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Draft: 1/5/22

Financial Stability (E) Task Force
and the Macroprudential (E) Working Group
Tampa, Florida
December 13, 2022

The Financial Stability (E) Task Force met in Tampa, FL, Dec. 13, 2022, in joint session with the Macroprudential (E) Working Group. The following Task Force members participated: Marlene Caride, Chair (NJ); Elizabeth Kelleher Dwyer, Vice Chair (RI); Evan G. Daniels represented by David Lee (AZ); Ricardo Lara represented by Susan Bernard (CA); Andrew N. Mais represented by William Arfanis (CT); Karima M. Woods represented by Philip Barlow (DC); Trinidad Navarro represented by Tom Hudson (DE); David Altmaier represented by Virginia Christy (FL); Doug Ommen represented by Carrie Mears (IA); Amy L. Beard represented by Roy Eft (IN); Vicki Schmidt represented by Tish Becker (KS); Gary D. Anderson represented by John Turchi (MA); Kathleen A. Birrane represented by Lynn Beckner (MD); Timothy N. Schott (ME); Chlora Lindley-Myers represented by John Rehagen (MO); Eric Dunning represented by Justin Schrader (NE); Adrienne A. Harris represented by Bob Kasinow (NY); Judith L. French represented by Dale Bruggeman (OH); Michael Humphreys represented by Melissa Greiner (PA); Michael Wise represented by Ryan Basnett (SC); Carter Lawrence represented by Trey Hancock (TN); Cassie Brown represented by Jamie Walker (TX); Scott A. White (VA); and Nathan Houdek (WI). The following Working Group members participated: Justin Schrader, Chair (NE); Carrie Mears, Vice Chair (IA); Susan Bernard (CA); William Arfanis (CT); Philip Barlow (DC); Virginia Christy (FL); Lynn Beckner (MD); Timothy N. Schott (ME); Steve Mayhew (MI); Fred Andersen (MN); John Rehagen (MO); Marlene Caride (NJ); Bob Kasinow (NY); Melissa Greiner (PA); Elizabeth Kelleher Dwyer (RI); Jamie Walker (TX); and Scott A. White (VA).

1. Heard Opening Remarks

Commissioner Caride said materials for consideration and discussion for this meeting are available on the NAIC website in the Committees section under the Financial Condition (E) Committee.

2. Adopted the Task Force's Oct. 28 and Summer National Meeting Minutes

Eft made a motion, seconded by Superintendent Dwyer, to adopt the Task Force's Oct. 28 (Attachment One) and Aug. 12 (*see NAIC Proceedings – Summer 2022, Financial Stability (E) Task Force*) minutes. The motion passed unanimously.

3. Heard an Update on FSOC Developments

Superintendent Dwyer reported on a few Financial Stability Oversight Council (FSOC) discussions identified publicly most directly related to the NAIC's work:

- The FSOC continues to be focused on climate risk across a range of financial markets and products, including insurance.
- President Joe Biden's executive order on climate-related financial risks that was issued in May 2021 kicked off a flurry of activity at the FSOC. In October 2021, the FSOC published its report on climate-related financial risk and issued over 30 recommendations to U.S. financial regulators on how best to identify and address climate-related risks to the financial system.

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- The FSOC formed a new staff-level committee, called the Climate-Related Financial Risk Committee (CRFC), with representation from all 15 FSOC members consistent with the recommendations in the FSOC's climate report. The CFRC began meeting regularly in February and serves as an active forum for interagency information sharing, coordination, and capacity building. The NAIC is taking a leading role as one of the 15 members of the CFRC in assessing climate-related risks in the insurance sector and weighing in on any discussion or effort that might affect insurers or policyholders.
- The FSOC also established the Climate-Related Financial Risk Advisory Committee (CFRAC) on Oct. 3, which includes the financial services industry, non-governmental research institutions, climate-related data and analytics providers, non-profit organizations, and academia. The CFRAC's goal is to leverage members' climate data and analytical expertise to support its efforts to translate climate-related risk into economic and financial impacts. The CFRAC is in the process of security onboarding members, and it hopes to be up and running in early 2023.
- President Joe Biden's executive order on climate-related financial risk also directed the Office of Financial Research (OFR) to assist the FSOC and assess climate-related financial stability risk. As a result, the OFR is setting up a climate data and analytics hub in 2023 with climate data mostly from federal government agencies that will provide tools to access and analyze the datasets included. The OFR expects to roll out this data hub in Q1 2023, starting with the Federal Reserve, but the goal is to provide access to the rest of the FSOC members later next year.
- The FSOC released its report on Digital Asset Financial Stability Risks and Regulation on Oct. 3, which summarizes some of the risks posed by digital assets, as illustrated by the recent failure of the FTX cryptocurrency exchange, and it provides recommendations to address such risks. In particular, legislation should be developed related to state insurance regulators' authority to have visibility into, and otherwise supervise, the activities of all the affiliates and subsidiaries.
- The FSOC made it a priority to evaluate and address the risks to U.S. financial stability posed by three types of non-bank financial institutions next year: 1) hedge funds; 2) open-ended funds; and 3) money market funds.

Superintendent Dwyer stressed that despite representing the primary insurance regulators on the FSOC, the NAIC does not have a vote on any aspect of the FSOC's work, and issues relevant to the insurance sector have only increased in recent years. She concluded that due to that structural weakness, the NAIC supports legislation that would improve the FSOC by granting the primary insurance regulators a vote on FSOC proceedings.

