate of medium or lower quality assets held represent a material amount of the related Modco/FWH liabilities.
    - Review Schedule S – Part 8 in comparison to Life RBC (asset schedules) to ensure asset subtotals match. If differences exist, inquire of the insurer, as differences may have an impact on the RBC calculation.
- Determine if assets held under Modco or FWH agreements are also pledged under other agreements [Annual Financial Statement, Notes to the Financials #5L(5)].

- Determine if assets held under Modco or FWH agreements contain a material amount of private credit assets or related party investments (or related to the reinsurer managing the portfolio). If so, consider additional procedures in the Private Credit section above and/or Related Party section below.

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

Collectability or Default of Investments Involving Related Parties

Determine related party exposure in the investment portfolio and assess any related credit risk.

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

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

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

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

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

Procedures / Data

- Review the Annual Financial Statement investment schedules, as disclosed in the column "Investments Involving Related Parties" and utilizing iSite+ tools, determine if the insurer has material related party exposures in its investment portfolio. This disclosure is included in:
  - Schedule B – Part 2
  - Schedule BA – Part 2
  - Schedule D – Part 1, Sections 1 and 2
  - Schedule DA – Part 1
  - Schedule DB – Part A Section 1
  - Schedule DL – Part 1 and 2

- Schedule E, Part 2

Consider exposure by asset class and in aggregate, and by the role of the related party in the investment as designed by the "Investments Involving Related Parties" disclosure.

- If concerns exist regarding a material related party exposure in the investment portfolio, assess the credit quality of those investments and assess any historical default experience.
- Determine if related party investments include a material amount of private credit assets (e.g. related investment manager or related reinsurer managing the Modco/FWH reinsurance assets). If so, consider additional procedures in the Private Credit or Modco/FWH sections above.

Yellow Highlights – Changes recommended by Commentors that Staff supports accepting.
Grey Highlights – Edits recommended by Staff.

LIQUIDITY RISK: Inability to meet contractual obligations as they become due because of an inability to liquidate assets or obtain adequate funding without incurring unacceptable losses.

The Liquidity Risk Assessment is focused primarily on overall liquidity, liquidity of investments, receivables, and cash flow from operations. In analyzing liquidity risk, analysts may analyze specific types of investments and receivables held by insurers. An analyst's risk-focused assessment of liquidity risk should take into consideration the following areas (but not be limited to):

- Liquidity ratios/metrics
- Liquidity of certain investments with ~~shallow markets~~ limited trading and limited public information, such as: private credit securities, including private placement bonds~~,~~; ~~and~~ common stock~~,~~; highly structured investments~~,~~; investments on Schedule BA~~,~~; and affiliated investments
- Liquidity of certain receivables, including health care receivables and special deposits
- Cash flow from operations
- Stockholder dividends
- Surrender and withdrawal activity for life insurers

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

Impact of Market Volatility on the Liquidity of the Aggregate Investment Portfolio

An important consideration when markets experience significant volatility and strains is the potential negative impact may not be on just one or a small number of investments held by insurers. Rather, market strains can have a significant impact on an entire asset class, several asset classes, or the entire investment portfolio. Particularly vulnerable are asset classes ~~that represent smaller~~ in markets that are typically less liquid, are ~~more~~ structurally complex or are assets that would be considered ~~less traditional~~ atypical for insurers. Therefore, state insurance regulators should consider the potential impact of significant market challenges on different asset classes in the investment portfolios of insurers.

Procedures

- Review and monitor material asset classes for significant changes in fair value and/or significant changes in relative liquidity. Utilize data in the Annual Statement, Financial Profile, Snapshot Investment Summary and investment dashboards. Also refer to specific liquidity guidance in this chapter on asset groups such as bonds, BA assets and mortgage loans. Do not limit considerations to one asset class but also consider

the aggregate of all such vulnerable asset classes. Examples of asset groupings that may represent notable exposures in insurer portfolios and that should be considered are:

- Below investment grade bonds (rated below BBB-/baa3).
- ~~Weaker investment grade ("BBB" rated) bonds.~~
- Commercial mortgage loans, ~~particularly~~ for example office properties (in the current market as of 2026).
- Mezzanine loans.
- Real estate equity.
- Structured securities, especially collateralized loan obligation (CLO) tranches (including CLO Combo Notes and Middle Market CLOs).
- Residential mortgage-backed securities (RMBS), specifically as to cash flow variability.
- Emerging markets investments.
- Hedge funds.
- Private equity funds.
- Private credit, including private placements (specifically non-144A) and private letter ratings.
- Derivatives transactions.
- Concentrations in exposure to sectors impacted by the current market, currently the auto, technology, consumer products and retail sectors, due to technology/software (AI), and energy, due to high oil prices ~~the potential impact of tariffs~~.

The ~~significance~~ materiality of these exposures should be evaluated in the context of the insurer's overall risk profile, including applicable NAIC capital requirements associated with the assets. Different situations may call for different materiality standards, so it is important to be able to explain the standard used.

When evaluating the liquidity of less liquid assets, analysts should consider the insurer's broader asset-liability management framework. Life i~~I~~nsurers for example, generally have long investment horizons due to the long-duration and generally predictable nature of their liabilities. Accordingly, insurers actively model asset and liability cash flows to ensure sufficient liquidity is available to meet policyholder obligations as they come due. Insurers generally do not invest in ~~L~~less liquid assets, including private equity, hedge funds, private credit, and commercial mortgage loans, ~~generally are not used~~ for day-to-day liquidity management. Rather, the ability to allocate a portion of the portfolio to ~~such~~ assets is a structural feature of the insurance business model that ~~and~~ can be a source of ~~provide~~ additional investment income~~return~~ while remaining consistent with prudent liquidity management.

- Refer to the Procedures for review of Actuarial Guideline 53 and Actuarial Guideline 55 in the Reserve Risk Chapter for additional related investment liquidity review.

Additional Review Considerations

i. For ~~the~~ identified asset classes ~~above~~, where there is not a readily available or exchange traded market, verify pricing and valuation sources and corresponding valuation methods. Close attention should be given to asset classes like private equity and real estate that usually report on a 3-month lag, as well as private credit whose valuations may be subjective.

ii. Inquire as to how the insurer is managing the potential risk of rating migration. Inquire as to how they may apply a credit rating transition matrix and calculate the resulting increased RBC charges.

iii. Inquire as to how the insurer is managing the above-mentioned challenges and other potential challenges in the investment marketplace. For example, consider the following questions:
   a. How is the insurer managing its liquidity needs given the changes in investment markets, including when/if ~~especially given~~ historically liquid assets may not be as liquid?
      1. How is the insurer managing changes in cash-flow expectations from prepayments (which are more likely when interest rates are decreasing), both generally and specifically associated with structured ~~mortgage-backed~~ securities?
   b. How is the insurer managing significant changes in fair value of portfolio assets, especially for longer dated investments?
      1. Are other-than-temporary- impairments (OTTI) appropriate?
      2. If there is an ongoing risk, should the insurer consider shortening the duration of future investments?

iv. Review the insurer's Liquidity Stress Test submission (if applicable) to evaluate results and assess the insurer's stress testing process and assumptions for reasonableness.

v. Inquire as to how changes in the investment profile (particularly duration) may impact asset/liability matching, asset adequacy analysis and cash-flow testing.

~~vi. Request an Opinion from the NAIC's Securities Valuation Office (SVO) or Structured Securities Group (SSG) on a specific investment holding or transaction. A state insurance regulator can ask for SVO or SSG analytical assistance with respect to any investment related activity or in connection with an assessment of investment-related aspects of a Regulatory Transaction (defined in the P&P Manual). The department can direct an insurance company to file relevant information with the SVO or SSG for the purpose of that analysis and the SVO or SSG will issue a report back to the department.~~

vii. Request a Preliminary Analysis from the NAIC's Capital Markets Bureau (CMB) to assess the insurer's overall portfolio of investment risk exposures and obtain additional follow-up procedures that can be performed by the department to address any overall portfolio issues identified. Request analytical assistance from the CMB to better understand and measure the investment risks related to a particular asset class, investment-related activity, or market trend.

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

Exposure to Private Credit Securities, Level 3 Securities, Bonds with Private Letter Ratings and Unfunded Commitments

In recent years, the insurance industry has seen an ongoing increase in the amount and diversity of private fixed income investments held by U.S. domestic insurers. Private fixed income encompasses a broad range of asset types, including traditional investment-grade private placements, private structured assets, direct lending, and

other credit-oriented investments. Many of these investments have been longstanding components of insurer portfolios and are generally well suited to insurers' long-duration liabilities and investment horizons.

The ability to invest in less liquid assets is a structural feature of the insurance business model and allows insurers to earn an illiquidity premium while continuing to meet policyholder obligations. While certain newer and more complex private credit structures may warrant enhanced regulatory attention, analysts should distinguish between private placements and emerging private credit strategies when assessing credit risk exposures. ~~In recent years, the insurance industry has seen an ongoing increase in the amount of private assets held by U.S. domestic insurers, including securities with NAIC designations supported by private letter ratings and securities that are valued based on Level 3 (unobservable) inputs.~~

Potential areas of focus may include investments that involve heightened complexity, limited transparency, reliance on unobservable valuation inputs, private letter ratings, or nontraditional structures.

While this increase is generally consistent with the broader capital markets trend of increased issuance of private assets, their relative opacity versus other asset types ~~the potential lack of transparency related to private assets~~ can complicate the assessment of credit quality and increase the liquidity risk of the portfolio.

~~Private credit generally refers to debt, or debt-like, securities that are not publicly issued or traded. Private credit is an evolving, alternative funding source. Non-bank lenders, including insurance companies, private debt funds, and business development companies, issue private loans directly to mostly small and middle-market companies that do not have—or have limited— access to the public corporate bond and loan markets. These small middle-market companies often have more debt than larger companies that access capital via leveraged loans and public bonds and, therefore, they are more susceptible to economic downturns and the impact of rising interest rates.~~

~~Private credit has~~ "Private credit" describes a variety of strategies that include direct lending, distressed debt, venture debt, mezzanine finance, and special situations. ~~Direct~~ According to Morgran Stanley Investment Management, direct lending comprised 52%[i] ~~is the largest segment and accounts for about 40%~~ of the U.S. private credit market as of Sept. 30, 2025. The largest investors in private credit are typically pension funds, insurance companies, and sovereign wealth funds. While direct lending to corporate issuers is the simplest and most common strategy, ~~type of private credit , it is evolving into~~ more complex investments like feeder fund structures, ~~private credit~~ middle market CLOs with private letter ratings, and asset-based financing (where loans are secured by collateral such as inventory, receivables, equipment, or property) are expanding.

Risks and mitigating factors include:

- Less liquidity: Private credit is generally issued directly by a non-bank lender or a small group of lenders, resulting in a relatively illiquid market where secondary trading is limited.
- Less transparency: The availability of information about a private credit security is often contractually restricted, which contributes to lower transparency compared to public securities and can make it more difficult to assess credit risk and determine appropriate valuation.
- Less frequent pricing: Private credit may be subject to less frequent valuation and pricing; and it may rely on third-party valuations and/or modeling, ~~which may be subjective~~.

[i] 52% as of September 2026 per Morgan Stanley Investment Management

- ~~Assessment of credit quality:~~
  - ~~While lack of transparency can make credit quality more difficult to assess,private credit lenders can often benefit from stronger control over documentation, as compared to a syndicate of lenders, and are able to customize terms of the transaction given their direct relationship with borrowers. In the event of stress, lenders and investors should be able to work directly with the borrower to modify the transaction terms or add investor safeguards.~~
- Private credit can contribute to an investment portfolio's diversification, with respect to issuers and duration, among other factors ~~also has the potential to provide a broader pool of debt issuers that results in portfolio diversification.~~
- ~~Future performance~~Risk/Reward Optimization:
  - Private credit generally offers higher spreads and yields than public corporate bonds and loans to compensate investors for the relative market illiquidity (lack of a secondary market) and complexity depending on the transaction type.
  - ~~As the nature of private credit evolves and expands, there is no assurance that current/historical performance trends (largely favorable) will continue. The solid historical performance of private lending may not be comparable performance as the market grows and as new entrants change focus to non-traditional alternative assets and more challenging and stressed credit environments occur, particularly higher interest rates.~~
  - Enhanced covenant protections and documentation relative to broadly syndicated lending markets.
  - Greater ability for lenders to negotiate transaction-specific terms and monitor borrower performance.
  - Diversification benefits through access to issuers and asset types not available in public markets.
  - Structural protections, including collateralization, overcollateralization, cash flow controls, and other credit enhancements depending on the investment structure.
  - Historical performance in certain private credit segments that has demonstrated recovery characteristics comparable to or stronger than similar public market exposures.

Refer also to guidance published by the NAIC Capital Markets Bureau on private credit and its characteristics.

Note that the Annual Statement includes new disclosures and reporting requirements to improve the identification of different types of private placements. For year-end 2026, insurers will be required to disclose the SEC registration status for each investment: public, Rule 144A, private placements (defined to include Regulation D, Section 4(a)(2) exempt or other exclusion from SEC registration), or not applicable because the investment is not within the scope of the Securities Act of 1933. An aggregate disclosure in Note 5.T—Private Securities to capture key data by each grouping of investments by registration status to allow for ease of regulator review. The reporting will be provided in an electronic column in all investment reporting schedules (held, acquired, disposed) for short-term investments, cash equivalents, issuer credit obligations, asset-backed securities, common stock, preferred stock and other long-term investments.

Fair Value Measurement Hierarchy

An important element in evaluating risks associated with valuation of private investments (equity or credit) is the level of input available to determine fair value. To increase consistency and comparability in fair value measurements and related disclosures, the fair value hierarchy (see SSAP No. 100) prioritizes the inputs to

valuation techniques used to measure fair value into three broad levels. The fair value hierarchy gives the highest priority to quoted prices (unadjusted) in active markets for identical assets (Level 1) and the lowest priority to unobservable inputs (Level 3).

- **Level 1** inputs are quoted prices (unadjusted) in active markets for identical assets that the reporting entity has the ability to access at the measurement date.

- **Level 2** inputs are inputs other than quoted prices included within Level 1 that are observable for the asset, either directly or indirectly. Level 2 inputs might include quoted prices for similar assets in active markets, quoted prices for identical or similar assets in inactive markets, or prices derived from inputs that are observable (e.g., interest rates and yield curves). Level 2D reflects use of internal models.

- **Level 3** inputs are unobservable inputs for the asset. Unobservable inputs are used to measure fair value to the extent that relevant observable inputs are not available. These inputs often involve significant judgment and estimation, including the use of internal models and assumptions.

When reviewing Level 3 assets, analysts should distinguish valuation classification from credit risk assessment. The fair value hierarchy is intended to identify the nature of inputs used to measure fair value, not to assign a credit risk classification. Therefore, a Level 3 classification reflects the use of a significant number of unobservable inputs and should not be interpreted, on its own, as evidence of elevated credit risk. Certain long-duration insurance assets may have limited observable market inputs but still exhibit stable contractual cash flows and strong credit characteristics. In addition, some assets may be classified as Level 3 because observable valuation inputs are not available at the measurement date, and those assets may subsequently migrate to Level 2 once observable inputs become available.

Information associated with fair value measurement is provided in Note 20 (Fair Value Measurements) of the Annual Statement and can assist regulators in assessing the risks associated with an insurer's private investment holdings. In addition, information on fair value hierarchy reported in the investment schedules can be utilized to identify individual securities warranting additional review.

Private Letter Ratings (PLRs)

Privately rated securities reported by U.S. insurance companies have become more prevalent in recent years. The greater use of PLRs is generally consistent with the overall increase in private credit investments by insurers, particularly life companies. PLRs provide proprietary details of investments and are only communicated to the issuer and a specified group of investors. Therefore, these investments do not benefit from the market validation that comes from market transparency (multiple investors, publicly viewable ratings, etc.) and often come as a single rating rather than multiple ratings. The NAIC has required insurance companies to submit PLRs for verification since 2018, whereby the NAIC's SVO reviews that the letter submitted is for the appropriate security and the current year. In addition, effective in 2022, insurers are required to file full rating rationale reports for PLR requests with the SVO, to partially mitigate concerns regarding the lack of transparency of PLRs.

When reviewing securities ~~supported by~~ that have been assigned PLRs, analysts should consider that the growth in PLRs is largely a reflection of increased private market issuance and the continued evolution of private credit markets, rather than, by itself, an indication of deteriorating credit quality. As market activity shifts toward newer

private credit asset classes, the use of PLRs may increase because these assets are often issued in private markets and may not be broadly or publicly rated or publicly disseminated. Analysts should also consider the insurer's broader credit assessment framework, including internal underwriting, investment committee review, and ongoing surveillance, as ~~investments in~~ private assets generally do not rely ~~solely~~ on agency ratings for credit evaluation.

Risk assessment procedures should be applied in a manner that distinguishes among:

1. Private placements and other established private fixed income investments;
2. Emerging or more complex private credit strategies, including certain direct lending, feeder funds, privately-rated CLO, and asset-based finance structures; and
3. Investments characterized by valuation uncertainty or limited transparency, including securities primarily reliant on private letter ratings or significant Level 3 valuation inputs.

The presence of a private letter designation rating alone should not be viewed as indicative of elevated risk. Analysts should prioritize review of investments exhibiting multiple risk characteristics, including lower credit quality, limited transparency, valuation complexity, concentrated exposures, or complex structures.

Unfunded Private Equity Commitments

Insurers have continued to expand their allocations to private equity, as evidenced by the increase in unfunded commitment (liability) levels in recent years. These funding commitments—contractual obligations to contribute capital to private equity funds over time—have grown along with insurers' appetite for higher-yielding, long-duration assets amid heightened market volatility. This trend underscores a strategic shift toward private markets, although it also introduces additional considerations around liquidity management and possible valuation uncertainty. Unfunded commitments may be commitments to private credit funds, but can also include commitments to private equity, hedge funds and real estate limited partnerships.

Private equity and private credit limited partnership agreements typically include a funding commitment, which may require the limited partners to reserve a significant amount of liquid assets to meet funding calls. Failure to meet a funding call could result in severe penalties. This could significantly impair the insurer's liquidity, as any reserved funds would not be readily available to pay the insurer's other obligations.

A~~a~~nalysts should evaluate whether the insurer has incorporated those commitments into its liquidity planning, cash-flow forecasting, and overall asset-liability management process.

Procedures / Data

- Ratio of private-placement bonds owned to policyholder surplus (P/C), to capital and surplus plus AVR (Life/A&H) and to capital and surplus (Health)
- Increase in private placement bonds from the prior year
  - Review Private Security Code details, Note 5.T disclosures, and available analytical tools to identify concentrations in:
    - Complex private credit structures;

- Securities backed by private letter ratings;
- Investments with significant Level 3 valuation inputs;
- Below-investment-grade or unrated private credit exposures; and
- Asset classes exhibiting elevated complexity, opacity, or valuation uncertainty.
- When evaluating private placements, analysts should consider credit quality, diversification, and performance characteristics and avoid relying solely on registration status as an indicator of risk
- ~~Review the Private Security Code details in the investment schedules, and aggregate private securities information in Note 5.T.; or utilize iSite+ tools, to identify a concentration in private securities.~~

  - Ratio of private securities in aggregate by asset type, and by security code category to total invested assets
  - Ratio of private credit securities in aggregate, by asset type, and by security code category to capital and surplus plus AVR (Life/A&H), to capital and surplus (Health), and to policyholder surplus (P&C)
  - Change in private securities from the prior year

- Review the SVO Administrative Symbols provided for the insurer's bond portfolio on Column 6 of Schedule D, or utilize iSite+ tools, to identify a concentration in securities ~~backed by~~ with PLRs (i.e., symbols PL and PLGI).
  - Ratio of securities with PLRs to total invested assets
  - Ratio of securities ~~backed by~~ with PLRs to capital and surplus plus AVR (Life/A&H), to capital and surplus (Health) and policyholder surplus (P&C)
  - Change in securities ~~backed by~~ with PLRs from the prior year, in aggregate and by asset type
- Review information provided in Note 20C of the Annual Statement (Fair Value Measurement) or utilize iSite+ tools, to identify the extent investments (by type of financial instrument) have a fair value determined with unobservable inputs (i.e., Level 3 inputs).
  - Ratio of Level 3 or Level 2D securities in aggregate to total invested assets
  - Ratio of Level 3 or Level 2D securities in aggregate and by asset type, to capital and surplus plus AVR (Life/A&H), to capital and surplus (Health) and policyholder surplus (P&C)
  - Change in Level 3 or Level 2D securities from the prior year, in aggregate and by asset type
- Review Note 14A1 to identify if the insurer has a material exposure to contingent commitments.
  - Change in contingent commitments (liabilities) since the prior year, in aggregate.
- Review Schedule BA Part 1, Column 19 total—Commitment for Additional Investment, as a percentage of Policyholders' Surplus, to assess the magnitude of the impact of unfunded commitments on the insurer's liquidity.

Additional Review Considerations

- Review Note 14 – Liabilities, Contingencies, and Assessments, to assess the insurer's exposure to unfunded commitments to private credit funds.
- If exposure to unfunded commitments is significant, consider whether the insurer's management and board have a clear understanding of differences in liquidity and market value drivers, as well as the reasons for different yield and cash-flow characteristics, as unfunded commitments contractually obligate the insurer to contribute capital to private equity funds over a designated period of time.
- Review Annual Financial Statement, Schedule D – Part 1A to determine the amount, issue type, NAIC designations, maturity distribution of privately-placed bonds owned, and the amount of privately placed bonds that are freely tradeable under U.S. Securities and Exchange Commission (SEC) Rule 144 or qualified for resale under SEC Rule 144A.

- For insurers with a concentration in bonds with Private Letter Ratings (PLRs):
  - ~~Request the support of the NAIC's Securities Valuation Office (SVO) to investigateidentify the rating sources for the securities (with a focus on concentrations with any one rating agency and/or securities with only one rating) and consider the potential impact on the insurer's RBC charges and investment risk exposures.~~
  - Request details from the company on its own internal ratings for securities ~~backed by~~ with PLRs where applicable and compare with rating agency rating for discrepancies.
- For insurers with a significant concentration in Level 3 or Level 2D securities, consider reviewing the investment schedule detail to identify whether the investments with Level 3 or Level 2D fair values are private, whether a private letter rating is the source of the NAIC designation for these items, and the extent the investments have aggregate deferred interest or paid-in-kind (PIK) interest.
- Utilize information on fair value hierarchy reported in the investment schedules to identify individual securities warranting additional review.
- If private placements, private credit investments, Level 3 or 2D securities, or assets with PLRs are material, consider inquiring of the insurer its infrastructure and investment management policies and procedures (i.e. portfolio management and credit analyst expertise, including approach to making investment decisions) in place either internally, or via an affiliate, and/or outsourced investment manager, to manage these investments.
- Consider requesting additional information on the ongoing performance of these assets and/or the pricing assumptions and methodologies used in fair value measurement.
- If necessary, consider utilizing an investment specialist to assist in asset valuation considerations.
- ~~If appropriate, consult with or request an Opinion from the NAIC's SVO or Structured Securities Group (SSG) on a specific investment holding or transaction. [A state insurance regulator can ask for SVO or SSG analytical assistance with respect to any investment related activity or in connection with an assessment of investment-related aspects of a Regulatory Transaction (defined in the P&P Manual). The department can direct an insurance company to file relevant information with the SVO or SSG for the purpose of that analysis and the SVO or SSG will issue a report back to the department.]~~
- Request a Preliminary Analysis from the NAIC's Capital Markets Bureau (CMB) to assess the insurer's overall portfolio investment risk exposures and suggest additional follow-up procedures that can be performed by the department to address overall portfolio issues identified. Request analytical assistance from the CMB to better understand and measure the investment risks related to a particular asset class, investment-related activity, or market trend.

~~Exposure to Private Placement Bonds~~

~~Significant investments in privately-placed bonds may cause concerns regarding the insurer's liquidity because some of these investments cannot be resold, while those that can be resold have restrictions on whom they can be sold to, including restrictions under securities laws. There is no structured market for privately-placed bonds like there is for publicly-traded bonds. Therefore, even if the privately-placed bonds can be sold, it may be difficult to find a willing buyer.~~

~~Procedures / Data~~

- ~~Ratio of private placement bonds owned to policyholder surplus (P/C), to capital and surplus plus AVR (Life/A&H) and to capital and surplus (Health)~~
- ~~Increase in private placement bonds from the prior year~~

~~Additional Review Considerations~~

- ~~Review Annual Financial Statement, Schedule D – Part 1A to determine the amount, issue type, NAIC designations, maturity distribution of privately placed bonds owned, and the amount of privately placed bonds that are freely tradeable under U.S. Securities and Exchange Commission (SEC) Rule 144 or qualified for resale under SEC Rule 144A.~~
- ~~For significant privately placed bonds rated by a chief revenue officer, review the issuer's rating or request the Securities Valuation Office's assessment of the designation to evaluate the issuer's financial position and ability to repay its debt.~~

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

Invested Asset Exposure to Climate Change, Transition and Asset Devaluation Risk

Identify and assess the potential exposure of the insurer's investment portfolio to the impact of material climate change and/or energy transition risks and asset devaluation risk. The insurer's investment portfolio is subject to prospective devaluation of the assets/changes in the asset return associated with its holdings of climate-affected assets. Transition risks refer to stresses on certain investment holdings arising from the shifts in policy, consumer and business sentiment, or technologies associated with the changes necessary to limit climate change. A few examples of investment holdings and sectors generally subject to greater levels of transition risk include, oil/gas, transportation, heavy manufacturing, and agriculture. In assessing an insurer's exposure to these risks, the analyst is encouraged to review information disclosed by the insurer in its responses to the NAIC's Climate Risk Disclosure Survey, U.S. Securities and Exchange Commission (SEC) filings, and/or the Own Risk and Solvency Assessment (ORSA) Summary Report filings. In addition, the analyst is encouraged to review the results of basic scenario analysis conducted by the NAIC using insurers' Annual Statement filings (U.S. Insurance Industry Climate Affected Investment Analysis) to identify potential concentrations in exposure.

Procedures

- Review information provided in the insurer's response to the NAIC's Climate Risk and Disclosure Survey (if available) on its exposure to material climate change/energy transition risk and related mitigation activity in this area.
- Review relevant information provided in the Own Risk and Solvency Assessment (ORSA) Summary Report, and/or U.S. Securities and Exchange Commission (SEC) 10-K or 10-Q filings (if available) that discusses the insurer's exposure to material climate change/energy transition risk and related mitigation activity in this area.
- Review information provided in the NAIC's U.S. Insurance Industry Climate Affected Investment Analysis to identify potential concentrations in insurer exposure.
- Review the Climate Affected Assets Dashboard to assess an insurer's exposure to assets that might be subject to transition risk in the coming years. The dashboard allows the user to view an individual insurer's investment portfolio as of year-end, which has been classified into buckets of climate affected assets (i.e., Fossil Fuel, Energy Intensive), with the ability to view those categories as a percentage of the overall portfolio. Companies that do not have assets subject to transition risk (i.e., Treasuries, Cash) will not be included.

Yellow Highlights – Changes recommended by Commentors to the CR and LQ chapter that Staff supports accepting also in the MK chapter for consistency.
Grey Highlights – Edits recommended by Staff.

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

ANNUAL MARKET RISK ASSESSMENT

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

Significant Investment Concentration by Asset Class

Determine whether the insurer's investment portfolio appears to be adequately diversified to avoid an undue concentration of investments by asset type, duration or issuer.

Various types of investments to total net admitted assets (excluding separate accounts for Life/A&H) are a measure of the diversity of the insurer's investment portfolio by type of investment. The results of these ratios may also provide some indication of the insurer's liquidity. In addition, the ratio of the investment in any one issuer to total net admitted assets (excluding separate accounts for Life/A&H) is a measure of the diversity of the insurer's investment portfolio by issuer.

For foreign securites, market risk may include material exposures that could result in credit losses if those investments are affected by negative changes in geopolitical or foreign economic environments.

For mortgage loans, market risk may include the risk that the insurer is not properly identifying, handling and recording foreclosed mortgage loans.

Procedures/Data

- Consider evaluating the following assets classes in comparison to total admitted assets[i] to determine the level of concentration *(See also Credit Risk Assessment for diversification of other asset classes):*
  - Asset-Backed Securities.
  - Foreign bonds.
  - Common stocks.
  - Mortgage loans.
  - Real Estate (before encumbrances), including home office real estate.
  - Total derivatives (notional value).
  - Investment in affiliates.
  - Any one single investment in foreign bonds, common stock, real estate and derivatives (excluding afiliated investments) *(Note that single investments in financial asset-backed securities are considered within the Credit Risk Assessment).*

Additional Review Considerations

- Review the percentage distribution of assets for significant shifts in the mix of investments owned during the past five years.

[i] For ratios in this asset concentration procedure, net admitted assets excludes separate accounts for Life/A&H.

