Executive Summary
NAIC 2020 Budget

National Association of Insurance Commissioners

About the NAIC

The National Association of Insurance Commissioners (NAIC) is the U.S. standard-setting and regulatory support organization created and governed by the chief insurance regulators from the 50 states, the District of Columbia, and five U.S. territories.

Through the NAIC, state insurance regulators establish standards and best practices, conduct peer reviews, and coordinate their regulatory oversight activities. NAIC staff supports these efforts and represents the collective domestic and international views of state insurance regulators.

NAIC members, together with the central resources of the association, form the national system of state-based insurance regulation in the U.S. NAIC members are elected or appointed state government officials who, along with their departments and staff, regulate the conduct of insurance companies and agents/brokers in their respective jurisdictions.

The NAIC's annual budget supports the many valuable services and benefits provided to state insurance regulators, insurance consumers, and the insurance industry. Each year, the budget is developed with the goal of enabling the membership to accomplish its key strategic priorities.

The 2020 budget incorporates funding for the final year of the NAIC's three-year strategic plan, *State Ahead*. The plan articulates a comprehensive vision for the future of state insurance regulation and how the NAIC can help the membership stay ahead of the curve in a rapidly evolving marketplace. The budget demonstrates a firm commitment to the initiatives outlined in *State Ahead*, with its support of technology advancements and the continuing modernization of insurance regulation in areas such as innovation, cybersecurity, and international standard-setting.

The budget also continues the NAIC's commitment to support the variety of programs, products, and services in the financial solvency and market regulatory arenas. The NAIC offers a wide range of publications, data, and information systems; accreditation reviews; and many other services to assist state insurance regulators in achieving their fundamental insurance regulatory goals in a timely and cost-effective manner.

For many years, the NAIC has collected data on behalf of the states for statutory financial statements, complaints data, and Market Conduct Annual Statements (MCAS). In recent years, the NAIC has expanded its services to include regulatory ad-hoc data collection efforts, such as the short-term limited duration data call. With the expansion of services, the NAIC is utilizing new technologies to develop and expand systems for collecting various regulatory data sets in a timely and cost-effective manner.

Identified in *State Ahead* as a significant element to achieving the plan's goals, the NAIC has committed to moving its technology platform to the Cloud. Through mid-2019, the NAIC has nine applications in the Cloud, including the Professional Designation program and MCAS. Cloud solutions will streamline data intake processes, expand the tools offered to the membership and the insurance industry, increase the level and timeliness of analysis, and allow for experimentation of new products and services without a significant financial investment.

Support of the Membership

The mission of the NAIC is to assist the state insurance regulators in serving the public interest and achieving its goals of protecting the public interest; promoting a competitive marketplace; facilitating the fair and equitable treatment of consumers of insurance; promoting the reliability, solvency, and financial solidity of insurers; and supporting and improving state insurance regulation. Leveraging NAIC technology solutions, regulatory tools, and staff resources allow member states to achieve these goals at a significant cost savings. Without these options, many systems would be cost-prohibitive for the states to implement on their own. Without membership in the NAIC, the amount of state funding required to provide or access similar type of services and data the NAIC provides — often at no extra charge — would far exceed what a state pays in member dues to the NAIC.

A Focus on Consumers

The NAIC provides a multi-channel approach to reach and assist consumers in making informed decisions on insurance matters. These multi-pronged public relations campaigns include items like consumer insights and alerts, a consumer section on naic.org, mobile apps, and targeted social campaigns. The NAIC also hosts a consumer hotline to help consumers contact their state insurance departments for assistance.

Valuable Products and Services

The NAIC seeks to support its mission through the wide variety of products and services offered to both the insurance industry and state regulators. NAIC web-based systems automate, standardize, and streamline regulatory processes by transmitting data and facilitating regulatory transactions between insurers, consumers, and state insurance regulators.

The NAIC is committed to maintaining and enhancing these systems to provide high-quality service to all stakeholders. The 2020 budget includes five technology-based fiscals, which represent initiatives to automate manual processes, enhance security, streamline billing processes, take advantage of cloud-based solutions, and improve delivery of products and services.

By the Numbers

NAIC products and services make life easier on a number of fronts.

- Life Policy Locator – 100,006 requests received in 2018, with 31,385 located life insurance policies for a total claims amount of more than $454 million
- System for Electronic Rates & Forms Filing (SERFF) – 557,089 transactions processed in 2018
- Online Premium Tax for Insurance (OPT*ins*) – 142,616 transactions processed in 2018
- State Based Systems (SBS) – provides back-office services for 30 jurisdictions in 2019
- Professional Designation Program – 1,211 designations awarded since the program's inception in October 2006
- Center for Insurance Policy and Research (CIPR) Key Research Issues – 150 briefs currently available online including NAIC key initiatives and topics ranging from cybersecurity and innovation to natural catastrophe risk and resiliency

Building the Budget

The NAIC strives for transparency in its budget process as well as in its operations. The budget process gets underway in the spring each year, when department managers evaluate current-year revenues and expenses in order to assess the year-end picture, then propose a budget for the following year based on their operational objectives and member initiatives. Managers carefully focus on variances between the current year's budget and projected results and anticipated business needs for the coming year. This process includes a review of all projects, products, programs, services, committee charges, and technology initiatives in light of the NAIC's mission and the membership's strategic priorities, particularly those outlined in *State Ahead*. NAIC senior management reviews each department budget in detail with its division director to make adjustments according to the strategic and financial needs of the association and ultimately consolidates all requests into a single, comprehensive budget.

Following the extensive development and internal review process, the budget is presented to the NAIC Officers, the Executive (EX) Committee and Internal Administration (EX1) Subcommittee, and the full NAIC membership before being released for public review and comment. To ensure transparency, a public hearing is held to receive public comments before final consideration and adoption by the NAIC Executive (EX) Committee and Plenary.

2019: The Halfway Point of *State Ahead*

State Ahead outlined 94 initiatives to be accomplished over three years. The NAIC is at the halfway mark with the completion of 35 of these initiatives, while 40 are being actively worked and 19 more are slated to start in 2020.

2019:
Building Full Speed Ahead

The NAIC continued to focus on building an infrastructure for data, technology, and talent to implement *State Ahead.*

Expected Results for 2019

Based on actual operating results (before adding investment income) through June 30, 2019, the NAIC projects a net negative operating margin of $8.8 million compared to a budgeted net negative operating margin of $11 million, an improvement of nearly $2.3 million. Investment income is projected to be $13.7 million, resulting in a net asset increase of $4.9 million.

Several initiatives outlined in the *State Ahead* blueprint resulted in fiscal impact statements for 2019. These fiscals were made available for public comment in advance of membership consideration, approval, and incorporation into the 2019 budget.

Additional information regarding 2019 projected variances is included throughout the detailed footnotes of the budget.

Year Three of the Plan

2020:
Transforming

By the end of 2020, the NAIC will be positioned to provide its members with new analytics, technology, and tools to more effectively regulate their markets.

2020 Budget

The 2020 budget demonstrates NAIC's continued strong focus on prudent financial management.

The 2020 NAIC operating budget (before adding investment income) reflects revenues of $114.5 million and expenses of $124.5 million, which represent a 6.5% and a 5.1% increase, respectively, from the 2019 budget, resulting in $10.0 million in projected expenses over revenues. Viewed in relation

to the 2019 projected totals, the 2020 budget represents operating revenue increase of 3.8% and operating expense increase of 4.6%. Additional information about the 2020 budget is included throughout the detailed footnotes of the budget.

A fiscal impact statement (fiscal) is prepared for new or existing NAIC initiatives with revenue, expense, or capital impacts of $100,000 or more either in the current budget or within the following few years' budgets or requires more than 1,150 internal technical resources to accomplish. Each fiscal includes a detailed description of the initiative; the impact on key stakeholders; the financial and operational impact of the initiative; and an assessment of the risks. The total financial impact of the five fiscals included in the 2020 budget is a net of $4.3 million in expenses over revenues. Additional information about each initiative is included in the various Fiscal tabs of the budget.

The 2020 budget includes $3.2 million in investment income from the NAIC's Long-Term Investment Portfolio. Investment income is composed of interest and dividends earned reduced by investment management fees – investment gains and losses are not projected nor included in the budget.

Combining budgeted results from operations with budgeted investment income, the 2020 budget has a reduction in net assets of $6.9 million.

Preparing for the Unknown

The budget proposal includes all known activities anticipated to occur in 2020. However, situations may arise during the course of the year that require additional funding. In such an event, a funding request is prepared and presented to the Executive (EX) Committee and Internal Administration (EX1) Subcommittee for consideration. Funding for any approved project comes from the Regulatory Modernization and Initiatives Fund, established in 2005 to manage requests

2020 Fiscal Impact Statements

- ***Cloud Transition Phase IV (Cloud Migration)*** – This fourth phase of the project focuses on minimal change to most of the targeted systems to be migrated, in order to do so quickly and at a minimal cost. This phase continues the culture transformation designed to make the organization nimbler, thus enabling more frequent and faster delivery of products, and provides technical support for cloud projects already in progress.
  - Net 2020 expense of $3.2M after NIPR cost-sharing
- ***Enhanced Regulatory Data Collection (RDC)*** – This project expands the current system into an enterprise solution that can integrate with other applications, improve data quality, and speed up the review process. This project will enable business owners to be more self-reliant and independent. This project will provide functionality that will be used by the Uniform Certificate of Authority Application (UCAA) redesign.
  - Expense in 2020 of $239K
- ***Financial Data Delivery Platform Enhancement*** – This initiative moves financial statement data order fulfillment to the Cloud, thereby eliminating outdated platforms and improving the NAIC's security profile. This project will allow customers to access their data in a more timely manner without manual intervention and support from NAIC staff.
  - Expense in 2020 of $397K
- ***SERFF Billing Enhancements*** – will simplify the SERFF transaction pricing structure by eliminating SERFF prepaid blocks and instead charging a fee based on prior-period usage. The NAIC will also collect the transaction fee at the time of filing, thereby reducing payment and collection efforts.
  - Expense in 2020 of $86K
- ***Uniform Certificate of Authority Application (UCAA) Redesign and Biographical Affidavit Database*** – moves the UCAA platform to the Cloud and expands the number of company licensing-related forms and applications, including Biographical Affidavits, by 2022.
  - Expense in 2020 of $390K, with $760K in 2021 and $295K in 2022

that arise following the adoption and implementation of an annual budget. The Fund is based on 1.5% of the NAIC's projected consolidated net assets as of December 31, 2020, or $1.9 million with the inclusion of fiscals.

Ensuring Financial Stability

The NAIC's operating reserve is designed to ensure the financial stability of the NAIC in the event of emerging business risks and uncertainties and to absorb new priority initiatives pursued by NAIC membership. The association's reserve status is of paramount consideration in the budgeting process, as is strong and prudent financial management of the NAIC's assets.

In July 2015, the Executive (EX) Committee and Internal Administration (EX1) Subcommittee approved a report from an independent financial advisory firm which established the NAIC's liquid operating reserve target range of 83.4% to 108.2%. This range was the result of a comprehensive review of current and future identified risks and an evaluation of comparable organizations. This report recognized the increased level of uncertainty facing the NAIC and anticipated future investments which would be required to enhance the association's information technology and technical infrastructure, which is represented by many elements of the 2020 budget.

Operating Reserve	
2018 Audited	93.0%
2019 Projected	94.7%
2020 Proposed	91.3%

Contact Information

The NAIC appreciates the opportunity to present this 2020 budget and believes it provides a comprehensive review of the NAIC's business and financial operations for the current and upcoming fiscal year. A summary of the 2020 budget's key components is included in the budget overview.

Please feel free to contact Jim Woody, Chief Financial Officer, at (816) 783-8015, or Carol Thompson, Senior Controller, at (816) 783-8038, should you have any questions or need additional information.

National Association of Insurance Commissioners

2020 BUDGET WITH FISCAL IMPACT STATEMENTS
REVENUE AND EXPENSE BY LINE

			2019				2020				
Description	Reference	2018 Actual	6/30/2019 Actual	12/31/2019 Projected	2019 Budget	2019 Projected Variance	**2020 Budget**	Increase (Decrease) from 2019 Budget	%	Increase (Decrease) from 2019 Projected	%
Member Assessments	R1	$2,108,679	$1,054,205	$2,109,460	$2,109,460		**$2,110,953**	$1,493	0.1%	$1,493	0.1%
Database Fees	R2	29,750,827	30,958,559	30,960,867	30,334,777	$626,090	**31,776,882**	1,442,105	4.8%	816,015	2.6%
Publications and Insurance Data Products	R3	16,059,955	7,259,383	16,156,765	15,912,690	244,075	**16,867,844**	955,154	6.0%	711,079	4.4%
Valuation Services	R4	26,918,340	9,324,749	27,449,436	26,942,918	506,518	**27,977,053**	1,034,135	3.8%	527,617	1.9%
Transaction Filing Fees	R5	10,752,404	6,229,960	11,454,121	11,117,239	336,882	**12,668,651**	1,551,412	14.0%	1,214,530	10.6%
National Meetings, NAIC Events, and Interim Meetings	R6	2,549,365	1,147,500	2,831,000	2,807,531	23,469	**2,923,648**	116,117	4.1%	92,648	3.3%
Education and Training	R7	391,930	124,365	376,666	414,398	(37,732)	**400,740**	(13,658)	-3.3%	24,074	6.4%
Administrative Services and License Fees	R8	17,166,364	9,723,962	18,869,204	17,730,385	1,138,819	**19,646,917**	1,916,532	10.8%	777,713	4.1%
Other	R9	43,601	21,623	100,993	61,500	39,493	**90,400**	28,900	47.0%	(10,593)	-10.5%
Total Operating Revenues		105,741,465	65,844,306	110,308,512	107,430,898	2,877,614	**114,463,088**	7,032,190	6.5%	4,154,576	3.8%
Salaries	E1	50,241,678	25,987,177	52,192,071	51,971,330	220,741	**54,739,393**	2,768,063	5.3%	2,547,322	4.9%
Temporary Personnel	E2	592,539	291,444	594,176	665,553	(71,377)	**611,936**	(53,617)	-8.1%	17,760	3.0%
Payroll Taxes	E3	3,386,310	2,022,437	3,496,794	3,571,105	(74,311)	**3,636,130**	65,025	1.8%	139,336	4.0%
Employee Benefits	E4	9,612,553	5,721,114	12,947,716	11,420,064	1,527,652	**12,740,356**	1,320,292	11.6%	(207,360)	-1.6%
Employee Development	E5	692,996	395,583	885,188	836,581	48,607	**804,191**	(32,390)	-3.9%	(80,997)	-9.2%
Professional Services	E6	10,165,645	4,903,215	16,094,271	16,522,999	(428,728)	**16,811,083**	288,084	1.7%	716,811	4.5%
Computer Services	E7	3,616,430	2,380,225	4,820,364	4,808,622	11,742	**5,848,629**	1,040,007	21.6%	1,028,264	21.3%
Travel	E8	5,020,501	2,626,496	5,154,662	5,235,116	(80,454)	**5,264,192**	29,076	0.6%	109,530	2.1%
Occupancy and Rental	E9	4,509,092	2,261,301	4,519,470	4,548,537	(29,067)	**4,661,327**	112,790	2.5%	141,857	3.1%
Computer Hardware and Software Maintenance	E10	4,292,368	2,441,422	5,169,101	5,342,933	(173,832)	**5,884,458**	541,525	10.1%	715,357	13.8%
Depreciation and Amortization	E11	4,435,747	2,019,166	4,051,787	4,270,732	(218,945)	**4,140,587**	(130,145)	-3.0%	88,800	2.2%
Operational	E12	1,922,027	1,100,812	1,874,789	1,926,066	(51,277)	**1,790,279**	(135,787)	-7.0%	(84,511)	-4.5%
Library Reference Materials	E13	330,262	165,731	334,926	333,225	1,701	**332,487**	(738)	-0.2%	(2,439)	-0.7%
Printing and Production	E14	88,681	42,620	81,753	137,847	(56,094)	**71,022**	(66,825)	-48.5%	(10,731)	-13.1%
National Meetings, NAIC Events, and Interim Meetings	E15	3,769,618	2,032,661	4,020,947	3,886,099	134,848	**4,133,484**	247,385	6.4%	112,537	2.8%
Education and Training	E16	57,165	41,220	119,502	141,844	(22,342)	**212,404**	70,560	49.7%	92,902	77.7%
Grant and Zone	E17	1,530,867	432,497	1,716,655	1,704,250	12,405	**1,676,730**	(27,520)	-1.6%	(39,925)	-2.3%
Other	E18	1,190,486	708,449	993,204	1,117,541	(124,337)	**1,140,642**	23,101	2.1%	147,438	14.8%
Total Operating Expenses		105,454,967	55,573,570	119,067,377	118,440,444	626,932	**124,499,330**	6,058,886	5.1%	5,431,953	4.6%
Revenues Over/(Under) Expenses before Investment Income		286,498	10,270,736	(8,758,865)	(11,009,546)	2,250,682	**(10,036,242)**	973,304		(1,277,377)	
Investment Income	II1	(3,183,385)	12,398,447	13,674,609	3,012,020	10,662,589	**3,153,072**	141,052		(10,521,537)	
Revenues Over/(Under) Expenses		($2,896,887)	$22,669,183	$4,915,744	($7,997,526)	$12,913,271	**($6,883,170)**	$1,114,356		($11,798,914)	

A detailed analysis of each line item is included in the Revenue Detail, Expense Detail, and Investment Income Detail tabs.

2020 Fiscal Impact Statements

(dollars in thousands)

Initiative	2020 Revenue	2020 Expense	Net Impact on 2020 Budget	2020 Capital
Cloud Transition Phase IV (Cloud Migration)	$133.1	$3,341.7	(3,208.6)	
Enhanced Regulatory Data Collection (RDC)		238.7	(238.7)	
Financial Data Delivery Platform Enhancement		396.8	(396.8)	
SERFF Billing Improvements		86.4	(86.4)	
Uniform Certificate of Authority Application (UCAA) Redesign and Biographical Affidavit Database		390.4	(390.4)	
Total Fiscal Impact Statements	**133.1**	**4,453.9**	**(4,320.8)**	**$0.0**
2020 Budget Before Fiscals	114,330.0	120,045.4	(5,715.5)	1,419.6
2020 Budget After Fiscals and Before Investment Income	114,463.1	124,499.3	(10,036.2)	1,419.6
Investment Income	3,153.1		3,153.1	
2020 Budget After Fiscals and Investment Income	**$117,616.2**	**$124,499.3**	**($6,883.3)**	**$1,419.6**

National Association of Insurance Commissioners & The Center for Insurance Policy and Research

Date: November 14, 2019

To: All NAIC Members and Interested Parties

From: Director Raymond G. Farmer, NAIC President-Elect
Michael Consedine, NAIC Chief Executive Officer
Andy Beal, NAIC Chief Operating Officer and Chief Legal Officer
Jim Woody, NAIC Chief Financial Officer

Re: Summary of Comments on the Proposed 2020 NAIC Budget

The NAIC received one comment letter from the National Association of Mutual Insurance Companies (NAMIC) (**Attachment One**) on the proposed 2020 budget after it was released for public comment on October 8, 2019. This document summarizes NAMIC's comments and includes the NAIC's response to each comment.

A Public Hearing will be held November 18, 2019, to discuss these comments. Participation instructions for the public hearing can be accessed at *http://www.naic.org/about_budget.htm*.

Contributions to Regulator Efficiency

- NAMIC noted the NAIC 2020 budget includes several programs and services that contribute to efficiencies in state-based insurance regulation and enable regulators to become more proficient in their roles. NAMIC cited the continued upgrade of financial analysis solvency tools through the FASTR project; the investments in the NAIC Professional Designation Program; the migration to and development of new programs within a cloud computing environment, and the steps taken to strengthen the NAIC's data security environment. NAMIC went on to provide detailed statements of support for each of these initiatives. NAMIC did caution NAIC "to not inject any regulatory biases or other ill-defined, aspirational goals that do not further state-based insurance regulation but do cause unnecessary compliance costs that are ultimately borne by policyholders."

NAIC Response: The NAIC appreciates NAMIC's support of these initiatives. The NAIC's goal is to ensure state-based insurance regulation keeps pace with a rapidly changing marketplace. The initiatives cited by NAMIC as well as numerous others outlined on the NAIC *State Ahead* website demonstrate that commitment. NAIC senior leadership developed an internal project review process several years ago, which requires all key initiatives be vetted before starting, to ensure the project is aligned with *State Ahead* and Member priorities and will provide benefits to state-based regulation. Any project meeting certain thresholds requires a fiscal impact statement, or fiscal. These thresholds are expenses exceeding $100,000, technology resources exceeding 1,150 hours, or any new revenue stream. Fiscals are posted on the NAIC's website prior to

membership consideration in order to allow for the public to comment. Both the internal vetting and the fiscal process are designed to ensure that all initiatives undertaken by NAIC staff will enhance or improve state-based insurance regulation and will not result in unnecessary costs.

Internal Data Protection and Security

- NAMIC noted the NAIC is spending time and financial resources to increase the level of data protection and security around the data and data repositories the NAIC maintains by conducting independent third-party audits. While supporting the direction the NAIC is taking to ensure data and systems are protected, NAMIC also stated it does not necessarily mean the insurance industry is comfortable providing additional data to the NAIC without justification.

NAIC Response: As NAMIC noted, the 2020 budget reflects NAIC's commitment to data protection and security, especially in light of the transition to the Cloud. The NAIC collects a wide variety of data from various sources, primarily from the insurance industry. It does so, however, based on a regulatory business need. There is no intent to collect data simply because of any technology expansion efforts. Data collection has been and will continue to be at the request of the NAIC membership for the purpose of regulating the insurance industry.

Cloud Development Tools Modernization

- One of the four initiatives specifically supported by NAMIC was the migration of the NAIC's applications to the Cloud, which is a significant element to the *State Ahead* strategic plan. NAMIC pointed out the investments associated with each of the four phases, noting the initiative has the capability to reduce maintenance costs, improve efficiencies, and strengthen security. NAMIC said its members are interested in reviewing a comprehensive cost/benefit analysis of the NAIC's migration to the Cloud and asked for the costs to develop and maintain the Cloud on an ongoing basis, the benefits and costs savings to operating in a Cloud environment, and the overall security enhancements that go along with managing and housing applications that contain sensitive and proprietary company information on the Cloud.

NAIC Response: The NAIC appreciates NAMIC's support of this critical initiative. Although the NAIC will be entering its fourth phase of the initiative in 2020, the work to complete migrations will continue past year-end 2020. A number of significant systems are scheduled to begin migrations in 2020, such as SERFF, State Based Systems, and I-SITE; however, given the size of these systems, it is not expected that all systems will be fully migrated to the Cloud by year-end 2020. The NAIC does, however, expect to complete the project utilizing internal resources, thereby not requesting additional fiscal funding.

As noted in the 2020 fiscal, the primary benefits of investing in the cloud platform are increased efficiencies including improved system availability; enhanced customer support; predictable costs and flexibility; and greater innovation opportunities. Cost savings are expected long term, but while the migration is in progress, the NAIC recognizes it must continue to invest in the on-premise systems as well as the cloud migrations in order to continue its operations. Having said that, the NAIC has taken steps to reduce costs where feasible. First, the NAIC has engaged an

industry-leading firm to provide consulting expertise as to how best to design and deploy cloud-based solutions. In addition, the NAIC has also implemented a cost management program managed by another industry-leading firm which pinpoints potential cost savings in the Cloud by taking certain actions. The NAIC will continue to investigate opportunities to reduce the cost of maintaining its Cloud infrastructure while taking advantages of the Cloud's technical capabilities.

IAIS Dues

- NAMIC noted that the NAIC dues paid to the International Association of Insurance Supervisors (IAIS) continue to increase at a significant rate and questioned the value proposition. NAMIC members asked whether the NAIC is one of the highest paying members and/or if they are assessed based on the number of jurisdictions in the United States.

NAIC Response: The IAIS annual dues paid by the NAIC cover the memberships of the NAIC itself and the individual 56 NAIC members. IAIS annual dues are calculated based on two parameters: the written premium within the jurisdiction and the jurisdiction's GDP per capita. The size of the US insurance market relative to the rest of the world and the US GDP, result in the NAIC's annual dues level. While the NAIC's IAIS dues increased 12.5% in 2020 compared to 2019, a 10% increase is expected in 2021 and annual fee increases will continue to decline in subsequent years. Additionally, the NAIC is continuing to work with IAIS Secretariat to control the level of spending and identify further operational improvements that can be reflected in annual budgets. Since the dues are billed in Swiss Francs, the actual rate the NAIC pays in US dollars may be higher or lower depending on the currency exchange rate when the payment is made.

Concluding Comments

The NAIC takes a holistic approach to the development of its annual budget. With the goal of transparency in mind, NAIC leadership welcomes the opportunity to publicly present the proposed 2020 NAIC budget and respond to questions and/or comments raised by interested parties. State insurance regulators, supported by the NAIC, are committed to protecting policyholders as well as ensuring the financial solvency of the insurance industry in a cost-effective and financially prudent manner. The NAIC continuously seeks opportunities to reduce operating costs while providing world-class support to its members, regulators, insurance customers, and interested parties. In addition, the NAIC will continue to utilize a portion of its Net Assets to ensure the products and services required by state insurance departments are delivered with minimal price changes.

NAMIC
NATIONAL ASSOCIATION OF MUTUAL INSURANCE COMPANIES

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November 7, 2019

Jim Woody
Chief Financial Officer
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1500
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VIA Email Transmission: jwoody@naic.org

RE: NAMIC Comments – NAIC Proposed 2020 Budget

Dear Mr. Woody:

The following comments are submitted on behalf of the members of the National Association of Mutual Insurance Companies[1] regarding the NAIC's proposed 2020 budget.

NAMIC members have long been supporters of the state-based regulatory system and are mindful of the many challenges facing state insurance departments, such as working with limited or dwindling resources or attracting and retaining talent. We therefore believe it is incumbent upon the NAIC to assure streamlined and efficient regulatory standards and guidance so as not to unduly burden states in carrying out their respective duties and responsibilities.

Regarding the 2020 budget, there are several programs and services that NAMIC believes will go a long way to helping state regulators become more efficient and proficient in their critical role as state regulators. Such programs and services include: the continued upgrade of financial analysis solvency tools (FASTR), the new investments made to the NAIC Professional Designation Program, the migration to and development of new programs within a cloud computing environment, and the enhancements made to the NAIC's own data security environment. These programs and others demonstrate that the NAIC is becoming a more important resource to the states in a society becoming more dependent on the use of new and innovative technology. However, as the NAIC continues to incorporate data analytics and other artificial intelligence into its internal analysis and workstream, caution should be taken not to inject any regulatory biases or other ill-defined, aspirational

[1] NAMIC membership includes more than 1,400 member companies. The association supports regional and local mutual insurance companies on main streets across America and many of the country's largest national insurers. NAMIC member companies write $268 billion in annual premiums. Our members account for 59 percent of homeowners, 46 percent of automobile, and 29 percent of the business insurance markets. Through our advocacy programs we promote public policy solutions that benefit NAMIC member companies and the policyholders they serve and foster greater understanding and recognition of the unique alignment of interests between management and policyholders of mutual companies.



goals that do not further state-based insurance regulation but do cause unnecessary compliance costs that are ultimately borne by policyholders.

The remainder of our comments will focus on these areas of interest but also include some commentary on the overall direction of the NAIC.

Financial Analysis Solvency Tools

The NAIC 2020 budget includes $135,000 in professional services for the continued work on the Financial Analysis Tool Redesign (FASTR). This program, which included dedicated Fiscal Statements in both the 2018 and 2019 budgets, is a long-term program designed to help the state financial analyst become more efficient and to make their jobs easier. As part of the State Ahead strategy, the first phase of FASTR included a redesign of the Financial Profile Report, an automated analysis tool that allows regulators to better identify issues and trends and to navigate financial data more efficiently. The second phase when fully implemented will include an update to the financial risk repositories, a massive database of insurer financial data that allows regulators to monitor the performance of the industry and identify concerns for further investigation. NAMIC members support the upgrades of these tools and are hopeful they will lead to more valuable insurer/regulator interactions.

NAIC Professional Designation Program

In addition to helping the states with new tools and enhanced ways to access and analyze data, another initiative that has potential to help state insurance regulators is the NAIC Professional Designation Program and specifically the increased investment into the program for the 2020 fiscal year. In conjuction with this program, the NAIC budget proposes an increase of $91,400 in professional fees. NAMIC supports this increase in spending and supports the overall program which started in 2006 and has awarded over 1,200 professional designations in that time. As communicated in the State Ahead Initiative, the NAIC wishes to increase regulator enrollment into the program and NAMIC also encourages more states to participate. Given the current state of demographics in the U.S. economy, a program like this is critical if states and the NAIC want to address the issue of the high rate of retiring baby-boomers. Continued investments into programs like this will help train the future regulators of tomorrow to deal with the complex and ever-changing insurance regulatory landscape.

Cloud Development Tools Modernization

A significant element in the State Ahead Initiative includes the migration of all the NAIC's applications to a Cloud environment. Since 2017, the NAIC has dedicated funds to developing a Cloud strategy and included minimal investments into Cloud programs and services. As the State Ahead Initiative was formalized, so too were increased investments into the NAIC's Cloud Strategy, starting in 2018 with an investment of $238,000. These initial investments were the start of migrating existing NAIC applications to the Cloud. Last year, according to the 2019 Fiscal Statement regarding the third phase of cloud transition, budgeted spending increased dramatically to $3.5 million; however, this represented the first full year of system migrations. Included in the 2020 budget is an additional request of $3.3 million in expenses. The aggregated



amount of spending for cloud migration projects totals just over $7 million over the last four budget cycles. The shear volume of these figures speaks to the NAIC's dedication to running programs and systems in a safer and more secure environment, such as the Cloud, and its' importance to the overall strength of the organization.

The migration to the Cloud has the opportunity to reduce IT maintenance costs and according to the commentary provided during the Open Hearing for the budget, some of those savings have started to emerge. Further, outdated and obsolete systems are being retired and the systems replacing them that are being hosted on the Cloud are more efficient. In addition, the new applications that are being initially developed on the Cloud have the benefit of being developed utilizing the latest technologies and security enhancements. With these potential benefits and the high development costs, NAMIC members are interested in reviewing a comprehensive cost/benefit analysis of the NAIC's migration to the Cloud. Included in this analysis would be the costs to develop and maintain the Cloud on an ongoing basis, the benefits and costs savings to operating in a Cloud environment, and the overall security enhancements that go along with managing and housing applications that contain sensitive and proprietary company information on the Cloud.

Internal Data Protection and Security

Data protection and security is another area where NAMIC supports the direction NAIC operations is taking, particularly as it pertains to the increasing amount of company information being shared between the NAIC and the states. Whether that includes financial data included as part of the risk repositories or the nearly 170 systems that will ultimately be run on the Cloud, NAMIC applauds the NAIC for taking steps to enhance the organizations information systems through conducting independent third-party audits to certify each of their systems against industry (SOC 2) standards. A note in the 2020 budgets on professional fees: audits, includes a line item of $180,000 for a SOC 2 gap assessment for cloud computing, $148,400 for a cybersecurity audit, and $90,000 for security testing related to cloud computing. This demonstrates the NAIC's recognition of how important it is to provide a safe and secure environment for their members (states) to work within. NAMIC strongly encourages the NAIC to continue its commitment the important area of data protection and security.

Simple technology upgrades and security measures, however, do not mean that the industry supports or is comfortable with any enhanced data requirements it may be asked to submit to the NAIC for regulatory approval. Requests should not be inordinate, excessive, or in any way justified simply because the NAIC has engaged in technology expansion. Further, as additional, critical, proprietary, and confidential information is submitted per regulatory requirements, the NAIC as the data hub for this information should continue to implement and explore extremely robust protections from external sources.

General Comments

Each of the last several years, revenues and expenses combined have outperformed the budget. Factoring in investment gains during those years has allowed the NAIC to operate at a deficit yet continue to grow its' net asset base. For the 2020 budget the NAIC is targeting a slight decrease to its' liquid operating reserve ratio; however, it remains in the necessary

range for adequate funding. Continued growth and expansion should be in proportion to expected needs and tempered by continued review for efficiencies and removal of redundancies that provide excessive costs to all stakeholders, thereby continuing to be good stewards of public and private funds.