4. Adopted the 2022 LST Framework

Schrader said the proposed 2022 Liquidity Stress Testing Framework (LST Framework) (Attachment Two) was released for a few days more than a 30-day public comment period on Oct. 28. He added that the exposed draft did not push for any substantive changes because 2022 is the first year of the revised *Insurance Holding Company System Regulatory Act* (#44) requirements incorporating the LST Framework, which will be effective in several states.

Schrader thanked the American Council of Life Insurers (ACLI) for its comment letter (Attachment Two-A), and he noted a couple of new deletions tracked in Section 7–Reporting to address corrections highlighted in the ACLI's comment letter to consistently reflect that the data templates will not be required to be completed and submitted for the company's own worst-case stress scenario results in the 2022 liquidity stress test (LST); and the assets template was updated with separate breakout lines for treasuries and agency bonds.

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Schrader said with respect to the ACLI's comments around suggested considerations in the 2022 LST Framework for the Interest Rate Spike scenario and regarding the inclusion of the non-insulated separate accounts, the lead state regulators will ultimately be responsible for guiding insurers on these matters. He added that the LST Study Group will hold meetings early next year to allow for views to be shared on the topics. He thanked interested parties for the offer to help in establishing more consistent market valuation assumptions for assets for the 2023 LST Framework, which will be taken up by the LST Study Group next year. Dave Leifer thanked NAIC staff. He asked if there were any further comments from interested parties, and hearing no comments, he asked for a motion from the Working Group to adopt the 2022 LST Framework.
Mayhew made a motion, seconded by Andersen, to adopt the 2022 LST Framework (Attachment Two). The motion passed unanimously by the Working Group.

Schrader made a motion, seconded by Mears, to adopt the 2022 LST Framework (Attachment Two). The motion passed unanimously by the Task Force.

5. Received a Working Group Update

Schrader said the primary macroprudential objective of the LST Framework is to assess the potential impact of asset sales that the life insurance sector would generate in various scenarios and provide supervisors with insights on individual insurers.

Schrader summarized the aggregated 2021 LST submissions and key findings (Attachment Three):

- Reviewed the narratives and quantitative results of 22 submissions by life insurance groups.
- Provided a detailed summary for regulators only and the public.
- Asset sales are reported by asset type, the aggregate for which is compared to average daily trading volumes and issues outstanding.
- Largest asset sales emanated from investment-grade corporate bonds, U.S. Treasury bonds, and Agency bonds.
- A comparison to market data showed that there would be no material impact on the markets from insurers' potential sales of the above reference asset classes.

Schrader added that lead state insurance regulators may follow up with their insurers regarding the economic variables assumed in the 2021 LST Interest Rate Spike stress scenario to address the concern to assess how the actual interest rate increases this year played out compared to the interest rate increase assumptions used.

Schrader said for work being performed by other NAIC committee groups on the 13 considerations with respect to private equity (PE) ownership of insurance, interested parties should sign up for those groups to follow the work in detail.

Schrader summarized the status of the 13 Working Group considerations with respect to PE ownership of insurance (Attachment Four):

- The Statutory Accounting Principles (E) Working Group and the Life Actuarial (A) Task Force have already completed some work items affecting these considerations, but more work is still ongoing.
- The Macroprudential (E) Working Group has been focused on offshore reinsurance transactions, which is the thirteenth consideration. The Working Group held several confidential meetings with both insurance

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groups, as well as jurisdictions, and it will wrap up those meetings next year. The Working Group's concerns have centered on developing a template to allow state insurance regulators to easily identify and understand the true economic impacts of the reinsurance transaction.

- Next year, the Working Group will address consideration number 5 related to operational, governance, and market conduct practices and hopefully conclude outreach efforts for considerations 12.b and 12.c related to pension risk transfer business supported by complex investments.

Schrader said the NAIC hoped to publish and release the full Macroprudential Risk Assessment report, but NAIC staff are still finalizing the contents, and he asked Miguel Romero (NAIC) to provide an update.

Romero summarized the status of the Macroprudential Risk Assessment report and provided an overview of the attached excerpts (Attachment Five):

- Overall Risk Dashboard: Provides an overarching view of the risks, then with more granular risk assessment and trends included in the full report.
- Draft Executive Summary: Includes discussion of key topics discussed in the report including investment trends, changes in ownership, increasing catastrophe risk losses, macroeconomic trends such as inflation and interest rates, as well as cyber security and insurance.
- Recommendations: The report includes recommendations that state insurance regulators and NAIC staff continue studying specific topics listed in the executive summary seeking industry input after the publication of the report on data sources.

After hearing no concerns, Schrader asked NAIC staff to move forward with the recommendations and bring matters back to the Working Group as the study progresses, and he requested that volunteers for the study contact Romero.

6. Heard an International Update

Tim Nauheimer (NAIC) reported that the International Association of Insurance Supervisors (IAIS) has completed the annual Global Monitoring Exercise (GME) for 2022, which includes analysis of data received from individual insurer monitoring (IIM) and sector-wide monitoring (SWM) exercises.