- Industry and Peer Comparison: Note that comparisons should be based on insurer type, but also should reflect the size of the company and more specific aspects of the insurer's liabilities.
    - Compare the insurer's distribution of cash and invested assets and recent changes in asset categories, with a particular focus on the last year or the previous few years, to industry averages and peer averages utilzing ~~on~~ iSite+ tools to determine significant deviations from the industry averages~~.~~ and comparison to peer companies.
    - Compare the insurer's investment portfolio to an appropriate peer group. Consider using the NAIC Peer Analysis Financial Profile report or the Snapshot Investment Summary in iSite+ to identify an compare to an appropriate group of peer companies for this purpose.
    - ~~The comparison should focus on an appropriate peer group based on insurer type and asset size.~~
- If the insurer's investments include a significant amount of foreign bonds, review the Annual Supplemental Investment Risks Interrogatories (#4 through #11). Consider the insurer's potential foreign currency exposure from holding bonds denominated in a foreign currency.
- Review of the Annual Supplemental Investment Risks Interrogatories to identify any unusual items or areas and determine whether the insurer's investment portfolio is adequately diversified to avoid significant aggregate market risk.
- Review of the Legal Risk Assessment to determine whether the insurer's investment portfolio is in compliance with the investment limitations and diversification requirements per the state's insurance laws.
- Review the most recent examination report and Summary Review Memorandum (SRM) for any findings regarding market risks associated with investment concentration and exposure to riskier asset classes.
- Inquire of the insurer its planned asset mix, and diversification strategies.

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

Impact of Market Volatility on the Aggregate Investment Portfolio

An important consideration when markets experience significant volatility and strains is the potential negative impact may not be on just one or a small number of investments held by insurers. Rather, market strains can have a significant impact on an entire asset class, several asset classes, or the entire investment portfolio. Particularly vulnerable are asset classes in ~~that represent smaller~~ markets that are typically less liquid, are ~~more~~ structurally complex or are assets that would be considered ~~less traditional~~ atypical for insurers. Therefore, state insurance regulators should consider the potential impact of significant market challenges on different asset classes in the investment portfolios of insurers.

Procedures

- Review and monitor material asset classes for significant changes in fair value and/or significant changes in relative liquidity. Utilize data in the Annual Statement, Financial Profile, Snapshot Investment Summary and investment dashboards. Also refer to specific liquidity guidance in this chapter on asset groups such as bonds, BA assets and mortgage loans. Do not limit considerations to one asset class, but also consider the aggregate of all such vulnerable asset classes. Examples of asset groupings that may represent notable exposures in insurer portfolios and that should be considered are:

- Below investment grade bonds. (rated below BBB-/baa3).
- ~~Weaker investment grade ("BBB" rated) bonds.~~
- Commercial mortgage loans, ~~particularly~~ for example office properties (in the current market as of 2026).
- Mezzanine loans.
- Real estate equity.
- Structured securities, especially collateralized loan obligation (CLO) tranches (including CLO Combo Notes and Middle Market CLOs).
- Residential mortgage-backed securities (RMBS), specifically as to cash flow variability.
- Emerging markets investments.
- Hedge funds.
- Private equity funds.
- Private credit, including private placements (specifically non-144A) and private letter ratings.
- Derivatives transactions.
- Concentrations in exposure to sectors impacted by the current market, currently the auto, technology, consumer products and retail sectors due to technology/software (AI), and energy, due to high oil prices ~~the potential impact of tariffs.~~

The materiality of these exposures should be evaluated in the context of the insurer's overall risk profile, including applicable NAIC capital requirements associated with the assets. Different situations may call for different materiality standards, so it is important to be able to explain the standard used.

When evaluating the liquidity of less liquid assets, analysts should consider the insurer's broader asset-liability management framework. Life insurers for example, generally have long investment horizons due to the long-duration and generally predictable nature of their liabilities. Accordingly, insurers actively model asset and liability cash flows to ensure sufficient liquidity is available to meet policyholder obligations as they come due. Insurers generally do not invest in less liquid assets, including private equity, hedge funds, private credit, and commercial mortgage loans, for day-to-day liquidity management. Rather, the ability to allocate a portion of the portfolio to ~~such~~ assets is a structural feature of the insurance business model that can be a source of additional investment income while remaining consistent with prudent liquidity management.

Additional Review Considerations

- For ~~the~~ identified asset classes ~~above~~, where there is not a readily available or exchange traded market, verify pricing and valuation sources and corresponding valuation methods. Close attention should be given to asset classes like private equity and real estate that usually report on a 3-month lag, as well as private credit whose valuations may be subjective.

- Inquire as to how the insurer is managing the potential risk of rating migration. Inquire as to how they may apply a credit rating transition matrix and calculate the resulting increased RBC charges.

- Inquire as to how the insurer is managing the above-mentioned challenges and other potential challenges in the investment marketplace. For example, consider the following questions:
  - How is the insurer managing significant changes in fair value of portfolio assets, especially for longer-dated investments?

- Are other-than-temporary- impairments (OTTI) appropriate?
- If there is an ongoing risk, should the insurer consider shortening the duration of future investments?

- Review the insurer's Liquidity Stress Test submission (if applicable) to evaluate results and assess the insurer's stress testing process and assumptions for reasonableness.

- Inquire as to how changes in the investment profile (particularly duration) may impact asset/liability matching, asset adequacy analysis and cash-flow testing.

- ~~Request an Opinion from the NAIC's Securities Valuation Office (SVO) or Structured Securities Group (SSG) on a specific investment holding or transaction. [A state insurance regulator can ask for SVO or SSG analytical assistance with respect to any investment related activity or in connection with an assessment of investment-related aspects of a Regulatory Transaction (defined in the P&P Manual). The department can direct an insurance company to file relevant information with the SVO or SSG for the purpose of that analysis and the SVO or SSG will issue a report back to the department.]~~

- Request a Preliminary Analysis from the NAIC's Capital Markets Bureau (CMB) to assess the insurer's overall portfolio of investment risk exposures and obtain additional follow-up procedures that can be performed by the department to address any overall portfolio issues identified. Request analytical assistance from the CMB to better understand and measure the investment risks related to a particular asset class, investment-related activity, or market trend.

Exposure to Private Credit Securities, Level 3 Securities, Bonds with Private Letter Ratings and Unfunded Commitments

In recent years, the insurance industry has seen an ongoing increase in the amount and diversity of private fixed income investments held by U.S. domestic insurers. Private fixed income encompasses a broad range of asset types, including traditional investment-grade private placements, private structured assets, direct lending, and other credit-oriented investments. Many of these investments have been longstanding components of insurer portfolios and are generally well suited to insurers' long-duration liabilities and investment horizons.

The ability to invest in less liquid assets is a structural feature of the insurance business model and allows insurers to earn an illiquidity premium while continuing to meet policyholder obligations. While certain newer and more complex private credit structures may warrant enhanced regulatory attention, analysts should distinguish between private placements and emerging private credit strategies when assessing credit risk exposures.

~~In recent years, the insurance industry has seen an ongoing increase in the amount of private assets held by U.S. domestic insurers, including securities with NAIC designations supported by private letter ratings and securities that are valued based on Level 3 (unobservable) inputs.~~

Potential areas of focus may include investments that involve heightened complexity, limited transparency, reliance on unobservable valuation inputs, private letter ratings, or nontraditional structures.

While this increase is generally consistent with the broader capital markets trend of increased issuance of private assets, their relative opacity versus other asset types ~~the potential lack of transparency related to private assets~~ can complicate the assessment of credit quality and increase the liquidity risk of the portfolio.

~~Private credit generally refers to debt, or debt-like, securities that are not publicly issued or traded. Private credit is an evolving, alternative funding source. Non-bank lenders, including insurance companies, private debt funds, and business development companies, issue private loans directly to mostly small and middle-market companies that do not have—or have limited— access to the public corporate bond and loan markets. These small middle-market companies often have more debt than larger companies that access capital via leveraged loans and public bonds and, therefore, they are more susceptible to economic downturns and the impact of rising interest rates.~~

~~Private credit has~~ "Private credit" describes a variety of strategies that include direct lending, distressed debt, venture debt, mezzanine finance, and special situations. ~~Direct~~ According to Morgran Stanley Investment Management, direct lending comprised 52%[ii] ~~is the largest segment and accounts for about 40%~~ of the U.S. private credit market as of Sept. 30, 2025.The largest investors in private credit are typically pension funds, insurance companies, and sovereign wealth funds. While direct lending to corporate issuers is the simplest and most common strategy ~~type of private credit, it is evolving into~~ more complex investments like feeder fund structures, ~~private credit~~ middle market CLOs with private letter ratings, and asset-based financing (where loans are secured by collateral such as inventory, receivables, equipment, or property).

Risks and mitigating factors include:

- Less liquidity: Private credit is generally issued directly by a non-bank lender or a small group of lenders, resulting in a relatively illiquid market where secondary trading is limited.
- Less transparency: The availability of information about a private credit security is often contractually restricted, which contributes to lower transparency compared to public securities and can make it more difficult to assess credit risk and determine appropriate valuation.
- Less frequent pricing: It may be subject to less frequent valuation and pricing.
- ~~Assessment of credit quality:~~
    - ~~While lack of transparency can make credit quality more difficult to assess, private credit lenders can often benefit from stronger control over documentation and are able to customize terms of the transaction given their direct relationship with borrowers. In the event of stress, lenders and investors should be able to work directly with the borrower to modify the transaction terms or add investor safeguards.~~
    - Private credit can contribute to an investment portfolio's diversification, with respect to issuers and duration, among other factors ~~it also has the potential to provide a broader pool of debt issuers that results in portfolio diversification~~.
- ~~Future performance~~Risk/Reward Optimization:
    - Private credit generally offers higher spreads and yields than public corporate bonds and loans to compensate investors for the relative market illiquidity (lack of a secondary market) and complexity depending on the transaction type.
    - ~~As the nature of private credit evolves and expands, there is no assurance that current/historical performance trends (largely favorable) will continue. The solid historical performance of private~~

[ii] 52% as of September 2026 per Morgan Stanley Investment Management

~~lending may not be comparable performance as the market grows and as new entrants change focus to non-traditional alternative assets and more challenging and stressed credit environments occur, particularly higher interest rates.~~

- Enhanced covenant protections and documentation relative to broadly syndicated lending markets.
- Greater ability for lenders to negotiate transaction-specific terms and monitor borrower performance.
- Diversification benefits through access to issuers and asset types not available in public markets.
- Structural protections, including collateralization, overcollateralization, cash flow controls, and other credit enhancements depending on the investment structure.
- Historical performance in certain private credit segments that has demonstrated recovery characteristics comparable to or stronger than similar public market exposures.

Refer also to guidance published by the NAIC Capital Markets Bureau on private credit and its characteristics.

Note that the Annual Statement includes new disclosures and reporting requirements to improve the identification of different types of private securities. For year-end 2026, insurers will be required to disclose the SEC registration status for each investment: public, Rule 144A, private placements (defined to include Regulation D, Section 4(a)(2) exempt or other exclusion from SEC registration), or not applicable because the investment is not within the scope of the Securities Act of 1933. An aggregate disclosure in Note 5.T—Private Securities to capture key data by each grouping of investments by registration status to allow for ease of regulator review. The reporting will be provided in an electronic column in all investment reporting schedules (held, acquired, disposed) for short-term investments, cash equivalents, issuer credit obligations, asset-backed securities, common stock, preferred stock and other long-term investments.

Fair Value Measurement Hierarchy

An important element in evaluating risks associated with valuation of private investments (equity or credit) is the level of input available to determine fair value. To increase consistency and comparability in fair value measurements and related disclosures, the fair value hierarchy (see SSAP No. 100) prioritizes the inputs to valuation techniques used to measure fair value into three broad levels. The fair value hierarchy gives the highest priority to quoted prices (unadjusted) in active markets for identical assets (Level 1) and the lowest priority to unobservable inputs (Level 3).

- **Level 1** inputs are quoted prices (unadjusted) in active markets for identical assets that the reporting entity has the ability to access at the measurement date.

- **Level 2** inputs are inputs other than quoted prices included within Level 1 that are observable for the asset, either directly or indirectly. Level 2 inputs might include quoted prices for similar assets in active markets, quoted prices for identical or similar assets in inactive markets, or prices derived from inputs that are observable (e.g., interest rates and yield curves).

- **Level 3** inputs are unobservable inputs for the asset. Unobservable inputs are used to measure fair value to the extent that relevant observable inputs are not available. These inputs often involve significant judgment and estimation, including the use of internal models and assumptions.

When reviewing Level 3 assets, analysts should distinguish valuation classification from credit risk assessment. The fair value hierarchy is intended to identify the nature of inputs used to measure fair value, not to assign a credit risk classification. Therefore, a Level 3 classification reflects the use of a significant number of unobservable inputs and should not be interpreted, on its own, as evidence of elevated credit risk. Certain long-duration insurance assets may have limited observable market inputs but still exhibit stable contractual cash flows and strong credit characteristics. In addition, some assets may be classified as Level 3 because observable valuation inputs are not available at the measurement date, and those assets may subsequently migrate to Level 2 once observable inputs become available.

Information associated with fair value measurement is provided in Note 20 (Fair Value Measurements) of the Annual Statement and can assist regulators in assessing the risks associated with an insurer's private investment holdings. In addition, information on fair value hierarchy reported in the investment schedules can be utilized to identify individual securities warranting additional review.

Private Letter Ratings (PLRs)

Privately rated securities reported by U.S. insurance companies have become more prevalent in recent years. The greater use of PLRs is generally consistent with the overall increase in private credit investments by insurers, particularly life companies. PLRs provide proprietary details of investments and are only communicated to the issuer and a specified group of investors. Therefore, these investments do not benefit from the market validation that comes from market transparency (multiple investors, publicly viewable ratings, etc.) and often come as a single rating rather than multiple ratings. The NAIC has required insurance companies to submit PLRs for verification since 2018, whereby the NAIC's SVO reviews that the letter submitted is for the appropriate security and the current year. In addition, effective in 2022, insurers are required to file full rating rationale reports for PLR requests with the SVO, to partially mitigate concerns regarding the lack of transparency of PLRs.

When reviewing securities that have been assigned PLRs, analysts should consider that the growth in PLRs is largely a reflection of increased private market issuance and the continued evolution of private credit markets, rather than, by itself, an indication of deteriorating credit quality. As market activity shifts toward newer private credit asset classes, the use of PLRs may increase because these assets are often issued in private markets and may not be broadly or publicly rated or publicly disseminated. Analysts should also consider the insurer's broader credit assessment framework, including internal underwriting, investment committee review, and ongoing surveillance, as ~~investments in~~ private assets generally do not rely ~~solely~~ on agency ratings for credit evaluation.

Risk assessment procedures should be applied in a manner that distinguishes among:

1. Private placements and other established private fixed income investments;
2. Emerging or more complex private credit strategies, including certain direct lending, feeder funds, privately-rated CLO, and asset-based finance structures; and
3. Investments characterized by valuation uncertainty or limited transparency, including securities primarily reliant on private letter ratings or significant Level 3 valuation inputs.

The presence of a private letter designation rating alone should not be viewed as indicative of elevated risk. Analysts should prioritize review of investments exhibiting multiple risk characteristics, including lower credit quality, limited transparency, valuation complexity, concentrated exposures, or complex structures.

Unfunded Private Equity Commitments

Insurers have continued to expand their allocations to private equity, as evidenced by the increase in unfunded commitment levels in recent years. These funding commitments—contractual obligations to contribute capital to private equity funds over time—have grown along with insurers' appetite for higher-yielding, long-duration assets amid heightened market volatility. This trend underscores a strategic shift toward private markets, although it also introduces additional considerations around liquidity management and possible valuation uncertainty.

Private equity and private credit limited partnership agreements typically include a funding commitment, which may require the limited partners to reserve a significant amount of liquid assets to meet funding calls. Failure to meet a funding call could result in severe penalties. This could significantly impair the insurer's liquidity, as any reserved funds would not be readily available to pay the insurer's other obligations.

Analysts should evaluate whether the insurer has incorporated those commitments into its liquidity planning, cash-flow forecasting, and overall asset-liability management process.

Procedures

- Review Private Security Code details, Note 5.T disclosures, and available analytical tools to identify concentrations in:
    - Complex private credit structures;
    - Securities backed by private letter ratings;
    - Investments with significant Level 3 valuation inputs;
    - Below-investment-grade or unrated private credit exposures; and
    - Asset classes exhibiting elevated complexity, opacity, or valuation uncertainty.
    - When evaluating private placements, analysts should consider credit quality, diversification, and performance characteristics and avoid relying solely on registration status as an indicator of risk
    - Ratio of private securities in aggregate by asset type, and by security code category to total invested assets
- ~~Review the Private Security Code details in the investment schedules, and aggregate private securities information in Note 5.T.; or utilize iSite+ tools, to identify a concentration in private securities.~~
    - Ratio of Private securities in aggregate and by security code category to capital and surplus plus AVR (Life/A&H), to capital and surplus (Health), and to policyholder surplus (P&C)
    - Change in private securities from the prior year
- Review the SVO Administrative Symbols provided for the insurer's bond portfolio on Column 6 of Schedule D, or utilize iSite+ tools, to identify a concentration in securities ~~backed by~~ with PLRs (i.e., symbols PL and PLGI).
    - Ratio of securities with PLRs to total invested assets
    - Ratio of securities backed by PLRs to capital and surplus plus AVR (Life/A&H), to capital and surplus (Health) and policyholder surplus (P&C)
    - Change in securities ~~backed by~~ with PLRs from the prior year

- Review information provided in Note 20C of the Annual Statement (Fair Value Measurement) or utilize iSite+ tools, to identify the extent investments (by type of financial instrument) have a fair value determined with unobservable inputs (i.e., Level 3 inputs).
  - Ratio of Level 3 or Level 2D securities in aggregate to total invested assets
  - Ratio of Level 3 securities to capital and surplus plus AVR (Life/A&H), to capital and surplus (Health), and policyholder surplus (P&C)
  - Change in Level 3 securities from the prior year
- Utilize information on fair value hierarchy reported in the investment schedules to identify individual securities warranting additional review.
- Review Note 14 – Liabilities, Contingencies, and Assessments, to assess the insurer's exposure to unfunded commitments.
- Review Schedule BA Part 1, Column 19 total—Commitment for Additional Investment, as a percentage of Policyholders' Surplus, to assess the magnitude of the impact of unfunded commitments on the insurer's valuation.

Additional Review Considerations

- For insurers with a concentration in bonds with PLRs:
  - ~~Request the support of the NAIC's Securities Valuation Office (SVO) to investigate the rating sources for the securities (with a focus on concentrations with any one rating agency and/or securities with only one rating) and consider the potential impact on the insurer's RBC charges and investment risk exposures.~~
  - Request details from the company on its own internal ratings for securities ~~backed by~~ with PLRs where applicable and compare with rating agency rating for discrepancies.
- For insurers with a significant concentration in Level 3 securities, consider reviewing the investment schedule detail to identify whether the investments with Level 3 fair values are private, whether a private letter rating is the source of the NAIC designation for these items, and the extent the investments have aggregate deferred interest or paid-in-kind (PIK) interest.
- Consider requesting additional information on the ongoing performance of these assets and/or the pricing assumptions and methodologies used in fair value measurement.
- If exposure to unfunded commitments is significant, consider whether the insurer's management and board have a clear understanding of differences in liquidity and market value drivers, as well as the reasons for different yield and cash-flow characteristics, as unfunded commitments contractually obligate the insurer to contribute capital to private equity funds over a designated period of time.
- If necessary, consider utilizing an investment specialist to assist in asset valuation considerations.
- ~~If appropriate, consult with or request an Opinion from the NAIC's SVO or Structured Securities Group (SSG) on a specific investment holding or transaction. [A state insurance regulator can ask for SVO or SSG analytical assistance with respect to any investment related activity or in connection with an assessment of investment-related aspects of a Regulatory Transaction (defined in the P&P Manual). The department can direct an insurance company to file relevant information with the SVO or SSG for the purpose of that analysis and the SVO or SSG will issue a report back to the department.]~~
- Request a Preliminary Analysis from the NAIC's Capital Markets Bureau (CMB) to assess the insurer's overall portfolio investment risk exposures and suggest additional follow-up procedures that can be performed by the department to address overall portfolio issues identified. Request analytical assistance from the CMB to

better understand and measure the investment risks related to a particular asset class, investment-related activity, or market trend.

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

Invested Asset Exposure to Climate Change, Transition and Asset Devaluation Risk

Identify and assess the potential exposure of the insurer's investment portfolio to the impact of material climate change and/or energy transition risks. The insurer's investment portfolio may be subject to prospective devaluation of the assets/changes in the asset return associated with its holdings of climate-affected assets. Transition risks refer to stresses on certain investment holdings arising from the shifts in policy, consumer and business sentiment, or technologies associated with the changes necessary to limit climate change. A few examples of investment holdings and sectors generally subject to greater levels of transition risk include oil/gas, transportation, heavy manufacturing, and agriculture. In assessing an insurer's exposure to these risks, review information disclosed by the insurer in its responses to the NAIC's Climate Risk Disclosure Survey, U.S. Securities and Exchange Commission (SEC) filings, and/or the Own Risk and Solvency Assessment (ORSA) Summary Report filings. In addition, review the results of basic scenario analysis conducted by the NAIC using insurers' Annual Statement filings (U.S. Insurance Industry Climate Affected Investment Analysis) to identify potential concentrations in exposure.

Procedures

- Review information provided in the insurer's response to the NAIC's Climate Risk and Disclosure Survey (if available) on its exposure to material climate change/energy transition risk and related mitigation activity in this area.
- Review relevant information provided in the Own Risk and Solvency Assessment (ORSA) Summary Report, and/or U.S. Securities and Exchange Commission (SEC) 10-K or 10-Q filings (if available) that discusses the insurer's exposure to material climate change/energy transition risk and related mitigation activity in this area.
- Review information provided in the NAIC's U.S. Insurance Industry Climate Affected Investment Analysis to identify potential concentrations in insurer exposure.
- Review the Climate Affected Assets Dashboard to assess an insurer's exposure to assets that might be subject to transition risk in the coming years. The dashboard allows the user to view an individual insurer's investment portfolio as of year-end, which has been classified into buckets of climate affected assets (i.e., Fossil Fuel, Energy Intensive), with the ability to view those categories as a percentage of the overall portfolio. Companies that do not have assets subject to transition risk (i.e., Treasuries, Cash) will not be included.

Additional Review Considerations

- Review the insurer's investment policies and strategies to assess whether material climate change, transition and asset devaluation risk considerations have been appropriately implemented into the company's investment processes.
- Review the most recent examination report and summary review memorandum (SRM) for any findings regarding climate change/energy transition risks.

- If concerns exist, consider requesting information from the insurer regarding how the insurer manages its exposure to material climate change/energy transition risk, including how it identifies and estimates current and prospective exposures and the limits (if any) in place to avoid concentrations.

----------Detail Removed to Conserve Space----------

ANNUAL CREDIT RISK ASSESSMENT

----------Detail Removed to Conserve Space----------

Credit Quality~~, Adequacy~~ and Appropriateness of Asset Intensive Reinsurance~~s Held for~~Placed Through Modco or FWH Agreements (Life/A&H Insurers)

Modified Coinsurance and Funds Withheld Agreements

Concerns may exist regarding the quality, adequacy and appropriateness of assets held to support asset intensive reinsurance placed through Modified Coinsurance (Modco) or Funds Withheld (FWH) ~~reinsurance~~agreements, particularly as investments become increasingly complex. Concerns may include controls and governance over investment practices, valuation and ratings of assets, and if material amounts of assets involve related party transactions.

Where collateral held is related to Modco and FWH reinsurance, the analyst should review the information in Note to the Financials #5L(1), #5L(4) and #5L(5), and Schedule S—Part 8—Reinsurance Agreements with Funds Withheld and Modified Coinsurance, in conjunction with other credit, operational and strategic risk of the insurer's reinsurance program. Additionally, review the analysis considerations related reserve reporting required by AG 53 (complex assets) and AG 55 (assets supporting reinsurance) outlined in the Reserving Risk Assessment and SOA procedures and guidance.

Where the company is engaged in material Modco and FWH arrangements, the analyst can use the detail of collateral received and held under Note 5L(4) to identify the types of assets held by investment schedule, and gain an understanding of the materiality of aggregate BACV of the collateral received to the insurer's asset portfolio. Further, the Note #5L(5) disclosure identifies if securities held as collateral under Modco or FWH agreements are also pledged under other arrangements, in which case they would not be for the benefit of the reinsurer or available to fulfill the liabilities of the reinsurance contract. The analyst can use the information in Schedule S—Part 8 to identify any concerns with the types of assets and credit quality of assets held under ceded or assumed Modco or FWH agreements.

Procedures / Data

- Identify the types of reinsurance agreements and jurisdiction of the reinsurer [Annual Financial Statement, Schedule S – Part 3] and determine if concerns may exist over the adequacy and quality of assets held by reinsurers in support of ceded reserves that may require further analysis or inquiry to the insurer.
    - Compare the BACV of the collateral received and assets held under Modco/FWH Reinsurance Agreements to the recognized obligation for Modco and FWH assets. [Annual Financial Statement, Notes to the Financials #5L(4)(m and n)].
    - Identify if investments held under FWH agreements (including Modco) are related to the Modco/FWH reinsurer [Annual Financial Statement, Notes to the Financials 5L(5)(o-v)].
    - Identify if the insurer is engaged in ceding business under Modco and FWH agreements with offshore reinsurers.

- Gain an understanding, through review of Schedule S - Part 3, of the types of insurance business ceded, the reinsurer's jurisdiction, if affiliated or non-affiliated, and applicable collateral requirements by type of reinsurer (i.e. authorized, unauthorized, reciprocal jurisdiction, certified). See the following sections for additional procedures for assessing risk for offshore unauthorized reinsurance.

- Review Schedule S – Part 8 to determine if concerns exist regarding the types of assets held or the credit quality of assets held under Modco/FWH agreements. Consider if the aggregate of medium or lower quality assets held represent a material amount of the related Modco/FWH liabilities.
  - Review Schedule S – Part 8 in comparison to Life RBC (asset schedules) to ensure asset subtotals match. If differences exist, inquire of the insurer, as differences may have an impact on the RBC calculation.
- Determine if assets held under Modco or FWH agreements are also pledged under other agreements [Annual Financial Statement, Notes to the Financials #5L(5)].

Additional Review Considerations

- If concerns exist regarding the types of assets held or the credit quality of assets held under Modco or FWH agreements, or concerns over reinsurance reporting, inquire of the insurer to:
  - Identify the applicable reinsurers and reinsurance agreements. Annual Financial Statement, Schedule S – Part 3, Financial Profile, Reinsurance Dashboard]
  - Has the insurer entered into new offshore unaffiliated Modco or FWH agreements for which the agreement was not required to be reviewed by the Department?
  - If offshore reinsurance, gain an understanding of the types of business ceded and the insurer's business purpose for ceding the business offshore.
  - Gain an understanding of the collateral requirements for the type of reinsurance and jurisdiction.
  - Request a copy of the applicable Modco/FWH reinsurance agreements and assess if the investment requirements are in compliance with the terms of the agreement and the state's reinsurance statutes.
  - Gain an understanding of the insurer's investment practices, who is managing the investments supporting the reserves, governance policies and use of asset managers for reinsurance assets.
  - If the management of the assets withheld or placed in trust in support of the reinsurance agreement is transferred to the reinsurer or an asset manager:
    - Assess ~~whether~~ the degree to which the ceding company has provided ~~sufficient~~ direction and oversight to the reinsurer in terms of investment guidelines and limitations.
    - Closely monitor the assets in the funds withheld or trust account to verify they are in compliance with state laws and ceding company guidelines, and ~~are not overly concentrated~~ identify concentrations in complex or risky investments.
- If a material amount of assets held under Modco or FWH agreements are also pledged under other arrangements, inquire of the insurer to gain a better understanding of their use of collateral assets within their reinsurance program and to ensure the insurer is in compliance with collateral requirements.
- Refer significant concerns identified to the examiner for further review, if warranted.

Reinsurance Ceded to Unauthorized Reinsurers in ~~Unauthorized~~ Offshore Jurisdictions

Additional concerns may exist when asset intensive reinsurance is placed with ~~in~~ unauthorized reinsurers from offshore jurisdictions with varying regulatory requirements and oversight. In recent years, regulators have observed a rise in the use of offshore reinsurance transactions (both affiliated and unaffiliated) to unauthorized reinsurers in these ~~unauthorized~~ jurisdictions. An underlying concern is that this activity could result in reduced policyholder protection or regulatory arbitrage, and rising reinsurance credit risk, if reinsurance reserves or the underlying collateral supporting those ceded reserves is not sufficient, all of which should be carefully assessed and monitored. Some additional considerations are provided below including an optional "reinsurance comparison worksheet" that can be used to compare different accounting, reserving and capital standards across jurisdictions. In certain international jurisdictions regulators have had difficulties determining if offshore reinsurance arrangements are affiliated or unaffiliated as information about the ownership of the reinsurer may not always be readily available or easily obtained, therefore it is important to have good communication with cedents and relevant foreign jurisdiction regulatory authorities.

A potential concern with utilizing unaffiliated third-party offshore unauthorized reinsurance is when management of the assets withheld or placed in trust in support of the agreement is transferred to the reinsurer or an asset management affiliate, which may be the case in some asset intensive reinsurance arrangements. In these situations, the reinsurer may have incentive to reallocate the portfolio into more complex assets to achieve a higher rate of return, including assets originated by or placed within its affiliated entities.

