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18 SUPERIOR COURT OF CALIFORNIA  
19 COUNTY OF LOS ANGELES

20 JERRY HILL, JOSEPHINE HILL,  
21 WILSON MALLORY and NORENE  
22 MALLORY, Individually and on Behalf of  
23 Themselves and All Others Similarly  
24 Situated and on Behalf of the General  
25 Public,

26 Plaintiffs,

27 vs.

28 STATE FARM MUTUAL  
AUTOMOBILE INSURANCE  
COMPANY, STATE FARM LIFE  
INSURANCE COMPANY, and DOES 1  
through 100, Inclusive,

Defendants.

**ORIGINAL FILED**

MAY 24 2002

**LOS ANGELES  
SUPERIOR COURT**

Case No. BC 194491 – CLASS ACTION  
UNLIMITED JURISDICTION

**APPLICATION FOR LEAVE TO FILE  
AMICUS CURIAE BRIEF IN SUPPORT OF  
STATE FARM'S MOTION TO DISMISS;  
BRIEF OF AMICUS CURIAE NATIONAL  
ASSOCIATION OF INSURANCE  
COMMISSIONERS IN SUPPORT OF  
STATE FARM'S MOTION TO DISMISS**

Judge: Hon. Charles W. McCoy  
Hearing Date: To Be Determined  
Time: To Be Determined  
Dept: 308, Central Civil West

Filing Date: July 17, 1998  
Discovery Cut-Off: None Set  
Motion Cut-Off: None Set  
Trial Date: None Set

[Declaration of Douglas A. Hartz; Appendix of  
Foreign Authorities; and [Proposed] Order  
Granting Leave to File *Amicus Curiae* Brief filed  
concurrently]

1 **TO THE HONORABLE CHARLES W. McCOY, SUPERIOR COURT JUDGE OF THE**  
2 **LOS ANGELES SUPERIOR COURT:**

3 The National Association of Insurance Commissioners (“NAIC”) submits this instant  
4 Application to file an *amicus curiae* brief in support of State Farm’s motion to dismiss. As  
5 demonstrated herein, this Application is made and the Brief submitted on the grounds that:

6 1. The NAIC is familiar with the facts of this case, the questions involved and the  
7 scope of their presentation to date.

8 2. The interest of the NAIC arises from the possibility that the class remedy sought in  
9 this case would determine a “reasonable” level of surplus for an insurer that differs from that  
10 which is applied by insurance regulatory authorities. The certification of a class here therefore  
11 will have a substantial impact on solvency standards applied by insurance regulators.

12 3. The NAIC membership consists solely of the principal insurance regulatory  
13 officials of the fifty states, the District of Columbia, the territories and insular possessions of the  
14 United States. Started in 1871, it is the nation’s oldest association (recently incorporated as a  
15 non-profit corporation) of state government officials. The members of the NAIC control its  
16 actions. Only a member may request consideration of the NAIC filing an *amicus curiae* brief and  
17 such requires approval of the Executive Committee of the NAIC, which is made up of at least  
18 fifteen of its members.

19 4. The members of the NAIC are uniquely qualified and situated to assist the Court  
20 by presenting the regulatory and public policy concerns involved in this case. Individually and  
21 collectively, the members of the NAIC have a wealth of experience in the financial regulation of  
22 insurers. The members of the NAIC have this experience, and are interested in this case, because  
23 they are required by federal and state law to regulate the corporate and financial affairs of  
24 insurers, which the plaintiffs in this case would have this Court undertake.

25 5. The NAIC is concerned that the remedy and class relief requested by the plaintiffs  
26 necessarily requires this Court to determine the adequacy of the surplus of an insurance company,  
27 the financial regulation of which is the statutory responsibility of a department of insurance in a  
28 different state.

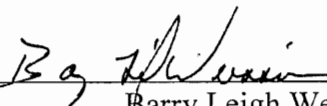
1           6.       The requested relief conflicts with state and federal law respecting the regulation  
2 by the several states of the insurance industry generally and the defendant State Farm Mutual  
3 Insurance Company specifically.

4           WHEREFORE, the NAIC respectfully prays this Court grant it leave to file the attached  
5 *Amicus Curiae* Brief.

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Dated: May 24, 2002

Respectfully submitted,  
SQUIRE, SANDERS & DEMPSEY L.L.P.

By:   
Barry Leigh Weissman  
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LosAngeles/82261.1

BRIEF OF *AMICUS CURIAE* NAIC IN SUPPORT OF STATE FARM'S MOTION TO DISMISS

1 The National Association of Insurance Commissioners (“NAIC”) files this *amicus curiae*  
2 brief to request this Court to consider certain insurance regulatory issues connected to its  
3 consideration of the pending Motion for Class Certification and defendant State Farm Mutual  
4 Automobile Insurance Company (“State Farm”)’s Motion to Dismiss. This case presents a matter  
5 of importance for state insurance regulation.

6 I.

7 **STATEMENT OF INTEREST OF AMICUS CURIAE**

8 The interest of the National Association of Insurance Commissioners arises from the  
9 possibility that the class remedy sought in this case would determine a “reasonable” level of  
10 surplus for an insurer that differs from that which is applied by insurance regulatory authorities.  
11 The certification of a class here will have a substantial impact on solvency standards applied by  
12 insurance regulators.

13 The NAIC membership consists solely of the principal insurance regulatory officials of  
14 the fifty states, the District of Columbia, the territories and insular possessions of the United  
15 States. Started in 1871, it is the nation’s oldest association (recently incorporated as a non-profit  
16 corporation) of state government officials. The members of the NAIC control its actions. Only a  
17 member may request consideration of the NAIC filing an *amicus curiae* brief and such requires  
18 approval of the Executive Committee of the NAIC, which is made up of at least fifteen of its  
19 members. *See* Bylaws of the National Association of Insurance Commissioners, art. IV,  
20 (Declaration of Douglas A. Hartz (“Hartz Decl.”), Exh. A.)

21 The mission of the NAIC, as set out in its Certificate of Incorporation, is to:

22 assist state insurance regulators, individually and collectively, in serving the  
23 public interest and achieving the following fundamental insurance regulatory  
24 goals in a responsive, efficient and cost-effective manner, consistent with the  
wishes of its members:

- 25 (a) Protect the public interest, promote competitive markets and facilitate the  
26 fair and equitable treatment of insurance consumers;  
27 (b) Promote, in the public interest, the reliability, solvency, and financial  
solidity of insurance institutions; and  
28 (c) Support and improve state regulation of insurance.

*See* Certificate of Incorporation of National Association of Insurance Commissioners, (Hartz  
Los Angeles/82261.1

1 Decl., Exh. B).

2 The members of the NAIC are uniquely qualified and situated to assist the Court by  
3 presenting the regulatory and public policy concerns involved in this case. Individually and  
4 collectively, the members of the NAIC have a wealth of experience in the financial regulation of  
5 insurers. The members of the NAIC have this experience, and are interested in this case, because  
6 they are required by federal and state law to regulate the corporate and financial affairs of  
7 insurers, which the plaintiffs in this case would have this Court undertake.

8 The members established the NAIC Financial Regulations Standards and Accreditation  
9 Program in June 1989 to ensure that each state satisfies certain baseline requirements deemed  
10 necessary to an effective regulatory system. The summary of this accreditation program provides  
11 in its introduction:

12 A system of effective solvency regulation provides crucial safeguards for  
13 America's insurance consumers. An effective system has certain basic  
14 components. It requires that regulators have adequate statutory and  
15 administrative *authority to regulate an insurer's corporate and financial  
affairs.*

16 NATIONAL ASS'N OF INS. COMMISSIONERS, THE NAIC FINANCIAL REGULATION STANDARDS AND  
17 ACCREDITATION PROGRAM 3 (2000) (emphasis added) (Hartz Decl., Exh. C).

18 The second standard for a state to qualify for accreditation is as follows:

19 Capital and Surplus Requirement - The Department should have the ability to  
20 require that insurers maintain a minimum level of capital and surplus to  
21 transact business. The Department should have the authority to require  
22 additional capital and surplus based upon the type, volume and nature of  
insurance business transacted. The Risk Based Capital (RBC) for Insurers  
Model Act or provisions substantially similar shall be included in state laws  
and regulations.

23 *Id.* at 12. If this Court certifies the class here, with the potential that this Court may order an  
24 Illinois domestic insurer to distribute \$47 billion to that class, such would call into question  
25 whether Illinois, or for that matter any state, has the ability to require that insurers domiciled in  
26 that state maintain a minimum level of capital and surplus. There is also a concern that if mutual  
27 company owners can force a distribution that threatens the solvency of an insurer, then stock  
28 company owners could likewise force such distributions without regard to the detriment to

1 policyholders relying on the insurer to cover claims.

2 **II.**

3 **ARGUMENT**

4 **A. Federal And State Law Require Deference To The Primary Jurisdiction Of Illinois**  
5 **Regulatory Authority Regarding The Corporate And Financial Affairs Of An Illinois**  
6 **Domestic Insurer**

7 This Court’s certification of a nationwide class will have the effect of applying California  
8 law extraterritorially to an Illinois domestic insurer. This result contravenes the law, which  
9 places the regulation of the business of insurance and of insurers’ corporate and financial affairs  
10 within the jurisdiction of the individual states.

11 **1. Consistent With Established Principles Of Insurance Regulation, States**  
12 **Regulate The Business Of Insurance And Insurers Corporate and Financial**  
13 **Affairs**

14 The McCarran-Ferguson Act clearly places responsibility for insurance regulation with  
15 the states in providing “that the continued regulation and taxation by the several States of the  
16 business of insurance is in the public interest . . . .” 15 U.S.C. § 1011. Further, “[t]he business of  
17 insurance . . . shall be subject to the laws of the several States which relate to the regulation or  
18 taxation of such business.” 15 U.S.C. § 1012(a). “No Act of Congress shall be construed to  
19 invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the  
20 business of insurance . . . unless such Act specifically relates to the business of insurance . . . .”  
21 15 U.S.C. § 1012(b). Thus, unless Congress specifically regulates the business of insurance,  
22 regulation is within the primary jurisdiction of the states.

23 The United States Supreme Court has supported the state-by-state method of regulation.  
24 *BMW of North America, Inc. v. Gore*, 517 U.S. 559 (1996), illustrates this understanding. The  
25 *Gore* case involved disclosure of certain pre-sale repairs to new vehicles. The U.S. Supreme  
26 Court recognized that states take differing approaches to common issues and, in the end, left  
27 undisturbed this manner of regulation. “No one doubts that a State may protect its citizens by  
28 prohibiting deceptive trade practices . . . . But the States need not, and in fact do not, provide such  
protection in a uniform manner. . . . The result is a patchwork of rules representing the diverse

1 policy judgments of lawmakers in 50 States.” *Id.* at 568-569. “That diversity demonstrates that  
2 reasonable people may disagree . . . .” *Id.* at 570.

3 **2. Each State May Regulate The Relationship Between An Insurer And That**  
4 **State’s Policyholders But Only The Domiciliary State May Regulate Its**  
5 **Insurer’s Corporate And Financial Affairs**

6 There is a difference between (a) regulating what an insurer does with policyholders in a  
7 state, and (b) regulating the corporate and financial affairs of another state’s domestic insurers.  
8 The *Gore* case above involved regulating what an insurer does with policyholders in a particular  
9 state. That case involved policyholders as policyholders. This case involves policyholders as  
10 owners and the regulation of that ownership relation by another state’s domestic insurer. In this  
11 case, class certification would affect the regulation of another state’s insurer’s corporate and  
12 financial affairs. California, through its courts, would be regulating an Illinois domestic insurer’s  
13 corporate and financial affairs. California may take a different approach than Illinois as to the  
14 regulation of California domestic insurer’s corporate and financial affairs. *See*, Part II.A.1.,  
15 *supra*. However, California cannot impose its approach on how Illinois regulates Illinois  
16 domestic insurer’s corporate and financial affairs.

17 As to what an insurer does with policyholders, “a state may determine who may engage in  
18 the insurance business within its boundaries, and prescribe terms upon which insurance  
19 companies may be authorized to transact such business. 19 APPLEMAN, INSURANCE LAW AND  
20 PRACTICE § 10322, at 15-16 (1982), citing *Western & Southern Life Ins. v. State Bd. of*  
21 *Equalization*, 4 Cal. App. 3d 21, 31, 84 Cal. Rptr. 88, 94 (1970).

22 Regulating what an insurer does with policyholders in a state derives from the state’s  
23 police power. *See First Nat. Ben. Soc. v. Garrison*, 58 F. Supp. 972 (S.D. Cal. 1945), *aff’d*, 155  
24 F.2d 522 (8<sup>th</sup> Cir. 1945).<sup>1</sup> On the other hand, regulating the corporate and financial affairs of  
25 domestic insurers derives as much from general corporate law (*see*, Part III.A.1. of Memorandum

26 <sup>1</sup> This case dealt with the effects of *United States v. South-Eastern Underwriters Ass’n*, 322  
27 U.S. 533 (1944) (holding that the business of insurance conducted across state lines is interstate  
28 commerce), but prior to the enactment of the McCarran-Ferguson Act (continuing the power of  
the states to tax and regulate the business of insurance despite its being interstate commerce).  
The affirming opinion simply stated, “Upon the authority of *Robertson v. California*, 66 S.Ct.  
1160, the judgment of the District Court, 58 F. Supp. 972, is affirmed.” 155 F.2d at 522.



1 in Support of State Farm's Motion To Dismiss ("State Farm Memo")) and sovereignty governing  
2 its own creations, as it does from the police power. In *Relfe v. Rundle*, 103 U.S. 222, 225 (1881),  
3 the Supreme Court said:

4 No state need allow the corporations of other states to do business within its  
5 jurisdiction unless it chooses, with perhaps the exception of commercial  
6 corporations; but, if it does, without limitation, express or implied, the  
7 corporation comes in as it has been created. Every corporation necessarily  
8 carries its charter wherever it goes, for that is the law of its existence. It may  
9 be restricted in the use of some of its powers while doing business away from  
its corporate home, but every person who deals with it everywhere is bound to  
take notice of the provisions which have been made in its charter for the  
management and control of its affairs both in life and after dissolution.

10 This was quoted in a case construing California law, which continued:

11 It is true that the courts in California cannot control the internal affairs of any  
12 foreign corporation. Such matters are to be conducted in pursuance of and in  
13 compliance with the provisions of the charter of the foreign corporation, and  
14 the laws of the country where it was created; but in the management and  
15 method of its business affairs in California with the citizens and residents  
thereof, in the sale or disposition or transfer of the shares of stock, it must  
conform to the laws of California in relation to such matters, and is bound  
thereby.

16 *London, Paris & American Bank, Ltd. v. Aronstein*, 117 F. 601, 609 (9<sup>th</sup> Cir. 1902).

17 In this case the remedy sought would require California to control the internal affairs of a  
18 foreign corporation. The *Aronstein* case dealt with the treatment of a single shareholder.  
19 Similarly, the case *Mission Ins. Group, Inc. v. Merco Construction Engineers, Inc.*, 147 Cal. App.  
20 3d 1059 (1983)<sup>2</sup> ("Mission"), relied upon by the Court of Appeal (Slip Op. at 7-8), dealt with a  
21 single policyholder. The distinguishing factor that separates this case from *Aronstein* and *Mission*  
22 is not that this case involves members versus shareholders, or life and auto insurance policies  
23 versus workers compensation. See Slip Op. at 9. The distinguishing factor is that the remedy  
24 sought in this case, class certification, by definition goes beyond how a single policyholder or  
25

26 <sup>2</sup> It should be noted that all of the insurers related to Mission became insolvent and were  
27 ordered into receivership within a few years of this decision. This may have been a very minor  
28 factor in relation to the subsequent insolvencies, but it probably did not help in efforts to prevent  
the insurers from weakening into insolvency. Often something like this can set off a chain  
reaction of events (i.e., a downgrade by rating agencies leads to policyholders having to switch  
carriers which leads to liquidity problems for the insurer which leads to another downgrade, etc.).

1 member is dealt with under California law. It would require California, through this Court, to  
2 both control the internal affairs of a foreign corporation and supplant the regulatory authority of  
3 Illinois over its domestic insurance companies.

4 The above can be summarized as follows, the difference between (a) regulating what an  
5 insurer does with policyholders and (b) regulating an insurer's corporate and financial affairs is  
6 the difference between regulating (a) the contract and (b) the company. California may regulate  
7 an Illinois insurer's contracts in California, but must defer to Illinois' regulation of the company,  
8 the insurer, and its corporate and financial affairs.

9 **B. States Regulate The Market To Protect Policyholders But Defer To The Insurer's**  
10 **State Of Domicile To Regulate The Corporate And Financial Affairs Of Its Insurers**  
11 **And California Should Do So Here**

12 The entirety of insurance regulation over the last 130 years has developed along two  
13 tracks, one related to regulating the market, the conduct of insurers, their contracts with  
14 policyholders, and the other related to financial and solvency regulation, the insurer's corporate  
15 and financial affairs. *See, e.g.*, Brian K. Atchinson, President of the NAIC, The NAIC's Risk-  
16 Based Capital System, Remarks Before the General Assembly of the Geneva Association,  
17 Bordeaux, France (June 7, 1996), *in* National Association of Insurance Commissioners, NAIC  
18 Research Quarterly, October 1996, Volume II, Issue 4, at 1-9, (Hartz Decl., Exh. D). *See also* R.  
19 KLINE, NATIONAL ASS'N OF INS. COMMISSIONERS, PRINCIPALS OF INSURANCE REGULATION – A  
20 REGULATOR'S INTRODUCTION TO THE INSURANCE INDUSTRY, ch. 8 (1999). This is also reflected  
21 in the Standing Committee structure of the NAIC as set out in article VI of the Bylaws of the  
22 National Association of Insurance Commissioners, where there are, separately, the Market  
23 Conduct and Consumer Affairs (D) Committee and the Financial Condition (E) Committee.  
24 (Hartz Decl., Exh. A)

25 Generally, states recognize that other states must be allowed to regulate what that state's  
26 insurers do in the other states' markets. This is market regulation. Equally, states recognize that  
27 another state's insurers' corporate and financial affairs are regulated by that state. This is  
28 financial and solvency regulation. Each state relies on the other states to effectively regulate the

1 financial condition and solvency of that state's insurers. California, through this Court in this  
2 case, should rely on Illinois to regulate the financial condition and solvency of its Illinois insurer.

3 California, in relying on Illinois to regulate the financial condition and solvency of its  
4 insurers, is relying on more than the resources of Illinois. The other states, working through the  
5 NAIC, provide an enormous amount of resources and assistance to Illinois (as well as every other  
6 state) in its regulation of the corporate and financial affairs of its domestic insurance companies.  
7 Over the last 130 years the states have developed increasingly complex, efficient and  
8 comprehensive systems to regulate the corporate and financial affairs of insurers. The NAIC  
9 assists state insurance regulators in the oversight of corporate and financial affairs of insurers. It  
10 does so through technical manuals; databases and automated analytical systems; professional  
11 accounting, analytical, financial, information systems and legal staff; and through education and  
12 training of the state's financial examiners, analysts and other staff. In support of these products  
13 and services, significant budgetary resources are allocated by the NAIC at the direction of the  
14 states. *See* NATIONAL ASS'N OF INS. COMMISSIONERS, 2001 ANNUAL REPORT 27 (attached hereto  
15 as Exhibit E).

16 There are dozens of organizations and thousands of professionals in these state-based  
17 systems. *See* NATIONAL ASS'N OF INS. COMMISSIONERS, 2000 INSURANCE DEPARTMENT  
18 RESOURCES REPORT 1, 4-8 (2001), (Hartz Decl., Exh. F). All of these resources are coordinated  
19 toward the goals of ensuring "the reliability, solvency, and financial solidity of insurance  
20 institutions" through effective regulation of their corporate and financial affairs. It is both Illinois  
21 and these enormously complex regulatory systems, developed over decades, that this Court would  
22 be supplanting should it certify the class here and necessitate its having to undertake the  
23 regulation of the corporate and financial affairs of an Illinois insurer.

24 C. **A Mutual Insurer's Main Source Of Capital Is Its Accumulated Surplus And**  
25 **Opening This To Attack May Threaten The Existence Of This Form Of Insurer**  
26 **Which Would Likely Be A Detriment To Policyholders**

27 In the chapter on Insurer Organizational Forms in R. KLINE, NATIONAL ASS'N OF INS.  
28 COMMISSIONERS, A REGULATOR'S INTRODUCTION TO THE INSURANCE INDUSTRY 5-4 (1999), the

1 author discusses the nature of insurers of this form:

2 [M]utual insurers are not motivated by profits but rather to serve their  
3 policyholder-members. This may be reflected in lessened incentives to incur  
4 risk in return for greater income, although growth may still be an important  
5 objective for some mutual insurers. On the other hand, mutual insurers have  
6 greater difficulty in raising capital to fund growth, and hence, must rely to a  
7 greater extent on accumulated surplus and income from new members to  
8 support growth. Scholars also believe that the managers of mutual insurers  
9 tend to exercise more discretion, which tends to favor long-term stability over  
10 greater risk.

11 The difficulty for mutual insurers to raise capital for growth, which in some markets  
12 impacts the insurers financial strength and even its solvency, has lead to a greatly increased  
13 activity in insurer demutualizations. *See, generally,* Thomas Mulhare, *Insuring Against*  
14 *Demutualization: Mutual Insurers Should Take Steps To Prevent Policyholders From Forcing A*  
15 *Demutualization That Could Threaten The Company's Long-Term Strategy And Survival*, BEST'S  
16 REVIEW, Nov. 2001; Matthias Rieker, *More Insurers Expected to Demutualize in Near Term*,  
17 AMERICAN BANKER, Oct. 29, 2001; Fran Matso Lysiak, *Consumer Groups Air Concerns over*  
18 *Anthem's Demutualization*, BEST'S INSURANCE NEWS, Oct. 3, 2001.

### 19 III.

### 20 CONCLUSION


21 In the present case, there is the potential for this Court having to set standards for solvency  
22 that are normally within the primary jurisdiction of state insurance regulators. We believe such a  
23 determination may have significant implications for consumer interests that have traditionally  
24 been protected by state insurance regulators as part of the executive branch of government.  
25 Solvency regulation has historically relied upon the considerable expertise of the domiciliary  
26 insurance regulator to regulate the corporate and financial affairs of its insurers, in accordance  
27 with widely recognized principles of state insurance regulation, no matter where such companies  
28 may do business. We therefore respectfully ask the Court to grant State Farm's Motion to  
Dismiss because of the potentially significant impact this case has on state insurance regulation.

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Dated: May 24, 2002

Respectfully submitted,

SQUIRE, SANDERS & DEMPSEY L.L.P.

