EXAMINATION OVERSIGHT (E) TASK FORCE

Examination Oversight (E) Task Force Dec. 8, 2019, Minutes
Examination Oversight (E) Task Force Sept. 13, 2019, Minutes (Attachment One)
Financial Analysis Solvency Tools (E) Working Group Sept. 4, 2019, Minutes (Attachment Two)
   Referral from the Group Solvency Issues (E) Working Group Regarding Guidance in the NAIC Financial Analysis Handbook Relating to Analysis Documentation Standards for Insurers that are Part of a Large Insurance Group (Attachment Two-B)
   Financial Analysis Research & Development (E) Working Group Exposure Draft to Change Life IRIS Ratios No. 4, 10 and 12 (Attachment Two-C)
IT Examination (E) Working Group Sept. 26, 2019, Minutes (Attachment Four)
   Revisions to Guidance in the NAIC Financial Condition Examiners Handbook; Section III, General Examination Considerations, and Exhibit C, IT Review Standards Summary Memorandum (Attachment Four-A)
   Revisions to Guidance in the Financial Condition Examiners Handbook Related to Salary Range Guidelines and C-Level Interviews (Attachment Five-A)
   Revisions to Guidance in the Financial Condition Examiners Handbook Related to Troubled Insurance Companies, Exhibit V – Overarching Prospective Risk Assessment, and Exhibit AA – Summary Review Memorandum (Attachment Five-B)
   Revisions to Guidance in the Financial Condition Examiners Handbook Related to Management Letters (Attachment Six)
The Examination Oversight (E) Task Force met in Austin, TX, Dec. 8, 2019. The following Task Force members participated: Jillian Froment, Chair, represented by Dwight Radel (OH); Allen W. Kerr, Vice Chair, represented by Mel Anderson (AR); Lori K. Wing-Heier represented by David Phifer (AK); Jim L. Ridling represented by Sheila Travis (AL); Michael Conway represented by Rolf Kaumann (CO); Andrew N. Mais represented by Kathy Belfi and William Arfanis (CT); Stephen C. Taylor represented by N. Kevin Brown (DC); Trinidad Navarro represented by Ryllynn Brown (DE); Colin M. Hayashida represented by Andrew Kurata (HI); Doug Ommen represented by Carrie Mears (IA); Dean L. Cameron represented by Nathan Faragher (ID); Stephen W. Robertson represented by Roy Eft (IN); Vicki Schmidt represented by Tish Becker (KS); Nancy G. Atkins represented by Sandy Batts (KY); James J. Donelon represented by Stewart Guerin (LA); Gary Anderson represented by James A. McCarthy (MA); Anita G. Fox represented by Judy Weaver (MI); Steve Kelley represented by Kathleen Orth (MN); Chlora Lindley-Myers represented by John Rehagen and Shannon Schmoege (MO); Jon Godfread represented by Matt Fischer (ND); Bruce R. Ramge represented by Justin Schrader and Lindsay Crawford (NE); Marlene Caride represented by Diana Sherman (NJ); John G. Franchini represented by Lea Geckler (NM); Glen Mulready represented by Eli Snowbarger (OK); Larry Deiter represented by Johanna Nickelson (SD); Kent Sullivan represented by Ignatius Wheeler and Shawn Frederick (TX); Todd E. Kiser represented by Jake Garn (UT); Scott A. White represented by Doug Stolte (VA); Tregenza A. Roach represented by Glendina Matthew (VI); Mike Kreidler represented by Patrick McNaughton (WA); Mark Afable represented by Amy Malm (WI); and Jeff Rude represented by Linda Johnson (WY).

1. **Adopted its Sept. 13 and Summer National Meeting Minutes**

Ms. Weaver made a motion, seconded by Ms. Malm, to adopt the Task Force’s Sept. 13 (Attachment One) and Aug. 4 (see *NAIC Proceedings – Summer 2019, Examination Oversight (E) Task Force, Attachment One*) minutes. The motion passed unanimously.

2. **Adopted the Reports of its Working Groups**

   a. **Electronic Workpaper (E) Working Group**

   The Electronic Workpaper (E) Working Group met Dec. 3 in regulator-to-regulator session, pursuant to paragraph 4 (internal or administrative matters of the NAIC or any NAIC member) of the NAIC Policy Statement on Open Meetings, to continue discussions in evaluating replacement options for TeamMate AM, which will be reaching its end of life in 2023.

   b. **Financial Analysis Solvency Tools (E) Working Group**

   The Financial Analysis Solvency Tools (E) Working Group met Sept. 4 (Attachment Two) to discuss changes to the *Financial Analysis Handbook* (Handbook) and Insurance Regulatory Information System (IRIS) for 2019 annual statement filings. The following proposals were adopted by e-vote on Oct. 15 (Attachment Three):

   1. Combined two quantitative procedures under property/casualty (P/C) reserving, where the materiality procedure and the related quantitative benchmark procedure were combined under one procedure.
   2. Exposed enhanced regulatory guidance to the Handbook related to parental guarantees and troubled insurance companies that resulted from referrals from the Financial Analysis (E) Working Group.
   3. Adopted Handbook guidance on salary compensation that was drafted by the Risk-Focused Surveillance (E) Working Group and exposed at the 2018 Fall National Meeting.
   4. Adopted previously exposed guidance updates to the Handbook related to intercompany pooling, which was referred by the Group Solvency Issues (E) Working Group.
   5. Adopted previously exposed changes to the Life IRIS for 2020 annual statement filings due to blank changes.

At the close of the open meeting, the Working Group adjourned into regulator-to-regulator session, pursuant to paragraph 3 (specific companies, entities or individuals) of the NAIC Policy Statement on Open Meetings.
c. Financial Examiners Coordination (E) Working Group

The Financial Examiners Coordination (E) Working Group met Aug. 5 in regulator-to-regulator session, pursuant to paragraph 3 (specific companies, entities or individuals) of the NAIC Policy Statement on Open Meetings, to receive reports on exam coordination efforts from selected states.

d. IT Examination (E) Working Group

Mr. McNaughton said the IT Examination (E) Working Group met Sept. 26 (Attachment Four) to adopt revisions on the following topics:

1. Information technology (IT) review conclusions – Revisions are intended to clarify the scope of the IT review and the way examiners should respond to IT review findings.
2. Use of third-party work – Revisions are intended to clarify the ways that third-party work can be evaluated and used during an exam’s IT review.
3. Cybersecurity self-assessment tools – Revisions allow state insurance regulators to incorporate the results of a company’s completed self-assessment. Additionally, a drafting group developed a mapping between IT exam guidance and the cybersecurity self-assessment tool developed by the Financial Services Sector Coordinating Council (FSSCC) to facilitate state insurance regulator use of the information contained within the tool.

Mr. Eft made a motion, seconded by Mr. Wheeler, to adopt the Task Force’s reports from the Electronic Workpaper (E) Working Group, the Financial Analysis Solvency Tools (E) Working Group, the Financial Examiners Coordination (E) Working Group, and the IT Examination (E) Working Group.

e. Financial Examiners Handbook (E) Technical Group

Mr. Schrader said the Financial Examiners Handbook (E) Technical Group met Nov. 14 and Sept. 12 to adopt revisions on the following topics:

1. Troubled Companies – Revisions incorporate insights from the Troubled Company Handbook on the following topics: priority ratings guidance, communication expectations for companies that are troubled or potentially troubled, and pre-receivership considerations.
2. Management Letters – Revisions clarify which level of the management a letter should be addressed to and the level of information that should be included therein.
3. Exhibit V (Prospective Risk Assessment) – Revisions encourage enhanced testing of overarching prospective risks and better facilitate the communication of examination results with the financial analysts.
4. Exhibit AA (Summary Review Memorandum) – Revisions add guidance for determining the level of concern and overall trend for a particular risk component.
5. C-level Interviews – Revisions address the order in which C-level interviews should be conducted and provide a new interview template for interviewing a chief marketing officer (CMO).
6. Regulator Compensation – Revisions include a description of commonly held roles and responsibilities for commonly held regulatory positions and suggest salary ranges for examiners and analysts based on the results of a state insurance regulator compensation study.

Before the Task Force meeting, Joseph Zolecki (Blue Cross Blue Shield Association—BCBSA) submitted a comment on behalf of interested parties, suggesting an amendment to the management letter revisions, which Susan Bernard (CA), chair of the Technical Group, accepted as a friendly amendment. The revisions would clarify that the judgements made by state insurance regulators regarding management letters would be based on the new guidance that the Technical Group agreed to add on its conference calls. Ms. Weaver and Ms. Belfi asked about the intent of the revisions. Mr. Zolecki they were to clearly link the discretion that the state insurance regulators have to the new revisions added, which detail some of the factors state insurance regulators may consider in issuing management letters. Mr. Schrader and Mr. Romero commented that the new revisions would likely not materially affect the issuance of management letters. Mr. Tom Finnell (America’s Health Insurance Plans—AHIP) offered an updated amendment, which would replace the use of the words “based on” with “considering.”

Ms. Belfi made a motion, seconded by Ms. Weaver, to adopt the Financial Examiners Technical Group’s report as amended during the Task Force meeting (Attachment Five and Attachment Six).
3. **Heard an Update on LIBOR**

The Task Force received an update from Michele Lee Wong (NAIC) that provided an update to state insurance regulators, noting that the use of the London Inter-bank Offered Rate (LIBOR) as a reference rate within U.S. financial markets would be changing soon. The NAIC’s Capital Markets Bureau (CMB) would be providing a further state insurance regulator-only update to clarify the implications to U.S. state insurance regulators.

4. **Heard an Update on Jumpstart Reports**

The Task Force received an update from Mr. Romero regarding state insurance regulator-only work that had taken place to update the NAIC’s Jumpstart reports. That work was completed at the end of 2019, and Mr. Romero noted that further state insurance regulator-only communication would be sent with information on the nature of the changes made.

Having no further business, the Examination Oversight (E) Task Force adjourned into regulator-to-regulator session, pursuant to paragraph 3 (specific companies, entities or individuals) of the NAIC Policy Statement on Open Meetings, to receive reports on exams open past 22 months.
The Examination Oversight (E) Task Force conducted an e-vote that concluded Sept. 13, 2019. The following Task Force members participated: Jillian Froment, Chair, represented by Dwight Radel (OH); Allen W. Kerr, Vice-Chair, represented by Mel Anderson (AR); Jim. L. Ridling represented by Richard Ford (AL); Ricardo Lara represented by Susan Bernard (CA); Michael Conway represented by Rolf Kaumann (CO); Andrew N. Mais represented by William Arfanis (CT); Trinidad Navarro represented by Rylynn Brown (DE); Colin M. Hayashida represented by Tian Xiao (HI); Doug Ommen represented by Jim Armstrong (IA); Stephen W. Robertson represented by Roy Eft (IN); Nancy G. Atkins represented by Sandra Batts (KY); Anita G. Fox represented by Judy A. Weaver (MI); Steve Kelley represented by Kathleen Orth (MN); Chlora Lindley-Myers represented by Shannon Schmoeger (MO); Jon Godfread represented by Matt Fischer (ND); Bruce R. Ramge represented by Lindsay Crawford (NE); John Elias represented by Doug Bartlett (NH); Marlene Caride represented by Steve Kerner (NJ); Glen Mulready represented by Joel Sander (OK); Deiter represented by Johanna Nickelson (SD); Kent Sullivan represented by Ignatius Wheeler (TX); Tregenza A. Roach represented by Gwendolyn Brady (USVI); Todd E. Kiser represented by Jacob W. Garn (UT); Mike Kreidler represented by Patrick H. McNaughton (WA); Mark V. Afable represented by Amy Malm (WI); and Jeffrey Rude represented by Linda Johnson (WY).

1. **Adopted its 2020 Proposed Charges**

The Task Force conducted an e-vote to consider adoption of an amendment to its 2019 charges *(see NAIC Proceedings – Fall 2019, Financial Condition (E) Committee, Attachment One-A).* New in 2020, the groups reporting to the Task Force will have charges updated as follows:

- The Electronic Workpaper (E) Working Group was asked to ensure its review of regulator needs includes consideration of both hosting and software needs and considers needs of the broader regulator community as well.
- Financial Analysis Solvency Tools (E) Working Group and the Financial Examiners Handbook (E) Technical Group had a charge related to their principle-based reserving (PBR) work removed. A broad charge asking that the groups work with the Life Actuarial (A) Task Force on PBR remains.

The motion passed unanimously.

Having no further business, the Examination Oversight (E) Task Force adjourned.
The Financial Analysis Solvency Tools (E) Working Group of the Examination Oversight (E) Task Force met via conference call Sept. 4, 2019. The following Working Group members participated: Judy Weaver, Chair (MI); Patricia Gosselin, Vice Chair represented by Douglas Bartlett (NH); Sheila Travis (AL); Scott Persten and Kurt Regner (AZ); Emma Hirschhorn (CA); Kathy Belfi and Lynn Reed (CT); N. Kevin Brown (DC); Eric Moser (IL); Roy Eft (IN); James Matheson (NY); Dwight Radel and Tim Biler (OH); Ryan Keeling (OR); Kimberly Rankin (PA); Jack Broccoli (RI); Amy Garcia (TX); and Kristin Forsberg (WI).


Ms. Weaver said an NAIC staff proposal was received to expose revisions to certain benchmarks and guidance in the Financial Analysis Handbook. She called on NAIC staff to summarize the proposed revisions.

Bree Wilson (NAIC) summarized a proposal to eliminate two questions from the annual property/casualty (P/C) reserving repository because of the lack of a materiality threshold and because the subsequent questions address both the metric and materiality threshold. She said eliminating these questions prevents the repositories from flagging the same exposure multiple times.

Ms. Wilson said other proposed revisions resulted from NAIC staff’s review of benchmarks across all analysis tools and that the proposed revisions are to sync-up the benchmarks in certain Financial Analysis Handbook procedures where differences were noted.

Ms. Wilson also summarized the proposed revisions to the P/C Statement of Actuarial Opinion Worksheet to align with changes in the current instructions.

Hearing no objections, Ms. Weaver said the proposals would be exposed for a 30-day public comment period ending Oct. 4.


Ms. Weaver said the Financial Analysis (E) Working Group sent two referrals to add enhanced regulatory guidance to the Financial Analysis Handbook related to parental guarantees and troubled insurance companies for the Working Group’s consideration.

Regarding parental guarantees, Ms. Weaver said that referral stems from the Financial Analysis (E) Working Group’s observation of situations where such agreements were not honored or fulfilled.

Ms. Weaver said the troubled insurance company referral was to consider adding new guidance in the Financial Analysis Handbook on communication expectations of troubled or potentially troubled insurers and pre-receivership considerations. She said this proposal resulted from recent revisions made to the Troubled Insurance Company Handbook.

Ms. Weaver called on NAIC staff to summarize the proposed updates to the Financial Analysis Handbook related to these referrals.

Rodney Good (NAIC) summarized the additional guidance in the Financial Analysis Handbook related to parental guarantees and capital maintenance agreements. He said that NAIC staff propose the additional guidance to be added to the analyst reference guide for strategic risk. The added guidance outlines certain considerations for the analyst in assessing current and prospective risks related to such agreements. For example, he said that in addition to reviewing and understanding the terms of the agreement, the guidance includes: 1) assessing the financial background of the entity providing the commitment; 2) obtaining additional information from the insurer, such as contingency plans if the agreement is not honored; and 3) for the
analyst to review the holding company analysis for additional insight into the parent company or ultimate controlling person, specifically the financial condition and in determining if there are liquidity concerns.

Regarding the troubled insurance company referral, Mr. Good summarized NAIC staff’s proposal to include the additional guidance under the Department Organization and Communication section of the Financial Analysis Handbook. Mr. Good said that this consists of a new section for Considerations for Troubled Insurance Companies. He said that, the associated guidance is a condensed version of what is included in the Troubled Insurance Company Handbook, which is a regulator-only resource. The proposed guidance in the Financial Analysis Handbook includes communication of troubled or potentially troubled companies within the department and with other states and/or other parties, as needed.

Hearing no objections, Ms. Weaver said the enhanced regulatory guidance to the Financial Analysis Handbook would be exposed for a 30-day public comment period ending Oct. 4.

3. **Adopted a Referral from the Risk-Focused Surveillance (E) Working Group**

Ms. Weaver said the third agenda item is to consider adoption of salary compensation guidance drafted by the Risk-Focused Surveillance (E) Working Group in the 2020 Financial Analysis Handbook. She called on NAIC staff to summarize the referral and updates to the handbook.

Mr. Good said the salary compensation guidance was drafted by the Risk-Focused Surveillance (E) Working Group and exposed at the 2018 Fall National Meeting for a 45-day comment period ending Jan. 18, 2019. No comments were received. As such, the guidance was referred to Financial Analysis Solvency Tools (E) Working Group and the Financial Examiners Handbook (E) Technical Group for consideration of adoption. The proposed guidance in the Financial Analysis Handbook reflects the final draft and is ready for consideration of adoption.

Ms. Rankin made a motion, seconded by Mr. Regner, to adopt the guidance in the 2020 Financial Analysis Handbook. The motion passed unanimously (Attachment Two-A).

4. **Adopted a Referral from the Group Solvency Issues (E) Working Group**

Ms. Weaver said that no comments were received on the previously exposed updates to the 2020 Financial Analysis Handbook related to analysis documentation standards for insurers that are part of a large insurance group, which resulted from a referral received from the Group Solvency Issues (E) Working Group. She called on NAIC staff to provide a brief overview of the referral.

Ralph Villegas (NAIC) said that these referrals were jointly exposed in June for a public comment period ending July 12. He said there was one comment letter received from Wisconsin to address how to efficiently document analysis of pooled insurance groups, as well as information on the insurance group when the ultimate controlling person of the group is an insurance entity, and additional information that would be expected from the non-lead state.


5. **Adopted its July 25 Minutes**

Ms. Weaver said the Working Group met on July 25 to expose revisions to the life Insurance Regulatory Information System (IRIS) Ratio 4, Adequacy of Investment Income; Ratio 10, Change in Product Mix; and Ratio 12, Change in Reserving for a 30-day public comment period ending Aug. 26.

Mr. Regner made a motion, seconded by Ms. Garcia, to adopt the Working Group’s July 25 minutes (See NAIC Proceedings – 2019 Summer, Examination Oversight (E) Task Force, Attachment One). The motion passed unanimously.

6. **Adopted Revisions to the Life IRIS**

Ms. Weaver said the next agenda item is to hear comments received from the exposed IRIS revisions and consider adoption of those changes. She called on NAIC staff to summarize the comments and revisions.
Kelly Hill (NAIC) said comments were received from the American Council of Life Insurers (ACLI), with the first two comments relating to the mortality risk column that was added by the Blanks (E) Working Group to the analysis by line of business table. She said that NAIC staff agreed that these elements should be included; therefore, the elements were added to IRIS (2A). Ms. Hill said the third comment was to include group credit life in the credit life element for Ratio 10. She agreed that these elements should be considered and revised the proposed changes to IRIS accordingly.

Mr. Regner made a motion, seconded by Mr. Broccoli, to adopt the IRIS revisions (Attachment Two-C). The motion passed unanimously.

Having no further business, the Financial Analysis Solvency Tools (E) Working Group adjourned.
Proposed Additions to Financial Analysis Handbook

It is proposed that a new section of guidance be adopted into the NAIC’s Financial Analysis Handbook to contain compensation guidance and recommended salary ranges for financial analysts. The guidance is proposed as follows:

I. Introduction
   A. Department Organization and Communication

Financial Analyst Salary Guidelines
The compensation guidelines in this section of the Handbook were developed in recognition of the importance of compensation particularly as it affects an Insurance Department’s ability to hire and retain well-qualified employees. The guidelines were developed based on surveys of analyst pay across Insurance Departments, as well as external comparisons to other similar professions, including other financial regulators, internal auditors and external auditors. In using the information below, the following are brief descriptions of the associated positions listed:

Financial Analyst
Financial Analysts are responsible for conducting Risk-Focused Financial Analysis on assigned insurers under the supervision of an Analyst Supervisor. The Financial Analyst reviews annual and quarterly insurer financial statements and all related supplemental regulatory filings to assess and monitor the current financial condition and prospective financial solvency of insurance companies.

Senior Financial Analyst
Senior Financial Analysts are responsible for conducting Risk-Focused Financial Analysis on assigned insurers under the supervision of the Supervising Analyst. The Senior Financial Analyst reviews annual and quarterly insurer financial statements and all related supplemental regulatory filings to assess and monitor the current financial condition and prospective financial solvency of more complex and higher priority insurance companies. Senior Financial Analysts may also be asked to provide guidance, support and training to Financial Analysts.

Supervising & Assistant Chief Analyst
A Supervising or Assistant Chief Analyst is responsible for supervising the Financial Analysts and Senior Financial Analysts conducting Risk-Focused Financial Analysis on assigned insurers. This position provides input on technical matters, acts as a reviewer of the work performed by the Financial Analysts and Senior Financial Analysts and ensures that analyst work is an appropriate execution of the Risk-Focused Analysis approach.

Chief Analyst
This position is responsible for overall staff performance & development and should serve as the department’s main point of contact for analysis and ongoing monitoring of regulated entities. This position should oversee company assignments and priority ratings. This position should work under the general direction of a Commissioner or Deputy Commissioner and should oversee a consistent Risk-Focused Financial Analysis process across the Department.
Use of Compensation Salary Tables:
The compensation salary tables included below generally require certain adjustments before being applied by a State or Jurisdiction in setting analyst compensation. Factors to consider in setting analyst compensation include:

- Specific job responsibilities and expectations
- Location or market based adjustments
- Complexity of industry
- Specialization requirements (e.g. Reinsurance/Investment/IT Specialist)
- Travel expectations (including consideration of amount of travel and in consideration of work from home or other similar arrangements)
- Retirement and other benefits (not included in table)

<table>
<thead>
<tr>
<th>Position</th>
<th>Low end</th>
<th>High end</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial Analyst</td>
<td>$46,000</td>
<td>$75,000</td>
</tr>
<tr>
<td>Senior Financial Analyst</td>
<td>$57,000</td>
<td>$90,000</td>
</tr>
<tr>
<td>Supervisor/Assistant Chief Analyst</td>
<td>$80,000</td>
<td>$130,000</td>
</tr>
<tr>
<td>Chief Analyst</td>
<td>$92,000</td>
<td>$150,000</td>
</tr>
</tbody>
</table>

Note: The data above is based on a national average and is not appropriate to be applied to all locations without consideration of market and cost of living variances.