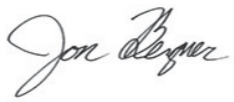
For instance, dues paid to the International Association of Insurance Supervisors continue to increase at a significant rate with no apparent end in sight – and for an increasingly questionable value proposition based on the direction of many of their workstreams. The increase from 2018 to 2019 was just over $50,000 and budgeted 2020 dues includes an additional $91,000 bringing total dues to be paid in 2020 to the IAIS to just over $671,000. NAMIC members inquire whether the NAIC is one of the highest paying members and/or if they are assessed based on the number of jurisdictions in the United States.

Closing

NAMIC members appreciate the opportunity to provide input on the NAIC 2020 annual budget. We believe the association is managing the significant finances of the organization and has invested in several projects that may benefit the states and ultimately the insurers and policyholders they serve.

Thank you for your consideration of these comments on this matter of importance to NAMIC, its member companies, and their policyholders.

Sincerely,



Jon Bergner
Assistant Vice President – Public Policy and Federal Affairs
National Association of Mutual Insurance Companies

TABLE 1
PROPOSED 2020 GRET FACTORS, Based on Average of 2017/2018 Data

Description	Acquisition Per Policy	Acquisition Per Unit	Acquisition Per Premium	Maintenance Per Policy	Companies Included*	Average Premium Per Policy Issued During Year	Average Face Amount Per Policy Issued During Year
Independent	$168	$0.90	42%	$50	118	3,263	200
Career	214	1.20	54%	64	63	2,661	217
Direct Marketing	217	1.20	54%	65	20	2,489	213
Niche Marketing	125	0.70	32%	38	21	757	13
Other*	140	0.80	35%	42	104	876	34
Total					326		

TABLE 2
CURRENT (2019) FACTORS, Based on Average of 2016/2017 Data

Description	Acquisition Per Policy	Acquisition Per Unit	Acquisition Per Premium	Maintenance Per Policy	Companies Included*	Average Premium Per Policy Issued During Year	Average Face Amount Per Policy Issued During Year
Independent	$167	$0.90	42%	$50	130	3,496	194
Career	231	1.30	58%	69	69	2,287	203
Direct Marketing	221`	1.20	55%	66	22	2,492	163
Niche Marketing	139	0.80	35%	42	21	702	20
Other*	136	0.70	34%	41	119	839	32
Total					361		

Appendix A -- Distribution Channels
The following is a description of distribution channels used in the development of recommended 2020 GRET values:

1. **Independent** – Business written by a company that markets its insurance policies through an independent insurance agent or insurance broker not primarily affiliated with any one insurance company. These agencies or agents are not employed by the company and operate without an exclusive distribution contract with the company. These include most PPGA arrangements.
2. **Career** – Business written by a company that markets insurance and investment products through a sales force primarily affiliated with one insurance company. These companies recruit, finance, train, and often house financial professionals who are typically referred to as career agents or multi-line exclusive agents.
3. **Direct Marketing**– Business written by a company that markets its own insurance policies direct to the consumer through methods such as direct mail, print media, broadcast media, telemarketing, retail centers and kiosks, internet or other media. No direct field compensation is involved.
4. **Niche Marketers** – Business written by home service, pre-need, or final expense insurance companies as well as niche-market companies selling small face amount life products through a variety of distribution channels.
5. **Other** – Companies surveyed were only provided with the four options described above. Nonetheless since there were many companies for which we did not receive a response (or whose response in past years' surveys confirmed an "other" categorization (see below), values for the "other" category are given in the tables in this memo. It was also included to indicate how many life insurance companies with no response (to this survey and prior surveys) and to indicate whether their exclusion has introduced a bias into the resulting values.

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Appendix B – Unit Expense Seeds

The expense seeds used in the 2014 and prior GRETs were differentiated between branch office and all other categories, due to the results of a relatively old study that had indicated that branch office acquisition cost expressed on a per Face Amount basis was about double that of other distribution channels. Due to the elimination of the branch office category in the 2015 GRET, non-differentiated unit expense seeds have been used in the current and immediately prior studies.

The unit expense seeds used in the 2019 GRET and the 2020 GRET recommendation were based on the average of the 2006 through 2010 Annual SOA expense studies. These studies differentiated unit expenses by type of individual life insurance policy (term and permanent coverages). As neither the GRET nor the Annual Statement data provided differentiates between these two types of coverage, the unit expense seed was derived by judgment based this information. The following shows the averages derived from the Annual SOA studies and the seeds used in this study. Beginning with the 2019 Annual Statement submission this information may become more readily available.

2006-2010 (average) CLICE Studies:

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Weighted Average	$149	$0.62	38%	$58
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Median	$196	$0.59	38%	$64
Permanent				
Weighted Average	$167	$1.43	42%	$56
Unweighted Average	$303	$1.57	49%	$70
Median	$158	$1.30	41%	$67

Current Unit Expense Seeds:

	Acquisition/ Policy	Acquisition/ Face Amount	Acquisition/ Premium	Maintenance/ Policy
All distribution channels	$200	$1.10	50%	$60

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TO: Reggie Mazyck, NAIC

FROM: Dale Hall, Managing Director of Research, Society of Actuaries (SOA)
Leon Langlitz, Chair, SOA Committee on Life Insurance Company Expenses

DATE: July 16, 2019

RE: 2020 Generally Recognized Expense Table (GRET) – SOA Analysis

As in previous years, the Society of Actuaries expresses its thanks to NAIC staff for their assistance and responsiveness in providing Annual Statement expense and unit data for the 2020 GRET analysis for use with individual life insurance sales illustrations. The analysis is based on expense and expense related information reported on companies' 2017 and 2018 Annual Statements. This project has been completed to assist the Life Actuarial Task Force (LATF) in its consideration of potential revisions to the GRET that could become effective for calendar year 2020. This memo describes the analysis and resultant findings.

NAIC staff provided Annual Statement data for life insurance companies for calendar years 2017 and 2018. This included data from 707 companies in 2017 and 722 companies in 2018. This increase breaks the trend of small decreases over the previous few years. Of the total companies, 326 were in both years and passed the outlier exclusion tests and were included as a base for the GRET factors (361 companies passed similar tests last year).

Approach Used

The methodology for calculating the recommended GRET factors based on this data is similar in broad outline to that followed the last several years. The methodology was last altered in 2015. The changes which were made at that time can be found in the recommendation letter sent on July 30, 2015[1].

To calculate updated GRET factors, the average of the factors from the two most recent years (2017 and 2018 for those with data available for both years) of Annual Statement data was used. For each company an actual to expected ratio was calculated. Companies with ratios that fall outside predetermined parameters are excluded and this process is competed three times in order to stabilize the average rates. The boundaries of the exclusions are modified from time to time and there was a slight adjustment this year to increase the number of companies in the final study. Unit expense seed factors (the seeds for all distribution channel categories are the same), as given in Appendix B, were used to compute total expected expenses. Thus, these seed factors were used to implicitly allocate expenses between acquisition and maintenance expenses, as well as among the three acquisition expense factors (on a direct of ceded reinsurance basis).

Companies were categorized by their reported distribution channel (four categories were used as described in Appendix A of this memo). There remain a significant number of companies for which no distribution channel was available, as no responses to the annual surveys have been received from those companies. The characteristics of these companies vary significantly, including companies not currently writing new business or whose major line of business is not individual life insurance. Any advice or assistance from LATF in future

[1] https://www.soa.org/Files/Research/Projects/research-2016-gret-recommendation.pdf

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years to increase the response rate to the surveys of companies that submit Annual Statements in order to reduce the number of companies in the "Other" category would be most welcomed.

Prior to 2014, when responding to the survey if a company indicated they used multiple channels to distribute their individual life sales, the percentage weights provided to us were applied to that company's reported results in the tabulations of each of the distribution channel's unit expense results. In 2015 this was changed so that all expenses for a company will go to the channel with the highest percentage weight. This approach was changed because: (1) as fewer channel types were used, it was expected that fewer companies would have multiple channels as currently defined and (2) an insufficient number of multiple distribution responses were provided in that year's survey to result in a significantly different outcome. The intention is to continue surveying the companies in future years to enable enhancement of this multiple distribution channel information.

Companies were excluded from the analysis if (1) their actual to expected ratios were considered outliers, often due to low business volume, (2) the average first year and single premium per policy was more than $40,000, (3) they are known reinsurance companies or (4) companies were not in both years of the data supplied by the NAIC. To derive the overall GRET factors, the unweighted average of the remaining companies' actual-to-expected ratios for each respective category was calculated. The resulting factors were rounded, as shown in Table 1.

The Recommendation

Employing the above methodology results in the proposed 2020 GRET values shown in Table 1. To facilitate comparisons, the current 2019 GRET factors are shown in Table 2.

Further characteristics of the type of companies represented in each category are included in the last two columns in Table 1, including the average premium per policy issued and the average face amount ($000s) per policy issued.

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In previous recommendations, an effort was made to reduce volatility in the GRET factors from year-to-year by limiting the change in GRET factors between years to about ten percent of the prior value. The changes from the 2019 GRET were reviewed to ensure that a significant change was not made in this year's GRET recommendation. Only the Niche Marketing distribution channel category experienced a change greater than ten percent so the factors for this line were capped at the ten percent level (the Acquisition per unit factor changed more than 10% because of rounding) from the corresponding 2019 GRET values. The change occurred due to the change in the composition of the companies in this category where there is a small number of companies included.

Usage of the GRET

Also asked in this year's survey, responded to by companies' Annual Statement correspondent, was a question regarding whether the 2018 GRET table was used by the company. Last year, 28% of the responders indicated their company used the GRET for sales illustration purposes, with similar percentage results by size of company; this contrasted with about 30% in the prior year. This year, 26% of responding companies indicated that they used the GRET in 2018 for sales illustration purposes, with similar results for each of the distribution channels with a significant number of responders. Based on the information received over the last several years, the variation in GRET usage appears to be in large part due to the relatively small sample size and different responders to the surveys.

We hope LATF finds this information helpful and sufficient for consideration of a potential update to the GRET. If you require further analysis or have questions, please contact Dale Hall at 847-273-8835.

Kindest personal regards,

Dale Hall, FSA, MAAA, CERA, CFA
Managing Director of Research
Society of Actuaries

Leon Langlitz, FSA, MAAA
Chair, SOA Committee on Life
Insurance Company Expenses



Appendix A -- Distribution Channels

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Actuarial Guideline (*VAED*)

Background:

Beginning in 2015, the NAIC commissioned a study of the reserve and RBC framework for Variable Annuity products. The study concluded that the existing requirements resulted in non-economic volatility, providing incentive for companies to engage in the use of financial planning techniques that the NAIC deemed inappropriate. Considerable effort was spent to develop and test updates to the reserve and RBC framework to address these issues. That revised framework was adopted by the NAIC during 2018, and the changes to NAIC models, the NAIC Valuation Manual, and the NAIC Life RBC instructions have been developed and adopted by the NAIC on August [xx], 2019. By the provisions of the SVL (Model 820), the changes to the Valuation Manual will be effective on January 1, 2020 and impact subsequent financial statements.

During the discussion of the Framework by the Variable Annuities Issues Working Group, the question was raised whether companies would have the option to 'early adopt'; that is, to apply the new framework for the reserve and RBC values used for the December 31, 2019 financial statements. Since the new framework has been determined to provide improved financial measurement of the company's liability and risk, there was agreement that optional application of the new framework for the December 31, 2019 financial statements would be appropriate.

Guideline:

A company may elect to apply the VM-21 requirements from the 2020 NAIC *Valuation Manual* as the *Valuation Manual* requirements for the valuation on December 31, 2019. For such election, the phase-in provision of *Valuation Manual* VM-21 Section 2.B. may not be elected. Any company electing early adoption of VM-21shall also:

1. apply the provisions of Actuarial Guideline XLIII as amended for 2020 to the December 31, 2019 valuation of contracts within the scope of that guideline;
2. apply the Life RBC instructions for 2020 in the calculation of C-3 RBC in LR027 for 2019;
3. follow the documentation and certification requirements of VM-31 from the 2020 Valuation Manual for the Variable Annuity Business. In the VA Summary, clearly indicate the use of the new requirements in the section on change in methods from prior year; and
4. notify the Commissioner of the state of domicile of such elections.

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National Association of Insurance Commissioners

Pending Adoption by Executive (EX) Committee and Plenary - 12/10/19
Adopted by Property and Casualty Insurance (C) Committee – 8/5/19
Adopted by Cannabis Insurance (C) Working Group – 7/9/19

REGULATORY GUIDE
UNDERSTANDING THE MARKET FOR CANNABIS INSURANCE

NAIC White Paper

July 9, 2019

Drafted by the
Cannabis Insurance (C) Working Group
of the
Property and Casualty Insurance (C) Committee

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I. INTRODUCTION

A. EXECUTIVE SUMMARY

The cannabis industry is evolving and expanding as more states legalize either or both medicinal and recreational cannabis use throughout the U.S. With new entrepreneurs, investors, large corporate businesses, companies going public and executives entering the market, there is a new level of sophistication to the cannabis industry. The state-legalized cannabis businesses, like any other businesses, face a variety of risks and would like to have access to insurance to mitigate these risks. It is important for state insurance regulators to understand the insurance needs of the cannabis industry and to consider steps to address insurance needs in their respective state markets. Several state insurance regulators have taken steps successfully to encourage insurers to provide insurance for state-legalized cannabis businesses. However, major cannabis insurance gaps exist in many states and even in those states that have encouraged successfully the entrance of insurers into the cannabis insurance market.

The National Association of Insurance Commissioners (NAIC) Cannabis Insurance (C) Working Group was formed in August 2018 to identify insurance issues, gaps and opportunities facing the cannabis industry and to identify best regulatory practices to address these issues—starting with developing a white paper. The purpose of this white paper is to provide information to state insurance regulators, insurers and the broader public about the architecture of the cannabis business supply chain, types of insurance needed by the cannabis industry, the availability of cannabis business insurance in state insurance markets and the extent of insurance gaps, and best practices that state insurance regulators can adopt to encourage insurers to write insurance for the cannabis industry.

B. CANNABIS

The cannabis market rapidly changed over the last few years and continues to change on a daily basis. In 2017, the cannabis industry took in nearly $9 billion in sales. Nationally, in 2018, the overall cannabis industry was worth $10.4 billion[1] and is anticipated to bring in $21 billion in 2021.[2] Other estimates project that by 2022, the cannabis industry will create an estimated $80 billion in sales annually.[3] “In 2017, sales

1. Kachelriess, R., 2019. “By the Numbers: A Year of Cannabis in 2018,” accessed at www.leafly.com/news/industry/by-the-numbers-year-of-cannabis-2018.
2. Smith, A., 2018. “The U.S. Legal Marijuana Industry is Booming,” accessed at https://money.cnn.com/2018/01/31/news/marijuana-state-of-the-union/index.html.
3. *Greencamp*.com, accessed at https://greencamp.com/recreational-cannabis-market-projections-for-2022/.

of medical and recreational cannabis in the U.S. were nearly nine times higher than Oreo cookies and almost on par with Americans' collective spending on Netflix subscriptions. With the addition of California's recreational market sales in 2018, cannabis sales could easily eclipse McDonald's annual U.S. revenue."[4]

Additionally, a majority of the U.S. population supports cannabis legalization. About six in 10 Americans say the use of cannabis should be legalized.[5] Since June 2019, cannabis is legal for medicinal use in 33 states and Washington, DC, and cannabis is legal for recreational use in 11 states and Washington, DC.

Not only is cannabis a growing industry, but also it is a significant employer. In 2017, the cannabis industry employed 121,000 people. With the current trajectory, the number of workers could reach 292,000 by 2021.[6] These jobs can range from budtenders[7] and extraction technicians to employees at ancillary companies that generate a large portion of revenue from the cannabis industry. The industry is projected to add as many as 340,000 full-time jobs by 2022. This type of increase in job availability is significant; but, despite the demand for employees in the cannabis sector, there remains an issue with inconsistent positions on the legality of cannabis.

One of the most complex issues facing the cannabis industry is the different treatment of cannabis under federal and state law in states that have legalized cannabis.[8] Despite being legal in many states, at the federal level, cannabis is a Schedule 1 substance that is illegal to manufacture, distribute or sell in the U.S.[9] Currently, federal law also prohibits the sale of cannabis for medical and adult recreational use. Because cannabis is illegal at the federal level, many individuals are not comfortable working in a field where their employment could be considered illegal. Moreover, financial institutions are hesitant or unwilling to work with cannabis companies. Most banks prohibit cannabis-based businesses from opening accounts, which has led to the cannabis industry being mostly cash-based. This proves problematic as cannabis businesses often find it difficult to engage in standard business practices such as paying employees and vendors. It also

4. *MSN Money*, accessed at https://www.msn.com/en-us/money/markets/us-retail-marijuana-sales-to-reach-up-to-dollar10-billion-this-year/ar-AAx15Nk.

5. Hartig, H., and A. Geiger, 2019. "About Six-in-Ten Americans Support Cannabis Legalization," Pew Research Center, accessed at *www.pewresearch.org/fact-tank/2018/10/08/americans-support-marijuana-legalization/ft_18-01-05_marijuana_line_update/*.

6. Smith, A., 2018. "The U.S. Legal Marijuana Industry is Booming," accessed at *https://money.cnn.com/2018/01/31/news/marijuana-state-of-the-union/index.html*.

7. Budtender—a person who serves customers at an establishment where cannabis is sold. Weedmaps, accessed at *https://weedmaps.com/learn/dictionary/budtender/*.

8 Please note that H.R. 2 of the 115th Congress (2017-2018) removed hemp from Schedule 1, accessed at https://www.congress.gov/bill/115th-congress/house-bill/2/text.

9. U.S. Drug Enforcement Administration. "Drug Scheduling," accessed at *www.dea.gov/drug-scheduling*.

makes many cannabis-based businesses targets for criminal activity because of the increased risk of robberies and other theft-related crimes.

In states that have legalized cannabis, some community banks and credit unions are providing banking services to the cannabis industry, but in other locales, state-chartered financial institutions are unavailable. For example, during a regulatory tour, Delaware regulators witnessed one vendor to the market (that was not growing or selling cannabis) receive notice from its state-chartered bank that it would no longer be doing business with the company because of its involvement in the cannabis industry. The magnitude of this concern should not be ignored. "An estimated 70 percent of cannabis businesses have no relationship with a financial institution and thus use cash for all transactions, including salaries for employees."[10]

The U.S. Department of the Treasury's Financial Crimes Enforcement Network (FinCEN) has issued guidance for financial institutions to follow regarding reporting revenues from the cannabis industry in those states in which cannabis is legal, which reflects the Treasury Department's recognition that some banks and credit unions are providing banking services to the cannabis industry. "Surplus lines insurers mainly focus on the development of new coverages and the structuring of policies and premiums appropriate for risks. New and innovative insurance products for which there is no loss history are difficult, if not impossible, to appropriately price using common actuarial methods. Often, after a new coverage has generated sufficient data, the coverage eventually becomes a standard product in the admitted market."[11] Despite the risks, state insurance regulators should encourage insurers who choose to enter the cannabis market to do so on the admitted market to drive the costs of policies down and make cannabis insurance more accessible for the cannabis industry.

C. Insurance Gaps

The following list shows the different types of cannabis businesses that are in the supply chain: cannabis cultivation, processors/harvesters, manufacturing, retail, distribution, testing labs and microbusinesses.

[10] Leavenworth, Stuart. 2018. "When Does Too Much Cash Become a Health Risk? When You Own a Marijuana Shop," McClatchy DC Bureau, accessed at https://www.mcclatchydc.com/news/nation-world/national/article198941964.html

[11] National Association of Insurance Commissioners (NAIC) 2019. Surplus Lines, accessed at https://www.naic.org/cipr_topics/topic_surplus_lines.htm

Below is a list of the types of insurance most frequently needed by the cannabis industry:

- Automobile, including Distribution (auto and cargo)
- Commercial General Liability
- Crop (Indoor/Outdoor)
- Crime Insurance
- Disaster Coverage
- Director and Officer Liability
- Employment Practices Liability
- Equipment Breakdown
- Errors and Omissions
- Excess/Umbrella
- General Liability
- Product Liability
- Premises Liability
- Property
- Surety Bonds
- Workers' Compensation

As the industry continues to expand, there are more cannabis businesses to insure. No longer is cannabis just the flower used for smoking; the market has expanded to oils, shatter, wax, edibles, topical products, the beauty industry, and other cannabis-infused products. However, even with the increased market activity, many insurers are not willing to write cannabis insurance products due to the cannabis industry's inability to bank, the federal illegality, and the unknown risks associated with insuring cannabis businesses. Insurance is essential to the security and safety of cannabis businesses, their employees, and their customers. Lack of insurance for the industry adds layers of unnecessary risk and exposure for all market participants.

While cannabis laws vary from state to state, the types of risks facing the cannabis industry generally remain the same. Many of the risks the cannabis industry faces are no different from any other business in the same area of business activity. Outdoor cannabis cultivators face the same risks that other cultivators or agricultural industry businesses face. Outdoor cannabis cultivators, for example, would be most vulnerable to adverse weather conditions and theft, which is not too different from other types of outdoor crop cultivators. The distinguishing factor with outdoor cannabis crops versus other types of outdoor crops is the federal illegality. For example, a cannabis farmer in Carpinteria, CA, was able to use his insurance policy with a payout in excess of $1 million after ash from

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the 2017 southern California Thomas Fire destroyed thousands of his cannabis plants.[12] Ash from the Thomas Fire seeped into the cannabis farmer's greenhouse and contaminated the cannabis plants with toxic chemicals, which triggered the "atmospheric change" language in the insurance policy.[13] This is the same exposure and the same coverage that applies to any other farm, nursery or orchard. The farmer accordingly filed a claim and received an insurance payout of more than $1 million. This may be the largest insurance payout given to a legal cannabis business to date.

In contrast, Delaware has not yet identified an insurer willing to write crop insurance for any Delaware cannabis growers. A cannabis farmer cannot get crop insurance in Delaware because he or she is growing cannabis and, consequently, it is considered "untouchable" per se. This difference between states illustrates that some insurers are treating cannabis businesses as regular commercial enterprises and are deciding to make a business risk decision, including financial and legal implications, to insure the cannabis industry, despite federal law differences, while in other states, some insurers are not ready to write insurance for the cannabis industry.

The cannabis industry is diverse in the type of insurance it needs from seed to sale. Crop failure and destruction can occur at the nursery and growth stage. Growing cannabis plants and keeping them healthy during the maturation phases is a laborious process. The cannabis is grown from its seedling stage in nurseries. It must be tended to by experienced cannabis farmers and growers and then harvested and trimmed (either by hand or machine). Even within the cannabis industry, there is great disparity between the sizes of companies and their operating and insurance needs. Crops can range from small craft batch cultivation to large scale nurseries. At the cultivation site alone, the types of insurance needed are different from the needs of a manufacturing site. One of the newest types of manufacturing sites is vertical integration locations where cannabis is grown and trimmed, and low-quality flowers are processed into oil and refined into shatter, wax or another concentrate through expensive machinery. Manufacturers will most likely want to insure these products. Once the cannabis product is in a consumable form, it is tested for contaminants and pesticides.

States often require some form of testing to ensure consumer protection. One bad test or pesticide report can make a crop or product completely unsafe and, therefore, unsellable. Many states have a track and trace system that records the movement of cannabis and cannabis products through the commercial supply chain. The cannabis plants are often tagged, and the packaging of cannabis products is marked with serial numbers to identify

12. Brugger, K., 2018. "Cannabis Farmer Gets Over $1 Million Insurance Payout," *Santa Barbara Independent*, accessed at www.independent.com/news/2018/mar/19/cannabis-farmer-gets-over-1-million-insurance-payo/.

13. Kennedy, B., 2018. "The Cannabist Article: California Cannabis Company Received Historic $1 Million Insurance Payout Following Fire," Cannabis Insurance Professionals, accessed at www.cannabisinsuranceprofessionals.com/news.

the chain of liability. This allows for the ease of pinpointing exactly where contamination occurred.

The ability to have insurance is critical, and these controls should make insurers confident that they can selectively underwrite this business. This ability to pinpoint exactly where the product contamination occurred helps to identify which cannabis producer should be accountable for a bad batch of cannabis products and, in turn, which insurer will be responsible for paying the claims.

As the cannabis industry continues to expand in states and U.S. territories, insurance availability lags behind the needs of the cannabis industry. Sectors of the cannabis industry that need to be insured include ancillary cannabis businesses, cannabis-infused product manufacturers, cannabis dispensaries, cannabis events, cannabis growers and harvesters, cannabis landlords, cannabis distributors and transporters, cannabis medical physicians, cannabis waste facilities, cyber liability, and more.

Insurance companies have hesitated to enter the admitted market due to little data, as well as the unknown risk factors. There is not only an increased need for insurance by the cannabis industry, but there is also a need for insurance with the roll-out of state and local licensing requirements. As regulations shift from being general to specific, many local and state licensing authorities require insurance. States such as California and Massachusetts require proof of insurance, such as a general liability policy, for cannabis business applicants seeking licensure from state and local jurisdictions.[14,15]

The risk tolerance differences between state regulatory systems can also be stark. For instance, to access a Delaware retail medical marijuana outlet, a patient must first enter a vestibule with locked doors on either end: one for ingress and the other egress. Patients are scanned in the vestibule when entering a facility. They must produce both a driver's license (or other state ID) and their Medical Marijuana Program (MMP) card before gaining entrance to a second locked chamber. Once there, patients pass their same ID to the intake processor. Only after satisfying the intake specialist protocol, the patient gains admittance to the store itself. No electronics are permitted in a Delaware cannabis store. In states that have legalized cannabis, security concerns are a prime concern of retail operators. However, state insurance regulators' security protocols differ for retail outlets.

14. State of Massachusetts, Code of Massachusetts Regulations, Title 935, Cannabis Control Commission, Code of Massachusetts Regulations §§ 500.101(c)(5) and (6) and § 500.105(10).

15. State of California, Bureau of Cannabis Control Proposed Text of Regulations, California Code of Regulations Title 16, Division 42. Bureau of Cannabis Control Regulations §§ 5008, 5308, 5312, 5709.

As the size of the cannabis industry continues to increase, the need and the demand for insurance in the cannabis industry correspondingly increases. State insurance regulators will be forced to deal with the intersection of cannabis and insurance. They should be ready by educating themselves about the cannabis industry and the various types of insurance risks associated with it.

This white paper will focus on the federal, state and local authority; seed-to-sale operations; the type, scope and availability of coverage and insurance gaps; and regulatory best practices and recommendations. State insurance regulators, should they choose to do so, can play an important role in encouraging insurers to write insurance for the cannabis industry.

II. OVERVIEW OF KEY AUTHORITIES

A. FEDERAL AUTHORITY

Legalization of cannabis for any purpose is a topic that has been discussed and debated for decades. While cannabis was once prohibited nationwide, in the 1970s, 12 states either removed or reduced the penalties for possession of small amounts of cannabis.[16] By the late 1970s, the momentum had stalled and would remain that way until the beginning of the 21st century.

However, by 2018, 33 states; Washington, DC; and the territories of Guam and Puerto Rico had legalized the use of cannabis for medical reasons.[17] Eleven states, and Washington, DC, now also permit the recreational use of cannabis.[18] Certainly, the pendulum of public opinion has swung since the late 1970s, with fewer people seeing cannabis as harmful when compared to 20 years ago.[19] While one reason for this change may be generational, public opinion has perhaps also been swayed by the rise in laws permitting the use of medical marijuana.

"Medical marijuana" refers to the use of cannabis, which may involve use of the entire plant or its extracts—most frequently, delta-9-tetrahydrocannabinol (THC) and/or cannabidiol (CBD)—as a physician-recommended form of medicine to treat symptoms of

16. Alaska, California, Colorado, Maine, Minnesota, Mississippi, Nebraska, New York, North Carolina, Ohio, Oregon and South Dakota. (South Dakota later reversed its decriminalization of the drug.)

17. National Conference of State Legislators,2018. "State Medical Marijuana Laws," accessed at www.ncsl.org/research/health/state-medical-marijuana-laws.aspx.

18. National Conference of State Legislators,2018. "State Medical Marijuana Laws," accessed at www.ncsl.org/research/health/state-medical-marijuana-laws.aspx.

19. Bachman, J.G., L.D. Johnston, P.M. O'Malley, and J.E. Schulenberg, 2012. "Monitoring the Future National Survey Results on Drug Use, 1975–2011," *Vol. I: Secondary School Students,* Ann Arbor, MI: Institute for Social Research, University of Michigan.

illness and other conditions.[20] By 2019, 12 states had enacted laws permitting the use of products rich in CBD, which does not have psychoactive effects. Currently, the U.S. Food and Drug Administration (FDA) has not recognized or approved the use of cannabis as medicine, due to its classification as a Schedule I substance under the federal Controlled Substances Act (CSA) of 1970. However, researchers continue to explore its possible uses for medical treatment. Now that hemp-derived CBD is legal, retailers continue to sell CBD products in all 50 states, claiming that they are derived from industrial hemp plants and, therefore, are legal. To date, this is a position that has received mixed treatment from the federal government.[21][22]

While not addressing every law or regulation that may apply to cannabis-related businesses or consumption, the following section will illustrate the myriad of laws that may complement or contradict each other. As will be seen, the legal and regulatory framework governing cannabis is in a constant state of flux. This constant change has led to great uncertainty in the cannabis industry with regard to business operations throughout the industry.

Signed into law by President Richard Nixon on Oct. 27, 1970, the CSA[23] is the federal U.S. drug policy under which the manufacture, importation, possession, use and distribution of certain narcotics, stimulants, depressants, hallucinogens, anabolic steroids and other chemicals are regulated. Any addition, deletion or change to schedule designation of a medicine or substance may be requested by the U.S. Drug Enforcement Agency (DEA), the U.S. Department of Health and Human Services (HHS), the FDA or from any other party via petition to the DEA.

The DEA implements the CSA and may prosecute violators of the laws set forth in the CSA at both the domestic and international level. Within the CSA, there are federal schedule designations (I–V) that are used to classify drugs based upon their:

- Abuse potential
- Accepted medical applications in the U.S.
- Safety and potential for addiction[24]

20. National Institute on Drug Abuse, 2018. "Marijuana as Medicine," accessed at www.drugabuse.gov/publications/drugfacts/marijuana-medicine.

21. *High Times*, 2017. "DEA: CBD Oil Is Not 'Legal in All 50 States,'" accessed at https://hightimes.com/news/politics/dea-cbd-oil-is-not-legal-in-all-50-states, but see W.M. Schuster and J. Wroldsen, 2018. "Entrepreneurship and Legal Uncertainty: Unexpected Federal Trademark Registrations for Marijuana Derivatives," *American Business Law Journal*, (55)1: 117.

22. The U.S. Food and Drug Administration (USDA) issued a memo regarding hemp provisions in the 2018 Farm bill, accessed at https://www.ams.usda.gov/sites/default/files/HempExecSumandLegalOpinion.pdf.

23. Controlled Substances Act of 1970, 21 U.S.C. § 801, *et seq*.

24. Drugs.com, 2018. "CSA Schedules," accessed at www.drugs.com/csa-schedule.html.

Cannabis is regulated as a Schedule I substance. Schedule I substances are those that have a high potential for abuse and for which there are currently no accepted medical uses in treatment in the U.S.[25]

At the federal level, the government's authority to regulate and control cannabis can be broken into three distinct categories: 1) criminal; 2) administrative; and 3) civil. While these categories are not mutually exclusive and often overlap, conceptualizing the federal level of control in this way is helpful to understand how federal law regulates cannabis and interacts with state and local law. It is also important to bear in mind that the executive, legislative and judicial branches of the federal government all have a role to play in each of these categories, and often, each branch seems to take a different approach in the regulation and control of cannabis.

B. Federal Criminal Laws

As mentioned above, cannabis is a Schedule I drug for purposes of the CSA, which triggers certain other federal criminal statutes. Of primary concern for this section, cannabis' prohibited status triggers three main federal criminal laws when individuals engage in transactions involving cannabis or proceeds from cannabis. The first, the federal Bank Secrecy Act (BSA),[26] requires financial institutions to report to the Treasury Department any transactions over $5,000 that the institution knows, or has reason to know, involve assets derived from illegal sources.

