FINANCIAL CONDITION (E) COMMITTEE

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The Financial Condition (E) Committee met via conference call Aug. 11, 2020. The following Committee members participated: Scott A. White, Chair (VA); Eric A. Cioppa, Vice Chair (ME); Michael Conway (CO); David Altmaier (FL); Robert H. Muriel (IL); Stephen W. Robertson (IN); Steve Kelley represented by Kathleen Orth (MN); Mike Chaney represented by David Browning (MS); Marlene Caride (NJ); Russell Toal (NM); Raymond G. Farmer (SC); Kent Sullivan represented by Doug Slape (TX); James A. Dodrill (WV); and Jeff Rude represented by Linda Johnson (WY).

1. **Adopted its July 1, June 12, May 15 and March 26 Minutes**

Commissioner White said the Committee met July 1, June 12, May 15 and March 26. During its July 1 meeting, the Committee adopted its Feb. 27 and Dec. 9, 2019, minutes. During its Feb. 27 meeting, the Committee took the following action: 1) adopted a Request for NAIC Model Law Development from the Receivership and Insolvency (E) Task Force and a separate Request for NAIC Model Law Development from the Financial Stability (EX) Task Force; and 2) adopted a request for extension from the Mortgage Guaranty Insurance (E) Working Group regarding ongoing work on an NAIC model. During its July 1 meeting, the Committee also took the following action: 1) adopted technical revisions to the Term and Universal Life Insurance Reserve Financing Model Regulation (#787) and acknowledged similar technical revisions made to Actuarial Guideline XLVIII—Actuarial Opinion and Memorandum Requirements for the Reinsurance of Policies Required to be Valued under Sections 6 and 7 of the NAIC Valuation of Life Insurance Policies Model Regulation (Model 830) (AG 48) by the Life Insurance and Annuities (A) Committee; and 2) adopted actions from the Capital Adequacy (E) Task Force, the Valuation of Securities (E) Task Force, and the Accounting Practices and Procedures (E) Task Force, with the exception of Interpretation (INT) 20-08: COVID-19 Premium Refunds, Limited-Time Exception, Rate Reductions and Policyholder Dividends, which was rejected and sent back to the Accounting Practices and Procedures (E) Task Force. During its June 12 meeting, the Committee took the following action: 1) adopted a memorandum from the Committee to all commissioners regarding the treatment of the London Interbank Offered Rate (LIBOR) under state investment laws; and 2) adopted an extension of mortgage forbearance previously adopted by the Committee through Sept. 30, 2019. During its March 26 meeting, the Committee adopted mortgage forbearance through June 30. The Committee’s May 15 meeting was an educational session on LIBOR.

Commissioner Caride made a motion, seconded by Commissioner Dodrill, to adopt the Committee’s July 1 (Attachment One), June 12 (Attachment Two), May 15 (Attachment Three) and March 26 (Attachment Four) minutes. The motion passed unanimously.

2. **Adopted INT 20-08**

Commissioner White reminded the Committee that on July 1, the Committee rejected a previous version of a proposed interpretation on this topic and gave direction to the Accounting Practices and Procedures (E) Task Force to revise it, with a strong recommendation to add more flexibility. Since then the Task Force has revised and adopted, with only one no vote, a new interpretation that notes that premium treatment is the default methodology, but it also provides the flexibility requested to allow underwriting expense treatment as a limited-time exception. The limited-time exception addresses the concern voiced by industry regarding permitted practices, as it allows reporting entities to apply the limited-time exception without having to seek a permitted practice. This flexibility only applies to Property and Casualty products to avoid the potential negative implications to the medical loss ratio (MLR) for underwriting expense reporting on health products. All payment types will be disclosed, and for those that apply the limited exception, the interpretation provides the transparency needed through disclosure in Note 1 in a similar manner as a prescribed practice. This will assist the states in analyzing the impact compared to the default method if such flexibility is not chosen. Director Farmer made a motion, seconded by Commissioner Caride, to adopt the revised interpretation (Attachment Seven). The motion passed unanimously.

3. **Adopted the Reports of its Task Forces and Working Groups**

Commissioner White stated that items adopted within the Committee’s task force and working group reports that are considered technical, noncontroversial and not significant by NAIC standards—i.e., they do not include model laws, model regulations, model guidelines or items considered to be controversial—will be considered for adoption by the Executive (EX) Committee and Plenary through the Financial Condition (E) Committee’s technical changes report process. Pursuant to this process, which was adopted by the NAIC in 2009, a listing of the various technical changes will be sent to NAIC members shortly after
completion of the Fall National Meeting, and the members will have 10 days to comment with respect to those items. If no objections are received with respect to an item, the technical changes will be considered adopted by the NAIC membership and effective immediately.

Commissioner Robertson made a motion, seconded by Superintendent Cioppa, to adopt the following task force and working group reports: the Accounting Practices and Procedures (E) Task Force, the Capital Adequacy (E) Task Force, the Receivership and Insolvency (E) Task Force, the Reinsurance (E) Task Force, the Valuation of Securities (E) Task Force, the Group Capital Calculation (E) Working Group (Attachment Five), and the Group Solvency Issues (E) Working Group (Attachment Six). The motion passed unanimously.

The Financial Analysis (E) Working Group met July 15, June 17, May 13, May 12, May 6 and May 5 in regulator-to-regulator session, pursuant to paragraph 3 (specific companies, entities or individuals) of the NAIC Policy Statement on Open Meetings, to discuss letter responses related to second-quarter 2019 financial results. Additionally, the Valuation Analysis (E) Working Group met in regulator-to-regulator session, pursuant to paragraph 3 (specific companies, entities or individuals) of the NAIC Policy Statement on Open Meetings, to discuss valuation items related to specific companies.

Having no further business, the Financial Condition (E) Committee adjourned.

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Financial Condition (E) Committee
Conference Call
July 1, 2020

The Financial Condition (E) Committee met via conference call July 1, 2020. The following Committee members participated: Scott A. White, Chair, Doug Stolte and David Smith (VA); Eric A. Cioppa, Vice Chair (ME); Michael Conway (CO); David Altmaier (FL); Robert H. Muriel represented by Kevin Fry (IL); Stephen W. Robertson and Roy Eft (IN); Steve Kelley represented by Kathleen Orth (MN); Mike Chaney represented by David Browning (MS); Marlene Caride (NJ); Russell Toal (NM); Raymond G. Farmer (SC); Kent Sullivan represented by Doug Slape and Jamie Walker (TX); James A. Dodrill represented by Jamie Taylor (WV); and Jeff Rude (WY). Also participating were: Trinidad Navarro (DE); Chlora Lindley-Myers (MO); and Jillian Froment (OH).

1. **Adopted its Feb. 27, 2020, and 2019 Fall National Meeting Minutes**

Commissioner White said the agenda for the conference call is focused on considering actions taken by the Committee’s technical groups that provide annual updates to various solvency-related publications. He said, before doing that, the Committee should consider adoption of the Committee’s minutes from the 2019 Fall National Meeting and the Feb. 27, 2020, conference call in which the Committee adopted two model law development requests and an extension to the Mortgage Guaranty Insurance (E) Working Group, which has been working on its own model law changes for mortgage insurers.

Commissioner Toal made a motion, seconded by Commissioner Caride, to adopt the Committee’s Feb. 27, 2020 (Attachment One-A) and Dec. 9, 2019 (see NAIC Proceedings – Fall 2019, Financial Condition (E) Committee) minutes. The motion passed unanimously.

2. **Adopted Technical Edits to Model #787**

Commissioner White said the next item is to consider adoption of technical edits to the Term and Universal Life Insurance Reserve Financing Model Regulation (#787). He noted how NAIC staff identified a small number of purely editorial items during a Jan. 29 conference call of the Reinsurance (E) Task Force, where these were adopted. He said similar technical edits were also being made by the Life Insurance and Annuities (A) Committee to Actuarial Guideline XLVIII—Actuarial Opinion and Memorandum Requirements for the Reinsurance of Policies Required to be Valued under Sections 6 and 7 of the NAIC Valuation of Life Insurance Policies Model Regulation (AG 48), noting that both Model #787 and AG 48 will be presented to the Executive (EX) Committee and Plenary for consideration at the Summer National Meeting.

Commissioner Caride made a motion, seconded by Commissioner Toal, to adopt the technical edits to Model #787 (Attachment One-B). The motion passed unanimously.

3. **Adopted Reports from Select Task Forces**

Commissioner White said the Committee received summary reports from the Accounting Practices and Procedures (E) Task Force (which met June 22), the Capital Adequacy (E) Task Force (which met June 3) and the Valuation of Securities (E) Task Force (which met May 14), noting that—with the exception of INT 20-08: COVID-19 Premium Refunds, Rate Reductions and Policyholder Dividends (INT 20-08), which would be considered separately—the intent is to adopt each Task Force’s actions and include such items that are technical, non-controversial and/or considered to be of a routine nature in maintaining the insurance financial solvency framework in a Financial Condition (E) Committee Technical Changes Report sent to all NAIC members. He noted that, under the process previously adopted by the Plenary, NAIC members will have 10 days to comment; otherwise, the technical changes will be considered adopted by the NAIC membership and effective immediately.

Commissioner Robertson made a motion, seconded by Ms. Orth, to adopt the actions taken by the Accounting Practices and Procedures (E) Task Force, the Capital Adequacy (E) Task Force and the Valuation of Securities (E) Task Force, with the exception of INT 20-08. The motion passed unanimously.
4. **Discussed INT 20-08**

Commissioner White said the last item is to consider INT 20-08, which was adopted by the Accounting Practices and Procedures (E) Task Force during its June 22 conference call, with more than 75% of the Task Force voting in favor of the adoption. Under this interpretation, the refunds and rate reductions that have been issued by many property/casualty insurers and some health insurers in response to COVID-19 and decreased exposure are treated as a reduction of premium.

Commissioner White said he participated on the Task Force’s June 22 conference call, and described how there was a lot of debate and not total agreement on the issue, as some of the regulators believed it would more be appropriate to treat these refunds as an underwriting expense. He stated that the interpretation as adopted utilizes the same accounting approach that has existed for years on premium refunds, which is a reduction of premium. He also noted the opinions of consumer representatives, who had emphasized the substance of these refunds being economically the equivalent of a return of premium, because it was due to a reduction in exposure and not an expense to the company.

Commissioner White described how the reduction also comes up in discussing the concerns of others related to the impact on premium taxes, because, in many cases, the tax law on premium taxes may be reduced for premiums returned. He explained that, in Virginia, matters dealing with premium taxes are outside of the insurance code and noted that, for Virginia, it really does not matter what guidance the NAIC issues for solvency purposes; Virginia taxes are determined by state taxation laws and paragraph 24 of the interpretation makes this point.

Commissioner White described how the interpretation retains the fundamental concepts of consistency and comparability, and specifically allows the use of prescribed and permitted practices to be issued by any insurance commissioner, with disclosure of that difference in Note 1. By doing so, non-domestic regulators can consider such accounting practice in their review of such insurers’ financial statements and will know that the loss ratios for those companies would be understated. He said he believes all of these points are what played into why the Task Force adopted the interpretation with 75% of the states voting in favor. For this reason, and due to the underlying policies of the Statutory Accounting Principles (E) Working Group, this guidance is actually considered adopted unless overturned by the Task Force with a two-thirds vote in opposition; however, only nine states dissented, so it was passed easily over what was required. He concluded by noting that this policy exists specifically to allow the NAIC membership to issue accounting interpretations quickly, noting how that same policy has already allowed the NAIC membership to provide guidance to many insurers on various COVID-19 issues.

Commissioner Robertson asked if the Committee could prevent this interpretation from moving forward if the Committee were to vote in opposition to INT 20-08. Commissioner White said this is a good question, because there would be no available accounting for the issue for the second quarter statements coming due. He described how, if that is the result, it would be best if the Committee sends the issue back to the Task Force to come to a decision supported by two-thirds of the members of that Task Force, because the current interpretation was adopted by more than two-thirds of the states.

Dan Daveline (NAIC) indicated that the Committee has the authority to overrule the issue. Commissioner White noted that the intent is to take a vote and, if the interpretation is not adopted, it would go back to the Task Force. Commissioner Robertson asked how many members are needed to overturn the Task Force’s adoption; specifically, if a two-thirds vote or a majority vote is required. Mr. Daveline responded that a majority vote would be sufficient to send the issue back to the Task Force.

Commissioner Robertson noted that a letter was distributed to the members of the Committee from the American Property Casualty Insurance Association (APCIA), which requests flexibility in accounting for the monies returned or credited to policyholders. He stated his preference that no company be allowed to use this as a reduction of premium and described how, in Indiana, the state would lose $1,250,000, which would equate to 20 jobs, or 20 people who would lose their jobs to make up that amount of money. He noted that while the Task Force emphasized comparability, he believes the Committee has a different duty, noting that the members have never experienced anything like this. He suggested that the Committee use more flexibility and not be so rigid and bureaucratic, and he warned against listening to the industry that the states regulate, noting that he believes the APCIA’s request is reasonable. He said he is not willing to tell his governor that he lost $1,250,000 in revenue due to a technicality vote that he does not think is necessary. He said each member must make their own decision, but the 28 people who voted not to honor the request of the APCIA will likely all have safe jobs, and a lot of people will lose their jobs if this goes through as-is. He described the need to take advantage of every opportunity to collect revenue for the state. He encouraged those voting to take a “bigger picture” perspective.

Commissioner Robertson made a motion to adopt the position of the APCIA as the method to treat the funds.
Commissioner White clarified that flexibility is allowed within the interpretation and simply needs to be disclosed in Note 1 of the financial statements. Commissioner Robertson asked if he only has authority over domestic companies or all companies doing business in Indiana. Commissioner White responded that his authority would only cover domestic insurers. Mr. Daveline agreed but noted that the commissioner may also have authority to prescribe certain tax treatment. Mr. Stolte said the Commissioner could issue a prescribed practice for all licensed companies. Commissioner Robertson stated his appreciation for Mr. Stolte’s comment but will make his motion later.

Commissioner Caride said it is her understanding that it only takes one state to not grant the same prescribed or permitted practice for the entire situation to be stalled. She said all states have been impacted by COVID-19, noting that New Jersey has asked its insurance companies to be flexible with consumers and give them the benefit of the doubt, even if it should not have been given. She described how New Jersey’s companies have worked with the state and taken its request to heart with regard to consumers in New Jersey and have worked to put consumers first at a time when there is high unemployment, health issues, health insurance being cancelled, and little money to pay rent, let alone car insurance. She said the industry has shown good faith, noting that the companies have been good corporate citizens and agree that the NAIC should show some flexibility during this period. She said this is something we have never seen before in our lifetime. She described the benefits of using consistent accounting but noted at the same time this is not a normal, everyday event; therefore, flexibility is needed. She said the accounting may not be pretty in terms of how the companies have to account for this, but her understanding from her carriers is that if they do it according to the interpretation, they would have to go back and deal with commissions paid and other issues. She said the least that can be done right now is to show flexibility. She said she abstained during the Task Force’s vote on the interpretation, but would vote against it if the Committee were to consider its adoption today.

Director Farmer expressed his appreciation for the work of the Task Force, but he could not say it any better than Commissioner Caride. He said regulators have asked companies to go outside of their comfort zone to give forbearance, and companies have made decisions to give refunds or dividends or whatever method they choose, noting that the companies have done this on their own. He said this was commendable and because we had asked them to be flexible, we should be as well. He noted that the states have not been down this road before and all states have had to be flexible on a number of issues.

Director Farmer made a motion to send the issue back to the Task Force and to provide flexibility to regulators and insurers.

Director Froment agreed with what has been said by the other Committee members, noting that Ohio has concerns with the interpretation. She discussed how Ohio worked with companies to provide relief and every company did something different in their offerings as a means to get monies into the hands of consumers, even though each company crafted things differently compared to the next. She described that in Ohio, not in one instance was a rate filing required; therefore, Ohio did not approve a reduction of premium but, rather, allowed the companies to offer relief. She said little upfront guidance was provided. She said Ohio would not be following the interpretation and will be providing flexibility to Ohio domestics, but she also has concerns about things not being done uniformly nationwide.

Director Lindley-Myers expressed her support for the positions taken by Ohio, South Carolina and New Jersey. She said she agrees that companies have sprung into action to do the best they could during this pandemic, and she wants to make sure Missouri is as flexible as possible to the companies.

Commissioner Conway said he would like to make sure he understands why the states do not want to provide the flexibility. He asked if there was something to consider besides consistency.

Commissioner White said one thing he hears often is the need for transparency, so that a non-domestic can look at Note 1. He said he believes there is flexibility through permitted and prescribed practices. He stated there is also concern that this could create a bad precedent. He noted that while everyone agrees with the way the industry has handled the issue, 28 “yes” votes at the Task Force was based on the principles of consistency and comparability, and using the same methodology that has been used in the past through Note 1 disclosure.

Commissioner Toal complimented the chair for explaining this appropriately. He described that he voted for INT 20-08 at the Task Force and would support it today. He said if he believed the states were not granted flexibility, he would not support it.

Commissioner Conway asked for a greater explanation of the permitted practices.
Superintendent Cioppa agreed with that request because Maine voted in favor of INT 20-08, but if, at the end of the day, another step is needed to get where things are desired, he is somewhat concerned. He stated that for that reason he is in favor of hearing more.

Mr. Stolte described the historical work completed by the Statutory Accounting Principles (E) Working Group to develop an accounting model that works and emphasized how it was never meant to overrule a state’s authority, and that is how prescribed and permitted practices were created. Footnote 1 shows both the state’s basis used in the financial statements and the NAIC’s basis to allow comparability, which has served its purpose for a long period of time. He said he does not understand the stigma or problem with the prescribed or permitted practices.

Commissioner White said he believes the question is the extra burden on the companies and the states, noting that the concern is more with the prescribed practices as it pertains to non-domestic companies. Mr. Stolte described that if a state issues a prescribed practice for all licensed companies, then that is the manner in which the item would have to be reported in all companies’ financial statements for the business in Virginia.

Robin Marcotte (NAIC) read from the Accounting Practices and Procedures Manual (AP&P Manual) and, more specifically, Question and Answer #2, which describes a permitted practice as an accounting practice requested by an individual insurer that departs from statutory accounting principles and has received approval from the domestic state. She said the AP&P Manual defines a prescribed practice as an accounting practice that is incorporated directly by state law, regulation or general administrative rule applicable to all applicable insurers. She said the AP&P Manual is not intended to preempt a state’s legislative and regulatory authority. In a prescribed practice, a state could tell all its licensed companies to follow a particular practice. She explained that it is possible for two states to decide to tax these refunds differently and it would apply to all carriers licensed in their respective state. She said, for example, Virginia could have a different practice for filing premium taxes than Missouri, and both would be disclosed in Note 1 if either differed from the accounting practice outlined in the AP&P Manual.

Commissioner Conway asked Ms. Marcotte if the non-domiciliary state issues a prescribed practice that disagrees with the domestic state, would the same result be the case. Ms. Marcotte said the company files the annual financial statement in accordance with its domiciliary state requirements. Ms. Marcotte noted that the distinction she made is related to premium and related premium taxes because those are driven by state law; therefore, domestic companies are required to follow all the rules in that state. So, for example, Virginia does not control premium and premium taxes for companies domiciled in Missouri.

Commissioner White asked if Colorado wants it to be treated as an expense for Colorado-licensed companies, if that would be allowed. Ms. Marcotte noted that for purposes of premium and related premium taxes, all Colorado licensed companies would be required to follow Colorado law.

Mr. Slape said he would like to make the distinction on the interpretation related to accounting and transparency through disclosure, noting that the accounting could have an impact on loss ratios but that is a completely different conversation than taxes. He stated that no matter what the NAIC says, it has no impact on how this is handled for premium taxes; he stated this needs to be clear because that is controlled by state law on how premium tax is determined. He noted that the state statute may define the terms generally, noting for example, in Texas, the Department of Insurance is not the premium tax agent; it is the comptroller. He said the members of the Committee should not think this has any impact on premium for premium tax purposes.

Commissioner White agreed with Mr. Slape, noting that paragraph 24 of the interpretation makes this same point.

Mr. Fry discussed the negative moniker that comes with permitted practices and how, for this particular interpretation, comes with an additional degree of administrative duties. He noted that the states need flexibility, given the transparency is also built in with the disclosure and, therefore, supports such flexibility.

Mr. Navarro said he believes Indiana made a motion and either a second must be made or the motion must be withdrawn, or at least that is normally the case.

Commissioner White said he believes a couple of motions were made, one by Commissioner Robertson and another by Director Farmer, noting that he would like to receive comments first.

Commissioner Robertson said he would withdraw his motion and instead second Director Farmer’s motion.
Commissioner White said Director Farmer’s motion was to send the issue back to the Task Force. Commissioner White asked if Director Farmer would like to proceed with the motion and take a vote at this time or if Director Farmer is supportive of hearing from the industry and interested parties, and then returning back to the motion to take a vote. Director Farmer said he is supportive of hearing further discussion and then returning back to the motion.

Philip Carson (APCIA) said the commissioners have raised the APCIA’s issues, noting that what the APCIA offered was a compromise that many of the commissioners seem to support. He said flexibility and fairness to policyholders was requested and the APCIA believes the commissioners should do the same thing. He stated that the discussion related to permitted and prescribed practices is one that creates a lot of confusion, noting that there would be a lot of burden on permitted practices, especially for those companies that operate in multiple states. He said there would be confusion if the states adopt different positions on the request for permitted practices, which would add a complication, stating that if the interpretation is adopted as it reads now, the companies would have no recourse if they were not allowed to obtain permitted practices in all the states in which they operate. He said the APCIA’s proposal harms no one, respects the good faith effort the companies put forth, and would be the fairest and cleanest way to proceed with the issue.

Jonathan Rodgers (National Association of Mutual Insurance Companies—NAMIC) echoed the comments made by the APCIA and noted the unprecedented times. He described how the discussion on permitted and prescribed practices demonstrates the complexity of the issue and noted how flexibility seemed to be the preference of the Committee, noting that it is just a matter of how that flexibility is granted. He said NAMIC believes the transparency exists with the APCIA’s proposal, regardless of whether it is recorded as a reduction of premium or as an expense.

Keith Bell (Travelers) said Travelers went through this issue and initially determined it was properly accounted for as a return of premium, even though companies have filed amendments to change their policies. Staff at Travelers wondered if they had missed something but when they went back and reviewed the guidance, it confirmed that they believe it is more properly reported as a return of premium, as it does not meet the definition of an expense and actually violates the Level 5 guidance in the Preamble of the AP&P Manual. Mr. Bell noted, however, in stepping back and looking at it, the amount charged to customers as premiums is one of the most important measures to insurer companies because it is a measure of risk and is used in several leverage ratios, but other financial measures used by insurers. Additionally, because the payments being made back to policyholders are the result of reduced possibility of loss, Travelers believes it should be recorded as a reduction of premium, because premium should represent the amount charged to take on the risk. He said he does not believe the accounting is that difficult when treated as a contra-revenue, recording the original premium and then the return premium would be recorded separately as a contra amount, allowing the company to track the original premium so that they could pay agents and brokers on the appropriate original amount, but would also allow the track of the gross and net amount so they can pay the correct premium tax based on the differences in state law or state requirements. He said Travelers’ lead state is having its Department of Revenue issue a bulletin to apply the premium tax to the gross amount and not the net amount on this matter.

Commissioner White thanked everyone for their comments, noting that there was not consensus, either among the industry or among regulators. He returned to the motion by Director Farmer to send the issue back to the Task Force to have INT 20-08 revised in a way that is still supported by two-thirds of the Task Force members. Director Farmer concurred that was his motion but added that he strongly urges the Task Force to incorporate flexibility so that the permitted practice burden does not have to be utilized. The motion was seconded by Commissioner Robertson. The motion passed, with New Mexico dissenting.

Having no further business, the Financial Condition (E) Committee adjourned.

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Financial Condition (E) Committee
Conference Call
February 27, 2020

The Financial Condition (E) Committee met via conference call Feb. 27, 2020. The following Committee members participated:
Scott A. White, Chair (VA); Eric A. Cioppa, Vice Chair, and Vanessa Sullivan (ME); Michael Conway represented by Rolf Kaumann (CO); David Altmaier represented by Carolyn Morgan and Robert Ridenour (FL); Robert H. Muriel represented by Kevin Fry and Kevin Baldwin (IL); Stephen W. Robertson and Roy Eft (IN); Steve Kelley represented by Fred Andersen (MN); Marlene Caride (NJ); Russell Toal (NM); Raymond G. Farmer represented by Daniel Morris (SC); Kent Sullivan represented by Jamie Walker (TX); James A. Dodrill represented by Jamie Taylor (WV); and Jeff Rude (WY).

1. Adopted a Request for NAIC Model Law Development from the Receivership and Insolvency (E) Task Force

Commissioner White made the Committee aware that the Executive (EX) Committee approved a request for model law development from the Group Capital Calculation (E) Working Group with respect to the Insurance Holding Company System Regulatory Act (#440) and the Insurance Holding Company System Model Regulation with Reporting Forms and Instructions (#450), which could have implications for this new request (Attachment One-A1) from the Receivership and Insolvency (E) Task Force related to the same models. He stated that while the two items are unrelated, it’s important for the Committee to understand whether this new work could slow down the work of the Group Capital Calculation (E) Working Group. More specifically, the goal is for the group capital calculation (GCC) to be adopted by the Working Group at the Summer National Meeting so the states can begin introducing it in early 2021. With that as a backdrop, Commissioner White requested that Mr. Baldwin provide a summary of the Task Force’s request. Mr. Baldwin stated that on Jan. 8, the Receivership and Insolvency (E) Task Force adopted a request to the Committee. He stated that the background for the Task Force’s request is a common issue that can arise in a receivership of an insurance company where affiliated entities provide essential services through inter-company agreements. The continuation of these services can be critical to the operation of the receivership, particularly when all staffing and information technology (IT) functions are outsourced. This issue is specific to agreements with affiliated entities that are formed for the sole purpose of providing services to the insurance company. For example, affiliated entities may handle all the insurance company’s administrative functions (e.g., handling, underwriting, statutory accounting and premium collection), but provide no services to entities outside of the group.

Mr. Baldwin said that when an insurance company is placed in receivership, the unilateral termination of services by an affiliate can lead to delay, waste, and significant expense to the receivership estate. An interruption in obtaining data can also impede a guaranty association’s ability to pay claims. Mr. Baldwin stated that the Task Force recognizes that there are some existing protections under the current Model #440, specifically the requirement for prior approval of affiliate transactions, which can afford state insurance regulators an opportunity to identify problematic agreements in advance of a receivership. There are also provisions in Model #450 that restrict such agreements from including unilateral or automatic terminations if an insurer is placed in receivership. Mr. Baldwin noted that a receiver can file legal action against an affiliated service provider that refuses to continue essential services under a contract or seek a court order requiring the affiliate to provide records. However, protracted litigation can result in delays and additional costs. Additionally, when the affiliate is in another jurisdiction, these efforts can be challenging.

Mr. Baldwin stated that in some cases the insurance company and an affiliate are inextricably intertwined. He stated that if the operations and records of the entities are commingled, it is difficult to handle the receivership without the affiliate’s cooperation. Sometimes it is necessary to place an affiliate in receivership and administer it with the insurance company. However, if the affiliate does not consent, the ensuing litigation will involve further time and expense.

Mr. Baldwin stated that one potential solution that the Task Force identified is to consider revisions to Model #440 by modifying the definition of “insurer” under state insurance holding company laws to encompass affiliated entities whose sole purpose is to provide services to an insurer. While the Task Force recognizes that there are significant issues to be worked through, including potential conflicts with other laws, the Task Force would endeavor to address those and any other issues as part of the work in developing a solution within Model #440 and Model #450.

Commissioner Caride made a motion, seconded by Mr. Kaumann, to adopt the request to make changes to Model #440 and Model #450 to develop revisions to address issues with continuity of essential services. The motion passed unanimously.
2. **Adopted a Request for Extension from the Mortgage Guaranty Insurance (E) Working Group**

Commissioner White reminded Committee members that the NAIC requires model law requests, such as the one adopted from the Receivership and Insolvency Task Force, to be adopted as NAIC model laws or model law changes within one year of the original request to the Executive (EX) Committee. He stated that to the extent that a model change is not completed within one year from the date approved by the Executive (EX) Committee, an extension must be requested and approved. With respect to the specific request from the Mortgage Guaranty Insurance (E) Working Group, he stated that while this work has been ongoing for a significant period, this was a project that he supported being completed, and he supported the request. He stated that the ongoing work has largely been the product of its technical nature and need for the NAIC to hire consultants and then modifications based upon the consultant’s work. He stated he was encouraged to hear that the Working Group does now appear to be close on finalizing this work, as they have now exposed a new Loan Level Capital Model for these mortgage insurers; all of the states on this Working Group are supportive of the direction. Superintendent Toal made a motion, seconded by Commissioner Caride, to adopt the request (Attachment One-A2). The motion passed unanimously.

3. **Adopted a Request for NAIC Model Law Development from the Financial Stability (EX) Task Force**

Commissioner White stated that the Committee had received an additional model law development request (Attachment One-A3) from the Financial Stability (EX) Task Force on Feb. 26, and it relates to a liquidity stress test that has been in the process of being developed for some time. He stated that while the actual stress test is not yet completed, it is like the GCC in that the primary purpose of any type of legislative change is to provide the necessary confidentiality protections. He stated that similar to the request from the Receivership and Insolvency (E) Task Force, it is too early to know whether the completion of this work could affect the GCC, but the idea is to make all three of the different legislative changes to Model #440 and Model #450 at the same time, assuming that all are ultimately supported and adopted.

Commissioner White stated that during the Feb. 26 conference call of the Financial Stability (EX) Task Force, one comment letter on this item was received from the American Council of Life Insurers (ACLI), and the general response on adopting the request was that while Model #440 and Model #450 might not ultimately be chosen as the ideal placement for holding this tool confidential, if it is, it makes sense that all three of the items be addressed at the same time. He described how far fewer companies were likely be impacted by this liquidity stress test than the GCC, with as few as 23 for this test. Commissioner Robertson and Mr. Eft expressed support for the confidentiality aspect of this request, but they expressed concern about one of the provisions that limits and decides what stress test gets used in a liquidation because it seems to reduce the states’ right to choose the stress. Commissioner Caride stated that work is ongoing, and all comments are welcome. Commissioner Robertson asked what was being voted on and whether the issue of what stress test is being used is still open for consideration. Commissioner White responded that the issue before the Committee was not adoption of the actual stress test, but rather the request to work on changes to Model #440 and Model #450 that would provide the authority and confidentiality protections of the liquidity stress test, but the stress test itself is still being developed. Commissioner Caride agreed that the item on the table was only to consider if the model is the appropriate venue. She stated that she would be happy to reach out to Commissioner Robertson subsequent to the conference call to better understand his concern regarding the actual stress test. Commissioner Robertson stated that he wanted it to be clear in the minutes that the action contemplated was only requesting the authority for the Task Force to work on the changes to the model law and not the actual stress test to be required. Commissioner White stated that was the case, and he stated that Commissioner Robertson’s concern would be noted in the minutes. Commissioner Caride made a motion, seconded by Superintendent Cioppa, to adopt the request for model law development. The motion passed unanimously.

Having no further business, the Financial Condition (E) Committee adjourned.
To: Financial Condition (E) Committee
From: Receivership and Insolvency (E) Task Force
Date: January 8, 2020

RE: Model Law Request for Insurance Holding Company System Regulatory Act (#440) and
Insurance Holding Company System Model Regulation with Reporting Forms and Instructions (#450)

The Receivership and Insolvency (E) Task Force requests the Committee consider opening the Insurance Holding Company System Regulatory Act (#440) and Insurance Holding Company System Model Regulation with Reporting Forms and Instructions (#450) to consider revisions to address issues with continuation of essential services through affiliated intercompany agreements that arise during the receivership of an insurance company, specifically agreements with affiliated entities whose sole business purpose is to provide services to the insurance company.

The Task Force is cognizant of other unrelated revisions being considered for Models 440 and 450 under an existing open Model Law Request and understands the sensitivity of the timing of that work. Work related to the continuation of essential services is not intended to delay or impede any other revisions; however, the Task Force feels it may be efficient to conduct its review and drafting concurrently with that work.

Background and Rationale

In 2018 the Financial Stability (EX) Task Force made a referral to the Receivership and Insolvency (E) Task Force as part of the Macro Prudential Initiative (MPI). At the 2019 Summer National Meeting, the Receivership and Insolvency (E) Task Force adopted a report including recommendations to address receivership powers that are implicit in state laws, rather than explicit. One such area is the power to ensure the continuity of essential services and functions within a holding company group once an insurer is placed into receivership.

The Financial Stability Board’s (FSB) Key Attributes (KAs) of Effective Resolution Regimes for Financial Institutions KA 3.2 states that a resolution authority should have the power to ensure the continuity of essential services and functions by requiring companies in the group to continue providing services. Under Common Framework for the supervision of Internationally Active Insurance Groups (ComFrame) (CF 12.7a), a resolution authority may take steps to provide continuity of essential services by requiring other entities within the IAIG (including non-regulated entities) to continue services. The
Task Force identified the following authority and remedies available within the US regime related to these international standards:

- The *Insurance Holding Company System Model Act* (§440) requires approval of affiliated transactions, allowing a regulator to identify agreements that could create obstacles in a receivership. The *Insurance Holding Company System Model Regulation* (§450), Section 19, provides that cost sharing and management agreements specify if the insurer is placed in receivership that an affiliate has no automatic right to terminate the agreement.
- The Receiver can take action against a provider that refuses to continue services under a contract, or seek an order requiring it to turn over records. If an affiliate providing services is inextricably intertwined with the insurer, the Receiver could also seek to place the affiliate into receivership.

However, it was noted that some of these authorities and remedies may not address the immediate need to continue services in some receiverships. Despite these available remedies, receivers continue to be challenged by this issue in receivership, often resulting in significant additional legal and administrative expenses to the receivership estate.

One potential solution is to revise the definition of “insurer” under state insurance holding company laws to encompass affiliated entities whose sole purpose is to provide services to the insurer.

The NAIC adopted 2020 charges for the Receivership Law (E) Working Group to: “Review and provide recommendations for remedies to ensure continuity of essential services and functions to an insurer in receivership by affiliated entities, including non-regulated entities. Consult with the Group Solvency Issues (E) Working Group as the topic relates to affiliated intercompany agreements.”

**Scope of the Proposed Revisions to Models 440 and 450**
The scope of the request is limited to addressing the issue of continuation of essential services through affiliated intercompany agreements that arise during the receivership of an insurance company. The Receivership Law (E) Working Group under the Receivership and Insolvency (E) Task Force would complete the review and recommend proposed draft Models 440 and 450 revisions. Revisions may be necessary to the following sections of Models 440 and 450 including, but not limited to:

- Model 440 Section 1. Definitions
- Model 440 Section 5. Standards and Management of an Insurer Within an Insurance Holding Company System
- Model 440 Section 12. Receivership
- Model 450. Consistency with any revisions to Model 440

Any questions about this memorandum may be directed to NAIC staff, Jane Koenigsman (jkoenigsman@naic.org, 816-783-8145).
To: Commissioner Scott White (VA), Chair, Financial Condition (E) Committee

From: Kevin Conley (NC), Chair, Mortgage Guaranty Insurance (E) Working Group

Date: February 7, 2020

Re: Updated Request for Extension

The Mortgage Guaranty Insurance (E) Working Group is in the process of fulfilling its charge to update the Mortgage Guaranty Insurance Model Act (Model #630). The Working Group anticipated completion of its Charge by the 2020 Spring National Meeting. As chair, I would like to update that request to the Financial Condition (E) Committee in accordance with NAIC procedures.

As background, the NAIC engaged Milliman to assist the Working Group in finalizing a Mortgage Guaranty Insurance Capital Model that will become the new capital standard for mortgage insurers. Following some delays due to a shift in focus directed by the Working Group, Milliman’s work was completed in early December of last year. Subsequent to discussion at the Fall National Meeting, the Working Group exposed the Draft Mortgage Guaranty Insurance Capital Model, Mortgage Guaranty Insurance Model Act (#630), Mortgage Guaranty Insurance Standards Manual, and a proposed Mortgage Guaranty Insurance Exhibit. The Working Group will discuss and address comments received on the exposure and send a referral to the Blanks (E) Working Group regarding the proposed exhibit during the next several months.

At this time, we believe we can complete this work by the 2020 Fall National Meeting. The request for additional time is to allow the necessary time to address comments regarding the above referenced documents and ensure that a comprehensive regulatory framework is in place to effectively regulate these complex insurance entities. We are aware that we have been unable to complete our work within the one-year time period expected under the NAIC model law process and request an extension until the 2020 Fall National Meeting in order to finalize a product that can be adopted by the domestic states of the mortgage insurers, as well as any other state also wishing to adopt the same.
To: Financial Condition (E) Committee
From: Financial Stability (EX) Task Force
Date: February 26, 2020

RE: Model Law Request for Insurance Holding Company System Regulatory Act (#440) and Insurance Holding Company System Model Regulation with Reporting Forms and Instructions (#450)

The Financial Stability (EX) Task Force requests the Financial Condition (E) Committee consider opening the Insurance Holding Company System Regulatory Act (#440) and Insurance Holding Company System Model Regulation with Reporting Forms and Instructions (#450) to consider revisions to establish regulatory authority to require liquidity stress testing processes and confidentiality protections for the data reported from the liquidity stress tests.

The Task Force is cognizant of other unrelated revisions being considered for Models 440 and 450 under an existing open Model Law Request and understands the sensitivity of the timing of that work. Work related to liquidity stress testing is not intended to delay or impede any other revisions; however, the Task Force feels it may be efficient to conduct its review and drafting concurrently with that work.

Background and Rationale

In the Task Force’s recent exposure of the 2019 Liquidity Stress Test, the regulatory authority and confidentiality rely upon the specific lead state’s examination laws and supporting processes (e.g., confidentiality agreements). For the ongoing liquidity stress tests performed in future years, a specific provision needs to be made in state statutes and/or regulations to provide more consistency in this authority and confidentiality protection.

Scope of the Proposed Revisions to Models 440 and 450

The scope of the request is limited to addressing the issue of establishing regulatory authority to require stress testing and disclosures related to liquidity risk and to establish in statute the confidentiality of those disclosures as appropriate. The Financial Stability (EX) Task Force would complete the review and recommend proposed draft Models 440 and 450 revisions. It is anticipated that these revisions will need to reference Liquidity Stress Testing Framework documents that will need to be able to be modified annually without opening up the models themselves (e.g., directions regarding the liquidity stress test, reporting templates, stress scenarios). Revisions may be necessary to the following sections of Models 440 and 450 including, but not limited to:

- Model 440 Section 1. Definitions
- Model 440 Section 5. Standards and Management of an Insurer Within an Insurance Holding Company System
- Model 440 Section 8: Confidential Treatment
- Model 450. Consistency with any revisions to Model 440

Any questions about this memorandum may be directed to NAIC staff, Todd Sells (tsells@naic.org, 816-783-8403).
TERM AND UNIVERSAL LIFE INSURANCE RESERVE FINANCING MODEL REGULATION

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Section 1. Authority

This regulation is adopted and promulgated by [title of supervisory authority] pursuant to [insert provision of state law equivalent to section 5B of the Credit for Reinsurance Model Law] of the [name of state] Insurance Code.

Section 2. Purpose and Intent

The purpose and intent of this regulation is to establish uniform, national standards governing reserve financing arrangements pertaining to life insurance policies containing guaranteed nonlevel gross premiums, guaranteed nonlevel benefits and universal life insurance policies with secondary guarantees; and to ensure that, with respect to each such financing arrangement, funds consisting of Primary Security and Other Security, as defined in Section 5, are held by or on behalf of ceding insurers in the forms and amounts required herein. In general, reinsurance ceded for reserve financing purposes has one or more of the following characteristics: some or all of the assets used to secure the reinsurance treaty or to capitalize the reinsurer (1) are issued by the ceding insurer or its affiliates; or (2) are not unconditionally available to satisfy the general account obligations of the ceding insurer; or (3) create a reimbursement, indemnification or other similar obligation on the part of the ceding insurer or any of its affiliates (other than a payment obligation under a derivative contract acquired in the normal course and used to support and hedge liabilities pertaining to the actual risks in the policies ceded pursuant to the reinsurance treaty).