By:   
Barry Leigh Weissman  
Attorneys for *Amicus Curiae*  
NATIONAL ASSOCIATION OF INSURANCE  
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OF COUNSEL:

Douglas A. Hartz



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**DECLARATION OF DOUGLAS A. HARTZ IN  
SUPPORT OF BRIEF OF *AMICUS CURIAE*  
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FARM'S MOTION TO DISMISS**

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to File *Amicus Curiae* Brief filed concurrently]

Los Angeles/82337.1

DECLARATION OF DOUGLAS A. HARTZ IN SUPPORT OF *AMICUS CURIAE* BRIEF

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I, DOUGLAS A. HARTZ, declare and state as follows:

1. I am the Senior Counsel of *amicus curiae* National Association of Insurance Commissioners ("NAIC"). In that capacity, I am familiar with the NAIC's operations and corporate filings with respect to financial reporting and corporate management. Similarly, I have first-hand knowledge with respect to the publications of NAIC, including The NAIC Research Quarterly and NAIC's Insurance Department Resources Report. I have personal knowledge of the facts set forth herein and, if called upon, could and would testify competently to those facts under oath.

2. Attached hereto as Exhibit A is a true and correct copy of the Bylaws of the NAIC.

3. Attached hereto as Exhibit B is a true and correct copy of the Certificate of Incorporation of the NAIC.

4. Attached hereto as Exhibit C is a true and correct copy of the NAIC Financial Regulation Standards and Accreditation Program.

5. Attached hereto as Exhibit D is a true and correct copy of an excerpt from the NAIC Research Quarterly, October 1996, Volume II, Issue 4.

6. Attached hereto as Exhibit E is a true and correct copy of the NAIC's 2001 Annual Report.

7. Attached hereto as Exhibit F is a true and correct copy of an excerpt from the NAIC's 2000 Insurance Department Resources Report.

I declare under penalty of perjury of the laws of the State of California that the foregoing is true and correct and that this declaration was executed on May 24, 2002 at Kansas City, Missouri.

  
\_\_\_\_\_  
Douglas A. Hartz



**BYLAWS OF THE**

**NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS**

**ARTICLE I**

**Name, Organization and Location**

The name of this corporation is **NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS** (NAIC). The NAIC is organized under the General Corporation Law of the State of Delaware. The NAIC may have one (1) or more office locations within or without the State of Delaware as the Executive Committee may from time to time determine.

**ARTICLE II**

**Membership**

Each member of the NAIC shall have the power to vote and otherwise participate in the affairs of the NAIC. This power may be exercised through a duly authorized representative who shall be a person officially connected with the member's department and is wholly or principally employed by said department. A proxy to vote or participate in the affairs of the Plenary Session during the regular meetings of the NAIC must be in writing.

A quorum for the transaction of business shall consist of a majority of the members.

Members failing to pay all NAIC assessments on a timely basis shall be placed in an inactive status. Members in an inactive status shall be denied membership on NAIC committees and task forces, access to mailings and services of the NAIC Executive Headquarters and satellite offices, as well as access to zone examination processes and other benefits of membership in the NAIC.

Receipt of full payment from the inactive member of all current and past due assessments shall serve to immediately remove them from the inactive status.

The Executive Committee is empowered to reinstate, in part or in whole, an inactive member's participation on the committees and task forces, access to mailings and services of the NAIC Executive Headquarters and satellite offices, as well as access to zone examination processes, and other benefits of membership in the NAIC upon good cause shown as determined by the Executive Committee.

### **ARTICLE III**

#### **Officers**

The officers of the NAIC shall be a President, a Vice President, and a Secretary-Treasurer. The officers shall be elected by the membership by secret ballot at the last National Meeting of the calendar year and shall take office at the close of such meeting. They shall hold office until the election and qualification of their successors. If an interim vacancy occurs in an officer position, an interim election shall be held to fill the vacancy. No member may hold any office for more than two consecutive years.

The President shall be the chief elective officer of the NAIC, shall serve as Chairman of the Executive Committee and shall preside at all general and Plenary Sessions of the NAIC.

The Vice President shall act in the absence of the President as required and shall serve as Vice-Chairman of the Executive Committee, presiding at all meetings of the Executive Committee and at the general Plenary Session in the absence of the President.

The Secretary-Treasurer shall assist the President in the conduct of meetings. The Secretary-Treasurer shall call the roll of the membership and certify the presence of a quorum. The Secretary-Treasurer shall receive, validate and maintain all proxies for Plenary Session elections. The Secretary-Treasurer shall also recommend to the Executive Committee such policies and procedures to maintain the history and continuity of the NAIC. The Secretary-Treasurer shall also assist the President and Vice President in all matters relating

to the budget, accounting, expenditure and revenue practices of the NAIC.

#### **ARTICLE IV**

##### **Executive Committee**

The governing body of the NAIC shall be the Executive Committee. The Executive Committee must be made up entirely of members of the NAIC. The Executive Committee shall consist of the following members: the officers of the NAIC; the most immediate past president; the twelve (12) members of the zones as provided for in the Bylaws; and all other past presidents who have continuously remained members of the NAIC since completing their terms in the office of president. Other than the most immediate past president, persons who become, after December 31, 1997, past presidents of the NAIC who have continuously remained members of the NAIC since completing their terms in office as NAIC president shall not be members of the Executive Committee in their capacities as past presidents of the NAIC.

1. The Executive Committee shall have the authority and responsibility to:

- (a) manage the affairs of the NAIC in a manner consistent with the Certificate of Incorporation and Bylaws;
- (b) make recommendations to achieve the goals of the NAIC based upon either its own initiative or the recommendations of the Standing Committees or Subcommittees reporting to it, for consideration and action by the members at any NAIC Plenary Session;
- (c) create and terminate one or more Task Forces reporting to it to the extent needed and appropriate;
- (d) establish and allocate, from time to time, functions and responsibilities to be performed by each Zone;
- (e) to the extent needed and appropriate, oversee an Executive Headquarters and satellite offices to assist the NAIC and the individual members in achieving the goals of the NAIC;

(f) submit to the NAIC at each National Meeting, during which a Plenary Session is held, its report and recommendations concerning the reports of the Standing Committees. All Standing Committee reports shall be included as part of the Executive Committee report;

(g) plan, implement and coordinate communications and activities with other state, federal and local government organizations in order to advance the goals of the NAIC and promote understanding of state insurance regulation.

## 2. Duties and Operations of the Executive Committee.

(a) The Executive Committee shall hold at least two (2) meetings annually at a designated time and place. Special meetings may be held when called by the President, or by three (3) members of the Executive Committee in writing. At least five (5) days notice shall be given of all special meetings. Meetings may be held in person, by telephone, or by any other legal means. In addition, the Executive Committee may act by written consent as provided by law.

(b) The Executive Committee may, with the concurrence of two-thirds of the members of the Executive Committee, establish rules for its conduct that shall not conflict with the Certificate of Incorporation and Bylaws. Such rules may be changed only by a concurrence of two-thirds of the members of the Executive Committee after twenty-four (24) hours notice to all members of the Executive Committee.

(c) The Executive Committee shall cause to be kept full and complete minutes of its meeting and have information of any action of a general character taken by it published to members qualified to vote.

### (d) Executive Headquarters

(i) The Executive Committee shall oversee an Executive Headquarters with management and staff personnel and appropriate resources for performance of duties and assigned responsibilities. Additional satellite offices may be established as needed. The Executive Committee shall have the authority to select, employ and terminate an Executive Vice President of the Executive Headquarters who shall not be a member of the NAIC and who shall have the primary responsibility for the internal management and functioning of the Executive Headquarters and all satellite offices within the direction of the Executive Committee. The Executive Committee, through the Internal Administration (EX1) Subcommittee, shall provide oversight and direction to the Executive Vice President regarding Executive Headquarters operations.

(ii) Consistent with the purposes of the NAIC, the role of the Executive Headquarters (and any satellite offices) is to: (1) provide services to the NAIC through support to the NAIC Committees, Subcommittees, Task Forces or otherwise; (2) provide services to individual State insurance departments, and (3) develop recommendations for consideration as to NAIC policy and administrative decisions of the NAIC.

(iii) In performing its role, subject to the oversight and direction specified in (paragraph i) the Executive Headquarters and its satellite offices may engage in a variety of functions including but not limited to the following: research; analysis; information gathering and dissemination; library services; data collection; data base building and maintenance; report generation and dissemination; government liaison; non-regulatory liaison; securities valuation; administration; litigation; legislative and regulatory drafting; and educational development.

(iv) The Executive Vice President shall prepare an annual budget, related to the priorities of the NAIC, for the Executive Headquarters and all satellite offices to be submitted through the EX1 Subcommittee to the Executive Committee, which shall make its recommendations to the members of the NAIC for action at the next Plenary Session of the NAIC.

### 3. Internal Administration (EX1) Subcommittee

The Internal Administration (EX1) Subcommittee shall be a Subcommittee reporting to the Executive Committee. Appointments of the Chair and Vice Chair of the Executive Subcommittee and members other than those specifically designated herein shall be made by the President and the Vice President:

This Subcommittee shall be comprised of the President, Vice President, the Secretary-Treasurer, the most immediate past President, and three (3) other members of the Executive Committee.

The Internal Administration (EX1) Subcommittee shall:

(a) Exercise such powers and authority as may be delegated to it by the Executive Committee.

(b) Generally oversee the Executive Headquarters and its satellite offices including, without limitation: (i) periodically monitor operations of the Executive Headquarters, (ii) review and revise the budget of the Executive Headquarters, hold an annual hearing to receive public comments on the budget of the Executive Headquarters and submit the revised budget to the Executive Committee, (iii) approve emergency expenditures which vary from the adopted budget and promptly certify its action in writing to the Executive Committee, (iv) evaluate the Executive Vice President and make appropriate recommendations to the Executive Committee, (v) assist the Executive Vice President in resolving competing demands for Executive Headquarters resources, (vi) review compensation of all senior management and (vii) quarterly prepare a report containing the current budget and expenditures which the Secretary-Treasurer shall present to the Executive Committee; and

(c) Establish Meetings Coordination, a standing task force charged with the coordination and scheduling of all meetings of the NAIC, including the time, place and facilities for such meetings; to coordinate with the respective Zone Chairs the assignment of items for National Meetings; coordination of such other functions of the NAIC as may be delegated by the Executive Committee.

## ARTICLE V

### Zones

To accomplish the purposes of the NAIC in a timely and efficient manner, the United States, its territories and insular possessions shall be divided into four Zones. Each Zone shall consist of a group of at least eight States, located in the same geographical area, with each State being contiguous to at least one other State in the group so far as practicable, plus any territory or insular possession that may be deemed expedient, all as determined by majority of the Executive Committee. Members of each Zone shall annually elect a Chairman, a Vice Chairman and a Secretary from among themselves prior to or during the Winter Meeting of the NAIC. The Chairman, Vice Chairman and Secretary of each Zone shall be members of the Executive Committee with terms of office corresponding to that of the officers. Each Zone shall perform such functions as are designated by the Executive Committee of the NAIC or by the members of the NAIC as a whole or by the members of the Zone. Each Zone may hold Zone Meetings for such purposes as may be deemed appropriate by members of the Zone.

## ARTICLE VI

## Standing Committees and Task Forces

### 1. General

The Standing Committees shall not be subcommittees of the Executive Committee and shall have no power or authority for the management of the business and affairs of the NAIC. Each Standing Committee shall be composed of not more than 13 members appointed by the President and Vice President. Standing Committees shall meet at least twice a year at National Meetings and may meet more often at the call of the Chair as required to complete its assignments from the Executive Committee in a timely manner.

The Executive Committee shall make all assignments of subject matter to the Standing Committees and shall require coordination between Committees and Task Forces of the subject matter if more than one Committee or Task Force is affected. The format of the Committee reports shall be prescribed by the Executive Committee. All appointments or elections of members of the NAIC to any office or Committee of the NAIC shall be deemed the appointment or election of a particular member and shall not automatically pass to a successor in office.

### 2. Specific Duties

The Standing Committees of the NAIC, their duties, powers and responsibilities shall be as follows:

- (a) Life Insurance and Annuities (A) Committee: This Standing Committee shall consider issues relating to life insurance and annuities.
  
- (b) Health Insurance and Managed Care (B) Committee: This Standing Committee shall consider issues relating to health and accident insurance and managed care.
  
- (c) Property and Casualty Insurance (C) Committee: This Standing Committee shall consider issues relating to personal and commercial lines of property and casualty insurance, worker's compensation insurance, statistical information, surplus lines, and casualty actuarial matters.

(d) Market Conduct and Consumer Affairs (D) Committee: This Standing Committee shall consider issues involving market conduct in the insurance industry; competition in insurance markets; the qualifications and conduct of agents and brokers; market conduct examination practices; the control and management of insurance institutions; consumer services of State insurance departments; and consumer participation in NAIC activities. The Market Conduct Examination Oversight Task Force is a standing task force reporting to the (D) Committee.

(e) Financial Condition (E) Committee: This Standing Committee shall consider both administrative and substantive issues as they relate to accounting practices and procedures; blanks; valuation of securities; the Insurance Regulatory Information System (IRIS), as it relates to solvency and profitability; the call, monitoring and concluding report of Zone Examinations; and financial examinations and examiner training. The following standing task forces report to the (E) Committee: Accounting Practices and Procedures Task Force; Blanks Task Force; Insolvency Task Force; and the Examination Oversight Task Force.

(f) Financial Regulation Standards & Accreditation (F) Committee: This Standing Committee shall consider both administrative and substantive issues as they relate to administration and enforcement of the NAIC Accreditation Program, including without limitation, consideration of standards and revisions of standards for accreditation, interpretation of standards, evaluation and interpretation of states' laws and regulations, and departments' practices, procedures and organizations as they relate to compliance with standards, examination of members for compliance with standards, development and oversight of procedures for examination of members for compliance with standards, qualification and selection of individuals to perform the examination of members for compliance with standards, and decisions regarding whether to accredit members.

(g) Special Insurance Issues (G) Committee: This Standing Committee shall have the responsibility for issues relating to the miscellaneous lines of insurance including, but not limited to, Title, Captive Insurers, Surety, Fidelity and Mortgage Guaranty; and issues relating to information systems, antifraud, and other significant regulatory issues which may occur from time to time which are not readily categorized under the A, B, C, D, E, F or H Committees. The Reinsurance Task Force reports to the (G) Committee as a standing task force.

(h) International Insurance Relations (H) Committee. This Standing Committee shall have the responsibility for issues relating to international insurance.

### 3. Task Forces



The Executive Committee, its Subcommittee and the Standing Committees may establish one or more Task Forces, subject to approval of the Executive Committee. Except as provided herein, a Task Force shall automatically terminate at the end of the NAIC Winter Meeting, unless the Executive Committee at that Meeting adopts the recommendation of the parent Committee or Subcommittee to continue the Task Force until the next NAIC Winter Meeting. The President and Vice President shall appoint members of Task Forces by January 30.

Vacancies in the positions of Chair or Vice Chair shall be filled by the parent Committee or Subcommittee from within or outside the present Task Force membership; provided, however, that the chief insurance regulatory official of the state of the former Chair or Vice Chair shall become a member of the Task Force. A vacancy in the position of member shall be filled by the chief insurance regulatory official of the vacating member's state.

If an existing Task Force is dealing with insurance problems that require continuing study, the Executive Committee may adopt the recommendation of the parent Committee or Subcommittee that the Task Force be designated a Standing Task Force. Such designation shall relieve the parent Committee or Subcommittee of its annual duty to recommend that the Task Force be continued. A Standing Task Force shall continue in effect until terminated by the Executive Committee.

## **ARTICLE VII**

### **Meetings of the Membership**

The NAIC shall hold at least two (2) National Meetings each calendar year at such time and place as the Executive Committee may designate. Special plenary sessions may be called by any five (5) members of the Executive Committee by giving all members notice of such meeting at least ten (10) days prior thereto, or by any twenty (20) members of the NAIC upon thirty (30) days notice to all members. Actions at any special plenary sessions shall be limited to the subject stated in the notice therefor. At any meeting of the NAIC, one or more of the sessions may be Executive Sessions as defined in NAIC policies on open meetings. Any member may attend and participate in any meeting of the NAIC or any meeting of a Standing Committee or Task Force whether or not such member has the right to vote. All National Meetings shall provide for a Plenary Session of the NAIC as a whole in order to consider and take action upon the matters submitted to the NAIC.

## **ARTICLE VIII**

### **Elections**

1. The election of officers of the NAIC shall be scheduled for the plenary session of the last National Meeting of the calendar year.
  
2. At the beginning of such Plenary Session, the Secretary-Treasurer shall ascertain and announce the presence of a quorum.
  
3. Upon the determination of a quorum, the chair shall briefly review the provisions of the Certificate of Incorporation and Bylaws in regard to voting.
  
4. The President shall ask for and announce all proxies. Proxies shall be held by the Secretary-Treasurer throughout the election session. Proxies shall be valid, subject to their term, until superseded by the member and shall be governed by ARTICLE IX of the Bylaws.
  
5. Every individual voting by proxy must meet the requirements of Article II of the Bylaws of the NAIC which requires that such a person be "...officially connected with the member's (the member delegating authority to vote) department, and is wholly or principally employed by said department."
  
6. Prior to opening the nominations for office, the Chair shall appoint three (3) members of the NAIC to act as tellers. The tellers shall distribute, collect and count ballots. If a teller is nominated for an office and does not withdraw as a candidate, he shall not be a teller for the election of the office to which he is nominated and the chair shall appoint another teller in his place.
  
7. The Chair shall announce the opening of nominations for offices in the following order:

(a) President

(b) Vice President

(c) Secretary-Treasurer

8. Only members or duly authorized proxyholders may make nominations.

9. One nominating speech, not to exceed three (3) minutes in duration, shall be allowed for each nominee.

10. After nominations are closed for each office, each nominee shall be permitted to address the membership for a period of up to five (5) minutes. Such addresses shall be given in the order by which the nominations were made.

11. The Secretary-Treasurer shall provide the ballots.

12. The votes of members or proxyholders constituting a majority of the quorum present at the meeting shall be necessary for election to such office. If no candidate receives a majority, the vote for each nominee shall be announced, ballots distributed and another vote taken. This process shall be continued until one nominee receives a majority. Each nominee shall remain on the ballot unless he withdraws.

## ARTICLE IX

### Proxies

Where the delegation of power to vote or participate in the membership of the NAIC is required by

ARTICLE II of these Bylaws to be in writing, such delegation must be effected by proxy. All proxies must be dated and give specific authority to a named individual who meets the requirements of ARTICLE II for duly authorized representatives. Documents such as electronic transmission, telegrams, mailgrams, etc. are acceptable as proxies if they otherwise meet the requirements contained herein. A member of the Executive Committee may not vote in a meeting of the Executive Committee or its subcommittees by proxy.

## **ARTICLE X**

### **Procedures**

The NAIC shall be governed by Robert's Rules of Order. Where Robert's Rules of Order conflict with the NAIC's Certificate of Incorporation or Bylaws, the Certificate of Incorporation and Bylaws shall govern.

## **ARTICLE XI**

### **Amendments**

These Bylaws may be altered or amended at any meeting of the NAIC by an affirmative vote of a majority of the members or authorized representatives, provided that previous notice of the proposed amendment has been mailed to all members by direction of the Executive Committee at least thirty (30) days prior to the meeting.

Adopted 1999 Proc., Third Quarter

**CERTIFICATE OF INCORPORATION**  
**OF**  
**NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS**  
**a Nonstock Corporation**

**Name**

The name of the Corporation is: **National Association of Insurance Commissioners (NAIC)**.

**Duration**

The period of duration of the NAIC is perpetual.

**Registered Office and Agent**

The NAIC's Registered Office in the State of Delaware is to be located at: 1209 Orange St., in the City of Wilmington, Zip Code 19801. The registered agent in charge thereof is The Corporation Trust Company.

**Authority to Issue Stock**

The NAIC shall have no authority to issue capital stock.

### **Incorporators**

The name and address of the incorporator are as follows:

Catherine J. Weatherford

National Association of Insurance Commissioners

120 W. 12<sup>th</sup> St., Suite 1100

Kansas City, MO 64106

### **Purpose**

The NAIC is organized exclusively for charitable and educational purposes within the meaning of Section 501(c)(3) of the Internal Revenue Code of 1986, as amended (or the corresponding provision of any future United States Internal Revenue law), including without limitation, to assist state insurance regulators, individually and collectively, in serving the public interest and achieving the following fundamental insurance regulatory goals in a responsive, efficient and cost-effective manner, consistent with the wishes of its members:

- (a) Protect the public interest, promote competitive markets and facilitate the fair and equitable treatment of insurance consumers;
  
- (b) Promote, in the public interest, the reliability, solvency and financial solidity of insurance institutions;  
and
  
- (c) Support and improve state regulation of insurance.

## **VII. Restrictions**

A. No substantial part of the activities of the Corporation shall be the carrying of propaganda, or otherwise attempting to influence legislation except as otherwise permitted by Section 501(h) of the Code and in any corresponding laws of the State of Delaware, and the Corporation shall not participate in or intervene in including the publishing or distribution of statements concerning any political campaign on behalf of or in opposition to any candidate for public office.

B. For any period for which the Corporation may be considered a private foundation, as defined in Section 509(a), the Corporation shall be subject to the following restrictions and prohibitions:

1. The Corporation shall not engage in any act of self-dealing as defined in section 4941(d) of the Code.
2. The Corporations shall make distributions for each taxable year at such time and in such manner so as not to become subject to the tax on undistributed income imposed by section 4942 of the Code.
3. The Corporation shall not retain any excess business holdings as defined in section 4943(c) of the Code.
4. The Corporation shall not make any investments in such manner as to subject it to tax under section 4944 of the Code.
5. The Corporation shall not make any taxable expenditures as defined in section 4945(d) of the Code.

## **VIII. Membership**

The NAIC shall have one class of members consisting of the Commissioners, Directors, Superintendents, or

other officials who by law are charged with the principal responsibility of supervising the business of insurance within each State, territory, or insular possession of the United States. Members only shall be eligible to hold office in and serve on the Executive Committee, Committees and Subcommittees of the NAIC. However, a member may be represented on a Committee or Subcommittee by the member's duly authorized representative as defined in the Bylaws. Only one official from each State, territory or insular possession shall be a member and each member shall be limited to one vote. Any insurance supervisory official of a foreign government or any subdivision thereof, which has been diplomatically recognized by the United States government, may attend and participate in all meetings of this Congress but shall not be a member and shall not have the power to vote.

## **IX. Activities**

The NAIC is a nonprofit charitable and educational organization and no part of the net earnings or property for the corporation will inure to the benefit of, or be distributable to its members, directors, officers or other private individuals, except that the NAIC shall be authorized and empowered to pay reasonable compensation for services rendered by employees and contractors, and to make payments and distributions in furtherance of the purposes set forth in Article VI hereof.

## **X. Powers**

The NAIC shall have all of the powers conferred by the Delaware General Corporation Law for non-profit corporations, except that, any other provision of the Certificate to the contrary notwithstanding, the NAIC shall neither have nor exercise any power, nor carry on any other activities not permitted: (a) by a corporation exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code of 1986, as amended (or the corresponding provision of any future United States Internal Revenue law); or (b) by a corporation contributions to which are deductible under Section 170(c)(2) of the Internal Revenue Code of 1986, as amended, (or the corresponding provision of any future United States Internal Revenue law).