Finally, while historically more common in property/casualty insurance, there have been recent indications that more reinsurance sidecars are being formed in the life/annuity reinsurance industry. Sidecars are limited purpose reinsurance transactions where third-party investors infuse capital in exchange for dividends, and may also provide other services, such as asset management services in exchange for fees. The purpose is to offer alternative capital to reduce volatility in earnings and capital of the ceding insurers. Since sidecars arrangements may be formed with different strategies and interests in mind (infuse capital support, specialized asset management expertise, favorable offshore capital/tax treatment, reduce volatility, etc.), it is important to understand the structure of the sidecar deal, and whether the ceding insurance company has sufficient governance and controls over services provided by the sidecar.

Procedures / Data

- Identify the type(s) of reinsurance agreements, type(s) of business ceded, and jurisdiction(s) of the unauthorized offshore reinsurer(s). Determine if amounts ceded to unauthorized offshore reinsurers are material. [Annual Financial Statement, Schedule S – Part 3; Financial Profile; Reinsurance Dashboard]

Additional Review Considerations

- For material new reinsurance transactions placed with unauthorized offshore reinsurers, regulators should gain an understanding of ~~and assess the appropriateness of t~~he business purpose for the transaction.
- Monitor the reinsurer's credit and financial strength ratings.
- Consider utilizing the Reinsurance Comparison Worksheet developed by the Macroprudential (E) Working Group to assist in understanding and evaluating cross-border reinsurance treaties where different regulatory systems are involved.
- Gain an understanding of the regulatory requirements for assets held to support the reinsurance agreement.
- ~~Verify~~ Assess the credit quality and liquidity of the funds-withheld assets supporting the agreement, including assessing risks associated with complex assets backing the reinsurance agreements. [e.g. for Life/A&H: Review of Actuarial Guideline 55 filing, if required; Annual Statement Note 5; Schedule S, Part 8 for Life/A&H]. Refer to additional Modco/FWH procedures above.

- For assets managed by third-party reinsurers or asset managers (i.e., funds withheld or held in trust), closely review the assets to identify relationships with the reinsurer and ensure compliance with ceding company guidelines and state investment laws (i.e., single issuer limitations).
- Consider engaging with foreign jurisdiction regulatory authorities to understand their applicable capital, investment, and reserving requirements as well as their understanding of the ownership structure of the reinsurer and the regulatory agency's supervisory plan for the reinsurer.
- Review information provided in the insurer's Actuarial Guideline 55 filing, if required, relating to asset adequacy analysis, reserves and assets supporting asset intensive reinsurance transactions, if applicable. (See additional guidance in the Life Reserve Risk chapter, III.B.8.b.ii)
  - Coordinate with the Valuation Analysis (E) Working Group, as appropriate, to access information from their targeted review of AG-55 filings and/or request additional support.
- Consider requesting information from the cedent, the reinsurer, or the reinsurer's domiciliary regulatory authority, for the Department's ongoing risk assessment. The level of detailed information requested may be dependent on the materiality and complexity of the transaction as well as the assessed likelihood and potential severity of loss due to default, after considering collateral, controls, and other mitigating factors. For example:
  - ~~Require reporting~~Reporting on the reinsurer (noting that other jurisdictions may have disclosure limitations). Examples include:
    - Financial condition of the reinsurer quarterly,
      - i. For Example: include RBC calculations for the entity under the fully compliant U.S. statutory basis and ~~foreign jurisdiction's approach~~under its domestic regulatory accounting requirements.
    - Audited financial statements of the reinsurer.
    - ~~Mid-year u~~Unaudited statements of the reinsurer~~. The financial statements audited are~~ (if possible, prepared under US GAAP and GAAS)~~,~~ and supplemental notes that provide detail on reserves/ capital, investments, and reinsurance activities.
    - Reinsurer's ~~annual~~ standalone cash flow testing results/memorandum, actuarial valuation report.
    - Assets supporting ~~that~~ the ceded business and asset adequacy testing that the reinsurer provides to their foreign regulatory authority.
    - ~~For~~The foreign regulatory authority's examination or inspection report of the reinsurer.
  - ~~Require reporting~~Reporting on the cedent in addition to statutory filing requirements (to the extent that it is not duplicative), such as:
    - Actuarial Opinion and the supporting Memorandum annually, as well as reporting of mortality and policyholder behavior experience development vs. pricing expectations
    - Regular summary reporting of all transactions, or other material blocks of business ceded (e.g. annual in conjunction with AG55 requirements).
  - ~~Require reporting~~Reporting on the transaction, specifically, noting that in unaffiliated transactions the cedant may not be aware of all of the aspects of the reinsurer's business plan or global risk management strategy and may not be able to compel their disclosure if they are not contractually required.
    - ~~Quarterly summary reporting of all transactions, or other material blocks of business ceded.~~
    - Gain an understanding of the operating results of the entire reinsurance structure from the perspective of each party involved, (i.e., cedent, reinsurer/retrocessionaire, unauthorized offshore reinsurer), noting constraints on availability referenced above

- Confirm if the transaction is subject to AG55 reporting
- Consider requesting projections of all material components of the reinsurance structure if not subject to AG55, with focus on impact to the cedant

EXAMPLE REPORTING REQUEST:

The following is an example of a detailed business plan request:

1. Request an updated business plan including the business purpose, investment guidelines ~~_____~~ and quarterly projections for operations of the entire reinsurance structure, including projection of all pertinent aspects of the business ceded from the perspectives of all entities in the reinsurance structure.
    - Three projections, each for twenty years, as the risk flows from entity to entity.
        - One is a level equity and interest projection to represent a baseline expectation.
        - Two projections from the 1000 stochastic projections developed as part of the quarterly reserve and capital calculation. The two projections represent the 15th and 5th worst ending surplus positions and are intended to approximate moderately adverse and minimum capital level projections.
    - The projections provide,
        - Broadly, product/treaty level detail as well as the aggregated cash flows. Annual projected amounts for reserves, capital, net after tax income, capital transfers among the entities within the system, and cedent RBC, among many other variables are provided for the system.
        - Present value of projected capital contributions from cedent to the reinsurers for each scenario.
        - Cedent's starting statutory reserve and details the ceded and assumed amounts throughout the system, giving insight into the amount of reserve and capital relief provided by the structure.

- If the agreement was approved by the Department, assess the compliance with the terms and conditions of any MOU, contractual agreement or conditions placed on the approval of the transaction.
- Conduct periodic in-depth meetings with the cedent's senior management where agenda items may include:
    - Financial/operating results for all material entities in the reinsurance structure on a U.S. statutory basis and pro-forma RBC, where relevant and available
    - ~~Company~~ Relevant initiatives and filings
    - Investment reporting on the assets supporting the agreement including investment income results, rebalancing, and monitoring
    - New sales reporting, and other supplemental information ~~depending on~~ that is relevant to the block of business ceded
    - Compliance with pre-approval conditions

- For the next scheduled examination, recommend the examiner verify the funds-held assets associated with foreign reinsurers to ensure existence, accuracy, and admissibility; and review of the reinsurance agreements for proper risk transfer.

Yellow Highlights – Changes recommended by Commentors that Staff supports accepting.
Grey Highlights – Edits recommended by Staff.

Special Notes:

The following procedures do not supersede state regulation but are merely additional guidance analysts may consider useful only if the state has adopted the *Insurance Holding Company System Model Regulation with Reporting Forms and Instructions*, (#450).

Form D – Prior Notice of a Transaction

Form D is transaction specific and is not part of the regular annual/quarterly analysis process. The review of these transactions may vary as some states may have regulations that differ for Form D.

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Assessment of Form D – Asset Intensive Reinsurance Transactions with Unauthorized ~~/Offshore~~ Reinsurers in Offshore Jurisdictions

Best Practices for Review of the Agreement:

Reinsurance transactions with unauthorized reinsurers in foreign/offshore jurisdictions ~~that are unauthorized and~~ (not reciprocal or certified reinsurers), may be based on capital and reserving standards that vary materially from U.S. standards. Therefore, it is important when reviewing these ~~unauthorized~~ transactions to understand the foreign jurisdiction's regulatory framework and the financial impacts of the transaction.

In addition to the procedures described above for Form D review, consider the following best practices for review, and pre-/post-approval considerations, of ceded reinsurance transactions with unauthorized reinsurers in offshore jurisdictions.

Coordination with other regulatory agencies should be prioritized where possible to ensure consistent and risk-aware guidance from all regulators. The best practices listed below are context dependent. Input from the reinsurer's domestic regulator may be helpful in determining what guardrails are most prudent.

To support an effective and efficient review, regulators may consider focusing initially on the most relevant information and expanding the scope of analysis where preliminary findings suggest additional review would be beneficial.

Note: While some of the following best practices may be relevant and useful for any unauthorized offshore reinsurance agreement, the following are intended primarily for life asset intensive life reinsurance agreements.

Analytical Tools and Practices

1. Assess the companies' governance and controls to monitor and mitigate risks such as reinsurer credit risk; identify information that can be obtained from companies' existing processes as well as potential blind spots.
2. Request information to complete the review. See the example. ~~such as:~~

EXAMPLE INFORMATION REQUEST

The following is an example of items to consider ~~include~~ in a request for information:

a. A business plan that includes the business purpose of the transaction, and projections including a three-year proforma financial statements and RBC for the insurer and the reinsurer.
    i. For the reinsurer, recommend amounts be reported not only in the framework that will be reported to the reinsurer's foreign regulatory authority but also request, at a minimum, a balance sheet and income statement for the reinsurer using U.S. GAAP presentation and U.S. Statutory presentation.
b. All licensing and other relevant transaction documents (e.g. master transaction agreement, reinsurance agreement, supplemental trust agreement, related investment management agreement, etc.)
c. Accounting narratives that fully explain the accounting of the transaction.
d. Company's risk transfer analysis

3. Utilize the Macroeconomic Working Group Reinsurance Worksheet, where appropriate. Note that Worksheet's may need to be modified and customized accordingly, for example, to work with funds withheld agreements, or where the U.S. state insurance regulator is imposing specific requirements~~–~~, in particular requirements based on US RBC ~~such as those based on fully compliant U.S. RBC~~.
4. Transactions should undergo review by both the analyst and supervisor and based on complexity, may also undergo an additional supervisory review.
5. Communication and Coordination with the entities during the review process, for example:
    a. ~~Require in-person~~ In-person meetings with the Company for transaction walkthroughs and initial discussions
    b. Weekly standing meetings with both the Company and the actuarial or other specialists assisting on the review.
6. Communicate with the unauthorized reinsurer's regulatory authority to discuss the transaction, gain an understanding of the foreign jurisdiction regulator's oversight and any concerns with the reinsurer.
7. Retain an actuarial specialist and/or an investment specialist to assist in the review of the transaction.
8. Perform an independent review conducted by a senior analyst in conjunction with a separate review performed by the specialists.

Analysis Procedures, in addition to general Form D procedures outlined above:

9. Perform a detailed review of all legal agreements.
    a. Assess if the transaction ~~contains all required arms-length terms and provisions.~~meets the requirements of the state's Holding Company Systems statute~~.~~, for example arms-length terms and provisions.
    b. Does the transaction contain ~~all contractual protections as in 3rd party transactions in order to support the arms-length standard under the~~ appropriate contractual protections against counterparty credit risk including, for example, collateral and recapture terms~~state's Insurance Holding Company Systems statute, including terms around overcollateralization, recapture and dividend restrictions;~~ and dividend restrictions?
10. Review the investment guidelines.

a. Do they define the asset classes eligible for the FWA/ the credit quality, duration, and concentration limits, with sub-limits by instrument and class?
b. Confirm that the management of the assets supporting the transaction are aligned with the cedent's investment policies and guidelines. Where not, identify reasons for the difference and assess the materiality and potential impact. ~~Confirmed that the assets supporting the transaction would be managed using the same investment policies and guidelines required for the cedent.~~
c. Review the investment and custody rules. Does the investment management agreement subject the manager to the policies established without authority to withdraw or transfer the assets? For funds withheld and modified coinsurance agreements, ~~Do~~ do the custody and title remain exclusively with the cedent?

11. Gain an understanding of the accounting framework being used by performing ~~Perform~~ a detailed actuarial review of material items:
    a. ~~Any alternative reserve methodology and plan of operations of the reinsurer~~ The reserve methodology (including if different from U.S. reserving standards), the plan of operations of the reinsurer, or changes in those plans, relevant to the the transaction.
    b. Pre-reinsurance vs post-reinsurance balance sheets, ceding commissions
    c. A comparison of the reserve and capital requirements for onshore vs offshore
    d. Recapture provisions
    e. Investment guidelines
    f. Company's standalone cash flow testing
2. Gain an understanding of any reinsurance collectability concerns
12. Perform a detailed review of the Company's risk transfer analysis to identify any terms that highlight concern or that could limit risk transfer. Determine if the agreement transfers risk.
13. Perform a limited-scope examination, if determined necessary, over standalone asset adequacy testing ~~for high-risk transactions~~
14. Assess the effectiveness of the cedent's counterparty risk mitigation, noting that different reinsurance structures may require different solutions (for example, if assets are in a trust or not). Gain an understanding of the basis for managing the solvency of the reinsurer.

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EXAMPLE REINSURANCE AGREEMENT TERMS:

The following is an example of terms of an agreement that were intended to help mitigate financial risk of failure:

a. *100% Quota Share Coinsurance w/ Funds Withheld* Coinsurance or Modified Coinsurance in place of ordinary coinsurance
b. *Assets with Book Value equal to 100% of U.S. Statutory Reserves retained on cedent's balance sheet.*
c. *Supplemental Trust with additional assets equal to 4.5% of U.S. Statutory Reserves are required to be held in a supplemental trust as overcollateralization with a US bank as Trustee.*
d. *Granular negotiated investment guidelines subject to state insurance department approval– i.e., failure to retain RBC ratio triggers more conservative investment guidelines.*
e. *Market-to-Book* Restrictions: Limitations or conditions on collateral assets when the market value of such assets is less than *85% of book value of those assets.*
f. *Excess collateral may not be withdrawn by reinsurer if RBC ratio is less than 250% CAL (500% ACL), calculated on a fully compliant U.S. statutory basis, or if the Market Value of collateral assets is less than 90% of book value.*
g. *Reinsurer cannot pay dividends if RBC ratio is less than 250% CAL (500% ACL) calculated on a fully compliant U.S. statutory basis.*
h. *Parental Guarantee*
i. ~~*Cedent can elect to*~~ *Recapture permitted if the reinsurer's RBC ratio falls below 200% CAL (400% ACL) or if the reinsurer fails to pay any amount due, including topping up the collateral accounts. If collateral fell to a specified percentage, such as 105%, and the reinsurer fails to top off, the cedent can recapture with full access to all 105% of statutory reserves in collateral.*
j. *Two layers of collateral: The funds withheld* ~~*trust*~~ *account must be equivalent to 100% of the*

15. Assess the ~~monthly settlement~~settlement mechanics. Is the settlement a cash settlement? Does it include a reconciliation of required reserves vs. the funds withheld asset balance with ~~monthly~~ scheduled top-off ~~by cedent~~, and top off of the Trust Account to a specified level?
16. Assess the termination and recapture triggers. Does the agreement provide~~s~~ for the cedent's right of recapture upon a reinsurer's insolvency event, ~~RBC~~capital (e.g., RBC) Level, and provides for a notification trigger upon the ~~ACL RBC~~capital ratio (e.g., RBC) falling below a specified level, e.g. 300% RBC.

Best Practices for Pre-Approval of the Transaction

Consider entering into a Memorandum of Understanding (MOU) or similar contractual agreement, or require conditions as part of the final approval of the transaction MOU~~-~~s. The terms of the MOU between the cedent and the insurance department or conditions for approval could include reporting, notification and capital requirements. For example:

EXAMPLE MOU:

The following is an example of terms of a Memoradum of Understanding as part of approval of the transaction:

1. For Modco and Funds Withheld agreements the cedent retains at all times the legal title and custody of the assets. ~~of the Funds Withheld Account (or Trust account)~~ For collateral held in trust, the assets are held in the name of the trustee.
    a. Funds withheld assets are held in a Trust where cedent is grantor and reinsurer is beneficiary. All assets are held on cedent's balance sheet in a segregated custody account in US banks.
    b. Investments held in the Funds Withheld Account account shall be in the name of the cedent.
    c. Custody is operated through a qualified custodian.
2. Funds Withheld Account or Trust account is established at, for example, 5% over the required statutory resources, where the Trust is voluntary contractual collateral, i.e. security, not for reinsurance credit.
3. Consider basing the terms of the agreement ~~Require the terms of the agreement to be based~~ on fully compliant U.S. Statutory Reserves and RBC, irrespective of how the foreign regulatory authority monitors solvency.
4. Consider ~~Require~~ restrictions on dividend and capital distributions without first obtaining Department approval.
    a. For example, the reinsurer cannot pay dividends within its first year. Subsequently it cannot pay dividends that will cause its RBC ratio to fall below, for example, 350% CAL RBC.
    b. For example, the cedant cannot pay dividends should its CAL RBC ratio fall below a sliding scale, for example, that starts at 400% and ends at 350% over 8 years. Any ordinary or extraordinary dividends require Department approval for the first three years after the transaction closes.
5. Consider requiring notification to the Department, such as for future or contemplated affiliated and non-affiliated reinsurance transactions, qualified financial contracts
6. ~~Require~~ Consider parental guarantees or keep-well agreements assuring the parent will provide capital support to maintain a certain RBC level or to ensure claims payments.
7. To the extent not already required by AG55, consider to monitor mortality and policyholder behavior experience, actual vs. expected, consider requiring on an annual basis, the cedent perform Asset Adequacy Testing for the ceded policies, under the same requirements and moderately adverse scenarios and using the same assumptions it uses for Asset Adequacy Testing generally, but on a stand-alone basis for the business subject to reinsurance. The results of the stand-alone Asset Adequacy Testing, including a summary of the analysis, assumptions, and results, would be submitted to the department as a separate opinion of the Appointed Actuary, concurrently with the filing of the annual Actuarial Opinion. To the extent that the funds withheld assets, exclusive of any Letters of Credit, are insufficient to satisfy all cash flows under such analysis, the cedent could be required to establish additional reserves ~~will be established at the cedent~~ accordingly. the cedent will submit to the department a separate opinion of the Appointed Actuary, summarizing the analysis, assumptions, and results of the stand-alone Asset Adequacy Testing.

EXAMPLE MOU, continued:

a. On an annual basis the cedent would ~~will~~ report on mortality experience, including expected to actual, along with any changes in mortality assumptions used in establishing reserves.
b. The Cedent would ~~will~~ make submissions to the Department for prior approval for additional cessions on an ongoing basis.
c. The Cedent would ~~will~~ report a quarterly summary of transactions to date on a level of detail as requested by the Department.
d. Targeted restrictions (for example, taking into consideration the location of the assets) on retrocessions without the prior approval of the department could be established to ensure that assets remain available to meet policyholder obligations, or for other purposes as specified by the Department. Any violation of this restriction ~~will~~ would result in the automatic retraction of the Department's approval.
e. Failure to comply with these conditions ~~will~~ would result in retraction of the Department's approval.

8. Where there are material differences in regulatory standards and reasonable approximations can't be developed, consider requiring ongoing reporting whereby the foreign reinsurer provides annual financial statements and CAL RBC ratio with reserves and capital including asset adequacy testing and RBC, in accordance with U.S. Statutory accounting, and U.S. RBC standards.
9. Require AG-55 Reporting or some subset thereof.
10. Quarterly reporting requirements for all entities in the reinsurance structure.
    a. "Reinsurance structure" in this best practice refers to the cedent, any reinsurer/retrocessionaire(s) in the middle, and the offshore unauthorized reinsurer, for a specific block of business.
    b. Capital ratio reporting for all entities in the reinsurance system, for example, X% capital ratio. This requirement is a minimum threshold set by the Department to act as a regulatory backstop to apply a consistent lens across the various regulatory regimes
    c. This quarterly reporting is intended to allow the Department to proactively identify capital adequacy trends or declines in RBC, and take appropriate regulatory action, well before reaching the 300% minimum. Consider requiring similar thresholds for recapture triggers or other risk-mitigating solutions in the reinsurance contract.
    d. Minimum RBC requirement for all entities in the reinsurance system, for example, CAL RBC 300%. The RBC requirement is a minimum threshold set by the Department to act as a regulatory backstop to apply a consistent RBC lens across the various regulatory regimes.
11. In addition to quarterly financial statements and RBC of the reinsurer, request the cedent provide quarterly and annual information detailing various aspects of the treaties, including:
    a. Asset-liability management data
    b. Investment guidelines compliance report
    c. Reinsurer's actuarial report
    d. Reinsurer's audited financial statements
    e. Peer review report on the work of the appointed actuary
    f. Summary of settlement activity
    g. Internal capital calculations

Post-Transaction Ongoing Monitoring – Analysis or Examination

After closing the transaction and during future ongoing monitoring, the analysis should focus on assessing the financial solvency of the reinsurer as well as the cedent, compliance with any terms or conditions of the approval and assessing the ongoing reserve adequacy, credit quality of supporting assets, counterparty risk, and risk mitigating strategies. See guidance and procedures in the Credit Risk and Life Reserve Risk chapters III.B.1 and III.B.8.ii. for Credit Quality, Adequacy and Appropriateness of Assets Held for Modco or FWH Agreements and Actuarial Guideline-55 review.

J. Insurers in Run-Off

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Insurance Business Transfers (IBT's) and Corporate Divisions (CD's)

Background:

Over the past few years, states have begun enacting statutes which provide opportunities for solvent insurers considering run-off of certain lines or their entire book of business to restructure their run-off with finality. These processes can be broken down into two categories generally referred to as insurance business transfer ("IBT") and corporate division ("CD").

An insurance business transfer (IBT) represents a transaction designed to transfer existing insurance obligations of one insurer (transferring insurer) to a second insurer (assuming insurer) without policyholder consent, subject to approval regulatory approval and court approval. While policyholder consent is not required, notice to policyholders, key stakeholders and the general public is required, and concerns regarding the transaction will be considered in the regulatory and/or court approval process. Following an IBT, the assuming insurer becomes directly liable to policyholders and the transferring insurer's obligations under the insurance policies and contracts are extinguished thereby achieving legal finality for the transferring insurer.

A corporate division (CD) is a division of one dividing insurer into two or more resulting insurers. The dividing insurer's assets and liabilities are allocated between or among the resulting insurers without requiring affirmative policyholder consent. Following a CD, the resulting insurer(s) becomes directly liable to policyholders and the dividing insurer's obligations under the insurance policies and contracts are extinguished thereby achieving legal finality for the dividing insurer.

Transaction Review Framework

Analysts should utilize the Best Practices Procedures for IBT/Corporate Divisions in Chapter IV.(tbd) when reviewing insurance business transfers (IBTs) and corporate divisions (CDs). Both transaction types can shift policy obligations without affirmative policyholder consent, so the guidance emphasizes robust regulatory review, transparency, and protections designed to ensure that policyholders, claimants, reinsurers, guaranty associations, and other stakeholders are not materially adversely affected. The review framework outlined in the Best Practices outlines key steps in the analyst's review process. It is organized around gaining a complete understanding of the transaction: who the involved insurers are, how the transaction is structured, what assets and liabilities will move, how capital and reserves will be affected, and whether the post-transaction entity will remain financially sound.A central theme is the need for independent, well-documented analysis. . In addition, it is recommended that the state(s) of domicile of the companies undergoing the IBT/CD should contact all states licensed to determine if there are any anti-novation statutes that would prohibit the IBT/CD or require additional regulatory approval from the licensed state before the IBT/CD is ultimately approved by the state of domicile.

Analysts should refer to the ~~work of the Restructuring Mechanisms (E) Working Group, including the "~~*Restructuring Mechanisms – An NAIC White Paper*~~" and the regulatory "Best Practices Procedures for IBT/Corporate Divisions"~~ for additional information specific to IBTs and CDs that may warrant consideration in the analysis and solvency oversight of these entities.

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Section II: Current Period Analysis

---DETAIL ELIMINATED TO CONSERVE SPACE---

7. Compliance Analysis: Review and assess state-specific compliance or other analysis required by the state insurance department. Document risks identified and assessed in the appropriate branded risk category of Section III: Risk Assessment~~.~~ (i.e., Compliance with state statutes and regulations, including those that are new or revised (e.g., hazardous financial condition analysis, investment limitation analysis, etc.) and compliance with the statutory minimum amount of surplus as required by state law (varies by state and business type).

~~a. Identify if the insurer is compliant with state statutes and regulations, including those that are new or revised (e.g., hazardous financial condition analysis, investment limitation analysis, etc.).~~

~~b. Assess if surplus meets the statutory minimum amount required by state law (varies by state and business type).~~

Section IV: Update Insurer Profile Summary (IPS)

---DETAIL ELIMINATED TO CONSERVE SPACE---

Summary and Conclusion: Develop an overall summary and conclusion based on the completion of the risk-focused analysis performed, and document it by updating the IPS, including the Supervisory Plan, if applicable~~, for the following:~~. No documentation of the summary and conclusion is required in Section IV of the RAW.

Examples of what ~~, but~~ the IPS should address, include: ~~the following topics:~~ ~~S~~Summary of the ~~above~~ risk-focused analysis results by risk classification; Prospective risks of the insurer in current analysis, as well as to identify future areas for analysis; ~~I~~impact of the holding company on the insurer; ~~C~~completed or in-progress communication or other follow-up with the insurer, other areas of the Department of Insurance (DOI), financial examiners and other state insurance regulators; ~~A~~additional analysis yet to be performed; ~~R~~regulatory actions; and, ~~A~~any other factors or information that, in the analyst's judgment, are relevant to evaluating the insurer's overall financial condition.

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Use of Artificial Intelligence Tools in Financial Analysis Work

If state insurance departments utilize artificial intelligence (AI) tools within financial analysis these tools should be used in a manner consistent with applicable confidentiality requirements. Given the nature of analysis information being confidential, non-public, personally identifiable, or proprietary, analysts should not input this information into external, public-facing AI platforms. Such information includes, but is not limited to:

- Insurer-specific financial or operational information
- Analysis workpapers
- Internal insurer communications or documents
- Any information protected under law, statute or regulation

To safeguard confidential information, analysts should limit their use of tools to those expressly approved by the state insurance department and hosted in secure, department-managed environments. If a secure AI tool is not available, analysts must ensure that any data is fully anonymized to remove any non-public or sensitive information. The expectations contained in this section apply equally to state insurance department analysts as well as any contract analysts or vendors a department may use in the course of analysis work.

A detailed review of the workpapers is especially critical if the analysis is utilizing AI during the analysis. The guidance applies when the use of AI contributes to the development of analysis evidence and does not apply to basic rewording, proofreading, and editing. Analysts should review and validate the accuracy, appropriateness, and relevance of any AI output used in the analysis process.

If AI-generated outputs are incorporated into analysis work, the analyst should also document the nature of the AI usage. Documentation should indicate which tool was used and that the analyst reviewed and validated the content prior to its inclusion.

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Commented [JK1]: For FASTWG Discussion. See APCIA comment suggesting this sentence be deleted. Note that this text was copied from existing guidance in the FCEH.

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

Understand the Insurance Holding Company System

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

Conduct Detailed Analysis of the Insurance Holding Company System

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

10. Group Capital Calculation (GCC):

    If the insurance group is subject to the requirements to perform and file a Group Capital Calculation (GCC), review and determine if any concerns or material risks exist regarding the overall group capital position, quantifiable risks, or capital interdependencies within the group as may be identified through analysis of the GCC. See chapters VI.H and VI.I for applicable optional GCC procedures and guidance.

PROCEDURE #10 instructs the analyst to evaluate the Group Capital Calculation (GCC) filing, if the insurance group is subject to GCC filing requirements. Analysts may consider optional procedures outlined in chapter VI.H when completing this assessment. Refer to additional guidance on the GCC in chapter VI.I.

VI.H. Group-Wide Supervision – Group Capital Calculation (Lead State) Procedures

GCC as Input into Group Profile Summary

The GCC is intended to be used as an input into the GPS. The expectation is that the GCC summary section will help to document a high-level summary of the analyst's take away of the GCC, as well as the Strategic branded risk. The manner in which the analyst determines what else should be documented beyond the GCC Summary and the Strategic branded risk should be based upon the following steps, since these steps contemplate the previously mentioned concept that the existing evaluation of the financial condition should be used in evaluating the depth of review of the GCC. Therefore, the following procedure steps are optional and should be customized to the evaluation of the GCC and the group's financial condition. The depth of the review in the "five-step process" and specific inquiries will vary based on each group's unique situation.

VI.I. Group-Wide Supervision – Group Capital Calculation (Lead State) – Analyst Reference Guide

Purpose of the Group Capital Calculation (GCC) in Holding Company Analysis

Background Information

In 2008, the NAIC Solvency Modernization Initiative (SMI) ~~began to~~ considered whether there were any lessons learned from the financial crisis that would cause the solvency framework to be modified. The NAIC determined that changes should be made in the area of group supervision, starting with the ~~new~~ annual requirement for the lead state of each group operating in the U.S. to complete a written holding company analysis. Since that time, other changes to state laws have been made to further enhance group supervision (e.g., Form F, Own Risk and Solvency Assessment (ORSA), ~~and~~ Corporate Governance reporting, Group Capital Calculation reporting). All of these ~~new~~ tools are inputs into the previously mentioned holding company analysis, which is summarized into the Group Profile Summary (GPS), a consistent tool used by all states~~, that is known as the Group Profile Summary (GPS)~~.

