EXECUTIVE (EX) COMMITTEE AND PLENARY

Executive (EX) Committee and Plenary Aug. 14, 2020, Minutes

- Adopted the Artificial Intelligence (AI) Guiding Principles (Attachment One)
- Executive (EX) Committee and Plenary Feb. 13, 2020, Minutes (Attachment Two)
  - Adopted Revisions to the *Suitability in Annuity Transactions Model Regulation* (#275) (Attachment Two-A)
- Adopted the Technical Revisions 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) (Attachment Three)
- Adopted Amendments to the *Valuation Manual* (Attachment Four)
- Adopted the *Actuarial Guideline XLVIX-A—The Application of the Life Illustrations Model Regulation to Policies with Index-Based Interest* (AG 49-A) (Attachment Five)
- Adopted the Considerations for State Insurance Regulators in Building the Private Flood Insurance Market (Attachment Six)
- Adopted the NAIC Continuing Education Reciprocity (CER) Agreement – 2019 Version (Attachment Seven)
- Adopted the 2019 Revisions to the *Credit for Reinsurance Model Law* (#785) and the *Credit for Reinsurance Model Regulation* (#786) as an Addition to the Part A Accreditation Standards (Attachment Eight)
- Adopted the *Term and Universal Life Insurance Reserve Financing Model Regulation* (#787) as a New Part A Accreditation Standard (Attachment Nine)
- Report on States' Implementation of NAIC-Adopted Model Laws and Regulations (Attachment Ten)

Draft Pending Adoption

Draft: 8/27/20

Executive (EX) Committee
Virtual Summer National Meeting
August 13, 2020

The Executive (EX) Committee met via conference call Aug. 13, 2020. The following Committee members participated: Raymond G. Farmer, Chair (SC); David Altmaier, Vice Chair (FL); Dean L. Cameron, Vice President (ID); Chlora Lindley-Myers, Secretary-Treasurer (MO); Eric A. Cioppa, Most Recent Past President (ME); Lori K. Wing-Heier (AK); Jim L. Ridling (AL); Michael Conway (CO); Doug Ommen (IA); James J. Donelon (LA); Gary D. Anderson (MA); Mike Chaney (MS); Jillian Froment (OH); Andrew R. Stolfi (OR); Jessica K. Altman (PA); Elizabeth Kelleher Dwyer (RI); and Larry D. Deiter (SD). Also participating were Jon Godfread (ND); and Scott A. White (VA).

1. Adopted the July 14 Report of the Executive (EX) Committee and the Internal Administration (EX1) Subcommittee

Director Farmer reported that the Executive (EX) Committee and the Internal Administration (EX1) Subcommittee met July 14 in a joint session. The meeting was held in regulator-to-regulator session, pursuant to paragraph 4 (internal or administrative matters of the NAIC) and paragraph 6 (consultations with NAIC staff members) of the NAIC Policy Statement on Open Meetings.

During this joint meeting, the Committee and Subcommittee took the following action: 1) adopted its May 12 minutes; and 2) adopted the Internal Administration (EX1) Subcommittee's May 20 minutes, which included the following action: a) received an update on the Defined Benefit Plan portfolio as of March 31; b) received an update on the NAIC long-term investment plan portfolio as of March 31; and c) approved a recommendation to replace one of the NAIC's fund managers responsible for short-term bond funds.

The Committee and Subcommittee also: 1) adopted the report of the Audit Committee, which met via conference call June 2 and received the 2019/2020 Service Organization Control (SOC) 1 and SOC 2 reports; 2) received an update on the 2020 financial results and preliminary 2021 budget assumptions and approved an extension of unused 2020 grant funds to the end of 2021; 3) established a Special Committee on Race and Insurance; 4) established the Climate & Resiliency (EX) Task Force and adopted its draft charges; 5) received a System for Electronic Rate and Form Filing (SERFF) Assessment and directed NAIC staff to prepare and issue a request for proposal (RFP) to solicit proposals to help complete a "modernization pilot" and "Wave One" as recommended in the SERFF Assessment; 6) approved Management's recommendation to extend the residential mortgage-backed securities (RMBS)/commercial mortgage-backed securities (CMBS) modeling contract with BlackRock for another year; 7) approved the release of the Economic Scenario Generator (ESG) fiscal for a two-week public review period prior to a final vote of the Executive (EX) Committee during a future meeting; 8) approved a U.S. Department of Labor (DOL) Information Sharing Agreement; 9) selected the meeting locations for the 2024 summer and fall national meetings: the 2024 Summer National Meeting will be held in Chicago, IL, and the 2024 Fall National Meeting will be held in Denver, CO; and 10) received the joint chief executive officer (CEO)/chief operating officer (COO) report.

Commissioner Conway made a motion, seconded by Director Froment, to adopt the July 14 report of the joint meeting of the Executive (EX) Committee and the Internal Administration (EX1) Subcommittee. The motion passed unanimously.

2. Adopted its May 12, April 2, Feb. 13 and Jan. 10 Interim Meeting Report

Director Lindley-Myers made a motion, seconded by Commissioner Altman, to adopt the Committee's May 12, April 2, Feb. 13 and Jan. 10 interim meeting report (Attachment One). The motion passed unanimously.

3. Adopted the Reports of its Task Forces

The Committee adopted written reports from the Financial Stability (EX) Task Force, the Government Relations (EX) Leadership Council, the Innovation and Technology (EX) Task Force, and the Long-Term Care Insurance (EX) Task Force.

Commissioner Godfread further reported that the Innovation and Technology (EX) Task Force met Aug. 7 and adopted the Artificial Intelligence (AI) Principles for the insurance industry adopted by the Artificial Intelligence (EX) Working Group on June 30.

During the meeting, the Task Force discussed the outstanding issues raised during its meeting on July 23. Each section of the AI Principles was discussed individually. The Task Force had a productive discussion that ultimately resulted in adoption of the AI Principles as amended during the meeting. The Principles will be presented for further adoption at the joint meeting of Executive (EX) Committee and Plenary on Aug. 14.

Commissioner White further reported that the Long-Term Care Insurance (EX) Task Force also adopted charges for three new subgroups during its Aug. 7 meeting. The Subgroups will move more discussions about the rate review methodology and RBOs and consumer notices work of the Task Force into the public realm. The Subgroup charges are a delegation of the Task Force charges and a consolidation of the six existing workstreams into three subgroups.

Director Wing-Heier made a motion, seconded by Director Cameron, to adopt the reports of the Financial Stability (EX) Task Force; the Government Relations (EX) Leadership Council; the Innovation and Technology (EX) Task Force, including the AI Principles; and the charges of the new subgroups of the Long-Term Care Insurance (EX) Task Force (Attachment Two, Attachment Two-A, Attachment Two-B). The motion passed unanimously.

4. Adopted a Model Law Development Request for Amendments to the *Insurance Holding Company System Regulatory Act* (#440) and the *Insurance Holding Company System Model Regulation with Reporting Forms and Instructions* (#450)

Commissioner White reported that at the 2019 Fall National Meeting, the Executive (EX) Committee approved a request from the Financial Condition (E) Committee and the Group Capital Calculation (E) Working Group to open up the *Insurance Holding Company System Regulatory Act* (#440) and the *Insurance Holding Company System Model Regulation with Reporting Forms and Instructions* (#450) to make sure the calculation is held confidential.

Commissioner White stated that prior to the scheduled Spring National Meeting, the Financial Condition (E) Committee received and approved two additional requests for amending Model #440 and Model #450. The first request was from the Receivership and Insolvency (E) Task Force to make changes for issues that can arise in a receivership of an insurance company where affiliated entities provide essential services through inter-company agreements. For example, in the cases of claims handling, underwriting and premium collection, 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. The request recommends developing language that gives the commissioner the authority over these situations. The second request was from the Financial Stability (EX) Task Force requesting an avenue to maintain the confidentiality of a liquidity stress test that the Task Force is currently developing for certain very large life insurers. This new requirement is being suggested as the key deliverable on the Macroprudential Initiative (MPI) led by Commissioner Marlene Caride (NJ). Commissioner White acknowledged that the three ongoing amendments may not be completed at the same time, but it is still important to proceed with all the work.

Commissioner Altmaier made a motion, seconded by Commissioner Conway, to adopt the request to develop amendments to Model #440 and Model #450 (Attachment Three). The motion passed unanimously.

5. Adopted a Model Law Development Request for Amendments to the *Standard Nonforfeiture Law for Individual Deferred Annuities* (#805)

Director Froment reported that the Request for NAIC Model Law Development for the *Standard Nonforfeiture Law for Individual Deferred Annuities* (#805) came to the Life Insurance and Annuities (A) Committee from the Life Actuarial (A) Task Force, and it arises out of concern with the 1% floor on the minimum nonforfeiture accumulation rate that is currently in the model. This minimum will be difficult for insurers to achieve in the current very low interest rate environment and significantly limit the availability of annuity products. This request to revise Model #805 is to address this minimum nonforfeiture rate floor.

Director Froment made a motion, seconded by Director Lindley-Myers, to adopt the request to develop amendments to Model #805 (Attachment Four). The motion passed unanimously.

6. Received the 2019 Annual Report of NAIC Designation Program Advisory Board Activities

Superintendent Dwyer provided an update on the NAIC Designation Program Advisory Board's activities and the 2019 achievements for the NAIC Insurance Regulator Professional Designation Program (Attachment Five). In 2019, there was an increase of more than 350 insurance regulator designation enrollments. At year-end, enrollments totaled 2,392 since its inception in 2006. In 2019, 1,310 new professional insurance regulation designations were awarded.

Superintendent Dwyer also reported that the Advisory Board, entered into a contract with Certemy to replace the existing enrollment site with Certemy's program management system. The Advisory Board made a number of changes to the program as requested by commissioners, including: 1) waiving the first retake fee; 2) removing tenure requirements for Associate Professional in Insurance Regulation (APIR) and Professional in Insurance Regulation (PIR); and 3) allowing courses to be taken "out of sequence."

Superintendent Dwyer thanked Commissioner Godfread, Mary Mealer (MO), Pat McNaughton (WA), Scott Sanders (GA) and Rachel Chester (RI) for their hard work and dedication in developing this program into the success it is today.

7. Received a Status Report on the NAIC *State Ahead* Strategic Plan Implementation

Director Farmer provided an update on the NAIC *State Ahead* implementation efforts. *State Ahead* is a three-year strategic plan intended to further advance the products, services and support that the NAIC provides to state insurance regulators in order to better meet the changing regulatory landscape. NAIC staff continue to make good progress on the many *State Ahead* projects (Attachment Six). Given the change in priorities with the COVID-19 outbreak, the development of *State Ahead* 2.0 is on pause and that important work will continue in 2021.

8. Received a Report of Model Law Development Efforts

Director Farmer presented a written report on the progress of ongoing model law development efforts (Attachment Seven).

9. Heard a Report from the Interstate Insurance Product Regulation Commission (Commission)

Superintendent Dwyer reported that the Commission held a joint meeting with its Management Committee Aug. 14. The Compact has been working on implementing several action items in its strategic plan, which was adopted at the 2019 Fall National Meeting.

Superintendent Dwyer stated that many of the action items in the strategic plan call for examining and enhancing various procedures, notices and information to keep members and others informed and encourage meaningful input. A key initiative in the strategic plan involved the restructuring of the outstanding debt repayment to the NAIC. This new agreement was approved by the Compact during its May meeting, and the Compact made its first of 10 annual payments to the NAIC at the end of May. The Compact is currently kicking off two strategic projects—a governance review and a business assessment. An RFP process was conducted for both projects and the selection process was completed last month. Squire Patton Boggs is performing the governance review project, and Rector & Associates Inc. is performing the business assessment engagement.

The Compact has a Governance Review Committee, which includes three officers—Superintendent Dwyer, Commissioner Mark Afable (WI), and Director Robert H. Muriel (IL)—along with Commissioner Kent Sullivan (TX) and Commissioner James A. Dodrill (WV). The Committee is managing these projects, along with coordinating a state-by-state review being conducted by the Compact Office to document meaningful differences between the Uniform Standards and state statutes.

Superintendent Dwyer also reported that in April, the Colorado Supreme Court issued an opinion in *Amica v. Wertz*, 462 P.3d 51, on the Compact and its delegated authority. The Compact was recognized as a valid delegation of authority at the district court level. When the case was appealed, the 10th Circuit Court of Appeals certified the delegation of authority question to the Colorado Supreme Court, as it involved a conflict between a state statute with a one-year suicide exclusion and the Compact's Uniform Standard that had a two-year suicide exclusion. The Colorado Supreme Court concluded that the Compact's Uniform Standards operate as regulations and with respect to an interstate compact that has not been approved by the U.S. Congress (Congress), the Colorado legislature may not delegate to an interstate agency the authority to adopt regulations that effectively override a Colorado statute. This opinion respects the Compact structure and focuses on where a provision in the Uniform Standards may conflict with a state statute, especially where the state law is more stringent. The Compact staff has been working with states and industry to identify those areas where the Compact standards conflict with a state statute.

Having no further business, the Executive (EX) Committee adjourned.

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Adopted by the Executive (EX) Committee, Aug. 13, 2020
Adopted by the Innovation and Technology (EX) Task Force, Aug. 7, 2020

National Association of Insurance Commissioners (NAIC) Principles on Artificial Intelligence (AI)

RECOMMENDS that insurance companies and all persons or entities facilitating the business of insurance that play an active role in the AI system life cycle, including third parties such as rating, data providers and advisory organizations (hereafter referred to as "AI actors") promote, consider, monitor and uphold the following principles according to their respective roles; and

THIS DOCUMENT is intended to establish consistent high-level guiding principles for AI actors. These principles are guidance and do not carry the weight of law or impose any legal liability. This guidance can serve to inform and establish general expectations for AI actors and systems emphasizing the importance of accountability, compliance, transparency, and safe, secure, fair and robust outputs.

Further, **THIS DOCUMENT**

Should be used to assist regulators and NAIC committees addressing insurance-specific AI applications. The level of regulatory oversight may vary based on the risk and impact to the consumer. These principles should be interpreted and applied in a manner that accommodates the nature and pace of change in the use of AI by the insurance industry and promotes innovation, while protecting the consumer.

Fair and Ethical

a. AI actors should respect the rule of law throughout the AI life cycle. This includes, but is not limited to, insurance laws and regulations, such as those relating to trade practices, unfair discrimination, access to insurance, underwriting, privacy, consumer protection and eligibility practices, ratemaking standards, advertising decisions, claims practices, and solvency.

b. Consistent with the risk-based foundation of insurance, AI actors should proactively engage in responsible stewardship of trustworthy AI in pursuit of beneficial outcomes for consumers and to avoid proxy discrimination against protected classes. AI systems should not be designed to harm or deceive people and should be implemented in a manner that avoids harmful or unintended consequences and corrects and remediates for such consequences when they occur.

Accountable

a. AI actors should be accountable for ensuring that AI systems operate in compliance with these principles consistent with the actors' roles, within the appropriate context and evolving technologies. Any AI system should be compliant with legal requirements governing its use of data and algorithms during its phase of the insurance life cycle. Data supporting the final outcome of an AI application should be retained and be able to be produced in accordance with applicable insurance laws and regulations in each jurisdiction. AI actors should be responsible for the creation, implementation and impacts of any AI system, even if the impacts are unintended. AI actors should implement mechanisms and safeguards consistent with the degree and nature of the risks posed by AI to ensure all applicable laws and regulations are followed, including ongoing (human or otherwise) monitoring and, when appropriate, human intervention.

Compliant

a. AI actors must have the knowledge and resources in place to comply with all applicable insurance laws and regulations. AI actors must recognize that insurance is primarily regulated by the individual states and territories of the United States as well as by the federal government, and that AI systems must comply with the insurance laws and regulations within each individual jurisdiction. Compliance is required whether the violation is intentional or unintentional. Compliance with legal requirements is an ongoing process. Thus, any AI system that is deployed must be consistent with applicable laws and safeguards against outcomes that are either unfairly discriminatory or otherwise violate legal standards, including privacy and data security laws and regulations.

Transparent

a. For the purpose of improving the public's confidence in AI, AI actors should commit to transparency and responsible disclosures regarding AI systems to relevant stakeholders. AI actors must have the ability to protect confidentiality of proprietary algorithms, provided adherence to individual state law and regulations in all states where AI is deployed can be demonstrated. These proactive disclosures include revealing the kind of data being used, the purpose of the data in the AI system and consequences for all stakeholders.

b. Consistent with applicable laws and regulations, stakeholders (which includes regulators and consumers) should have a way to inquire about, review and seek recourse for AI-driven insurance decisions. This information should be easy-to-understand and describe the factors that lead to the prediction, recommendation or decision. This information may be presented differently and should be appropriate for applicable stakeholders.

Secure, Safe and Robust

a. AI systems should be robust, secure and safe throughout the entire life cycle so that in conditions of normal or reasonably foreseeable use, or adverse conditions, they can function in compliance with applicable laws and regulations. To this end, AI actors should ensure a reasonable level of traceability in relation to datasets, processes and decisions made during the AI system life cycle. AI actors should enable analysis of the AI system's outcomes, responses and other insurance-related inquiries, as appropriate in keeping with applicable industry best practices and legal requirements.

b. AI actors should, based on their roles, the situational context and their ability to act, apply a systematic risk management approach to each phase of the AI system life cycle on a continuous basis to address risks related to AI systems, including privacy, digital security and unfair discrimination as defined by applicable laws and regulations.

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Draft for Adoption

Executive (EX) Committee and Plenary
Orlando, Florida
February 13, 2020

The Executive (EX) Committee and Plenary met in joint session in Orlando, FL, Feb. 13, 2020. The following members participated: Raymond G. Farmer, Chair (SC); David Altmaier, Vice Chair (FL); Dean L. Cameron, Vice President (ID); Chlora Lindley-Myers, Secretary-Treasurer (MO); Eric A. Cioppa, Most Recent Past President (ME); Lori K. Wing-Heier (AK); Jim L. Ridling (AL); Allen W. Kerr (AR); Ricardo Lara (CA); Michael Conway (CO); Andrew N. Mais (CT); Karima M. Woods (DC); John F. King (GA); Dafne M. Shimizu (GU); Colin M. Hayashida represented by Martha Im (HI); Doug Ommen (IA); Robert H. Muriel (IL); Stephen W. Robertson (IN); Vicki Schmidt (KS); Sharon P. Clark (KY); Gary Anderson (MA); Al Redmer Jr. (MD); Anita G. Fox (MI); Mike Chaney (MS); Mike Causey (NC); Jon Godfread (ND); Bruce R. Ramge (NE); Marlene Caride (NJ); Barbara D. Richardson (NV); Linda A. Lacewell (NY); Jillian Froment (OH); Glen Mulready (OK); Andrew R. Stolfi (OR); Jessica K. Altman (PA); Rafael Cestero-Lopategui (PR); Elizabeth Kelleher Dwyer (RI); Larry D. Deiter (SD); Hodgen Mainda (TN); Kent Sullivan (TX); Todd E. Kiser (UT); Scott A. White (VA); Tregenza A. Roach (VI); Michael S. Pieciak (VT); Mike Kreidler (WA); Mark Afable (WI); James A. Dodrill represented by Tonya Gillespie (WV); and Jeff Rude (WY).

1. Adopted Revisions to the *Suitability in Annuity Transactions Model Regulation* (#275)

Director Froment presented draft revisions to the *Suitability in Annuity Transactions Model Regulation* (#275) that will enhance the model in protecting consumers by requiring a heightened standard of conduct for producer recommendations of an annuity to be made in "the best interest" of the consumer, and it will require insurers to develop procedures to comply with these requirements.

Director Froment noted that the model has been protecting consumers since it was adopted in 2003. The Annuity Suitability (A) Working Group sent draft revisions to the Life Insurance and Annuities (A) Committee for its consideration at the 2019 Fall National Meeting. The Committee gave preliminary approval to the proposed revisions, but it tasked the Working Group to complete additional revisions to the appendices. The Working Group revised the appendices and sent them to the Committee for consideration.

The Committee met Dec. 30, 2019, to discuss the revisions to the model, including the revised appendices, and adopted the revisions.

The resulting revisions establish a "best interest" standard of conduct and require producers and insurers to satisfy the requirements outlined in four obligations: 1) a care obligation; 2) a disclosure obligation; 3) a conflict of interest obligation; and 4) a documentation obligation. The revisions also include enhancements to the current model's insurer supervision system to assist in compliance.

The revisions make it clear that all recommendations by producers and insurers must be "in the best interest of the consumer," and producers and insurers may not place their financial interests ahead of the consumer's interest in making a recommendation. The revisions also require producers and insurers to act with "reasonable diligence, care and skill" in making a recommendation.

The revisions require producers to: 1) know the consumer's financial situation, insurance needs and financial objectives; 2) understand the available recommendation options; 3) have a reasonable basis to believe the recommended option effectively addresses the consumer's financial situation, insurance needs and financial objectives, and communicate the basis of the recommendation to the consumer; 4) disclose their role in the transaction, their compensation and any material conflicts of interest; and 5) document, in writing, any recommendation and the justification for such recommendation.

The revisions also include heightened supervision requirements for insurers to achieve compliance with this regulation. This includes procedures to review recommendations by producers to ensure that the recommended annuity would effectively address the particular consumer's financial situation, insurance needs and financial objectives.

Draft for Adoption

The insurer is also required to establish systems for complying with all four obligations outlined in this regulation. Additionally, insurers must eliminate any sales contests, sales quota, bonuses and non-cash compensation that are based on the sales of specific annuities within a limited period of time.

Recognizing that the sale of annuities and those who sell annuities can be subject to multiple regulatory authorities, the Working Group made significant efforts to remain cognizant of the work being done by these state insurance regulators. As a result, these revisions also align well with the U.S. Securities and Exchange Commission's (SEC's) Regulation Best Interest.

Additionally, the revisions expand the model's current safe harbor provisions to apply the safe harbor to any producer that is regulated as a broker-dealer, investment adviser or plan fiduciary. The producer must be in compliance with business rules, controls and procedures that satisfy a "comparable standard" to this model's new standard of conduct. This could include the SEC's Regulation Best Interest.

Superintendent Lacewell stated that New York recognizes this proposal as better than what existed before and that some states would like to go further but face obstacles that do not allow them individually to get there. She stated that she believes the role of the NAIC should be to "lift up" all states and not use "the common denominator of what can be agreed to by 50-plus jurisdictions." New York's standard is the "best interest of the consumer without consideration of the producer's financial or other interest in the matter." Superintendent Lacewell stated that she believes this is not the standard applied in the model. New York standards also apply to life insurance, not just annuities, and apply to in-force transactions and decisions made under the in-force transaction.

Superintendent Lacewell stated:

> New York's view is that we regulate industry, and it is our obligation to facilitate the safety and soundness of the industry, but a large component of safety and soundness of industry is the integrity of the industry and the impact on the millions of people served and protected by the products and services of industry. The consumer should have access to all the information that they need and accurate information before they part with their money or make financial decisions in their lives. That is not achieved here because if the producer is going to make a recommendation and say, 'Here is what I think you should do …,' implicit in that recommendation is 'Trust me.' I would like us to find ways of communicating and helping states who want to get there and cannot do it on their own.

Commissioner Ommen stated that supporting this model is supporting a framework to go back to your states and find out through your own constituency what is good for your states. He stated, "We think that this rule as a model does reach where we need to be in Iowa, and it is very reflective of additional consumer protection that we believe does achieve best interest."

Superintendent Cioppa stated, "Maine supports the model as a step forward from the current 'suitability' model we have and respects other states' opinions, but it achieves a good consensus. I think the harmonization is important, but most importantly, I think it steps up our game in protecting consumers. The requirements of the model will help consumers in the end and benefit them."

Commissioner Lara stated that California has been an active participant in promoting the strongest standards possible to protect consumers when purchasing annuities. He stated, "In California, some of our standards are stronger, including a provision that requires that any annuity be in the best interest of the consumers overall. California does support, and would prefer, a standard that establishes a fiduciary duty that producers sell products that put consumers first instead of commissions or other producer incentives. I believe this model is not perfect. I will be voting in favor of the draft amendments to the model regulation because they do contain significant amendments that afford increased consumer protections over the existing protections. Although some of the draft amendments are problematic for California, it would be better for consumers than the existing model regulation."

Commissioner Redmer requested a clarification to the safe harbor provisions allowing satisfaction by a "comparable standard even if that standard does not otherwise apply to that product." Commissioner Ommen stated that some producers are licensed in both securities and insurance. He stated:

Draft for Adoption

> Historically, and what is in our current model, is a safe harbor for those agencies (broker dealers/agents) registered under the Financial Industry Regulatory Authority (FINRA) and subject to the FINRA suitability and supervision regiment applied also in the sales and recommendation surrounding fixed index products. This language in the model extends that safe harbor to true fiduciaries, which would include the investment advisors that are in the securities side of the business.

Commissioner Ommen also stated:

> If the supervision and suitability structure, which now has been raised to a best interest and supervision structure, is comparable to what we require here under this rule, that would be deemed compliant. It also should be noted that the insurance regulator does not lose its authority to go in and actually determine whether or not they are comparable; we still have oversight, and there is additional language that does not relieve the insurance company of using their oversight in order to ensure compliance.

Superintendent Dwyer stated that Rhode Island has taken action against companies that had not dealt appropriately with consumers in Rhode Island in the sales of annuities under the old NAIC model act and have been successful. She states, "To me, this is a step up, and we can take action against bad actors to protect consumers."

Director Fox expressed support for the revised standard and also the amendments that were made to the safe harbor. She stated, "We recognize fiduciary duties from other contexts and make sure that we have continuity of regulation, but, like Commissioner Ommen stated, it did not detract in any way from our ability to make things comparable."

Commissioner Richardson stated that she will support the amendment, "but, like California and Rhode Island, we believe that there are already some protections in place, and in Nevada, specifically, we have a fiduciary standard in place. For us, this is raising the water."

Director Froment made a motion, seconded by Commissioner Chaney, to adopt the revisions to the *Suitability in Annuity Transactions Model Regulation* (#275) (Attachment Two-A). The motion passed, with New York opposing.

Having no further business, the Executive (EX) Committee and Plenary adjourned.