Discussion of Analysis for Intercompany Pooling Arrangements

Intercompany pooling arrangements involve the establishment of a quota share reinsurance agreement under which pooled business is ceded to a lead entity and then retroceded back to pool participants in accordance with stipulated shares (if any). This generally results in pool participants sharing exposure to the various insurance risks ceded into the pool. Because of this structure, financial analysts may be able to gain efficiencies by conducting and documenting the analysis of insurance risks associated with the pooled business on a combined basis and then leveraging the results of that work to complete legal entity analysis. For example, in situations where the majority of the group’s writings are ceded into the intercompany pool and there are few unique legal entity risks, the analyst may choose to create and maintain a combined risk assessment and/or IPS for all of the legal entities participating in the pool (if domiciled in the same state). In other situations, it may be more appropriate to maintain separate risk assessment worksheets and/or IPSs for each legal entity, but to reference work completed in the pool lead’s documentation or include substantially similar information in each legal entity’s risk assessment worksheet and IPS.

While insurers participating in intercompany pooling arrangements often share exposure to pooled insurance risks, differences in the overall risk exposure of participants may arise due to a number of factors including, but not limited to, the following:

- Surplus/RBC levels
- Balance sheet composition
- Pool participation percentages
- The timing of pool participation
- Premiums not ceded to the pool
- Reinsurance arrangements outside of the pool (e.g., facultative placement prior to cessions to the pool lead).
- Current or legacy risks (e.g., asbestos exposure) disclosed within the financial statement

Regardless of the method utilized to assess and document the analysis of the pool, the financial analyst should ensure that all significant, unique exposures of each pool participant are separately assessed and addressed within analysis documentation.

If pool participants are domiciled in various states, communication and coordination across states is strongly encouraged to achieve efficiencies in analysis. For example, it might be appropriate for the domestic state of the pool lead to complete the analysis of the pooled insurance risks early in the analysis cycle to enable other states with domestic in the pool to leverage the completed work.

In situations where an insurer cedes business to an intercompany pool, but does not participate in retrocession, the analysis of the pooled business should be obtained/reviewed to evaluate reinsurance credit risk. If the pool is troubled or potentially troubled, this may require more in-depth analysis to evaluate the potential impact of claims associated with the insurer’s direct writings not being covered by the pool.
VI.C. Group-Wide Supervision – Insurance Holding Company System Analysis Guidance (Lead State)

Lead State Holding Company Analysis – Process and Procedures

In completing the process of holding company analysis and developing a GPS, analysts are encouraged to customize the work performed and documented at a level commensurate with the nature and complexity of the group. Analysts may elect to limit the amount of analysis and supporting documentation performed outside of the GPS and/or eliminate certain sections of the GPS to promote efficiencies in conducting analysis work. Conversely, analysts working on very complex groups may elect to perform additional analysis (including those listed in the Additional Procedures on Key Risk Areas – Insurance Holding Company System) as well as provide additional documentation within the GPS and/or in supporting analysis workpapers. Keep in mind, the GPS should provide sufficient information about the group and its risks to enable other state, federal and international regulators to understand the group risks that may be relevant to their regulated legal entities.

If the domestic insurers in a holding company system consist of only run-off companies, the domestic regulator, at its discretion, should determine the value, if any of performing a holding company system analysis. If it is determined that a holding company system analysis would be of no added value, this determination should be documented.

If the ultimate controlling person of the holding company is an insurance company, the analyst may consider preparing one document that includes elements of the IPS and the GPS, in order to promote efficiency in the overall analysis. For example, in addition to the standard elements of the IPS, such a hybrid document may also include sections such as corporate governance, ERM/ORSA, non-insurance affiliates/subsidiaries, etc.

As the lead state, the department should coordinate the ongoing surveillance of companies within the group with input from other affected states (with the understanding that the domestic state has the ultimate authority over the regulation of the domestic insurer under its jurisdiction). The documentation contained in the GPS is considered to be part of the workpapers, and represents proprietary, confidential information that is not intended to be distributed to individuals other than state regulators.

Confidentiality of Information: Financial analysts are reminded that information collected from the group, generally under the authority of their holding company statutes or their more specific statutes dealing with the ORSA Summary Report may be confidential by law. Accordingly, before sharing statutorily confidential information with other jurisdictions, regulators will need to review their own statutory authority to do so, which generally requires that the receiving jurisdiction is able to maintain also the confidentiality of such information.

UCP is an Insurer: If the ultimate controlling person (UCP) of the holding company is a U.S. domiciled insurance company with a cocode, the analyst may consider preparing one document that includes all the elements of the IPS and the GPS, in order to promote efficiency in the overall analysis. For example, in addition to the standard elements of the IPS, the document may also include sections such as corporate governance, ERM/ORSA, non-insurance affiliates/subsidiaries, etc. In addition, depending on the nature and extent of risks, the analyst should consider whether it is more appropriate to assess and document certain risk exposures from a group or legal entity perspective (or both) in the IPS/GPS. In all cases, the analyst is expected to document and complete both the legal entity and holding company analysis work in accordance with timeliness expectations. Therefore, the analyst and supervisor should demonstrate that the combined IPS/GPS is updated for both the results of legal entity analysis and holding company analysis through separate signoffs at different dates, as necessary.
Special Notes: The following procedures are intended to be performed by non-lead domestic states to develop and document an analysis of the impact of the holding company system on the domestic insurer. Form procedures do not supersede state regulation, but are merely additional guidance an analyst may consider useful.

Name of Holding Company System ____________________
Name of Lead State ____________________

Compliance Assessment - Form B (and C)

1. Review the registration statement to determine if it was filed in accordance with the state’s Insurance Holding Company System Regulatory Act¹ and if it included the required current information. The information provided should include a description of the transaction or agreement, including, at least, the nature and purpose of the transaction, the nature and amounts of any payments or transfers of assets between the parties, the identity of all parties to the transaction, and the relationship of the affiliated parties to the registrant. (LG)

2. Did each domiciled registered insurers properly report dividends and other distributions to shareholders in accordance with the following Model #440 requirements? (LG)

3. If dividends and other distributions to shareholders were considered extraordinary, did the transaction receive proper regulatory approval? (LG)

4. Did the insurer receive proper prior regulatory approval for any transaction, which occurred during the last calendar year involving the insurer and others in its holding company system that required such prior regulatory approval? (LG)

Assess the Impact of the Holding Company Group on the Domestic Insurer

Assessment of Group Profile Summary from the Lead State

5. Obtain a copy of the lead state’s Group Profile Summary (GPS).

6. Consider the GPS’s branded risk assessment in determining the impact of the holding company on the domestic insurer.

7. Review the conclusion and supervisory plan of the GPS. Did the lead state identify any holding company risks impacting the domestic insurers’ in the group and/or supervisory plans that impact your state’s domestic insurer?

8. Consider the nature of the domestic insurer(s)’ interdependence on the holding company group or affiliated entities for business operations or financial stability (e.g., employees, services provided, reinsurance and/or capital support in the near term). (OP, CR, ST)

¹ The list provided is based on the NAIC Insurance Holding Company System Regulatory Act (#440); however analysts should review the Form B compliance in relation to their own state’s requirements.
9. Consider the level of reputational risk that the holding company (as a group) poses to the domestic insurer(s). (RP)

10. Determine if income of the domestic insurer(s) is being used to service holding company debt or other corporate initiatives (e.g., acquisitions). (OP, ST)

**Assessment of Form B (and C)**

11. Based upon a review of the registration statement, were any significant and/or unusual items noted, such as, but not limited to, the following?

   a. Person(s) holding 10% or more of any class of voting security who also have a history of transacting business of any kind directly or indirectly with the insurer. (OP, ST)

   b. Biographical information about directors or officers, which may elevate concerns such as convictions of crimes. (OP, ST)

   c. Any litigation or administrative proceeding involving the ultimate controlling entity or any of its directors and officers, such as criminal prosecutions or proceedings which may have a material effect upon the solvency or capital structure of the ultimate holding company, such as bankruptcy, receivership, or other corporate reorganization. (LG)

   d. The absence of an affirmative statement that transactions entered into since the filing of the prior year’s annual registration statement are not part of a plan or series of like transactions to avoid statutory threshold amounts. (OP, ST)

**Assessment of Affiliated Risks on the Domestic Insurer**

12. Were any material deficiencies or risks noted during the annual review of the domestic insurer’s Notes to Financial Statements, Interrogatories, Schedule Y – Part 2, Holding Company, Forms B & C, or recent examination reports with respect to affiliated transactions? (CR, LQ, OP, ST)

   a. Management agreements

   b. Third-party administrative agreements

   c. Managing general agent agreements

   d. Investment management pools

   e. Reinsurance agreements and pools

   f. Consolidated tax sharing agreements

   g. Other

13. If any of the following forms have been filed with the domestic regulator since the last review, indicate if risks or concerns were noted in any of the reviews of these forms.

   a. Form A (Acquisition of Control or Merger)

   b. Form D (Prior Notice of a Transaction)

   c. Form E (Pre-Acquisition Notification) or Other Required Information

   d. Extraordinary Dividend/Distribution
V.A. Domestic and/or Non-Lead State Analysis – Holding Company Procedures (Non-Lead State)

Assessment of Form F - Enterprise Risk Statement

14. Obtain either the Form F from the lead state, if available, and/or the lead state’s analysis of the Form F if it addresses the impact of the holding company on each your state’s domestic insurer(s).

15. Based on the analyst’s review of Form F and/or the lead state’s analysis of the Form F, and any additional information related to enterprise risk available (e.g., Form B, other filings), document any material concerns regarding enterprise risk that could impact the financial condition of the domestic insurer.

16. Do any of the risks identified pose an immediate material risk to the insurer’s policyholder surplus or risk-based capital position, insurance operations (e.g., changes in writings, licensure, and organizational structure), balance sheet, leverage or liquidity?

Assessment of Own Risk and Solvency Assessment (ORSA), if applicable

17. Obtain the lead state’s analysis of the ORSA Summary Report (see section VI.F-Own Risk and Solvency Assessment Procedures).

18. Did the lead state document in its analysis any risks or concerns that in its opinion have an impact on the overall financial condition of the insurance holding company system? If so, do any of the risks or concerns identified pose a material risk to the domestic insurer?

Assessment of Corporate Governance Annual Disclosure (CGAD), if applicable

19. Obtain the lead state’s analysis of the CGAD and determine if it addresses corporate governance policies and practices of the group applicable to your state’s domestic insurer(s).

   a. If the CGAD analysis does not address corporate governance policies and practices of the group applicable to the non-lead states’ domestic insurer, request the CGAD from the insurer.

20. Based on the analyst’s review of the CGAD or the lead state’s analysis of the CGAD, and any additional available information related to corporate governance, document any material concerns regarding corporate governance impacting the domestic insurer.

21. Do any of the concerns identified pose an immediate material risk to the domestic insurer’s financial condition (e.g., operations, policyholder surplus or capital position)?

Communication & Follow-Up with the Lead State

- Notify the lead state of any additional material events or concerns applicable to the domestic insurer, or the group as a whole, that the lead state may not otherwise be aware of, and that should be considered in the evaluation of the overall financial condition of the holding company system.

- If any material risks or events were identified during your holding company analysis that were not discussed in the lead state’s holding company analysis, communicate those findings to the lead state.
V.A. Domestic and/or Non-Lead State Analysis – Holding Company Procedures (Non-Lead State)

Update the Insurer Profile Summary

Update the Insurer Profile Summary of the domestic insurer with the summary and conclusion of the impact of the holding company system on the domestic insurer based on the above analysis performed.

<table>
<thead>
<tr>
<th>Analyst:</th>
<th>Date:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Supervisor Review:</td>
<td>Date:</td>
</tr>
<tr>
<td>Supervisor Comments:</td>
<td>Date:</td>
</tr>
</tbody>
</table>
Non-Lead State Holding Company System Analysis Procedures

Refer to section VI.C. Group-Wide Supervision - Insurance Holding Company System Analysis Guidance (Lead State) for guidance on the Lead State’s holding company analysis procedures.

Procedures #5-17 assist the analyst in assessing the impact of the holding company system on the domestic insurer. This includes five primary segments of the analysis as follows.

- **#5-10** Assessment of the Group Profile Summary (GPS) from the Lead State: If the Lead State is not your state, the Lead State should provide a GPS to the non-lead states in the group by Oct. 31. Using the GPS consider the risks identified and assessed by the Lead State to determine any material impacts on the branded risks of the domestic insurer, the interdependence of the holding company and its affiliated entities, including the domestic insurer, dividend obligations of the domestic insurer to service holding company debt or fund other holding company initiatives, and the holding company’s reputation.

- **#11** Assessment of Form B (and C): Model #440 defines insurance holding companies and the related registration, disclosure, and approval requirements. Form B is the insurance holding company system annual registration statement. Model #440 requires every insurer, which is a member of an insurance holding company system, to register by filing a Form B within 15 days after it becomes subject to registration, and annually thereafter. Any non-domiciliary state may require any insurer that is authorized to do business in the state, which is a member of a holding company system, and which is not subject to registration in its state of domicile, to furnish a copy of the registration statement.

An insurance holding company system consists of two or more affiliated individuals, one or more of which is an insurer. An affiliate is an entity that directly or indirectly, through one or more intermediaries, controls, is controlled by, or is under common control with, another entity. Control is presumed to exist when an entity or person, directly or indirectly, owns, controls, holds with the power to vote, or holds proxies, representing 10 percent or more of the voting securities.

- **#12-13** Assessment of Affiliated Risks on the Domestic Insurer: Affiliated risks may exist due to interdependence of the holding company and its affiliated entities through affiliated transactions. Consider also the guidance included in the Operational Risk Analyst Reference Guide as well as guidance in this section regarding supplemental form filings for review of affiliated agreements.

- **#14-165** Assessment of Form F – Enterprise Risk Statement: The purpose of the Form F is to identify if there is any contagion risk within the group, and domestic states should not be discouraged from reviewing such information because ultimately they are required to relate the financial condition of the group to their domestic state. The Form F must be reviewed by the lead state but other domestic states are also expected to review it. To the extent the Lead State’s analysis of Form F assesses the impact of any contagion risk of the group on the non-lead state’s domestic insurer, that analysis may be leveraged by the non-lead state to reduce the analysis work of the non-lead state. If the Lead State’s analysis of Form F does not assess the impact of the group on the non-lead state’s domestic insurer, consider a review as noted in Procedures #15 and #16, or similar to the procedures in section VI.G. Group-Wide Supervision - Form F - Enterprise Risk Report Procedures for reviewing Form F.
• **#176-187** Assessment of Own Risk and Solvency Assessment (ORSA): If the Holding Company files an ORSA Summary Report, it is the responsibility of the Lead State to review and perform analysis of the report. At the completion of this review, the lead state should prepare a thorough summary of its review, which would include an initial assessment of each of the three sections. The lead state should also consider and include key information to share with other domestic states that are expected to place significant reliance on the lead state’s review. Non-lead states are not expected to perform an in-depth review of the ORSA, but instead rely on the review completed by the lead state. The non-lead state’s review of an ORSA should be performed only for the purpose of having a general understanding of the work performed by the lead state, and to understand the risks identified and monitored at the group-level so the non-lead state may better monitor and communicate to the lead state when its legal entity could affect the group. Any concerns or questions related to information in the ORSA or group risks should be directed to the lead state.

• **#19-21** Assessment of Corporate Governance Annual Disclosure (CGAD): Analysis of CGAD only applies where states have enacted such legislation as that in the Corporate Governance Annual Disclosure Model Act (#305) and Corporate Governance Annual Disclosure Model Regulation (#306). The purpose of the CGAD is to provide a summary of an insurer or insurance group’s corporate governance structure, policies and practices to permit the regulator to gain and maintain an understanding of the insurer’s corporate governance framework. The CGAD must be filed to the lead state if on a group basis or the domestic state if on a legal entity basis, but other domestic states are may request the filing. To the extent the Lead State’s analysis of a group CGAD assesses the impact of corporate governance practices and procedures of the group on the non-lead state’s domestic insurer, that analysis may be leveraged by the non-lead state to reduce the analysis work of the non-lead state. If the Lead State’s analysis of CGAD does not assess the impact of the group on the non-lead state’s domestic insurer, review the filing to identify and assess any material concerns and determine if any material immediate risks impact the domestic insurer’s financial condition.

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VI.D. Group-Wide Supervision – Corporate Governance Disclosure Procedures

Special Note: The following procedures do not supersede state regulation, but are merely additional guidance an analyst may consider useful.

The Corporate Governance Annual Disclosure Model Act (#305) and Corporate Governance Annual Disclosure Model Regulation (#306) provide a summary of an insurer or insurance group’s corporate governance structure, policies and practices to permit the Commissioner to gain and maintain an understanding of the insurer’s corporate governance framework. As of the date of this publication, most states had not adopted such legislation. The following procedures are applicable to only those states that have adopted such legislation.

All other states should instead consider completion of applicable questions within the Operational and Strategic risk repositories of this Handbook based upon the level of concern an analyst may have with management performance and the driving forces behind operations. The risk repositories may also be used by an analyst of a state that has obtained the disclosure for an insurer or insurance group subject to the aforementioned corporate governance disclosure. However, the analyst should avoid duplicate information requests.

Introduction

Model #305 and #306 requires an insurer, or an insurance group, to file a summary of an insurer or insurance group’s corporate governance structure, policies and practices with the commissioner by June 1 of each calendar year. Model #305 allows the information to be at the ultimate controlling parent level, an intermediate holding company level and/or the individual legal entity level, depending upon how the insurer or insurance group has structured its system of corporate governance. Because most corporate governance is driven at a controlling or intermediate holding company level, this guidance is contained within this section dealing with group supervision. Although by inclusion in this section, reviewing the corporate governance disclosure of a group is a responsibility of the lead state, the approach on this is different from that taken with the Own Risk Solvency and Analysis (ORSA). This is because it’s common for most groups to have different layers of governance that is important in achieving the objectives of the group. More specifically, most groups have some level of governance at the individual legal entity level. However, because it is common for legal entity governance to be a less significant aspect of the governance objectives, even those companies that incorporate governance at the individual legal entity level are likely to include materially less documentation on such, may instead summarize such processes and list those entities for which they exist.

Non-Lead State Reliance on the Lead State Analysis of Corporate Governance Annual Disclosure:

Because Model #305 allows requires the filing to be made with the lead state, however, non-lead domestic states may request the CGAD filing from the insurer. Because the filing may be made on a group basis or legal entity basis, it may contain group information that applies to all insurers within the group or it may contain information applicable to a specific legal entity. It may be necessary for the lead state to share the filing with another state that has adopted a substantially similar law including similar confidentiality requirements. Alternatively, or in addition, it may be necessary or acceptable for the lead state to share its work papers with another state, related to such filing, provided such information is shared in accordance with the confidentiality provisions of Model #305. This is because similar to other solvency regulation models, Model #305 contemplates both off-site and on-site examination of such information. The Lead State can share the analysis of the filing through NAIC tools (i.e., iSite+ Regulator File Sharing System) or other means deemed appropriate. Before a non-lead states requests the CGAD filing or conducts a full review of CGAD to determine its impact on their domestic insurers, non-lead domestic states should consider obtaining and reviewing the Lead State’s analysis of CGAD to reduce duplication of analysis efforts.
VI.D. Group-Wide Supervision – Corporate Governance Disclosure Procedures

To the extent the Lead State’s analysis of the Corporate Governance Annual Disclosure (CGAD) addresses policies and practices of the group applicable to the non-lead state’s domestic insurer, that analysis may be leveraged by the non-lead state to reduce the analysis work of the non-lead state. If the Lead State’s analysis of CGAD does not assess the impact on the non-lead state’s domestic insurer or the CGAD is on a legal entity basis, the non-lead domestic state should consider a review of CGAD. Analysis steps are included in the non-Lead State analysis procedures.

Procedures #1 - 2 assist the analyst in reviewing the Corporate Governance disclosure for completeness and help guide the analyst through each of the major items of information required by Model #306.

Procedures #3 - 5 assist the analyst in summarizing any concerns relative to the insurer or insurance group’s corporate governance and its impact.

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Form F-Enterprise Risk Report

The 2010 revisions to Model #440 and Insurance Holding Company System Model Regulation with Reporting Forms and Instructions (#450) introduced a new filing requirement for a Form F. The Form F requires the ultimate controlling person to identify the material risks within the insurance holding company system that could pose enterprise risk to the insurer. The Form F may be completed using information contained in the financial statement, annual report, proxy statement, statement filed with a governmental authority, or other documents if such information meets the disclosure requirements. Form F is focused on disclosing the enterprise risk associated with the entire insurance holding company system including non-regulated entities. The Form F is filed with the lead state commissioner of the insurance holding company system for every insurer subject to registration under Model #440. Adoption of the applicable Form F and related confidentiality provisions outlined in the 2010 revisions to Model #440 is required for a state to be designated the lead state for Form F filings. Lead states and other domestic states receiving and sharing the Form F must have in place confidentiality agreements as prescribed in #Model 440.