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

Staff Note: The following edits are added to align with existing guidance in the GPS Example (VI.C.1), therefore these changes do not represent new Handbook guidance.

Contents of the Group Profile Summary (GPS)

The following analysis work should be documented in the GPS. See the GPS example in chapter VI.C.1 for additional guidance and sample text:

- **Financial Snapshot (Selected Summary Data)** - Present financial data as well as any notes and explanations of the data to outline the group's financial position, segment performance and other key information that is customized and relevant for an understanding of the specific group.
- **Group Capital Calculation Summary** - Present a summary of an assessment of the GCC both quantitatively and qualitatively, including any such items as may not be applicable to a branded risk category. The GCC summary is intended to be high-level. Therefore, other more detailed observations from reviewing the GCC should generally not be documented into the GPS unless they are specifically insightful, add to a high-level understanding of the Group's financial condition, or are specific to a branded risk category as stated.

NAIC NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

MEMORANDUM

TO: Danielle Smith (MO), Chair, Financial Analysis Solvency Tools (E) Working Group

FROM: Mike Yanacheak (IA), Co-Chair and Jack Broccoli/ William Arfanis (CT) Co-Chairs, Own Risk Solvency Assessment (ORSA) Implementation Subgroup

DATE: June 12, 2026

RE: ORSA Review Template Revisions Related to Overarching Issues Guidance

The Own Risk and Solvency Assessment (ORSA) Implementation (E) Subgroup meets periodically to discuss, among other matters, revisions to the ORSA Guidance Manual. During these meetings, the Subgroup also considers alignment between the ORSA Guidance Manual and the ORSA Review Template contained in the Financial Analysis Handbook (FAH), including the treatment of overarching issues.

As a result of these discussions, the ORSA Subgroup is referring the following issue to the Financial Analysis Solvency Tools (E) Working Group for consideration.

The proposed revision to the ORSA Review Template would add a section for regulators to document overarching issues identified during the review of an ORSA filing. This addition is intended to enhance regulatory documentation by capturing significant contextual matters that may materially inform the ORSA review. While such a section may not be necessary for every ORSA filing, its inclusion, when appropriate, would provide important context and support a more effective understanding of both the filing and the associated review.

In addition, corresponding guidance is proposed for inclusion in the Financial Analysis Handbook to support completion of the ORSA Review Template. This guidance would include a summary of overarching issues, along with illustrative examples. The proposed section would enable analysts to identify and summarize significant cross-cutting considerations, such as the influence of foreign regulatory frameworks; dividend-paying capacity that relates to goals, limits, risks, stresses, and capital; and the omission of material risks from the ORSA. These considerations may materially inform the ORSA review and provide important context for the scope and depth of documentation reflected in the regulatory Lead State ORSA Review Template.

Thank you for your consideration of this referral. Please see the attached materials for the proposed language and placement within the Financial Analysis Handbook.

To facilitate alignment and timing of revisions to both the Financial Analysis Handbook and the ORSA Guidance Manual in advance of the Summer National Meeting, this referral is being provided while the related ORSA Guidance Manual changes are also out for exposure and subsequent public adoption. The Subgroup encourages monitoring these efforts and coordinating, as appropriate, to maintain consistency between the Financial Analysis Handbook and the ORSA Guidance Manual with respect to the ORSA Review Template- Overarching Issues Guidance.

If there are any questions regarding the issues discussed, please contact me or NAIC staff (Sherry Flippo sflippo@naic.org) for clarification.

EXAMINATION OVERSIGHT (E) TASK FORCE
FINANCIAL ANALYSIS SOLVENCY TOOLS (E) WORKING GROUP

SUBMIT TO
NAIC – KC
By June 1, 2026

Financial Analysis Handbook Proposed Revision Form

INSTRUCTIONS	FOR NAIC USE ONLY
1. Complete this form for EACH Handbook proposal. Under "Identification of Item(s) to be Changed," include section & page number, line or item identifier. 2. All attachments should be presented in a format wherein new language is underscored and deletions struck through. 3. Please consider whether this revision proposal is also addressed elsewhere in the Handbook. 4. CAUTION: before completing this form, please read additional instructions on reverse side of this form.	DISPOSITION [ ] ADOPTED [ ] REJECTED [ ] DEFERRED [ ] OTHER (SPECIFY) [ ] _____
DATE: 6/11/2026 NAME: ORSA Subgroup -Sherry Flippo, NAIC staff TITLE: STATE: ADDRESS: TELEPHONE: CONTACT PERSON : sflippo@naic.org	NOTES

HANDBOOK SECTION NAME AND NUMBER TO WHICH PROPOSAL APPLIES

If STATEMENT TYPE SPECIFIC, ALSO IDENTIFY THE TYPE:

[ ] Life/A&H [ ] Property & Casualty [ ] Title [ ] Health

All statement types

IDENTIFICATION OF ITEM(S) TO BE CHANGED

- **The ORSA Lead State Review Template**
- **Narrative guidance related to the ORSA Lead State Review Template**
- **Illustrative examples of situations that might *warrant* disclosure of an overarching issue affecting the entire ORSA**
- **See attached proposed wording and placement**

REASON OR JUSTIFICATION FOR CHANGE **
(STATE, IN SPECIFIC TERMS, THE BENEFIT TO BE DERIVED FROM THIS PROPOSAL)

**** This section must be completed on all forms.**

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The ORSA and the ORSA Lead State Review Template may identify broad, overarching issues that, when clearly summarized, help convey key themes to readers of the Lead State ORSA Review Template. While this section may not be necessary for every ORSA filing, its inclusion—when appropriate—provides important context and supports a more effective understanding of the ORSA and the associated review. Illustrative examples of such overarching issues may include the use of a group-wide risk management or capital framework (e.g., a Solvency II–based framework) that drives risk identification, stress testing, and capital assessment across jurisdictions, or other enterprise-level considerations that influence multiple components of the ORSA.

Additional Instructions and Information

The Financial Analysis Solvency Tools (E) Working Group meets via conference call throughout the year to consider proposed changes to the NAIC *Financial Analysis Handbook* (Handbook). Suggestions to the Handbook should be submitted by **June 1, 2026**. Send proposals via email to Ralph Villegas, Life/Health Financial Analysis Manager, rvillegas@naic.org, or send to Rodney Good, Property/Casualty Financial Analysis Manager, rgood@naic.org. Original copies may be sent to:

National Association of Insurance Commissioners
Financial Analysis & Examination Unit
Financial Regulatory Services Department
1100 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

For questions, call the Financial Analysis & Examination Unit at (816) 842-3600.

Proposed Revisions

- During the Working Group's review, changes proposed via this form will be considered along with an analysis conducted by the NAIC Financial Analysis & Examination Unit of the effectiveness and usefulness of procedures, ratio limits and language.

- The NAIC Financial Analysis & Examination Unit also studies adopted changes to the Annual Statements and provides revision proposals to the Working Group. The NAIC Financial Analysis & Examination Unit automatically makes changes to the Handbook for minor changes, such as for page and line numbers.

- The Handbooks are automated on i-Site+. The Handbook is intended to be a dynamic tool. The Working Group is interested in feedback on both analytical and software features. Please contact the NAIC Help Desk at (816) 842-3600 before submitting a form. Many enhancements have been proposed which could not be implemented. Also, some proposals may relate to existing features that the Help Desk may be able to explain.

**** This section must be completed on all forms.**

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INTRODUCTION

The process for assessing enterprise risk management (ERM) within the group will vary depending upon its structure and scale. Approximately 90 percent of the U.S. premium is subject to reporting an annual Own Risk Solvency Assessment (ORSA) Summary Report. However, all insurers are subject to an assessment of risk management during the risk-focused analysis and examination, and this review is a responsibility of the lead state. In addition, all groups are required to submit the Form F - Enterprise Risk Report under the requirements of the NAIC *Insurance Holding Company System Regulatory* Act (#440) unless they have been granted an exemption by the state. In addition, both the ORSA Summary Report and the Form F are subject to the supervisory review process, which contemplates both off-site and on-site examination of such information proportionate to the nature, scale and complexity of the insurer/group's risks. Those procedures are discussed in the following two sections. In addition, any risks identified throughout the entire supervisory review process are subject to further review by the lead state in either the periodic meeting with the insurer/group and/or any targeted examination work. When reviewing the ORSA and Form F, the lead state analyst should consider consistency between the documents, as well as information provided in the Corporate Governance Annual Disclosure (CGAD).

ORSA SUMMARY REPORT

The NAIC *Risk Management and Own Risk and Solvency Assessment Model Act* (#505) requires insurers above a specified premium threshold, and subject to further discretion, to submit a confidential annual ORSA Summary Report. Model #505 gives the individual insurer and the insurance group discretion as to whether the report is submitted by each individual insurer within the group or by the insurance group as a whole. Regardless of whether the ORSA is filed on an individual or group basis, any noninsurance operations that present material and relevant risks to the insurer should be included in the scope of the ORSA Summary Report. (See the NAIC *Own Risk Solvency Assessment Guidance Manual* (ORSA Guidance Manual) for further discussion).

- **Lead State:** In the case where the insurance group chooses to submit one ORSA Summary Report for the group, it must be reviewed by the lead state. The lead state is to perform a detailed and thorough review of the information and initiate any communications about the ORSA with the group. The suggestions below set forth some possible considerations for such a review. At the completion of this review, the lead state should prepare a thorough summary of its review, which would include an initial assessment of each of the three sections. The lead state should also consider and include key information to share with other domestic states that are expected to place significant reliance on the lead state's review. The lead state should share the analysis of ORSA with other states that have domestic insurers in the group. The group ORSA review and sharing with other domestic states should occur within 120 days of receipt of the ORSA filing.

- **Non-Lead State:** Non-lead states are not expected to perform an in-depth review of the ORSA, but instead rely on the review completed by the lead state. The non-lead states' review of the lead state's ORSA review should be performed only for the purpose of having a general understanding of the work performed by the lead state, and to understand the risks identified and monitored at the group-level so the non-lead state may better monitor and communicate to the lead state when its legal entity could affect the group. Any concerns or questions related to information in the ORSA or group risks should be directed to the lead state.

- **Single Insurer ORSA:** In the case where there is only one insurer within the insurance group, or the group decides to submit separate ORSA Summary Reports for each legal entity, the domestic state is to perform a detailed and thorough review of the information, which would include an initial assessment of each of the three sections and initiate any communications about the ORSA directly with the legal entity. Such a review should also be shared with the lead state (if applicable) so it can develop an understanding of the risks within the entire insurance group. Single insurer ORSA reviews should be completed within 180 days of receipt of the ORSA filing.

Throughout a significant portion of the remainder of this document, the term "insurer" is used to refer to both a single insurer for those situations where the report is prepared by the legal entity, as well as to refer to an insurance group. However, in some cases, the term group is used to reinforce the importance of the group-wide view. Similarly, throughout the remainder of this document, the term "lead state" is used before the term "analyst" with the understanding that in most situations, the ORSA Summary Report will be prepared on a group basis and therefore reviewed by the lead state.

Background Information

To understand the appropriate steps for reviewing the ORSA Summary Report, regulators must first understand the purpose of the ORSA. As noted in the ORSA Guidance Manual, the ORSA has two primary goals:

1. To foster an effective level of ERM at all insurers, through which each insurer identifies, assesses, monitors, prioritizes and reports on its material and relevant risks identified by the insurer, using techniques that are appropriate to the nature, scale and complexity of the insurer's risks, in a manner that is adequate to support risk and capital decisions.
2. To provide a group-level perspective on risk and capital, as a supplement to the existing legal entity view.

In addition, separately, the ORSA Guidance Manual discusses the regulator obtaining a high-level understanding of the insurer's ORSA and discusses how the ORSA Summary Report may assist the commissioner in determining the scope, depth and minimum timing of risk-focused analysis and examination procedures.

There is no expectation with respect to specific information or specific action that the lead state regulator is to take as a result of reviewing the ORSA Summary Report. Rather, each situation is expected to result in a unique ongoing dialogue between the insurer and the lead state regulator focused on the key risks of the group. For this reason, as well as others, the lead state analyst may want to consider additional support in the form of a broader review team as necessary in reviewing the ORSA Summary Report, subject to the confidentiality requirements outlined in statute. In reviewing the final ORSA filing prior to the next scheduled financial examination, the analyst should consider inviting the lead state examiner to participate on the review team. Regardless of which individuals are involved on a review team, the 120-day or 180-day timeliness standards are applicable to the review. Additionally, the lead state analyst and examiner may want to include the review team in ongoing dialogues with the insurer since the same team will be part of the ongoing monitoring of the insurer and an ORSA Summary Report is expected to be at the center of the regulatory processes.

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

General Summary of Guidance for Each Section

The guidance that follows is designed to assist the lead state analyst in the review of the ORSA and to allow for effective communication of analysis results with the non-lead states. It is worth noting that this guidance is expected to evolve over the years, with the first couple of years focused on developing a general understanding of ORSA and ERM. It should be noted that each of the sections can be informative to the other sections. As an example, Section II affords an insurer the opportunity to demonstrate the robustness of its process through its assessment of risk exposure. In some cases, it's possible the lead state analyst may conclude the insurer did not summarize and include information about its framework and risk management tools in Section I in a way that

allowed the lead state analyst to conclude its effectiveness, but in practice by review of Section II, such a conclusion was able to be reached. Likewise, the lead state analyst may assess Section II as effective but may be unable to see through Section III how the totality of the insurer's system is effective because of a lack of demonstrated rigor documented in Section III. Therefore, the assessment of each section requires the lead state analyst to consider other aspects of the ORSA Summary Report. This is particularly true of Section I, because as discussed in the following paragraphs, the other two sections have very distinct objectives, whereas the assessment of Section I is broader.

Overarching Comments on the ORSA Review Template provides a place for analysts to document broad issues affecting the overall ORSA.

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

Section I procedures are focused on assessing the insurer's overall risk management framework. The procedures are presented as considerations to be taken into account when reviewing and assessing an insurer's implementation of each of the risk management principles highlighted in the NAIC's ORSA Guidance Manual. In assessing implementation, regulators should consider whether the design of ERM/ORSA practices appropriately reflects the nature, scale and complexity of the insurer.

Section II takes a much different approach. It provides guidance to allow the lead state analyst to better understand the range of practices they may see in ORSA Summary Reports. However, such practices are not intended to be requirements, as that would eliminate the "Own" aspect of the ORSA and defeat its purpose. As such, analysts should not expect or require insurers to organize or present their risks in a particular manner (i.e., by branded risk classification). Rather, the guidance can be used in a way to allow the lead state analyst to better understand the information in this section. Section II guidance has been developed around reviewing key risks assessed by the insurer, evaluating information provided on the assessment and mitigation of those risks and classifying them within the nine branded risk classifications outlined in the Handbook, which are used as a common language in the risk-focused surveillance process for ongoing tracking and communication. As such, the analyst should attempt to classify each key risk assessed by the insurer into a branded risk classification(s) for incorporation into general analysis documentation Insurer Profile Summary (IPS) or Group Profile (GPS) as appropriate. The branded risk classifications are intentionally broad in order to allow almost any risk of an insurer to be tracked within one or more categories, but the analyst may also use an "Other" classification as necessary to track exposures.

Section III is also unique in that it provides a specific means for assisting the lead state analyst in evaluating the insurer's determinations of the reasonableness of its group capital and its prospective solvency position on an ongoing basis. Section III of the ORSA Summary Report is intended to be more informative regarding capital than other traditional methods of capital assessment since it sets forth the amount of capital the group determines is reasonable to sustain its current business model rather than setting a minimum floor to meet regulatory or rating agency capital requirements.

Overarching Comments Concerning the ORSA on the Review Template

The ORSA and ORSA Review Template may include broad, overarching issues that, when clearly summarized, help convey the key themes to readers of the Lead State ORSA Review Template. Although this section may not be necessary for every ORSA filing, its inclusion—when appropriate—provides important context that supports a more effective understanding of the ORSA and the associated review. The following examples illustrate how such overarching issues may be presented:

- ABC International Group operates across the UK, and the United States. Because most of its premiums and enterprise risk management activities are based in Europe, the risk profile and risk appetite discussed in Section 1 are dictated by the Solvency II framework. Accordingly, the group capital methodology, stress testing, coverage ratio, and projected three-year coverage ratios presented in Section 3 are also aligned with Solvency II principles and capital structure. The Solvency Capital Requirement (SCR) presented in Section 3 is the regulatory capital.

- DEF Insurance group's structure and expectations to pay dividends. In this case, dividend-paying capacity could represent a key risk, with stress testing used to evaluate scenarios that could constrain or prohibit dividend payments and corresponding capital projections prepared under varying dividend assumptions.

- HIJ Health Insurer is currently operating under an RBC recovery plan with the Department of Insurance due to a prior year-end RBC ratio in company action level. The ORSA filing identifies only operational risks in Section 1, and these are assessed qualitatively in Sections 2 and 3. The filing does not address liquidity or financial risks (e.g., pricing/underwriting, reserving, market, etc.). The analyst considers liquidity to be the company's primary risk and will request that liquidity and financial risks be incorporated into the next ORSA. Because Sections 2 and 3 contain no quantitative assessments of risk exposure or capital, the analyst did not prepare detailed documentation for those sections. The company did, however, include its most recent monthly report to the Department—containing capital levels and projections—in Appendix. This monthly report, which appears at the end of Section 3 in the template, is the most quantitative component of the submission and therefore the most helpful to that analyst.

As demonstrated by these examples, a summary of overarching issues upfront helps direct the regulators's attention to the most relevant aspects of the ORSA and therefore the ORSA Review Template rather than following the documentation strictly in sequence. It also communicates the rationale behind the level of detail included in each section of the template.

Background Information

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

- **Attestation** – The report includes an attestation signed by the chief risk officer (CRO) (or other executive responsible for ERM oversight) indicating that the information presented is accurate and consistent with ERM reporting shared with the board of directors (or committee thereof).
- **Entities in Scope** – The scope of the report is clearly explained and identifies all insurers covered. The scope of a group report also indicates whether material non-insurance operations have been covered. The lead state analyst could utilize Schedule Y, the Lead State report and other related tools/filings to review which entities are accounted for in the filing.
- **Accounting Basis** – The report clearly indicates the accounting basis used to present financial information in the report, as well as the primary valuation date(s).
- **Key Business Goals** – The report provides an overview of the insurer's/group's key business goals in order

to demonstrate alignment with the relevant and material risks presented within the report.

- **Changes From Prior Filing(s)** – The report clearly discusses significant changes from the prior year filing(s) to highlight areas of focus in the current year review including significant changes to the ERM framework, risks assessed, stress scenarios, overall capital position, modeling assumptions, etc.

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

ORSA Review Template

Group/Insurer: _____
Group Code/CoCode: _____
State _____
Valuation Date: _____
Submission Date: _____

General Instructions:

This template is intended to be used to document a review and assessment of the ORSA Summary Report by the lead/domestic state. Regulators should document the results of their annual review of the ORSA and utilize the appendixes to track and communicate feedback to the insurer and procedures for regulatory follow-up. See VI.E. Group-Wide Supervision – Enterprise Risk Management Process Risks Guidance for additional guidance in completing this template.

Prepared/Reviewed By:	Date:

Date of Last Exam:	
Date of Next Exam:	

Analyst Overarching Comments Concerning the ORSA/Review Template

Summarize any issues that dominate in the ORSA/ Review Template.

Background Information

Summarize and assess background information provided in the report, where available. Key documentation elements are presented below.

1. **Attestation**:

2. **Entities in Scope:**

3. **Accounting Basis:**

4. **Key Business Goals:**

5. **Changes from Prior Filing(s):**

SUBSEQUENT DETAIL ELIMINATED TO CONSERVE SPACE

RESERVING RISK: Actual losses and other contractual payments reflected in reported reserves or other liabilities will be greater than estimated.

The Reserving Risk Assessment is focused primarily on two key aspects of reserving: 1) reserve valuation; and 2) reserve adequacy. Analysis of reserves relies heavily on the review of the Statement of Actuarial Opinion (SAO) and other related filings. In analyzing reserving risk, the analyst may analyze specific types of reserves established by life insurers, reserving methodologies and various aspects of life, annuity, and accident and health (A&H) insurance that affect reserving. For example, an analyst's risk-focused assessment of reserving risk may consider the following areas (but not limited to):

- Reserve valuation in accordance with the appropriate valuation requirements.
- Reasonableness of valuation bases utilized, testing, assumptions, and methodologies to determine reserves.
- Adequacy of assets to support policyholder benefits.
- Appropriate reporting of reserves.
- Lines of business written by the insurer.
- Types of reserves for life, ~~accident, and health (~~A&H~~)~~ and annuity lines of business.
- Reserve development.
- Reinsurance.
- Reserving for guarantees on separate accounts.

The analyst may need to review other risks in conjunction with reserves. For example:

- Reserves are also addressed in the Actuarial Opinion Worksheet.
- Separate Accounts are also addressed in ~~the~~ Operations and Liquidity Risks.
- Surrender activity is also addressed in ~~the~~ Liquidity Risk.
- Quality and valuation of assets supporting modified coinsurance and funds-withheld reinsurance in Credit and Market Risks.

GENERAL GUIDANCE

The Annual Reserve Risk Assessment Procedures are designed to identify potential areas of concern to the analyst. While the underlying actuarial techniques relating to life, annuity, and A&H reserves are quite complicated, the analyst should remember that there are two basic objectives regarding life, annuity, and A&H reserves. The first objective is that the insurer's life, annuity, and A&H reserves are calculated using the appropriate valuation methodology (formula or principle-based), and the second objective is that the insurer's assets are adequate to support the future policy obligations. To meet the first objective, reserves for policies and contracts subject to the formula-based valuation methodology, including the formula reserves required by VM-20/VM-21/VM-22, should be calculated in accordance with the minimum formula statutory valuation standards, using the appropriate valuation assumptions and valuation methods. For policies and contracts subject to a principle-based valuation

methodology, in addition to the formula reserves, reserves should be calculated in accordance with the principle-based valuation requirements of VM-20/VM-21/VM-22.

Involvement of an Actuary: The analyst should involve an actuary where indicated in the procedures or as needed. To stay within any required deadlines for reviews, the analyst should document any greater in-depth reviews being performed by the actuary (such as involving the confidential actuarial memorandum or the confidential principle-based reserving (PBR) report for life and annuity reserves) and supplement the documentation when such actuarial review is complete. Questions or requests for assistance regarding PBR and for asset adequacy analysis may be made to the NAIC actuarial resources. Please see the NAIC website for the Valuation Analysis (E) Working Group for contact information regarding the use of NAIC actuarial resources and use of the Working Group if needed.

Depth of Review: Life, annuity, ~~PBR~~ and ~~accident and health (~~A&H~~)~~ involve many products and complex requirements. A complete determination of compliance with all of these requirements during the course of an annual financial analysis review is typically not practical for many companies. Judgment in a risk-focused approach will need to be exercised regarding greater focus and use of actuarial expertise in any procedure provided below.

ANNUAL ASSESSMENT OF ACTUARIAL FILINGS

Statement of Actuarial Opinion Based on an Asset Adequacy Analysis

To assess reserving risk, consider procedures for reviewing the Actuarial Opinion and other actuarial filings for compliance and assessment of risks. In many states, the Actuarial Opinion and related filings are reviewed by actuarial staff. Whether the SAO review is performed by the analyst or the actuary, the risk assessment provides for the results of the SAO review to be documented and communicated to the analyst.

Refer to the Overview sections at the end of this chapter for more guidance on the SAO and Asset Adequacy Analysis.

PROCEDURES #1A AND #1B. Determine that the SAO was prepared by a qualified actuary and that the reserve amounts agree with the Annual Financial Statement.

PROCEDURES #1C–#1F. Determine that the insurer's policy reserves were calculated properly in accordance with the minimum standards required by the NAIC Model Standard Valuation Law, and that the insurer's assets will adequately support the insurer's future policy obligations. The qualified actuary's opinion that the insurer's assets are adequate with regard to policy reserves provides significant comfort to the analyst that policy obligations will be met in the future.

RAAIS and Actuarial Memorandum Worksheet

PROCEDURES #2 AND #3. Review the RAAIS and document any concerns noted. For example, the analyst should further review any comments made by the appointed actuary on any interim results that may be of significant concern.

Additional prospective risk procedures the analyst may consider performing are provided if concerns exist based on the review of the RAAIS. The analyst should take into consideration the current economic environment (i.e., interest rate trends) when performing the analysis.

PROCEDURE #4. Review the actuarial memorandum that supports the SAO. The actuarial memorandum is a comprehensive document that provides an understanding of the insurer's reserves, the assets available to support the reserves, and the projected impact on the insurer's financial condition of varying economic and interest rate projection scenarios. It is not automatically filed with the Annual Financial Statement but is provided to the regulator only upon request. The decision as to whether to request the actuarial memorandum is an important

one. The actuarial memorandum should be requested for insurers with known financial problems, significant changes in product mix or investment strategy, or significant growth in a particular product line.

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

1) The number of additional interest rate scenarios that were tested identifying separately the number of deterministic scenarios and stochastic scenarios. Also identify the number of such scenarios which produced ending negative surplus values on market value basis.

2) If sensitivity testing was performed, identify the assumptions tested and describe the variation in ending surplus values on a market value basis from the base case values.

3) If negative ending surplus results under certain tests in the aggregate, the amount of additional reserve which, if held, would eliminate the aggregate negative ending surplus values.

4) The extent to which the appointed actuary uses assumptions in the asset adequacy analysis which are materially different than the assumptions used in the previous asset adequacy analysis.

5) The amount of reserves and the identity of the product lines, which have been subject to asset adequacy analysis in the prior opinion but were not subject to such analysis for the current opinion.

6) Comments should be provided on any interim results that may be of significant concern to the appointed actuary.

7) The methods used by the actuary to recognize the impact of reinsurance on the company's cash flows, including both assets and liabilities, under each of the scenarios tested.

8) Whether the actuary has verified that all options embedded in fixed income securities and equity-like features in any investments have been appropriately considered in the asset adequacy analysis.

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

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

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

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

Procedures 4.g. asks the analyst if an insurer that is within the scope of AG-55 has filed the required reporting within the AOMR. Further guidance on that reporting is provided below in procedure #5.

PROCEDURE #5. Document any concerns based on the review of the actuarial memorandum. Additional procedures the analyst may consider performing are provided if additional concerns exist based on the review of the RAAIS, the actuarial memorandum and the asset adequacy testing performed. The procedures should be used to help identify how the insurer will fund a negative cash flow. Procedures 5.a. through 5.d. are applicable to insurers utilizing the New York 7 actuarial interest rate scenario tests. Procedure 5.e. is applicable to other cash flow scenario testing. Explanations of negative cash flow provided by the appointed actuary should explain how the insurer will: 1) sell marketable assets and which type; or 2) borrow, with an explanation of any existing agreements to include security, duration and notice period required. If the appointed actuary wrote in his/her report that the insurer expects to sell assets, the modeling should be consistent for the sale of assets. Likewise, if the appointed actuary wrote that the insurer expects to borrow, then the modeling should be consistent with borrowing. If the insurer expects to borrow, the analyst should consider asking the insurer if a formal Lending Agreement is in place.

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

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

Procedure 5.g. is applicable to AG-55 reporting on asset intensive reinsurance transactions. Refer to the guidance above regarding the scope of which insurers are included in this reporting requirement. In line with the goal of AG-55 to enhance reserve adequacy requirements for life insurance companies by requiring that asset adequacy analysis use a cash flow testing methodology that evaluates ceded reinsurance as an integral component of asset-intensive business, the analyst or reviewing state actuary, should consider if the reporting identifies any concerns that may warrant further investigation or follow-up with the insurer. The analyst should also consider procedures in the Credit Risk chapter III.B.1 regarding assets supporting modified coinsurance and funds withheld reinsurance transactions in conjunction with the review of reinsurance reserves.

Non-Guaranteed Elements Opinion (if applicable)

PROCEDURE #6. Determine that a qualified actuary prepared the non-guaranteed elements opinion.

PROCEDURES #6B AND #6C. Review the non-guaranteed elements opinion in order to determine that the insurer's reserves were determined in a manner that considered the non-guaranteed elements for individual life and annuities policies.

ANNUAL RESERVING RISK ASSESSMENT

Refer to the Overview sections at the end of this chapter for more guidance on Life, Annuity, A&H and Long-Term Care reserves.