"Financial institution" is defined broadly and includes banks, credit unions, broker-dealers, insurance companies, pawnbrokers, travel agencies and a host of other institutions that may come into contact with assets derived from illegal sources. Because cannabis is a prohibited substance, any institution that transacts business with a cannabis or cannabis-related entity is subject to these reporting requirements. The penalty for a violation of the BSA is severe: up to a $250,000 civil penalty and up to five years in prison. Any transaction associated with a cannabis business must be reported under the BSA, even if that activity is legal under state law, and a violation of the BSA may result in a financial institution's loss of its charter.

The second federal statute implicated in transactions involving cannabis is the money laundering statute.[27] This statute makes it a felony for any person to engage in a financial transaction that the individual knows involves the proceeds of an unlawful activity. Because cannabis is a prohibited substance, any transaction that derives proceeds,

25. U.S. Drug Enforcement Administration, 2018. "Drug Scheduling," accessed at www.dea.gov/drug-scheduling.
26. 31 U.S.C. §§ 5301, et. seq.
27. 18 U.S.C. §§ 1956–7.

directly or indirectly, from cannabis transactions could be considered money laundering for the purposes of the money laundering statute. The penalties for violating this statute are severe: up to a $500,000 civil penalty or twice the value of the property involved in the transaction, whichever is greater, and up to 20 years in prison.

The third federal statute implicated by cannabis transactions is the unlicensed money transmitter statute.[28] Under this statute, it is a felony to engage in an unlicensed money transmitting business. The statute defines "unlicensed money transmitting business" to include a transaction that involves the transportation or transmission of funds that are known to have been derived from a criminal offense or are intended to be used to promote unlawful activity. Because of this definition, any transaction that involves the transmission or transportation of funds derived, directly or indirectly, from the cannabis industry is a violation of the unlicensed money transmitter statute and subjects the individual to up to five years' imprisonment.

In enforcing these statutes, the executive branch has, on the one hand, been consistent and on the other hand inconsistent. Regarding clearly illegal cannabis activities, the executive branch has been consistent in its enforcement and prosecution of such activities. However, the executive branch has been less consistent in its treatment of cannabis in states where it has become legal. For example, in February 2014, then Deputy Attorney General James Cole issued a memorandum that announced guidance to U.S. Department of Justice (DOJ) attorneys on the Obama administration's priorities in the prosecution of cannabis-related federal crimes.[29] Intended to update federal guidance considering ongoing changes to state laws, it applied to all federal enforcement activity, both civil and criminal, in all states.

Noting that the DOJ had previously issued memoranda setting forth federal enforcement priorities in jurisdictions that authorized cannabis cultivation and distribution for medical use, Deputy Attorney General Cole concluded that, with some exceptions, the federal government would again exercise discretion in its enforcement determinations in jurisdictions that had implemented strong, effective regulatory and enforcement systems to control the cultivation, distribution, sale and possession of cannabis for industrial or recreational use.[30] While noting that any cannabis transaction was prosecutable, the Cole

28. 18 U.S.C. § 1960.
29. U.S. Department of Justice, 2014. "Guidance Regarding Marijuana Related Financial Crimes," accessed at www.justice.gov/sites/default/files/usao-wdwa/legacy/2014/02/14/DAG%20Memo%20-%20Guidance%20Regarding%20Marijuana%20Related%20Financial%20Crimes%202%2014%2014%20%282%29.pdf.
30. Continued priorities included preventing the distribution of marijuana to minors and preventing revenue from the sale of marijuana going to criminal enterprises.

Memorandum indicated that the DOJ would not actively seek to prosecute legalized cannabis transactions.

The exceptions to the Cole Memorandum were eight federal priorities for prosecution, including criminal enterprises, sale to minors, growing cannabis on public grounds, and preventing diversion of legal cannabis into states where cannabis was illegal. However, in January 2018, former Attorney General Jeff Sessions rescinded the Cole Memorandum by way of his own memorandum that emphasized the DOJ's "well-established principles" with regard to the prosecution of cannabis crimes.[31] While the memorandum did not specifically address legalized cannabis, it did indicate a return to a more active DOJ role in regulation and control of cannabis. The federal guidance previously issued by former Attorney General Sessions leaves financial institutions that now accept money from cannabis-related businesses potentially exposed to violations of federal law, including money laundering statutes. In 2019 Attorney General William Barr indicated he will not pursue cannabis businesses that are operating legally within their state jurisdiction.[32] Insurers have no assurance that the Attorney General's comments extend to financial institutions engaging with cannabis businesses, nor, is there any guarantee that this policy extends beyond the tenure of the Attorney General who made the statement. Insurers must assess a business risk decision, including legal risks and financial implications, about whether they will provide services to the cannabis industry.

The federal judiciary has been more consistent in its interpretation of the CSA and related cannabis prohibitions. The U.S. Supreme Court, in its landmark 2005 *Gonzales v. Raich* opinion, reaffirmed the supremacy of the CSA over state legalization statutes.[33] Since the *Gonzales* decision, the judiciary has upheld criminal prosecutions involving cannabis transactions, even where legalized at the state level. To date, the Supreme Court has not expressed a willingness to revisit the *Gonzales* decision. Similarly, lower federal courts have shown a reluctance to address the issue of state legalized cannabis.

In February 2018, a federal judge dismissed a lawsuit seeking to legalize cannabis under federal law. The plaintiffs in that suit argued that the CSA's classification of cannabis as a Schedule I substance is unconstitutional and that the federal cannabis policies in the U.S. discriminate against minorities. In dismissing the suit, the judge found that the plaintiffs should first petition the DEA to ask that it be removed from the list of dangerous substances, as that agency, along with the FDA, oversees the classification and

31. U.S. Department of Justice, 2018. "Marijuana Enforcement."
32. CBS News, 2019. "Trump's Attorney General Nominee May Shift Policy on Marijuana Enforcement," accessed at www.cbsnews.com/news/william-barr-on-marijuana-legalization-attorney-general-nominee/.
33. *Gonzales v. Raich*, 545 U.S. 1 (2005).

scheduling of the drug. Given these judicial developments, state legalization of cannabis does not pose a bar to prosecution in the federal judiciary.[34]

The legislative branch, however, has been ambivalent to state-legalized cannabis. In 2003, in the face of several states legalizing cannabis on some level, U.S. Rep. Maurice Hinchey (D-NY) brought an amendment to the House floor that would have prohibited the DOJ from expending funds to prosecute state-legalized medical cannabis operations.[35] While this amendment would ultimately fail by a 152-273 vote, by 2014 the amendment was revived by U.S. Rep. Dana Rohrabacher (R-CA) and had been included as an amendment to the 2014 omnibus spending bill.[36] Since the enactment of this amendment, Congress has reapproved it yearly in appropriations bills. Other legislative enactments, however, have seen less enthusiasm from Congress.

On June 7, 2018, U.S. Sen. Cory Gardner (R-CO) and U.S. Sen. Elizabeth Warren (D-MA) introduced the Strengthening the Tenth Amendment Through Entrusting States (STATES) Act (S. 3032 and H.R. 6043). The STATES Act was aimed at amending the CSA to exempt cannabis-related activities that were in accordance with state laws. It also sought to protect banks working with cannabis businesses and legalize at the federal level the cultivation of industrial hemp. As of June 2019, The STATES Act has been introduced this congressional session (S. 1028 and H.R. 2093). .

In March 2019, the House Financial Services Committee voted in favor of advancing the SAFE Banking Act (H.R. 1595), which would allow cannabis businesses to work with banks and credit unions.[37] It would bar federal regulators from terminating a bank's FDIC deposit insurance, a threat that prevents most banks from accepting cannabis businesses. One of the greatest obstacles of entry for admitted market insurers is the threat of felonious liability under federal law. The SAFE Banking Act would remove some of the direct conflict between state and federal law barriers for insurer and broker participation in the cannabis market. As of June 2019, H.R. 1595 has been discharged from the Judiciary Committee. The bill's advancement is a significant step for the cannabis industry. With the bill's passage, it is likely that more banks would open their doors to cannabis businesses. In turn, cannabis businesses would be able to operate as normal businesses. The regulatory landscape of the cannabis industry is evolving rapidly.

34. Huddleston Jr., T., 2018. "Why a Federal Judge Dismissed a Lawsuit That Could Have Legalized Marijuana Nationwide," *Fortune Magazine* accessed at *http://fortune.com/2018/02/27/federal-judge-dismiss-lawsuit-marijuana-legalization-jeff-sessions*. *See also, Bortell, et al. v. Sessions, et al.*, Case No. 1:17-cv-5625, U.S. District Ct. for the Southern District of New York.

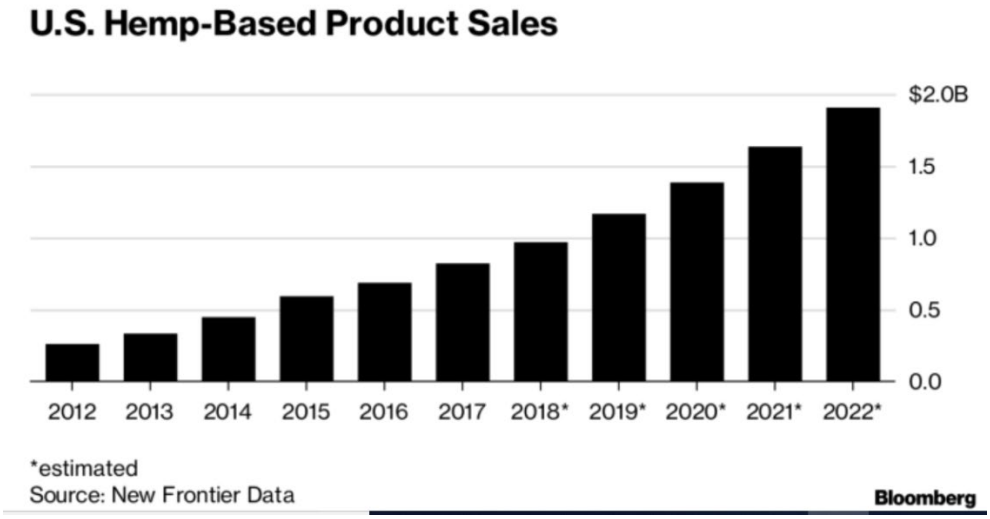
35. Departments of Commerce, Justice, and State, the Judiciary, and Related Agencies Appropriations Act, 2004, H.R. 2799, H. Amdt. 297 (2003).

36. Commerce, Justice, Science, and Related Agencies Appropriations Act, 2015, H.R. 4660, H.Amdt.748 (2014).

37. Congress.gov. Accessed at https://www.congress.gov/bill/116th-congress/house-bill/1595/all-actions?overview=closed#tabs.

Thus, it's critical to stay up-to-date on federal and state cannabis-related legislation. Doing so ensures the insurance industry's underwriting risk assessment and client policy advisement reflects recently passed laws.

Recent developments on both the federal and state levels support the notion that as the commercial investment and scientific research intersect with changing public attitudes about cannabis usage, the risk management portfolio of firms on the supply side will expand to meet market needs. With passage of the new Farm Bill in 2018, Congress moved to fully legalize hemp,[38] opening the way for broad distribution of CBD products and creating the first cannabis market insurers may find to be a much more palatable risk. The United States Department of Agriculture (USDA) also subsequently issued a memorandum on new hemp authorities.[39]



Driving demand is CBD, a non-psychoactive cannabinol that can be derived from hemp or cannabis. CBD is one of the substances in cannabis, but in hemp, it comes with no mind-altering effect from THC. Proponents say CBD helps relieve pain, anxiety, nausea and inflammation. Currently sold mostly online and in specialty shops, CBD can be found in oils, candies, capsules and even sparkling water. In June 2018, the FDA approved the first CBD-based medicine, Epidiolex, made by GW Pharmaceuticals to treat childhood epilepsy.

38. Kaskey, J., 2018. "Pending Legislation Makes Insurance Available to Hemp Growers," *Property Casualty 360*, accessed at www.propertycasualty360.com/2018/11/29/pending-legislation-makes-insurance-available-to-hemp-growers/?slreturn=20190312125750.

39. The U.S. Food and Drug Administration (USDA) issued a memo regarding hemp provisions in the 2018 Farm bill, accessed at https://www.ams.usda.gov/sites/default/files/HempExecSumandLegalOpinion.pdf.

C. Federal Regulatory Level

At the federal regulatory level, state-legalized cannabis faces numerous challenges as individuals engaged in business in the cannabis industry attempt to navigate a host of complex federal regulatory regimes. While it is impossible to enumerate every point at which the cannabis industry interacts with federal regulatory regimes, some of these include banking, finance and insurance; securities; environmental protection; intellectual property; taxation; and agriculture, just to name a few.

D. Financial Services Sector

The first area of regulatory authority is in the financial services sector. As noted above, many of the criminal laws that are implicated by legalized cannabis are financially orientated, and lack of access to banking and financial services even in states where cannabis is legal is a significant issue. For example, in order to comply with the BSA, financial institutions must send Suspicious Activity Reports (SARs) to the Treasury Department when the institution is involved in a transaction involving funds over $5,000 that the institutions knows, or has reason to know, come from illegal sources, such as cannabis.[40]

Beyond mere compliance with federal criminal law, a host of other regulations complicate financial transactions involving legalized cannabis. For example, for financial institutions to be able to transmit funds electronically through the Federal Reserve's electronic network, the institution must have a master account with the Federal Reserve. However, the Federal Reserve has been reluctant to provide master accounts to institutions that deal exclusively in legal cannabis due to the federal prohibition on cannabis, leaving such institutions without the ability to transmit money.[41] There are exceptions such as Colorado, which has a limited scope and strict parameters, but it does have a Federal Reserve account. Even where cannabis businesses attempt to raise funds outside the ordinary banking system, federal regulations may pose a barrier. If a cannabis business seeks to raise capital through the issuance of securities, such securities must be registered by the U.S. Securities and Exchange Commission (SEC) unless the security falls within an exemption.[42] It is unclear whether the SEC would approve such securities given the prohibited status of cannabis.

40. 31 CFR § 1020.320.
41. *Fourth Corner Credit Union v. Federal Reserve Bank of Kansas City*, 861 F.3d 1052 (10th Cir. 2017).
42 Frank Robison, *Going Green: Legal Considerations for Marijuana Investors and Entrepreneurs*, 6 A. U. Bus. L. Rev. 57 (2016).

In response to these concerns, and in recognition of the Obama administration's deprioritizing of criminal prosecution of cannabis-related businesses in cases where they are otherwise compliant with the laws of the state in which they are operating, on February 14, 2014, FinCEN issued its own guidance. This guidance was intended to clarify how financial institutions can provide services to such businesses while remaining compliant with their obligations under the BSA. It instructed financial institutions providing such services—when they reasonably believed, based on their due diligence, that a given business did not implicate the Cole Memorandum's priorities or state law—to file a "Marijuana Limited" SAR. Further, a financial institution that reasonably believed a cannabis-related business *was* violating a Cole Memorandum priority or state law was instead instructed to file a "Marijuana Priority" SAR, and FinCEN's guidance set forth the "red flags" that would suggest the business was engaged in such activity.[43] Despite the guidance issued by Attorney General Sessions in 2018, FinCEN has stated that the structure set forth in its 2014 guidance remains in place.[44] What FinCEN's guidance did not and could not do, however, was amend federal law or grant immunity to a financial institution providing services to a cannabis-related business.

Despite FinCEN's guidance, the number of financial institutions accepting this risk dropped slightly in the months that immediately followed its issuance. It has, however, grown steadily since then. According to FinCEN, by the end of March 2018, 411 banks and credit unions were "actively" operating accounts for marijuana-related businesses.[45] States continue their attempts to navigate these murky waters between federal and state law. By way of example, in 2014, Colorado passed a law that would allow the formation of "cannabis credit co-ops." These co-ops were to function similarly to a credit union and had restrictions on the number of businesses they could serve.[46] Despite the passage of this bill, no co-ops have been formed under this law.[47] Several other state initiatives have been introduced since.[48] On July 3, 2018, the New York State Department of Financial Services published its own guidance to encourage banks and credit unions to offer services to marijuana-related businesses licensed by the state and advised them to continue to follow FinCEN's 2014 guidance. Still, given the risk of not only losing their

43. Those subject to FinCEN's regulations were still required to report currency transactions in connection with marijuana-related business the same as they otherwise would.

44. Angell, T., 2018. "Congressional Committee Protects Medical Marijuana from Jeff Sessions," *Forbes*, accessed at www.forbes.com/sites/tomangell/2018/05/17/congressional-committee-protects-medical-marijuana-from-jeff-sessions/#546c1ca11e55.

45. Angell, T., 2018. "More Banks Working With Marijuana Businesses, Despite Federal Moves," *Forbes*, accessed at www.forbes.com/sites/tomangell/2018/06/14/more-banks-working-with-marijuana-businesses-despite-federal-moves/#39002b6b1b1b.

46. House Bill 14-1398. Accessed at www.leg.state.co.us/clics/clics2014a/csl.nsf/fsbillcont3/06F7F4159729909387257CCA0082B929?Open&file=1398_enr.pdf.

47. Miyoga, D., 2014. "Promise for Pot-Banking Co-Op Sees Little Progress Since It Was Law," *The Denver Post*, accessed at www.denverpost.com/marijuana/ci_26525249/promise-pot-banking-co-op-sees-little-progress.

48. Morton, H., 2018. "2014–2018 Financial Institutions and Cannabis/Hemp/Marijuana Legislation," National Conference of State Legislators Legislative Summit, accessed at https://comm.ncsl.org/productfiles/112183917/Financial_Institutions_Cannabis_Hemp.pdf.

charter but also the threat of facing criminal prosecution for a federal offense, many financial institutions have been hesitant to embrace the cannabis business.

E. Intellectual Property

The cannabis industry faces other complications related to federal regulation. One example of this is in the area of intellectual property. As the cannabis industry has become legitimized, many cannabis businesses such as growers, distributors, and retailers have sought to protect their intellectual property in brand names, business names and similar identifiers. However, the U.S. Patent and Trade Office (USPTO) has historically taken the position that trademarks cannot be granted to applications promoting or involving illegal conduct.[49] To date, the USPTO has not approved any filings for trademarks or copyrights for products related to cannabis. Interestingly, however, the USPTO has approved trademarks for certain cannabis derivatives. Specifically, the USPTO has approved trademarks for specific types of CBD products. As noted above, these approvals stemmed from confusion as to whether CBD was illegal under the CSA. This confusion has since been resolved. However, the CBD trademarks are still valid and still exist. Thus, while the USPTO has seemed to take a straightforward approach to the registration of cannabis trademarks, there is still some inconsistency in how the USPTO previously handled such trademarks.

F. Environmental and Agricultural Regulations

One last area of interest worth noting is the cannabis industry's interaction with environmental and agricultural regulations. Cannabis, after all, is an agricultural product, which gives rise to environmental concerns. There are two key areas of concern at the federal level in this regard: 1) the federal Clean Water Act (CWA); and 2) the provision of water rights from federally administered facilities. The CWA regulates, in part, the pollution generated by agriculture operations. However, the CWA relies, in large part, on federal-state cooperation.[50] The CWA is largely implemented at the state level using federal funds and grant projects. Given the prohibited status of cannabis at the federal level, it is unclear whether such grants would be available to states for cannabis remediation projects. Indeed, state programs aimed at environmental cleanup and

49. Schuster, W.M. and J. Wroldsen, 2018. "Entrepreneurship and Legal Uncertainty: Unexpected Federal Trademark Registrations for Marijuana Derivatives," *American Business Law Journal*, 55(1): 117.

50. Stoa, R.B., 2017. "Marijuana Agriculture Law: Regulation at the Root of an Industry," Florida Law Review, (69)2: 297. U.S. Department of Justice, 2014. "Guidance Regarding Marijuana Related Financial Crimes," accessed at https://scholarship.law.ufl.edu/cgi/viewcontent.cgi?article=1361&context=flr.

partnership with the cannabis industry have been subject to federal raids and subpoenas.[51]

An additional agricultural concern arises regarding water rights and irrigation. In particular, regulatory complexities arise for cannabis growers in the western U.S., who must contend with the U.S. Bureau of Reclamation (USBR). The USBR is the largest wholesaler of water in the U.S. and provides one out of five western farmers with irrigation water.[52] Because of the prohibited status of cannabis under the CSA, the USBR has issued guidance stating that it will not approve the use of its facilities for the cultivation of cannabis.[53] As such, cannabis cultivators and growers may find it difficult to find the water sources necessary to support their growth operations.

G. Civil Level

At the civil level, the federal judiciary has created confusion as to civil obligations. This section will highlight two of significant importance: 1) the enforceability of contracts; and 2) the ability to declare bankruptcy. The enforceability of contracts brings questions on whether contracts involving cannabis transactions are void against public policy. Without guidance from the U.S. Supreme Court, lower courts have been left to address this issue as a matter of first impression.

In *Tracy v. USAA Casualty Insurance Company*, the District Court for the District of Hawaii was asked to determine whether a contract of insurance was enforceable against an insurer in order to provide coverage for legal cannabis plants that had been lost during a fire.[54] The Court in that case determined that since cannabis is illegal under the CSA, the Court would decline enforcing the contract on the grounds that it was against public policy. As such, no coverage was available under the policy. The opposite conclusion was reached in the District Court for the District of Colorado. In *Green Earth Wellness Center, LLC v. Atain Specialty Insurance Company*, the Court was asked whether a policy of insurance could cover legal cannabis plants that were damaged due to a wildfire.[55] In addressing the "void as against public policy" argument, the Court reasoned that over the years, the federal public policy had eroded; thus, there no longer existed a clear and consistent public policy against legalized cannabis. As such, the Court expressly declined to follow *Tracy* and found that the contract of insurance provided coverage for legal cannabis plants. While there appears to be a trend of courts following *Green Earth* as

51. Flatow, N., 2013. "How the Drug Enforcement Administration Killed a County Program to Police Pot," accessed at https://thinkprogress.org/how-the-drug-enforcement-administration-killed-a-county-program-to-police-pot-91815d4e5148/.
52. Bureau of Reclamation. "About Us – Fact Sheet," accessed at www.usbr.gov/main/about/fact.html.
53. Bureau of Reclamation. "Use of Reclamation Water or Facilities for Activities Prohibited by the Controlled Substance Act of 1970," accessed at www.usbr.gov/recman/temporary_releases/pectrmr-63.pdf.
54. *Tracy v. USAA Casualty Insurance Company*, No. 11-00487 LEK-KSC, 2012 WL 928186 (Mar. 16, 2012 D. Haw).
55. *Green Earth Wellness Center, LLC v. Atain Specialty Insurance Company*, 163 F.Supp.3d 821 (D. Colo. 2016).

opposed to *Tracy*, until there is a definitive ruling on this issue by the Supreme Court, the enforceability of contracts involving cannabis will still be a point of contention.

One last area of concern at the civil level is the ability of cannabis-related businesses to declare bankruptcy. The ability of a business to seek bankruptcy protection is essential to a business when operations prove unsuccessful. However, this tool may not be available to cannabis-related businesses. In the case *In re: Arenas*, the 10th Circuit Court of Appeals was asked to determine the availability of bankruptcy protections for cannabis growers.[56] In that case, after litigation returned a negative verdict against the cannabis growers, the growers sought bankruptcy protection. The U.S. Trustee objected to the bankruptcy, and the bankruptcy court dismissed the petition due to the criminal nature of the business. The 10th Circuit affirmed the dismissal, reasoning that since the substantial assets of the estate were cannabis, and since cannabis was illegal under federal law, the U.S. Trustee could not administer the bankruptcy estate without violating federal law.[57] As such, the Court ruled that dismissal of the bankruptcy was permissible. As with the enforceability of contracts, until guidance is provided by the Supreme Court, there will be uncertainty as to whether bankruptcy protections are available to cannabis-related businesses. In addition, different states have distinctive laws allowed in bankruptcies, such as a homestead exemption, so there are no general bankruptcy laws applicable to all states.

H. McCarran-Ferguson Act

One of the areas unique to insurance is how the federal laws affecting cannabis interact with the federal McCarran-Ferguson Act.[58] The McCarran-Ferguson Act precludes federal law from preempting state law regarding the business of insurance unless the federal law specifically relates to the business of insurance. Arguments have been made that because the CSA does not specifically apply to the business of insurance, state laws governing cannabis insurance are not preempted; therefore, states are free to engage the cannabis insurance industry without concern of federal liability.[59] However, the nuances of how federal cannabis laws interact with the federal McCarran-Ferguson Act have not been clearly explored, and uncertainty still exists in this regard.

While it is true that the CSA does not specifically relate to the business of insurance, this, in and of itself, does not save a state statute regulating cannabis insurance from

56. *In re Arenas*, 535 B.R. 845 (10th Cir. 2015).
57. *See also*, *In re Rent-Rite Super Kegs West Ltd*, 484 B.R. 799 (D. Colo. 2012) (Dismissing a Bankruptcy Petition Because Marijuana Remains Illegal Under the CSA).
58. 15 U.S.C. § 1011.
59. Queen, M., 2017. "The Growing Cannabis Industry and Captive Insurance," *Insurance Journal*, accessed at www.insurancejournal.com/magazines/magfeatures/2017/10/16/467075.htm.

preemption. While the fixing of rates, regulation of advertising of insurance policies, and the licensing of companies and their agents are clearly the business of insurance and, therefore, are not subject to preemption under the federal McCarran-Ferguson Act,[60] other aspects of cannabis insurance regulation are not so clearly regulating the business of insurance as to prevent preemption. For example, the Supreme Court has held that priority provisions of state insolvency law, to the extent that they are attempting to provide for priority of payments beyond policyholders, are not saved from preemption under the federal McCarran-Ferguson Act.[61] Thus, state insurance regulators may find that their authority to orderly liquidate an insurer may, to a greater or lesser extent, be preempted by the CSA.

Another example of where a state's law may not be protected by the federal McCarran-Ferguson Act is in the field of corporate transactions. While the licensing of insurers is clearly protected by the federal McCarran-Ferguson Act, the Supreme Court has held that the SEC may unwind transactions that are in violation of federal securities law.[62] Therefore, a state insurance regulator may approve a transaction involving a cannabis insurer only to see it unwound by the SEC on the grounds of illegality.

Putting aside the CSA, other federal laws directly affecting the cannabis insurance industry are clearly not protected by the federal McCarran-Ferguson Act. Specifically, the criminal statutes mentioned above (the BSA, the money laundering statutes and the unlicensed money transmitted statute) are all not subject to the anti-preemption provisions of the federal McCarran-Ferguson Act. This is because each of these laws specifically relates to the business of insurance. Each of these acts specifically defines financial institutions to include insurers[63]; therefore, on the statutes' face, the anti-preemption provisions of the federal McCarran-Ferguson Act do not apply. As such, the federal government may enforce these criminal provisions against both the industry and potentially state insurance regulators. Indeed, courts that have been faced with the question of whether the federal McCarran-Ferguson Act bars prosecution under these statutes have found no such bar to exist.[64]

Despite issues at the federal level, states recognize the additional revenue that could be generated by the sale of cannabis, and those that currently have this income stream are using it to fund projects they may not otherwise have been able to afford. For example, Colorado is using the first $40 million of tax revenue to fund school construction costs, and Nevada intends to earmark 40% of its wholesale tax to the state's Distributive School

60. *Securities and Exchange Commission v. National Securities, Inc.*, 393 U.S. 453, 460 (1969).
61. *U.S. Department. of Treasury v. Fabe*, 508 U.S. 491 (1993).
62. *SEC v. National Securities, Inc.*, 393 U.S. 453, 460 (1969).
63. 31 U.S.C. § 5312(a)(2)(M); 18 U.S.C. § 1956(c)(6)(A).
64. *U.S. v. Blumeyer*, 114 F.3d 758 (8th Cir. 1997); *U.S. v. Cavin*, 39 F.3d 1299 (5th Cir. 1994).

Account (DSA). Others intend to use the extra money to fund drug treatment and enforcement programs.[65]

The additional revenue, however, may not come without a cost. To balance public safety concerns with the rights of individual users, cities and towns are also beginning to regulate the use of medical and recreational cannabis. The myriad of local laws further complicates the landscape as evidenced by the attempt to summarize the specific policies for all 482 cities in the state of California.[66] This summary serves to further illustrate the patchwork of laws and lack of uniformity with respect to this issue.

III. SEED-TO-SALE OPERATIONS—AN OVERVIEW AND ARCHITECTURE OF THE CANNABIS INDUSTRY

A. OVERVIEW

States have taken varying approaches to regulating the cannabis industry. While some states regulate medical and recreational cannabis separately, others have delegated authority to a single administrative agency. For example, Oregon has had a medical cannabis program since 1998 and a recreational program since 2016. The medical program is run by the Oregon Health Authority (OHA), which registers and regulates medical cannabis patients, medical cannabis growers, grow sites, processors, dispensaries and caregivers. OHA also promulgates cannabis testing rules. The recreational program is run by the Oregon Liquor Control Commission (OLCC), which licenses producers, wholesalers, processors, laboratories, retailers and researchers. The OLCC also issues permits for individual workers in the recreational cannabis industry.

In contrast, both medical and recreational cannabis in Colorado are regulated by the Colorado Department of Revenue (DOR). Medical cannabis was decriminalized through an amendment (Amendment 20) to the Colorado Constitution in 2000. Recreational cannabis was added in 2012 (Amendment 64).

Colorado and Oregon represent two versions—one separate and one unified—of the regulation of the cannabis industry. As cannabis remains illegal under federal law, individual states have, and increasingly are, legalizing parts of the cannabis industry and setting up regulatory structures unique to their respective states. It can be anticipated that

65. Wells Fargo Advisors, 2018. "Trump May Support Less Federal Intrusion on State Marijuana Laws," accessed at *www.wellsfargoadvisors.com/research-analysis/asg/marijuana-impacts-on-municipal-bonds.htm*.

66. The Cannifornian, 2018. "Searchable Database: See How Cannabis Laws, Support Differ Among California Cities," accessed at *www.thecannifornian.com/cannabis-business/database-see-cannabis-laws-support-differ-among-california-cities/*.

as these regulatory structures mature, there will be increased emphasis on unification and coordination to avoid regulatory pressure points caused by differing legal and regulatory schemes.

B. Cultivation

The cannabis cultivation component of the industry has developed along two paths: 1) a "cottage" industry of small-scale craft cultivation (i.e., cultivation for home and/or personal use); 2) and the development of large-scale producers engaged in cannabis as a commercial crop. There are further subdivisions between recreational and medicinal cannabis.

States typically allow residents to grow a limited number of home-grown cannabis plants for personal use,[67] while registered medical and recreational cannabis caregivers can produce in greater quantities. Registered medical cannabis producers are often required by states to be vertically integrated in some way with the rest of the supply chain. For example, registered growers in Oregon must be designated by a patient to produce cannabis on their behalf. The patient may designate themselves or another person as their grower. There are 16,600 registered growers who are producing at 13,959 grow sites.

In Colorado, medical cannabis caregivers who cultivate more than 36 plants must register with the Colorado Department of Public Health and Environment and disclose: 1) the location of each cultivation; 2) the cannabis registration identification number for each patient they serve; and 3) any extended plant count numbers (patients with physician recommendations exceeding six plants and their patient registry numbers).[68] As of December 2018, caregiver cultivation registrations numbered 1,963.[69]

Medical marijuana cultivators ("optional premises cultivation" (OPC) or "grow" operations) in Colorado must be vertically integrated or associated with a licensed medical marijuana center (a business that sells medical cannabis to patients or primary caregivers, but is not, itself, a primary caregiver) or a licensed manufacturer who creates products infused

67. Oregon residents are allowed up to four homegrown plants per residence. (ORS 475B.301) Colorado home grow laws allow no more than 12 plants in any residence. Counties and municipalities may have stricter laws in place. The plants must be kept in an enclosed, locked space and inaccessible to anyone under 21 years of age living in or outside of the residence. (Colorado Marijuana Official State Web Portal: www.colorado.gov/pacific/marijuana/home-grow-laws.

68. Colorado Department of Revenue, 2018. *2018 Sunset Reviews: Colorado Medical Marijuana Code and Colorado Retail Marijuana Code*, pp. ii, 57–58, accessed at www.colorado.gov/pacific/sites/default/files/2018%20Sunset%20reivew%20report.pdf.