Nauheimer summarized the GME:

- The IIM and SWM data collections helped inform the scope of the annual collective discussions, which took place in September.
- The annual collective discussions formed the basis for topics in the annual Global Insurance Market Report (GIMAR).
- The Macroprudential Supervision Working Group (MSWG) met at the NAIC office in New York City, NY, in October to finalize the drafting of two chapters of the GIMAR that originated from the SWM process: PE ownership in insurance as well as changing interest rates and inflation.
- The Climate Risk Steering Group (CRSG) addressed the climate risk theme and drafted one chapter on climate change for the GIMAR.
- The IAIS will publish a GIMAR special topic on cyber next year.
- The IAIS has launched a public consultation on the review of the IIM Assessment Methodology, with interested parties encouraged to submit comments by Feb. 6 and for which the NAIC will follow its

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established practice of approving and submitting any comments through the International Insurance Relations (G) Committee. The IIM Assessment Methodology will continue to identify select firms for the collective discussion by the IAIS based on established quantitative threshold criteria.

- The next cycle of the GME may include additional data on credit risk, PE, and interest rate risk, but it may also include deletions to strike a balance for insurers and supervisors, which will hopefully result in no additional rows added to the data collections.
- The IAIS published a report, "Liquidity Metrics as an Ancillary Indicator," for the GME in November, which will serve as a tool for the IAIS to monitor the global insurance sector's liquidity risk and assess insurers' liquidity exposure from a macroprudential perspective. The liquidity metrics were developed as part of a multi-year project, which has benefited from two public consultations and intensive testing of IIM data.

Nauheimer also reported that the Financial Stability Board (FSB) announced its decision to discontinue the annual identification of global systemically important insurers (G-SIIs), formally endorsing the IAIS Holistic Framework for the assessment and mitigation of systemic risk in the global insurance sector (Holistic Framework). He said the FSB decision was informed by work undertaken by the IAIS over the past three years to assess the implementation of the Holistic Framework. He added that the FSB decision represents a significant milestone for the IAIS because it acknowledges that the Holistic Framework is more effective in assessing and mitigating systemic risk in the insurance sector than the G-SII Framework. He concluded that the FSB decision was also a recognition of the work performed by state insurance departments, NAIC staff, and Team USA, which includes the Federal Insurance Office (FIO) and the Federal Reserve.

7. Discussed Other Matters

Commissioner Caride announced that Schrader is leaving the Nebraska Department of Insurance (DOI) by the end of the year, and she thanked him for his many years of service.

Having no further business, the Financial Stability (E) Task Force and Macroprudential (E) Working Group adjourned.

SharePoint/NAIC Support Staff Hub/Member Meetings/2022 Fall National Meeting/

Plan for the List of MWG Considerations – PE Related and Other

Some of these Working Group projects will continue for several years. The status of the 13 MWG Considerations is as follows as of ***March 22, 2023***:

1. Holding Company Structures:

   Sent a referral for new work to the Group Solvency Issues (E) Working Group.

   GSIWG Update: *The GSIWG plans to discuss this issue at its Dec. 14 meeting to determine next steps in addressing the referral.*

2. Ownership and Control:

   Sent a referral for new work to the Group Solvency Issues (E) Working Group.

   GSIWG Update: *The GSIWG plans to discuss this issue at its Dec. 14 meeting to determine next steps in addressing the referral.*

3. Investment Management Agreements (IMAs):

   Sent a referral to the Risk-Focused Surveillance (E) Working Group to add this consideration to existing work involving affiliated agreements and Form D filings. Also sent a referral to the Valuation of Securities (E) Task Force (VOSTF) to highlight the regulatory discussion involving topics it administers.

   RFSWG Update: *The RFSWG received and discussed this referral during its Nov. 1 interim meeting. During the meeting, the RFSWG agreed to defer further work on this issue until its ongoing project to update general guidance in NAIC handbooks related to affiliated service agreements is completed in early 2023.*

4. Owners of Insurers with Short-Term Focus and/or Unwilling to Support a Troubled Insurer:

   Sent a referral to the Risk-Focused Surveillance (E) Working Group to add this consideration to existing work involving affiliated agreements and fees. Also sent a referral to the Life Actuarial (A) Task Force recognizing its existing work to ensure the long-term life liabilities (reserves) and future fees to be paid out of the insurer are supported by appropriately modeled assets.

RFSWG Update: *The RFSWG received and discussed this referral during its Nov. 1 interim meeting. During the meeting, the RFSWG agreed to defer further work on this issue until its ongoing project to update general guidance in NAIC handbooks related to affiliated service agreements is completed in early 2023.*

LATF Update: *Asset adequacy analysis requirements in NAIC Model #820 and VM-30 require that company Appointed Actuaries perform testing to ensure that the reserves held for the company's liabilities are adequate in light of the assets supporting the business. Regulators review associated company Statements of Actuarial Opinion periodically*.

5. Operational, Governance and Market Conduct Practices:
The MWG will keep developing more specific suggestions before likely referring this consideration to the Risk-Focused Surveillance (E) Working Group.

MWG Update: *No new action has occurred for this consideration as the regulators have focused on the reinsurance consideration*.

6. Definition of Private Equity (PE):
No action was deemed necessary for this consideration.

No update.

7. Identifying Related Party-Originated Investments (Including Structured Securities):
Sent a referral to the Statutory Accounting Principles (E) Working (SAPWG) Group recognizing its existing work regarding disclosures for related-party issuance/acquisition. Once MWG regulators work with these SAPWG disclosures and regulatory enhancements from referrals to other groups, further regulatory guidance may be considered as needed.