Inappropriate or Inaccurate Valuation of Life Reserves,

OR

Reasonableness of Actuarial Methodologies and Assumptions

- High Expenses affecting Cash Flow Assumptions
- Potential for Understated Life Reserves due to Spread Analysis

Determine whether the insurer's life reserves for policies and contracts subject to a formula-based valuation methodology are valued in accordance with the minimum formula statutory valuation standards. Risks include that reserves may be understated due to reserve computations that are not performed correctly; assumptions that are unreasonable or not compliant with minimum requirements; high expenses leading to cash flow deficiencies; or, spread analysis that indicates either the need to record additional asset adequacy reserves (asset liability matching (ALM)), changes to policy design to limit guaranteed returns, or potential for investment portfolio changes to improve returns. In this regard, the analyst must rely, to a large extent, on the opinion provided by the qualified actuary, the information provided in the actuarial memorandum documenting all of the asset and liability assumptions, and the methods used, and scenarios run to determine the reserve adequacy.

Qualitative and Additional Review Considerations

- Review the results of the Statement of Actuarial Opinion worksheet. Identify any concerns regarding the valuation of the insurer's reserves in accordance with minimum statutory valuation standards.
- Review the Notes to Financial Statements, Note #31 – Reserves for Life Contracts and Annuity Contracts and note any unusual items regarding the valuation of life reserves.
- Review the trends of reserve amounts for the various basis groupings in Exhibit 5 over recent annual statements. Contact the state insurance department's actuary or other actuarial resource for assistance with this analysis.
- If questions or concerns are noted, contact the state insurance department's actuary or other actuarial resource to discuss the nature and scope of the life reserve valuation procedures performed.
- Assess the lines of business written by the insurer and gain an understanding of the impact that the difference in types of plans may have on reserving assumptions and methodologies.
    - Through the analyst's interdepartmental communication with the policy forms department, inquire as to whether the insurer had any new and unusual policy forms approved during the past 12 months by either the department or Interstate Insurance Product Regulation Commission (IIPRC). Unusual filings could be product lines the company has not written before or contain new or innovative products or benefit designs.

- If concerns are noted about the types of life policies written, review the insurer's life insurance plan descriptions and/or policy forms to better understand the types of plans offered and the specific policy features and benefits.
- If questions or concerns are noted, contact the state insurance department's actuary for assistance in completing the analysis.
- If concerns are noted, consider a target examination of reserves in which the field examination staff request a valuation listing by plan and issue year, and test a sample of individual policy reserves from each of the major life insurance plans for accuracy.
- In considering any limited scope examination or any analysis needed, the analyst may consider use of the state's equivalent authority to the NAIC Standard Valuation Law (#820), Section 11F, which provides the commissioner may engage a qualified actuary at the expense of the company to perform an actuarial examination of the company and opine on the appropriateness of any reserve assumption or method used by the company, or to review and opine on a company's compliance with any requirement set forth in Model #820.

Determine whether any changes in life reserve valuation bases during the year were proper for policies and contracts. From time to time, an insurer may decide to change the valuation basis for a particular segment of the business. The insurer may change the valuation mortality table used, the valuation rate of interest or the valuation method. Reserve strengthening occurs when the insurer substitutes a more conservative basis of valuation for any given block of business. Reserve weakening may also occur but normally requires approval of the domiciliary state and reserves cannot be reduced below the minimum reserve standard as defined in the Standard Valuation Law.

The analyst may also consider performing procedures that involve testing the actual reserve calculations for a sampling of individual life insurance policies to ensure that the minimum statutory valuation standards have been met.

Procedures / Data

- Has there been a weakening of reserves resulting from a change in the basis of valuation during the year that resulted in an increase in the current year capital and surplus. [Annual Financial Statement, Exhibit 5A]

Qualitative and Additional Review Considerations

- Review the specific changes in valuation bases applied to life products noted in Annual Financial Statement, Exhibit 5A, and determine that individual changes in specific mortality tables, interest rates, or valuation methods meet the minimum statutory valuation standards.
- Identify if any changes in life reserve valuation bases did not receive appropriate regulatory approval, if required.
- Request from the insurer information regarding the reason for the change in valuation basis.

Inappropriate or Inaccurate Valuation of PBR Life Reserves,

OR

Accuracy of PBR Reserve (or Exemption) Computations,

OR

Reasonableness of PBR Methodologies and Assumptions

Determine whether the insurer's life reserves for policies and contracts subject to a principle-based valuation methodology appear to be valued in accordance with the requirements of VM-20. Risks include that reserves may be understated due to reserve computations that are not performed correctly or due to assumptions that are unreasonable or not compliant with minimum requirements; or, that exemption test are not computed correctly, resulting in inaccurate exemptions. In this regard, the analyst will need to review and rely on the VM-31, PBR Actuarial Report Requirements for Business Subject to a Principle-Based Reserve Valuation, actuarial report that documents the deterministic and stochastic ~~exemption~~exclusion tests, all company experience assumptions and margins, and all the procedures and processes used to calculate the reserves under a principle-based valuation methodology. In addition, the analyst will need to review the VM-20 supplement, which is part of the annual statement filing and contains the various components of the PBR. The analyst may seek the assistance of actuarial staff at the NAIC related to any verification of exclusion test calculations, as well as validation of PBR for a small random sample of policies and contracts subject to a principle-based valuation methodology. Please see the NAIC website for the Valuation Analysis (E) Working Group for contact information regarding the use of NAIC actuarial resources and use of the Working Group if needed.

Qualitative and Additional Review Considerations

- Review Section 1 of the VM-20 Supplement to the annual statement for the business PBR and the resulting reported PBR reserves. Consider the business PBR was applied with respect to the applicability of PBR provided in the *Valuation Manual* (VM), Section II for products within the scope of VM-20 requirements.
- Review Section 2 of the VM-20 Supplement to determine if the company has chosen to delay implementation of VM-20 requirements per Section II(c) of the VM.
- Review Section 3 of the VM-20 Supplement to the annual statement to determine if the company qualifies for the ~~companywide exemption~~Life PBR Exemption.
- Based on the judgment of the analyst and after discussing with the department actuary or the NAIC actuarial resources, determine if the VM-31, PBR Report Requirements, report should be requested from the company for review. The state insurance department actuary should perform the following procedures for any VM-31 Actuarial Report to be reviewed. The NAIC actuarial resources may be contacted for any questions or help in this review.
- Review the VM-31 Actuarial Report to identify the insurer's life insurance plan descriptions to understand the types of plans offered and the specific policy features and benefits.
- Review the VM-31 Actuarial Report to identify valuation assumptions based on company experience and valuation assumptions based on industry experience tables.
- For valuation assumptions based on company experience, contact the company valuation actuary to request to see the latest experience studies for those assumptions and evaluate the process used to establish the assumptions and the margins for those assumptions and the credibility factors used for each experience assumption.
- For mortality based on company experience, review the determination of the credibility percentage, the sufficient data period, the mortality segments, and the industry mortality tables to which company experience mortality is graded. Review whether the level of company mortality experience is appropriate in determining the credibility percentage and the sufficient data period. This is significant as the larger the body of experience used the smaller the resulting mortality margins and the lower the PBR reserves. Review to assure the use of any larger body of aggregate mortality experience is appropriate. As mentioned above, the NAIC actuarial resources may be consulted for any questions or support in this review.
- Review the VM-31 Actuarial Report to determine the contracts or plans that passed the stochastic and deterministic exclusion tests. Consider requesting the assistance of the NAIC actuarial resources to independently verify that such contracts and plans do pass the deterministic and stochastic exclusion tests.

- Consider whether to request that a limited-scope examination (or interim examination procedures) be performed to address concerns ~~by~~, including reproducing net premium reserve (NPR) calculations on a sample basis. Reproducing calculations may be conducted by asking the company to calculate NPR reserves for a sample of contracts and plans or requesting the NAIC actuarial resources to recalculate the NPR reserves for the same sample of contracts and plans and compare results. Also consider whether to request the NAIC actuarial resources for help in any testing of the deterministic (DR) and stochastic reserve (SR) if there are unusual relationships between the NPR, DR, and SR.
- In considering any limited scope examination or any analysis needed, the analyst may consider use of the state's equivalent authority to Model #820, Section 11F, which provides the insurance commissioner may engage a qualified actuary at the expense of the company to perform an actuarial examination of the company and opine on the appropriateness of any reserve assumption or method used by the company, or to review and opine on a company's compliance with any requirement set forth in this model.

Understatement of Reserves,

OR

Insufficient Asset Adequacy

Determine whether the insurer's underlying assets are adequate to support the future obligations of its life insurance policies. Risks may include the potential for understated reserves if unusual or specific policy features and benefits are not valued and reserved for correctly; or, if asset adequacy testing results reflect the assets held and may not be sufficient to support future policy obligations. If the insurer filed an SAO based on an asset adequacy analysis, then the SAO itself, and the supporting actuarial memorandum, if requested, can provide the analyst with comfort in this regard. If a SAO that does not include an asset adequacy analysis is filed, the analyst can review net interest spread ratios for insights regarding the relationship of investment income with tabular interest. Insurance Regulatory Information System (IRIS) ratio #11 is included in the procedures as a test of reserve consistency between the current year and the prior year.

The analyst may also consider performing a review of the actuarial memorandum, if available. This will provide the analyst with substantial analyses with regard to asset adequacy. If an actuarial memorandum is not available, the analyst should consider the need to have an independent asset adequacy analysis conducted. Additional procedures regarding the SAO are found in Section III.B.8.~~d~~b.i. Additional guidance for new reporting requirements for AG-53 regarding high-yielding complex assets is found ~~above.~~in the discussion of procedure #5.f above. Additional guidance for new reporting requirements for AG-55 regarding asset intensive reinsurance transactions is found in the discussion of procedure #5.g above.

Procedures / Data

- Net interest spread on life reserves (net investment income, less tabular interest, divided by average life reserves)
- Change in Asset Mix (IRIS ratio #11)

Qualitative and Additional Review Considerations

- If the insurer filed a Statement of Actuarial Opinion based on an asset adequacy analysis, review the results of the Actuarial Opinion Assessment, and note any concerns regarding the adequacy of the insurer's underlying assets to support future life insurance policy obligations.
- Pursuant to the review of the Regulatory Asset Adequacy Issues Summary (RAAIS) in the Actuarial Opinion Assessment, note whether the responses to the questions were satisfactory.

- If concerns still exist upon review of the asset adequacy analysis, discuss with the appointed actuary and the company, and request any additional information or work to be performed to address these concerns. If the insurance commissioner determines that the supporting actuarial memorandum fails to meet the standards prescribed by the Valuation Manual or is otherwise unacceptable to the insurance commissioner, the insurance commissioner may engage a qualified actuary at the expense of the company to review the opinion and basis for the opinion and prepare the supporting actuarial memorandum required by the insurance commissioner. See the state's equivalent authority to NAIC Model #820, Section 3B(3)(b). This also is noted in the Actuarial Opinion Worksheet.
- Review the Actuarial Guideline 53 reporting relating to assumptions and sensitivity testing for reinvested high-yielding complex assets within the asset adequacy analysis, if applicable. Determine whether concerns exist in meeting asset adequacy requirements. See further guidance in the AOMR procedures and reference guide.
- Review the Actuarial Guideline 55 reporting related to assumptions and cash flow testing for assets that support long-duration reinsurance transactions within asset adequacy analysis, if applicable. Determine whether concerns exist in meeting asset adequacy requirements. See further guidance in the AOMR procedures and reference guide.

Understated Reserves Associated with Separate Account Products ~~&~~and Guarantees

Review and identify situations where separate accounts products may be creating contingent liabilities to the general account that may not be sufficiently reserved for on the general account. This is largely a function of the types of separate accounts products offered by the insurer, and the analyst should rely on general knowledge of the insurer's products at this stage of the analysis.

The analyst should review disclosures in Separate Accounts General Interrogatories, Analysis of Operations by Line of Business (Page 6), Analysis of Increase in Reserves During the Year (Page 7) and the Notes to the Financial Statements of the general account to gain an understanding of the types of products included in the separate account and the general account guarantees on separate account products, as well as identify any concerns with reserving or asset adequacy that may require additional analysis of actuarial filings. The analyst should gain an understanding of any products in the separate account that contain guarantees that are held in the separate account instead of the general account and the types of guarantees (guaranteed minimum death benefit [GMDB], guaranteed minimum income benefit [GMIB], etc.). Where the general account provides an inherent/ultimate guarantee, the analyst should review the Separate Account General Interrogatories #2.7 to identify the materiality of the BACV of the separate account assets attributed to those products (i.e. pension risk transfer group annuities, registered index linked annuities, other group and individual annuities and life insurance), the related risk charges to the general account and if the asset were included in asset adequacy testing.

Exposure to Separate Account Products ~~&~~and Guarantee Liabilities and Accuracy of Separate Account Reserve Liabilities

Procedures / Data

- Identify the materiality of Separate Account assets with General Account guarantees [Separate Account General Interrogatories #2.71].
- Identify if any of the separate accounts have guarantees that are designed to mirror an established index (Annual Financial Statement, Note #35B).
- Identify if any of the separate accounts have material non-indexed guarantees. [Annual Financial Statement, Note #35B]

Qualitative and Additional Review Considerations

- If material guarantees exist, or if non-insulated products exist, determine whether the assets associated with these products are being invested in accordance with statutory guidelines.
- If material guarantees exist, gain an understanding of the types of Separate Account products for which the guarantees are provided [Separate Account General Interrogatories #2.71].
- If material guarantees exist, determine whether the assets associated with these products were included in asset-adequacy testing [Separate Account General Interrogatories #2.71].
- Review Separate Account General Interrogatories #5 to identify if the insurer reported a material amount of assets in the separate account at amortized cost rather than fair value. If yes, consider additional analysis of actuarial and asset adequacy reporting.
- Review Separate Account Analysis of Operations by Line of Business (Page 5) and Analysis of Increase in Reserves During the Year (Page 6) to identify if any concerns exist regarding the types of products included in the Separate Account and reserving for those products. If yes, consider additional analysis of actuarial and asset adequacy reporting.
- Based upon an overall understanding of the insurer's separate accounts products, assess if there is evidence that such products may be creating contingent liabilities to the general account with product features such as minimum guaranteed death benefits, minimum guaranteed interest rates, etc.
- If concerns or questions are noted, contact the state insurance department's actuary or other actuarial resource to discuss the nature and scope of the valuation procedures performed relating to guarantees included with separate accounts products. If determined to be necessary, contact the company's qualified actuary.
- Determine whether growth in separate accounts appears to be financed through borrowings of the general account and, if so, whether any concerns exist regarding the terms of repayment or collateralization.
- Determine whether the insurer writes any modified guaranteed annuities and, if so, the overall materiality and potential negative impact on the insurer's general account.
- Through the analyst's quarterly interdepartmental communication with the policy forms department, inquire as to whether the insurer filed any new and unusual separate account policy forms during the past 12 months.
- If concerns are noted about the types of policies included in separate accounts, review the insurer's separate accounts plan descriptions and/or policy forms to better understand the types of plans offered and the specific policy features and benefits, particularly minimum guarantees.
- If concerns are noted about reserving for separate accounts, consider a target examination of reserves, request that the field examination staff request a valuation listing by plan and issue year, and test a sample of the individual policy reserves for accuracy.
- Assess if there is any indication of contingent liabilities created by the separate accounts for the general account.
- Assess if separate account assets and liabilities were subject to asset adequacy analysis. If "no," review the actuarial opinion for an explanation.
- Request from the insurer separate accounts plan descriptions and/or policy forms to better understand the types of plans offered and the specific policy features and benefits, particularly minimum guarantees.
- Request information from the insurer regarding any significant changes in reserve methodologies and assumptions, underwriting practices, case reserving, or claims handling practices with the potential to affect reserve setting.

Exposure to Maximum Guarantees to the Separate Account

Qualitative and Additional Review Considerations

- Identify the variable annuity account value - general account. Document the variable annuity account value, percentage of capital and surplus, and percentage of total admitted assets.
- Assess if any separate accounts have collected amounts from the general account within the past five years related to separate account guarantees. [Annual Financial Statement, Separate Account General Interrogatories, #2.2]
    - If "yes," identify any concerns regarding the amounts or trend of guarantees paid.
    - If "yes," determine if guarantees were appropriately reserved for in the general account.
- Perform an industry peer comparison of the total maximum guarantee and the guaranteed amounts paid by the general account on a company-by-company basis to determine if the amounts appear reasonable.

Risk of Providing Guarantees While Not Receiving Risk Fees

Identify if the insurer reports a maximum guarantee exposure amount in Separate Accounts Annual Financial Statement, General Interrogatory #2.2 and guarantees paid in Separate Accounts General Interrogatory #2.3 but does not report risk charges paid in Separate Accounts General Interrogatory #2.6, which indicates the insurer is providing guarantees and may not be receiving a risk fee in return for that guarantee. Note that, while group products require risk charges, there may be no requirements for risk charges on individual products. Also note that in some instances, risk fees may be imbedded in the management fees paid to the general account. The analyst should gain an understanding of how risk fees are reported by the insurer and if concerns exist regarding the risk fees, the analyst should consider requesting additional details from the insurer. Additional procedures assist the analyst in determining that contingent liabilities to the general account of the insurer created by separate accounts assets are properly recorded. Guarantees included with separate accounts products must be recorded as a liability of the general account.

Qualitative and Additional Review Considerations

- Determine if there have been any risk charges paid to the general account related to separate account guarantees. [Annual Financial Statement, Separate Account General Interrogatories, #2.6, and #2.71]
- Determine if the insurer reported maximum guarantees that the general account would provide or pay amounts on guarantees in the current year and report no risk charges to the general account.

Inappropriate or Inaccurate Valuation of Annuity Reserves

Determine whether the insurer's annuity reserves are valued in accordance with the minimum formula statutory valuation standards. In this regard, the analyst must rely, to a large extent, on the opinion provided by the qualified actuary. The analyst can also gain comfort in this regard by evaluating the change in reserves in relation to increases or decreases in premiums during the year.

Procedures / Data

- Determine if anything has occurred since the last reporting period to raise concern that the insurer's annuity contracts are not valued in accordance with the minimum formula statutory valuation standards.
- Change in individual annuity reserves for the year as a percentage of individual annuity premiums (plus annuity investment income less annuity benefits and other fund withdrawals).

- Change in group annuity reserves as a percentage of group annuity premiums (plus annuity investment income less annuity benefits and other fund withdrawals).

Qualitative and Additional Review Considerations

- Review the results of the Actuarial Opinion assessment. Identify any concerns regarding whether the valuation of the insurer's reserves is in accordance with minimum statutory valuation standards.
- Review the Annual Financial Statement, Notes to Financial Statements, Note #31 – Reserves for Life Contracts and Annuity Contracts and note any unusual items regarding the valuation of annuity reserves (surrender values promised in excess of the reserve, significant changes in components of reserves, etc.).
- Review the trends of reserve amounts for the various basis groupings in Exhibit 5 over recent Annual Statements. Contact the state insurance department's actuary or other actuarial resource for assistance with this analysis.
- If questions or concerns are noted, contact the state insurance department's actuary or other actuarial resource to discuss the nature and scope of the annuity reserve valuation procedures performed. If determined to be necessary, contact the company's qualified actuary.

Assess information on annuity contract benefits offered that may indicate the impact of type of business, reserving assumptions and methodologies.

- Through the analyst's quarterly interdepartmental communication with the policy forms department, inquire as to whether the insurer filed new and unusual policy forms during the past 12 months.
- If concerns are noted about the types of policies, review the insurer's annuity plan descriptions and/or policy forms to better understand the types of plans offered and the specific policy features and benefits.
- If concerns are noted about reserving for annuity products, consider a target examination of reserves, request that the field examination staff request a valuation listing by plan and issue year, and test a sample of individual policy reserves from each of the major annuity plans for accuracy.
- In considering any limited scope examination or any analysis needed, the analyst may consider use of the state's equivalent authority to Model #820, Section 11F, which provides the insurance commissioner may engage a qualified actuary at the expense of the company to perform an actuarial examination of the company and opine on the appropriateness of any reserve assumption or method used by the company, or to review and opine on a company's compliance with any requirement set forth in this model.
- Request a spread analysis where the current spread earned is compared to the original pricing spread on the annuity block in question. Products with higher guaranteed minimum interest rates relative to the current interest environment. The state insurance department actuary can assist in this review.

Concerns with Changes in Reserves Basis

Determine whether any changes in annuity reserve valuation basis during the year were appropriate. From time to time, an insurer may decide to change the valuation basis for a particular segment of the business. The insurer may change the mortality table used, the rate of interest or the valuation method. Reserve strengthening occurs when the insurer substitutes a more conservative basis of valuation for any given block of business. Reserve weakening may also occur but normally requires approval of the domiciliary state.

The analyst may also consider testing the actual reserve calculations for a sampling of individual annuity policies to ensure that the minimum statutory valuation standards have been met.

Procedures / Data

- Note whether there has been a weakening of reserves resulting from a change in the basis of valuation during the year that resulted in an increase in capital and surplus. [Annual Financial Statement, Exhibit 5A – Changes in Bases of Valuation During the Year]

Qualitative and Additional Review Considerations

- Review the specific changes in valuation basis applied to annuity products noted in Annual Financial Statement, Exhibit 5A – Changes in Bases of Valuation During the Year and determine that individual changes in specific mortality tables, interest rates, or valuation methods meet the minimum statutory valuation standards.
- Determine if changes in annuity reserve valuation bases received appropriate regulatory approval, if required.
- Test check the calculations involved in applying a change in valuation basis. Contact the state insurance department's actuary or other actuarial resource for assistance with this assessment.
- Request from the insurer information regarding the reason for the change in valuation basis.
- Request information from the insurer regarding any significant changes in reserve methodologies and assumptions, underwriting practices, case reserving, or claims handling practices with the potential to affect reserve setting.

Inappropriate or Inaccurate Valuation of PBR Annuity Reserves,

OR

Accuracy of PBR Reserve (or Exemption) Computations,

OR

Reasonableness of PBR Methodologies and Assumptions

Determine whether the insurer's annuity reserves for contracts subject to a principle-based valuation methodology appear to be valued in accordance with the requirements of VM-21 (variable annuities and similar contracts containing guaranteed benefits) or VM-22 (non-variable annuities). Risks include that reserves may be understated due to reserve computations that are not performed correctly or due to assumptions that are unreasonable or not compliant with minimum requirements; or, that exclusion tests under VM-22 are not computed correctly, resulting in inaccurate exemptions of the stochastic reserve; or, that the Standard Projection Amount under VM-21 has not been computed in accordance with prescribed assumptions. In this regard, the analyst will need to review and rely on the VM-31, PBR Actuarial Report Requirements for Business Subject to a Principle-Based Reserve Valuation, actuarial report that documents the stochastic exclusion test (under VM-22), all company experience assumptions and margins, the hedging strategy documentation (under VM-21), and all the procedures and processes used to calculate the reserves under a principle-based valuation methodology. In addition, the analyst will need to review the VM-21 supplement and/or VM-22 supplement, which are part of the annual statement filing and contain the various components of the PBR. The analyst may seek the assistance of actuarial staff at the NAIC related to any verification of exclusion test calculations, as well as validation of PBR for a small random sample of contracts subject to a principle-based valuation methodology. Please see the NAIC website for the Valuation Analysis (E) Working Group for contact information regarding the use of NAIC actuarial resources and use of the Working Group, if needed.

Note that VM-22 has an optional effective date of January 1, 2026, and a mandatory effective date of January 1, 2029. During the transition period, both formula-based methodologies (CARVM and related Actuarial Guidelines, including VM-V) and the VM-22 principle-based methodology may apply to different blocks of an insurer's non-variable annuity business depending on the insurer's transition election and the date of contract issue.

Qualitative and Additional Review Considerations

- Review VM-21/22 Supplement to the annual statement for the business PBR and the resulting reported PBR reserves. Consider the business PBR was applied with respect to the applicability of PBR provided in the *Valuation Manual* (VM), Section II for products within the scope of VM-21/22 requirements.
- Based on the judgment of the analyst and after discussing with the department actuary or the NAIC actuarial resources, determine if the VM-31, PBR Report Requirements, report should be requested from the company for review. The state insurance department actuary should perform the following procedures for any VM-31 Actuarial Report to be reviewed. The NAIC actuarial resources may be contacted for any questions or help in this review.
- Review the VM-31 Actuarial Report to identify the insurer's annuity product descriptions to understand the types of plans offered and the specific policy features and benefits.
- Review the VM-31 Actuarial Report to identify valuation assumptions based on company experience and valuation assumptions based on industry experience tables.
- For valuation assumptions based on company experience, contact the company valuation actuary to request to see the latest experience studies for those assumptions and evaluate the process used to establish the assumptions and the margins for those assumptions and the credibility factors used for each experience assumption.
- For mortality based on company experience, review the determination of the credibility percentage, the sufficient data period, the mortality segments, and the industry mortality tables to which company experience mortality is graded. Review whether the level of company mortality experience is appropriate in determining the credibility percentage and the sufficient data period. This is significant as the larger the body of experience used the smaller the resulting mortality margins and the lower the PBR reserves. Review to assure the use of any larger body of aggregate mortality experience is appropriate. As mentioned above, the NAIC actuarial resources may be consulted for any questions or support in this review.
- Review the VM-31 Actuarial Report to determine the contracts that passed the stochastic exclusion test (SET) under VM-22 and the contracts subject to the Single Scenario Test (SST). Consider requesting the assistance of the NAIC actuarial resources to independently verify that such contracts do pass the SET and, where applicable, satisfy the SST.
- Consider whether to request the NAIC actuarial resource for help in any testing of the standard projection amount for VM-21, the deterministic reserve (DR) for VM-22, or the stochastic reserve (SR) if there are unusual relationships between the amounts.
- In considering any limited scope examination or any analysis needed, the analyst may consider use of the state's equivalent authority to Model #820, Section 11F, which provides the insurance commissioner may engage a qualified actuary at the expense of the company to perform an actuarial examination of the company and opine on the appropriateness of any reserve assumption or method used by the company, or to review and opine on a company's compliance with any requirement set forth in this model.

Adequacy of Annuity Reserves (Risk of Understatement of Reserves)

Determine whether the insurer's underlying assets are adequate to support the future obligations of its annuity policies. If the insurer filed an SAO based on an asset adequacy analysis, then the actuarial opinion itself, and the supporting actuarial memorandum, if requested, can provide the analyst with comfort in this regard. If an SAO that does not include an asset adequacy analysis is filed, the analyst can review net interest spread ratios for insights regarding the relationship of investment income with tabular interest.

The analyst may also consider a review of the actuarial memorandum, if available, as this will provide the analyst with substantial analyses with regard to asset adequacy. If an actuarial memorandum is not available, the analyst should consider the need to have an independent asset adequacy analysis conducted. Additional guidances for new reporting requirements for AG-53 regarding high-yielding complex assets and for AG-55 regarding asset intensive reinsurance transactions are found above.

Procedures / Data

- Net interest spread (net investment income, less tabular interest, divided by average annuity reserves) on individual annuity reserves.
- Net interest spread (net investment income, less tabular interest, divided by average annuity reserves) on group annuity reserves.
- Change in Asset Mix (IRIS ratio #11)

Qualitative and Additional Review Considerations

- If the insurer filed a statement of actuarial opinion based on an asset adequacy analysis, review the results of the Actuarial Opinion Assessment, and note any concerns regarding the adequacy of the insurer's underlying assets to support future annuity policy obligations. Review the actuary's comments regarding the analysis performed and conclusions reached.
- If available, or if concerns or questions are noted, request and review the RAAIS, and note whether the responses to the questions were satisfactory.
- If concerns exist upon review of the asset adequacy analysis, conduct an independent asset adequacy analysis.
- Review the Actuarial Guideline 53 reporting relating to assumptions and sensitivity testing for reinvested high yielding complex assets within the asset adequacy analysis, if applicable. Determine whether concerns exist in meeting asset adequacy requirements. See further guidance in the AOMR procedures and guidance.
- Review the Actuarial Guideline 55 reporting related to assumptions and cash flow testing for assets that support long-duration reinsurance transactions within asset adequacy analysis, if applicable. Determine whether concerns exist in meeting asset adequacy requirements. See further guidance in the AOMR procedures and guidance.
-

Concerns with Withdrawal and Surrenders Impact on Reserves

Identifying other areas of concern with withdrawal and surrenders that may affect annuity reserves. For example, annuities can have a significant impact on the insurer's liquidity position, particularly significant levels of GICs or amounts subject to withdrawal with minimal or no surrender charge.

Procedures / Data

- Guaranteed interest contracts as a percent of capital and surplus
- Annuity benefits, surrenders and other fund withdrawals for individual and group annuities as a percent of capital and surplus.
- Change in annuity benefits, surrenders, and other fund withdrawals for individual and group annuities and deposits, as a percentage of premiums

- Note significant amounts subject to withdrawal without any surrender charge or market value adjustment (i.e., as a percentage of total annuity reserves and deposit liability). [Annual Financial Statement, Notes to Financial Statements, Note #32]

Qualitative and Additional Review Considerations

- Request from the insurer and review the insurer's annuity plan descriptions and/or policy forms to better understand the types of plans offered and the specific policy withdrawal features and surrender charges.

Adequacy of A&H Reserves (Risk of Understatement of Reserves / A&H Reserve Deficiency)

Determine whether an understatement of A&H reserves would be significant to the insurer. The ratios of gross and net A&H reserves to capital and surplus are leverage ratios which are calculated gross and net of reinsurance ceded. The net A&H reserves to capital and surplus ratio indicates the margin of error an insurer has in estimating its A&H reserves. For an insurer with a net A&H reserve to capital and surplus ratio of 300%, a 33% understatement of its A&H reserves would eliminate its entire surplus. In evaluating these leverage ratios, the analyst should also consider the nature of the insurer's business. For example, an insurer which has written primarily A&H business for many years and has proven that it can manage the business profitably is probably not as risky as an insurer which has just begun writing A&H business, even if both insurers have the same leverage ratio results.