Section 3. Applicability

This regulation shall apply to reinsurance treaties that cede liabilities pertaining to Covered Policies, as that term is defined in Section 5B, issued by any life insurance company domiciled in this state. This regulation and [insert provision of state law equivalent to the Credit for Reinsurance Model Regulation] shall both apply to such reinsurance treaties; provided, that in the event of a direct conflict between the provisions of this regulation and [insert provision of state law equivalent to the Credit for Reinsurance Model Regulation], the provisions of this regulation shall apply, but only to the extent of the conflict.

Section 4. Exemptions from this Regulation

This regulation does not apply to the situations described in Subsections A through F.

A. Reinsurance of:

(1) Policies that satisfy the criteria for exemption set forth in [insert provision of state law equivalent to Section 6F of the Valuation of Life Insurance Policies Model Regulation] or [insert provision of state law equivalent to Section 6G of the Valuation of Life Insurance Policies Model Regulation]; and which are issued before the later of:
(a) The effective date of this regulation, and

(b) The date on which the ceding insurer begins to apply the provisions of VM-20 to establish the ceded policies’ statutory reserves, but in no event later than Jan 1, 2020;

(2) Portions of policies that satisfy the criteria for exemption set forth in [insert provision of state law equivalent to Section 6E of the Valuation of Life Insurance Policies Model Regulation] and which are issued before the later of:

(a) The effective date of this regulation, and

(b) The date on which the ceding insurer begins to apply the provisions of VM-20 to establish the ceded policies’ statutory reserves, but in no event later than Jan. 1, 2020;

(3) Any universal life policy that meets all of the following requirements:

(a) Secondary guarantee period, if any, is five (5) years or less;

(b) Specified premium for the secondary guarantee period is not less than the net level reserve premium for the secondary guarantee period based on the Commissioners Standard Ordinary (CSO) valuation tables and valuation interest rate applicable to the issue year of the policy; and

(c) The initial surrender charge is not less than one hundred percent (100%) of the first year annualized specified premium for the secondary guarantee period;

(4) Credit life insurance;

(5) Any variable life insurance policy that provides for life insurance, the amount or duration of which varies according to the investment experience of any separate account or accounts; nor

(6) Any group life insurance certificate unless the certificate provides for a stated or implied schedule of maximum gross premiums required in order to continue coverage in force for a period in excess of one year.

B. Reinsurance ceded to an assuming insurer that meets the applicable requirements of [insert provision of state law equivalent to Section 2D of the Credit for Reinsurance Model Law]; or

C. Reinsurance ceded to an assuming insurer that meets the applicable requirements of [insert provisions of state law equivalent to Sections 2A, 2B or 2C, of the Credit for Reinsurance Model Law], and that, in addition:

(1) Prepares statutory financial statements in compliance with the NAIC Accounting Practices and Procedures Manual, without any departures from NAIC statutory accounting practices and procedures pertaining to the admissibility or valuation of assets or liabilities that increase the assuming insurer’s reported surplus and are material enough that they need to be disclosed in the financial statement of the assuming insurer pursuant to Statement of Statutory Accounting Principles No. 1 (“SSAP 1”); and

(2) Is not in a Company Action Level Event, Regulatory Action Level Event, Authorized Control Level Event, or Mandatory Control Level Event as those terms are defined in [insert provision of state law equivalent to the Risk-Based Capital (RBC) for Insurers Model Act] when its RBC is calculated in accordance with the life risk-based capital report including overview and instructions for companies, as the same may be amended by the NAIC from time to time, without deviation; or

D. Reinsurance ceded to an assuming insurer that meets the applicable requirements of [insert provisions of state law equivalent to Sections 2A, 2B or 2C, of the Credit for Reinsurance Model Law], and that, in addition:
(1) Is not an affiliate, as that term is defined in [insert provision of state law equivalent to Section 1A of the Insurance Holding Company System Regulatory Model Act], of:

(a) The insurer ceding the business to the assuming insurer; or

(b) Any insurer that directly or indirectly ceded the business to that ceding insurer;

(2) Prepares statutory financial statements in compliance with the NAIC Accounting Practices and Procedures Manual;

(3) Is both:

(a) Licensed or accredited in at least 10 states (including its state of domicile), and

(b) Not licensed in any state as a captive, special purpose vehicle, special purpose financial captive, special purpose life reinsurance company, limited purpose subsidiary, or any other similar licensing regime; and

(4) Is not, or would not be, below 500% of the Authorized Control Level RBC as that term is defined in [insert provision of state law equivalent to the Risk-Based Capital (RBC) for Insurers Model Act] when its Risk-Based Capital (RBC) is calculated in accordance with the life risk-based capital report including overview and instructions for companies, as the same may be amended by the NAIC from time to time, without deviation, and without recognition of any departures from NAIC statutory accounting practices and procedures pertaining to the admission or valuation of assets or liabilities that increase the assuming insurer’s reported surplus; or

E. Reinsurance ceded to an assuming insurer that meets the requirements of either [insert provision of state law equivalent to Section 5B(4)(a) of the Credit for Reinsurance Model Law, pertaining to certain certified reinsurers] or [insert provision of state law equivalent to Section 5B(4)(b) of the Credit for Reinsurance Model Law, pertaining to reinsurers meeting certain threshold size and licensing requirements]; or

Drafting Note: A state may satisfy the requirements of Section 4E above by either adopting Section 5B(4) of the Credit for Reinsurance Model Law (#785), or it may include the specific provisions of Section 5B(4) of the Credit for Reinsurance Model Law (#785) directly into its adoption of this regulation, Term and Universal Life Insurance Reserve Financing Model Regulation (#787).

F. Reinsurance not otherwise exempt under Subsections A through E if the commissioner, after consulting with the NAIC Financial Analysis Working Group (FAWG) or other group of regulators designated by the NAIC, as applicable, determines under all the facts and circumstances that all of the following apply:

(1) The risks are clearly outside of the intent and purpose of this regulation (as described in Section 2 above);

(2) The risks are included within the scope of this regulation only as a technicality; and

(3) The application of this regulation to those risks is not necessary to provide appropriate protection to policyholders. The commissioner shall publicly disclose any decision made pursuant to this Section 4F to exempt a reinsurance treaty from this regulation, as well as the general basis therefor (including a summary description of the treaty).

Drafting Note: The exemption set forth in Section 4F was added to address the possibility of unforeseen or unique transactions. This exemption exists because the NAIC recognizes that foreseeing every conceivable type of reinsurance transaction is impossible; that in rare instances unanticipated transactions might get caught up in this regulation purely as a technicality; and that regulatory relief in those instances may be appropriate. The example that was given at the time this exemption was developed pertained to bulk reinsurance treaties where the ceding insurer was exiting the type of business ceded. The exemption should not be used with respect to so-called “normal course” reinsurance transactions; rather, such transactions should either fit within one of the standard exemptions set forth in Sections 4A, B, C, D, or E or meet the substantive requirements of this regulation.
Section 5. Definitions

A. “Actuarial Method” means the methodology used to determine the Required Level of Primary Security, as described in Section 6.

B. “Covered Policies” means the following: Subject to the exemptions described in Section 4, Covered Policies are those policies, other than Grandfathered Policies, of the following policy types:

1. Life insurance policies with guaranteed nonlevel gross premiums and/or guaranteed nonlevel benefits, except for flexible premium universal life insurance policies; or,

2. Flexible premium universal life insurance policies with provisions resulting in the ability of a policyholder to keep a policy in force over a secondary guarantee period.

C. “Grandfathered Policies” means policies of the types described in Subsections B1 and B2 above that were:

1. Issued prior to January 1, 2015; and

2. Ceded, as of December 31, 2014, as part of a reinsurance treaty that would not have met one of the exemptions set forth in Section 4 had that section then been in effect.

D. “Non-Covered Policies” means any policy that does not meet the definition of Covered Policies, including Grandfathered Policies.

E. “Required Level of Primary Security” means the dollar amount determined by applying the Actuarial Method to the risks ceded with respect to Covered Policies, but not more than the total reserve ceded.

F. “Primary Security” means the following forms of security:

1. Cash meeting the requirements of [insert provision of state law equivalent to Section 3A of the Credit for Reinsurance Model Law];

2. Securities listed by the Securities Valuation Office meeting the requirements of [insert provision of state law equivalent to Section 3B of the Credit for Reinsurance Model Law], but excluding any synthetic letter of credit, contingent note, credit-linked note or other similar security that operates in a manner similar to a letter of credit, and excluding any securities issued by the ceding insurer or any of its affiliates; and

3. For security held in connection with funds-withheld and modified coinsurance reinsurance treaties:

   a. Commercial loans in good standing of CM3 quality and higher;

   b. Policy Loans; and

   c. Derivatives acquired in the normal course and used to support and hedge liabilities pertaining to the actual risks in the policies ceded pursuant to the reinsurance treaty.

G. “Other Security” means any security acceptable to the commissioner other than security meeting the definition of Primary Security.

H. “Valuation Manual” means the valuation manual adopted by the NAIC as described in Section 11B(1) of the Standard Valuation Law, with all amendments adopted by the NAIC that are effective for the financial statement date on which credit for reinsurance is claimed.

Drafting Note: Section 5H presumes that each state is permitted under its state laws to directly reference the Valuation Manual adopted by the NAIC. If a state is required by its state laws to reference a state law or regulation, it should modify Section 5H as appropriate to do so.

**Drafting Note:** Sections 5H and I presume that each state is permitted under its state laws to “adopt” the Valuation Manual in a manner similar to how the Accounting Practices and Procedures Manual becomes effective in many states, without a separate regulatory process such as adoption by regulation. It is desirable that all states adopt the Valuation Manual requirements and that such adoption be achieved without a separate state regulatory process in order to achieve uniformity of reserve standards in all states. However, to the extent that a state may need to adopt the valuation manual through a formal state regulatory process, these sections may be amended to reflect any state’s need to adopt the Valuation Manual through regulation or otherwise.

### Section 6. The Actuarial Method

#### A. Actuarial Method

The Actuarial Method to establish the Required Level of Primary Security for each reinsurance treaty subject to this regulation shall be VM-20, applied on a treaty-by-treaty basis, including all relevant definitions, from the Valuation Manual as then in effect, applied as follows:

1. For Covered Policies described in Section 5B(1) above, the Actuarial Method is the greater of the Deterministic Reserve or the Net Premium Reserve (NPR) regardless of whether the criteria for exemption testing can be met. However, if the Covered Policies do not meet the requirements of the Stochastic Reserve exclusion test in the Valuation Manual, then the Actuarial Method is the greatest of the Deterministic Reserve, the Stochastic Reserve, or the NPR. In addition, if such Covered Policies are reinsured in a reinsurance treaty that also contains Covered Policies described in Section 5B(2) above, the ceding insurer may elect to instead use paragraph 2 below as the Actuarial Method for the entire reinsurance agreement. Whether Paragraph 1 or 2 are used, the Actuarial Method must comply with any requirements or restrictions that the Valuation Manual imposes when aggregating these policy types for purposes of principle-based reserve calculations.

2. For Covered Policies described in Section 5B(2) above, the Actuarial Method is the greatest of the Deterministic Reserve, the Stochastic Reserve, or the NPR regardless of whether the criteria for exemption testing can be met.

3. Except as provided in Paragraph (4) below, the Actuarial Method is to be applied on a gross basis to all risks with respect to the Covered Policies as originally issued or assumed by the ceding insurer.

4. If the reinsurance treaty cedes less than one hundred percent (100%) of the risk with respect to the Covered Policies then the Required Level of Primary Security may be reduced as follows:

   a. If a reinsurance treaty cedes only a quota share of some or all of the risks pertaining to the Covered Policies, the Required Level of Primary Security, as well as any adjustment under Subparagraph (c) below, may be reduced to a pro rata portion in accordance with the percentage of the risk ceded;

   b. If the reinsurance treaty in a non-exempt arrangement cedes only the risks pertaining to a secondary guarantee, the Required Level of Primary Security may be reduced by an amount determined by applying the Actuarial Method on a gross basis to all risks, other than risks related to the secondary guarantee, pertaining to the Covered Policies, except that for Covered Policies for which the ceding insurer did not elect to apply the provisions of VM-20 to establish statutory reserves, the Required Level of Primary Security may be reduced by the statutory reserve retained by the ceding insurer on those Covered Policies, where the retained reserve of those Covered Policies should be reflective of any reduction pursuant to the cession of mortality risk on a yearly renewable term basis in an exempt arrangement;

   c. If a portion of the Covered Policy risk is ceded to another reinsurer on a yearly renewable term basis in an exempt arrangement, the Required Level of Primary Security may be
For any other treaty ceding a portion of risk to a different reinsurer, including but not limited to stop loss, excess of loss and other non-proportional reinsurance treaties, there will be no reduction in the Required Level of Primary Security.

It is possible for any combination of Subparagraphs (a), (b), (c), and (d) above to apply. Such adjustments to the Required Level of Primary Security will be done in the sequence that accurately reflects the portion of the risk ceded via the treaty. The ceding insurer should document the rationale and steps taken to accomplish the adjustments to the Required Level of Primary Security due to the cession of less than one hundred percent (100%) of the risk.

The Adjustments for other reinsurance will be made only with respect to reinsurance treaties entered into directly by the ceding insurer. The ceding insurer will make no adjustment as a result of a retrocession treaty entered into by the assuming insurers.

(5) In no event will the Required Level of Primary Security resulting from application of the Actuarial Method exceed the amount of statutory reserves ceded.

(6) If the ceding insurer cedes risks with respect to Covered Policies, including any riders, in more than one reinsurance treaty subject to this Regulation, in no event will the aggregate Required Level of Primary Security for those reinsurance treaties be less than the Required Level of Primary Security calculated using the Actuarial Method as if all risks ceded in those treaties were ceded in a single treaty subject to this Regulation;

(7) If a reinsurance treaty subject to this Regulation cedes risk on both Covered and Non-Covered Policies, credit for the ceded reserves shall be determined as follows:

(a) The Actuarial Method shall be used to determine the Required Level of Primary Security for the Covered Policies, and Section 7 shall be used to determine the reinsurance credit for the Covered Policy reserves; and

(b) Credit for the Non-Covered Policy reserves shall be granted only to the extent that security, in addition to the security held to satisfy the requirements of Subparagraph (a), is held by or on behalf of the ceding insurer in accordance with [cite the state’s version of Sections 2 and 3 of the Credit for Reinsurance Model Law]. Any Primary Security used to meet the requirements of this Subparagraph may not be used to satisfy the Required Level of Primary Security for the Covered Policies.

B. Valuation used for Purposes of Calculations

For the purposes of both calculating the Required Level of Primary Security pursuant to the Actuarial Method and determining the amount of Primary Security and Other Security, as applicable, held by or on behalf of the ceding insurer, the following shall apply:

(1) For assets, including any such assets held in trust, that would be admitted under the NAIC Accounting Practices and Procedures Manual if they were held by the ceding insurer, the valuations are to be determined according to statutory accounting procedures as if such assets were held in the ceding insurer’s general account and without taking into consideration the effect of any prescribed or permitted practices; and

(2) For all other assets, the valuations are to be those that were assigned to the assets for the purpose of determining the amount of reserve credit taken. In addition, the asset spread tables and asset default cost tables required by VM-20 shall be included in the Actuarial Method if adopted by the
Section 7. Requirements Applicable to Covered Policies to Obtain Credit for Reinsurance; Opportunity for Remediation

A. Requirements

Subject to the exemptions described in Section 4 and the provisions of Section 7B, credit for reinsurance shall be allowed with respect to ceded liabilities pertaining to Covered Policies pursuant to [insert provisions of state law equivalent to Sections 2 or 3 of the Credit for Reinsurance Model Law] if, and only if, in addition to all other requirements imposed by law or regulation, the following requirements are met on a treaty-by-treaty basis:

1. The ceding insurer’s statutory policy reserves with respect to the Covered Policies are established in full and in accordance with the applicable requirements of [insert provisions of state law equivalent to the Standard Valuation Law] and related regulations and actuarial guidelines, and credit claimed for any reinsurance treaty subject to this regulation does not exceed the proportionate share of those reserves ceded under the contract; and

2. The ceding insurer determines the Required Level of Primary Security with respect to each reinsurance treaty subject to this regulation and provides support for its calculation as determined to be acceptable to the commissioner; and

3. Funds consisting of Primary Security, in an amount at least equal to the Required Level of Primary Security, are held by or on behalf of the ceding insurer, as security under the reinsurance treaty within the meaning of [insert provision of state law equivalent to Section 3 of the Credit for Reinsurance Model Law], on a funds withheld, trust, or modified coinsurance basis; and

4. Funds consisting of Other Security, in an amount at least equal to any portion of the statutory reserves as to which Primary Security is not held pursuant to Paragraph (3) above, are held by or on behalf of the ceding insurer as security under the reinsurance treaty within the meaning of [insert provision of state law equivalent to Section 3 of the Credit for Reinsurance Model Law]; and

5. Any trust used to satisfy the requirements of this Section 7 shall comply with all of the conditions and qualifications of [insert provision of state law equivalent to Section 124 of the Credit for Reinsurance Model Regulation], except that:

   a. Funds consisting of Primary Security or Other Security held in trust, shall for the purposes identified in Section 6B, be valued according to the valuation rules set forth in Section 6B, as applicable; and

   b. There are no affiliate investment limitations with respect to any security held in such trust if such security is not needed to satisfy the requirements of Section 7A(3); and

   c. The reinsurance treaty must prohibit withdrawals or substitutions of trust assets that would leave the fair market value of the Primary Security within the trust (when aggregated with Primary Security outside the trust that is held by or on behalf of the ceding insurer in the manner required by Section 7A(3)) below 102% of the level required by Section 7A(3) at the time of the withdrawal or substitution; and

   d. The determination of reserve credit under [insert provision of state law equivalent to Section 124 of the Credit for Reinsurance Model Regulation] shall be determined according to the valuation rules set forth in Section 6B, as applicable; and

NAIC’s Life Actuarial (A) Task Force no later than the Dec. 31st on or immediately preceding the valuation date for which the Required Level of Primary Security is being calculated. The tables of asset spreads and asset default costs shall be incorporated into the Actuarial Method in the manner specified in VM-20.
(6) The reinsurance treaty has been approved by the commissioner.

B. Requirements at Inception Date and on an On-going Basis; Remediation

(1) The requirements of Section 7A must be satisfied as of the date that risks under Covered Policies are ceded (if such date is on or after the effective date of this regulation) and on an ongoing basis thereafter. Under no circumstances shall a ceding insurer take or consent to any action or series of actions that would result in a deficiency under Section 7A(3) or 7A(4) with respect to any reinsurance treaty under which Covered Policies have been ceded, and in the event that a ceding insurer becomes aware at any time that such a deficiency exists, it shall use its best efforts to arrange for the deficiency to be eliminated as expeditiously as possible.

(2) Prior to the due date of each Quarterly or Annual Statement, each life insurance company that has ceded reinsurance within the scope of Section 3 shall perform an analysis, on a treaty-by-treaty basis, to determine, as to each reinsurance treaty under which Covered Policies have been ceded, whether as of the end of the immediately preceding calendar quarter (the valuation date) the requirements of Sections 7A(3) and 7A(4) were satisfied. The ceding insurer shall establish a liability equal to the excess of the credit for reinsurance taken over the amount of Primary Security actually held pursuant to Section 7A(3), unless either:

(a) The requirements of Section 7A(3) and 7A(4) were fully satisfied as of the valuation date as to such reinsurance treaty; or

(b) Any deficiency has been eliminated before the due date of the Quarterly or Annual Statement to which the valuation date relates through the addition of Primary Security and/or Other Security, as the case may be, in such amount and in such form as would have caused the requirements of Section 7A(3) and 7A(4) to be fully satisfied as of the valuation date.

(3) Nothing in Section 7B(2) shall be construed to allow a ceding company to maintain any deficiency under Section 7A(3) or 7A(4) for any period of time longer than is reasonably necessary to eliminate it.

Section 8. Severability

If any provision of this regulation is held invalid, the remainder shall not be affected.

Section 9. Prohibition against Avoidance

No insurer that has Covered Policies as to which this regulation applies (as set forth in Section 3) shall take any action or series of actions, or enter into any transaction or arrangement or series of transactions or arrangements if the purpose of such action, transaction or arrangement or series thereof is to avoid the requirements of this regulation, or to circumvent its purpose and intent, as set forth in Section 2.

Section 10. Effective Date

This regulation shall become effective [insert date] and shall pertain to all Covered Policies in force as of and after that date.
The Financial Condition (E) Committee met via conference call June 12, 2020. The following Committee members participated: Scott A. White, Chair, Doug Stolte and David Smith (VA); Eric A. Cioppa, Vice Chair (ME); Michael Conway represented by Rolf Kaumann (CO); David Altmaier and Carolyn Morgan (FL); Robert H. Muriel represented by Kevin Fry (IL); Stephen W. Robertson and Roy Eft (IN); Steve Kelley represented by Constance Peterson (MN); Russell Toal (NM); Raymond G. Farmer (SC); Kent Sullivan represented by Jamie Walker (TX); and Jeff Rude (WY).

1. **Adopted the Draft Memorandum from Committee Regarding LIBOR**

Commissioner White reminded the Committee of a May 15 educational session on the topic of the London Interbank Offered Rate (LIBOR) in which the Committee took no action on a proposal (Attachment Two-A) from the American Council of Life Insurers (ACLI). Commissioner White said the proposal requests two things: 1) a safe harbor to address the fact that all state laws essentially limit the type of derivatives insurers can engage in; and 2) deem these types of derivatives as effective hedges. He said the proposal was received, but action was deferred since it was an educational-focused conference call. He said under the LIBOR transition, insurance companies will be receiving certain swaps that do not easily fit into those allowable categories. He noted that the only way an insurance company would not be forced to sell these swaps the day they were received, and potentially incur losses, would be to receive a clarification issued by the insurance commissioner that allows these as permissible investments. Commissioner White said he thinks that issuance of such a clarification is appropriate because the issue is not something the insurers have any control over and when coupled with the potential for an insurer losing what he would consider policyholder money from this LIBOR transition, it is the correct position to take in his state. He stated for that reason, and because he did not hear any pushback from the Committee members during the May 15 conference call, he prepared a memorandum that summarizes his views on this issue. Mr. Smith recommended that the word “forbearance” in the subject line of the memorandum be replaced with the word “clarification” (Attachment Two-B). Commissioner White agreed, and so did the other Committee members.

Commissioner White said issuing a clarification on state law is an issue each individual commissioner would have to decide. He stated that the accounting issue embedded in the original request from the ACLI should be referred to the Statutory Accounting Principles (E) Working Group. Michael Lovendusky (ACLI) stated the ACLI appreciates the action from the Committee and supports the clarification that these should be permissible. However, he said the ACLI questioned the referral. He stated the ACLI did discuss the issue briefly and did not believe the issue needed to be addressed by the Statutory Accounting Principles (E) Working Group. Commissioner White reiterated his previous views regarding the accounting issue and said it is appropriate to break out the accounting issue separately.

Commissioner Toal made a motion, seconded by Superintendent Cioppa, to adopt the draft memorandum and refer the accounting issue to the Statutory Accounting Principles (E) Working Group. The motion passed unanimously.

2. **Adopted an Extension on Mortgage Forbearance**

Commissioner White directed the Committee to the previously issued March 27 guidance from the Committee on this issue, and the question was whether this guidance should be extended. Bruce Oliver (Mortgage Bankers Association) said there were several moving parts, including their most recent letter (Attachment Two-C) to the Committee, being considered at this time. He referenced the previously issued guidance that lasts until the end of June and referenced subsequent clarifications. Mr. Oliver said the Mortgage Bankers Association has since sent a letter to the Life Risk-Based Capital (E) Working Group making specific changes to the guidance for year-end, including addressing various issues it identified in a previous letter. Mr. Oliver introduced John Waldeck (Pacific Life Insurance Company), speaking on behalf of the ACLI. Mr. Waldeck stated that members of the ACLI have been working with borrowers regarding possible loan modifications without knowing how long things would last and when things may begin to reopen. He said that many decisions have been made by insurance companies on this forbearance issue in a prudent manner. He said some insurers may decide that such agreements should be extended. Therefore, working with guidance in the federal Coronavirus Aid, Relief and Economic Security (CARES) Act or to the banks, they still need time to work with borrowers since reopening is just beginning to occur. He said that the request to the Life Risk-Based Capital (E) Working Group had been until the end of the year and for year-end and, therefore, requested an extension until such time, or at least until September. Mr. Waldeck said the request to the Life Risk-Based Capital (E) Working Group issues were
broader, but the extension issue before the Committee was the most pressing issue at this time. He said the intent of this request was not to forestall impairments but rather prudently work with borrows, and he noted that the ACLI believes the extension is appropriate.

Commissioner White noted the Committee believes the original guidance is appropriate to help assist in addressing this broader issue for borrowers throughout the country when done so prudently. He stated he supports the Life Risk-Based Capital (E) Working Group discussing the broader guidance before the Committee takes any further action after today but that extending this guidance until the end of September seems appropriate to him.

Commissioner Robertson made a motion, seconded by Commissioner Dodrill, to extend the original forbearance guidance until Sept. 30 and update the guidance posted to the NAIC website. The motion passed unanimously.

Having no further business, the Financial Condition (E) Committee adjourned.
MEMORANDUM

TO: Commissioners, Directors and Superintendents

FROM: Commissioner Scott A. White (VA)
Chair of the Financial Condition (E) Committee

DATE: June 12, 2020

RE: Support for Commissioner Clarification Regarding State Law on Derivatives

Background Information
The London Interbank Offered Rate (LIBOR) is a set of reference rates based on average rates for short-term interbank unsecured loans quoted by London banks, and it is not expected to be available as a financial reference rate after 2021. As part of a market-wide transition away from LIBOR and toward the Secured Overnight Financing Rate (SOFR), U.S. central clearing counterparties (CCPs) will shift their discounting rate from the Effective Federal Funds Rate (EFFR) to the SOFR using a one-time special valuation cycle. This is expected to occur on Oct. 16. As part of this unique market event, the CCPs will revalue existing cleared swaps and issue basis swaps on a mandatory basis to all parties that clear swaps on the CCPs to restore a counterparty’s original risk profile. Insurance companies use derivatives, such as interest rate swaps and credit default swaps, primarily for hedging purposes, including to manage risks associated with matching an insurer’s projected liabilities with large bond portfolios and protect an insurer’s exposure to various cash instruments and market conditions.

When using derivatives, insurance companies are required to abide by investment guidelines and legal and regulatory constraints established by the commissioner for their general account assets in a state. Most state laws limit insurers’ derivative use to activities such as hedging, replication, and certain income-generation activities. Life insurance companies have asked for clarification that the basis swaps they will receive as part of CCP’s transition to the SOFR discounting and certain transactions entered into in connection with receipt of those basis swaps will be deemed effective hedges under the uses of derivatives allowed by regulation in a state and under any derivative use plan required to be submitted under state insurance law.

Support for Commissioner Clarification
Due to the above circumstances and the fact that insurers have no control over the distribution of such basis swaps to them, and recognizing that insurers may be disadvantaged if required to dispose of such basis swaps upon receipt or a time thereafter, the Financial Condition (E) Committee is issuing this memorandum to make commissioners, directors and superintendents aware of this issue and offering support for those who issue bulletins on this issue.
The Committee, however, has not concluded that the basis swaps should be deemed effective hedges, but rather, they should be deemed “permissible derivative investments.” Therefore, the Committee supports that for the purposes of applicable state law, any basis swap (or group thereof) incurred by an insurer in connection with a clearinghouse’s shift in discounting from the EFFR to the SOFR (CCP Cutover) shall be deemed a permissible derivative investment for up to one year past the date of the CCP Cutover. We recognize that a commissioner’s decision to provide clarification on a state law set forth by state legislatures is an individual one, and we would respect that some commissioners may wish to perform further due diligence with their own domestic insurers before issuing a bulletin offering such clarification.
To: All Insurers  
RE: June 12 Question & Answer on Guidance for Mortgages for March 31 - September 30 Statutory Financial Statements and Related Interim Risk-Based Capital Filings

Background Information  
On March 27 and June 12, the Financial Condition (E) Committee issued guidance to encourage insurers to work with borrowers who are unable to, or may become unable to meet their contractual payment obligations because of the effects of COVID-19. Nothing in that guidance supersedes the requirement or authority of any state, particularly any state that has separately issued COVID-19 orders, directives or other guidance the impact of which may lead to debt becoming troubled and/or needing to be restructured.

Original Questions  
**Q1** - Is the June 12 guidance also intended to apply to insurers that are not required to report risk-based capital calculations to their domestic regulator or the NAIC for March 31, June 30 and September 30?  
A1 - Yes. The guidance applies to all U.S. insurers filing and is not specific only to insurers that are required to report quarterly risk-based capital calculations. The reference to risk-based capital calculations prepared by insurers for March 31, June 30 and September 30 is intended to provide guidance for periodic internal reporting and reporting to policyholders, the public, and rating agencies that is not otherwise a prohibited announcement under state law.

**Q2** - Is this guidance intended to apply to all COVID-19 loan modifications that occur through September 30, 2020, so that an insurer that modifies a loan in accordance with the parameters of the guidance within that period is not required to adjust the origination date, valued date, or property value as of the modification date (as required under current RBC rules for loan restructures) for current or future RBC reporting periods?  
A2 - Yes. The intent of the guidance is to encourage insurers to make prudent loan modifications for borrowers who are temporarily unable to meet their contractual payment obligations because of the effects of COVID-19 and is not intended to have long-term negative impacts under current RBC rules. Consistent with this intent, if an insurer modifies a loan in accordance with the parameters of the guidance, the insurer is not required to adjust the origination date, valued date, or property value for current or future RBC reporting periods. In addition, an insurer is not required to reclassify to a different RBC category (such as within CM categories (e.g., CM1 to CM2) or within standing categories (e.g., In Good Standing, Overdue, Not in Process, In Process of Foreclosure)) for March 31, June 30 and September 30. The expectation is that further, more deliberative discussion is expected to occur in the future through the Life Risk-Based Capital (E) Working Group, regarding these loans for future reporting periods.

**Q3** - Some construction projects are not allowed to operate because of government imposed stay-at-home orders. Current RBC rules specify that a loan with “construction loan issues” (e.g., abandoned) is required to have a CM5 rating. Is the guidance that loans are not required to be reclassified to a different RBC category as a result of government-mandated delays in any required principal and interest payments in the first and second quarters of 2020 also intended not to require reclassification of construction loans in cases of government-mandated delays in construction?  
A3 - Yes. No RBC category change is required to be changed for March 31, June 30 and September 30 as a result of government-mandated construction delays in the first, second and third quarters of 2020. The expectation is that...
further, more deliberative discussion is expected to occur in the future through the Life Risk-Based Capital (E) Working Group, regarding these loans for future reporting periods.

Q4 - Many properties for which borrowers are not requesting relief may be impacted by valuation and NOI changes resulting from the COVID-19 pandemic. What will be the risk-based capital treatment of these loans?
A4 - The expectation is that further, more deliberative discussion on valuation, NOI impacts and other impacts COVID-19 may cause will occur in the future through the Life Risk-Based Capital (E) Working Group.

Additional Questions
Q1 - The guidance indicates support for loan modifications as a result of COVID-19 but seems to restrict to only those loans that are troubled debt restructures, was this intentional?
A1 - No, the guidance was intending to apply to all loan modifications made as a result of COVID-19 before September 30 even if they would otherwise be categorized a troubled debt restructure; setting forth a safe harbor for all such changes made as a result of COVID-19 during that time period with the intent of the Life RBC Working Group developing more explicit and detailed RBC guidance for both 4Q and beyond, as well as how loan modifications made subsequent to the September 30 date would be treated. While such a safe harbor was intending to encourage loan modifications that are prudent so that there was no long-term impact on policyholders asset values, the view was that guidance on things such as operating income or other considerations within the RBC formula that attempt to measure the future risk of loans would be better addressed by the Life RBC Working Group. (Modifications of loan terms do not automatically result in TDRs. According to U.S. GAAP, a restructuring of a debt constitutes a TDR if the creditor, for economic or legal reasons related to the debtor’s financial difficulties, grants a concession to the debtor that it would not otherwise consider. Short-term modifications made on a good faith basis in response to COVID-19 to borrowers who were current prior to any relief, are not TDRs. This includes short-term (e.g., six months) modifications such as payment deferrals, fee waivers, extensions of repayment terms, or other delays in payment that are insignificant. Borrowers considered current are those that are less than 30 days past due on their contractual payments at the time a modification program is implemented. Working with borrowers that are current on existing loans, either individually or as part of a program for creditworthy borrowers who are experiencing short-term financial or operational problems as a result of COVID-19, generally would not be considered TDRs.)

A2 - The guidance is meant to apply to both situations, the CM categories and the standing categories.
To: All Insurers  
From: Financial Condition (E) Committee  
Date: June 12, 2020  
RE: Guidance for Troubled Debt Restructurings for March 31 - September 30 Statutory Financial Statements and Related Interim Risk-Based Capital Filings (where required)

Background Information
This guidance is being issued by the Financial Condition (E) Committee to all U.S. insurers filing with the NAIC in an effort to encourage insurers to work with borrowers who are unable to, or may become unable to meet their contractual payment obligations because of the effects of COVID-19. The Committee, which is the NAIC parent committee of all the solvency policy making task forces and working groups of the NAIC, supports the use of prudent loan modifications that can mitigate the impact of COVID-19.

Parameters of Guidance
This guidance applies to a troubled debt restructuring issued as a result of COVID-19 and is applicable to the term of the loan modification, but solely with respect to a modification, including a forbearance arrangement, an interest rate modification, a repayment plan, and any other similar arrangement that defers or delays the payment of principal or interest, which occurs during the applicable reporting period for a loan that was not more than 30 days past due as of December 31, 2019. Nothing in this guidance supersedes the requirement or authority of any state, particularly any state that has separately issued COVID-19 orders, directives or other guidance the impact of which may lead to debt becoming troubled and/or needing to be restructured.

Direct Mortgage Loans & Schedule BA Mortgages
For purposes of any risk-based capital calculations prepared by insurers for March 31, June 30 and September 30, all direct mortgages and Schedule BA mortgages for which the insurer chooses, or is government mandated, to allow delays in any required principal and interest payments in accordance with the above parameters are not required to be reclassified to a different RBC category (e.g. will not affect the origination date, valued date, and net operating income or be treated as delinquent) than was utilized during the December 31, 2019 RBC filing and which may have otherwise required a higher capital charge for such a mortgage.

RMBS and CMBS Securities
For purposes of the reporting of NAIC designations in the financial statements prepared for March 31, June 30, and September 30 or any risk-based capital calculations prepared by insurers for March 31, June 30 and September 30, all RMBS and CMBS securities which were modeled by the NAIC for year-end 2019 and for which any required principal and interest payments have been deferred in accordance with the above parameters are not required to receive an updated NAIC designation despite the fact that payments may have been deferred as previously described.

Related Accounting Guidance & Updates
Please see the following for both related accounting guidance and updates to this guidance via Q&A. 
https://content.naic.org/cmte_e_app_blanks.htm  
(Please see related documents tab)

Questions
Any questions on this guidance should be directed to Dan Daveline by e-mail at ddaveline@naic.org
Financial Condition (E) Committee
Conference Call
May 15, 2020

The Financial Condition (E) Committee met via conference call May 15, 2020. The following Committee members participated: Scott A. White, Chair, and Doug Stolte and David Smith (VA); Eric A. Cioppa, Vice Chair (ME); Michael Conway represented by Rolf Kaumann (CO); David Altmaier, Carolyn Morgan and Virginia Christy (FL); Robert H. Muriel represented by Kevin Fry, Shannon Whalen and Susan Berry (IL); Stephen W. Robertson represented by Roy Eft (IN); Steve Kelley represented by Constance Peterson (MN); Mike Chaney represented by David Browning (MS); Marlene Caride and John Sirovetz (NJ); Russell Toal represented by Mark Jordon (NM); Raymond G. Farmer and Daniel Morris (SC); Kent Sullivan represented by Jamie Walker (TX); and Jeff Rude represented by Linda Johnson (WY).

1. Heard an Educational Session on LIBOR

Commissioner White described that the purpose of the conference call is educational on the topic of the London Interbank Offered Rate (LIBOR), which will no longer be supported past 2021. He described how insurance companies would be affected as early as October 2020 and the reason for a proposal from the industry to alleviate the potential adverse impact away from LIBOR. He described how the core issue is ultimately how some of the derivatives that are delivered to insurers may not be in conformance with state law since derivatives are usually only allowed to be one of one of three types—hedging, income generation and replication—and that those derivatives that derived from the LIBOR exchange may not fit into one of those three buckets.

Michael Lovendusky (American Council of Life Insurers—ACLI) introduced member companies that would collectively facilitate the educational session. The presenters included Kathleen O'Neill, Associate General Counsel at New York Life Insurance Company and Vice Chairwoman of the ACLI Derivatives Policy Working Group; Joseph J. Demetrick, Managing Director, Derivatives & Liquid Markets at MetLife Investment Management and Chairman of the ACLI Derivatives Policy Working Group; and Chris McAlister, Managing Director at Prudential Financial. Ms. O'Neill presented most of the information in the written presentation (Attachment Three-A). During the presentation, she emphasized how as the clearinghouse, which is a large financial player, changes its valuation rate, it is expected to generate a lot of liquidity across the Secured Overnight Financing Rate (SOFR) term structure, which is expected to facilitate the transition of new transactions away from LIBOR. She describes this as a technical move that had a large impact, and she referenced how the mechanics were described in the appendix of the written presentation. Essentially, the clearinghouses will make a one-time move to change their valuation process on a single day on Oct. 16. Ms. O'Neill described how there are two steps involved in this process. First, the clearinghouses will conduct a standard end-of-day valuation cycle using federal funds, just like any other day, and the clearinghouses will run a special valuation cycle on the same positions using the SOFR. The two sets of data will be compared, and they will make a one-time adjustment that includes a cash component that adjusts each account that offsets the value transfer as a result of these discounting changes. Second, the clearinghouses book mandatory federal funds SOFR basis swaps that have one leg in federal funds and then one leg in the SOFR. This will restore the accounts’ original risk profile. These accounts will have the same risk profile at the end of the day as the beginning of the day by having these derivatives distributed to them on a mandatory basis. This is where the tension with state insurance law occurs since in many states, insurers can only enter for hedging, replication or income generation, and it is not clear where these would fit into those categories. Ms. O’Neill pointed out that the clearinghouses are planning to put in an auction process for those that do not want to hold the basis swaps, but those processes have not been finalized; therefore, it creates further issues. She also noted that it is not possible for insurers to move away from clearinghouses since under the federal Dodd Frank Wall Street Reform and Consumer Protection Act, many of these are mandated to be cleared under these clearinghouses.

Ms. Berry asked about the duration of these swaps. Mr. McAlister responded how the proposals from the clearinghouses are to give swaps across several durations—two, five, seven, 10, 20 and 30-year swaps—so that it is across a wide number of durations. Commissioner White asked why the clearinghouses used 2020 given that LIBOR does not go away until 2021. Mr. Demetrick stated that part of this is designed to create additional SOFR liquidity and activate transition portfolios. He stated that this will help liquidity to build in the SOFR. Commissioner White asked if state law was considered in determining this approach. Mr. McAlister indicated that he was not sure that it was considered, but he noted that banks used federal funds across their franchise and manage it holistically. This is just part of their federal funds risk, and they are concerned that what is at these clearinghouses will offset something else they have in their franchise, and banks requested that these basis swaps be granted. Mr. McAlister indicated that Prudential voiced that this is not something they preferred, but he implied that the banks...
are more influential in the clearinghouses. Mr. Demetrick added that it is important to know that the clearinghouses have to remain in a balanced risk position; therefore, if they are going to offer basis swaps to one party, they automatically have to deliver them to the people on the other side of the transaction. Otherwise, they would be taken on market risk by the clearinghouse itself. Commissioner White asked hypothetically if insurers were not allowed a full year to dispose of these basis swaps what would occur. Mr. Demetrick described how this was a one-off event and that the differential between the LIBOR and SOFR rates are close, but if insurers are required to unwind early, that could drive a technical widening and therefore disadvantage life insurers. Dan Daveline (NAIC) requested information on the rationale behind the derivatives being effective hedges and whether they could be classified as something else. Ms. O'Neill stated that while state laws differ, her understanding is that under New York state law, the insurer is required to show that the hedge is effective; therefore, it is hard to understand how the effectiveness testing would operate. Consequently, the ACLI is looking for clarification on whether it is both a hedge and an effective hedge so that insurers would not have to make that determination. Ms. O’Neill stated that she would like to think through this more, but she noted that having a hedge would be helpful, but the effective hedge aspect of this could be worked around.