Non-Lead State Reliance on the Lead State Analysis of Form F:

Although by inclusion in this section, reviewing the group Form F report is a responsibility of the lead state, the approach on this is different from that taken with the ORSA. Generally speaking, a non-lead state should not review the ORSA with the same level of depth as the lead state. However, that same approach is not encouraged with respect to the Form F. The entire purpose of the Form F is to identify if there is any contagion risk within the group, and domestic states should not be discouraged from reviewing such information because ultimately they are required to relate the financial condition of the group to their domestic state. Most believe that the ORSA is much more detailed and less related to contagion as it is the group’s actual risk management processes used to mitigate risk.

The Form F must be reviewed by the lead state and significant findings incorporated into the GPS. However, other domestic states are also expected to review the Form F in order to assess the impact of the group on their domestic insurer. One exception for non-lead states should be noted. To the extent the Lead State’s analysis of Form F assesses the impact of any contagion risk of the group on the non-lead state’s domestic insurer, that analysis may be leveraged by the non-lead state to reduce the analysis work of the non-lead state. If the Lead State’s analysis of Form F does not assess the impact of the group on the non-lead state’s domestic insurer, the non-lead domestic state should review Form F. The Lead State can share the Form F and its analysis through NAIC tools (Form F Sharing Tool for the filings and the iSite+ Regulator File Sharing System for the analysis). Analysis steps are included in the non-Lead State analysis procedures with that in mind. To reduce duplication, domestic states should consider obtaining and reviewing the Lead State’s analysis of Form F before determining if a full review of the filing is necessary to determine its impact on their domestic insurers.

NAIC Enterprise Risk Report (Form F) Implementation Guide

In March 2018, the Group Solvency Issues (E) Working Group adopted the NAIC Enterprise Risk Report (Form F) Implementation Guide, which is located at:

https://www.naic.org/documents/committees_e_isftf_group_solvency_related_form_f_guide.pdf?97

As outlined in the Guide, it is intended to assist insurers and regulators in maximizing the usefulness of the Form F by proposing best practices for consideration in preparing and reviewing filings. Therefore, while the Guide does not constitute authoritative guidance for information to be included in a Form F filing, filers are requested to consider the best practices outlined within the Guide when preparing their Form F filing. By adhering to the best practices outlined within the Guide, registrants will be able to reduce the extent of regulator follow-up and correspondence necessary to utilize the information provided, which should lead to a more effective and efficient process. The regulators’ goal in developing this document was to provide some consistency and uniformity across states in reviewing and utilizing information obtained through the Form F. Therefore, it is recommended that states utilize the best practices outlined in the Guide to support their review and feedback process.

Procedures

Procedures #1 - 2 assist the analyst in reviewing the Form F filing for completeness and help guide the analyst through each of the major items of information required by Form F. The analyst should review Form F in conjunction with a review of Form B and should document any nondisclosure of information.

Procedures #3 - 7 assist the analyst in evaluating the risks described within Form F. The analyst should consider whether any enterprise risks not reported in Form F exist, and for all risks identified both within Form F and by the analyst, the analyst should review information available and document any concerns. The analyst should also evaluate whether the risks identified result in an impact to the insurers financial condition (e.g., surplus, RBC, insurance operations, or balance sheet, leverage and liquidity).
Financial Analysis Research & Development (E) Working Group

Exposure Draft to Change Life IRIS Ratios No. 4, 10, and 12 for a 30-day Public Comment Period

Public Comment Period Ends August 26, 2019

Updates made since July 25, 2019 call:

1. A YRT Mortality Risk Only Column was added to page 6.1 so the columns were adjusted for Attachment A-2 and A-3.
2. The Group Credit Life Column from page 6.2 was moved from 10.E to 10.D to more accurately match prior year.

Recommendation to change three IRIS ratios due to Blanks changes beginning with the 2019 annual filings.

- **Attachment A-1** – Life IRIS Ratio 4 (Adequacy of Investment Income) change recommendation
- **Attachment A-2** – Life IRIS Ratio 10 (Change in Product Mix) change recommendation
- **Attachment A-3** – Life IRIS Ratio 12 (Change in Reserving) change recommendation

The 2019 Fraternal IRIS report will no longer be available, due to the removal of the Fraternal blanks, beginning with the 2019 filings. Fraternal societies will file on the Life blank beginning in 2019.
Life IRIS Ratio No. 4 (Adequacy of Investment Income)

A. Net Investment Income
   - Page 4, Line 3, Column 1

B. Tabular Interest Involving Life or Disability Contingencies
   - Page 7.1, Line 4, Column 1 + Page 7.2, Line 4, Column 1 + Page 7.3, Line 4, Column 1 + Page 7.4, Line 4, Column 1

C. Tabular Fund Interest on Accident and Health Contracts
   - Page 14, Exhibit of Aggregate Reserve for Accident and Health Contracts, Line 18, Column 1

D. Investment Earnings Credited to Deposit-Type Contract Accounts
   - Page 15, Exhibit of Deposit-Type Contract Accounts, Line 3, Column 1

Result = \( \frac{A}{B+C+D} \times 100 \%

- If \( B+C+D \) is zero, result is 999.
- If insurer has no beginning or ending reserves per page 7 of the annual financial statement and item B is zero, no result is calculated (NR).
### Life IRIS Ratio No. 10 (Change in Product Mix)

<table>
<thead>
<tr>
<th>CURRENT YEAR AMOUNT</th>
<th>CY % OF TOTAL</th>
<th>PRIOR YEAR AMOUNT</th>
<th>PY % OF TOTAL</th>
<th>COL (2) LESS</th>
</tr>
</thead>
</table>

#### Premiums & Annuity Considerations

**Current Year Amount (Col 1)**
- A. Industrial Life, **Column 2**
- B. Ordinary Life Ins., **Column 3**
- C. Ind. Annuities, **Column 4**
- D. Credit Life, **Column 6**
- E. Group Life, **Column 7**
- F. Group Annuities, **Column 8**
- G. Group A&H, **Column 9**
- H. Credit A&H, **Column 10**
- I. Other A&H, **Column 11**
- J. Total

**Prior Year Amount (Col 2)**
- A. Industrial Life
- B. Ordinary Life Insurance
- C. Individual Annuities
- D. Credit Life
- E. Group Life
- F. Group Annuities
- G. Group A&H
- H. Credit A&H
- I. Other A&H

**Result** = \( \frac{K}{9} \) %

- If J for either current or prior year is zero or negative, no result is calculated (NR).
- Ratio is calculated as follows: First determine the percentage of premium from each product line for CY and PY. Next, determine the difference in the percentage of premium between the two years for each product line. Finally, the total of these differences, without regard to sign, is divided by the number of product lines to determine the change in the percentage of premium for the average product line.
## Life IRIS Ratio No. 12 (Change in Reserving)

<table>
<thead>
<tr>
<th>Category</th>
<th>Pages and Columns</th>
<th>CURRENT YEAR</th>
<th>PRIOR YEAR</th>
</tr>
</thead>
<tbody>
<tr>
<td>A. Increase in Agg. Reserves – Industrial Life</td>
<td>Page 6.1, Line 19, Column 2</td>
<td></td>
<td></td>
</tr>
<tr>
<td>B. Increase in Agg. Reserves – Ordinary Life Ins.</td>
<td>Page 6.1, Line 19, Column 3, 4, 5, 6, 7, 8, 9, 11, 12</td>
<td></td>
<td></td>
</tr>
<tr>
<td>C. Net Single Premiums – Industrial Life</td>
<td>Page 9, Line 10.4, Column 2</td>
<td></td>
<td></td>
</tr>
<tr>
<td>D. Net Renewal Premiums – Industrial Life</td>
<td>Page 9, Line 19.4, Column 2</td>
<td></td>
<td></td>
</tr>
<tr>
<td>F. Net Renewal Premiums – Ordinary Life Ins.</td>
<td>Page 9, Line 19.4, Column 3</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Result = \[ ((\text{CY} \ (A+B)) / (\text{C+D+E+F})) - (\text{PY} \ (A+B)) / (\text{C+D+E+F})) \] \times 100

- If (A+B) and (C+D+E+F) for current or prior year are both zero or negative, \((A+B) / (C+D+E+F) = 0\) for that year.
- If (A+B) is positive and (C+D+E+F) is zero or negative for current or prior year, \((A+B) / (C+D+E+F) = 100\%\) for that year.
- This ratio represents the number of percentage points of difference between the reserving ratio for current and prior years. For each of these years, the reserving ratio is equal to the aggregate increase in reserves for individual life insurance taken as a percentage of renewal and single premiums for individual life insurance.
Financial Analysis Solvency Tools (E) Working Group  
E-Vote  
October 15, 2019

The Financial Analysis Solvency Tools (E) Working Group of the Examination Oversight (E) Task Force conducted an e-vote that concluded Oct. 15, 2019. The following Working Group members participated: Patricia Gosselin, Vice Chair (NH); Kurt Regner (AZ); Emma Hirschhorn (CA); Lynn Reed (CT); N. Kevin Brown (DC); Eric Moser (IL); Debbie Doggett (MO); John Sirovetz (NJ); Tim Biler (OH); Ryan Keeling (OR); Kimberly Rankin (PA); Jack Broccoli (RI); Amy Garcia (TX); and Kristin Forsberg (WI).

1. **Adopted Exposed Revisions to the 2020 Financial Analysis Handbook**

The Working Group conducted an e-vote to consider adoption of exposed revisions (Attachment Three-A) to the 2020 Financial Analysis Handbook from its Sept. 4, 2019, conference call.

A majority of the Working Group members voted in favor of adopting these revisions. The motion passed.

Having no further business, the Financial Analysis Solvency Tools (E) Working Group adjourned.

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### Exposure to Discounted Losses and LAE Reserves

5. Determine whether loss and LAE reserves have been discounted and, if so, whether concerns exist regarding the loss reserve discounting.

<table>
<thead>
<tr>
<th>Other Risks</th>
<th>Benchmark</th>
<th>Result</th>
<th>Outside Benchmark</th>
</tr>
</thead>
<tbody>
<tr>
<td>a. Time value of money discount on unpaid losses and LAE</td>
<td>&gt;0</td>
<td>[Data]</td>
<td>[Data]</td>
</tr>
<tr>
<td>b. Time value of money discount on unpaid losses and LAE to surplus</td>
<td>&gt;5%</td>
<td>[Data]</td>
<td>[Data]</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Other Risks</th>
</tr>
</thead>
<tbody>
<tr>
<td>c. Review the Annual Financial Statement, Notes to Financial Statements, Note #32, consider the following:</td>
</tr>
<tr>
<td>• The lines of business with discounted reserves</td>
</tr>
<tr>
<td>• The interest rates used to discount reserves, including the basis indicated for using those rates</td>
</tr>
<tr>
<td>• The amount of discount in relation to surplus</td>
</tr>
<tr>
<td>• If the interest rates used to discount the prior accident years’ reserves have changed from the previous Annual Financial Statement, document the change in discounted reserves due to the change in interest rate assumptions and the effect on surplus</td>
</tr>
<tr>
<td>d. Determine whether the interest rates used to discount reserves appear to be reasonable considering the insurer’s investment yield and the insurer’s comments in Note #32 regarding the basis for the interest rates used.</td>
</tr>
<tr>
<td>e. If the insurer is using discounting procedures that depart from the guidance in Statement of Statutory Accounting Principles (SSAP) No. 65—Property and Casualty Contracts, ensure that the insurer received a permitted practice to do so. (The insurer may describe permitted practices in the Annual Financial Statement, Notes to Financial Statements, Note #1. The NAIC’s iSite+ also has a Permitted Practices for Accounting report for each insurer in the Financial Analysis/Examination report category.)</td>
</tr>
</tbody>
</table>
### III.B.8.a. Reserving Risk Repository – P/C Annual

**Exposure to Salvage and Subrogation**

6. Determine whether unpaid losses and LAE are reduced for anticipated salvage and subrogation recoveries and whether concerns exist regarding the use of anticipated salvage and subrogation recoveries in the development of unpaid losses and LAE.

<table>
<thead>
<tr>
<th>Other Risks</th>
<th>Benchmark</th>
<th>Result</th>
<th>Outside Benchmark</th>
</tr>
</thead>
<tbody>
<tr>
<td>a. Anticipated salvage and subrogation</td>
<td>&gt;0</td>
<td>[Data]</td>
<td>[Data]</td>
</tr>
<tr>
<td>b. Anticipated salvage and subrogation to surplus</td>
<td>&gt;10%</td>
<td>[Data]</td>
<td>[Data]</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Other Risks</th>
</tr>
</thead>
<tbody>
<tr>
<td>c. Review the Annual Financial Statement, Schedule P, Part 1 to determine which lines of business have unpaid losses and LAE that have been reduced due to consideration of anticipated salvage and subrogation.</td>
</tr>
<tr>
<td>d. For the more significant lines of business, review Annual Financial Statement, Schedule P – Part 1 and compare the ratio of anticipated salvage and subrogation to unpaid losses and LAE (gross of anticipated salvage and subrogation) to the ratio of salvage and subrogation received to claims paid (gross of salvage and subrogation received) to determine the reasonableness of anticipated salvage and subrogation.</td>
</tr>
</tbody>
</table>
Uncollected Premium and Agents’ Balances

12. Review and assess uncollected premiums and the agents’ balances for potential collectability issues.

<table>
<thead>
<tr>
<th>Other Risks</th>
<th>Benchmark</th>
<th>Result</th>
<th>Outside Benchmark</th>
</tr>
</thead>
<tbody>
<tr>
<td>a. Ratio of uncollected premiums and agents’ balances to surplus [IRIS ratio #10]</td>
<td>LQ</td>
<td>&gt;2040%</td>
<td>[Data]</td>
</tr>
<tr>
<td>b. Change in uncollected premiums and agents’ balances from the prior year</td>
<td></td>
<td>&gt;25% or &lt;-25%</td>
<td>[Data]</td>
</tr>
<tr>
<td>c. Ratio of uncollected premiums to net premium income</td>
<td>LQ</td>
<td>&gt;5%</td>
<td>[Data]</td>
</tr>
<tr>
<td>d. Ratio of non-admitted uncollected premiums to total uncollected premiums</td>
<td>LQ</td>
<td>&gt;10%</td>
<td>[Data]</td>
</tr>
<tr>
<td>e. Net agents’ balances and premium balances charged off and recovered to total uncollected agents’ balances and premium balances</td>
<td></td>
<td>&gt;5%</td>
<td>[Data]</td>
</tr>
</tbody>
</table>

f. Review amounts non-admitted and compare to prior years.

g. With respect to agents’ balances, verify the creditworthiness of the agent.
III.B.1.a. Credit Risk Repository – P/C Quarterly

DETAIL ELIMINATED TO CONSERVE SPACE

Reinsurance Recoverable and Reinsurer Credit Quality

3. Determine whether amounts recoverable (both paid and unpaid losses on claims and reserve credits) or amounts receivable from reinsurers are significant and collectable.

<table>
<thead>
<tr>
<th>Other Risks</th>
<th>Benchmark</th>
<th>Result</th>
<th>Outside Benchmark</th>
</tr>
</thead>
<tbody>
<tr>
<td>a. Reinsurance amounts recoverable on paid losses to surplus</td>
<td>LQ</td>
<td>&gt;1020%</td>
<td>[Data]</td>
</tr>
<tr>
<td>b. Change in reinsurance recoverables, where recoverables are greater than 1020% of surplus</td>
<td>LQ</td>
<td>&gt;10% or &lt;-10% from the prior quarter OR &gt;35% or &lt;-35% from the prior year-end</td>
<td>[Data]</td>
</tr>
<tr>
<td>c. Provision for Reinsurance to surplus</td>
<td></td>
<td>&gt;10%</td>
<td>[Data]</td>
</tr>
</tbody>
</table>

DETAIL ELIMINATED TO CONSERVE SPACE

Uncollected Premium and Agents’ Balances

5. Review and assess uncollected premiums and the agents’ balances for potential collectability issues.

<table>
<thead>
<tr>
<th>Other Risks</th>
<th>Benchmark</th>
<th>Result</th>
<th>Outside Benchmark</th>
</tr>
</thead>
<tbody>
<tr>
<td>a. Ratio of uncollected premiums and the agents’ balances to surplus</td>
<td>LQ</td>
<td>&gt;2040%</td>
<td>[Data]</td>
</tr>
<tr>
<td>b. Change in uncollected premiums and the agents’ balances from the prior year-end</td>
<td>LQ</td>
<td>&gt;25% or &lt;-25%</td>
<td>[Data]</td>
</tr>
<tr>
<td>c. Change in non-admitted uncollected premiums from the prior year-end</td>
<td>LQ</td>
<td>&gt;25% or &lt;-25%</td>
<td>[Data]</td>
</tr>
</tbody>
</table>
III.B.9.a. Strategic Risk Repository – Annual (All Statement Types)

Financial Analysis Handbook

Capital Adequacy

10. Evaluate the adequacy of the insurer’s risk-based capital (RBC) position in light of its business/strategic plans and risk exposures.

<table>
<thead>
<tr>
<th>Other Risks</th>
<th>Benchmark</th>
<th>Result</th>
<th>Outside Benchmark</th>
</tr>
</thead>
<tbody>
<tr>
<td>a. RBC ratio</td>
<td>OP</td>
<td>&lt;250 %</td>
<td>[Data]</td>
</tr>
<tr>
<td>b. If RBC ratio &lt;300%, has there been a significant change from prior year?</td>
<td>OP</td>
<td>&gt;30 pts or &lt;30 pts</td>
<td>[Data]</td>
</tr>
<tr>
<td>c. Change in Total Adjusted Capital from prior year</td>
<td>OP</td>
<td>&lt;10%</td>
<td>[Data]</td>
</tr>
<tr>
<td>d. Change in Authorized Control Level from prior year</td>
<td>OP</td>
<td>&gt;10%</td>
<td>[Data]</td>
</tr>
<tr>
<td>e. RBC trend test triggered</td>
<td>OP</td>
<td>=YES</td>
<td>[Data]</td>
</tr>
<tr>
<td>f. Decrease in RBC over last two years</td>
<td>OP</td>
<td>=YES</td>
<td>[Data]</td>
</tr>
</tbody>
</table>

Other Risks

<table>
<thead>
<tr>
<th>Other Risks</th>
</tr>
</thead>
<tbody>
<tr>
<td>g. If there has been a downward trend in RBC over the last two years, document the cause(s) of the decline. If a broader trend (e.g., five or more years decline) has been noted, document how the insurer plans to mitigate this continued decline.</td>
</tr>
<tr>
<td>h. If the insurer reported an increase in Total Adjusted Capital due to special surplus or capital infusions, etc., document the source and plan for continued support.</td>
</tr>
<tr>
<td>i. Review the RBC risk component(s) and document the underlying causes of any significant changes.</td>
</tr>
<tr>
<td>j. If the insurer triggered the RBC Trend Test review and document the reason(s).</td>
</tr>
<tr>
<td>k. If the insurer has triggered an RBC Action Level event and if authorized by state statute, obtain and review a copy of the insurer's RBC plan and monitor the overall progress.</td>
</tr>
</tbody>
</table>

Actuarial Opinion – Assurance That an Actuarial Report Has Been Prepared, Signature, Requirements for Actuarial Report

9. Determine whether the Appointed Actuary indicates that an Actuarial Report has been prepared that supports the findings expressed in the Actuarial Opinion. Determine whether the Actuarial Opinion has been signed according to the Instructions. If the Actuarial Report is requested, determine if the report contains the required elements.

| a. The Appointed Actuary indicates that an Actuarial Report and underlying actuarial work papers supporting the Actuarial Opinion will be maintained at the company and available for regulatory examination for seven years. | Comments |
| b. The Actuarial Opinion concludes with the signature, the printed name, the employer's name, the address, the telephone number and the email address of the Appointed Actuary, as well as the date the Actuarial Opinion was rendered. | |
| c. Copy of the Actuarial Report requested. | |
| d. Requirements of the Actuarial Report (to be verified by analyst if report is requested): | |
| i. The Actuarial Report is signed and dated by the Appointed Actuary. | |
| ii. The Actuarial Report is consistent with Actuarial Standard of Practice (ASOP) No. 41, *Actuarial Communications* and includes: | |
| • Narrative component that provides sufficient detail to clearly explain to company management, the board of directors, the regulator, or other authority the findings, recommendations and conclusions, as well as their significance. | |
| • Technical component that provides sufficient documentation and disclosures for another actuary practicing in the same field to evaluate the work and shows the analysis from the basic data (e.g., loss triangles) to the conclusions. | |
### III.B.8.a.ii. Statement of Actuarial Opinion Worksheet – P/C Annual

<table>
<thead>
<tr>
<th>iii. Actuarial report includes required elements from the Instructions:</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>•</strong> Description of the Appointed Actuary’s relationship to the company with clear presentation of the Appointed Actuary’s role in advising the board of directors and/or management regarding the carried reserves. The actuarial report should identify how and when the Appointed Actuary presents the analysis to the board of directors.</td>
</tr>
<tr>
<td><strong>•</strong> An exhibit that ties to the Annual Statement and compares the Appointed Actuary’s conclusions to the carried amounts consistent with the segmentation of exposure or liability groupings used in the analysis. The Appointed Actuary’s conclusions include the Appointed Actuary’s point estimate(s), range(s) of reasonable estimates or both.</td>
</tr>
<tr>
<td><strong>•</strong> An exhibit that reconciles and maps the data used by the Appointed Actuary, consistent with the segmentation of exposure or liability groupings used in the analysis, to the Annual Financial Statement, Schedule P line of business reporting. An explanation should be provided for any material differences.</td>
</tr>
<tr>
<td><strong>•</strong> An exhibit or appendix showing the change in the Appointed Actuary’s estimates from the prior Actuarial Report, including extended discussion of factors underlying any material changes. If the Appointed Actuary is newly appointed and does not review the work of the prior Appointed Actuary, the Appointed Actuary should disclose this.</td>
</tr>
<tr>
<td><strong>•</strong> Extended comments on trends that indicate the presence or absence of risks and uncertainties that could result in material adverse deviation.</td>
</tr>
<tr>
<td><strong>•</strong> Extended comments on factors that led to unusual IRIS ratios for One-Year Reserve Development to Surplus (#11), Two-Year Reserve Development to Surplus (#12) or Estimated Current Reserve Deficiency to Surplus (#13), and how these factors were addressed in current and prior year analyses.</td>
</tr>
<tr>
<td><strong>•</strong> Disclosure of all reserve amounts associated with A&amp;H long duration contracts</td>
</tr>
</tbody>
</table>

Risk Assessment Levels and Trends

Developing an Overall Assessment
Risk assessment, either for an individual risk component or for the overall branded risk classification reflected in the heat map of the IPS, should be based on the ultimate overall assessment of the risk to the insurer, which should take into account any known positive attributes including risk-mitigation strategies and internal controls established by the insurer to ensure management’s business objectives are being followed. Risk-mitigation strategies and internal controls are assessed during examinations; however, they may not all be apparent or known to the analyst during interim analysis periods. To the extent known either through current analysis, recent examination results or communication with the insurer, the analyst should factor risk-mitigation strategies and internal controls into the overall assessment of the risk. Analysts should also consider that changes in risk-mitigation strategies and internal controls may occur between examinations, which will affect the overall risk assessment process. Therefore the overall assessment reflects the ultimate impact of unmitigated risks on the insurer after consideration of mitigation strategies and controls.