69. Colorado Department of Public Health & Environment. "MED Caregiver Cultivation Registration," accessed at www.colorado.gov/pacific/enforcement/med-caregiver-cultivation-registration.

with medical cannabis intended for use/consumption other than by smoking.[70] There were 673 licensed medical cannabis cultivation entities in Colorado in January 2019.[71]

In contrast to the medical cannabis grow operations, the recreational side shows significantly larger-scale operations. In Oregon, there are 1,108 licensed recreational producers who participate in some aspect of producing, cultivating, growing and drying cannabis. In Colorado, there were 735 recreational cultivation entities in January 2019. Although there was a similar number of medicinal cultivation entities, the monthly average ratio of cannabis plants cultivated as of June 30, 2018, was almost 3:1 recreational over medicinal.[72]

There are often more stringent limits on the amount of medical cannabis that can be produced as compared to the limits for recreational cannabis. For example, in Oregon, the largest non-grandfathered medical-only producer is limited to 48 mature plants.[73] On the other hand, the largest-tier outdoor recreational producer is not limited by the number of plants and can produce on as much as 40,000 square feet of land.[74] In Colorado, recreational cannabis cultivators can grow up to 1,800 plants at a time (Tier 1), and after one harvest season of sales, may seek authorization to grow more plants at progressive increments up to the tier in excess of 13,800 plants (Tier 5).[75]

C. Distribution, Manufacturing and Delivery/Transportation

States have taken varying approaches to licensing the distribution, manufacturing and transportation of cannabis products. In Oregon, wholesalers purchase cannabis from licensed producers (cultivators). They may dry, trim, arrange for lab testing, package, store and deliver cannabis to retailers. There are 139 licensed wholesalers in Oregon.[76] Processors extract oils from cannabis plants and package them into vaporizers or vaporizer cartridges. Processors may also produce cannabinoid extracts and bulk oil used for manufacturing edibles or topical products. Edible manufacturers are required to obtain

70. Colorado Department of Revenue, 2018. *2018 Sunset Reviews: Colorado Medical Marijuana Code and Colorado Retail Marijuana Codes*, pp. 21 and 34, accessed at www.colorado.gov/pacific/sites/default/files/2018%20Sunset%20reivew%20report.pdf.

71. Colorado Marijuana Official State Web Portal, accessed at www.colorado.gov/pacific/med-resources-and-statistics.

72. Colorado Department of Revenue, 2018. *MED 2018 Mid-Year Update*, pp. 4–6; accessed www.colorado.gov/pacific/sites/default/files/MED%202018%20Mid%20Year%20Update.pdf.

73. ORS 475B.831.

74. OAR 845-025-2040.

75. Colorado Department of Revenue, 2018. *2018 Sunset Reviews: Colorado Medical Marijuana Code and Colorado Retail Marijuana Code*, Oct. 15, 2018, pp. 19 and 28; accessed at www.colorado.gov/pacific/sites/default/files/2018%20Sunset%20reivew%20report.pdf.

76. Oregon Liquor Control Commission, November 2018. For current data, visit www.oregon.gov/olcc/marijuana/Documents/mj_app_stats_by_county.pdf.

a processor license. There are 204 licensed processors in Oregon, with three registered processors in the medical cannabis program.[77,78]

Colorado's regulatory system is different in that a cultivation facility is licensed to cultivate, prepare and package recreational cannabis and sell it to retail stores, product manufacturing facilities or other retail cultivation facilities. Consequently, Colorado does not have a wholesaler category. However, it does have separate categorizations for medicinal and recreational manufacturers who concentrate and make products for consumption other than by smoking, including edibles, ointments and tinctures.[79] There are 239 medical infused product manufacturers and 282 recreational product manufacturing facilities in Colorado as of January 2, 2019.[80]

In Oregon, an entity must be a licensed producer, wholesaler, processor, laboratory or retailer in order to transport cannabis. Wholesalers may provide transportation services to other licensees throughout the supply chain. Colorado's structure provides for licensure of a transporter. A medical cannabis transporter is a person or business that transports medical cannabis from one business to another and may include the provision of logistics, distribution and storage of medical cannabis and manufactured medical cannabis products. There are 10 medical cannabis transporters licensed in Colorado. On the recreational side, there are 13 transporters licensed in Colorado.[81]

D. Retail and Consumers

Retailers sell items directly to consumers. Medical cannabis dispensaries receive cannabis, immature cannabis plants or cannabis products and transfer them to a patient or a patient's caregiver. There are approximately five registered dispensaries in Oregon. Retailers are responsible for verifying the age of every customer for every purchase. Retailers may sell usable cannabis, cannabinoid products, cannabinoid extract or concentrate, immature plants, and cannabis seeds. There are 598 licensed recreational

77. Oregon Liquor Control Commission, November 2018. For current data, visit www.oregon.gov/olcc/marijuana/Documents/mj_app_stats_by_county.pdf.

78. Oregon Health Authority, 2018. *Oregon Medical Marijuana Program Statistical Snapshot October 2018*, accessed at www.oregon.gov/oha/PH/DISEASESCONDITIONS/CHRONICDISEASE/MEDICALMARIJUANAPROGRAM/Documents/OMMP%20Statistical%20Snapshot%2010-2018.pdf.

79. Colorado Department of Revenue, 2018. *2018 Sunset Reviews: Colorado Medical Marijuana Code and Colorado Retail Marijuana Code*, pp. 19 and 29, accessed at www.colorado.gov/pacific/sites/default/files/2018%20Sunset%20reivew%20report.pdf.

80. Colorado Department of Revenue, 2019. *MED Resources and Statistics*, as of Jan. 2, 2019, accessed at www.colorado.gov/pacific/enforcement/med-resources-and-statistics.

81. Colorado Department of Revenue, 2019. *MED Resources and Statistics*, as of Jan. 2, 2019, accessed at www.colorado.gov/pacific/enforcement/med-resources-and-statistics.

cannabis retailers in Oregon[82] and approximately 620 licensed cannabis retailers in California [83]

In Colorado, as of November 1, 2018, there are 477 distinct licensed medical cannabis centers; of those, there are 413 unique licensees. There are 547 distinct licenses held for recreational retail stores; of those, there are 457 unique licensees.[84] There are several products available to the consumer, which fall under the flower and non-flower categories. In Oregon, cannabis flower represented 54.4% of recreational sales in 2018, followed by concentrate/extract at 29.4% and edible products at 10.3%. All other products represent roughly 6% of sales.

The flower also holds most of the market share in Colorado at 54.1% of recreational and 61.2% of medicinal use.[85] In 2015, the non-flower products were about 25% of total sales. In 2017, the non-flower products sales jumped to 37.7% of the regulated market. The non-flower products include concentrate, edibles and non-edibles.

Recreational Sales by Type of Product

State	Flower	Extract/Concentrate	Edibles
OR (2018)	54.4%	29.4%	10.3%
CO (2017)	54.1%	23.4%	13.4%

E. Testing

Testing is an important regulatory component in the cannabis supply chain. States that have legalized the use of cannabis generally require that product be tested by a lab before distribution to a dispensary and sale to the consumer. Labs use a variety of testing methods based on different products (oils, shatter, wax, edibles, topical products, etc.) in

82. Oregon Liquor Control Commission, November 2018. For current data, visit www.oregon.gov/olcc/marijuana/Documents/mj_app_stats_by_county.pdf.

83. California Bureau of Cannabis Control, April 23, 2019, accessed at https://aca5.accela.com/bcc/customization/bcc/cap/licenseSearch.aspx

84. Colorado Department of Revenue, 2018. *MED Licensed Facilities*, as of Dec. 3, 2018, accessed at www.colorado.gov/pacific/enforcement/med-licensed-facilities.

85. Marijuana Policy Group, 2018. *Market Size and Demand for Marijuana in Colorado 2017 Market Update*, accessed at www.colorado.gov/pacific/sites/default/files/MED%20Demand%20and%20Market%20%20Study%20%20082018.pdf.

order to determine potency—the amount of THC, CBD and pesticide concentrations in the product. However, the testing and methodologies have not developed standardized metrics or methods, which leave these aspects open for future research.

All cannabis products in Oregon are required to be tested by a licensed laboratory before being sold to consumers. Laboratories test for contaminants, pesticides, solvents and potency. There are 23 licensed laboratories in Oregon.[86] In Colorado, under both the recreational and medical cannabis laws, regulated cannabis must be tested in five categories: 1) microbials (bacteria and fungi); 2) mycotoxins (toxins produced by fungi); 3) residual solvents; 4) pesticides; and 5) potency. Licensed retail entities must submit samples of recreational cannabis and recreational cannabis products to a licensed testing facility for testing in the five categories. All medical cannabis products must be labeled with a list of all chemical additives that were used in the cultivation and production of a medical cannabis product. Persons holding a retail testing license may not have an interest in any other cannabis license, either recreational or medical.[87] Currently, there are 11 each of testing facilities for medical and recreational cannabis in Colorado.[88]

F. Tracking

Oregon and Colorado have several risk management requirements for cannabis-related businesses. Participants in the recreational and medical cannabis industries must use state-administered systems to track inventories throughout the production, processing, transportation, sale and testing of cannabis. Every plant is assigned a unique code and tracked through the supply chain in order to allow for more effective audits, to satisfy federal guidelines and to allow for product recalls when consumer safety issues are present.

G. Security

Most states require individuals who work in the cannabis industry to obtain some sort of license. The scope of the licensing laws may vary. For example, all employees who perform work on behalf of an Oregon licensed producer, processor, wholesaler or retailer—including, but not limited to, individuals who participate in the possession, securing, or selling of cannabis items—are required to possess a valid cannabis worker permit. In Colorado, all individuals who own or work for a licensed cannabis business

86. Oregon Liquor Control Commission, November 2018. For current data, visit www.oregon.gov/olcc/marijuana/Documents/mj_app_stats_by_county.pdf.

87. Colorado Department of Revenue, 2018. *2018 Sunset Reviews: Colorado Medical Marijuana Code and Colorado Retail Marijuana Code*, pp. 19 and 29; accessed at www.colorado.gov/pacific/sites/default/files/2018%20Sunset%20reivew%20report.pdf.

88. Colorado Department of Revenue, 2018. *MED 2018 Mid-Year Update*, pp. 4 and 6, accessed at www.colorado.gov/pacific/sites/default/files/MED%202018%20Mid%20Year%20Update.pdf.

must pass a fingerprint-based criminal history background check and demonstrate Colorado residency and financial responsibility. Cannabis businesses must also document their funding sources and ownership structure.

In Colorado and Oregon, all entities in the cannabis supply chain are required to implement certain security precautions, including:

- Video cameras that produce 24/7 high-quality, non-light dependent recordings of all areas where cannabis items are present.
- Armed alarm systems.
- Panic buttons or the equivalent to call for emergency services.
- The ability to lock and secure cannabis items at all times.

H. Existing Economic Impacts

The cannabis industry provides a significant source of jobs and tax revenue in states where it has been legalized. The market is characterized by steady growth. In jurisdictions where recreational cannabis was legalized after the legalization of medical cannabis, recreational production and sales have overtaken the medical side to be the dominant force in the market.

The legalization of cannabis provides employment opportunities directly within the cannabis industry, such as retail stores, dispensaries, cultivation, infused product manufacturing, transportation and laboratory testing. Additional ancillary jobs include security guards, construction and HVAC specialists, consulting, legal, and other business services. In Colorado, as of Nov. 1, 2018, there are 41,429 individuals licensed in the cannabis industry.[89] There are 36,228 individuals licensed to work in Oregon.[90] Considering worker turnover, economists estimate that about 12,500 individuals are employed at any one time.[91]

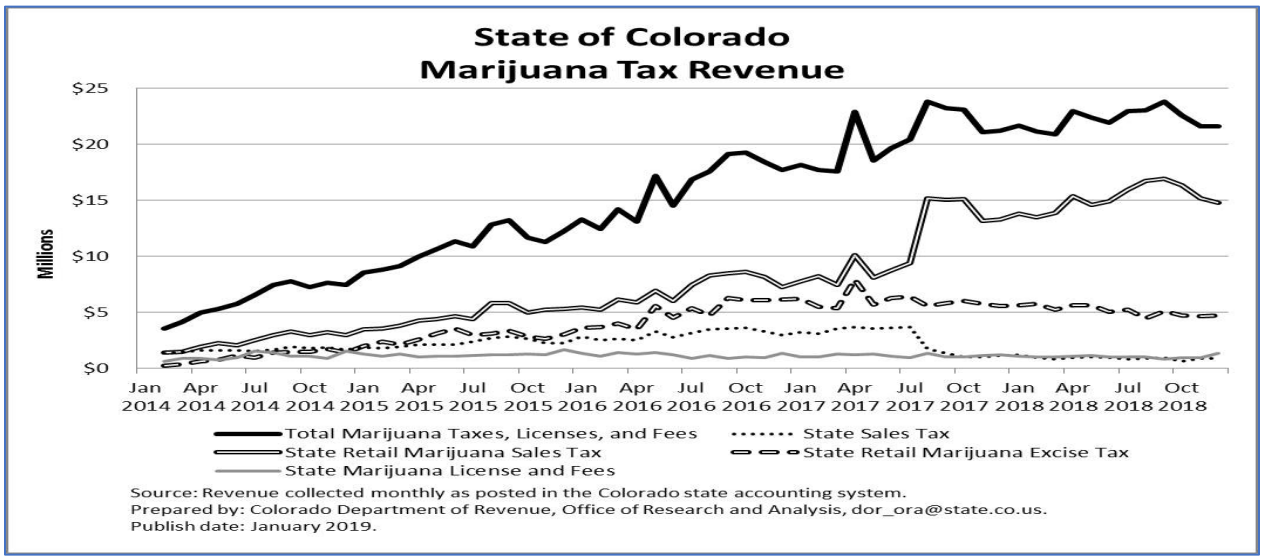
States realize a significant increase in tax revenues from the sale of cannabis. For example, Colorado's revenues from excise and sales tax increased 91.1% from 2014 to

89. Colorado Marijuana Official State Web Portal, accessed at *www.colorado.gov/pacific/enforcement/med-resources-and-statistics*.

90. Oregon Liquor Control Commission, 2018. *Marijuana License Application Statistics as of November 30, 2018*, accessed at *www.oregon.gov/olcc/marijuana/Documents/mj_app_stats_by_county.pdf.*

91. Whitney, B.R., 2017. *Cannabis Employment Estimates*, accessed at *https://olis.leg.state.or.us/liz/2017R1/Downloads/CommitteeMeetingDocument/99775*.

2015 and are expected to increase 23% by 2020 and surpass cigarette revenues.[92] The tax, license and fee revenue for calendar year 2018 was almost $267 million.



In Oregon, $82 million in cannabis tax dollars were collected in FY 2018. This represents a 17% increase from FY 2017.[93] Recreational cannabis tax revenue is expected to increase by another 34% by the 2019–2021 biennium.[94] Since recreational cannabis became legal in Oregon in 2016, sales have steadily increased. Consumer sales in July 2018 were approximately $57.5 million, approximately 20% higher than the consumer sales in July 2017.[95] Sales of all types of products—including edibles, extracts and usable cannabis—have steadily increased.[96]

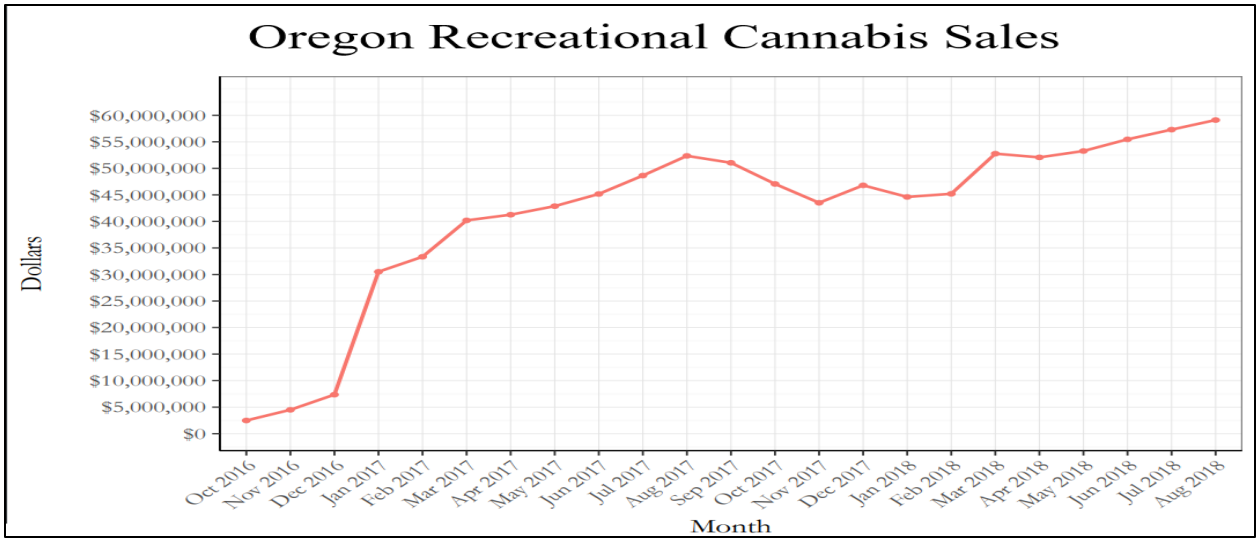
92. Marijuana Policy Group, 2016. *The Economic Impact of Marijuana Legalization in Colorado*, accessed at www.mjpolicygroup.com/pubs/mpg%20impact%20of%20marijuana%20on%20colorado-final.pdf.

93. Oregon Department of Revenue. December 2018. For current data, visit www.oregon.gov/DOR/programs/gov-research/Documents/Financial-reporting-receipts-public.pdf.

94. Office of Economic Analysis, Oregon Department of Administrative Services, 2018. *Oregon Economic and Revenue Forecast, December 2018*, accessed at www.oregon.gov/das/OEA/Documents/forecast1218.pdf.

95. Oregon Liquor Control Commission. December 2018. For current data, visit www.oregon.gov/olcc/marijuana/Documents/CTS/OregonCannabisTrackingSystemData.pdf.

96. Ibid.



Source: OLCC Market Trend Data.

In contrast, the number of medical cannabis growers, processors and dispensaries has declined sharply since 2016, when recreational cannabis was legalized in Oregon.[97] There has been a significant amount of consolidation in the industry, which has led to frequent ownership changes and continuous business structure modifications.[98]

Nationwide, the *NAMIC Issue Analysis* cites information from the *Marijuana Business Daily* in May 2017 that estimated demand for recreational cannabis approaches $45 billion to $50 billion compared to $106 billion for beer, $76.9 billion for cigarettes and $70.3 billion for nutraceuticals.[99] Moreover, the *NAMIC Issue Analysis* summarizes:

> In 2017, the legal medical and adult-use market reached $8.5 billion, according to the "State of Legal Marijuana Markets" executive report. The same report projects that the U.S. Cannabis market will reach $23.4 billion by 2022. Another report even likened the industry's 25 percent compound growth rate through 2021 to cable television at 19 percent in the 1990s and broadband internet at 29 percent in the 2000s. Other reports project the industry would reach as much as $50 billion by 2026 if marijuana were legalized at the federal level. In addition, medical and adult use retail cannabis tax revenues

97. From October 2015 to October 2018, the number of growers dropped from 48,699 to 16,600. From October 2016 to October 2018, the number of processing sites dropped from 117 to three, and the number of dispensaries dropped from 46 to five. Oregon Health Authority, October 2015, 2016 and 2018. *Oregon Medical Marijuana Program Statistical Snapshot,* accessed at www.oregon.gov/oha/PH/DISEASESCONDITIONS/CHRONICDISEASE/MEDICALMARIJUANAPROGRAM/Pages/data.aspx.

98. Oregon Liquor Control Commission (OLCC), 2018. "Update on Marijuana Licensing," accessed at www.oregon.gov/olcc/marijuana/Documents/Bulletins/Licensing_Delay_DirectorsMessage.pdf.

99. Bergner, J., 2018. "Cannabis: From Criminality to Commercial Enterprise Understanding the Intersection with Property/Casualty Insurance," National Association of Mutual Insurance Companies (NAMIC), accessed at www.namic.org/pdf/publicpolicy/181101cannabis.pdf.

topped $645 million in 2017 and are expected to hit $2.3 billion in 2020.[100]

IV. TYPE, SCOPE, AND AVAILABILITY OF COVERAGE AND INSURANCE GAPS

A. INTRODUCTION

The cannabis industry can be broken down into multiple segments. This includes cultivation, processors/harvesters, manufacturing, retail distribution, testing labs, and microbusinesses or affiliated businesses (e.g., construction, security, cargo/transportation companies). While each of these segments is unique and require insurance products specific to their type of business, there are coverages that apply to all the business segments. These coverages include, but are not limited to, general liability, workers' compensation, product liability, and property insurance.

There are a few admitted insurers issuing policies in the cannabis industry, and they are treating cannabis businesses as "regular" businesses despite the federal illegality of the product. One exception to this statement is workers' compensation. Some states—including Colorado, Oregon and California—include a workers' compensation market of last resort through a state-admitted carrier for this coverage. However, most other available insurance products for the cannabis industry are currently insured through the non-admitted (surplus lines) market.

The primary challenge in engaging admitted insurers in many states to write any coverage type is the requirement of a "lawful purpose." Under general law, any contract or agreement entered for an illegal purpose is not legally binding. Because cannabis continues to be illegal at the federal level, the argument is made that there can be no legal contract or insurance policy. There are legislative efforts underway at both the federal and state level to address this conundrum of legality in a state and illegality at the federal level.[101]

Moving toward an admitted market for cannabis business insurance is a key objective for states that have legalized. This is a rapidly changing area with businesses seeking admitted coverage but only able to find coverage in the non-admitted market. As the

100. Bergner, J., 2018. "Cannabis: From Criminality to Commercial Enterprise Understanding the Intersection with Property/Casualty Insurance," National Association of Mutual Insurance Companies (NAMIC), accessed at www.namic.org/pdf/publicpolicy/181101cannabis.pdf.

101. See discussion at p. 24.

cannabis industry develops, their insurance needs become more sophisticated and differentiated.

The chart below is intended to provide examples on the needs of the industry ranging from general coverages anticipated for all cannabis businesses to those more specialized for various business segments, such as testing labs.

Sample General Insurance Needs for Cannabis Industry (Product Liability)

- Business Owners Policy Programs
- Commercial General Liability
- Premises Liability
- Products/Completed Operations Coverage

Sample Specialized Coverage Needs by Business Segments

Cultivation	Processors/ Manufacturers	Testing Labs	Distribution	Retail
• Crop Insurance • Equipment Breakdown • Earthquake /Volcanic Eruption /Sprinkler Leakage	• Equipment Breakdown • Errors and Omissions • Directors and Officers Liability	• Equipment Breakdown • Errors and Omissions • Directors and Officers Liability	• Automobile Liability • Cargo	• Employment Practices • Directors and Officers Liability • Employee Theft • Crime Insurance

Other Potential Insurance Needs

- Lessor's Risk
- Medical Professional Liability
- Surety Bonds

B. How Insurers Determine Cannabis Rates

The cannabis insurance market is presently expanding with insurers emerging onto the admitted market. These insurers are submitting rate filings for regulated products, which allows state insurance regulators to gain insights into the types of coverages and design ratemaking approaches with respect to the coverage filings. Preliminary reviews of recent admitted-market filings suggest that policies and coverages offered to cannabis-oriented operations are similar to those provided to other non-cannabis businesses, including various limit and deductible options that are routinely offered in the commercial insurance marketplace. As the cannabis insurance market continues to grow the types of coverage and options do as well.

a. General Observations Regarding Cannabis Insurance Rates

Optional coverages such as earthquake, terrorism and sprinkler leakage are generally available at an additional premium to insureds who elect these coverages. Both rates and minimum premiums can vary on the basis of the nature of the risk (e.g., the classification of the insured as a store, dispensary, grower, warehouse, distributor, and whether the insured grows the product solely for its own use or for sale to other businesses) and the territory (as defined by the insurer in its rating plan). Possible segments include, but are not necessarily limited to, the following: 1) store/dispensary; 2) indoor cultivation; 3) outdoor cultivation; and 4) manufacturing/processing.

Exposure bases for loss costs can be either sales or payroll, as appropriate, based on the coverage and the business operations. For multiplicative increased-limits factors (ILFs), lower factors apply to lower limits of coverage; higher factors apply to higher limits. Claims-made policies are available, with options to choose retroactive dates and extended reporting periods. The further back the retroactive date is in the past, the larger the premium. Premiums for extended reporting periods are determined as percentages of the annual premium.

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Schedule rating is often available to adjust the manual rates up to +/-25%, and in infrequent cases up to +/- 40% (also depending on allowable schedule-rating constraints pursuant to the laws of individual states). Some cannabis-specific characteristics that some insurers use in schedule rating include: 1) number and type of cannabis licenses; 2) depth of experience in cannabis operations; and 3) the use of blockchain, including Hyperledger, technology in processing, distribution and retail transactions.

Some rates may be premised on certain packages of coverages being mandatory. For instance, some insurers may require a package of general liability and property coverages to be purchased together, while other coverages—e.g., product liability, crime, earthquake, sprinkler leakage or terrorism—may be optional.

Package discounts for property and liability coverages together may be available, along with multi-policy credits. Rates may be affected by the owner's years of experience and financial position. New ventures may be significantly surcharged, as may inexperienced business owners or insureds with prior bankruptcies.

Rates may also depend on the following attributes: 1) presence of video surveillance; 2) use of locked display/storage cases; 3) use of flammable solvents, tinctures and/or hash oil; 4) local surroundings, including traffic volume and proximity to police services; and 5) the selection and training of employees. Rates may also be premised on the business complying with certain requirements, such as background checks on employees.

b. Businessowners' Policy (BOP) Programs

Classification relativities for various businesses are often derived from existing proxy classifications. For instance, some insurers have noted the following similarities in their filed rating plans:

- Distributors have similarities to warehouses and wholesale businesses, such as baked goods, tobacco, and grocery.
- Testing labs have similarities to businesses specializing in scientific tools and instruments and dental labs.
- Dispensaries have similarities to other retail stores, such as drug stores and tobacco stores.
- Manufacturers have similarities to other small business operation/manufacturing exposures, such as bakeries (no restaurant) and beverage stores (no liquor).

c. Commercial General Liability (CGL) Insurance

Many CGL exposures can be rated with gross sales as the exposure base. However, certain classifications pertaining to transportation and/or distribution may be rated based on payroll, while classifications pertaining to subcontracted work may be rated based the cost of that work. Within a schedule-rating plan, underwriters may consider such criteria of individual risks as: 1) the experience of the management; 2) internal controls; 3) structural features and condition of the building; 4) compliance with safety protocols; 5) types of equipment; and 6) the selection, training and experience of employees.

Loss costs for liability coverages and related endorsements are affected by:

- Applicable limitations on territories.
- Requirements for persons on premises to be escorted by employees.
- Hours of operation.
- Customer age restrictions.
- Type of exit packaging.
- Advertising injury liability, which is affected by restrictions on marketing to youthful persons.
- Requirements for security guards and protective devices. For instance, rates may be affected by: 1) employing state-certified security guards; 2) whether they are employees or subcontractors; and 3) whether they are armed or unarmed.

d. Premises/Operations Coverage

Premises or operations coverage can be rated by area of building. Possible hybrid exposure bases would be the square footage if the building area is smaller and gross sales if the building area is larger. Deductibles per occurrence are often available. The potential for inhalation/exposure liability is likely to be higher than for other typical properties and would be reflected in rates accordingly.

e. Products/Completed Operations Coverage

For products or completed operations coverage, gross sales are a possible exposure base. Rates vary by type of operation; e.g., medical dispensaries may be charged different rates from retail stores. Deductibles per occurrence are often available. There may be a default deductible, and further discounts could apply for the selection of higher deductibles.

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f. Optional Coverages for Businessowners' and/or Commercial General Liability Programs

In exchange for additional premiums, the following optional coverages may be available:

- Coverage for risks arising from employment of security guards (rated based on payroll/cost of security guards).
- Hired and non-owned automobile coverage (may be available for flat additional premiums).
- Assault and battery coverage (premium for various sublimits may be calculated as a percentage of the main commercial general liability coverage premium, with variation based on whether defense coverage is within or outside the policy limits).
- Terrorism (federal Terrorism Risk Insurance Act [TRIA]) coverage (premium may be calculated as a percentage of the main commercial general liability coverage premium).
- Waiver of subrogation (may be available for flat additional premium).
- Product withdrawal expense coverage (may be available for flat premium charges, based on the limit of coverage, with deductibles per occurrence set as dollar amounts and/or percentages of the limit of coverage).
- Special event coverage, which may be considered short-term coverage for which premium is fully earned. Premiums may vary depending on the type of event and may be proportional to the duration of the special event in days. Special events may include trade shows, fairs and music festivals. Rates vary based on the perceived level of hazard, which may be categorized as low, moderate or high. Event history, on-site security and limitations on consumer access are all factors taken into consideration.

g. Crime Insurance

Coverages for employee dishonesty, money and securities, and counterfeit money are highly affected by the current cash nature of the business. Rating is highly variable accordingly, with the potential for high premiums to be set. Several large brokerages have represented that the theft hazard is the most significant among the risks faced by cannabis-related businesses today.

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h. Crop Insurance

Crop insurance availability is a significant issue because federal crop insurance is not offered for cannabis crops. Private crop insurance for cannabis-related operations is also virtually impossible to secure. Insurers do not wish to cover any product that crosses state lines, due to fear of federal involvement. Accordingly, information regarding rates for crop insurance for cannabis is extremely limited.

i. Earthquake/Volcanic Eruption/Sprinkler Leakage Insurance

Coverages pertaining to the perils of earthquake or volcanic eruption can be purchased via an endorsement to a commercial property policy. Rates are often developed per dollar amount of insured exposure.

j. Lessor's Risk Insurance

Special rates for lessor's risk insurance are often applicable if the cannabis occupancy is more than a certain threshold of the property (e.g., more than 25%). Otherwise, the exposure is just rated on the standard policy. Rating appears to follow the approach used in insurers' standard lessors' risk programs. Cannabis factors are higher than for regular mercantile operations, ranging from +80% to +200% over standard mercantile rates. Categories include dispensaries, retail, medicinal, labs, product manufacturer, infused products, oil extraction and cultivation/grower. Additional schedule rating may apply to manual rates, with +/-25% maximum schedule-rated credits or debits.

k. Medical Professional Liability (Medical Malpractice) Insurance

Many traditional medical professional liability policies may exclude liability for recommended prescription of controlled substances. Accordingly, practitioners who prescribe or recommend medical cannabis to patients may seek special coverage limited to liability losses arising from prescription, recommendation or failure to prescribe or recommend medical cannabis.[102] Coverage limits for such policies resemble those of traditional medical professional liability policies; the base limit is often $1 million per occurrence/$3 million annual aggregate. Rates are derived based on traditional medical professional liability policies in a given jurisdiction. Base-rate adjustments reflect a focus

102. The DEA Practitioner's manual indicates that all drugs listed in Schedule I have no currently accepted medical use in treatment in the United States and therefore may not be prescribed, administered, or dispensed for medical use," some states are using the terms "prescribe" or "prescription" rather than "recommend" or "recommendation" in their statutes with respect to cannabis. Therefore, both terms "prescribe" or "prescription" and "recommend" or "recommendation" are used in this section. See https://www.deadiversion.usdoj.gov/pubs/manuals/pract/section2.htm

on claims arising from medical cannabis. Otherwise, classification plans may follow those filed for traditional medical professional liability insurance products.

An insurer's actuaries may estimate, often with historical data as a reference where available (although such historical data may be sparse), the proportion of medical cannabis-related losses to total medical professional liability losses and adjust the loss costs implied in the traditional medical professional liability policy rates accordingly. Afterward, the loss costs could be adjusted by a typically multiplicative load to reflect the insurer's expenses and targeted profit provision. It is possible that data related to frequency and severity of medication errors could be used as a proxy for data related to medical cannabis-related losses. This could result in a conservative estimate of loss costs because medication errors are a broader category.

I. Product Liability

The available programs for product liability insurance are often on a claims-made basis. Loss costs may vary between "producer" and "retail" classes. Producers include cultivators, growers and manufacturers, while the retail class includes distributors. Cultivator-only licensees receive a discount (sometimes substantial) from general producer rates.