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Adopted by the Life Insurance and Annuities (A) Committee – Dec. 30, 2019

Draft: 12/30/19
Model #275

SUITABILITY IN ANNUITY TRANSACTIONS
MODEL REGULATION

Table of Contents

Section 1. Purpose

A. The purpose of this regulation is to require producers, as defined in this regulation, to act in the best interest of the consumer when making a recommendation of an annuity and to require insurers to establish and maintain a system to supervise recommendations ~~and to set forth standards and procedures for recommendations to consumers that result in transactions involving annuity products~~ so that the insurance needs and financial objectives of consumers at the time of the transaction are ~~appropriately~~ effectively addressed.

B. Nothing herein shall be construed to create or imply a private cause of action for a violation of this regulation or to subject a producer to civil liability under the best interest standard of care outlined in Section 6 of this regulation or under standards governing the conduct of a fiduciary or a fiduciary relationship.

Drafting Note: The language of subsection B comes from the NAIC Unfair Trade Practices Act. If a State has adopted different language, it should be substituted for subsection B.

Drafting Note: Section 989J of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank Act") specifically refers to this model regulation as the "Suitability in Annuity Transactions Model Regulation." Section 989J of the Dodd-Frank Act confirmed this exemption of certain annuities from the Securities Act of 1933 and confirmed state regulatory authority. This regulation is a successor regulation that exceeds the requirements of the 2010 model regulation.

Section 2. Scope

This regulation shall apply to any sale or recommendation ~~to purchase, exchange or replace~~of an annuity ~~made to a consumer by an insurance producer, or an insurer where no producer is involved, that results in the purchase, exchange or replacement recommended~~.

Section 3. Authority

This regulation is issued under the authority of [insert reference to enabling legislation].

Drafting Note: States may wish to use the Unfair Trade Practices Act as enabling legislation or may pass a law with specific authority to adopt this regulation.

Section 4. Exemptions

Unless otherwise specifically included, this regulation shall not apply to transactions involving:

A. Direct response solicitations where there is no recommendation based on information collected from the consumer pursuant to this regulation;

B. Contracts used to fund:

(1) An employee pension or welfare benefit plan that is covered by the Employee Retirement and Income Security Act (ERISA);

(2) A plan described by sections 401(a), 401(k), 403(b), 408(k) or 408(p) of the Internal Revenue Code (IRC), as amended, if established or maintained by an employer;

(3) A government or church plan defined in section 414 of the IRC, a government or church welfare benefit plan, or a deferred compensation plan of a state or local government or tax-exempt organization under section 457 of the IRC; or

(4) A nonqualified deferred compensation arrangement established or maintained by an employer or plan sponsor;

C.~~(5)~~ Settlements of or assumptions of liabilities associated with personal injury litigation or any dispute or claim resolution process; or

D.~~(6)~~ Formal prepaid funeral contracts.

Section 5. Definitions

A. "Annuity" means an annuity that is an insurance product under State law that is individually solicited, whether the product is classified as an individual or group annuity.

B. "Cash compensation" means any discount, concession, fee, service fee, commission, sales charge, loan, override, or cash benefit received by a producer in connection with the recommendation or sale of an annuity from an insurer, intermediary, or directly from the consumer.

C. "Consumer profile information" means information that is reasonably appropriate to determine whether a recommendation addresses the consumer's financial situation, insurance needs and financial objectives, including, at a minimum, the following:

(1) Age;

(2) Annual income;

(3) Financial situation and needs, including debts and other obligations;

(4) Financial experience;

(5) Insurance needs;

(6) Financial objectives;

(7) Intended use of the annuity;

(8) Financial time horizon;

(9) Existing assets or financial products, including investment, annuity and insurance holdings;

(10) Liquidity needs;

(11) Liquid net worth;

(12) Risk tolerance, including but not limited to, willingness to accept non-guaranteed elements in the annuity;

(13) Financial resources used to fund the annuity; and

(14) Tax status.

~~B~~D. "Continuing education credit" or "CE credit" means one continuing education credit as defined in [insert reference in State law or regulations governing producer continuing education course approval].

~~C~~E. "Continuing education provider" or "CE provider" means an individual or entity that is approved to offer continuing education courses pursuant to [insert reference in State law or regulations governing producer continuing education course approval].

~~D~~F. "FINRA" means the Financial Industry Regulatory Authority or a succeeding agency.

~~E~~G. "Insurer" means a company required to be licensed under the laws of this state to provide insurance products, including annuities.

~~F. "Insurance producer" means a person required to be licensed under the laws of this state to sell, solicit or negotiate insurance, including annuities.~~

H. "Intermediary" means an entity contracted directly with an insurer or with another entity contracted with an insurer to facilitate the sale of the insurer's annuities by producers.

I. (1) "Material conflict of interest" means a financial interest of the producer in the sale of an annuity that a reasonable person would expect to influence the impartiality of a recommendation.

(2) "Material conflict of interest" does not include cash compensation or non-cash compensation.

J. "Non-cash compensation" means any form of compensation that is not cash compensation, including, but not limited to, health insurance, office rent, office support and retirement benefits.

K. "Non-guaranteed elements" means the premiums, credited interest rates (including any bonus), benefits, values, dividends, non-interest based credits, charges or elements of formulas used to determine any of these, that are subject to company discretion and are not guaranteed at issue. An element is considered non-guaranteed if any of the underlying non-guaranteed elements are used in its calculation.

L. "Producer" means a person or entity required to be licensed under the laws of this state to sell, solicit or negotiate insurance, including annuities. For purposes of this regulation, "producer" includes an insurer where no producer is involved.

~~G~~M. (1) "Recommendation" means advice provided by ~~an insurance~~ a producer~~, or an insurer where no producer is involved,~~ to an individual consumer that was intended to result or does result ~~results~~ in a purchase, an exchange or a replacement of an annuity in accordance with that advice.

(2) Recommendation does not include general communication to the public, generalized customer services assistance or administrative support, general educational information and tools, prospectuses, or other product and sales material.

~~H~~N. "Replacement" means a transaction in which a new ~~policy or contract~~annuity is to be purchased, and it is known or should be known to the proposing producer, or to the proposing insurer ~~if there is no~~whether or not a producer is involved, that by reason of the transaction, an existing annuity or other insurance policy ~~or contract~~ has been or is to be any of the following:

(1) Lapsed, forfeited, surrendered or partially surrendered, assigned to the replacing insurer or otherwise terminated;

(2) Converted to reduced paid-up insurance, continued as extended term insurance, or otherwise reduced in value by the use of nonforfeiture benefits or other policy values;

(3) Amended so as to effect either a reduction in benefits or in the term for which coverage would otherwise remain in force or for which benefits would be paid;

(4) Reissued with any reduction in cash value; or

(5) Used in a financed purchase.

Drafting Note: The definition of "replacement" above is derived from the NAIC Life Insurance and Annuities Replacement Model Regulation. If a State has a different definition for "replacement," the State should either insert the text of that definition in place of the definition above or modify the definition above to provide a cross-reference to the definition of "replacement" that is in State law or regulation.

~~I. "Suitability information" means information that is reasonably appropriate to determine the suitability of a recommendation, including the following:~~

~~(1) Age;~~

~~(2) Annual income;~~

~~(3) Financial situation and needs, including the financial resources used for the funding of the annuity;~~

~~(4) Financial experience;~~

~~(5) Financial objectives;~~

~~(6) Intended use of the annuity;~~

~~(7) Financial time horizon;~~

~~(8) Existing assets, including investment and life insurance holdings;~~

~~(9) Liquidity needs;~~

~~(10) Liquid net worth;~~

~~(11) Risk tolerance; and~~

~~(12) Tax status.~~

O. "SEC" means the United States Securities and Exchange Commission.

Section 6. Duties of Insurers and ~~of Insurance~~ Producers

A. Best Interest Obligations. A producer, when making a recommendation of an annuity, shall act in the best interest of the consumer under the circumstances known at the time the recommendation is made, without placing the producer's or the insurer's financial interest ahead of the consumer's interest. A producer has acted in the best interest of the consumer if they have satisfied the following obligations regarding care, disclosure, conflict of interest and documentation:

~~A. In recommending to a consumer the purchase of an annuity or the exchange of an annuity that results in another insurance transaction or series of insurance transactions, the insurance producer, or the insurer where no producer is involved, shall have reasonable grounds for believing that the recommendation is suitable for the consumer on the basis of the facts disclosed by the consumer as to his or her investments and other insurance products and as to his or her financial situation and needs, including the consumer's suitability information, and that there is a reasonable basis to believe all of the following:~~

(1) (a) Care Obligation. The producer, in making a recommendation shall exercise reasonable diligence, care and skill to:

(i) Know the consumer's financial situation, insurance needs and financial objectives;

(ii) Understand the available recommendation options after making a reasonable inquiry into options available to the producer;

(iii) Have a reasonable basis to believe the recommended option effectively addresses the consumer's financial situation, insurance needs and financial objectives over the life of the product, as evaluated in light of the consumer profile information; and

(iv) Communicate the basis or bases of the recommendation.

(b) The requirements under subparagraph (a) of this paragraph include making reasonable efforts to obtain consumer profile information from the consumer prior to the recommendation of an annuity.

(c) The requirements under subparagraph (a) of this paragraph require a producer to consider the types of products the producer is authorized and licensed to recommend or sell that address the consumer's financial situation, insurance needs and financial objectives. This does not require analysis or consideration of any products outside the authority and license of the producer or other possible alternative products or strategies available in the market at the time of the recommendation. Producers shall be held to standards applicable to producers with similar authority and licensure.

(d) The requirements under this subsection do not create a fiduciary obligation or relationship and only create a regulatory obligation as established in this regulation.

(e) The consumer profile information, characteristics of the insurer, and product costs, rates, benefits and features are those factors generally relevant in making a determination whether an annuity effectively addresses the consumer's financial situation, insurance needs and financial objectives, but the level of importance of each factor under the care obligation of this paragraph may vary depending on the facts and circumstances of a particular case. However, each factor may not be considered in isolation.

(f) The requirements under subparagraph (a) of this paragraph include having a reasonable basis to believe the consumer would benefit from certain features of the annuity, such as annuitization, death or living benefit or other insurance-related features.

(g) The requirements under subparagraph (a) of this paragraph apply to the particular annuity as a whole and the underlying subaccounts to which funds are allocated at the time of purchase or exchange of an annuity, and riders and similar producer enhancements, if any.

(h) The requirements under subparagraph (a) of this paragraph do not mean the annuity with the lowest one-time or multiple occurrence compensation structure shall necessarily be recommended.

(i) The requirements under subparagraph (a) of this paragraph do not mean the producer has ongoing monitoring obligations under the care obligation under this paragraph, although such an obligation may be separately owed under the terms of a fiduciary, consulting, investment advising or financial planning agreement between the consumer and the producer.

(j) In the case of an exchange or replacement of an annuity, the producer shall consider the whole transaction, which includes taking into consideration whether:

(i) The consumer will incur a surrender charge, be subject to the commencement of a new surrender period, lose existing benefits, such as death, living or other contractual benefits, or be subject to increased fees, investment advisory fees or charges for riders and similar product enhancements;

(ii) The replacing product would substantially benefit the consumer in comparison to the replaced product over the life of the product; and

(iii) The consumer has had another annuity exchange or replacement and, in particular, an exchange or replacement within the preceding 60 months.

(k) Nothing in this regulation should be construed to require a producer to obtain any license other than a producer license with the appropriate line of authority to sell, solicit or negotiate insurance in this state, including but not limited to any securities license, in order to fulfill the duties and obligations contained in this regulation; provided the producer does not give advice or provide services that are otherwise subject to securities laws or engage in any other activity requiring other professional licenses.

(2) Disclosure obligation.

(a) Prior to the recommendation or sale of an annuity, the producer shall prominently disclose to the consumer on a form substantially similar to Appendix A:

(i) A description of the scope and terms of the relationship with the consumer and the role of the producer in the transaction;

(ii) An affirmative statement on whether the producer is licensed and authorized to sell the following products:

(I) Fixed annuities;

(II) Fixed indexed annuities;

(III) Variable annuities;

(IV) Life insurance;

(V) Mutual funds;

(VI) Stocks and bonds; and

(VII) Certificates of deposit;

(iii) An affirmative statement describing the insurers the producer is authorized, contracted (or appointed), or otherwise able to sell insurance products for, using the following descriptions:

(I) One insurer;

(II) From two or more insurers; or

(III) From two or more insurers although primarily contracted with one insurer.

(iv) A description of the sources and types of cash compensation and non-cash compensation to be received by the producer, including whether the producer is to be compensated for the sale of a recommended annuity by commission as part of premium or other remuneration received from the insurer, intermediary or other producer or by fee as a result of a contract for advice or consulting services; and

(v) A notice of the consumer's right to request additional information regarding cash compensation described in subparagraph (b) of this paragraph;

Drafting Note: If a state approves forms, a state should add language to subparagraph (a) reflecting such approvals.

(b) Upon request of the consumer or the consumer's designated representative, the producer shall disclose:

(i) A reasonable estimate of the amount of cash compensation to be received by the producer, which may be stated as a range of amounts or percentages; and

(ii) Whether the cash compensation is a one-time or multiple occurrence amount, and if a multiple occurrence amount, the frequency and amount of the occurrence, which may be stated as a range of amounts or percentages; and

(c~~1~~) Prior to or at the time of the recommendation or sale of an annuity, the producer shall have a reasonable basis to believe ~~The~~the consumer has been ~~reasonably~~ informed of various features of the annuity, such as the potential surrender period and surrender charge, potential tax penalty if the consumer sells, exchanges, surrenders or annuitizes the annuity, mortality and expense fees, investment advisory fees, any annual fees, potential charges for and features of riders or other options of the annuity, limitations on interest returns, potential changes in non-guaranteed elements of the annuity, insurance and investment components and market risk~~;~~.

Drafting Note: If a State has adopted the NAIC Annuity Disclosure Model Regulation, the State should insert an additional phrase in ~~paragraph (1)~~ subparagraph (c) above to explain that the requirements of this section are intended to supplement and not replace the disclosure requirements of the NAIC Annuity Disclosure Model Regulation.

~~(2) The consumer would benefit from certain features of the annuity, such as tax deferred growth, annuitization or death or living benefit;~~

~~(3) The particular annuity as a whole, the underlying subaccounts to which funds are allocated at the time of purchase or exchange of the annuity, and riders and similar product enhancements, if any, are suitable (and in the case of an exchange or replacement, the transaction as a whole is suitable) for the particular consumer based on his or her suitability information; and~~

~~(4) In the case of an exchange or replacement of an annuity, the exchange or replacement is suitable including taking into consideration whether:~~

~~(a) The consumer will incur a surrender charge, be subject to the commencement of a new surrender period, lose existing benefits (such as death, living or other contractual benefits), or be subject to increased fees, investment advisory fees or charges for riders and similar product enhancements;~~

~~(b) The consumer would benefit from product enhancements and improvements; and~~

~~(c) The consumer has had another annuity exchange or replacement and, in particular, an exchange or replacement within the preceding 36 months.~~

(3) Conflict of interest obligation. A producer shall identify and avoid or reasonably manage and disclose material conflicts of interest, including material conflicts of interest related to an ownership interest.

(4) Documentation obligation. A producer shall at the time of recommendation or sale:

(a) Make a written record of any recommendation and the basis for the recommendation subject to this regulation;

(b) Obtain a consumer signed statement on a form substantially similar to Appendix B documenting:

(i) A customer's refusal to provide the consumer profile information, if any; and

(ii) A customer's understanding of the ramifications of not providing his or her consumer profile information or providing insufficient consumer profile information; and

(c) Obtain a consumer signed statement on a form substantially similar to Appendix C acknowledging the annuity transaction is not recommended if a customer decides to enter into an annuity transaction that is not based on the producer's recommendation.

Drafting Note: If a state approves forms, a state should add language to subparagraphs (b) and (c) of this paragraph reflecting such approvals.

~~B. Prior to the execution of a purchase, exchange or replacement of an annuity resulting from a recommendation, an insurance producer, or an insurer where no producer is involved, shall make reasonable efforts to obtain the consumer's suitability information.~~

~~C. Except as permitted under subsection D, an insurer shall not issue an annuity recommended to a consumer unless there is a reasonable basis to believe the annuity is suitable based on the consumer's suitability information.~~

(5) Application of the best interest obligation. Any requirement applicable to a producer under this subsection shall apply to every producer who has exercised material control or influence in the making of a recommendation and has received direct compensation as a result of the recommendation or sale, regardless of whether the producer has had any direct contact with the consumer. Activities such as providing or delivering marketing or educational materials, product wholesaling or other back office product support, and general supervision of a producer do not, in and of themselves, constitute material control or influence.

~~D~~B. Transactions not based on a recommendation.

(1) Except as provided under paragraph (2)~~ of this subsection~~, ~~neither an insurance~~a producer~~, nor an insurer,~~ shall have ~~any~~no obligation to a consumer under subsection A(1) ~~or C~~ related to any annuity transaction if:

(a) No recommendation is made;

(b) A recommendation was made and was later found to have been prepared based on materially inaccurate information provided by the consumer;

(c) A consumer refuses to provide relevant ~~suitability~~consumer profile information and the annuity transaction is not recommended; or

(d) A consumer decides to enter into an annuity transaction that is not based on a recommendation of ~~the insurer or~~ the ~~insurance~~ producer.

(2) An insurer's issuance of an annuity subject to paragraph (1) shall be reasonable under all the circumstances actually known to the insurer at the time the annuity is issued.

C. Supervision system.

(1) Except as permitted under subsection B, an insurer may not issue an annuity recommended to a consumer unless there is a reasonable basis to believe the annuity would effectively address the particular consumer's financial situation, insurance needs and financial objectives based on the consumer's consumer profile information.

~~E. An insurance producer or, where no insurance producer is involved, the responsible insurer representative, shall at the time of sale:~~

~~(1) Make a record of any recommendation subject to section 6A of this regulation;~~

~~(2) Obtain a customer signed statement documenting a customer's refusal to provide suitability information, if any; and~~

~~(3) Obtain a customer signed statement acknowledging that an annuity transaction is not recommended if a customer decides to enter into an annuity transaction that is not based on the insurance producer's or insurer's recommendation.~~

~~F.~~ ~~(1)~~(2) An insurer shall establish and maintain a supervision system that is reasonably designed to achieve the insurer's and its ~~insurance~~ producers' compliance with this regulation, including, but not limited to, the following:

(a) The insurer shall establish and maintain reasonable procedures to inform its ~~insurance~~ producers of the requirements of this regulation and shall incorporate the requirements of this regulation into relevant ~~insurance~~ producer training manuals;

(b) The insurer shall establish and maintain standards for ~~insurance~~ producer product training and shall establish and maintain reasonable procedures to require its ~~insurance~~ producers to comply with the requirements of section 7 of this regulation;

(c) The insurer shall provide product-specific training and training materials which explain all material features of its annuity products to its ~~insurance~~ producers;

(d) The insurer shall establish and maintain procedures for the review of each recommendation prior to issuance of an annuity that are designed to ensure ~~that~~ there is a reasonable basis to determine that ~~a recommendation is suitable~~the recommended annuity would effectively address the particular consumer's financial situation, insurance needs and financial objectives. Such review procedures may apply a screening system for the purpose of

identifying selected transactions for additional review and may be accomplished electronically or through other means including, but not limited to, physical review. Such an electronic or other system may be designed to require additional review only of those transactions identified for additional review by the selection criteria;

(e) The insurer shall establish and maintain reasonable procedures to detect recommendations that are not ~~suitable~~in compliance with subsections A, B, D and E. This may include, but is not limited to, confirmation of the consumer's ~~suitability~~consumer profile information, systematic customer surveys, producer and consumer interviews, confirmation letters, producer statements or attestations and programs of internal monitoring. Nothing in this subparagraph prevents an insurer from complying with this subparagraph by applying sampling procedures, or by confirming the ~~suitability~~consumer profile information or other required information under this section after issuance or delivery of the annuity; ~~and~~

(f) The insurer shall establish and maintain reasonable procedures to assess, prior to or upon issuance or delivery of an annuity, whether a producer has provided to the consumer the information required to be provided under this section;

(g) The insurer shall establish and maintain reasonable procedures to identify and address suspicious consumer refusals to provide consumer profile information;

(h) The insurer shall establish and maintain reasonable procedures to identify and eliminate any sales contests, sales quotas, bonuses, and non-cash compensation that are based on the sales of specific annuities within a limited period of time. The requirements of this subparagraph are not intended to prohibit the receipt of health insurance, office rent, office support, retirement benefits or other employee benefits by employees as long as those benefits are not based upon the volume of sales of a specific annuity within a limited period of time; and

Drafting Note: The intent of this subparagraph (h) is to prohibit sales contests, sales quotas, bonuses and non-cash compensation based on the sale of a particular product within a limited period of time, but not to prohibit general incentives regarding the sales of a company's products with no emphasis on any particular product.

~~(f)~~(i) The insurer shall annually provide a written report to senior management, including to the senior manager responsible for audit functions, which details a review, with appropriate testing, reasonably designed to determine the effectiveness of the supervision system, the exceptions found, and corrective action taken or recommended, if any.

~~(2)~~(3) (a) Nothing in this subsection restricts an insurer from contracting for performance of a function (including maintenance of procedures) required under ~~paragraph (1)~~this subsection. An insurer is responsible for taking appropriate corrective action and may be subject to sanctions and penalties pursuant to section 8 of this regulation regardless of whether the insurer contracts for performance of a function and regardless of the insurer's compliance with subparagraph (b) of this paragraph.

(b) An insurer's supervision system under ~~paragraph (1)~~this subsection shall include supervision of contractual performance under this subsection. This includes, but is not limited to, the following:

(i) Monitoring and, as appropriate, conducting audits to assure that the contracted function is properly performed; and

(ii) Annually obtaining a certification from a senior manager who has responsibility for the contracted function that the manager has a reasonable basis to represent, and does represent, that the function is properly performed.

~~(3)~~(4) An insurer is not required to include in its system of supervision ~~an insurance~~:

(a) A producer's recommendations to consumers of products other than the annuities offered by the insurer; or

(b) Include consideration of or comparison to options available to the producer or compensation relating to those options other than annuities or other products offered by the insurer.

~~G~~D. Prohibited Practices. Neither a producer nor an insurer shall ~~An insurance producer shall not~~ dissuade, or attempt to dissuade, a consumer from:

(1) Truthfully responding to an insurer's request for confirmation of the ~~suitability~~consumer profile information;

(2) Filing a complaint; or

(3) Cooperating with the investigation of a complaint.

~~H~~E. Safe harbor.

(1) Recommendations and sales of annuities~~Sales~~ made in compliance with comparable standards ~~FINRA requirements pertaining to suitability and supervision of annuity transactions~~ shall satisfy the requirements under this regulation. This subsection applies to ~~FINRA broker-dealer~~all recommendations and sales of annuities made by financial professionals in compliance with business rules, controls and procedures that satisfy a comparable standard even if such standard would not otherwise apply to the product or recommendation at issue ~~if the suitability and supervision is similar to those applied to variable annuity sales~~. However, nothing in this subsection shall limit the insurance commissioner's ability to investigate and enforce ~~(including investigate)~~ the provisions of this regulation.

Drafting Note: Non-compliance with comparable standards ~~FINRA requirements~~ means that the ~~broker-dealer transaction~~recommendation or sale is subject to compliance with the ~~suitability~~ requirements of this regulation.

(2) Nothing in paragraph (1) shall limit the insurer's obligation to comply with Section 6C(1) of this regulation, although the insurer may base its analysis on information received from either the financial professional or the entity supervising the financial professional.

~~(2)~~(3) For paragraph (1) to apply, an insurer shall:

(a) Monitor the ~~FINRA member broker-dealer~~relevant conduct of the financial professional seeking to rely on paragraph (1) or the entity responsible for supervising the financial professional, such as the financial professional's broker-dealer or an investment adviser registered under federal [or state] securities laws using information collected in the normal course of an insurer's business; and

(b) Provide to the ~~FINRA member broker-dealer~~entity responsible for supervising the financial professional seeking to rely on paragraph (1), such as the financial professional's broker-dealer or investment adviser registered under federal [or state] securities laws, information and reports that are reasonably appropriate to assist ~~the FINRA member broker-dealer~~such entity to maintain its supervision system.

(4) For purposes of this subsection, "financial professional" means a producer that is regulated and acting as:

(a) A broker-dealer registered under federal [or state] securities laws or a registered representative of a broker-dealer;

(b) An investment adviser registered under federal [or state] securities laws or an investment adviser representative associated with the federal [or state] registered investment adviser; or

(c) A plan fiduciary under Section 3(21) of the Employee Retirement Income Security Act of 1974 (ERISA) or fiduciary under Section 4975(e)(3) of the Internal Revenue Code (IRC) or any amendments or successor statutes thereto.

Drafting Note: The requirement that a producer be "regulated and acting" as a broker-dealer, an registered representative of a broker-dealer, an investment adviser, an investment adviser representative or a plan fiduciary means that a producer who is not explicitly acting in compliance with the relevant comparable standards, as specified in paragraph (4) below, is not eligible for this safe harbor and is subject to compliance with the requirements of this regulation.

(5) For purposes of this subsection, "comparable standards" means:

(a) With respect to broker-dealers and registered representatives of broker-dealers, applicable SEC and FINRA rules pertaining to best interest obligations and supervision of annuity recommendations and sales, including, but not limited to, Regulation Best Interest and any amendments or successor regulations thereto;

(b) With respect to investment advisers registered under federal [or state] securities laws or investment adviser representatives, the fiduciary duties and all other requirements imposed on such investment advisers or investment adviser representatives by contract or under the Investment Advisers Act of 1940 [or applicable state securities law], including but not limited to, the Form ADV and interpretations; and

Drafting Note: State-registered investment advisers in this safe harbor are included in brackets so that each individual state that implements this model regulation may determine whether to include the state-regulated investment advisers. Given the varying treatment of annuities, particularly variable annuities, under state law, the varying structures of state securities and insurance departments, and the varying levels of cooperation between the two agencies, this is a decision best made in each individual state.

(c) With respect to plan fiduciaries or fiduciaries, means the duties, obligations, prohibitions and all other requirements attendant to such status under ERISA or the IRC and any amendments or successor statutes thereto.

Section 7. ~~Insurance~~ Producer Training

A. ~~An insurance~~A producer shall not solicit the sale of an annuity product unless the ~~insurance~~ producer has adequate knowledge of the product to recommend the annuity and the ~~insurance~~ producer is in compliance with the insurer's standards for product training. ~~An insurance~~A producer may rely on insurer-provided product-specific training standards and materials to comply with this subsection.