Having no further business, the Financial Condition (E) Committee adjourned.
Executive Summary

- Availability of LIBOR is not assured past 2021
- As part of the transition to SOFR, Central Clearing Parties (CCP) for cleared swaps plan to switch their discounting rate from Fed Funds to SOFR in October 2020
- As part of this switch, parties that trade on the CCP will be compelled to receive basis swaps
- We request that state regulators clarify that derivatives entered into directly in connection with the CCP discounting change are categorized as hedging transactions

LIBOR Transition and Insurance Companies – General Considerations

- Insurance companies experience LIBOR exposure across a wide array of markets, requiring a flexible approach across asset classes that may be coalescing around different approaches, such as for floating rate notes, CLOs, securitized products, private placements, real estate and derivatives
- Within derivatives, there are different issues posed by over-the-counter derivatives and cleared derivatives
- The specific issue we will discuss today arises from a planned change at CCPs, who will shift their discounting rate on uncleared swaps from Fed Funds to SOFR, affecting life insurers' cleared derivatives
CCP Transition to SOFR

- The cleared derivatives market in the US is expected to shift to SOFR via a staged approach, in line with the ARRC’s Paced Transition Plan.
- This will entail both a shift in discounting (planned for October 2020) and ultimately a shift in reference index (from LIBOR to SOFR).
- The first step is a migration of the calculation of discounting and price alignment interest for cleared USD interest rate swap products from the daily Effective Federal Funds Rate (EFFR) to SOFR.
- This move at the CCPs is seen as a key step in generating liquidity across the SOFR term structure. This will facilitate transitioning new transactions away from LIBOR.

CCP Transition to SOFR – mechanics

- The switch from EFFR discounting to SOFR discounting will be undertaken in two steps, occurring on October 16, 2020:
  - **Step 1 – Valuation**
    - The CCP will conduct a standard end-of-day valuation cycle based on EFFR and then run a “special valuation cycle” on the same positions, using SOFR as the discounting rate.
  - **Step 2 – Adjustment**
    - The CCP will (1) make a cash adjustment to each account to offset the value transfer arising from the discounting change and (2) book mandatory EFFR/SOFR basis swaps to each account to restore the account’s original risk profile.
- As a result, all CCP participants, including life insurers, will be allocated basis swaps on a mandatory basis.
- CCPs are contemplating an “auction” process for participants that do not want to hold the basis swaps, but the feasibility of these auctions and their mechanics have not been finalized.

Proposed Relief

- **Proposal**: We are requesting a bulletin/circular letter from state insurance regulators providing a safe harbor for derivatives entered into in connection with the CCPs’ transition from EFFR to SOFR discounting.
- “For the purposes of [applicable state law], any basis swap (or group thereof) incurred by a life insurer with the purpose of mitigating risk in connection with a clearinghouse’s shift in discounting from the federal funds effective rate to the secured overnight financing rate (a “CCP Cutover”) shall be deemed an effective hedging transaction notwithstanding any other provision of [applicable state law] or such life insurer’s derivatives use plan, so long as the life insurer has documented the fact that it has engaged in such basis swap (or group thereof) with the express purpose of mitigating risk in connection with a CCP Cutover. This would apply for a period up to 1 year past the date of the CCP Cutover.”

Appendix
The World's Most Important Number

LIBOR & Its Impact

Current Libor Setting Methodology

Most LIBOR submissions not based on Observable Transactions
Market Transactions Underlying LIBOR Have Decreased Significantly

Funding Volumes of G-SIBs

Source: FR2420 Report of Selected Money Market Rates and DTCC. Federal Reserve staff calculations based on daily volumes aggregated across fed funds, Eurodollar, certificates of deposit, and unsecured commercial paper transactions of the 30 global systematically important banks with tenors between 25 and 35 calendar days (for one-month), 80 and 100 calendar days (three-month), or 150 and 210 calendar days (six-month) over the period October 15, 2016 to June 30, 2017.

Key Dates in LIBOR Phase Out

- 2014: International Organization of Securities Commissions ("IOSCO") establishes Principles for Financial Benchmarks by Administrators of EURIBOR, LIBOR and TIBOR.
  - Principles indicate that reference rates should be transitioned to "rates that are anchored in observable transactions."
- 2014: International Regulators begin work on establishing alternative reference rates.
- US Fed establishes the Alternate Reference Rates Committee ("ARRC") to identify alternative, transaction-based reference rate to replace LIBOR.
- June 2017: ARRC identifies Secured Overnight Financing Rate ("SOFR") – a broad overnight rate based on Repo financing rates – as alternative to USD LIBOR.
- July 2017: UK Financial Conduct Authority ("FCA") announces that it will no longer compel or persuade banks to submit to LIBOR panels after the end of 2021.
- October 2017: ARRC adopts its Paced Transition Plan, including a switch to SOFR discounting/PAR at CCPs.
- November 2017: FCA announces voluntary agreement with all IBOR panel banks to sustain LIBOR until the end of 2021.

IOSCO Summary of Principles

- Governance - intended to ensure that Administrators have appropriate governance arrangements in place to protect the integrity of the Benchmark determination process and to address conflicts of interest.
- Benchmark quality - intended to promote the quality and integrity of Benchmark determinations through the application of design factors that result in a Benchmark that reflects a credible market for the Interest rate measured by that Benchmark.
- Methodology quality - intended to promote the quality and integrity of Methodologies by setting out information that should be addressed within a Methodology. The Principles require that information be Published or Made Available so that Stakeholders may understand and make their own judgments concerning the overall credibility of a Benchmark. They also require that the Methodology address the need for procedures that control when material changes are planned, as a means of alerting Stakeholders to these changes that might affect their positions, financial instruments or contracts.
- Accountability - require that Administrators establish complaints processes, documentation standards and audit reviews intended to provide evidence of compliance by the Administrator with its quality standards, as defined by the Principles and its own policies. The Principles also addressed making this information available to relevant Market Authorities.

What is SOFR?

- Secured Overnight Financing Rate ("SOFR")
- Overnight, nearly "risk free" rate that is correlated with other money market rates.
- Fully transaction based, reflecting broad measure of overnight US Treasury repurchase ("Repo") financing transactions.
- Encompasses robust underlying market with over $500 billion in daily transactions.
- FRBNY proposes to use an unadjusted volume weighted median as the measure for SOFR.
- FRBNY began publishing SOFR and its summary statistics in April 2018.
**LIBOR vs SOFR**

<table>
<thead>
<tr>
<th>Feature</th>
<th>LIBOR</th>
<th>SOFR</th>
</tr>
</thead>
<tbody>
<tr>
<td>London Interbank Offered Rate (LIBOR)</td>
<td>Average interest rate for short-term, inter-bank unsecured loans</td>
<td>Secured Overnight Financing Rate (SOFR)</td>
</tr>
<tr>
<td>Term (O/N, 1-mo, 3-mo, 6-mo)</td>
<td>Overnight (compounded)</td>
<td>Non-compounded</td>
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<tr>
<td>Incorporates credit risk premiums</td>
<td>No credit risk premiums</td>
<td>No credit risk premiums</td>
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<tr>
<td>Forward-looking</td>
<td>Daily Fixing</td>
<td>Daily Fixing</td>
</tr>
<tr>
<td>Based on submissions from panel banks</td>
<td>Based on observable market transactions</td>
<td>Based on observable market transactions</td>
</tr>
<tr>
<td>Liquid, deep, and transparent</td>
<td>Liquid, deep, and transparent</td>
<td>Liquid, deep, and transparent</td>
</tr>
<tr>
<td>Reflects Banks’ costs of funding</td>
<td>Reflects cost of borrowing against Treasuries</td>
<td>Reflects cost of borrowing against Treasuries</td>
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<tr>
<td>Source</td>
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<td>Federal Reserve Bank of NY</td>
</tr>
<tr>
<td>Time</td>
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<td>8:30 am NY Time</td>
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**SOFR Daily Trading Volumes Dwarf Alternatives**

**SOFR-linked Transaction Growth**

**IBOR Replacements**

<table>
<thead>
<tr>
<th>Country / Region</th>
<th>IBOR Index</th>
<th>Proposed Replacement</th>
<th>Underlying Transactions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Europe</td>
<td>EUR-LIBOR</td>
<td>ESTER</td>
<td>Unsecured overnight borrowing, overnight euro money market</td>
</tr>
<tr>
<td>Japan</td>
<td>JPY-LIBOR</td>
<td>TONAR</td>
<td>Secured overnight yen call rate swap</td>
</tr>
<tr>
<td>Switzerland</td>
<td>TGS</td>
<td>SARON</td>
<td>Secured transactions in the overnight call rate market</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>UK-LIBOR</td>
<td>SONIA</td>
<td>Unsecured overnight sterling transactions in the overnight sterling money market</td>
</tr>
<tr>
<td>United States</td>
<td>USD-LIBOR</td>
<td>SOFR</td>
<td>Reflects cost of borrowing against US Treasuries</td>
</tr>
</tbody>
</table>

Attachment Three-A
Financial Condition (E) Committee
8/11/20
Global Transition Progress

**Asset Markets**
- Defined recommended fallback language for new transactions by asset type
- Pursuing legislative action for legacy assets (U.S. only)
- Promoting issuance and liquidity while driving infrastructure and technology progress
- Exploring possibility of creating term SOFR and IDCA rates for use in some asset markets

**Derivatives Markets**
- Developed and issued fallback definitions (Nov. 2019)
- Australian BBB
- Canadian CDOR
- Euro-PF Libor, TIBOR, Euribor, TIBOR
- Sterling Libor, GBP Libor
- United States USD Libor
- Swiss francs CHF Libor
- Developed and issued consultations on Pre-Cessation Issues and DSE ISDA Definition Protocol

LIBOR Cessation – Documentation Issues for Life Insurers

- Across asset classes (securitizations, floating rate notes, derivatives, repo, etc.), no consistency regarding mechanics to replace LIBOR
- The “missing mechanics” are known as “fallback triggers” and “fallback rates”
- “Fallback Triggers” are events that cause a switch from one floating rate to another (trigger can be general (e.g., “LIBOR ceases to be published” or “LIBOR is no longer representative”) or bespoke (e.g., “50% or more of collateral assets in a securitization switch from LIBOR”)
- “Fallback Rates” replace LIBOR following a Fallback Trigger; either hardwired into a document (e.g., “term SOFR”) or left to negotiation (e.g., “as reasonably determined by the Calculation Agent”)
- The market has not converged on a single mechanism and asset classes will diverge (e.g., derivatives versus cash products); these differences can give rise to basis risk both within deals (e.g., securitizations) and across deals (hedges v. hedged positions)

LIBOR Cessation – Derivatives Issues for Life Insurers

- Cleared OTC derivatives incorporate by reference ISDA definitions that do not provide Fallback Rates to replace LIBOR
- US cleared market will shift to SOFR via a staged approach that entails first a shift in discounting (planned for Fall 2020) and ultimately a shift in reference index (from LIBOR to SOFR)
- Basis swaps will be allocated to insurance companies during the cleared swap discounting shift on a mandatory basis
- Regulators (e.g., CFTC, Fed, OCC, etc.) and standard-setting bodies (e.g., FASB, IASB) have been releasing rules and guidance providing “flexibility” so that changes to terms of existing transactions relating to LIBOR cessation do not trigger undesirable accounting, tax and regulatory consequences
- State insurance regulators should follow suit to assure life insurers’ compliance with their regulatory schema

LIBOR Cessation – Derivatives Issues for Life Insurers

- Over-the-counter ("OTC") uncleared derivatives typically incorporate ISDA definitions that do not provide a Fallback Rate to replace LIBOR
- US uncleared market will adopt compounded-in-arrears SOFR for new trades via updated ISDA definitions (currently being finalized) and for existing trades via an optional “protocol” to retroactively apply the new ISDA definitions to existing transactions
- Some insurers and their counterparties may negotiate bilateral terms for swap transactions as needed
- Regulators (e.g., CFTC, Fed, OCC, etc.) and standard-setting bodies (e.g., FASB, IASB) have issued rules and guidance providing “flexibility” so that changes to terms of existing transactions relating to LIBOR cessation do not trigger undesirable accounting, tax and regulatory consequences
The Financial Condition (E) Committee conducted an e-vote that concluded March 26, 2020. The following Committee members participated: Scott A. White, Chair (VA); Eric A. Cioppa, Vice Chair, (ME); Michael Conway represented by Rolf Kaumann (CO); David Altmaier (FL); Robert H. Muriel represented by Kevin Fry and Kevin Baldwin (IL); Stephen W. Robertson and Roy Eft (IN); Steve Kelley represented by Fred Andersen (MN); Mike Chaney represented by David Browning (MS); Raymond G. Farmer (SC); Kent Sullivan represented by Doug Slape and Jamie Walker (TX); and Jeff Rude (WY).


   The Financial Condition (E) Committee conducted an e-vote to consider adoption of the guidance. A majority of the members voted in favor of adopting the guidance (Attachment Four-A). The motion passed.

   Having no further business, the Financial Condition (E) Committee adjourned.
To: All Insurers
From: Financial Condition (E) Committee
Date: March 27, 2020
RE: Guidance for Troubled Debt Restructurings for March 31-June 30 Statutory Financial Statements and Related Interim Risk-Based Capital Filings (where required)

Background Information
This guidance is being issued by the Financial Condition (E) Committee to all U.S. insurers filing with the NAIC in an effort to encourage insurers to work with borrowers who are unable to, or may become unable to meet their contractual payment obligations because of the effects of COVID-19. The Committee, which is the NAIC parent committee of all the solvency policy making task forces and working groups of the NAIC, supports the use of prudent loan modifications that can mitigate the impact of COVID-19.

Parameters of Guidance
This guidance applies to a troubled debt restructuring issued as a result of COVID-19 and is applicable to the term of the loan modification, but solely with respect to a modification, including a forbearance arrangement, an interest rate modification, a repayment plan, and any other similar arrangement that defers or delays the payment of principal or interest, which occurs during the applicable reporting period for a loan that was not more than 30 days past due as of December 31, 2019. Nothing in this guidance supersedes the requirement or authority of any state, particularly any state that has separately issued COVID-19 orders, directives or other guidance the impact of which may lead to debt becoming troubled and/or needing to be restructured.

Direct Mortgage Loans & Schedule BA Mortgages
For purposes of any risk-based capital calculations prepared by insurers for March 31 and June 30, all direct mortgages and Schedule BA mortgages for which the insurer chooses, or is government mandated, to allow delays in any required principal and interest payments in accordance with the above parameters are not required to be reclassified to a different RBC category (e.g. will not affect the origination date, valued date, and net operating income or be treated as delinquent) than was utilized during the December 31, 2019 RBC filing and which may have otherwise required a higher capital charge for such a mortgage.

RMBS and CMBS Securities
For purposes of the reporting of NAIC designations in the financial statements prepared for March 31 and June 30 or any risk-based capital calculations prepared by insurers for March 31 and June 30, all RMBS and CMBS securities which were modeled by the NAIC for year-end 2019 and for which any required principal and interest payments have been deferred in accordance with the above parameters are not required to receive an updated NAIC designation despite the fact that payments may have been deferred as previously described.

Related Accounting Guidance & Updates
Please see the following for both related accounting guidance and updates to this guidance via Q&A.
https://content.naic.org/cmte_e_app_blanks.htm
(Please see related documents tab)

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

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

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

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

2. **Considered Comments Received on Exposed Revised Template and Instructions**

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

   a. **Use of the GCC**

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

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

   b. **Calibration Level**

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

c. **Scope of Application**

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


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

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

Having no further business, the Group Capital Calculation (E) Working Group adjourned.
Group Capital Calculation (E) Working Group
Conference Call
July 21, 2020

The Group Capital Calculation (E) Working Group of the Financial Condition (E) Committee met via conference call July 21, 2020. The following Working Group members participated: David Altmaier, Chair (FL); Kathy Belfi, Vice Chair (CT); Kim Hudson (CA); Philip Barlow (DC); Carrie Mears, Mike Yanacheak and Kim Cross (IA); Shannon Whalen (IL); Roy Eft (IN); Christopher Joyce (MA); Judy Weaver (MI); Fred Anderson (MN); John Rehagen (MO); Jackie Obusek (NC); Justin Schrader and Lindsay Crawford (NE); Dave Wolf (NJ); Edward Kiffel and Bob Kasinow (NY); Dale Bruggeman (OH); Joe DiMemmo (PA); Trey Hancock (TN); Doug Slape and Jamie Walker (TX); Doug Stolte and David Smith (VA); and Amy Malm (WI).

1. Discussed Further Modifications to Exposed Exemptions

Commissioner Altmaier stated his appreciation for the comments received (Attachment Five-A1) on the Working Group’s previously exposed proposed changes to the Insurance Holding Company System Regulatory Act (#440). He said that NAIC staff had developed a revised Model #440, which incorporates changes to address many of the comments, and that this conference call will be specifically focused on those comments that either did not have specific language or would represent a change from the Working Group’s previously developed intent. He stated those comments for which the Working Group believed further changes should be made would be incorporated in the revised Model #440 and re-exposed. He asked Dan Daveline (NAIC) to summarize each of the comments along with a recommendation disposition, and then allow the Working Group to decide on each.

a. Specificity of Exemptions

Mr. Daveline said that Texas recommended in its comment that the Working Group consider giving the insurance commissioner the authority to provide exemptions by rule and moving some of the more detailed exemptions that may be adjusted in the future into a regulation. He said the exemption criteria, and in particular those where commissioner discretion is allowed, is very detailed and that moving such to a model regulation seemed reasonable. Ms. Walker said how the request would be particularly helpful in this time of regulatory fatigue, particularly knowing that some of these changes would require quick adoption, especially in her state where the legislature does not meet annually. Commissioner Altmaier stated he does not oppose the movement of some of the items highlighted and shared some of the concerns of Texas. Mr. Hudson noted how this was consistent with other models and said that California is not opposed to the change. No Working Group members disagreed with the change.

b. Additional Discretion to Waive Schedule 1

Mr. Daveline said that this comment relates to a request for the insurance commissioner to be able to waive the Schedule 1 filing if he or she does not believe it provided value. Mr. Daveline noted that NAIC staff appreciated that with some small groups, the Schedule 1 may not provide the state insurance regulator the value desired, and for that reason proposed language that could be used in the revised Model #440 to provide this discretion. Commissioner Altmaier asked Jonathan Rodgers (National Association of Mutual Insurance Companies—NAMIC) if the proposed resolution addressed their issue. Mr. Rodgers stated the language seemed reasonable but added that he would like to consider the language more closely during the comment period. However, he said he believes it was positive toward addressing their comment. No Working Group members disagreed with the change.

c. Development of a Process for Recognizing and Accepting the GCC by Another Jurisdiction

Mr. Daveline said that the comments on this issue were extensive. He noted that NAIC staff agreed with the concept of the comment and more specifically the need to develop a process and an NAIC Working Group responsible for maintaining a list of jurisdictions deemed to have recognized and accepted the group capital calculation (GCC), although there was no specific action that needed to be taken at this time. Mariana Gomez-Vock (American Council of Life Insurers—ACLI) emphasized the need for a transparent process in terms of how decisions are made and asked if this issue would be fleshed out in the regulation. Commissioner Altmaier stated he appreciates the need for such a process and referenced the work done on reinsurance as a possible blueprint to follow for consistency sake. No Working Group members disagreed.
d. **Initial Filing of the GCC**

Mr. Daveline said that the comment seemed to question the need for an initial filing of the GCC before the insurance commissioner has the discretion to exempt a group going forward. He noted that he believes the Working Group’s rational for the initial filing to suggest obtaining one filing would enable the state insurance regulator to better assess on an individual company basis whether the calculation would provide information that was of value, thus making it more easy for the state insurance regulator to more confidently exempt the group going forward. Tom Finnell (America’s Health Insurance Plans—AHIP) stated he was seeking clarity and having received that, AHIP has no further comments. No Working Group members were opposed to not making any further changes for this issue.

e. **Exemption for Non-U.S. Groups**

Mr. Daveline said he believes one of the comments was addressed through incorporation of proposed language from another commenter that was incorporated into the revised Model #440. Jeff Johnson (John Hancock) stated the language incorporated into a revised Model #440 aligns with the concepts John Hancock was attempting to address and at this point, they have no further comments. No Working Group members were opposed to not making any further changes for this issue.

f. **Broad Definition of Financial Entity**

Mr. Daveline said this comment was focused on the broad definition of a financial entity within the GCC instructions. He noted, however, that the exemption limitation is very narrow and only applies to financial entities that are subject to a specified regulatory capital framework. He stated NAIC staff did not suggest incorporating further specificity and did not believe any further changes were needed. Mr. Finnell stated the concern was that the broad definition may somehow prevent a group from availing themselves of an exemption, but after looking at the language further along with the description, he said AHIP had no further comments at this time. No Working Group members were opposed to not making any further changes for this issue.

g. **Limit Sharing of the GCC Information**

Mr. Daveline said this was an informal comment made during the course of communicating with various parties on the confidentiality language. He said the comment suggested the GCC could only be shared with members of a supervisory college. Mr. Daveline said that while he is not certain the GCC itself will actually be shared by the lead state with other domestic states, information from the GCC definition will through the Group Profile Summary. As a result, the suggestion to limit the sharing seems problematic, and he noted that NAIC staff believe existing state confidentiality language around the examination and analysis process should be sufficient for such sharing. Commissioner Altmaier reinforced that while the Working Group is very supportive of confidentiality protections, this does seem to be too limiting. Michael Gugig (Transamerica), representing the Coalition, stated the Coalition appreciates the points and have no further comments on this issue. No Working Group members were opposed to not making any further changes for this issue.

h. **Expand Exemptions**

Mr. Daveline said this comment suggested adding an additional exemption for companies with premium thresholds of $100 million. He said the current exemptions already allow groups of this size to be exempted if further conditions are met, and also noted NAIC staff had some concern with further modifications that could create a conflict with the covered agreement. Mr. Rodgers stated that given the previous additional flexibility added, he has no further comments given that seemed to address the very small mutual insurance companies that this comment was also directed at. No Working Group members were opposed to not making any further changes for this issue.

i. **Confidentiality Language**

Mr. Daveline said this issue was related to a very small part of the confidentiality language at the end originally developed by the Coalition. He said he believes the existing language that described the GCC as a regulatory tool for assessing group risk is accurate, even though he appreciates the fact that the tool is then used to evaluate the impact on the insurer. Mr. Rodgers noted NAMIC believed it was another tool to be used for evaluating solvency on the insurers’ risk given legal entity regulation is what drives the GCC but stated he had no further points. No Working Group members were opposed to not making any further changes for this issue.
j. Commissioner Authority for Further Exemptions

Stephen Broadie (American Property Casualty Insurance Association—APCIA) said the APCIA recommends the Working Group incorporate more broad discretion for unique circumstances similar to language in the Risk Management and Own Risk and Solvency Assessment Model Act (#505). He mentioned an example where there was one insurer above the $1 billion premium threshold, but only had one other affiliate that had de minimis business. Mr. Daveline noted NAIC staff were concerned about a potential conflict with the “Bilateral Agreement Between the United States of America and the European Union on Prudential Measures Regarding Insurance and Reinsurance” (EU Covered Agreement). Mr. Finnell noted AHIP’s position is different from ACPIA’s but could be used as regulatory guidance in further considering exemptions under the specific thresholds. No Working Group members expressed an interest in considering incorporation of the language from Model #505. However, Commissioner Altmaier stated he is willing to further consider the comments and, to the extent agreeable, consider further changes to the revised proposed Model #440.

k. Deleting Language from Section 8 That Applies to Rest of Model #440

Mr. Daveline said that during the course of communicating with various interested parties in the interim on the confidentiality language, it was noted that some parties recommended deletion of language that already pertains to other aspects of Model #440 and how NAIC staff had always sought out not making any changes to the existing confidentiality protections. Therefore, NAIC staff recommended no further changes as suggested by some that may remove such protections. He noted that this did not mean some of the language could not be applied specifically to the GCC and that perhaps such consideration could be given by parties in the forthcoming re-exposure of Model #440. Mr. Ridgeway agreed with Mr. Daveline’s characterization of the process under which NAIC staff worked with various parties to try to simplify the confidentiality language where “less is more” when it comes to state legislatures that would be asked to consider the model. He described how Model #505 had become the gold standard in terms of confidentiality protections and that the NAIC would be wise to consider some of those same provisions for other sections. He stated during the re-exposure, he would continue to review the language and work with NAIC staff to continue to improve. No Working Group members disagreed with making no changes.

I. Reciprocity Issue

Mr. Daveline directed the Working Group to language proposed by Reinsurance Group of America (RGA), which was exposed since it incorporates the aspect of reciprocity as discussed during the Working Group’s June 2 conference call. He said that the proposed language modifies the language dealing with exemptions for non-U.S. groups by specifying those exemptions shall not apply if the non-U.S. groupwide supervisor requires subgroup reporting. He indicated the Working Group has discussed subgroup reporting in the past and that it was not intended for the GCC in that it would not provide value. However, this language indicates subgroup reporting only comes into play if the non-U.S. group reporting requires subgroup reporting.

Michael Demuth (Allianz) stated Allianz is supportive of efforts to reduce regulatory burden. However, he said the proposal has a series of practical issues that Allianz believes should be taken into consideration before making a final decision since it could create practical and legal challenges, which could create problems both for Allianz and the entire industry.

Mr. Broadie stated the APCIA had two goals: 1) It strongly believes each insurance group should be subject to only one GCC and that should be a parent level and none should be applied at the subgroup level; and 2) it strongly supports reciprocity and the concept of mutual recognition and a level playing field. He stated the APCIA does not support the language and if it was included in the model, language would have to be developed for clarity. He stated the NAIC can develop a transparent process for determination if reciprocity does not exist at the subgroup level and should include coordination with international colleagues with the intent of supporting mutual recognition to get to a place that each group is only submitting one GCC, whether a U.S. group or non-U.S. group.

Matthew Wulf (Swiss Reinsurance Group) stated Swiss Reinsurance Group believes these questions of reciprocity should be asked and discussed with state insurance regulators. He said they understand the goal of the GCC and the insurance capital standard (ICS) and that there are broader goals. He noted there is a great deal more that needs to be laid out and determined but should not be included due to the legislative fatigue. He said he is not sure what the current proposed language means. He said this does not apply to troubled companies and that there are so many reasons why this is not practical and is too cumbersome.

Joseph Sieverling (Reinsurance Association of America—RAA) agreed with the previous commenters on the practical concerns. He said the RAA supports one group capital at the group level, but one thing that is unclear are the facts on the ground—whether many, or some or lot, or one jurisdiction actually report subgroup reporting for U.S. groups. Ultimately, he
said it comes down to the supervisory purpose, and there really is no supervisory purpose of subgroup reporting. He said putting subgroup reporting into the model to try to get reciprocity is just the wrong way to approach this issue.

Ms. Gomez-Vock said the ACLI worked very hard with its members to try to reach an agreement that was actually unanimously agreed upon. She said this includes one group capital at the group level and that subgroup regulation is undesirable. However, the ACLI ultimately came back with supporting the reciprocity provision as long as it is supported by a transparent process and equitable to insurers in all jurisdictions. She said this issue went all the way up to the chief executive officers (CEOs), where it was still unanimously supported.

Ian Adamczyk (Prudential Financial) said Prudential Financial fully supports the concept of mutual recognition across supervisory regimes, but as internationally active insurance groups (IAIGs), that should include recognition and accepting the GCC as part of that support. He stated this should be included in the model act because: 1) it would further the objective of mutual recognition; 2) it is an overarching concept that sets an expectation; and 3) it would help promote consistency across the states. He stated Prudential Financial acknowledges there are some practical considerations, but there are solutions that could be implemented for all parties. Commissioner Altmaier stated the language was included in the draft as a means to generate discussion. He stated he expects further discussion but that timing would be dependent upon other factors.

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

W:\National Meetings\2020\Summer\Cmte\E\GCCWG\June 2 Call\June 2 2020 GCC min.docx
Comments on Exposure

This document is intended to serve as a detail agenda for considering the comments received.

The following does NOT attempt to address all of the specific comments related to each of the issues, but rather a summary, and points the reader to the specific comments for further review.

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<tr>
<td>Issue 1- Specificity of Exemptions</td>
<td>We recommend Model 440 give authority for the commissioner to provide exemptions by rule and moving some of the more detailed exemptions that may be adjusted in the future to Model Regulation 450.</td>
<td>Texas</td>
<td>7</td>
</tr>
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</table>

Staff Summary of the Issue:
During the June 2 call, direction was given to draft exemptions for 1) small county mutual insurers; 2) a group filing the BBA with the Federal Reserve, provided the BBA has to be filed with the lead state; 3) a group whose group-wide supervisor is an located in a reciprocal jurisdiction; 4) non-US groups that provide sufficient information to the lead state and either accepts the GCC in their jurisdiction for US groups or accepts the GCC as an acceptable ICS and indicates as such to the IAIS.

In addition, the direction given was the commissioner should have discretion to exempt other groups that are under the $1 billion ORSA premium threshold; don’t have insurers in another country and don’t have a bank with a capital requirements within the group. However, this exemption can only be granted after the group has filed one GCC with the lead state and the state has determined the group has de minimis affiliated transactions and de minimis risky entities within its holding company. This criteria is intended to give specificity as requested by RAA and APCIA and at the same time make sure the commissioner can require the GCC on a group where the group has material affiliated transactions (for which the GCC would be helpful) or has other noninsurers in the group which could cause material risk (for which the GCC may be helpful). Finally, paragraph (g) allows all of these entities that meet the exemption criteria just noted to instead have to complete an annual Schedule 1 (from the GCC and related trending of that information) and also grants this Schedule 1 allowance to other entities (mutual or other entities whose UCP is a US insurance company that files RBC).

Recommended Action:
NAIC Staff recommends the Working Group further discuss the Texas proposal. This may be a reasonable suggestion as it relates to some of the very detailed exemption requirements. More specifically, the language discussed in the preceding paragraph (or paragraphs (f) and (g) in the exposed model) which provide the additional “flexibility” might be reasonable for inclusion in a model regulation instead of the model act since its exceptionally detailed. A model regulation may also be helpful in addressing other more detailed items suggested by Met Life/Prudential/RGA, if the Working Group decides to include the subgroup reciprocity paragraphs.
## Comments on Exposure

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<tr>
<td>Issue #2- Combine Exemption Discretion and Schedule 1 Discretion</td>
<td>Our second section would be to combine and modify Section 4L(2)(f) and 4L(2)(g) to not require the Schedule 1 at the Commissioner's discretion.</td>
<td>NAMIC</td>
<td>69</td>
</tr>
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</table>

**Staff Summary of the Issue:**
NAMIC notes that the purpose of this recommendation is so the lead state commissioner has the discretion to waive the GCC and Schedule 1 if the regulator does not feel it adds any value. We strongly feel if the ultimate controlling parent is an RBC filer, the GCC results would be substantially similar, therefore, we think the commissioner should have the authority to waive the GCC and other components.

**Recommended Action:**
NAIC Staff notes that while we are not opposed to combining these two sections, there are complications in doing so in that section 4L(2)(g) specifically allows mutuals to be exempt from the GCC and only file the Schedule 1 since RBC produces substantially the same results as the GCC. NAIC staff can appreciate the reason why the Schedule 1 may not provide value to a regulator for some small groups and would support the following modified language to allow such:

> The lead-state commissioner has the discretion to either require or exempt the ultimate controlling person from filing a limited group filing or report on an annual basis if either of the following are met:

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<tr>
<td>Issue #3- Development of Process for “Recognizes and Accepts the GCC”</td>
<td>“As 4L(2)(d) is written, the non-U.S. group wide supervisor must “recognize and accept” the U.S. GCC for non-U.S. groups to qualify for an exemption from the GCC.” “…the phrase “recognizes and accepts” will need to be clarified by establishing a transparent process in an accompanying regulation or regulator guidance.” “It could for example, be defined to allow supervisory regimes to demonstrate reciprocity through regulatory action.”</td>
<td>ACLI</td>
<td>33</td>
</tr>
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**Staff Summary of the Issue:**
This comment letter provides greater detail on potential item to be addressed, although NAIC staff has already incorporated one of the identified items (recognizes and accepts if another jurisdiction does not require a US group to complete a GCC) including the NAIC acting as a central body to establish and maintain a record of jurisdictions that “recognize and accept” the GCC.
Comments on Exposure

Recommended Action:
NAIC agrees that it will be necessary to create a list of jurisdictions that recognize the GCC and to have an NAIC group responsible for developing such a process and possibly even codifying such a listing, unless other more streamlined processes can be recommended (e.g. inclusion on the listing may be dependent upon identification from a member of the industry operating in that jurisdiction and NAIC staff confirming with such jurisdiction).

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<tr>
<td>Issue #4- Initial Filing Requirement</td>
<td>In some cases, for which exemption is apparently provided in the draft HCA text, the group must nonetheless make an initial filing of the GCC with the Lead State, and only subsequent to that could the commissioner grant the exemption. It is not clear why an initial filing would be required, and which would seem to contradict the notion of an exemption.</td>
<td>AHIP</td>
<td>48</td>
</tr>
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</table>

Staff Summary of the Issue:
The comment is directed at the Working Group’s previous decision to require an initial filing to determine the benefits of the calculation for the applicable groups.

Recommended Action:
NAIC staff understood the Working Group’s rational for the initial filing to suggest that obtaining one filing would enable the regulator to better assess on an individual company basis whether the calculation would provide collective information or individual information that was of value; if not the regulator would more confidently be able to exempt the group going forward. Therefore rejection of this comment appears appropriate.

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<tr>
<td>Issue #5- Exemption for non-US Groups</td>
<td>The draft Act does not include language similar to Section 6(D) of the ORSA Model Act, which allows regulators to grant an ORSA exemption “based upon unique circumstances.” APCIA recommends including similar language in Sections 4(L)(2)(f) and (g) of the draft Act.</td>
<td>John Hancock</td>
<td>25</td>
</tr>
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Staff Summary of the Issue:
While the comment letter provides a great deal of backdrop, ultimately the comment recommends the following changes:

   c. An insurance holding company:
      (i) That has provided information to the accredited lead state, either directly or indirectly through the group-wide supervisor, who has determined such
Comments on Exposure

Information is satisfactory to allow the lead-state to comply with the NAIC principles of group supervision as detailed in the NAIC Financial Analysis Handbook, and the lead state has determined that because of this the group capital calculation is not required to be filed; and

(ii) Whose non-U.S. group-wide supervisor, as determined in accordance with the principles of section 7.1, meets either of the following requirements:

a. Where a non-U.S. jurisdiction does not apply its own group capital reporting requirements to U.S. groups or the parent of a U.S. subsidiary operating in that jurisdiction, then the U.S. would not require insurance groups or their parent company domiciled outside the U.S. to file the group capital calculation Recognizes and accepts the group capital calculation for U.S. insurance groups who operate in the jurisdiction of that group-wide supervisor; or

Drafting Note: The phrase “Recognizes and accepts” does not require the non-U.S. group-wide supervisor to require the U.S. insurance groups to actually file the group capital calculation with the non-U.S. supervisor but rather does not require its own version of a group capital filing.

b. For jurisdictions where no U.S. insurance groups operate, recognizes the group capital calculation as an acceptable international capital standard by indicating such formally in writing to the lead state with a copy to the International Association of Insurance Supervisors. The requirement to file the group capital calculation is at the discretion of the U.S. designated group-wide supervisor for the internationally active insurance group.

Recommended Action:
As it relates to the recommended changes to (iv)(a), NAIC staff believes that the concept embedded in the recommended changes to (iv)(a) was intended to be addressed in the drafting note. For that reason, NAIC staff has incorporated language from other comment letters that likely address this. As it relates to the recommended changes to (iv)(b), it’s not clear why the NAIC should not encourage, through other jurisdictions, the acceptance of the GCC where the result would be the same (such non-US group is exempt from the GCC). Meaning, if the discretion exists, its likely the state would do so. With existing language, the jurisdiction need only to make the recommendation to the IAIS as a means to support more mutual recognition through the use of different methodologies.

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<td>Issue #6- Broad Definition of Financial Entity</td>
<td>Affiliates that are integral to the performance of the insurance contract or provision of the insurance or financial products or services to policyholder, members or depositors will be treated as financial entities. AHIP suggests that the reference to “specified regulatory capital framework within is holding company structure be clarified to refer to the capital remine of the other sectoral regulators (e.g. federal or state banking agencies).</td>
<td>AHIP</td>
<td>48</td>
</tr>
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Staff Summary of the Issue:
The comment is referring to the following requirement that must be met in order for an exemption to be granted.

“The holding company includes no banking, depository or other financial entity that is subject to a specified regulatory capital framework.”

Recommended Action:
NAIC staff believes the language is clear that this criteria only exists for financial entities that have a capital requirement, we hesitate to add too much specificity which may undermine the concept of believing its reasonable of not allowing a group that has a non-insurer within its group that is subject to a capital requirements to be exempt given the state may receive some pressure of being able to share group information with that capital regulator.

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<tr>
<td>Issue #7- Add Language limiting sharing through a supervisory college</td>
<td>Add language to limit sharing</td>
<td>Coalition</td>
<td>N/A-Informal comments</td>
</tr>
</tbody>
</table>

Staff Summary of the Issue:
Some have recommended adding the following additional provision to 8(c)2:

Notwithstanding paragraph (1) above, the commissioner may only share confidential and privileged documents, material, or information reported under Section 4L(2) with commissioners of states that are members of the subject insurer’s supervisory college, and whose states have statutes or regulations substantially similar to Subsection A and who have agreed in writing not to disclose such information.

Recommended Action:
NAIC staff find this language problematic as this would only permit the GCC to be shared with commissioners who are part of the supervisory college. Staff noted that lead states need to be able to share key figures of the information from the GCC with all domestic regulators of companies that are part of that group and have examination and/or analysis statutes that protect such information. We believe existing confidentiality requirements are sufficient to do so.