Rating factors can relate to:

- Compliance with testing protocols.
- Operational maturity of the business.
- Management experience in the industry.
- Presence of a compliance officer.
- Compliance with packaging standards.
- Counterfeit products.
- Cleanliness of water supply.
- Location of suppliers.
- Use of petroleum gases during the extraction process.
- Existence of prior product recalls or regulatory infractions.
- Existence and quality of documentation of standard operating protocols.
- Whether the product needs to be applied topically or is vaporized.

m. Property Insurance

Premiums for property insurance may vary by type of covered property and the coverages purchased; e.g., building, business personal property, stock, business income/extra expense. Some insurers may require insureds who wish to purchase property coverage to also purchase general liability coverage. The insured may have an option to include or exclude coverage resulting from the peril of theft. Premium, including the minimum premium, may vary based on that selection.

Rates may be set proportionally to the insured value of the property. For plants before harvest, coverage limits may be set per plant and may vary based on the developmental stage of the plant; e.g., cloned/pre-vegetative, vegetative, pre-flowering, and flowering. For harvested plants, coverage limits may be set up to a fixed dollar amount per unit of weight (e.g., per pound). Coverage may also be available for the replacement cost of unplanted seeds. Additional property coverages may be purchased for: 1) money and securities; 2) accounts receivable; 3) personal effects; 4) valuable papers; 5) property of others; 6) signs; 7) tenant glass; 8) robbery and safe burglary; and 9) loss arising from employee dishonesty.

Loss costs for property coverages and related endorsements are often affected by the following considerations:

- Applicable limitations on territories where owned property is located; e.g., no out-of-state coverage.
- Ordinances/laws requiring cannabis businesses to make improvements to properties.
- Theft exclusions.
- Natural disasters, which could affect business interruption/loss of income coverages.
- Legal requirements applicable to tracking of inventory.
- Exposure to fungus.

n. Surety Bonds

The rating structure for surety bonds may use multiple tiers, determined based on such characteristics as commercial credit score, business experience, risk-management programs and prior regulatory actions. Rates may range between 2% to 10% of the bond amount, depending on tier. Additional schedule rating with variation up to +/-25% is available, with some insurers selecting a narrower range of variation in schedule-rated credits and debits.

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C. Gaps in Coverage

Cannabis insurance is still relatively new to both the surplus and admitted market and the cannabis industry is constantly evolving and changing. With regulations and new laws being implemented at the federal, state, and local levels the way that the cannabis industry cultivates, manufactures, distributes, sells, and is consumed changes daily. The adequacy of coverage can change substantially in a short amount of time. For example, the price of cannabis can increase and decrease quickly and change for different regional areas. Therefore, a sufficient level of loss protection for the asset of cannabis will change. The quantitative measurement in the adequacy of coverage is in constant change especially with the cannabis industry evolving with innovation. For example, new strains of cannabis are being cultivated and new technology for vape pens for ease and increased consumption are emerging at a rapid pace. With new products emerging daily, it's difficult for insurers to not only assess the risk; but, also provide policies that meet the cannabis industry's needs. In addition, insurers are looking for data to determine the risk associated with cannabis to fill the gaps in coverage. But, with little to no data in areas such as drug-free workplace standard procedures or auto insurers impacted by the current inability to test for cannabis intoxication of drivers, insurers are finding it difficult to fulfill all insurance coverage needs in the cannabis industry. The lack of data creates an unknown which in turn creates gaps. It is difficult for insurance to keep up with the demands of such a bourgeoning industry.

V. BEST PRACTICES AND RECOMMENDATIONS

A. EDUCATION, OUTREACH AND PUBLIC COMMUNICATION

Understanding the various facets of the cannabis industry is critical to learning about its insurance needs. Educational site visits to the different types of cannabis business operations (such as cultivation sites, manufacturing companies, distribution companies, testing labs and retail operations) should help state insurance regulators understand how the cannabis products are regulated on a state and local level. They will also assist in identifying where the areas of risk are decreased/increased throughout the supply chain.

Another educational avenue available to most regulators is reaching out to the cannabis industry trade associations, such as the National Cannabis Industry Association (NCIA), or a state trade association, such as the California Cannabis Industry Association (CCIA) as well as insurance trade associations. Many of the cannabis trade associations have insurance subgroups that meet and discuss matters related to the topics of insurance availability, gaps and emerging trends in the cannabis insurance space. Insurance trade

associations are able to identify and work with their individual insurer members to encourage writing cannabis insurance products. Reaching out to both the cannabis and insurance trade associations is a helpful way to begin a dialogue about the importance of cannabis insurance and the presence of the state insurance regulator.

State insurance regulator participation in various outreach events is another option to learn more about the cannabis industry and teach the cannabis industry about insurance. Interacting with other state insurance regulators and stakeholders at conferences, workshops and meetings can also be beneficial. Doing so provides information on how the cannabis insurance intersects with other state insurance departments and entities, such as state cannabis licensing agencies. It also allows for more information on the various supply chain risks.

B. Dedicated Internal Infrastructure and Resources

State insurance departments should have a web page or outreach materials dedicated to providing information and answering commonly asked questions regarding cannabis insurance coverage. In addition to a web page, it is advisable to have an in-house subject-matter expert (SME) on the issue of cannabis insurance. This expert can help bridge the gaps between state insurance department staff, the cannabis industry and the insurance industry. At a minimum, each insurance department should have a point of contact to guide interested parties in reaching the appropriate department staff. Additionally, departments should identify an internal team across the department to ensure all critical players of the process are engaged and understand the various issues or goals. This also helps to streamline needed answers or resources to insurers interested in writing cannabis insurance.

C. Monitoring the Market and Gap Analysis

As the degree to which insurers are meeting the coverage needs of cannabis businesses continues to evolve, it would be useful for regulators and policy makers to have up to date information on the types of coverages available in each state and gaps in the market. State insurance departments could survey carriers and producers on the types of policies available in there state, and this information could be aggregated and posted on the NAIC website.

D. California's Path to Approving Admitted Carriers

California was the first state to approve admitted insurance carriers for cannabis-based businesses in the cannabis industry. Through education and outreach the California

Department of Insurance (CDI) laid the groundwork for cannabis insurance on the admitted market. As of the publication of this white paper, the CDI had approved six carriers. It launched the Cannabis Insurance Initiative (Initiative) in 2017 in anticipation of the insurance industry's role in the legalization of cannabis for adult recreational use, which took effect on January 1, 2018 with the passage of Proposition 64. The first phase of the Initiative focused on education and outreach in order to develop the CDI and insurers' understanding of the cannabis industry. The goal was to ensure the availability of insurance products for the cannabis industry by identifying challenges, opportunities, and solutions.

The CDI encouraged insurers to write on the admitted market by bringing them together in a meeting with leaders in the cannabis industry. The meeting focused on educating insurers about the cannabis industry and its insurance needs. The cannabis industry discussed issues they faced with finding and obtaining insurance. Insurers were able to ask questions and have an open discussion.

Subsequently, the insurer meeting participants were invited to a tour of an indoor grow, dispensary and manufacturing facility in San Jose, California. This allowed insurers to witness first-hand the sophistication, risk management, regulatory oversight, professionalism and transparency of the cannabis industry and the opportunities for the insurance industry. This further allowed the insurance industry to gain a better understanding of the cannabis industry and its insurance needs, while addressing questions and concerns.

The CDI continued educational efforts to bridge the gap between the cannabis and insurance industries on a larger stage by hosting a public hearing in Los Angeles, California in October 2017. The hearing was co-hosted by the California Cannabis Industry Association (CCIA) and the LA Cannabis Task Force. Hundreds of participants attended to hear cannabis businesses and the insurance industry provide their respective perspectives on cannabis insurance gaps. The public hearing revealed that while there was some insurance availability from surplus lines insurers, insurance was limited in scope and the California market would benefit from the entrance of admitted commercial carriers.

In addition to education and outreach efforts, CDI implemented operational procedures within the department to facilitate approval of admitted insurers for the cannabis industry. An in-house cannabis insurance SME was designated to lead the Initiative and serve as the primary point of contact to stakeholders. An internal cross-departmental team, which included rate filing and legal staff, also served respective roles to reach the goal of product availability. A website with key resources and contacts for the Initiative was launched.

Through these resources, interested stakeholders and insurers can immediately identify an entry point to the CDI on cannabis insurance, as well as educational materials and upcoming events.

These efforts by the CDI led to the filing and approval of the first admitted commercial insurance company to offer coverage to cannabis business owners in November 2017. This was just months away from the January 1, 2018 legalization of adult cannabis use. Golden Bear Insurance Company was the first insurance company in California to write insurance on the admitted market.

Since the first filing and approval, five additional admitted market insurance companies have followed suit. Additionally, in 2018, the American Association of Insurance Services (AAIS) designed the new Cannabis Business Owners Policy (CannaBOP) for cannabis dispensaries, storage facilities, processors, manufacturers, distributors, and other cannabis-related businesses operating in the state. CannaBOP is the first-of-its-kind standardized cannabis policy form that was approved by CDI.

E. Industry Trends and Policy Engagement

Given federal laws, such as the CSA and Banking Secrecy Act/Anti-Money Laundering Law, various industries (including insurance) are hesitant to engage in the cannabis supply chain. They fear exposure to criminal or civil liability. Policy changes at the federal level could play a critical role in encouraging more admitted insurers to write cannabis insurance.

Despite existing laws that may deter regulators, there has been an increase in federal legislative efforts to provide states greater regulatory authority over cannabis businesses without federal interference. Currently, the Rohrabacher-Blumenauer amendment, which prevents the DOJ from spending funds on prosecuting cannabis businesses in states that have medical cannabis laws, was extended through a federal spending bill.[103] As mentioned above, the STATES Act, if passed, would allow states to regulate cannabis without federal interference.

However, as the cannabis industry continues to expand, there is a degree of uncertainty under President Trump and his administration. Former Attorney General Sessions had a longstanding public opposition toward the cannabis industry and actively removed

103. Angell, T., 2018. "Congressional Committee Protects Medical Marijuana from Jeff Sessions," accessed at www.forbes.com/sites/tomangell/2018/05/17/congressional-committee-protects-medical-marijuana-from-jeff-sessions/#546c1ca11e55.

protections. Recently appointed Attorney General Barr has indicated that he will not go after states that have legalized cannabis.[104]

Many operators in the cannabis industry are willing to move forward despite these actions; but, such activities at the federal level also worried others outside of the cannabis space about the industry's stability. President Trump repudiated former Attorney General Sessions' rescission of the Cole Memorandum based on a request from U.S. Sen. Cory Gardner (R-CO), but the rescission nonetheless influenced business decisions such as offering insurance to the industry.[105] The change in the attorney general presents a new opportunity for the DOJ to clarify the administration's position on state-legalized cannabis. However, it is too soon to tell what Attorney General Barr's priorities will be with respect to the cannabis industry other than his public statements that he will not pursue state-legalized cannabis businesses.

With new regulations, rising consumer demands and the market landscape constantly changing, the cannabis business is booming and needs insurance protections in the cannabis industry. As such, state insurance regulators should follow the legislative landscape and impacts related to the cannabis industry. Policy changes at the federal level may influence the readiness of admitted insurers to write cannabis insurance. Thus, knowledge of the environment may guide insurance departments in their preparation for potential filings.

Collaboration with federal, state, and local entities may also serve to address barriers that prohibit access to insurance protection for cannabis business owners. With the deep knowledge of insurance issues, state insurance regulators can and should contribute their subject matter expertise and perspectives in these public policy discussions. Federal, state, and local entities may find it helpful to identify staff to address specific departmental and outreach needs. Additionally, state insurance regulators may sponsor legislation related to cannabis insurance. They may also further engage in policy-making by offering support for legislation addressing barriers.

104. Smith, A., 2018. "The U.S. Legal Cannabis Industry is Booming," accessed at https://money.cnn.com/2018/01/31/news/cannabis-state-of-the-union/.

105. Matthews, M.K., 2018. "President Trump to Cory Gardner: Colorado's Legal Marijuana Won't Be Targeted by Jeff Sessions, Justice Department," *The Denver Post*, accessed at www.denverpost.com/2018/04/13/trump-gardner-colorado-marijuana-industry-not-targeted/.

VI. CONCLUSIONS

As more states continue to legalize cannabis, the need and demand for cannabis insurance will only continue to increase. There are substantial gaps in insurance coverage for the cannabis industry, which means that consumers, workers, vendors, owners and investors face risks that are not covered as they interact or engage with the cannabis industry. It is important for state insurance regulators to understand and address insurance availability and coverage gaps in their markets. State insurance regulators who have encouraged insurers to cover the cannabis industry have been successful in getting more insurers to enter this market. State insurance regulators can play a critically important role in working with the insurance industry to encourage more insurance availability for the cannabis industry.

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ADDITIONAL CANNABIS INFORMATIONAL RESOURCES

- Americans for Safe Access: https://www.safeaccessnow.org/
- Cannabis Business Times: https://www.cannabisbusinesstimes.com/
- Cannabis Now: https://cannabisnow.com/
- Drug Policy Alliance: http://www.drugpolicy.org/
- Global Commission on Drug Policy: http://www.globalcommissionondrugs.org/
- Law Enforcement Action Partnership: https://lawenforcementactionpartnership.org/
- Marijuana Policy Project (MPP): https://www.mpp.org/
- MJ Business Daily: https://mjbizdaily.com/
- National Cannabis Industry Association: https://thecannabisindustry.org/
- National Conference of State Legislatures: http://www.ncsl.org/research/health/state-medical-marijuana-laws.aspx
- National Organization for the Reform of Marijuana Laws: https://norml.org/
- Patients out of Time: https://www.medicalcannabis.com/
- Smart Approaches to Marijuana: https://learnaboutsam.org/
- Students for Sensible Drug Policy: https://ssdp.org/
- Transform Drug Policy Foundation: https://transformdrugs.org/
- Veterans for Cannabis: http://www.vfcusa.com/
- White House, Office of National Drug Control Policy- Marijuana: https://www.whitehouse.gov/ondcp/key-issues/marijuana/

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Pending Adoption by Executive (EX) Committee and Plenary – 12/10/19
Adopted by Property and Casualty Insurance (C) Committee – 8/5/19
Adopted by Transparency and Readability of Consumer Information (C) Working Group – 7/26/19



POST-DISASTER
CLAIMS GUIDE

State DOI Info Here
Address
Phone Number

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THERE'S BEEN A DISASTER - **WHAT SHOULD I DO NOW?**

Learn more in the sections described below.



SAFE AND SOUND

After a disaster hits, make sure you and your family are safe. Then secure your belongings. Do what you can to secure your home and property to prevent more damage or theft. For example, if windows are broken, board them up. If the roof has a few holes, cover it with a tarp to prevent water damage.



REPORT A CLAIM

Once you've determined your home is damaged and needs to be repaired or rebuilt, report or file a claim as soon as possible. The easiest way to report a claim is to call your insurance company or agent. You may be able to report or file a claim online or from your cell phone. If you have trouble finding a phone number, try searching for your insurance company online.



ESTIMATE DAMAGE

An insurance adjuster will figure out how much damage was done to your home and property. The adjuster will ask you for a home inventory (a list of your personal property) if your personal belongings were damaged or destroyed. The adjuster will visit your home to inspect and estimate the damage done. In this section, you can learn about the different types of adjusters who may work on your claim and what you should do to prepare to meet the adjuster.



DETERMINE COVERAGE

Once the adjuster has figured out how much it will cost to rebuild, repair or replace your home or property, the adjuster will review your policy to calculate how much the insurance company will pay. If you've never filed a claim before, this process can seem overwhelming. But you can read this section to learn how claim payments are calculated and how your coverage will impact what your insurance company pays. You can learn the meaning of some of the words insurance companies use.



REBUILD, REPAIR AND REPLACE

Your recovery from a disaster is not complete until you're living back in your home. During the recovery phase, you'll be replacing personal items (if damaged), choosing building materials and working with contractors. Read this section to find tips about working with contractors and how to avoid becoming a victim of fraud.



PREPARE

It may sound strange, but the recovery process is the best time to start preparing for the next disaster or claim. Create a home inventory list as you're replacing your belongings. Also as you're rebuilding, consider using building materials that will resist damage – so if there's another disaster, your home may have less damage. For example, you could use impact-resistant shingles or impact-resistant siding.

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PROPERTY INSURANCE **CLAIMS GUIDE**

Disasters happen everywhere and can happen at any time. Any of the following can cause a significant amount of damage to homes and personal property:


TORNADOES


WILDFIRES


HURRICANES


FLOODS


EARTHQUAKE

This might be the first time you've had an insurance claim – or maybe a claim this big.

This Guide will help you understand what to do after a natural disaster damages your home. It also gives you helpful tools and tips to navigate the insurance claims process, whether this is your first insurance claim or not.

This Guide provides general information to help you in any type of disaster. But remember, most policies won't cover damage from floods or earthquakes unless you bought that coverage separately.

Your state insurance department will help you and answer any questions – free of charge.



SAFE AND **SOUND**

A disaster has hit my area and my home has been damaged. I've made sure my family is safe. What should I do next?

Make sure there are no safety issues like downed electrical lines or broken gas lines. If there are safety issues, leave your home and wait for or listen to your local authorities to learn when you can return.

When inspecting your home, avoid broken glass and sharp objects or remove them. Watch out for things that could cause you to trip or fall.

Take photos or videos of the damaged areas and personal property. You also can jot down notes about any significant damage you see.

My family and I were evacuated from our home. When can we go home?

Wait to return to your home until your state or local authorities tell you it's safe. The authorities won't let you return to your home if there are hazards like downed power lines or broken gas lines. This is for your safety.

There's a lot of damage to my home. What should I do about the damage?

Try to prevent further damage by making essential repairs, like covering roofs, or windows with plywood, tarp, canvas, or other waterproof materials.

IMPORTANT: KEEP ALL RECEIPTS FOR EMERGENCY REPAIRS TO GIVE TO YOUR INSURANCE COMPANY. Because you have to prevent more damage, you may want to hire a contractor to make any emergency repairs.

Don't make permanent repairs before talking with your insurance agent or insurance company. Your company may not pay for repairs it didn't authorize.

If you're contacted by any contractors, review the section on Avoiding Insurance Fraud to avoid being taken advantage of.

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There's so much damage to my home, there's no way I can stay. What should I do?

Do your best to secure your home and personal belongings.

Gather important papers, including insurance policies and a list of all damaged or destroyed personal property (a home inventory list), if you have one. Take those with you if you can't stay in your home.

If you can't stay in your home, save any hotel receipts. Your insurance company will need the receipts to repay you.

Contact your doctor's office, pharmacy, or health plan if your prescription medicines were lost or if you lost your glasses, contacts, hearing aids, walker, wheelchair, or other medical equipment in the disaster.

Make sure you notify utilities and your mortgage company and make arrangements for mail deliveries.



ADDITIONAL **LIVING EXPENSE (ALE)**

Most homeowners policies also will pay the additional expenses you have if you can't stay in your home because of damage from a covered disaster. For example, if you've to move into a hotel or apartment while your home is repaired or rebuilt, the insurance company will pay your costs for temporary housing.

Just don't expect the insurance company to pay for your stay at a 5-star spa and resort or to eat out every night at the most expensive restaurant in town.

ALE is limited; see below for more information.

What types of living expenses does ALE pay for?

The insurance company will not pay ALL of your living expenses. ALE is to help pay those expenses that are beyond your normal expenses because you can't live in your home. For example, ALE coverage will pay hotel lodging, but it won't make your mortgage payment.

ALE typically covers hotel bills, reasonable restaurant meals (if you're staying in a hotel room with no kitchen), and other living costs above and beyond your normal housing expenses while you can't live in your home because of damage.

You need to be sure you keep ALL receipts for any additional costs you have. The insurance company will need the receipts to reimburse you.

Is there a limit to how long or how much I can use for my additional living expenses?

Keep in mind that ALE coverage is limited. Some policies have a dollar limit; some also may have a time limitation.

The good news – these limits are separate from any coverage you have to rebuild or repair your home. They're also separate from any coverage you have to replace your belongings.

Ask your insurance company or adjuster what your policy covers and any time or dollar limits that apply.

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REPORTING AN **INSURANCE CLAIM**

When should I report damage to my home or personal property?

Before reporting the property damage to your home, find out what your deductible is. If the damage is minor, for example, just a few shingles were damaged, you might decide you're better off paying for the repairs out of pocket instead of filing an insurance claim. But, remember you might not be able to see all the damage. You may want to have a contractor inspect your home.

If you believe the damage will cost more than your deductible to repair, or there's a lot of damage, you may want to file a claim. It's important to notify your insurance company as soon as you know there's damage and you decide to file a claim.

The easiest way to report damage is to call your insurance company or agent directly.

What should I do if I don't have my company or agent's phone number?

If you have cell service, use your cell phone to search for phone numbers or the insurance company's website. There may be a phone number to report a claim.

If you can access social media, you can search for information from your insurance company or state department of insurance about how to file a claim.

If you have limited or no cell service, look for mobile claims centers in your area. Local news outlets and social media usually announce their locations.

What do I need to know when I call to make a claim?

It will help if you have your policy number. But if you don't, your insurance company or agent can find your policy with your name, address, and phone number. You'll need to briefly explain what happened and describe the type and extent of the property damage.

If you aren't staying in your home, be prepared to give your insurance company and agent your new contact information—a phone number and an address.

Let your insurance company and agent know when you call if you've taken photos and videos of the damage and have cost estimates.



What is a contractor?

An individual you hire to manage the repair of your home. The contractor is responsible for supplying the necessary equipment, material, labor and services to complete repairs.

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What do I need to ask when I file a claim?

You should ask:

- For the name and phone number for every person you talk to.
- For your claim or reference number.
- How long you have to file a claim.
- If you need estimates to make repairs or rebuild before you can file a claim.
- For a general idea of what your policy will cover.
- If your insurance policy covers hotel costs. For how much? For how long?
- For information about your deductible. Are there separate deductibles for hail, hurricane, or wind damage? What are those?
- If there are any special processes or procedures you need to know about.
- When you can expect an adjuster to call.
- What other information the company will need to process the claim.

What other information or paperwork could the insurance company or agent ask for during the claims process?

A list of all damaged or destroyed personal property (a home inventory list) and receipts, if you have them, showing when you bought the damaged or destroyed items.

A list of damage to the home and other structures, like a garage, tool shed, or in-ground swimming pool. You'll need this list when you meet with the adjuster.

What if I don't have a completed home inventory list?

Don't worry; the adjuster will give you some time to make a list. Ask the adjuster how much time you have to submit this inventory list.

Work from memory if your property was destroyed and you have no records.

Review photos, for example on your cell phone or from family or friends, taken inside your home. That may help you make the list.

Search online shopping websites or online retailers to help estimate costs.

The National Association of Insurance Commissioners (NAIC) has a printable inventory listing that may help you as you're making your list.

https://www.insureuonline.org/home_inventory_checklist.pdf

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ESTIMATING THE **DAMAGE**

What is an adjuster and what does an adjuster do?

An adjuster is a person who determines the amount of damage to your home and property - what can be repaired or replaced, and at what cost. An adjuster reviews your insurance policy to determine if the damage is covered and if there are any dollar limits or deductibles that apply. They also should explain your policy's coverage for the claim.

ARE THERE DIFFERENT TYPES OF ADJUSTERS?

COMPANY **INDEPENDENT** **PUBLIC**

Remember in larger weather events or disasters, not all adjusters will live or work in your state. Some adjusters may be sent from other states to help when there's a large number of claims.

What is a company adjuster?

- A company adjuster works only for that insurance company.
- The insurance company hires and pays a company adjuster. This adjuster will settle the claim based on the insurance coverage you have and the amount of damage to your home and property.
- You do *not* pay a company adjuster.

What is an independent adjuster?

- An independent adjuster works for several different insurance companies. An insurance company uses independent adjusters when it doesn't have its own adjusters on staff or when it needs more adjusters than it has available; this often happens in a large disaster.
- An independent adjuster does the same work as a company adjuster (see above).
- You do *not* pay an independent adjuster.

What is a public adjuster?

- A public adjuster is a professional you can hire to handle your insurance claim.
- Public adjusters have no ties to the insurance company.
- They estimate the damage to your home and property, review your insurance coverage, and negotiate a settlement of the insurance claim for you.
- Many states require public adjusters to be licensed. Some states prohibit public adjusters from negotiating insurance claims for you. In those states, only a licensed attorney can represent you.
- You have to pay a public adjuster.

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WORKING WITH THE **INSURANCE ADJUSTER**

How long after I file a claim will an adjuster come to inspect my home?

It depends – every disaster can be different. Ask your insurance company when you file the claim.

If you don't hear from an adjuster in a reasonable amount of time, contact your agent or the company. A reasonable amount of time could be 3 to 5 days for a minor claim. But, it may take longer for the adjuster to reach you following a large disaster in your area. Be sure they know how to contact you.

What should I do to prepare to meet with the adjuster?

- Make a list of all damaged or destroyed personal property. Make a list of damage to the home and other structures, like a garage, tool shed, or in-ground swimming pool. Work from memory or from photos if you have no records of your destroyed property.
- Gather any photos or videos of your home and property before they were damaged or destroyed.
- Include receipts from when you bought the damaged or destroyed items, if you have them. Search online shopping sites or online retailers to help estimate costs.
- If you have time before the adjuster inspects your home, try to get written bids from contractors. You aren't required to have bids, but it can help. The bids should detail the materials to be used, prices of those materials, and labor on a line-by-line basis.
- Take notes when you meet with the adjuster. Get the adjuster's name and contact information and ask when you can expect to hear back. You can write this information down in the Claims Communication Section in the back of this resource.

What will happen when the insurance adjuster comes to my home?

- You should be there when the adjuster comes to your home. You can show the adjuster where you believe there has been structural damage and give the lists you've prepared of property or structural damage, photos or videos you've taken, and bids from contractors.
- The adjuster will inspect your home and take photographs and measurements. While the adjuster is there, they may even do some calculations of the damage and cost to repair.
- Before the adjuster leaves, make sure you have their contact information. Ask the adjuster what the next steps will be and to estimate when you'll hear back from them.
- Ask the adjuster if there's any other information you should provide. After the adjuster leaves, you may need to gather more information or start a personal property inventory list.

If I hire a public adjuster, will the insurance company still send its own adjuster?

The insurance company doesn't have to accept your public adjuster's estimates.

The insurance company will typically send either a company adjuster or an independent adjuster to assess and estimate damage to your home or property.

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How is a public adjuster paid?

- If you hire a public adjuster, it's your responsibility to pay their fee.
- Depending on the laws of your state, public adjusters can charge a flat fee or a fee that's based on a percentage of the settlement you get from your insurer.
- In some states, the maximum a public adjuster can charge is set by law. The maximum also may vary depending on whether a widespread catastrophe caused your loss.
- A public adjuster should give you a contract. The contract should explain what services the adjuster will provide and how much you will pay.
- If you hire a public adjuster after your insurer has made an initial offer, ask about the fee. The contract should say if the fee you'll pay will be based on the total the insurance company pays or on the amount the public adjuster negotiates for you.
- You should ask your public adjuster to routinely provide you updates on the status of your claim.



DETERMINING **COVERAGE**
(SETTLING A CLAIM)

How do I get a settlement offer? Who gives me that?

The company adjuster or independent adjuster will calculate the amount of damage to your home and property. They will review your policy and determine what deductibles may apply and if there are any limits on what will be paid. Once they've made those calculations, they'll contact you and your public adjuster or lawyer (if you have one) and share their estimates and calculations with you. They also may contact your contractor about their estimates and calculations.

Will I get a lump sum payment and when will I receive money?

The settlement process is not a single transaction. You'll get a number of payments for different parts of your claim to help you start the rebuilding and repairing process. You'll likely receive a payment for your additional living expenses mentioned above. Then you'll start to receive payments to replace your personal property, followed by payments for the repairs and construction on your home.

Why did the insurance company make the check payable to me AND my mortgage company?

If you have a mortgage on your home, your lender has an interest in making sure the home is rebuilt – or that your loan is paid in full. Your mortgage lender required you to add them as an additional insured on your homeowners policy. Because of this, the insurer is obligated to include them on the check it pays for major repairs. You'll need to work with your mortgage lender to get the claim money released for repairs. If you have problems working with your mortgage lender, contact your state's agency that regulates banks and mortgage lenders or your state's Attorney General's Office for assistance. The federal government also has a website where you can make a complaint against your bank or mortgage lender, if you aren't getting the help you need. That website is: https://www.usa.gov/complaints-lender. Your state department of insurance also may have suggestions for you.

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How long will it take for my insurance claim to be settled?

Everyone wants the process to be done as fast as possible so they can return to a normal life.

If there's substantial damage involving your home and property, an insurance claim is not going to be closed with a single payment. There will be claims payments for various parts of your claim as the rebuilding process moves along. Most people find it takes at least 18 to 24 months to repair/rebuild their home and replace their possessions after a major disaster. Your insurance claim will stay open until the insurer has made all payments you're entitled to under your policy.

You should feel free to contact your insurance company or adjuster for a status on your claim at any time during the claims process.

What if I'm not satisfied with the amount of my insurance settlement?

- Your settlement won't necessarily be the same as your neighbor's. Your coverages, deductible, and policy limits may be different even if the damage looks the same.
- If the insurance company denies any part of the claim, ask for the denial in writing. Keep all paperwork.
- If you don't believe the offer is fair, call the insurance company. Be prepared to explain why you think the offer is unfair. If you're not satisfied with the response, contact your state insurance department.

What if the insurance company doesn't agree with the public adjuster's or my contractor's estimate of the damage?

Differences in construction estimates are common. Ideally, you and the insurance company should reach agreement on a "scope of loss". This is a detailed list of the quantities of construction materials, labor, profit and overhead, building code compliance, and every single item required to repair or rebuild your home.

Once you've submitted all the information that your insurance company needs, including written estimates from contractors, the adjuster will calculate the total cost.

If you disagree with the claim amount the adjuster has calculated, there are different ways to settle that disagreement without going to court. Two ways are appraisal and arbitration.

Appraisal: If you can't agree with your insurance company about how much it will cost to rebuild your home and/or repair or replace your property, you can use the appraisal process to resolve the differences. This isn't the same as an appraisal you may have of your home's value.

The appraisal process begins with two appraisers comparing their estimates. The appraisal process only determines costs, not if your policy covers these costs. It isn't a court proceeding.

If you use the appraisal process, you'll have to pay some of the costs. What you'll have to pay will depend on your state's law.

If your policy has an appraisal clause, you must go through the appraisal process before you can sue your insurance company.

Arbitration: Arbitration is a legal process, but you don't have to go to court. In an arbitration hearing, a neutral third party (arbitrator) hears from both you and your insurance company. Both parties agree to accept the arbitrator's decision. Usually the decision is binding so you can't go to court to appeal the decision.

Some insurance policies require arbitration to settle differences. Other policies will say how arbitration will work if both you and your insurance company agree to use it. If you use arbitration, you'll have to split the cost with the insurance company. But, some state laws may require you or your insurance company to pay the full cost if you aren't successful.

What can I do if my claim was denied?

If you think the insurance company should have paid your claim, you can use arbitration or file a lawsuit to get the insurance company to reverse its decision. But, before you do any of those, contact your state insurance department for help.

Some states may have a mediation process that you can use. Contact your state department of insurance for more information.

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HOW IS A CLAIM PAYMENT AMOUNT **CALCULATED?**

A number of important insurance terms will help you understand how your insurance claim will be paid. The following sections explain terms like deductible, depreciation, Actual Cash Value, and Replacement Cost.

What is a deductible?

A deductible is the part (or amount) of the claim you're responsible for. Insurance companies will deduct this amount from any claim settlements they pay to you or on your behalf. So if your insurance policy has a $1,000 deductible, that means you've agreed to pay $1,000 out of your pocket for the damage to your home.

Are there different types of deductibles?

Yes. A deductible can be either a specific dollar amount or a percentage of the total amount of insurance. There are special deductibles that apply to certain types of claims; some deductibles are applied to specific parts of your home. Look at the declarations page or the front page of most homeowners insurance policies to learn about your policy's deductible.

HOW ARE DEDUCTIBLES USED TO **CALCULATE A CLAIM?**

FLAT DOLLAR DEDUCTIBLE $500 DEDUCTIBLE PER LOSS	**PERCENTAGE DEDUCTIBLE** 2% DEDUCTIBLE PER LOSS
A disaster destroyed your home. Your home was insured for $250K (structure only) and it will cost $250K to rebuild it. You have a $500 deductible.	A disaster destroyed your home. Your home was insured for $250K (structure only) and it will cost $250K to rebuild it. You have a 2% deductible.
	Insured Value: $250,000
	2% Deductible: $250,000 x 2% = $5,000
Damage and Cost to Rebuild: $250,000	Damage and Cost to Rebuild: $250,000
Minus the Deductible: - $500	Minus the Deductible: - $5,000
Claim Settlement Amount: $249,500	**Claim Settlement Amount: $245,000**

Some insurance policies have a special deductible for losses caused by wind, hurricanes, or other types of storms. The insurer applies this deductible when one of those types of disasters causes the damage. If something else damages your home, then the "all peril" deductible would apply.