SAPWG Completed Actions:

- *Ref #2021-21 included revisions that clarified guidance for related parties and developed a blanks proposal which provided new investment schedule column with reporting codes to identify investments that involve related parties. (Adopted May 2022)*

- *Ref #2021-22BWG added six related party reporting codes effective for year-end 2022. The investment schedule disclosures include codes that identify the role of the related party in the investment, e.g., a code to identify direct credit exposure as well as codes for relationships in securitizations or similar investments. (Adopted May 2022)*

8. Identifying Underlying Affiliated/Related Party Investments and/or Collateral in Structured Securities:

Sent a referral to the Statutory Accounting Principles (E) Working Group in recognition of existing work to develop disclosures to identify the role of the related party in the investment and codes for relationships in securitizations or similar investment. Also sent a referral for new work to the Examination Oversight (E) Task Force for the CLO/structured security considerations.

SAPWG Completed Actions:

- *See above descriptions (Ref # 2021-21 and Ref #2021-22 BWG) on investment reporting codes for year end 2022 reporting.*

- *Ref #2019-34 included revisions that clarify: 1) identification of related parties; 2) a non-controlling ownership over 10% results in a related party classification regardless of any disclaimer of control or affiliation; 3) a disclaimer of control or affiliation does not eliminate the classification as a "related party" and the disclosure of material transactions. This agenda item also resulted in the creation of a new Schedule Y Part 3, which was effective for year-end 2021. This schedule identifies all entities with greater than 10% ownership – regardless of any disclaimer of affiliation - and whether there is a disclaimer of control/disclaimer of affiliation and identifies the ultimate controlling party. (Ref #2019-34 and Ref #2020-37BWG, both adopted March 2021)*

EOTF Update: *The EOTF delegated work on this referral to its Financial Analysis Solvency Tools (E) Working Group and its Financial Examiners Handbook (E) Technical Group. Both groups developed new guidance for inclusion in 2023 NAIC handbooks related to the new related party investment disclosures developed by SAPWG and the AG 53 standards developed by LATF that will be in place for 12/31/22 reporting. The groups may develop additional guidance for NAIC handbooks, as well as supporting regulatory reports and tools, as work proceeds in this area.*

9. Asset Manager Affiliates and Disclaimers of Affiliation:

MWG regulators are comfortable waiting to realize the benefits of the recently implemented Schedule Y, Part 3, along with the changes other NAIC committee groups will make for several of the previously listed referrals, before determining if additional work is needed. Also, a referral was sent to the Statutory Accounting Principles (E) Working Group recognizing its existing work to

revamp Schedule D reporting along with the previously mentioned code disclosures will assist with this consideration.

SAPWG Completed Actions:

- *See above descriptions of Schedule Y Part 3. (Ref #2019-34 and Ref #2020-37BWG).*

SAPWG Ongoing Work:

- *Ref #2022-15, which clarifies affiliated investment reporting, is planned for adoption consideration at the Spring National Meeting . It adds guidance on reporting of affiliated investments.*

- *As part of a project known as the bond project, the SAPWG is developing a proposal to revise Schedule D reporting, which intends to determine what is considered a qualifying bond and to identify different types of investments more clearly. For example, the current bond proposal would divide Schedule D-1 into a Schedule D-1-1 for issuer credit obligations and a Schedule D-1-2 for asset-backed securities. The proposal includes more detailed reporting lines to provide more granularity on the actual types of investments held. The effective date of the bond proposal, and the reporting changes, is anticipated for January 1, 2025. Reporting changes to reflect the Schedule D-1 proposed changes were exposed by the Blanks (E) Working Group on March 7, 2023. Updated revisions to the statutory accounting guidance are planned for exposure by the Statutory Accounting Principles (E) Working Group at the 2023 Spring National Meeting.*

- *Ref #2022-17, which clarifies interest income disclosures, is planned for adoption consideration at the Spring National Meeting.*

10. Privately Structured Securities:

Sent a referral to the Life Actuarial (A) Task Force recognizing its existing work on an Actuarial Guideline including disclosure requirements for the risks of privately structured securities and how the insurer is modeling the risks. Sent a referral to the VOSTF highlighting the MWG regulators' support for the blanks proposal to add market data fields for private securities being considered by the Valuation of Securities (E) Task Force (VOSTF). MWG regulators will wait on any further work or referrals until they have an opportunity to work with the results of the VOSTF proposal and the SAPWG Schedule D revamp project. Sent a referral for new work to the RBC

Investment Risk and Evaluation (E) Working Group to address the tail risk concerns not captured by reserves.

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LATF Update: *Actuarial Guideline 53 (AG 53) has been adopted by the NAIC's Executive (EX) Committee and Plenary and was effective for year-end 2022 reporting. Starting in Spring 2023, regulators on the Valuation Analysis (E) Working Group will be conducting AG 53 reviews. This will involve a targeted review of asset adequacy analysis related to modeling of business supported with projected high net yield assets.*

VOSTF Update: The VOSTF sent referrals to the Financial Condition (E) Committee, Financial Stability (E) Task Force, Macroprudential (E) Working Group, Capital Adequacy (E) Task Force, Risk-Based Capital Investment Risk and Evaluation (E) Working Group, Life Actuarial (A) Task Force, Financial Analysis (E) Working Group, Statutory Accounting Principles (E) Working Group and Valuation Analysis (E) Working Group requesting feedback on a proposal to have the NAIC's SVO develop the analytical capability to produce risk metrics for bond investments, and model measures of interest rate sensitivity and project investment cash flows and estimated losses for any given interest rate or economic scenario for regulator use. These groups were asked if they support the proposal and to describe different ways they envision being able to take advantage of such a capability within the NAIC.