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<tr>
<td>Issue #8 Reciprocity Those Opposed</td>
<td>The comment letter suggests a significant number of issues would need to be addressed before reciprocity paragraphs are appropriate</td>
<td>Allianz / Transamerica</td>
<td>1</td>
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### Comments on Exposure

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<tr>
<th>Position</th>
<th>Comment</th>
<th>Organization/Author</th>
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<tr>
<td>Opposed</td>
<td>“Hardwiring one solution into the Act or state law is not, in our opinion, the appropriate way to proceed.” “Instead the NAIC should develop a process...” “…this process should involve consultation and coordination with U.S. regulators’ international colleagues, and it should be made clear that the purpose of this process is to support mutual recognition and a level regulatory playing field.”</td>
<td>APCIA</td>
</tr>
<tr>
<td>Opposed</td>
<td>While Swiss Re agrees with the premise that a country’s group capital calculation should not apply at the subgroup level, we do not support including this language in the model act.</td>
<td>Swiss Re</td>
</tr>
<tr>
<td>Opposed</td>
<td>We cannot support the revised language proposed in subsections 4.L.(2)d. and e. and the drafting note, which would require a U.S. subgroup capital calculation for a non-U.S. group if the group-wide supervisor of that non-U.S. insurance group does not treat subgroups of U.S. groups in a similar manner (i.e. reciprocal treatment).</td>
<td>RAA</td>
</tr>
<tr>
<td>Support</td>
<td>The ACLI supports the inclusion of a reciprocity provision, such as subsection 4L(2)(e) in the Model Holding Company Act. We believe that the phrase “recognizing and accepts” will need to be clarified upon implementation, perhaps in an accompanying regulation, or by a process that is transparent on how reciprocity is determined in practice, and equitable to insurers based in all jurisdictions.</td>
<td>ACLI</td>
</tr>
<tr>
<td>Support</td>
<td>We support the inclusion of Section 4L(2)(e) to clarify that reciprocal treatment applies at the subgroup level as well as the groupwide level.</td>
<td>Met/PRU/RG A</td>
</tr>
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Comments on Exposure

Staff Summary of the Issue:
During 2019, the Working Group discussed the idea of “subgroup reporting” of the GCC, or more specifically whether the GCC should be required for the US operations (e.g. US insurers) of non-US groups and generally concluded they were not interested in this concept, noting that the GCC was not designed for this purpose. During the June 2 conference call of the Working Group, one of the commenters (RGA) discussed the concern that many companies have relative to Subgroup reporting, and more specifically that some jurisdictions could potentially require this for US groups with insurers in such jurisdictions, but that reciprocity was important to help prevent this from becoming a widespread practice that could eventually disadvantage US insurers. Responses from two regulators indicated a desire to discuss reciprocity more and as a result, language from RGA that incorporates the reciprocity was incorporated into the exposed draft to assist in such a discussion. More specifically, the language in (e) below was included to indicate that non-US groups otherwise exempt under either (c) or (d) below would NOT be exempt if the other jurisdiction required “subgroup reporting for a US group in that jurisdiction”, and would actually require the non-US group to file a “US subgroup GCC.” Note, subgroup reporting is ONLY required if done so first by another jurisdiction.

d. An insurance holding company whose non-U.S. group-wide supervisor, as determined in accordance with the principles of section 7.1, is located within a Reciprocal Jurisdiction [insert cross-reference to appropriate section of Credit for Reinsurance Law].

e. An insurance holding company:
   (iii) That has provided information to the accredited lead state, either directly or indirectly through the group-wide supervisor, who has determined such information is satisfactory to allow the lead-state to comply with the NAIC principles of group supervision as detailed in the NAIC Financial Analysis Handbook, and the lead state has determined that because of this the group capital calculation is not required to be filed; and
   (iv) Whose non-U.S. group-wide supervisor, as determined in accordance with the principles of section 7.1, meets either of the following requirements:
      a. Recognizes and accepts the group capital calculation for U.S. insurance groups who operate in the jurisdiction of that group-wide supervisor; or
      b. For jurisdictions where no U.S. insurance groups operate, recognizes the group capital calculation as an acceptable international capital standard by indicating such formally in writing to the lead state with a copy to the International Association of Insurance Supervisor.

f. The exemptions in Sections 4L(2)(c) and 4L(2)(d) shall not apply to the U.S. operations of a non-U.S. insurance holding company if its group-wide supervisor does not recognize and accept the group capital calculation for any U.S. insurance group’s operations in that group-wide supervisor’s jurisdiction.

Recommended Action:
NAIC staff recommends the Working Group further discuss if they support the subgroup reporting/RGA reciprocity concept. Even if the Working Group decides against retaining the language, further guidance will still need to be developed around a process of listing jurisdictions the NAIC considers having shown reciprocity to the GCC. If the Working Group decides for reciprocity, the language proposed by Met Life/Prudential/could serve as a possible language to be included in a model language that describes such a process. Doing so may also limit the need for incorporation of the specific language in the model act, but rather including in the model regulation that defines reciprocity in more detail, although all other reciprocity language included in the revised proposed draft could be retained in the Model Act. In summary, the model regulation could house this detail on reciprocity as well as the commissioner’s discretion to grant exemptions for groups below the ORSA thresholds, which is very detailed.
## Comments on Exposure

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<td>Issue #9- Expand Exemptions</td>
<td>Our suggestion is to expand the exemption criteria in Section 4L(2)(a) to include holding company groups with direction premiums less than $100,000,000.</td>
<td>NAMIC</td>
<td>68</td>
</tr>
</tbody>
</table>

**Staff Summary of the Issue:**
Some have recommended adding the following additional provision to 8(c)2:

> Notwithstanding paragraph (1) above, the commissioner may only share confidential and privileged documents, material, or information reported under Section 4L(2) with commissioners of states that are members of the subject insurer’s supervisory college, and whose states have statutes or regulations substantially similar to Subsection A and who have agreed in writing not to disclose such information.

**Recommended Action:**
NAIC staff notes that under the current exposure, all mutual insurance companies are exempt from filing the GCC since their ultimate controlling person is a U.S. regulated insurer that already completes an annual RBC filing and only need file the Schedule 1 and related analytics. NAIC staff further notes insurers with less than $1 billion in premium (which would include those with less than $100 million) can be exempted from the GCC if other limited requirements are met. Finally, NAIC staff notes that insurers that are not in a holding company structure (e.g. no other affiliates) would not be subject to the GCC as they are not subject to the Holding Company Act.

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<td>Issue #10- Confidentiality Language</td>
<td>We would request on minor change to Section 8 to reflect the intent of the GCC but also acknowledge the GCC not a tool to assess group risk, but rather as an additional tool to assess and insurer’s risk.</td>
<td>NAMIC</td>
<td>72</td>
</tr>
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**Staff Summary of the Issue:**
They recommend the following change:

> It is the judgement of the legislature that the group capital calculation and resulting group capital ratio required under Section 4L(2) is a regulatory tool for assessing group insurer’s risks and capital adequacy, and is not intended as a means to rank insurers or insurance holding company systems generally

**Recommended Action:**
NAIC staff disagrees, noting that the original language proposed from the Coalition accurately captures that the GCC is a tool for assessing group risk, even though we agree that the purpose of determining group risk is to evaluate its potential impact on the insurer. However, we believe the proposed language is inaccurate.
### Comments on Exposure

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<td><strong>Issue #11- Commissioner Authority for Further Exemptions</strong></td>
<td>The draft Act does not include language similar to Section 6(D) of the ORSA Model Act, which allows regulators to grant an ORSA exemption “based upon unique circumstances.” APCIA recommends including similar language in Sections 4(L)(2)(f) and (g) of the draft Act.</td>
<td>APCIA &amp; AHIP</td>
<td>12 &amp; 48</td>
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**Staff Summary of the Issue:**
This comment recommends the following additional exception authority be added:

> An insurer that does not qualify for exemption pursuant to subsections (e) and (f) may apply to the commissioner for a waiver from the requirements of this Act based upon unique circumstances. In deciding whether to grant the insurer’s request for waiver, the commissioner may consider the type and volume of business written, ownership and organizational structure, and any other factor the commissioner considers relevant to the insurer or insurance group of which the insurer is a member. If the insurer is part of an insurance group with insurers domiciled in more than one state, the commissioner shall coordinate with the lead state commissioner and with the other domiciliary commissioners in considering whether to grant the insurer’s request for a waiver.

**Recommended Action:**
This issue has not been discussed previously although NAIC staff has some concerns with this suggestion, specifically that a group that does business in a covered agreement jurisdiction could be exempted, creating an issue.

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<tr>
<td><strong>Issue #12- Deleting Language from Section 8A which applies to rest of Act</strong></td>
<td>ORSA Model 505 does not contain this language</td>
<td>AHIP</td>
<td>57</td>
</tr>
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**Staff Summary of the Issue:**
The language in reference is as follows but is currently part of the Form F and other existing HCA authorities for the Commissioner:

> The Commissioner shall not otherwise make the documents, materials or other information public without the prior written consent of the insurer to which it pertains unless the commissioner, after giving the insurer and its affiliates who would be affected thereby notice and opportunity to be heard, determines that the interest of policyholder, shareholder or the public will be served by the publication thereof, in which event the commissioner may publish all or any part in such manner as may be deemed appropriate.
Comments on Exposure

Recommended Action:
Some comments suggest deleting the language to mirror the Confidentiality of the Risk Management and Own Risk and Solvency Assessment Model Act (#505) with respect to ORSA Summary Report. However, this language is applicable to more than just the Group Capital Calculation, and consideration needs to be given to whether it is necessary to retain this authority for other aspects of this section, NAIC recommends this language not be deleted for this reason. NAIC staff is not opposed to AHIP proposing language that would specify this language is not applicable to the GCC.
Group Capital Calculation (E) Working Group
Conference Call
June 2, 2020

The Group Capital Calculation (E) Working Group of the Financial Condition (E) Committee met via conference call on June 2, 2020. The following Working Group members participated: David Altmaier, Chair (FL); Kathy Belfi, Vice Chair (CT); Kim Hudson (CA); Philip Barlow (DC); Carrie Mears, Mike Yanacheak and Kim Cross (IA); Susan Berry and Vincent Tsang (IL); Roy Eft (IN); John Turchi and Christopher Joyce (MA); Judy Weaver (MI); John Rehagen (MO); Jackie Obusek (NC); Justin Schrader and Lindsay Crawford (NE); Edward Kiffel (NY); Dale Bruggeman and Tim Biler (OH); Greg Lathrop (OR); Kimberly Rankin (PA); Trey Hancock (TN); Mike Boerner and Jamie Walker (TX); Doug Stolte and David Smith (VA); and Amy Malm (WI).

1. Discussed Further Modifications to Exposed Exemptions

Commissioner Altmaier stated that the purpose of this conference call is for the Working Group to consider whether further modifications are needed to the previously exposed exemptions on who would be required to file the group capital calculation (GCC). He described how the Working Group had received quite a bit of feedback on those exposed exemptions in the form of comments letters (Attachment Five-B1) and that the intent is to work through the comments based upon themes, where he will seek input from Working Group members on their views of each of the themes.

a. Size Threshold

Commissioner Altmaier stated that the previously exposed exemptions did not include the concept of a size threshold, be that the comments overwhelming support the concept of a size threshold like that contained within the Risk Management and Own Risk and Solvency Assessment Model Act (#505). Commissioner Altmaier stated that he believes most of the state insurance regulators were of the opinion that the GCC would be a tool that would be helpful for analysts for any group regardless of its size or where it writes its business, but that the Working Group should think about its characteristics and when it would be most helpful. He noted that the Working Group may determine that it may not be most useful for all groups and that care should be taken with the approach. He stated he believes that groups that do not meet the size exemptions of the Own Risk and Solvency Assessment (ORSA) or have international business are the types where state insurance regulators would want the GCC to be completed. He stated, however, that beyond that, he would be open to a proposal that authorized state insurance regulator discretion for groups that did not meet such a threshold. He stated that while there are some individuals that may be concerned with that type of discretion without any guiding principles or criteria, it would be important for the Working Group to consider how best to effectuate.

Mr. Schrader stated he thinks this is an important issue and that regardless of what approach the Working Group takes, either all groups filing or some type of threshold, he believes it is important to have regulatory discretion to either include or exclude those that are outside of the normal given the unique groups that exist. He stated he thinks the ORSA threshold may be a bit high because there were many groups under that threshold that were fairly complex, but that he is in favor of getting for all groups since analysts are expected to perform holding company analysis on all groups. However, if the analyst or state insurance regulators feel there is no value for that company, then they should have the authority to waive them. He stated with commissioner discretion, there is a potential for either a lot of companies to be exempted or no companies exempted. Commissioner Altmaier stated that was a reasonable viewpoint, particularly in the early years, until a determination can be made on how helpful the GCC was.

Mr. Eft stated he is in support of an ORSA exemption, but authority to exempt others if deemed necessary, but not cast as wide of an approach as suggested by Nebraska. Ms. Berry stated that Illinois was of the view that they wanted a threshold closer to the ORSA along with making sure companies with international business would still be captured, but they also see value in an exception where smaller companies are allowed to just file a listing out the companies and some of the other related information, but not the actual GCC itself. Commissioner Altmaier stated that could be helpful in developing a compromise position. Ms. Belfi stated that after listening to Mr. Schrader and others, what she would really like to do as a regulator is eventually let her largest entities to be completing the GCC only and originally was in the camp of the ORSA threshold. However, after thinking about what Mr. Schrader said, she said she does not think it would be a bad idea to cast a wide net to take a one-time look at their group and learn about the risks of the group. Ms. Belfi stated the fact these groups do not complete an ORSA may be a reason to obtain the GCC at least once. Then going forward, if the GCC is not particularly helpful, they could be exempted.
going forward. Mr. Barlow stated he supports Mr. Schrader and Ms. Belfi’s view where at least for the first year, the GCC should be completed and that the state insurance regulator should have to justify excluding a company as opposed to including it. He stated it is better to determine it is not needed based upon experience rather than not obtain it and recognize it should have been obtained. Mr. Hudson described that they were agreement with Ms. Belfi where they started in the ORSA exemption camp, but believe it would be helpful to initially obtain information for all groups.

Commissioner Altmaier stated there appears to be a consensus at least for those that provided their views, and while he expects discussions will need to continue, it would be helpful to first receive a written proposal. He requested NAIC staff to draft language where initially everyone should file the GCC, but lead states should have the discretion to exempt groups below the ORSA and international threshold, but for those that are exempted requiring a filing of the information from the inventory tab of the GCC. He stated ideally, information could be obtained on the number of groups affected, recognizing states’ resources are important. He stated future discussion on guardrails would be helpful as well. Stephen Broadie (American Property Casualty Insurance Association—APCIA) stated the APCIA supports an ORSA threshold and will continue to do so and listen with interest. He suggested the Working Group note that it would be difficult to revise the exemptions given the Working Group is considering putting the exemptions in the Insurance Holding Company System Regulatory Act (#440). Commissioner Altmaier agreed and noted they would be sensitive to that fact.

b. Accept the RBC Ratio as the GCC for a Top-Tiered RBC Filer

Commissioner Altmaier noted that for this issue, there was dovetail with the GCC Instructions. Therefore, he said he would like to postpone this discussion until after the exposure period on the GCC Instructions ends in the second half of July.

c. Accept the RBC Ratio as the GCC for a Top-Tiered RBC Filer

Commissioner Altmaier stated the Working Group has discussed this issue in the past and has generally stated it would not be in favor of any duplicative regulatory requirements and be open to not requiring the GCC for groups that are required to complete the building block approach (BAA) and file with the Federal Reserve. He stated that if states can obtain a copy of the BBA, he recalls this being the past position. Mr. Boerner agreed with the statements by Commissioner Altmaier. Mr. Schrader stated that until state insurance regulators see what the BBA looks like, there may still be some value of obtaining a listing of entities and related financial information for these groups like the recommendation made for smaller groups as previously made by Ms. Berry. Mariana Gomez-Vock (American Council of Life Insurers—ACLI) stated the ACLI strongly supports this recommendation. She stated the BBA has a similar schedule as the Inventory and other Federal Reserve forms and was quite extensive. Dale Berry (TIAA) indicated the TIAA supports the recommendation and stated he does not believe there is much daylight between the GCC and the BBA. Ms. Belfi stated that it might be helpful for NAIC staff to provide a comparison between the GCC and the BBA.

d. Reciprocal or Qualified Jurisdictions

Joseph Sieverling (Reinsurance Association of America—RAA) stated that the RAA supports this exemption because it supports the premise that groups should be subject to a single group capital measure per their group-wide supervisor. Andrew Vedder (Northwestern Mutual) stated that Northwestern Mutual, along with New York Life and Travelers, are generally supportive of this exemption but had some nuances—specifically, looking at the ORSA allowance to make available comparable information that is available to the insurance group to make sure the lead state has the relevant information, which is consistent with the approach being taken by the Working Group on the BBA. He stated under 4(L)2C, the definition of a reciprocal jurisdiction currently does not exempt U.S. groups, and this could be fixed by inserting non-U.S. before group-wide supervisor. Ian Adamczyk (Prudential Financial) stated Prudential Financial’s position is nuanced. He said while it supports the one group and one group standard, Prudential Financial views that from the perspective of applying that exemption at the worldwide level and does not believe the exemption should extend to U.S. subgroups of foreign-based insurers with U.S. subgroups. He summarized the points from Prudential Financial’s comment letter on this subgroup. Kim Welch (Reinsurance Group of America—RGA) stated RGA agrees with the principle of one group capital measure per one group-wide supervisor but that it disagrees with the concept of subgroup reporting. She stated that while the issue is hypothetical now, RGA sees it as a real possibility, and it is concerned that the current wording does not allow a determination of reciprocity. She discussed the need for U.S. regulators to have leverage to encourage reciprocity. She also stated RGA has concerns with the reciprocity in the qualified jurisdictions being limited to reinsurance and, therefore, the exemption should be limited to reciprocal jurisdictions. Matthew Wulf (Swiss Reinsurance Group) stated Swiss Reinsurance Group does not agree with Prudential and whether those concerns come into play, not to mention the difficulty of drawing a box around companies for U.S. subgroups.
Mr. Rehagen stated he believes reciprocity is a very important issue and thinks this is something the Working Group should consider.

e. Unintended Exemptions

Ms. Gomez-Vock stated she believes the conversation, as well as the current draft, may have addressed this issue. She did, however, describe how at some point in time it might be helpful to have a memorandum that describes each of the exemptions and the rationale for each.

f. Commissioner Discretion Concern

Commissioner Altmaier noted that this issue may have already been raised and asked if there were additional issues that required further discussion at this time. Mr. Sieverling stated he believes Commissioner Altmaier already covered this but noted that if the focus was on either scoping groups out of the calculation, that would make things easier but certainly being more specific on the criteria is what would be needed. Mr. Broadie agreed with Mr. Sieverling.

g. Commissioner Discretion Concern

Commissioner Altmaier discussed the importance of this issue and how it is a driving force behind embedding the GCC into a model law. He stated one comment suggested the need to address the confidentiality of the BBA if filed with the lead state, and he said he believes this is a fair comment. He asked Ms. Gomez-Vock if the ACLI could send language to NAIC staff for further consideration. He noted America’s Health Insurance Plans (AHIP) seemed to suggest the current language seems to allow the sharing of the GCC with the International Association of Insurance Supervisors (IAIS). It was noted this would be taken up on a future conference call. Commissioner Altmaier also noted Prudential made some comments. Mr. Adamczyk summarized some of Prudential’s concerns taken from its comment letter. There was no reaction from Working Group members on these comments.

2. Discussed Other Matters

Commissioner Altmaier indicated NAIC staff had drafted a Frequently Asked Questions (FAQ) document and for individuals to be aware it will be posted. He also indicated that NAIC staff was intending to hold a webinar to those wishing to participate in understanding how the GCC is intended to work; it would not be an official meeting of the Working Group.

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

State Farm Mutual® Automobile Insurance Company and its affiliates ("State Farm"), appreciate the opportunity to submit these comments concerning the Draft Memorandum ("Draft Memo") from the Group Capital Calculation (E) Working Group (the "Working Group") to the Chair of the Group Solvency Issues (E) Working Group ("GSI"), Mr. Justin Schrader (NE). The Working Group is charged with constructing a U.S. group capital calculation (the "GCC") using a risk-based capital ("RBC") aggregation approach.

The stated purpose of the Draft Memo is to seek assistance from the GSI in drafting changes to existing National Association of Insurance Commissioners ("NAIC") model laws. The noted needed changes are to create a requirement that the GCC be completed annually and that confidentiality be provided. To that end the Draft Memo makes the following suggested changes to two different sections of NAIC’s Holding Company Act, Model #440:

**Section 4**

- Require a new item “M” that requires submission of an annual GCC to the lead state regulator (like Item L Enterprise Risk Filing) through a new Form G filing required by the *Insurance Holding Company System Model Regulation with Reporting Forms and Instructions* (#450).
- Specify the following entities as being exempt from the GCC:
  - Small mutual insurance companies (similar to the exemption in the *Annual Financial Reporting Model Regulation* (#205)).
  - Groups required to file with the U.S. Federal Reserve, but separately require that such groups provide a copy of the filing with the Federal Reserve to file to the lead state.
  - Groups for which the group-wide supervisor is a reciprocal or qualified jurisdiction per the Credit for Reinsurance Model Law (#785).
• Group not considered a reciprocal or qualified jurisdiction but for which the group-wide supervisor: i) accepts the GCC for any U.S. insurance group; or ii) recognizes the GCC as an acceptable international capital standard to the International Association of Insurance Supervisors (IAIS); and iii) has been sponsored by an accredited lead-state.

• With respect to the exemptions, the model should provide the lead state commissioner the authority to require the GCC of any group otherwise determined to be exempt, like the language in the Own Risk and Solvency Assessment (ORSA). Also, with respect to a company previously exempt, the model should provide appropriate transition guidance.

Section 8.1
• Confidentiality language consistent with that recommended by a comment letter directed to the Working Group from the Coalition (see attached) which, among other things, prohibits the filing of the report with the NAIC unless supported by a confidentiality agreement (similar to the Risk Management and Own Risk and Solvency Assessment Model Act [#505]).

State Farm appreciates the effort and transparency the Working Group has utilized in developing the GCC. State Farm participated as a volunteer group and provided feedback as to the GCC calculation and its supporting informational elements during its development. State Farm understands that the GCC provides an evaluation tool for domestic regulators to consider along with various other risk information provided by groups such as the ORSA Report filing.

However, State Farm is concerned that the Draft Memo should include additional exemptions and recognitions. As noted above, State Farm participated as a volunteer company with the development of the GCC, but it also participated in the Qualitative Impact Study (“QIS”) on the U.S. Federal Reserve Notice of Proposed Rulemaking (“NPR”) concerning its development of group capital calculation and corresponding capital requirements. State Farm notes that the calculation of the NPR is very similar to the GCC and both generated very similar results for State Farm. This similarly was by design as noted by the NAIC President’s opening remarks at the Fall 2019 meeting.¹

State Farm noted that the similarity in results is due to the basis of the calculations that start with an aggregation method based on the Risk Based Capital (“RBC”) calculation for insurers, the assets and liabilities being measured are predominately derived by the business of insurance and the parent of the holding company is itself a regulated insurance entity. In fact, the NPR, GCC, as well as the RBC, generate substantially the same ratio results. State Farm asserts if the

Working Group is suggesting that groups filing with the Federal Reserve or other equivalent regulatory schemes should be exempt, that a similar exemption should be included for groups when the expected results of the GCC are similar to the RBC for a regulated insurer parent of a group that predominately derives its assets and liabilities from the business of insurance as it is another equivalent regulatory framework used by regulators.

State Farm appreciates the Working Group recognizing the duplicative effort and willingness to utilize other equivalent regulatory processes and information. In the case of State Farm, and other similarly situated groups, it should be recognized that State Farm Mutual Automobile Insurance Company’s (“State Farm Mutual”) RBC provides equivalent regulatory information that should be accepted in lieu of the GCC. State Farm Mutual’s RBC rolls up the assets and liabilities of its affiliates and subsidiaries utilizing the same aggregate approach after which the GCC is modeled, with only those non-insurance entities receiving a slightly different scaled calculation in the GCC that makes up less than a few percentage points of State Farm’s overall assets and liabilities. As a result of the assets and liabilities being so heavily based on the business of insurance, the results of the GCC are not significantly different than the RBC. The result was expected by the Working Group and State Farm, and unsurprisingly, the Federal Reserve also expected the NPR, under the similar aggregation method, would produce near the same result as the RBC for State Farm Mutual.

The domestic regulator that manages the solvency of the entities that make up such a group, which receives an abundance of financial information such as receiving quarterly and annual financial statements, holding company filings, ORSA, Form F and individual legal entity RBC calculations, is in the best position to determine if such exemption is appropriate. This is especially true when the group is predominately conducting the business of insurance. Furthermore, as proposed in the Draft Memo, the domestic regulator will have the ability to require a group to complete the GCC regardless of the exemption. Groups should not be required to complete the GCC for the sake of uniformity especially when the proposal is already exempting groups for the various stated reasons and when completion of the GCC does not provide any additional insight to the domestic regulator who is charged with the responsibility to regulate solvency.

The GCC is requesting information that the domestic regulator already receives or has access to if the domestic regulator deems it necessary to evaluate the risk of the group. State Farm is not aware of any specific information contained in the GCC that is not already available to its domestic regulators and does not believe that the GCC needs to apply to State Farm, or any other group, for that purpose. The domestic regulator has information on financial institutions it does not regulate, such as State Farm Bank, as a result of Supervisory Colleges and through the provisions of the Holding Company Act.
Since the Working Group is willing to exempt a group on the basis of its filing with the Federal Reserve presumably being deemed equivalent to the GCC as well as the other stated exemptions, the Working Group should not argue against an exemption for a group, such as State Farm, for the reason that the GCC provides new information. There is no new information provided in the GCC that is not already provided to the domestic regulator and, if there is any information not already provided, it most likely pertains to an immaterial aspect of the group that is mainly an insurance business.

State Farm is concerned that the GCC may be needlessly applied to State Farm and other similarly situated insurers for the purported purpose of satisfying an international regulatory standard and Covered Agreement.\(^2\) State Farm does not believe that uniform application of the GCC is necessary when such groups are not internationally active and there is an equivalent regulatory tool. A group like State Farm should not have to pass along the costs to its policyholders as a result of a uniform application of the GCC so that internationally active groups are not confronted with dual regulation. The presumed driver of this is the Covered Agreement, however, State Farm is not aware that the Covered Agreement requires the uniform application and suggests that for those internationally active groups that desire to be regulated under a single regulator that those groups can opt into completing the GCC.

State Farm urges the Working Group to include a stated exemption for a group when that group’s parent is a regulated insurance company that files under the Risk Based Capital provisions with an accredited lead state by amending the Draft Memo to include the following language in the suggested changes to Section 4 of Model #440:

Specify the following entities as being exempt from the GCC:

Groups required to file with the U.S. Federal Reserve an equivalent group solvency calculation, but separately require that such groups provide a copy of the filing with the Federal Reserve to file to the lead state; or a group when that group’s parent is regulated insurance company that files under the Risk Based Capital provisions with an accredited lead state.

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As an alternative to an explicit exemption as suggested above, State Farm requests that the Working Group amend the Draft Memo to include generic authority to exempt a group from filing the GCC similar to the ORSA provision of Model #505 which provides:

D. An insurer that does not qualify for exemption pursuant to subsection A may apply to the commissioner for a waiver from the requirements of this Act based upon unique circumstances. In deciding whether to grant the insurer's request for waiver, the commissioner may consider the type and volume of business written, ownership and organizational structure, and any other factor the commissioner considers relevant to the insurer or insurance group of which the insurer is a member. If the insurer is part of an insurance group with insurers domiciled in more than one state, the commissioner shall coordinate with the lead state commissioner and with the other domiciliary commissioners in considering whether to grant the insurer's request for a waiver.

This would allow the domestic regulator to determine the need for a group to complete the GCC on a case by case basis and for any number of reasons. Adding such a provision also is balanced in that the Working Group in the Draft Memo is already suggesting that Section 4 include the ORSA provision to require a group to complete the GCC regardless of whether that group otherwise is exempted.

Finally, State Farm would like to take this opportunity to comment on the GCC calculation process. State Farm urges the Working Group to limit the “destacking” of entities within the GCC when entities are subsidiaries of RBC filing insurance companies. This dramatically reduces the burden in completing the GCC, especially for more streamlined organizations. In addition, State Farm requests that the Working Group consider a materiality threshold in the requirements to reduce the burden of including entities that do not impact the overall GCC result.

If the GSI proposes amendments to the NAIC’s Holding Company Act, Model #440, State Farm will comment more fully on the language of that proposal.

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

Sincerely,

Chuck Feinen
State Farm Mutual Automobile Insurance Company
February 13, 2020

Dan Daveline  
Director, Financial Regulatory Services  
NAIC  
Submitted via Email  

Re:  Draft Letter to Chair of the Group Solvency Issues (E) Working Group  
Regarding Confidentiality of Group Capital Calculation  

Dear Mr. Daveline:

Teachers Insurance and Annuity Association of America (“TIAA”) appreciates the opportunity to submit the following comments in response to the draft letter (the “Draft Letter”) from the Chair of the National Association of Insurance Commissioners’ (“NAIC”) Group Capital Calculation (E) Working Group (the “GCC Working Group”) to the Chair of the NAIC Group Solvency Issues (E) Working Group regarding the confidentiality of the proposed group capital calculation (“GCC”).1 Below, we provide our thoughts in response to certain sections of the Draft Letter. We hope that our ideas and suggestions will assist the NAIC as it considers revising its Insurance Holding Company System Regulatory Act (#440) (“Model #440”).

About TIAA

Founded in 1918, TIAA is a life insurance company and the leading provider of retirement and financial services for those in academic, research, medical, and cultural fields. Over our century-long history, TIAA’s mission has always been to aid and strengthen the institutions and participants we serve and to provide life insurance and other financial products that meet their needs. To carry out this mission, we have evolved to include a range of financial services, including asset management and retail services. Today, TIAA manages over $1

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trillion in assets, and our investment model and long-term approach aim to benefit the five
million retirement plan participants we serve across more than 15,000 institutions.2 With our
strong nonprofit heritage, we remain committed to the mission we embarked on in 1918 of
serving the financial needs of those who serve the greater good.

**TIAA supports the proposed exemption for groups required to file with the Federal Reserve.**

The Draft Letter proposes that groups required to file with the Board of Governors of the
Federal Reserve System (the “Federal Reserve”) be exempt from the requirement to file an
annual GCC (as a prospective Form G or other filing), so long as they are separately
required to provide a copy of their Federal Reserve capital requirement filings to their lead
state regulator. TIAA strongly supports this proposed exemption. TIAA is subject to
regulation and supervision by the Federal Reserve as a savings-and-loan holding company
significantly engaged in the business of insurance (an “Insurance SLHC”). As the NAIC is
aware, the Federal Reserve recently proposed capital requirements that are designed
specifically for Insurance SLHCs, which we expect will be finalized later this year. The
Federal Reserve’s proposed approach would construct “building blocks,” or groups of
entities in the Insurance SLHC’s organization that are covered under the same capital
framework, to calculate an entity’s combined, enterprise-level available capital and capital
requirement. The Federal Reserve has also proposed a capital conservation buffer that
Insurance SLHCs must meet to avoid certain restrictions in addition to the minimum capital
requirement.

We believe the Federal Reserve’s proposed approach is not only appropriately tailored to
the unique business model of insurers but also generally consistent with the approach and
requirements of the GCC. As such, we think it is appropriate for Insurance SLHCs like TIAA
and other groups required to file with the Federal Reserve to be exempt from the annual
GCC filing requirement, so long as such entities provide a copy of their Federal Reserve
capital requirement submission to their lead state regulator. This approach would ensure
that Federal Reserve-supervised insurance companies are covered under a sufficiently
stringent enterprise-wise capital framework (with sufficient line of sight for their state
regulators), but are not subject to a needlessly duplicative regulatory regime under the GCC.

**TIAA supports the proposed addition of confidentiality language to Model #440.**

The Draft Letter proposes to include in Model #440 GCC-specific confidentiality language
consistent with the NAIC’s Own Risk and Solvency Assessment (“ORSA”) confidentiality
language, as set forth in the *Risk Management and Own Risk & Solvency Assessment*

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2 Data are as of September 30, 2019.
Model Act ("Model #505"). This proposal echoes a recommendation made in a comment letter regarding GCC confidentiality directed to the GCC Working Group from a coalition of ten companies.³ TIAA supports the addition of the proposed confidentiality language. We believe entities’ GCC information, including any Federal Reserve capital requirement submissions to lead state regulators, should receive the highest level of confidential treatment, and should not be disclosed by the NAIC or any other entity for any non-regulatory purpose. For this reason, we believe that adding broad confidentiality provisions to Model #440, including provisions that would prevent public disclosure of any entity’s GCC filings, would be appropriate. We encourage the NAIC to adopt the approach recommended by the Coalition to ensure that sensitive GCC information is adequately protected.

Conclusion

TIAA commends the GCC Working Group for its focus on these issues, and we appreciate the opportunity to comment on the Draft Letter. We hope our suggestions above prove helpful as the NAIC continues working to formulate a robust GCC framework. We would welcome the opportunity to engage further on any aspects of this letter.

Sincerely,

Bret C. Hester

Via Electronic Mail

February 14, 2020

Commissioner David Altmaier, Chair
NAIC Group Capital Calculation Working Group
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

Mr. Dan Daveline
Director, Financial Regulatory Services
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

RE: Comments on Group Capital Calculation Referral Letter

Dear Messrs. Altmaier and Daveline:

The Reinsurance Association of America (RAA), headquartered in Washington, D.C., is the leading trade association of property and casualty reinsurers doing business in the United States. The RAA is committed to promoting a regulatory environment that ensures the industry remains globally competitive and financially robust. RAA membership is diverse, including reinsurance underwriters and intermediaries licensed in the U.S. and those that conduct business on a cross border basis.

The RAA appreciates the opportunity to comment on the draft Group Capital Calculation (GCC) referral letter to the Group Solvency Issues Working Group regarding the scope of application of the GCC, confidentiality protections and establishing the regulatory authority to require annual GCC filings. We agree that the insurance holding company act and regulation (NAIC Models 440 and 450) are the appropriate locations to incorporate the regulatory authority and guidance for annual GCC reporting.

Scope Exemptions:
The RAA’s longstanding position on group capital measures is centered on the premise that insurance groups should only be subject to a single group capital measure and only be subject to group supervision administered by their global group-wide supervisor. An important corollary to this position is that insurance groups should not be subject to multiple group capital measures and related requirements applied extraterritorially, whether they involve U.S. based multinational insurance groups or Non-U.S. groups with operations in the United States. This position appears broadly held as it was a central theme in the coalition of U.S. insurance trades’ comments on the NAIC’s August 7, 2018 Scope of Group Testing Memorandum.
Viewed through this prism, the RAA supports the scope exemption proposals outlined in the draft referral letter, subject to the following suggestions or clarifications:

- We support an exemption for small groups but believe the $1M annual premium threshold referenced from NAIC model #205 is too low. While it is important that nearly all insurance entities have annual statutory audits, requiring a GCC for all these groups appears unnecessary and overly burdensome. The coalition of trades suggested in 2018 that a better exemption threshold would be the ORSA standard, which is $1B in annual premium. The RAA still supports an ORSA based threshold, but if the NAIC determines that this threshold is too high, we suggest it consider adopting a threshold such as the $500M threshold used in section 17 of model #205 regarding Management’s Report of Internal Control over Financial Reporting. The NAIC/AICPA working group annually monitors this threshold, which currently encompasses over 93% of U.S. gross premium.
- We support the proposed exemption for groups regulated by the Federal Reserve because it would avoid duplicative group capital filing requirements.
- We support the proposed exemptions for groups domiciled in a reciprocal or qualified jurisdiction under the Credit for Reinsurance Model Law and for groups supervised by jurisdictions that recognize the GCC as an acceptable international capital standard comparable with the ICS. This proposal is essentially identical to the industry position outlined in the August 2018 trade coalition letter on scope issues.

Commissioner Discretion:
The RAA is concerned that the proposal to grant commissioner discretion to require the GCC for insurance groups otherwise exempt could be too broad. The language in the referral letter refers to ORSA guidance, but that guidance is expansive. The ORSA guidance manual lists several very general factors as examples that could justify an otherwise exempt entity having to file an ORSA, but the judgment ultimately depends on “unique circumstances” that are undefined. The ORSA model #505, provides better and more specific examples such as triggering an RBC action level or being deemed to be in hazardous financial condition, but these are only examples used within a context of broad commissioner discretion.

The RAA believes that any provision for commissioner discretion to disregard the scope exceptions to the GCC described above should be both distinct and limited. The exercise of broad commissioner discretion in this regard could violate the terms of the US/EU Covered Agreement, which provides relatively narrow exceptions for Host supervisors to impose group solvency requirements on Home party insurance or reinsurance groups. Recognizing that the discretion granted in the covered agreement applies to both parties, it follows that states should prefer provisions that limit any potential application of multiple capital requirements to insurance groups, since they would affect U.S. based groups as well.

Except for narrow circumstances relating to identifiable solvency concerns, each insurance group should be subject to only one group capital requirement and only the single group-wide supervisor should require a group capital measurement. Foreign supervised insurance groups should generally be exempt from the GCC and U.S.-based insurance groups should be accorded reciprocal treatment in non-U.S. jurisdictions.
Confidentiality:
The RAA supports strong confidentiality protections to prevent disclosure of GCC results. Such protections should be both explicit and robust and should preclude disclosure of any group’s GCC outside the regulatory community, whether by regulators, their consultants or by insurance groups themselves. We reviewed the July 30, 2019 “confidentiality coalition” letter referenced in the referral memorandum and broadly agree with their recommended revisions to Section 8 of NAIC Model #440.

Thank you for the opportunity to provide these comments. We look forward to continued discussion of these issues at future working group meetings.

Sincerely,

Joseph B. Sieverling
Senior Vice President
February 17, 2020

Commissioner David Altmaier
Florida Office of Insurance Regulation
Chairman, NAIC Group Capital Calculation (E) Working Group
via email to Dan Daveline ddaveline@naic.org

Re: "Confidentiality of Group Capital Calculation" Memorandum

Dear Commissioner Altmaier:

A coalition of 16 companies (Athene Holding Ltd., Brighthouse Financial, CNO Financial, Genworth Financial, Global Atlantic Financial Group, Hannover Life Reassurance Company of America, Jackson National Life Insurance, Lincoln Financial Group, National Life Group, Ohio National, Principal Financial Group, Protective Life, Reinsurance Group of America, Sammons Financial Group, Standard Insurance Company/StanCorp Financial Group, and Transamerica; collectively, the “Coalition”) appreciates the opportunity to respond to the memorandum (the "Memorandum") from the Chair of the Group Capital Calculation (GCC) Working Group (GCCWG) to the Chair of the Group Solvency Issues Working Group (GSIWG), regarding "Confidentiality of Group Capital Calculation.” The Coalition's primary purpose is to advocate for the creation of a GCC that is faithful to domestic state legal entity rules.

In its Memorandum, the GCCWG states that it seeks assistance from the GSIWG to open the Insurance Holding Company System Regulatory Act (#440) (the “Holding Company Act”) so that "confidentiality protection and other legal authorities needed for the GCC” can be incorporated into the Holding Company Act. The Coalition agrees that statutory authority is necessary to govern the confidentiality and scope (and potentially other facets) of the GCC, and that the use of the Holding Company Act is appropriate for this purpose.

The Coalition does not have a collective view on issues relating to scope, but scope is of interest to many Coalition companies, and individual companies may separately provide comments on the topic. Regarding confidentiality, we appreciate that Commissioner Altmaier's Memorandum suggests to the GSIWG that the starting point for GCC confidentiality-related Holding Company Act amendments be the Coalition letter of July 30, 2019. As set forth in that letter, the Coalition believes that individual group GCCs be subject to the most robust confidentiality protection allowed by law. This would include prohibiting companies from disclosing their own GCC results, because doing so will help alleviate some of the competitive playing field issues that the GCC could create. We refer the GCCWG to the Coalition letter of July 30 for a comprehensive discussion of why such a high level of confidentiality would be needed for GCC results and for suggested amendments to the Holding Company Act to cover the confidentiality issue.

We also note that the NAIC’s accreditation standards require states to adopt the Holding Company Act in substantially similar form to the Model itself. Thus, in amending the Holding Company Act, the Coalition urges the NAIC to ensure that all of the due process
protections surrounding the adoption of accreditation standards are applied to GCC-related Holding Company Act changes.

Finally, the Coalition would oppose any effort to amend the Holding Company Act such that the GCC would be permitted to deviate from state legal entity rules, particularly with respect to the issue of “on-top adjustments” to statutory capital where such capital is included in an insurance company’s RBC. It is the Coalition’s firm belief that it would be inappropriate for the GCC to deviate from legal entity rules, when such rules have been considered and passed by the NAIC with all necessary due process protections, and relied upon by many insurance companies in making now virtually irreversible capital deployment decisions. Our objection to permitting the GCC to deviate from legal entity rules includes not only to draft model law/model regulation language, but also to any guidance manual or similar NAIC document that would instruct groups as to how to complete the GCC.

The Coalition thanks the GCCWG for permitting us to comment on the Memorandum, and remains available to answer any questions that the GCCWG may have.