Some policies also may have a special deductible that applies to a specific part of your home, like your roof. In these cases, the deductible could be either a flat dollar amount or a percentage.

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REPLACEMENT COST VERSUS ACTUAL CASH VALUE

If you have **Replacement Cost Value (RCV)** coverage, your policy will pay the cost to repair or replace your damaged property without deducting for depreciation.

If you have **Actual Cash Value (ACV)** coverage, your policy will pay the depreciated cost to repair or replace your damaged property.

Check the declarations page of your homeowners policy to see whether the policy provides replacement cost coverage. If it doesn't specify replacement cost, then your policy likely only covers actual cash value. If it specifies replacement cost, then you have replacement cost coverage.

Under an RCV or ACV policy, your dwelling coverage pays for damage to the structure and will pay only up to the policy limit.

Even if you bought an RCV policy, there may be other limits on what the policy will pay for damage to certain surfaces, such as roofs. In some cases, the policy may pay ACV on your roof, but RCV on the rest of your home and property. If you have questions, call the adjuster or your insurer and ask what type of coverage you have.

Example:

The Smiths and the Johnsons are next door neighbors. Their homes are exactly the same size, built in the same year, and have the exact same floorplan. One night, a terrible storm tears through their town, destroying the Smith's and the Johnson's roofs. Both roofs have the same damage. The Smiths and the Johnsons have a $1,000 deductible, and both roofs will cost $15,000 to replace. The Smiths have a replacement cost policy, while the Johnsons have an actual cash value policy.

SMITH'S REPLACEMENT COST VALUE
Insurance valuation method: RCV
Cost of Smith's roof ten years ago: $15,000
Policy deductible: $1,000
Cost to replace roof: $15,000
Depreciation not applicable for RCV
Insurance payment:
$15,000 cost of new roof
– $0 depreciation (no depreciation with RCV)
– $1,000 deductible
= $14,000 insurance payment

JOHNSON'S ACTUAL CASH VALUE
Insurance valuation method: ACV
Cost of Johnson's roof ten years ago: $15,000
Policy deductible: $1,000
Cost to replace roof: $15,000
Depreciation schedule: $1,000/year
Insurance payment:
$15,000 cost of new roof
– $10,000 depreciation ($1000/yr x 10 years)
– $1,000 deductible
= $4,000 insurance payment

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HOW DOES **DEPRECIATION WORK?**

IS ALL DEPRECIATION THE SAME?

No. Depreciation in an insurance claim is much different than depreciation on assets for taxes and is different from an accountant's calculation of depreciation on property.

In an insurance claim, the deduction for depreciation may be significant, especially if the damaged property was at or near the end of its useful life. For example, if a covered cause of loss destroys your 20 year old roof and it must be replaced, a policy that pays RCV will cover the full cost to replace the roof. However, an ACV policy may pay as little as 20% of the cost to replace the roof, since the useful life of a roof is usually about 25 years.

WHAT IS "DEPRECIATION" AND HOW DOES THAT AFFECT MY CLAIM?

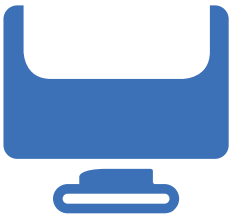
Everything covered under your homeowners policy is assigned a value. Your home, and most of its contents and components, are likely to decline in value over time because of age or wear and tear. This loss in value is known as depreciation.

Insurers usually calculate depreciation based on the condition of the property when it was lost or damaged, what a new one would cost, and how long the item would normally last.

For example, your two-year old laptop that was in good condition was destroyed in a disaster. A similar new laptop would cost $750. Your laptop normally lasts four years, so it had lost 50% of its value (25% a year). So, the value of your laptop at the time it was destroyed was half of $750, or $375. Your insurance settlement would include $375 to reimburse you for this laptop.

$750 – **$375** = **$375**

Cost of new laptop (Replacement cost value)	50% depreciation (2 years x 25% per year)	Value of your laptop (Actual cash value)



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I have a replacement cost policy, but my insurance company only paid for part of the claim. Can they do that?

When you have an RCV policy and turn in a claim for a covered loss, the insurer at first may pay only the ACV for the damage to your home or personal property.

But, when you present evidence that the damaged property has been repaired or replaced, the insurer will pay the difference (this is referred to as "recoverable depreciation") up to the replacement cost.

Recoverable depreciation is calculated as the difference between an item's replacement cost and ACV.



Is there a time limit on when I can get paid for the recoverable depreciation?

Yes, there's usually a time limit. That time limit can range from 6 months to up to one year, depending on your state's laws and your policy.

In certain circumstances, like a very large-scale disaster, insurance companies know it will take longer to rebuild homes and replace property. They'll give you more time if you ask. Your state insurance department may require the insurance company to give you more time.

If you have questions about this time frame, ask your adjuster. You also can contact your state insurance department.

I was told I have to replace with "like kind and quality". What does that mean?

Most insurance policies that are Replacement Cost cover repairs or replacements with property of "like kind and quality".

Your insurance policy isn't intended to pay for expensive improvements or upgrades. For example, if you had a 3-tab shingle roof before the loss, your insurance policy would cover the cost of another 3-tab shingle roof, but not a more expensive slate roof. If you had ceramic bathroom sinks in your home, your insurance policy won't pay the extra cost to replace those with granite countertops.

What is "Functional Replacement"?

Another type of coverage becoming more common, particularly with older homes, is known as "Functional Replacement Coverage" (FRC). FRC replaces the damaged property with a functional replacement, which isn't necessarily the same quality and craftsmanship as the original materials.

A simple example would be replacing plaster walls with drywall. Both provide solid walls and have the same function, yet the cost varies greatly between the two. Another example would be a damaged banister in a home. The repair could be made with wood carved in the same architectural style, but using a less expensive wood – for instance, replacing an oak banister with a pine banister. Another example would be replacing a tile roof with a shingle roof.

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My adjuster mentioned that some of my property has a special limit. What is that?

A special limit caps how much money you'll be paid for certain types of property. Don't confuse this with the contents or personal property limits. A special limit will apply to specific categories of property like jewelry, furs, guns, antiques, collector items, and coins.



My home and/or property were destroyed and can't be repaired. Can I use the insurance settlement to build or buy another home somewhere else?

Check your insurance policy and talk with your agent or company. You also can call your state department of insurance.

You may not get the same settlement if you don't rebuild on the same location.



WHAT IS ORDINANCE AND LAW COVERAGE?

- In many instances, your local government may require your home to be repaired or rebuilt to meet current local building codes. Unless you have Ordinance and Law coverage, a standard homeowners policy doesn't cover that added expense.
- Ordinance and Law coverage in your homeowners insurance policy covers part or all of the cost to repair or rebuild your home to meet current local building codes. For example, electrical wiring, plumbing, windows, and roofing materials are some things that may need to be updated.
- Standard homeowners policies don't cover the added expense to meet current building codes when you repair or replace your home. Look at the declarations page of your policy to see if you have Ordinance and Law coverage.

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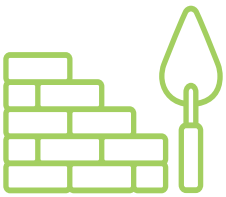
THE THREE "R'S" OF **RECOVERY**



REBUILD



REPAIR



REPLACE

I've accepted the insurance company's settlement and I'm ready to repair/rebuild. What do I need to know?

- Use reputable contractors. Reputable contractors usually don't ask for a large payment upfront.
- Contractors may be licensed or registered. The difference is important. A licensed contractor has passed exams and met other requirements to show that he or she is competent. A registered contractor has provided contact information to a government authority. You can learn more about licensing and registration of contractors by calling your state Department of Insurance. They can help you contact the state agency that licenses and regulates contractors.
- Ask your contractor to show you the building permits. Contractors most likely will need to apply and pay for building permits before beginning work. And, don't forget to check with your local officials about any requirements for permits or inspections.
- Get an estimate from more than one contractor. An estimate from a contractor that's much lower than any of the others doesn't mean it's the best deal. Make sure all the quotes include the same things and check references.
- Contact your insurance company and adjuster any time you find damage that hasn't already been reported or inspected or if you learn something new about damage to your home or property.

What should I know about a contractor before hiring one?

Get the following information:

- a copy of the contractor's identification (the contractor's name and the name of the business);
- a copy of the contractor's business license (check the expiration date);
- a copy of the contractor's proof of worker's compensation insurance; and
- a copy of the contractor's proof of liability insurance. A licensed insurance agent or company issues this certificate. The proof of insurance should show the company's name, phone number, and the policy number. Call the insurance company to verify the coverage.

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ASSIGNMENT OF **BENEFITS**

Some states allow assignments of benefits (AOB) after a loss. This agreement transfers your rights under your insurance policy and your claim to a third party, most often your contractor.

Be cautious if you're asked to sign an AOB. Typically, there's a promise from the contractor to handle all matters with the insurance company for you, which may sound great. But you also may be giving up some, most, or even all of your rights, including having a lawsuit filed without your approval or knowledge.

Take your time to review any AOB carefully. Talk to your claims adjuster or you can ask an attorney to review and give you advice. You can also call your state department of insurance.



WHAT CAN I DO TO AVOID **INSURANCE FRAUD?**

After storms and other disasters, fraudsters and scam artists often arrive quickly. Watch for contractors who offer to do your repairs with upgraded or free building materials. Here are a few tips to help you avoid becoming a victim of a disaster fraudster or scam artist:

- If you're working with contractors you don't know, find out where they're from. Many fraudsters will travel from state to state.
- Before you sign any contracts or pay any money, ask for references.
- Never pay the full amount before the work is complete.
- Ask your local Better Business Bureau and state Attorney General's Office about complaints.
- Check online for information about the contractor.
- Most importantly, report any suspected fraud to your insurance agent and your state's department of insurance as soon as possible.

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MOVING ON & **LOOKING FORWARD**

I've just gone through one disaster. What do I need to do to prepare for the next disaster?
There are two different parts of preparation – preparing your home and preparing yourself financially.

Preparing your home
While you're rebuilding, think about what you can do to minimize damage to your home during the next storm or disaster. This is called mitigation.

WAYS YOU CAN LIMIT FUTURE DAMAGE:

You can make changes to your home to limit damage during a future tornado, wildfire, hurricane, or high wind.



Secure entry doors. Make sure entry doors have a two-inch deadbolt and three hinges with screws long enough to secure the door and frame to the wall. The frame should be well anchored.



Install impact-resistant windows. Local building codes in some areas require this.

Leave the windows closed in a storm. Opening the window doesn't equalize the pressure between the inside and outside of the house. Instead, it pressurizes the inside of the house, like blowing up a balloon until it pops. The air pushes off the roof or a wall and the house collapses.



Create a wildfire defense area. Remove flammable materials from around your home. Trim over hanging branches. Remove dead trees and bushes. Clean gutters and clear them of leaves and pine needles.

Install mesh screens over exterior vents. This will prevent fire embers from getting inside your home.



Brace your garage door. You can buy bracing products that will make your door stronger and more wind resistant. If you're expecting bad weather and haven't braced your garage door, you can put a vertical brace into the wall framing and floor, much as you would board up a window before a hurricane.



Install wind-resistant roof structures. Roofs are usually installed with roofing nails. But this type of roof can come off in high winds. Using hurricane clips to attach roofs creates a stronger connection between the roof and the house. Roofing clips come in a range of protection; the one you need depends on the weight of your roof. The building codes in hurricane-prone areas requires roofing clips, but they're a good idea in tornado-prone areas too.



Store firewood and other flammable materials away from home, garage, or deck.

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A number of great resources are available online can give you more ideas about ways you can reduce or avoid damage to your home.

- **Ready.gov (US Department of Homeland Security)**
- **FEMA Mitigation Resources (US Department of Homeland Security)**
- **Ready, Set Go! (Wildfire resiliency)**

PREPARING YOURSELF **FINANCIALLY**

Once you've rebuilt or repaired your home, and you're replacing damaged property, it's time to prepare for the future.

- You should make a list of all your stuff, called an inventory list. If you don't want to write everything down or type it into a spreadsheet, you can film a video to show your household items. As you film, you can describe important items, including when you bought the item, its condition, and how much you paid for it, if you know. There also are many mobile apps that will make it easier to create an inventory list. The National Association of Insurance Commissioners (NAIC) has a free app called the MyHOME Scr.APP.book that can be downloaded in the Apple App Store or on Google Play.



- Make a copy of your inventory list and keep it with your insurance policy. You could put the copy somewhere safe, such as a bank safety deposit box. You also could store a copy online.
- Put your insurance company name, policy number, and company contact information somewhere you could find it in a disaster.
- Review your policy with your insurance agent each year to see if your needs have changed.

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CLAIM INFORMATION

Name of Insurance Company:
Claim Number:
Phone Number:

INSURANCE ADJUSTER INFORMATION

Adjuster Name:
Adjuster Company:
Phone Number:
Adjuster License Number:
Website:

CONTRACTOR(S)

Name of Company:				
Representative:				
Phone Number:				
License Number:				
I checked:	☐ They have liability Insurance	☐ With my Insurance Company	☐ With the Better Business Bureau	☐ Online Search

Name of Company:				
Representative:				
Phone Number:				
License Number:				
I checked:	☐ They have liability Insurance	☐ With my Insurance Company	☐ With the Better Business Bureau	☐ Online Search

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CLAIM COMMUNICATION LOG

Who did I talk to:
Name of Company:
Date/Time:
What we talked about:
What is Next:

Who did I talk to:
Name of Company:
Date/Time:
What we talked about:
What is Next:

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What is Next:

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EMERGENCY REPAIR LOG

To help you keep track of any emergency repairs, here are some forms to help you.

Repair:
Cost of Repair:
Date of Repair:

Repair:
Cost of Repair:
Date of Repair:

Repair:
Cost of Repair:
Date of Repair:

Repair:
Cost of Repair:
Date of Repair:

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Date of Repair:

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Pending Adoption by Executive (EX) Committee and Plenary – 12/10/19
Adopted by the Reinsurance (E) Task Force – 10/22/19

Process for Evaluating Qualified and Reciprocal Jurisdictions

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I. Preamble

Purpose

The revised *Credit for Reinsurance Model Law* (#785) and *Credit for Reinsurance Model Regulation* (#786) (collectively, the Credit for Reinsurance Models) require an assuming insurer to be licensed and domiciled in a "Qualified Jurisdiction" in order to be eligible for certification by a state as a certified reinsurer for reinsurance collateral reduction purposes. In 2012, the NAIC Reinsurance (E) Task Force was charged to develop an NAIC process to evaluate the reinsurance supervisory systems of non-U.S. jurisdictions, for the purposes of developing and maintaining a list of jurisdictions recommended for recognition by the states as Qualified Jurisdictions. This charge was extended in 2019 to encompass the recognition of Reciprocal Jurisdictions in accordance with the 2019 amendments to the Credit for Reinsurance Models, including the maintenance of a list of recommended Reciprocal Jurisdictions. The purpose of the *Process for Evaluating Qualified and Reciprocal Jurisdictions* is to provide a documented evaluation process for creating and maintaining these NAIC lists.

Background

On November 6, 2011, the NAIC Executive (EX) Committee and Plenary adopted revisions to the Credit for Reinsurance Models. These revisions serve to reduce reinsurance collateral requirements for certified reinsurers that are licensed and domiciled in Qualified Jurisdictions. Under the previous version of the Credit for Reinsurance Models, in order for U.S. ceding insurers to receive reinsurance credit, the reinsurance was required to be ceded to U.S.-licensed reinsurers or secured by collateral representing 100% of U.S. liabilities for which the credit is recorded. When considering revisions to the Credit for Reinsurance Models, the Reinsurance (E) Task Force contemplated establishing an accreditation-like process, modeled on the current NAIC Financial Regulation Standards and Accreditation Program, to review the reinsurance supervisory systems of non-U.S. jurisdictions. Under the revised Credit for Reinsurance Models, the approval of Qualified Jurisdictions is left to the authority of the states; however, the models provide that a list of Qualified Jurisdictions will be created through the NAIC committee process, and that individual states must consider this list when approving jurisdictions.

The enactment in 2010 of the federal Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) created the Federal Insurance Office (FIO), which has the following authority: (1) coordinate federal efforts and develop federal policy on prudential aspects of international insurance matters; (2) assist the Secretary of the U.S. Department of the Treasury in negotiating covered agreements (as defined in the Dodd-Frank Act); (3) determine whether the states' insurance measures are preempted by covered agreements; and (4) consult with the states (including state insurance regulators) regarding insurance matters of national importance and prudential insurance matters of international importance. Further, the Dodd-Frank Act authorizes the U.S. Treasury Secretary and the U.S. Trade Representative (USTR), jointly, to negotiate and enter into covered agreements on behalf of the United States. It is the NAIC's intention to communicate and coordinate with the FIO and related federal authorities as appropriate with respect to the evaluation of the reinsurance supervisory systems of non-U.S. jurisdictions.

On September 22, 2017, the United States and the European Union (EU) entered into the "*Bilateral Agreement Between the United States of America and the European Union on Prudential Measures Regarding Insurance and Reinsurance.*" A similar agreement with the United Kingdom (UK) was signed on December 18, 2018. Both agreements (collectively referred to as the "Covered Agreements") will require the states to eliminate reinsurance collateral requirements for reinsurers licensed and domiciled in these jurisdictions within 60 months (five years) after signing or face potential federal preemption by the Federal Insurance Office (FIO) under the Dodd-Frank Act.

Reciprocal Jurisdictions

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On June 25, 2019, the NAIC Executive (EX) Committee and Plenary adopted revisions to the Credit for Reinsurance Models. These revisions were intended to conform the Models to the relevant provisions of the Covered Agreements. The Covered Agreements would eliminate reinsurance collateral requirements for EU and UK reinsurers that maintain a minimum amount of own funds equivalent to $250 million and a solvency capital requirement (SCR) of 100% under Solvency II, among other conditions. Conversely, U.S. reinsurers that maintain capital and surplus equivalent to 226 million euros with a risk-based capital (RBC) of 300% of authorized control level would not be required to maintain a local presence in order to do business in the EU or UK or post reinsurance collateral. Under the revised Credit for Reinsurance Models, jurisdictions that are subject to in-force Covered Agreements are considered to be Reciprocal Jurisdictions, and reinsurers that have their head office or are domiciled in a Reciprocal Jurisdiction are not required to post reinsurance collateral if they meet all of the requirements of the Credit for Reinsurance Models.

Under the revised Credit for Reinsurance Models, not only are jurisdictions that are subject to Covered Agreements treated as Reciprocal Jurisdictions for reinsurance collateral purposes, but any other Qualified Jurisdictions can also qualify for collateral elimination as Reciprocal Jurisdictions. States that meet the requirements of the NAIC Financial Standards and Accreditation Program are also considered to be Reciprocal Jurisdictions.

The NAIC has updated and revised this *Process for Evaluating Qualified and Reciprocal Jurisdictions* to specify how Qualified Jurisdictions that recognize key NAIC solvency initiatives, including group supervision and group capital standards, and also meet the other requirements under the revised Credit for Reinsurance Models, will be recognized as Reciprocal Jurisdictions and receive similar treatment as that provided under the EU and UK Covered Agreements, including the elimination of reinsurance collateral and local presence requirements by the states.

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II. Principles for the Evaluation of Non-U.S. Jurisdictions

1. The NAIC model revisions applicable to certified reinsurers are intended to facilitate cross-border reinsurance transactions and enhance competition within the U.S. market, while ensuring that U.S. insurers and policyholders are adequately protected against the risk of insolvency. To be eligible for certification, a reinsurer must be domiciled and licensed in a Qualified Jurisdiction as determined by the domestic regulator of the ceding insurer. A Qualified Jurisdiction not subject to an in-force Covered Agreement under the Dodd-Frank Act may also be determined to be a Reciprocal Jurisdiction, and reinsurers that have their head office or are domiciled in any such Reciprocal Jurisdiction will not be required to post reinsurance collateral, provided they meet the minimum capital and financial strength requirements and comply with the other requirements of the Credit for Reinsurance Models.

2. The evaluation of non-U.S. jurisdictions as Qualified Jurisdictions and Reciprocal Jurisdictions will be conducted in accordance with the provisions of the Credit for Reinsurance Models and any other relevant guidance developed by the NAIC.

3. The evaluation of non-U.S. jurisdictions as Qualified Jurisdictions is intended as an outcomes-based comparison to financial solvency regulation under the NAIC Financial Regulation Standards and Accreditation Program (Accreditation Program), adherence to international supervisory standards, and relevant international guidance for recognition of reinsurance supervision. It is not intended as a prescriptive comparison to the NAIC Accreditation Program. In order for a Qualified Jurisdiction that is not subject to an in-force Covered Agreement to be evaluated as a Reciprocal Jurisdiction, that Qualified Jurisdiction must agree to recognize the states' approach to group supervision, including group capital, and other such requirements as provided under the Credit for Reinsurance Models.

4. The states shall evaluate the appropriateness and effectiveness of the reinsurance supervisory system within the Qualified Jurisdiction, both initially and on an ongoing basis, and consider the rights, benefits and the extent of reciprocal recognition afforded by the jurisdiction to reinsurers licensed and domiciled in the U.S. The determination of Qualified Jurisdiction status is based on the effectiveness of the entire reinsurance supervisory system within the jurisdiction.

5. Each state may evaluate a non-U.S. jurisdiction to determine if it is a Qualified Jurisdiction. A list of Qualified Jurisdictions will be published through the NAIC committee process. A state must consider this list in its determination of Qualified Jurisdictions, and if the state approves a jurisdiction not on this list, the state must thoroughly document the justification for approving this jurisdiction in accordance with the standards for approving Qualified Jurisdictions contained in the Credit for Reinsurance Models. The creation of this list does not constitute a delegation of regulatory authority to the NAIC. The regulatory authority to recognize a Qualified Jurisdiction resides solely in each state and the NAIC List of Qualified Jurisdictions is not binding on the states.

6. A list of Reciprocal Jurisdictions will be published through the NAIC committee process. Jurisdictions subject to an in-force Covered Agreement and states that meet the requirements of the NAIC Financial Standards and Accreditation Program are automatically included on the List of Reciprocal Jurisdictions. A state must consider this list in its determination of Reciprocal Jurisdiction status, and if the state approves a jurisdiction not on this list, the state must thoroughly document the justification for approving this jurisdiction in accordance with the standards for approving Reciprocal Jurisdictions contained in the Credit for Reinsurance Models

7. In order to facilitate multi-state recognition of assuming insurers and to encourage uniformity among the states, the NAIC has initiated a process called "passporting" under which the commissioner has the discretion to defer to another state's determination that a jurisdiction is a Qualified or Reciprocal Jurisdiction. Passporting is based

upon individual state regulatory authority, and states are encouraged to act in a uniform manner in order to facilitate the passporting process. States are also encouraged to utilize the passporting process to reduce the amount of documentation filed with the states and reduce duplicate filings. The NAIC Lists of Qualified and Reciprocal Jurisdictions are intended to facilitate the passporting process.

8. Both Qualified Jurisdictions and Reciprocal Jurisdictions must agree to share information and cooperate with the state with respect to all applicable reinsurers domiciled within that jurisdiction. Critical factors in the evaluation process include but are not limited to the history of performance by assuming insurers in the applicant jurisdiction and any documented evidence of substantial problems with the enforcement of final U.S. judgments in the applicant jurisdiction. A jurisdiction will not be a Qualified Jurisdiction if the commissioner has determined that it does not adequately and promptly enforce final U.S. judgments or arbitration awards.

9. The determination of Qualified Jurisdiction status can only be made with respect to the reinsurance supervisory system in existence and applied by a non-U.S. jurisdiction at the time of the evaluation.

10. The NAIC and the states will communicate and coordinate with the FIO, USTR and other relevant federal authorities as appropriate with respect to the evaluation of the reinsurance supervisory systems of non-U.S. jurisdictions.

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III. Procedure for Evaluation of Non-U.S. Jurisdictions

1. Initiation of Evaluation of the Reinsurance Supervisory System of an Individual Jurisdiction.

a. Priority will be given to requests from the states and from those jurisdictions specifically requesting an evaluation by the NAIC.

b. Formal notification of the NAIC's intent to initiate the evaluation process will be sent by the NAIC to the reinsurance supervisory authority in the jurisdiction selected, with copies to the FIO and other relevant federal authorities as appropriate. The NAIC will issue public notice on the NAIC website upon confirmation that the jurisdiction is willing to participate in the evaluation process. The NAIC will at this time request public comments with respect to consideration of the jurisdiction as a Qualified Jurisdiction. The process of evaluation and all related documentation are private and confidential matters between the NAIC and the applicant jurisdiction, unless otherwise provided in this document, subject to a preliminary confidentiality and information sharing agreement between the NAIC, relevant states and the applicant jurisdiction.

c. Relevant U.S. state and federal authorities will be notified of the NAIC's decision to evaluate a jurisdiction.

2. Evaluation of Jurisdiction

a. Evaluation Materials. The Qualified Jurisdiction Working Group will initiate evaluation of a jurisdiction's regulatory system by using the information identified in Section A through Section G of the Evaluation Methodology (Evaluation Materials). The Qualified Jurisdiction Working Group will begin by undertaking a review of the most recent Financial Sector Assessment Program (FSAP) Report prepared by the International Monetary Fund (IMF), including the Technical Note on Insurance Sector Supervision, and any other publicly available information regarding the laws, regulations, practices and procedures applicable to the reinsurance supervisory system. The Qualified Jurisdiction Working Group will also invite each jurisdiction or its designee to provide information relative to Section A through Section G of the Evaluation Methodology in order to update, complete or supplement publicly available information. The Qualified Jurisdiction Working Group may also request or accept relevant information from reinsurers domiciled in the jurisdiction under review.

b. The Qualified Jurisdiction Working Group will notify the jurisdiction of any information upon which the Working Group is relying. In that communication, the NAIC will invite the supervisory authority to compare the materials identified by the NAIC to the materials described in Appendix A and Appendix B, and provide information required to update the identified public information or supplement the public information, as required, to address the topics identified in Section A through Section G of the Evaluation Methodology. The use of publicly available information (e.g., the FSAP Report and/or the Insurance Sector Technical Note) is intended to lessen the burden on applicant jurisdictions by requiring the production of information that is readily available, while still addressing substantive areas of inquiry detailed in the Evaluation Methodology. The Qualified Jurisdiction Working Group's review at this stage will be focused on how the jurisdiction's laws, regulations, administrative practices and procedures, and regulatory authorities regulate the financial solvency of its domestic reinsurers in comparison to key principles underlying the U.S. financial solvency framework[1] and other factors set forth in the Evaluation Methodology.

[1] The U.S. financial solvency framework is understood to refer to the key elements provided in the NAIC Financial Regulation Standards and Accreditation Program. Appendix A and Appendix B are derived from this framework.

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c. After reviewing the Evaluation Materials, the Qualified Jurisdiction Working Group may request that the applicant jurisdiction submit supplemental information as necessary to determine whether the jurisdiction has sufficient authority to regulate the solvency of its reinsurers in an effective manner. The Working Group will address specific questions directly with the jurisdiction related to items detailed in the Evaluation Methodology that are not otherwise addressed in the Evaluation Materials.

d. The NAIC will request that all responses from the jurisdiction being evaluated be provided in English. Any responses submitted with respect to a jurisdiction's laws and regulations should be provided by a person qualified in that jurisdiction to provide such analyses and, in the case of statutory analysis, qualified to provide such legal interpretations, to ensure that the jurisdiction is providing an accurate description.

e. The NAIC does not intend to review confidential company-specific information in this process, and has focused the procedure on reviewing publicly available information. No confidential company-specific information shall be disclosed or disseminated during the course of the jurisdiction's evaluation unless specifically requested, subject to appropriate confidentiality safeguards addressed in a preliminary confidentiality and information-sharing agreement. If no such agreement is executed or the jurisdiction is unable to enter into such an agreement under its regulatory authority, the NAIC will not accept any confidential company-specific information.

3. NAIC Review of Evaluation Materials

a. NAIC staff and/or outside consultants with the appropriate knowledge, experience and expertise will review the jurisdiction's Evaluation Materials.

b. Expenses with respect to the evaluations will be absorbed within the NAIC budget. This will be periodically reviewed.

c. Timeline for review. A project management approach will be developed with respect to the overall timeline applicable to each evaluation.

d. Upon completing its review of the Evaluation Materials, the internal reviewer(s) will report initial findings to the Qualified Jurisdiction Working Group, including any significant issues or concerns identified. This report will be included as part of the official documentation of the evaluation. Copies of the initial findings may also be made available to FIO and other relevant federal authorities subject to appropriate confidentiality and information-sharing agreements being in place.

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4. Discretionary On-site Review

a. The NAIC may ask the jurisdiction under consideration for the opportunity to perform an on-site review of the jurisdiction's reinsurance supervisory system. Factors that the Qualified Jurisdiction Working Group will consider in determining whether an on-site review is appropriate include the completeness of the information provided by the jurisdiction under review, the general familiarity of the jurisdiction by the NAIC staff or other state regulators participating in the review based on prior conduct or dealings with the jurisdiction, and the results of other evaluations performed by other regulatory or supervisory organizations. If the review is performed, it will be coordinated through the NAIC, utilizing personnel with the appropriate knowledge, experience and expertise. Individual states may also request that representatives from their state be added to the review team.

b. The review team will communicate with the supervisory authority in advance of the on-site visit to clearly identify the objectives, expectations and procedures with respect to the review, as well as any significant issues or concerns identified within the review of the Evaluation Materials. Information to be considered during the on-site review includes, but is not limited to, the following:

    i. Interviews with supervisory authority personnel.

    ii. Review of organizational and personnel practices.

    iii. Any additional information beneficial to gaining an understanding of document and communication flows.

c. Upon completing the on-site review, the reviewer(s) will report initial findings to the Qualified Jurisdiction Working Group, including any significant issues or concerns identified. This report will be included as part of the official documentation of the evaluation.

5. Standard of Review

The evaluation is intended as an outcomes-based comparison to financial solvency regulation under the NAIC Accreditation Program, adherence to international supervisory standards and relevant international guidance for recognition of reinsurance supervision. The standard for qualification of a jurisdiction is that the NAIC must reasonably conclude that the jurisdiction's reinsurance supervisory system achieves a level of effectiveness in financial solvency regulation that is deemed acceptable for purposes of reinsurance collateral reduction, that the jurisdiction's demonstrated practices and procedures with respect to reinsurance supervision are consistent with its reinsurance supervisory system, and that the jurisdiction's laws and practices satisfy the criteria required of Qualified Jurisdictions as set forth in the Credit for Reinsurance Models.

6. Additional Information to be Considered as Part of Evaluation

The NAIC may also consider information from sources other than the jurisdiction under review. This information includes:

a. Documents, reports and information from appropriate international, U.S. federal and U.S. state authorities.

b. Public comments from interested parties.

c. Rating agency information.

d. Any other relevant information.

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7. Preliminary Evaluation Report

a. NAIC staff and/or outside consultants will prepare a Preliminary Evaluation Report for review by the Qualified Jurisdiction Working Group. This preliminary report will be private and confidential (i.e., may only be reviewed by Working Group members, designated NAIC staff, consultants, the states, the FIO and other relevant federal authorities that specifically request to be kept apprised of this information, provided that such entities have entered into a preliminary confidentiality and information-sharing agreement with the foreign jurisdiction. Any outside consultants retained by the NAIC will be required to enter into a confidentiality and nondisclosure agreement.).

b. The report will be prepared in a consistent style and format to be developed by NAIC staff. It will contain detailed advisory information and recommendations with respect to the evaluation of the jurisdiction's reinsurance supervisory system and the documented practices and procedures thereunder. The report will contain a recommendation as to whether the NAIC should recognize the jurisdiction as a Qualified Jurisdiction.

c. All workpapers and reports, including supporting documentation and data, produced as part of the evaluation process are the property of the NAIC and shall be maintained at the NAIC Central Office. In the event that the NAIC shall come into possession of any confidential information, the information shall be held subject to a confidentiality and information-sharing agreement, which will outline the appropriate actions necessary to protect the confidentiality of such information.