SAPWG Ongoing Work:

- *As discussed above, the Schedule D bond proposal is planned for 2025 reporting.*

RBCIREWG Update: *The Risk-Based Capital Investment Risk and Evaluation (E) Working Group added this item to its working agenda. While not specifically addressing privately structured securities, the Working Group's current work on collateralized loan obligations may contribute to addressing this item.*

11. Reliance on Rating Agencies:

Sent a referral to the VOSTF indicating the MWG regulators' agreement to monitor the work of its ad hoc group addressing various rating agency considerations.

VOSTF Update:

- The Task Force adopted an amendment at it Feb. 21 meeting that effective Jan. 1, 2024, financially modeled collateralized loan obligations (CLO) will not be eligible to use credit rating provider ratings to determine an NAIC Designation.
- The Task Force has drafted a list of questions to discuss with each rating agency in future regulatory-only meetings. The questions are in the materials for the Spring National Meeting and will likely being exposed for public comment.
- The Securities Valuation Office (SVO) has proposed an amendment to remove Structured Equity and Funds transactions from being eligible to use credit rating provider (CRP) ratings to assign an NAIC Designation. The SVO has proposed defining Structured Equity and Funds investments as investments which, through the insertion of an intervening entity such as a special purpose vehicle (SPV) or limited partnership, enable underlying assets that may not qualify as 'bonds' or be eligible to receive an NAIC Designation under the current regulatory guidance, to be reported as 'bonds' because the intervening entity issues notes and those notes receive a credit rating provider rating. The SVO identified multiple regulatory reporting arbitrage opportunities with these investments that circumvent regulatory guidance using a CRP rating to accomplish that result.
- The Task Force adopted a new charge for 2023 to stablish criteria to permit staff's discretion over the assignment of NAIC designations for securities subject to the FE process (the use of CRP ratings to determine an NAIC designation) to ensure greater consistency, uniformity, and appropriateness to achieve the NAIC's financial solvency objectives. The criteria have not yet been proposed.

12. Pension Risk Transfer (PRT) Business Supported by Complex Investments.

a. LATF's Actuarial Guideline:

Sent a referral to the LATF recognizing its work on an Actuarial Guideline which should address the reserve considerations of pension risk transfer (PRT) business. Sent a referral to the SAPWG to address the related disclosure considerations as the goal was to have them in the Notes to Financial Statements.

LATF Update: *The PRT Drafting Group of the VM-22 SG is considering the development of PRT/longevity risk mortality factors. The DG hopes to share data with the Longevity Risk*

Subgroup of LATF that the Subgroup could consider for C-2 RBC for PRT products and longevity risk transactions.

SAPWG Completed Actions:

- *Ref #2020-37: Separate Account – Product Identifiers and Ref #2020-38: Pension Risk Transfer - Separate Account Disclosure, which did not result in statutory accounting revisions but instead resulted in modifications to the reporting of PRT transactions in the annual financial statements, was adopted by the SAPWG May 2021. Ref #2021-03BWG was adopted by Blanks (E) Working Group in 2021.*

  ***Comment** – The 2022 review of the initial 2021 disclosures noted that although the instructions were clarified to require by product reporting including the use of a distinct disaggregated product identifier for each product represented; most entities are still broadly grouping PRT activity in the disclosures. Review of 2022 data is planned to be completed in the first half of 2023.*

b. Department of Labor Protections:

MWG Update: *NAIC staff are continuing to hold discussions with Department of Labor representatives.*

c. State Guaranty Funds Compared to PBGC Protection – NOLHGA 2016 Study:

No further action was deemed necessary.

MWG Update: *However, NAIC staff have contacted PBGC representatives to inquire if they have any items they wish to address with the MWG.*

d. RBC Treatment of PRT Business:

Sent a referral to the Longevity Risk (E/A) Subgroup recognizing its work will also address PRT business and indicating the MWG regulators will monitor this work.

LATF Update: *The Longevity Risk (E/A) Subgroup will review the currently exposed VM-22 PBR methodology once it is finalized and adopted. The Subgroup will consider whether to develop and recommend longevity risk factor(s) for the product(s) that were excluded from the application of the current longevity risk factors.*

13. Offshore/Complex Reinsurance:

MWG Update: *MWG regulators are wrapping up the confidential discussions with industry participants and other jurisdictions regarding the use of offshore reinsurers and complex affiliated reinsurance vehicles. They are continuing discussions to identify the best mechanism to ensure reviewing/approving regulators can identify the true economic impacts of the reinsurance transaction. MWG regulators will consider further work and/or referrals once they have concluded these discussions.*

1. **The worksheet is an option for regulators to require.** The regulator will inform the insurer if it is needed and provide the insurer the version of the worksheet to be completed.

2. **As such, the initial Worksheet's categories are listed generically to allow for variations.** For example, regulators may wish to use more than 3 Asset Categories to get more detailed data for specific risk characteristics, liquidity characteristics, etc. Similarly, different/more granular liability categories may wish to be used (e.g., one for annuities and another for life insurance). For the capital categories, if there is no rating agency involved, then the categories would be reduced to one line for "required capital" and another line for "additional capital." Similarly, the worksheet includes an "Other Jurisdiction" column as well as an "Alternate Method" column to allow for jurisdictions with optionality (e.g., Bermuda); if the jurisdiction has no optionality, only the single column is needed.