Regards,

Athene Holding Ltd.
Brighthouse Financial
CNO Financial
Genworth Financial
Global Atlantic Financial Group
Hannover Life Reassurance Company of America
Jackson National Life Insurance
Lincoln Financial Group
National Life Group
Ohio National
Principal Financial Group
Protective Life
Reinsurance Group of America
Sammons Financial Group
Standard Insurance Company/StanCorp Financial Group
Transamerica
February 17, 2020

Via Electronic Delivery

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

Attention: Dan Daveline

Re: GCC - Draft Memo on Confidentiality and Exemptions

Commissioner Altmaier:

We appreciate the opportunity to comment on your draft memo (the “Memo”) on behalf of the Group Capital Calculation (E) Working Group (“GCCWG”) addressed to the Chair of the Group Solvency Issues (E) Working Group regarding potential exemptions from the GCC requirement and confidentiality of GCC reporting.

We continue to support the NAIC’s development of a group capital calculation (“GCC”). We believe that the calculation, if designed appropriately, will provide a useful supervisory tool to assist lead states in analyzing the financial condition of insurance groups by complementing entity-based solvency requirements.

Our primary purpose in writing today is to address the Memo’s proposal on how to identify insurance groups that will be exempt from the GCC (i.e., those that will be outside the “scope of application” of the GCC). As we have observed in prior comments, the scope of application should be a function of the purpose that the GCC is expected to serve. The NAIC’s GCC proposal document as of December 7, 2019, references the need to provide a consistent and coherent analytical framework to better understand an insurance group’s financial risk profile for the purpose of enhancing protection of policyholders. The scope of application should be sufficiently broad such that this need is met, while at the same time avoiding unnecessary burdens for groups for which this perspective would not provide a supervisory benefit or would be duplicative of tools already available to state insurance regulators.

As we have previously commented, to the extent limits are placed on the scope of application, we believe these should align with other risk focused regulatory tools such as the Own Risk and Solvency Assessment (the “ORSA”). Doing so would ensure consistency across risk focused regulatory tools, provide enhanced insight into risk across a material portion of the U.S.
insurance market rather than a narrow subset of it, and maintain a level regulatory playing field for the industry.

With that background, we are generally supportive of the exemptions proposed in the Memo. We believe the exemptions could be improved, however, through better alignment with the concepts embodied in the Risk Management and Own Risk and Solvency Assessment Model Act (#505) and in the NAIC Own Risk and Solvency Assessment (ORSA) Guidance Manual. First, the ORSA exemption for small companies sets a higher size threshold than that proposed in the Memo. The ORSA threshold may strike a better baseline balance between cost and benefit for the use of available state insurance regulatory and insurer resources. Second, ORSA provides that an insurer may comply with the reporting requirement by submitting a report including comparable information that is submitted to a supervisor or regulator of a foreign jurisdiction. This concept may be implied within the third and fourth bullets of the GCC exemption mechanism, but it may be desirable to fully articulate this in order to ensure that state insurance regulators have access to relevant group capital results applicable to the insurers that they regulate. Lastly, we support the provision in the Memo that gives the lead state commissioner the authority to require the GCC reporting of any group otherwise determined to be exempt, the same as the provision in the ORSA requirement.

We also note that the definition of “Reciprocal Jurisdiction” per the Credit for Reinsurance Model Law (#785) includes a U.S. jurisdiction that meets NAIC accreditation standards. We believe this reference is unintentional and would not be the basis for an exemption from the GCC; however, if it was intended to be included, additional explanation is needed to better understand the intent.

On the secondary issue, i.e., confidentiality of GCC reporting, now that the mechanism for establishing the GCC requirement has been confirmed, we do not object to the confidentiality treatment proposed by the Memo. That said, if it is desirable from a regulatory perspective for the NAIC to align the GCC confidentiality language to better match the terms of existing confidentiality language, our first preference would be the language used within the ORSA requirement and secondarily, the Holding Company Model Law.

* * *

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We are grateful for your time and attention to our comments. If you would like to discuss this letter with us, please let us know.

Sincerely,

Douglas A. Wheeler  
Senior Vice President  
Office of Governmental Affairs  
New York Life Insurance Company

Andrew T. Vedder  
Vice President - Solvency Policy & Risk Management  
The Northwestern Mutual Life Insurance Company

D. Keith Bell  
Senior Vice President  
Corporate Finance  
The Travelers Companies, Inc.
February 13, 2020

Commissioner David Altmaier
Chair, Group Capital Calculation (E) Working Group
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1500
Kansas City, MO 64106

VIA Email Transmission: ddaveline@naic.org; lfelice@naic.org

RE: NAMIC Comments on Draft Memorandum to the Group Solvency Issues (E) Working Group from the Group Capital Calculation (E) Working Group Requesting Assistance on Drafting and Adopting Changes to NAIC Models

Dear Mr. Altmaier:

The following comments are submitted on behalf of the member companies of the National Association of Mutual Insurance Companies regarding the draft memorandum to the Group Solvency Issues Working Group that was made public on January 8. The memorandum serves as a request for assistance from the GSIWG in drafting and adopting needed changes to the Insurance Holding Company System Regulatory Act (#440) and Insurance Holding Company System Model Regulation (#450). We appreciate the opportunity to provide comments and to participate in discussions that will ultimately lead to the development and adoption of an insurance group capital assessment tool.

The changes currently contemplated and communicated in the memorandum would be to both Model #440 and #450, including adding a new filing requirement - an annual GCC report – to be filed by the ultimate controlling parent with the lead state regulator. This change will involve a similar process to what the NAIC did in 2010 when they added the annual enterprise risk report; that required a change to both Models, including adding a new filing form to Model #450. In this case, the memorandum recommends the addition of a Form G to collect GCC information. Additional changes contemplated by the working group to Model #440 include adding exemption criteria to determine who is required to file the GCC and amending the confidentiality section so that it is similar to the language included in the Risk Management and Own Risk and Solvency Assessment Model Act (#505).

1 NAMIC is the largest property/casualty insurance trade association in the country, with more than 1,400-member companies representing 39 percent of the total market. NAMIC supports regional and local mutual insurance companies on main streets across America and many of the country’s largest national insurers. NAMIC member companies serve more than 170 million policyholders and write more than $230 billion in annual premiums. Our members account for 54 percent of homeowners, 43 percent of automobile, and 32 percent of the business insurance markets. Through our advocacy programs we promote public policy solutions that benefit NAMIC member companies and the policyholders they serve and foster greater understanding and recognition of the unique alignment of interests between management and policyholders of mutual companies.
NAMIC members are supportive of amending both Model #440 and #450 as a means to provide exemptions based on certain criteria and to include strong confidentiality protection for documents, communications, and workpapers (created or received by regulators) used for the production of the GCC. However, we have significant concerns with the exemption criteria recommendation and suggest amending the memorandum before it is sent to the GSIWG. While we appreciate the thought given to exempting companies that may have to comply with more than one capital aggregation approach and companies of the very smallest size, NAMIC would suggest, as we have from the beginning of this project, for the NAIC to take a more proportional and principled approach to exemption criteria, similar to how other NAIC solvency models have incorporated these concepts. In addition to a size-threshold exemption similar to ORSA and the Model Audit Rule, NAMIC recommends that the lead-state regulator be allowed to accept the RBC results of a top-tier insurance regulated entity domiciled in their state if those results are substantially similar to expected GCC results. The remainder of our letter will go into more detail regarding our rational for these recommendations and will also provide other suggestions for the working group to consider.

Size-Related Exemption from Group Capital Calculation Reports

NAMIC recommends that small insurers – including those with less than $500 million in direct written premium – should be exempted from the proposed Group Capital Calculation Report (Form G) filing requirement. There is precedent for exempting small companies from the provisions of other NAIC models:

- The Risk Management Own Risk and Solvency Assessment model act exempts small companies (i.e., premium threshold of $500 million for individual insurers or $1 billion for an insurance group).

- The Model Audit Rule exempts insurers with less than $500 million of annual direct written and assumed premium from the requirement that they file a Management Report of Internal Control over Financial Reporting.

Small insurers are being treated to one-size fits all regulatory requirements related to many different NAIC models. The ERR (Form F) is just one of the many requirements that does not balance the cost vs. the benefit for small insurers. Further, the Corporate Governance Annual Disclosure provides no distinction to the size of insurer and requires corporate governance information for companies of all sizes. Each new requirement, filing, or report adds to the expense of providing insurance products. This added expense impacts small companies disproportionately. Mutual insurers feel a particular responsibility to their customers to do everything they can to make policymakers aware of the expense impact of each new requirement.

Both the ERR and CGAD, along with RBC, help regulators assess the risk within an organization. Adding a new GCC filing form on top of the existing Form F will be viewed as duplicative for these smaller groups and others, as the purpose of both tools is to help regulators assess the risks coming from other non-insurance organizations within a groups’ structure.

It is important to understand that while any new requirement presents potential concerns and uncertainty for all companies, larger companies employ full-time legal, internal audit, accounting, finance, and enterprise risk management staff. There will
still be a cost for these large companies as there is for any new form requirement, but without a doubt, the cost of compliance and accuracy is a higher percentage of annual revenue for small companies. NAMIC strongly feels that proportionality needs to be part of the discussion when deciding on exemption criteria. Given that, NAMIC recommends modifying the second bullet in the draft memorandum regarding Section 4 to read:

Small mutual insurance companies that have annual direct written and unaffiliated assumed premiums of less than $500,000,000 for individual insurers or $1 billion for an insurance group (excluding premiums reinsured with the Federal Crop Insurance Corporation and Federal Flood Program) (similar to the exemption in the Annual Financial Reporting Model Regulation (#205 Risk Management Own Risk and Solvency Assessment Model Act (#505)).

Accept Ultimate Controlling Parent RBC if GCC Expected Results are Similar

The primary purpose of the GCC is to help regulators understand large and complex groups. NAMIC members have long held the view that where the ultimate controlling parent is an underwriting company that directly or indirectly owns or controls all of the other entities within the group, that the annual RBC report of the UCP should be an acceptable alternative to reporting a GCC. NAMIC members that have participated in field-testing exercises where the top-tier entity is an insurance underwriter that files RBC have concluded that annual RBC is substantially similar to the expected results of the GCC.

As we’ve stated in our comment letter to the Federal Reserve on their Building Block Approach to group capital, U.S. RBC for a top-tier insurance underwriting holding company is a proxy for consolidation. For a top-tier insurance underwriting holding company, all the activities and investments made, including in any subsidiary insurers are rolled up into the parent’s insurance RBC calculation. The existing insurance RBC formula already incorporates necessary adjustments for inter-affiliate transactions, such as capital invested in a subsidiary by the parent; thus, the top-tier insurance underwriting holding company RBC is, in effect a consolidated view of the group’s capital position. For these reasons, NAMIC believes the draft memorandum should be amended to include language that would exempt an UCP that is an RBC filer from having to file an annual GCC report. In lieu of requiring an annual GCC report, the lead-state regulator would accept the groups’ annual RBC, as these results would be substantially similar to the expected results of a GCC.

In consideration of including language around exempting an UCP that is an RBC filer, NAMIC recommends that an additional bullet be added to the list of entities exempt from the GCC in the draft memorandum:

The model should provide flexibility to accept annual RBC where the ultimate controlling parent is an underwriting company, as the expected results of the GCC would be substantially similar to RBC in lieu of requiring an annual GCC report.
Confidentiality

NAMIC is supportive of modifying the confidentiality provisions within the HCA to mirror the language included in the ORSA model. Of particular importance is including language about documents, communications, and workpapers that have been created by or received by other regulators as part of the analysis of the GCC. Because the information that will be submitted to regulators will be used to analyze various stress scenarios and testing options, protecting any information that would be created by regulators and subsequently shared with other regulators in order to complete their analysis of the GCC is of utmost importance to NAMIC members.

Thank you for your consideration of these comments on this matter of importance to NAMIC, its member companies and their policyholders. If there are any questions, please feel free to contact me at 317-876-4206.

Sincerely,

[Signature]

Jonathan Rodgers
Director of Financial and Tax Policy
National Association of Mutual Insurance Companies
February 17, 2020

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

Re: Referral Memorandum on Changes to the Insurance Holding Company Regulatory Act (#440)

Dear Commissioner Altmaier:

The American Property Casualty Insurance Association (APCIA) appreciates the opportunity to comment on the Group Capital Calculation (E) Working Group’s referral memorandum regarding amendments to the Insurance Holding Company Regulatory Model Act (#440) to incorporate the Group Capital Calculation (GCC). APCIA is the primary national trade association for home, auto, and business insurers. APCIA promotes and protects the viability of private competition for the benefit of consumers and insurers, with a legacy dating back 150 years. APCIA members represent all sizes, structures, and regions—protecting families, communities, and businesses in the U.S. and across the globe.

Exemption for Groups Subject to Another Group-Wide Capital Assessment

The referral memorandum specifies four classifications of groups to be exempt from the GCC. However, the memo also recommends that lead state commissioners have the authority to require the GCC of any group otherwise determined to be exempt. APCIA is concerned with the recommendation to grant commissioners the authority to require the GCC from exempt groups—particularly for groups that are already subject to a group-wide capital assessment. Insurers should not be required to comply with more than one group-wide capital measure. Groups subject to the Federal Reserve’s Building Block Approach (BBA), as well as insurers with a group-wide supervisor in a Reciprocal Jurisdiction outside the United States, should be, without exception, exempt from the GCC.

For groups required to file with the Federal Reserve, the exemption contemplated in the referral memorandum would require a copy to be filed with the lead state. Similarly, for insurers where the group-wide supervisor is a Reciprocal Jurisdiction under the Credit for Reinsurance Model Law, paragraph 10 of the August 2, 2019 GCC Field Testing Instructions specified conditions for a potential GCC exemption, including access to information for lead state regulators. Specifically, paragraph 10 of the field-test instructions provides the following:

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...After field testing a determination will be made as to whether a non-U.S. based group (a group with a non-U.S. group-wide supervisor) may be exempt from the GCC based on the following:

i. The non-U.S. based group is based in a Reciprocal Jurisdiction that recognizes the U.S. regulatory regime and accepts the GCC from U.S. based groups to satisfy the Reciprocal Jurisdiction’s group capital requirement;

ii. The non-U.S. Group-Wide Supervisor’s home jurisdiction requires a group capital calculation be applied at a level that includes the same (or substantially similar) Scope of Application as would otherwise be determined by the Lead State Regulator in the absence of this exemption; and

iii. The Lead State Regulator can obtain information from the foreign group’s Group-Wide Supervisor either through a Supervisory College or otherwise, that allows the Lead State Regulator to understand the financial condition of the group and complete the expectations of other states in its Group Profile Summary (GPS).

With the assurance that lead state regulators have access to group-wide information through the conditions provided above, or through BBA filings, an exception to the GCC exemptions is not necessary. Therefore, APCIA believes that groups subject to the BBA, as well as insurers with a group-wide supervisor in a Reciprocal Jurisdiction outside the United States, should be exempt from the GCC without exception.

**Exemption for Insurers Not Required to File an ORSA**

Furthermore, APCIA also recommends adding an exemption from the GCC for insurers that are not required to file an Own Risk and Solvency Assessment (ORSA). The referral memorandum only recommends an exemption for small mutual insurers, which is expected to be similar to the exemption for small insurers in the Annual Financial Reporting Model Regulation, with an annual threshold of $1 million in premium. However, we believe the exemption criteria set forth in the model law for the filing of an ORSA is more relevant in the context of the GCC, as the purpose of both the GCC and an ORSA is to provide a group-level perspective on insurers’ capital and risk. An exemption for insurers that do not file an ORSA would recognize proportionality in the application of supervisory measures, and it would allow regulators to focus resources on companies and the areas within companies that pose the most risk. Therefore, we recommend an exemption from the GCC for insurers that fall below the premium thresholds (i.e., less than $500 million of direct written premium by the insurer and less than $1 billion of direct written premium by the insurer’s group) in Section 6(A) of the Risk Management and Own Risk and Solvency Assessment Model Act as well as an exemption like that in Section 6(D), which can be granted by a commissioner “based upon unique circumstances.”

**Process for Considering GCC Design Decisions**

While the Working Group’s memorandum is in the form of a referral to the Group Solvency Issues (E) Working Group, it appears to contain some preliminary decisions on GCC design (such as the scope issues mentioned above). In September 2018, APCIA’s predecessor associations and four other industry associations (Joint Trades) filed a comment letter with the Working Group in which we discussed our recommendations on a number of open design issues. Other interested parties did the same. Rather than engage in public discussion and resolution of those comments at that time, the Working Group decided to leave them open during 2019 field testing. While we
understand the rationale for that decision, there has still been no public discussion of these issues, yet apparently some of them have been decided, at least on a tentative basis. We look forward to an opportunity to engage in more thorough discussion of these issues before further decisions are made about the final design of the GCC.

Thank you for considering the points addressed in this letter, and we continue to support NAIC staff and the Working Group in their successful development of the Group Capital Calculation.

Sincerely,

Stephen W. Broadie
Vice President, Financial & Counsel
February 17, 2020

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

By e-mail to: Dan Daveline, NAIC, at ddaveline@naic.org

Re: Group Capital Calculation (E) Working Group Exposure

Dear Commissioner Altmaier:

America’s Health Insurance Plans (AHIP) is pleased to comment on the Draft Memorandum that you propose to send in your capacity as Chair of the NAIC’s Group Capital Calculation (E) Working Group (GCCWG) to the chair of the NAIC’s Group Solvency Issues (E) Working Group. The Draft Memorandum concerns suggested amendments to the Insurance Holding Company Regulatory Model Act (#440) proposed by the GCCWG to implement the Group Capital Calculation (GCC).

AHIP’s comments pertain to several aspects of the suggestions in the Draft Memorandum, i.e., regarding confidentiality, exemptions, and process.

Confidentiality:

The Draft Memorandum suggests that “Confidentiality language consistent with that recommended by a comment letter directed to the Working Group from the Coalition which, among other things, prohibits the filing of the report with the NAIC unless supported by a confidentiality agreement (similar to the Risk Management and Own Risk and Solvency Assessment [ORSA] Model Act [#505]).” The Coalition’s letter of July 30, 2019 includes a redline of the confidentiality provisions in Section 8 of Model #440, and AHIP generally supports these redline changes. However, two additional adjustments are in order.

First, the language in Section 8.C(1) which appears to allow a group’s GCC to be shared with “international regulatory agencies” should be modified to prohibit sharing with the IAIS unless the group or insurer grants its consent.
Second, language should be added to the end of Section 8.C(4)(iii) as follows: “…and require the NAIC or third-party consultant to provide certification or other proof satisfactory to the insurer or group that all such materials are no longer stored and have been destroyed, deleted, returned, or otherwise rendered inaccessible.”

Exemptions:

The Draft Memorandum suggests several situations for which it is suggested that a group be exempt from filing the GCC with its lead state regulator. Some of those situations parallel recommendations made in the September 20, 2018 letter submitted to the GCCWG by AHIP together with the American Insurance Association and the Property Casualty Insurers Association of America (now merged as the American Property Casualty Insurance Association), Blue Cross Blue Shield Association, the National Association of Mutual Insurance Companies, and the Reinsurance Association of America (the “Joint Trade Letter”). However, there are some variances from the Joint Trade Letter as well. These similarities and differences are presented below, as they serve to frame AHIP’s current comments on the related text in the Draft Memorandum:

1. Group size exemption: The Joint Trade Letter supported exemption of a U.S.-based group from filing a GCC if the group is not required to file an ORSA with its lead state regulator, i.e., if the insurance group of which the insurer is a member has annual direct written and unaffiliated assumed premium including international direct and assumed premium, but excluding premiums reinsured with the Federal Crop Insurance Corporation and Federal Flood Program, of less than $1 billion. The Draft Memorandum suggests an exemption only for small mutual insurance companies, citing the exemption in the Annual Financial Reporting Model Regulation (#205), which has a threshold of $1 million in such premiums.

AHIP is concerned about the apparent wide chasm between the views of many in industry as expressed in the Joint Trade Letter and of GCCWG members as to the apparent value to the regulatory process that could be gained by requiring a large number of small(er) insurance groups to file the GCC. AHIP again suggests that the GCCWG consider the ORSA-like threshold and, after gaining experience with the utility of the GCC from its experience with larger groups that are subject to ORSA, that the threshold might then be lowered to a level (but likely much greater than $1 million in annual premiums) to include more groups but nonetheless balances the cost and benefit/utility of the GCC to groups and regulators alike.

2. Mutual company exemption: The Joint Trade Letter proposed an exemption for U.S. groups where the Ultimate Controlling Party (UCP) is an underwriting company that directly or indirectly owns all of the other entities within the Broader Group. In such a situation the UCP could provide its Annual RBC report as an acceptable alternative to the GCC. This suggestion has apparently not been considered for inclusion in the Draft Memorandum.
Memorandum, and AHIP would like to understand the basis for that exclusion (see “Process”, below). AHIP notes that the suggested exemption, if permitted, would not only pertain to many mutual insurance companies, but also to other types of entities such as non-profit health plans, both of which are among AHIP’s membership.

3. Groups regulated by the Federal Reserve Board (FRB): The Draft Memorandum suggests that groups required to file with the FRB be exempt from filing the GCC with their lead state regulator, but that those groups be required to provide a copy of the filing with the FRB to the lead state. AHIP appreciates this suggestion, which is consistent with the Joint Trade Letter.

4. Foreign-based groups: The Draft Memorandum provides two situations for which it is suggested that a foreign-based group be exempt from filing the GCC:
   a. If it is a reciprocal or qualified jurisdiction per the Credit for Reinsurance Model Law (#785);
   b. Other groups for which the group-wide supervisor otherwise accepts the GCC for any U.S. insurance group or recognizes the GCC as an acceptable international capital standard to the International Association of Insurance Supervisors (IAIS), and has been sponsored by an accredited lead-state.

While this seems somewhat consistent with the Joint Trade Letter, there are some nuanced variances for which AHIP would appreciate a better understanding, e.g., the concept of being “sponsored by an accredited lead state” (see “Process”, below).

Process:

As mentioned previously, the Joint Trade Letter was submitted September 20, 2018, and was part of a series of exposures and comments from interested parties in 2018 leading up to the launch of GCC field testing in 2019. Despite the input sought by the GCCWG in 2018, and the numerous recommendations offered by Interested Parties, the GCCWG did not act to either adopt or reject many of those recommendations. Rather, the decision was made to leave those aspects open as options to be explored through field testing. With the 2019 field test exercise now completed, the open dialogue that might otherwise have occurred back in 2018 has still not occurred. However, the GCCWG Draft Memorandum appears to represent decisions (at least proposed decisions) that have since been made by the GCCWG in the absence of any related open dialogue with Interested Parties. In other written and oral submissions, recommendations were made on issues other than exemptions as well. This explains why AHIP looks forward to further policy-based discussions between regulators and Interested Parties before moving ahead with the memo to the GSIWG or other unresolved questions related to the GCC. We suggest those discussions could happen during the GCCWG meeting in Phoenix in March, and in subsequent conference calls as needed, but we would urge the Working Group to begin those discussions with an open exchange and inventory of pending issues, and an analysis of which can be answered now, and which must be further postponed due to lack of available information or other reasons.

* * * * *
AHIP appreciates this opportunity to comment and would be glad to address any questions you or other GCCWG members may have at your convenience.

Sincerely,

America’s Health Insurance Plans

Bob Ridgeway
Bridgeway@AHIP.org
501-333-2621
Re: Exposure Memorandum addressing confidentiality and scope of the Group Capital Calculation

Dear Commissioner Altmaier,

The American Council of Life Insurers appreciates the opportunity to share our views on the NAIC Group Capital Calculation (E) Working Group’s exposed draft memorandum to the Group Solvency Issues (E) Working Group. The memo recommends updating the Insurance Holding Company System Regulatory Act (#440) to create the legal filing mechanism and confidentiality protections for the Group Capital Calculation (“GCC”).

i. Confidentiality

As noted in many of our past comments on the GCC, ACLI strongly supports robust confidentiality protections to guard against disclosure of GCC results. The NAIC has historically acknowledged and recognized the potential for the misuse of certain regulatory filings like non-public RBC reports or plans by limiting the ability of companies or state insurance regulators to disclose these reports. The GCC, as contemplated by the NAIC, will be a regulatory tool that helps state insurance regulators “better understand an insurance group’s financial risk profile for the purpose of enhancing policyholder protections.” A high degree of regulatory acumen will likely be necessary to ensure that the results, and the nuances contained within them, are understood in the appropriate context. As such, we appreciate the NAIC’s apparent commitment to strong confidentiality protections for GCC data and results.

One area that may require additional consideration is protecting the confidentiality of reports and results submitted by holding companies regulated by the Federal Reserve Board (the “Board”). Nonpublic information submitted to the Board must be subject to similar confidentiality protections as GCC data and results.

ii. “Small mutual holding company” exemption

ACLI supports an exemption for small companies and groups, but we believe the Working Group should increase the proposed threshold. The memo proposes an exemption for “small mutual insurance companies” with less than $1,000,000 in annual premium and fewer than 1,000 policy or contract holders. We believe that a GCC small-company/group exemption level that mirrors the thresholds used in the Own Risk and Solvency Assessment (“ORSA”) Act would be more appropriate.
and a better use of supervisory resources. Further, given that the NAIC plans to use the GCC as a tool, not a standard or requirement, to “complement existing group supervisory tools already available to state insurance supervisors” including the Own Risk and Solvency Assessment Summary Report, Form F and Form B filings, we think it makes sense to align the threshold with ORSA. ACLI believes that requiring these small groups to perform the calculation would burden them and their regulators without providing any additional insight into the group as their structures are typically less complex and not difficult to understand. As such, we recommend increasing the exemption threshold to a requirement that will allow states to focus their resources on groups where additional transparency into the group and non-insurance financial entities may provide the most benefit to regulators and policyholders.

iii. Groups regulated by the Federal Reserve Board

ACLI supports the proposed exemption for groups that are regulated by the Federal Reserve Board (“Board”) who provide a copy of their Board filings to their lead state regulator. We believe this is appropriate and avoids duplicative requirements of having to file two group capital assessments at the world-wide parent level for Board-regulated insurance holding companies. To the extent those filings include non-public information, they must be protected by express confidentiality protections in section 8.

iv. Placement of the GCC within section 4 of the Insurance Holding Company System Regulatory Act (#440)

The placement of the GCC within section 4 of the Insurance Holding Company System Regulatory Act (hereafter the “Holding Company Act”) appears to create an implicit exemption that was not expressly discussed in the memo. As noted in the memo, the NAIC Group Capital Calculation Working Group recommends placing the regulatory authority for the GCC in section 4 of the Holding Company Act, which governs registration and reporting requirements for insurance companies who are part of an insurance holding company system. With that in mind, it appears that companies who do not file registration reports under section 4 of the Holding Company Act, are also exempt from filing the GCC, regardless of whether they exceed the proposed exemption for “small mutual insurance companies” or any of the other proposed exemptions. Additional clarification on this issue, as well as more fulsome analysis and rationale for each exemption and the scope of application, would benefit all stakeholders and permit stakeholders to provide input on those issues.

Conclusion

We look forward to continuing these discussions and appreciate the Working Group’s attention to scope of application. We look forward to continuing to engage on these important topics as more information becomes available on these or other topics required to implement an effective GCC. We encourage the NAIC GCCWG to release a proposed mark-up of section 4 and 8, which would help our stakeholders and permit stakeholders to provide input on those issues.

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2 With some exceptions, insurers are exempt from ORSA if the insurer’s annual premiums are less than $500 million and they belong to a group with fewer than $1 billion in annual written/assumed premiums. ORSA also preserves supervisory discretion to exempt or apply ORSA to firms.

3 NAIC GCCWG Request for Model Law Development (October 30, 2019).

4 Section 1 of the NAIC Insurance Holding Company System Regulatory Act (#440) defines an insurance holding company system as two (2) or more affiliated persons, one or more of which is an insurer. An affiliate is defined as “a specific person, is a person that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, the person specified.”

5 Id. at 1.
members evaluate the proposed exemptions and confidentiality protections with greater certainty, and thus provide more detailed feedback.

Regards,

Mariana Gomez-Vock  
Associate General Counsel  
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Patrick Reeder  
VP & Deputy General Counsel  
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David Leifer  
VP & Associate General Counsel  
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Commissioner David Altmaier, Chair  
NAIC Group Capital Calculation Working Group  
National Association of Insurance Commissioners  
[via-email: ddaveline@naic.org]  
February 18, 2020

Re: Comments on Group Capital Calculation Working Group Referral Memorandum

Dear Commissioner Altmaier:

Reinsurance Group of America, Incorporated (RGA) is a global life and health reinsurer headquartered in the United States. RGA appreciates the opportunity to comment on the NAIC Group Capital Calculation (E) Working Group’s exposed draft referral memorandum to the Group Solvency Issues (E) Working Group.

RGA supports amending the Insurance Holding Company System Regulatory Act (#440) to ensure confidentiality, appropriate scope, and legal authority for the Group Capital Calculation (GCC). We are writing specifically to request clarification with respect to the third and fourth proposed exemptions to the GCC to ensure that there is reciprocity for U.S. groups as intended:

- Groups for which the group-wide supervisor is a reciprocal or qualified jurisdiction per the Credit for Reinsurance Model Law (#785).

- Group not considered a reciprocal or qualified jurisdiction but for which the group-wide supervisor: i) accepts the GCC for any U.S. insurance group; or ii) recognizes the GCC as an acceptable international capital standard to the International Association of Insurance Supervisors (IAIS); and iii) has been sponsored by an accredited lead-state.

RGA supports the position that insurance and reinsurance groups should be subject to only one group capital calculation, standard or requirement (measure), which should be administered only by the group’s own group-wide supervisor. As such, we support excluding certain non-U.S. groups described in exemptions 3 and 4 from the Group Capital Calculation (GCC) requirement at the level of their worldwide group so long as those exemptions are conditioned on U.S. groups being accorded reciprocal treatment in those non-U.S. jurisdictions. We recommend that this reciprocity requirement be clearly stated in the exemptions.

16600 Swingley Ridge Road, Chesterfield, Missouri 63017 (t) 612 217-6101 memerson@rgare.com
We also request clarification on reciprocal treatment with respect to *subgroup* reporting, as opposed to reporting at the level of the worldwide group. As currently written, it appears that the GCC exemptions would apply to a group from a non-U.S. jurisdiction that imposes a group capital measure on a U.S. group’s subgroup located in that non-U.S. jurisdiction.

While we do not object to the NAIC exempting U.S. subgroups of non-U.S. groups from the GCC requirement, such exemption should be conditioned on that non-U.S. group’s home jurisdiction likewise abstaining from requiring a U.S. group to file a group capital measure at the subgroup level in that jurisdiction. Otherwise, the reciprocity principle as adopted in the U.S. will inadvertently disadvantage U.S. groups.

We note that the EU-U.S. and UK-U.S. Covered Agreements and the Credit for Reinsurance Model provisions on reciprocal or qualified jurisdictions do not appear to resolve the subgroup issue. While Article 4(b) of the EU-U.S. Covered Agreement generally prohibits a “Host” supervisory authority from exercising group supervision, including capital, at the *worldwide* group level, it does not prohibit the host supervisor from exercising group supervision over the “Home” group at the subgroup level, i.e., “at the level of the parent undertaking in the territory of the Host Party”. Article 4(b) further provides that “Host supervisory authorities do not otherwise exercise worldwide group supervision with regard to a Home Party insurance or reinsurance group, without prejudice to group supervision of the insurance or reinsurance group at the level of the parent undertaking in the territory of the Host Party.” (Emphasis added.)

Article 4(h) addresses group capital specifically and provides that with respect to a group capital assessment that fulfills certain criteria, “the Host supervisory authority does not impose a group capital assessment or requirement at the level of the worldwide parent undertaking of the insurance or reinsurance group according to the applicable law in its territory.” (Emphasis added.) Thus, the prohibition on the Host supervisor’s imposition of a group capital measure appears to be limited to the worldwide parent, and not the subgroup in that jurisdiction. Similarly, Sections 9(B)(1) and 9(B)(3) of the Credit for Reinsurance Model Regulation on reciprocal jurisdictions appear to address worldwide, but not subgroup, reporting.

RGA requests that the referral memorandum’s third and fourth exemptions be amended to clarify that reciprocity is required not only at the worldwide group level but at the subgroup level as well. Thank you for the opportunity to provide these comments. We would be happy to discuss this issue further.

Sincerely,

Michael L. Emerson  
EVP & Head of U.S. and L/S Markets

16600 Swingley Ridge Road, Chesterfield, Missouri 63017 (t) 612 217-6101 memerson@rgare.com
February 20, 2020

Via Electronic Delivery

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

Re: The National Association of Insurance Commissioners ("NAIC’s") Draft Confidentiality of Group Capital Calculation Memorandum ("the draft memorandum")

Dear Commissioner Altmaier:

Prudential Financial, Inc. ("we") thank the Group Capital Calculation Working Group ("Working Group") for continuing to seek input on key elements of the Group Capital Calculation ("GCC"). We support the development of supervisory tools that enhance state regulators’ ability to protect policyholders and insurance markets.

We believe determining the companies to which the GCC applies should be a function of its overarching objective. The May 29, 2019 NAIC Proposed GCC document provided the following context on why the NAIC is developing the GCC and the objective it is intended to achieve:

“The GCC is a natural extension of work state insurance regulators had begun, in part driven by lessons learned from the most recent financial crisis, to better understand an insurance group’s financial risk profile for the purpose of enhancing policyholder protections. State insurance regulators already exercise their legal powers to obtain any information regarding the capital positions of affiliated business entities. However, there has not been a consistent or coherent analytical framework for evaluating such information and monitoring trends. As such, the GCC is designed to meet this need, delivering financial solvency regulators a panoramic, transparent view of the interconnectedness, business activities, and underlying capital support for an insurance group.”

We support the stated objectives and to achieve them, we believe the GCC should broadly apply to insurers operating in the U.S. with limited exceptions. Such an approach would ensure that policyholders benefit equally from the insights the GCC may provide, and that the panoramic view of the U.S. insurance market state regulators and the NAIC are pursuing is not subject to significant gaps. That said, we recognize the importance of exercising proportionality to avoid instances where application of a regulatory tool would introduce an undue burden on an insurer/insurance group. With these considerations in mind, we believe the following exemptions from completing the GCC would be appropriate:

1. Small insurance companies/groups
**Rationale** – We believe it is appropriate to extend existing exemptions from various risk related reporting requirements to the GCC.

2. Groups required to file with the U.S. Federal Reserve System ("the Fed"), but separately require that such a group provide a copy of the Fed filing to its lead state regulator.

**Rationale** – We believe insurance groups – at the worldwide parent level – should be subject to only one group capital calculation or requirement. While the GCC is intended to serve as an analytical tool, the framework the Fed imposes will be a binding requirement. Given this difference as well as the concerted efforts of the NAIC and Fed to align their respective frameworks to enhance regulatory consistency in the U.S., we believe it would be appropriate for the lead state to accept a copy of the filing with the Fed in lieu of requiring completion of the GCC.

3. Foreign-based insurance groups that are subject to a group capital calculation or requirement provided:
   i) The group-wide supervisor accepts the GCC for any U.S. insurance group; and
   ii) The group-wide supervisor shares relevant information with the lead state upon request

**Rationale** – As noted above, we believe insurance groups – at the worldwide parent level – should be subject to only one group capital calculation or requirement. Thus, in the case of foreign-based insurance groups, we believe the lead state should respect the sovereignty of the insurance regulator in the jurisdiction of the worldwide parent and not require the completion of a second group capital calculation. Similar deference should be provided by the insurance regulator of the foreign jurisdiction for U.S. companies operating in their respective market. Such an approach would be consistent with Article 1, Objectives (c) of the *Bilateral Agreement between the U.S. and the EU on Prudential Measures Regarding Insurance and Reinsurance* ("the Covered Agreement"), which outlines expectations for Host and Home supervisory authorities:

> "the role of the Host and Home supervisory authorities with respect to prudential group supervision of an insurance or reinsurance group whose worldwide parent undertaking is in the Home Party, including, under specified conditions, (i) the elimination at the level of the worldwide parent undertaking of Host Party prudential insurance solvency and capital, governance, and reporting requirements, and (ii) establishing that the Home supervisory authority, and not the Host supervisory authority, will exercise worldwide prudential insurance group supervision, without prejudice to group supervision by the Host Party of the insurance or reinsurance group at the level of the parent undertaking in its territory;

While we support an exemption from the GCC for the worldwide parent of foreign-based insurance groups, we believe the lead state should require submission of the GCC for its U.S. operations ("U.S. sub-group"). Requiring U.S. sub-group compliance with the GCC is appropriate and important for several reasons, including:

- Making sure policyholders receive the benefit of equal prudential oversight from state regulators;
- Securing a sufficiently panoramic view of the U.S. insurance market, which would better enable lead states and the NAIC to identify trends and emerging risks and position the GCC as a complement to tools being developed under the Macroprudential Initiative ("MPI");

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Avoiding an unlevel playing field – although the GCC has been framed as a tool rather than a requirement, we believe supervisors would feel compelled to act if presented with a concerning GCC ratio; and

Aligning with practices and/or requirements in foreign markets, which have already determined there is value in receiving such information

More broadly, we believe language in the Covered Agreement does not preclude application of prudential tools at the sub-group level; rather, section (ii) of objective (c) implicitly recognizes that supervisors may feel the need to apply tools that encompass all operations within their jurisdiction.

Finally, we are generally supportive of the suggested edits to the Insurance Holding Company System Regulatory Act (#440) text to address confidentiality protections for the GCC. However, we believe the text would be improved through the following changes:

Section 8.A. – “….. However, the commissioner is authorized to use the documents, materials or other information in the furtherance of any regulatory or legal action brought as a part of the commissioner's official duties, but notwithstanding the foregoing, the commissioner shall seek to maintain the confidentiality of the group capital calculation and Group Capital Ratio, including in such documents during the course of any such regulatory or legal action. With respect to all other documents, materials or other information covered by this paragraph, the commissioner…..”

Rationale – We believe the proposed edits would better align the text with the NAIC's intention for the GCC to serve as additional tool for identifying potential risks within the group rather than a minimum standard or requirement that triggers regulatory or legal action if breached.

Section 8.G. – “It is the judgment of the legislature that the group capital calculation and resulting Group Capital Ratio is a regulatory tool for assessing group risks and capital adequacy, and is not intended as a means to rank insurers or insurer groups generally. Therefore, except as otherwise may be required under the provisions of this Act or as may be customary for engagement with investors, the making, publishing, disseminating, circulating or placing before the public, or causing, directly or indirectly to be made, published, disseminated, circulated or placed before the public, in a newspaper, magazine, website or other publication, or in the form of a notice, circular, pamphlet, letter or poster, e-mail, or over any radio or television station, or in any other way, an advertisement, announcement or statement containing an assertion, representation or statement with regard to the group capital calculation or Group Capital Ratio of any insurer or any insurer group, or of any component derived in the calculation, by any insurer, agent, broker or other person engaged in any manner in the insurance business would be misleading and is therefore prohibited; provided, however, that if any materially false statement with respect to the group capital calculation or resulting Group Capital Ratio or an inappropriate comparison of any other amount to an insurer's or insurance group's group capital calculation or resulting Group Capital Ratio is published in any written or electronic publication and the insurer is able to demonstrate to the commissioner with substantial proof the falsity of such statement, or the inappropriateness, as the case may be, then the insurer may publish an announcement in a written or electronic publication if the sole purpose of the announcement is to rebut the materially false statement.”
**Rationale** – We believe the proposed edits would appropriately carve out the current market practice of sharing solvency related information with the investor community and modernize the disclosure to account for potential publication via electronic means.

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

Sincerely,

Ann Kappler  
Senior Vice President, Deputy General Counsel and Head of External Affairs  
Prudential Financial, Inc.
The Group Capital Calculation (E) Working Group of the Financial Condition (E) Committee met via conference call on May 19, 2020. The following Working Group members participated: David Altmaier, Chair, and Ray Spudeck (FL); Kathy Belfi, Vice Chair (CT); Laura Clements (CA); Philip Barlow (DC); Carrie Mears, Mike Yanacheak and Kim Cross (IA); Susan Berry and Vincent Tsang (IL); Roy Eft (IN); Christopher Joyce (MA); Judy Weaver (MI); Constance Peterson and Barbara Carey (MN); John Rehagen and Karen Milster (MO); Jackie Obusek (NC); Justin Schrader (NE); Dave Wolf (NJ); Edward Kiffel and Mark McLeod (NY); Dale Bruggeman and Tim Biler (OH); Greg Lathrop (OR); Joe DiMemmo (PA); Trey Hancock and Hui Wattanaskolpant (TN); Mike Boerner and Jamie Walker (TX); Doug Stolte and David Smith (VA); and Amy Malm and Levi Olson (WI).