Examples of risk-mitigation strategies that may be considered positive attributes during the analysis may include (but are not limited to):

- reinsurance programs intended to mitigate underwriting & strategic risks
- derivatives hedging programs intended to mitigate market risks
- strong enterprise management controls over IT systems to mitigate operational risks
- regular auditing and strong oversight of MGAs & TPAs to mitigate underwriting and operational risks
- strong corporate governance and enterprise risk management that mitigate various risk components
- capital maintenance agreements with a financially strong parent holding company that ensure payment of claims and/or maintenance of capital above certain thresholds to mitigate strategic risk

Parental Guarantees and Capital Maintenance Agreements

Procedure #11X assists the analyst in assessing current and prospective risk related to existing Parental Guarantees and/or Capital Maintenance agreements.

Parental Guarantees and Capital Maintenance Agreements are commitments aimed at providing assurance that the insurer will be able to meet minimum financial obligations if financial or liquidity issues arise. These documents should be carefully reviewed along with the financial background of the entity required to fund the guarantee or agreement. The analyst may also inquire of the insurer if a contingency plan is in place in the event the parental guarantee or capital maintenance agreement is not honored.

Review and assess any parental guarantees, capital maintenance agreements or other commitments in place and determine if concerns exist regarding financial support or failures to act on these commitments. The analyst should thoroughly review the terms related to the agreement to gain a clear understanding of what is covered in the agreement (e.g. limit on lines of business, commitment to pay policyholder claims, commitment to maintain RBC level, etc.) and the impact to the insurer.

The analyst should also consider the following:

- **Expected source and form** of liquidity should guarantees be called upon.
- If the parental guarantee or capital maintenance agreement specifically address the concerns identified and provide adequate support to the insurer:
  - If concerns exist, consider requesting additional information, as necessary to understand the level of commitment.
- Whether the document contains detailed requirements or expectations for capital support.
- The financial stability of the parent holding company to determine if the parent is adequately capitalized to support maintenance of capital in the insurer above certain thresholds.

If a holding company analysis group profile summary (GPS) is available, the analyst should review the GPS for insight into the parent company or ultimate controlling person (UCP) and its ability to meet the financial demands of the guarantee currently or prospectively. Review pertinent data on the holding company and its organizational structure as well as the operations and financial condition of the holding company or UCP. Determine if there are liquidity or other concerns identified within the GPS that warrant additional information from the company.

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Considerations for Troubled Insurance Companies

In troubled or potentially troubled insurance company situations, proactive and timely communication to the appropriate persons within the department and with non-domiciliary state departments (for multi-state companies) is critical. It is also important that the non-domiciliary state communicate with the domestic regulator prior to taking any action against the insurer. In certain circumstances, it may also be appropriate to communicate certain information with other parties (e.g., other regulatory bodies, company management, state guaranty funds, etc.) Establishing a coordinated communication system among the relevant parties will help facilitate the domestic regulator’s surveillance of the troubled or potentially troubled insurance company. The Troubled Insurance Company Handbook provides additional guidance to assist in enhancing a state’s monitoring and surveillance of troubled insurance companies, including communication and coordination of troubled or potentially troubled insurance companies.

At some point, the insurance department may determine that a corrective action plan cannot be implemented or completed successfully. Under these circumstances, the department may determine that the appropriate course of action is to place the troubled company in receivership. The Troubled Insurance Company Handbook outlines specific steps the department should take at all times during the development and implementation of a corrective action plan to prepare itself for this eventuality. This includes knowledge and control over the company’s assets, determining and reviewing the company’s obligations, operational considerations, information gathering, data/IT systems, other jurisdiction/regulatory considerations, etc. In addition to the Troubled Insurance Company Handbook, and the Receiver’s Handbook for Insurance Company Insolvencies provides detailed information and guidance regarding pre-receivership considerations.
The IT Examination (E) Working Group of the Examination Oversight (E) Task Force met via conference call Sept. 26, 2019. The following Working Group members participated: John Jacobson, Chair (WA); Jerry Ehlers, Vice Chair (IN); Blase Abreo (AL); Mel Heaps (AR); Ber Vang (CA); William Arfanis and Ken Roulier (CT); Ginny Godek (IL); Shane Mead (KS); Greg Brelsford (MD); Kim Dobbs and Cynthia Amann (MO); Justin Schrader (NE); Eileen Fox (NY); Metty Nyangoro (OH); Eli Snowbarger (OK); Melissa Greiner (PA); and Dave Jensen (WI).

1. **Adopted Revisions to Handbook Guidance**

Mr. Ehlers and Jacob Steilen (NAIC) provided a brief overview of updates to the revisions to the NAIC *Financial Condition Examiners Handbook* (Handbook) that were being considered by the Working Group. The guidance considered covered three topics. The first topic relates to the conclusions reached on IT General Controls at the end of an information technology (IT) examination. The second topic relates to updates on using IT work performed by a third party to assist in a state insurance regulator’s IT review process. The final agenda topic for revisions would create a new reference to cyber self-assessments and create a mapping to one of those self-assessments developed by the Financial Services Sector Coordinating Council (FSSCC). The revisions would affect Section 1-3 and Exhibit C of the Handbook guidance. Materials were previously exposed and subject to a public comment period ending Aug. 30, with several comments received and incorporated into the newly updated conference call materials. Mr. Steilen provided an update on updates that were incorporated to the draft guidance.

Tom Finnell (America’s Health Insurance Plans—AHIP) inquired as to whether the updated Section 1-3 guidance was clear enough that the use of cyber assessment tools was optional. The way the guidance is stated, companies may opt to use cyber tools depending on their business type. Mr. Finnell noted that the wording made it sound like IT examiners should choose between the listed examples. A friendly amendment was added to clarify that use of the tool is optional.

The next comment related to the criteria for concluding on a generally effective versus ineffective IT general controls environment. Criteria were added to the existing list that included in-process remediation and management’s risk tolerance as mitigating factors that could be used to conclude that an IT general controls environment is generally effective. Mr. Roulier, Ms. Dobbs and Mr. Mead suggested the revisions be removed as they did not consider the new factors to be appropriate considerations in evaluating the impact of findings on IT general controls. A friendly amendment was therefore made to remove the previously added guidance. As these criteria are also reflected on Exhibit C, the Working Group elected to make the same changes for internal consistency. Michael Monahan (ACLI) had two additional clarification suggestions in Section 1-3 that were accepted as friendly amendments. The first edit changed the phrase “may be required to perform additional testing” to “may perform additional testing.” The second edit changed the phrase “may also need to consider additional procedures” to “may also consider additional procedures.”

On Exhibit C – IT Review Standard Summary Memorandum, Ms. Dobbs suggested a friendly amendment to change a sentence to the past-tense because at the time an IT examiner would be filling out the Summary Review Memorandum, the work would already have been performed. The suggested change was accepted as a friendly amendment. Mr. Nyangoro asked if non-IT factors should be considered in the “mitigating factors” column on the Exhibit C findings chart. Miguel Romero (NAIC) stated that the mitigating factors columns is meant to allow IT examiners to provide context in support of why their individual findings were or were not significant to the broader conclusion on IT general controls. The group did not have questions or concerns on the remainder of Exhibit C.

In conjunction with the edit regarding the optional nature of using cyber assessment reports, Mr. Romero suggested adding a similar clarification to the instructions provided at the beginning of the FSSCC mapping tool. There were no objections to this suggestion.

Mr. Roulier made a motion, seconded by Mr. Jensen, to adopt the Handbook guidance (Attachment Four-A), which would include the friendly amendments noted above. The motion passed.

Having no further business, the IT Examination (E) Working Group adjourned.
III. GENERAL EXAMINATION CONSIDERATIONS

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

A. General Information Technology Review
B. Materiality
C. Examination Sampling
D. Business Continuity
E. Using the Work of a Specialist
F. Outsourcing of Critical Functions
G. Use of Independent Contractors on Multi-State Examinations
H. Considerations for Insurers in Run-Off
I. Considerations for Potentially Troubled Insurance Companies
J. Comments and Grievance Procedures Regarding Compliance with Examination Standards

A. General Information Technology Review

The examination of information technology (IT) utilized by an insurer has become an increasingly important part of the examination process as companies have placed a greater reliance on IT systems to run their business. IT general controls (ITGCs) are policies and procedures that help ensure proper operation of computer systems, including controls over network operations, software acquisition and maintenance, and access security. ITGCs provide a foundation necessary to ensure the completeness, integrity and availability of IT systems and data and comprise the environment from which application controls are designed, implemented and operated. An effective ITGC environment can, therefore, provide examiners with greater assurance regarding the overall reliability of a company’s IT systems and the reports generated from those systems. In addition, this allows the opportunity to test and rely on automated application controls during Phase 3 of the exam. As such, a formalized process to complete a general IT review has been developed to assist the IT examiner in completing this important section of the financial condition examination. In a risk-focused examination, steps 1–5 of the general IT review process should be performed prior to the completion of planning the overall financial condition examination. Step 6 of the IT review process should be performed in conjunction with the remaining portion of the overall examination. The following steps document the process to be followed in completing the general IT review:

1. Gather Necessary IT Planning Information

The first step in performing a general IT review is to gather the information necessary to plan the IT review of the insurer. At this time, the examiner-in-charge (EIC) and the IT examiner should work together to request that the insurer complete the Information Technology Planning Questionnaire (ITPQ), included in Exhibit C – Part One, to assist in the planning process. In addition, other relevant information to obtain in planning the IT review might include prior examination workpapers, work on IT systems performed by internal/external auditors or consultants, and information maintained by the insurance department’s financial analysts. The reports and results from third-party cyber self-assessment tools may also be utilized for an IT review. Note that if companies do not use these tools, the examiner can continue with the normal IT review process. There are a variety of cyber self-assessment tools that companies may opt to use depending on their business type. Examples of cyber assessment tools that have been developed include, but are not limited to, tools developed by, or to facilitate compliance with the following: the Financial Services Sector Coordinating Council (FSSCC), the Health Information Technology for Economic and Clinical Health Act (HITECH), and the Health Insurance Portability and Accountability Act of 1996 (HIPAA). Based on a consideration of the assessment tool’s scope, date of preparation, and quality of information presented (including whether or not the information has been validated by an independent third-party), the state insurance regulator may determine the information contained within the assessment that...
can be extensively leveraged during the IT review. Depending on the assessment of the IT examiner, the results of the cyber self-assessment tool may be used to:

- Populate Exhibit C with risk statements and controls to be tested.
- Reduce the extent of testing within Exhibit C if the state insurance regulator determines that the self-assessment has already been sufficiently validated.

2. Review Information Gathered

After the information for planning the IT review has been gathered, including the ITPQ, the IT examiner should review the information obtained to assist in planning and determining the scope of the general IT risks to be reviewed. Some factors to consider as part of this process include:

- The complexity of the insurer’s information systems and IT risk mitigation strategies;
- The extent to which reliance will be placed on those risk mitigation strategies in the financial examination;
- The length of time the existing system has been in place and any significant changes to the system;
- The types of subsystems being used and how data is shared among systems;
- The hardware and software being used and whether the software was internally or externally developed;
- The extent to which the insurer outsources its IT functions;
- Past issues the insurer may have had with its systems;
- Answers provided from the insurer via the ITPQ;
- Documentation available from other sources, including external and internal auditors;
- The insurer’s participation in electronic business and electronic data interchange;
- The amount of reliance placed on the work of third parties;
- The type, volume, and external availability of sensitive information that is processed and/or stored by the company and;
- Changes to the company’s controls and/or processes to ensure compliance with the General Data Protection Regulation (GDPR), if applicable, or other relevant data protection requirements.

The IT examiner should consider which risks included on the Evaluation of Controls in Information Technology (IT) Work Program (Exhibit C – Part Two) are applicable to the insurer under examination and determine if there are additional general IT risks that should be reviewed for this insurer. Additionally, based on the review of internal and external audit work, the IT examiner may determine that sufficient testing has been performed to fully address specific risks or areas of concern. In this case, the IT examiner may document in the IT planning memo their comfort with, and planned reliance on, the specific internal and/or external audit work included in the file. Additionally, the IT examiner need not include these specific risks or areas of concern in the IT work program.

3. Request Insurer Control Information and Complete IT Review Planning

After the initial planning information has been gathered and reviewed, the Evaluation of Controls in Information Technology (IT) Work Program (Exhibit C – Part Two) to be utilized in the review should be created. As part of this process, the IT examiner should customize the standard work program to include only the general IT risks that are of concern for the insurer under examination. In addition to providing a list of risks in the work program, the IT examiner may wish to provide a list of common controls that indicate how a typical insurer may mitigate these risks to assist the insurer in developing its response. Finally, the IT examiner may consider prompting the insurer to include information supporting the IT controls in place to mitigate risks by including an information request in the work program distributed to
the insurer. The IT review team should coordinate with the appropriate staff at the insurer to request a response. The insurer’s response should indicate their controls in place to mitigate the risks identified in the work program. The IT examiner should review the company responses, considering the adequacy of the controls identified, and request evidence to test the effectiveness of the insurer’s mitigating controls. The IT examiner may consider some of the examination procedures listed in the Evaluation of Controls in Information Technology (IT) Work Program (Exhibit C – Part Two), and complete the planning of the IT review.

After the work program has been finalized, the IT examiner should document the plan to complete the IT review. The plan should document the staffing to be used to complete the review, the scope of work to be performed and a proposed budget to complete the review. The plan should be subject to the review and approval of the EIC and additional examination supervisors, as considered appropriate by the state. This plan may be documented through the use of an IT review planning memo, or other workpaper that documents the approval of the EIC.

4. Conduct IT Review Fieldwork

The IT examiner should schedule examination fieldwork, with the initial fieldwork to include conducting interviews of key IT staff. These interviews should serve as an opportunity to substantiate and clarify some of the information provided by the insurer in Exhibit C – Part Two. The IT examiner may also gain additional information relating to key activities, risks, and risk mitigation strategies for the financial examination. As such, the IT examiner may want to invite the examiner-in-charge and/or other financial examination staff to participate in the interview process. Some of the potential candidates for interview include the Chief Information Officer, Chief Technology Officer, Chief Security Officer, System Architect, Chief System Engineer, and any other individuals responsible for maintaining, updating and testing the insurer’s business continuity and disaster recovery plans. Example agenda items for IT interviews, subject to the areas of expertise for the interviewee, include but are not limited to:

- IT Strategic Planning;
- IT Governance;
- Leadership development and succession planning;
- Organizational structure;
- Risk management;
- Development and maintenance of policies;
- Budgeting;
- Security;
- E-Business;
- Business continuity;
- Acquisitions and integration;
- Architecture, development and implementation of major programs;
- External environment, and
- Any other items necessary to evaluate the insurer’s general IT controls.

After the IT review team has completed the interviews, the team should begin to test the general controls identified by the insurer. This work should be completed with the assistance of the insurer’s IT staff and should utilize the existing work of others, if deemed appropriate. As noted in step 2 above, if the IT examiner has determined that reliance will be placed on all or some of the work performed by external auditors or the company’s internal audit function (if deemed independent) to fully address a specific risk or area of concern, the IT examiner would not be required to include those specific risks or areas of concern on the work program. However, if the IT examiner determines that the work performed by the third-party only partially addresses a risk, but additional work would be required to fully address that risk, the IT
examiner should include the relevant third-party documentation in the file and map or link it to the respective risk in the work program.

While it is expected that audit work (external/internal) would be the most common type of work relied on by the exam team, work performed by other regulatory agencies and/or cybersecurity experts may also be leveraged to reduce the independent work performed during an exam. Regardless of the work being reviewed, state insurance regulators should specifically consider the scope of work, the independence and qualifications of the entity (or person) performing the work, the timing of the work performed, and the findings included in any report received. Qualifications should be evaluated based on the training, experience, and education of personnel performing the work (see Section 1-2 Letter E for more information on the use of specialists). Based on the state insurance regulator’s review of the third-party work, state insurance regulators may be able to use the work to enhance the risk assessment, interview, and scoping process performed during the IT review. While the IT examiner is responsible for performing his/her own independent risk assessment, third-party work that directly addresses an identified risk may be relied upon in a similar manner to external/internal audit work. In this case, the IT examiner should briefly document his/her understanding of the third-party testing performed and any conclusions reached from the testing procedures. To the extent that findings are noted in the report obtained, state insurance regulators may find it more useful to corroborate the remediation of the findings as opposed to performing an independent review of the company’s controls to confirm the findings’ existence.

After considering the utilization of existing work, testing of general IT controls and other procedures should be performed in order to gain an appropriate level of understanding of the insurer’s IT environment and the effectiveness of general IT controls in place. As noted above, the IT examiner may consider performing examination procedures listed in the Evaluation of Controls in Information Technology (IT) Work Program (Exhibit C – Part Two) or any other procedures necessary to conclude upon the effectiveness of the company’s general controls in mitigating the risks identified. All testing should be documented appropriately to ensure that the work may be referenced within the financial examination workpapers, as necessary.

5. Document Results of IT Review

At the conclusion of the IT review fieldwork (at or prior to the conclusion of planning of the financial examination process), the IT examiner should have a completed IT controls work program supported by documentation and testing as a deliverable. In addition, a summary of findings regarding the insurer’s IT environment and general IT controls should be prepared at this time. The findings may be considered prospective in nature (resulting in recommendations to the company) or current in nature (which may have an impact on the financial exam). These findings should be documented through the use of an IT summary report (or similar document), which should include a description of recommendations to the company and/or how the findings may impact the examiner’s reliance on general IT controls and approach to application control testing in Phase 3. The IT summary report may also include a summary of the insurer’s IT operations, and detail on the IT review work performed. Based on the impact of the findings, the IT examiner should determine whether the ITGC environment is generally effective. A generally effective environment would indicate that IT risks have been sufficiently mitigated and findings are not pervasive enough to limit the ability to allow for testing of application controls in Phase 3. If the IT general control environment is not deemed effective, the examiner would be required to perform additional testing in later phases of the exam before relying on system generated reports or controls in place at the insurer.

Whether the IT general control environment is deemed effective ultimately depends on the IT examiner’s professional judgment. From the IT examiner’s perspective, controls over IT systems are considered generally effective when they maintain the integrity of information and the security of the data that such systems process and when they include effective general IT controls and application controls. Typically, at the end of the IT review, the ITGC environment would be considered generally effective, unless specific...
adverse findings summarized in the IT summary memorandum indicate otherwise. Professional judgement and skepticism should be exercised when making this determination. Often, even when issues are identified, the IT examiner may be able to determine that the finding is isolated to a specific system or point in time and, therefore, would not impact the overall reliability of the ITGC environment. In this case, the IT examiner should document in the IT summary memo which key activities or specific applications may be impacted by IT review findings and how.

In some instances, the overall ITGC environment may be deemed ineffective. In reaching this conclusion, the IT examiner should consider whether the findings outlined in the IT summary report:

- Are pervasive throughout the ITGC general control environment.
- Significantly impact the systems used in calculating and reporting financial results or the accuracy of information used in reaching major strategic decisions.
- Indicate deficiencies relating to management involvement and oversight of the IT strategy and direction.
- Are not alleviated by other mitigating factors.

If the ITGC general control environment is not deemed generally effective, the examiner would be required to perform additional testing in later phases of the exam before relying on system generated reports or application controls in place of the insurer. The additional testing procedures should be designed to prove that the application control or system report is complete and correct despite the generally ineffective ITGC environment. Whether the ITGC general control environment is deemed generally effective ultimately depends on the IT examiner’s professional judgment. To determine the impact of the IT review findings on the remainder of the examination, the examiner should next consider if the nature of the findings affects the quality of information produced by the company’s applications and systems. For instance, a finding that the company has inadequate continuity management controls may be significant. However, such a finding would be unlikely to affect information produced by the company’s IT systems. The IT examiner should assess ITGCs with regard to their effect on applications and data that become part of the financial statements or are used in making strategic business decisions.

The examiner may also consider performing additional procedures to determine the extent of the impact of specific findings. For instance, the company may have deficient user access controls. If the examiner is able to determine that in the period under examination, the key systems to the exam were not accessed inappropriately, the impact of the examination’s findings may not substantively affect the examination in later phases of the exam beyond the reporting of the finding. Given the complexity of evaluating the impact of individual findings and/or findings in the aggregate, communication of the results and mitigating factors in the IT Summary Conclusion Memorandum is important.