## **XI. Immunity**

All officers and members of the Executive Committee shall be immune from personal liability for any civil damages arising from acts performed in their official capacity, and shall not be compensated for their services as an officer or member of the Executive Committee on a salary or a prorated equivalent basis. The



immunity shall extend to such actions for which the member of the Executive Committee or officer would not otherwise be liable, but for the Executive Committee member's or officer's affiliation with the NAIC. This immunity shall not apply to intentional conduct, wanton or willful conduct or gross negligence. Nothing herein shall be construed to create or abolish an immunity in favor of the NAIC itself. Nothing herein shall be construed to abolish any immunities held by the state officials pursuant to their individual state's law.

## **XII. Exculpation and Indemnification**

A member of the Executive Committee shall not be liable to the NAIC or its members for monetary damages for breach of fiduciary duty as a member of the Executive Committee, provided that this provision shall not eliminate or limit the liability of a member of the Executive Committee for any breach of the duty of loyalty to the NAIC or its members, for acts or omissions not in good faith, or which involve intentional misconduct or a knowing violation of law, or for any transaction from which the member of the Executive Committee involved derived an improper personal benefit. Any amendment, modification or repeal of the foregoing sentence shall not adversely affect any right or protection of a member of the Executive Committee of the Corporation hereunder in respect of any act or omission occurring prior to the time of such amendment, modification, or repeal. If the Delaware General Corporation Law hereafter is amended to authorize the further elimination or limitation of the liability of the members of the Executive Committee, then the liability of a member of the Executive Committee, in addition to the limitation provided herein, shall be limited to the fullest extent permitted by the amended Delaware General Corporation Law.

The NAIC shall indemnify to the full extent authorized or permitted by the laws of the State of Delaware, as now in effect or as hereafter amended, any person made or threatened to be made a party to any threatened, pending or completed action, suit or proceeding (whether civil, criminal, administrative or investigative, including an action by or in the right of the NAIC) by reason of the fact that the person is or was a member of the Executive Committee, officer, member, committee member, employee or agent of the NAIC or serves any other enterprise as such at the request of the NAIC.

The foregoing right of indemnification shall not be deemed exclusive of any other rights to which such person may be entitled apart from this Article XII. The foregoing right of indemnification shall continue as to a person who has ceased to be a member of the Executive Committee, officer, member, committee member, employee or agent and shall inure to the benefit of the heirs, the executors and administrators of such a person.

## **XIII. Dissolution**

In the event of the dissolution of the NAIC, the Executive Committee shall, after paying or making provision for the payment of all of the liabilities of the NAIC, dispose of all the assets of the NAIC equitably to any state government which is represented as a member of the NAIC at the time of dissolution, provided that the assets are distributed upon the condition that they be used primarily and effectively to implement the public purpose of the NAIC, or to one or more such organizations organized and operated exclusively for religious, charitable, education, scientific, or literary purposes or similar purposes as shall at the time qualify: (a) as an exempt organization under Section 501(c)(3) of the Internal Revenue Code of 1986, as amended (or the corresponding provision of any future United States Internal Revenue law); and (b) as an organization contributions to which are deductible under Section 170(c) of the Internal Revenue Code of 1986, as amended (or the corresponding provision of any future United States Internal Revenue law), as the Executive Committee shall determine.

### **Bylaws**

The Bylaws of the NAIC may prescribe the powers and duties of the several officers, members of the Executive Committee and members and such rules as may be necessary for the work of the NAIC provided they are in conformity with the Certificate of Incorporation.

### **XV. Amendments**

This Certificate of Incorporation may be altered or amended at any meeting of the full membership (Plenary Session) of the NAIC by an affirmative vote of two-thirds of the members qualified to vote, or their authorized representatives, provided that previous notice of the proposed amendment has been mailed to all members by direction of the Executive Committee at least thirty (30) days prior to the meeting.

**IN WITNESS WHEREOF**, this Certificate of Incorporation has been signed this 4th day of October 1999.

/signature/

Catherine J. Weatherford, Incorporator

ADOPTED 1999, Proc. Third Quarter

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# **Financial Regulation Standards and Accreditation Program**

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**March 2002**

***NAIC***  
**National Association  
of Insurance Commissioners**

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## THE NAIC FINANCIAL REGULATION STANDARDS AND ACCREDITATION PROGRAM

*(Note: The official standards, policies and procedures of the NAIC Financial Regulation Standards and Accreditation Program are contained in the Proceedings of the NAIC and should be consulted for complete, accurate and up to date information on the Program.)*

*This pamphlet contains only general information about the NAIC Financial Regulation Standards and Accreditation Program and is not a comprehensive statement of the official standards, policies and procedures of the Program. Although this pamphlet is periodically updated to reflect changes in the Program, the reader is advised that it may not reflect the current Program requirements.)*

### Introduction

A system of effective solvency regulation provides crucial safeguards for America's insurance consumers. Insurance consumers benefit when the insurance industry is strong enough financially to be able to pay and settle claims in a timely manner, to provide diverse and competitively priced products and to provide meaningful customer service.

An effective system of solvency regulation has certain basic components. It requires that regulators have adequate statutory and administrative authority to regulate an insurer's corporate and financial affairs. It requires that regulators have the necessary resources to carry out that authority. Finally, it requires that insurance departments have in place organizational and personnel practices designed for effective regulation.

To guide state legislatures and state insurance departments in the development of effective solvency regulation, the NAIC began, in 1988, the process which led to the adoption of the Financial Regulation Standards (Standards) in June 1989. These Standards, discussed in greater detail below, establish baseline requirements for an effective regulatory system in each state.

To provide guidance to the states regarding the baseline Standards and an incentive to put them in place, the NAIC adopted in June 1990 a formal certification program. Under this plan, each state's insurance department will be reviewed by an independent review team whose job is to assess that department's compliance with the Standards. Departments meeting the Standards will be publicly acknowledged, while departments not in compliance will be given guidance by the NAIC to bring the department into compliance.

The objective of the accreditation program is to provide a process whereby solvency regulation of multi-state insurance companies can be enhanced and adequately monitored with emphasis on the following:

- 1) Adequate solvency laws and regulations in each accredited state to protect insurance consumers.
- 2) Effective and efficient financial analysis and examination processes in each accredited state.
- 3) Appropriate organizational and personnel practices in each accredited state.

As of March 2002, forty-nine departments—Alabama, Alaska, Arizona, Arkansas, California, Colorado, Connecticut, Delaware, District of Columbia, Florida, Georgia, Hawaii, Idaho, Illinois, Indiana, Iowa, Kansas, Kentucky, Louisiana, Maine, Maryland, Massachusetts, Michigan, Minnesota, Mississippi, Missouri, Montana, Nebraska, Nevada, New Hampshire, New Jersey, New Mexico, North Carolina, North Dakota, Ohio, Oklahoma, Oregon, Pennsylvania, Rhode Island, South Carolina, South Dakota, Tennessee, Texas, Utah, Vermont, Virginia, Washington, Wisconsin and Wyoming—are accredited.

Moreover, since the program began, all 50 states and the District of Columbia have adopted laws and regulations designed to bring them closer to meeting the NAIC's accreditation standards.

The Financial Regulation Standards and Accreditation Committee of the NAIC (formerly known as the Financial Regulation Standards and Accreditation Subcommittee), consisting of regulators from across the country, decides whether a state meets the requirements set forth in the Standards. The meetings in which matters of state accreditation are discussed are held in executive session to protect the states, regulators, and in some instances, insurers from disclosure of confidential information.

## **How The Accreditation Program Works**

The Accreditation Program establishes requirements under which a state insurance department may seek accreditation. Additionally, the Program establishes guidelines for states already accredited to maintain their accredited status.





## Accreditation Review Process

### Procedures in Preparation for an Accreditation Review

1. A state requests an accreditation review by contacting the Executive Headquarters of the NAIC.
2. NAIC requests that the state submit a Self-Evaluation Guide. This Guide provides the state with the detailed requirements of the Standards including laws and regulations that must be adopted, financial analysis and examination procedures that must be in place and organizational and personnel practices that must be established.
3. NAIC notifies the chair of Financial Regulation Standards and Accreditation Committee (FRSAC) that the state has requested an accreditation review and provides the chair with a list of qualified Review Team candidates, comprised of experts in insurance regulation.
4. The Chair of FRSAC selects the Review Team and the Review Team Leader from the list of qualified candidates. The Review Team consists of three to six individuals depending upon the size of the state. The Review Team should include at least one disinterested former executive level regulator.
5. NAIC notifies the state of the selection of the Review Team. The state is given the opportunity to object to any of the Review Team members.
6. NAIC notifies the Review Team members. The Review Team members are paid by the NAIC at a set hourly rate for time spent on the accreditation review plus reasonable actual expenses incurred.
7. NAIC works with the state to schedule the site visit and notifies the Review Team of the dates. Generally, a site visit requires three to five days depending upon the size of the state.
8. NAIC sends copies of the state's completed Financial Regulation Standards Self-Evaluation Guide with any applicable supporting documentation to the Review Team.
9. NAIC notifies the state of the data, documentation, staff interviews, and other needs of the Review Team for its on-site review.

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### **On-Site Accreditation Review Procedures**

10. The Review Team conducts the on-site review following a general outline of procedures to be performed to allow for uniformity in the evaluation process among the states. In addition, an NAIC staff representative is an observer on each site visit to help ensure uniformity and consistency in the on-site reviews. Before the on-site review, there is an initial meeting of the team members to discuss comments and concerns from review of the Financial Regulation Standards Self-Evaluation Guide and supporting documentation.
11. The on-site review consists of the following:
  - a. Review of laws and regulations.
  - b. Review of examination reports and supporting work papers and analytical reviews.
  - c. Inspection of financial analysis and regulatory files for selected companies.
  - d. Interviews with department personnel.
  - e. Review of organizational and personnel practices.
  - f. Walk-through of the department to gain an understanding of document and communication flows.
  - g. Meetings of the team members to discuss comments and findings from the review.
  - h. Team members vote using a scoring system to determine whether a state is in compliance with the accreditation standards.
  - i. Closing conference with the state to discuss findings.
  - j. Draft copies of the compliance report and management letter comments are provided to the state, along with a copy of the scores.

12. As a result of the site visit, a review team report, compliance report and management letter comments are prepared by the Review Team and submitted to the FRSAC by the Team Leader. The reports summarize the scope of the procedures performed during the site visit, document the findings on an exception basis, highlight major recommendations as a result of the review, and conclude with the Review Team's recommendation as to whether the state should be accredited by the FRSAC.

#### **Committee Evaluation Process**

13. FRSAC meets, normally at the NAIC National Meetings, to discuss the Review Team's reports. FRSAC also has copies of the state's Financial Regulation Standards Self-Evaluation Guide and supporting documentation available. In addition, the Team Leader and the NAIC observer are present at the meeting as needed. Representatives of the state are in attendance to respond to questions from FRSAC or to comment upon the Review Team's reports and recommendation.
14. Representatives of the state are then excused. Based on the recommendation of the Review Team and as a result of this meeting, the FRSAC makes a decision as to whether or not the state should be accredited or, if the state is already accredited, whether or not the state should retain its accreditation.
15. FRSAC informs the state of its decision.
  - a) If the decision is favorable, the state receives recognition at the Opening Session of the NAIC National Meeting, and a press release acknowledging the accreditation will be issued.
  - b) If the decision is unfavorable, and the state is currently not accredited, the state has three options: withdraw its request for accreditation; ask FRSAC to hold its decision in abeyance pending legislative or other corrective action to bring the state into compliance with the standards; or appeal the decision of FRSAC. These options are available only if the state is not currently accredited.
  - c) If the decision is unfavorable, and the state is currently accredited, the state may either accept the decision or choose to appeal the decision of FRSAC. In case of an appeal, the state retains its accredited status during the appeals process.

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### Post Committee Evaluation Process

16. If the state chooses to appeal a decision of FRSAC in regards to its accreditation, a notice of appeal must be filed with the Office of the General Counsel of the NAIC within 30 days of the date that written notice of the decision of the FRSAC to deny, suspend or revoke the state accreditation is mailed or delivered to the state.
17. The Office of the General Counsel will notify the President of the NAIC of the appeal within three working days of receipt of the notice of appeal. Within five working days of receipt of notice, the President shall nominate three members of the NAIC as an appeal hearing panel. The NAIC members nominated shall not be members of FRSAC and no more than one nominee may be selected from each zone. The members of the appeal hearing panel shall commit to be impartial in all respects in hearing and deciding the state's appeal.
18. The state shall be entitled to a hearing no later than 60 days from the date its appeal request is filed with the Office of the General Counsel. At least 30 days prior to the hearing, the appeal hearing panel shall mail or deliver to the state written notice of the date, time and place of the hearing, the identity of the NAIC members comprising the appeal hearing panel, the state's right to appear in person, to be accompanied by legal counsel and to present information in support of its position and its right to request a change in the date or time of the hearing for good cause.
19. The members of the appeal hearing panel shall choose one of the members to preside at the hearing. At the hearing, the burden shall be on the state that is appealing the decision of the FRSAC to show that the decision of FRSAC should be reversed. The appeal hearing panel or the appealing state may request the attendance of the Review Team to respond to questions from the appeal hearing panel or the state's representatives.

20. The appeal hearing panel shall review the information presented in the hearing and determine, by a majority vote of its three members, whether the decision of FRSAC shall be affirmed, reversed or modified. The appeal hearing panel shall prepare a written summary of its findings. A written decision will be issued stating the facts on which its decision is based and shall be mailed or delivered to the appealing state and the Office of the General Counsel of the NAIC within 30 days after the completion of the hearing. The decision shall be final and binding on FRSAC and the appealing state, and there shall be no other appeal to any other committee of the NAIC.
21. Accreditation is for a five-year period, subject to annual reviews of the state's Financial Regulation Standards Self-Evaluation Guide. Once accredited, a state is subject to a full accreditation review every five years. If information comes to the attention of FRSAC that suggests that a state may no longer meet the Standards, a special review may be conducted. If FRSAC concludes that the state's accreditation should be suspended or revoked, the specific reasons are documented in a report to the state. The state would have a right to appeal the decision of FRSAC utilizing the procedures outlined in paragraphs 16-20 above.

### **Interim Annual Reviews**

1. Annually, on the anniversary of the state's accreditation, the state shall submit an updated Financial Regulation Standards Self-Evaluation Guide (Interim Annual Reviews) to the NAIC Executive Headquarters.
2. The state's report in the first year after accreditation shall also respond to all recommendations made in the Review Team's report and/or management letter prepared during the accreditation process.
3. NAIC staff will review the documentation submitted by the state and summarize for presentation to FRSAC.
4. After hearing the report from the NAIC staff, FRSAC will determine whether the state remains in compliance with the Standards. (FRSAC may request that a representative of the state be present to answer questions, if desired.)
5. If FRSAC finds the state to be out of compliance with the Standards, the specific reasons will be documented in a letter to the state and the state's accreditation will be suspended or revoked. The state would have the right to appeal the decision of FRSAC utilizing the procedures outlined in paragraphs 16-20 under "Accreditation Review Process."

## A Closer Look At The Standards

The Standards have been divided into three major categories: laws and regulations (Part A); regulatory practices and procedures (Part B); and organizational and personnel practices (Part C).

### Laws and Regulations

#### Preamble

The purpose of the Part A Law and Regulation Standards is to assure that an accredited state has sufficient authority to regulate the solvency of its multi-state domestic insurance industry in an effective manner. The Part A standards are the product of laws and regulations that are believed to be basic building blocks for sound insurance regulation. A state may demonstrate compliance with a Part A standard through a law, a regulation, an established practice which implements the general authority granted to the state, or any combination of laws, regulations or practice which achieves the objective of the standard.

The Part A standards apply to traditional forms of "multi-state domestic insurers." This scope includes the life and health and property/casualty/liability insurers and reinsurers which are domiciled in the accredited state and licensed, accredited or operating in at least one other state. This scope also includes insurers which are domiciled in the accredited state and operating in at least one other state as excess and surplus lines insurers or as risk retention groups; except that the term does not include risk retention groups incorporated as captive insurers. The terms "insurer" and "insurers" used in the Part A standards fall within the definition of "multi-state domestic insurers."

#### 1. Examination Authority

The Department should have the authority to examine companies whenever it is deemed necessary. Such authority should include complete access to the company's books and records and, if necessary, the records of any affiliated company, agent, and/or managing general agent.

Such authority should extend not only to inspect books and records but also to examine officers, employees, and agents of the company under oath when deemed necessary with respect to transactions directly or indirectly related to the company under examination. The NAIC Model Law on Examinations or substantially similar provisions shall be part of state law.

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2. Capital and Surplus Requirement

The Department should have the ability to require that insurers maintain a minimum level of capital and surplus to transact business. The Department should have the authority to require additional capital and surplus based upon the type, volume and nature of insurance business transacted. The Risk Based Capital (RBC) for Insurers Model Act or provisions substantially similar shall be included in state laws and regulations.

3. NAIC Accounting Practices and Procedures

The Department should require that all companies reporting to the Department file the appropriate NAIC annual statement blank, which should be prepared in accordance with the NAIC's instructions handbook and follow those accounting procedures and practices prescribed by the NAIC's *Accounting Practices and Procedures Manual*.

*(Note: Beginning January 1, 2004, the Codified version of the NAIC's Accounting Practices and Procedures Manual is required.)*

4. Corrective Action

State law should contain the NAIC's Model Regulation to Define Standards and Commissioner's Authority for Companies Deemed to be in a Hazardous Financial Condition or a substantially similar provision which authorizes the Department to order a company to take necessary corrective action or cease and desist certain practices which, if not corrected, could place the company in a hazardous financial condition.

5. Valuation of Investments

The Department should require that securities owned by insurance companies be valued in accordance with those standards promulgated by the NAIC's Securities Valuation Office. Other invested assets should be required to be valued in accordance with the procedures promulgated by the NAIC's Financial Condition (E) Committee.

6. Holding Company Systems

State law should contain the NAIC Model Insurance Holding Company System Regulatory Act or an Act substantially similar, and the Department should have adopted the NAIC's model regulation relating to this law.

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7. Risk Limitation

State law should prescribe the maximum net amount of risk to be retained by a property and liability company for an individual risk based upon the company's capital and surplus. This limitation should be no larger than 10% of the company's capital and surplus.

8. Investment Regulations

State statute should require a diversified investment portfolio for all domestic insurers both as to type and issue and include a requirement for liquidity. Foreign companies should be required to substantially comply with these provisions.

9. Liabilities and Reserves

State statute should prescribe minimum standards for the establishment of liabilities and reserves resulting from insurance contracts issued by an insurer; including life reserves, active life reserves, and unearned premium reserves and liabilities for claims and losses unpaid and incurred but not reported claims. The NAIC's Standard Valuation Law and Actuarial Opinion and Memorandum Regulation or substantially similar provisions shall be in place.

10. Reinsurance Ceded

State law should contain the NAIC Model Law on Credit for Reinsurance, the NAIC's Credit for Reinsurance Model Regulation and the 1992 NAIC Life and Health Reinsurance Agreements Model Regulation or substantially similar laws.

11. CPA Audits

State statute or regulation should contain a requirement for annual audits of domestic insurance companies by independent certified public accountants, based on the December 1990 version of the NAIC's Model Rule Requiring Annual Audited Financial Reports.

*(Note: Beginning January 1, 2004 the 1998 version of the NAIC's Model Rule Requiring Annual Audited Financial Reports is required.)*



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12. Actuarial Opinion

State statute or regulation should contain a requirement for an opinion on reserves and loss and loss adjustment expense reserves by a qualified actuary or specialist on an annual basis for all domestic insurance companies.

13. Receivership

State law should set forth a receivership scheme for the administration, by the insurance commissioner, of insurance companies found to be insolvent as set forth in the NAIC's Insurers Rehabilitation and Liquidation Model Act.

14. Guaranty Funds

State law should provide for a regulatory framework such as that contained in the NAIC's model acts on the subject, to ensure the payment of policyholders obligations subject to appropriate restrictions and limitations when a company is deemed insolvent.

15. Filings with NAIC

State statute, regulation or practice should mandate filing of annual and quarterly statements with the NAIC in a format acceptable to the NAIC except states may exempt from this requirement those companies that operate only in their state of domicile.

16. Producer Controlled Property/Casualty Insurers

States should provide evidence of a regulatory framework, such as that contained in the NAIC's Model Law for Business Transacted with Producer Controlled Property/Casualty Insurer Act or similar provisions.

17. Managing General Agents

States should provide evidence of a regulatory framework, such as that contained in the NAIC Managing General Agents Model Act or similar provisions.

## 18. Reinsurance Intermediaries

States should provide evidence of a regulatory framework, such as that contained in the NAIC Reinsurance Intermediaries Model Act or similar provisions.

**Note:** If a state can provide evidence that none of the entities contemplated in above standards 14, 16, 17 or 18, is either present or allowed to operate in the state, it will not need to demonstrate compliance with that standard.

## Regulatory Practices and Procedures

### Preamble

The purpose of Part B is to identify base-line regulatory practices and procedures required to supplement, and support enforcement of, the states' financial solvency laws for the states to attain substantial compliance with the core standards established in Part A. Part B identifies standards that are to be applied in the regulation of all forms of multi-state insurers.

Part B sets out standards required to ensure adequate solvency regulation of multi-state insurers. Each state must make an appropriate allocation of its available resources to effectively address its regulatory priorities. In addition to a domestic state's examination and analysis activities, other checks and balances exist in the regulatory environment. These include other states' regulation of licensed foreign companies, the appropriate application of FAST and IRIS ratios, the analyses by NAIC's staff, the NAIC Financial Analysis Working Group, the NAIC Analyst Team System, and to some extent the evaluation by private rating agencies.

The scope of Part B is broader than the scope of Part A. "Multi-state insurer" as used in Part B encompasses all forms of insurers domiciled in the accredited state and operating in at least one other state. The term "insurer" in Part B includes traditional insurance companies as well as, for instance, health maintenance organizations and health service plans, captive risk retention groups, and other entities organized under other statutory schemes. While the unique organizational characteristics of some of these entities may require specialized laws, their multi-state activity demands solvency oversight that employs the base-line regulatory practices and procedures identified in Part B.

The accreditation program recognizes that complete standardization of practices and procedures across all states may not be practical or desirable because of the unique situations each state faces. States differ with respect to staff and technology resources that are available as well as the characteristics of the domestic industry regulated. For example, states may choose to emphasize automated analysis over manual or vice versa. Reliable results may be obtained using alternative, yet effective, financial solvency oversight methodologies. The accreditation program should not emphasize form over substance in its evaluation of the states' solvency regulation.

[NOTE: FRSAC has adopted Review Team Guidelines that provide detailed guidance to the review teams regarding how compliance with the Part B, Regulatory Practices and Procedures Standards should be assessed. These guidelines can also assist states in preparing for the accreditation review of their Department.]