Procedures / Data

- For non-life insurers, the gross A&H reserves to capital and surplus ratio.
- Net A&H reserves to capital and surplus ratio.

Determine whether A&H policies appear to have been adequately reserved and valued in accordance with the minimum formula statutory valuation standards. In this regard, the analyst must rely, to a large extent, on the opinion provided by the qualified actuary. Therefore, the analyst should review the results of the SAO Procedures to determine whether any concerns were noted regarding the valuation of the insurer's A&H reserves in accordance with Appendix A-010, *Minimum Reserve Standards for Individual and Group Health Insurance Contracts*, of the AP&P Manual.

The analyst might want to contact the qualified actuary who signed the insurer's SAO to discuss the nature and scope of A&H valuation procedures performed and/or request a copy of the qualified actuary's actuarial memorandum to review for comments regarding the analysis of A&H reserves performed and the conclusions reached.

Qualitative and Additional Review Considerations

- Review the results of the Actuarial Opinion Assessment. Note any concerns regarding the valuation of the insurer's reserves and if in accordance with minimum statutory valuation standards.
- Request and review the insurer's description of the valuation standards used in calculating the additional contract reserves (which is required to be attached to and filed with the Annual Financial Statement) and consider whether the reserve basis, interest rates and methods appear reasonable.
- If questions or concerns are noted, contact the qualified actuary who signed the insurer's Statement of Actuarial Opinion to discuss the nature and scope of the A&H reserve valuation procedures performed.
- Request from the insurer A&H insurance plan descriptions and/or policy forms to better understand the types of plans offered and the specific features and benefits.

The ratio of A&H reserve deficiency measures the adequacy of A&H reserves established in the prior year. A positive result for this ratio represents additional or "adverse" development on the reserves originally established by the insurer (the amount by which the A&H reserves originally established have proved to be understated based on subsequent activity). Current or prospective reserve deficiency could represent a material impact on the insurer's capital and surplus. If the insurer's ratio results consistently show additional development, this could be an indication that the insurer is intentionally understating its A&H reserves. The A&H loss ratio is also reviewed as a part of this procedure. Significant increases in this ratio might be indicative of additional A&H reserves being established due to prior understatements while significant decreases might be indicative of current A&H reserve understatements. Other steps included in this procedure include the review of Exhibit 5A – Changes in Bases of Valuation During the Year, of the Annual Financial Statement to determine whether there has been a change in the valuation basis of the A&H policies during the year which resulted in a decrease in A&H reserves in an amount greater than 5% of capital and surplus.

The analyst may also consider reviewing Annual Financial Statement, Schedule H – Accident and Health Exhibit to determine which A&H lines of business are being written and which A&H lines of business had positive development in reserves during the year.

Procedures / Data

- A&H reserve deficiency ratio.
- Review the Schedule H claims test and note/explain any adverse trend or unusual fluctuation of one-year A&H loss development during the past five years.
- Assess loss ratios as indicators of reserve adequacy.
    - A&H Loss Ratio
    - Change in A&H loss ratio from the prior year.

Qualitative and Additional Review Considerations

- Review Annual Financial Statement, Schedule H – Accident and Health Exhibit, and perform the following:
    - Determine which A&H lines of business are being written by the insurer.
    - Review Schedule H – Part 3, to determine which A&H lines of business had positive development during the year.
- Review the A&H loss percentage ratio for unusual fluctuations or trends over a multi-year period.
- Compare the A&H loss percentage ratio to the industry average to determine any significant deviations from the industry average.
- Request an explanation from the insurer for any adverse loss development results or adverse trends indicated in the analyst's review of the Schedule H claims test.
- Request information from the insurer regarding A&H claims paid after year-end that were incurred prior to year-end and test the reasonableness of the year-end claim liabilities established by the insurer.

Consider: 1) reviewing the insurer's A&H insurance plan descriptions and/or policy forms to better understand the types of plans offered and the specific policy features and benefits; and 2) contacting the policy forms section of the insurance department and inquiring as to whether the insurer has filed any new and unusual A&H policy forms during the past year.

The analyst might also consider requesting that the field examination staff request a valuation listing of A&H reserves by policy and testing a sample of policies to determine that the reserve factors were appropriate and that the reserves were correctly computed. If the adequacy of claim liabilities is a concern, the analyst might want

to request information from the insurer regarding claims paid after year-end that were incurred prior to year-end, in order to test the reasonableness of the year-end claim liabilities established by the insurer.

Qualitative and Additional Review Considerations

- Assess information on policy benefits offered that may indicate the impact of type of A&H business on reserving assumptions and methodologies.
    - Review the Notes to Financial Statements, MD&A, or other correspondence with the insurer and note whether the insurer initiated any internal changes that could impact the reserve estimates.
    - Through the analyst's quarterly interdepartmental communication with the policy forms department, inquire as to whether the insurer has filed any new and unusual A&H policy forms during the past year.
    - If concerns are noted about the types of policies, review the insurer's A&H insurance plan descriptions and/or policy forms to better understand the types of plans offered and the specific features and benefits.
    - If concerns are noted about reserving for A&H, consider a target examination of reserves, request that the field examination staff request a valuation listing of A&H policy reserves by policy and test a sample of policies to determine that the reserve factors used were appropriate and that the reserves were correctly computed.

Adequacy of Long-Term Care LTC Reserves (Risk of Understatement of Reserves)

Review the LTC Experience Reporting Form of the Annual Financial Statement and the AG 51 reporting filed to the department if the insurer writes LTCI to gain an understanding of the reserve adequacy of the LTCI line of business. If concerns exist, consider requesting additional information as necessary to assess actual vs. projected results, legacy vs. newer blocks of business separately, any recent rate increases and capital support. If the insurer has recently filed for rate increases on LTCI blocks, consider intra-departmental discussion with the rate increase analysis and outcome with the rate review staff (if a different person than the analyst/actuary performing the valuation reserve analysis).

Qualitative and Additional Review Considerations

Review and assess long-term care (LTC) insurance reserves.

- Review the information reported in the LTC Experience Reporting Form of the Annual Financial Statement the Actuarial Guideline-LI—The Application of Asset Adequacy Testing to Long-Term Care Insurance Reserves (AG 51) reporting, actuarial memorandum or any other related actuarial information filed to the department and identify any concerns with reserve adequacy of LTC insurance business. Request a department actuary to assist in the review, if available.
    - Gain an understanding of the asset adequacy and cash-flow testing for LTCI on a stand-alone basis.
    - Consider any negative development in total LTCI reserve, asset adequacy reserves (if available), active life reserves, disabled lives reserves and premium deficiency reserves over the last five years.
    - Evaluate the appropriateness of investment return assumptions factoring in the status of the current economic and interest rate environment.
- If concerns exist:
    - Evaluate actual results vs. original or revised assumptions and financial projections to identify trends and concerns.
    - Consider evaluating legacy blocks of business separately from newer blocks of business.

- Rate Increases: Obtain and review the following information related to the status of rate increases and reduced benefit options. Consider that some information may be available from rate review staff for recent rate increase filings.
  - Track the progress of rate increases across states where a material amount of business is written.
  - Review projections illustrating the impact of proposed rate increases or reduced benefit options on the company's future profitability.
  - Determine the extent that future rate increases are included in the amount ($) of reserve offsets, asset adequacy/cash-flow testing and the reasonableness of the assumptions.
  - Consider the impact of historical approvals on the company's ability to obtain the rate increases presented in the projections. If concerns are identified in this area, obtain and review information on the company's plans to address these issues.
  - Compare the average percent of rate increases requested to the average approved.
  - Identify the amount of written premium change due to approved rate increases.
- Regarding the adequacy of internal capital to support the LTCI business, compare the current total LTC reserves (active life and other), net of reinsurance, to the amount of internal capital the company has set aside for LTCI (e.g., internal capital per Own Risk and Solvency Assessment [ORSA] if applicable, or rating agency if higher than internal). If necessary, request information to gain an understanding of the degree of conservatism in such capital assumptions.

Impact of Changes in Valuation Bases of Reserves

Review the insurer's description of the valuation standards used in calculating the additional contract reserves and consider whether the reserve bases, interest rates, and methods used appear reasonable. The insurer's description of the valuation standards used is required to be attached to the filed Annual Financial Statement.

If there was a change in the valuation basis of A&H policies during the year, the analyst should consider the following: 1) obtaining information regarding the reason for the change in the valuation basis; 2) determining whether the amount of the change in the actuarial reserve as a result of the change in the valuation basis is reasonable; and 3) determining whether the change in the valuation basis was approved by the domiciliary state insurance department, if required.

Assess the impact of changes in valuation bases on reserves.

Procedures / Data

- Note whether there has been a weakening of reserves resulting from a change in the basis of valuation during the year that resulted in an increase in capital and surplus. [Annual Financial Statement, Exhibit 5A]

Qualitative and Additional Review Considerations

- If there was a change in the valuation basis of the A&H policies during the year, consider performing the following:
  - Obtain information regarding the reason for the change in valuation basis and assess the change in the actuarial reserve.
  - Determine if changes in A&H reserve valuation bases received appropriate regulatory approval, if required.

Adequacy of Reserves on Captive (Non-Traditional) Reinsurance

Review reserve valuation of captive reinsurance transactions. Refer to the guidance in Chapter III.B.9. Strategic Risk Assessment for an explanation of potential risks. Also, for affiliated transactions, refer to the guidance for Form D captive reinsurance transactions in Chapter V.C. Domestic and/or Non-Lead State Analysis for procedures that may have been conducted at the time the transaction was approved.

Qualitative and Additional Review Considerations

If business is ceded to a captive (non-traditional) reinsurer, consider the following procedures.

- Determine the percentage of gross premium written that is ceded to affiliated captive reinsurers (Schedule S, Part 3, Sections 1 and 2) (Utilize Reinsurance Dashboard).
- Review the information provided in the Form D application for compliance with reserve valuation standards for fixed annuities.
- Consider Handbook procedures similar to the procedures required for XXX/AXXX captive reinsurance (III.C. Special Analysis Procedures).
- Within the Actuarial Opinion Memorandum, require the insurer provide the results of cash flow testing and true-up of the statutory sufficiency of the reserve credit taken on gross reserves ceded to the affiliated reinsurer, including appropriate sensitivity tests (e.g., lapse, utilization, combined surrender and utilization, and credit defaults, etc.).
- If the captive reinsurance arrangement is an asset-intensive transaction, determine whether the transaction is in scope of Actuarial Guideline LV (AG-55) and, if so, review the AG-55 reporting for the cash flow testing, attribution analysis, and risk identification supporting the ceded reserves.
- Consider including confidential disclosure in the Insurer Profile Summary to other state insurance departments if the commissioner approved assets not meeting criteria A–C defined within the *Credit for Reinsurance Model Regulation* (#785) for Funds Withheld.

ADDITIONAL PROCEDURES

Examination Findings

Consider a review of the recent examination report, summary review memorandum and communication with the examination staff to identify if any reserving risk issues were discovered during the examination.

- If outstanding issues are identified perform follow-up procedures as necessary to address concerns.
- Request that the field examination staff request a valuation listing by plan and issue year and test a sample of the individual policy reserves for accuracy.

Inquire of the Insurer

Consider requesting additional information from the insurer if reserving risk concerns exist.

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

- If questions or concerns are noted, contact the insurer to request if the insurer initiated any internal changes that could impact the reserve estimates.
- Request a copy of the insurer's business plan and review the insurer's plans to assess and mitigate reserve risks.

- Request information on who ultimately determines the level of reserves to be booked by the insurer and the board of directors' role in overseeing the reserving process.
- If filed on an insurance entity basis or if your state is the lead state, review the insurer's Corporate Governance Annual Disclosure (CGAD) filing to understand and assess the board of director~~'~~s' role in overseeing the reserving process. If your state is not the lead state, rely on the information provided in the Group Profile Summary (GPS) or provided by the lead state, where the CGAD is filed on a group basis.

Own Risk and Solvency Assessment (ORSA)

Obtain and review the latest ORSA Summary Report for the insurer or insurance group (if available) to assist in identifying, assessing and addressing reserving risks faced by the insurer.

If the insurer is required to file an ORSA or is part of a group that is required to file an ORSA,

- Review the ORSA Summary Report analysis conducted by the lead state for any reserving risks that require further monitoring or follow-up.
- Review the ORSA Summary Report analysis conducted by the lead state for any mitigating strategies for existing or prospective reserving risks.

Holding Company Analysis

Obtain and review the holding company analysis work completed by the lead state to assist in identifying, assessing and addressing reserving risks that could affect the insurer.

- Review the Holding Company analysis conducted by the lead state for any reserving risks impacting the insurer that require further monitoring or follow-up.
- Review the Holding Company Analysis conducted by the lead state for any mitigating strategies for existing or prospective reserving risks impacting the insurer.

QUARTERLY RESERVING RISK ASSESSMENT

The quarterly reserving risk assessment is intended to identify significant changes in reserves that have occurred since the prior year Annual Financial Statement or the prior Quarterly Financial Statement.

Changes in Life Reserves and Reserve Adequacy

Procedures / Data

Determine changes in life reserves to assess any change in the adequacy of reserves.

- Change in reserve from the prior year-end where the aggregate reserve for life contracts exceeds 10% of capital and surplus.
- Change in any asset categories from the prior year-end. [Quarterly Financial Profile – "Mix of Cash ~~&~~and Invested Assets" section]
- Review, by line of business, the year-to-date direct premiums for the current and prior year quarter and note significant changes in direct premiums for any line of business from the prior year, same quarter. [Quarterly Financial Statement, Exhibit 1]

Changes in Accident and Health (A&H) Reserves and Reserve Adequacy

Procedures / Data

Determine changes in accident and health reserves to assess any change in the adequacy of reserves.

- Change in reserve from the prior year-end where the aggregate reserve for A&H contracts exceeds 10% of capital and surplus.
- Change in policy and contract claims from the prior year-end, where the A&H policy and contract claims exceed 10% of capital and surplus.
- Change in benefits from the prior year, same quarter where the disability benefits and benefits under A&H contracts exceed 10% of capital and surplus.
- Aggregate reserve for A&H contracts to capital and surplus ratio.
- Review, by line of business, the year-to-date direct premiums for the current and prior year quarter and note significant changes in direct premiums for any line of business from the prior year, same quarter. [Quarterly Financial Statement, Exhibit 1]

Changes in Annuity Reserves and Reserve Adequacy

Procedures / Data

Determine changes in annuity reserves to assess any change in the adequacy of reserves.

- Change in liability from the prior year-end where the liability for deposit-type contracts exceeds 3.5% of capital and surplus.
- Change in surrender benefits and other fund withdrawals change from the prior year, same quarter. [Quarterly Financial Statement, Summary of Operations]
- Change in any asset categories from the prior year-end. [Quarterly Financial Profile – "Mix of Cash ~~&~~and Invested Assets" section]
- Review, by line of business, the year-to-date direct premiums and deposit-type contract funds for the current and prior year and note whether direct premiums for any line of business or deposit-type contract funds have changed significantly from the prior year, same quarter. [Quarterly Financial Statement, Exhibit 1]

For additional guidance on individual procedure steps, please see the corresponding annual procedures discussed above.

ACTUARIAL OPINION AND REGULATORY ASSET ADEQUACY ISSUES SUMMARY ASSESSMENT (RAAIS) OVERVIEW

Life insurers required to file an Annual Financial Statement and are also required to file an SAO as a supplement to the Annual Financial Statement. The specific requirements for the SAO are described in the NAIC *Valuation Manual*, VM-30, Actuarial Opinion and Memorandum Requirements (AOMR). The SAO must be issued by an Appointed Actuary. The Appointed Actuary must be a qualified actuary appointed either directly by, or by the authority of, the board of directors through an executive officer of the company other than the qualified actuary. "Qualified actuary" as used herein means a member in good standing of the American Academy of Actuaries, or an individual who has otherwise demonstrated his or her actuarial competence to the satisfaction of the domiciliary state insurance department. Requirements regarding the Appointed Actuary and Qualified Actuary must conform to those prescribed by the *Valuation Manual* authorized by Section 3B of the Standard Valuation Law as amended by the NAIC in December 2009. The Actuarial Opinion should include the general account and the separate accounts.

Life insurers are required to file a comprehensive SAO based on an asset adequacy analysis. The actuarial opinion is supported by an actuarial memorandum. The actuarial memorandum includes the results of the qualified actuary's asset adequacy analysis. While the SAO must be filed with the Annual Financial Statement, the actuarial memorandum is only provided to the regulator upon request. There is also a confidential executive summary, the RAAIS, filed with the insurance departments. In addition to an actuarial opinion, the insurer must also file a non-guaranteed elements opinion if policies containing non-guaranteed elements are currently being issued or are in-force. The specific requirements for the non-guaranteed elements opinion are described in the NAIC *Annual Financial Statement Instructions for Life, Accident and Health Insurance Companies*.

The SAO must follow the guidelines and standards for statements of actuarial opinion prescribed by the *Valuation Manual* authorized by Section 3B of the Standard Valuation Law as amended by the NAIC in December 2009. The SAO should consist of a paragraph identifying the qualified actuary, a scope section identifying the subjects on which an opinion is to be expressed and describing the scope of the qualified actuary's work, and an opinion paragraph expressing the qualified actuary's opinion with respect to such subjects. If there has been a material

change in the actuarial assumptions from those previously employed, that change should be described in either the Annual Financial Statement or in a paragraph of the SAO. In addition, the scope paragraph should list those items and amounts to which the qualified actuary is expressing an opinion, including the following from the Annual Financial Statement: 1) aggregate reserves for life contracts (Exhibit 5); 2) aggregate reserves for A&H contracts (Exhibit 6); 3) deposit-type contracts (Exhibit 7); and 4) contract claims – liability end of current year (Exhibit 8, Part 1). If the actuary has not examined the underlying records but has relied upon listings and summaries of policies in force prepared by the company, the scope paragraph should include a sentence to this effect.

The Appointed Actuary must report to the board of directors or the Audit Committee each year on the items within the scope of the SAO. The minutes of the board of directors shall indicate that the Appointed Actuary has presented such information to the board of directors or the Audit Committee. A separate SAO is required for each company filing an Annual Statement. If the qualified actuary is unable to form an opinion, the actuary should issue a statement specifically stating the reason(s) why an opinion cannot be formed. If the qualified actuary's opinion is adverse or qualified, the actuary should issue an adverse or qualified actuarial opinion specifically stating the reason(s) for such an opinion. An adverse opinion is an actuarial opinion which the Appointed Actuary determines that the reserves and liabilities are not adequate.

DISCUSSION OF ACTUARIAL OPINION ASSESSMENT PROCEDURES

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

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

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

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

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

Asset Adequacy Analysis

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

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

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

Actuarial Guideline 53

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

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

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

A. Over $5 billion of general account actuarial reserves (from Exhibits 5, 6, 7, and 8 of the Annual Statement) and non-unitized separate account assets; or,

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

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

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

Actuarial Guideline 55

Beginning with annual 2025, certain insurers will be required to document support for asset adequacy analysis for the assets that support reinsurance transactions exceeding certain amount of reserve credit plus modified coinsurance reserves pursuant to *Actuarial Guideline LV—Application of the Valuation Manual for Testing the Adequacy of Reserves Related to Certain Life Reinsurance Treaties (AG ~~-~~55)*.

As stated in ~~AG55~~AG-55, the reporting provides information for the analyst "to better understand the amount of reserves and type of assets supporting long duration insurance business that relies substantially on asset returns. In particular, there is risk that domestic life insurers may enter into reinsurance transactions that materially lower the amount of reserves and thereby facilitate releases of reserves that prejudice the interests of their policyholders. The goal of this Guideline is to enhance reserve adequacy requirements for life insurance companies by requiring that asset adequacy analysis use a cash flow testing methodology that evaluates ceded reinsurance as an integral component of asset-intensive business."

This Guideline applies to all life insurers with asset intensive reinsurance transactions ~~exceeding~~that exceed certain amount of reserve credit plus modified coinsurance reserves (see AG ~~-~~55 for specific scope limits~~).~~) and whose reinsurers are not required to submit a VM-30 memorandum to US state regulators.

The AG ~~-~~55 documentation, sensitivity test results, and attribution analysis referenced within AG ~~-~~55 are to be incorporated as a separate, easily identifiable section of the actuarial memorandum required by VM-30 or as a standalone document, with a due date of April 1 following the applicable valuation date. Similar memorandum may also be allowed under certain circumstances.

The NAIC Valuation Analysis Working Group (VAWG) ~~anticipates conducting~~conducts reviews of AG-55 asset adequacy analysis filings, on a targeted basis, and coordinating with states as appropriate. VAWG will serve as a resource for state insurance departments for their own AG-55 reviews as well as providing periodic reports identifying outliers and concerns regarding the analysis to help inform regulators about the effectiveness of this Guideline in meeting the objectives.

LIFE RESERVING RISK ASSESSMENT (INCLUDING PRINCIPLE-BASED RESERVING) OVERVIEW

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

To implement the principle-based valuation methodology, amendments to the Standard Valuation Law were adopted in 2009, and a *Valuation Manual* was developed. The *Valuation Manual*, which is referred to in the

amended Standard Valuation Law, provides reserve requirements for life, health and annuity products issued on and after the manual's operative date. Requirements include all of the details of the methodology for determining a principle-based reserve (PBR), as well as any changes to the formula-based valuation methodology that occurs on and after the operative date of the *Valuation Manual*.

Unless a change in the *Valuation Manual* specifies a later effective date, changes to the *Valuation Manual* shall be effective Jan. 1 following the date when the change to the *Valuation Manual* has been adopted by the NAIC by an affirmative vote of at least three-fourths of the members of the NAIC voting but not less than a majority of the total membership and such members voting in the affirmative represent jurisdictions totaling greater than 75% of the direct premiums written as reported in the most recent life, A&H annual statements; health annual statements; or fraternal annual statements. No state legislative adoption is needed to effect changes to the valuation manual.

The *Valuation Manual* defines the insurance contracts that are subject to a principle-based valuation (Section II). Unless otherwise specified in Section II, the principle-based valuation methodology will apply to life insurance contracts issued on and after the operative date of the *Valuation Manual*. However, a company may elect to defer the implementation of the principle-based valuation methodology to life insurance contracts issued during the first three years following the operative date of the *Valuation Manual*.

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

The NAIC will acquire modeling software and develop actuarial staff expertise in modeling insurance cash flows to assist the Valuation Analysis (E) Working Group and the individual states in conducting analysis and examinations to verify the PBR and exclusion test calculations performed by the company.

As mentioned in the procedures, any questions or requests for assistance regarding PBR and for asset adequacy analysis may be made to the NAIC actuarial resources. Please see the NAIC website for the Valuation Analysis (E) Working Group for contact information regarding the use of NAIC actuarial resources and use of the Working Group if needed.

LIFE FORMULA-BASED VALUATION METHODOLOGY

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

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

The interest rate assumptions are intended to be significantly lower than current money and capital market yields. Thus, the life reserves developed are generally conservative.

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

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

1. **Ordinary Life Reserves**

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

2. **Group Life Reserves**

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

3. **Industrial Life Reserves**

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

4. **Life Reserves Relating to Riders**

   Life insurance policies frequently include riders for additional benefits such as accidental death and disability and waiver of premium upon disability. The minimum valuation standards for reserves are the same as for the base life insurance except that specialized mortality and disability tables are used, and the net level premium valuation method is required.

5. **Miscellaneous Life Reserves**

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

6. **Minimum Aggregate Reserves**

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

LIFE PRINCIPLE-BASED VALUATION METHODOLOGY

In general, under a principle-based valuation methodology, all of the liability cash flows emanating from the contract benefits provided in the product are determined for each period and compared with all of the asset cash flows for each period determined from the assets the insurance company has purchased or plans to purchase or sell to fund the liability cash flows. The resulting differences between the asset and liability cash flows for each period are valued under a range of likely or plausible economic scenarios. Economic scenarios may consist of interest rates or market returns or both depending on the nature of the asset and liability cash flows. A single economic scenario represents multiple consecutive periods (such as 30 or 40 years) of movements in the underlying interest rate or market rate returns. The length of the scenario period is determined by the length of the liabilities being valued. The economic scenarios are stochastically (randomly) generated using a prescribed ~~economic scenario generator (ESG).~~Generator of Economic Scenarios (GOES). The prescribed ~~ESG~~GOES can be found on the ~~Society of Actuaries (SOA)~~Conning's website.

The reserve liability under a principle-based valuation methodology is determined as a function of the discounted value of the differences between the asset and liability cash flows for each period over the range of economic scenarios. The objective is to determine if there is a reasonable likelihood that assets are insufficient to cover the obligations of the company, and by what amount they may be insufficient. Under economic scenarios where assets are insufficient, the principle-based methodology determines all the amounts of the insufficiencies and discounts them back to the valuation date. The largest discounted value is known as the Greatest Present Value of Accumulated Deficiencies (GPVAD) for that scenario. The stochastic reserves may be set at a CTE (70) level (conditional tail expectation at the 70% level). The function CTE (70) means the average of the 30% (100% - 70%) worst (largest) GPVADs. So, for example, if a company randomly generates 1,000 economic scenarios, it would then determine the largest accumulated amount of deficiency for each of the 1,000 scenarios. The CTE (70) stochastic reserve (SR) level would be determined by taking the average of the 300 [1,000 x (100% - 70%)] worst GPVADs out of the 1,000 scenarios.

The principle-based valuation methodology developed for life insurance contracts defines three components of a PBR: 1) a net premium reserve (NPR); 2) a deterministic reserve (DR); and 3) an SR. The level of risk embedded in a life insurance contract will determine whether the PBR will consist of all three reserve components (NPR, DR, SR), only two reserve components (NPR, DR), or only one reserve component (NPR). The principle-based valuation methodology defines a stochastic exclusion test and a deterministic exclusion test, each of which are designed to measure the level of risk embedded in a life insurance contract. Life insurance contracts that pass an exclusion test are then exempt from the calculation of the associated PBR component. For example, all life insurance contracts that pass the stochastic exclusion test but fail the deterministic exclusion test must calculate the NPR

and DR components. Life insurance contracts that pass both the stochastic and deterministic exclusion tests must only calculate the NPR component. For groups of policies other than variable life or universal life with a secondary guarantee (ULSG), a company may provide a certification by a qualified actuary that the group of policies is not subject to material interest rate risk or asset return volatility risk in lieu of performing the stochastic exclusion test. In addition, a company is not required to compute SR and DR on any of its ordinary life policies if it meets the requirements for a "~~Companywide~~Life PBR Exemption" provided in Section II of the *Valuation Manual*. If the domestic commissioner does not reject a company's application for the ~~companywide exemption~~Life PBR Exemption pursuant to the *Valuation Manual*, Section II, then the company will compute reserves for its ordinary life policies per the requirements provided in VM-A and VM-C of the *Valuation Manual*.

Note that some states incorporated a "~~companywide exemption~~Life PBR Exemption" in the Standard Valuation Law that may override Section II of the ~~VM-20~~Valuation Manual, Requirements for Principle-Based Reserves for Life Products. In such cases, the state's Standard Valuation Law will determine whether a company is not subject to computing the stochastic and deterministic reserves. Note also, the insurance commissioner may exempt specific product forms or product lines of a domestic company that is licensed and doing business only in a single state as defined in Section 15 of the amended Standard Valuation Law.

As part of the calculation process, the principle-based valuation methodology allows companies to aggregate or group policies with similar risk characteristics. For example, all term policies that provide only a death benefit and do not provide any cash surrender values may be grouped together by underwriting class. The exclusion tests are then applied on a group or aggregated basis and not a contract-by-contract basis. Also, the DR and the SR are calculated on an aggregated or group basis. The NPR component is a fully prescribed formula-based reserve and can be applied on a contract-by-contract basis.

The annual statement blank contains a VM-20 Supplement. This supplement breaks out the PBR into its various components of NPR, DR and SR. State insurance regulators may request the assistance of NAIC modeling staff and or the Valuation Analysis (E) Working Group in verifying exclusion testing, as well as various components of the PBR on a smaller sample set of company contracts.

ACTUARIAL OPINION AND ASSET ADEQUACY ANALYSIS

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

ACCIDENT AND HEALTH RESERVING RISK ASSESSMENT OVERVIEW

The purpose of A&H insurance is to protect the insured against economic losses resulting from accident and/or sickness. There are many different types of A&H policies issued by insurers. The economic losses covered, and the types of benefits provided, vary with the different types of A&H policies. For example, a medical insurance policy may provide reimbursement for hospital, surgical, medical and drug expenses and a dental insurance policy may cover dental expenses. Another type of A&H insurance policy issued is disability insurance which provides monthly

benefits for loss of income due to disability on either a short-term or long-term basis. A&H insurance is provided through individual policies, group policies and certain special types of policies such as credit disability insurance.