B. (1) (a) ~~An insurance~~ A producer who engages in the sale of annuity products shall complete a one-time four (4) credit training course approved by the department of insurance and provided by the department of insurance-approved education provider.

(b) ~~Insurance p~~Producers who hold a life insurance line of authority on the effective date of this regulation and who desire to sell annuities shall complete the requirements of this subsection within six (6) months after the effective date of this regulation. Individuals who obtain a life insurance line of authority on or after the effective date of this regulation may not engage in the sale of annuities until the annuity training course required under this subsection has been completed.

(2) The minimum length of the training required under this subsection shall be sufficient to qualify for at least four (4) CE credits~~,~~ but may be longer.

(3) The training required under this subsection shall include information on the following topics:

(a) The types of annuities and various classifications of annuities;

(b) Identification of the parties to an annuity;

(c) How product specific annuity contract features affect consumers;

(d) The application of income taxation of qualified and non-qualified annuities;

(e) The primary uses of annuities; and

(f) Appropriate standard of conduct, sales practices, replacement and disclosure requirements.

(4) Providers of courses intended to comply with this subsection shall cover all topics listed in the prescribed outline and shall not present any marketing information or provide training on sales techniques or provide specific information about a particular insurer's products. Additional topics may be offered in conjunction with and in addition to the required outline.

(5) A provider of an annuity training course intended to comply with this subsection shall register as a CE provider in this State and comply with the rules and guidelines applicable to ~~insurance~~ producer continuing education courses as set forth in [insert reference to State law or regulations governing producer continuing education course approval].

(6) A producer who has completed an annuity training course approved by the department of insurance prior to [insert effective date of amended regulation] shall, within six (6) months after [insert effective date of amended regulation], complete either:

(a) A new four (4) credit training course approved by the department of insurance after [insert effective date of amended regulation]; or

(b) An additional one-time one (1) credit training course approved by the department of insurance and provided by the department of insurance-approved education provider on appropriate sales practices, replacement and disclosure requirements under this amended regulation.

~~(6)~~(7) Annuity training courses may be conducted and completed by classroom or self-study methods in accordance with [insert reference to State law or regulations governing producer continuing education course approval].

~~(7)~~(8) Providers of annuity training shall comply with the reporting requirements and shall issue certificates of completion in accordance with [insert reference to State law or regulations governing to producer continuing education course approval].

~~(8)~~(9) The satisfaction of the training requirements of another State that are substantially similar to the provisions of this subsection shall be deemed to satisfy the training requirements of this subsection in this State.

(10) The satisfaction of the components of the training requirements of any course or courses with components substantially similar to the provisions of this subsection shall be deemed to satisfy the training requirements of this subsection in this state.

~~(9)~~(11) An insurer shall verify that ~~an insurance~~a producer has completed the annuity training course required under this subsection before allowing the producer to sell an annuity product for that insurer. An insurer may satisfy its responsibility under this subsection by obtaining certificates of completion of the training course or obtaining reports provided by commissioner-sponsored

database systems or vendors or from a reasonably reliable commercial database vendor that has a reporting arrangement with approved insurance education providers.

Section 8. Compliance Mitigation; Penalties; Enforcement

A. An insurer is responsible for compliance with this regulation. If a violation occurs, either because of the action or inaction of the insurer or its ~~insurance~~ producer, the commissioner may order:

(1) An insurer to take reasonably appropriate corrective action for any consumer harmed by a failure to comply with this regulation by the ~~insurer's~~insurer, an entity contracted to perform the insurer's supervisory duties or by ~~its insurance producer's, violation of this regulation~~the producer;

(2) A general agency, independent agency or the ~~insurance~~ producer to take reasonably appropriate corrective action for any consumer harmed by the ~~insurance~~ producer's violation of this regulation; and

(3) Appropriate penalties and sanctions.

B. Any applicable penalty under [insert statutory citation] for a violation of this regulation may be reduced or eliminated [, according to a schedule adopted by the commissioner,] if corrective action for the consumer was taken promptly after a violation was discovered or the violation was not part of a pattern or practice.

Drafting Note: Subsection B above is intended to be consistent with the commissioner's discretionary authority to determine the appropriate penalty for a violation of this regulation. The language of subsection B is not intended to require that a commissioner impose a penalty on an insurer for a single violation of this regulation if the commissioner has determined that such a penalty is not appropriate.

Drafting Note: A State that has authority to adopt a schedule of penalties may wish to include the words in brackets. In that case, "shall" should be substituted for "may" in the same sentence. States should consider inserting a reference to the NAIC Unfair Trade Practices Act or the State's statute that authorizes the commissioner to impose penalties and fines.

C. The authority to enforce compliance with this regulation is vested exclusively with the commissioner.

Section 9. ~~[Optional]~~ Recordkeeping

A. Insurers, general agents, independent agencies and ~~insurance~~ producers shall maintain or be able to make available to the commissioner records of the information collected from the consumer, disclosures made to the consumer, including summaries of oral disclosures, and other information used in making the recommendations that were the basis for insurance transactions for [insert number] years after the insurance transaction is completed by the insurer. An insurer is permitted, but shall not be required, to maintain documentation on behalf of ~~an insurance~~a producer.

Drafting Note: States should review their current record retention laws and specify a time period that is consistent with those laws. For some States this time period may be five (5) years.

B. Records required to be maintained by this regulation may be maintained in paper, photographic, micro-process, magnetic, mechanical or electronic media or by any process that accurately reproduces the actual document.

Drafting Note: This section may be unnecessary in States that have a comprehensive recordkeeping law or regulation.

Section 10. Effective Date

The amendments to this regulation shall take effect [~~six (6)~~X] months after the date the regulation is adopted or on [insert date], whichever is later.

APPENDIX A

INSURANCE AGENT (PRODUCER) DISCLOSURE FOR ANNUITIES

Do Not Sign Unless You Have Read and Understand the Information in this Form

Date: _____

INSURANCE AGENT (PRODUCER) INFORMATION ("Me", "I", "My")

First Name: _____ Last Name: _____

Business\Agency Name: _____ Website: _____

Business Mailing Address: _____

Business Telephone Number: _____

Email Address: _____

National Producer Number in [state]: _____

CUSTOMER INFORMATION ("You", "Your")

First Name: _____ Last Name: _____

What Types of Products Can I Sell You?

I am licensed to sell annuities to you in accordance with state law. If I recommend that You buy an annuity, it means I believe that it effectively meets Your financial situation, insurance needs, and financial objectives. Other financial products, such as life insurance or stocks, bonds and mutual funds, also may meet Your needs.

I offer the following products:

- ☐ Fixed or Fixed Indexed Annuities
- ☐ Variable Annuities
- ☐ Life Insurance

I need a separate license to provide advice about or to sell non-insurance financial products. I have checked below any non-insurance financial products that I am licensed and authorized to provide advice about or to sell.

- ☐ Mutual Funds
- ☐ Stocks/Bonds
- ☐ Certificates of Deposits

Whose Annuities Can I Sell to You?

I am authorized to sell:

☐ Annuities from Only One (1) Insurer	☐ Annuities from Two or More Insurers
☐ Annuities from Two or More Insurers although I primarily sell annuities from: _____	

How I'm Paid for My Work:

It's important for You to understand how I'm paid for my work. Depending on the particular annuity You purchase, I may be paid a commission or a fee. Commissions are generally paid to Me by the insurance company while fees are generally paid to Me by the consumer. If You have questions about how I'm paid, please ask Me.

Depending on the particular annuity You buy, I will or may be paid cash compensation as follows:

- ☐ Commission, which is usually paid by the insurance company or other sources. If other sources, describe: _____.
- ☐ Fees (such as a fixed amount, an hourly rate, or a percentage of your payment), which are usually paid directly by the customer.
- ☐ Other (Describe): _____.

If you have questions about the above compensation I will be paid for this transaction, please ask me.

I may also receive other indirect compensation resulting from this transaction (sometimes called "non-cash" compensation), such as health or retirement benefits, office rent and support, or other incentives from the insurance company or other sources.

***Drafting Note**: This disclosure may be adapted to fit the particular business model of the producer. As an example, if the producer only receives commission or only receives a fee from the consumer, the disclosure may be refined to fit that particular situation. This form is intended to provide an example of how to communicate producer compensation, but compliance with the regulation may also be achieved with more precise disclosure, including a written consulting, advising or financial planning agreement.*

***Drafting Note:** The acknowledgement and signature should be in immediate proximity to the disclosure language.*

By signing below, you acknowledge that you have read and understand the information provided to you in this document.

_____
Customer Signature

_____
Date

_____
Agent (Producer) Signature

_____
Date

APPENDIX B

CONSUMER REFUSAL TO PROVIDE INFORMATION

Do Not Sign Unless You Have Read and Understand the Information in this Form

Why are you being given this form?

You're buying a financial product – an annuity.

To recommend a product that effectively meets your needs, objectives and situation, the agent, broker, or company needs information about you, your financial situation, insurance needs and financial objectives.

If you sign this form, it means you have not given the agent, broker, or company some or all the information needed to decide if the annuity effectively meets your needs, objectives and situation. You may lose protections under the Insurance Code of [this state] if you sign this form or provide inaccurate information.

Statement of Purchaser:

☐ I **REFUSE** to provide this information at this time.

☐ I have chosen to provide LIMITED information at this time.

_____
Customer Signature

_____
Date

APPENDIX C

Consumer Decision to Purchase an Annuity NOT Based on a Recommendation

Do Not Sign This Form Unless You Have Read and Understand It.

Why are you being given this form? You are buying a financial product – an annuity.

To recommend a product that effectively meets your needs, objectives and situation, the agent, broker, or company has the responsibility to learn about you, your financial situation, insurance needs and financial objectives.

If you sign this form, it means you know that you're buying an annuity that was not recommended.

Statement of Purchaser:

I understand that I am buying an annuity, but the agent, broker or company did not recommend that I buy it. If I buy it **without a recommendation,** I understand I may lose protections under the Insurance Code of [this state].

_____
Customer Signature

_____
Date

_____
Agent/Producer Signature

_____
Date

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Project History

SUITABILITY IN ANNUITY TRANSACTIONS MODEL REGULATION (#275)

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

In 2017, the Life Insurance and Annuities (A) Committee established the Annuity Suitability (A) Working Group and charged the Working Group to review and revise, as necessary, the *Suitability in Annuity Transactions Model Regulation* (#275) and as part of that charge, consider how to promote greater uniformity across NAIC-member jurisdictions. The Committee adopted the charge and established the Working Group, in part, in response to the U.S. Department of Labor's (DOL) fiduciary rule, which was finalized in April 2016 but vacated in its entirety in March 2018. The DOL fiduciary rule would have expanded the scope of who is considered a fiduciary to federal Employee Retirement Income Security Act of 1974 (ERISA) retirement plans and individual retirement accounts (IRAs) to include a broader set of insurance agents, insurance brokers and insurers. Separately, the U.S. Securities and Exchange Commission (SEC) released a proposed rule package in May 2018, which included Regulation Best Interest (Reg BI). The SEC finalized Reg BI in June 2019. The final Reg BI establishes a best interest standard of conduct for broker-dealers beyond the existing suitability obligation. The new standard of conduct requires a broker-dealer when making a recommendation of any securities transaction or investment strategy involving securities to a retail customer to act in the best interest of the retail customer at the time a recommendation is made without placing the financial or other interest of the broker-dealer or associated persons ahead of the interest of the retail customers.

While acknowledging the SEC's and the DOL's role in the regulatory landscape and believing that consumers are better protected when, to the extent possible, there is harmonization of the regulations enforced by the states, the SEC and the DOL, the Working Group continued its work to draft revisions to Model #275 to establish a framework for an enhanced standard of conduct that is more than the model's current suitability standard but not a fiduciary standard.

In 2018, the Working Group held two two-day interim meetings—one in June in Kansas City, MO, and one in October in Chicago—to discuss drafts of proposed revisions to Model #275. Additionally, the Working Group held several conference calls and additional in-person meetings at each national meeting.

After the SEC finalized its Reg BI in June 2019, as directed by the Life Insurance and Annuities (A) Committee at the 2019 Spring National Meeting, the Working Group met soon after in mid-June during an in-person interim meeting in Columbus, OH, to level set and work toward its goal of fleshing out the meaning of "best interest" and incorporating a best interest standard of conduct into the Model #275 revisions. During its June meeting, the Working Group discussed and agreed on a framework for the model revisions to include a best interest standard and a path forward for completing its work as soon as possible.

Based on this framework, the Working Group developed a draft of proposed model revisions including a best interest standard of care a producer or insurer can meet if the producer or insurer satisfies the four obligations under this standard of care: 1) the care obligation; 2) disclosure obligation; 3) material conflict of interest obligation; and 4) documentation obligation. The Working Group exposed the draft for public comment until Sept. 30, 2019.

The Working Group met Oct. 8, Oct. 15, Oct. 29 and Nov. 5, 2019, via conference call to discuss the comments received. The Working Group received comments from many stakeholders, including industry, consumers and producers. More than 100 interested parties and state insurance regulators participated in each of the conference calls. The Working Group adopted the proposed revisions to Model #275 on Nov. 5, 2019, via conference call. The Working Group agreed that it had completed its work as directed by the Life Insurance and Annuities (A) Committee during the 2019 Spring National Meeting and forwarded the draft to the Committee for its consideration. The Committee chair exposed the draft for a public comment period ending Nov. 26, 2019. At the 2019 Fall National Meeting, the Committee discussed the comments received and made some revisions to the Working Group's draft of proposed revisions to Model #275. During this meeting, the Committee provided preliminary approval to the proposed Model #275 revisions. The Committee also directed the Working Group to discuss the comments received on the proposed appendices during a meeting following the 2019 Fall National Meeting. The Working Group met Dec. 19, 2019, via conference call to discuss the Nov. 26, 2019, comments received on the proposed appendices. During this meeting, the Working Group revised the appendices and forwarded its work to the Committee for its consideration. The Committee met Dec. 30, 2019, via conference call to consider adoption of the proposed revisions to Model #275. The Committee adopted the proposed revisions to Model #275 by a vote of 11 to 1.

The proposed revisions establish a best interest standard of conduct for producers and insurers. This new standard of conduct is more than the model's current suitability standard, but it is not a fiduciary standard. Under this new standard of conduct, when making a recommendation of an annuity, a producer or insurer shall act in the best interest of the consumer under the circumstances known at the time the recommendation is made, without placing the producer's or the insurer's financial interest ahead of the consumer's financial interest. To satisfy this best interest obligation, a producer or an insurer must satisfy the four obligations: 1) care; 2) disclosure; 3) conflict of interest; and 4) documentation. The proposed revisions also revise the model's current insurer supervision requirements, including a new supervision requirement for the insurer to establish and maintain reasonable procedures to identify and eliminate certain sales incentives that are based on sales of specific annuities within a limited period of time. The proposed revisions also expand the model's current safe harbor provisions to apply the safe harbor to any financial professional in compliance with business rules, controls and procedures that satisfy a comparable standard, such as Reg BI, to the model's new standard of conduct. The proposed revisions define a financial professional to include a producer that is regulated and acting as: 1) a broker-dealer; 2) an investment adviser; or 3) a plan fiduciary. The proposed revisions also include new appendices to provide guidance to producers and insurers in satisfying the new disclosure and documentation obligations.

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

The Annuity Suitability (A) Working Group of the Life Insurance and Annuities (A) Committee drafted the proposed revisions to Model #275. The members of the Working Group were: Alabama, California, Delaware, Idaho, Iowa, Kansas, Nebraska, New Hampshire, New York, Ohio, Oklahoma, Rhode Island, Tennessee and Wisconsin. Idaho chaired the Working Group in 2017 and 2018, and Ohio chaired the Working Group in 2019. The Life Insurance and Annuities (A) Committee also discussed and drafted proposed revisions to Model #275 after the Working Group completed its work. The members of the Committee were: Alabama, Arizona, Delaware, District of Columbia, Idaho, Iowa, Louisiana, Nebraska, Nevada, New York, North Dakota, Ohio, Puerto Rico, Tennessee and Wisconsin.

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

The Life Insurance and Annuities (A) Committee established the Annuity Suitability (A) Working Group in 2017 to carry out the charge below:

"Review and revise, as necessary, the *Suitability in Annuity Transactions Model Regulation* (#275) and consider how to promote greater uniformity across NAIC-member jurisdictions."

4. A General Description of the Drafting Process (e.g., drafted by a subgroup, interested parties, the full group, etc.; include any parties outside the members that participated)

Beginning in March 2017 and ending in December 2019, the Working Group reviewed and discussed all of the comments received as part of the drafting process. Numerous interested parties participated in the process. The interested parties represented all stakeholder groups, including consumers, insurers and producer representatives. Each draft of proposed revisions was posted to the Working Group's web page and the Committee's web page on the NAIC website. All comment letters received also were posted. The Working Group held open in-person interim meetings and met via conference call during the drafting process. The Working Group also met in person at each NAIC national meeting.

5. A General Description of the Due Process (e.g., exposure periods, public hearings or any other means by which widespread input from industry, consumers and legislators was solicited)

Beginning in March 2017 and ending in December 2019, the Working Group reviewed and discussed all of the comments received. Numerous interested parties participated in the drafting process. The interested parties represented all stakeholder groups, including consumers, insurers and producer representatives. Each draft of proposed revisions was posted to the Working Group's web page and the Committee's web page on the NAIC website. All comment letters received also were posted. The Working Group held open in-person interim meetings and met via conference call during the drafting process. The Working Group also met in person at each NAIC national meeting.

6. A Discussion of the Significant Issues (items of some controversy raised during the drafting process and the group's response)

Several significant issues were raised throughout the drafting process. Those issues included: 1) expanding Model #275 to include investment-type life insurance products; 2) specifically applying the proposed revisions to in-force annuity products; 3) applying the proposed revisions to producers who may not have direct contact with the consumer, but participated in a material way to developing and making the recommendation purchase an annuity; and 4) including the drafting note stating that the proposed model revisions are a successor to the 2010 model revisions.

With respect to expanding Model #275 to include investment-type life insurance products, the Working Group discussed this issue during one of its first in-person interim meetings. The Working Group decided that given its charge to "review and revise, as necessary, the *Suitability in Annuity Transactions Model Regulation* (#275) and consider how to promote greater uniformity across NAIC-member jurisdictions," expanding Model #275 to include investment-type life insurance products was beyond the scope of its charge. The Working Group concluded that the Life Insurance and Annuities (A) Committee was the appropriate forum for raising and considering this issue.

Another significant issue discussed was whether the model revisions should specifically apply to in-force annuity contracts. The Working Group discussed this issue extensively during multiple meetings. It decided ultimately not to include language in the proposed revisions specifically applying to in-force annuity contracts. However, during these discussions, it was suggested that in certain situations, in making a recommendation, a producer or insurer would have to and would be expected to consider a consumer's existing insurance products, including annuities, to determine whether the recommended option effectively addresses the consumer's financial situation, insurance needs and financial objectives as part of satisfying the best interest standard of conduct.

The Working Group also extensively discussed whether the model revisions should apply to producers not having direct contact with a consumer, but exercised material control or influence in the making of the recommendation. The Working Group decided to add language applying the model revisions to such producers under certain circumstances. Specifically, in Section 6A(5), the model revisions provide that any requirement applicable to a producer under Section 6—Duties of Insurers and Producers applies to every producer who has exercised material control or influence in the making of a recommendation and has received direct compensation as a result of the recommendation or sale regardless of whether the producer has had any direct contact with the consumer.

Another issue the Working Group discussed was whether the revised model establishing the new best interest standard of conduct would be considered for purposes of Section 989J of the federal Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act) a successor to the 2010 model revisions, which established the suitability standard of conduct. The proposed revisions include a drafting note in Section 1—Purpose expressly stating the proposed revisions are a successor to the 2010 model revisions. The Working Group deferred the issue to the NAIC Legal Division for additional research. The NAIC Legal Division did not expressly provide an opinion, but initial research found that with or without the Section 1 drafting note, the revised model most likely would be considered a successor to the 2010 model. The Working Group determined that this was a policy issue for the Committee, the Executive (EX) Committee and Plenary to decide. The model revisions, as adopted by the Committee, retain the proposed drafting note.

7. Any Other Important Information (e.g., amending an accreditation standard)

None.

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Adopted by the Life Actuarial (A) Task Force, February 20, 2020
Adopted by the Life Insurance and Annuities (A) Committee, July 10, 2020

Actuarial Guideline XLVIII
(*Applies to 2017 and Subsequent Year Valuations)*

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)

Background

The NAIC Principle-Based Reserving Implementation (EX) Task Force ("PBRI Task Force") serves as the coordinating body for all NAIC technical groups involved with projects related to the Principle-Based Reserves (PBR) initiative for life and health policies. The PBRI Task Force was also charged with further assessing, and making recommendations regarding, the solvency implications of life insurance reserve financing mechanisms addressed in the June 6, 2013 NAIC White Paper of the Captives and Special Purpose Vehicle Use (E) Subgroup of the Financial Condition (E) Committee. Some of these reinsurance arrangements have been referred to as "XXX/AXXX Captive arrangements," although not all such arrangements actually involve reinsurers organized as captives. In this connotation, XXX denotes the reserves prescribed by Section 6 of the NAIC *Valuation of Life Insurance Policies Model Regulation* (Model #830) while AXXX denotes the reserves prescribed by Section 7 of Model #830, and by *Actuarial Guideline XXXVIII—The Application of the Valuation of Life Insurance Policies Model Regulation* (AG 38). On June 30, 2014, the PBRI Task Force adopted a framework as found in Exhibits 1 and 2 of the June 4, 2014 report from Rector & Associates, Inc. (the "June 2014 Rector Report"). Exhibit 2 of the report included a charge to the Life Actuarial (A) Task Force (LATF) to develop a level of reserves (the "Required Level of Primary Security") that must be supported by certain defined assets ("Primary Security"). The level of reserves is to be calculated by a method referred to as the "Actuarial Method." Another charge to LATF was to promulgate an actuarial guideline specifying that, in order to comply with the NAIC *Actuarial Opinion and Memorandum Regulation*, Model 822 ("AOMR") as it relates to XXX/AXXX reinsurance arrangements, the opining actuary must issue a qualified opinion as to the ceding insurer's reserves if the ceding insurer or any insurer in its holding company system has engaged in a XXX/AXXX reserve financing arrangement that does not adhere to the Actuarial Method and Primary Security forms adopted by the NAIC. The initial version of *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) was developed in response to that charge, with an effective date of January 1, 2015.

Coordination between this Actuarial Guideline and the NAIC Term and Universal Life Insurance Reserve Financing Model Regulation (Model #787)

Subsequently, on January 8, 2016, the NAIC adopted revisions to the *Credit for Reinsurance Model Law* (Model #785). Among other things, the revisions to Model #785 provide commissioners with the authority to enact, by regulation, additional requirements for ceding insurers to claim credit for reinsurance with respect to certain XXX/AXXX financing arrangements. On December 13, 2016, the NAIC adopted the *Term and Universal Life Insurance Reserve Financing Model Regulation* (Model #787) as the regulation permitted by Model #785. LATF subsequently received a charge to redraft AG 48 to make it as consistent as possible with the provisions of Model #787. The current version of this actuarial guideline is the result.

The following is an overview of the interrelationship between this actuarial guideline and Model #787, and the regulatory strategy that led to the adoption of each:

1. The initial version of this actuarial guideline immediately established national standards for the use of XXX/AXXX financing arrangements in an attempt to quickly set minimum standards based on the framework adopted by the PBRI Task Force on June 30, 2014. This initial version applied to such reinsurance arrangements entered into on or after 1/1/2015.

2. The revised statute (the NAIC *Credit for Reinsurance Model Law* (Model #785)) and a new regulation (the NAIC *Term and Universal Life Insurance Reserve Financing Model Regulation* (Model #787)) were then developed and adopted by the NAIC.

3. Except as noted in #4 below, this actuarial guideline will cease to be effective, on a state by state basis, as individual states enact Model #785 and adopt Model #787 to replace it.

4. Notwithstanding, it is anticipated that in a small number of states, Model #787 will need to be adopted on a "prospective" basis only (that is, it will only apply to ceded policies issued on or after the effective date thereof). In those cases, this actuarial guideline will remain as the authority for ceded policies subject to this actuarial guideline but to which Model #787, as adopted in a given state, does not apply. So although its role might diminish, this actuarial guideline will remain an essential part of the regulatory framework for a small number of states for many years to come.

5. To ensure uniformity of treatment between states, companies, and ceded policies (whether governed by this actuarial guideline or by Model #787) and to avoid confusion, this actuarial guideline is being updated, effective as of January 1, 2017, to make it as substantively identical to Model #787 as possible.

Authority, Avoidance, and Purpose

The requirements in this actuarial guideline derive authority from Section 3 of the AOMR, or, after the Operative Date of the *Valuation Manual*, from Section 1 of VM-30 of the *Valuation Manual*. Both Section 3 of the AOMR and Section 1 of VM-30 provide that the commissioner has the authority to specify specific methods of actuarial analysis and actuarial assumptions when, in the commissioner's judgment, these specifications are necessary for an acceptable opinion to be rendered relative to the adequacy of reserves and related items. As contained in the framework adopted by the PBRI Task Force on June 30, 2014, this actuarial guideline defines new terms, such as Primary Security and Required Level of Primary Security, specifies the Actuarial Method used to calculate the Required Level of Primary Security, and specifies other requirements that must be followed when reinsurance is involved in order for the appointed actuary to render an actuarial opinion that is not qualified.

No statute, regulation or guideline can anticipate every potential XXX/AXXX captive arrangement. Common sense and professional responsibility are needed to assure not only that the text of this actuarial guideline is strictly observed, but also that its purpose and intent are honored scrupulously. To that end, and to provide documentation to the appointed actuary as to the arrangements that are subject to review under this actuarial guideline, the appointed actuary may request from each ceding insurer, and may rely upon, the certification by the Chief Financial Officer or other responsible officer of each ceding insurer filed with the insurer's domiciliary regulator that the insurer has not engaged in any arrangement or series of arrangements involving XXX or AXXX reserves that are designed to exploit a perceived ambiguity in, or to violate the purpose and intent of, this actuarial guideline.