1. Financial Analysis

(a) Sufficient Qualified Staff and Resources

The Department should have the resources to review effectively on a periodic basis the financial condition of all domestic insurers.

(b) Communication of Relevant Information To/From Financial Analysis Staff

The Department should provide relevant information and data received by the Department which may assist in the financial analysis process to the financial analysis staff and ensure that findings of the financial analysis staff are communicated to the appropriate person(s).

(c) Appropriate Supervisory Review

The Department's internal financial analysis process should provide for appropriate supervisory review and comment.

(d) Priority-Based Review

The Department's financial analysis procedures should be priority-based to ensure that potential problem companies are reviewed promptly. Such a prioritization scheme should utilize appropriate factors as guidelines to assist in the consistent determination of priority designations.

(e) Appropriate Depth of Review

The Department's financial analysis procedures should ensure that domestic insurers receive an appropriate level or depth of review commensurate with their financial strength and position.

(f) Documented Analysis Procedures

The Department should have documented financial analysis procedures and/or guidelines to provide for consistency and continuity in the process and to ensure that appropriate analysis procedures are being performed on each domestic insurer.

(g) Reporting of Material Adverse Findings

The Department's procedures should require that all material adverse indications be promptly presented to the commissioner or an appropriate designee for determination and implementation of appropriate regulatory action.

(h) Action on Material Adverse Findings

Upon the reporting of any material adverse findings from the financial analysis staff, the Department should take timely action in response to such findings or adequately demonstrate the determination that no action was required.

2. Financial Examinations

(a) Sufficient Qualified Staff and Resources

The Department should have the resources to effectively examine all domestic insurers on a periodic basis in a manner commensurate with the financial strength and position of each insurer.

(b) Communication of Relevant Information To/From Examination Staff

The Department should provide relevant information and data received by the Department which may assist in the examination process to the examination staff and ensure that findings of the examination staff are communicated to the appropriate person(s).

(c) Use of Specialists

The Department's examination staff should include specialists with appropriate training and/or experience or otherwise have available qualified specialists which will permit the Department to effectively examine any insurer. These specialists should be utilized where appropriate given the complexity of the examination or identified financial concerns.

(d) Appropriate Supervisory Review

The Department's procedures for examinations should provide for supervisory review of examination workpapers and reports to ensure that the examination procedures and findings are appropriate and complete and that the examination was conducted in an efficient and timely manner.

(e) Use of Appropriate Guidelines and Procedures

The Department's policies and procedures for the conduct of examinations should generally follow those set forth in the NAIC's Examiners Handbook. Appropriate variations in methods and scope should be commensurate with the financial strength and position of the insurer.

(f) Scheduling of Examinations

In scheduling financial examinations, the Department should follow procedures such as those set forth in the NAIC's Examiners Handbook that provide for the periodic examination of all domestic companies on a timely basis. This system should accord priority to companies which exhibit adverse financial trends or otherwise demonstrate a need for examination.

(g) Examination Reports

The Department's reports of examination should be prepared in accordance with the format adopted by the NAIC and should be sent to other states in which the insurer transacts business in a timely fashion.

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(h) Reporting of Material Adverse Findings

The Department's procedures should require that all material adverse findings be promptly presented to the commissioner or an appropriate designee for determination and implementation of appropriate regulatory action.

(i) Action on Material Adverse Findings

Upon the reporting of any material adverse findings from the examination staff, the Department should take timely action in response to such findings or adequately demonstrate the determination that no action was required.

3. Communication With States and Procedures for Troubled Companies

(a) Communication With States

States should allow for the sharing of otherwise confidential information, administrative or judicial orders, or other action with other state regulatory officials providing that those officials are required, under their law, to maintain its confidentiality. The Department should have a documented policy to cooperate and share information with respect to domestic companies with other state regulators directly and also indirectly through committees established by the NAIC which may be reviewing and coordinating regulatory oversight and activities. This policy should also include cooperation and sharing information with respect to domestic companies subject to delinquency proceedings.

(b) Procedures for Troubled Companies

The Department should generally follow and observe procedures set forth in the NAIC's Troubled Insurance Company Handbook. Appropriate variations in application of procedures and regulatory requirements should be commensurate with the identified financial concerns and operational problems of the insurer.

## Organizational and Personnel Practices

### 1. Professional Development

The Department should have a policy which encourages the professional development of staff involved with financial surveillance and regulation through job-related college courses, professional programs, and/or other training programs.

### 2. Minimum Educational and Experience Requirements

The Department should establish minimum educational and experience requirements for all professional employees and contractual staff positions in the financial regulation and surveillance area which are commensurate with the duties and responsibilities of the position.

### 3. Retention of Personnel

The Department should have the ability to attract and retain qualified personnel for those positions involved with financial surveillance and regulation.

## Evolving Standards: The Impact of Changes in the Financial Regulation Standards

As insurance industry practices evolve, so must solvency regulation. Therefore, the NAIC has anticipated that the Standards, outlined above, would not be static, but would be dynamic.

In March 1998, the NAIC adopted a more flexible process when adding new standards or modifying existing standards. The process seeks extensive input from public officials, consumers, academics, regulators and industry representatives when changes in the Financial Regulation Standards and Accreditation Program are considered.

The procedures identify three ways in which the solvency standards may be modified:

1. The development of new models or amendment of existing models;
2. Additional or more specific requirements to Parts B and C of the standards; or
3. Indirect modification of current requirements through changes in manuals or books incorporated by reference in the standards, such as modification of the annual statement blank required to be filed by all companies.

The process uses a set schedule to complete the deliberation process which allows all interested parties to clearly understand the decision timetable.



With regard to the development of new models or amendment of existing models, the proposal would be discussed at the Spring National Meeting by FRSAC with public testimony taken at the Summer National Meeting. FRSAC will notify all interested parties including all regulators, industry, consumer groups, the National Conference of State Legislatures (NCSL), National Governors' Association (NGA), National Conference of Insurance Legislators (NCOIL), and others, both of the potential change in the model and the process for public comment.

Additionally, any suggested addition or change to the accreditation standards will be accompanied by the following:

1. A statement and explanation of how the standard is directly related to solvency surveillance and why the proposal should be included in the Standards.
2. A statement as to why ultimate adoption by every jurisdiction may be desirable.
3. A statement as to the number of jurisdictions that have adopted and implemented the proposal or a similar proposal and their experience to date.
4. A statement as to the provisions needed to meet the minimum requirements of the standard.
5. An estimate of the cost for insurance companies to comply with the proposal and the impact on state insurance departments to enforce it.
6. An explanation of the potential or likely impact on insurance consumers should such proposal not be included in the standards.

After consideration of the testimony, FRSAC will determine whether the proposal should be exposed as a potential standard. At the Fall National Meeting, Executive Committee and Plenary will vote on the proposal.

If the proposal is adopted by Plenary, a two-year exposure period for law and regulation standards will commence during which time all interested parties will evaluate the effectiveness of the proposal.

During the final year of the exposure period, FRSAC will review the proposal at the Spring National Meeting to see what action, if any, should be taken to formally adopt the new proposal. At the Summer National Meeting, a public hearing will be held and FRSAC will decide whether to add the proposal to the standards with a 60% majority vote needed to adopt. At the Fall National Meeting, Executive Committee and Plenary would also take action with 60% required to adopt. Once adopted by Plenary, the standard will become effective two years immediately following the next January 1. This provides a total of at least four full years for all parties to consider amendments or additions to the law and regulation standards.

For additional or more specific requirements to Parts B and C of the standards or indirect modification of current requirements through changes in manuals or books incorporated by reference in the standards, no seasoning period is required, and these changes become effective two years following the next January 1.

If FRSAC determines that a waiver of the above procedures is necessary to expeditiously consider modification or alteration of the Standards, it may upon a three-fourths (3/4) majority vote, move to recommend adoption of changes or modifications to the Executive Committee. The Report of FRSAC shall fully explain the necessity for expeditious action and attempt to summarize in an objective manner, the positions of the various interested parties. The Executive Committee and Plenary would vote on the Report, with a 60% majority required for adoption.

In June 1997, the NAIC adopted significant changes to the accreditation standards. These changes increase the flexibility of states in meeting the Guaranty Funds, Producer Controlled Insurer, Managing General Agents and Reinsurance Intermediaries Standards by requiring a "regulatory framework" showing that basic regulatory tools are available and exercised by states. Strict adherence to NAIC model laws on these matters is not needed. However, states that have already enacted NAIC models on these matters are encouraged to retain them. Furthermore, if a state can provide evidence that none of the entities contemplated in the above standards are either present or allowed to operate in the state, it will not need to demonstrate compliance with that standard. Additionally, two standards—the Disclosure of Material Transactions Model Act and the Risk Retention Model Act have been deleted from the standards. These revisions have been implemented and published herein. Revised standards in Part B, Regulatory Practices and Procedures and in Part C, Organizational and Personnel Practices were also adopted.

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In October 2001, the NAIC added the NAIC Accounting Practices and Procedures Manual (As of March 2001) and the 1998 revisions to the Model Rule Requiring Annual Audited Financial Reports as required standards. They will become effective on January 1, 2004.

**WHAT THE  
FUTURE HOLDS:  
A STRONG  
SYSTEM OF  
SOLVENCY  
REGULATION**

The regulation of the insurance industry for solvency stands as a unique example of how an effective regulatory system can be built. The strength of that system resides in the interdependence of independent state regulators, each responsible to his or her own constituencies, yet jointly responsible for the financial health of an entire industry. At every step along the way, state insurance regulators bear in mind their duty to safeguard consumers.

Governors, legislators and state insurance regulators, not content to rest on past success, have devised in the Financial Regulation Standards Accreditation Program, a powerful means of achieving the necessary degree of consistency among states without sacrificing the multi-state diversity that has been instrumental to that success. Since 1990, every state and the District of Columbia have adopted legislative packages designed to bring their departments of insurance into compliance with the Standards. The partnership among state government officials has been key to the success of the accreditation program, solvency regulation, and effective consumer protection.

← Back

# NAIC

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# Staffing

State insurance departments are continually changing to accommodate the varying size and nature of the insurance industry. This requires a change in the makeup of the insurance department staff whose job is to regulate the insurance industry. The responsibility of regulating the insurance industry falls on the individual state governments.

## Insurance Commissioner

It is the job of the state insurance commissioner (superintendent or director in some states) to oversee the regulation of the insurance industry in his/her state. The majority of insurance commissioners are appointed to their positions. However, commissioners in 12 of the 55 states and territories are currently elected to their positions by the vote of the general public. These different approaches to selection cause the length of a commissioner's term to vary from state to state, with many serving at the pleasure of the governor.

The duties of the commissioner also differ between states. In the majority of the states the insurance department is a separate agency, allowing the commissioner to concentrate solely on insurance regulation. In other states the commissioner's responsibilities also include the oversight of other areas. Examples of other offices held by state insurance commissioners include that of Fire Marshal, Treasurer and Lieutenant Governor.

## Staff

It is the job of each state's insurance department to ensure the solvency of insurance companies doing business in the state, license insurance producers, assist insurance consumers and protect both consumers and companies from insurance fraud.

Ensuring the solvency of insurance companies is the primary function of insurance regulators. Solvency monitoring systems, such as the Insurance Regulatory Information System (IRIS) and risk-based capital (RBC), are used to identify and prioritize companies for detailed review, either through desk audits or financial examinations. Insurance companies are generally audited every three to five years, but evidence of potential impairment can also trigger an audit.

Historically, a large portion of each insurance department's staff has been employed for solvency monitoring and financial examinations. As the number of insurance companies and the complexity of their business

dealings have increased, departments have increased the number and training of financial examiners and analysts.

Other important charges of state insurance departments are the licensing of insurance producers and rate and policy form regulation. Each state sets its own licensing requirements for companies, agents, brokers, etc., and has the authority to revoke licenses for illegal or unethical conduct. Each state also sets its own rate and policy form filing requirements.

The task of assisting insurance consumers takes many forms. Insurance department staff members answer consumers' questions, look into complaints against insurance agents and companies, and perform market conduct examinations to ensure that insurance producers and companies are dealing with consumers in a fair and consistent manner.

Just as many companies have been contracting for services in the last few years to use their limited resources more efficiently, the state insurance departments have also been using contract staff. Frequently states also use the services of employees from other state agencies. For instance, some states do not have attorneys on staff; instead they use the services of their state's attorney general's office. Insurance departments also use the services of other state agencies in the areas of liquidations, receiverships and examinations, among others.

With the expansion of technology, the state insurance regulators' need for employees with computer expertise has grown. The communication link between the examiners who work at the site of the insurance companies and internal insurance department staff through networks has greatly improved the efficiency of the examination process. The ability for insurance department staff to electronically access the NAIC database information has also been a benefit for state regulators. The latest technology plays an important role as insurance regulation enters the 21<sup>st</sup> century.

Staffing data were compiled as of Dec. 31, 2000. In certain instances, employees of a department may perform work in more than one of the categories listed. For example, company examiners may perform both financial and market conduct examinations in some states. When such a situation occurs, an attempt is made to match the amount of time the employee spends doing each function and report it as such. Therefore, if half of an examiner's time is spent doing financial exams and half performing market conduct exams, it is recorded as 0.5 financial examiners and 0.5 market conduct examiners in the relevant tables.

4 Staffing

Figure 1

### Insurance Department Staff 1993-2000

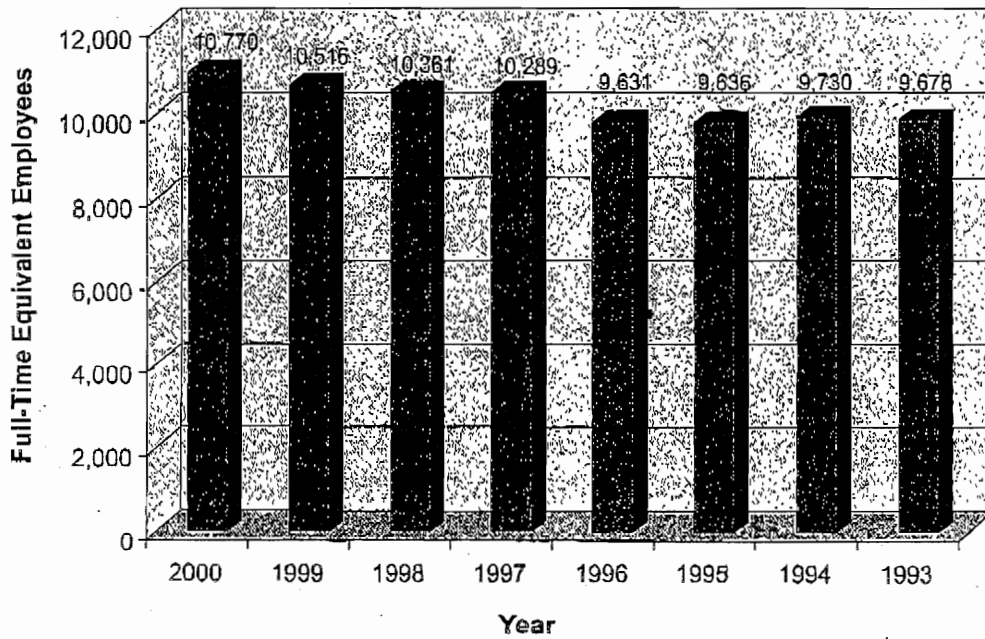


Figure 2

### Insurance Department Staff Breakdown - 2000

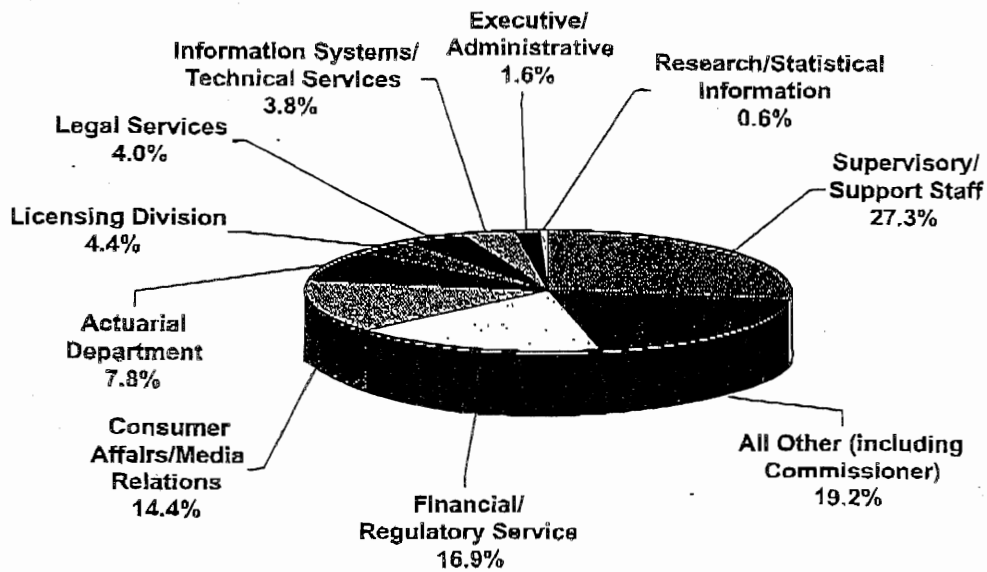


Table 3

## Full-Time Equivalent Staffing - By Position - 2000

State	Executive/ Administrative	Legal	Actuarial Department			
	Deputy/Assistant Commissioners	Attorneys	Actuaries - L/H	Actuaries - P/C	Rate/Form Analysts - L/H	Rate/Form Analysts - P/C
Alabama	2.00	6.00	0.00	0.00	1.00	3.00
Alaska	1.00	0.00	1.00	1.00	3.00	4.00
American Samoa	n/a	n/a	n/a	n/a	n/a	n/a
Arizona	9.00	0.00	0.50	0.00	4.00	7.00
Arkansas	2.00	4.00	1.00	0.00	2.00	5.00
California	11.00	91.00	6.00	4.00	3.00	68.00
Colorado	3.00	0.00	1.00	2.00	3.00	2.00
Connecticut	2.00	6.00	3.00	2.00	5.00	5.00
Delaware	1.00	2.00	1.00	1.00	1.00	1.00
Dist. of Columbia	4.00	3.00	1.00	1.00	4.00	1.00
Florida	1.00	41.00	7.00	10.00	12.00	26.00
Georgia	2.00	5.00	0.00	1.00	5.00	4.00
Guam	n/a	n/a	n/a	n/a	n/a	n/a
Hawaii	1.00	3.00	0.00	0.00	5.00	5.00
Idaho	1.00	0.00	0.00	0.00	1.00	1.00
Illinois	4.00	10.00	3.00	4.00	12.00	5.00
Indiana	4.00	3.00	0.00	0.00	3.00	2.00
Iowa	1.00	0.00	1.00	1.00	2.00	2.00
Kansas	1.00	7.00	1.00	0.00	3.00	12.00
Kentucky	2.00	15.00	1.00	2.00	11.00	5.00
Louisiana	12.00	11.00	1.00	1.00	3.00	3.00
Maine	2.00	5.00	1.00	2.00	5.00	5.00
Maryland	9.00	11.00	3.00	2.00	13.00	5.00
Massachusetts	2.00	26.80	2.00	1.00	3.00	3.50
Michigan	3.00	4.00	1.00	0.00	1.00	3.00
Minnesota	2.00	1.50	2.00	3.00	5.00	8.00
Mississippi	1.00	1.00	0.00	0.00	1.00	4.00
Missouri	6.00	9.00	1.00	1.00	7.00	8.00
Montana	1.00	4.00	1.00	1.00	2.00	1.00
Nebraska	0.00	5.00	1.00	1.00	2.00	3.00
Nevada	3.00	2.00	0.00	1.00	4.00	4.00
New Hampshire	2.00	1.00	1.00	1.00	4.00	4.00
New Jersey	14.00	9.00	5.00	5.00	12.00	16.00
New Mexico	3.00	2.00	1.00	1.00	3.00	2.00
New York	4.00	23.00	28.00	4.00	6.00	14.00
North Carolina	2.00	4.00	3.00	5.00	22.00	4.00
North Dakota	1.00	2.00	0.00	1.00	3.00	1.50
Ohio	11.00	13.00	1.00	4.00	16.00	9.00
Oklahoma	3.00	8.00	1.00	0.00	2.00	7.00
Oregon	2.00	2.00	1.00	2.00	6.00	2.00
Pennsylvania	5.00	15.00	13.00	5.00	9.00	2.00
Puerto Rico	n/a	n/a	n/a	n/a	n/a	n/a
Rhode Island	0.00	0.00	0.00	0.00	2.00	2.50
South Carolina	2.00	4.00	1.00	2.00	6.00	3.00
South Dakota	1.00	3.00	0.00	0.00	2.00	2.00
Tennessee	1.00	0.00	3.00	2.00	0.00	0.00
Texas	10.00	43.50	9.00	9.00	42.95	37.00
U.S. Virgin Islands	1.00	1.00	0.00	0.00	0.00	0.00
Utah	3.00	2.00	1.00	0.00	3.00	1.00
Vermont	1.50	3.50	0.00	0.00	3.50	2.00
Virginia	3.00	4.00	1.00	0.00	9.00	14.00
Washington	9.00	6.00	3.00	3.00	9.00	3.00
West Virginia	1.00	6.00	0.00	0.00	2.50	2.50
Wisconsin	2.00	5.00	0.50	0.50	4.00	3.00
Wyoming	1.00	1.00	0.00	0.00	2.00	2.00
<b>Total</b>	<b>175.50</b>	<b>434.30</b>	<b>113.00</b>	<b>86.50</b>	<b>301.95</b>	<b>339.00</b>

n/a - Not Available

## 6 Staffing

Table 3 (continued)