1. **Consider Adoption of its 2019 Fall National Meeting Minutes**

Ms. Belfi made a motion, seconded by Mr. Bruggeman, to adopt the Working Group’s Dec. 7, 2019, minutes (see NAIC Proceedings – Summer 2019, Financial Condition (E) Committee, Attachment Two). The motion passed unanimously.

2. **Consider the Exposure of the NAIC Staff Post-Field Test Recap of the GCC and Initial Suggested GCC Revisions**

Commissioner Altmaier stated that NAIC staff would be presenting a PowerPoint (Attachment Five-C1) summarizing preliminary input and revisions resulting in adjustments to the draft revised group capital calculation (GCC) instructions and a revised GCC template. He stated that the goal was to expose the documents for a 60-day public comment period, and the bulk of questions and comments should be handled via the comment period. He asked Lou Felice (NAIC) to begin the presentation.

Mr. Felice opened by saying that the bulk of the presentation would focus on the PowerPoint with some references to the instructions. He stated that the template will operationalize what is in the instructions, so the template was provided more for information and descriptive purposes. He pointed out that the materials were developed to be agnostic to pending decisions as to what groups would be required to submit a GCC template. He highlighted directional adjustments to the instructions and template, which include the following:

- Expanded language on possible entities that could be excluded from the GCC scope of application.
- Expanded opportunities for the grouping of non-financial entities and narrowing capital calculation options to two.
- An equity-based factor in the base capital calculation for non-financial entities and non-operating holding companies.
- Addition of a two-step approach to establishing an allowance for senior and hybrid debt as additional capital, including the reporting of paid-in and contributed capital.
- Selection of proxy allowance for senior debt (30%) and hybrid debt (15%).
- A potential course for removal of an informational sensitivity analysis for XXX/AXXX captives.
- Selection of a single scalar option for certain jurisdictions based on the Pure Relative Ratio Approach.
- Additional sensitivity analysis items and the retention of others.
- Expanded collection of “other information” useful for lead-state analysis or to inform future GCC enhancements.
- Added, deleted and relocated data entries on Schedule 1, the Inventory Tab, and in other areas of the instructions/template, including the addition of an attestation.

Commissioner Altmaier expanded on the XXX/AXXX slide, stating that those who wish to comment on this issue should bear in mind that once another group is identified and takes up a charge to conduct further review of XXX/AXXX captives, the informational sensitivity analysis for those captives will be removed from the template.

Mr. Felice also pointed out some areas where feedback is specifically requested. These include, but are not limited to:

- Adding principals and guidance criteria for excluding entities from the GCC scope of application.
- Clarifying modifying the definitions for what is a financial vs. non-financial entity.
- Including greater granularity in applying a capital calculation to non-financial entities.
• Adding criteria for “tracked down streamed” debt and whether that category should be dropped from the template in favor of relying on “paid-in and contributed capital.”
• Limiting the allowance of additional capital from debt to 50% of total adjusted carrying value.
• Proposals for alternatives for scalars and for the treatment of jurisdictions with less developed capital requirements.
• Collecting information on the source of foreign currency conversion.

Commissioner Altmaier reinforced that there are several areas where the Working Group is actively seeking feedback on the materials. He asked state insurance regulators and interested parties if there are any initial questions.

Stephen Broadie (American Property Casualty Insurance Association—APCIA) asked whether options presented are for Working Group discussion and decision or choices for the group filling the template to pick from when completing the template. Commissioner Altmaier agreed that there is some optionality on the scope of application based on lead-state interaction with the group, while other options are directional, presented with the goal of ultimately agreeing on a common treatment in the template. Mr. Felice agreed, stating that there are directional items and those in which specific feedback could influence the inputs or methodologies included in the GCC template.

Tom Finnell (America’s Health Insurance Plans—AHIP) noted that there is an opportunity for differences in the scope of application across groups based on the application of criteria by lead-states. Commissioner Altmaier stated that the Working Group is trying to balance useful information to the state insurance regulator with comparability between groups. He added that the lead-state has the last word on what is included in the template, and there are opportunities, such as the supervisory colleges, to provide information to other involved state insurance regulators.

Patrick C. Reeder (American Council of Life Insurers—ACLI) asked about the longer-term workplan for the rest of the year beyond the 60-day exposure. Commissioner Altmaier stated that the Working Group will be conducting parallel discussions on the analytics and the proposed revisions to the Insurance Holding Company System Regulatory Act (#440). He added that the agenda for the Working Group beyond the comment period would depend on the comments received during the comment period. The goal is to adopt the template and instructions at some point after the exposure period. Commissioner Altmaier offered the possibility of a mid-exposure webinar if interested parties felt it was useful to address initial technical questions or provide further information on the changes. The materials were exposed for a 60-day public comment period without objection.

3. Form a Drafting Group to Review and Improve Staff Developed Guidance for How GCC Will Be Used

Commissioner Altmaier stated that as an analytical tool, enhancing group-wide analysis for state insurance regulators is the main purpose for the GCC. He noted that NAIC staff have developed an initial guidance and metrics document that could eventually be passed along for inclusion in the Financial Analysis Handbook or to the Group Solvency Issues (E) Working Group. He added that it was the intent to advance the development via a small drafting group made up of state insurance regulators and interested parties and bring the result of the drafting group’s work back to the Group Capital Calculation (E) Working Group. There were no objections to that course of action. Commissioner Altmaier asked those wishing to volunteer for the drafting group to contact Dan Daveline (NAIC).

Mr. Daveline said the document is laid out in a manner generally consistent with the way risk-based capital (RBC) is used in the Financial Analysis Handbook for looking at trends and thresholds and then drilling down into the root causes and underlying data behind the trends. He added that feedback from the drafting group is needed on whether the data elements collected in the GCC template are sufficient to support the analytics.

4. Discuss Other Matters

Commissioner Altmaier stated that one or two open Working Group calls would be scheduled in June to address comments and further discuss the proposed revisions to Model #440 related to adding the GCC and any updates on the analytics guidance.

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

- Scope of Application and Calibration
- Grouping and De-stacking of Financial and Non-financial Subsidiaries
- Treatment of Financial Entities without Regulatory Capital Requirements
- Treatment of Non-insurance / Non-financial Entities
  - Schedules A and BA
- Allowance for Capital Instruments as Additional Capital
- XXX / AXXX
- Choice of Scalars
- Applying Sensitivity Analysis

Scope of Application (Instructions pages 6-8, 15-16)

- Unchanged: Starting Point is the Ultimate Controlling Party and all Entities Within the Group (Schedule Y) in Alignment with the HCA
- Staff supports the following:
  - A consistent set of principles for establishing the scope of application of the GCC ratio based on evaluation of all entities within the group
- Working with the lead-state regulator a reduction or limit on the scope of entities to be included may be accomplished in most instances via request by the Group to exclude certain non-financial entities that do not pose material risk
  - The lead-State may accept the request for all or some entities while rejecting it for others
- In some cases of large decentralized groups a reduction in scope of application up front may be requested
  - It is preferable that the regulatory evaluation of such requests is based on established guidance (Examples include materiality of risk, structural separation, no history of cross subsidies, or other criteria supporting regulatory judgement)
  - Group requests for reducing the scope of application of the base GCC should be based on defined criteria documented and applied by the Group
  - Rationale for lead-State acceptance of the request should be documented with information on excluded entities made available upon request of the regulator

Scope (cont.) and Calibration Level

- Scope – Cont.
  - Collecting information on criteria and rationale are important to support future improvements to the Base GCC
  - No single suggestion for a threshold for materiality had consensus from the field test volunteers
- Suggested Base Calibration Level:
  - All RBC filers capital calculations will be included in the Base GCC ratio at 300% x ACL RBC (Trend Test Level)
  - Capital calculations for all entities that are subject to scaling based on RBC levels will use the trend test RBC Level
### Grouping and De-Stacking (Instructions Pages 14-15)

- **Unchanged**: Continue to Allow Grouping of Financial Entities without a Regulatory Capital Requirement Using Current Criteria
  - Same business type
  - Same accounting basis
- **Suggested Change**: Allow grouping for Non-insurance / Non-financial Entities Not Owned by RBC Filers or Financial Entities with a Regulatory Capital Requirement for those Entities
- **Suggested Change**: Do Not Require De-Stacking of Non-insurance / Non-financial Entities Owned by Either RBC Filers or Financial Entities with a Regulatory Capital Requirement that Includes a Capital Charge
- **Suggested Change**: Use RBC of UCP Mutual Insurer at 300% x ACL RBC Calibration with Only Financial Affiliates De-stacked
  - If no financial entities in the group, then TAC and RBC of top mutual is all that is required in the Inventory Tab
  - Data for other schedules still required for each grouping or entity as applicable

### Capital Calculation For Financial Entities (Instructions pages 9, 29-30)

- **Staff Suggestion is That all Financial Entities within the Larger Group should be Included in the GCC**
  - Subject to further discussion / discretion based on the breadth of definition of a financial entity
- **Suggested Changes**: Options for Financial Entities Without Regulatory Capital Requirements Reduced to 2
  - Retain Basel op risk type charge applied to 3 years average gross revenue
    - Current charge is 12% but Basel moving to 15%
  - Option: Scaled version of the charge based on Average RBC ratios
    - Currently 4%, but could increase to close to 5% based on 15% full Basel charge
- **Suggested Change**: Consider treating all financial entities without regulatory the same (incl. asset managers)
  - Decision on full vs. scaled charge may be dependent on the breadth of entity types that are classified as financial entities
  - Impact: Minor since field test Base Ratio used 12% and Tested scaled charge with scaled version also tested

### Capital Calculation For Non-Financial Entities (Page 30)

- **Suggested Change**: Capital charges for Non-insurance / Non-financial Entities Reduced to 2 Approaches (one in Base GCC and another for information)
  - Consider applying a 7% equity charge (based on average post covariance charge on this entity type in RBC) or tailor the equity factor by insurer type
  - Alternate Option: Apply a 3 - 5% risk charge to reporting year gross revenue or tailor the factor by industry type
  - Note: The two alternatives above only apply to non-financial entities not owned by RBC filers or by financial entities with a regulatory capital requirement
  - Impact: The equity charge is lower than what was used in the field test base ratio and the revenue charge is not significantly different from what was tested
- **Suggested Change**: Consider treating all non-insurance / non-financial entities the same
  - Option: Apply either the equity or revenue charge based on the nature of the non-financial entity operating activities
- **Non-operating Hold Cos**
  - **Suggested Change**: Apply same equity charge used for other non-insurance / non-financial entities (7% of tailored)
  - Discuss positive value only vs. netting (also consider for non-financial entities)
  - Impact: More than the zero-value used in field test base ratio, but less than alternative equity charge of 22.5% applied in field test. Netting decreases the impact further.

### Capital Instruments (Instructions pages 35-37)

- **Suggested Change**: All Capital Instruments to be Reported in this Tab and Adjusted for GCC Allowance Purposes
  - No longer reported in Schedule 1
- **Suggested Change**: Include Allowance for Additional Capital in Base GCC Adjusted for any Double Counting
  - Exception: No allowance should be calculated where the lead-State accepts a GCC submission that excludes the UCP issuer of the debt
  - Question: Should HC values reported be adjusted for debt allowance for purposes of a capital calculation?
  - **Two Step Approach**
    - Step 1 - Down-streamed comparison (Similar to what was used in field test)
      1. Tracked based on criteria (New - Criteria to be Suggested)
      2. Total paid-in and contributed capital and surplus from insurer annual statements (New item in Template)
      3. Larger of two items above is carried into step 1
Two Step Approach
- Step 2 - Proxy Allowance (Recommended selection from field test Options)
  1. Qualifying Senior Debt @ 30% x (Total Adjusted Carrying Value from Inventory B + Outstanding Senior and Hybrid Debt)
  2. Qualifying Hybrid Debt @ 15% x (Total Adjusted Carrying Value from Inventory B + Outstanding Senior and Hybrid Debt)
- Larger of Step 1 or Step 2 Becomes Additional Capital Allowance (Subject to Max = 100% of Outstanding Senior and Hybrid Debt – Same as field test)
- Suggested Limits on Allowance:
  - Overall additional allowance can be no more than 50% of total adjusted carrying value in Inventory B (field test applied limit of 100%)
- Impact: Of 24 Volunteers that Reported Senior and / or Hybrid Debt, 6 Could Not Include 100% of Their Qualifying Debt as Additional Capital.
  - 3 of the 6 could not include more than 10% of their outstanding senior and hybrid debt (11% - 27%)

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

Based on Impact Analysis staff suggests that the Working Group Consider Replacing the Down-streamed Option Altogether in Favor of Defining Paid-in Capital and Surplus as Structurally Subordinated Down-streamed Debt in Step 1
- No allowance for debt Classified as “Other”
  - Description provided in Capital Instruments Tab
  - Other debt may be included in Sensitivity Analysis @ 15% x (Total Adjusted Carrying Value from Inventory B + Outstanding Senior, Hybrid and Other Debt)
  - Use information collected to determine if qualifying criteria can be established.

XXX / AXXX Assets and Liabilities
- Suggested Change: Provisionally Exclude Sensitivity Analysis for XXX / AXXX Captives from the GCC Template upon referral to an E Committee Group or Subgroup for Further Risk Assessment / Data Collection Associated with Implementation of Economic Reserves and Recognition of non-SAP assets as available capital
  - With particular focus on review of grandfathered XXX / AXXX captives
- Sensitivity Analysis (Based on Field Test Method 3) to be Removed from the GCC Template Once the Appropriate E Committee Group or Subgroup is Identified and an Agenda is Adopted

Scalars (Instructions pared to reflect the selected method)
- Suggested Change: Apply Pure Relative Ratio Option at 300% RBC Calibration in Base GCC for Jurisdictions Where Data is Available
  - Separated UK from EU and added new jurisdictions
- Other Jurisdictions
  - Use 100% of the capital requirement at PCR level in Base GCC
- Treatment for regimes without capital requirements
  - For discussion: Suggestions during field test made to set calc capital of between 50% and 100% of available capital in Base GCC
- Continue to Explore Other Potential Methods for Scaling (in conjunction with similar work for ICS – AM)
- Impact: Any Current Scalar (except Japan) Increases the GCC Ratio Compared to the Base Ratio in the Field Test which used 100% Values
  - Any new options would need to be evaluated as to impact on the GCC ratio
Suggested Change: Sensitivity Analysis Tab Added (Instructions pages 38-39)

- Sensitivity Analysis is Available on an Informational Only Basis to Assess the Capital Impact of Various Adjustments
- The Analysis will Not Impact the Base GCC Ratio
- Main Sensitivity Analyses include:
  ➢ XXX / AXXX adjustments
    - Sensitivity analysis will apply Method 3 from the field test
  ➢ Permitted and prescribed practices
    - Sensitivity analysis excludes values for permitted and prescribed accounting practices along with associated capital charges
  ➢ Foreign insurer capital requirements unscaled
    - Sensitivity analysis includes all jurisdictions at 100% PCR requirement
  ➢ Alternative calculated capital
    - Financial entities without a regulatory capital requirement
    - Non-financial entities

Sensitivity Analysis – Cont. (Instructions pages 38-39, 42)

- Type 2: To evaluate Data to Inform Potential Future Criteria:
  ➢ Excluded entities
    - Sensitivity analysis will exclude entities requested by the filer but not accepted by the lead-State
  ➢ Additional capital allowance for capital instruments classified as “Other”
    - Sensitivity analysis will include an additional allowance for capital instruments designated as “Other”
  ➢ Other regulator discretion
    - This will allow Regulators to adjust valuation for intragroup transactions where there is a question as to appropriate reserve, investment or other valuations compared to statutory accounting values

Other Information (Instructions Pages 43-44)

- Material Risk Definition Applied by Lead-State to Approve Reduced Scope of Application
- Intangible Assets
- Currency Adjustments
- Methodology for Tracking Down-streamed Debt (if Down-streamed Debt Category is Retained)

Suggested Changes: Schedule 1 (Instructions pages 17-21)

- Instructions
  ➢ Added entity categories to the entity type chart
  ➢ Clarify required entries in Schedule 1B, Column 16 (Treatment for RBC purposes)
  ➢ Eliminate most alternative capital calculation options used in the field test and underlying data
  ➢ Clarify entity categories, particularly for regulated vs. non-regulated financial entities and affiliate entity types
- Data Removed
  ➢ Financial strength ratings
  ➢ Assumed and ceded premiums
  ➢ Debt (all debt moved to Capital Instruments Tab)
  ➢ Intergroup capital maintenance agreements, contracts and guarantees (moved to Other Information Tab)
  ➢ Most field test capital calculation options for financial and non-financial entities along with supporting data (few remaining moved to inventory Tab)
- Data Added
  ➢ Surplus / equity reconciliation
  ➢ Dividends paid and received
  ➢ Capital contributions paid and received
  ➢ Intra-group reinsurance assumed and ceded
  ➢ Other data needed to support new analysis tab
**Suggested Changes: Inventory Tab**

- **Instructions**
  - Added charts to instructions regarding carrying values to be reported in Columns 1 and 2 of Inventory B and Inventory C (parent and local carrying values / capital calculations) [Pages 23 & 31]
  - Added examples for financial entities without a regulatory capital requirement and for non-financial entities
  - Added examples for financial vs. non-financial subsidiaries of insurance companies
- **Template**
  - Add column (+ instructions) for accounting adjustments (e.g. GAAP to SAP and or other regulatory adjustments)
  - Add columns for revenue-based options (moved from Schedule 1)
  - Remove permitted and prescribed practices columns (moved to Sensitivity Analysis Tab)

**Suggested Other Changes**

- **Attestation Added** [Instructions Page 11]
- **Analytics and Guidance to be Added** [Separate doc]
  - Addresses use of GCC
  - Uses data collected in the template
  - Guidance and instructions to be reviewed concurrently with revised template / instructions
- **Potential Changes to Informational Grouping**
  - Alternative and Instructions (Working with some IPS)
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July 24, 2020

Commissioner David Altmaier  
Chairman, NAIC Group Capital Calculation (E) Working Group  
Florida Office of Insurance Regulation  
[via-email to lfelice@naic.org]

Re: NAIC Group Capital Calculation (“GCC”) Working Group’s exposure on the GCC template and instructions

Dear Commissioner David Altmaier,

ACLI is pleased to have the chance to provide an overview of our views on the exposed GCC template and instructions. We fully acknowledge the deadlines the NAIC is working against. However, the GCC instructions and template asked for feedback on a broad range of substantive issues, ranging from scalars, the definition and treatment of financial and non-financial entities, the treatment of senior and hybrid debt, plus others. The issues in the exposure are complex and the consequences for our members are potentially significant. In addition to the complexity inherent in this group level calculation, the ongoing, extraordinary circumstances related to the coronavirus make it even harder to properly analyze and assess the GCC without assessing its impact over time. ACLI members agree that more time is needed to analyze many of the GCC components. ACLI members expect other areas of concern, beyond those identified in this letter, to emerge as regulators and industry observe the GCC’s performance over time. Therefore, as indicated in several instances below, the ACLI urges the NAIC to continue to engage with stakeholders and to publicly consult again on these key elements, overall design and implementation of the GCC over the coming months.

To the greatest extent possible, our letter provides ACLI’s specific recommendations on the exposure. ACLI has also provided a set of general, overarching comments on the GCC, and highlights several process and governance related issues. In addition to those areas, our letter provides a preliminary issue-spotting list of other areas that are in need of additional analysis and work by the NAIC, including the treatment of capital instruments in the GCC, and the treatment of financial entities and non-financial entities.
PART I. OVERARCHING COMMENTS ON THE GCC AND EXPOSURE

This part of our letter provides general, overarching comments that are generally applicable to the entire exposure, instead of a single recommendation.

ACLI fully supports an aggregation-based approach that is consistent with the existing legal entity RBC framework. ACLI supports the development of an aggregation-based approach that is “intended to build on existing legal entity capital requirements where they exist, rather than developing replacement/additional standards.”* We fully support this objective and believe the GCC should leverage and adhere to the existing regulatory frameworks – including legal entity RBC rules – and industry practices and norms to the greatest extent possible.

ACLI encourages the Working Group to ensure that design choices enhance transparency into group risk and avoid introducing procyclicality into the GCC. ACLI believes the current proposal may include elements that could be procyclical and have the unintended consequence of disrupting the ability of regulators and insurance groups to navigate periods of stress. For example, the proposed debt limits, which are based on available capital could have procyclical effects in times of stress, when available capital tends to contract and capital requirements tend to increase. ACLI urges the Working Group to devote the appropriate resources and time to review these items to avoid introducing procyclical risks into the GCC.

ACLI believes GCC design choices should be consistent with the intent for the GCC to be a tool, rather than a standard or binding requirement. ACLI supports the NAIC’s development of a GCC as an additional “tool” that is intended to provide regulators with greater insight into insurance groups.² However, we are concerned some aspects of the instructions and the preliminary Draft Analysis Handbook give rise to a GCC that goes beyond this objective and would have the effect of turning the GCC into a binding standard or constraint.

All references to “Base GCC” should be eliminated. The references to “Base GCC” may be a holdover from previous versions of the instructions when formal on-top adjustments were contemplated. We are concerned that the use of the term “Base GCC” throughout the document insinuates that there are multiple GCC’s, and we believe this could cause unnecessary confusion around the GCC.

ACLI believes the process for developing and refining the GCC requires further consideration. Given the potential consequences the GCC may have on members, ACLI believes the Working Group should take time to consider further alternative approaches to certain elements and perform additional quantitative analysis. We also believe a clear process must be established for future revisions to the GCC, a rationale for decisions should be provided that is consistent with the stated

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² See Attachment B-2, GCC Instructions, at p. 5, para. 2 (describing the GCC as a tool intended to provide regulators greater insight into insurance groups – e.g., a holistic understanding of the non-insurance entities in the group, insight into capital distribution across the group, etc.).
purpose of the GCC, and the Draft Analysis Handbook should be exposed for public review and comment before it is finalized.

Decision points on items in the instructions should be guided by the purpose and objective of the GCC, as described in the Instructions. ACLI believes the decision points should favor design choices that provide more transparency to regulators and do not conflict existing standards or introducing new standards. Although this is not directly addressed in the Instructions, we believe a prudent group solvency regime should avoid imposing measures that impede the ability of regulators and insurers to navigate periods of stress.

PART II. ACLI’S COMMENTS ON RELATED PROCESS AND GOVERNANCE ISSUES

This section identifies and issues recommendations on process and governance issues related to the GCC and exposure.

ACLI believes alternative approaches should be considered and additional data collection, quantitative analysis and monitoring should be performed prior to finalizing the design of the GCC. ACLI strongly believes that this is critical to determine if the GCC components are fit for purpose and would be consistent with the Working Groups message that getting the GCC right is more important than getting it done soon.

ACLI believes a clear and transparent process for future revisions to the GCC framework must be established. Paragraph 7 of the draft instructions notes that the GCC instructions are expected to be "modified, improved, and maintained in the future." We believe the process for making changes to the GCC should require notice to stakeholders and include an opportunity for public consultation. We recommend that the Working Group develop a GCC governance process like what is used for the Accounting Practices and Procedures Manual and the Valuation Manual. Separately, we believe the process for updating scalars for design changes or to account for evolution in supervisory regimes should also be transparent and subject to a clearly defined governance process.

The Draft Analysis Handbook should be exposed. The Draft Analysis Handbook should be exposed for public review and comment before it is finalized. While ACLI appreciates the opportunity to serve as a participant in a drafting group composed of a limited number of regulators and industry participants, we believe all interested parties should have an opportunity to weigh in on the content given the significant impact it may have on the role the GCC plays in practice. For example, the previously distributed version of the draft analysis included a proposed 175% intervention point, which appears to conflict with the description of the GCC as a tool meant to enhance transparency into a group’s risks rather than a binding standard or constraint. Given the high-profile nature of the GCC, public exposure of the Handbook and any potential intervention points are necessary.

3 The avoidance of new standards is consistent with the description of the GCC in the Instructions and the NAIC’s August 16, 2018 letter to Senators Scott and Rounds. In the August letter, the NAIC notes that the “NAIC is not creating a new capital standard for insurers that will necessitate higher capital levels. Rather, the GCC will be an additional reporting requirement built off existing legal authorities.” Available at https://www.naic.org/documents/government_relations_181816_scott_rounds_letter.pdf.
PART III. RECOMMENDED IMPROVEMENTS TO THE GCC INSTRUCTIONS AND TEMPLATE

This section of our comments addresses the issues where ACLI has provided specific recommendations for the instructions or template during our preliminary review. Some of these items, such as the treatment of senior debt, are also candidates for further work and analysis.

1. Scalars. ACLI members recommend the Excess Capital Ratio Approach.

The primary goal of a scalar is to ensure aggregated data and thereby ratios across jurisdictions are comparable. While the Pure Relative Ratio ("Pure") and Excess Capital Ratio ("Excess") Approaches are both relevant supervisory capital metrics, only the Excess Approach uses a total balance sheet approach and leads to an appropriate measure of excess capital.

As a result, ACLI recommends the Excess Approach over the Pure Approach. Unlike the Pure Approach, the Excess Approach keeps the total asset requirement (reserves plus required capital) constant before and after scaling. As a result, the Excess Approach places greater weight on differences in reserve requirements, which can vary significantly across the globe. We believe this creates a more level playing field regardless of an insurer’s subsidiary locations and will provide a comprehensive approach for aligning foreign regimes to the U.S. RBC framework.

The Pure Approach does not adjust for available capital and could result in a distortion of excess capital levels, depending on the entity’s capitalization levels and its jurisdiction. For example, by not taking into account the intervention levels of local regimes, the Pure Approach would allow entities that a jurisdiction deems to be undercapitalized to be considered adequately capitalized for group ratio purposes, simply due to scaling, which could ultimately detract from the credibility of the GCC.

Another benefit of the Excess Approach is that it maintains the actual levels of excess capital because it adjusts both available and required capital, which improves the accuracy of the GCC with respect to the actual amounts of excess capital held by a group. The management and maintenance of excess capital levels is a top priority for treasurers of insurance companies, and the GCC should accurately reflect the amount of excess capital levels that is held by a group.

Members also believe that the total balance sheet approach employed by the Excess Approach may better position the GCC, and Aggregation Method ("AM"), for the forthcoming efforts to secure recognition of the AM as comparable to the market-based version of the Insurance Capital Standard ("ICS"). The principles and criteria for the comparability assessment will take into account analysis of individual elements of a group solvency approach, i.e. valuation, capital resources, and capital requirement. Consequently, a scaling approach that effectively provides for a translation of reserve levels and capital requirements would be better suited for the comparability assessment than the Pure Approach. Further, the Excess Approach supports the goal of comparability by providing a more accurate comparison of the total assets (all loss absorbing resources within a

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group) that are required when comparing regimes. We have attached a brief explanation of the differences between the Pure and Excess Approaches.

2. **The calibration of the GCC and scalars for foreign insurance regimes should be 200% ACL RBC.**

ACLI disagrees with the proposed calibration of the non-U.S. insurance scalars and the GCC ratio at the RBC trend test level (300% ACL RBC). We believe the GCC should be calibrated to the 200% ACL RBC, which is consistent with 100% Company Action Level (CAL) RBC. In addition, calibrations of other factors and regimes should be based on 200% ACL level RBC as well. Using 300% as the calibration for the GCC is likely to introduce confusion because the GCC calibration will depart from a well-established market-norms for legal entity insurers of assessing RBC based on a 100% CAL level, without offering any identifiable benefits. We are also concerned that establishing a different calibration point for the GCC could result in unintended consequences such as changes in market expectations for the capitalization of underlying insurance entities.

3. **The GCC’s proposed treatment of capital instruments, in particular the qualifying criteria for senior and hybrid debt, should be subject to further study and analysis.**

We believe that the current debt caps are too restrictive and could negatively impact a group’s ability to prudently manage capital and liquidity risks. Further, it is not clear how the inclusion of the proposed limits would enhance transparency into risks within an insurance group, which the NAIC has noted is the primary intent of the GCC.

There are times when companies may need to quickly raise capital, and issuing senior or hybrid debt is a reliable way to accomplish this, especially during times of economic stress. We do not believe it is appropriate for the GCC to introduce constraints that may inhibit the ability for insurers to prudently use these capital instruments. In addition, we believe that tying the constraint to a percentage of the group’s available capital embeds an undesirable element of procyclicality into the GCC, because a company’s available capital is likely to decrease in times of stress, especially if markets crash.5

To the extent the Working Group believes some form of limit is necessary, we believe it must consider a suite of less restrictive options and would welcome the opportunity to work with you to conduct further analysis on the subject.

On a more granular level, the GCC instructions (p. 34, para. 65) require that the capital instrument has a fixed term of a minimum of 5 years at the date of issuance or refinance, including call options. The presence of call options should not prevent a capital instrument’s inclusion as a qualifying instrument. Call options are a common feature of U.S. issued capital instruments. This

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5 ACLI is aware that the analysis of field-testing results showed that approximately 25% of volunteers would not receive full credit for the capital instruments they issued because of the prescribed limits. We are concerned that the field testing captured a point-in-time point of view that may not demonstrate the impact these restrictions might have on groups during periods of economic decline. During periods of economic stress, an insurer’s available capital tends to constrict, and its capital requirement rises, which would further limit the recognition of these capital instruments and discourage their use.
criterion would shorten the term and prevent most instruments from qualifying as structurally subordinated. We recommend removing the call option criteria, because the exercise of a call option is typically followed by refinancing of the instrument which supports its permanence and structural subordination.

4. Capital Instruments. ACLI recommends eliminating the down-stream tracking requirement.

ACLI agrees with the NAIC staff’s recommendation to eliminate the down-stream tracking requirement for senior debt. There are a number of reasons why the downstream tracking requirement could prove difficult to implement, such as complications that could arise when the debt has been refinanced by the parent, or how to track upsize transactions where debt is borrowed at one date and then down-streamed on a different date. Downstream tracking also raises questions about how to treat up-streamed dividends (are they netted against down-streamed capital?), as well as how to treat M&A transactions. For example, if a company is acquired, does the new parent company assume the historical relationship to the down-streamed debt, so long as its debt at least equals the debt of the old parent company?

Some of our members have also expressed concern that groups with an operating holding company who utilize a more centralized capital and liquidity management strategy that prioritizes holding funds at the holding company level would be disadvantaged by this approach. If the proceeds must be down-streamed for the company to get any credit, then a group would have to issue more debt at the legal entity insurance level if it wished to maintain the same debt-funding levels at the operating holding company level without hurting its capital ratio.

5. ACLI supports the Working Groups recommendation to remove parts of the Sensitivity Tab, and more broadly, believes the remaining elements of the tab should be removed from the template.

ACLI has long advocated that the GCC should be consistent with entity level RBC rules and we are concerned that the inclusion of approaches within the GCC that deviate from legal entity rules, such as the unwinding of permitted and prescribed practices should not be included in a sensitivity tab. Further, ACLI members ability to comment on the specifics of the sensitivity tab was also constrained by the lack of formulas inside the tabs. Therefore, further discussion of its purpose and use, as well as a discussion on the context of this information is warranted if the tab is retained. To the extent the information on the Sensitivity Analysis Tab is of interest to state regulators, ACLI believes they should use their discretionary powers to obtain it rather than embedding it in the GCC template.

Irrespective of the tabs continued existence (or not) in the template, we strongly believe that all references to “Base GCC” should be removed from the Instructions and replaced with “GCC”. Using the term “Base GCC” creates confusion and a potentially false narrative that there are multiple versions of the GCC. Eliminating this need to distinguish between a “Base GCC” and multiple alternative GCCs will provide a stronger foundation for the NAIC to advance an AM at the global level.

6. Grouping/De-stacking and Materiality
ACLI supports efforts to simplify and streamline the GCC by permitting companies to either group related entities, or to relax the requirements to “de-stack” an entity. ACLI also supports the grouping or netting of non-operating holding companies. To the extent there are concerns that these simplification efforts may obstruct a regulator’s ability to obtain adequate insight into the potential group risks, this is addressed by giving regulators the option to ask groups to submit more detailed information (i.e., supervisors may direct a company to de-stack certain entities or desegregate some groupings).

In general, ACLI believes that the GCC should be consistent with the legal entity rules applied to insurance legal entities – including the subsidiaries of insurance legal entities. The GCC de-stacks subsidiaries from insurance legal entities and in some cases, applies a GCC treatment to the subsidiary that differs from the legal entity treatment. To the extent that there are differences between the two, we recommend the Working Group explain the rationale for the difference (e.g., achieving substantial consistency in charges regardless of corporate organizational structure) and, if appropriate, refer the issue to the appropriate RBC working for further dialogue. In the long run, we believe this approach will benefit regulators and the industry by promoting a more consistent and up-to-date risk framework.

ACLI believes it would be helpful if the GCC Instructions employed a consistent definition and threshold of materiality for de-stacking and other GCC purposes where consistent with the purposes of the GCC. However, this is an area that clearly requires additional thought and consideration to establish an appropriate threshold for materiality.

PART IV. ACLI’S PRELIMINARY LIST OF ISSUES NEEDING FURTHER ANALYSIS

This section of our comments addresses issues that ACLI members have identified as significant concerns, but that require additional clarity from the Working Group and/or further member development and discussion, in order for ACLI to make a specific recommendation. These are areas where we suggest more time be allowed for NAIC staff and interested parties to work together to develop specific recommendations.

1. Financial entities and non-financial entities

1.1. Additional clarity is needed for the definition of financial entity, non-financial entities, and material schedule A/BA affiliates.

The definition of financial entity remains unclear and needs additional clarification. In general, we believe that financial entities should be limited to operating entities with meaningful obligations to third parties. Passive investment vehicles or subsidiaries that manage or hold investments predominantly on behalf of the insurer should not be considered financial entities. An operating entity may issue debt, create syndications, issue loans, accept deposits and/or generally act as a fiduciary. The activities of an operating entity require active management on behalf of third parties. In contrast, a passive investment vehicle, like an investment subsidiary, as defined by NAIC rules [Schedule D], or other subsidiary that holds investments on behalf of the insurer (e.g., Schedule BA entities), should not be considered a financial entity. This rubric of using active management on behalf of others versus simply holding or managing an
investment on behalf of the insurer works well to determine if an entity should be classified as a financial entity or non-financial entity, even when an entity, like a mutual fund, may have a mix of activities.6

Based on the existing definition of “financial entity” in the Instructions, we believe that the Working Group intended to exclude passive investment vehicles and subsidiaries that manage or hold investments predominantly on behalf of the insurer, but we believe additional clarity is necessary to telegraph that intent.

As such, we recommend the following for your consideration:

“For purposes of this definition, a subsidiary of an insurance company whose predominant purpose is to manage or hold investments on behalf of the insurance company and its affiliated insurance (greater than 90% of the investment subsidiary’s assets are for these insurance affiliates) should NOT be considered a Financial Entity.”

If the interpretation of the definition of financial entity is correct, additional clarity is requested on how to record the various affiliates, including but not limited to non-US statutory investment entities and funds that roll-up to the ultimate financial entity and that may manage and hold investments on behalf of the insurer and third parties. Should such entities be split on the basis of US/non-US statutory status or simply included under the financial entity?

1.2 Additional clarity is also needed for the “exception to the exception” for “material” A/BA entities.

ACLI requests additional clarification on what the impacts are of building an exclusion for Schedule A/BA into the definition of “affiliate,” when it seems like the Schedule A/BA exclusion is an exclusion from de-stacking. We believe this may be better placed in the de-stacking instructions.

ACLI recommends that the exception to the exception for material A/BA items be limited to operating entities, and not apply to passive investment vehicles, which may be of significant size but would not provide a regulatory benefit by de-stacking from existing RBC treatment. If the Working Group adopts this exception it will also be necessary to adopt a threshold for materiality. (see comments above regarding desire for consistency in materiality thresholds). In addition, the Working Group will need to address the inconsistency between the “exception to the exception” and the direction in Paragraph 50 that values for non-insurance / non-financial U.S. RBC filers will not be de-stacked.

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6 For example, a mutual fund may have a mix of activities such as taking deposits, holding investments on behalf of third parties, they collect fee income. However, even if a mutual fund has passive investment activity, a mutual fund will generally have liabilities in excess of 5%, which means the mutual fund cannot be classified as an investment subsidiary under NAIC rules.
1.3 Treatment or charge for non-financial entities without a capital requirement and material Schedule A/BA entities

ACLI was unable to discern how the proposed charges for “other non-insurance/non-financial entities” and “material Schedule A/BA entities” were created. The Working Group field tested seven different potential charges for these entities, but staff is now recommending a new charge that was not field tested. Additionally, despite NAIC staff’s attempt to explain how the new 7% charge was created, our members are still unsure how the charge was derived, why it was selected, and why it differs substantially from the corresponding RBC treatment. Further clarification on this issue is necessary, including an explanation of why the Working Group is recommending a novel approach that has not been subject to field testing.

2. GCC Instructions.

2.1 The Instructions should be reviewed to ensure consistency regarding regulatory discretion and clarify expectations for certain elements.

For example, the Instructions provide several clear examples of lead-state supervisory discretion that could impact how the lead-state supervisor and the insurance group define the scope of the group (see e.g., para 18, para 20, and drafting note to para 61).

We recommend supplementing the Instruction’s definition of “ultimate controlling person” with a reference to the discretion provided to the lead-state supervisor in the Instructions (see e.g., para 18, para 20, and drafting note to para 61). This clarification ensures that the definitions are consistent with the discretionary language in the instructions, as provided in paragraphs 18, 20, and the note accompanying paragraph 61:

“Ultimate Controlling Person: As used in the NAIC’s Insurance Holding Company System Regulatory Act (Model #440) and as implemented by the lead state supervisor.”

2.2. We request that the Working Group revise the Instructions to provide clarity on the following items:

In light of the instructions for when de-stacking is not required, there needs to be additional, corresponding instructions about what should be included in “Schedule 1” and “Inventory” tabs, in light of instructions for when de-stacking is not required. For example, if an entity is not to be de-stacked, then presumably it should not be listed on Schedule 1/Inventory tabs. Otherwise, this sets up a confusing “include/exclude” decision, which is a different issue (goes to “scope of application”). We request that the instructions include language that clearly address this issue.

For Schedule Y entities that are not de-stacked, should they all be listed on the Questions tab, like Schedule A/BA are currently?

Additional instruction on Inventory B, Column 5 (reported intra-group guarantees, LOCs and other) would benefit from examples that demonstrate application. It appears that this column, like those near it, is intended only to eliminate double counting of capital. If the presumption is correct, then it would be helpful if this was noted in the instructions.

ACLI believes that scalars are an integral part of an aggregation method. We remain concerned that a significant number of countries lack a scalar. It is our understanding that the NAIC staff sought to develop scalars for the countries that had a material amount of business from U.S. parented groups within its borders. While it was understandable for the initial focus to be on countries with a material percentage of U.S. based insurers doing business there, the lack of scalars for certain jurisdictions has created material differences in their GCC ratio. If the NAIC lacks access to the appropriate dataset to create the scalars, we recommend allowing the lead state some flexibility with default assumptions.

In addition, there are formula errors in Column K. For example, K14 is supposed to be taking 12% of the average revenue, but instead it is taking 12% of Reported Calc Capital. Similar issues exist in cells K16, K18, K19, K21 and K22.

We believe the scaling factors for Non-Insurance Entities need a broad review. Specifically, the scaling factors for Asset Managers, financial entities with regulatory requirement, financial entities without a regulatory requirement, and other non-insurance/non-financial entities. The NAIC has selected some of the more conservative scaling factors from the 2019 field test and provided no explanation for their decisions. These factors require a larger discussion.

CONCLUSION

Thank you for the opportunity to provide these comments. ACLI welcomes the opportunity to discuss our comments with you in the future, and we would also welcome the opportunity to contribute to additional analysis and discussion regarding the issues raised in our letter.