The IT examiner is cautioned against defaulting to the conclusion that the overall ITGC environment is ineffective, as such a conclusion could have a significant impact on the approach taken by the financial examiner on the remainder of the examination. For instance, in Phase 3, the examiner would be required to test manual or compensating controls for an identified risk if application controls cannot be relied upon and, therefore, may not be able to reach strong controls reliance. This may lead to additional detail testing in Phase 5 to fully address the identified risk. Additionally, the examiner would be required to test the accuracy and completeness of system generated reports, prior to those reports being utilized in addressing the identified risk in Phase 5.

The IT review process outlined up to this point, along with the corresponding documentation of results, may be performed on each examination, regardless of insurer size. These documents should also be appropriately presented and discussed with the examiner-in-charge to help facilitate a general understanding of the IT systems in place at the insurer and the impact that any findings may have on the ongoing exam.
6. Assist on Financial Examination

Following the completion of the IT review of the examination, the IT examiners involved in the IT review should remain available to assist in the completion of the financial portion of the examination. Such assistance could include data mapping, ACL testing, clarification of work performed during the IT review, assistance in completing the examination report and recommendation letter, and additional assistance in testing IT application controls to mitigate risks identified by the financial examination team.

Although the identification and assessment of risk mitigation strategies is the responsibility of the examination team as a whole, the IT review staff may have additional insight and experience that may be beneficial in identifying and testing IT controls associated with particular insurer applications. The involvement of IT review staff in this area of the examination may be especially beneficial when examining companies with well documented internal controls that may allow the examination team to reduce substantive testing.

Cybersecurity Considerations

As the examiner reviews an insurer’s operations, he or she may determine that the insurer has significant exposure to cybersecurity risks. The specific risk exposure for the insurer may vary based on volume, type of sensitive information (e.g. Social Security numbers, protected health information, personally identifiable health information, etc.) and the broad security environment in which the insurer is operating. The examiner should be mindful that the insurer is not required to use any particular IT security framework, nor are its IT security systems or controls required to include all of the components of any single or particular IT security framework or the examiner’s work program. The examiner should broadly consider not only the volume and type of sensitive information obtained, maintained or transmitted by the insurer, but also the laws and regulations to which the insurer is subject, as well as the size and complexity of the insurer’s operations and the nature and scope of its activities. All of these factors will influence the cybersecurity policies and systems and the IT security framework or frameworks that are appropriate for a particular insurer to effectively protect its sensitive information. As a result, responding to a particular insurer’s risk will require judgment by the examiner in tailoring the use of existing Handbook guidance. In these situations, examination teams should review the insurer’s risk mitigation strategies and/or controls that identify cybersecurity risks to protect against and detect cybersecurity incidents, and respond to and recover from cybersecurity incidents when they do occur.

When assessing the level of an insurer’s cybersecurity controls/processes, the examiner should take into account the distinction between the roles of the insurer’s board of directors and its senior management. The examiner should recognize that, while it is the role of the board to understand and oversee the insurer’s cybersecurity policies, systems and controls, it is the role of its senior management to implement the insurer’s cybersecurity policies and to ensure the performance and outcomes of the insurer’s risk mitigation strategies and controls are appropriate. Strategies and controls should identify, protect against, and detect cybersecurity incidents, as well as allow the insurer to respond/recover from such incidents. Each of the primary information security functions are described below:

- Identify - The identification of cybersecurity risks is important in helping the organization understand the best way to deploy its limited resources. Internal risk assessment is crucial for organizations to understand constantly evolving risks. Participation in information networks, though not required, is likely to enhance understanding of risks. In a robust control environment, insurers devote resources to a risk assessment process that includes some amount of management/board involvement, appropriate to the distinct roles of the board and senior management, as well as a sufficient level of technical expertise to ensure that issues are well understood and responded to appropriately.

- Protect - Protection is an important element in the overall strategy for any risk and cybersecurity is no exception. A robust risk mitigation strategy may include a combination of strong policies, system and
network access controls, and data security protection (e.g. data-at-rest, in use, in transit, and in storage are protected, etc.), as appropriate to the broad security environment in which the insurer is operating, including the volume and type of sensitive information obtained, maintained, or transmitted by the insurer, the security laws and regulations to which it is subject, its size and complexity, and the nature and scope of its activities. When applicable, controls should directly address risks presented by third party access to the insurer’s network, systems and data (including access by vendors, agents, brokers, third-party administrators [TPAs] and managing general agents [MGAs]). Training is also an important part of the insurer’s response to cybersecurity risks as many incidents occur due to improper execution of controls rather than the lack of controls. Control effectiveness is limited if employees are not provided adequate training to understand the objectives and importance of their assigned responsibilities.

- Detect - Insurers should also have a strong set of detective controls that enable timely identification and mitigation of threats to the organization. These may include anti-virus and anti-malware software as well as network monitoring and intrusion detection related processes and controls. Organizations may perform vulnerability scans and penetration tests to ensure that weaknesses in the protective/detective controls are identified and addressed.

- Respond and Recover - A review of the insurer’s incident response plan is an important consideration in the overall assessment of cybersecurity at an insurer. The response to a cybersecurity incident may leverage concepts from the insurer’s broader disaster recovery plan, but may also require unique considerations since recovering from a cybersecurity incident requires a different response than recovering from an environmental incident (e.g. fire, earthquake, tornado, etc.). The examiner should note, however, that network threats and incidents are not rare events like environmental incidents. It is also important that people with assigned responsibilities within the disaster recovery plan have the necessary background/training to perform the assigned duties. Insurers should include in their plan who they are required to contact in the event of a security incident (regulators, affected parties, etc.) and how public relations will be managed to limit the impact of the incident on the organization’s reputation. Importantly, response plans should be tested to ensure that the organization is ready to deploy the plan in the event of an actual incident.

When significant incidents do occur, it is important that the insurer performs a thorough post-remediation analysis and restores services that were affected as a result of the incident in accordance with the response plan. Examination teams may consider reviewing incident reports to consider how the organization has learned and adapted when security protocols are breached.

Depending on the insurer’s operations, there may be unique risks that the examiner identifies for further review. For instance, some insurers may leverage controls at service providers to provide assurance over cybersecurity risks. While this may be appropriate, insurers should be able to confirm that the service provider has appropriate risk mitigations strategies and controls in place and that appropriate protections are built into their service agreement (e.g. indemnification clauses, right to audit, technology errors and omissions insurance coverage, etc.) to address the risks presented to the insurer.

Although uncommon, if the examiner determines that the insurer has significant exposure to cybersecurity risk, the examiner may consider incorporating the use of a cybersecurity expert to assist in performing cybersecurity procedures. The specific risk exposure assessment for the insurer should be based on the IT examiner’s judgment and may consider the insurer’s line of business, the size and complexity of operations, known cybersecurity incidents; risks presented by third-party access to the insurer’s network systems and data, recent acquisitions, concerns about the controls in place to protect against, detect, respond and recover from cybersecurity incidents, or any other significant risk factors related to cybersecurity. Note that the decision to use additional expertise to address cybersecurity concerns should be based on the accumulation of circumstances and not necessarily due to any one situation discussed above.
The following insights may assist regulators and/or cybersecurity experts as they assess the strength of the insurer’s security program and therefore the risk that cybersecurity events present to the insurer. These insights are for informational purposes and are not intended to be requirements for insurers. Companies may be assessed by their individual risk profile and the organization’s risk strategy.

Events, Incidents and Breaches

As regulators engage insurers in discussion regarding past cybersecurity events, it may be useful to understand the difference between various types of events. A “cybersecurity event” can be defined as an event resulting in unauthorized access to, disruption or misuse of an information system or information stored on such an information system. Insurance companies may also use terms such as incidents and breaches or may distinguish between successful and unsuccessful events as they discuss their cybersecurity program. Regardless, regulators should gain an understanding of how the insurer defines its events and incidents. Insurers should consider both unsuccessful cybersecurity events and successful cybersecurity events (incidents), as appropriate. For instance, while an unsuccessful event may only access the company’s network without accessing sensitive information, it may still represent an event that the insurer should consider, correlate with other activity, and learn from to ensure security practices are enhanced, as appropriate. Timely, effective incident response is extremely critical in minimizing the impact of a cybersecurity incident.

Integration of Cybersecurity Risk into Enterprise Risk Management

As noted before, an insurer’s board and/or senior management often play a significant role overseeing a cybersecurity program. As an insurer’s cybersecurity risk increases, examination teams may want to scrutinize the integration of cybersecurity risk into the insurer’s Enterprise Risk Management. This may include consideration of the level of information provided to the board and/or senior management and the appropriateness of the insurer’s risk identification and assessment process. It may be appropriate for board and/or senior management to receive summary level information, but there should be a designated person with cybersecurity expertise that is responsible for developing the insurer’s response to mitigate cybersecurity risks. This person should be deemed the insurer’s cybersecurity risk owner and should receive information that is tailored to the insurer’s specific cyber risk exposures. For instance, use of third-party service providers, integration of acquired companies, legacy systems, etc. may all represent unique exposures that require specific consideration as mitigation strategies are developed.

Information Security Program

Note: The guidance that follows should only be used in states that have enacted the NAIC Insurance Data Security Model Law (#668). Moreover, in performing work during an exam in relation to the Model #668, it is important the examiners first obtain an understanding and leverage the work performed by other units in the department, including, but not limited to, market conduct-related work.

Specific requirements related to an insurance company’s information security program are included in Model #668. States that have passed the law may have an enhanced ability to encourage remediation of control issues in relation to issues identified during the exam. To the extent a state has adopted Model #668 and it is in effect at the time of the examination, examiners may consider tailoring the IT review to include consideration of the items below. As evidenced below, implementation of each control identified for consideration shall be done based on the insurer’s individual risk assessment:

Section 4-C of Model #668 details the requirements for performing a risk assessment. As part of a risk assessment, the licensee shall perform the following:

1. Designate one or more employees, an affiliate or an outside vendor designated to act on behalf of the licensee who is responsible for the Information Security Program.
2. Identify reasonably foreseeable internal or external threats that could result in unauthorized access, transmission, disclosure, misuse, alteration or destruction of nonpublic information, including the security of information systems and nonpublic information that are accessible to, or held by, third-party service providers.

3. Assess the likelihood and potential damage of these threats, taking into consideration the sensitivity of the nonpublic information.

4. Assess the sufficiency of policies, procedures, information systems and other safeguards in place to manage these threats, including consideration of threats in each relevant area of the licensee’s operations, including:
   a. Employee training and management.
   b. Information systems, including network and software design, as well as information classification, governance, processing, storage, transmission and disposal.
   c. Detecting, preventing and responding to attacks, intrusions or other systems failures.

5. Implement information safeguards to manage the threats identified in its ongoing assessment, and no less than annually, assess the effectiveness of the safeguards’ key controls, systems and procedures.

Based on this risk assessment, Section 4-D requires the licensee to execute the following:

1. Design its Information Security Program to mitigate the identified risks, commensurate with the size and complexity of the licensee’s activities, including its use of third-party service providers, and the sensitivity of the nonpublic information used by the licensee or in the licensee’s possession, custody or control.

2. Determine which security measures listed below are appropriate, and implement such security measures.
   a. Place access controls on information systems, including controls to authenticate and permit access only to authorized individuals to protect against the unauthorized acquisition of nonpublic information.
   b. Identify and manage the data, personnel, devices, systems and facilities that enable the organization to achieve business purposes in accordance with their relative importance to business objectives and the organization’s risk strategy.
   c. Restrict access at physical locations containing nonpublic information only to authorized individuals.
   d. Protect by encryption or other appropriate means all nonpublic information while being transmitted over an external network and all nonpublic information stored on a laptop computer or other portable computing or storage device or media.
   e. Adopt secure development practices for in-house developed applications utilized by the licensee and procedures for evaluating, assessing or testing the security of externally developed applications utilized by the licensee.
   f. Modify the information system in accordance with the licensee’s Information Security Program.
   g. Utilize effective controls, which may include multifactor authentication procedures for any individual accessing nonpublic information.
h. Regularly test and monitor systems and procedures to detect actual and attempted attacks on, or intrusions into, information systems.

i. Include audit trails within the Information Security Program designed to detect and respond to cybersecurity events and designed to reconstruct material financial transactions sufficient to support normal operations and obligations of the licensee.

j. Implement measures to protect against destruction, loss or damage of nonpublic information due to environmental hazards, such as fire and water damage or other catastrophes or technological failures.

k. Develop, implement and maintain procedures for the secure disposal of nonpublic information in any format.

3. Include cybersecurity risks in the licensee’s ERM process.

4. Stay informed regarding emerging threats or vulnerabilities, and utilize reasonable security measures when sharing information relative to the character of the sharing and the type of information shared.

5. Provide its personnel with cybersecurity awareness training that is updated as necessary to reflect risks identified by the licensee in the risk assessment.

Review section 3 of the Model #668 for legal definitions of relevant and commonly used terms. For purposes of the exam process, licensees include, but are not limited to, insurance companies. Model #668 also covers the topics of board of directors oversight, third-party service providers, program adjustments, incident response plan, and the annual certification to the commissioner of the domiciliary state. Review Model #668 language for further insights on the topics above.

Evaluating Employee Training / Security Awareness Programs

Employees often represent the front line of any strong security program. However, without proper training, employees may also represent vulnerability in the company’s defense program. Therefore, strong security awareness training can help in mitigating the risk presented by phishing e-mails and other social engineering attacks. Strong security awareness training may be characterized by:

- Use of real world examples to help users be able to identify phishing e-mails;
- Use of phishing emails sent to the user community by the insurers internal security specialists or security vendor to measure effectiveness of user training;
- A clear protocol that provides employees help in identifying and reporting phishing e-mails; and
- Elements of a training that are tailored to the employee’s specific roles, responsibilities, and access rights.

Since cybersecurity threats are constantly evolving, it is important to have a strong and up-to-date training regimen. Additionally, in a strong cybersecurity program trainings should be performed on a consistent and periodic (e.g. annually) basis to ensure the information reaching the employees is commensurate with the modern-day threats facing the company. As regulators evaluate the appropriateness of the program, they should consider whether the training is mandatory for all employees and whether it includes procedures and instructions for employees to follow.
in the event that the employee has a good faith, fact-based belief that a breach or cybersecurity event may have occurred.

Vulnerability Management

In the most robust information security programs, companies understand that not all vulnerabilities can be eliminated, typically due to business needs or time and resources. However, companies should have an understanding and should inventory their identified vulnerabilities as well as have a plan to ensure vulnerabilities that can’t be eliminated are mitigated as much as possible. For instance, if the insurer is unable to confirm that a third-party service provider is able to secure their own access to the company’s information system, the company should ensure they monitor the service provider’s access to determine if improper activity occurs on the company’s network. As many vulnerabilities originate with a company’s patching practice, it is important that regulators obtain an understanding of the company’s patch management. Research suggests that in any given year, the majority of breaches have a root in a Common Vulnerability and Exposure (CVE) that often has been known and identified for several years. An insurer should maintain a strong practice of patch management, or at least a practice of understanding and mitigating existing vulnerabilities as an important part of a robust security program.

Company Acquisitions

Finally, in situations where a company has recently acquired/integrated another company, the IT examiner should also pay special attention to the procedures performed in integrating company systems. This is often when companies are most vulnerable to cybersecurity threats as controls are often in flux and mistakes in integration may create vulnerabilities that are not easily identified or remedied.

Exhibit C, Part Two (Instruction Note 3) includes specific mention of risk statements and sections of the exhibit that can be applied to ensure the examination has an appropriate response to identified cybersecurity risks.

Note that the findings identified through the review of the company’s cybersecurity control environment should be communicated to the financial examiner via the IT Summary Memo.

Customization for Small Companies

When conducting an IT review of a small company or a company with a non-complex IT environment, it is acceptable to limit the extent of test procedures performed. However, the examination must adhere to the six-step process outlined above. This includes obtaining the ITPQ responses from the insurer, completing a basic work program, and preparing a summary memo concluding on the results of the IT review and its impact on the rest of the examination.

The most significant area to be customized for small insurers is the IT work program. Regardless of size or complexity, some level of testing is required to be performed to verify the basic design and operating effectiveness of the insurer’s IT environment; however, the presentation of such work may vary. It is recommended that IT examiners perform some level of review for ITGCs in place within each domain of the COBiT Framework. This may be shown using a customized version of Exhibit C – Part Two, where a limited number of controls applicable to the insurer are populated and reviewed. In limited circumstances, as described below, IT examiners may bypass the utilization of Exhibit C – Part Two:

1. If the CPAs or the company’s internal audit function (if deemed independent) have performed a review of ITGCs that sufficiently cover risks within each of the COBiT domains, the IT examiner may rely on such work without mapping or linking the work to a separate work program. However, the IT examiner must document their comfort with and planned reliance on the work performed.

2. When the IT environment is simplistic and the insurer utilizes purchased software programs from well-known vendors, IT examiners may choose to summarize, in memo format, the procedures performed for
each domain of the COBiT Framework. However, before determining that it is appropriate to bypass the utilization of Exhibit C, IT examiners should consider whether the company has made significant modifications to the software being used, as modifications may impact the software’s reliability. In situations where significant modifications have been made and continue to be made, IT examiners should utilize Exhibit C – Part Two to document a consideration of risks relating to change management.

---Detail Eliminated to Conserve Space---

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A summary memorandum should be developed by the IT examiner to communicate the results of the IT review to the examiner-in-charge, or any other users. Some of the topics the IT examiner may want to consider incorporating into the summary memorandum are included in the illustration below, along with a brief description of information that could be discussed relating to each topic. This document should provide sufficient detail of the results of the IT review for use during the financial condition examination.

Salutation

This section should be in any format the state deems appropriate for its purposes. At a minimum, all states that are placing reliance on the IT review should be included in the distribution of this memo.

Background and Scope

This section should include an introductory paragraph identifying the following: companies under examination (domiciliary state and type may be helpful), the exam as-of date and time period under examination, where the work was performed, when the work was performed, and who performed the work, and the scope/topic of the work performed.

Summary of Control Environment

This section should provide a summary description of the IT environment and the general IT controls assessed during the IT review. This section should also provide a general description of the insurer’s overall processes and controls, including access controls, in place to protect sensitive information. This section should also include discussion of any breaches identified during the period under exam.

Work Performed

This section of the memo should provide an overview of the work performed to evaluate general IT controls throughout the IT review process, as well as the reliance placed on external sources (e.g., Model Audit Rule documentation/testing, Sarbanes-Oxley documentation, external audit work, etc.). If the results of external audit, third-party work, and/or cyber self-assessment tools are utilized to populate Exhibit C procedures, include a review of the external work in this section. This review could include an assessment of the source, scope, and robustness of the third-party work being utilized.

Summary / Detail of Findings (Including Cybersecurity Related Findings)

This section should provide a summary description of the findings that were identified while performing the IT review. These findings may include: areas that affect the company’s current operations; areas that will be relevant for future examinations; or areas of recommendation for the company to consider. The IT examiner should document the recommendation and impact of the finding on the financial examination and provide reference to the supporting detail located in the completed Exhibit C, Part Two (or similar document). The IT examiner should consider mitigating factors in their assessment of the impact that findings will have on the exam (additional testing may be required to assess the effectiveness of the mitigating factors). Findings that are sufficiently mitigated by other factors may be found to have a minimal ongoing impact for examination purposes. The following table(s) or similar format may be used in assessing findings, mitigating factors, and the overall impact on the exam:
Findings

<table>
<thead>
<tr>
<th>IT Review Finding</th>
<th>Recommendation for Company</th>
<th>Mitigating Factors</th>
<th>Impact on Financial Examination</th>
<th>Supporting Detail Reference</th>
</tr>
</thead>
<tbody>
<tr>
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</table>

Conclusion/Results of IT General Control Review

This section should document the conclusion/results of the ITGC review. Based on the impact of the findings, the IT examiner should determine whether the ITGC environment is effective and would, therefore, indicate that IT risks have been sufficiently mitigated to allow for reliance on general IT controls and testing of application controls in Phase 3. If the ITGC environment is not effective, the examiner would be required to perform additional testing in later phases of the exam before relying on system-generated reports or controls in place at the insurer. The IT examiner should consider the impact of the findings on the exam in totality and consider the following when concluding between a generally effective or ineffective ITGC environment. In some instances, the overall ITGC environment may be deemed ineffective. In reaching this conclusion, the IT examiner should consider whether the findings outlined in the IT summary report:

- Are pervasive throughout the ITGC environment.
- Significantly impact the systems used in calculating and reporting financial results or the accuracy of information used in reaching major strategic decisions.
- Indicate deficiencies relating to management involvement and oversight of the IT strategy and direction.
- Are not alleviated by other mitigating factors.

If the impact of a finding is isolated to a point in time or a less significant system, the IT examiner may still determine a generally effective ITGC environment while listing the particular system(s) as an exception. The IT examiner should document the possible implications on the exam with the goal of helping the exam team adjust their testing approach around the affected area. For additional guidance regarding the conclusion of the ITGC review refer to Section 1, Part III, A – General Information Technology Review.

Note: The IT Examiner should provide a conclusion on the effectiveness of the ITGCs using the terminology prescribed by the Handbook (effective or ineffective). Using alternate language may leave the Financial Examiner in an unclear position on whether ITGC’s can be relied upon and may lead to inefficiencies later in the examination process.

Meeting with Examiner-In-Charge and Other Financial Examiners

This section should document the date and time of the meeting with the EIC and other examiners (e.g., examiners from other states participating in the financial examination) that was conducted to discuss the findings and results of the IT review.