## Full-Time Equivalent Staffing - By Position - 2000

State	Financial/Regulatory Services				Consumer Affairs/Media Relations	
	Financial Examiners	Market Conduct Examiners	Financial Analysts/Auditors	Liquidations Personnel	Complaint Analysts	Consumer Advocates
Alabama	17.00	0.00	8.00	3.00	4.00	0.00
Alaska	5.00	3.00	2.00	0.00	3.00	0.00
American Samoa	n/a	n/a	n/a	n/a	n/a	n/a
Arizona	0.00	0.00	0.00	6.00	19.00	0.00
Arkansas	6.00	2.00	7.00	0.00	4.00	1.00
California	120.00	27.00	7.00	0.00	140.00	5.00
Colorado	17.00	8.00	3.00	0.00	12.00	0.00
Connecticut	25.00	7.00	13.00	1.00	13.00	0.00
Delaware	8.00	2.00	0.00	1.00	7.00	0.00
Dist. of Columbia	2.00	3.00	2.00	0.00	6.00	0.00
Florida	37.00	16.00	57.00	13.00	88.00	1.00
Georgia	1.00	1.00	12.00	0.00	29.00	0.00
Guam	n/a	n/a	n/a	n/a	n/a	n/a
Hawaii	5.00	0.00	6.00	0.00	3.00	0.00
Idaho	3.00	0.00	2.00	0.00	7.00	0.00
Illinois	52.00	16.00	20.00	0.00	20.00	0.00
Indiana	15.00	0.00	8.00	0.00	4.00	0.00
Iowa	24.00	2.00	5.00	0.00	5.00	3.00
Kansas	10.00	2.00	8.00	0.00	13.00	3.00
Kentucky	0.00	0.00	2.00	0.00	9.00	1.00
Louisiana	13.00	3.00	11.00	3.00	12.00	26.00
Maine	9.00	3.00	8.00	0.00	7.00	2.00
Maryland	12.00	10.00	9.00	0.00	35.00	2.00
Massachusetts	30.00	4.00	4.50	0.00	8.00	0.00
Michigan	19.00	0.00	1.00	0.00	7.00	0.00
Minnesota	11.00	2.00	10.00	0.00	16.00	9.00
Mississippi	3.00	0.00	1.00	0.00	5.00	0.00
Missouri	34.00	33.00	8.00	1.00	10.00	0.00
Montana	3.00	0.00	2.00	0.00	8.00	0.00
Nebraska	7.00	5.00	4.75	0.00	6.75	1.00
Nevada	0.00	1.00	2.00	0.00	6.00	0.00
New Hampshire	12.00	3.00	2.00	0.00	0.00	2.00
New Jersey	37.00	15.00	5.00	4.00	22.00	9.00
New Mexico	3.00	0.00	0.00	0.00	2.00	0.00
New York	205.00	87.00	0.00	0.00	36.00	0.00
North Carolina	16.00	11.00	19.00	7.00	24.00	0.00
North Dakota	2.00	1.00	1.00	0.00	2.00	2.00
Ohio	24.00	11.00	12.00	2.00	27.00	4.00
Oklahoma	0.00	0.00	5.00	0.00	7.00	0.00
Oregon	5.00	3.00	6.00	0.00	8.00	4.00
Pennsylvania	34.00	8.00	15.00	1.00	24.00	0.00
Puerto Rico	n/a	n/a	n/a	n/a	n/a	n/a
Rhode Island	12.00	4.00	4.00	0.00	2.50	0.00
South Carolina	9.00	3.00	4.00	1.00	9.00	0.00
South Dakota	0.00	0.00	3.00	0.00	1.00	0.00
Tennessee	21.00	0.00	0.00	0.00	13.00	0.00
Texas	70.00	8.00	52.00	15.00	61.50	0.00
U.S. Virgin Islands	9.00	0.00	0.00	0.00	0.00	0.00
Utah	5.00	7.00	4.00	0.00	6.00	0.00
Vermont	12.00	1.00	1.00	0.00	3.00	0.00
Virginia	17.00	18.00	16.00	0.00	16.00	1.00
Washington	16.00	5.00	4.00	1.00	10.00	7.00
West Virginia	4.00	0.00	8.00	0.00	6.00	1.00
Wisconsin	18.50	7.00	7.00	0.00	7.00	0.00
Wyoming	3.00	0.00	4.00	0.00	3.00	0.00
<b>Total</b>	<b>1,016.50</b>	<b>342.00</b>	<b>400.25</b>	<b>60.00</b>	<b>818.75</b>	<b>84.00</b>

n/a - Not Available



Table 3 (continued)

## Full-Time Equivalent Staffing - By Position - 2000

State	Consumer Affairs/ Media Relations		Licensing Division		Research/Statistical Information	
	Fraud Investigators	Media/Public Info. Personnel	Producer Licensing Personnel	Company Licensing Personnel	Economic/Finance Researchers	Statistical Reporting
Alabama	0.00	0.00	0.00	1.00	0.00	0.00
Alaska	3.00	0.00	3.00	0.00	0.00	0.00
American Samoa	n/a	n/a	n/a	n/a	n/a	n/a
Arizona	11.00	2.00	7.00	2.00	0.00	0.00
Arkansas	6.00	1.00	9.00	0.00	0.00	0.00
California	186.00	4.00	40.00	12.00	4.00	10.00
Colorado	3.00	1.00	2.00	1.00	0.00	0.00
Connecticut	0.00	0.00	14.00	0.00	0.00	0.00
Delaware	7.00	1.00	3.00	1.00	0.00	0.00
Dist. of Columbia	3.00	2.00	2.00	1.00	1.00	0.00
Florida	98.00	10.00	20.00	7.00	0.00	0.00
Georgia	5.00	3.00	0.00	0.00	0.00	0.00
Hawaii	n/a	n/a	n/a	n/a	n/a	n/a
Hawaii	5.00	0.00	3.00	2.00	0.00	0.00
Idaho	5.00	0.00	4.50	0.00	0.00	0.00
Illinois	11.00	1.00	10.00	4.00	3.00	3.00
Indiana	3.00	1.00	9.00	0.00	0.00	0.00
Iowa	3.00	1.00	3.00	0.00	0.00	0.00
Kansas	2.00	1.00	10.00	0.00	0.00	0.00
Kentucky	9.00	3.00	15.00	0.00	0.00	0.00
Louisiana	8.00	2.00	8.00	18.00	0.00	5.00
Maine	0.00	1.00	2.00	2.00	0.00	1.00
Maryland	7.00	1.00	6.00	2.00	1.00	0.00
Massachusetts	4.00	1.00	9.00	4.50	3.00	0.60
Michigan	5.00	2.00	5.00	4.00	1.00	2.00
Minnesota	0.00	1.00	6.00	2.00	0.00	0.00
Mississippi	1.00	1.00	9.00	1.00	0.00	0.00
Missouri	6.00	2.00	20.00	1.00	1.00	6.00
Montana	1.00	0.00	5.00	0.00	0.00	0.00
Nebraska	1.00	1.00	5.00	0.25	0.00	0.00
Nevada	3.00	0.00	5.00	0.00	0.50	0.00
New Hampshire	2.00	0.00	0.00	0.00	0.00	0.00
New Jersey	23.00	2.00	4.00	2.00	0.00	0.00
New Mexico	3.00	1.00	7.00	2.00	0.00	3.00
New York	39.00	6.00	5.00	1.00	1.00	0.00
North Carolina	11.00	3.00	6.00	1.00	0.00	0.00
North Dakota	0.50	0.00	2.50	1.00	0.00	0.00
Ohio	13.00	5.00	9.00	3.00	0.00	0.00
Oklahoma	6.00	2.00	10.00	0.00	0.00	0.00
Oregon	4.00	1.00	8.00	0.00	0.00	0.00
Pennsylvania	10.00	1.00	14.00	2.00	0.00	0.00
Puerto Rico	n/a	n/a	n/a	n/a	n/a	n/a
Rhode Island	0.00	0.00	5.00	2.00	0.00	0.00
South Carolina	0.00	1.00	7.00	0.50	0.00	0.00
South Dakota	2.00	0.00	3.00	1.00	0.00	0.00
Tennessee	1.00	0.00	0.00	0.00	0.00	1.00
Texas	37.00	13.00	39.50	9.00	0.00	5.00
U.S. Virgin Islands	0.00	0.00	1.00	1.00	0.00	0.00
Utah	7.00	1.00	6.00	1.00	0.00	1.00
Vermont	0.00	0.50	2.00	1.00	0.00	0.00
Virginia	0.00	0.00	7.00	0.00	7.00	0.00
Washington	5.00	3.00	8.00	0.00	0.00	0.00
West Virginia	1.00	0.00	0.00	0.00	0.00	0.00
Wisconsin	0.00	2.00	4.00	1.50	0.00	0.00
Wyoming	0.00	0.00	3.00	0.00	0.00	0.00
<b>Total</b>	<b>562.50</b>	<b>84.50</b>	<b>383.50</b>	<b>94.75</b>	<b>22.50</b>	<b>37.60</b>

n/a - Not Available

## 8 Staffing

Table 3 (continued)

## Full-Time Equivalent Staffing - By Position - 2000

State	Information Systems/Technical Services			Other Staff		Total
	System/LAN Personnel	Computer Prog./Analysts	Data Services Personnel	Supervisory Support	All Other	Full Time Employees
Alabama	1.00	2.00	1.00	27.00	38.00	108.00
Alaska	0.00	4.00	0.00	19.00	1.00	53.00
American Samoa	n/a	n/a	n/a	n/a	n/a	n/a
Arizona	1.00	3.00	0.00	71.50	3.00	146.00
Arkansas	1.00	2.00	0.00	41.00	45.00	141.00
California	25.00	27.00	3.00	322.80	261.00	1,376.80
Colorado	1.00	0.00	0.00	25.00	7.00	91.00
Connecticut	3.00	2.00	0.00	55.00	18.00	174.00
Delaware	0.00	1.00	0.00	24.00	17.00	79.00
Dist. of Columbia	1.00	0.00	0.00	27.00	9.00	73.00
Florida	18.00	15.00	16.00	360.50	236.50	1,090.00
Georgia	1.00	1.00	0.00	51.00	1.00	122.00
Guam	n/a	n/a	n/a	n/a	n/a	n/a
Hawaii	0.00	0.00	0.00	15.00	14.00	67.00
Idaho	1.00	2.00	2.00	12.00	27.00	68.50
Illinois	3.00	10.00	2.00	67.00	155.00	415.00
Indiana	1.00	0.00	0.00	21.00	13.00	87.00
Iowa	0.00	0.00	0.00	18.00	23.50	94.50
Kansas	4.00	0.00	0.00	24.00	1.00	107.00
Kentucky	3.00	5.00	0.00	88.00	23.00	194.00
Louisiana	0.00	2.00	4.00	64.00	63.00	273.00
Maine	0.00	0.00	0.00	17.00	9.00	81.00
Maryland	0.00	2.00	2.00	106.00	22.00	260.00
Massachusetts	5.00	2.00	2.00	36.50	39.00	191.40
Michigan	0.48	1.20	1.68	53.53	8.75	134.64
Minnesota	0.10	1.00	0.25	20.30	1.00	101.15
Mississippi	1.00	3.00	0.00	29.00	47.00	103.00
Missouri	1.00	6.00	3.00	44.00	15.00	223.00
Montana	1.00	0.00	0.00	6.50	9.50	46.00
Nebraska	0.00	2.00	0.00	30.00	10.00	85.75
Nevada	0.50	0.00	0.00	29.00	7.00	68.00
New Hampshire	1.00	0.00	0.00	20.00	2.00	57.00
New Jersey	8.00	8.00	2.00	143.00	1.00	346.00
New Mexico	1.00	0.00	0.00	26.00	5.00	65.00
New York	4.00	30.00	5.00	303.00	80.00	903.00
North Carolina	3.00	3.00	1.00	92.00	160.00	397.00
North Dakota	1.00	0.00	0.00	6.00	18.00	45.50
Ohio	2.00	5.00	2.00	67.00	42.00	282.00
Oklahoma	1.00	1.00	5.00	53.00	29.00	140.00
Oregon	1.00	0.00	0.00	34.50	4.00	93.50
Pennsylvania	5.00	9.00	0.00	74.00	65.00	309.00
Puerto Rico	n/a	n/a	n/a	n/a	n/a	n/a
Rhode Island	0.00	0.00	0.00	11.00	2.00	45.00
South Carolina	3.00	2.00	1.00	46.50	1.00	106.00
South Dakota	0.00	0.00	0.00	8.00	3.00	31.00
Tennessee	0.00	0.00	0.00	47.00	4.00	93.00
Texas	32.00	23.00	8.00	101.50	409.50	1,045.50
U.S. Virgin Islands	0.00	0.00	0.00	8.00	1.00	22.00
Utah	1.00	2.00	2.00	22.50	6.50	82.00
Vermont	1.00	0.00	0.00	14.50	2.75	49.25
Virginia	4.00	0.00	0.00	46.00	50.00	213.00
Washington	1.00	2.00	1.00	38.00	22.00	156.00
West Virginia	0.00	3.00	0.00	33.00	1.00	71.00
Wisconsin	3.00	6.00	1.00	30.50	32.00	134.50
Wyoming	0.00	0.00	0.00	6.00	3.00	25.00
<b>Total</b>	<b>145.08</b>	<b>187.20</b>	<b>74.93</b>	<b>2,937.63</b>	<b>2,068.05</b>	<b>10,769.99</b>

n/a - Not Available





***The NAIC's Risk-Based Capital System***

Remarks of Brian K. Atchinson, President of the NAIC, before the General Assembly of the Geneva Association, Bordeaux, France, June 7, 1996

This speech was delivered by NAIC President Brian Atchinson to the General Assembly of the Geneva Association, an international association for the study of insurance economics. The speech points out the difference between a regulatory risk-based capital system, like the one employed by the NAIC, and risk-based capital systems used by companies.



***New York's Emerging Nonstandard Auto Insurance Market***

By Bent Kirsch, CPCU, CFE, CIE

This article explores New York's emerging nonstandard automobile insurance market. The nonstandard automobile insurance market or substandard market consists of insureds that for one or more reasons are considered by underwriters to have a greater potential for loss than average insureds.



***1995 Insurance Department Resources Report Review***

Compiled by the NAIC Staff

A preview of the 1995 Insurance Department Resources Report is provided within this article. Graphs are used to illustrate data from the report.



***Health Organizations RBC Survey: Questions & Answers***

This is a brief summary of the Health Organizations RBC Survey conducted during 1996. The survey, which was sent to over 2,000 health organizations, was a working model of the RBC formula recommended by the American Academy of Actuaries at the June 1996 meeting of the NAIC's Health Organizations RBC Working Group.



***1996 Health Organizations RBC Survey Blue Cross Blue Shield Association Questions & Answers***

Comments, questions and answers submitted by the Blue Cross Blue Shield Association in response to the 1996 NAIC HO RBC Survey.



***1996 HORBC Survey Frequently Asked Questions Received by NAIC Staff***

Comments, questions and answers received by NAIC staff during the 1996 NAIC HO RBC Survey.



***1996 HORBC Survey Frequently Asked Questions Received by American Association of Health Plans Staff***

Comments, questions and answers submitted by the American Association of Health Plans, a trade organization representing HMOs and other managed care organizations, during the 1996 NAIC HORBC Survey.

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The National Association of Insurance Commissioners (NAIC) is a voluntary organization of the chief insurance regulatory officials of the 50 states, the District of Columbia, American Samoa, Guam, Puerto Rico and the Virgin Islands. The NAIC provides its members with a forum for discussing common interests and for working cooperatively on regulatory matters that transcend the boundaries of their own jurisdictions.

**The views expressed in these articles do not necessarily represent the view of the NAIC members, individually or collectively.**

# The NAIC's Risk-Based Capital System

*Remarks of Brian K. Atchinson, President of the NAIC, before the General Assembly of the Geneva Association, Bordeaux, France, June 7, 1996*

*Editor's Note: The following speech was delivered by NAIC President Brian Atchinson to the General Assembly of the Geneva Association, an international association for the study of insurance economics. Risk-based capital systems have been used internally by insurers for years to develop appropriate capital structure. Beginning in 1993, the NAIC instituted formal regulatory risk-based capital requirements to place a floor on the amount of capital that an insurance company could hold without triggering regulatory attention. In his speech, Superintendent Atchinson points out the difference between a regulatory risk-based capital system, like the one employed by the NAIC, and risk-based capital systems used by companies. The invitation extended to the president of the NAIC to address the Geneva Association illustrates the interest of European insurers in the risk-based capital concept.*

The NAIC is an organization of all the state insurance regulators from the 50 states, the District of Columbia and the four U.S. territories. It is the oldest association of state government officials in the United States. This year, 1996, the NAIC is celebrating its 125th anniversary.

State insurance commissioners are charged with the duty of protecting consumer interests while practicing fair and reasonable regulation of the insurance industry. The most important duty of insurance commissioners is to help maintain the financial stability of the insurance industry—that is, to guard against insolvencies.

Among the greatest weapons against insolvency are the risk-based capital requirements. The risk-based capital system uses a formula that establishes the minimum amount of capital necessary for an insurance company to support its overall business operations, considering its size and risk profile. That amount is then compared to the company's actual statutory capital to determine whether a company is technically solvent. The formula results, in combination with the authority granted in the state's Risk-Based Capital for Insurers law, allows state regulators to intervene in a timely manner when a company fails to meet these minimum standards. Companies failing to meet the minimum capital standard developed by the formula are subject to increasingly stringent regulatory intervention, depending upon the degree to which they fail the minimum standard.

Currently, the establishment of capital and surplus standards that are risk-based is the subject of active study and debate. The intent of proponents of the risk-based capital approach is to establish formulas that reflect the types of risks that a company is writing. In principle, the imposition of risk-based capital and surplus standards has a clear attraction. Property-casualty insurers that present higher risks would be required to maintain greater levels of capital than their counterparts that present lower risks.

The NAIC's risk-based capital system, in effect, limits the amount of risk a company can take on by requiring higher amounts of capital for bearing higher amounts of risk. The risk factors for the NAIC's risk-based capital formula, which produces a Regulatory Minimum Risk-Based Capital, focuses on four major areas: asset risk, liability or

underwriting risk, business risk and miscellaneous risk.

Asset risk encompasses the risk that asset values will be lower than expected. Examples include bond defaults and changes in the market value of common stock. An insurer holding a portfolio of high-quality bonds obviously has more stability in its investment earnings than an insurer holding junk bonds or exotic derivative securities. The risk-based capital charge for high-risk securities is commensurably higher. Figure 1 shows some examples of risk charges for various classes of assets typically found in a U.S. insurer's investment portfolio.

Investment risk is a very important component of the total risk posture for large life insurers, but for most property-casualty companies, the major underlying risk is its liabilities. In 1995, U.S. property-casualty insurers reported nearly \$400 billion in loss and loss expense reserves on their balance sheets. This amount represents a best estimate of existing obligations. However, estimates are prone to error, and the estimation error differs significantly by line of business. Insurers holding long duration obligations are required to hold relatively more capital to support those estimation errors.

In addition, there is a delay between the time when an insurer winds up its calendar year and the time that a regulator is able to review its annual statement filing for that calendar year. Studies have shown that the major cause of insolvencies in property-casualty insurers is underpricing or underestimation of reserves. If an insurer is producing underpriced business during the calendar year just ending, it is likely that the insurer will keep producing that underpriced business well into the new year. Therefore, RBC also generates a surplus requirement prospectively by line of business.

Figure 2 shows the industry breakdown of total RBC for both life and non-life insurers. As this figure shows, for property-casualty insurers, the predominant risks are underestimation of the reserves and overestimation of the profitability of incoming business. Therefore, the lion's share of the total RBC generated by the P&C formula falls into the underwriting risk categories. Conversely, life insurers tend to generate relatively more asset risk. The fundamental differences in the risk

posture faced by life and non-life insurers are the driving force behind differences in the basic formulas.

It is useful to note the difference between Real Risk-Based Capital and Regulatory Minimum Risk-Based Capital (see Figure 3). Since capital is basically assets minus liabilities, capital also can be thought of as the degree to which a company pledges its assets to guaranty its promises to other parties (that is, its liabilities).

Capital serves as a cushion against insolvency. Therefore, most companies that have relatively higher risk already carry relatively higher amounts of capital. Figure 4 shows a moving average of the surplus-to-assets ratio for 2,400 property-casualty insurers, arranged in ascending order by asset size. As companies grow larger and more diversified, their operating results tend to be relatively more stable. More stability in results usually translates to less need for capital, but that rule of thumb is frequently violated. Not all companies carry an amount of capital that would generally be considered prudent. The NAIC's risk-based capital system essentially sets minimum standards for a company's self-insurance against insolvency. Because these standards can, in effect, alter the normal business decisions of insurers in the market, they must be carefully established to have the maximum effectiveness while at the same time minimizing market disruptions.

Real Risk-Based Capital is an economic concept. Companies hold the amount of capital that they perceive to be optimal or desirable. Regulatory Minimum Risk-Based Capital is a regulatory concept that sets a floor value for a company's own internally generated "optimal" or "desirable" capital decisions. Companies may hold any amount of capital in excess of the minimum established by law, but holding capital levels in excess of the regulatory minimums does not imply that a company is financially strong—it simply means that it is not weak as defined by the risk-based capital formula. A company's Real Risk-Based Capital will almost always be higher than the Regulatory Minimum Risk-Based Capital, but it may not be enough and it may not be optimal. Therefore, the NAIC's risk-based capital standards are inappropriate as measures of financial strength and should never be used to compare one adequately capitalized company to another.

The purpose of computing risk-based capital is to help determine when and what actions regulators should take in the event a company's actual capital and surplus falls below its calculated minimum. Using the risk-based capital formula fits with today's regulatory needs, which require prompt, easily applied and easily understood measures.

To understand the need for a consistent and uniform approach, an historic overview is in order. In the late 1980s there were a number of large insurer failures, and as a result, the importance of monitoring the financial soundness of insurance companies became even greater. So, in 1990, as part of the NAIC Solvency Policing Agenda, a working group was established to determine the feasibility of developing statutory, risk-based capital requirements for insurers. After conducting a thorough study and soliciting input from insurers and other interested parties, the working group concluded that risk-based capital requirements for insurers are preferable to the generally prevailing system of minimum capital and surplus requirements. The working group also determined that the purpose of establishing risk-based capital requirements would be to develop a more realistic capital base for insurers. It developed a formula and a companion NAIC model act that would provide the basis for treating insurers that did not meet the requirements.

Separate risk-based capital requirements for life-health and property-casualty were drafted. During 1991 and 1992, the appropriate requirements, instructions and models were developed. During the drafting process, extensive research was conducted and expert advice was sought from regulators, industry and consumers. The members of the NAIC adopted the life-health risk-based capital requirements in December 1992 and the property-casualty requirements in December 1993.

Having a formula in place to compute uniform minimum capital standards for insurers is only part of the risk-based capital system, though. Regulators also need some legal basis to act. Prior to risk-based capital, a state regulator would have to petition the courts and try to prove that an insurer was operating in an unsound manner before being allowed to take decisive action. However, if the state has adopted some version of the Risk-Based Capital for Insurers Model Act, the

regulator is granted the authority to act when an insurer triggers one of the intervention levels in the formula.

Generally, state insurance regulators concentrate their efforts on those companies domiciled in that state and rely on other state regulators to scrutinize those foreign insurers operating in their jurisdiction. Each state compares each of its companies' Total Adjusted Capital against that company's risk-based capital requirement to determine if regulatory action is warranted under that state's version of the Risk-Based Capital for Insurers Model Act. There are four intervention levels in the model act, but the Authorized Control Level Risk-Based Capital is the base standard against which Total Adjusted Capital is compared (see Figure 5).

Of the 2,419 property-casualty companies that submitted a risk-based capital report to the NAIC in 1995, 2,344 had sufficient capital to pass the RBC test. Once the test is passed, no further action is required. However, for the 3 percent of insurers that triggered some form of regulatory intervention, the RBC formula provides a spectrum of increasingly stringent regulatory responses. This allows the regulator to tailor an appropriate regulatory action to a company's financial problems, thus maintaining the maximum amount of discretion commensurate with prudent regulatory policies.