The purpose and intent of this actuarial guideline is to establish uniform, national standards governing XXX or AXXX reserve financing arrangements[1] in conformity with the PBRI Task Force framework and, in connection with such arrangements, to ensure that Primary Security, in an amount at least equal to the Required Level of Primary Security, is held by or on behalf of the ceding insurer. As described further in Section 4.B., the provisions of this actuarial guideline are not intended to apply to policies that were issued prior to 1/1/2015 if those policies were included in a captive reserve financing arrangement as of 12/31/2014. Further, the requirements of this actuarial guideline should be viewed as minimum standards and are not a substitute for the diligent analysis of reserve financing arrangements by regulators. A regulator should impose requirements in addition to those set out in this actuarial guideline if the facts and circumstances warrant such action.

Text

1. Authority

Pursuant to Section 3 of the AOMR or, after the Operative Date of the *Valuation Manual*, to Section 1 of VM-30 of the *Valuation Manual*, the commissioner shall have the authority to specify specific methods of actuarial analysis and

[1] In general, reserve financing arrangements are those where the security/assets backing part or all of the reserves have one or more of the following characteristics: such security/assets (1) are issued by the ceding insurer or its affiliates; and/or (2) are not unconditionally available to satisfy the general account obligations of the ceding insurer; and/or (3) create a reimbursement, indemnification or other similar obligation on the part of the ceding insurer or any if 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 arrangement).

actuarial assumptions when, in the commissioner's judgment, these specifications are necessary for an acceptable opinion to be rendered relative to the adequacy of reserves and related items.

2. Scope

This actuarial guideline applies to reinsurance contracts that cede liabilities pertaining to Covered Policies as that term is defined in Section 4.

3. Exemptions

This actuarial guideline 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 Section 6F or Section 6G of Model #830; and which are issued before the later of:

(a) The effective date of Model #787 in the state of domicile of the ceding insurer, 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 January 1, 2020;

(2) Portions of policies that satisfy the criteria for exemption set forth in Section 6E of Model #830 and which are issued before the later of:

(a) The effective date of Model #787 in the state of domicile of the ceding insurer, 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 January 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 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; or

(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; or

B. Reinsurance ceded to an assuming insurer that meets the applicable requirements of Section 2D of Model #785; or

C. Reinsurance ceded to an assuming insurer that meets the applicable requirements of Sections 2A, 2B or 2C, of Model #785, 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—Accounting Policies, Risks & Uncertainties and Other Disclosures* ("SSAP No. 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 the NAIC *Risk-Based Capital (RBC) for Insurers Model Act* (Model #312) 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 Sections 2A, 2B or 2C, of Model #785, and that, in addition:

(1) Is not an affiliate, as that term is defined in Section 1A of the NAIC *Insurance Holding Company System Regulatory Model Act* (Model #440), 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 Model #312 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~~ Section 5B(4)~~(a)~~ of Model #785~~, pertaining to certain certified reinsurers or Section 5B(4)(b) of Model #785, pertaining to reinsurers meeting certain threshold size and licensing requirements~~; or

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 actuarial guideline (as described in the Authority, Avoidance and Purpose section above);

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

(3) The application of this actuarial guideline to those risks is not necessary to provide appropriate protection to policyholders. The commissioner shall publicly disclose any decision made pursuant

to this Section 3F to exempt a reinsurance treaty from this actuarial guideline, as well as the general basis therefor (including a summary description of the treaty).

Drafting Note: *The exemption set forth in Section 3F 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 actuarial guideline 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 3A, B, C, D, or E or meet the substantive requirements of this actuarial guideline.*

4. Definitions

A. "Actuarial Method" means the methodology used to determine the Required Level of Primary Security, as described in Section 5.

B. "Covered Policies" means the following: Subject to the exemptions described in Section 3, 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.

Note*: Although "Covered Policies" is defined to include all the policies described in Subsections B1 and B2 above, it is noted that whether a given "Covered Policy" is subject to this actuarial guideline or, instead, to Model #787 should be determined under Section 8 (Sunset).*

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 3 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 Section 3A of Model #785;

(2) Securities listed by the Securities Valuation Office meeting the requirements of Section 3B of Model #785, 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.

I. "VM-20" means "Requirements for Principle-Based Reserves for Life Products," including all relevant definitions, from the *Valuation Manual*.

5. The Actuarial Method

A. Description of Actuarial Method

The Actuarial Method to establish the Required Level of Primary Security for each reinsurance treaty subject to this actuarial guideline 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 4B(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 4B(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. The mortality basis for the NPR shall be the 2017 CSO Mortality Table.

(2) For Covered Policies described in Section 4B(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. The mortality basis for the NPR shall be the 2017 CSO Mortality Table.

(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 reduced by the amount resulting by applying the Actuarial Method including the reinsurance section of VM-20 to the portion of the Covered Policy risks ceded in the exempt arrangement, except that for Covered Policies issued prior to Jan 1, 2017, this adjustment is not to exceed [c_x/ (2 * number of reinsurance premiums per year)] where c_x is calculated using the same mortality table used in calculating the Net Premium Reserve; and

(d) 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 actuarial guideline, 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 actuarial guideline.

(7) If a reinsurance treaty subject to this actuarial guideline cedes risk on both Covered and Non-Covered Policies:

(a) The Actuarial Method shall be used to determine the Required Level of Primary Security for the Covered Policies; and

(b) Any Primary Security and/or Other Security used to meet any requirements pertaining to the Non-Covered Policies may not be used to satisfy any requirements related to the Required Level of Primary Security and/or Other 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 NAIC's Life Actuarial (A) Task Force no later than the December 31 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. Required Actuarial Analysis and Actuarial Opinion and Memorandum Requirements

A. Required Actuarial Analysis

Before the due date of each actuarial opinion, as to each reinsurance treaty in which Covered Policies have been ceded, the appointed actuary of each ceding insurer must perform an analysis on a treaty by treaty basis, of such Covered Policies to determine whether, as of the immediately preceding December 31 (the valuation date):

(1) 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 Section 3 of Model #785, on a funds withheld, trust, or modified coinsurance basis; and

(2) 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 (1) above, are held by or on behalf of the ceding insurer as security under the reinsurance treaty within the meaning of Section 3 of Model #785; and

***Note**: For the sake of clarity, funds consisting of Primary Security pursuant to Paragraphs (1) may exceed the Required Level of Primary Security, and Other Security is only required under Paragraph (2) to the extent that there is any portion of the statutory reserves as to which Primary Security is not so held. For example, if a ceding insurer's statutory reserves equal $1 Billion, its Required Level of Primary Security is $600 Million, and it holds $1 Billion in Primary Security pursuant to Paragraph (1), no Other Security is required under Paragraph (2).*

(3) Any trust used to satisfy the requirements of this Section 6 complies with all of the conditions and qualifications of Section 12~~11~~ of the NAIC *Credit for Reinsurance Model Regulation* (Model #786), except that:

(a) Funds consisting of Primary Security or Other Security held in trust, shall for the purposes identified in Section 5B, be valued according to the valuation rules set forth in Section 5B, 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 6A(1); 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 6A(1)) below 102% of the level required by Section 6A(1) at the time of the withdrawal or substitution.

B. Qualified Actuarial Opinion; Remediation

(1) The appointed actuary of the ceding insurer performing the analysis required by Section 6A above must issue a qualified actuarial opinion as described in Section 6.D. of the AOMR or Section 3A(10) of VM-30 of the *Valuation Manual*, as applicable, unless:

(a) The requirements of Section 6A(1) and 6(A)(2) 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 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 6A(1) and 6A(2) to be fully satisfied as of the valuation date; or

(c) The ceding insurer has established a liability equal to the excess of the credit for reinsurance taken over the amount of Primary Security actually held pursuant to Section 6A(1).

(2) In addition to the requirement set forth in Section 6B(1) above, the appointed actuary of the ceding insurer performing the analysis required by Section 6A above must issue a qualified actuarial option as described in Section 6.D. of the AOMR or Section 3A(10) of VM-30 of the *Valuation Manual*, as applicable, if the appointed actuary for any affiliated reinsurer of the ceding insurer issues a qualified actuarial opinion with respect to such affiliated reinsurer where (a) the affiliate reinsures Covered Policies of the ceding insurer and (b) the qualified actuarial opinion pertaining to the affiliated reinsurer results, in whole or in part, from the analysis required by this actuarial guideline.

Note*: The remediation option set forth in Section 6B(1)(c) mirrors that set forth in Model #787. Under this option, a ceding company may choose to avoid the consequence (a qualified opinion under this actuarial guideline) by establishing a liability equal to the excess of the credit for reinsurance taken over the amount of Primary Security actually held. For example, suppose a ceding insurer has established statutory reserves of $1 Billion and has Primary Security of $550 Million and Other Security of $450 Million. Suppose further that the actuary determines that the insurer's Required Level of Primary Security is $600 Million. Under Section 6B(1)(c), the insurer may avoid a qualified opinion by establishing a liability equal to $450 Million (the difference between the statutory reserve of $1 Billion and the $550 Million amount of Primary Security actually held).*

C. Additional Requirements for the Actuarial Opinion and Memorandum for Companies that have Covered Policies Requiring the Analysis Pursuant to this actuarial guideline

(1) In the statement of actuarial opinion, the appointed actuary of the ceding insurer must state whether (i) he has performed an analysis, as to each reinsurance arrangement under which Covered Policies have been ceded, of the security supporting the Covered Policies and whether 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 contract, on a funds withheld, trust, or modified coinsurance basis and (ii) funds consisting of Primary Security or Other Security in an amount equal to the statutory reserves are held by or on behalf of the ceding insurer as security under the reinsurance arrangement.

(2) In the actuarial memorandum as described by Section 7 of the AOMR or Section 3B of VM-30 of the *Valuation Manual*, as applicable, the appointed actuary of the ceding insurer must document the analysis and requirements applied by this actuarial guideline as to each reinsurance arrangement under which Covered Policies are ceded.

(3) In the event that a reinsurance treaty contains both (1) Covered Policies subject to this actuarial guideline rather than to Model #787, and (2) Covered Policies subject to Model #787 rather than to this actuarial guideline, the treaty shall be tested as a whole for purposes of a ceding insurer's compliance with both (a) the requirements of Section 6A(1) and Section 6A(2) of this actuarial guideline and (b) the requirements of Section 7A(3) and Section 7A(4) of Model #787; provided further, that:

(a) If funds consisting of Primary Security are held in amounts less than the Required Level of Primary Security, such funds consisting of Primary Security shall be allocated first to fulfill the Required Level of Primary Security for the Covered Policies subject to this actuarial guideline, with any remainder allocated to those Covered Policies subject to Model #787; and

(b) If funds consisting of Other Security are held in amounts less than the requirements of Section 6A(2), such funds consisting of Other Security shall be allocated first to fulfill the Other Security requirements for the Covered Policies subject to this actuarial guideline, and any remainder shall be allocated to those Covered Policies subject to Model #787.

7. Effective Dat

This actuarial guideline shall become effective as of January 1, 2017 with respect to all Covered Policies. This actuarial guideline supersedes and replaces all previous versions thereof with respect to actuarial opinions rendered as to valuation periods ending on or after January 1, 2017.

***Note**: For the avoidance of doubt, actuarial opinions issued with respect to the year ended December 31, 2016, shall be governed by the version of AG 48 in effect on December 31, 2016, as included in the Accounting Practices and Procedures Manual.*

8. Sunset Provision

This actuarial guideline shall cease to apply as to Covered Policies that are both (a) issued by ceding insurers domiciled in a jurisdiction that has in effect, as of December 31st[t] of the calendar year immediately preceding the year in which the actuarial opinion is to be filed, a regulation substantially similar to Model #787 adopted by the NAIC on December 13, 2016; and (b) subject to Model #787 as so adopted by the ceding insurer's jurisdiction of domicile. This Actuarial Guideline shall continue to apply, without interruption, to any and all Covered Policies not included in both (a) and (b) of the immediate preceding sentence.

***Note**: It is anticipated that, for most states, this actuarial guideline will sunset pursuant to (a) and (b) of Section 8 and will continue only with respect to the limited number of states in which their version of Model #787 applies prospectively only, i.e., applies only to Covered Policies issued on or after the effective date of their version of Model #787. It is anticipated, however, that most states will be able to adopt a version of Model #787 that, like the Model itself, applies to all Covered Policies (subject to the applicable exemptions and grandfathering provisions) that are "in force" on or after the effective date, even if the policies were originally issued prior to that effective date. The goal of Section 8 is to ensure that **all** Covered Policies ceded in reinsurance transactions within the scope of this actuarial guideline continue to be subject to this actuarial guideline unless and until they become subject to Model #787.*

W:\National Meetings\2020\Summer\Plenary\Att 3 A_AG 48 with applicable 787 edits-af.pdf

Adopted by Life Insurance and Annuities(A) Committee, 7-9-20

Amendments for the 2021 Valuation Manual
for the Consideration of
Joint Meeting of the Executive (EX) Committee and Plenary
July 10, 2020

LATF VM Amendment	Valuation Manual Reference	Valuation Manual Amendment Proposal Descriptions	LATF Adoption Date
2019-58	Section A.1	Clarify that prescribed templates are subject to the VM governance requirements for substantive changes	5/21/20
2019-60	VM-20 Section 9.C.5.a, 9.C.7.b.ii	VM-20 restriction on using different credibility methods for significantly different blocks of business	2/6/20
2019-61	Section II, Subsection 1.D.3	The Life PBR Exemption restriction is intended to apply to ULSG with material secondary guarantees regardless of whether the secondary guarantee is an embedded guarantee or is a separate rider.	2/6/20
2019-62	VM-20 Sec 9.C.4 and VM-31 Sec 3.B.3, Sec 3.D.1.d, Sec 3.D.3, Sec 3.D.4 and Sec 3.D.8.a	Reserving for additional risk arising from term conversions	2/27/20
2020-05	VM-20 3.C.4	Clarify that the NPR assumes continuous deaths and immediate payment of claims, and does not apply to surrenders	6/11/20
2020-06	VM-20 Section 9.F.8.d., VM-31 Section 3.D.6	Guidance for replacement of LIBOR in swap spread determination	6/25/20
2020-07	VM-02 Section 3.A	Remove 4% Floor from Life Standard Nonforfeiture Rate	6/25/20

Att. 1

Life Actuarial (A) Task Force/ Health Actuarial (B) Task Force
Amendment Proposal Form

1. Identify yourself, your affiliation and a very brief description (title) of the issue.

   Staff of Office of Principle-Based Reserving, California Department of Insurance – Address the topic of prescribed templates.

2. Identify the document, including the date if the document is "released for comment," and the location in the document where the amendment is proposed:

   Valuation Manual (January 1, 2020 edition), Introduction, Section I, A.1

3. Show what changes are needed by providing a red-line version of the original verbiage with deletions and identify the verbiage to be deleted, inserted or changed by providing a red-line (turn on "track changes" in Word®) version of the verbiage. (You may do this through an attachment.)

   See attached

4. State the reason for the proposed amendment? (You may do this through an attachment.)

   See attached

NAIC Staff Comments:

Dates: Received	Reviewed by Staff	Distributed	Considered
APF 2019-58 (CA APF DN)			

Att. 1

ISSUE:

Now that the concept of a prescribed template has been introduced into VM-31, it should be made clear what the rules are surrounding making changes to such templates.

SECTIONS:

Introduction, Section I, Process for Updating the *Valuation Manual*, Section A.1

REDLINE:

1. Substantive Items

> Substantive changes to the *Valuation Manual* are proposed amendments to the *Valuation Manual* that would change or alter the meaning, application or interpretation of a provision. All changes to the *Valuation Manual* (or to templates prescribed for use by the *Valuation Manual*) will be considered substantive, unless specifically identified as either a nonsubstantive item or an update to a table by simple majority vote of the Life Actuarial (A) Task Force/Health Actuarial (B) Task Force. Any item placed on the Active List as substantive will be exposed by the Life Actuarial (A) Task Force/Health Actuarial (B) Task Force for a public comment period commensurate with the length of the draft and the complexities of the issue, but for no less than 21 days. The comment period will be deemed to have begun when the draft has been placed on the appropriate public NAIC web page. The Life Actuarial (A) Task Force/Health Actuarial (B) Task Force will hold at least one open meeting (in person or via conference call) to consider comments before holding a final vote on any substantive items. Subsequent exposures of substantive items will be for a minimum of seven days. Meeting notices for Life Actuarial (A) Task Force/Health Actuarial (B) Task Force meetings will indicate if a vote is anticipated on any substantive items. Adoption of all changes at the Life Actuarial (A) Task Force/Health Actuarial (B) Task Force will be by simple majority.

REASONING:

Help assure readers that there no back doors through which to create new requirements.

Life Actuarial (A) Task Force/ Health Actuarial (B) Task Force
Amendment Proposal Form*

1. Identify yourself, your affiliation and a very brief description (title) of the issue.

   Rachel Hemphill, Texas Department of Insurance
   Mary Bahna-Nolan, Pacific Life

   VM-20 restriction on using different credibility methods for significantly different blocks of business

2. Identify the document, including the date if the document is "released for comment," and the location in the document where the amendment is proposed:

   VM-20 Sections 9.C.5.a and 9.C.7.b.ii

   January 1, 2020 NAIC Valuation Manual

3. Show what changes are needed by providing a red-line version of the original verbiage with deletions and identify the verbiage to be deleted, inserted or changed by providing a red-line (turn on "track changes" in Word®) version of the verbiage. (You may do this through an attachment.)

   See attached.

4. State the reason for the proposed amendment? (You may do this through an attachment.)

   Currently, a company must select a single credibility methodology, Limited Fluctuation or Bühlmann, for all business that company has that is subject to VM-20 and requires credibility percentages. The Bühlmann methodology is technically allowed for Simplified Issue business within the Valuation Manual; however, at present, it is not practically possible since there are no industry factors available for Simplified Issue. Therefore, only the Limited Fluctuation method can currently be used for determining credibility for Simplified Issue business. The factors in VM-20 for the Bühlmann were developed to only be used in conjunction with the 2015 VBT. Thus, currently, a company with any Simplified Issue business subject to VM-20 that requires credibility calculations must use the Limited Fluctuation method for all of their business subject to VM-20 that requires credibility calculations, including the fully underwritten business. We do not see this as a reasonable restriction. VM-20 already requires that companies not change their credibility method once selected unless they receive commissioner approval for the change, and we believe that that constraint is sufficient to avoid any significant gaming of the credibility method selection.

NAIC Staff Comments:

Dates: Received	Reviewed by Staff	Distributed	Considered
11/6/19			
Notes: APF 2019-60			

VM-20 Section 9.C.5.a

5. Credibility of Company Experience

a. For valuations in which the industry basic mortality table is the 2008 VBT, determine an aggregate level of credibility over the entire exposure period using a methodology to determine the level of credibility that follows common actuarial practice as published in actuarial literature (for example, but not limited to, the Limited Fluctuation Method or Bühlmann Empirical Bayesian Method).

For valuations in which the industry basic mortality table is the 2015 VBT, determine an aggregate level of credibility following either the Limited Fluctuation Method by amount, such that the minimum probability is at least 95% with an error margin of no more than 5% or Bühlmann Empirical Bayesian Method by amount. ~~Once chosen, the credibility method must be applied to all business subject to VM20 and requiring credibility percentages.~~

Not all blocks of a company's business subject to VM-20 necessarily need to use the same credibility method. However, a~~A~~ company seeking to change the credibility method~~s~~ for a given block of business must request and subsequently receive the approval of the insurance commissioner. The request must include the justification for the change and a demonstration of the rationale supporting the change.

VM-20 Section 9.C.7.b.ii

7. Process to Determine Prudent Estimate Assumptions

a. If applicable industry basic tables are used in lieu of company experience as the anticipated experience assumptions, or if the level of credibility of the data as provided in Section 9.C.5 is less than 20%, the prudent estimate assumptions for each mortality segment shall equal the respective mortality rates in the applicable industry basic tables as provided in Section 9.C.3, including any applicable improvement pursuant to Section 9.C.3.g, plus the prescribed margin as provided in Section 9.C.6.c, plus any applicable additional margin pursuant to Section 9.C.6.d.v and/or Section 9.C.6.d.vi.

b. If the company uses company experience mortality rates as the anticipated experience assumptions, the following process shall be used to develop prudent estimate assumptions:

i. Determine the values of A, B and C from the Grading Table below, based on the level of credibility of the data as provided in Section 9.C.5.

Grading Table

Credibility of company data (as defined in Section 9.C.5 above) rounded to nearest %	A	B	C
20% - 30%	10	2	8
31%–32%	11	3	8
33%–34%	12	3	8
35%–36%	13	3	9
37%–38%	14	3	9
39%–40%	15	3	10
41%–42%	16	3	10
43%–44%	17	3	10
45%–46%	18	3	11
47%–48%	19	3	11
49%	20	3	11
50%	20	4	12
51%	21	4	12

52%–53%	22	4	12
54%	23	4	13
55%	24	4	13
56%	25	4	13
57%	25	5	13
58%	26	5	14
59%	27	5	14
60%–61%	28	5	14
62%	29	5	15
63%	30	6	15
64%–65%	31	6	15
66%	32	6	16
67%	33	6	16
68%–69%	34	6	16
70%	35	7	17
71%	36	7	17
72%	37	7	17
73%	38	7	18
74%	39	7	18
75%	40	7	18
76%	41	7	19
77%	42	8	19
78%	43	8	19
79%	44	8	20
80%	45	8	20
81%	46	8	20
82%	47	8	21
83%	48	9	21
84%	49	9	21
85%–87%	50	9	22
88%–89%	50	9	23
90%	50	10	23
91%–93%	50	10	24
94%–100%	50	10	25

ii. Determine the value of D, which represents the last policy duration that has a substantial volume of claims, using the chosen data source(s) as specified in Section 9.C.2.b. D is defined as the last policy duration at which there are 50 or more claims (not the first policy duration in which there are fewer than 50 claims), not counting riders. This may be determined at either the mortality segment level or at a more aggregate level if the mortality for the individual mortality segments was determined using an aggregate level of mortality experience pursuant to Section 9.C.2.d.

Guidance Note: The same level of aggregation is used in Section 9.C.2.d for determining company experience mortality rates, Section 9.C.5.b for determining credibility, and Section 9.C.7.b.ii for determining the value of D. Thus, when determining the value of D, all claims being aggregated will have used the same credibility method in Section 9.C.5.

Life Actuarial (A) Task Force/ Health Actuarial (B) Task Force
Amendment Proposal Form*

1. Identify yourself, your affiliation and a very brief description (title) of the issue.

   Identification:
   Rachel Hemphill, Texas Department of Insurance

   Title of the Issue:
   The Life PBR Exemption restriction is intended to apply to ULSG with material secondary guarantees regardless of whether the secondary guarantee is an embedded guarantee or is a separate rider.

2. Identify the document, including the date if the document is "released for comment," and the location in the document where the amendment is proposed:

   VM Section II, Subsection 1.D.3

   January 1, 2020 NAIC Valuation Manual

3. Show what changes are needed by providing a red-line version of the original verbiage with deletions and identify the verbiage to be deleted, inserted or changed by providing a red-line (turn on "track changes" in Word®) version of the verbiage. (You may do this through an attachment.)

   See attached.

4. State the reason for the proposed amendment? (You may do this through an attachment.)

   ULSG policies with material secondary guarantees are intended to be excluded from the Life PBR Exemption, regardless of whether the secondary guarantee is embedded in the base policy or is a separate rider. The VM does say that non-ULSG base policies with secondary guarantee riders follow the reserving requirements for ULSG policies in Section II, Subsection 6.C: "ULSG and other secondary guarantee riders shall be valued with the base policy and follow the reserve requirements for ULSG policies under VM-20, VM-A and/or VM-C, as applicable." It should be made clear that following the reserve requirements for ULSG includes exclusion from the Life PBR Exemption, when the secondary guarantee is material.

NAIC Staff Comments:

Dates: Received	Reviewed by Staff	Distributed	Considered
11/6/19			
Notes: APF 2019-61			

VM Section II, Subsection 1.D.3

3. Policies Excluded from the Life PBR Exemption:
a. Universal life with secondary guarantee (ULSG) policies with a secondary guarantee, or policies – other than ULSG – that contain a rider with a secondary guarantee, in which the secondary guarantee ~~that~~ does not meet the VM-01~~, Definitions for Terms in Requirements,~~ definition of a "non-material secondary guarantee."

Life Actuarial (A) Task Force/ Health Actuarial (B) Task Force
Amendment Proposal Form*

1. **Identify yourself, your affiliation and a very brief description (title) of the issue.**

   American Academy of Actuaries' Life Reserves Work Group.

2. **Identify the document, including the date if the document is "released for comment," and the location in the document where the amendment is proposed:**

   January 1, 2020, edition of the Valuation Manual with NAIC adoptions through August 6, 2019
   Locations with proposed changes : VM-20 and VM-31

3. **Show what changes are needed by providing a red-line version of the original verbiage with deletions and identify the verbiage to be deleted, inserted or changed by providing a red-line (turn on "track changes" in Word®) version of the verbiage. (You may do this through an attachment.):**

   See attached.

4. **State the reason for the proposed amendment? (You may do this through an attachment.)**

   The Valuation Manual already requires that if there is additional risk arising from the conversion of term life insurance, whether group or individual, it must be reserved for. The purpose of this APF is to emphasize this requirement and to provide guidance on what must be included in the Life PBR Actuarial Report with respect to conversions.

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* This form is not intended for minor corrections, such as formatting, grammar, cross–references or spelling. Those types of changes do not require action by the entire group and may be submitted via letter or email to the NAIC staff support person for the NAIC group where the document originated.

NAIC Staff Comments:

Dates: Received	Reviewed by Staff	Distributed	Considered
11/12/19			
Notes: VM APF 2019-62 rev.02-10-20; 14-day re-exposure through 2/26/20; Adopted 2/27/20			

VM-20 Section 9.C.4 - Add Section 9.C.4.d

c. The mortality rates from the resulting anticipated experience assumptions must be no lower than the mortality rates that are actually expected to emerge and that the company can justify.

d. In satisfying Section 9.C.4.c, the company must ensure that any excess mortality is appropriately reflected in the anticipated experience mortality rates. This includes but is not limited to excess mortality associated with policies issued via conversion from term policies or from group life contracts.

Exposure of the proposed section 9.C.4.c includes the following changes which have been reviewed and accepted by the Task Force:

VM-31 Section 3.B.3 [Executive Summary – policy overview]

3. Policies – A summary of the base policies within each VM-20 reserving category. Include information necessary to fully describe the company's distribution of business. For direct business, use PBR Actuarial Report Template A located on the NAIC website (https://www.naic.org/pbr_data.htm?tab_3) to provide descriptions of each base policy product type and underwriting process (including a description of the process, the time period in which it was used, and the level of any additional margin), with a breakdown of policy count and face amount by base policy product type and underwriting process. Also include the target market, primary distribution system, and key product features that affect risk, including conversion privileges.