Assistance on the Financial Examination

This section should identify the remaining areas of the financial examination in which the IT review team will be asked to provide assistance. This may include testing application controls in conjunction with Phase 3 of the risk-focused examination, performing data mapping or ACL testing, and/or assisting with drafting the examination report and/or management letter.
Completed Exhibit C, Part Two (or Similar Document) and Supporting Documentation

A completed IT Review Work Program should be referenced here and provided to the EIC. Detail findings should be noted within the work program and referenced in the “Detail of Findings” section above.

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The Financial Examiners Handbook (E) Technical Group of the Examination Oversight (E) Task Force met via conference call Nov. 14, 2019. The following Technical Group members participated: Susan Bernard, Chair (CA); William Arfanis (CT); N. Kevin Brown (DC); Cindy Andersen (IL); Shannon Schmoeger (MO); Justin Schrader (NE); Colin Wilkins (NH); John Sirovetz (NJ); Tracy Snow (OH); Joel Sander (OK); Melissa Greiner (PA); Pat McNaughton (WA); and John Litweiler (WI).

1. **Adopted Minutes from its Sept. 12, Conference Call**

The Financial Examiners Handbook (E) Technical Group met via conference call Sept. 12 and took the following action: 1) adopted salary range guidelines for inclusion in the Financial Condition Examiners Handbook (Handbook); 2) adopted Handbook guidance to emphasize the importance and timing of interviews; 3) adopted a new template for interviewing a chief marketing officer; 4) exposed Handbook guidance related to troubled insurance companies, management letters, Exhibit V – Overarching Prospective Risk Assessment, and Exhibit AA – Summary Review Memorandum; 5) received an update on the status of the examination repository updates; and 6) received an update from IT Examination (E) Working Group on the status of its projects.

Mr. Schrader made a motion, seconded by Ms. Greiner, to adopt the Sept. 12 conference call minutes (Attachment Five-A). The motion passed unanimously.

2. **Adopted Handbook Guidance**

   a. **Troubled Insurance Companies**

Ms. Bernard said NAIC staff developed proposed revisions to incorporate considerations when examining a troubled or potentially troubled insurance company in response to a referral from the Financial Analysis (E) Working Group. The revisions provide guidance regarding specific key elements from the *Troubled Insurance Company Handbook*, including communication expectations for companies that are troubled or potentially troubled, and pre-receivership considerations. Ms. Bernard said the referral also requested consideration of guidance regarding the priority rating framework. However, because existing guidance addresses the priority framework, no additional changes were made. Ms. Bernard said no comment letters were received regarding this proposed change.

These considerations may include: 1) the level at which corrective measures can be taken; 2) whether the findings meet the definitions for significant deficiency or material weakness; 3) the likelihood of the finding having a significant adverse impact on the insurer’s overall condition; 4) whether a conflict of interest exists; and 5) whether management has sufficient understanding and capacity to anticipate and respond to changing conditions.

Tom Finnell (America’s Health Insurance Plans—AHIP) said that it appears that amendments made to the exposure draft, based on the comments provided in the interested party comment letter, appear to capture the spirit of the interested party
feedback. Mr. Finnell requested that the guidance explaining that two management letters may be prepared be moved after the paragraph describing how to determine the significance of the findings. Mr. Finnell suggested that it would be clearer to discuss the difference in issues to be reported and because of that, it may be appropriate to prepare two different letters. There were no objections, and therefore, the suggestion was accepted and incorporated into the proposed revisions.

Mr. Finnell asked if it was common for there to be a conflict of interest with the management at the legal entity level that would necessitate sending a management letter to a level above the legal entity. Ms. Bernard said that there are circumstances when many or all individuals of the management team are also members of the board of directors. In this case, it would be beneficial to be able to send the management letter to a higher level within the organization to ensure independence in considering the communication provided and action taken, if needed. Joe Zolecki (Blue Cross Blue Shield Association—BCBSA) agreed with commentary provided by Mr. Finnell.

Mr. Arfanis requested that additional guidance be added to indicate that the content and recipient(s) of the management letter(s) is at the discretion of the examination team. There were no objections, and therefore, the suggestion was accepted and incorporated into the proposed revisions.

Ms. Bernard said that enhancements will be added to the Financial Exam Electronic Tracking System (FEETS) to all regulators to proactively share the management letter with each other. Changes are expected to be implemented early 2020. Mr. Snow asked if management letters shared in FEETS will be kept confidential. Ms. Henning said that FEETS is a regulator-only tool. Furthermore, it is expected that a management letter is uploaded to FEETS or an explanation is provided regarding why a management letter was not uploaded. Additional language is anticipated to be added to indicate that the viewer should contact the domestic regulator with any questions or to request a management letter if it is not uploaded to FEETS. Mr. Snow asked if all FEETS users would have access to view the management letter. Ms. Henning said that all FEETS users have access to view all information in the application.

c. Exhibit V and Exhibit AA Enhancements

Ms. Bernard said NAIC staff developed proposed revisions to Exhibit V – Overarching Prospective Risk Assessment and Exhibit AA – Summary Review Memorandum to enhance the documentation prospective risk assessment. Changes include: 1) revised column headings to clarify the purpose of each column; 2) additional columns to align the assessment made on Exhibit V with the communication used on the SRM/IPS when transitioning information between exam and analysis; and 3) updated the examples shown on Exhibit V. Minor changes to Exhibit AA – Summary Review Memorandum were made to include definitions and considerations related to the trend and risk assessment level for identified risks. Ms. Bernard said no comment letters were received regarding this proposed change.

Mr. Arfanis made a motion, seconded by Ms. Andersen, to adopt the guidance related to 1) Troubled Insurance Companies; 2) Management Letters, as amended; 3) Exhibit V – Overarching Prospective Risk Assessment; and 4) Exhibit AA – Summary Review Memorandum (Attachment Five-B)

3. Discussed 2019 Project Listing

Bailey Henning (NAIC) said that most of the items on the project listing have been completed. Ms. Henning said that volunteers from the Technical Group have met to discuss updates to the reserves examination repositories and that work is ongoing. Ms. Henning said that the volunteers expect to wrap up their work and provide a recommendation to the Technical Group to consider in spring 2020. Ms. Henning also stated that the Technical Group will need to consider the impact of changes to the NAIC Credit for Reinsurance Model Law and Regulation (#785/786) on the guidance provided in the Handbook.

4. Received an Update on IT Examination (E) Working Group Projects

Mr. Romero informed the Technical Group that the IT Examination (E) Working Group recently adopted revisions related to: 1) language used when documenting the conclusions reached as a result of the information technology (IT) review; 2) considerations when using the work of third parties; and 3) considerations when using company-prepared cybersecurity self-assessments to supplement the IT review.

Having no further business, the Financial Examiners Handbook (E) Technical Group adjourned.
The Financial Examiners Handbook (E) Technical Group of the Examination Oversight (E) Task Force met via conference call Sept. 12, 2019. The following Technical Group members participated: Susan Bernard, Chair, and Laura Clements (CA); Richard Ford (AL); William Arfanis (CT); N. Kevin Brown (DC); Grace Kelly (MN); Levi Nwasoria (MO); Lindsay Crawford (NE); Colin Wilkins (NH); John Sirovetz (NJ); Joel Bengo (NV); Tracy Snow (OH); Jamille Jaffurs (OK); Melissa Greiner (PA); John Jacobson (WA); and John Litweiler (WI).

1. **Adopted Handbook Guidance**

   a. **Salary Range Guidelines**

   Ms. Bernard said the Risk-Focused Surveillance (E) Working Group referred proposed revisions regarding salary range guidelines for the Technical Group to consider. The proposed salary range guidelines were developed based on a survey of the states, as well as research to understand compensation practices in similar job roles, such as public accounting, private industry and other areas of financial regulation.

   To avoid causing undue burden to the states using the existing salary and per diem guidance within the *Financial Condition Examiners Handbook* (Handbook), the Working Group recommends that the existing guidance be retained, with explanatory language describing its purpose and expectations. The Working Group also recommends that each set of salary guidelines be maintained, with annual updates to the existing salary and per diem guidelines and biennial updates to the proposed salary range guidelines.

   Ms. Bernard said no comment letters were received regarding this proposed change.

   b. **Interviews**

   Ms. Bernard said NAIC staff developed proposed revisions to address a referral received in 2018 from the Risk-Focused Surveillance (E) Working Group regarding takeaways from the 2018 Exam Peer Review sessions. These revisions attempt to emphasize the importance of customizing questions that are asked during C-level interviews in examination planning. The proposed revisions also suggest that the chief risk officer be among the first C-level individuals to be interviewed, when possible, as the information obtained through that interview can help inform subsequent interviews. NAIC staff also developed a new template for interviewing a chief marketing officer. This template provides possible questions that the exam team may consider when conducting this interview.

   Ms. Bernard said two comment letters were received regarding these proposed changes. Ms. Clements said the comment letter that California submitted suggested additional language to clarify that information obtained during each interview could be used to tailor subsequent interviews. Ms. Bernard said these suggestions were incorporated as friendly amendments.

   A comment letter that Tom Finnell (America’s Health Insurance Plans—AHIP) submitted suggested additional language to clarify specific questions on the interview template for the chief marketing officer. These minor revisions were accepted as friendly amendments. Ms. Bernard said that other comments provided in the letter related to items already covered in other sections of the Handbook and, therefore, were not incorporated. Mr. Finnell thanked the Technical Group for considering the comment letter provided.

   Mr. Arfanis made a motion, seconded by Mr. Nwasoria, to adopt the guidance related to salary range guidelines and C-level interviews (Attachment Five-A1). The motion passed unanimously.
2. Exposed Handbook Guidance

a. Troubled Insurance Companies

Ms. Bernard said NAIC staff developed proposed revisions to incorporate considerations when examining a troubled or potentially troubled insurance company in response to a referral from the Financial Analysis (E) Working Group. The proposed revisions provide guidance regarding specific key elements from the Troubled Insurance Company Handbook, including communication expectations for companies that are troubled or potentially troubled, and pre-receivership considerations. Ms. Bernard said the referral also requested consideration of guidance regarding the priority rating framework. However, because existing guidance addresses the priority framework, no additional changes were made.

b. Management Letters

Ms. Bernard said NAIC staff developed proposed revisions to guidance for management letters in response to a referral from the Chief Financial Regulator Forum. The proposed revisions clarify that there may be circumstances in which the insurance department provides the management letter to a different level within the holding company structure. Situations when this may be appropriate include when the examination team wishes to issue a group management letter covering multiple entities and when a board of directors with members independent of management exists above the legal entity level.

Ms. Bernard said the referral also requested that the Technical Group consider whether the management letter issued as part of a financial examination should be proactively shared among the states using the Financial Exam Electronic Tracking System (FEETS). Ms. Bernard said that FEETS implementation is pending and asked NAIC staff to continue to monitor the status of implementation.

c. Exhibit V – Prospective Risk Assessment and Exhibit AA – Summary Review Memorandum

Ms. Bernard said the referral regarding 2018 Exam Peer Review takeaways also suggested that the Technical Group consider the format of Exhibit V – Prospective Risk Assessment. The referral indicated that peer review attendees thought the format of the exhibit created confusion and did not appropriately emphasize the importance of the risks that should be addressed using the exhibit. Proposed revisions to the exhibit include revising the columns and column headers to more clearly indicate the expected documentation and aligning the exhibit more closely with the Summary Review Memorandum (SRM) and the Insurer Profile Summary (IPS). The examples provided in the Exhibit were also updated to reflect the proposed format changes. Ms. Bernard said that proposed guidance for the second part of the exhibit clarifies that common areas of concern are included for reference only. Examiners are not required to included risks for each common area of concern, nor are they required to provide a rationale for not identifying a risk for each area of concern. Proposed revisions also include using the Own Risk and Solvency Assessment (ORSA) filing, when available, as a source for identifying potential prospective risks. Ms. Bernard said that Exhibit AA – Summary Review Memorandum was revised to include definitions and considerations for determining the trend and risk assessment level of identified risks.

Mr. Finnell said that examiners may need to engage a specialist to assist in performing some of the procedures that are illustrated within the examples on Exhibit V. He also said that examiners should attempt to test mitigation strategies in place at the insurer before conducting independent testing, as some of the testing can become very specialized and require additional resources. Ms. Bernard agreed that examiners are expected to first gain an understanding of the mitigation strategies and controls in place, and only perform additional independent testing if warranted based on the risk assessment.

The Technical Group agreed to expose the proposed revisions to: 1) Troubled Insurance Companies; 2) Management Letters; 3) Exhibit V – Overarching Prospective Risk Assessment; and 4) Exhibit AA – Summary Review Memorandum for a 30-day public comment period ending Oct. 14.

3. Received an Update on Reserves/Claims Handling Repository Project

Bailey Henning (NAIC) said that a group of volunteers from the Technical Group has now reviewed two of the three reserves/claims handling repositories, using input provided by the Life Actuarial (A) Task Force, the Health Actuarial (B) Task Force and the Actuarial Opinion (C) Working Group. She said the volunteers plan to meet at the end of September to discuss the remaining repository. After each repository has been reviewed, the volunteers expect to meet at least once more before providing a recommendation of changes for the Technical Group to consider. Miguel Romero (NAIC) said that it is possible
that this project may extend into 2020.

4. **Received an Update on IT Examination (E) Working Group Projects**

Mr. Romero informed the Technical Group that the IT Examination (E) Working Group plans to meet via conference call Sept. 26 to consider adopting revisions related to: 1) language used when documenting the conclusions reached as a result of the information technology (IT) review; 2) considerations when using the work of third parties; and 3) considerations when using company-prepared cybersecurity self-assessments to supplement the IT review. Mr. Romero said that due to the technical nature of the subject matter, the IT Examination (E) Working Group has authority to adopt guidance directly into the Handbook. Therefore, anybody wishing to be part of the discussion should attempt to participate in the upcoming conference call.

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

This section of the Handbook addresses the following subjects:

A. Examiner Definitions and Qualifications

B. Authority and Responsibility of the Examiner-In-Charge

C. Duties and Responsibilities of Non-Domestic Participating Examiners

D. Salary and Per Diem Guidelines

E. General Salary Guidelines

Note: The guidance in A.-D. was initially developed for zone examinations but is also used as a reference point for states in setting compensation for their Department. In contrast, the guidance in E. General Salary Guidelines is intended to provide flexibility in setting salary expectations for purposes of all staff performing Risk-Focused Surveillance.

E. General Salary Guidelines

The compensation guidelines in this section of the Handbook were developed in recognition of the importance of compensation particularly as it affects an Insurance Department’s ability to hire and retain well-qualified employees. The guidelines were developed based on surveys of examiner pay across Insurance Departments, as well as external comparisons to other similar professions, including other financial regulators, internal auditors and external auditors. In using the information below, the following are brief descriptions of the associated positions listed:

Financial Examiner
Financial Examiners are responsible for performing tasks in accordance with the Risk-Focused Examination approach under the supervision of the Examiner-In-Charge. The Financial Examiner is responsible for investigating and analyzing insurance company risks, policies, procedures, and controls in an attempt to assist the Insurance Department in its responsibility to assess and monitor the current financial condition and prospective financial solvency of insurance companies.

Senior Financial Examiner
Senior Financial Examiners are responsible for performing tasks in accordance with the Risk-Focused Examination approach under the supervision of the Examiner-In-Charge. The Senior Financial Examiner is responsible for investigating and analyzing insurance company risks, policies, procedures, and controls in an attempt to assist the Insurance Department in its responsibility to assess and monitor the current financial condition and prospective financial solvency of insurance companies. Senior Financial Examiners may also be asked to provide guidance and support to Financial Examiners and may assist in all areas of examinations, as requested.

Examiner-In-Charge (EIC)
EIC’s are responsible for the execution of the Risk-Focused Examination approach. The EIC is responsible for ensuring the exam approach is appropriately designed to investigate and analyze insurance company risks, policies, procedures, and controls in an attempt to assist the Insurance Department in its responsibility to assess and monitor the current financial condition and financial solvency of insurance companies. The EIC provides guidance to Financial Examiners and Senior Financial Examiners, conducts detailed reviews of examiner work and ensures a proper flow of communication with company management and Department officials, as appropriate.

Supervising & Assistant Chief Examiner
A Supervising or Assistant Chief Examiner is responsible for supervising EIC’s on examinations. This person provides input on technical matters, acts as a reviewer of the work performed by the EIC and ensures that examination work is an appropriate execution of the Risk-Focused Examination approach.

Chief Examiner
This position is responsible for overall examination staff performance & development, the ongoing scheduling of financial examinations and general communications regarding the examinations of regulated entities. This position should work under the general direction of a Commissioner or Deputy Commissioner and should oversee a consistent Risk-Focused Examination process across the Department.

Use of Salary Tables:

The salary tables included below generally require certain adjustments before being applied by a State or Jurisdiction in setting examiner compensation. Factors to consider in setting examiner compensation include:

- Specific job responsibilities and expectations
- Location or market-based adjustments
- Complexity of industry
- Specialization requirements (e.g. Reinsurance/Investment/IT Specialist)
Suggested Salary Ranges:

<table>
<thead>
<tr>
<th>Position</th>
<th>Low end</th>
<th>High end</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial Examiner</td>
<td>$46,000</td>
<td>$75,000</td>
</tr>
<tr>
<td>Senior Financial Examiner</td>
<td>$57,000</td>
<td>$90,000</td>
</tr>
<tr>
<td>Examiner-In-Charge (EIC)/Supervisor/Assistant Chief Examiner</td>
<td>$80,000</td>
<td>$130,000</td>
</tr>
<tr>
<td>Chief Examiner</td>
<td>$92,000</td>
<td>$150,000</td>
</tr>
</tbody>
</table>

Note: The data above is based on a national average and is not appropriate to be applied to all locations without consideration of market and cost of living variances.
PHASE 1 – UNDERSTAND THE COMPANY AND IDENTIFY KEY FUNCTIONAL ACTIVITIES TO BE REVIEWED

In Phase 1 of a risk-focused examination, key activities will be confirmed or identified using background information gathered on the company from various sources. Some of this information will already have been available in the department prior to the initial planning meeting, or can be obtained from the company’s internal audit department or external auditors. A Phase 1 goal is to gather any additional or current information necessary to begin a risk-focused examination. Sources of information may include organizational charts, filings required by sections 302 and 404 of the Sarbanes-Oxley Act of 2002 (where applicable), interviews with senior management, or other publicly available information.

To ensure the appropriate risk-focused examination scope, it is important to identify the key functional activities (i.e., business activities) of the company. Information gathered by understanding the company, the company’s corporate governance structure, and assessing the company’s audit function will form the basis for determining key activities.

Essential to executing the risk-focused surveillance process is interviewing executive management and possibly board members of the company to identify key activities and risks. Risks identified through these interviews and each part of Phase 1 should be documented on Exhibit CC – Issue/Risk Tracking Template or a similar document to ensure they are carried through the remaining phases of the examination. Examiners and company officials should attempt to maintain an ongoing dialogue to assist the examiners in understanding the company and identifying key functional activities. It is also critical for the examination team to understand and leverage the company’s risk management program; that is, how the company identifies, controls, monitors, evaluates and responds to its risks. For companies required to submit an Own Risk and Solvency Assessment (ORSA) summary report to the lead or domestic state, the report provided by the company may be a useful tool in this evaluation.

The discipline and structure of risk management programs vary dramatically from company to company. “Best practices” are emerging for risk management programs and more companies are appointing chief risk managers whose responsibilities go well beyond the traditional risk management function (the buying of insurance). The Committee of Sponsoring Organizations (COSO) has published internal control standards that are widely-held, although not required, in many industries and has released an Enterprise Risk Management Integrated Framework, which is anticipated to be incorporated by several entities, as well as guidance to apply the integrated framework and internal control standards to small public companies. The examination team should evaluate the strength of the company’s risk management process, which can include a “hind-sight” evaluation of why a particular negative surprise or event occurred (i.e., why was it not identified in the current risk management program of the company).

One crucial aspect to a successful planning process is the tailoring of planning procedures to the company under review. As the exam team learns about risks, subsequent planning procedures should be tailored to ensure they provide further information on the risks already identified. For instance, if after meeting with the Department’s analyst, the examination identifies a risk related to the company’s planned expansion of business into new jurisdictions, subsequent procedures performed in planning (i.e. C-Level Interviews, review of company ERM, etc.) should be tailored to include consideration on the risk.

There are five parts to Phase 1 that are key components of performing a risk assessment, the results of which drive the direction of the risk-focused examination: (1) Understanding the Company; (2) Understanding the Corporate Governance Structure; (3) Assessing the Adequacy of the Audit Function; (4) Identifying Key Functional Activities; and (5) Consideration of Prospective Risks for Indications of Solvency Concerns. The Risk Assessment Matrix (Exhibit K), the tool developed to serve as the central location for the documentation of risk assessment and testing conclusions, should be updated with the identified key activities of the company after the
examiner is able to obtain an understanding of the company and corporate governance structure. The five parts of Phase 1 are discussed as follows:

A. Part 1: Understanding the Company
B. Part 2: Understanding the Corporate Governance Structure
C. Part 3: Assessing the Adequacy of the Audit Function
D. Part 4: Identifying Key Functional Activities
E. Part 5: Consideration of Prospective Risks for Indications of Solvency Concerns

A. Part 1: Understanding the Company

Step 1: Gather Necessary Planning Information

Meet with the Assigned Analyst

Gathering information becomes is the first step in gaining an understanding of the company. While general information may have been requested from the company during examination pre-planning through use of Exhibits B and C, the examination team should determine what other information is already available to the department before making additional information requests. To do so, the examination team should meet (in-person or via conference call) with the assigned financial analyst (and/or analyst supervisor) prior to requesting additional information for use in examination planning. An email exchange, in and of itself, is not deemed sufficient to achieve the expectation of a planning meeting with the assigned analyst.