The first level of regulatory intervention in the RBC law is the Company Action Level. In 1995, 32 companies (about 1.3 percent of the total) triggered this level. When a company files a risk-based capital report indicating that its Total Adjusted Capital is higher than its Regulatory Action Level Risk-Based Capital but lower than its Company Action Level Risk-Based Capital, the insurer must submit to the insurance commissioner a comprehensive financial plan. That plan must identify the conditions in the insurer that contribute to the company's financial condition, contain proposals to correct the company's financial problems and provide projections of the company's financial condition, both with and without the proposed corrections. The plan also must list the key assumptions underlying the projections and identify the quality of, and problems associated with, the insurer's business.



When a company's Total Adjusted Capital falls between the Regulatory Action Level Risk-Based Capital and the Authorized Control Level Risk-Based Capital, or if the company fails to file a risk-based capital plan when required, the insurance commissioner shall perform any examinations or analysis of the insurer's business and operations that he or she deems necessary and issue any appropriate corrective orders to address the company's financial problems. In 1995, 15 insurers (0.6 percent) triggered this level of intervention.

If the company's Total Adjusted Capital falls below the Authorized Control Level Risk-Based Capital, in addition to those actions available to the insurance commissioner for less serious financial problems mentioned earlier, the commissioner may place the insurer under regulatory control. Only six insurers triggered this level in the 1995 RBC filings submitted to the NAIC. Finally, if the company's Total Adjusted Capital falls below the Mandatory Control Level Risk-Based Capital, the insurance commissioner will be required to place the insurer under regulatory control. Twenty-two insurers (about 0.9 percent of the total) triggered this level in 1995. However, about half of the companies that trigger a Mandatory Control Level event are actually already insolvent—that is, they register negative surplus. Ideally, the RBC system will trigger one of the higher intervention levels first, and thus allow regulators an opportunity to work with the troubled insurer on a solution. However, with many smaller insurers, the first indication of financial impairment is also the last.

According to a February *National Underwriter* article, some United Kingdom regulators are studying the U.S. risk-based capital model and are moving ahead to develop their own system. Lloyd's of London has published its own proposal which requires that the risk-based formula parameters are made public, but the actual results of the calculations are confidential. Another company, Swiss Re, which is based in Zurich, is developing risk-based capital standards for all its subsidiaries. Eagle Star Re is moving forward on developing its own standards as well. The reason, according to one of its actuaries, is because "risk-based capital has done the U.S. insurance industry a lot of good, and I believe that insurance companies in Europe can only benefit from its introduction."

Fixed capital standards may have been adequate in the days when life companies issued

plain vanilla policies with simple savings components and property-casualty companies simply wrote fire insurance. On the asset side, simple bonds, a few common stocks and some high quality mortgages generated stable streams of investment income. However, the world has changed and the insurance industry has changed even more rapidly. Today's life insurance company can write a wide array of complex products backed by a bewildering portfolio of exotic investments that did not even exist just 10 years ago.

The nature of risk, both on the investment side and the underwriting side, has become extremely complex. Regulation has had to become more complex to meet the new solvency challenges while at the same time minimizing the amount of interference in legitimate business pursuits. Thus, regulators have had to move from relatively simple, one-size-fits-all fixed dollar capital standards to a new, fluid, flexible set of capital standards tailored to the risk profile of each individual company.

The European Community countries use a formula approach coupled with fixed minimums to establish minimum capital standards for insurers, similar to the approach used by the members of the NAIC. The real difference lies in the degree of complexity. The diversity of insurers in the United States, coupled with the diversity of 55 different regulatory jurisdictions requires a set of common standards that recognize this great diversity. To the maximum extent possible, the NAIC formula has to recognize the unique risk profile of each individual company and set the minimum capital requirements commensurate with that risk.

While by no means a perfect formula, the NAIC's RBC formulas are a quantum leap toward capturing the unique solvency risk posed by each insurer. The NAIC formulas use company experience adjustment factors in portions of the calculation to recognize the relative experience of individual companies relative to their peers, tiered rating factors to recognize the decreasing risk of large insurance portfolios, and an overall covariance adjustment to recognize the effects of diversification and risk-spreading within a company's balance sheet.

The NAIC's risk-based capital system cannot alone prevent insolvencies. It can, however, help to alleviate insolvency costs by allowing insurance regulators to step in early while there is still a

chance to save a dying company. Think of it as a wrench in the NAIC toolbox that can help stop a leaky faucet before it floods the entire house. It gives insurance regulators the flexibility to help prevent disasters before they occur.

One of the other reasons risk-based capital works so well in the U.S. is because it is part of another NAIC innovation that derived from the insurer failures in the 1980s — the accreditation program.

The accreditation program also was designed to improve the quality of solvency regulation by state insurance departments. To ensure that regulation is adequate in all jurisdictions, the NAIC established the accreditation program to provide a baseline level of uniformity among the states to coordinate solvency monitoring. One of the requirements for accreditation is the adoption of the Risk-Based Capital for Insurers Model Act by the states. Independent review teams conduct thorough on-site reviews to evaluate a state's fitness for accreditation, and part of that review includes checking to see that each state has adopted the risk-based capital model by July 1, 1997.

Working along with the risk-based capital formula are a number of other tools used to monitor solvency. Examples of these tools include financial reporting, examination, and solvency screening systems such as the Insurance Regulatory Information System (IRIS) and the Financial Analysis and Solvency Tracking System (FAST). These tools are used more to identify higher-risk behavior, but unlike risk-based capital, they don't actually force an insurer to limit risk. Following are more details about each of these tools.

Designing a system that can identify insurers that are in, or are heading toward a hazardous condition is one of the greatest challenges that regulators face. The trick is to create a system that detects problems early enough so that they can be corrected, but doesn't raise false warnings about sound insurers. Financial reporting plays a large role in the solvency early warning system. The annual financial statement filed by insurers provides a relatively complete picture of financial condition. The statement has evolved considerably since being developed by the NAIC in 1875 to now include a balance sheet and income statement as

well as a number of supporting exhibits and schedules. Most insurers also are required to file quarterly statements containing information on assets, liabilities, income, changes in investment holdings, premiums written, losses and reserves.

All of this information on individual insurance companies is amassed in an extensive financial database maintained by the NAIC. These databases are electronically accessible by state insurance departments and contain information on approximately 5,000 insurance companies dating back to the 1970s. The NAIC database serves as the core of the solvency surveillance and other analysis activities of state insurance regulators and the NAIC.

In addition, the NAIC maintains a number of other databases that state regulators use for financial analysis and other regulatory functions. The Alien Reporting Information System provides financial reports that show reinsurance ceded to domestic or alien reinsurers along with federal employer identification numbers, alien reinsurer identification numbers and reinsurer locations. The Regulatory Information Retrieval System contains information on completed regulatory actions against insurers and agents. The Special Activities Database is another source to check for market conduct information. These two databases enhance regulators' ability to share information on individuals or companies suspected of illegal or questionable activities, helping to prevent their infiltration into new areas.

Finally, examinations and risk scoring system tools help detect trouble spots. The basic purposes of an examination system are to detect as early as possible those insurers in financial trouble or engaging in unlawful activities and to develop the information needed for appropriate regulatory action.

Risk scoring models and other automated warning systems are used to allocate resources so examiners can concentrate on problem areas in a timely and efficient manner. A number of systems are used. The Insurance Regulatory Information System (IRIS) serves as a baseline solvency screening system for state regulators and the NAIC. IRIS helps regulators prioritize insurers for detailed financial analysis and allocate their resources according to need by producing a number of financial ratios. Examiners use the ratios and

statements of insurers to determine if there is a need for further analysis by their domiciliary regulators.

Another system state regulators put to good use is the Financial Analysis and Solvency Tracking System (FAST). This system is an expansion of IRIS to encompass a new solvency screening model and analytical process to facilitate peer review of domiciliary regulation of "nationally significant" insurers. Its objective is to ensure that domiciliary regulators are taking effective action with respect to nationally significant insurers that are in financial difficulty. Nationally significant insurers are defined as companies that write business in 17 or more states and have gross premiums written in excess of \$50 million for life-health companies and \$30 million for property-casualty insurers. Like IRIS, FAST also consists of a series of financial ratios based on annual statement data. However, FAST goes a step further and assigns different point values for different ranges of ratio results. A company's cumulative score is used to prioritize further analysis.

These are just a few of the things in the NAIC arsenal with regard to solvency monitoring. The NAIC continues to evaluate and refine capital requirements for all types of insurers and is taking the next step in protecting consumers through risk-based capital standards by developing standards for health organizations. The NAIC's Health Organizations Risk-Based Capital Working Group is drafting a separate risk-based capital formula for health insurance including traditional health insurers, health maintenance organizations (HMOs), Blue Cross/Blue Shield plans, and health

service plans. The plan is to expand the provisions in the current life-health formula to better measure risk in various health organizations.

In fact, at the NAIC's September 1996 National Meeting, the working group received a preliminary report regarding a draft health risk-based capital formula from the American Academy of Actuaries. The working group is now testing the formula on health entities. Following the testing and evaluation, the working group will recommend a final version for adoption by the NAIC.

By working with industry, consumers and other interested parties over the years, the NAIC has developed a valuable tool for state insurance regulators to use to monitor the solvency of insurers. As the 21st century approaches, it is obvious that significant changes in the structure of the insurance industry will continue to challenge the way that regulators do business. New technologies will continually and dramatically change the way we monitor insurers' insolvency risk.

The goal is for insurance regulators to continue to do their best to ensure that insurance companies do the best they can to provide their product to consumers. State regulators in the United States, through the NAIC, have done an admirable job of regulating insurance for 125 years and plan on building on our great track record into the next century and beyond.

**Figure 1**  
**Sample of RBC Charges for Selected Asset Categories**

TYPE OF INVESTMENT	RBC FACTOR
U.S. Government Bonds	0.000
Highest Quality Corporate Bonds	0.003
Cash And Short-Term Investments	0.003
High Quality Corporate Bonds	0.010 TO 0.100
Bonds In Default On Principle Or Interest	0.300
Mortgages And Collateral Loans	0.050
Unaffiliated Common Stock	0.150
Real Estate	0.100
Partnerships And Joint Ventures	0.200
Reinsurance Recoverables	0.100
Miscellaneous Recoverables	0.050

**Figure 2**  
**1995 Industry Aggregate RBC By Category (in \$ Millions)**

Major Category	Life Industry	% of Total	P&C Industry	% of Total
Asset Risk	57,366	65%	62,578	39%
Underwriting Risk	17,356	20%	96,683	61%
Reserves			62,281	39%
Written Premiums			34,402	22%
Other	13,569	15%	N/A	
Total	88,291	100%	159,261	100%

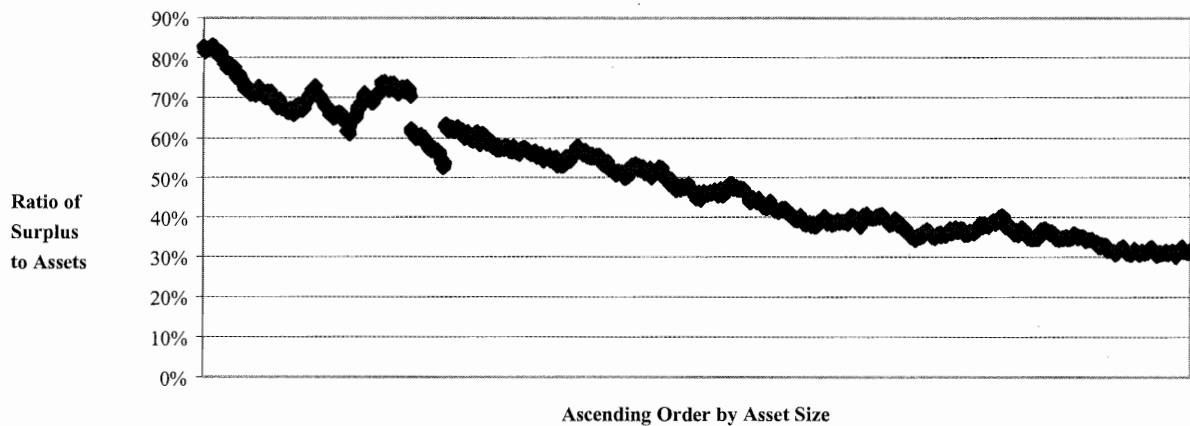
**Figure 3**  
**The Difference Between Risk-Based Capital and  
Regulatory Minimum Risk-Based Capital**

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- Regulatory minimum standards are set at minimum levels so as to impose a floor level of safety on the operations of an insurance company
  - System allows companies maximum freedom as long as they are above the minimums
  - Minimizes market disruptions by non-management while still maintaining safety levels
  - Regulatory Minimum Risk-Based Capital standard makes comparisons between companies inappropriate
- 

**Figure 4**  
**Moving Average of Surplus to Assets Ratio for Property-Casualty Insurers  
Arranged in Ascending Asset Size  
1995 Data**

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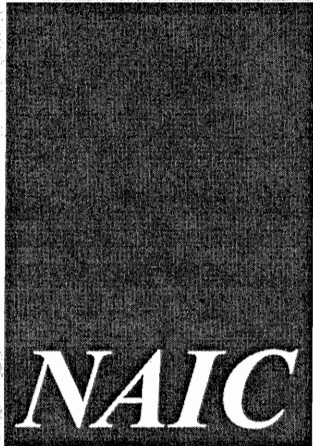
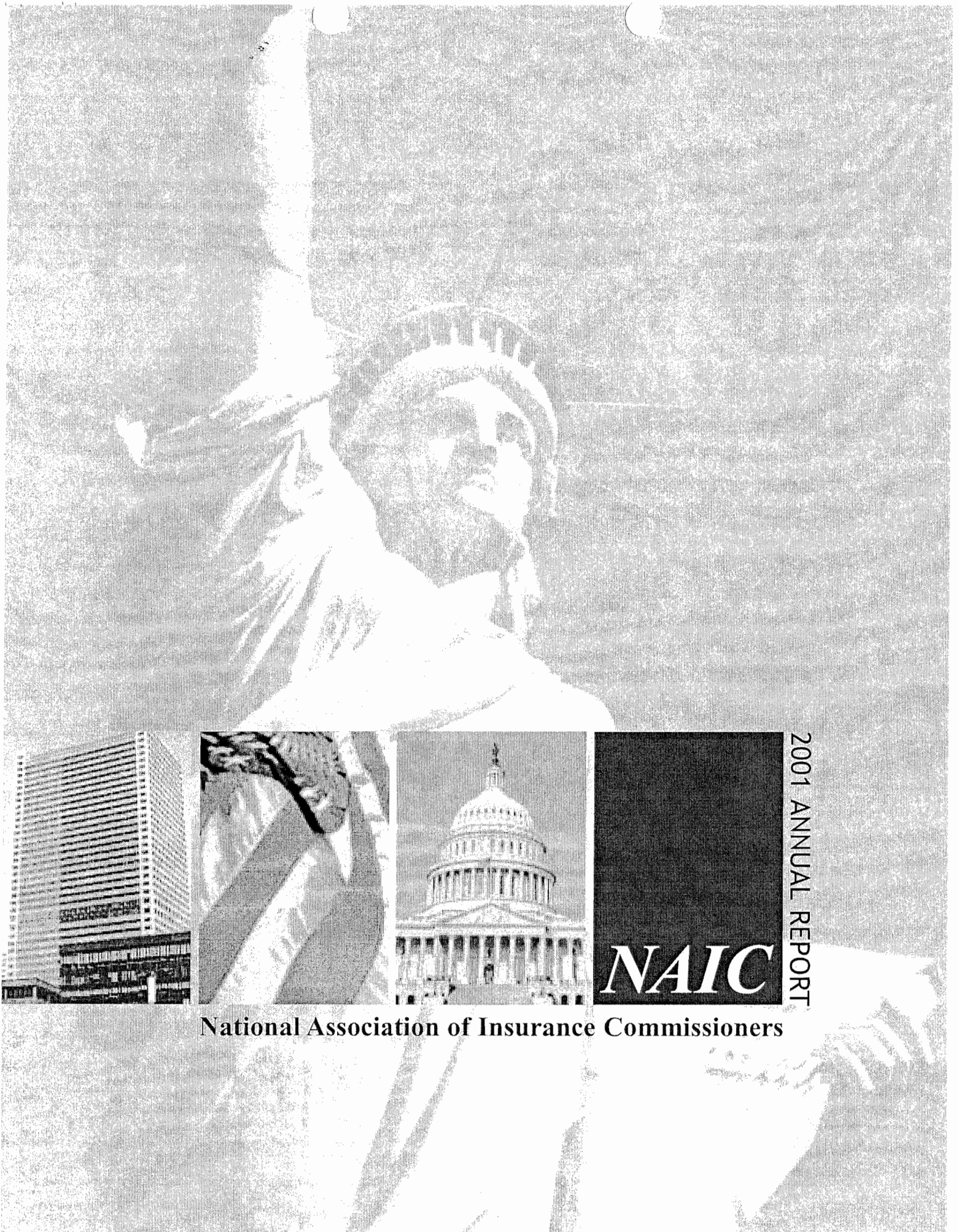
**Figure 5**  
**Risk-Based Capital Levels**

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Name of Risk-Based Capital (RBC) Level	Percentage of Authorized Control Level RBC
Company Action Level RBC	200 Percent
Regulatory Action Level RBC	150 Percent
Authorized Control Level RBC	100 Percent
Mandatory Control Level RBC	70 Percent

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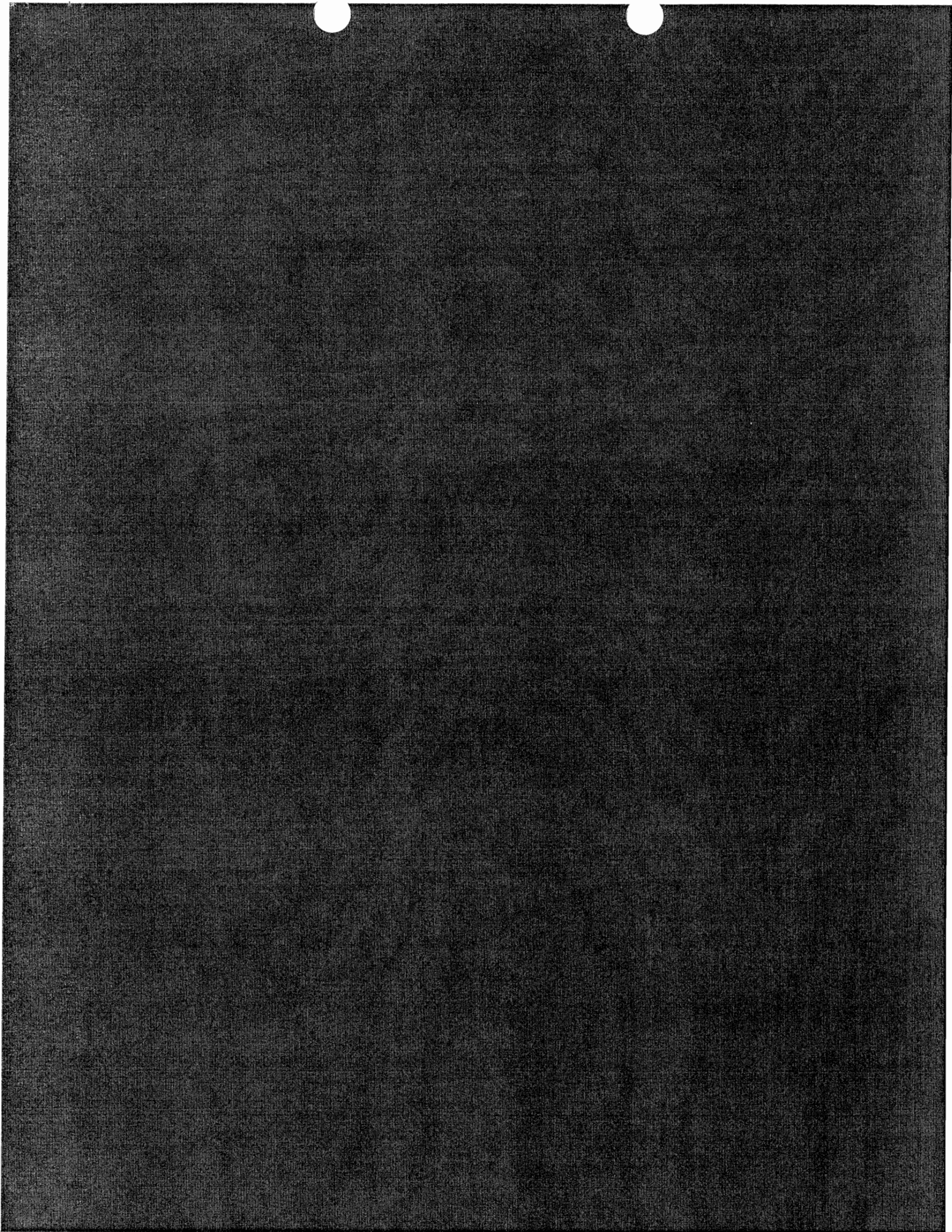




2001 ANNUAL REPORT

**National Association of Insurance Commissioners**





## *Table of Contents*

Mission Statement	2
Association Profile	3
Officers' Message	4
Letter from the Executive Vice President	6
Effect of Sept. 11 on the Insurance Industry	8
Progress on Modernization Initiatives	11
Responding to the NARAB Requirement	
Speed-to-Market Initiatives	
National Treatment and Coordination	
Implementing Privacy Protections	
Coordinating with Federal Regulators	
Consumer Protection and Anti-fraud	15
Consumer Protection and Anti-fraud Division	
Consumer Protection Working Group	
Consumer Information Source	
Market Conduct	
Anti-fraud	
Technology	18
SERFF	
UCAA	
NIPR	
International Issues	20
Financial Stability Forum	
International Association of Insurance Supervisors	
International Commission on Holocaust Era Insurance Claims	21
Health Care	22
Funded Consumers	23
NAIC Members	24
2001 NAIC Membership	
Past Members (Served in 2001)	
2001 NAIC Officers, Zone Officers	
Financial Statement	27
Organizational Chart	28

### *Mission Statement*

The mission of the NAIC is to assist state insurance regulators, individually and collectively, in serving the public interest and achieving the following fundamental insurance regulatory goals in a responsive, efficient and cost-effective manner, consistent with the wishes of its members;

Protect the public interest, promote competitive markets and facilitate the fair and equitable treatment of insurance consumers;

Promote the reliability, solvency and financial solidity of insurance institutions; and

Support and improve state regulation of insurance.

## *Association Profile*

The National Association of Insurance Commissioners is a voluntary organization of the chief insurance regulatory officials of the 50 states, the District of Columbia, American Samoa, Guam, Puerto Rico and the Virgin Islands. Formed in 1871, it is the oldest association of state officials.

The NAIC provides its members with a national forum through quarterly national meetings for discussing common issues and interests and for working cooperatively on regulatory matters that transcend the boundaries of their own jurisdictions. Every state regulator or the designated staff member serves on one or more NAIC committees, subcommittees or task forces.