3. **When should regulators use this worksheet?** It is probably most valuable to new treaties when regulators are considering approvals, but it could be helpful for treaties already in place where there are significant and material questions/concerns. The worksheet is meant to be a tool to help the regulator understand the impacts of the reinsurance transaction; so if the regulator fully understands these impacts, a completed worksheet would not be necessary.

4. **For which product types?** Again, the worksheet is generic and can be used for whichever product(s) for which the regulator needs clarity. The "Total Asset Requirement" is more explicit/understood for annuities through C-3 Phases 1 and 2, so the concept might need to be clarified for life insurance.

5. **This worksheet should be completed at the individual block of business level.**

6. **Cross-border or U.S. to U.S. as well?** The worksheet was designed for cross-border reinsurance treaties where there are regulatory differences involved. However, if a regulator would find this information useful for a U.S. to U.S. transaction, there is no reason for the regulator to not pursue its completion.

7. **Who should provide the responses in this worksheet?** It is expected the insurer will complete the worksheet initially. However, in situations where a consultant is engaged and/or there are concerns with information being provided by the insurer, it may be appropriate for the consultant to generate the completed worksheet.

DRAFT: Cross-border Affiliated Reinsurance Comparison Worksheet - by Treaty

Category	US Stat. Pre-Transaction	Impacts of Transaction (Col's B-D)	US Stat. Post-Transaction		Other Jurisdiction	(Alternate Method) - Other Jurisdiction
BALANCE SHEET COMPARISON:						
Asset Grouping 1 (e.g., Cash/Investments)						
Asset Grouping 2 (e.g., Policy Loans)						
Asset Grouping3 (e.g., Separate Accounts)						
Other Assets						
TOTAL ASSETS *						
Liab. Grouping1 (e.g., Gen. Acct. Reserves)						
Liab. Grouping2 (e.g., Gen. Acct. Policy Loan Reserves)						
Liab. Grouping3 (e.g., Separate Accounts)						
Unauthorized Reinsurance Liability						
Other Liabilities (*See NOTES SECTION*)						
TOTAL LIABILITIES						
TOTAL ASSET REQUIREMENT COMPARTISON:						
Reserve Grouping1 (e.g., Separate Account Reserves)						
Reserve Grouping2 (e.g., GA Policy Loan Reserves)						
Reserve Grouping3 (e.g., GA Policy Reserves)						
TOTAL RESERVES						
Capital Grouping1 (e.g., Required Capital)						
Capital Grouping2 (e.g., Add'l Capital for Rating Agency)						
Capital Grouping3 (e.g., in Excess of Rating Agency Cap.)						
TOTAL CAPITAL						
TOTAL ASSET REQUIREMENT						
CHANGE IN CAPITAL AND SURPLUS:						
Capital and Surplus						
Net Income						
Change in Liability for Unauthorized Reinsurance						
Aggregate Write Ins for gains and losses in surplus						
Capital Contribution/(Dividends)						
Other Changes in surplus						
TOTAL LIABILITIES & CAPITAL						
SOLVENCY RATIO						
* Supported by listings of asset categories and amounts to highlight differences in supporting assets after the transaction.						
NOTES SECTION:						
(e.g., explain product line, describe transaction and any unique aspects)						
(If Asset Adequacy Testing is included in "Other Liabilities," additional regulatory guidance may be needed, e.g., on counterparty asset assumptions where access is limited.)						

Transaction Details

Please identify the following transaction details if applicable:	Contract 1 (if needed)	Contract 2 (if needed)	Contract 3 (if needed)	Contract 4 (if needed)
Which party of the contract are you (assuming or (retro)ceding)?				
Description risk category covered (mortality, longevity, Cat Risk, etc.)				
Start date				
End date				
Currency				
Sum Insured / Gross Notional amount / PML				
Capital at risk				
Line of Business (e.g. annuities, term, participating guarantee, etc.)				
Risks covered (e.g. longevity, mortality, etc.)				
Type of reinsurance treaty (XoL, Quota share – proportionate, etc.)				
Collateral value				
Value of guarantee				
Name(s) of the reinsurer(s) (please only include top 3 by premium share if more than one)				
Rating of reinsurer(s)				
Countries of reinsurer(s)				
Assets pledged by reinsurer				
Initial premium				
Initial fees				
Value of reserves				
Ceding commission structure		If yes, provide description of these derivatives		
Any experience refund or loss carryforward features		If yes, provide description of these derivatives		
Do you use or plan to use any form of derivatives for reinsurance purposes (e.g. longevity or mortality swaps)?		If yes, provide description of these derivatives		

Please identify and describe if any of the following types of arrangements are associated with this transaction:	**Description**
Trust	
Funds Withheld	
Coinsurance	
Modified Coinsurance	
Sidecars	
Any other Joint Venture or SPV	
Third-party capital	

Exit mechanism

Ceded and Retroceded Details	**Reinsurer Name**	**Jurisdiction**
If ceding to an offshore affiliate please identify the assuming affiliated reinsurer(s) and their regulatory jurisdiction		
If ceding to an offshore affiliate and that affiliate is going to retrocede to another reinsurer, please identify the ultimate assuming reinsurer(s) and their regulatory jurisdiction		