In addition to gaining an understanding of the information already available to the department, the meeting with the analyst should focus on the company’s financial condition, prospective risks and operating results since the last examination. The analyst should be asked to discuss risks and concerns highlighted in the Insurer Profile Summary (IPS)/Group Profile Summary (GPS) and to describe the reasons for unusual trends, abnormal ratios and transactions that are not easily discernible. The analyst may also request specific matters or concerns for verification and review during the financial examination. To summarize the input received from financial analysis, the examination team should document risks identified by the analyst for further review on the examination and post significant items to Exhibit CC – Issue/Risk Tracking Template for incorporation into the examination process. When possible, the examiner should meet with the department analyst prior to scheduling “C”-Level interviews with company personnel. Meeting with the analyst can help the examiner gain a basic understanding of the company, which can then be used in planning and scoping the interview process and subsequent planning procedures.

If the company under examination has redomesticated since the prior exam, the department analyst will typically take a primary role in communicating with the prior domestic regulator in order to adequately transfer regulatory insights accumulated over years of oversight. The department analyst would then share these insights with the examiner in charge during the examiner/analyst meeting during the planning phase of the examination. This communication may include a discussion of the Insurer Profile Summary and key risks, the supervisory plan, the former regulator’s assessment of Senior Management, the Board of Directors and corporate governance, and other relevant solvency monitoring information. If after meeting with the analyst the examiner requires additional information or further clarification, the examiner may consider contacting the former regulator.

The avoidance of redundancy between analysis and examination processes is of critical importance for an enhanced and more efficient overall regulatory process that will benefit both regulators and industry. An efficient regulatory process fosters clarity and consistency, which results in a better understanding of how individual insurers operate across the different aspects of the regulatory spectrum, including the areas of financial examination, financial analysis and other solvency-related regulation.

By utilizing information and input provided by the analysts, the examination team can request updates to existing information available to the department rather than duplicating requests for information already provided to the
analyst. This process eliminates the need for examiners to redevelop the financial analysis information in the examination workpapers so that examination resources may instead be used to update the information while on-site at the insurer. Similar to the benefits of reviewing and using external or internal auditor workpapers, examiners use of detailed financial analysis workpapers in the examination files should result in examinations being more efficient and streamlined.

B. Part 2: Understanding the Corporate Governance Structure

This section’s purpose is to assist the examiner in documenting the understanding and assessment of an insurer’s board of directors and management. A favorable overall assessment of governance does not, by itself, serve to reduce the scope or extent of examination procedures; rather, specific governance controls need to be assessed for their adequacy in managing specific risks, in conjunction with other controls designed to manage the same. See Exhibit M – Understanding the Corporate Governance Structure for additional guidance in understanding the corporate governance structure of the company. When completing this assessment, the examiner should utilize the Corporate Governance Annual Disclosure (CGAD), which is required to be filed with the Department of Insurance (DOI) annually in accordance with Corporate Governance Annual Disclosure Model Act (#305) and Corporate Governance Annual Disclosure Model Regulation (#306). The CGAD provides a narrative description of the insurer’s or insurance group’s corporate governance framework and structure and may enhance examination efficiencies when leveraged. Examiners should inquire of the financial analyst to gain an understanding of and leverage the analyst’s work in assessing the company’s corporate governance.

Management

Interviews with senior management at the “C” level should be used at the beginning of the examination or at any time during the examination as necessary. “C” level management may include the CEO (Chief Executive Officer), CFO (Chief Financial Officer), COO (Chief Operating Officer), CIO (Chief Information Officer), CRO (Chief Risk Officer), Controller, Chief Actuary or other appropriate executive-level management. Examiners should consider the size of the organization in determining which individual(s) would provide the examiner with the most beneficial information regarding the company for the stage of the examination. This interview process is a key step in the “top down” approach, beginning with senior management and then drilling down through the various levels of management to obtain a thorough understanding of the organization to assist in scoping the examination. Topics of these high-level interviews should include, but not be limited to (1) corporate strategic initiatives; (2) external/environmental factors of concern to management; (3) political/regulatory changes that might affect business; (4) competitive advantages/disadvantages; (5) management of key functional activities; and (6) how management establishes and monitors the achievement of objectives.

The examiners should consider which individuals should be interviewed and the sources of data to be evaluated to complete each planning step. The examiners should also consider the order in which the interviews are conducted as information gleaned from certain “C”-level individuals can assist in providing additional information to tailor subsequent interviews. In order to select the individuals to interview, the examiners should obtain an organizational chart from the company and compile a list of potential interviewees. In addition to accounting department personnel, the interview list should include managers of key functional business units (depending on the company structure, lines of business or revenue centers might be more appropriate). Because all companies have different organizational structures, it is important that the interview schedule and the examination plan match the company. Examiners should form their objectives, or what they want to get out of the interview, prior to conducting the interview. In order to accomplish this, the examiner should have a basic knowledge of the job function of the person that they are interviewing. This will allow the examiner to ask relevant questions and get the most information possible in one setting, as it may be difficult to coordinate multiple contacts with a “C”-level interviewee or a member of the board of directors. The information contained in Exhibit Y – Examination...
Interviews provides some basic questions that an examiner may consider when conducting “C”-level interviews. Exhibit Y, however, does not provide examples for functional positions at the insurer (e.g., claims handling, sales and marketing, etc.). These functional interviews are typically best documented in a narrative format and may be done in conjunction with walkthroughs or other control documentation procedures. Exhibit CC – Issue/Risk Tracking Template or a similar document may should be used in conjunction with Exhibit Y to document significant risks or concerns accumulated during the interview process.

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EXHIBIT Y
EXAMINATION INTERVIEWS

Overview

Interviews are a useful examination tool to gather information about key activities, risks and risk mitigation strategies. Employees can also provide information on fraudulent activity within the company. It is critical for the examination team to understand and leverage the company’s risk management program; i.e., how the company identifies, controls, monitors, evaluates and responds to its risks. The discipline and structure of risk management programs vary dramatically from company to company. Interviews should be performed in the early stages of the examination so that regulators can adjust their procedures accordingly. An examiner can perform alternate, additional or fewer detail and control tests as a result of interviews with the company.

Interviews should be conducted with key members within management of the company, as well as members of the board of directors, audit committee, internal/external auditors and any other employees deemed necessary. These interviews can be used at the beginning of the examination or at any time during the examination, as necessary. In order to conduct a productive interview, the examiner should have However, a basic understanding of the company is essential to obtain prior to commencing the interviews process. When possible, the examiner should meet with the department analyst prior to scheduling interviews with company personnel to assist in gaining this basic understanding. Examiners should continue to tailor each interview as information is learned about the company throughout the planning process.

Examiners should consider the size and complexity of the organization in determining which individuals to interview. This interview process is a key step in the “top–down” approach, beginning with senior management and then drilling down through the various levels of management to obtain a thorough understanding of the organization to assist in scoping the examination. In order to select the individuals to interview, the examiners should obtain an organizational chart from the company and compile a list of potential interviewees. Interviews of board members and senior company management should be conducted by examiners who possess the appropriate background and training. The examiner should also carefully consider the order of interviews as information gleaned from certain “C”-level individuals can inform subsequent interviews. For example, the Chief Risk Officer (CRO) is uniquely positioned to have an awareness of the various risks facing the company from multiple perspectives. The information obtained through an interview with the CRO can help the examiner have a greater understanding of the key risk areas of the company, which can then be used to further customize subsequent interviews as well as determine which additional members of management should be interviewed. While it can be challenging to coordinate the interview schedule with company personnel at this level, examiners are encouraged to attempt interviewing the CRO as early in the interview process as possible.

Interviews should be performed in person, if possible. This allows the interviewer to receive both verbal and nonverbal communication. The interviews should be kept confidential when possible; however, if a significant fraud or other pertinent issue was discovered through the interviews, the regulator has a duty to report the conflict to the appropriate officials.

The examiner should conduct the interview in a location where both parties are free to talk openly. The examiner should ask relevant questions, with the most general questions posed first as building blocks for additional conversation. The examiner may want to consider alternating between open-ended questions (e.g., “Explain to me how this process works.”) vs. closed-ended questions (e.g., “How many claim processors do you have in your department?”) to obtain the information. Open-ended questions are generally better suited for explanation and processes, while closed-ended questions are better suited to obtain concise information. The examiner should be prepared, listen carefully and focus on the speaker’s entire message, as well as the non-verbal cues expressed during the interview process.
Significant risks and concerns identified through completion of the examination interviews should be adequately addressed within the examination workpapers. As such, all significant risks identified by the examiner during the interview process should be recorded in a central location for tracking purposes, such as Exhibit CC – Issue/Risk Tracking Template or a similar document.

Because information obtained from the interview serves as important evidence in the examination process, the examiner should develop techniques to plan, conduct, document and consider interview information. Although interviews play a key role in gaining useful insight into company operations, interviews alone are not sufficient exam evidence and should be corroborated with other exam documentation to evaluate the accuracy of the information.

Sample Interview Questions for the Chief Marketing Officer

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

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

Reporting Structure
- Describe the reporting structure of the marketing function, including to whom you report, as well as those reporting to you.
- Is there a marketing committee?
  - How is it organized and who are its members?
  - How are differences resolved?
- Describe your interaction with the CFO/CEO/BOD.
  - Do you provide them with any specific reports?

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

Risk Areas
- How are key risks faced by the company identified and monitored?
  - What are the key prospective risks the company faces?
- How are these risks communicated to senior management and throughout the company?
- What is the current marketing strategy? Describe any changes over the past five years.
Risk Mitigation Strategies (Internal Controls)
  • What is the formal procedure for reporting on risk management to senior management and the board?

Corporate Strategy
  • Give a general description of the company’s marketing philosophy.
  • Where is the company headed strategically? What type of plan is in place to implement this strategy? How does the strategy impact activities within your department?
  • Explain strengths or weaknesses of the company, as well as opportunities and threats the company is facing, and how the company’s marketing strategy and tactics is responding to each.
  • Explain what types of key tools or reports you utilize to evaluate marketing decisions.
  • What key measures do you assess to evaluate the company’s performance and competitive position?

Other Topics
  • Explain any significant turnover in the marketing department.
  • Explain the distribution channels used by the company.
  • What is the compensation/commission structure for each distribution channel?
III. GENERAL EXAMINATION CONSIDERATIONS

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

A. General Information Technology Review
B. Materiality
C. Examination Sampling
D. Business Continuity
E. Using the Work of a Specialist
F. Outsourcing of Critical Functions
G. Use of Independent Contractors on Multi-State Examinations
H. Considerations for Insurers in Run-Off
I. Considerations for Potentially Troubled Insurance Companies
J. Comments and Grievance Procedures Regarding Compliance with Examination Standards

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I. Considerations for Potentially Troubled Insurance Companies

A troubled insurance company is broadly defined as an insurance company that is either in or is moving towards a financial position that subjects its policyholders, claimants and other creditors to greater-than-normal financial risk, including the possibility that the company may not maintain compliance with the applicable statutory capital and/or surplus requirements (Troubled Insurance Company Handbook). The “Prioritization Framework” as discussed in the NAIC’s Financial Analysis Handbook identifies troubled companies as Priority 1. The Troubled Insurance Company Handbook provides a number of insights to assist in enhancing a state’s monitoring and surveillance, and it outlines several regulatory actions available to Departments of Insurance (DOIs). In situations in which an examination is being planned for a troubled insurance company (i.e., Priority 1 company), the NAIC’s Accreditation Program Manual (Part B3: Department Procedures and Oversight) indicates that “the department should generally follow and observe procedures set forth in the NAIC Troubled Insurance Company Handbook.” However, regulators may also consider leveraging the insights in the Troubled Insurance Company Handbook for Priority 2 companies, which are defined in the Financial Analysis Handbook as “high-priority insurers that are not yet considered troubled but may become so if recent trends or unfavorable metrics are not addressed.”

The following guidance provides an overview of key elements to consider during an examination. Additional insights to assist in enhancing a state’s monitoring and surveillance of troubled insurance companies, including regulatory actions available to Departments of Insurance (DOIs), can be found in the Troubled Insurance Company Handbook.

Communication Expectations

If an examination is planned or ongoing for a troubled or potentially troubled company, or through the course of the examination the domestic regulator elevates the priority level of the company to troubled or potentially troubled, it is critical that the domestic regulator communicates proactively and timely with other impacted state insurance regulators. It is also important that the non-domiciliary state communicate with the domestic regulator prior to taking any action against the insurer. This can be particularly important if the corrective action plan implemented by the domestic regulator depends on continued operations of the insurer in other states. Depending on the circumstances, it may also be appropriate to communicate certain information with other parties, such as other regulatory bodies, company management, and state guaranty funds. Establishing a coordinated
communication system among the relevant parties will help facilitate the domestic regulator’s surveillance of the troubled company.

The timeliness of communication with other regulators should be commensurate with the severity of the event and should include information about the troubled company’s situation and the proposed corrective action. It may also include a request for other jurisdictions to assist in implementation of the plan. When determining which states to notify, the department may consider those in which the company 1) has a significant amount of written, assumed or ceded insurance business; 2) has significant market share; 3) is licensed; 4) has affiliates; 5) utilizes fronting entities; 6) has pooled companies; and 7) is seeking to write business or obtain a license. If it is reasonably anticipated that corrective plans will not prevent a finding of insolvency or insolvency is reasonably possible, advance communication to the guaranty funds is critically necessary for a successful transition to liquidation. If the guaranty funds are notified in a timely manner, they may be able to provide additional guidance and assistance in preparing the company for liquidation.

Pre-Receivership Considerations

Depending on the circumstances of the troubled company’s situation, the department may determine that the appropriate course of action is to place the company in receivership. There are several steps the department can take to ensure a smooth transition to receivership, should that be necessary. Having a thorough understanding of the company’s rights and ownership of its assets, as well as its liabilities and obligations can help the department manage the possible transactions that could occur if the company is placed in receivership. It may also help the regulator understand if inappropriate transactions occur in anticipation of receivership, such as preferential payments to related entities and payment of management bonuses or expense reimbursements. As part of the corrective plan, the department may consider requesting implementation of controls surrounding the troubled company’s operations. For instance, it may be necessary for management to establish controls around acceptance of new business or new commitments by the company, as well as recordkeeping requirements if the insurer is involved with reinsurers.

If an examination is planned or ongoing for a troubled or potentially troubled company, the examination should increase its review of risks and controls surrounding financial reporting processes in the areas discussed above. For example, the exam may have a greater focus on the following areas:

- Gaining an understanding of the location (i.e., bank accounts, deposits, custodial accounts, letters of credit, etc.) and ownership (i.e., funds held with reinsurers, intermediaries, MGAs/TPAs, etc.) of company assets;
- Gaining an understanding of possible encumbrances on company assets that may be triggered if the financial position of the company continues to deteriorate;
- Gaining an understanding of the provisions within various agreements that company has entered into (i.e., reinsurance agreements, agreements with service providers, investment advisors, etc.) that could be impacted by being placed into receivership;
- Reviewing transactions involving the movement of company assets;
-Identifying primary responsibility for obligations and liabilities such as tax payments, pension plan contributions, pledges of assets, etc.; and
- Additional testing to ensure the completeness of policy and claims data.

If receivership or liquidation is triggered, and assets are transferred to the receiver or guaranty fund to settle obligations, it is important that the company’s data be maintained in such a format to ensure that policies can continue to be maintained and claims can continue to be paid. For example, the company should have the ability to export its claims data through a defined format (Uniform Data Standards—UDS) that would allow the data to be received and utilized by a third-party guaranty fund. Therefore, the examination may include additional
procedures as part of the IT review to identify and locate data storage and processes, understand the format of the data, and ensure proper functionality exists for timely and efficient export of policy and claims data in the event of a receivership.
EXHIBIT V – OVERARCHING PROSPECTIVE RISK ASSESSMENT

Background

The concept of risk on a risk-focused examination encompasses not only risks as of the examination date, but also risks that extend or commence during the time in which the examination was conducted, as well as risks that are anticipated to arise or extend past the point of examination completion. As such, consideration of "prospective risks" (including moderate or high residual risks existing at the balance sheet date that will impact future operations, risks anticipated to arise due to assessments of company management and/or operations, or risks associated with future business plans of the company) is an intrinsic element of a risk-focused examination and should occur throughout all phases of the examination process.

Use of this Exhibit

In completing this exhibit and documenting the examiner’s consideration of prospective risks throughout the examination process, the examiner should conduct an evaluation and, if possible, conduct examination procedures on the noted prospective insolvency risks to assess the degree of risk present and recommend future monitoring. Throughout the examination process and at the conclusion of the exam, the examiner should communicate with the department’s financial analysts to keep them informed of the identified prospective risks and examiner assessments. The branded risk classifications, risk assessment level and trend and associated rationale should be used to summarize prospective risks identified for communication to the analyst via Exhibit AA—Summary Review Memorandum (SRM). This communication should include relevant details obtained during the examination that will enhance the ongoing monitoring of the company.

In conducting examinations of insurers that are part of a holding company group, it is important to note that many critical prospective risks may occur at the holding company level. The exam team should seek to coordinate the identification and assessment of prospective risk in accordance with the exam coordination framework and lead state approach outlined in Section 1 of this Handbook. Where possible, in a coordinated examination, the lead state’s work on prospective risk should be utilized to prevent duplication of effort and to leverage examination efficiencies.

As discussed throughout this Handbook guidance, the consideration of prospective risks should occur throughout each phase of the examination process. If the examiner identifies a prospective risk that relates to one specific key activity of the company, this prospective risk should be documented in the corresponding risk matrix for that key activity and treated similarly to other identified risks. However, if the examiner identifies an overarching prospective risk (a prospective risk that does not relate to a specific key activity identified, or relates to more than one key activity identified), the examiner should utilize this exhibit to document the process to consider the investigation of the overarching prospective risks. Individual risks should either be addressed on Exhibit V or a key activity matrix, but not both.

By the end of Phase 1, the examiner should have a preliminary listing of overarching prospective risks included on Exhibit V – Overarching Prospective Risk Assessment. By the end of Phase 2, the list of risks on Exhibit V should be updated to include all significant overarching prospective risks identified on Exhibit CC – Issue/Risk Tracking Template.

Prospective risks may continue to be identified beyond Phase 1 and Phase 2, but all significant overarching prospective risks identified during later phases of the exam should continue to be documented and investigated on Exhibit V, regardless of the phase in which the risk was identified.

All of the instructions for the investigation of prospective risks on Exhibit V should be completed by the end of Phase 5. It is not required that the various steps to investigate prospective risks on Exhibit V directly coincide with the seven-phase exam approach, but it is recommended that examiners complete each step of Exhibit V as early in the exam as practical to ensure each risk identified is sufficiently tested and reviewed.
Exhibit V, Part One – Overarching Prospective Risk Testing Template

Examiners should use this worksheet to document a review and testing investigation of overarching prospective risks throughout the examination. Examiners may also use the examples provided on the template as a guide to assist in determining the nature and extent of the prospective risk review to be performed. Please Note: The risk mitigation strategies identified in the template are only examples, and the examiner should be aware that the insurer might use other strategies to mitigate the identified risk. Instructions for completing and documenting a review of prospective risk within the template are as follows:

<table>
<thead>
<tr>
<th>Template Column</th>
<th>Instructions for Completing</th>
</tr>
</thead>
<tbody>
<tr>
<td>Overarching Prospective Risk Identified</td>
<td>Based on the knowledge and understanding of the company obtained during the planning stages of the exam, document any overarching prospective risks identified.</td>
</tr>
<tr>
<td>Branded Risk Classification</td>
<td>For each identified risk, document the associated branded risk classification(s) from the following list: Credit (CR), Legal (LG), Liquidity (LQ), Market (MK), Operational (OP), Pricing/Underwriting (PR/UW), Reputation (RP), Reserving (RV), and Strategic (ST).</td>
</tr>
<tr>
<td>Risk Mitigation Strategies</td>
<td>Identify risk mitigation strategies in place at the insurer (if any) to address the prospective risk.</td>
</tr>
<tr>
<td>Testing to support mitigation strategies</td>
<td>Test the mitigation strategies identified by management. Consider both the design and operating effectiveness of the mitigation strategies as part of the procedures performed. Provide corroborating evidence and documentation to support the procedures performed.</td>
</tr>
<tr>
<td>Risk Exposure</td>
<td>Perform additional independent testing, if necessary, to further understand or address the risk. Testing may include evaluation of the company’s historical trends, stress testing of company exposures, or other additional procedures specifically tailored by the examiner based on the company’s risk. Attach and reference supporting workpapers.</td>
</tr>
<tr>
<td>Corroborating Evidence and Documentation</td>
<td>Provide corroborating evidence and documentation supporting the risk mitigation strategy. Attach and reference supporting workpapers.</td>
</tr>
<tr>
<td>Prospective Risk Assessment</td>
<td>Using professional judgment, determine the appropriate prospective risk level (High, Moderate or Low) after considering the nature of the risk and the company’s mitigation strategies. Provide a brief explanation regarding the prospective risk level determined.</td>
</tr>
<tr>
<td>Risk Assessment Level</td>
<td>Document the risk assessment level of the identified risk considering the test procedures performed (i.e., Significant, Moderate, or Minimal). Refer to Exhibit AA—Summary Review Memorandum for guidance on determining an appropriate risk assessment level.</td>
</tr>
<tr>
<td>Trend</td>
<td>Document the trend level of the identified risk considering the test procedures performed to indicate the direction the risk is moving (i.e., Increasing, Static, or Decreasing). Refer to Exhibit AA—Summary Review Memorandum for guidance on determining an appropriate trend level.</td>
</tr>
<tr>
<td>Rationale</td>
<td>Document the rationale for the trend and level of concern.</td>
</tr>
<tr>
<td>Ongoing Examination Procedures and Follow-Up</td>
<td>Document any additional procedures deemed necessary to be performed to further understand or address the risk. Document specific information to be communicated to the department analyst. Information should include specific procedures for continual monitoring, specific documents to obtain from the company, expected timelines for follow-up, and contact information. Describe the plan for follow-up, such as specific procedures for continual monitoring, communication with the analyst, limited-scope examinations, revisions to the Supervisory Plan or Insurer Profile Summary, etc.</td>
</tr>
</tbody>
</table>