Collectively, commissioners work to develop model legislation, rules, regulations and white papers to coordinate regulatory policy. The overriding objective is to protect consumers and help maintain the financial stability of the insurance industry.

The NAIC provides a wide range of services to support the work of NAIC committees, state insurance departments, state and federal



officials, and the public. The association maintains three offices. The Executive Headquarters is located in Kansas City, Mo. The two branch offices are the Securities Valuation Office (SVO), located in New York, N.Y., and the Federal and International Relations Office, located in Washington, D.C.

The NAIC is committed to using state-of-the-art information technology. To this end, the association maintains an extensive database and computer network linking all insurance departments.

The NAIC offers financial, actuarial, legal, computer, research, market conduct and economic expertise. Staff maintain database services, research and prepare standard and custom reports, develop uniform statutory financial statements, monitor federal activity, submit legal briefs, track alien insurers, create publications, conduct education and training programs, and much more. ★

## Officers' Message



2001 was a challenging, yet ground-breaking, year for NAIC members in moving toward our goal of modernizing state regulation of insurance. It was a year marked by unity – unity of purpose in tackling the post-Sept. 11 insurance issues and unity of progress in implementing our *Statement of Intent* initiatives.

We have come to a point where a number of the goals set out in the *Statement of Intent* have worked their way through the state legislative process. From the Producer Licensing Model Act to privacy regulations, NAIC members have proven a commitment to modernizing insurance regulation and protecting consumers – as we have done for the past 130 years.

These are new times, and we have faced many new challenges. There was continued talk of optional federal charter

legislation, which will most likely be introduced in Congress during 2002. However, we will remain focused on the future, because we believe consumers are – and will continue to be – best served by the states.

A striking example of this is the industry's response to the events of Sept. 11. We are pleased that the industry responded in a timely and compassionate manner. But never before has the role of state insurance regulators been more clear. The industry is solvent and able to pay claims due in great part to the fact that our laws and rules on solvency are working. It's the essence of what we do.

We convened the Commissioners Summit in Washington, D.C., in October, to discuss in greater depth the insurance issues related to Sept. 11. We had representatives from both houses

of Congress and the White House in attendance, in addition to primary insurers and reinsurers, and we were able to discuss these key issues in a public forum.

In addition to that, there were a host of other initiatives on which NAIC members showed unity of purpose and direction. We exceeded the Gramm-Leach-Bliley NARAB requirement more than a year before the deadline, with 39 states having enacted producer-licensing legislation. We implemented privacy protections in 49 states. We successfully launched CARFRA and processed our first multi-state filing within the self-imposed 45-day deadline.

We're using the technology in SERFF, which is in place in all jurisdictions, as expeditiously as possible. The Uniform Certificate of Authority Application and a new company licensing system are now being implemented. All 50 states and the District of Columbia have agreed to accept these uniform applications. In addition, we've made great advancements in the market conduct and anti-fraud arenas.

The House and the Senate have sought the NAIC's opinion and expertise on a wide range of

issues. Throughout the year, NAIC members testified and delivered remarks on our progress on the implementation of the GLBA and uniform agent-licensing initiatives, in addition to issues related to Sept. 11 and the International Commission on Holocaust Era Insurance Claims.

This is amazing progress, and we would like to thank every one of you who has assisted in these efforts. Based on what we've seen happen in the past 12 months, we are confident that 2002 will produce just as many, if not more, results.

There is no question that our past and future successes are tied to working together as we move forward. We have taken up the challenge to make the state system of insurance regulation better, and we will continue to make progress in implementing our vision. ★



A stylized, cursive signature of Kathleen Sebelius in white ink on a dark background.

**Kathleen Sebelius**  
2001 NAIC President  
and Kansas Insurance  
Commissioner



A stylized, cursive signature of Terri Vaughan in white ink on a dark background.

**Terri Vaughan**  
2001 NAIC Vice President and  
Iowa Insurance Commissioner



A stylized, cursive signature of Mike Pickens in white ink on a dark background.

**Mike Pickens**  
2001 NAIC Secretary-Treasurer  
and Arkansas Insurance  
Commissioner

## *Letter from the Executive Vice President*

**Dear Members:**

One of the most daunting challenges we faced as an association this year was dealing with the effects of Sept. 11 on our staff and their families. As you know, both the Washington, D.C., and New York City offices were directly affected by the terrorist attacks. Thankfully, not a single employee nor NAIC member was injured. As a nation – and as an association – we mourned for the lives that were lost as we tried to grapple with getting “back to business” in the days and weeks that followed.

The NAIC’s Securities Valuation Office, with a staff of 44, was located in the 7 World Trade Center building, which collapsed the afternoon of Sept. 11. After confirming the safety and well-being of every SVO employee, the association’s business-recovery plan went into full effect. A plan for re-opening the office at an alternate site was underway within hours.

SVO staff moved into their new offices Oct. 15, 2001. In the interim, a few SVO employees

were temporarily housed in donated office space in New York City, with many others working out of NAIC headquarters in Kansas City.

While the relocation of the SVO and the cancellation of our Fall National Meeting caused unexpected costs and a significant reduction in revenues, I am pleased to announce that, overall, NAIC revenues for 2001 exceeded expenses by \$2.5 million. This is due in no small part to drastic cost-cutting measures undertaken by NAIC’s management team, who slashed expenses in the areas of travel, professional services and external training. In addition, thanks to our collections department, we were able to collect \$700,000 in aged receivables.

I believe the NAIC has proven its value to you, our members, in our good stewardship of financial resources, our commitment to customer service and our ability to recruit and retain highly skilled and qualified staff. We look forward to continuing to support you in the ongoing efforts to modernize insurance regulation. ★



A handwritten signature in cursive script that reads "Catherine J. Weatherford".

2001 Executive Vice President  
Catherine J. Weatherford



## *In Memory of Neil D. Levin*

1954-2001

Neil D. Levin was the New York Superintendent of Insurance from April 1997 through April 2001. Neil was instrumental in leading the NAIC to create an international commission to secure unpaid insurance claims for Holocaust survivors and their heirs.

He was involved in NAIC efforts relative to the Securities Valuation Office reorganization, international issues, solvency regulation and a number of initiatives to improve state insurance regulation through technological and financial modernization. He was also a member of the National Insurance Producer Registry (NIPR) board of directors in 2001. Neil was a true leader, as well as a trusted friend and colleague.

Neil was but one of the thousands of lives lost, but his leadership reminds us how important our roles are in ensuring the solvency of this vast insurance industry and in ensuring consumer protection for all Americans.

In an act of remembrance, the NAIC donated \$10,000 to the Neil D. Levin Education Foundation. Our efforts in 2001 are dedicated to his memory.



## *Effect of Sept. 11 on the Insurance Industry*

The tragic events of Sept. 11, 2001, had a profound impact on our country, and that impact was acutely felt within the insurance community and the NAIC family.

The NAIC's Securities Valuation Office in New York was located in the 7 World Trade Center building, which collapsed the afternoon of Sept. 11. The efforts of the NAIC on that day were focused on verifying the well being of personnel in its New York and D.C. offices. Thankfully, no NAIC employees were injured.

The association's Business Recovery Plan was immediately implemented. After ensuring the safety of all employees, work began to find a new location for the SVO office, which later moved to the ninth floor of the World Apparel Center at 1411 Broadway in New York City.

### **Response**

The first responsibility of the nation's insurance regulators was to find out what happened and determine how it might affect America's policyholders and insurers. The second responsibility was to take whatever steps were necessary

to ensure the system continued to function smoothly and properly.

Regulators immediately engaged in a state-by-state review of the domestic industry to understand exposure relative to expected liabilities. Financial audits were performed to verify insurer solvency and assess insurers' ability to pay claims, which included property losses, business interruption claims, workers' compensations, health, life and auto insurance claims.

Regulators also watched the activities of foreign insurers very closely – notably those engaged in the global system of reinsurance – as their obligations are critical to American financial markets.

### **Committee Activities**

In order to allow the association's members time to address the many insurance issues involved with Sept. 11, the NAIC's Fall National Meeting was canceled. Regulators held more than 45 conference calls in October alone to discuss these issues.

The NAIC's International Insurers Department (IID) Plan of Operation Working Group



and the Reinsurance Task Force began immediate discussions on how best to monitor the activities of foreign insurers and reinsurers. Regulators gathered exposure data from all affected reinsurers and were in constant contact with Lloyd's of London and the London International Underwriting Association (IUA) to gather their exposure data.

Working in conjunction with these groups, the NAIC's Financial Analysis Working Group then designed a consistent and coordinated approach to assessing the financial impact on insurers with possible exposure to losses to ensure that companies were

able to not only endure these losses but also to remain standing strong for the future.

### **New Ad Hoc Groups**

In the beginning of October, NAIC members formed two ad hoc working groups to focus on market conduct, claims payment, and legal issues resulting from the Sept. 11 terrorist attacks.

The National Claims Handling Protocol Ad Hoc Group began focusing on claims resulting from the disasters. Members mobilized support staff from other states to assist the New York, Connecticut and New Jersey offices in the event they became inundated with consumer complaints or questions.

The Legal Issues Ad Hoc Group was developed to fulfill a two-fold mission. First, the group identified legal issues arising from the attack and developed a unified position and recommendations. Second, the group worked closely with federal authorities to enhance cooperation of the industry in the investigation.

### **Commissioners Summit**

State regulators were aware that the insurance industry could not withstand multiple events of this magnitude without harm to all

consumers. In response to this threat, they encouraged Congress to look at proposals for a federal backstop for terrorism insurance.

To assist in this effort, NAIC members adopted 19 guiding principles to use in evaluating possible federal terrorism insurance legislation. The principles were drafted by the Catastrophe Insurance Working Group and adopted by the full NAIC membership in October.

Later that month, the NAIC hosted a two-day summit involving regulators, industry representatives, Congressional members and key insurance department staff to discuss in greater depth the insurance issues related to Sept. 11, as well as to discuss how to best support and protect consumers.



*“I do believe the response of the insurance industry to the 9/11 events is significant testimony to the success of the state system. The industry is solvent and able to pay claims, due in no small part to the fact that our laws and rules on solvency and reserves are working.”*

*— Kathleen Sebelius,  
2001 NAIC President  
and Kansas Insurance  
Commissioner*

In the last three months of 2001, NAIC members provided testimony three times to Congress on the state of the insurance industry. They worked closely with industry, Congressional and Administration leaders, and federal financial services regulators to try to develop a mechanism for terrorism coverage to ensure the continued stability and solvency of the private market.

#### Next Steps

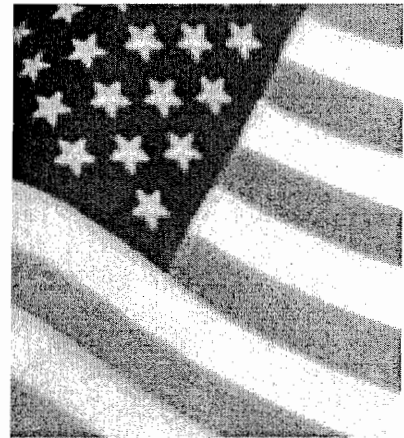
As Congress adjourned without action on a federal backstop for acts of terrorism, NAIC members came to an agreement regarding the wording of insurance policy exclusions for acts of terrorism. Working with a sense of unity and purpose, regulators agreed to approve some exclusions in order



to protect the solvency of companies in the commercial lines market and to ensure the continued availability of coverages other than terrorism. In addition, the Statistical Information Task Force was given the charge to collect information from states related to rate increases and changes in market conditions attributed to the events of Sept. 11. The task force will also begin to survey states regarding the rationale provided by insurers to support

revised rate levels for property/casualty insurance products.

In 2002, the nation's insurance regulators will continue to monitor the stability of the marketplace and work with Congress to find a solution to this issue that will protect the public interest and promote competitive markets. ★



*"Insurance products are meant to help people and businesses restore order from chaos. In this time of need, it is the insurance industry that will be called upon to deliver on the promises that it has made. The NAIC and its members plan to work closely with Congress and fellow regulators, as set forth in the Gramm-Leach-Bliley Act, so that the needs of Americans are met in a timely and compassionate way."*

*— Kathleen Sebelius, 2001 NAIC President and Kansas Insurance Commissioner*

## *Progress on Modernization Initiatives*

This year has been marked by unexpected obstacles and tragedy, but it has also been marked by the tremendous unity and cooperation state insurance regulators have shown. Without this unity, along with a strong commitment to increased efficiency and consumer protection, state regulators could not have accomplished critical progress on the initiatives outlined in the *Statement of Intent – The Future of Insurance Regulation*.

These initiatives will help move state insurance regulation beyond the specific requirements of the Gramm-Leach-Bliley Act (GLBA) by promoting uniformity and greater efficiency for agent and company licensing, while speeding up the process for bringing new products to market. To that end, following is an outline of where

the state insurance regulators stand on each of the *Statement of Intent* initiatives:

### **Responding to the NARAB Requirement**

Even before the passage of GLBA, the NAIC was working toward the goal of making the agent-licensing process more efficient and uniform. The NAIC shares many of the same objectives as the National Association of Registered Agents and Brokers (NARAB) provisions contained in GLBA. These provisions require that at least 29 states meet either the NARAB reciprocity or uniformity requirement by November 2002.

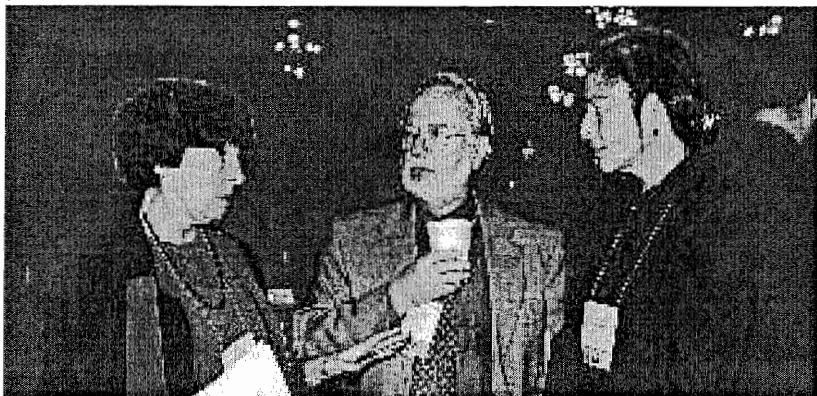
Through the ambitious efforts of the states in adopting the NAIC's Producer Licensing Model Act (PLMA), more than the requisite number of states are on track to



meet the NARAB reciprocity standards for producer licensing. As of January 2002, 39 states had enacted the PLMA. However, reciprocity among the states for non-resident agent licensing is only the first step. Through nationwide enactment of the PLMA, state insurance regulators are committed to achieving their ultimate goal of uniformity in producer licensing.

In addition to helping the states meet the requirements of NARAB reciprocity, the PLMA creates uniformity in agent-licensing procedures, defines exceptions to licensing, simplifies the licensing process and promotes the use of the National Insurance Producer Registry (NIPR) and the Producer Database (PDB). The PLMA also preserves states' rights and eliminates retaliatory fees.

Besides implementing the PLMA, several states have begun to process non-resident licensing applications electronically through NIPR.



### Speed-to-Market Initiatives

State insurance regulators recognize that traditional methods of insurance regulation need to be modernized to allow the insurance industry to keep pace with competitors and ensure that regulators are able to serve the best interests of insurance consumers. For this reason, regulators remain strongly committed to the product speed-to-market modernization initiative with unprecedented consensus.

To best address speed-to-market challenges, the NAIC appointed two working groups in 2000: the Coordinated Advertising Rate and Form Review Authority (CARFRA) Working Group and the Improvements to State-Based Systems Working Group.

The Improvements to State-Based Systems plan calls for all insurance products not reviewed by CARFRA



(including all property/casualty products and many life and health products) to be reviewed within a 30-day time period. The plan also calls for the implementation of an informational filing system, or competitive rating system, for all commercial lines rates. The plan also details the following process improvements:

- Development of state filing transmittal and review standards checklists
- Greater uniformity and consistency among state filing requirements
- Agreement to a review and compliance timeframe of 30 days
- Full implementation of the System for Electronic Rate and Form Filings (SERFF)

In February 2001, the NAIC membership appropriated \$1 million to fund expedited implementation of the SERFF program. SERFF is the direct result of a number of states and insurance companies seeking to improve the performance of state-based regulation by automating rate and form filing. The system is also integral in the

CARFRA filing process, enabling reviewers to communicate and evaluate filings more efficiently.

By December 2001, all 50 states and the District of Columbia were licensed to use SERFF. In the month of October alone, 1,000 filings were processed through SERFF. In addition, all 50 states and the District of Columbia have implemented rate and form-filing checklists and review standards, which are generally linked to the NAIC Web site.

The Improvements to State-Based Systems Working Group also developed uniform filing transmittal documents that have been implemented in many states. They are currently working on a product-coding system that will provide for common filing metrics across the country.

The limited launch of CARFRA, which began May 1, 2001, allows a single point of filing with coordinated regulatory review based on an agreed upon set of national product standards for certain products. Early products for the limited launch include annuities, Medicare supplemental policies and term life.

CARFRA was launched in 10 states as a coordinated product

filing and approval review mechanism. The first CARFRA filing was approved by the limited-launch states within the self-imposed 45-day deadline. The CARFRA Working Group continues to add new product standards and states to the limited launch.

### **National Treatment and Coordination**

As a component of the *Statement of Intent*, the National Treatment and Coordination Working Group was established to identify issues relating to multistate insurance company transactions. Presently, the working group is focused on bringing greater uniformity and coordination in the areas of company licensing and company acquisitions and mergers. Consistent with the other initiatives of the *Statement of Intent*, all insurers, U.S. and international, are expected to benefit from these efforts.

The Uniform Certificate of Authority Application (UCAA), a company licensing system that expedites the review process of a new state license, was designed and implemented in 2001. All jurisdictions have agreed to accept licensing applications according to UCAA system forms and guidelines.

Work also progressed on a "Form A" database designed to facilitate information sharing on acquisition and merger filings. The working group viewed a prototype of the Form A database in June and plans a rollout of the database in March 2002. This database, in conjunction with other related work will help ensure effective communication among states on merger and acquisition filings, as well as provide regulatory efficiencies to the insurance industry.

### **Implementing Privacy Protections**

A year and a half after adoption of the NAIC model privacy regulation, 48 states and the District of Columbia have laws and/or regulations that meet GLBA's privacy standards – and discussions among the states about uniform interpretation got underway in 2001.

*A year and a half after adoption of the NAIC model privacy regulation, 48 states and the District of Columbia have laws and/or regulations that meet GLBA's privacy standards — and discussions among the states about uniform interpretation got underway in 2001.*



In order to pioneer next steps in the implementation process, the Privacy Working Group was reconstituted during the association's Summer National Meeting. The working group was formally re-established in an effort to increase dialogue among regulators and interested parties. Improved communication is critical now that most states have privacy protections in place and are moving to the next phase involving interpretation and enforcement.

In 2001, the Privacy Notice Content Task Force was formed to draft sample language to guarantee that privacy notices are understandable to consumers, while ensuring for industry operational uniformity and compliance with the requirements of the NAIC model privacy regulation. The principal goal of this new working group is to provide a forum for discussing privacy-related issues and



developing consensus regarding how the regulations are meant to work.

### **Coordinating with Federal Regulators**

Improved cooperation and communication with federal financial services regulators is critical in the wake of GLBA enactment and the convergence of the financial services industries.

NAIC members have long recognized the importance of stepping up this federal-state regulatory dialogue and over the past several years have held a series of high-level meetings for NAIC officers and members with the top federal regulators from the Office of the Comptroller of the Currency (OCC), Office of Thrift Supervision (OTS), Federal Deposit Insurance Corporation (FDIC) and Federal Reserve.

Ongoing regulator-to-regulator consultations have also been held to discuss examination procedures and enhance the development of information exchange with respect to regulatory trends in the changing financial services marketplace. In addition to examination procedures, NAIC members continue to meet with leading federal regulators to discuss insurance sales rules,



debt-cancellation agreements and mortgage insurance issues.

The development of regulatory cooperation agreements with federal agencies has been a high priority for NAIC members. These model agreements provide for the sharing of relevant regulatory information, including information about examinations, enforcement and consumer protections. They also include provisions to ensure the protection of confidential information.

In 2000, the NAIC approved a model regulatory cooperation agreement with the OTS. By the end of 2001, 45 states had signed agreements with the OTS, using this model as a basis. In early 2001, the NAIC approved model agreements with the OCC, FDIC and Federal Reserve. By the end of 2001, 23 states had signed agreements with the OCC, 31 states had agreements with the FDIC and eight states had agreements with the Federal Reserve. More states are expected to sign agreements with these agencies in 2002. ★

## *Consumer Protection and Anti-fraud*

The *Statement of Intent* declares that the primary goal of state insurance regulators is to protect insurance consumers. NAIC members recognize that consumers, as well as companies, are well served by efficient, market-oriented regulation of the business of insurance. In order to better meet this commitment, the emphasis on consumer protection was renewed in 2001.

### **Consumer Protection**

#### **Consumer Protection and Anti-fraud Division**

In April, the NAIC formed the Consumer Protection and Anti-fraud Division. The division's mission is to assist state insurance regulators in their efforts to protect consumers, address fraudulent activities and supervise insurance market-related



activities in a responsive, efficient and cost-effective manner, consistent with the wishes of the NAIC members.

The division is responsible for coordinating the NAIC's activities to attain fair and equitable treatment for insurance consumers. The department is also instrumental in facilitating the continual improvement of the underwriting and market practices of insurers and producers, and assisting in the market conduct examination process, including the facilitation of market conduct examinations and interstate communication.

As the primary liaison for consumers to provide input on insurance regulation, the division also aids in the coordination of anti-fraud activities between the states and with federal authorities when appropriate.

#### **Consumer Protection Working Group**

At the Spring National Meeting, the Consumer Protection Working Group was appointed to focus specifically on consumer issues. The ultimate goal of this new working group is protecting



consumers while holding insurance companies accountable.

The working group formed a sub-group, which focused on creating an action plan for consumer access to the consumer-complaint database, developing a system for consumer access to insurers' financial information and developing a questionnaire for state insurance departments on private and public enforcement statutes, rules and regulations.

#### **Consumer Information Source**

Late in 2001, members of the Consumer Protection Working Group successfully launched an interactive Web tool, the Consumer Information Source (CIS), specifically created for consumer research of company complaints and financial data.

CIS allows consumers to locate basic information about a specific insurance company, including amount of premiums written,





assets, liabilities and licensing information. The Web site also allows consumers to file consumer complaints and review statistical information on previously resolved complaints against a company.

The launch of the new Web site was the conclusion of a cooperative effort by the working group's task force of state insurance regulators along with consumer and industry representatives.