Sincerely,

Mariana Gomez
Pure Relative Ratio vs. Excess Capital Ratio

- NAIC GCC proposals uses scalars to add capital regimes with the goal of comparability
- Pure Relative Ratio (PRR) approach adjusts required capital only
  - Available capital is not adjusted and results in excess capital being distorted
- Excess Capital Approach (ECA) adjusts both available and required capital (ie. total asset requirements)
  - Excess capital is not affected

Implications

- The capital ratio and excess capital are both relevant supervisory capital metrics
- ECA better supports comparability by addressing both metrics
- Excess Capital Approach takes a whole balance sheet approach as it assesses total asset required and accounts for reserve differentials.
- Excess Capital Approach creates a more level playing field regardless of an insurers’ subsidiary locations
- Pure Relative Ratio will create an unlevel playing field depending on an insurer’s subsidiary locations
Pure Relative Ratio (PRR) Example

PRR preserves the relative capital position versus industry average however it distorts excess capital.

- SII subsidiary’s capital ratio remains above industry avg after scaling and Japan stays below (see blue circles)
- Excess capital changes after scaling which creates an unlevel playing field (see red circles)

### US insurer with SII subsidiary

**Unscaled**

- Excess Capital
- Required Capital
- Reserve Margin
- Best Estimate Liability

#### PRR Scaled

1. Assuming US insurer is operating at industry avg capital ratio, Euro is above and Japan is below avg

### US insurer with Japan subsidiary

**Unscaled**

- Excess Capital
- Required Capital
- Reserve Margin
- Best Estimate Liability

#### PRR Scaled

1. Assuming US insurer is operating at industry avg capital ratio, Euro is above and Japan is below avg

### US insurer with SII Consolidated

**Unscaled**

- Excess Capital
- Required Capital
- Reserve Margin
- Best Estimate Liability

#### PRR Scaled

1. Assuming US insurer is operating at industry avg capital ratio, Euro is above and Japan is below avg

### US insurer with Japan Consolidated

**Unscaled**

- Excess Capital
- Required Capital
- Reserve Margin
- Best Estimate Liability

#### PRR Scaled

1. Assuming US insurer is operating at industry avg capital ratio, Euro is above and Japan is below avg
Excess Capital Approach (ECA) Example

ECA preserves both relative capital position versus industry average and excess capital by adjusting available capital and creates comparability:

- SII subsidiary’s capital ratio remains above industry avg after scaling and Japan stays below (see blue circles)
- Excess capital remains unchanged after scaling (see red circles)

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US insurer with Japan subsidiary

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July 20, 2020

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

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

Re: Exposure of Proposed Group Capital Calculation Instructions and Template

Dear Commissioner Altmaier:

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

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

- The overall approach maintains that the GCC is an analytical tool for use by the lead state that will not, in and of itself, dictate capital requirements.
- Appropriate exemptions and expedited treatments from filing all or part of the GCC template have been provided and which provide, in certain instances, for the Lead State Commissioner to use discretion to allow filing only of Schedule 1, i.e., as an analytical construct it could be a sufficient supervisory measure without aggregation to a single group-wide measure.
- Groups could exclude certain non-financial entities from the Scope of Application and large, decentralized groups could request up front a reduction in the scope.
• Determination of materiality of risk posed to the insurance group by non-insurance entities in the broader group will be a qualitative determination (the Financial Analysis Handbook Drafting Group is to consider appropriate criteria).
• Modified instructions for the GCC template are less onerous (than in field testing), i.e., with more grouping and less de-stacking.
• Senior and hybrid debt criteria and limits will accommodate a large majority of debt held by insurance groups to be recognized in group capital.

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

I. Scope of Application

Determination of Material Risk

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

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

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

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

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

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

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

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

As well, Enterprise Risk Reports filed with the lead state already provide information as to the existence of “enterprise risk” defined as “any activity, circumstance, event or series of events involving one or more affiliates of an insurer that, if not remedied promptly, is likely to have a material adverse effect upon the financial condition or liquidity of the insurer or its insurance holding company system as a whole…”
Taken together, Forms B and D and Enterprise Risk Reports establish examples of “cross support mechanisms” as well as whether there is risk that could have a material impact to the insurers in the group (presumably via transfer through at least one such mechanism). It stands to reason that in the GCC, only such risks of non-insurance non-financial entities outside the insurance group that are already identified through those processes could therefore have a material impact and for which the subject entity(ies) that are the source of that risk would therefore be included in the scope of the GCC.

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

II. Risk Charges for Material Non-Insurance Entities

Non-Financial Entities

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

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

Financial Entities

On a related matter, AHIP is concerned with the breadth of the expanded definition of “financial entity” in the GCC Instructions. If the Working Group maintains this expanded definition of “financial entity”, we recommend using a capital charge that is roughly equivalent to an entity’s current post-covariance RBC charge. If it is desired to consider changes to underlying RBC levels, that should be handled through the appropriate (e.g., Health) RBC Working Group.
The exposed GCC Instructions provide that certain non-insurance affiliates of an insurer be deemed as financial. We understand that the Working Group views such affiliates to be of greater risk relative to other types of affiliates, and by deeming them to be financial, they would be listed separately for analytical purposes as well as subjected to a higher capital charge. Specifically, the exposed GCC Instructions add the following to the definition of “financial entity”:

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

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

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

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

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

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

III. Treatment of Debt as Qualifying Capital

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

IV: Other Comments

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

* * * * * *

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

Sincerely,

Bob Ridgeway
Senior Government Relations Counsel
Attachment to Comment Letter of AHIP on the GCC Instructions and Template

1. We note that there are many areas within the template that are labeled “further work needed” or “technical discussions needed.” For example, “Summary Group Alternative 4” is blank. Also, in Summary 2 – Top Level: No formulas appear in the sensitivity section. When will companies have a completed template to review and test, and what other opportunities will there be to provide input on the template based on their review?

2. “Summary Alternative 5 – Organizational Option” is missing from both the template and the instructions. This option is intended to allow the reporting entity to present a summary of the results to assist regulators with understanding the submission.

3. Schedule 1D – Reporting “net dividends paid/(received)” is more practical and meaningful, because many entities act as “pass-through” for moving dividends up the corporate structure. In that context, “dividends received and not retained” becomes unnecessary.

4. I.A.2 in the instructions suggests that another consequence of “subsidization” may be “upward pressure on premiums to the detriment of insurance policyholders.” This implies that the GCC might somehow be a factor in regulating insurance premium rates, which we believe to be an inappropriate use of the GCC based on our understanding of its objectives.

5. I.A.2 in the instructions states that the GCC “provides an additional early warning signal to regulators so they can begin working with a company to resolve any concerns in a manner that will ensure that policyholders will be protected” and will “allow them to make informed decisions on both the need for action, and the type of action to take.” As stated, this is an overly ambitious aspiration for the GCC. In particular, at least in early years of implementation, the GCC will produce a ratio that would require much reliance on other existing regulatory tools to interpret – not the other way around. We understand that the Financial Analysis Handbook Drafting Group is working on guidance for regulators as to how the GCC would be utilized as part of financial analysis and in developing the Group Profile Summary. We recommend deleting the cited phrases in the instructions and await to comment on the work of the Drafting Group in that regard.

6. II.E.20. of the instructions discusses an annual redetermination of scope. This raises concerns about the meaningfulness of year-to-year trends in the GCC should the scope change. And if companies automate processes to produce the GCC, revisions would have to made on an annual basis.
7. AHIP is unclear as to why the NAIC is proposing to collect data on intangible assets, which is not an element that is necessary to calculate the GCC.
July 20, 2020

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

Re: Proposed Revisions to the Group Capital Calculation Instructions

Dear Commissioner Altmaier:

The American Property Casualty Insurance Association (APCIA) appreciates the opportunity to comment on the Group Capital Calculation (E) Working Group’s revised draft Group Capital Calculation (GCC) Instructions. APCIA is the primary national trade association for home, auto, and business insurers. APCIA promotes and protects the viability of private competition for the benefit of consumers and insurers, with a legacy dating back 150 years. APCIA members represent all sizes, structures, and regions—protecting families, communities, and businesses in the U.S. and across the globe.

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

I. Scope of Application

A. Determination of Material Risk

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

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

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

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

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

• The extent to which there is risk diversification (e.g., where risks of one or more entities outside the Insurance Group are potentially offset (or exacerbated) by risks of other entities) and whether the corporate structure or agreements allow for the benefits of such diversification to protect the Insurance Group.

• The degree to which capital management across the Broader Group has historically relied on funding by the Insurance Group to cover losses of the subject entity.

• The degree of risk correlation between the subject entity and the Insurance Group.

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

B. Scope of Application Starting Point

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

II. Risk Charges for Material Non-Insurance Entities

A. Non-Financial Entities

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

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

**B. Financial Entities**

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

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

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

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

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

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

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

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

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

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

A. Qualifying Instruments

APCIA recommends using criteria, rather than defined terms, to identify qualifying capital instruments. The GCC takes the approach of testing whether certain types of debt qualify as capital—specifically, senior debt, hybrid debt, surplus notes and “similar” instruments, and “other debt”. This contrasts with the approach taken by the IAIS in its ICS V.2.0 for the Monitoring Period, and by the FED in its proposed BBA. Both the ICS and the FED focus on criteria (e.g., permanence, loss absorbency, etc.) that are agnostic as to the title or name of a particular instrument.
There are two implications that we see. First, should the GCC go forward as currently proposed, the Working Group may need to supplement the GCC Instructions with definitions for each type of instrument. For example, “hybrid debt” is not defined in the Instructions. We understand that rating agencies treat subordinated debt issued by a parent company as “hybrid debt” as long as it is long-dated and has provisions to defer interest payments for a period of time. This could give rise to variation in treatment of hybrid debt (e.g., it may be unclear to a group if it should classify it as “hybrid” or as “subordinated” debt). On another level, comparability with the ICS needs to be considered, and on this point it seems that the more important issue is not whether types of debt are called out by name or more generically by tier, but whether comparable criteria to the ICS are used.

B. Treatment of Senior and Hybrid Debt

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

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

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

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

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

While APCIA is of course not privy to the confidential, company-specific results of GCC field testing, it appears based on the wording in the GCC Instructions alone that in the vast majority of cases the amount of paid-in capital and surplus will exceed tracked down-streamed proceeds and, possibly, the proxy values as well. (The NAIC reported that field-test results showed only a handful of groups that were impacted by the limit, and only half of those resulted in a “haircut” greater than 10% of reported debt). This, in part, is because the calculation includes the paid-in capital and surplus of all U.S. insurance entities in the group, regardless of the source of that capital (whether from debt proceeds or otherwise).
The GCC Must Test for Subordination to Policyholders. There are indications in the exposed GCC Instructions that consideration is being given to simplifying the process by eliminating the down-streaming criterion altogether such that qualified debt would be the greater of (3) over (2), above, subject to the caps. If so, there would in effect be no explicit test to support that the debt is structurally subordinated. Recognizing that U.S. senior debt is not contractually subordinated, this could raise issues about international perceptions about the GCC. Team USA argued long and hard to support structural subordination in the ICS, finally achieving victory in Abu Dhabi last November. While use of structural subordination in the ICS is termed by the IAIS as a “national discretion”, it is an option nonetheless in the ICS that is now recognized by the IAIS and its key member jurisdictions on the IAIS Executive Committee who voted to adopt ICS 2.0. Therefore, we have concerns with the notion of deleting the down-streaming criteria without any other criteria to support subordination, as explained in the following paragraphs.

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

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

Therefore, to the questions posed by the exposed GCC Instructions as to whether the down-streaming/tracking test should be maintained and, if so, what criteria should be in place, APCIA recommends keeping the test and using the criteria (with any U.S.-specific refinements necessary) that have been approved in ICS 2.0 for the Monitoring Period. That is, structurally subordinated debt should increase available capital to the extent the group and its lead state have determined such amount supports the insurance operations and is insulated from recourse by the lender, through tracking of down-streamed proceeds of the instruments into insurance subsidiaries.
There is, however, one other criterion for down-streaming that the Working Group could consider as an option to tracking down-streaming. Fundamentally, jurisdictional supervisors who permit subordinated debt to be treated for regulatory purposes as capital do so because policyholders remain protected; whether structurally subordinated or by the terms of the instrument, legally enforced restrictions and safeguards prevent the lender from “pulling the rug out from under” policyholders such that the debt is considered sufficiently permanent and loss absorbing. The issue becomes, to what assets and how much of those assets would the lender nonetheless have recourse?

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

C. Other Debt

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

D. Surplus Notes

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

E. Foreign Debt

APCIA likewise supports the GCC’s treatment of foreign debt. For debt issued by foreign entities, the GCC respects the treatment afforded by the local supervisor while also holding to the principle of subordination, whether that be achieved structurally or through the terms of the
instrument. If subordination is in place and if approved by the local supervisor as capital, the debt would qualify as capital in the GCC, a position with which APCIA agrees.

F. Overall Limitations on Debt as Capital

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

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

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

Sincerely,

Stephen W. Broadie
Vice President, Financial & Counsel

Matthew B. Vece
Manager & Tax Counsel
July 20, 2020

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

Re: GCC Working Group Exposures

Dear Commissioner Altmaier:

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

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

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

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

Sincerely,

Brighthouse Financial  
CNO Financial  
Genworth Financial  
Global Atlantic Financial Group  
Hannover Life Reassurance Company of America  
Jackson National Life Insurance
Lincoln Financial Group
National Life Group
Principal Financial Group
Protective Life
Reinsurance Group of America
Sammons Financial Group
Standard Insurance Company/StanCorp Financial Group
Transamerica
July 20, 2020

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

Dear Mr. Felice,

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

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

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

Capital Calibration

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

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

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

Downstream Tracking of Debt

The current instructions rely on downstream tracking in order to count debt proceeds as part of available capital. In practice, our company borrows externally in order to downstream it to the insurance companies; however, we have not found it necessary to track downstream transactions and question whether a tracking system would simply introduce complexity without providing a benefit.
We are in favor of a proposal to eliminate downstream tracking logic and replace it with a simple comparison to paid-in capital and surplus, for the following reasons:

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

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

Scalar Methodology

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

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

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

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

Scalar Formulation

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

We believe the following themes should define the scalars:

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

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

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

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

1. How is the country average computed? Is the concept of country average based on equal weighting each firm? Alternatively, is it size weighted, such that a large provider in Country Y may dominate the average of Country Y?

2. How frequently will the scalars be updated?

3. Will scalars derived from Year 20XX be applied to 20XX actual results, or will timing of filings and data availability create a lag?

4. Will scalars take into consideration only a single year, or alternatively, will a rolling average mechanism be utilized?

GAAP Equity

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

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

Sincerely,

Lauren Scott
Head of Regulatory and Government Affairs
Global Atlantic Financial Group
July 20, 2020

Via Electronic Delivery

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

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

Dear Commissioner Altmaier:

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

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

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

Sincerely,

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

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

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

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

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

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

Should the Working Group insist on maintaining limitations, we request the following changes to better acknowledge the presence of existing market guardrails and reduce the potential for the GCC to inhibit an insurer’s ability to manage its capital structure in a manner it feels is most appropriate and have procyclical effects during economic downturns. Further, the purpose of any imposed limitations that are retained should be explained in light of the stated intent for the GCC to serve as tool to obtain insight into risks as opposed to a binding constraint.
The cap of the allowance at 50% of total adjusted carrying value in Inventory B should be eliminated given that the underlying allowances, which are modeled largely after rating agency approaches, already have conservatism embedded in them.

- Specifically, the 30% factor for senior debt and 15% for hybrid debt are being applied to a more conservative base than rating agencies use for establishing limits – i.e., the GCC intends to apply the factors to the sum of total adjusted carrying value + outstanding senior and hybrid debt while rating agencies typically base their assessment on the group’s total consolidated U.S. GAAP equity.

- Adding a limit of 50% of total adjusted carrying value to the conservative 30% and 15% limits for senior and hybrid debt (relative to total adjusted carrying value + outstanding senior and hybrid debt) effectively lowers the 45% permitted (i.e., 30% + 15%) to approximately 33%.

More broadly, the different objectives of the GCC versus rating agency frameworks must also be considered. For example, S&P’s capital model is calibrated to much higher confidence levels (e.g., 97.2% for “BBB”) and views 20% to 40% financial leverage, based on a group’s total consolidated U.S. GAAP equity, plus outstanding debt, as “neutral”.

Requirements for tracking the down-streaming of debt issuance proceeds to regulated entities should be eliminated. Keeping funds at the holding company level is a prudent strategy that provides insurance groups flexibility to quickly and easily manage capital and liquidity needs across the group. We believe a tracking requirement could give rise to unintended consequences such as reducing the availability and fungibility of capital resources and forcing U.S. insurance groups to issue greater amounts of debt.

**The Base GCC Should Use the Excess Capital Ratio Scalar Approach**

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

Through its simplistic approach of only focusing on required capital, the Pure Relative Ratio Approach fails to adequately account for key differences in insurance regimes (e.g., level of conservatism embedded in reserves versus required capital, different valuation and asset admissibility standards, etc.). While the limited analysis to date may suggest the two approaches yield similar results, we believe they would diverge in cases where individual insurer or industry capitalization levels change and that the conceptual shortcomings of the Pure Relative Ratio Approach could result in false positives or negatives.
More broadly, we are concerned that adopting the Pure Relative Ratio Approach for purposes of the Base GCC would undermine the ongoing work at the NAIC’s work at the global level to secure recognition of the AM as comparable to the reference method version of the Risk-based Global Insurance Capital Standard ("ICS"). Specifically, we believe that the decision would prejudge the Pure Relative Ratio Approach as the methodology that should be adopted for the AM. Further, we believe it will be essential for the comparability assessment work to take a holistic approach to accounting for the different tools and methods supervisors employ to ensure insurers hold adequate loss absorbing resources to protect policyholders; of the two approaches the Working Group has considered, the Excess Capital Ratio Approach – with its total balance sheet approach – is the only one of the two that would accomplish this.

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

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

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

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

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

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

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

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

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

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

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

**The Draft Financial Analysis Handbook Guidance Should Be Exposed for Comment**

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

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

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

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

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

Commissioner Altmaier:

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

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

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

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

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

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

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

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

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

The paragraph provides a Drafting Note providing guidance to regulators:

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

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

State Farm believes that there should be some consistency in application under these provisions and that materiality should be based on the group’s net worth given the GCC is measuring risk of the group and not a particular entity in the group. RBC calculation along with other regulatory...
requirements provides the Lead State Regulator the information necessary to evaluate the solvency risk of an individual insurance entity and the GCC should be focused on information that a Lead State Regulator doesn’t already receive and be focused on the impacts to the group. Including a Drafting Note provides guidance, allows the Lead State Regulator and the preparer to utilize a different value for unique situations, and allows the focus of the GCC on those matters that truly impact a particular group.

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

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

Sincerely,

Chuck Feinen
State Farm Mutual Automobile Insurance Company
July 20, 2020

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

Via electronic mail to Lou Felice

Re: Comments on GCC Instructions and Template

Dear Commissioner Altmaier:

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

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

**Comments on the Instructions**

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

Our comments in both sections are labeled according to the paragraph labels in the GCC Instructions.
**Instructions Comments – Key Concerns**

**Key Concern #1: Calibration Level**

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

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

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

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

**Key Concern #2: Definition of “Financial Entity”**

IV.22: We believe that the definition of “Financial Entity” is far too broad, in that it sweeps in “Affiliates that are integral to the performance of the insurance contract or the provision of insurance or financial products or services to policyholders, members or depositors,” such as “claims adjusters or processors, third party administrators, pharmacy, medical provider groups, and other benefit managers,” etc., even when those entities are not material to the group or calculation as a whole. Affiliates that merely provide contracted services to a carrier should not be defined as “financial”: they do not create any more financial
risk to their affiliated insurers than do non-affiliates that provide the same services to other insurers. In fact, given that regulators have oversight over inter-affiliate service agreements, we suggest that affiliated service providers present less risk than do non-affiliates. In the case of health groups, some of the examples given actually diversify risk for the insurance entity in the group, facilitating more access to capital by the insurance entity. The aim of the working group should not be to promote smaller, less integrated or diversified groups.

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

**Key Concern #3: Intangible Assets**

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

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

We note also that the increasingly digital economy is based on software and information assets. Under GAAP, the capitalization of software assets is narrow, and amortization relatively short, compared to traditional fixed assets. Furthermore, changes made to GAAP in 2001 eliminated both the “pooling of interests” accounting in acquisitions and the amortization of goodwill. Accordingly, both business trends and accounting changes have made the differentiation of “intangible” assets increasingly less relevant.
Key concern #4: Use of the GCC

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

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

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

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

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

We also have a concern that the instructions as written may not make clear that the GCC is intended to be used solely by the lead state regulator. In the statement that the GCC “provides an additional early warning signal to regulators so they can begin working with a company to resolve any concerns,” the use
of the word “company,” rather than “group,” could be taken to suggest that the GCC is intended to be a tool for any regulator responsible for any legal entity within a group. Likewise, the statement, “State insurance regulators already have broad authority to take action when an insurer is financially distressed, and the GCC is designed to … allow them to make informed decisions on both the need for action, and the type of action to take,” suggests that the GCC will be used by the domiciliary regulator of each insurer. We do not believe that is intended to be the function of the GCC.

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

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

I.A.3. This paragraph contains a statement indicating that the GCC could be used “in conjunction with group-specific risks and stresses identified in the Own Risk and Solvency Assessment (ORSA) Summary Report as well as risks identified in Form F filings that may not be captured in legal entity RBC filings.” While the GCC, the ORSA, and Form F are all intended to evaluate the risks of the group, we think it likely will be misleading to financial analysts to suggest that the GCC can be used together with the other two. They lack comparability to each other, for several reasons:

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

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

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

3. State insurance regulators currently perform group analysis on all U.S. insurance groups, including assessing the risks and financial position of the insurance holding company system based on currently available information; however, they do not have the benefit of a consolidated statutory accounting system
and financial statements to assist them in these efforts. It was noted prior to development that a consistent method of calculating group capital for typical group risks would provide a very useful tool for state financial regulators to utilize in their group assessment work. It was also noted that a group capital calculation could serve as a baseline quantitative measure to be used by regulators, to supplement in conjunction with the view of group-specific risks and stresses provided by identified in the Own Risk and Solvency Assessment (ORSA) Summary Report filings and as well as risks identified in Form F filings that may not be captured in legal entity RBC filings. Finally, it’s important to understand that regulators believed that a group capital calculation would be another valuable tool to complement the states’ legal entity focused solvency assessments.

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

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

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

**Instructions Comments – Additional Concerns**

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

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

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

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

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

- Is this limited to formal, legally enforceable financial guarantees among members of the group?
- Does it matter whether such guarantees can only result in payment to insurers, not from insurers?
• Can the definition of “cross support mechanisms” ever result in the ultimate controlling person being out of scope?
• If the ultimate controlling person is always in scope, would all of its subsidiaries of material size automatically be in scope, since they could have a material impact on the ultimate controlling person?

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

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

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

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

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

IV.28: The “Ultimate Controlling Person” is defined to be, “As used in the NAIC’s Insurance Holding Company System Regulatory Act (Model #440).” Model #440 does indeed use the term, but while it defines “control” and “person,” “ultimate controlling person” itself is never defined—that is, there is no
explanation of what “ultimate” means. This seems an important concept that should be defined more precisely, especially since the “head of the Insurance Group” may be distinct from the “Ultimate Controlling Person.”

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

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

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

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

Comments on the Template

Although we understand the need to have a tool that quantitatively calculates group results, we suggest it is inappropriate to use the tool as a way to simply gather information about unregulated entities that do not impact the results of the GCC calculation itself, especially as most of this information is available to regulators from other filings. The following are examples of the information being collected that does not impact the results of the calculation:
• a significant amount of information related to trend analytics, which - on the legal entity basis-
are not meaningful to the calculation;
• Reinsurance Assumed from Affiliates and Reinsurance Ceded to Affiliates. We question the
relevance of the information to the calculation and note that this information is readily available
in the annual statements;
• the notional values of both Intercompany Guarantees and Capital Maintenance Agreements,
because 1) most, like insolvency reinsurance, have no stated value or have values that are based
upon a calculation and not a fixed amount; and 2) in practice, these have extremely low
probability of triggering guarantor action (earlier versions of this analysis weighted any notional
amount by currently expected use);
• the value of intangible assets;
• descriptions related to intragroup assets; the values of some intragroup assets are also asked for
on the Questions tab;
• descriptions related to reported adjustments;
• dividends paid and received;
• how downstream debt proceeds are tracked; and
• a listing of Schedule A and BA assets, which can easily be found in the NAIC financial statements.

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

Sincerely,

James R. Braue
Director, Actuarial Services
UnitedHealth Group

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

Some of the Introductory wording could be revised and/or moved to the Analysis Guidance being drafted & reviewed by the drafting subgroup, particularly with reference to cross subsidization. Comments on other thresholds applied in the analysis guidance can be addressed there. Staff notes that industry representatives are assisting in revising and reviewing the analysis guidance.

Although the GCC in totality can be viewed as an early warning vehicle, the GCC ratio itself is just one piece. This is similar to other analytical tools. Early warning is distinct from capital standard driving statutorily authorized regulator action. Although made clear throughout the GCC process that it will not be a capital standard, clarification of language to avoid any such inference will be considered.

As a group rather than entity-based tool, the submission itself is limited to the lead-State regulator (s/b addressed in Model Holding Company Act), it seems logical that post review regulatory concerns may be shared with other involved regulators in collaborative forums. Staff will look at the suggested language.

### Issue 2

<table>
<thead>
<tr>
<th>Calibration Level</th>
<th>ACLI Global Atlantic Prudential</th>
<th>Adopt a 200% ACL calibration level for the GCC. In addition, calibrations of other factors and regimes should be based on 200% ACL level RBC as well.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>United HealthCare</td>
<td>Lower 300% Calibration (consider lower than 200%) and/or add a diversification component</td>
</tr>
<tr>
<td></td>
<td></td>
<td>The calibration does not adequately consider the capital mitigation in diversified integrated holding company systems.</td>
</tr>
</tbody>
</table>

**Initial NAIC Staff Comments:**

Staff recommends that a 300% calibration be retained for a group-wide analytical tool that compliments entity-based RBC. The working group should consider whether using CAL or lower could imply that some specified regulatory action is imminent, especially within the context recommended by some commenters that risk charges mirror entity RBC. Staff believes that would add confusion between RBC as a standard and GCC as an analytical tool. Using a level above CAL RBC is consistent with a regulator analytical tool and consistent with an RBC reference point (Trend Test). Further it applies a reference point that is agnostic to the structure of the group.

A secondary issue is ability to be somewhat consistent with the AM – ICS being proposed by the NAIC in cooperation with other U.S. regulatory partners.

Staff believes that issues related to calibration are better addressed via the working group decisions on the definition of a financial entities, level of post-covariance charges to be applied to non-financial entities, and definition of material risk for purposes of potential exclusion of entities from the calculation.

Staff agrees that there should be careful coordination between the GCC Template, and the analysis guidance as regards the level of the GCC ratio. Staff notes that industry representatives are assisting in revising and reviewing the analysis guidance.
### Issue 3

<table>
<thead>
<tr>
<th>Commenter</th>
<th>Essence of Comment</th>
<th>Primary Rationale</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Scope of Application</strong></td>
<td>AHIP APCIA</td>
<td>GCC Instructions should explicitly state that non-material entities (including financial) within the Broader Group (but outside the Insurance Group) should be excluded from the Scope of Application.</td>
</tr>
<tr>
<td>State Farm</td>
<td>Requests that excluded entities not be required to be on the Inventory Tab or, at least, the Lead State Regulator have the discretion to not require excluded entities on the Inventory Tab if requested by the preparer.</td>
<td>Gathering information under the GCC from entities that are excluded from the GCC seems counterintuitive and duplicative in certain situations.</td>
</tr>
<tr>
<td>State Farm</td>
<td>Questions why the Draft Instructions do not allow exclusion of immaterial financial or insurance entities that are isolated from the group as are non-financial entities.</td>
<td>Acknowledging the isolation of financial and insurance entities fits within already existing regulatory arrangements as well as the GCC and acknowledges that capital is not freely fungible for use by the group or entities within the group.</td>
</tr>
</tbody>
</table>

**Initial NAIC Staff Comments:**

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

The instructions currently limit the amount of data that is required from entities that the lead-State regulator agrees should be excluded.
<table>
<thead>
<tr>
<th>Issue 4</th>
<th>Commenter</th>
<th>Essence of Comment</th>
<th>Primary Rationale</th>
</tr>
</thead>
<tbody>
<tr>
<td>Excluded entities / Material Risk</td>
<td>ACLI, AHIP, APCIA</td>
<td>GCC Instructions should provide a definition of “material risk” for purposes of the Scope of Application as follows “risk emanating from a non-insurance entity that is of a magnitude that would adversely impact a group’s insurance operations and its ability to pay policyholder claims.” GCC Instructions should provide a principles-based definition of “material risk” for purposes of the Scope of Application. Suggest that “material risk” should be defined as “risk emanating from a non-insurance entity that could adversely impact a group’s insurance operations and ability to pay policyholder claims.” APCIA recommends developing a list of factors related to whether an entity could adversely impact a group’s ability to pay policyholder claims. (List included in letter – Page 2). No single factor is determinative of materiality of risk, nor should these factors be used as a scorecard or checklist.</td>
<td>- Follows the fundamental reason for state insurance regulation and the stated objective of the GCC: policyholder protection. - Is in accordance with international standards. For example, under ICP 23. - Given the diverse structures and business models of insurers, it would be impracticable to develop a one-size-fits-all checklist of guidelines that would be useful for materiality determinations across all groups. - Form B and D processes and Enterprise Risk Reports entail similar considerations and are already enshrined in the state regulatory process. Insurers and regulators could then use these factors to undertake a materiality analysis based on the totality of the facts and circumstances by considering the factors and how they apply to the group’s business.</td>
</tr>
<tr>
<td>State Farm</td>
<td>Requests a baseline materiality definition be provided while maintaining Lead State Regulator discretion to determine if a higher or lower material threshold is appropriate. Suggests a group equity threshold for materiality with a drafting note suggesting 5% threshold subject to regulator discretion.</td>
<td>There should be some consistency in application under these provisions and that materiality should be based on the group’s net worth given the GCC is measuring risk of the group and not a particular entity in the group. Baseline for materiality while still allowing the Lead State Regulator and the preparer to use a higher or lower threshold given circumstances presented by the preparer.</td>
<td></td>
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</table>

Initial NAIC Staff Comments:

Staff agrees that materiality of risk is important in deciding whether to exclude non-financial entities. Staff supports a definition to promote consistency in completion of the GCC. We are supportive of principles-based criteria being included in the instructions. We are also supportive of quantitative Criteria if preferred by the working group but recognize that there has not up until now been coalescence around a single quantitative benchmark.

See staff comments above under Scope of Application (Issue #3) regarding financial entities.
<table>
<thead>
<tr>
<th>Issue 5</th>
<th>Commenter</th>
<th>Essence of Comment</th>
<th>Primary Rationale</th>
</tr>
</thead>
<tbody>
<tr>
<td>Grouping</td>
<td>Prudential</td>
<td>Supports flexibility of current grouping language, but state regulators should retain the option of requesting more granular information should they feel it is needed to obtain a sufficient view of risks within the group.</td>
<td>Self-Explanatory</td>
</tr>
</tbody>
</table>

**Initial NAIC Staff Comments:**

Although staff believes this is implicit, we support adding explicit language.
<table>
<thead>
<tr>
<th>Issue 6</th>
<th>Commenter</th>
<th>Essence of Comment</th>
<th>Primary Rationale</th>
</tr>
</thead>
<tbody>
<tr>
<td>Definition of Financial Entities</td>
<td>AHIP</td>
<td>Disagrees with the notion that certain affiliates are inherently riskier than others and more generally with the expanded definition of financial affiliates. Third-party administrators and pharmacy benefit managers, provider groups, and pharmacy benefit managers should not be considered financial entities.</td>
<td>• There is a wide array of types of non-affiliated entities within insurance groups, and it is overly simplistic to conclude that all that are somehow associated with assisting the insurer with contract performance or policyholder services are inherently riskier than others.</td>
</tr>
<tr>
<td></td>
<td>APCIA</td>
<td>APCIA is concerned with the expanded definition of financial entity in the GCC.</td>
<td>• Form B and D processes recognize that transactions with affiliates may have risks.</td>
</tr>
<tr>
<td></td>
<td>United HealthCare</td>
<td>Base comments are similar to AHIP Comments. This is amplified by lack of diversification credit for the wide array of entities defined as “financial”</td>
<td>• Affiliates that merely provide contracted services to a carrier should not be defined as “financial”: they do not create any more financial risk to their affiliated insurers than do non-affiliates that provide the same services to other insurers.</td>
</tr>
<tr>
<td></td>
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<td></td>
<td>• Some of the examples given diversify risk for the insurance entity in the group, facilitating more access to capital by the insurance entity. The aim of the working group should not be to promote smaller, less integrated or diversified groups.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>• Greater regulatory oversight to certain currently defined entities and regulatory review of intercompany agreements should be considered to reduce the group’s risk.</td>
</tr>
</tbody>
</table>

Initial NAIC Staff Comments:
Staff appreciates the comments on the breadth and targeting of defining certain affiliates as financial entities as that was one of several areas of the instructions where comments were specifically requested. The issue of an appropriate definition of financial entities impacts other concerns identified in the comments including, calibration, scope of application, materiality of risk, and consistency across group structures. The instructions currently do identify some specific financial entities without regulatory capital requirements and some associated activities, so the working group could consider more specificity related to activities based on the activities of those identified entities. As intended, staff also believes that the quantitative aspects of the GCC in the context of a regulatory view, as well as the additional data supporting analytics does compliment rather than overlap the benefits of other regulatory filing requirements.
<table>
<thead>
<tr>
<th>Issue 7</th>
<th>Commenter</th>
<th>Essence of Comment</th>
<th>Primary Rationale</th>
</tr>
</thead>
<tbody>
<tr>
<td>Treatment / Charges Financial Entities</td>
<td>ACLI</td>
<td>To the extent that there are differences in the GCC and legal RBC treatment for subsidiaries that have been de-stacked and reported separately from their legal entity parent, then it seems desirable for the GCC and RBC treatment to align. To the extent that there are differences between the two, we recommend the Working Group explain the rationale for the difference (e.g., achieving substantial consistency in charges regardless of corporate organizational structure) and, if appropriate, refer the issue to the appropriate RBC working for further dialogue.</td>
<td>ACLI believes that the GCC should be consistent with the legal entity rules applied to insurance legal entities – including the subsidiaries of insurance legal entities. In the long run, we believe this approach will benefit regulators and the industry by promoting a more consistent and up-to-date risk framework.</td>
</tr>
<tr>
<td></td>
<td>AHIP</td>
<td>Recommends applying the equity-based capital charge that is recommended for non-financial affiliates to all affiliates that are not subject to a regulatory capital requirement.</td>
<td>Subjecting these entities to a capital charge for financial entities (12% of 3-year average gross revenue – possibly to be increased to 15%) could result in a significant additional charge as compared to current RBC.</td>
</tr>
<tr>
<td></td>
<td>APCIA</td>
<td>in the short term, use a capital charge that is roughly equivalent to the current post-covariance charge (presumably equity charge) for such affiliates in RBC.</td>
<td>Over the first few years of the GCC’s implementation, data can be collected and used to derive a more risk-sensitive charge that is pragmatic (e.g., a differentiated charge for entities of high/medium/low risk as determined by specified criteria).</td>
</tr>
<tr>
<td></td>
<td>Prudential</td>
<td>Supports adopting a single approach for establishing a proxy capital measure for all financial entities that are not subject to a regulatory capital requirement. Supports a method that most closely aligns with how the AM - ICS will ultimately treat this item.</td>
<td>• Ensuring state regulators obtain adequate insight into the entities within the insurance group and risks associated with them is the key point of consideration for these entities and this is best accomplished through the inventory element of the GCC as opposed to an arbitrary proxy capital calculation. • To the extent a state regulator believes an entity poses material risk to the group, they have discretion to request additional information to understand the risks.</td>
</tr>
</tbody>
</table>
Initial NAIC Staff Comments:
Staff notes that as a complimentary group analytical tool covering entities other than those owned by RBC filer, total consistency with RBC is not entirely relevant, particularly for financial entities. Staff does agree that the Capital Adequacy Task Force should determine whether the treatment of financial entities in the GCC is relevant for U.S. Insurer entity-based RBC. This can be tasked to the current Ad Hoc Affiliates Subgroup or directly to the RBC Working Groups.

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

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

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

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

Staff supports the 15% charge as reflective of a 300% calibration and consistency whether where international standards are headed but understands that the working group may consider a scaled version as a starting point for the near-term. Staff supports the proposal to consider refinements over time for financial entities not subject to a regulatory capital requirement in order to be more risk sensitive along the lines of the low / medium / high approach suggested by APCIA (e.g. lower risk entities could go with the post covariance non-financial entity charge / medium risk entities, a scaled revenue-based charge / and high risk entities, the full revenue based charge).
<table>
<thead>
<tr>
<th>Issue 8</th>
<th>Commenter</th>
<th>Essence of Comment</th>
<th>Primary Rationale</th>
</tr>
</thead>
<tbody>
<tr>
<td>Treatment / Charges - Non-Financial Entities (incl. material non-financial A / BA)</td>
<td>ACLI</td>
<td>ACLI was unable to discern how the proposed charges for “other non-insurance/non-financial entities” and “material Schedule A/BA entities” were created.</td>
<td>Further clarification on this issue is necessary, including an explanation of why the Working Group is recommending a novel approach that has not been subject to field testing.</td>
</tr>
</tbody>
</table>
| AHIP | Risk charges for non-financial entities should be equal or very similar to the current charge in the sectoral RBC formulas, i.e., 3% post-covariance charge in the case of health insurers.                                                                                                                                                                                                                                                                                                                                                             | - The GCCWG has not provided data to suggest that a more substantial risk charge is needed to protect policyholders.  
- Form B and D processes are already in place to ensure that the regulated legal entity is protected from the non-regulated, non-insurance entity. |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |
| APCIA | During the first few years of the GCC’s implementation use 3% of 3-year average revenue. Once some experience is gained with the GCC, the Working Group should consider a simple variable risk charge (low / medium / high risk charge) that is more risk-sensitive based on industry and activity. | A period during which experience will be gained that can then be analyzed in more detail and across more groups than was possible in field testing.                                                                                                                                                                                                                                                                               |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |
| Prudential | Supports adopting a single approach for establishing a proxy capital measure for all non-financial entities. | See rationale for financial entities.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                     |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |
| United HealthCare | Charge should be based on the group specific after covariance equity charge. | Using an average industry post covariance charge is not reflective of the proportion of insurance vs. non-insurance business within a group.                                                                                                                                                                                                                                                                                                                                                     |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |

**Initial NAIC Staff Comments:**

Once materiality of risk has been established, Staff supports a post covariance equivalent equity-based charge that is broadly consistent with RBC treatment for non-financial entities that are “included” in the GCC. The current template uses a single average post covariance factor across all industry types, but Staff believes that an industry specific charge has merit. A group specific charge was previously tested and could be considered by the working group, but unlikely to have a significant impact on the GCC. However, NAIC Staff would be interested in information to the contrary by a group that has run the numbers given that the NAIC will not be receiving the GCC filings.