VM-31 Section 3.D.1.d [Life Report – Assumptions and Margins]

d. Assumption and Margin Development – The following information for each risk factor: description of the methods used to determine anticipated experience assumptions and margins, including the sources of experience (e.g., company experience, industry experience, or other data); how changes in such experienceare monitored; any adjustments made to increase mortality margins above the prescribed margin (such as to reflect increased uncertainty ~~with~~ due to newer underwriting approaches; and any other considerations, such as conversion features, helpful in or necessary to understanding the rationale behind the development of assumptions and margins, even if such considerations are not explicitly mentioned in the Valuation Manual.

VM-31 Section 3.D.3.~~x~~ j(new section) [Life Report – Mortality]

(We suggest placing after Adjustments for Mortality Improvement and before Mortality for Impaired Lives)

j. Mortality for Converted Policies – Description of the treatment of mortality for Mortality policies issued under group or term conversion privileges including:

i. A description of the method(s) by which any excess conversion mortality was taken into account in the development of company experience mortality rates (e.g., through the use of separate mortality segments for policies issued upon conversion, through aggregation of claim experience, or through use of other methods), the rationale -for the method(s) used, and any changes in the method(s) from those used in previous years.

ii. The source(s) of the data used in the method(s) employed.

~~j~~k. Mortality for Impaired Lives or Policyholder Behavior – Disclosure of:

i. the percentage of business that is on impaired lives;

ii. whether impaired lives were included or excluded from the mortality study upon which company experience mortality was based; and

iii. whether any adjustments to mortality assumptions for impaired lives or policyholder behavior were found to be necessary and, if so, the rationale for the adjustments that were used.

Item (iii) above is a required disclosure for post-level term mortality assumptions even if the company uses a 100% shock lapse assumption, since it pertains to the analysis demonstrating whether there are post-level term profits.

VM-31 Section 3.D.4.~~x~~l and ~~y~~m (new sections) [Life Report – Policyholder Behavior]

k. Post-Level Term Testing – For products with a level term period:

i. Summary results of the seriatim comparison of the present value of postlevel term cash inflows and outflows for the DR as required by VM-20 Section 9.D.6.

ii. If this comparison showed that there were post-level term profits, describe how anti-selection was handled in the post-level term period, including the prudent estimate premium, mortality and lapse assumptions used.

iii. If the comparison showed that there were post-level term losses, confirm that the prudent estimate premium, mortality and lapse assumptions for the post-level period were addressed in Section 3.D.1.a and were used in the reserve calculation.

l. Term Conversions – Description of~~be~~ how the company reflects the impact of any term conversion~~s~~ privilege contained in the policy.

m. Lapse R~~r~~ates for Converted Policies – Description of and rationale for lapse rates used for policies issued under any group or term -conversion privilege.

VM-31 Section 3.D.8.a [Life Report – Reinsurance]

a. Agreements – For those reinsurance agreements included in the calculation of the minimum reserve as per VM-20 Section 8.A, a description of each reinsurance agreement, including, but not limited to, the type of agreement, the counterparty, the risks reinsured, any provisions related to converted policies, the portion of business reinsured, identification of both affiliated and non-affiliated, as well as captive and non-captive, or similar relationships, and whether the agreement complies with the requirements of the credit for reinsurance under the terms of the AP&P Manual.

Life Actuarial (A) Task Force/ Health Actuarial (B) Task Force
Amendment Proposal Form*

1. Identify yourself, your affiliation and a very brief description (title) of the issue.

   Jason Kehrberg, Vice President, PolySystems, Inc.

2. Identify the document, including the date if the document is "released for comment," and the location in the document where the amendment is proposed:

   VM-20 Section 3.C.4, 2020 Valuation Manual

3. Show what changes are needed by providing a red-line version of the original verbiage with deletions and identify the verbiage to be deleted, inserted or changed by providing a red-line (turn on "track changes" in Word®) version of the verbiage. (You may do this through an attachment.)

   Current VM-20 3.C.4 (per 2020 Valuation Manual):

   4. The NPR shall reflect the immediate payment of claims.

   Proposed VM-20 3.C.4 (revised):

   4. The NPR shall reflect continuous deaths and the immediate payment of death claims, including death claims on any riders or supplemental benefits for which the NPR is being calculated.

4. State the reason for the proposed amendment? (You may do this through an attachment.)

   I believe the intent was that 3.C.4 apply to death claims, e.g. not to payment of positive cash surrender values upon lapse, and that on a present value basis the calculated periodic death claim payments equate to immediate claim payment on deaths assumed to occur continuously.

NAIC Staff Comments:

Dates: Received	Reviewed by Staff	Distributed	Considered
3/30/20	RM		
Notes: VM APF 2020-05R			

Re-Exposure of APF 2020-06Updated 6/11/20 v.2
This version of APF is the same as the initial version exposed after the June 11 LATF call with the exception that the following sentences

"When LIBOR is terminated or its use becomes de minimis, the LIBOR rates will be replaced with the most appropriate replacement rates for the specified purpose. The NAIC will monitor these market observable values and, in the event the then current values are discontinued or replaced, will recommend an appropriate replacement to the Life Actuarial (A) Task Force."

have been replaced by the sentence below

When the NAIC determines LIBOR is no longer effective, the NAIC shall recommend a replacement to LATF which shall be effective upon adoption by Life Actuarial (A) Task Force.

Life Actuarial (A) Task Force/ Health Actuarial (B) Task Force
Amendment Proposal Form*

1. Identify yourself, your affiliation and a very brief description (title) of the issue.

   Brian Bayerle, ACLI – Interest Rate Swap Spread Determination

2. Identify the document, including the date if the document is "released for comment," and the location in the document where the amendment is proposed:

   Valuation Manual Jan. 1, 2020 Edition; VM-20 Section 9.F.8.d., VM-31 Section 3.D.6.

3. Show what changes are needed by providing a red-line version of the original verbiage with deletions and identify the verbiage to be deleted, inserted or changed by providing a red-line (turn on "track changes" in Word®) version of the verbiage. (You may do this through an attachment.)

   See attached.

4. State the reason for the proposed amendment? (You may do this through an attachment.)

   Interest Rate Swap Spreads are currently being calculated by the NAIC under methodology outlined in the Valuation Manual. This APF changes the methodology for calculation of the 3-month and 6-month swap spreads to use market observable values for Treasury rates and LIBOR, rather than the average of these values from JP Morgan and Bank of America.

   With the forthcoming termination of LIBOR, the requirements of the Valuation Manual will need to change. This APF provides broad guidance allowing for one or more currently unnamed rate to replace LIBOR in these calculations.

Additionally, this APF allows the company to calculate its own current swap spreads based on market observable values. The spread requirements are currently included in VM-20, with VM-21 referencing the applicable sections. With the potential of VM-22 likely having similar references, LATF may want to consider moving these and other asset requirements to their own section.

NAIC Staff Comments:

Dates: Received	Reviewed by Staff	Distributed	Considered
05/4/20			
Notes: VM APF 2020-06			

Options for LATF consideration: Per the 6/11 LATF discussion, in addition to adopting the full text of the APF, regulators wanted to consider not allowing for companies to produce their own current swap spreads. This option would be to retain "prescribed" instead of "calculated", would strike the paragraph beginning "The company may elect to product their own current swap curves…", and would remove the VM-31 Section 3.D.6.v and VM-31 Section 3.F.4.h language.

VM-20 Section 9.F.8.d

Interest rate swap spreads over Treasuries shall be ~~prescribed~~calculated by the NAIC for use throughout the cash-flow model wherever appropriate for transactions and operations including, but not limited to, purchase, sale, settlement, cash flows of derivative positions and reset of floating rate investments. A current and long-term swap spread curve shall be prescribed~~calculated~~ for year one and years four and after, respectively, with yearly grading in between. The three-month and six-month points on the swap spread curves ~~represent the corresponding London Interbank Offered Rate (LIBOR) spreads over Treasuries.~~shall be the market-observable values for these tenors. Currently, this shall be the corresponding London Interbank Offered Rate (LIBOR) spreads over Treasuries. ~~When LIBOR is terminated or its use becomes de minimis, the LIBOR rates will be replaced with the most appropriate replacement rates for the specified purpose. The NAIC will monitor these market-observable values and, in the event the then-current values are discontinued or replaced, will recommend an appropriate replacement to the Life Actuarial (A) Task Force.~~ When the NAIC determines LIBOR is no longer effective, the NAIC shall recommend a replacement to LATF which shall be effective upon adoption by LATF.

~~The company may elect to produce their own current swap spread curves based on current observable rates. The company will document the data source(s) of the observable rates and the methodology of interpolation of non-published rates in the VM-31 report.~~

VM-20 Appendix 2.F.1
F. Current Benchmark Swap Spreads

1. For tenors of one-year to thirty-years, e~~E~~xtract swap spread data determined as of the last business day of the month by maturity. For Bank of America data, convert the swap rate for each maturity to a swap spread by subtracting the corresponding maturity Treasury yield from the swap rate. For JP Morgan, the swap spread is provided for each maturity.

~~VM-31 Section 3.D.6.v (additional bullet):~~

~~v. Current Swap Spreads Data Source: If the company used something other than the NAIC produced current swap spreads as permitted by VM-20 Section 9.F.8.d, documentation of the data source(s) used in the determination of the swap spreads, and the methodology used to determine the non-published tenors.~~

~~VM-31 Section 3.F.4.h (additional bullet):~~

~~v. Current Swap Spreads Data Source: If the company used something other than the NAIC produced current swap spreads as permitted by VM-20 Section 9.F.8.d, documentation of the data source(s) used in the determination of the swap spreads, and the methodology used to determine the non-published tenors.~~

Life Actuarial (A) Task Force/ Health Actuarial (B) Task Force
Amendment Proposal Form*

1. Identify yourself, your affiliation and a very brief description (title) of the issue.

   Identification:
   Brian Bayerle, ACLI

   Title of the Issue:
   Remove 4% Floor from Life Standard Nonforfeiture Rate.

2. Identify the document, including the date if the document is "released for comment," and the location in the document where the amendment is proposed:

   January 1, 2020 NAIC Valuation Manual – VM-02 Section 3.A

3. Show what changes are needed by providing a red-line version of the original verbiage with deletions and identify the verbiage to be deleted, inserted or changed by providing a red-line (turn on "track changes" in Word®) version of the verbiage. (You may do this through an attachment.)

   See attached.

4. State the reason for the proposed amendment? (You may do this through an attachment.)

   Upon any possible tax code (IRC, S. 7702) modifications to remove the hardcoded interest rate floor starting in 1/1/2021, the life standard nonforfeiture rate is being updated to ensure the minimum funding under state requirements does not exceed the maximum funding under federal requirements for life insurance contracts issued starting in 1/1/2021.

NAIC Staff Comments:

Dates: Received	Reviewed by Staff	Distributed	Considered
05/19/20			
Notes: VM APF 2020-07			

VM-02

Version 1: Remove floor

Section 3: Interest

A. The nonforfeiture interest rate for any life insurance policy issued in a particular calendar year beginning on and after the operative date of the *Valuation Manual* shall be equal to 125% of the calendar year statutory valuation interest rate defined for the NPR in the *Valuation Manual* for a life insurance policy with nonforfeiture values, whether or not such sections apply to such policy for valuation purposes, rounded to the nearer one-quarter of 1%, provided, however, that the nonforfeiture interest rate shall not be less than the applicable interest rate ~~used~~ prescribed to meet the definition of life insurance in the Cash Value Accumulation Test under Section 7702 (*Life Insurance Contract Defined*) of the U.S. Internal Revenue Code ~~4%~~.

Guidance Note: For flexible premium universal life insurance policies as defined in Section 3.D of the *Universal Life Insurance Model Regulation* (#585), this is not intended to prevent an interest rate guarantee less than the nonforfeiture interest rate.

W:\National Meetings\2020\Summer\Plenary\Att 4 2020 VM Package.pdf

Adopted by Life Actuarial Task Force June 25, 2020
Adopted by Life Insurance and Annuities (A) Committee July 10, 2020

Actuarial Guideline XLIX-A
THE APPLICATION OF THE LIFE ILLUSTRATIONS MODEL REGULATION TO POLICIES WITH INDEX-BASED INTEREST SOLD AFTER [greater of 5 months after LATF adoption and 3 months after EX/Plenary Adoption*]

Background

The *Life Insurance Illustrations Model Regulation* (#582) was adopted by the NAIC in 1995. Since that time there has been continued evolution in product design, including the introduction of benefits that are tied to an index or indices. Although these policies are subject to Model #582, not all of their features are explicitly referenced in the model, resulting in a lack of uniform practice in its implementation. In the absence of uniform guidance, two illustrations that use the same index and crediting method often illustrated different credited rates. The lack of uniformity can be confusing to potential buyers and can cause uncertainty among illustration actuaries when certifying compliance with Model #582.

In 2019, the NAIC decided that illustrations of products with multipliers, cap buy-ups, and other enhancements that are linked to an index or indices should not illustrate better than products without such features. This new requirement is intended to apply to illustrations on policies sold on or after the effective date of this guideline while the existing requirements continue to apply for inforce illustrations on policies sold before the effective date of this guideline.

This guideline provides uniform guidance for policies with index-based interest. In particular, this guideline:

(1) Provides guidance in determining the maximum crediting rate for the illustrated scale and the earned interest rate for the disciplined current scale.

(2) Limits the policy loan leverage shown in an illustration.

(3) Requires additional consumer information (side-by-side illustration and additional disclosures) that will aid in consumer understanding.

Text

1. Effective Date

   This Actuarial Guideline shall be effective for all new business and in force illustrations on policies sold on or after [greater of 5 months after LATF adoption and 3 months after EX/Plenary Adoption].

2. Scope

   This Actuarial Guideline shall apply to any life insurance illustration that meets both (i) and (ii), below:

   i. The policy is subject to Model #582.

   ii. The policy offers Indexed Credits.

3. Definitions

A. Alternate Scale: A scale of non-guaranteed elements currently being illustrated such that:

i. The Annual Rate of Indexed Credits for each Index Account does not exceed the lesser of the maximum Annual Rate of Indexed Credits for the illustrated scale less 100 basis points and the credited rate for the Fixed Account. If the insurer does not offer a Fixed Account with the illustrated policy, the Annual Rate of Indexed Credits for each Index Account shall not exceed the average of the maximum Annual Rate of Indexed Credits for the illustrated scale and the guaranteed Annual Rate of Indexed Credits for that account. However, the Annual Rate of Indexed Credits for each Index Account shall never be less than the guaranteed Annual Rate of Indexed Credits for that account.

ii. If the illustration includes a loan, the illustrated Policy Loan Interest Credited Rate shall not exceed the illustrated Policy Loan Interest Rate. For example, if the illustrated Policy Loan Interest Rate is 4%, the Policy Loan Interest Credited Rate shall not exceed 4%.

iii. All other non-guaranteed elements are equal to the non-guaranteed elements for the illustrated scale.

B. Annual Net Investment Earnings Rate: Gross portfolio annual earnings rate of the general account assets (excluding hedge assets for Indexed Credits), less provisions for investment expenses and default cost, allocated to support the policy. Charges of any kind cannot be used to increase the Annual Net Investment Earnings Rate.

C. Annual Rate of Indexed Credits: The total annualized Indexed Credits expressed as a percentage of the account value used to determine the Indexed Credits.

D. Benchmark Index Account: An Index Account with the following features:

i. The interest calculation is based on the percent change in S&P 500® Index value only, over a one-year period using only the beginning and ending index values. (S&P 500® Index ticker: SPX)

ii. An annual cap is used in the interest calculation.

iii. The annual floor used in the interest calculation shall be 0%.

iv. The participation rate used in the interest calculation shall be 100%.

v. Interest is credited once per year.

vi. The Hedge Budget used to determine the cap in 3 (D) (ii) does not exceed the Annual Net Investment Earnings Rate. Charges of any kind cannot be used to increase the annual cap.

vii. There are no enhancements or similar features that provide additional Indexed Credits in excess of the interest provided by 3 (D) (i) through 3 (D) (v), including but not limited to experience refunds, multipliers, or bonuses.

viii. There are no limitations on the portion of account value allocated to the account.

ix. A single Benchmark Index Account will be determined for each policy. This can be either an Index Account offered with the illustrated policy or determined according to Section 4 (A) (ii) for purposes of complying with this guideline. A policy shall have no more than one Benchmark Index Account.

E. Fixed Account: An account where there are no Indexed Credits.

F. Hedge Budget: For each Index Account, the total annualized amount assumed to be used to generate the Indexed Credits of the account, expressed as a percent of the account value in the Index Account. This total annualized amount should be consistent with the hedging program of the company.

G. Index Account: An account where some or all of the amounts credited are Indexed Credits.

H. Indexed Credits: Any interest credit, multiplier, factor, bonus, charge reduction, or other enhancement to policy values that is linked to an index or indices. Amounts credited to the policy resulting from a floor greater than zero on an account with any interest credit, multiplier, factor, bonus, charge reduction, or other enhancement to policy values that is linked to an index or indices are included.

I. Loan Balance: Any outstanding policy loan and loan interest, as defined in the policy.

J. Policy Loan Interest Rate: The current annual interest rate as defined in the policy that is charged on any Loan Balance. This does not include any other policy charges.

K. Policy Loan Interest Credited Rate: The annualized interest rate credited that applies to the portion of the account value backing the Loan Balance:

i. For the portion of the account value in the Fixed Account that is backing the Loan Balance, the Policy Loan Interest Credited Rate is the applicable annual interest crediting rate.

ii. For the portion of the account value in an Index Account that is backing the Loan Balance, the Policy Loan Interest Credited Rate is the Annual Rate of Indexed Credits, net of any applicable Supplemental Hedge Budget, for that account.

L. Supplemental Hedge Budget: For each Index Account, the Hedge Budget minus the minimum of the Annual Net Investment Earnings Rate and the Hedge Budget that is used in the determination of the Benchmark Index Account. The Supplemental Hedge Budget will never be less than zero. This amount should be consistent with the hedging program of the company.

4. Illustrated Scale

The total Annual Rate of Indexed Credits for the illustrated scale for each Index Account shall be limited as follows:

A. Calculate the geometric average annual credited rate for the Benchmark Index Account for the 25-year period starting on 12/31 of the calendar year that is 66 years prior to the current calendar year (e.g., 12/31/1949 for 2015 illustrations) and for each 25-year period starting on each subsequent trading day thereafter, ending with the 25- year period that ends on 12/31 of the prior calendar year.

i. If the insurer offers a Benchmark Index Account with the illustrated policy, the illustration actuary shall use the current annual cap for the Benchmark Index Account in 4 (A).

ii. If the insurer does not offer a Benchmark Index Account with the illustrated policy, the illustration actuary shall use actuarial judgment to determine a hypothetical, supportable current annual cap for a hypothetical, supportable Index Account that meets the definition of the Benchmark Index Account, and shall use that cap in 4 (A).

B. For the Benchmark Index Account the Annual Rate of Indexed Credits shall not exceed the minimum of (i) and (ii):

i. the arithmetic mean of the geometric average annual credited rates calculated in 4 (A).

ii. 145% of the Annual Net Investment Earnings Rate.

C. For any other Index Account that is not the Benchmark Index Account in 3 (D), the Annual Rate of Indexed Credits illustrated as a percentage of the account value in the Index Account prior to the deduction of any charges used to fund a Supplemental Hedge Budget shall not exceed the minimum of (i) and (ii):

i. The Annual Rate of Indexed Credits for the Benchmark Index Account calculated in 4 (B) plus the Supplemental Hedge Budget for the Index Account.

ii. The Annual Rate of Indexed Credits reflecting the fundamental characteristics of the Index Account and the appropriate relationship to the expected risk and return of the Benchmark Index Account. The illustration actuary shall use actuarial judgment to determine this value using lookback methodology consistent with 4 (A) and 4 (B) (i) where appropriate.

D. For the purposes of compliance with Section 6 (C) of Model #582, the Supplemental Hedge Budget is subtracted from the Annual Rate of Indexed Credits before comparing to the earned interest rate underlying the disciplined current scale.

At the beginning of each calendar year, the insurer shall be allowed up to three (3) months to update the credited rate for each Index Account in accordance with 4 (B) and 4 (C).

5. Disciplined Current Scale
The earned interest rate for the disciplined current scale shall be limited as follows:

A. If an insurer engages in a hedging program for Indexed Credits in an account, the assumed earned interest rate underlying the disciplined current scale for that account, inclusive of all general account assets, both hedge and non-hedge assets, that support the policy, net of default costs and investment expenses (including the amount spent to generate the Indexed Credits of the policy) shall not exceed the lesser of (i) and (ii):

i. the Annual Net Investment Earnings Rate, plus 45% of the lesser of (1) and (2):

1. Hedge Budget minus any annual floor, to the extent that the floor is supported by the Hedge Budget.

2. The minimum of the Annual Net Investment Earnings Rate and the Hedge Budget that is used in the determination of the Benchmark Index Account.

ii. the Annual Rate of Indexed Credits plus the Annual Net Investment Earnings Rate minus the Hedge Budget.

These rates should be adjusted for timing differences in the hedge cash flows to ensure that fixed interest is not earned on the Hedge Budget minus any annual floor, to the extent that the floor is supported by the Hedge Budget.

Guidance Note: The above approach does not stipulate any required methodology as long as it produces a consistent limit on the assumed earned interest rate underlying the disciplined current scale.

For a policy with multiple Index Accounts, a maximum rate in 5 (A) should be calculated for each account. All accounts, fixed and indexed, within a policy can be tested in aggregate.

B. If an insurer does not engage in a hedging program for Indexed Credits, the assumed earned interest rate underlying the disciplined current scale shall not exceed the Annual Net Investment Earnings Rate.

C. These experience limitations shall be included when testing for self-support and lapse-support under Model #582, accounting for all illustrated benefits including any illustrated benefits and bonuses that impact the policy's account value.

6. Policy Loans

   If the illustration includes a loan, the illustrated Policy Loan Interest Credited Rate shall not exceed the illustrated Policy Loan Interest Rate by more than 50 basis points. For example, if the illustrated Policy Loan Interest Rate is 4.00%, the Policy Loan Interest Credited Rate shall not exceed 4.50%.

7. Additional Standards

   The basic illustration shall also include the following:

   A. A ledger using the Alternate Scale shall be shown alongside the ledger using the illustrated scale with equal prominence.

   B. A table showing the minimum and maximum of the geometric average annual credited rates calculated in 4 (A).

   C. For each Index Account illustrated, a table showing actual historical index changes and corresponding hypothetical Indexed Credits using current index parameters for the most recent 20-year period.

Comments for the Center for Economic Justice

To the NAIC Executive Committee and Plenary

Regarding Proposed Revisions to Actuarial Guideline XLIX ("Proposed AG49-A") for Indexed Universal Life Illustrations

August 5, 2020

The Center for Economic Justice (CEJ) urges the NAIC Executive Committee and Plenary to fix two critical problems with the proposed revisions to Actuarial Guideline 49 forwarded by the Life and Annuities (A) Committee.

1. Protect all consumers by applying the revised AG49 to all new illustrations – whether for new policies or for new illustrations on in-force policies regardless of date of issue – on and after the effective date. This requested change is:

1. Effective Date

This Actuarial Guideline shall be effective for all new ~~business~~ and in force illustrations on policies regardless of the date the policy was sold on or after [greater of 5 months after LATF adoption and 3 months after EX/Plenary Adoption]

2. Eliminate misleading and deceptive loan arbitrage by prohibiting illustration of crediting rates greater than policy loan rates. This requested change is:

6. Policy Loans

If the illustration includes a loan, the illustrated Policy Loan Interest Credited Rate shall not exceed the illustrated Policy Loan Interest Rate~~ by more than 50 basis points~~. For example, if the illustrated Policy Loan Interest Rate is 4.00%, the Policy Loan Interest Credited Rate shall not exceed 4.00~~50~~%.

It is important to point out that these two issues are not technical issues, but core policy decisions regarding protection of consumers from misleading and deceptive marketing information. And these policy issues received no discussion during the A Committee meeting in which proposed AG49-A was accepted.

Background – What is AG49?

AG49 is an actuarial guideline that, once effective, has the force of law in the states. AG49 was originally developed in 2015 to rein in unrealistic and misleading illustrations for indexed universal life (IUL) products. Insurers promptly started to game AG49 with new product designs that avoided the caps on the illustrated credits for the products. These so-called "innovations" – complex product designs requested by no consumers – included "multipliers," "bonuses," and "cap buy-ups". The result was even more unrealistic projected policy value accumulations despite lower crediting rates and much higher policy fees. The proposal before you is an attempt to stop this some of the abuses in IUL illustrations.

Why are the AG49 consumer protections so important?

IUL products are marketed as safe investments that allow policyholders to achieve high returns without the market risk associated with the higher-return, higher-risk investments. Illustrations showing how much the policy value will grow over time are the principal marketing tool and the competition among insurers is to design products – including complex crediting schemes and indexes – that maximize the illustrated accumulation amount.

Consumers purchasing IUL are led to believe that these products will provide income for retirement. In volatile economic times, consumers are particularly susceptible to promises about safe and high returns on investments. Yet, the IUL illustrations are profoundly misleading and set unrealistic expectations for consumers about product performance.

The problems with IUL illustrations have been an ongoing issue and the proposal before you – AG49A – is the latest attempt to rein in the unrealistic and misleading illustrations.

The AG49A proposal fails to protect all current IUL policyholders.

The AG49A proposal before you addresses some of the abuses in in IUL illustrations – but only for illustrations on new policies issued on or after the effective date of the guideline. It continues to permit the same unrealistic and misleading illustrations for new illustrations on policies issued before the effective date. As a result, those consumers who were the victims of misleading illustrations will continue to see misleading illustrations and are excluded from the protections in the revised AG49.

The failure to protect current policyholders from ongoing deception is both inexplicable and contrary to your past decisions about AG49. In 2018, you revised AG49 specifically to apply to all new illustrations – for new and existing policies – on and after the effective date.