**Market Conduct**

In April 2001, the Market Affairs Department was assimilated into the new Consumer Protection and Anti-fraud Division. This transition has helped better define the market conduct examination initiatives and the market regulatory initiatives of the NAIC.

The Market Regulation & Consumer Affairs Committee continued to

examine the focus, structure and implementation of state market conduct examination efforts.

In addition, the committee launched new initiatives in 2001, including the development of a model market analysis program, priority-focused use of regulatory resources and a zone approach to market conduct examinations.

With greater emphasis placed on more uniform and efficient insurance regulation, the committee coordinated a national privacy compliance survey focusing on company compliance with the new privacy protection provisions of GLBA.

The Market Regulation Task Force continued to make improvements to the NAIC *Market Conduct Examiners Handbook* with the adoption of new procedures for conducting long-term care examinations.

And, the NAIC offered the first regulator-only Consumer Assistance Training Program to help states identify the best practices and uniform procedures for providing consumer assistance.

**Anti-fraud**

It is estimated that financial fraud costs the financial services

industry more than \$100 billion each year, most of which is passed on to consumers through higher prices. In Congressional testimony, regulators outlined specific ways state and federal financial regulators could work together to protect consumers and fight insurance fraud. Regulators also proposed ways of achieving this goal, which included access to FBI and National Association of Securities Dealers (NASD) databases and confidentiality in the sharing of regulatory information.

In May, NAIC officers wrote a letter to the House Financial Services Committee regarding H.R. 1408, the Anti-fraud Network Act. Members urged Congress to authorize insurance regulators greater access to critical FBI law enforcement information. Regulators also



expressed specific concern regarding the bill's FBI provisions, noting that the bill imposes an unnecessary layer of federal regulation and bureaucracy to screen data supplied by the FBI before it is transmitted to state regulators. The letter was effective in getting that provision of H.R. 1408 changed.

H.R. 1408 was passed by the House of Representatives Nov. 6, 2001, and moved into the Senate for consideration.

Anticipating possible access to FBI databases, the NAIC debuted the prototype of a new electronic system for fingerprint background checks. Unveiled during the 2001 E-Regulation Conference, the LiveScan Electronic Fingerprint Technology would be used to help regulators access FBI criminal history information once Congress gives approval. The LiveScan Fingerprint technology is just one more way NAIC members are working together to make the licensing process more efficient and effective for agents, and safer for consumers.

The LiveScan Fingerprint technology would reduce the turn around time for FBI fingerprint results from several months to a couple of days, greatly



expediting the licensing process and helping prevent crimes against insurance consumers.

In November, the NAIC Anti-fraud Task Force announced the creation of a new subgroup, the NAIC/NASAA Enforcement Coordination Subgroup. The objective of the group is to further enhance investigative and fraud-fighting cooperation between NAIC, the North American Securities Administrators Association (NASAA) and the individual state insurance and securities regulators. ★



*CIS allows consumers to locate basic information about a specific insurance company, including amount of premiums written, assets, liabilities and licensing information.*

## Technology

Fueled by enhanced technology and globalization, the world financial markets are undergoing rapid changes. In order to protect and serve more sophisticated, but also more informed insurance consumers of the future, state insurance regulators are committed to modernizing insurance regulation through technology to meet the realities of an increasingly dynamic, and internationally competitive, financial services marketplace.

### SERFF

In 2001, SERFF reached many important milestones in advancing the insurance industry's speed-to-market filing process nationwide. State reviewers use SERFF to facilitate the management, analysis, disposition and storage



of filings. The application enables insurers to submit rate and form filings electronically to state reviewers, reducing the time and cost involved in making regulatory filings.

Early in 2001, the SERFF board of directors eliminated license fees for SERFF. By the end of the year, all 50 states and the District of Columbia were licensed for SERFF, with 42 jurisdictions accepting rate and form filings. For states using SERFF, the average filing turnaround time decreased to 16 days – with many filings approved in one to two days. In addition, 94 percent of filings received by SERFF were approved without the need for additional correspondence between company and regulator.

More than 369 insurance companies were on board with SERFF by December 2001. Annual SERFF filings totaled nearly 3,700.

The SERFF application also received special recognition in the NASCIO Recognition Awards for Outstanding Achievement in the Field of Information Technology. NASCIO – a national association representing state chief information officers – gives annual recognition to state



information technology programs and systems that have created cost-effective, innovative solutions in the operation of state government.

### UCAA

NAIC members announced in October the launch of a pilot program that automates applications for expansion licenses using the Uniform Certificate of Authority Application (UCAA). As of December 2001, 49 states and the District of Columbia were participating in the UCAA program.

UCAA, part of the NAIC's Accelerated Licensure Evaluation and Review Techniques (ALERT) program, was developed in 1997. Previously, the 50 states and the District of Columbia had separate application processes.

The goal of UCAA is to provide a streamlined and uniform application process for insurers seeking to do business in multiple



states. Although initially focused on expansion licenses, the automated UCAA program will eventually include amendments to a company's certificate of authority, such as additions to the lines of business, name changes, re-domestications and primary applications.

A centralized database hosted by the NAIC serves as a routing mechanism through which applications are submitted. All states to which the applicant applies will be able to access the information electronically using this database.

### **NIPR**

Incorporated in 1996, the National Insurance Producer Registry (NIPR) is the premier public-private partnership supporting the re-engineering and streamlining of the insurance producer-licensing process through uniformity for the benefit of consumers, industry and regulators.

NIPR, a non-profit affiliate of the NAIC, also continues to develop and implement the Producer Database (PDB), Electronic Appointments/Terminations (formerly PIN) and Electronic Non-Resident Licensing (NRL).

The PDB is an electronic database consisting of information relating to insurance agents and brokers (producers). The PDB links participating state regulatory licensing systems into one common repository of producer information. The PDB allows immediate access to detailed disciplinary history, immediate electronic notification of administrative action, and the ability to verify licensure and good standing in all participating states. There are currently 3 million producers listed on the database.

Electronic Appointments/Terminations is a communication network that links state insurance regulators with the entities they regulate to facilitate the electronic exchange of producer information. Data standards are in development for the exchange of license application, license renewal, appointment and termination information. The key benefits include reduction in

paperwork and data entry, development of national standards for electronic transmission of licensing data and a faster turnaround time.

NIPR's efforts in the region of electronic non-resident licensing (NRL) also continued in 2001. NRL allows producers to quickly and easily obtain a license in a non-resident state. Kansas and North Carolina were among the states added to the NRL efforts in 2001. ★



## *International Issues*

On the global front, state regulators continued addressing the issues that affect consumers throughout the international market.

### **Financial Stability Forum**

In an effort to achieve global stability in financial markets, the NAIC, together with the U.S. Department of the Treasury and several other offices, announced the completion of a series of self-assessments relating to compliance with international financial standards. The NAIC completed the self-assessment based on principles and standards of insurance supervision created by the International Association of Insurance Supervisors (IAIS).

The assessments cover the 12 key standards highlighted by the Financial Stability Forum (FSF) in its Compendium of Standards.



The United States is a member of the FSF and helped identify these standards. The NAIC worked closely with the federal government on insurance supervision-related issues raised by the FSF, including preventing money laundering and problems associated with offshore financial centers.

### **International Association of Insurance Supervisors**

Established in 1994, the IAIS represents insurance supervisory authorities of nearly 100 jurisdictions to promote cooperation among insurance regulators, set international standards for insurance supervision and coordinate work with regulators in the other financial sectors and international financial institutions.

As part of its mission to promote global financial stability, the NAIC continues to take an active role in IAIS, the world's only global association of insurance regulators. The NAIC participates as a permanent member of the IAIS



Executive Committee and as chair of several subcommittees and task forces, in addition to actively participating in the IAIS work on areas such as reinsurance, solvency, accounting and electronic commerce.

In addition to working with the IAIS, the NAIC plays an active role in other efforts to enhance the supervision of insurance markets worldwide. For example, in 2001, NAIC members consulted with finance and insurance supervisory officials from Vietnam, China, Brazil, Japan, India, Egypt and Poland to exchange information and provide technical assistance. ★

## ICHEIC

In 1998, the NAIC established the International Commission on Holocaust Era Insurance Claims (ICHEIC) in cooperation with several European insurance companies, European regulators, representatives of several Jewish organizations and the State of Israel. The Commission is charged with establishing a just process that will expeditiously address the issue of unpaid insurance policies issued to victims of the Holocaust.

ICHEIC established a claims-processing office in London, and NAIC members continued to reach out to potential claimants in the United States to make them aware of the Holocaust-era insurance claims payment process.

In an effort to address ongoing concerns with part of the process, on Sept. 5, 2001, NAIC members unanimously adopted a resolution expressing dissatisfaction with the positions taken by the German Foundation in negotiations regarding payment of Holocaust-era insurance claims. The resolution called on states to consider a broad range of actions in response – including reconsideration of safe harbor provisions, holding informational

hearings and making relevant court filings.

To encourage the cooperation of the German Foundation, the NAIC resolution stated: "Until this matter is resolved, individual states should, as appropriate, take any or all of the following steps as allowed by law: Re-evaluate the formal or informal 'safe harbor' provisions given to affected insurers; hold hearings about the German Foundation-ICHEIC negotiations and also about the progress made by ICHEIC member companies in processing and paying legitimate claims; and make filings in relevant court cases involving the matter of unpaid Holocaust-era insurance claims."

In December 2001, regulators once again demonstrated a unified front to strongly urge Holocaust survivors and heirs to submit Holocaust-era insurance claims to the ICHEIC by the filing deadline. ★



*As part of its mission to promote global financial stability, the NAIC continues to take an active role in IAIS, the world's only global association of insurance regulators.*

## Health Care

To protect consumers, NAIC members have been regulating health insurers and managed care entities for many years. The states have taken this role seriously. They have worked diligently to protect consumers' health information privacy. They have enacted patient protections for consumers in individual and group plans. And, they have established an infrastructure to enforce these rights.

In keeping with this tradition, NAIC members remained active in health insurance issues at the state and federal level during 2001. In particular, state insurance regulators were pivotal in thwarting efforts to add Association Health Plan (AHP) legislation to the federal Patients' Bill of Rights and in including amendments that would allow states to retain their laws through a certification process.



NAIC members testified before Congress on issues related to health insurance "patient protections." In doing so, NAIC members reiterated that Congress should:

- 1) Recognize that the states have already enacted patient protection laws;
- 2) Give states the greatest amount of flexibility in preserving and enforcing patient protections;
- 3) Give states the same amount of deference regarding internal and external review processes as the other patient protections; and
- 4) Recognize that the states have an extensive infrastructure in place to protect consumers.

Regarding the privacy of consumers' health information, NAIC members were actively involved in the refinement of the U.S. Department of Health and Human Services' (HHS) health information privacy regulation. The NAIC offered guidance and



submitted comment letters regarding the HHS regulation – specifically, NAIC members strongly opposed inclusion of the regulation's marketing exception. During the NAIC's Winter National Meeting, the Health Information Privacy Working Group was created in order to give guidance to the states and discuss issues related to this HHS regulation.

In order to protect consumers, NAIC members issued an alert that warned consumers and agents about entities claiming to be "ERISA plans" or "union plans" and, therefore, exempt from state regulation. The alert included tips to help consumers analyze whether a health plan is legitimate and being sold by a licensed insurer. ★

## *Funded Consumers*

The year 2001 marked the tenth anniversary of the NAIC's Consumer Liaison Committee. Consumer representatives have played an active role and brought a unique perspective to regulators' many deliberations and discussions over the past 10 years — and this year was no exception.

During 2001, consumer liaison representatives actively participated in a variety of projects at the NAIC, including Consumer Protection Working Group activities; recommendations for revisions to the Property and Casualty Model Rating Law; GLBA Working Group's activities, most notably the Improvements to State Based Systems Working Group and National Treatment Working Group; development of the Credit Personal Property



Model Act; discussion of regulations related to small-face amount life insurance contracts; issues related to the federal intervention in terrorism insurance and federal aid to insurers; credit insurance and predatory lending; senior issues such as Medicare supplement insurance; and NAIC activities related to debt-cancellation agreements.

Each year, the NAIC sends applications to more than 350 consumer representatives. From the applications received, the Consumer Board of Trustees selects the consumer representatives who will receive funding to participate in NAIC meetings for one year. The NAIC budgets \$60,000 to reimburse the selected consumer representatives for NAIC meeting expenses. In 2001, this budget was increased \$1,500 in order to fund one guest speaker for the Spring National Meeting. ★



Following are the 2001 NAIC/ Funded Consumer Representatives:

- Sonia L. Alleyne, Massachusetts Affordable Housing Alliance
- Leila T. Amirhamzeh, New Jersey Citizen Action
- Brendan M. Bridgeland, Center for Insurance Research
- Birny Birnbaum, Center for Economic Justice
- Bonnie Burns, California Health Advocates
- Pamela J. Byrnes, Connecticut Citizen Research Group
- Brenda J. Cude, Dept. of Housing & Consumer Economics, University of Georgia
- Deborah Goldberg, Center for Community Change
- J. Robert Hunter, Consumer Federation of America
- Bonita A. Kallestad, Mid-Minnesota Legal Assistance
- Karroll Kitt, Assn. of Financial Counseling & Planning Education, University of Texas at Austin
- Brian Lindberg, Consumer Coalition for Quality Health Care
- Jeffrey L. Williams, Legal Aid of Western Missouri



## *NAIC Members*

### The 2001 NAIC Membership

**Bob Lohr**  
Director, Alaska  
Division of Insurance

**David Parsons**  
Commissioner, Alabama  
Department of Insurance

**Mike Pickens**  
Commissioner, Arkansas  
Department of Insurance

**Elisara T. Togiai**  
Insurance Commissioner,  
American Samoa Government

**Chuck Cohen**  
Director, Arizona  
Department of Insurance

**Harry W. Low**  
Commissioner, California  
Department of Insurance

**William J. Kirven III**  
Commissioner, Colorado  
Division of Insurance

**Susan F. Cogswell**  
Commissioner, Connecticut  
Department of Insurance

**Larry Mirel**  
Commissioner, Department of  
Insurance & Securities Regulation,  
Government of the  
District of Columbia

**Donna Lee H. Williams**  
Commissioner, Delaware  
Department of Insurance

**Tom Gallagher**  
Commissioner, Florida  
Department of Insurance

**John Oxendine**  
Commissioner, Georgia  
Department of Insurance

**George V. Cruz**  
Commissioner, Department of  
Revenue & Taxation, Insurance  
Branch, Government of Guam

**Wayne Metcalf**  
Commissioner, Hawaii  
Insurance Division

**Terri Vaughan**  
Commissioner, Iowa  
Division of Insurance

**Mary L. Hartung**  
Director, Idaho  
Department of Insurance

**Nathaniel S. Shapo**  
Director, Illinois  
Department of Insurance

**Sally McCarty**  
Commissioner, Indiana  
Department of Insurance

**Kathleen Sebelius**  
Commissioner, Kansas  
Department of Insurance

**Janie A. Miller**  
Commissioner, Kentucky  
Department of Insurance

**J. Robert Wooley**  
Acting Commissioner, Louisiana  
Department of Insurance

**Linda Ruthardt**  
Commissioner, Massachusetts  
Division of Insurance

**Steven B. Larsen**  
Commissioner, Maryland  
Insurance Administration

**Alessandro Iuppa**  
Superintendent, Maine  
Bureau of Insurance

**Frank Fitzgerald**  
Commissioner, Michigan Office  
of Financial and Insurance Services

**James C. Bernstein**  
Commissioner, Minnesota  
Department of Commerce

**Scott Lakin**  
Director, Missouri  
Department of Insurance

**George Dale**  
Commissioner, Mississippi  
Insurance Department

**John Morrison**  
Commissioner, Montana  
Department of Insurance

**Jim Long**  
Commissioner, North Carolina  
Department of Insurance

**Jim Poolman**  
Commissioner, North Dakota  
Department of Insurance

**Tim Wagner**  
Director, Nebraska  
Department of Insurance

**Paula Rogers**  
Commissioner, New Hampshire  
Department of Insurance

**Donald Bryan**  
Acting Commissioner, New Jersey  
Department of Insurance

**Eric P. Serna**  
Superintendent, New Mexico  
Department of Insurance

**Alice Molasky-Arman**  
Commissioner, Nevada  
Division of Insurance

**Gregory V. Serio**  
Superintendent, New York  
Department of Insurance

**Lee Covington**  
Director, Ohio  
Department of Insurance

**Carroll Fisher**  
Commissioner, Oklahoma  
Department of Insurance

**Joel S. Ario**  
Insurance Administrator, Oregon  
Insurance Division

**Diane Koken**  
Commissioner, Pennsylvania  
Insurance Department

**Fermin M. Contreras-Gomez**  
Commissioner, Puerto Rico  
Department of Insurance

**Alfonso E. Mastrostefano**  
Superintendent, Rhode Island  
Insurance Division

**Ernst Csiszar**  
Director, South Carolina  
Department of Insurance

**Darla L. Lyon**  
Director, South Dakota  
Division of Insurance

**Anne Pope**  
Commissioner, Tennessee  
Department of Commerce  
& Insurance

**Jose Montemayor**  
Commissioner, Texas  
Department of Insurance

**Merwin Stewart**  
Commissioner, Utah  
Department of Insurance

**Alfred W. Gross**  
Commissioner, State Corporation  
Commission, Bureau of Insurance,  
Commonwealth of Virginia

**Gerard (Luz) James, II**  
Lieutenant Governor/Commissioner,  
Division of Banking & Insurance,  
Virgin Islands

**Elizabeth R. Costle**  
Commissioner, Vermont Division  
of Insurance

**Mike Kreidler**  
Commissioner, Washington Office  
of the Insurance Commissioner

**Connie O'Connell**  
Commissioner, Wisconsin Office  
of the Commissioner of Insurance

**Jane L. Cline**  
Commissioner, West Virginia  
Department of Insurance

**John P. McBride**  
Commissioner, Wyoming  
Department of Insurance

**Past Members  
(Served in 2001)**

**Joseph T. Duenas**  
Commissioner, Department of  
Revenue and Taxation, Insurance  
Branch, Government of Guam

**Keith Wenzel**  
Director, Missouri  
Department of Insurance

**Don Letherer**  
Superintendent, New Mexico  
Department of Insurance

**Karen L. Suter**  
Commissioner, New Jersey  
Department of Insurance

**Neil D. Levin**  
Superintendent, New York  
Department of Insurance

**Juan Antonio Garcia**  
Commissioner, Puerto Rico  
Department of Insurance

**Executive Committee**

**Kathleen Sebelius, Chair**  
Kansas

**Terri Vaughan, Vice-Chair**  
Iowa

**Mike Pickens, Secretary-Treasurer**  
Arkansas

**Jim Long,**  
Most Immediate Past President  
North Carolina

**Northeastern Zone**

**Diane Koken, Chair**  
Pennsylvania

**Alfonso Mastrostefano, Vice-Chair**  
Rhode Island

**Donna Lee H. Williams, Secretary**  
Delaware

**Southeastern Zone**

**Anne Pope, Chair**  
Tennessee

**Tom Gallagher, Vice-Chair**  
Florida

**Alfred W. Gross, Secretary**  
Virginia

**Midwestern Zone**

**Nathaniel S. Shapo, Chair**  
Illinois

**Lee Covington, Vice-Chair**  
Ohio

**Sally McCarty, Secretary**  
Indiana

**Western Zone**

**William J. Kirven III, Chair**  
Colorado

**Merwin Stewart, Vice-Chair**  
Utah

**Bob Lohr, Secretary**  
Alaska

## Financial Statement

National Association of Insurance Commissioners  
Statement of Financial Position (including JIR, Zones,  
SERFF, 2301 McGee, Education Fund, and FDR)

As of December 31, 2001

### Assets

Cash and Cash Equivalents	\$ 6,823,905
Receivables, Net	5,366,619
Interest Receivable	141,745
Prepaid Expenses	3,199,989
Inventory	925,483
Investments	15,400,085
Furniture & Equipment (Net)	13,199,119
<b>Total Assets</b>	<b>\$ 45,056,945</b>

### Liabilities and Unrestricted Net Assets

#### Liabilities:

Accounts Payable	\$ 9,055,488
Deferred Revenue	1,073,208
<b>Total Liabilities</b>	<b>\$ 10,128,696</b>

#### Unrestricted Net Assets:

Allocated Unrestricted Net Assets (1)	32,876,165
Unallocated Unrestricted Net Assets	2,052,084
<b>Total Unrestricted Net Assets</b>	<b>\$ 34,928,249</b>
<b>Total Liabilities and Unrestricted Net Assets</b>	<b>\$ 45,056,945</b>

(1) Allocated Unrestricted Net Asset for NAIC \$24,903,096 (six months of Budgeted Operating Expenses), JIR \$157,059, Zones \$789,730, Education Fund \$864,210, SERFF (\$1,309,393), 2301 McGee \$2,384,267, and Financial DataBase Re-engineering \$5,087,196.

## Schedule of Revenues and Expenses

Year Ended December 31, 2001

### Revenue:

Database Fees	\$ 20,358,959
Publications and Subscriptions	12,613,701
Services	7,266,956
Other Income	2,361,833
State Assessments	1,656,994
Meetings Registration Fees	1,502,675
Education and Training	996,582
Investment Income	211,365
<b>Total Revenue</b>	<b>\$ 46,969,065</b>

### Expenses:

Salaries	\$ 20,302,086
Rental and Maintenance	5,760,336
Employee Benefits	5,375,298
Professional Services	4,726,112
Depreciation/Amortization	3,619,138
Office Services	1,386,390
Travel and Examiner Team	1,346,061
Printing	1,133,410
Education and Training	1,117,155
Bad Debt Expense	840,918
Meetings	721,289
Temporary Personnel	544,985
Other Expenses	448,696
Insurance and Taxes	227,464
<b>Total Expenses</b>	<b>\$ 47,549,338</b>

**Total Revenues over/under Expenses (1)** (\$580,273)

(1) Total Revenues over/(under) Expenses for NAIC \$2,491,885, JIR (\$61,636), Zones (\$41,588), Education Fund (\$420,988), SERFF (\$1,280,501), 2301 McGee (\$454,179), and Financial DataBase Re-engineering (\$813,266).

## *NAIC Organizational Chart*

This chart shows the organizational structure of the three NAIC offices. Each division director is named.

**Catherine J. Weatherford**  
Executive Vice President  
& Chief Executive Officer

**Judy Lee**  
Chief Operations Officer  
Kansas City

**Andrew Beal**  
General Counsel  
Kansas City

**Gary Gummig**  
Chief Information Officer  
Kansas City

**Eric Nordman**  
Director of Research  
Kansas City

**David Wetmore**  
Director of Federal &  
International Relations  
Washington, D.C.

**Chris Evangel**  
Managing Director,  
Securities Valuation Office  
New York City

**Chlora Lindley-Myers**  
Director of Consumer  
Protection & Anti-fraud  
Kansas City

**Jeff Johnston**  
Director of Financial  
Reporting & Analysis  
Kansas City

**Brady Kelley**  
Director of Financial Services  
Kansas City