A&H reserves are complex and difficult to analyze because of the wide variety of types of coverage included in the A&H lines of business and the diversity of benefits which must be reserved for. A&H reserves are comprised of two separate liability line items in the Annual Financial Statement: 1) the aggregate reserve for A&H policies; and 2) the A&H policy and contract claims liability. These liabilities are discussed in more detail below.

1. **Aggregate Reserve for A&H Policies**

   The aggregate reserve for A&H policies consists of two different components: 1) policy reserves; and 2) claim reserves.

   a. **Policy Reserves**

      Policy reserves are required in recognition of the fact that premiums cover future liabilities as well as current claims and expenses. Policy reserves include unearned premium reserves, additional contract and actuarial reserves, reserves for future contingent benefits, and reserves for rate credits. The various types of policy reserves are discussed in more detail below.

      Unearned premium reserves represent the amount of the premium applicable to coverage which extends beyond the valuation date (date of the statement). The unearned portion of the premium is generally computed on a pro rata basis.

      Additional contract reserves are required for those policies with level premiums where the risk of loss increases with the age of the insured. For these policies, the insurer is required to set aside a portion of the current premium to pay claims that experience indicates will be incurred as the policy continues in force. These reserves are actuarially determined and are similar in concept to life reserves with the added requirement to consider morbidity assumptions as well as mortality and interest assumptions. The NAIC AP&P Manual prescribes the minimum standards used in determining the A&H policy reserves. Insurers may establish A&H policy reserves which equal or exceed these minimum standards. These minimum A&H policy reserve standards for most types of A&H insurance include: 1) a given morbidity table; 2) a maximum rate of interest; and 3) a valuation method. In no event, however, may the aggregate reserve for all policies be less than the unearned gross premiums under such policies. For financial statement purposes, the additional contract reserves represent the excess of the required A&H policy reserves over the unearned gross premiums on A&H policies. The insurer is required to attach to the Annual Financial Statement a description of the valuation standards used in calculating the additional contract reserves, specifying the reserve bases, interest rates, and methods.

      Determine if additional actuarial reserves are required as a result of actuarial cash flow testing and asset adequacy analysis.

      If the A&H policy provides for future contingent benefits, a portion of the current premium must also be reserved for such coverage. For example, some A&H policies provide for deferred maternity benefits (which cover medical expenses incurred in childbirth for approximately nine months after the cessation of premium payments, even though the policy has been canceled, so long as conception occurred prior to the policy being canceled). An actuarially determined estimate of the costs associated with this future contingent benefit must be reserved for out of the current premium.

      Some A&H policies provide for rate refunds based on policy year experience. For these policies, a reserve is required to be established for the rate credits based on the amount of the expected credit as of the valuation date. The reserve for rate credits is a difficult liability to establish because many policy years do not end on the valuation date (date of the statement), and subsequent experience may cause the rate credit to be greater or less than the liability established. However, the liability established must be reasonable under the circumstances and consistently calculated.

b. **Claim Reserves**

Claim reserves (sometimes referred to as disabled life reserves) are required for claims which involve continuing loss. The claim reserves represent the actuarially determined present value of future benefits or future covered benefits not yet due as of the valuation date (date of the statement) which are expected to arise under claims which have been incurred as of the statement date. However, although the liability for future covered benefits which are expected to arise under claims which have been incurred as of the statement date on medical insurance policies should be included in claim reserves according to *Statement of Statutory Accounting Principles* (*SSAP) No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses*, some insurers include this liability in the A&H policy and contract claims liability which is discussed below.

2. **A&H Policy and Contract Claims Liability**

The A&H policy and contract claims liability includes: 1) due and unpaid claims; 2) claims in the course of settlement; and 3) incurred but not reported (IBNR) claims.

a. **Due and Unpaid Claims**

Due and unpaid claims are those which are complete except for the payment of the amount due. The amount of an insurer's due and unpaid claims is generally very small, and this liability is generally determined on an exact inventory basis of claims ready to be paid.

b. **Claims in the Course of Settlement**

Claims in the course of settlement include claims which have not been paid because all of the required information has not yet been received as of the statement date, resisted claims and the accrued portion (amount that is payable as of the statement date) of the next periodic payment on disability claims. The unaccrued portion of the next periodic payment on disability claims would be included in claim reserves discussed above. The liability for claims in the course of settlement, other than disability claims, may be determined based on estimates for each outstanding claim or the development of average claim factors or formulas based on historical experience.

c. **IBNR Claims**

IBNR claims are those claims which have occurred but have not yet been reported to the insurer. Since neither the number nor dollar amount of IBNR claims are known as of the statement date, the liability for IBNR claims is difficult to estimate. The liability for IBNR claims is generally estimated based on an actuarial analysis of past experience or on the development of lag studies using historical experience.

Due to the variety of types of A&H policies issued and the complexity of determining the aggregate reserve for A&H policies and the A&H policy and contract claims liability, most insurers rely on actuaries or individuals with actuarial training to assist in estimating these liabilities. Although some insurers do not use actuaries to actually set the A&H reserves, insurers are required to annually obtain an opinion regarding the reasonableness of the established A&H reserves by a qualified actuary. Therefore, qualified actuaries are involved in setting and/or reviewing the A&H reserve liabilities established for virtually all insurers.

ANNUITY RESERVING RISK ASSESSMENT (INCLUDING PRINCIPLE-BASED RESERVING) OVERVIEW

Annuity reserves represent the liability established by the insurer to pay future policy benefits. While life insurance provides protection from the loss arising from dying too soon, an annuity protects against the loss from living too long. Theoretically, annuity reserves represent the present value of future guaranteed benefits reduced by the present value of expected future net premiums. An annuity can be in either an accumulation mode or a payout

mode. Annuity policies take three forms: 1) annual premium deferred annuity; 2) single premium deferred annuity; and 3) single premium immediate annuity. Under an annual premium deferred annuity, annual premiums are paid during an accumulation period until such time as the policyholder (i.e., annuitant) receives income, surrenders the policy, or it terminates upon death. These annual premiums may be a specified amount or subject to the discretion of the owner under "flexible premium" annuities. Even if premiums are discontinued, the cash value of the policy will continue to accumulate until income is elected or the policy is otherwise terminated for its value. At income commencement, the annuitant receives the monthly income based upon cash value of the policy at that time and the annuity factor guaranteed in the policy or currently being applied, if more favorable, for the annuitant's attained age. The single premium deferred annuity also accumulates until such time as the annuitant desires to take income or the policy is otherwise terminated. However, only a single premium is paid at the time the annuity is purchased.

ANNUITY FORMULA-BASED VALUATION METHODOLOGY

The AP&P Manual prescribes the minimum standards to be used in determining reserves. Appendix A-820*, Minimum Life & Annuity Reserve Standards* of the AP&P Manual defines the minimum standards for all types of policy reserves, including life ~~&~~and annuity policies. Insurers may establish annuity reserves, which equal or exceed these minimum standards. These minimum annuity reserve standards specify a: 1) given mortality table (if applicable); 2) maximum rate of interest; and 3) valuation method. The valuation method used to define minimum annuity reserves for statutory accounting purposes is referred to as the Commissioners Annuity Reserve Valuation Method (CARVM). The mortality rate assumptions, if applicable, are substantially lower than what the insurer can expect to realize from medically underwritten insurance policies. The interest rate assumptions are intended to be significantly lower than current money and capital market yields. Thus, the annuity reserves developed are generally conservative.

As described below, the type of annuity dictates the amount of the annuity reserve that must be established and the duration for maintaining the reserve. In addition, special situations arise that require unique reserving techniques. The following summarizes the major types of annuities and the related reserving implications:

1. **Deferred Annuities (Annual Premium and Single Premium)**

   All deferred annuities are reserved using the CARVM method. The reserve on any specific valuation date requires a calculation of the present value of future guaranteed benefits less the present value of future required net premiums for the current duration of the policy and for each future duration. For purposes of calculating this series of "excesses," premiums are only considered to be payable for the specific duration for which the excess is being calculated. The reserve is the greatest of these excesses. Reserves for guaranteed benefits must consider all contractual guarantees including cash values, death benefits, annuity income, etc. Cash values are actually guaranteed under the policy provisions.

2. **Immediate Annuities**

   Immediate annuities are those that are in payout mode. Reserves are determined using the CARVM method, except that, in the case of supplemental contracts without life contingencies, mortality tables are not used.

3. **Guaranteed Interest Contracts**

   Guaranteed interest contracts (GICs) represent a type of funding vehicle used where group deferred annuities are involved. Under a basic GIC, the insurer accepts a single deposit from the plan sponsor (i.e., the employer) for a specified period of time, such as five years. Interest earned during the period may accumulate until the period expires, or the earned interest may be paid out annually. At the end of the period, the account balance, including any accumulated interest, is returned to the plan sponsor. Numerous variations of this basic guaranteed interest contract have been developed that: 1) allow the plan sponsor to make monthly

contributions rather than the single deposit; and 2) provide that the principal and interest can be paid out in installments to make benefit payments to plan participants.

4. **Structured Settlements**

   Structured settlements are a form of immediate annuity generally established in connection with the settlement of a property/casualty claim wherein a predetermined future benefit stream is desired. Reserves are determined using the CARVM method with special actuarial guidelines that prescribe specialized mortality tables and govern the use of lump sum balloon payments.

5. **Variable Annuities**

   Variable annuities are annuities where the amount of each benefit payment is not specified in the annuity contract but rather fluctuates according to the earnings of a separate account fund. The primary concern relating to variable annuities reserves relates to the treatment of the CARVM expense allowance in the general account. The CARVM method is generally used, but the current thinking is that CARVM may not be appropriate for certain types of variable annuities that do not include guaranteed benefits.

Due to the complexity in determining annuity reserves, insurers must rely on actuaries to assist with valuation of these reserves. Insurers are required to annually obtain an opinion regarding the reasonableness of the reserves by a qualified actuary. In the aggregate, policy reserves for all annuity policies that are reported in the statutory financial statements must equal or exceed reserves calculated by using the assumptions and methods that produce the minimum standard valuation.

ANNUITY PRINCIPLE-BASED VALUATION METHODOLOGY

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

The Valuation Manual establishes two parallel principle-based frameworks for annuity contracts: VM-21, applicable to variable annuities and similar contracts containing guaranteed benefits, and VM-22, applicable to non-variable annuities. The two frameworks differ in scope, reserve components and applicability of exclusion testing, but share the same stochastic projection mechanics and use of the prescribed economic scenarios.

VM-21 — Variable Annuities

VM-21 became effective January 1, 2020 and applies to variable annuity contracts (with or without guaranteed minimum death benefits (GMDB) or variable annuity guaranteed living benefits (VAGLB)), any group annuity contracts containing guarantees similar in nature to GMDBs or VAGLBs, and other contracts containing guarantees similar in nature to GMDBs or VAGLBs. The principle-based valuation methodology developed for variable annuity contracts defines two components of a principle-based reserve: 1) a Stochastic Reserve (SR); and 2) an Additional Standard Projection Amount (ASPA). The VM-21 reserve is determined as the sum of the SR and the ASPA. The ASPA is computed using prescribed (rather than prudent estimate) assumptions for policyholder behavior, mortality and other key drivers and is intended to constrain the impact of company-specific assumption setting on the reserve outcome. Where the insurer's hedging program meets the requirements of a Clearly Defined Hedging Strategy (CDHS), the impact of the hedging program may be reflected in the projection in accordance with VM-21.

The stochastic reserve under VM-21 is determined as a function of the discounted value of the differences between the asset and liability cash flows for each period over the range of economic scenarios. Economic scenarios may consist of interest rates or market returns or both depending on the nature of the asset and liability cash flows. A single economic scenario represents multiple consecutive periods of movements in the underlying interest rate or market rate returns; the length of the scenario period is determined by the length of the liabilities being valued. The economic scenarios are stochastically (randomly) generated using the prescribed Generator of Economic Scenarios (GOES). The prescribed GOES can be found on Conning's website. The objective is to determine if there is a reasonable likelihood that assets are insufficient to cover the obligations of the company, and by what amount they may be insufficient. Under economic scenarios where assets are insufficient, the principle-based methodology determines all the amounts of the insufficiencies and discounts them back to the valuation date. The largest discounted value is known as the Greatest Present Value of Accumulated Deficiencies, or "GPVAD," for that scenario. The stochastic reserve under VM-21 is set at a CTE(70) level (conditional tail expectation at the 70% level). The function CTE(70) means the average of the 30% (100%-70%) worst (largest) GPVADs. So, for example, if a company randomly generates 1,000 economic scenarios, it would then determine the largest accumulated amount of deficiency for each of the 1,000 scenarios. The CTE(70) stochastic reserve level would be determined by taking the average of the 300 [1,000 x (100% - 70%)] worst GPVADs out of the 1,000 scenarios.

The VM-21 reserve is calculated on an aggregated basis for all contracts subject to VM-21 and is then allocated to contracts using prescribed methods. Aggregation is permitted across variable annuity contracts with similar risk characteristics within the constraints set out in the Valuation Manual.

VM-22 — Non-Variable Annuities

VM-22 has an optional effective date of January 1, 2026, and a mandatory effective date of January 1, 2029. During the transition period, an insurer may elect to apply VM-22 to in-scope non-variable annuity contracts, subject to the Valuation Manual's transition provisions. Once elected for a category of business, VM-22 generally applies to all subsequent issues within that category. VM-22 replaces the formula-based CARVM methodology for in-scope contracts. The prior VM-22 (interest rate requirements for certain immediate annuities) has been redesignated as VM-V and continues to apply under the formula-based framework. The principle-based valuation methodology developed for non-variable annuity contracts defines 2 principal components of a principle-based reserve: 1) a Deterministic Reserve (DR); and 2) a Stochastic Reserve (SR). The level of risk embedded in a non-variable annuity contract will determine whether the PBR will consist of both reserve components (DR and SR) or only the DR component. VM-22 defines a Stochastic Exclusion Test (SET) that is designed to measure the level of risk embedded in the contract; blocks of business that pass the SET are exempt from the calculation of the SR. VM-22 also defines a Single Scenario Test (SST), a test that may be applied to blocks of business where contractholder behavior is not materially influenced by economic conditions. A group of contracts that passes the SST may be valued using only the DR, without computing the SR.

The stochastic reserve under VM-22 follows the same general framework as VM-21. Economic scenarios are stochastically (randomly) generated using the prescribed Generator of Economic Scenarios (GOES), and the GPVAD is determined for each scenario. The stochastic reserve under VM-22 is set at a CTE 70 (conditional tail expectation) determined by averaging the worst GPVADs across the generated scenarios. VM-22 also incorporates reinvestment guardrails to constrain assumed reinvestment yields under stochastic scenarios so that the projected reinvestment behavior remains within prescribed bounds.

As part of the calculation process, VM-22 allows companies to aggregate or group contracts with similar risk characteristics. For example, all fixed deferred annuities with similar crediting features and guaranteed minimum values may be grouped together. The SET is then applied on a group or aggregated basis and not a contract by

contract basis, and the DR and SR are likewise calculated on the aggregated or group basis. Aggregation is permitted across payout and accumulation product categories within prescribed boundaries; however, aggregation decisions can materially affect the reserve outcome and should be reviewed for reasonableness and consistency with the insurer's risk management framework.

The annual statement blank includes supplements for VM-21 and VM-22 that break out the principle-based reserve into its components. Regulators may request the assistance of NAIC modeling staff and/or the Valuation Analysis (E) Working Group in verifying exclusion testing as well as various components of the PBR on a smaller sample set of company contracts.

LONG-TERM CARE INSURANCE (LTCI) OVERVIEW

"Long-term care insurance" means any insurance policy or rider advertised, marketed, offered or designed to provide coverage for not less than 12 consecutive months for each covered person on an expense incurred, indemnity, prepaid or other basis, for one or more necessary or medically necessary diagnostic, preventive, therapeutic, rehabilitative, maintenance or personal care services, provided in a setting other than an acute care unit of a hospital[1]. Historically, insurers that wrote LTCI encountered difficulties accurately projecting claims costs, lapse rates, investment returns, and other factors associated with LTCI, and subsequently many writers have experienced unprofitability in older (legacy) blocks of LTCI business. This has led many companies to request significant rate increases, modify product benefits or exit the product line altogether. Therefore, many insurers continue to experience significant solvency challenges related to this line of business, and state insurance regulators should continue to carefully evaluate and monitor the solvency position of all insurers with a material amount of LTCI business.

These same risks also affect reinsurers because the reinsurance contract may not arbitrarily allow for ceded premium increases. Additionally, in order to effectuate a true transfer of risk, the reinsurer may not have the ability to require the direct writer to request rate increases. As some insurers look for avenues to minimize or eliminate its risk from the LTCI block, they may look to new reinsurance opportunities or nontraditional buyers.

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

Actuarial Guideline 51

Effective for reserves reported with the Dec. 31, 2017, financial statement, Actuarial Guideline 51—*The Application of Asset Adequacy Testing to Long-Term Care Insurance Reserves* (AG 51) now applies. The *Health Insurance Reserves Model Regulation* (#10) and the *Valuation Manual* VM-25, Health Insurance Reserves Minimum Reserve Requirements, contain requirements for the calculation of LTCI reserves. AG 51 requires companies with more than 10,000 LTCI enrollees to submit stand-alone LTCI asset adequacy analyses to the state. AG 51 is intended to provide uniform guidance and clarification of requirements for the appropriate support of certain assumptions for the asset adequacy testing applied to a company's LTCI block of contracts. AG 51 requires reporting to the department within the appointed actuary's actuarial memorandum required by VM-30 or in a special actuarial memorandum containing LTCI-specific information on the results of the analysis, assumptions on mortality, voluntary lapse, morbidity, investment returns and rate increase assumptions.

[1] Definition per *Long-term Care Insurance Model Act* (#640) Section 4.A.

Factors Affecting LTCI Reserves and Rates

This following guidance provides additional information that may assist state insurance department staff in understanding the differences in premium rate review and approval, and valuation review of reserve adequacy assumptions in order to maintain or improve state insurance departments' current intra-departmental coordination/communication practices between the states' rate reviewers, valuation actuaries and analysts/ examiners.

Reserve Increase Factors

1. **Background**

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

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

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

2. **Long-Term Care Insurance**

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

   With LTCI, some factors are likely to play out in a straightforward manner. A combination of higher life expectancy and lower lapses will lead to more people than expected reaching prime LTCI claims ages of 80 and above, which leads to companies holding higher reserves than originally anticipated. Similarly, all companies have experienced the decreasing interest rate environment, which has led to lower-than-expected investment returns and the need to hold higher reserves because investment income is relied upon to help pay claims.

   Mortality, lapse, and interest rate factors become observable and can develop credibility during the premium-paying years prior to policy years when significant claims tend to occur.

3. **Morbidity Assumptions**

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

   There has not been uniform experience development in morbidity, except that length of claim has tended to increase, likely because cognitive (e.g., dementia and Alzheimer's disease) claims tend to be longer than

average and incidence has been higher than expected, likely due to more people reaching the age when cognitive claims tend to occur.

Because of divergent experience among companies and because morbidity becomes observable and credible during the later claim-paying years, establishing and regulating LTCI morbidity assumptions has not been straightforward. However, as with other factors and other products, the handling of these situations is addressed in Model #820, *Valuation Manual* and ASOPs. Examples of these standards include:

- Model #820 Section 12A(3)(a): "Assumptions shall, to the extent that company data is not available, relevant or statistically credible, be established using other relevant, statistically credible experience."
- Model #820 Section 12A(4): "Provide margins for uncertainty … such that the greater uncertainty, the larger the margin and resulting reserve."
- AG 51 (providing guidance on VM-30) Section 4.B.: "The analysis shall comply with applicable Actuarial Standards of Practice, including standards regarding identification of key risks. Material assumptions associated with the LTCI business shall be determined testing moderately adverse deviations in actuarial assumptions."
- *Acounting Practices and Procedures Manual* (AP&P Manual), Appendix A-010 paragraph 48.e (referenced in VM-30): "The total contract reserve established shall incorporate provisions for moderately adverse deviations."
- AP&P Manual, Appendix A-010 paragraph 51 (referenced in VM-30): "Annually, an appropriate review shall be made of the insurer's prospective contract liabilities … and appropriate increments … if such tests indicate that the basis of such reserves is no longer adequate."

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

4. **Rate Increases**

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

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

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

The reserve assumption changes can occur with initiation by the company, through formal or informal agreement between regulators or companies, or by relying on Model #820 Section 11.6., which allows a commissioner to require a company to change reserve assumptions and adjust reserves.

Example:

A typical example of a chain of events would first involve a block issued in 1995 to 1998 to policyholders with issue ages ranging from 52 to 62. By 2019, enough policyholders have reached prime LTC claim ages of 80+. This experience is what drives reserve assumption changes. As policyholders enter ages in the upper 80s and 90s, additional experience will be attained that will predict future LTCI costs and result in further changes in reserve assumptions. The development of older-age morbidity experience is expected to generate volatility in LTCI reserves. For some companies, the older-age morbidity experience will likely be unfavorable, with increased reserves needed. For most other companies, the older-age morbidity experience will likely be as expected, leading to no significant, unforeseen reserve increases.

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

5. **Rate Increase Factors**

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

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

6. **Intra-Department Communication and Coordination of Actuarial Review Work**

While every state insurance department may be structured differently, many state insurance departments have the same staff members perform work on both LTCI reserve valuation analysis and rate increase reviews, while others have separate staff perform these functions. In the latter instance, department staff should be aware of or coordinate the intra-department review work related to each function.

The following are suggested steps a state may consider ensuring that actuarial assumptions associated with the rate increase request are consistent with the assumptions embedded in the asset adequacy testing.

- Inquire of the company's actuary or senior management regarding:
  - The relationship of the actuarial assumptions embedded in the rate filing versus those made for annual statement reporting.
  - Explanation if there is inconsistency between assumptions reported.
  - How AG 51 affects the company's rates and reserves.
  - Affirmation that the assumptions underlying the projections are consistent with the assumptions used in asset adequacy analysis.
  - A copy of the company's rate increase plan when rate increase filings disclose that future rate increase filings, beyond what is currently being requested, are planned.
- Consider reviews of different filings for consistency. For example:
  - Compare reserving assumptions to rate increase assumptions,
    - e.g., review the RAAIS and the Actuarial Opinion and Memorandum (AOM) to ensure that assumptions used for pricing and reserving are similar in nature.
  - Identify assumptions underlying the asset adequacy testing memorandum that appear to be an outlier and then compare against a subsequent rate increase filing.

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

Analysis Documentation: The Statement of Actuarial Opinion Worksheet is intended to provide procedures for reviewing the Statement of Actuarial Opinion, Actuarial Opinion Summary, and Actuarial Report for compliance and assessment of risks. Results of the reserving risk analysis should be documented in Section III: Risk Assessment of the insurer.

Note that reserving risks also are included in the Reserving Risk Assessment.

Actuarial Opinion - General

1. Determine whether the insurer is exempt from filing the Actuarial Opinion.

	Comments
a. Actuarial Opinion filed	
b. Exemption granted	
i. Exemption ~~attached to~~filed with Annual ~~Financial~~ Statement	
ii. Reason for exemption: • Small company • Under supervision or conservatorship • Nature of business • Financial hardship • Other	

Commented [JL1]: Changed "Annual Financial Statement" to "Annual Statement" throughout this worksheet. The document is called the "Annual Statement."

Actuarial Opinion - Identification

2. Determine whether the Actuarial Opinion was prepared by a qualified actuary who was appointed by the insurer's board of directors prior to Dec. 31 of the calendar year for which the opinion was rendered.

	Comments
a. Appointed Actuary:	
i. Name	
ii. Relationship to ~~insurer~~company: • E~~Office/e~~mployee of ~~insurer~~ company or group (E) • Consultant (C)	
iii. Qualification (List the same qualification as listed in the Actuarial Opinion): • Fellow of the Casualty Actuarial Society (F) • Associate of the Casualty Actuarial Society (A) • Fellow of the Society of Actuaries ~~through the General Insurance track~~ (S) (P/C only) • ~~Member of the~~Approved by ~~American Academy of Actuaries~~Academy's ~~approved by the~~ Casualty Practice Council (M) • Other (O)	

Commented [JL2]: Exhibit A uses the term "company."

Commented [JL3]: Edited this in accordance with changes to the 2026 instructions.

Commented [JL4]: The P/C instructions don't say that the person has to be an MAAA (though we suspect that the Casualty Practice Council would not review someone who's not an MAAA).

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iv. Appointed by the board of directors by Dec. 31 of the calendar year for which the opinion was rendered	
v. Same actuary who was appointed for the previous Actuarial Opinion ("yes" or "no")	
If "no": • The insurer notified the insurance department of the state of domicile ~~domiciliary~~ ~~state insurance regulator~~ within five days of the replacement. • Within 10 days of above notification, the insurer ~~provided~~ provided the domiciliary commissioner a separate ~~n additional~~ letter stating whether there were any disagreements with the former A~~a~~ppointed A~~a~~ctuary and also in writing requested the former A~~a~~ppointed A~~a~~ctuary ~~provide~~ provide a letter ~~of agreement~~stating whether the former Appointed Actuary agrees with the statements in the insurer's letter. • The insurer ~~furnished~~ provided the former A~~a~~ppointed A~~a~~ctuary's letter to the domiciliary commissioner ~~of agreement~~.	
vi. IDENTIFICATION paragraph indicates the Appointed Actuary's relationship to the company, qualifications for acting as Appointed Actuary and date of appointment and specifies that the appointment was made by the Board of Directors.	

Commented [JL5]: General clean-up in this section to bring the text into closer alignment with the instructions.

One note: I'm not sure we always use the word "furnish" correctly in the instructions (i.e., "request such former Appointed Actuary to furnish a letter addressed to the Insurer" and "the Insurer shall furnish such responsive letter from the former Appointed Actuary to the domiciliary commissioner") and so changed "furnish" to "provide" here where it seemed to be warranted. I believe the common usage is "furnish [someone] with [something]."

Commented [JL6]: This requirement seems to have been missing from the worksheet. The current worksheet does not specify what needs to be in the IDENTIFICATION paragraph.

3. Determine whether the appointed actuary made the required disclosures if the insurer is a member of an intercompany pooling arrangement. (P/C only)

	Comments
a. Member of intercompany pooling arrangement ("yes" or "no") (The analyst should refer to Annual ~~Financial~~ Statement, Notes to Financial Statements, Note #26 to verify.)	
i. If "yes," the Actuarial Opinion includes: • Description of pool • Pool lead company identification • List of pool members, states of domicile and pooling percentages	
ii. Exhibits A and B represent company's share of pool and reconcile to company's financial statement	
iii. If company has 0% share: • The Actuarial Opinion reads similar to that provided for the lead company • Responses to Exhibit B, items #5 and #6 are $0 and "not applicable," respectively	

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• Lead company's Exhibits A and B are attached	

Actuarial Opinion - Scope

4. Determine whether the Appointed Actuary included the appropriate loss reserves, loss adjustment expense (LAE) reserves, and (if appropriate) other loss and premium reserves within the scope of the opinion as required by the *Annual Statement Instructions Property/Casualty (P/C)* and *Annual Statement Instructions Title (Title)* and whether the reserve amounts included in Exhibit A and Exhibit B of the Actuarial Opinion agree with the amounts reported in the Annual Statement.

Commented [JL7]: This is italicized later in the document and it seemed right to have consistency.

	Comments
a. SCOPE paragraph contains a sentence such as: • "I have examined the actuarial assumptions and methods used in determining reserves listed in Exhibit A, as shown in the Annual Statement of the Company as prepared for filing with state regulatory officials, as of Dec. 31, 20xx, and reviewed information provided to me through xxx date." • "I have examined the reserves listed in Exhibit A, as shown in the Annual Statement of the Company as prepared for filing with state regulatory officials, as of Dec. 31, 20xx and reviewed information provided to me through xxx date." • Other or none (provide comments).	
b. Exhibit A:	
i. Attached to or made part of the Actuarial Opinion	
ii. Lists items and amounts with respect to which the Appointed Actuary is expressing an opinion, including: • Reserve for net unpaid losses • Reserve for net unpaid LAE • Reserve for direct and assumed unpaid losses • Reserve for direct and assumed unpaid LAE	
iii. Shows amounts that reconcile to corresponding Annual ~~Financial~~ Statement references. If amounts do not reconcile, the analyst should discuss any differences and concerns.	
iv. Lists other items on which the Appointed Actuary is expressing an opinion ~~(P/C only),~~ including: • Reserve for retroactive reinsurance assumed (page 3 write-in item) (P/C only) • Other loss reserve items • Reserve for direct and assumed unearned premiums for P&C long duration contracts (should be shown on Exhibit A regardless of whether the amounts are material) (P/C only) • Reserve for net unearned premiums for P&C long duration contracts (should be shown on Exhibit A regardless of whether the amounts are material) (P/C only)	

Commented [JL8]: The title Exhibit A has a line item for "other items on which the Appointed Actuary is expressing an Opinion."