Please list the asset types and amounts backing the ceded business and indicate with a * (or some other symbol) if they do not meet the statutory accounting definition of admitted assets

Asset Listing		
Description	**Book Value**	**Market Value**

To: Commissioner Marlene Caride, Chair of the Financial Stability (E) Task Force
From: Fred Andersen, Chair of the Valuation Analysis (E) Working Group
Date: December 12, 2022
Re: Response to Request from the Financial Stability (E) Task Force

I. Executive Summary

In 2019, the Financial Stability (E) Task Force (FSTF) made a request to the Valuation Analysis (E) Working Group (VAWG) to assess a potential concern related to Economic Scenario Generators (ESGs) developed by the American Academy of Actuaries (Academy). It was suggested that there is a deficiency in the current ESG in that it doesn't adequately consider a very low or negative interest rate environment, and more specifically that this raises a material risk at the macro prudential level in the U.S., particularly for variable annuities. To allay any concerns during the interim period until a new ESG is in place, the FSTF asked the VAWG to assess this concern and provide assurance that any issues either have been addressed, or will be able to be addressed.

VAWG previously responded to the FSTF in 2019 and 2021 and has continued to assess the materiality of variable annuity interest rate risk and the approaches companies have taken to measure and manage it. The current report involves a request to 24 companies to perform a stress test for disclosure as of year-end 2021 (2021 VA Stress Test). The purpose of the 2021 VA Stress Test was to assess, at an industry level, the impact of a continuation of persistently low interest rates on VA reserves and risk-based capital (RBC). This report provides details and key findings from the 2021 VA Stress Test as well as an update on the development of the new ESG.

For the 2021 VA Stress Test, companies were asked to repeat the calculations for reserves and RBC as of 12/31/2021, after replacing the economic scenarios used for year-end reporting with a modified set of scenarios. The modified set included many interest rate scenarios that sustained low rates for much of the projection period.

Results from the 2021 VA Stress Test were compared against the baseline of actual 12/31/21 reported reserves and RBC. For the 24 companies combined:

- Pre-reinsurance ceded guaranteed benefit reserves increased $1.8 billion (6%) from $30.0 billion to $31.8 billion
- RBC increased $1.5 billion (24%) from $6.4 billion to $7.9 billion

The VAWG has found that, to address the risk of prolonged low interest rates, many companies took actions in 2021 as well as in one or more prior years. Many companies are also considering potential future actions for the near term. These are similar to past actions, such as performing testing and additional analysis, implementing product changes, or adjusting hedging.

The implementation of a new ESG is in progress. The results of an industry field test are currently under review. A recalibration of the ESG is expected, followed by a second field test. Ultimately, *Valuation Manual* amendments and RBC instruction changes will be necessary to incorporate prescription of the new ESG, which is now anticipated to be no sooner than 1/1/25.

Additional VA stress tests will be considered as needed prior to adoption of the new ESG. However, the ESG field tests enable VAWG to monitor the impacts of negative and prolonged low interest rates. Thirty-one VA writers participated in the ESG field test, representing a high percentage of the industry. Participants include most of the 24 companies that performed the 2021 VA stress test.

II. 2021 VA Stress Test

A. Background

Twenty-four VA writers, representing a majority of U.S. VA business inforce, were contacted in February 2022 and asked to perform a stress test for disclosure by 4/30/2022 and to respond to a series of related questions. The purpose of the test was for VAWG to assess, at an industry level, the impact of a continuation of persistently low interest rates on VA reserves and RBC.

B. Instructions

Companies were asked to perform the 2021 VA Stress Test according to the following instructions:

> After calculating 12/31/21 variable annuity reserves and capital as normal, repeat the calculations, replacing the economic scenarios with a modified set of scenarios which will be emailed to you [separately]. These scenarios were developed by modifying the Academy ESG to better reflect the risk of low for long scenarios. This was done by changing the mean reversion parameter (MRP) in the Academy ESG to 1.5% and lowering the soft floor on long-term rates from 1.15% to 0.01%. Additionally, the Academy's Scenario Picking Tool was used to select a representative subset of 1,000 scenarios, and this subset should be used for the Stress Test (whether or not the company used 1,000 scenarios for 12/31/21 annual statement reporting). If the company used scenarios as of a date prior to 12/31/21 for annual statement reporting, the company should use the Stress Test scenarios as of that date.
>
> For the Stress Test, all components of the modeling other than the ESG-generated economic scenarios and scenario selection should remain the same (e.g., the same investment strategy, CDHS modeling, etc. should be used for the stress test).

C. Summary of Results

Results for the 2021 VA Stress Test were calculated in comparison to a baseline of actual 12/31/21 reported reserves and RBC. Shown below, for the 24 companies combined, is the increase in total reserves for guaranteed benefits (which excludes the cash surrender value) plus RBC over the baseline.

	Baseline	Increase over Baseline	% Increase over Baseline
Pre-Reinsurance Ceded Reserve for Guaranteed Benefits	$30.0 B	$1.8 B	6%
Risk-Based Capital	$6.4 B	$1.5 B	24%
Total	$36.4 B	$3.3 B	9%

At the company level, changes to the pre-reinsurance ceded reserve for guaranteed benefits ranged from approximately a 75% decrease to a 500% increase. Changes to RBC ranged from approximately a 100% decrease to a 250% increase. Additional details about the distribution of results are shown below.