The purpose of the AG49 revision exercise is to stop unrealistic illustrations and provide consumers with better information and expectations about how the IUL product will operate and perform. Logic dictates that the consumer protections in a revised AG49 should be available to all consumers – whether they are consumers receiving an illustration as part of a new policy purchase or as a new, updated illustration for an in-force policy.

What was the rationale for denying consumers of in-force policies with the new consumer protections? Industry offered two arguments – it would be a "retroactive" change to the policy and it would confuse the consumer. The "retroactive" claim is without merit because application of revised AG49 to new illustrations after the effective date does not change any contract provisions or features. It merely gives the consumer of an in-force policy who gets a new illustration a better illustration – better by definition of the purpose of the revisions to AG49.

Claims about consumer confusion with application to all new illustrations are without any empirical support and given current illustrations, the claims about consumer confusion by getting a more realistic illustration are insulting. It makes no sense to permit insurers to continue with an illustration methodology that regulators have acknowledged as failing to protect consumers. There is absolutely no logic to the argument that because insurers used unrealistic illustrations for a product in the past they should be permitted to continue to use a methodology that perpetuates unrealistic and misleading illustrations.

If this point wasn't already clear, Mr. Sanders of NAIFA drove it home with his comments that giving a consumer a more realistic new illustration on an in-force policy would erode the producer-client relationship because the client might ask the producer why the illustration has changed and not be satisfied with the answer – perhaps becoming unhappy with the product.

According to Mr. Sanders' logic, the consumer should continue to get illustrations that are now unrealistic because providing the consumer with more realistic expectations about the performance of the product might reduce the client's confidence in the producer and that this client is better off not learning that the illustrations they had been receiving were unrealistic until years later when it may be too late to take any action to protect their retirement savings or after the producer has retired. This logic may make sense in the world of insurer or insurance producer trade associations, but it is insane from the perspective of consumer protection.

To ensure all consumers received the protections of proposed AG49-A, the following change is needed.

1. Effective Date

This Actuarial Guideline shall be effective for all new ~~business~~ and in force illustrations on policies regardless of the date the policy was sold on or after [greater of 5 months after LATF adoption and 3 months after EX/Plenary Adoption]

The proposed AG49-A fails to rein in deceptive loan arbitrage.

A fundamental flaw in the life insurance illustration regime is the presentation of account values accumulating at the same amount year after year with no demonstration of the risk or impact of the volatility of returns. If policy loan interest rates can be illustrated at values less than the account crediting rates, the IUL will illustrate like a riskless ATM.

Current AG49 and proposed AG49-A permit policy loans to be illustrated with a policy loan interest rate less than the crediting rate for illustrating account value accumulation. Stated differently, if you illustrate account value credits at 6.5% every year, you can illustrate a policy loan cost at 6%. This is an example of illustrating riskless arbitrage – the consumer can borrow money at one rate and use it earn a higher rate of return without any risk. This is analogous to taking out a mortgage on your home and using that money to invest in the stock market – because the market has averaged returns of, say, 8%, while your mortgage loan rate is 3%. Of course this would be terrible financial advice because the loan cost is fixed – you have to pay the interest regardless of what your investment returns might be and the investment returns are erratic and may be negative in several years.

By being able to illustrate riskless loan arbitrage, IUL illustrations are used to present future loans on the policy as cash disbursements that never need to be paid back because the policy is continuing to earn the constant better-than-loan-interest-rate returns. Does anyone recall the vanishing premium illustration debacle?

By being able to illustrate riskless loan arbitrage, IUL products are sold in connection with premium finance loans, in which a consumer borrowers money to buy an IUL policy.

If the NAIC's stated commitment to ensuring retirement security for consumers is to have any meaning at all, loan arbitrage in AG49 must be eliminated. The following change to proposed AG49-A is needed.

6. Policy Loans

If the illustration includes a loan, the illustrated Policy Loan Interest Credited Rate shall not exceed the illustrated Policy Loan Interest Rate~~ by more than 50 basis points~~. For example, if the illustrated Policy Loan Interest Rate is 4.00%, the Policy Loan Interest Credited Rate shall not exceed 4.00~~50~~%.

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CONSIDERATIONS FOR STATE INSURANCE REGULATORS IN BUILDING THE PRIVATE FLOOD INSURANCE MARKET

DECEMBER 9, 2019

Table of Contents

BACKGROUND AND PURPOSE

State insurance regulators have first-hand experience with the devastating effects that floods have on the constituents in their states, and they believe it is critical that flood insurance is both available and affordable in order to encourage purchases that thereby protect homes, businesses and personal property. Although private flood insurance is being written largely in the commercial market, this paper will focus on the residential flood insurance market.

For more than a half-century, the federal government's National Flood Insurance Program (NFIP) has been the primary player in the residential flood insurance market, underwriting most policies while private insurers have largely focused on a relatively small residential supplemental market. While the NFIP has done a laudable job in making flood insurance available for millions of residential properties, a significant flood insurance gap exists across the U.S.[1] with flood event after flood event revealing a substantial number of damaged properties being uninsured.[2] A Federal Emergency Management Agency (FEMA) analysis from 2018 indicates that 69% of American homes in high-risk flood zones do not have flood insurance. Concurrently, there has been a heightened interest amongst private carriers to expand their residential flood insurance offerings, greatly assisted by the development of more sophisticated flood mapping and risk modeling technologies.

Funding for continuation of the NFIP expired in September 2017, and since then, the U.S. Congress has passed numerous short-term extensions, and more are expected. The federal Biggert-Waters Flood Insurance Reform Act of 2012 (Biggert-Waters) requires lenders to accept private flood insurance policies meeting certain requirements just as they would an NFIP policy to satisfy the federal mandatory purchase mortgage requirement. The NAIC has been engaged legislatively and with the federal banking regulators on their rulemaking.[3] In February 2019, after six years of deliberation, the federal banking regulators finalized their rule. The final rule provides the requirements[4] for lenders to accept provide flood insurance policies. The rule also provides lenders the option to accept private flood insurance policies that do not meet the mandatory acceptance requirements set forth in Biggert-Waters subject to certain conditions.

State insurance regulators and the NAIC support a long-term NFIP reauthorization, as well as the facilitation of increased private sector involvement in the sale of flood insurance, which can help ensure that consumers have access to multiple options. In 2016, the NAIC developed the "NAIC Principles for National Flood Insurance Program (NFIP) Reauthorization"[5] and has testified in Congress on the importance of ensuring a viable private flood insurance market as an alternative to the NFIP.[6]

[1] *https://riskcenter.wharton.upenn.edu/wp-content/uploads/2019/02/Moving-the-Needle-on-Closing-the-Flood-Insurance-Gap.pdf.*
[2] *www.pciaa.net/docs/default-source/industry-issues/4_lessonslearned.pdf.*
[3] *https://www.naic.org/documents/government_relations_comment_letter_federal_banking_private_flood_insurance.pdf.*
[4] The key conditions in the final rule are: 1) a requirement that the policy provide sufficient protection for a designated loan, consistent with general safety and soundness principles; and 2) a requirement that the regulated lending institution document its conclusion regarding the sufficiency of protection in writing. The final rule also allows regulated lending institutions to exercise their discretion to accept certain plans providing coverage issued by "mutual aid societies."
[5] *https://www.naic.org/documents/government_relations_161019_nfip_guiding_principles.pdf.*
[6] *https://www.naic.org/documents/government_relations_160113_testimony_private_flood_insurance.pdf.*

Following from this NAIC action, the purpose of this document is to provide state insurance regulators with concrete actions that can be and/or have been taken to assist with the development of the burgeoning private insurance market for residential flood insurance.

OVERALL STATE OF THE FLOOD INSURANCE MARKET

According to the most recent data collected by the NAIC (Table 1), approximately $644 million of direct premium was written in the private flood insurance market in 2018 throughout the U.S. In 2018, the private flood insurance market represented 15% of the total flood insurance market ($4.2 billion). The private flood insurance market has been growing over the past few years, with the $644 million in direct premium written in 2018 being an increase of 9% from 2017 direct written premiums, and an increase of 71% since 2016. In 2018, California, Florida, Louisiana, New Jersey, New York, Pennsylvania, Puerto Rico and Texas each had $20 million or more of private flood insurance direct written premium (Table 1), with these eight states/jurisdictions representing nearly 60% of the total private flood insurance market.

It is important to note that the NAIC Annual Statement data used in Table 1 and Table 2 does not differentiate between residential private flood insurance premium and commercial private flood insurance premium. The NAIC is exploring data collection via a supplement and/or data call to collect data for residential private flood insurance and commercial private flood insurance separately.

Beyond this aggregate view of premium being written by state, for a relative sense of market penetration and growth of the private flood market, two other views of the NAIC data are presented: 1) private flood as a percentage of total flood written per state in 2018 (Table 1); and 2) private flood growth by state from 2016 to 2018 (Table 2).

Table 1: Private Flood as a Percentage of Total Flood Written per State in 2018

State	Direct Premium Written – Private	Direct Written Premium – NFIP	Total	Private Flood Percentage
AK	$ 726,128	$ 2,173,734	$ 2,899,862	25%
AL	$ 4,717,310	$ 37,369,849	$ 42,087,159	11%
AR	$ 2,918,840	$ 13,387,226	$ 16,306,066	18%
AS	$ 17	$ 38,356	$ 38,373	0%
AZ	$ 13,616,250	$ 20,785,412	$ 34,401,662	40%
CA	$ 83,598,726	$ 184,728,154	$ 268,326,880	31%
CO	$ 6,815,467	$ 17,996,733	$ 24,812,200	27%
CT	$ 8,554,006	$ 52,057,947	$ 60,611,953	14%
DC	$ 2,023,055	$ 1,481,959	$ 3,505,014	58%
DE	$ 1,870,439	$ 19,394,560	$ 21,264,999	9%
FL	$ 79,664,174	$ 974,338,089	$ 1,054,002,263	8%
GA	$ 13,822,654	$ 59,793,148	$ 73,615,802	19%
GU	$ 23,475	$ 348,208	$ 371,683	6%
HI	$ 3,511,428	$ 40,778,877	$ 44,290,305	8%
IA	$ 9,261,662	$ 12,894,876	$ 22,156,538	42%
ID	$ 1,685,637	$ 4,443,509	$ 6,129,146	28%
IL	$ 15,571,396	$ 41,782,653	$ 57,354,049	27%
IN	$ 9,754,263	$ 22,122,449	$ 31,876,712	31%
KS	$ 5,619,810	$ 8,096,167	$ 13,715,977	41%

Table 1: Private Flood as a Percentage of Total Flood Written Per State in 2018 (cont'd)				
State	**Direct Premium Written – Private**	**Direct Written Premium – NFIP**	**Total**	**Private Flood Percentage**
KY	$ 5,562,791	$ 19,859,236	$ 25,422,027	22%
LA	$ 20,518,942	$ 332,451,130	$ 352,970,072	6%
MA	$ 17,035,775	$ 77,215,928	$ 94,251,703	18%
MD	$ 6,161,138	$ 38,179,561	$ 44,340,699	14%
ME	$ 1,826,143	$ 8,778,305	$ 10,604,448	17%
MI	$ 7,287,062	$ 20,395,079	$ 27,682,141	26%
MN	$ 6,072,364	$ 7,828,757	$ 13,901,121	44%
MO	$ 10,054,439	$ 21,828,499	$ 31,882,938	32%
MP	$ 1,406	$ -	$ 1,406	100%
MS	$ 5,401,764	$ 43,786,173	$ 49,187,937	11%
MT	$ 1,107,818	$ 3,679,000	$ 4,786,818	23%
NC	$ 10,477,327	$ 109,932,602	$ 120,409,929	9%
ND	$ 1,808,961	$ 6,508,148	$ 8,317,109	22%
NE	$ 3,426,045	$ 8,737,796	$ 12,163,841	28%
NH	$ 1,579,406	$ 8,531,507	$ 10,110,913	16%
NJ	$ 33,570,528	$ 215,735,820	$ 249,306,348	13%
NM	$ 2,025,523	$ 10,462,171	$ 12,487,694	16%
NV	$ 4,598,626	$ 8,083,596	$ 12,682,222	36%
NY	$ 47,243,273	$ 205,299,097	$ 252,542,370	19%
OH	$ 15,400,298	$ 33,185,859	$ 48,586,157	32%
OK	$ 3,076,462	$ 11,092,205	$ 14,168,667	22%
OR	$ 6,248,012	$ 23,928,017	$ 30,176,029	21%
PA	$ 22,141,354	$ 65,301,183	$ 87,442,537	25%
PR	$ 21,658,142	$ 7,645,531	$ 29,303,673	74%
RI	$ 2,317,465	$ 18,409,898	$ 20,727,363	11%
SC	$ 13,703,417	$ 137,792,886	$ 151,496,303	9%
SD	$ 834,247	$ 3,115,261	$ 3,949,508	21%
TN	$ 12,179,549	$ 24,574,361	$ 36,753,910	33%
TX	$ 63,221,041	$ 435,173,125	$ 498,394,166	13%
UT	$ 2,712,200	$ 2,509,861	$ 5,222,061	52%
VA	$ 9,475,832	$ 78,057,383	$ 87,533,215	11%
VI	$ 37,329	$ 2,185,181	$ 2,222,510	2%
VT	$ 698,550	$ 4,937,502	$ 5,636,052	12%
WA	$ 12,061,004	$ 31,765,783	$ 43,826,787	28%
WI	$ 5,896,222	$ 11,790,299	$ 17,686,521	33%
WV	$ 1,804,872	$ 16,683,897	$ 18,488,769	10%
WY	$ 899,933	$ 1,580,170	$ 2,480,103	36%
Total	**$ 643,879,997**	**$ 3,571,032,713**	**$ 4,214,912,710**	**15%**

Table 2: Private Flood Growth by State from 2016 to 2018					
State	Direct Premium Written – 2018	Direct Premium Written – 2017	Direct Premium Written – 2016	Percentage of Change Premium Written from 2017 to 2018	Percentage of Change Premium from 2016 to 2018
AK	$ 726,128	$ 957,063	$ 555,129	-24%	31%
AL	$ 4,717,310	$ 4,799,724	$ 3,005,135	-2%	57%
AR	$ 2,918,840	$ 2,826,120	$ 1,607,656	3%	82%
AS	$ 17	$ -	$ -	N/A	N/A
AZ	$ 13,616,250	$ 11,068,965	$ 6,260,448	23%	117%
CA	$ 83,598,726	$ 71,951,648	$ 48,786,070	16%	71%
CO	$ 6,815,467	$ 6,097,813	$ 4,735,996	12%	44%
CT	$ 8,554,006	$ 9,810,824	$ 6,787,613	-13%	26%
DC	$ 2,023,055	$ 2,838,882	$ 1,829,183	-29%	11%
DE	$ 1,870,439	$ 1,669,426	$ 740,005	12%	153%
FL	$ 79,664,174	$ 84,491,040	$ 47,796,186	-6%	67%
GA	$ 13,822,654	$ 12,154,732	$ 6,953,126	14%	99%
GU	$ 23,475	$ 61,491	$ 9,396	-62%	150%
HI	$ 3,511,428	$ 4,707,292	$ 3,149,891	-25%	11%
IA	$ 9,261,662	$ 7,973,218	$ 6,739,156	16%	37%
ID	$ 1,685,637	$ 1,246,073	$ 842,501	35%	100%
IL	$ 15,571,396	$ 14,022,683	$ 9,770,834	11%	59%
IN	$ 9,754,263	$ 9,359,454	$ 5,834,525	4%	67%
KS	$ 5,619,810	$ 5,187,276	$ 3,519,857	8%	60%
KY	$ 5,562,791	$ 5,184,777	$ 3,636,333	7%	53%
LA	$ 20,518,942	$ 17,883,168	$ 11,495,497	15%	78%
MA	$ 17,035,775	$ 15,255,682	$ 8,980,394	12%	90%
MD	$ 6,161,138	$ 4,881,020	$ 3,004,956	26%	105%
ME	$ 1,826,143	$ 1,393,303	$ 1,449,308	31%	26%
MI	$ 7,287,062	$ 5,784,426	$ 3,112,100	26%	134%
MN	$ 6,072,364	$ 6,034,414	$ 4,382,496	1%	39%
MO	$ 10,054,439	$ 8,579,964	$ 5,611,173	17%	79%
MP	$ 1,406	$ 673	$ -	109%	N/A
MS	$ 5,401,764	$ 4,954,089	$ 3,545,564	9%	52%
MT	$ 1,107,818	$ 965,222	$ 546,157	15%	103%
NC	$ 10,477,327	$ 9,385,350	$ 5,916,463	12%	77%

Table 2: Private Flood Growth by State from 2016 to 2018 (cont'd)					
State	**Direct Premium Written – 2018**	**Direct Premium Written – 2017**	**Direct Premium Written – 2016**	**Percentage of Change Premium Written from 2017 to 2018**	**Percentage of Change Premium from 2016 to 2018**
ND	$ 1,808,961	$ 1,518,138	$ 1,033,168	19%	75%
NE	$ 3,426,045	$ 2,733,969	$ 1,819,577	25%	88%
NH	$ 1,579,406	$ 1,773,337	$ 1,516,804	-11%	4%
NJ	$ 33,570,528	$ 28,862,467	$ 17,035,409	16%	97%
NM	$ 2,025,523	$ 1,735,136	$ 662,921	17%	206%
NV	$ 4,598,626	$ 4,574,608	$ 2,440,079	1%	88%
NY	$ 47,243,273	$ 47,674,483	$ 27,419,308	-1%	72%
OH	$ 15,400,298	$ 14,202,904	$ 5,628,305	8%	174%
OK	$ 3,076,462	$ 3,507,498	$ 1,746,619	-12%	76%
OR	$ 6,248,012	$ 4,730,473	$ 2,910,035	32%	115%
PA	$ 22,141,354	$ 18,832,760	$ 13,240,946	18%	67%
PR	$ 21,658,142	$ 19,554,982	$ 19,436,229	11%	11%
RI	$ 2,317,465	$ 2,623,963	$ 1,286,538	-12%	80%
SC	$ 13,703,417	$ 12,726,603	$ 10,633,358	8%	29%
SD	$ 834,247	$ 770,092	$ 572,506	8%	46%
TN	$ 12,179,549	$ 8,584,856	$ 5,939,417	42%	105%
TX	$ 63,221,041	$ 53,512,832	$ 31,771,120	18%	99%
UT	$ 2,712,200	$ 1,958,666	$ 1,050,341	38%	158%
VA	$ 9,475,832	$ 8,527,381	$ 4,727,129	11%	100%
VI	$ 37,329	$ 43,449	$ 122,459	-14%	-70%
VT	$ 698,550	$ 520,374	$ 297,124	34%	135%
WA	$ 12,061,004	$ 11,566,163	$ 9,609,189	4%	26%
WI	$ 5,896,222	$ 4,140,377	$ 2,300,499	42%	156%
WV	$ 1,804,872	$ 1,986,325	$ 1,614,061	-9%	12%
WY	$ 899,933	$ 959,541	$ 713,965	-6%	26%
Total	**$ 643,879,997**	**$ 589,147,189**	**$ 376,130,254**	**9%**	**71%**

Clearly, this data suggests that there are considerable opportunities for private flood insurance placement and market development. However, it is important to note that in 2018, the majority of growth occurred in the private commercial flood insurance market. The residential private flood insurance market showed a slight decline from 2017.[7]

As insurers' familiarity with flood catastrophe models grows, as underwriting experience develops and as state regulatory structures evolve, the number of private flood insurance policies in force could continue to grow, including among admitted carriers. Therefore, it is important to understand what the states have done (or not done) to enhance this growth.

[7] *https://www.insurancejournal.com/research/app/uploads/2019/06/FINAL-Private-Flood-Insurance-Report-2019.pdf.*

STATE ACTION

During the six years of uncertainty regarding the federal banking rules for private flood insurance, a number of states began undertaking efforts to encourage the growth of a private flood insurance market in their state. Florida's efforts to establish a private flood insurance market have been applauded as a potential model to be used in other states looking to expand their residential private flood insurance offerings. Florida has the largest flood insurance market in the country; approximately 35% of NFIP policies are written there.[8] Florida has enacted legislation to create a statutory framework, allowing private insurers to offer multiple types of flood coverage ranging from standard coverage, which mirrors the NFIP, to other enhanced coverages. This legislation includes: 1) streamlining the rate filing process for private flood insurers; 2) eliminating the diligent search requirement for flood policies issued by surplus lines carriers until July 2019; and 3) providing a process by which the Office of Insurance Regulation (OIR) will certify that a private insurer's policy equals or exceeds coverage provided by the NFIP. Florida's OIR issued an informational memorandum providing guidance on how private insurers will need to demonstrate the financial capacity to assume this risk, as well as options for developing private flood rates and policy forms.

In addition to Florida, we can draw upon the existing experiences from other states in developing a robust flood insurance market along the key aspects of insurance regulation.

The NAIC reached out to the states on the drafting group to provide information that was not readily available on the states' websites, as well as to gather information from other resources, including: 1) the Wharton School of the University of Pennsylvania study *The Emerging Private Residential Flood Insurance Market in the United States*; 2) Government Accountability Office (GAO) reports; and 3) a recently updated Congressional Research Service (CRS) report regarding private flood insurance and the NFIP. In the future, the NAIC might want to consider sending a more detailed questionnaire to the states to gather more information regarding the developing private flood insurance market.

State efforts to grow a viable private flood insurance market include:

Legislative and Regulatory Changes

- Supporting private flood insurance legislation.
- Approving private flood insurance products.
- Tailoring rate and form requirements for private flood insurance coverage.
- Allowing private flood insurers to submit rates on an informational basis.
- Removing diligent search requirements.

Consumer Information

- Conducting consumer outreach.
- Listing private flood insurance products on a department of insurance's (DOI) website.
- Collecting residential private flood insurance data.

Agent and Lender Actions

- Implementing specific continuing education (CE) requirements for producers.
- Increasing the weighting of flood insurance questions on producer licensing exams.
- Conducting agent education.
- Conducting lender education.

[8] *www.floods.org/ace-files/documentlibrary/committees/Insurance/Emerging_Flood_Insurance_Market_Report-Wharton-07-13-18.pdf.*

LEGISLATIVE AND REGULATORY CHANGES

Supporting Private Flood Insurance Legislation

In addition to Florida's legislation, West Virginia has passed legislation requiring insurers to file their private flood insurance plan of operation with the insurance commissioner and authorizing expedited processing of surplus lines policies for flood insurance.

Approving Private Flood Insurance Products

Personal lines private flood insurance products are being approved by a number of states. Currently, Alabama, California, Mississippi and Pennsylvania are among states approving new personal lines private flood insurance products for entry into the market.

In January 2018, the Insurance Services Office (ISO) developed a new private flood insurance form, for both personal and commercial flood insurance. The ISO forms are similar to a homeowner's policy form. However, the damage to the property must be caused by flooding. As of March 2018, ISO personal flood insurance forms have been filed in 43 jurisdictions, and commercial flood insurance forms have been filed in 45 jurisdictions. The states with independent rating bureaus are not reflected in these numbers.

TAILORING RATE AND FORM REQUIREMENTS FOR PRIVATE FLOOD INSURANCE COVERAGE

The states might want to consider permitting insurers to file private flood insurance products without a prior approval requirement. For example, Florida law permits private flood insurance rates to be implemented without prior approval at the time of filing. However, insurers are required to keep supporting actuarial data for two years. Furthermore, Florida law allows insurers to request the state to certify that a private policy provides flood coverage that equals or exceeds that offered by NFIP. (See Appendix I for information on Florida's process.)

Maryland, South Carolina and Pennsylvania have not relaxed the rate and form filing requirements. However, they are committed to an efficient and swift overview of private flood insurance filings, and they will work with insurers to make the filing and approval process as smooth as possible.

EXPORT LIST / WAIVING DILIGENT SEARCH REQUIREMENTS

Insurance generally must be sold in the admitted market. Only after a "diligent search" of the admitted market is performed and coverage is denied can insurance be placed in the surplus lines market. However, states make exceptions for those types of insurance that are known to not be available in the admitted market. These insurance products are listed on what is known as an "Export list." When a type of insurance is listed on an Export list, the applicant can go straight to the surplus lines market without the need for the diligent search, thereby obtaining coverage more easily and quickly. At least 14 states have placed flood insurance on their "Export list," including: Alaska, Arizona, Connecticut, Idaho, Louisiana, New Jersey, Oklahoma, Oregon, Pennsylvania, Rhode Island, Texas, Virginia, West Virginia and Wisconsin.

Allowing Private Flood Insurers to Submit Rates on an Informational Basis

Allowing insurers to submit rates on an informational basis in states with prior approval rate filing laws is another way to encourage the growth of the private flood insurance market. Two states that have

taken this approach include Florida and New Jersey.[9] (See Appendix I for information on Florida's process.)

CONSUMER INFORMATION

Consumer Outreach

It is important to understand that everyone lives in a flood zone. Some people live in higher-risk flood zones than others, but we all live in a flood zone.

When people say they live or do not live in a flood zone, they typically mean what is known as a "special flood hazard area". A "special flood hazard area" is an area within FEMA's 100-year flood plain. This is where flood insurance is typically mandatory as a condition of obtaining a property loan. But there are flood zones outside of the 100-year flood plain as well. For example, there is also what FEMA classifies as moderate risk flood zones. These are the properties in the 500-year flood plain. By definition, and according to FEMA, these properties have between a 0.2% and a 1% chance of flooding in any given year. That might sound small, but over the course of a 30-year mortgage, these properties, according to FEMA, have between a 6% and 26% chance of being inundated by a flood. And flood insurance is not mandatory as a condition of obtaining a property loan in these moderate-risk flood zones.

Consumers need to understand that their property may still be at risk for flooding even if they do not live in a special flood hazard area and are not required to purchase it. They also need to understand that flood insurance can be relatively inexpensive, especially when the property is not in the highest-risk flood zones. There are options available to them, from both the NFIP and the private flood insurance market. And they can purchase lower limits of coverage; they do not need to insure the full replacement cost of their home if they do not wish to do so. Purchasing just $20,000 of coverage, for example, might go a long way in the event of a flood and may be cheaper to purchase than believed. Further, renters can buy policies that cover only their personal property and not the dwelling that they rent.

There are also many consumers under the misconception that flood damage will be covered by their homeowners insurance policy or rental insurance policy. Therefore, they are unaware of their actual flood risk, and they learn that they are uninsured for this catastrophic peril only after a flood event for which they have no coverage.