Commented [JL9]: Added to 2026 instructions

Commented [JL10]: Added to 2026 instructions

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• Other premium reserve items such as premium deficiency reserves	
~~v. Cite any concerns with amounts or unusual findings with other items~~	
~~vi.~~v. ~~Statement~~ Appointed Actuary states that items in Exhibit A reflect the disclosure items #8 through #12.24 ~~(~~(#8 through #13 for Title)~~)~~ in Exhibit B	

5. Determine whether the Appointed Actuary relied on an ~~officer of~~individual at the company for data preparation and whether the data used in forming the Appointed Actuary's opinion were reconciled to Annual ~~Financial~~ Statement, Schedule P – Part 1 (P/C) or Schedule P – Parts 1 and 2 (Title).

	Comments
a. SCOPE paragraph:	
i. Gives the name and title of the individual at the company that the Appointed Actuary relied on for data preparation.	
ii. States that the Appointed Actuary evaluated that data for reasonableness and consistency.	
iii. States that the Appointed Actuary reconciled ~~or reviewed the of the~~at data used in the analysis to Annual ~~Financial~~ Statement, Schedule P – Part 1 (P/C) or Schedule P – Parts 1 and 2 (Title).	
iv. If the data was not reconciled, the analyst should document any reasons provided by the Appointed Actuary as to why the reconciliation was not performed. Further, if the reconciliation was performed but the data did not reconcile, the analyst should document any reasons provided by the Appointed Actuary as to why the data did not reconcile.	
v. States that the Appointed Actuary's examination included a review of the actuarial assumptions and methods used and tests of the calculations as considered necessary.	

Actuarial Opinion - Opinion

6. Determine whether the Actuarial Opinion states that reserves meet the requirements of the insurance laws of the state of domicile, are computed in accordance with accepted ~~loss reserving~~actuarial standards ~~and principles~~, and make a reasonable provision for all unpaid loss and LAE obligations of the insurer under the terms of its ~~policies~~ contracts and agreements~~, and whether all portions of the insurer's reserves are covered by the Actuarial Opinion~~.

	Comments
a. OPINION paragraph states that the:	
i. Amounts shown in Exhibit A meet the requirements of the insurance laws of the state of domicile.	

Commented [JL11]: This seems to be covered in iii. above.

Commented [JL12]: Needed updating due to removal of pool disclosure in Exhibit B and associated changes in numbering.

Commented [JL13]: P/C instructions for 2026 no longer specify that the person has to be an officer.

Commented [JL14]: This is not in paragraph 4 of the instructions. The instructions provide information in paragraph 7 to guide disclosures in the report if the AA reviewed a reconciliation performed by others.

Commented [JL15]: This is not in the instructions.

Commented [JL16]: Added for 2026 instructions

Commented [JL17]: The term used in the instructions is "actuarial standards," not "loss reserving standards."

Commented [JL18]: We removed this from the instructions because the CAS reserving principles have been rescinded.

Commented [JL19]: Instructions use the term "contracts."

Commented [JL20]: The actuarial opinion does not have to cover "all portions of the insurer's reserves," e.g., the actuary does not need to opine on UEPR for short duration contracts.

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ii. Amounts shown in Exhibit A are computed in accordance with accepted actuarial standards ~~and principles~~ or similar language, such as "consistent with reserves computed in accordance with …".	
iii. Amounts shown in Exhibit A make a reasonable provision (carried reserve is within the Appointed Actuary's range of reasonable reserve estimates) for all unpaid loss and LAE obligations of the ~~insurer~~ company under the terms of its contracts and agreements.	
~~• If "no," the type of opinion is:~~ ~~○ Deficient or Inadequate. (Carried reserve is less than the minimum amount that the Appointed Actuary believes is reasonable.)~~ ~~○ Redundant or Excessive. (Carried reserve is greater than the maximum amount that the Appointed Actuary believes is reasonable.)~~ ~~○ Qualified. (Carried reserves for a certain item or items are in question because they cannot be reasonably estimated or the Appointed Actuary is unable to render an opinion on those items.)~~ ~~○ No Opinion. (The Appointed Actuary cannot reach a conclusion due to deficiencies or limitations in the data, analysis, assumptions, or related information.)~~	
b. If the SCOPE includes material unearned premium reserves for P&C long duration contracts, the OPINION paragraph states that the amounts shown in Exhibit A make a reasonable provision for the unearned premium reserves for P&C long duration contracts. (P/C only) • If the Unearned Premium Reserves for P&C Long Duration Contracts reported on lines 7 or 8 of Exhibit A are nonzero but the Appointed Actuary deems the amounts immaterial and is not issuing an opinion on these amounts, the Appointed Actuary should include clarifying comments in the SCOPE, OPINION, and/or RELEVANT COMMENTS sections of the opinion.	
~~b.~~ c. If the SCOPE includes other material loss or premium reserve items on which the Appointed Actuary is expressing an opinion, the OPINION paragraph states that the amounts shown in Exhibit A make a reasonable provision for the other loss or premium reserve items.	
• If amounts on Exhibit A do not meet the requirements of the insurance laws of the state of domicile, are not computed in accordance with accepted actuarial standards and principles, or do not make a reasonable provision, the type of opinion is:	

Commented [JL21]: We removed this from the instructions because the CAS reserving principles have been rescinded.

Commented [JL22]: I moved this section below the sections on long duration UEPR and other premium or loss reserve items, because if reserves for these items are not deemed reasonable and the amounts are material, the entire opinion may be of a type other than "reasonable."

Commented [JL23]: Added to 2026 instructions

Commented [JL24]: 2026 instructions say, "If the Scope includes material Unearned Premium Reserves for P&C Long Duration Contracts, Other Loss Reserve items, or Other Premium Reserve items on which the Appointed Actuary is expressing an opinion…" I think the word "material" is understood to go with "other loss reserve items" and "other premium reserve items."

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○ Deficient or Inadequate. (Carried reserve is less than the minimum amount that the Appointed Actuary believes is reasonable.) ○ Redundant or Excessive. (Carried reserve is greater than the maximum amount that the Appointed Actuary believes is reasonable.) ○ Qualified. (Carried reserves for a certain item or items are in question because they cannot be reasonably estimated or the Appointed Actuary is unable to render an opinion on those items.) ○ No Opinion. (The Appointed Actuary cannot reach a conclusion due to deficiencies or limitations in the data, analyses, assumptions, or related information.)	
~~c.~~ If the Appointed Actuary ~~made~~ used another actuary's analysis that was not produced under the Appointed Actuary's direction ~~of the analysis of another actuary not within the Appointed Actuary's control~~ for a material portion of the reserves, ~~t~~: ~~d.~~ ~~T~~he other actuary is identified by name, credential and affiliation. ~~e.~~d. ~~The Appointed Actuary discloses whether he or she reviewed the other actuary's underlying analysis. If a review was conducted, the Appointed Actuary should disclose the extent of the review including items such as the methods and assumptions used and the underlying arithmetic calculations.~~	
~~f.~~e. If the Appointed Actuary ~~made use of~~used the work of a non-actuary ~~not within the Appointed Actuary's control~~ for a material portion of the reserves: i. The individual is identified by name and affiliation. ii. The Appointed Actuary describes the type of analysis the non-actuary performed.	
~~g. If the Appointed Actuary made use of the work of another not within the Appointed Actuary's control for a material portion of the reserves, what percentage of the total reserves was based on the work of others?~~	

Commented [JL25]: We removed the "made use of" and "control" language from the instructions.

Commented [JL26]: This is a requirement for the report, not the opinion.

Commented [JL27]: We removed the "made use of" and "control" language from the instructions.

Commented [JL28]: The AA is not required to disclose this in the opinion. In the 2026 instructions, the report requires disclosure of "The dollar amount of the reserves covered by the other's analysis or opinion and the percentage of the total reserves subject to the Appointed Actuary's opinion that these other reserves represent."

7. If applicable, identify the reasons why the Actuarial Opinion states the reserves do not make a reasonable provision for unpaid loss and LAE obligations.

	Comments
a. If the Appointed Actuary issues a Qualified Opinion, the Appointed Actuary: i. Discloses the item(s) to which the qualification relates, the reason(s) for the qualification and the amounts ~~of~~ for such items.	

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ii. States whether the carried reserves make a reasonable provision for the liabilities, except for the item(s) to which the qualification relates.	
b. If the Appointed Actuary issues a statement of No Opinion, the Appointed Actuary includes a description of the reasons why no opinion could be given.	
c. Review and assess, as applicable: i. If the type of opinion is Deficient or Redundant, the differences between the Appointed Actuary's indicated reserves (or range of reasonable reserves) and those carried by the insurer, and the impact of the differences on the insurer's policyholders' surplus. ii. The reasons why a Qualified Opinion or No Opinion was given. iii. The need to perform additional analysis and procedures on the items or risks affected.	

Actuarial Opinion – Relevant Comments and Exhibit B Disclosures

8. Determine whether the Appointed Actuary commented on various topics and issues reflected in Exhibit B of the Actuarial Opinion as required by the *Annual Statement Instructions Property/Casualty and Title ~~Insurers~~*.

	Comments
a. Risk of Material Adverse Deviation:	
i. Description of company-specific risk factors	
ii. Identification of materiality standard and the basis for establishing this standard	
iii. Risk of material adverse deviation ("yes" or "no")	
iv. Bright Line Indicator triggered (If "yes," comments from the Appointed Actuary should be pursued if the Appointed Actuary does not believe a risk of material adverse deviation exists.) (P/C only)	
b. Other disclosures in Exhibit B:	
i. The following amounts in Exhibit B match the corresponding Annual ~~Financial~~ Statement references. ~~The Appointed Actuary may include~~ RELEVANT COMMENT paragraphs should describe~~ing~~ the significance of the items. P/C • ~~Statutory surplus~~ • Anticipated net salvage and subrogation • Nontabular discount • Tabular discount • ~~Net reserves for the company's share of voluntary and involuntary pools' and associations' reserves~~	

Commented [JL29]: The requirement is a "should," not a "may."

Commented [JL30]: Surplus is item 7 on Exhibit B. The AA is only asked to comment on the significance of the amounts in items 8 through 13.

Commented [JL31]: Deleted from 2026 instructions

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• Net asbestos reserves • Net environmental reserves • Extended reporting endorsement policy reserve associated with claims-made contracts reported as loss and LAE reservesclaims-made loss reserves • Extended reporting endorsement policy reserve associated with claims-made contracts reported as • Extended claims-made unearned premium reserves • Net reserves for A&H Long Duration Contracts • Other items on which the Appointed Actuary is providing relevant comment Title • Known claims reserve • Statutory premium reserve • Aggregate of other reserves required by law • Supplemental reserve • Anticipated net salvage and subrogation • Discount included as a reduction to reserves • Other items on which the Appointed Actuary is providing relevant comment If the amounts do not match the Annual Statement references, discuss the differences and any concerns.	
c. Reinsurance:	
i. Discussion of retroactive reinsurance	
ii. Discussion of financial reinsurance	
iii. Discussion of reinsurance collectability: • No discussion • Discussion with little comment • The Appointed Actuary solicited information from management on actual collectability problems • The Appointed Actuary reviewed ratings of reinsurers • The Appointed Actuary reviewed Schedule F of the Annual Financial Statement for indications of regulatory action or reinsurance recoverable on paid losses over ninety (90) days past due	
d. Exceptional values for one or more reserve-related IRIS ratios (P/C only): • None • One-year reserve development to PY PHSpolicyholders' surplus (#11) • Two-year reserve development to 2nd PY PHSpolicyholders' surplus (#12) • Estimated current reserve deficiency to PHS policyholders' surplus (#13)	

Commented [JL32]: We adjusted the wording of this item in Exhibit B for the 2026 instructions.

Commented [JL33]: This was added to Exhibit B several years ago.

Commented [JL34]: This is in the instructions and might be helpful to put here so that the analyst knows why the AA is instructed to review Schedule F.

Commented [MF35]: Names as stated in the NAIC's IRIS manual.

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The Appointed Actuary must include relevant comment on the factors that led to the unusual value(s) if IRIS tests #11, #12, or #13 have exceptional values.	
e. ~~Comment~~ The Appointed Actuary must include relevant comment on the factors that led to the exceptional reserve development if reserves cause the ratio of one-year or two-year known claims reserve development or one-year or two-year reserve development to the respective prior year's policyholders' surplus to be greater than 20% (Title only).	
f. Significant change in the actuarial assumptions or methods from those previously employed	
g. Comments on any additional topics (e.g., lack of historical data, etc.)	

Commented [JL36]: It seems like this requirement might be important to explicitly include so that analysts know to look for the explanation if warranted.

Commented [JL37]: We added this requirement years ago.

Actuarial Opinion – Assurance That an Actuarial Report Has Been Prepared, Signature, Requirements for Actuarial Report

9. Determine whether the Appointed Actuary indicates that an Actuarial Report has been prepared that supports the findings expressed in the Actuarial Opinion. Determine whether the Actuarial Opinion has been signed according to the Instructions. If the Actuarial Report is requested, determine if the report contains the required elements.

	Comments
a. The Appointed Actuary indicates that an Actuarial Report and underlying actuarial work papers supporting the Actuarial Opinion will be maintained at the company and available for regulatory examination for seven years.	
b. The Actuarial Opinion concludes with the signature, the printed name, the employer's name, the address, the telephone number and the email address of the Appointed Actuary, as well as the date the Actuarial Opinion was rendered.	
c. Copy of the Actuarial Report requested.	
d. Requirements of the Actuarial Report (to be verified by analyst if report is requested):	
i. The Actuarial Report is signed and dated by the Appointed Actuary.	
ii. The Actuarial Report is consistent with Actuarial Standard of Practice (ASOP) No. 41, *Actuarial Communications* and includes:	
• Narrative component that provides sufficient detail to clearly explain to company management, the board of directors, the regulator, or other authority the findings, recommendations and conclusions, as well as their significance.	
• Technical component that provides sufficient documentation and disclosures for another actuary	

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practicing in the same field to evaluate the work and shows the analysis from the basic data (e.g., loss triangles) to the conclusions.	
iii. Actuarial report includes required elements from the Instructions:	
• Description of the Appointed Actuary's relationship to the company with clear presentation of the Appointed Actuary's role in advising the board of directors and/or management regarding the carried reserves. The actuarial report should identify how and when the Appointed Actuary presents the analysis to the board of directors and, where applicable, to the officer(s) of the Company responsible for determining the carried reserves.	
• An exhibit that ties to the Annual Statement and compares the Appointed Actuary's conclusions to the carried amounts consistent with the segmentation of exposure or liability groupings used in the analysis. The Appointed Actuary's conclusions include the Appointed Actuary's point estimate(s), range(s) of reasonable estimates or both.	
• An exhibit that reconciles and maps the data used by the Appointed Actuary, consistent with the segmentation of exposure or liability groupings used in the analysis, to the Annual ~~Financial~~ Statement, Schedule P line of business reporting. An explanation should be provided for any material differences.	
• An exhibit or appendix showing the change in the Appointed Actuary's estimates from the prior Actuarial Report, including extended discussion of factors underlying any material changes. If the Appointed Actuary is newly appointed and does not review the work of the prior Appointed Actuary, the Appointed Actuary should disclose this.	
• Extended comments on trends that indicate the presence or absence of risks and uncertainties that could result in material adverse deviation.	
• Extended comments on factors that led to unusual IRIS ratios for One-Year Reserve Development to Surplus (#11), Two-Year Reserve Development to Surplus (#12) or Estimated Current Reserve Deficiency to Surplus (#13), and how these factors were addressed in current and prior year analyses. (P/C only)	
• Extended comments on factors that led to exceptional reserve development and how these factors were addressed in prior and current analyses. (Title only)	

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• If the Appointed Actuary has used an analysis or opinion not material portion of the reserves: ▪ The dollar amount of the reserves covered by the other's analysis or opinion and the percentage of the total reserves subject to the Appointed Actuary's opinion that these other reserves represent. ▪ Whether and to what extent the Appointed Actuary reviewed the other's underlying analysis, including items such as methods and assumptions used and underlying arithmetic calculations. ▪ If the Appointed Actuary reviewed the other's underlying analysis, the Appointed Actuary's conclusions from the review.	
• Disclosure of all reserve amounts associated with A&H long duration contracts. (P/C only)	

Commented [JL38]: Added to 2026 P/C instructions

Actuarial Opinion Summary (P/C only)

10. Determine whether the Actuarial Opinion Summary (AOS) was prepared according to regulatory requirements.

a. Domiciliary state insurance regulator requires a confidential AOS. i. Required AOS was submitted by March 15 or by a later date specified by the domiciliary state. ii. AOS was signed and dated by the same Appointed Actuary who signed the Actuarial Opinion.	

11. If the insurer is a member of an intercompany pooling arrangement, verify that the AOS discloses pooling information. ~~(P/C only)~~

Commented [JL39]: Moved "P/C only" to the top of the section because title insurers do not file the AOS.

	Comments
a. Member of intercompany pooling arrangement:	
i. Percentage of company's share of pool is disclosed.	
ii. Numbers for non-0% companies reflect the company's share of the pool. Numbers for 0% pool participants are those of the lead company.	

12. Determine whether the AOS contains the required comparisons and whether the amounts in the AOS reconcile with those in the Actuarial Opinion, Actuarial Report and Annual ~~Financial~~ Statement.

	Comments
a. The AOS includes:	

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i. The Appointed Actuary's range of reasonable estimates for loss and LAE reserves, net and gross of reinsurance, when calculated. ii. The Appointed Actuary's point estimates for loss and LAE reserves, net and gross of reinsurance, when calculated. iii. The company's carried loss and loss adjustment expense reserves, net and gross of reinsurance. iv. The difference between the company's carried reserves and the Appointed Actuary's estimates calculated in i. and ii. above, net and gross of reinsurance.	
b. Net and gross reserve amounts reported by the Appointed Actuary in the AOS reconcile to the corresponding values reported in the insurer's Annual Statement, the Appointed Actuary's Actuarial Opinion and the Actuarial Report. If not, the Appointed Actuary provides an explanation of the difference.	
c. If the company's carried reserves are below the Appointed Actuary's point estimate or below the midpoint of the Appointed Actuary's range, how material is the difference? • As a percent of surplus • As a percent of carried reserves • In relation to the company's risk-based capital (RBC) position ~~(P/C only)~~ • Is the difference greater or less than the materiality standard	

13. Determine whether the Appointed Actuary's opinion implied by the comparisons in the AOS is consistent with the type of opinion rendered in the Actuarial Opinion.

	Comments
a. The AOS is consistent with the Appointed Actuary's conclusion that the amounts shown in Exhibit A are Reasonable, Deficient, or Redundant; the Opinion is Qualified; or No Opinion can be given. i. Opinion type is "Reasonable": Carried reserves are at or near the Appointed Actuary's point estimate and/or within the Appointed Actuary's range. ii. Opinion type is "Deficient": Carried reserves are materially below the Appointed Actuary's point estimate and/or below the low end of the Appointed Actuary's range. iii. Opinion type is "Redundant": Carried reserves are materially above the Appointed Actuary's point estimate and/or above the high end of the Appointed Actuary's range. iv. Opinion type is Qualified or No Opinion: The Appointed Actuary's choice of presentation in AOS will vary.	

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14. Determine whether the AOS is compliant with reporting requirements regarding persistent adverse development. ~~(P/C only)~~

	Comments
a. The company has experienced one-year adverse development in excess of 5% of prior year's surplus, as measured by the Annual ~~Financial~~ Statement, Schedule P – Part 2 – Summary, in three or more of the past five calendar years.	
i. If "yes," the Appointed Actuary includes an explicit description of the reserve elements or management decisions that were the major contributors.	

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NAIC NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

MEMORANDUM

TO: Commissioner Sharon Clark (TN), Chair, Financial Regulation Standards and Accreditation (F) Committee

FROM: Danielle Smith (MO), Chair, Financial Analysis Solvency Tools (E) Working Group

DATE: July 29, 2026

RE: Accreditation Part B Expectations for Group Capital Calculation Filing Review

The Financial Analysis Solvency Tools (E) Working Group (FASTWG) is responsible for maintaining the NAIC's *Financial Analysis Handbook* (Handbook) for risk-focused analysis and monitoring of the financial condition of insurance companies and groups. As part of its ongoing maintenance responsibilities, FASTWG and its support staff routinely receive questions from states regarding analysis expectations and requirements.

As the Accreditation Part A requirements related to Group Capital Calculation filings became effective 1/1/2026, FASTWG staff have received questions regarding expectations for analyst review and utilization of GCC filings within the holding company analysis process. To clarify expectations in this area, FASTWG has proposed the new Lead State holding company analysis procedure and accompanying edits to be included in the 2026 Annual/2027 Quarterly Edition of the Handbook in the following Attachment A.

As noted in the procedure, Lead State analysts will not be required or expected to complete the optional GCC review procedures in the Handbook in conducting the annual holding company analysis. However, the Lead State analyst will be expected to perform a review of the filing each year (if received) and to incorporate any findings and takeaways into the Group Profile Summary in accordance with analysis timelines and expectations.

As such, we recommend that the Committee consider updates to the Accreditation Part B guidelines for financial analysis to include this expectation, as shown in tracked changes below.

Part B1: Financial Analysis

e. Documented Analysis Procedures

Process-Oriented Guidelines:

1) The analyst should review and consider information from each of the following sources in conducting a risk-focused analysis. The review should be evidenced by sign-off and dating of the information source, a procedure step or a simplified checklist:
   - Annual statement.
   - Actuarial opinion.
   - Actuarial Opinion Summary (property/casualty [P/C]) or Regulatory Asset Adequacy Issues Summary (life/health [L/H] and fraternal).
   - Management's discussion and analysis.
   - Annual audited financial statements.

- Holding company filings (i.e., Form A, Form B, Form C, Form D, Form E, Form F (Lead State), Group Capital Calculation (Lead State) and external filings: U.S. Securities and Exchange Commission [SEC] and International Financial Reporting Standards [IFRS]) as applicable to either the domestic regulator or lead state depending on the filing.

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

Thank you for your consideration of this referral. If there are any questions regarding the issues discussed, please contact me or NAIC support staff for clarification.

Attachment A

FINANCIAL ANALYSIS HANDBOOK

2026 Annual /2027 Quarterly

(Note that detail before/after the following excerpts are eliminated to conserve space)

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

Understand the Insurance Holding Company System

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

Conduct Detailed Analysis of the Insurance Holding Company System

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

10. Group Capital Calculation (GCC):

    If the insurance group is subject to the requirements to perform and file a Group Capital Calculation (GCC), review and determine if any concerns or material risks exist regarding the overall group capital position, quantifiable risks, or capital interdependencies within the group as may be identified through analysis of the GCC. See chapters VI.H and VI.I for applicable optional GCC procedures and guidance.

PROCEDURE #10 instructs the analyst to evaluate the Group Capital Calculation (GCC) filing, if the insurance group is subject to GCC filing requirements. Analysts may consider optional procedures outlined in chapter VI.H when completing this assessment. Refer to additional guidance on the GCC in chapter VI.I.

VI.H. Group-Wide Supervision – Group Capital Calculation (Lead State) Procedures

GCC as Input into Group Profile Summary

The GCC is intended to be used as an input into the GPS. The expectation is that the GCC summary section will help to document a high-level summary of the analyst's take away of the GCC, as well as the Strategic branded risk. The manner in which the analyst determines what else should be documented beyond the GCC Summary and the Strategic branded risk should be based upon the following steps, since these steps contemplate the previously mentioned concept that the existing evaluation of the financial condition should be used in evaluating the depth of review of the GCC. Therefore, the following procedure steps are optional

and should be customized to the evaluation of the GCC and the group's financial condition. The depth of the review in the "five-step process" and specific inquiries will vary based on each group's unique situation.

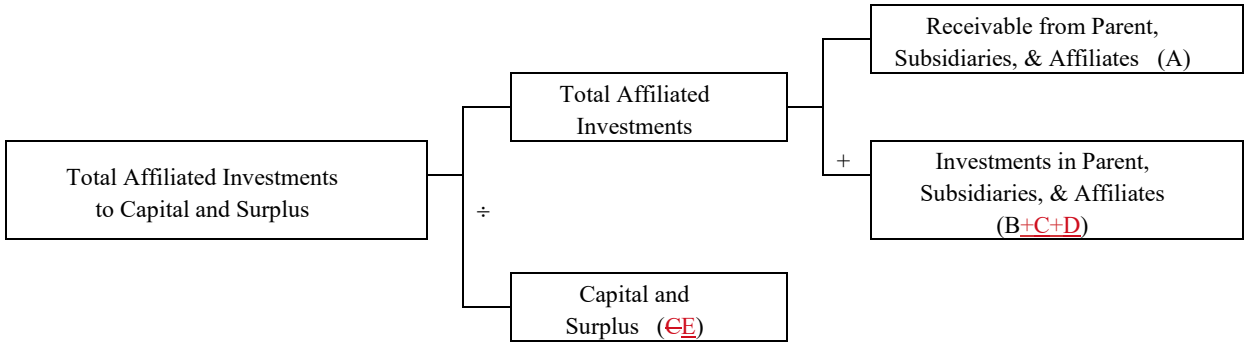
VI.I. Group-Wide Supervision – Group Capital Calculation (Lead State) – Analyst Reference Guide

Purpose of the Group Capital Calculation (GCC) in Holding Company Analysis

Background Information

In 2008, the NAIC Solvency Modernization Initiative (SMI) ~~began to~~ considered whether there were any lessons learned from the financial crisis that would cause the solvency framework to be modified. The NAIC determined that changes should be made in the area of group supervision, starting with the ~~new~~ annual requirement for the lead state of each group operating in the U.S. to complete a written holding company analysis. Since that time, other changes to state laws have been made to further enhance group supervision (e.g., Form F, Own Risk and Solvency Assessment (ORSA), ~~and~~ Corporate Governance reporting, Group Capital Calculation reporting). All of these ~~new~~ tools are inputs into the previously mentioned holding company analysis, which is summarized into the Group Profile Summary (GPS), a consistent tool used by all states~~, that is known as the Group Profile Summary (GPS)~~.

LIFE/A&H INVESTMENT RATIO 7 – TOTAL AFFILIATED INVESTMENTS TO CAPITAL AND SURPLUS



A. Receivable from Parent, Subs., & Affiliates	Page 2, Line 23, Column 3	
B. Investments in Parent, Subs., & Affiliates: Bonds, Mortgage Loans, Other Assets, Short-Term	Page 22, Line ~~49~~44+47+48+49, Column 1	
C. Investments in Parent, Subs., & Affiliates: Preferred Stock	Page E18, Line 0899999, Column 6 - 8	
D. Investments in Parent, Subs., & Affiliates: Common Stock	Page E18, Line 1699999, Column 6 - 8	
~~C~~E. Capital and Surplus	Page 3, Line 38, Column 1	

Result = (A+B+C+D) / ~~C~~ E *100 %

- If ~~C~~ E is zero or negative and (A+B+C+D) is positive, result is 999.
- If (A+B+C+D) and ~~C~~E are zero or negative, result is zero.

This ratio is a measure of the amount of capital and surplus invested in affiliated investments and receivables that may not be liquid or available to meet policyholder obligations. Investments in parent, subs., & affiliates is adjusted to exclude non-admitted amounts for affiliated preferred and common stock.

A relatively large value for this ratio should be questioned. The usual range includes all results less than 100 percent. See the general comments on investments titled "Life/A&H Investment Ratios," preceding Ratio 4.

Branded Risk(s): CR, LQ, MK

Impact of the Proposed Changes on 2025 IRIS Results

The Insurance Regulatory Information System (IRIS) Ratio 7–Total Affiliated Investments to Capital and Surplus currently pulls the investments in parents, subs and affiliates value from the five-year historical data table, which includes both admitted and non-admitted amounts for affiliated preferred and common stock. This creates a double penalty for insurers with non-admitted affiliated amounts as capital and surplus already excludes non-admitted. In 2025, forty-four insurers had an unusual result for IRIS 7. With the suggested change to minimize the potential

for over penalizing an insurer, the impact of the change didn't result any additional insurers being triggered with an unusual result if the calculation excluded the non-admitted values. Two life companies would not trigger Ratio #7. Therefore, committee support recommended changing the source for affiliated preferred and common stocks from the five-year historical data table to Schedule D, Part 6, where the net admitted value can be obtained. This is consistent with the change that was adopted for P&C IRIS ratio in 2025.

LIFE/A&H INVESTMENT RATIOS

For life insurers and fraternal societies, investments represent a particularly critical element in insurer performance and stability. Ratios 4, 5, 6 and 7 concern various investment aspects of significance in analyzing the financial condition of an insurer. Familiarize yourself with the insurer's investments on the Assets page of the annual financial statement and review the insurer's results on Ratio 11, Change in Asset Mix, to assist in determining the stability of the insurer's investment policy.

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

Review the amount of investments in affiliated insurers and receivables from affiliates as a percentage of invested assets and as a percentage of capital and surplus (Ratio 7). If the amount is high, an insurer may experience illiquidity or a low yield. Large investments in affiliated insurers may also increase the overall risk to which an insurer is subject. The ratio result could be distorted by the increasingly common use of reinsurance, whereby surplus is reduced by the risk transferred to the reinsurer, but assets remain in the numerator due to accounting of Modco/FWH. A company with a lower affiliated investment allocation but a heavy use of reinsurance could appear to be more "at risk" than a company with a higher affiliated investment allocation but lower use of reinsurance. Determine whether the insurer's investments in and amounts due from affiliates are consistent with protecting the interest of policyholders.