8. Review of Preliminary Evaluation Report

a. The Qualified Jurisdiction Working Group's review of the Preliminary Evaluation Report will be held in regulator-to-regulator session in accordance with the NAIC Policy Statement on Open Meetings.

b. The Qualified Jurisdiction Working Group will make a preliminary determination as to whether the jurisdiction under consideration satisfies the Standard of Review and is deemed acceptable to be included on the NAIC List of Qualified Jurisdictions. If the preliminary determination is that the jurisdiction should not be included on the NAIC List of Qualified Jurisdictions, the Qualified Jurisdiction Working Group will set forth its specific findings and identify those areas of concern with respect to this determination.

c. The results of the Preliminary Evaluation Report will be immediately communicated in written form to the supervisory authority of the jurisdiction under review.

9. Opportunity to Respond to Preliminary Evaluation Report

a. Upon receipt of the Preliminary Evaluation Report, the supervisory authority will have an opportunity to respond to the initial findings and determination. This is not intended to be a formal appeals process that would initiate U.S. state administrative due process requirements.

b. The Qualified Jurisdiction Working Group will consider any response, and will proceed to prepare its Final Evaluation Report. The Qualified Jurisdiction Working Group will consider the Final Evaluation Report for approval in regulator-to-regulator session in accordance with the NAIC Policy Statement on Open Meetings. This report will be approved upon an affirmative vote of a majority of the members in attendance at this meeting.

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c. Upon approval of the Final Evaluation Report, the Qualified Jurisdiction Working Group will issue a public statement and a summary of its findings with respect to its determination. At this time, the Working Group will release the summary for public comment. The detailed report will be a confidential, regulator-only document. The report may be shared with any state indicating that it is considering relying on the NAIC List of Qualified Jurisdictions and has entered into a preliminary confidentiality and information-sharing agreement with the foreign jurisdiction.

10. NAIC Determination regarding List of Qualified Jurisdictions

a. Once the Qualified Jurisdiction Working Group has adopted its Final Evaluation Report, it will submit the summary of its findings and its recommendation to the Reinsurance (E) Task Force at an open meeting. Upon approval by the Reinsurance (E) Task Force, the summary and recommendation will be submitted to the Executive (EX) Committee and Plenary, as well as to the FIO, USTR and other relevant federal authorities for consultation purposes. Upon approval as a Qualified Jurisdiction by the Executive (EX) Committee and Plenary, the jurisdiction will be added to the NAIC List of Qualified Jurisdictions. The NAIC will maintain the List of Qualified Jurisdictions on its public website and in other appropriate NAIC publications.

b. In the event that a jurisdiction is not approved as a Qualified Jurisdiction, the supervisory authority will be eligible for reapplication at the discretion of the NAIC.

c. Upon final adoption of the Qualified Jurisdiction Working Group's determination with respect to a jurisdiction, the Final Evaluation Report will be made available to individual U.S. state insurance regulators upon request and confirmation that the information contained therein will remain confidential.

11. Memorandum of Understanding (MOU)

a. A Qualified Jurisdiction must agree to share information and cooperate on a confidential basis with the U.S. state insurance regulatory authority with respect to all certified reinsurers domiciled within that jurisdiction.

b. The International Association of Insurance Supervisors (IAIS) Multilateral Memorandum of Understanding (MMoU) is the recommended method under which a Qualified Jurisdiction will agree to share information and cooperate with U.S. state insurance regulatory authorities. However, until such time as a state has been approved as a signatory to the MMoU by the IAIS, the state may rely on an MOU entered into by a "Lead State" designated by the NAIC. This Lead State will act as a conduit for information between the Qualified Jurisdiction and other states that have certified a reinsurer domiciled and licensed in that jurisdiction, and will share information with these states consistent with the terms governing the further sharing of information included in the applicable IAIS MMoU or bilateral MOU between the Lead State and the Qualified Jurisdiction and pursuant to the NAIC Master Information Sharing and Confidentiality Agreement. The jurisdiction must also confirm in writing that it is willing to permit this Lead State to act as the contact for purposes of obtaining information concerning its certified reinsurers, provided the Lead State share that information with the other states requesting the information consistent with the terms governing the further sharing of information included in the applicable IAIS MMoU or bilateral MOU between the Lead State and the Qualified Jurisdiction.

c. If a Qualified Jurisdiction has not been approved by the IAIS for use of the MMoU, it must enter into an MOU with a Lead State. The MOU will also provide for appropriate confidentiality safeguards with respect to the information shared between the jurisdictions.

d. The NAIC and the states will communicate and coordinate with the FIO, USTR and other relevant federal authorities as appropriate with respect to this process.

12. Process for Evaluation after Initial Approval

a. The process for determining whether a non-U.S. jurisdiction is a Qualified Jurisdiction is ongoing and subject to periodic review. The Qualified Jurisdiction Working Group will perform a yearly review of Qualified Jurisdictions to determine whether there have been any significant changes over the prior year that might affect their status as Qualified Jurisdictions. This yearly review shall follow such abbreviated process as may be determined by the Qualified Jurisdiction Working Group to be appropriate.

b. Qualified Jurisdictions must provide the Qualified Jurisdiction Working Group with notice of any material change in the applicable reinsurance supervisory system that may affect the status of the Qualified Jurisdiction. A U.S. jurisdiction should also notify the Qualified Jurisdiction Working Group if it receives notice of any material change in the applicable reinsurance supervisory system, or any adverse developments with respect to enforcement of final U.S. judgments, that may affect the status of the Qualified Jurisdiction. Upon receipt of any such notice, the Qualified Jurisdiction Working Group will consider whether it is necessary to re-evaluate the status of the Qualified Jurisdiction.

c. If the Qualified Jurisdiction Working Group finds the jurisdiction to be out of compliance at any time with the requirements to be a Qualified Jurisdiction, the specific reasons will be documented in a report to the jurisdiction under review, and the status as a Qualified Jurisdiction may be placed on probation, suspended or revoked.

d. The Qualified Jurisdiction Working Group will monitor those jurisdictions that have been approved as Qualified Jurisdictions by individual states, but are not included on the NAIC List of Qualified Jurisdictions.

13. Review of Qualified Jurisdictions as Reciprocal Jurisdictions

a. In undertaking the evaluation of a Qualified Jurisdiction as a Reciprocal Jurisdiction, the Qualified Jurisdiction Working Group shall utilize such processes and procedures as outlined in the immediately-preceding paragraphs 1 – 12 of Section III. *Procedure for Evaluation of Non-U.S. Jurisdictions* such as the Qualified Jurisdiction Working Group deems is appropriate. Specifically, the Qualified Jurisdiction Working Group will use processes and procedures outlined in paragraph 1 (*Initiation of Evaluation of the Reinsurance Supervisory System of an Individual Jurisdiction*), paragraph 3 (*NAIC Review of Evaluation Materials*), paragraph 7 (*Preliminary Evaluation Report*), paragraph 8 (*Review of Preliminary Evaluation Report*), paragraph 9 (*Opportunity to Respond to Preliminary Evaluation Report*), paragraph 10 (*NAIC Determination regarding List of Qualified Jurisdictions*), paragraph 11 (*Memorandum of Understanding*) and paragraph 12 (*Process for Evaluation after Initial Approval*), as modified for use with Reciprocal Jurisdictions.

b. A Qualified Jurisdiction may not be reviewed for inclusion on the NAIC List of Reciprocal Jurisdictions, unless it has undergone the *Evaluation Methodology* outlined in Section IV, and remains in good standing with the NAIC as a Qualified Jurisdiction. The Qualified Jurisdiction Working Group may, if it determines an extended review period to be appropriate after its initial approval of a new Qualified Jurisdiction, defer consideration of that jurisdiction as a possible Reciprocal Jurisdiction until there has been sufficient United States experience with that jurisdiction and its Certified Reinsurers that the Working Group believes it is appropriate to progress from collateral reduction to collateral elimination. Nothing in this process requires a finding that a Qualified Jurisdiction meets the standards for recognition as a Reciprocal Jurisdiction, and

the Qualified Jurisdiction Working Group may base such recommendation on factors not specifically included in this process.

c. A list of Reciprocal Jurisdictions will be published through the NAIC committee process. Jurisdictions subject to an in-force Covered Agreement and states that meet the requirements of the NAIC Financial Standards and Accreditation Program are automatically included on the NAIC List of Reciprocal Jurisdictions. In making its recommendation with respect to whether a Qualified Jurisdiction that is not automatically designated as a Reciprocal Jurisdiction should be added to the NAIC List of Reciprocal Jurisdictions, the Qualified Jurisdiction Working Group shall undertake the following analysis in making its evaluation:

    i. The Qualified Jurisdiction must confirm that an insurer which has its head office or is domiciled in that jurisdiction shall receive credit for reinsurance ceded to a U.S.-domiciled assuming insurer in the same manner as credit for reinsurance assumed by insurers domiciled in that jurisdiction is received by United States ceding insurers;

    ii. The Qualified Jurisdiction must confirm that it does not require a U.S.-domiciled assuming insurer to establish or maintain a local presence as a condition for entering into a reinsurance agreement with any ceding insurer subject to regulation by that jurisdiction or as a condition to allow the ceding insurer to recognize credit for such reinsurance;

    iii. The Qualified Jurisdiction must recognize the U.S. state regulatory approach to group supervision and group capital, by providing written confirmation by its competent regulatory authority that insurance groups that are domiciled or maintain their worldwide headquarters in this state or another jurisdiction accredited by the NAIC shall be subject only to their U.S. home jurisdiction's worldwide prudential insurance group supervision including worldwide group governance, solvency and capital, and reporting, as applicable, and will not be subject to group supervision at the level of the worldwide parent undertaking of the insurance or reinsurance group by the Qualified Jurisdiction;

    iv. The Qualified Jurisdiction must provide written confirmation by its competent regulatory authority that information regarding insurers and their parent, subsidiary, or affiliated entities, if applicable, shall be provided to the states in accordance with a memorandum of understanding or similar document between a state and the Qualified Jurisdiction, including but not limited to the IAIS MMoU or other multilateral memoranda of understanding coordinated by the NAIC This requirement may be satisfied by an MOU with a Lead State, which shall provide for appropriate confidentiality safeguards with respect to the information shared between the jurisdictions, similar to the MOU requirement outlined in paragraph 11 of this section III; and

    v. The Qualified Jurisdiction must confirm that it will provide to the states on an annual basis confirmation that each eligible assuming insurer that is domiciled in the Qualified Jurisdiction continues to comply with the requirements set forth in in Section 9C(2) and (3) of Model #786; i.e., must maintain minimum capital and surplus of no less than $250,000,000, and maintains on an ongoing basis the required minimum solvency or capital ratio, as applicable.

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d. In order to satisfy the requirements of subsection (c) above, the chief insurance supervisor of the Qualified Jurisdiction being evaluated as a Reciprocal Jurisdiction may provide the NAIC with a written letter confirming, as follows:

> [Jurisdiction] is a Qualified Jurisdiction under the NAIC *Credit for Reinsurance Model Law* (#785) and *Credit for Reinsurance Model Regulation* (#786), and is currently in good standing on the *NAIC List of Qualified Jurisdictions*. As the lead insurance regulatory supervisor for [Jurisdiction], I hereby confirm to the National Association of Insurance Commissioners (NAIC) and the chief insurance regulators of the 50 states, the District of Columbia and five U.S. territories the following:
>
> - An insurer which has its head office or is domiciled in [Jurisdiction] shall receive credit for reinsurance ceded to a U.S.-domiciled assuming insurer in the same manner as credit for reinsurance assumed by insurers domiciled in [Jurisdiction] is received by United States ceding insurers. [Jurisdiction] does not require a U.S.-domiciled assuming insurer to establish or maintain a local presence as a condition for entering into a reinsurance agreement with any ceding insurer subject to regulation by [Jurisdiction] or as a condition to allow the ceding insurer to recognize credit for such reinsurance.
>
> - [Jurisdiction] recognizes the U.S. state regulatory approach to group supervision and group capital, and confirms that insurance groups that are domiciled or maintain their worldwide headquarters in jurisdictions accredited by the NAIC shall be subject only to their U.S. home jurisdiction's worldwide prudential insurance group supervision including worldwide group governance, solvency and capital, and reporting, as applicable, and will not be subject to group supervision at the level of the worldwide parent undertaking of the insurance or reinsurance group by the [Jurisdiction].
>
> - [Jurisdiction] confirms that information regarding insurers and their parent, subsidiary, or affiliated entities, if applicable, shall be provided to the states in accordance with a memorandum of understanding or similar document between a state and the [Jurisdiction].
>
> - [Jurisdiction] will annually provide to the states confirmation that applicable assuming insurers domiciled in [Jurisdiction] maintain minimum capital and surplus of no less than $250,000,000, and maintain on an ongoing basis the required minimum solvency or capital ratio, as applicable.
>
> - Finally, I confirm that [Jurisdiction] will immediately notify the NAIC upon any changes to the assurances provided in this letter.

e. The Qualified Jurisdiction Working Group will perform a due diligence review of available public and confidential documents to confirm that to the best of its determination, the representations in the letter are true and accurate, and will prepare for the review by the Reinsurance Task Force a Summary of Findings and Determination recommending that the Qualified Jurisdiction be recognized as a Reciprocal Jurisdiction. Upon approval by the Task Force, the Summary of Findings and Determination must be adopted by a vote of the NAIC Executive (EX) Committee and Plenary for inclusion on the List of Reciprocal Jurisdictions.

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f. The Qualified Jurisdiction Working Group, working in coordination with the Qualified Jurisdiction and the Reinsurance Financial Analysis (E) Working Group, must make a determination on a minimum solvency or capital ratio under which reinsurers licensed and domiciled in the Qualified Jurisdiction may assume insurance from U.S. ceding companies without posting reinsurance collateral. The applicable minimum solvency or capital ratio must be an effective measure of solvency, comparable to either an NAIC risk-based capital (RBC) ratio of three hundred percent (300%) of the authorized control level, or one hundred percent (100%) of the solvency capital requirement (SCR) as calculated under the Solvency II Directive issued by the European Union, giving due consideration to any applicable equivalency assessment conducted by the European Insurance and Occupational Pensions Authority (EIOPA) on the Qualified Jurisdiction with respect to Solvency II.

g. Except for Reciprocal Jurisdictions entitled to automatic recognition, a jurisdiction's status as a Reciprocal Jurisdiction may be placed on probation, suspended or revoked for good cause in the same manner as provided for Qualified Jurisdictions under paragraph 12. If cause is found to question the fitness of a Reciprocal Jurisdiction that is subject to an in-force covered agreement, or its compliance with applicable requirements of the covered agreement, the Qualified Jurisdiction Working Group would report any concerns to its parent Task Force for further discussion and communication with appropriate federal and/or international authorities.

IV. Evaluation Methodology

The Evaluation Methodology was developed to be consistent with the provisions of the NAIC Credit for Reinsurance Models. It is intended to provide an outcomes-based comparison to financial solvency regulation under the NAIC Accreditation Program, adherence to international supervisory standards and relevant international guidance for recognition of reinsurance supervision. Although the methodology includes a comparison of the jurisdiction's supervisory system to a number of key elements from the NAIC Accreditation Program, it is not intended as a prescriptive assessment under the NAIC Accreditation Program. Rather, the NAIC Accreditation Program simply provide the framework for the outcomes-based analysis. The NAIC will evaluate the appropriateness and effectiveness of the reinsurance supervisory system within the jurisdiction and consider the rights, benefits and the extent of reciprocal recognition afforded by the jurisdiction to reinsurers licensed and domiciled in the U.S. The determination of a Qualified Jurisdiction is based on the effectiveness of the entire reinsurance supervisory system within the jurisdiction.

The Evaluation Methodology consists of the following:

- Section A: Laws and Regulations
- Section B: Regulatory Practices and Procedures
- Section C: Jurisdiction's Requirements Applicable to U.S.-Domiciled Reinsurers
- Section D: Regulatory Cooperation and Information Sharing
- Section E: History of Performance of Domestic Reinsurers
- Section F: Enforcement of Final U.S. Judgments
- Section G: Solvent Schemes of Arrangement

This information will be the basis for the Final Evaluation Report and the determination of whether the jurisdiction will be included on the NAIC List of Qualified Jurisdictions.

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Section A: Laws and Regulations

The NAIC will review publicly available information, as well as information provided by an applicant jurisdiction with respect to its laws and regulations, in an effort to evaluate whether the jurisdiction has sufficient authority to regulate the solvency of its reinsurers in an effective manner. This will include a review of elements believed to be basic building blocks for sound insurance/reinsurance regulation.[2] A jurisdiction's effectiveness under Section A may be demonstrated through law, regulation or established practice that implements the general authority granted to the jurisdiction, or any combination of laws, regulations or practices that meet the objective.

The Qualified Jurisdiction Working Group will initiate evaluation of a jurisdiction's regulatory system by gathering and undertaking a review of the most recent FSAP Report, ROSC and any other publicly available information regarding the laws, regulations, practices and procedures applicable to the reinsurance supervisory system. The Qualified Jurisdiction Working Group will simultaneously invite each jurisdiction (or its designee) to provide information relative to Section A (and other sections, as relevant) to assist the NAIC in evaluating its laws and regulations. The NAIC will review this information in conjunction with Appendix A, which provides more detailed guidance with respect to elements the NAIC intends to consider on an outcomes basis in the evaluation under this section. Appendix A is not intended as a prescriptive checklist of requirements a jurisdiction must meet in order to be a Qualified Jurisdiction. Rather, it is provided in an effort to facilitate an outcomes-based comparison to financial solvency regulation under the NAIC Accreditation Program. An applicant jurisdiction is requested to address the following information, which the NAIC will consider, at a minimum, in determining whether the outcomes achieved by the jurisdiction's laws and regulations meet an acceptable level of effectiveness for the jurisdiction to be included on the NAIC List of Qualified Jurisdictions:

1. Confirmation of the jurisdiction's most recent FSAP Report, including relevant updates with respect to descriptions or elements of the FSAP Report in which changes have occurred since the assessment or where information might otherwise be outdated.
2. Confirmation of the jurisdiction's ROSC, including relevant updates with respect to descriptions or elements of the ROSC in which changes have occurred since the report was completed or where information might otherwise be outdated.
3. If materials responsive to the topics under review have been provided in response to information exchanges between the jurisdiction under review and the NAIC, such prior responses may be cross-referenced provided updates are submitted, if required to address changes in laws or procedures.
4. Any other information, descriptions or responses the jurisdiction believes would be beneficial to the NAIC's evaluation process in order to address, on an outcomes basis, the key elements described within Appendix A.

The NAIC will review the information provided by the applicant jurisdiction and determine whether it is adequate to reasonably conclude whether the jurisdiction has sufficient authority to regulate the solvency of its reinsurers in an effective manner. After reviewing the initial submission, the NAIC may request that the applicant jurisdiction submit supplemental information as necessary in order to make this determination. An applicant jurisdiction is strongly encouraged to provide thorough, detailed and current information in its initial submission in order to

[2] The basic considerations under this section are derived from Model #786, Section 8C(2), which include: (a) the framework under which the assuming reinsurer is regulated; (b) the structure and authority of the jurisdiction's reinsurance supervisory authority with regard to solvency regulation requirements and financial surveillance; (c) the substance of financial and operating standards for reinsurers domiciled in the jurisdiction; and (d) the form and substance of financial reports required to be filed or made publicly available by reinsurers domiciled in the jurisdiction and the accounting principles used.

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minimize the number and extent of supplemental information requests from the NAIC with respect to Section A of this Evaluation Methodology. The NAIC will provide a complete description in the Final Evaluation Report of the information provided in the Evaluation Materials, and any updates or other information that have been provided by the applicant jurisdiction.

Section B: Regulatory Practices and Procedures

Section B is intended to facilitate an evaluation of whether the jurisdiction effectively employs baseline regulatory practices and procedures to supplement and support enforcement of the jurisdiction's financial solvency laws and regulations described in Section A. This evaluation methodology recognizes that variation may exist in practices and procedures across jurisdictions due to the unique situations each jurisdiction faces. Jurisdictions differ with respect to staff and technology resources that are available, as well as the characteristics of the domestic industry regulated. A determination of effectiveness may be achieved using various financial solvency oversight practices and procedures. This evaluation is not intended to be prescriptive in nature.

The NAIC will utilize the information provided by the jurisdiction as outlined under Section A in completing this section of the evaluation. The NAIC will review this information in conjunction with Appendix B, which provides more detailed guidance with respect to elements the NAIC intends to consider on an outcomes basis in the evaluation under this section. Appendix B is not intended as a prescriptive checklist of requirements a jurisdiction must meet in order to be a Qualified Jurisdiction. Rather, it is provided in an effort to facilitate an outcomes-based comparison to financial solvency regulation under the NAIC Accreditation Program. An applicant jurisdiction should also provide any other information, descriptions or responses the jurisdiction believes would be beneficial to the NAIC's evaluation process in order to address, on an outcomes basis, the key elements described within Appendix B.

Section C: Jurisdiction's Requirements Applicable to U.S. Domiciled Reinsurers

The jurisdiction is requested to describe and explain the rights, benefits and the extent of reciprocal recognition afforded by the non-U.S. supervisory authority to reinsurers licensed and domiciled in the U.S.

Section D: Regulatory Cooperation and Information-Sharing

The Credit for Reinsurance Models require the supervisory authority to share information and cooperate with the U.S. state insurance regulators with respect to all certified reinsurers domiciled within their jurisdiction. The jurisdiction is requested to provide an explanation of the supervisory authority's ability to cooperate, share information and enter into an MOU with U.S. state insurance regulators and confirm that they are willing to enter into an MOU. This should include information with respect to any existing MOU with U.S. state and/or federal authorities that pertain to reinsurance. Both the jurisdiction and the states may rely on the IAIS MMoU to satisfy this requirement, and any states that have not yet been approved by the IAIS as a signatory to the MMoU may rely on an MOU entered into by a Lead State with the jurisdiction until such time that the state has been approved as a signatory to the IAIS MMoU. The NAIC and the states will communicate and coordinate with the FIO, USTR and other relevant federal authorities as appropriate with respect to this process.

Section E: History of Performance of Domestic Reinsurers

The jurisdiction is requested to provide a general description with respect to the historical performance of reinsurers domiciled in the jurisdiction. The NAIC does not intend to review confidential company-specific information under this section. Rather, it is intended that any information provided would be publicly available, unless specifically addressed with the jurisdiction under review. This discussion should address, at a minimum, the following information:

a. Number of reinsurers domiciled in the jurisdiction, and a list of any reinsurers domiciled in the jurisdiction that have and maintain, on an ongoing basis, minimum capital and surplus, or its equivalent, of no less than $250,000,000.

b. Up to a 10-year history of any regulatory actions taken against specific reinsurers.

c. Up to a 10-year history listing any reinsurers that have gone through insolvency proceedings, including the size of each insolvency and a description of the related outcomes (e.g., reinsurer rehabilitated or liquidated, payout percentage of claims to priority classes, payout percentage of claims to domestic and foreign claimants).

d. Up to a 10-year history of any significant industry-wide fluctuations in capital or profitability with respect to domestic reinsurers.

Drafting Note: The NAIC will determine the appropriate time period for review on a case-by-case basis with respect to this information.

Section F: Enforcement of Final U.S. Judgments

The NAIC has previously collected information from a number of jurisdictions with respect to enforcement of final U.S. judgments. The jurisdiction is also requested to provide a current description or explanation of any restrictions with respect to the enforcement of final foreign judgments in the jurisdiction. Based on the foregoing information, the NAIC will make an assessment of the effectiveness of the ability to enforce final U.S. judgments in the jurisdiction. This will include a review of the status, interpretations, application and enforcement of various treaties, conventions and international agreements with respect to final judgments, arbitration and choice of law. The Qualified Jurisdiction Working Group will monitor the enforcement of final U.S. judgments and the Qualified Jurisdiction is requested to notify the NAIC of any developments in this area.

Section G: Solvent Schemes of Arrangement

The jurisdiction is requested to provide a description of any legal framework that allows reinsurers domiciled in the jurisdiction to propose or participate in any solvent scheme of arrangement or similar procedure. In addition, the jurisdiction is requested to provide a description of any solvent scheme of arrangement or similar procedure that a domestic reinsurer has proposed or participated in and the outcome of such procedure.

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V. Appendices: Specific Guidance with Respect to Section A and Section B

It is important to note that Part IV, Section A: Laws and Regulations, and Part IV, Section B: Regulatory Practices and Procedures, are derived from the NAIC Financial Regulation Standards and Accreditation Program, which is intended to establish and maintain standards to promote sound insurance company financial solvency regulation among the U.S. states. As such, the NAIC Accreditation Program requires the states to employ laws, regulations and administrative policies and procedures substantially similar to the NAIC accreditation standards in order to be considered an accredited state.

However, it is not the intent of the Evaluation Methodology to require applicant jurisdictions to meet the standards required by the NAIC for accreditation. Instead, Section A and Section B (and their corresponding appendices) are intended to provide a framework to facilitate an outcomes-based evaluation by the NAIC and state insurance regulators of the effectiveness of the jurisdiction's supervisory authority. This framework consists of a description of the jurisdiction's laws, regulations, practices and procedures applicable to the supervision of its domestic reinsurers. The amount of detail provided within these appendices should not be interpreted as specific requirements that must be met by the applicant jurisdiction. Rather, the information is intended to provide direction to the applicant jurisdiction in an effort to facilitate a complete response and increase the efficiency and timeliness of the evaluation process.

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Appendix A: Laws and Regulations

1. Examination Authority

Does the jurisdiction have the authority to examine its domestic reinsurers? This description should address the following:

a. Frequency and timing of examinations and reports.

b. Guidelines for examination.

c. Whether the jurisdiction has the authority to examine reinsurers whenever it is deemed necessary.

d. Whether the jurisdiction has the authority to have complete access to the reinsurer's books and records and, if necessary, the records of any affiliated company.

e. Whether the jurisdiction has the authority to examine officers, employees and agents of the reinsurer when necessary with respect to transactions directly or indirectly related to the reinsurer under examination.

f. Whether the jurisdiction has the authority to share confidential information with U.S. state insurance regulatory authorities, provided that the recipients are required, under their law, to maintain its confidentiality.

2. Capital and Surplus Requirement

Does the jurisdiction have the authority to require domestic reinsurers to maintain a minimum level of capital and surplus to transact business? This description should address the following:

a. Whether the jurisdiction has the authority to require reinsurers to maintain minimum capital and surplus, including a description of such minimum amounts.

b. Whether the jurisdiction has the authority to require additional capital and surplus based on the type, volume and nature of reinsurance business transacted.

c. Capital requirements for reinsurers, including reports and a description of any specific levels of regulatory intervention.

3. Accounting Practices and Procedures

Does the jurisdiction have the authority to require domestic reinsurers to file appropriate financial statements and other financial information? This description should address the following:

a. Description of the accounting and reporting practices and procedures.

b. Description of any standard financial statement blank/reporting template, including description of content/disclosure requirements and corresponding instructions.

4. Corrective Action

Does the jurisdiction have the authority to order a reinsurer to take corrective action or cease and desist certain practices that, if not corrected or terminated, could place the reinsurer in a hazardous financial condition? This description should address the following:

a. Identification of specific standards which may be considered to determine whether the continued operation of the reinsurer might be hazardous to the general public.

b. Whether the jurisdiction has the authority to issue an order requiring the reinsurer to take corrective action when it has been determined to be in hazardous financial condition.

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5. Regulation and Valuation of Investments

What authority does the jurisdiction have with respect to regulation and valuation of investments? This description should address the following:

a. Whether the jurisdiction has the authority to require a diversified investment portfolio for all domestic reinsurers as to type, issue and liquidity.

b. Whether the jurisdiction has the authority to establish acceptable practices and procedures under which investments owned by reinsurers must be valued, including standards under which reinsurers are required to value securities/investments.

6. Holding Company Systems

Does the jurisdiction have laws or regulations with respect to supervision of the group holding company systems of reinsurers? This description should address the following:

a. Whether the jurisdiction has access to information via the parent or other regulated group entities about activities or transactions within the group involving other regulated or non-regulated entities that could have a material impact on the operations of the reinsurer.

b. Whether the jurisdiction has access to consolidated financial information of a reinsurer's ultimate controlling person.

c. Whether the jurisdiction has the authority to review integrity and competency of management.

d. Whether the jurisdiction has approval and intervention powers for material transactions and events involving reinsurers.

e. Whether the jurisdiction has authority to monitor, or has prior approval authority over:

i. Change in control of domestic reinsurers.

ii. Dividends and other distributions to shareholders of the reinsurer.

iii. Material transactions with affiliates.

7. Risk Management

Does the jurisdiction have the authority to require its domestic reinsurers to maintain an effective risk-management function and practices? This description should address the following:

a. Whether the jurisdiction has Own Risk and Solvency Assessment (ORSA) requirements and reporting.

b. Any requirements regarding the maximum net amount of risk to be retained by a reinsurer for an individual risk based on the reinsurer's capital and surplus.

c. Whether the jurisdiction has authority to monitor enterprise risk, including any activity, circumstance, event (or series of events) involving one or more affiliates of a reinsurer that, if not remedied promptly, is likely to have a material adverse effect on the financial condition or liquidity of the reinsurer or its insurance holding company system as a whole.

d. Whether the jurisdiction has corporate governance requirements for reinsurers.

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8. Liabilities and Reserves

Does the jurisdiction have standards for the establishment of liabilities and reserves (technical provisions) resulting from reinsurance contracts? This description should address the following:

a. Liabilities incurred under reinsurance contracts for policy reserves, unearned premium, claims and losses unpaid, and incurred but not reported (IBNR) claims (including whether discounting is allowed for reserve calculation/reporting).

b. Liabilities related to catastrophic occurrences.

c. Whether the jurisdiction requires an opinion on reserves and loss and loss adjustment expense reserves by a qualified actuary or specialist for all domestic reinsurers, and the frequency of such reports.

9. Reinsurance Ceded

What are the jurisdiction's requirements with respect to the financial statement credit allowed for reinsurance retroceded by its domestic reinsurers? This description should address the following:

a. Credit for reinsurance requirements applicable to reinsurance retroceded to domestic and non-domestic reinsurers.

b. Collateral requirements applicable to reinsurance contracts.

c. Whether the jurisdiction requires a reinsurance agreement to provide for insurance risk transfer (i.e., transfer of both underwriting and timing risk).

d. Requirements applicable to special purpose reinsurance vehicles and insurance securitizations.

e. Affiliated reinsurance transactions and concentration risk.

f. Disclosure requirements specific to reinsurance transactions, agreements and counterparties, if such information is not provided under another item.

10. Independent Audits

Does the jurisdiction require annual audits of domestic reinsurers by independent certified public accountants or similar accounting/auditing professional recognized in the applicant jurisdiction? This description should address the following:

a. Requirements for the filing of audited financial statements prepared in conformity with accounting practices prescribed or permitted by the supervisory authority.

b. Contents of annual audited financial reports.

c. Requirements for selection of auditor.

d. Allowance of audited consolidated or combined financial statements.

e. Notification of material misstatements of financial condition.

f. Supervisor's access to auditor's workpapers.

g. Audit committee requirements.

h. Requirements for reporting of internal control-related matters.

11. Receivership

Does the jurisdiction have a receivership scheme for the administration of reinsurers found to be insolvent? This should include a description of any liquidation priority afforded to policyholders and the liquidation priority of reinsurance obligations to domestic and non-domestic ceding insurers in the context of an insolvency proceeding of a reinsurer.

12. Filings with Supervisory Authority

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Does the jurisdiction require the filing of annual and interim financial statements with the supervisory authority? This description should address the following:

a. The use of standardized financial reporting in the financial statements, and the frequency of relevant updates.

b. The use of supplemental data to address concerns with specific companies or issues.

c. Filing format (e.g., electronic data capture).

d. The extent to which financial reports and information are public records.

13. Reinsurance Intermediaries

Does the jurisdiction have a regulatory framework for the regulation of reinsurance intermediaries?

14. Other Regulatory Requirements with respect to Reinsurers

Any other information necessary to adequately describe the effectiveness of the jurisdiction's laws and regulations with respect to its reinsurance supervisory system.