State DOIs, as well as the NAIC, are launching consumer outreach programs to help address this coverage gap.

Some states now require a flood disclosure with homeowners policies. For example, Texas recently passed a law requiring a conspicuous disclosure when homeowners policies do not include flood coverage.

The NAIC Communications Department has also launched a flood campaign this year to inform consumers of the importance of purchasing flood insurance, either private flood insurance or flood insurance provided by the NFIP. Additionally, the NAIC recently released a special section of its website dedicated to educating consumers about the risks of flooding and what kinds of coverage options are available to protect against those risks.

Finally, the NAIC's Transparency and Readability of Consumer Information (C) Working Group has created both a basic flood insurance document and several graphic materials containing flood facts, to be used by DOIs for consumer outreach via social media.

[9] *https://riskcenter.wharton.upenn.edu/wp-content/uploads/2018/07/Emerging-Flood-Insurance-Market-Report.pdf* and state DOIs.

Listing Private Flood Insurance Writers on a DOI Website

While many DOIs include information regarding NFIP policies on their websites, some states, including Florida, Louisiana, New Jersey and Pennsylvania, provide a list of private flood insurance writers and their contact information on their websites.

It is worthwhile to note that surplus lines writers are generally not listed by the line of business they write. However, it has been suggested that there would be value for the states to provide information regarding which surplus lines writers are writing residential private flood insurance. Pennsylvania lists the surplus lines producers placing residential flood insurance on its website.

Collecting Residential Private Flood Insurance Data

Florida and Texas both collect comprehensive data regarding residential private flood insurance.[10] As described previously, the NAIC has been collecting private flood insurance data since the data year 2016. Before that, the private flood insurance line was not a separate entry in the annual statement. While residential and commercial private flood insurance are not separated in the property/casualty (P/C) annual statement blank, the NAIC, through its Property and Casualty Insurance (C) Committee, is considering enhancements to the annual statement that would require insurers to report the residential private flood insurance premiums and commercial private flood insurance premiums independently. The Surplus Lines (C) Task Force is considering similar changes to alien surplus lines private flood insurance data that is reported to the International Insurers Department (IID).

The Wholesale & Specialty Insurance Association (WSIA) is also providing the Reinsurance Association of America (RAA) with data regarding surplus lines insurance. The RAA is working on an open source database that provides information regarding private flood insurance.

These changes would allow state insurance regulators and FEMA to better measure the growth of the private residential flood insurance market.

AGENT AND LENDER ACTIONS

Continuing Education and Producer Licensing Requirements

FEMA requires all insurance producers licensed in property, casualty or personal lines of authority who sell flood insurance through the NFIP to complete a one-time course, as required by the federal Flood Insurance Reform Act of 2004. This is also the only educational requirement in many states.

At least one state has increased the weighting of the flood insurance questions on their producer licensing exam.

Agent Education

Selling flood insurance requires an agent to understand the intricacies of NFIP and private flood insurance policies.[11]

When purchasing insurance, many times the insurance agent is the consumer's first point of contact. Therefore, it would be valuable if an agent could explain the risks of flooding, even if a consumer does not own or rent property in a high-risk flood zone. Recent flood events remind us that where it can rain, it can flood, and many floods occur outside of a high-risk flood zone. If agents help to educate the consumer, it will help eliminate the cost of inaction, as the occurrence of a flood event could be financially unbearable for homeowners or renters if they are not insured or are underinsured. It is critical

[10] *https://riskcenter.wharton.upenn.edu/wp-content/uploads/2018/07/Emerging-Flood-Insurance-Market-Report.pdf.*
[11] www.floods.org/ace-files/documentlibrary/committees */Insurance/Emerging_Flood_Insurance_Market_Report-Wharton-07-13-18.pdf.*

for agents to make a special effort to educate homeowners regarding the need for flood insurance, even if a business or home is not located in a high-risk flood zone.

DOIs can provide agents with information that they have learned as a result of a flood event, and they can foster agent education by requiring CE requirements to improve an agent's knowledge of flood insurance.

Other states' adoption of such practices would likely improve agents' knowledge of flood insurance, therefore helping their clients to obtain more effective flood coverage, whether through the NFIP or the private market.

Lender Education

A large percentage of Americans have a mortgage on their home. Therefore, lender education is another opportunity for consumer flood insurance education. Recent catastrophic flooding events have illustrated that floods can happen anywhere. Therefore, it may be in the best interest of homeowners to purchase flood insurance even if they do not live in a high-risk flood zone.

While state insurance regulators do not have the authority to regulate lenders, lenders should still be educated regarding the importance of flood insurance. When navigating the loan process, lenders do not always discuss purchasing flood insurance unless the borrower's home is in a high-risk flood zone. A discussion about purchasing flood insurance even if the homeowner does not live in a high-risk flood zone should ideally be addressed with the borrower.

DOIs can raise awareness regarding flood insurance by bringing agents, consumers, lenders, FEMA, private flood insurance writers, etc. together in communities to discuss the importance of a homeowner purchasing flood insurance.

MARKET UNCERTAINTY AND THE DEVELOPMENT OF A PRIVATE FLOOD INSURANCE MARKET

The May 2019 CRS report, "Private Flood Insurance and the National Flood Insurance Program," identified some of the barriers to the development of a private flood insurance market. Some of the barriers identified in the report include: 1) regulatory uncertainty; and 2) continuous coverage.

Most directly relevant for the NAIC members is the notion of regulatory uncertainty, which is covered below. The remaining topics will be addressed in Appendix II.

In 2016, the U.S. experienced several major flood catastrophes, causing billions of dollars in property losses.[12] Following these storms, it was found that somewhere between 50% and 80% of these losses were not insured, which implies that communities are unable to bounce back quickly following large catastrophic events.

Floods are expected to cost U.S. households $20 billion each year[13]. An Insurance Information Institute (I.I.I.) survey indicated that 15% of American homeowners had a flood insurance policy in 2018[14] and that there were approximately 5.18 million flood insurance policies held by the NFIP.[15] Milliman estimates the potential private residential flood insurance market to represent between $34 billion and

[12] https://www.pewtrusts.org/en/research-and-analysis/articles/2017/02/01/flooding-disasters-cost-billions-in-2016
[13] Milliman
[14] https://www.iii.org/fact-statistic/facts-statistics-flood-insurance
[15] https://www.fema.gov/total-policies-force-calendar-year

$48 billion in direct written premium.[16] This data clearly indicates an opportunity for growth in the residential private flood insurance market in the U.S.

Recently, comments have surfaced regarding the possibility of the residential private flood insurance market cherry-picking their risks. It is important to remember the NFIP was meant to be a temporary solution that was put into place 50 years ago due to private insurers not insuring flood. While the NFIP is important, every state has some type of residual market that aids in insuring and providing insurance coverage for those who are unable to obtain insurance coverage available in the market. While not directly related to flood insurance, two good examples of successful residual markets are Florida Citizens and Louisiana Citizens. As the market has grown and shrunk in both Florida and Louisiana, both Florida Citizens and Louisiana Citizens needed to and provided a safe and reliable source of insurance for consumers. The NFIP can continue to evolve and do the same thing. Milliman believes Risk Rating 2.0 will help the NFIP and provide helpful information regarding the actual risk of a flood insurance policy; however, it was recently announced that the implementation of Risk Rating 2.0 will be delayed until Oct. 1, 2021 to allow for more analysis of its impact.

Milliman is of the opinion that a private market can coexist alongside the NFIP. Private flood insurance can be written in the admitted and non-admitted market. However, it needs to be determined if the guaranty funds will cover flood insurance in the admitted market, as flood may be excluded in many states.

Many private insurers have not serviced or written flood insurance policies. Additionally, private insurers do not have access to historical data; this poses a problem. It will be important to balance the need to protect consumers against the need to promote the private flood insurance market.

New entrants to the private flood insurance market are likely to purchase significant amounts of reinsurance. Flood insurance is inherently high-risk and volatile, so insurers may require higher amounts of profit and contingencies built into rates than for a typical homeowner's insurance product. States allowing these options might make it easier for an insurer to offer private flood insurance. For example, Wisconsin has no limitations or requirements for reinsurance cost and profit provision assumptions.

The issue of continuous coverage is problematic. In order for an NFIP policyholder to preserve any subsidies provided by the NFIP, a policyholder is required to have continuous flood insurance coverage. Currently, a policyholder loses subsidies or cross-subsidies when private flood insurance is purchased, if the policyholder chooses to return to the NFIP.

Unless there is legislation in place allowing private flood insurance to be deemed as continuous coverage, homeowners may be averse to purchasing private flood insurance. Homeowners do not want to find themselves in a situation causing them to lose their subsidy should they elect to return to the NFIP for flood insurance coverage. While legislation has been introduced in the U.S. House of Representatives allowing private flood insurance to count towards continuous coverage, legislation has yet to be passed.

The availability of private flood insurance provides the added benefit of increasing consumer choice. As private insurers are entering the flood insurance market, some of the policies offered are providing broader coverage than that provided by the NFIP. Additionally, some policyholders are finding private flood insurance policies to be less expensive than those offered by the NFIP.[17]

[16] Milliman
[17] Congressional Research Service report, "Private Flood Insurance and the National Flood Insurance Program, May 7, 2019

SUMMARY

In the past few years, many states have experienced catastrophic flooding. Following the flood events, it has become even more apparent that a significant number of consumers are either uninsured or underinsured for the flood peril.

While the NFIP still writes a majority of the residential flood insurance policies, there are considerable opportunities for the development of the residential private flood insurance market.

This document provides details about how a few states have put procedures in place to enhance the private flood insurance market in a state. These procedures include: 1) supporting private flood insurance legislation and initiatives; 2) tailoring rate and form requirements for residential private flood insurance products; and 3) consumer, agent and lender education.

It is noteworthy to say that the states experiencing large flooding events have seen growth in the private flood insurance market regardless of any other actions. For example, following Hurricane Harvey, Texas saw growth in its residential private flood insurance market. Catastrophic events are a reminder to consumers of the devastation caused by flooding.

While there are several barriers for the residential private flood insurance market, the most significant barrier for private insurers may be uncertainty about the state regulatory environment.

To avoid unintended consequences policymakers interested in facilitating a private flood insurance market should familiarize themselves with the requirements for residential customers with a federally backed mortgage to purchase flood insurance coverage and with the existing private insurance markets that provide coverage for flood damage, including coverage provided under: (a) commercial policies, (b) residential policies providing coverage in excess of required flood insurance coverage limits, (c) residential policies for those not mandated to purchase flood insurance, and (d) comprehensive auto coverages. With such knowledge, legislative and regulatory changes can be tailored to accomplish the policy objectives without adversely impacting existing flood insurance markets.

The attached appendices discuss steps that Florida has taken in its approach to cultivate the private residential flood insurance market and discussion of other barriers to the entrance of residential private flood insurers.

Appendix I – Actions Florida Has Taken

FLORIDA'S FORM FILING PROCESS EXAMPLE

Florida reviews form filings, providing flood coverage differently based on the type of flood coverage being provided.

Subject to the Requirements of Florida's Flood Statute

The coverage provided under the policy must meet one of the definitions of type of flood coverage, as defined by S. 627.715, F.S. Of the five defined types, "standard," "preferred" and "customized" are defined to meet or exceed the coverage provided by the standard NFIP policy. "Flexible" flood insurance must cover losses from the peril of "flood" as defined by the statute, but it does not have to provide coverage comparable to the entire NFIP policy. "Supplemental" flood coverage is meant to supplement an NFIP or private flood policy. Policies that fall under these definitions may have certain provisions that differ from that which would otherwise be required if not written under the flood statute.

Items Not Subject to the Requirements of Florida's Flood Statute

The coverage does not have to meet or exceed the coverage provided by the standard NFIP policy. However, the provisions of the flood statute that allow changes to the form and rate requirements, as well as allowing for a certification provided by the Florida OIR, do not apply. This means that forms and rates would be subject to all the requirements of Florida law, and the coverage does not have to meet the definition of "flood" under the statute.

Florida's private flood insurance statute, S. 627.715 F.S., does not apply to the commercial lines market. Forms providing commercial flood coverage must comply with all applicable Florida laws.

REVIEW OF FLORIDA'S FORM FILING PROCESS

How the Florida OIR Reviews Form Filings Subject to its Flood Statute

The Florida OIR coordinates with FEMA about training to educate forms analysts about the details and nuances of a federal NFIP policy. Forms analysts:

- Review the policy or endorsement and compare it to the NFIP policy.
- Review the provisions of the underlying policy that are not superseded by changes made in the endorsement.
- Make sure that the flood coverage in total (including definitions, deductibles, limits, conditions, property not covered, exclusions, etc.) are as broad as that provided under the NFIP policy.
- Exclude provisions, specific to the NFIP, that would not make sense to be in a private company's policy.

State Law Conflict

There are certain provisions in the federal private flood definition that may conflict with a state's law.

For example, the statute of limitations under the standard NFIP policy is one year after the date of denial. In Florida, the statute of limitations for most claims is five years from the date of loss. The insurer could use the standard NFIP provision, or the insurer could use a provision such as one year after the date of denial of a claim or five years from the date of the loss, whichever is greater. The modified provision would be considered as providing better coverage.

Another potential area in which there could be conflict between the standard NFIP policy and state law is the requirement for notice of cancellation. The NFIP requires 45 days, which may be more or less than state provisions.

In Florida, to comply with the flood statute or other than Flexible or Supplement flood insurance, the insurer would have to give at least 45 days notice.

The general filing requirement for forms is found in S. 627.410, F.S., which requires the Florida OIR to approve forms before use.

For commercial flood coverage, the insurer has the option to file the forms as informational pursuant to S. 627.4102, F.S.

FLORIDA RATE PROCESS EXAMPLE

Florida allows insurers to offer personal residential flood insurance coverage that meets the requirements of the flood statute. Insurers may decide to either submit the rate filings subject to the normal filing requirements of review and approval or (until Oct. 1, 2025) submit the filing for informational purposes.

Personal residential flood insurance rates submitted for informational purposes are subject to examination by the Florida OIR for a period of two years from the effective date to determine if the rates are excessive, inadequate or unfairly discriminatory.

If the coverage does not meet the requirements of the "flood statute," the rate filing is subject to the normal filing requirements of review and approval. Commercial non-residential property rates (including that for flood coverage) are informational due to a separate provision of Florida laws, and they are an exception to these filing requirements.

FLORIDA FLOOD STATUTE – FLOOD POLICY TYPES

Florida's flood statute (S. 627.715, F.S.) sets up five types of flood coverage that may be written using the special deviations allowed for flood insurance.

- *Standard flood insurance (equivalent to coverage provided under the standard flood policy under the NFIP).*
- *Preferred flood insurance.*
- *Customized flood insurance.*
- *Flexible flood insurance.*
- *Supplemental flood insurance.*

Flexible and supplemental coverage are the only flood coverage types under the statute that do not require flood insurance coverage to meet or exceed what is provided under the standard NIFP policy. Flexible coverage must provide coverage for the peril of flood as defined by the statute (which mirrors that of the NFIP). However, there are ancillary coverages that are not required to be provided.

APPENDIX II – BARRIERS TO THE RESIDENTIAL PRIVATE FLOOD INSURANCE MARKET

Flood Coverage Being "At Least as Broad as" the NFIP

Biggert-Waters specifies that private flood insurance satisfies the mandatory purchase mortgage requirement when a private flood insurance policy affords coverage that is "at least as broad as" the coverage offered by an NFIP flood insurance policy.[18]

Since there was not a federal banking rule in place regarding private flood insurance following the passage of Biggert-Waters, it was challenging to implement the use of private flood insurance for the mandatory purchase mortgage requirement. Some lending institutions thought that they did not have the knowledge necessary to assess whether a flood insurance policy met the definition of private flood insurance set forth in Biggert-Waters.

The federal banking rule became effective July 1, 2019. The rule fulfills the condition in Biggert-Waters that regulated lending institutions accept private flood insurance policies satisfying the conditions specified in the Act. Furthermore, the federal banking rule allows lending institutions to accept an insurer's written assurances stated in a private flood insurance policy that the appropriate criteria is met. The rule also permits lending institutions to accept some flood insurance coverage plans provided by mutual aid societies.

Theoretically, the federal banking rule removes the acceptance of private flood insurance as a barrier to the private flood insurance market. However, educating the banking industry is clearly still needed as state insurance regulators are still hearing that lenders are telling borrowers that the only flood insurance policy that is acceptable is an NFIP flood policy. Thus, further education regarding the federal banking rule needs to be done. States may want to consider drafting a bulletin that can be used for these purposes.

Lenders may accept private flood insurance that meets the "discretionary acceptance" definition, which states that lending institutions may accept private flood insurance policies that do not meet the "mandatory acceptance" requirements, provided that certain conditions are met, such as that the policy provides sufficient protection of the loan, consistent with general safety and soundness principles.[19] This distinction may be important for insurers with a product designed with higher-deductible options and/or a shorter cancellation notice for nonpayment of premiums.

Finally, many property owners are not required to purchase flood insurance because their home is outside of a Special Flood Hazard Area (SFHA) or because they do not have a federally backed mortgage. As a result, any flood insurance policy covering such properties is not required to be as broad as the NFIP policy.

Continuous Coverage

If an NFIP policy holder lets an NFIP policy lapse, by either not paying premium or going to a private flood insurer, any subsidy the NFIP policy holder would have received is immediately eliminated.[20] Legislation currently being considered by Congress to reauthorize the NFIP includes the ability of policyholders to leave the NFIP in order to purchase a private flood insurance policy and then return to the NFIP without penalty.

[18] 42 U.S.C §4012a(b).
[19] Ibid
[20] As required by §100205(a)(1)(B) of Biggert-Waters (P.L. 112-141, 126 Stat. 917), only for NFIP policies that lapsed in coverage as a result of the deliberate choice of the policyholder.

Non-Compete Clause

FEMA dropped its non-compete clause in 2018. FEMA now allows Write Your Own (WYO) companies to sell NFIP policies. Therefore, this is no longer a barrier.

NFIP Subsidized Rates

One of the hurdles facing private flood insurance growth involves the NFIP's subsidized rates, as NFIP premiums do not always reflect the full risk of flooding. NFIP rates allow certain policyholders to have more affordable premiums. Additionally, NFIP rates do not incorporate profit, which is an important element for private flood insurers.[21] Private flood insurers need to charge rates that represent the full risk of the peril.[22]

If the NFIP were to reform its rate structure to collect full-risk rates, it might result in the encouragement of more private insurers to write policies in the private flood insurance market. Full-risk NFIP rates would fall closer to what a private insurer would charge. It is important to note that full-risk rates would likely lead to higher rates than those that currently exist.[23]

Presently, FEMA is in the process of redesigning its rating system. The new NFIP rating system will be known as Risk Rating 2.0. This new rating structure will add replacement cost value and consider the distance between a property and a source of water. Additionally, Risk Rating 2.0 takes into consideration things that are not reflected in the current rating structure, such as intense rainfall.[24] As stated previously it was recently announced that Risk Rating 2.0 will be delayed until Oct. 1, 2021 to allow for more analysis on its impact.

Ability to Assess Flood Risk Accurately

On June 11, 2019, the NFIP released data on flood losses and claims. Prior to the release of this data, insurers viewed the lack of access to NFIP data on flood losses and claims as a barrier for private companies offering flood insurance.

For private flood insurers to manage and diversify their risk exposure, consumer participation to manage and diversify their risk exposure is required. Many private insurers have expressed the view that broader participation in the flood insurance market would be necessary to address adverse selection and maintain a sufficiently large risk pool.[25]

An established goal of the NFIP is to increase the number of flood insurance policies in force. Even though there is a mandatory purchase requirement for homeowners to purchase flood insurance in certain flood zones, this does not always occur.

As more insurers begin to write private flood insurance, it is likely that consumers will be offered more choices. Private flood insurers may also offer coverages not available through the NFIP. These coverages might include coverage such as basement coverage, business interruption, additional living expenses, etc. Private insurers might also be able to offer higher coverage limits than those offered by the NFIP.

[21] *www.floods.org/ace-files/documentlibrary/committees/Insurance/Emerging_Flood_Insurance_Market_Report-Wharton-07-13-18.pdf.*
[22] Ibid.
[23] Ibid.
[24] Ibid.
[25] GAO, Jan. 22, 2014. "Flood Insurance: Strategies for Increasing Private Sector Involvement," 14–127, accessed online at *https://www.gao.gov/products/GAO-14-127.*

Private flood insurance offered as an endorsement to a standard homeowners insurance policy could possibly eliminate instances where it is necessary to differentiate between flood and wind damage.[26]

[26] CRS, May 7, 2019. "Private Flood Insurance and the National Flood Insurance Program," accessed online at *https://www.everycrsreport.com/files/20190507_R45242_968aced5ccda33b36e57f26022e80552ffa6f32d.pdf.*

PROJECT HISTORY

Catastrophe Insurance (C) Working Group's
Considerations for State Insurance Regulators in Building the Private Flood Insurance Market

1. Description of the project, issues addressed, etc.

The Property and Casualty Insurance (C) Committee referred the charge of writing a document to discuss things state insurance regulators could do to build the private flood insurance market to the Catastrophe Insurance (C) Working Group.

The considerations document is a document the state insurance departments can use to provide state insurance regulators with things their department of insurance (DOI) can do to help build the private flood insurance market in their state. The considerations document provides information regarding state actions that can be taken, including: 1) supporting private flood insurance legislation; 2) approving private flood insurance products; 3) tailoring rate and form requirements for private flood insurance coverage; 4) allowing private flood insurers to submit rates on an informational basis; 5) removing diligent search requirements; 6) conducting consumer outreach; 7) listing private flood insurance products on a DOI website; 8) conducting agent education; 9) implementing specific continuing education (CE) requirements for producers; 9) increasing the weighing of flood insurance questions on producer licensing exams; and 10) conducting agent education.

The considerations document provides detailed information regarding ways in which state DOIs can apply the information listed above to enhance the private flood insurance market in their state. The Catastrophe Insurance (C) Working Group plans to continue building on this document by including information used by additional states as the private flood insurance market grows.

2. Name of group responsible for drafting the model and states participating.

The Catastrophe Insurance (C) Working Group of the Property and Casualty Insurance (C) Committee was responsible for drafting the considerations document and formed a drafting group to draft the document. Participating states included: Alabama; Connecticut; Florida; Illinois; Louisiana; Mississippi; Missouri; Pennsylvania; Rhode Island; South Carolina; and Texas.

3. Project authorized by what charge and date first given to the group.

The project was authorized by the charges of the Catastrophe Insurance (C) Working Group of the Property and Casualty Insurance (C) Committee to: "Continue to examine ways to help state insurance regulators facilitate the private flood insurance market."

4. A general description of the drafting process (e.g., drafted by a subgroup, interested parties, the full group, etc.). Include any parties outside the members that participated.

In 2018, the Catastrophe Insurance (C) Working Group began discussing items to be included in a private flood document to aid state insurance regulators regarding helping states enhance and/or develop a private flood insurance market in their states. The Working Group formed a drafting group to work on the document. The drafting group met via conference call on a frequent basis to complete the drafting of the document.

5. A general description of the due process (e.g., exposure periods, public hearings or any other means by which widespread input from industry, consumers and legislators was solicited).

The drafting group of the Catastrophe Insurance (C) Working Group met regularly via conference call, during which the Working Group heard comments and discussed suggested revisions from state insurance regulators. Following the drafting of the document, the document was exposed on July 10, 2019, for a 30-day public comment period. The considerations document was adopted by the Catastrophe Insurance (C) Working Group on Aug. 3, 2019. The considerations document was then adopted by the Property and Casualty Insurance (C) Committee during its Aug. 5, 2019, meeting at the 2019 Summer National Meeting.

6. A discussion of the significant issues (items of some controversy raised during the due process and the group's response).

There were no items of controversy raised during the due process.

7. Any other important information (e.g., amending an accreditation standard).

Not applicable.

W:\National Meetings\2020\Summer\Plenary\Att 6 ConsiderationsofPrivateFlood_Final 2-7-20.pdf

NAIC CONTINUING EDUCATION RECIPROCITY (CER) AGREEMENT - 2019 VERSION

Adopted by the Market Regulation and Consumer Affairs (D) Committee Dec. 9, 2019
Adopted by the Producer Licensing (D) Task Force Dec. 7, 2019

Whereas, the Commissioners find that it is in the best interest of each of their states and insurance producers to simplify the CER course approval process and reduce barriers to non-resident continuing education (CE) providers.

Whereas, the undersigned Insurance Commissioners of the NAIC, hereafter the Commissioners, have determined that it is redundant for each state to perform a substantive review of CE courses or individual instructors that have previously been approved by another state.

Definitions:

Home State: the state in which the CE provider organization maintains his, her or its principal place of residence or principal place of business.

Home State Course Approval: approval of a course that has had a substantive review in a home state.

Reciprocal State: state other than the home state and a party to this CER agreement.

Substantive Review: a thorough review of the course to confirm compliance with the home state's applicable laws and regulations for the approval of insurance CE. The review includes a determination of whether the:

i. Subject matter meets the criteria for insurance education, to include approvable and non-approvable topic guidelines.

ii. Provider has procedures for reviewing course material in order to keep itup to date and timely.

iii. Course design and instructional strategies are appropriate for the method of delivery.

iv. Credit hours are properly calculated based on the instruction method.

v. Criteria for completing the course meets the standards applicable to the instruction method.

The Commissioners agree as follows:

1. Each state will conduct a substantive review of CE courses submitted for home state approval. When a CE provider has received a **home state course approval**, a **reciprocal state** will not conduct a **substantive review** of that same course as a condition of approval. A CE provider's **home state** means the state in which the CE provider organization maintains his, her or its principal place of residence or principal place of business. If the laws or regulations of the **home state** restrict or limit the minimum or maximum number of credit hours for which a course may be approved for in that state, or restricts certain course topics, the CE provider may elect to recognize another **home state** in order to obtain a **home state course approval**.

2. Unless specifically limited by state laws and regulations, a reciprocal state will award a course the same number of credits as approved by the CE provider's home state.

3. A reciprocal state agrees to approve a course submission within 30 days of receipt, provided that the course is filed using the NAIC Uniform CER Course Filing Form (Appendix A) or an equivalent electronic submission method and contains a **home state course approval**.

4. Each state will accept the NAIC Uniform CER Course Filing Form (Appendix A), or a substantially similar form, including an equivalent electronic submission method, and the required home state course approval document as the sole requirement for a reciprocal course submission.