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Exhibit V, Part Two – Common Areas of Concern

Examiners should use this as a reference guide to assist in identifying categories of prospective risk that may be relevant for review and inclusion on the Exhibit V, Part One. **Note:** examiners are not required to identify a risk from each category listed or provide a rationale for not identifying risks from the common areas of concern.
# PART ONE – OVERARCHING PROSPECTIVE RISK TESTING TEMPLATE

<table>
<thead>
<tr>
<th>Overarching Prospective Risk Identified</th>
<th>Branded Risk</th>
<th>Risk Mitigation Strategies</th>
<th>Investigate Risk Exposure</th>
<th>Risk Assessment Level</th>
<th>Trend</th>
<th>Rationale</th>
<th>Communicate Findings to Financial Analysis</th>
</tr>
</thead>
<tbody>
<tr>
<td>Example Prospective Risk 1:</td>
<td>ST RP</td>
<td>The company has processes in place to monitor and manage its financial performance in accordance with metrics considered significant by rating agencies. The company utilizes modeling to determine its economic and rating agency capital needs.</td>
<td>Reviewed financial reports for evidence of monitoring of rating agency performance measures and management review, noting that the company appears to be meeting its benchmarks (See wp A.1.4). Obtained and reviewed the economic capital calculation at 12/31/XX, noting that rating agency considerations are included in the process and that the company appears to hold capital in excess of the calculated amount. See A.1.5 for more information.</td>
<td>Moderate</td>
<td>Static</td>
<td>The company has product lines sensitive to a ratings decrease; however, it appears the company has appropriate controls and strategies in place to maintain strong ratings.</td>
<td>If a future rating downgrade occurs the DOI should meet to determine an appropriate course of action (e.g., limited scope exam).</td>
</tr>
</tbody>
</table>

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<table>
<thead>
<tr>
<th>Example Prospective Risk 2:</th>
<th>Mergers and acquisitions are part of the company’s growth strategy and incorporated into its 3-year strategic plan.</th>
<th>Obtained the most recent strategic plan and verified that it discussed the company’s plan for future mergers and acquisitions to support its strategic goals.</th>
<th>Moderate</th>
<th>Increasing</th>
<th>Although the company is actively involved with merger and acquisition activities, the exam team verified that this activity is part of its strategic plan and that an effective due diligence process is in place. However, given the significance of the last transaction and the stage of implementation, trend is rated as increasing.</th>
<th>The exam team is comfortable with the Company’s abilities with regard to mergers and acquisitions. However, if the analyst identifies changes to the Company’s strategic business plan, the DOI should meet to discuss whether the changes warrant action before the next examination date.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mergers, acquisitions and business divestitures are not successfully executed, resulting in excessive cost and/or regulatory concerns.</td>
<td>The company has a defined due diligence process which includes detailed procedures for mergers &amp; acquisitions, and business divestitures. The process is reviewed annually, making changes as needed, and approved by the Board of Directors and senior management.</td>
<td>Reviewed minutes from the 20XX annual Board of Directors meeting, noting that the mergers &amp; acquisitions process was reviewed and approved by the Board of Directors and Management. (See wp B.2.2)</td>
<td></td>
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<tr>
<td></td>
<td>The company has a mergers and acquisitions steering committee that meets quarterly to review analyses and forecasts prepared for planned and/or in-process mergers/acquisitions/divestitures.</td>
<td></td>
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<tr>
<td></td>
<td>The exam team also obtained documentation from the company’s most recent acquisition of XLX Corporation and confirmed that the due diligence process outlined in the M&amp;A policy was followed. (see additional detail regarding documents reviewed at B.2.PRG)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Reviewed minutes from Q1 and Q3 M&amp;A steering</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
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<td></td>
</tr>
<tr>
<td>Overarching Prospective Risk Identified</td>
<td>Investigate Risk Exposure</td>
<td>Risk Mitigation Strategies</td>
<td>Branded Risk</td>
<td>Communicate Findings to Financial Analysis</td>
<td></td>
<td></td>
</tr>
<tr>
<td>---------------------------------------</td>
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<td>---------------------------</td>
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<td>------------------------------------------</td>
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<td></td>
</tr>
<tr>
<td>Example Prospective Risk 3: The company is developing new products and may experience issues in pricing, underwriting, and reserving.</td>
<td>committee meetings and verified that financial details regarding the anticipated acquisition of FLH insurance company were discussed. (see wps B.2.3 and B.2.4).</td>
<td>Company analysts perform significant research regarding current market conditions and define products and market characteristics on a regular basis. Reports summarizing the findings are generated monthly.</td>
<td>The company has a verified history of successful product launches and the process for launching products going forward is fully vetted throughout the company.</td>
<td>The analyst will be asked to monitor financial ratios related to new lines of business and report any significant deviations to the exam unit.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>PR/UW</td>
<td>Reviewed the monthly market condition report, noting that the company has compiled detailed industry information regarding similar products and pricing, market demand, customer location, etc. (see A.2.1).</td>
<td>Reviewed the qualifications and background of the employees within the product development group specifically charged with developing, marketing and pricing new products. This group has significant experience in every aspect of product development.</td>
<td>The company has a group of individuals from departments across the company (legal, actuarial, marketing, financial, etc.) that compose an ad-hoc team specifically charged with background of the employees within the product development team, noting that all members have extensive experience in the many aspects of product development.</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

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<table>
<thead>
<tr>
<th>Overarching Prospective Risk Identified</th>
<th>Branded Risk</th>
<th>Risk Mitigation Strategies Investigate Risk Exposure</th>
<th>Risk Assessment Level</th>
<th>Trend</th>
<th>Rationale</th>
<th>Communicate Findings to Financial Analysis</th>
</tr>
</thead>
<tbody>
<tr>
<td>company strategy and new product development</td>
<td>Further, noted that this group maintains an action plan, approved by the board of directors, which details key procedures and areas of research necessary for product development, as well as a description of the various levels of review that occur throughout the product development process (see A.2.3). Obtained meeting minutes from the committee of the board of directors demonstrating discussion of potential new products, considerations for pricing, and board approval for the issuance of the new product (see A.2.4). Board meeting materials were also reviewed (A.2.5).</td>
<td></td>
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</tr>
</tbody>
</table>
PART TWO – COMMON AREAS OF CONCERN

The prospective risk categories provided within this exhibit are not designed to be an all-inclusive list and might not apply to all insurance companies under examination. The examiner’s understanding of the company obtained in Phase 1, including a review of the company’s Enterprise Risk Report (Form F) and/or ORSA Filing, should be utilized to determine whether risks in these categories might be applicable to the company. The company will likely face additional prospective risks that do not fit within the categories in this exhibit.

<table>
<thead>
<tr>
<th>Prospective Risk Category</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Merger and Acquisition Activity</td>
<td>If applicable, review the company’s process to identify and perform due diligence on potential acquisitions. In addition, consider reviewing the company’s process to integrate acquired entities and business into its systems.</td>
</tr>
<tr>
<td>Product Development</td>
<td>If applicable, review and assess the company’s process to identify, develop, price and market new products in accordance with the company’s strategy and business needs.</td>
</tr>
<tr>
<td>Legal and Regulatory Changes</td>
<td>If applicable, review how the company identifies, monitors and addresses changes to the legal and regulatory environment it operates within. For example, review the company’s processes in place to analyze the impact that health care reform could have on the company, including support for company projections and strategies for appropriateness.</td>
</tr>
<tr>
<td>HR/Personnel Risks</td>
<td>If applicable, review and assess the company’s HR processes to identify, mitigate and monitor risks related personnel management (including succession planning for critical positions) as well as hiring, managing, retaining and terminating personnel in accordance with company needs.</td>
</tr>
<tr>
<td>Strategic Planning</td>
<td>If applicable, review and assess the company’s processes for strategic planning to determine whether the company regularly analyzes its strengths and weaknesses, as well as opportunities and threats, on an ongoing basis. In addition, it might be appropriate to review the company’s process to update its overall business plan on a regular basis.</td>
</tr>
<tr>
<td>Compensation Structure</td>
<td>If applicable, review the company’s process for developing, monitoring and adjusting its compensation structure to ensure that employees are appropriately compensated without creating an incentive to misrepresent financial results.</td>
</tr>
<tr>
<td>Rating Agency Downgrade</td>
<td>If applicable, review the company’s process to monitor and prepare for potential adverse changes in its credit ratings. If a future rating agency downgrade is deemed likely, consider whether the company is adequately prepared to handle the results of such a downgrade.</td>
</tr>
<tr>
<td>Costs of Capital</td>
<td>If applicable, review the company’s access and ability to obtain capital, reinsurance and letters of credit, if necessary, to meet funding and risk diversification needs.</td>
</tr>
<tr>
<td>Business Continuity</td>
<td>If applicable, review the company's business continuity plan. Follow the steps outlined in Section 1, Part III.</td>
</tr>
<tr>
<td>Climate Change</td>
<td>If applicable, review the company’s process for identifying and monitoring risks resulting directly or indirectly from the impact of climate change risk.</td>
</tr>
</tbody>
</table>
The following is an illustration of how a summary review memorandum (SRM) may be set up to assist examiners in documenting the key issues and results of a risk-focused examination that should be shared with the Chief Examiner and the assigned analyst. The illustration also includes a high-level overview of the insurer’s holding company structure (if applicable) and how that structure affected exam coordination with other states. Additionally, the SRM includes discussion of the insurer’s governance and risk management practices, and a summary, by branded risk classification, of significant exam findings and/or concerns warranting communication. These findings may include overarching solvency concerns, examination adjustments, other examination findings, management letter comments, subsequent events and other residual risks or concerns the examiner may want to communicate to department personnel. The final sections, prioritization level and changes to the supervisory plan, provide discussion of the examiner’s overall conclusions regarding ongoing monitoring, including specific follow-up recommended to the analyst.

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

COMPANY NAME: EXAMINATION DATE:

EXAMINATION BACKGROUND

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

GOVERNANCE AND RISK MANAGEMENT

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

This section of the memorandum should be organized to address each of the nine branded risk classifications: Credit; Legal; Liquidity; Market; Operational; Pricing/Underwriting; Reputation; Reserving; and Strategic. If needed, an Other category may also be used. In documenting each assessment, consideration should first be given to the branded risk assessments provided by the analyst in the initial IPS. The examiner then summarizes the work performed during the examination to arrive at a final assessment for each classification. For those branded risk classifications that are not impacted by examination results and provide no additional information for the ongoing monitoring of the insurer, this can be noted without further explanation. For those classifications that are impacted, documentation in the summary should focus on new information uncovered during the course of the examination and should not duplicate the summary initially provided in the IPS. The summary for each classification should be prepared at a level of detail that will enable the analyst to update the existing IPS and understand the context for items that require additional follow-up or specific monitoring procedures. This may be done within the table format provided below, referencing other examination documents as necessary.

In documenting the key points for each branded risk classification, consideration should be given to the following areas, if deemed applicable:

- Prospective solvency concerns
- Examination adjustments
- Control/risk mitigation strategy issues
- Report findings and management letter comments
- Responses to issues raised by financial analysis
- Subsequent events
- Residual risks and concerns

Following the summary, the examiner should update the areas of concern, as needed, based on the information obtained during the examination and provide an overall assessment of minimal, moderate or significant concern for each branded risk classification. The SRM is a primary tool for communicating the results of an examination to the financial analysis function. Therefore, it is important that the examiners have the same understanding of the considerations going into the risk assessment level and trend. The following guidelines may be used to assist in assigning the risk assessment level and trend, when necessary. Additional guidance for selecting the risk assessment level and trend is available in the Financial Analysis Handbook.

Risk Assessment Level Considerations:

- **Significant**: The highest level of severity of risk from a solvency perspective. Risks assessed at this level require an elevated level of ongoing monitoring and/or regulatory action.

- **Moderate**: The medium level of severity of risk from a solvency perspective. Risks assessed at this level require routine ongoing regulatory monitoring and oversight and/or regulatory action.

- **Minimal**: The lowest level of severity of risk from a solvency perspective. Risks assessed at this level do not currently indicate a need for additional monitoring or regulatory actions.

Risk Assessment Trend Considerations:

- Consider trending within quantitative metrics to assist in determining the trend assessment
- Consider qualitative factors such as the insurer’s planned business strategies to address the risk
- Consider both historical/current and prospective/planned trends in exposure
If the examiner’s assessment is different from the original assessment documented in the IPS, the information summarized must provide sufficient detail to support the change. Issues that require specific monitoring or follow-up by the analyst should then be identified individually in the table under the section designated for recommended follow-up. This table includes a brief reference to the issue, recommended follow-up or action items to be performed and the timeline in which the analyst should expect to obtain information referenced in the follow-up procedures.

**Branded Risk Classification (Example: Credit)**

*Note: A separate summary and table should be completed for each of the nine branded risk classifications, as well as a category for Other, if deemed necessary.*

**Analyst Initial Assessment**

**Credit:** This risk is considered moderate, driven primarily by a fairly conservative investment mix (96.4% of bonds are NAIC 1 designation, with 28% U.S. government, 14% U.S. states and most of the rest high-quality corporates) and limited exposure to equities, offset by a relatively high amount of real estate ($33 million), growing agent balances ($99 million) and significant reinsurance recoverables (paid and unpaid) of $81 million. However, the reinsurance recoverables are diversified across a number of highly rated reinsurers.

<table>
<thead>
<tr>
<th>No/Minimal Concern</th>
<th>Moderate Concern</th>
<th>Significant Concern</th>
<th>Trend</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bonds</td>
<td></td>
<td></td>
<td>↔</td>
</tr>
<tr>
<td>Reinsurance Recoverables</td>
<td></td>
<td></td>
<td>↑</td>
</tr>
<tr>
<td>Real Estate – Home Office</td>
<td></td>
<td></td>
<td>↔</td>
</tr>
<tr>
<td>Agent Balances and Uncollected Premiums</td>
<td></td>
<td></td>
<td>↑</td>
</tr>
</tbody>
</table>

**Examiner Summary and Assessment**

**Credit:** Examiner agrees with analyst assessment regarding bonds and reinsurance recoverables. Although the reinsurance recoverables balance has increased significantly in recent years, the change is in line with increases in premium volume and strategic plan of partnering with high-quality reinsurers to increase the volume of its product liability business. Real Estate – Home Office was tested during the exam, with a recent appraisal reviewed showing the value of the property to be $40 million. Therefore, the examiner proposes that the credit risk associated with the home office be reclassified as a minimal concern. In reviewing agent balances, the exam team recognized a growing concern regarding slow-paying agents for the company’s growing product liability business. In discussing this with the company, a lack of company controls related to agency audits was noted. As such, the exam team agrees with the analyst’s assessment of high credit risk in this area and has included a management letter comment regarding agency audits as described below.

<table>
<thead>
<tr>
<th>No/Minimal Concern</th>
<th>Moderate Concern</th>
<th>Significant Concern</th>
<th>Trend</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bonds</td>
<td></td>
<td></td>
<td>↔</td>
</tr>
<tr>
<td>Reinsurance Recoverables</td>
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<tr>
<td>Agent Balances and Uncollected Premiums</td>
<td></td>
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</tr>
</tbody>
</table>

**Examination Overall Assessment:** Moderate  
**Overall Trend:** ↔
ISSUES OF NON-COMPLIANCE

The purpose of this section is to describe any issues of non-compliance identified during the examination. These issues typically do not have a significant impact on the assessment of each branded risk classification, but are important to communicate and ensure proper follow-up is performed.

PRIORITIZATION AND ONGOING MONITORING

The purpose of this section of the memorandum is to allow the examiner to document any suggested changes to the prioritization level and/or to document the examiner’s rationale for maintaining the current prioritization level.

PROPOSED CHANGES TO SUPERVISORY PLAN

The purpose of this section of the memorandum is to propose any changes to the supervisory plan that the examiner believes are necessary based on the preceding information.

Recommended Follow-Up

<table>
<thead>
<tr>
<th>Issue</th>
<th>Recommended Follow-Up</th>
<th>Timeline</th>
</tr>
</thead>
<tbody>
<tr>
<td>See ML #2 – Lack of a</td>
<td>Company was asked to establish a consistent agency audit plan to ensure accurate and</td>
<td>Company has stated that it plans to increase its IA staffing over the</td>
</tr>
<tr>
<td>consistent agency audit</td>
<td>complete premium and claim reporting. Analyst is asked to follow-up on company</td>
<td>next six months to support additional agency audits. Therefore, follow-up</td>
</tr>
<tr>
<td>process</td>
<td>activity in this area by requesting a copy of the audit plan and selecting a sample</td>
<td>as part of the next annual financial statement analysis is recommended.</td>
</tr>
<tr>
<td></td>
<td>of agency audit reports to request and review.</td>
<td></td>
</tr>
</tbody>
</table>

See ML #1 – Schedule F reporting

Company was asked to report reinsurance data on Schedule F on a gross basis in all instances. Analyst asked to follow-up by closely monitoring Schedule F and reinsurance Jumpstart reports.

Follow-up recommended in conjunction with quarterly and annual financial statement analysis through 20XX.

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PHASE 7 – DRAFT EXAMINATION REPORT AND MANAGEMENT LETTER

This section of the Handbook addresses the following subjects:

A. Examination Report
B. Management Letter
C. Summary Review Memorandum
D. Letter of Representation

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

B. Management Letter

Significant results and observations noted during the examination that are not appropriate or necessary for inclusion in the public report, as determined by the state insurance department conducting the examination, should be communicated to the board and/or management. A management letter is considered an examination workpaper and may be used for this purpose. Those states not utilizing the management letter should communicate comments to the board and/or management during the exit conference or other means deemed appropriate. For group examinations, the lead state, after discussion with other participating states, will determine which results and observations will be included.

The letter to management, or other means of communication as determined by the state, can serve as a vehicle for an ongoing dialogue between the regulator and the insurer and should be shared with those states an insurer is licensed in, as long as confidentiality can be maintained. This letter or communication should be issued and delivered by the regulators to the board members and/or management based on the scope and severity of the issues identified. Judgements on the matters covered within the management letter(s) and the recipient(s) of the management letter(s), and considering the following guidance, are to be determined at the discretion of the examination team.

Based on the findings to be included in the management letter, the examiner should determine the most appropriate party within the holding company structure to whom the letter should be provided. There may be circumstances when the examination team considers sharing the management letter to a level of the organization above the legal entity’s management and/or Board of Directors (i.e. parent company Board). Depending on the issues to be communicated, it may also be appropriate to prepare two different management letters; one to be delivered to management and/or BoD of the legal entity, and one to be delivered to a level of the organization above the legal entity.

When determining which findings are appropriate to communicate to a higher level within the organizational structure, the exam team should consider the significance and severity of the findings or comments, as well as the level at which corrective measures can be taken. For financial reporting matters, the exam team may utilize the definitions for material weakness or significant deficiency (refer to Phase 4 for definitions) to help with this assessment. Findings and comments meeting these definitions may be appropriate for communication to the board of directors and/or audit committee at a level above the legal entity. For other than financial reporting matters and issues or comments related to prospective risks, the examiner should consider the likelihood of such having a significant adverse impact on the insurer's overall condition. Additional considerations include whether management at the legal entity level has a conflict of interest with the items to be communicated and/or whether management has sufficient understanding and capacity to anticipate and respond to changing conditions. Because there may be differences in the significance of issues to be communicated it may be appropriate to prepare two
different management letters; one to be delivered to management and/or BoD of the legal entity, and one to be
delivered to a level of the organization above the legal entity.

Examples of when it may be appropriate to provide the management letter at a level above the legal entity’s
management and/or Board of Directors may include when a conflict of interest exists with the legal entity
management/Board of Directors, and when a group management letter covering multiple companies is prepared.

The examiner should request a response from the company regarding the plan to address the identified issues.
This response should be received within a reasonable time frame (e.g., 90 days) from the date the examiner issued
the letter or communication. In addition to communication with the insurer, the examiner is responsible for
communicating significant results and observations to the analyst and should consider including the analyst
throughout the communication process with the insurer. In accordance with the Financial Analysis Handbook, the
analyst must follow-up and document a review of any management letter comments. The examiner should
coordinate with the analyst on the follow-up of the identified issues. As the examiner moves on to other
examinations, it is important that the analyst be involved with the resolution and monitoring of the identified
issues.

Example Management Letter
An example management letter template has been developed below to provide a suggested format to examiners in
drafting this correspondence. As with the elements that may be included within these non-public letters, the actual
format utilized should be determined by the state insurance department conducting the examination.

June 1, 20XX
Board of Directors
XYZ Insurance Company (XYZ)

The Board of Directors (Board) has a duty to ensure that XYZ Insurance Company is operated in a safe and sound
manner in the best interest of the policyholders. The Department of Insurance (the Department) is charged with
the responsibility to protect insurance consumers and other creditors.

Following are comments related to the examination of XYZ Insurance Company as of December 31, 20XX, and
other related information regarding XYZ. The Department has identified the following issues and concerns
regarding specific operations or practices of the Company. In accordance with the nature of these items, the
department has chosen not to include these comments within the Report of Examination.

For each item/issue noted:

• State the issue using a concise statement of the problem identified;
• Provide commentary on the examiner’s understanding on what caused or created this issue;
• Illustrate the effect of this issue including the materiality impact, and what impact it has had on the financial
  statements, the company’s financial condition, or company operations; and
• Provide information regarding the criteria that elevated this issue (i.e., non-compliance with statute).

We will review the response and determine what further actions are appropriate. Please contact me by telephone
(number) or email (xxxxx@xxxxx) if you have any questions.

Sincerely,
Examiner