Staff supports the suggestion to make future refinements based on continued collection of data but again notes that NAIC will not have access to the submissions.
<table>
<thead>
<tr>
<th>Issue 9</th>
<th>Commenter</th>
<th>Essence of Comment</th>
<th>Primary Rationale</th>
</tr>
</thead>
</table>
| Allowance for Debt | ACLI | The current debt caps are too restrictive. | • Could negatively impact a group’s ability to prudently manage capital and liquidity risks.  
• Tying the constraint to a percentage of the group’s available capital embeds an undesirable element of procyclicality into the GCC, because a company’s available capital is likely to decrease in times of stress, especially if markets crash.  
• The 30% factor for senior debt and 15% for hybrid debt are being applied to a more conservative base than rating agencies use for establishing limits  
• Adding a limit of 50% of total adjusted carrying value to the conservative 30% and 15% limits for senior and hybrid debt (relative to total adjusted carrying value + outstanding senior and hybrid debt) effectively lowers the 45% permitted (i.e., 30% + 15%) to approximately 33%.  
• Interpretations related to how to support “tracking” will be difficult to verify and may lead to inconsistencies across groups. |
| | Prudential | Requirements for tracking the down-streaming of debt issuance proceeds to regulated entities should be eliminated. | • Keeping funds at the holding company level is a prudent strategy that provides insurance groups flexibility to quickly and easily manage capital and liquidity needs across the group.  
• A tracking requirement could give rise to unintended consequences such as reducing the availability and fungibility of capital resources and forcing U.S. insurance groups to issue greater amounts of debt. |
<p>| | United HealthCare | | |
| ACLI | Prudential United HealthCare | | |
| | | | |
| ACLI | Remove the call option criteria, because the exercise of a call option is typically followed by refinance of the instrument which supports its permanence and structural subordination. | Relative to the 5-year term, the presence of call options should not prevent a capital instrument’s inclusion as a qualifying instrument. Call options are a common feature of U.S. issued capital instruments. |</p>
<table>
<thead>
<tr>
<th>Allowance for Debt</th>
<th>Global Atlantic</th>
<th>Eliminate downstream tracking logic and replace it with a simple comparison to paid-in capital and surplus.</th>
</tr>
</thead>
<tbody>
<tr>
<td>APCIA</td>
<td>The treatment of debt differs in some key respects from that which was adopted by the International Association of Insurance Supervisors (IAIS) in the Insurance Capital Standard (ICS) in 2019.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>FED BBA is more closely aligned with the principles-based criteria in the ICS than with the approach taken in the exposed GCC Instructions</td>
<td></td>
</tr>
<tr>
<td>Working Group</td>
<td>Working Group may need to supplement the GCC Instructions with definitions for each type of instrument. For example, “hybrid debt” is not defined in the Instructions</td>
<td></td>
</tr>
</tbody>
</table>
|                    | • Rating agencies treat subordinated debt issued by a parent company as “hybrid debt” if it is long-dated and has provisions to defer interest payments for a period of time. This could give rise to variation in treatment of hybrid debt (e.g., it may be unclear to a group if it should classify it as “hybrid” or as “subordinated” debt)  
• Comparability with the ICS needs to be considered, and on this point it seems that the more important issue is not whether types of debt are called out by name or more generically by tier, but whether comparable criteria to the ICS are used. |
<p>|© 2020 National Association of Insurance Commissioners |</p>
<table>
<thead>
<tr>
<th>Allowance for Debt</th>
<th>APCIA</th>
<th>Replace terminology “additional capital allowance” with “within supervisory limits”.</th>
<th>Focusing the Instructions’ text on “limits”, rather than “allowance”, will help in some respects with perceptions about comparability.</th>
</tr>
</thead>
</table>
|                    |       | Add criteria supporting structural subordination to “Tracked Down-streamed Debt” proceeds rather than eliminate that test. | • Team USA argued long and hard to support structural subordination in the ICS.  
• While down-streaming has raised many questions about how debt proceeds can be tracked and verified, the ICS criteria are workable and rely in large measure on each group and its group-wide supervisor to make that determination in light of the unique facts and circumstances.  
• The IAIS avoided prescribing detailed rules or criteria for tracking. APCIA believes the NAIC should do the same in the GCC, leaving the determination of the amount down streamed to the lead state working in conjunction with the group.  
• This would include criteria to support that the qualifying amount of debt to be treated as capital is actually subordinated (either contractually by the terms of the instrument, or structurally), and other principle-based criteria, as in the ICS, to support permanence, loss absorbency, etc. Some refinement of the ICS criteria may be necessary to address U.S.-specific nuances for the GCC. |
|                    |       | Another option to test structural subordination is to limit the amount of senior debt to qualify as capital to that which is in excess of the liquid assets in the holding company. | As a practical matter, the lender would have recourse only to the liquid assets that remain in the entity that issued the debt (i.e., the holding company in the case of senior debt). The unconsolidated balance sheet of the holding company (reflects a very large, illiquid investment in insurance subsidiaries, control over which is subject to regulatory oversight and approval. |
|                    |       | APCIA is open to the possibility of some allowance for other debt in the future. | Self-Explanatory |
|                    |       | It would seem appropriate that the overall limitation should apply to all debt, including surplus notes and... | |
| APCIA | foreign debt. That said, and as noted above, APCIA supports no limit on surplus notes of mutual insurers. We do not offer a view on the overall limit of 50%. However, the ICS comparability issue is also an important goal and encourage the Working Group to give due consideration in the context of the overall limit. | See Staff Comments The comparability issue is also an important part of navigating the way forward with the GCC and encourage the Working Group to give due consideration in the context of the overall limit. |

**Initial NAIC Staff Comments:**

Staff is open to eliminating the tracked down-streamed option as suggested by some commenters. The arguments put forth by APCIA are relevant, however, structural subordination is strongly represented by insurer paid in capital and surplus which has the most rigorous regulatory control over distributions.

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

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

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

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

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

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

**Allowance for Debt as additional capital is an area of potential divergence between the GCC and AM-ICS.**
<table>
<thead>
<tr>
<th>Issue 10</th>
<th>Commenter</th>
<th>Essence of Comment</th>
<th>Primary Rationale</th>
</tr>
</thead>
</table>
| Scalars  | ACLI      | Use the Excess Approach over the Pure Approach. Use the Excess Relative Ratio Approach for scaling non-U.S. capital ratios to U.S. RBC. | • This method utilizes two anchor points for scaling.  
• The Pure Relative Ratio lacks a mechanism to ensure that a non-U.S. firm at the regulatory intervention level within its respective country will be at the U.S. RBC intervention level once scaled.  
• The Pure Relative Ratio Approach fails to adequately account for key differences in insurance regimes (e.g., level of conservatism embedded in reserves versus required capital, different valuation and asset admissibility standards, etc.).  
• The decision would prejudge the Pure Relative Ratio Approach as the methodology that should be adopted for the AM and could undermine the ongoing work at the NAIC’s work at the global level to secure recognition of the AM. |
|          | Global Atlantic Prudential | Transparency of how the scalars are calculated will be critical, regardless of which scaling methodology is selected | • Consistency – scalars should be calculated and applied consistently across all non-U.S. regimes.  
• Specificity – scalars should be discretely computed and applied amongst life, property casualty and health insurance companies.  
• Stability – the results of applying scalars to Non-U.S. capital ratios should not be volatile; for example, converting to U.S. RBC should not yield a significant headwind in one year, and a significant tailwind in the following year. |

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

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

The working group should be aware of ongoing work on the AM-ICS as scalar methodology is an area of potential convergence between the GCC and AM-ICS.
<table>
<thead>
<tr>
<th>Issue 11</th>
<th>Commenter</th>
<th>Essence of Comment</th>
<th>Primary Rationale</th>
</tr>
</thead>
</table>
| Sensitivity Analysis | ACLI Prudential | Eliminate Sensitivity Analysis Tab altogether | • Narrowing the design of the GCC will ensure insurers, supervisors (domestic and foreign) and other stakeholders have a clear vision and understanding of what the GCC is (e.g., it would eliminate the need to distinguish between a “Base” view and alternative measures).  
• To the extent broader information on the insurance group is of interest to a state regulator, we believe it should be obtained through discretionary powers as opposed to embedding it in the GCC template. |
| Coalition | Supports Eliminating the XXX/AXXX analysis in favor of a referral. | • The need for the GCC to adhere fully to legal entity rules in support of the state-based legal entity solvency system |

**Initial NAIC Staff Comments:**

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

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

Staff believes that the data is more readily accumulated in the Sensitivity Tab from other parts of the template. Separating it would require additional work particularly for non-insurance entities.
<table>
<thead>
<tr>
<th>Issue 12</th>
<th>Commenter</th>
<th>Essence of Comment</th>
<th>Primary Rationale</th>
</tr>
</thead>
</table>
| Other Information Collected | United HealthCare | Questions the rationale for collecting information on intangible assets (such as deferred acquisition costs, provider contracts, customer lists, and goodwill). | • The focus on intangible assets, to the exclusion of other types of assets, seems unwarranted.  
• Regardless of their availability for sale, intangible assets do produce a stream of income to the group; otherwise, GAAP accounting would require that they be written down in value or written off entirely.  
• As businesses rely more and more on digital assets and intellectual property as the basis for their operations, and less and less on fixed assets, there is more scrutiny of the value of those assets, and there should be less concern about whether the stated values are appropriate. We  
• Both business trends and accounting changes have made the differentiation of “intangible” assets increasingly less relevant. |

**Initial NAIC Staff Comments:**
Staff notes that the GCC represents a regulatory view of group available capital. It is not intended that the value of intangibles allowed under GAAP, SAP or another accounting basis should be excluded. However, staff believes that there is some value in quantifying the extent that group capital is comprised of illiquid non-physical assets. This can provide good regulatory information in in addition to the views of rating agencies or other group stakeholders.

Staff is comfortable with assessment of the value of the data collected in the Tab by the Analytics Guidance Drafting Group and making any adjustments accordingly.

<table>
<thead>
<tr>
<th>Issue 13</th>
<th>Commenter</th>
</tr>
</thead>
<tbody>
<tr>
<td>Other Technical Comments, Language Edits, Clarification requests and Second Tier Concerns</td>
<td>AHIP, APCIA, UHG</td>
</tr>
</tbody>
</table>

**Initial NAIC Staff Comments:**
These items will be reviewed and accepted, adjusted or rejected after this meeting based on the direction taken in response to the comments discussed today.
The Group Solvency Issues (E) Working Group of the Financial Condition (E) Committee met via conference call July 29, 2020. The following Working Group members participated: Justin Schrader, Chair (NE); Jamie Walker, Vice Chair (TX); Susan Bernard and Kim Hudson (CA); Kathy Belfi (CT); Charles Santana (DE); Virginia Christy and Carolyn Morgan (FL); Kim Cross (IA); Cindy Andersen and Eric Moser (IL); Roy Eft (IN); John Turchi (MA); Judy Weaver (MI); Debbie Doggett and John Rehagen (MO); Diana Sherman (NJ); Dale Bruggeman (OH); Kimberly Rankin (PA); Doug Stolte (VA); and Steve Junior (WI).

1. **Adopted its 2019 Fall National Meeting Minutes**

   Mr. Schrader stated that the Working Group last met at the 2019 Fall National Meeting, but also met Feb. 11, 2020, via conference call in regulator-to-regulator session, pursuant to paragraph 6 (consultations with staff on technical guidance) of the NAIC Policy Statement on Open Meetings.

   Ms. Walker made a motion, seconded by Mr. Bruggeman, to adopt the Working Group’s Dec. 7, 2019, minutes (see NAIC Proceedings – Fall 2019, Financial Condition (E) Committee, Attachment Seven). The motion passed.

2. **Heard an Update from the ORSA Implementation (E) Subgroup**

   Ms. Belfi provided an update of recent activities of the ORSA Implementation (E) Subgroup, noting that the Subgroup met via conference call July 13 in joint session with the Risk-Focused Surveillance (E) Working Group. The meeting was held in regulator-to-regulator session, pursuant to paragraph 3 (discussions of specific companies, entities or individuals) of the NAIC Open Meetings Policy, to discuss takeaways from the 2019 Own Risk and Solvency Assessment (ORSA) Peer Review session and the development of potential changes to NAIC handbooks in response to those takeaways.

   Ms. Belfi stated that as each of the NAIC handbooks containing ORSA review guidance are public documents, any revisions to such guidance will be discussed on public conference calls and subject to a public comment period. As such, the Subgroup plans to continue working in this area and schedule open calls to discuss the proposed revisions as necessary.

   In addition, Ms. Belfi stated that the Subgroup has received inquiries from companies regarding regulator expectations for COVID-19 exposure and scenario analysis in ORSA filings. Ms. Belfi stated that the Subgroup intends to schedule a conference call to discuss regulator expectations and may develop some considerations for the industry in this area.

3. **Heard a Report on IAIS Activities**

   Mr. Schrader provided a report on recent group-related activities of the International Association of Insurance Supervisors (IAIS), including the status of ongoing projects of the Insurance Groups Working Group (IGWG). While the efforts of the IGWG have been affected by COVID-19, virtual meetings continue to be held. As such, work continues to move forward on updates to the Application Paper on Supervisory Colleges to reflect revisions to Insurance Core Principle (ICP) 3 (Information Sharing and Confidentiality Requirements) and ICP 25 (Supervisory Cooperation and Coordination), which were adopted in November 2019.

   The IGWG is also contemplating developing an application paper or training and educational materials on best practices supporting a supervisory assessment framework. The idea is to collect good supervisory practices from IAIS members supporting a group-wide supervisory assessment framework. These materials would be developed as a “members-only” document.
4. Discussed a Referral from the Group Capital Calculation (E) Working Group

Mr. Schrader stated that the Working Group received a referral from the Group Capital Calculation (E) Working Group requesting assistance in quantifying and evaluating the impact of XXX/AXXX reserves held by grandfathered captives on the group’s overall capital position. Mr. Schrader stated that a drafting group of several member states was formed to take up the request and will be reporting its results to the full Working Group.

5. Discussed Comments Received on ComFrame Gap Analysis

Mr. Schrader stated that the next agenda item relates to a new charge the Working Group received for 2020: “Assess the IAIS Common Framework for the Supervision of Internationally Active Insurance Groups (ComFrame) and make recommendations on its implementation in a manner appropriate for the U.S.”

Mr. Schrader stated that the IAIS adopted ComFrame on Nov. 14, 2019, which establishes supervisory standards and guidance focusing on the effective group-wide supervision of internationally active insurance groups (IAIGs). The intent of ComFrame is to help supervisors address group-wide risks and avoid supervisory gaps by supporting coordination across jurisdictions. ComFrame builds on, and expands upon, the high-level standards and guidance currently set out in the ICPs of the IAIS, which generally apply on both an insurance legal entity and group-wide level. There are ComFrame elements included in 10 of the 25 ICPs, as well as the ICP Introduction and Assessment Methodology. Consistent with the application of the ICPs, the minimum requirements established by ComFrame are expected to be implemented and applied in a proportionate manner. However, supervisors have the flexibility to tailor implementation of supervisory requirements and application of insurance supervision to achieve the outcomes described in ComFrame standards.

Mr. Schrader stated that as the IAIS has now finalized and adopted ComFrame, it is time for state insurance regulators to review and assess their implementation domestically. Mr. Schrader stated that while certain elements of ComFrame were already incorporated into the 2014 revisions to the Insurance Holding Company System Regulatory Act (§440), there have been several additions and enhancements to ComFrame since that time. As such, following discussions on implementation considerations at the 2019 Fall National Meeting, the Working Group asked NAIC staff to proceed with performing a ComFrame gap analysis to highlight any elements that might need to be considered for implementation in the U.S. system of state-based insurance regulation.

Mr. Schrader stated that in conducting the analysis, NAIC staff noted that many of the key elements of ComFrame have already been incorporated into the U.S. system through amendments to the holding company models, the establishment of ORSA requirements and other ongoing regulatory practices. NAIC staff also noted that some of the more prescriptive elements of ComFrame do not appear appropriate for the U.S. system and are not being recommended for consideration. However, NAIC staff identified certain other elements of ComFrame that do not appear to be fully addressed and should be considered for implementation.

Mr. Schrader asked Bruce Jenson (NAIC) to provide an overview of the results of the gap analysis performed, focusing on the key recommendations for consideration. Mr. Jenson stated that the key recommendations include proposed additions to the NAIC’s Financial Analysis Handbook and Financial Condition Examiners Handbook, as well as potential updates to the ORSA Guidance Manual for ComFrame elements. Mr. Jenson also recommended that the Working Group consider whether it is appropriate to require a Corporate Governance Annual Disclosure (CGAD) filing and/or ORSA Summary Report filing at the Head of the IAIG level to implement ComFrame elements. Finally, Mr. Jenson noted that ongoing projects of other NAIC groups will assist in implementing ComFrame elements in the areas of group capital, recovery and resolution planning, and liquidity stress testing.

Mr. Schrader stated that after the gap analysis was completed and a summary was provided to the Working Group, it was exposed for a public comment period that ended March 18. Five comment letters were received, and Mr. Schrader invited each commenter to summarize the key points from their letter during the meeting.

Tom Finnell (America’s Health Insurance Plans—AHIP) stated that while much of the ComFrame wording tends to encourage a centralized approach to IAIG monitoring and oversight, the introductory guidance and assessment methodology in the ICPs allow for additional flexibility in applying oversight to different types of insurance groups. Mr. Finnell stated that the gap analysis performed by NAIC staff appears to overlook some of these overarching concepts and overemphasizes review and
assessment of groupwide governance and control functions. Mr. Finnell also stated that the recommendation to require a groupwide ORSA Summary Report should keep in mind guidance in ICP 23 (Group-wide Supervision), which states certain entities or activities of the full group can be omitted from group supervision if there is no linkage that would cause risks to be transferred to the insurance operations. As such, Mr. Finnell encouraged regulators to engage in additional dialogue with the industry in assessing any ComFrame gaps and to put more consideration into the overarching principles allowing for flexibility in approaches.

Wayne Mehlman (American Council of Life Insurers—ACLI) stated that the industry would like to see more detail supporting the ComFrame gap analysis, including whether the proposed implementation efforts are intended to address the IAIS’ Holistic Framework considerations.

Mr. Bruggeman asked whether the proposed recommendations in the gap analysis are geared more towards meeting IAIS expectations than fitting with the U.S.’ existing system of state-based insurance regulation. Mr. Schrader stated that NAIC staff were asked to do a comprehensive gap analysis to identify any potential gaps and recommend potential enhancements to address those gaps. Mr. Schrader stated that it will be up to the Working Group to determine whether the potential enhancements are appropriate for incorporation into the existing system of state-based insurance regulation. Mr. Jenson provided an example of ComFrame language requiring a groupwide investment policy and oversight practices at the Head of the IAIG and noted that investment policies and practices outside of the insurance entities may not currently be within the scope of state analysis and examination functions. Mr. Finnell recommended that as regulators conduct their work in relation to various ICPs, they keep the overarching concepts in mind to determine whether reviewing all control functions from a groupwide perspective is necessary.

Stephen Broadie (American Property Casualty Insurance Association—APCIA) stated his support for additional discussion with the industry regarding the support for any gaps identified, as well as the importance of considering the overarching concepts in implementation activities. Throughout the ComFrame development process, interested parties expressed concerns to the IAIS regarding the language emphasizing a top-down approach to ComFrame, which may not be a good fit for the U.S. system given that groups are organized in so many different ways. As such, Mr. Broadie encouraged regulators to keep the overarching concepts and the existing U.S. system in mind in considering whether some of the more prescriptive elements of ComFrame should be implemented. For example, Mr. Broadie stated that the APCIA does not feel it is appropriate to require all IAIGs to file a CGAD and ORSA Summary Report at the Head of the IAIG level across the board. In addition, Mr. Broadie stated that interested parties would like to be involved in any detailed discussions around additions to NAIC handbooks to implement ComFrame elements.

Mr. Schrader stated his agreement with concerns that ComFrame takes too much of a top-down approach in certain areas and agreed that regulators should continue to keep the overarching concepts in mind in determining what is appropriate for the U.S. system. However, U.S. regulators will need to be able to demonstrate to their international counterparts how they determine that an adequate level of governance and risk management is in place across the entire IAIG. Ms. Belfi stated that regulators are going to need to be able to show their international counterparts how they get to the same result by using a different approach and that the handbook guidance should be drafted with that goal in mind.

Jonathan Rodgers (National Association of Mutual Insurance Companies—NAMIC) stated his association’s support for incorporating any necessary ComFrame enhancements into NAIC handbooks, as opposed to revising model laws or regulations. Mr. Rodgers also stated his support for keeping the overarching concepts of ComFrame in mind that would allow flexibility in implementation.

Bill Schwegler (Transamerica) asked regulators how they intend to incorporate the IAIS’ Holistic Framework and whether that will be done in tandem with ComFrame implementation given how the guidance is comingled in the ICPs. Mr. Schrader stated that implementation of the Holistic Framework is charged to the Financial Stability (EX) Task Force, but the Working Group will need to coordinate efforts given that the two projects are so closely linked.

Mr. Jenson stated that the ongoing Financial Sector Assessment Program (FSAP) that state insurance regulators are participating in includes some review of ComFrame implementation. While the results of the FSAP have not yet been publicly released, the report is expected to be released in the coming weeks and will include comments and recommendations regarding ComFrame implementation. As such, regulators and interested parties should consider and evaluate those recommendations once they become available.
Mr. Shrader thanked interested parties for their comments and expressed a commitment towards working together to develop targeted enhancements to the U.S. system of stat-based insurance regulation to incorporate ComFrame elements, where appropriate. Mr. Schrader outlined a plan to form two drafting groups to develop proposed enhancements to NAIC handbooks for the Working Group to consider. In addition, Mr. Schrader recommended that the ORSA Implementation (E) Subgroup take on the project to consider ComFrame elements related to ORSA and risk management, as well as whether the CGAD and ORSA Summary Report should be received from the Head of the IAIG. Ms. Belfi stated her support for assigning this project to the ORSA Implementation (E) Subgroup.

Ms. Doggett asked whether the handbook drafting work should be referred over to the Risk-Focused Surveillance (E) Working Group. Mr. Schrader stated his preference for forming separate drafting groups as opposed to referring the work to another group and asked NAIC staff for their recommendation. Mr. Jenson stated that forming drafting groups under the Working Group would allow for states that act as group-wide supervisors of IAIGs to be more involved in the project.

Ms. Berry asked whether guidance related to the determination of the Head of the IAIG is intended to be addressed by one of the drafting groups. Mr. Schrader stated that he expects the analysis drafting group to review ICP 23 and incorporate guidance into the handbook in that area.

Having no further business, the Group Solvency Issues (E) Working Group adjourned.
Interpretation of the Statutory Accounting Principles Working Group

INT 20-08: COVID-19 Premium Refunds, Limited-Time Exception, Rate Reductions and Policyholder Dividends

INT 20-08 Dates Discussed

Email Vote to Expose May 5, 2020; May 20, 2020; June 15, 2020, July 22, 2020

INT 20-08 References

SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets
SSAP No. 24—Discontinued Operations and Unusual or Infrequent Items
SSAP No. 53—Property Casualty Contracts—Premiums
SSAP No. 54R—Individual and Group Accident and Health Contracts
SSAP No. 65—Property and Casualty Contracts
SSAP No. 66—Retrospectively Rated Contracts

INT 20-08 Issue

COVID-19

1. A previously unknown virus began transmitting between October 2019 and March 2020, with the first deaths in the U.S. reported in early March 2020. The disease caused by the virus is known as Coronavirus Disease 2019 (COVID-19). Several states and cities have issued “stay home” orders and forced all non-essential businesses to temporarily close. This led to a significant increase in unemployment and the potential permanent closure of many businesses. Total economic damage is still being assessed however the total impact is likely to exceed $1 trillion in the U.S. alone.

Refunds, Rate Reductions and Policyholder Dividends

2. The federal, state or local government orders requiring non-essential workers to “stay home” caused a significant reduction in commercial and non-commercial activity, including automotive usage. Some consumer groups wrote letters and issued press releases calling for insurance premium refunds or pricing decreases, which included specific comments directed toward consumer automotive lines. The comments presumed that the decrease in activity would result in fewer losses.

3. Many insurers began issuing voluntary premium refunds, future rate reductions or policyholder dividends because of the decreased activity. The majority of the refunds were related to automotive lines of business however, some accident and health products also provided payments. Insurers have provided the reductions in a variety of ways. Some of the rate reductions were specific for in-force policies, whereas some of the rate reductions would apply to future policy renewals. Insurers provided unprecedentedly large payments to policyholders in an expedited fashion. These payments were viewed by regulators and insurers as being in the best interests of policyholders.

Voluntary

4. The majority of the refunds or rate reductions are being offered voluntarily and are not amounts required under the policy terms. The aggregate monetary amount of the return of funds is considered materially significant.
Jurisdiction Directed

5. In addition, a few jurisdictions have issued bulletins directing refunds and rate reductions on accident and health insurance and varying lines of property and casualty insurance, including but not limited to: private passenger automobile, commercial automobile, workers’ compensation, commercial multiple peril, commercial liability and medical professional liability. In addition, some jurisdictions have indicated support for refunds or rate reductions, but also directed that payment of such amounts require either premium rate filings or policy form amendments.

Accounting Issues

6. This intent of this interpretation is to address questions related to refunds, rate reductions and policyholder dividends in response to the decreased activity related to COVID-19. Because there are a variety of ways that reporting entities are accomplishing a similar objective of returning money or reducing premiums, this interpretation provides guidance on the following issues:

- Issue 1: How to account for refunds not required under the policy terms.
- Issue 2: How to account for refunds required under the policy terms.
- Issue 3: How to account for rate reductions on inforce and renewal business.
- Issue 4: How to account for policyholder dividends.
- Issue 5: Where to disclose refunds, rate reductions and policyholder dividends related to COVID-19 decreases in activity.

INT 20-08 Discussion

7. As an overall guiding principle, the accounting shall follow existing statutory accounting principles and annual statement reporting where feasible with more specific accounting applicable for the issues within this interpretation.

INT 20-08 Consensus

Issue 1: How to Account for Refunds Not Required Under the Policy Terms

7-8. The Working Group reached a consensus that voluntary refunds because of decreased activity related to COVID-19 and jurisdiction-directed refunds which are not required by the policy terms, are fundamentally a return of premium. Absent meeting the criteria for the limited-time exception to report as an aggregate write in for other underwriting expense as discussed in paragraphs 12-13, such refunds shall be accounted for as immediate adjustments to premium. The refunds shall be recognized as a reduction to written or earned premium and the unearned premium reserve adjusted accordingly.

8-9. Refunds shall be recognized as a liability when the definition of a liability in SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets is met. For example, the declaration of a voluntary dividend by the board of directors will trigger liability recognition. In cases where the refunds are directed by a jurisdiction, the SSAP No. 5R definition of a liability shall be used to determine timing of liability recognition.

9-10. Immediate adjustment to premium is consistent with the existing guidance in SSAP No. 53—Property Casualty Contracts—Premiums. SSAP No. 53 guidance requires adjustments to the premium charged for changes...
in the level of exposure to insurance risk. It is also consistent with the treatment of loss sensitive premium adjustments in SSAP No. 66—Retrospectively Rated Contracts. While some of the voluntary or jurisdiction-directed refunds may not be required by the explicit policy terms, the principle of reversing premium in the same way that the premium was originally recognized continues to apply.

11. Immediate adjustments to premium for voluntary accident and health premium refunds is also consistent with the guidance in SSAP No. 54R—Individual and Group Accident and Health Contracts on contracts subject to redetermination. While some of the voluntary or jurisdiction-directed refunds may not be required by the explicit policy terms, the principle of reversing premium in the same way that the premium was originally recognized continues to apply. The liability for voluntary health premium refunds attributable to COVID-19 and which are not required under the policy terms shall be recognized in aggregate write-ins for other liabilities.

**Limited-Time Exception – Expense Reporting**

12. Reporting the voluntary or jurisdiction-directed refund as an expense is not consistent with statutory accounting guidance. However, due to the variety of ways that COVID-19 premium reductions were approved by the various jurisdictions, this interpretation grants a limited-time exception to the existing reporting guidance to allow underwriting expense reporting. This limited-time exception applies to property and casualty lines of business in which the reporting entity filed policy endorsements or manual rate filings prior to June 15, 2020 which allow for discretionary payments to policyholders due to the COVID-19 related issues. In these cases, the reporting entities disclosed to the jurisdictions where the policies are written their intention to report their payments to policyholders as expenses. These property and casualty lines of business are permitted to report such policyholder payments as other underwriting expenses. This interpretation intends to be clear that manual rate filings and policy endorsements are not a source of authoritative accounting and this limited-time exception should not be used as an analogy for application to other such filings.

13. Application of this limited-time exception shall also be subject to the additional disclosures provided in Issue 5 below. Reporting the COVID-19 premium reductions as an expense as provided for in this limited-time exception, shall be disclosed as if it were a permitted practice. The reporting entity shall complete the permitted practices disclosures required by SSAP No. 1—Accounting Policies, Risks & Uncertainties, and Other Disclosures in annual statement Note 1 and any other disclosures pursuant to Issue 5 of this interpretation. This interpretation provides a limited-time exception for reporting premium refunds, and does not require domiciliary jurisdiction approval as a permitted practice if the requirements of this interpretation are met. However, disclosure in Note 1 in a manner consistent with permitted practices is required because of the impact on premium which is a key measurement metric for insurers. If a domestic jurisdiction disapproved reporting as an underwriting expense, the limited-time exception does not apply.

42. Reporting the voluntary or jurisdiction-directed refund as an expense is not consistent with statutory accounting guidance and would inappropriately present the expense ratios in the statutory accounting financial statements. Reporting the refund as an expense, or any other method besides a decrease to premium, would be considered a permitted or prescribed practice and shall be disclosed as required by SSAP No. 1—Accounting Policies, Risks & Uncertainties, and Other Disclosures:

a. Reporting the refunded amounts as a miscellaneous underwriting expense is not consistent with the underwriting expense description. This reporting option is inconsistent with the characterization of the amount as a return of premium.

b. Reporting the refunds as premium balances charged off (e.g., bad debt expense) is inconsistent with guidance in SSAP No. 53, paragraph 14, on earned but uncollected premium. It is also inconsistent
with the annual statement instructions as the amount is not an uncollectible amount, but rather a voluntary choice by the reporting entity to reduce the amount charged.

**Issue 2: How to Account for Refunds Required Under the Policy Terms**

43.14. While most of the premium refunds are voluntary or jurisdiction-directed and not required under the policy terms, some policies have terms that require an adjustment to premium based on either the level of exposure to insurance risk or the level of losses. If the policy terms change the amount charged, existing guidance in SSAP No. 53, SSAP No. 54R or SSAP No. 66 continues to apply:

a. SSAP No. 53 provides guidance for policies in which the premium amount is adjusted for changes in the level of exposure to insurance risk. This is often seen in commercial lines of business such as workers’ compensation. The guidance notes that audits often occur after the policy term or mid-term in the policy. SSAP No. 53 refers to the adjustment to premium (either due to the customer or to the insurer) as earned but unbilled (EBUB) premium. SSAP No. 53 requires such adjustment to premium to be made immediately either through written premium or earned premium. SSAP No. 53 also requires recognition of the related liabilities and expenses such as commissions and premium taxes based on when the premium is earned.

b. SSAP No. 54R provides guidance for policies subject to redetermination in which the premium is subject to adjustments by contract terms. This is commonly seen in federal and state groups. The guidance notes that estimates are based on experience to date and premium adjustments are estimated for the portion of the policy that has expired. Accrued return premiums are recorded as a liability with a corresponding entry to written premium. Refunds required under the policy terms would continue to be reported as retrospective or redetermination premium liabilities if applicable.

c. SSAP No. 66 provides guidance for policies whose terms or legal formulas determine premium based on losses. SSAP No. 66 references other applicable statements based on contract type for the initial accrual of premium. Estimates of premium adjustments are accrued based on activity to date and result in immediate adjustments to premium. SSAP No. 66 guidance specifies the corresponding annual statement reporting lines for different entity types.

**Issue 3: How to Account for Rate Reductions**

44.15. Some reporting entities are offering rate reductions instead of premium refunds. Some of these rate reductions provide one-time price decreases to future payments on in-force policies. Other reporting entities have provided offers of rate reductions on future renewals. Some of the offers for future rate reductions are only applicable to inforce policyholders as of a specified date. Some reporting entities have offered one-time rate reductions for future renewals for both existing and new policyholders for 2020.

a. Rate reductions on in-force business, shall be recognized as immediate adjustments to premium.

b. Rate reductions on future renewals shall be reflected in the premium rate charged on renewal. This is because it is outside of the policy boundary to require the accrual before contract inception. While the amount of future rate reduction can be estimated, it is not a change to existing policy terms and policyholders are not obligated to renew at the reduced rate, therefore, payment of the amount is avoidable. Such amounts shall be disclosed as discussed in Issue No. 5.
**Issue 4: How to Account for Policyholder Dividends**

45-16. _SSAP No. 65—Property and Casualty Contracts_, paragraph 46 requires that dividends to policyholders immediately become liabilities of the reporting entity when they are declared by the board of directors and shall be recorded as a liability.

46-17. The Working Group noted that policyholder dividends are typically only provided on participating policies or policies issued by non-stock companies, such as mutual entities and other corporate entity types in which profits are shared with policyholders.

47-18. Research during the development of this item identified that a small number of jurisdictions have legal restrictions which only allow policyholder dividends to be provided after the expiration of the policy period for which the dividend was earned. This interpretation only addresses policyholder dividends which are permitted by the applicable jurisdiction.

48-19. The property and casualty annual statement blank provides specific reporting lines for policyholder dividends including, but not limited to a liability line and a line in the income statement and statement of cash flow. For those entities whose policies are participating or whose corporate shell type and/or membership structure allow for policyholder dividends, the accounting for policyholder dividends is unchanged by this interpretation.

49-20. This interpretation does not change the policyholder dividend disclosure or reporting but provides additional guidance that such policyholder dividends issued in response to COVID-19 decreases in activity shall also be disclosed as discussed in Issue 5.

**Issue 5: Where to Disclose Refunds, Rate Reductions and Policyholder Dividends Related to COVID-19 Decreases in Activity**

20-21. There are various places in the notes to the statutory annual statement where disclosures of various aspects of premium refunds, premium reductions or policyholder dividends are required. This interpretation does not recommend changes to those existing disclosures. This interpretation does, however, recommend providing a consistent annual statement disclosure for all such amounts to allow for comparable disclosures.

21-22. _SSAP No. 24—Discontinued Operations and Unusual or Infrequent Items_ requires disclosure of the nature and financial effects of each unusual or infrequent event or transaction. Gains or losses of a similar nature that are not individually material shall be aggregated. This disclosure shall include the line items which have been affected by the event or transaction considered to be unusual and/or infrequent. This disclosure is currently required to be reported in annual statement Note 21A. (Reporting entities shall maintain jurisdiction-specific information to be made available upon request from department of insurance or revenue regulators.)

23. To allow for aggregate, consistent assessment, the Working Group came to a consensus that all COVID-19 inspired premium refunds, rate reductions, and policyholder dividends shall be disclosed as unusual or infrequent items in annual statement Note 21A. This disclosure is in addition to other existing disclosures on various items related to the policyholder payments.

a. For clarification, refunds required under policy terms in-force prior to the federal declaration of emergency for the COVID-19 pandemic as discussed in paragraph 13 (i.e., policies that require an adjustment to premium based on either the level of exposure to insurance risk or the level of losses) are not required to be aggregated in disclosures of COVID-19 inspired premium refunds, rate reductions and policyholder dividends.
b. Policies whose terms were modified after the declaration of emergency in response to COVID-19 are required to disclose the COVID-19 inspired premium refunds, rate reductions and policyholder dividends.

24. All reporting entities shall provide the following information regarding their COVID-19 premium refunds, limited-time exception payments, rate reductions and policyholder dividends as unusual or infrequent items:


   b. The amount of COVID-19 “payments” to policyholders by major category (premium refunds, limited-time exception payments, rate reductions or policyholder dividends).

25. Reporting entities that utilize the limited-time exception expense reporting described in paragraphs 12 and 13 shall additionally provide the following to illustrate in annual statement Note 1 the impact of reporting the payments as an aggregate underwriting expense rather than a return of premium as if it were a permitted practice. As detailed in paragraph 13 domiciliary jurisdiction approval as a permitted practice is not required to apply the limited-time exception. Disclosure is required because of the impact on premium which is a key measurement metric for insurers:

   a. A statement that the accounting practice is a limited-time exception to recognize such amounts as an aggregate underwriting expense rather than a return of premium. This disclosure shall include the financial statement reporting line(s) predominantly impacted by the limited-time exception. (Although most practices impact net income or surplus, direct reference to those lines should be avoided. The intent is to capture the financial statement line(s) reflecting the practice which ultimately impacts net income or statutory surplus.) Additionally, a reference to Note 1 shall be included in the individual notes to financial statements impacted by the limited-time exception as applicable.

   b. The monetary effect on revenue and expense.

   c. If a reporting entity’s risk-based capital would have triggered a regulatory event had it not used the limited-time exception, that fact should be disclosed.

   d. The reasons the reporting entity elected to use the limited-time exception rather than as a return of premium.

   e. Note 1 shall also identify the impact of not reporting such amounts as a return of premium on the operating percentages and other percentages reported in the Five Year Historical Data Exhibit and disclose the percentages/ratios as reported and as adjusted to report payments to policyholders as a return of premium.

   i. The operating ratios to be reported include:

      1. Premium earned,

      2. Losses incurred,

      3. Loss expenses incurred,

      4. Other underwriting expenses incurred, and
5. Net underwriting gain or loss.

   ii. The other ratios to be reported include:
       
       1. Other underwriting expenses to net premiums written,
       
       2. Losses and loss expenses incurred to premiums earned, and
       
       3. Net premiums written to policyholder’s surplus.

26. If a domiciliary jurisdiction’s prescribed or permitted practices allow voluntary COVID-19 payments which are either consistent with the limited-time exception or different from a reduction in premium, the reporting entity shall complete the disclosures in Note 1 which identify that a permitted or prescribed practice was applied and in paragraphs 24 and 25 of this Interpretation. The disclosure in paragraph 25 in such instances shall reflect the impact on the ratios in paragraph 25 compared to the default premium treatment.

**INT 20-08 Consensus**

22. The Working Group reached a consensus to prescribe statutory accounting guidance for insurance reporting entities providing refunds in response to COVID-19. Pursuant to this consensus:

   a. Reporting entities that provide voluntary or jurisdiction-directed refunds which are not required under the policy terms shall follow the guidance in paragraphs 8-12 of this interpretation. This guidance stipulates that such refunds shall be recognized as a reduction of premium. Refunds that are recognized in a different manner (e.g., as an expense), shall be considered a permitted or prescribed practice pursuant to SSAP No. 1.

   b. Reporting entities that provide refunds in accordance with insurance policy terms shall follow paragraph 13 of this interpretation. This guidance indicates that existing statutory accounting principles in SSAP No. 53, SSAP No. 54R or SSAP No. 66 shall be followed as applicable.

   c. Reporting entities that provide rate reductions shall follow paragraph 14 of this interpretation. This guidance provides direction based on whether the rate reduction is for in-force or future policies.

   d. Reporting entities that provide policyholder dividend shall follow the existing guidance for policyholder dividends which is summarized in paragraphs 15-19 and in addition, shall complete the disclosures described in paragraphs 20-22.

   e. This interpretation, paragraphs 20-22 indicates that reporting entities shall continue to comply with all statutory accounting disclosure requirements, but also requires that all premium refunds, rate reductions and/or policyholder dividends provided because of the decreased activity due to COVID-19 shall be aggregated and reported in Note 21A as unusual or infrequent items.

**Does Not Address Premium Taxation**

27. The Working Group noted that premium taxation requirements vary by jurisdiction and this interpretation is not intended to address premium taxation in any jurisdiction. Taxation is determined by the jurisdiction where the premium is written/returned to the policyholder according to the laws, regulations and general administrative rules applicable to all insurance enterprises licensed in a of that jurisdiction. This interpretation defers to each jurisdiction’s premium tax requirements for purposes of determining taxable amounts.
Effective Date

23-28. The limited-time exception allowance for expense reporting for endorsements and rate filings prior to June 15, 2020, applies only to these specific issues arising from COVID-19, is effective for second quarter reporting and will sunset January 1, 2021. This interpretation will be automatically nullified on January 1, 2021 and will be included as a nullified INT in Appendix H – Superseded SSAPs and Nullified Interpretations in the “as of March 2021” Accounting Practices and Procedures Manual.

INT 20-08 Status

24-29. This interpretation was amended on July 22, 2020 to include the limited-time exception and specific related disclosures by a two-thirds majority of the Accounting Practices and Procedures (E) Task Force membership. No further discussion is planned.

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