	Approximate % of Companies that showed:		
	More than a 20% increase over baseline	An increase over baseline of 0% to 20%	A decrease from the baseline
Pre-Reinsurance Ceded Reserve for Guaranteed Benefits	35%	25%	40%
Risk-Based Capital	20%	35%	45%

Companies explained their stress test results. Many noted offsetting effects of different calculation elements. The scenarios used for the 2021 VA Stress Test (Stress Test Scenarios) and the scenarios used for the baseline (Baseline Scenarios) were often compared to provide additional insight. The following general observations were made:

- For most companies, the interest rates in the Stress Test Scenarios were generally lower than those in the Baseline Scenarios, and had the effect of raising reserves and RBC.
- In contrast, the equity returns in the Stress Test Scenarios were generally more favorable than those in the Baseline Scenarios, which improved results significantly for many companies. The favorable equity scenarios reflect a limitation of the methodology currently used to select scenario subsets (out of a total of 10,000 scenarios). A 1,000 scenario subset was selected for the stress test since this is what VA writers typically use to calculate reserves and RBC. The current scenario selection process relies on the 20-year UST and therefore may not be effective at selecting subsets for products sensitive to equity performance (i.e., they may not be representative of the full set of 10,000 equity scenarios produced by the ESG). A newly formed VM-20/VM-21 ESG Drafting Group will be reviewing the existing methodology used to select scenario subsets.
- Hedging generally improved results. Some companies noted an increase in hedging gains or a decrease in hedging losses due to lower or less volatile interest rates in the Stress Test Scenarios.
- Some of the companies used a proprietary ESG for their baseline results. A subset of these companies noted that the Stress Test Scenarios were less conservative than their Baseline Scenarios.
- Some companies noted that the stress test resulted in more scenario reserves exceeding the cash surrender value floor.

D. Summary of Responses to Questions

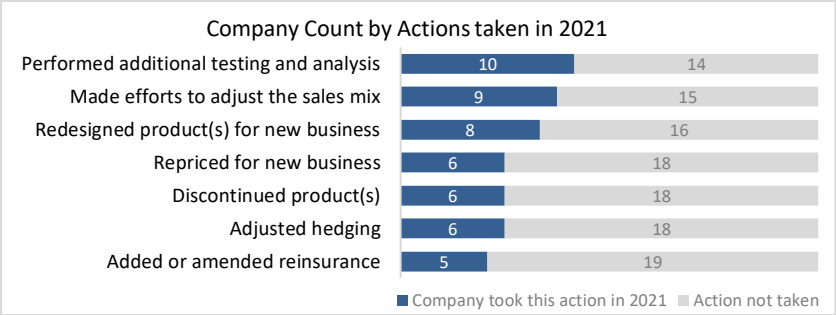
Companies were asked to respond to a series of questions, summarized below.

1. **View of moderately adverse:** Many companies viewed the Stress Test Scenarios as beyond moderately adverse. However, given the low interest rate environment as of 12/31/2021, some companies commented that the Stress Test Scenarios were in the range of being moderately adverse.

2. **Other stress tests:** Many companies have conducted their own stress test using low interest rates for a prolonged period of at least 10 years. Some companies have been using a stress test focused on a shorter period of low interest rates or with an immediate shock scenario.

3. **Negative interest rates:** Many companies can calculate reserves and RBC using scenarios with negative interest rates. Some companies have conducted stress tests using negative interest rates. Some companies view the use of negative interest rates as beyond moderately adverse. Many companies indicated that actions considered if interest rates remain low for a prolonged period would also be considered if interest rates become negative.

4. **Actions taken in 2021 for the VA block of business:** Many companies took at least one action in 2021.



Other actions included changing fees for inforce business, adjusting investment strategies, implementing ESG changes, and adjusting asset/liability management.

5. **Potential future actions:** When asked about the timing of potential future actions if interest rates continue to remain low, many companies indicated that at least one action was likely within the next two years.

Potential Future Actions	Company Count* of Action:	
	Likely within 2 years	Likely in 3-5 years
Perform additional testing and analysis	17	
Reprice for new business	13	1
Redesign product(s) for new business	11	2
Make efforts to adjust the sales mix	12	
Discontinue product(s)	6	4
Adjust hedging	9	
Change fees for inforce business	2	5
Adjust investment strategy	4	2

*If multiple time periods were selected as likely for an action, only the first time period was counted

Other potential actions included adjusting asset/liability management, adding or amending reinsurance, and implementing ESG changes (prior to potentially required ESG changes).

III. Update on the Economic Scenario Generator

The implementation of a new ESG is in progress. An ESG Drafting Group, consisting of members of the Life Actuarial (A) Task Force and Life Risk-Based Capital (E) Working Group, the selected ESG vendor (Conning), representatives of the Academy and American Council of Life Insurers, and other subject matter experts, developed specifications for an industry field test. Review of field test results is currently underway. This is expected to lead to a recalibration of the ESG, followed by a second industry field test. Ultimately, *Valuation Manual* amendments and RBC instruction changes will be necessary to incorporate prescription of the new ESG, which is now anticipated to be no sooner than 1/1/25.

IV. VAWG Plans for Future VA Stress Tests

Additional VA stress tests will be considered as needed prior to adoption of the new ESG. However, the ESG field tests enable VAWG to monitor the impacts of negative and prolonged low interest rates. Thirty-one VA writers participated in the ESG field test, representing a high percentage of the industry. Participants include most of the 24 companies that performed the 2021 VA stress test.