Appendix B: Regulatory Practices and Procedures

1. Financial Analysis

What are the jurisdiction's practices and procedures with respect to the financial analysis of its domestic reinsurers? Such description should address the following:

a. Qualified Staff and Resources
The resources employed to effectively review the financial condition of all domestic reinsurers, including a description of the educational and experience requirements for staff responsible for financial analysis.

b. Communication of Relevant Information to/from Financial Analysis Staff
The process under which relevant information and data received by the supervisory authority are provided to the financial analysis staff and the process under which the findings of the financial analysis staff are communicated to the appropriate person(s).

c. Supervisory Review
How the jurisdiction's internal financial analysis process provides for supervisory review and comment.

d. Priority-Based Analysis
How the jurisdiction's financial analysis procedures are prioritized in order to ensure that potential problem reinsurers are reviewed promptly.

e. Depth of Review
How the jurisdiction's financial analysis procedures ensure that domestic reinsurers receive an appropriate level or depth of review commensurate with their financial strength and position.

f. Analysis Procedures
How the jurisdiction has documented its 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 reinsurer.

g. Reporting of Material Adverse Findings
The process for reporting material adverse indications, including the determination and implementation of appropriate regulatory action.

h. Early Warning System/Stress Testing
Whether the jurisdiction has an early warning system and/or stress testing methodology that is utilized with respect to its domestic reinsurers.

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2. Financial Examinations

What are the jurisdiction's practices and procedures with respect to the financial examinations of its domestic reinsurers? Such description should address the following:

a. Qualified Staff and Resources
The resources employed to effectively examine all domestic reinsurers. This should include whether the jurisdiction prioritizes examination scheduling and resource allocation commensurate with the financial strength and position of each reinsurer, and a description of the educational and experience requirements for staff responsible for financial examinations.

b. Communication of Relevant Information to/from Examination Staff
The process under which relevant information and data received by the supervisory authority are provided to the examination staff and the process under which the findings of the examination staff are communicated to the appropriate person(s).

c. Use of Specialists
Whether the supervisory authority's examination staff includes specialists with appropriate training and/or experience or whether the supervisory authority otherwise has available qualified specialists that will permit the supervisory authority to effectively examine any reinsurer.

d. Supervisory Review
Whether the supervisory authority's procedures for examinations provide for supervisory review.

e. Examination Guidelines and Procedures
Description of the policies and procedures the supervisory authority employs for the conduct of examinations, including whether variations in methods and scope are commensurate with the financial strength and position of the reinsurer.

f. Risk-Focused Examinations
Does the supervisory authority perform and document risk-focused examinations and, if so, what guidance is utilized in conducting the examinations? Are variations in method and scope commensurate with the financial strength and position of the reinsurer?

g. Scheduling of Examinations
Whether the supervisory authority's procedures provide for the periodic examination of all domestic reinsurers, including how the system prioritizes reinsurers that exhibit adverse financial trends or otherwise demonstrate a need for examination.

h. Examination Reports
Description of the format in which the supervisory authority's reports of examinations are prepared, and how the reports are shared with other jurisdictions under information-sharing agreements.

i. Action on Material Adverse Findings
What are the jurisdiction's procedures regarding supervisory action in response to the reporting of any material adverse findings.

3. Information Sharing

Does the jurisdiction have a process for the sharing of otherwise confidential documents, materials, information, administrative or judicial orders, or other actions with U.S. state regulatory officials, provided that the recipients are required, under their law, to maintain its confidentiality?

4. Procedures for Troubled Reinsurers

What procedures does the jurisdiction follow with respect to troubled reinsurers?

5. Organization, Licensing and Change of Control of Reinsurers

What processes does the supervisory authority use to identify unlicensed or fraudulent activities? The description should address the following:

a. Licensing Procedure
Whether the supervisory authority has documented licensing procedures that include a review and/or analysis of key pieces of information included in a primary licensure application.

b. Staff and Resources
The educational and experience requirements for staff responsible for evaluating company licensing.

c. Change in Control of a Domestic Reinsurer
Procedures for the review of key pieces of information included in filings with respect to a change in control of a domestic reinsurer.

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Pending Adoption by Executive (EX) Committee and Plenary – 12/10/19
Adopted by Financial Condition (E) Committee – 10/31/19
Adopted by Receivership and Insolvency (E) Task Force – 8/4/19

GUIDELINE FOR STAY ON TERMINATION OF NETTING AGREEMENTS AND QUALIFIED FINANCIAL CONTRACTS

Drafting Note: State receivership and insolvency laws may permit a contractual right to cause the termination, liquidation, acceleration or close-out obligations with respect to any netting agreement or qualified financial contract (QFC) with an insurer because of the insolvency, financial condition or default of the insurer, or the commencement of a formal delinquency proceeding. These laws are based upon similar provisions contained in the federal bankruptcy code and the Federal Deposit Insurance Act (FDIA). The FDIA also provides for a twenty-four-hour stay to allow for the transfer of QFCs by the receiver to another entity rather than permitting the immediate termination and netting of the QFC. 12 U.S.C. § 1821(e)(9)-(12). States that permit the termination and netting of QFCs may want to consider adopting a similar stay provision following the appointment of a receiver.

States that consider the enactment of a stay should take into account the relevant federal rules. In 2017 the Board of Governors of the Federal Reserve System (the Federal Reserve), the Federal Deposit Insurance Corporation (the FDIC) and the Office of the Comptroller of the Currency (the OCC) each adopted final rules and accompanying interpretive guidance (Final Rules) setting forth limitations to be placed on parties to certain financial contracts exercising insolvency-related default rights against their counterparties that have been designated as a global systemically important banking organization (GSIB).[1] The Final Rules include the definition of master netting agreement that allows netting even though termination of the transaction in the event of an insolvency may be subject to a "stay" under several defined resolution regimes including Title II of Dodd Frank, the FDIA, as well as comparable foreign resolution regimes. Notwithstanding NAIC's request for inclusion, stays under the state insurance receivership regime (State Receivership Stays) were not included as an exemption within the definition. Therefore, unless the Final Rules are amended to recognize State Receivership Stays, if a state implements a stay as contemplated by the Guideline, insurers would find themselves disadvantaged, potentially resulting in additional costs and/or collateral requirements given the regulatory treatment for contracts that do not meet requirements for QFCs. Therefore, if a state is considering implementation of this Guideline, consideration should be given to whether the rules of the Federal Reserve, FDIC and OCC have been amended to recognize State Receivership Stays. For example, a state could adopt a stay that would be effective if and when the Final Rules recognize State Receivership Stays.

The following statutory language is not an amendment to the NAIC receivership models, but is intended as a Guideline for use by those states seeking to require a stay with respect to the termination of a netting agreement or QFC of an insurer in insolvency:

Stay on Termination of Netting Agreements and Qualified Financial Contracts

A person who is a party to a netting agreement or qualified financial contract under [cite to applicable state law addressing qualified financial agreements] with an insurer that is the subject of an insolvency proceeding may not exercise any right that the person has to terminate, liquidate, accelerate or close-out the obligations with respect to the contract by reason of the insolvency, financial condition or default of the insurer, or by the commencement of a formal delinquency proceeding,

(1) Until 5:00 p.m. (eastern time) on the business day following the date of appointment of a receiver; or

(2) After the person has received notice that the contract has been transferred pursuant to [cite applicable state law addressing transfer of qualified financial contracts].

Chronological Summary of Action (all references are to the Proceedings of the NAIC)

2013 Proc. 2nd Quarter, Vol. I 113, 127, 131-132, 537-538 (adopted).

[1] *Restrictions on Qualified Financial Contracts of Systemically Important U.S. Banking Organizations and the U.S. Operations of Systemically Important Foreign Banking Organizations*; Revisions to the Definition of Qualifying Master Netting Agreement and Related Definitions, 82 FR 42882 (13 November 2017), available at https://www.federalregister.gov/d/2017-19053; *Restrictions on Qualified Financial Contracts of Certain FDIC Supervised Institutions*; Revisions to the Definition of Qualifying Master Netting Agreement and Related Definitions, 82 FR 50228 (30 October 2017), available at https://www.federalregister.gov/d/2017-21951; *Restrictions on Qualified Financial Contracts of Certain FDIC-Supervised Institutions*; Revisions to the Definition of Qualifying Master Netting Agreement and Related Definition, 82 FR 61443 (28 December 2017), available at https://www.federalregister.gov/d/2017-27971; *Mandatory Contractual Stay Requirements for Qualified Financial Contracts*, 82 FR 56630 (29 November 2017), available at https://www.federalregister.gov/d/2017-25529.

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PROJECT HISTORY

GUIDELINE FOR STAY ON TERMINATION OF NETTING AGREEMENTS AND QUALIFIED FINANCIAL CONTRACTS

1. Description of the Project, Issues Addressed, etc.

In 2017 the Board of Governors of the Federal Reserve System (the Federal Reserve), the Federal Deposit Insurance Corporation (the FDIC) and the Office of the Comptroller of the Currency (the OCC) each adopted final rules and accompanying interpretive guidance (Final Rules) setting forth limitations to be placed on parties to certain financial contracts exercising insolvency-related default rights against their counterparties that have been designated as a global systemically important banking organization (GSIB).[2] The Final Rules include the definition of master netting agreement that allows netting even though termination of the transaction in the event of an insolvency may be subject to a "stay" under several defined resolution regimes including Title II of Dodd Frank, the FDIA, as well as comparable foreign resolution regimes.

Notwithstanding NAIC's request for inclusion through a formal comment letter and subsequent discussions, stays under the state insurance receivership regime (State Receivership Stays) were not included as an exemption within the definition. Therefore, unless the Final Rules are amended to recognize State Receivership Stays, if a state implements a stay as contemplated by the *Guideline for Stay on Termination of Netting Agreements and Qualified Financial Contracts* (Guideline #1556), insurers would find themselves disadvantaged, potentially resulting in additional costs and/or collateral requirements given the regulatory treatment for contracts that do not meet requirements for qualified financial contracts (QFCs).

On Dec. 2, 2017, the Receivership and Insolvency (E) Task Force received a referral from the Financial Stability (EX) Task Force that included three tasks, one of which was to "evaluate whether there are any current misalignments between federal and state laws that could be an obstacle to achieving effective and orderly recovery and resolutions for U.S. insurance groups (e.g., federal rule recognizing importance of temporary stays on the termination of master netting agreements for QFCs that does not recognize the utility and import of state-based stays in state receivership proceedings).

The RITF assigned the task of evaluating these issues to a drafting group, who evaluated the impact of the federal rule recognizing temporary stays on terminating master netting agreements for QFCs. The regulators held discussions with federal banking authorities regarding the handling of QFCs in banking resolutions to assess the utility of a stay on terminations in insurance receiverships.

To address the conflict with the federal rule, the drafting group proposed amendments to the drafting note of Guideline #1556 explaining the above issue. Therefore, if a state is considering implementation of Guideline #1556, consideration should be given to whether the rules of the Federal Reserve, FDIC and OCC have been amended to recognize State Receivership Stays. For example, a state could adopt a stay that would be effective if and when the Final Rules recognize State Receivership Stays.

2. Name of Group Responsible for Drafting the Guideline and States Participating

The Receivership and Insolvency (E) Task Force is responsible for Guideline #1556. The 2019 members of the Task Force are: Texas (Chair); District of Columbia (Co-Vice Chair), Alaska, American Samoa, Arkansas, California, Colorado, Connecticut, Florida, Illinois, Iowa, Kansas, Kentucky, Louisiana, Massachusetts, Missouri, Montana, Nebraska, New Jersey, New Mexico, North Carolina, Oklahoma, Pennsylvania, Rhode Island, South Carolina, Tennessee, Utah, Virginia, and Washington.

The amendments to Guideline #1556 were drafted by the Task Force's drafting group. The drafting group was comprised of Texas (Lead), Colorado, Connecticut, District of Columbia, Illinois, Massachusetts, Michigan, New Jersey, New Mexico, Pennsylvania. Washington, and Wisconsin.

[2] *Restrictions on Qualified Financial Contracts of Systemically Important U.S. Banking Organizations and the U.S. Operations of Systemically Important Foreign Banking Organizations*; Revisions to the Definition of Qualifying Master Netting Agreement and Related Definitions, 82 FR 42882 (13 November 2017), available at https://www.federalregister.gov/d/2017-19053; *Restrictions on Qualified Financial Contracts of Certain FDIC Supervised Institutions*; Revisions to the Definition of Qualifying Master Netting Agreement and Related Definitions, 82 FR 50228 (30 October 2017), available at https://www.federalregister.gov/d/2017-21951; *Restrictions on Qualified Financial Contracts of Certain FDIC-Supervised Institutions*; Revisions to the Definition of Qualifying Master Netting Agreement and Related Definition, 82 FR 61443 (28 December 2017), available at https://www.federalregister.gov/d/2017-27971; *Mandatory Contractual Stay Requirements for Qualified Financial Contracts*, 82 FR 56630 (29 November 2017), available at https://www.federalregister.gov/d/2017-25529.

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3. Project Authorized by What Charge and Date First Given to the Group

The Receivership and Insolvency (E) Task Force is charged with addressing any issues that affect receivership laws, including amendments to models and guidelines. The request to address misalignments with federal rules was first considered by the Task Force on March 25, 2018, at the NAIC 2018 Spring National Meeting, when a work plan to address the Financial Stability (EX) Task Force's referral and formation of drafting groups were discussed.

4. A General Description of the Drafting Process and Due Process

The drafting group of the Receivership and Insolvency (E) Task Force discussed the proposed amendments on a conference call on March 14, 2019, which included twenty interested parties.

The Receivership and Insolvency (E) Task Force discussed the proposed amendments in open session on April 7, 2019, at the NAIC Spring National Meeting. The Task Force exposed the proposed amendments for a 30-day public comment period ending May 7, 2019. One comment was received supporting the need for Federal rule changes. No changes were made to the Guideline #1556.

The Receivership and Insolvency (E) Task Force adopted the amendments on Aug. 4, 2019, at the NAIC Summer National Meeting.

The Financial Condition (E) Committee adopted the amendments on October 31, 2019.

The NAIC Executive (EX) Committee and Plenary adopted the amendments on [DATE TBD].

5. A Discussion of the Significant Issues

None.

6. Any Other Important Information

None.

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National Association of Insurance Commissioners & The Center for Insurance Policy and Research

To: Commissioner Todd E. Kiser (UT), Chair of Financial Regulation Standards and Accreditation (F) Committee

From: Jeff Hunt (TX) and Joel Sander (OK), Co-Chairs of National Treatment and Coordination (E) Working Group

Date: February 15, 2019

Re: Company Licensing Accreditation Standards

Executive Summary

The National Treatment and Coordination (E) Working Group (Working Group) is charged with monitoring usage of the Form A database and implementation of company licensing best practices. As of a result of this monitoring, updates and enhancements are made that must also be considered for their impact on the accreditation program and, specifically, Part D: Organization, Licensing and Change of Control of Domestic Insurers (Part D).

On February 14, 2019 the Working Group adopted a recommendation regarding the Part D Accreditation Standards to a) update the guidelines to reflect current practices, b) expand the scope to include redomestications, and c) include Part D in the review team's recommendation with the result that the outcome can affect a state's accredited status.

A baseline set of standards for the completion of primary applications for the licensing of new companies and redomestications, and Form A filings promotes reliance on other states in these important functions. Each application requires consideration of financial solvency of the insurers to both strengthen financial regulation and prevent unlicensed or fraudulent activities. The significant reliance on other states combined with the potential solvency impact of non-compliance with the Part D standards result in the recommendation to the Financial Regulation Standards and Accreditation (F) Committee outlined in this referral.

The Working Group recommends that the revisions to the guidelines be adopted with an effective date of January 1, 2020. However, the Working Group also recommends that the effective date for subjecting Part D to Recommendation A or B and thus impacting a state's accredited status, be effective January 1, 2022. This timeline allows states to adjust to the revised guidelines before elevating the status of the Part D standards. The recommendations are intended to be prospective and applicable to filings received on or after the effective date.

Summary of Changes

<u>Updates to Reflect Current Practices</u>
Following is a summary of the Working Group's recommended revisions to the Part D accreditation guidelines:

1) update the scope to include primary applications for redomestications,
2) update timing guidelines to rely on department policies along with state statute or regulation or the Company Licensing Best Practices Handbook,

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3) add a new standard for the scope and performance of procedures for redomestications which includes elements of a quality review in addition to communication expectations,
4) update the process-oriented guidelines for Form A filings to include documenting an assessment of business plans and the quality and expertise of key persons, and
5) require updates to the Form A database at a minimum every six months for open filings.
6) update the title of Part D to "Primary Licensing, Redomestications and Change of Control"

Expand Scope to Redomestications

Insurance companies redomicile for a variety of reasons. When a redomestication occurs, state regulators take on the responsibility to review the request. The Working Group believes it is key for regulators in both states to communicate, review the information provided, and understand the reasons for the redomestication. In addition, the Working Group received a referral from the Financial Analysis (E) Working Group (FAWG) supporting inclusion of redomestications in the Part D Standards based on their work monitoring troubled and potentially troubled companies. As an example, FAWG has identified situations where companies have sought to take advantage of the redomestication process to achieve regulatory arbitrage. The recommended accreditation guidelines include elements for a quality review of these transactions as well as communication requirements with other regulators.

Subject to Recommendation A or B

In 2016, The Working Group together with the Group Solvency Issues (E) Working Group redesigned the Form A Database to enhance regulatory reviews and provide a more dynamic regulatory tool. The database now captures more information regarding mergers, acquisitions, consolidated hearings and/or coordinated reviews of Form A filings. The Form A is reviewed and analyzed by the state in which the Form A is filed, and the appropriate action is taken by the state to either approve or disapprove the transaction within a specified time frame. Making this information available to regulators in each state via the Form A Database provides awareness of other similar transactions such as a large insurer initiating acquisitions in numerous states or denials/issues with filings from the same ultimate controlling party. The database can also lead to efficiencies in analyzing similar transactions using the Lead State concept incorporated into the database.

To fully realize the regulatory value the Form A Database can provide, all states must effectively use the database for each applicable transaction. The Working Group recommends subjecting the Part D accreditation guidelines to a Recommendation A or B as defined in the accreditation manual to ensure a complete database of information.

In the primary application process for new companies, other states may not immediately rely on the work done by the domiciliary state, but as soon as the insurer begins requesting licenses in other states, heavy reliance is placed on the initial application process done by the domiciliary state. In the primary application process for redomestications, other states rely on the new domestic regulator as discussed above.

Therefore, primary applications for new companies and redomestications, in addition to Form A filings, are equally important and should be encompassed in the Recommendation A or B for the entirety of Part D.

A statement and explanation of how the potential standard is directly related to solvency surveillance and why the proposal should be included in the standards:

The purpose of subjecting primary licensing, redomestications and mergers/acquisitions to Recommendation A or B is to ensure that states have effective processes in place that other states may rely on when these functions are performed. A quality review of each filing includes assessing the financial solvency of the company to ensure the interests of the policyholders are met. These filings promote interstate communication and coordination, which are key elements of effective solvency regulation and an area of increased focused as holding company assessments, supervisory colleges and other coordinated efforts increase the effectiveness of regulation.

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In addition, the Form A Database provides a system to communicate whether any similar or related Form A has been approved, denied or withdrawn from another state. The purpose of this database is to: 1) facilitate the communication of actions taken by the states on all Form A filings; and 2) facilitate the coordination of Form A reviews in an attempt to avoid the duplication of regulatory processes via a Web-based application. This database will assist insurance regulators by producing a streamlined regulatory process that maintains the integrity of state holding company laws, while being responsive to a dynamic and evolving industry.

A statement as to why ultimate adoption by every jurisdiction may be desirable:

States place significant reliance on the work of another state's review and approval/denial of a primary application for a new company or redomestication or a Form A filing. Elements within the standard such as review of items submitted by the company along with communication between states enhance the system of state-based regulation. Reliance is most effective when states have comfort that other states are in compliance with the minimum uniform standards.

In addition to increasing the uniformity of review, the updated guidelines are designed to enhance the value of the Form A Database. As of December 2018, a substantial number of Form A filings had not been updated in over a year, likely due to delays outside the state's control. The revised guidelines will require a status update in the Form A Database at least once every six months. With more current information available, states have more tools to avoid fraudulent or questionable acquisitions that could lead to insolvency of an insurer.

A statement as to the number of jurisdictions that have adopted and implemented the proposal or a similar proposal and their experience to date:

Part D initially became effective for accreditation in 2012 as an "unscored" section of the accreditation program. This meant that a state could not fail accreditation based solely on the lack of compliance with these standards. If deficiencies were noted, the review team would provide management comments to the state insurance department, requesting the state to consider improvements as needed, but Part D would not factor into a state's accredited status. Because state's have been subject to this section since 2012, there is already a base level of compliance. Including the standards in the review team's recommendation appropriately elevates the importance of the reliance placed on these processes.

Note: The accreditation program moved from a scoring system to a recommendation system effective January 1, 2017.

A statement as to the provisions needed to meet the minimum requirements of the standard:

Revised standards and guidelines for Part D are attached.

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PART D: ~~ORGANIZATION, LICENSING AND CHANGE OF CONTROL OF DOMESTIC INSURERS~~PRIMARY LICENSING, REDOMESTICATIONS AND CHANGE OF CONTROL

Preamble for Part D

The focus of the Part D standards is on strengthening financial regulation and the prevention of unlicensed or fraudulent activities. The scope of this section only includes primary applications for the licensing of new companies and redomestications, and Form A filings. The section applies to only traditional life/health and property/casualty companies, and this scope is narrower than that of Part B in that it does not include entities such as health maintenance organizations, health service plans, and captive insurers (including captive risk retention groups). These standards only deal with the department's analysis of domestic companies or those applying for redomestication, and do not include foreign or alien insurers. The initial company licensing process does not consider the "multi-state" concept since the company is in its initial licensing phase. The standards regarding primary applications for redomestications, and Form A filings ~~deal with~~ apply to only those filings submitted that are related to multi-state insurers, as that term is defined in the Part B Preamble.

Part D: ~~Organization, Licensing and Change of Control of Domestic Insurers~~Primary Licensing, Redomestications and Change of Control

a. Sufficient Qualified Staff and Resources

Standard: The department should have the appropriate staff and resources to effectively and timely review applications for primary licensure of new companies and redomestications, and Form A filings for all domestic insurers.

Results-Oriented Guidelines:

1. The department should have qualified staff with appropriate skill sets, abilities, knowledge and experience levels to satisfactorily and effectively perform a thorough review of applications for primary licensure of new companies and redomestications, and Form A filings. When assessing whether a department has qualified staff and resources, consideration should be given to the quality of work ~~performed by department staff~~ as documented in the files.

2. The review of applications for primary licensure of new companies and redomestications, and Form A filings should be completed timely, as described by department procedures.~~as discussed in the Compliance Guidelines~~process-oriented guidelines.~~.~~ If the review was not completed timely, the department should document the reasons for such, and the review team may take extenuating circumstances into consideration.

Process-Oriented Guidelines:

1. The department staff responsible for reviewing the applications for primary licensure of new companies and redomestications, and Form A filings should have an accounting, insurance, financial analysis and/or actuarial background. College degrees should focus on accounting,

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insurance, finance or actuarial science. Professional designations and credentials may also demonstrate expertise in insurance and/or financial analysis.

2. The department should have a policy that establishes timing requirements for the review of applications for primary licensure of new companies and redomestications, and Form A filings. The policy should include timing expectations for initial review from date of receipt, notification to the insurer, and completion of the review. The policy should account for any requirements mandated by the state's statute or regulation. The use of the Company Licensing Best Practices Handbook is considered acceptable.

~~The department should review applications for primary licensure of new companies and , redomestications, and Form A filings within 30 days of receipt. If additional or supplementary information is needed from the insurer based on the initial review for completeness, the insurer should be notified of such within 45 days of receipt of the application.~~

~~3. For primary applications of new companies and redomestications, the review should be completed in accordance with timing requirements mandated by the state's statute or regulation, unlessif the state's statutes or regulations do not specify timing requirements, in which case, the review should be completed within 90 calendar days of receipt. A review of an application is complete once the insurer is notified of approval or denial. If additional information not originally requested in the application is needed to finalize the review of the application, the review may take longer to complete. Once a request for information is made, the timing requirement is suspended until the information is received from the applicant.~~

~~For Form A filings, Tthe review of the primary application or Form A should be completed in accordance with timing requirements mandated by the state's statute or regulation.~~

b. Scope and Performance of Procedures for Primary Applications

Standard: The department should have documented licensing procedures to provide for consistency in the review process and to ensure that appropriate procedures are performed on all primary applications. The use of the Company Licensing Best Practices Handbook is considered acceptable.

Results-Oriented Guidelines:

1. The review process should adequately assess primary applications and allow the department to reach appropriate conclusions regarding whether the primary applications are approved or denied.

Process-Oriented Guidelines:

1. The department should review and document its assessment of each of the following:
   - Business and strategic plans.
   - Pro forma financial projections.
   - Adequacy of proposed reinsurance program.
   - Adequacy of investment policy.
   - Adequacy of short-term and long-term financing arrangements:

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- Initial financing of proposed operations or transactions.
- Maintenance of adequate capital and surplus levels.

- Biographical affidavits
- Assessment of the quality and expertise of the following:
  - Ultimate controlling person.
  - Proposed officers and directors.
  - Appointed actuary.
  - Appointed accountant.
- Related party agreements' compliance with Statement of Statutory Accounting Principles *(SSAP) No. 25—Affiliates and Other Related Parties*.

2. The department should review the NAIC Form A and ~~Special Activities Database (SAD)~~Market Action Tracking System (MATS) databases for related information about the primary applicant and other key persons.

c. Scope and Performance of Procedures for Redomestications

Standard: The department should have documented procedures for the review of redomestication applications to provide for consistency in the review process and to ensure that appropriate procedures are performed for all redomestications. The use of the Company Licensing Best Practices Handbook and/or Financial Analysis Handbook are considered acceptable.

Results-Oriented Guidelines:

1. The review process should adequately assess the redomestication application and accompanying information to effectively allow the department to reach appropriate conclusions regarding whether a redomestication application is approved or denied.

2. The department should effectively communicate with the domestic state to gain an understanding of the reasons for redomestication and any concerns of the domestic state. Any concerns raised should be assessed and documented with rationale to support the conclusion.

Process-Oriented Guidelines:

1. The department should review the application and accompanying information and document, at a minimum, its assessment of each of the following:
   - Business and strategic plans of the insurer.
   - Actuarial Opinion
   - Annual and Quarterly statements
   - Risk-based capital (RBC) report
   - Independent CPA audit report
   - Insurance Holding Company System Annual Registration Statement and Exhibits (Form B)
   - Assessment of senior management, board of directors and corporate governance

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2. The department should meet with the domestic regulator to obtain, discuss, and conclude on, at a minimum, the items listed below. The meeting should be held via conference call; an email exchange alone is not considered sufficient.
   - Most recent Insurer Profile Summary (IPS) and supervisory plan, including supporting analysis detail for significant risks
   - Reason for redomestication
   - Concerns identified with the insurer/group
   - History of communication with the insurer/group
   - History of regulatory actions
   - Results of recent examinations (financial and market conduct), including findings and resolutions
   - Status of and responsibilities for annual financial analysis and group analysis, if applicable
   - Status of and responsibilities for the financial examinations

3. The department should notify the lead state of the insurance holding company group of receipt of a primary application for redomestication and obtain a copy of the most recent Group Profile Summary (GPS), if applicable.

d~~e~~. Scope and Performance of Procedures for Form A Filings

Standard: The department should have documented procedures for the review of Form A filings to provide for consistency in the review process and to ensure that appropriate procedures are performed on all Form A filing reviews. The use of the Company Licensing Best Practices Handbook and/or Financial Analysis Handbook is considered acceptable.

Results-Oriented Guidelines:

1. The review process should ~~be designed to~~ adequately assess the Form A filings and accompanying information and ~~to~~ effectively allow the department to reach appropriate conclusions regarding whether the Form A filings are approved or denied.

Process-Oriented Guidelines:

1. The department should~~'s~~ review and document its assessment of each of ~~of Form A filings should include~~ the following:
   - Business and strategic plans of the insurer.
   - Identity and background of the applicant and individuals associated with the applicant including use of biographical affidavits to assess the quality and expertise of the following:
     - Ultimate controlling person
     - Proposed officers and directors (as listed on Jurat Page of most recent or upcoming financial statement)
     - Other owners of 10% or more of voting securities
   - The source, nature and amount of the consideration used or to be used in effecting the merger or other acquisition of control.

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- Fully audited financial information regarding the earnings and financial condition of the acquiring parties for the preceding five years. If fully audited financial information is not available, substantially similar information such as compiled financial statements or tax returns, as deemed acceptable to the commissioner, may be reviewed in lieu of fully audited financial information.
- Unaudited financial information regarding the earnings and financial condition of the acquiring parties as of a date not earlier than 90 days prior to the filing of ~~each statement~~the Form A.

2. The department should ~~utilize and update~~review the Form A Database for prior filings made by the Form A applicant and the ultimate outcome of such filing(s).

3. Pertinent and relevant information from the Form A filing should be manually entered into the Form A Database within 10 business days of receipt of the Form A.

4. Any changes to the status of the filing or other data elements should be entered into the Form A Database within 10 business days.

~~4.~~5.If the progress of a filing stalls, the Form A database should be updated at a minimum every six months to confirm the status of the filing and document the reason the filing has stalled.

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Date: 10/28//19

State Implementation Reporting of NAIC-Adopted Model Laws and Regulations

Executive (EX) Committee

- Adoption of the new ***Insurance Data Security Model Law*** **(#668)**—This model was adopted by the Executive (EX) Committee and Plenary at the 2017 Fall National Meeting. Eight states have enacted this model.

Life Insurance and Annuities (A) Committee

- Amendments to the ***Standard Nonforfeiture Law for Individual Deferred Annuities*** **(#805)**—These revisions were adopted by the Executive (EX) Committee and Plenary at the 2017 Summer National Meeting. One state has enacted these revisions to the model.

Health Insurance and Managed Care (B) Committee

- Amendments to the ***Health Insurance Reserves Model Regulation*** **(#10) (Cancer Expense Table)—**These revisions were adopted by the Executive (EX) Committee and Plenary at the 2017 Spring National Meeting. Two states have enacted these revisions to the model.

- Amendments to the ***Health Carrier Prescription Drug Benefit Management Model Act*** **(#22)**—These revisions were adopted by the Executive (EX) Committee and Plenary at the 2018 Spring National Meeting. NAIC staff are not aware of any state activity regarding this model.

- Amendments to the ***Accident and Sickness Insurance Minimum Standards Model Act*** **(#170)**—These revisions were adopted by the Executive (EX) Committee and Plenary at the 2019 Spring National Meeting. NAIC staff are not aware of any state activity regarding this model.

- Adoption of the ***Limited Long-Term Care Insurance Model Act*** **(#642)**—This model was adopted by the Executive (EX) Committee and Plenary at the 2018 Fall National Meeting. NAIC staff are not aware of any state activity regarding this model.

- Adoption of the ***Limited Long-Term Care Insurance Model Regulation*** **(#643)**—This model was adopted by the Executive (EX) Committee and Plenary at the 2018 Fall National Meeting. NAIC staff are not aware of any state activity regarding this model.

Property and Casualty Insurance (C) Committee

- Adoption of the ***Travel Insurance Model Act*** (#632)—This model was adopted by the Executive (EX) Committee and Plenary at the 2018 Fall National Meeting. Six states have enacted this model.

Market Regulation and Consumer Affairs (D) Committee

- Amendments to the ***Privacy of Consumer Financial and Health Information Regulation*** **(#672)**—These revisions were adopted by the Executive (EX) Committee and Plenary at the 2017 Spring National Meeting. Eleven states have enacted these revisions to the model.

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Financial Condition (E) Committee

- Amendments to the ***Credit for Reinsurance Model Law*** **(#785)**—These revisions were adopted by the Executive (EX) Committee and Plenary during the June 26, 2019 conference call. NAIC staff are not aware of any state activity regarding this model.

- Amendments to the ***Credit for Reinsurance Model Regulation*** **(#786)**—These revisions were adopted by the Executive (EX) Committee and Plenary during its June 26, 2019 conference call. NAIC staff are not aware of any state activity regarding this model.

- Amendments to the ***Term and Universal Life Insurance Reserve Financing Model Regulation*** **(#787)**—These revisions were adopted by the Executive (EX) Committee and Plenary at the 2016 Fall National Meeting. Four states have enacted this model.

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