5. Each state accepts and will use the following standards for substantive course reviews:

   a. For classroom and webinar courses, one credit will be awarded for every 50 minutes of contact instruction.

   b. For self-study/online courses, credit will be awarded based on the NAIC's Recommended Continuing Education Guidelines for Online Courses and Course Guidelines for Classroom Webinar/Webcase Delivery (Appendix B and Appendix C).

   c. The minimum number of credits that will be awarded is one credit; no partial credits will be awarded, and there is no maximum number of credits.

   d. Credits will only be awarded for courses whose subject matter will increase technical knowledge of insurance principles, coverages, ethics, laws or regulations and will not be awarded for topics such as personal improvement, motivation, time management, supportive office skills or other matters not related to technical insurance knowledge. If any credits are awarded for sales and/or marketing, those credits will be separately noted on the course approval document. Credits for sales and/or marketing will only be awarded in states that are permitted by law or regulation to accept credit for those topics. Additional guidance can be found in the NAIC's Recommended Approved/Not Approved Course Topics (Appendix D).

   e. Each state will use its own method to determine if an instructor is qualified, and no instructor will be approved unless the CE provider has provided sufficient information to demonstrate that the instructor is qualified, according to that state's laws and regulations, to teach the topics covered in the outline.

6. A state's course approval document or approved course application will include, at a minimum, the following information: course title, credit hours, credit category, method of instruction, and if it is a **home state** approval.

7. Each state reserves the right to disapprove individual instructors or CE providers who have been the subject of disciplinary proceedings or have otherwise failed to comply with a state's laws and regulations.

8. Each state agrees that it will notify other states when a CE provider or instructor has been the subject of a formal administrative action or other disciplinary action by that state.

APPENDIX A

Adopted by NAIC Membership April 2019.

UNIFORM CONTINUING EDUCATION RECIPROCITY COURSE FILING FORM

Please clearly print or type information on this form. Thank you for helping us promptly process your application.

Provider Information

Provider Name					FEIN # (if applicable)
Contact Person		E-mail Address of Contact Person			
Phone Number ( ) - ext.	Fax Number ( ) -	Home State	Home State Provider #	Reciprocal State	Reciprocal State Provider #
Mailing Address		City		State	Zip
Submitter Name (if different from provider contact person above)					
Submitter Phone Number		E-mail Address of Submitter			

Course Information

Course Title	
Date of Course Offering (if applicable)	Existing Course Number (if applicable)

Method of Instruction

Non-Contact / Asynchronous*	**Contact / Synchronous***
Self – Study	**Classroom**
☐ Correspondence	☐ Seminar/Workshop
☐ On-Line Training (Self-Study)	☐ Other _____
☐ Recorded Media	**Webinar**
☐ Other _____	☐ Virtual Class/Webinar/Video Conference
Word Count _____	☐ Other _____
Mandatory Run-time _____ (Interactive Components of Course)	

Measurement used for successful completion: ☐ Attendance ☐ Final Exam ☐ Other _____

Is this course open to the public? ☐ Yes ☐ No

National Designation? ☐ Yes ☐ No
If yes, Designation Type: _____

Difficulty (Check): ☐ Basic ☐ Intermediate ☐ Advanced

Credit Hours Requested and Course/Hours Decision

Course Concentration	Hrs Requested by Provider		Hrs Approved by Home State		Hrs Approved by Reciprocal State	
	Sales/Mktg	Insurance	Sales/Mktg	Insurance	Sales /Mktg	Insurance
A. Producer Topics: (Circle Appropriate Course Concentration)						
Life / Health						
Property / Casualty/Personal Lines						
Ethics						
General (Applies to all lines)						
Insurance Laws						
Other (LTC, NFIP, Viaticals, Annuities, etc.) _____						
Total Hours						
B. Adjuster Topics (Circle Appropriate Course Concentration)						
General						
Workers Comp						
Ethics						
Other _____						
Total Hours						
C. Public Adjuster (Circle Appropriate Course Concentration)						
General						
Ethics						
Other _____						
Total Hours						
Information Below is for Regulator Use Only						
Approval Date						
Course Number assigned						
Course approval expiration date						
Signature of Home State Regulator/Representative **OR** ATTACH Provider Home State Approval Form						
Signature of Reciprocal State Regulator/Representative **OR** ATTACH Reciprocal State Approval Form						

INSTRUCTION SHEET

NOTE: This course may NOT be advertised or offered as approved in the state to which application has been made until approval has been received from the insurance department.

1. **If you are a PROVIDER filing for approval from the Home State:**
   - *1.1* Complete all the fields in the "Provider Information" section except "Reciprocal State" and the adjacent "Provider #" fields.
   - *1.2* Complete the Course Information Section.
   - *1.3* In the "Credit Hours Requested and Course/Hours Decision" section, complete the "Hrs. Requested by Provider" columns, detailing in the respective columns the number of hours for sales – and marketing-related instruction and the number of hours for other insurance-related instruction. Please note the following:
     - 1.3.1 When using this application, which is governed by the NAIC CE Reciprocity Agreement in conjunction with 'states' laws, only whole numbers of credit hours will be approved – partial hours will be eliminated.
     - 1.3.2 States that approve sales/marketing topics will consider the hours in the "sales/Mktg" column and the hours in the "Insurance" column when deciding the number of hours to approve. States that do not permit sales/marketing topics as part of continuing education credit hours will only consider the hours shown in the "Insurance" column when making their credit-hour approval decisions.
     - 1.3.3 Contact the individual state to determine whether there are any state specific requirements for submitting courses.
   - *1.4* Submit the application form along with required course materials, a detailed course outline, instructor information, if required, and the required course application fee.

2. **If you are a PROVIDER filing for approval from a Reciprocal State:**
   - *2.1* Make a sufficient number of photocopies of the Home State approval form to enable you to submit a copy of this application to each of the Reciprocal States where you are seeking credit.
   - *2.2* On each application, write the Reciprocal State and the provider number assigned to you by that state in the "Reciprocal State" and adjacent "Provider #" fields.
   - *2.3* Send the CER application, home state approval, if home state issues one, a detailed course outline, and the required fee to the reciprocal state. If this is a National Course *, the Providers will be allowed to submit an agenda that must include date, time, each topic and event location in lieu of a detailed course outline.
   - *2.4* Subsequent national course offerings should only be reported for events that are conducted in the "home" state.

* **National Course** is defined as an approved program of instruction in insurance related topics, offered by an approved provider, and leads to a national professional designation or is a course offered to individuals who must update their designation once it is earned.

3. **If you are the HOME STATE or designated representative of the Home State:**
   - *3.1* After reviewing the course materials, complete the "Hrs Approved by Home State" column.
     - 3.1.1 Multiple types of credit and delivery methods can be approved using one CER Form.
   - *3.2* Enter the date of approval, course # assigned, course approval expiration date. Sign the CER Form <u>OR</u> attach the home state approval form.
   - *3.3* If the course is not approved, note it on the bottom of the CER Form.

4. **If you are the RECIPROCAL STATE or designated representative of the Reciprocal State:**
   - *4.1* After reviewing "Hrs approved by Home State" complete the "Hrs Approved by Reciprocal State".
     - 4.1.1 It is unnecessary for each state to perform a substantive review of continuing education courses that have previously been approved by the Home State.
     - 4.1.2 Reciprocal states cannot award different credits than the home state unless certain aspects are not allowed by state law.
   - *4.2* Enter the date of approval, course number assigned, course approval expiration date. Sign the CER Form <u>OR</u> attach the reciprocal state approval form.
   - *4.3* If the course is not approved, note it on the bottom of the CER Form.
   - *4.4* The reciprocal state agrees to approve the CER submission within 30 days of receipt.

Substantive Review – A thorough review of the course to confirm compliance with the home state's applicable laws and regulations for the approval of insurance continuing education. The review includes a determination whether the:

1. Subject matter meets the criteria for insurance education, to include approvable and non-approvable topic guidelines;
2. Provider has procedures for reviewing course material in order to keep it up to date and timely;
3. Course design and instructional strategies are appropriate for the method of delivery;
4. Credit hours are properly calculated based on instruction method;
5. Criteria for completing the course meets the standards applicable to the instruction method.

***Drafting Note**: The instructor information matrix was eliminated in 2018 as this information should be readily available on individual state/jurisdiction websites.

APPENDIX B

Continuing Education Recommended Guidelines for Online Courses

Adopted by NAIC Membership March 2015.

Goal: To deliver functional computer-based internet courses that offer quality insurance and/or risk management material in a password-protected online environment.

Key Components:

- Material that is current, relevant, accurate, and that includes valid reference materials, graphics and interactivity.
- Clearly defined objectives and course completion criteria
- Specific instructions to register, navigate and complete the course work
- Technical support/provider representative should be available during business hours and response provided within 24hours of initial contact.
- Instructors/subject matter experts must be available to answer student questions during provider business hours
- Process to authenticate student identity such as passwords and security prompts
- Method for measuring the student's successful completion of course which includes the material, exam and any proctor requirements.
- Process for requesting and receiving CE course-completion certificate and reporting student results to the appropriate regulator
- Require each agent to enroll for the course before having access to course material.
- Prevent access to the course exam before review of the course materials.
- Prevent downloading of any course exam.
- Provide review questions at the end of each unit/chapter and prevent access to the final exam until each set of questions are answered at a 70% rate.
- Provide final exam questions that do not duplicate unit/chapter questions.
- Prevent alternately accessing course materials and course exams. This does not apply if the state allows for "open book" exams.
- Have monitor affidavit containing specific monitor duties and responsibilities printed for monitor's use to direct the taking of the final exam. Monitor will complete the affidavit after the exam is completed. (This only for states that require a monitored exam).

Final Assessment (exam) Criteria:

- Minimum of 10 questions for 1 credit hour course with additional 5 questions for each subsequent credit hour and a score of 70% or greater
- At least enough questions to fashion a minimum of 2 versions with a least 50% of questions being new/different in each subsequent version
- Inability to print the exam or to view the exam prior to reviewing material
- Proctor, if required by the state, who verifies identity by photo identification and processes affidavit testifying the student received no outside assistance

Procedures to determine Appropriate Number of Credit Hours:

Word Count/Difficulty Level

- Divide total number of words by 180 (documented average reading time) = number of minutes to read material
- Divide number of minutes by 50 = credit hours
- Course difficulty level is identified by the CE provider on the CER form and should be based on the NAIC CE Standardized Terms-Definitions for basic, intermediate and advanced course difficulty levels.
- Multiply number of hours by 1.00 for a basic level course; 1.25 for an intermediate level; 1.50 for an advanced course for additional study time = total number of credit hours (fractional hours rounded up if .50 or above and rounded down if .49 or less)

Interactive Course Content

- Elements included in the online course, in addition to text, such as video, animation, interactive exercises, quizzes, case studies, games, and simulations.
- Interactive elements should be applicable to course material and facilitate student learning.
- Only mandatory interactive elements should be included in the calculation of CE credit hours.
- Calculation of CE hour credits should be based on the run time of the interactive elements.
- CE providers will indicate run time of the interactive elements in the course content and upon request provide access to the state for review of the course.

Professional Designation Course

- Course that is part of a nationally recognized professional designation
- Credit hours equivalent to hours assigned to the same classroom course material

Final Assessment

- Time spent completing the final assessment should not be used in calculation of CE credit hours.

Adopted by the NAIC Membership March 2015

APPENDIX C

COURSE GUIDELINES FOR CLASSROOM WEBINAR/WEBCAST DELIVERY

Adopted by NAIC Membership April 2014.

- These guidelines are intended to apply to courses conducted and viewed in real time (live) in all locations and are not intended to apply when courses have been recorded and are viewed at a later time or to other online courses.
- Each student will be required to log in to the webinar using a distinct username, password and/or email. Students that view webinars in group settings which is two or more individuals should alternatively verify their participation in the form of sign-in and sign-out sheets submitted by a monitor with an attestation or verification code.
- The provider will verify the identity and license number, or National Producer Number (NPN), of all students.
- A provider representative, using computer-based attendance-monitoring technology, must monitor attendance throughout the course.
- The provider must have a process to determine when a participant is inactive or not fully participating, such as when the screen is minimized, or the participant does not answer the polling questions and/or verification codes.
- For webinars not given in a group setting, no less than two polling questions and/or attendance verification codes must be asked, with appropriate response provided, at unannounced intervals during each one-hour webinar session to determine participant attentiveness.
- The provider will maintain an electronic roster to include records for each participant's log-in/log-out times. If required by states chat history and polling responses should be captured as part of the electronic record.
- When a student is deemed inactive or not fully participating in the course by the course monitor of failure to enter appropriate polling question response or verification codes, continuing education (CE) credit is denied.
- All students and the instructor do not need to be in the same location.
- Students in all locations must be able to interact in real time with the instructor. Students should be able to submit questions or comments at any point during the webinar session.
- The course pace must be set by the instructor and does not allow for independent completion.
- Instruction time is considered the amount of time devoted to the actual course instruction and does not include breaks, lunch, dinner or introductions of speakers.
- One credit will be awarded for each 50 minutes of webinar/webcast instruction, and the minimum number of credits that will be awarded for webinar/webcast courses is one credit.
- The provider must have a procedure that informs each student in advance of course participation requirements and consequences for failing to actively participate in the course.
- A comprehensive final examination is not required.

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APPENDIX D

RECOMMENDED APPROVED/NOT APPROVED TOPICS FOR CE CREDIT

Adopted by NAIC Membership August 2018.

Approved Topics

1. Actuarial mathematics, statistics and probability – in relation to insurance
2. Assigned risk – in relation to insurance
3. Claims adjusting
4. Courses leading to and maintaining insurance designations
5. Employee benefit plans – in relation to insurance
6. Errors and omissions – in relation to insurance
7. Estate planning/taxation – in relation to insurance
8. Ethics
9. Fundamentals/principles of insurance (including but not limited to: annuities, crop and hail, life, accident and health, property/casualty [P/C], etc.)
10. Insurance accounting/actuarial considerations
11. Insurance contract/policy comparison and analysis
12. Insurance fraud
13. Insurance laws, rules, regulations and regulatory updates
14. Insurance policy provisions
15. Insurance product-specific knowledge
16. Insurance rating/underwriting/claims
17. Insurance tax laws
18. Legal principles – in relation to insurance
19. Long-term care/partnership
20. Loss prevention, control and mitigation – in relation to insurance
21. Managed care
22. Principles of risk management – in relation to insurance
23. Proper uses of insurance products
24. Real Estate Settlement Procedures Act (RESPA) – in relation to insurance
25. Restoration – addresses claims, loss control issues and mitigation – in relation to insurance
26. Retirement planning – in relation to insurance
27. Securities – in relation to insurance
28. Suitability in insurance products
29. Surety bail bond
30. Underwriting principles – in relation to insurance
31. Viaticals/life settlements – in relation to insurance

Other topics approved that contribute substantive knowledge relating to the field of insurance and expands competence of the licensee.

NAIC National Association of Insurance Commissioners

RECOMMENDED APPROVED/NOT APPROVED TOPICS FOR CE CREDIT

Adopted by NAIC Membership August 2018.

Not Approved Topics

1. Automation
2. Clerical functions
3. Computer science
4. Computer training/skills or software presentations
5. Courses on investments – stocks, bonds, mutual funds, Financial Industry Regulatory Authority (FINRA)/U.S. Securities and Exchange Commission (SEC) compliance (National Association of Securities Dealers [NASD]/SEC), etc.
6. Courses that are primarily intended to impart knowledge of specific products of specific insurers
7. Customer service
8. General management training
9. Goal-setting
10. Health/stress/exercise management
11. Marketing/telemarketing
12. Motivational training
13. Company and vendor-specific product launches
14. Office skills or equipment or procedures
15. Organizational procedures and internal policies of an individual insurer
16. Personal improvement
17. Prospecting
18. Psychology
19. Relationship building
20. Restoration – promoting products or services
21. Sales training
22. Service standards or service vendors
23. Time management

Other topics or courses not related to insurance knowledge or competence of the licensee.

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(Traditional insurers) Nov. 15, 2019 referral adopted by the Financial Regulation Standards and Accreditation (F) Committee – Dec. 7, 2019

(Risk retention groups) In addition, the March 3, 2020 referral also attached will be considered for adoption by the Financial Regulation Standards and Accreditation (F) Committee on August 12, 2020. This referral clarifies that the model provisions in the Nov. 15 referral also apply to risk retention groups. It is recommended , for clarity purposes, the Executive (EX) Committee and Plenary consider adoption of both referrals at the same time.

MEMORANDUM

To: Financial Regulation Standards and Accreditation (F) Committee

From: Reinsurance (E) Task Force

Date: November 15, 2019

Re: 2019 Revisions to *Credit for Reinsurance Model Law* (#785) and *Credit for Reinsurance Model Regulation (#786)*

Executive Summary

On June 25, 2019, the NAIC Executive (EX) Committee and Plenary unanimously adopted revisions to the NAIC *Credit for Reinsurance Model Law* (#785) and *Credit for Reinsurance Model Regulation* (#786). These revisions were intended to incorporate the relevant provisions of the "Bilateral Agreement Between the United States of America and the European Union on Prudential Measures Regarding Insurance and Reinsurance" (Covered Agreement), which was signed on Sept. 22, 2017. The Covered Agreement would eliminate reinsurance collateral and local presence requirements for European Union (EU) reinsurers that maintain a minimum amount of own funds equivalent to $250 million and a solvency capital requirement (SCR) of 100% under Solvency II. Conversely, U.S. reinsurers that maintain capital and surplus equivalent to 226 million euros with a risk-based capital (RBC) of 300% of authorized control level would not be required to maintain a local presence in order to do business in the EU or post collateral in any EU jurisdiction. On Dec. 18, 2018, a similar Covered Agreement was signed with the United Kingdom (UK). In addition, the 2019 revisions extend similar treatment to Qualified Jurisdictions and accredited NAIC jurisdictions.

At the 2019 Summer National Meeting, Director Chlora Lindley-Myers (MO), Chair of the NAIC Reinsurance (E) Task Force, made the following recommendation to the Financial Regulation Standards and Accreditation (F) Committee: 1) the Committee recognize that states may begin adoption of provisions that are substantially similar to the 2019 revisions to Model #785 and Model #786 and remain in compliance with the *Reinsurance Ceded* accreditation standard; 2) the accreditation standard be modified in accordance with the normal processes and procedures outlined in the Accreditation Program Manual, and that the Task Force and Financial Condition (E) Committee prepare a formal recommendation to the Financial Regulation Standards and Accreditation (F) Committee for consideration at the 2020 Spring National Meeting; and 3) in the interim, states should be

EXECUTIVE OFFICE • 444 North Capitol Street NW, Suite 700 • Washington, DC 20001-1509 p | 202 471 3990 f | 816 460 7493
CENTRAL OFFICE • 1100 Walnut Street, Suite 1500 • Kansas City, MO 64106-2197 p | 816 842 3600 f | 816 783 8175
CAPITAL MARKETS & INVESTMENT ANALYSIS OFFICE • One New York Plaza, Suite 4210 • New York, NY 10004 p | 212 398 9000 f | 212 382 4207
www.naic.org

encouraged to adopt the 2019 revisions in the form adopted by Plenary within the 60-month timeframe set forth in the Covered Agreement to best avoid potential federal preemption. Committee Chair Commissioner Todd E. Kiser (UT) asked if there were any objections to the approach proposed in the referral from the Reinsurance (E) Task Force, and none were noted.

At its meeting on October 22, the Reinsurance (E) Task Force agreed to submit the following new recommendations to the Financial Regulation Standards and Accreditation (F) Committee:

1. The 2019 revisions to Model #785 and Model #786 should be adopted as a new accreditation standard by the NAIC, *Reciprocal Jurisdictions*, with significant elements as outlined in Attachment A.

2. The Financial Regulation Standards and Accreditation (F) Committee should consider a waiver of procedure as provided for in the Accreditation Program Manual and expeditiously consider adoption of this standard. The Task Force recommends that the accreditation standard become effective Oct. 1, 2022, the end of the 60-month period when federal preemption determinations must be completed, with enforcement of the standard to commence Jan. 1, 2023. **[Note: after the Oct. 22 conference call, NAIC staff had conversations with representatives of the Federal Insurance Office (FIO), in which they advised NAIC staff that in their opinion the end of the 60-month period when federal preemption determinations must be completed is Sept. 1, 2022].**

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

The current *Reinsurance Ceded* accreditation standard requires that state law shall contain the significant elements from Model #785 and Model #786. The models serve to provide regulators with an effective method of monitoring the reinsurance activities of U.S. companies. U.S. primary insurance companies may be given reinsurance credit on their statutory financial statements for insurance risk they transfer via reinsurance that meets the legal and accounting risk transfer requirements and other relevant laws. Both the 2011 revisions to the credit for reinsurance models, which served to reduce reinsurance collateral requirements for certified reinsurers domiciled in qualified jurisdictions, and the 2019 revisions with respect to Reciprocal Jurisdictions, address the reinsurance collateral requirements necessary for U.S. ceding companies to take credit for certain reinsurance transactions.

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

The *Dodd-Frank Wall Street Reform and Consumer Protection Act* provides that a state insurance measure shall be preempted to the extent that the Director of FIO "determines" that the measure is inconsistent with the covered agreement and results in less favorable treatment of a non-U.S. insurer domiciled in a foreign jurisdiction that is subject to a "covered agreement" than a U.S. insurer domiciled, licensed or otherwise admitted in that state. A "covered agreement" under Dodd-Frank is an agreement entered into between the U.S. and foreign government(s) on prudential measures with respect to the business of insurance or reinsurance that achieves a level of protection for consumers that is "substantially equivalent" to the level of protection under state law. The revisions to Model #785 and #786 are considered by the Reinsurance (E) Task Force to be consistent with the requirements of the Covered Agreements entered into with the EU and UK.

Article 9(4) of the Covered Agreements provide, as follows with respect to Implementation of the Agreement:

> 4.Provided that this Agreement has entered into force, **on a date no later than the first day of the month, 42 months after the date of signature of this Agreement [22 September 2017], the United States shall begin evaluating a potential preemption determination** under its laws and regulations with respect to any U.S. State insurance measure that the United States determines is inconsistent with this Agreement and results in less favourable treatment of an EU insurer or reinsurer than a U.S. insurer or reinsurer domiciled, licensed, or otherwise admitted in that U.S. State. Provided that this Agreement has entered into force, **on a date no later than the first day of the month 60 months after the date of**

> **signature of this Agreement [22 September 2017], the United States shall complete any necessary preemption determination** under its laws and regulations with respect to any U.S. State insurance measure subject to such evaluation. For the purposes of this paragraph, the United States shall prioritise those States with the highest volume of gross ceded reinsurance for purposes of potential preemption determinations. [Emphasis added].

To summarize, FIO may begin evaluating potential preemption "determinations[1]" 42 months after the signature of the Covered Agreement, or March 1, 2021. FIO must complete any necessary preemption determinations 60 months after signature, which they believe to be Sept. 1, 2022. In order to avoid potential federal preemption determinations by the FIO Director, each state should adopt the 2019 revisions to Model #785 and Model #786 in a timely manner.

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

The pre-2011 versions of Model #785 and Model #786 are currently part of the *Reinsurance Ceded* accreditation standard, and the significant elements have been adopted in substantially similar form by all NAIC-accredited jurisdictions. The 2011 revisions to these models implemented reinsurance collateral reduction for *Reinsurance Ceded to Certified Reinsurers* domiciled in qualified jurisdictions. At the current time, all NAIC accredited jurisdictions have adopted the 2011 revisions to Model #785, and only 5 jurisdictions have not adopted the 2011 revisions to Model #786, which became part of the accreditation standard effective January 1, 2019.

We are not currently aware of any states that have adopted the 2019 revisions to Model #785 and Model #786, although we have been advised that many states have begun their legislative processes for adoption of these revisions. We are not aware of any negative impact to any jurisdiction or its domiciliary ceding insurers that has adopted these revisions, which are similar in function and format to the Reciprocal Jurisdiction requirements of the 2019 revisions.

A statement as to the provisions needed to meet the minimum requirements of the standard. **That is, whether a state would be required to have "substantially similar" language or rather a regulatory framework. If it is being proposed that "substantially similar" language be required, the referring committee, task force or working group shall recommend those items that should be considered significant elements:**

The current accreditation standard for Model #785 and Model #786 requires state adoption on a substantially similar basis. In addition, the Covered Agreements themselves and the Dodd-Frank Act require that the United States cannot impose reinsurance collateral or local presence requirements that result in less favorable treatment for EU or UK reinsurers, and further that any state insurance measures cannot be inconsistent with the Covered Agreements. Therefore, the Reinsurance (E) Task Force recommends that the attached proposed significant elements for *Reciprocal Jurisdictions* (Attachment A) be adopted by NAIC-accredited jurisdictions in a "substantially similar" manner, as that term is defined in the Accreditation Interlineations of the NAIC Financial Regulation Standards and Accreditation Program. **Note: While the Task Force is recommending that the Committee adopt a "substantially similar" standard for accreditation purposes, it should be noted that Dodd-Frank requires the state insurance measure to be "consistent" with the Covered Agreement in order to avoid federal preemption, which may be interpreted as a higher standard. It is the recommendation of the Task Force that states adopt the 2019 revisions in close to identical form to the models in order to best avoid the possibility of federal preemption.**

An estimate of the cost for insurance companies to comply with the proposal and the impact on state insurance departments to enforce it, if reasonably quantifiable:

The NAIC has not performed a cost/benefit analysis with respect to the 2019 revisions to Model #785 and Model #786, nor do we believe that the specific costs for insurance companies to comply with the proposal and the impact on state insurance departments to enforce it are reasonably quantifiable.

[1] 31 U.S.C. §313(f) provides the process for making a "determination" in this context:

(2) Determination.—

(A) Notice of potential inconsistency.—Before making any determination under paragraph (1), the Director shall—

(i) notify and consult with the appropriate State regarding any potential inconsistency or preemption;

(ii) notify and consult with the United States Trade Representative regarding any potential inconsistency or preemption;

(iii) cause to be published in the Federal Register notice of the issue regarding the potential inconsistency or preemption, including a description of each State insurance measure at issue and any applicable covered agreement;

(iv) provide interested parties a reasonable opportunity to submit written comments to the Office; and

(v) consider any comments received.

***

(C) Notice of determination of inconsistency.—Upon making any determination under paragraph (1), the Director shall—

(i) notify the appropriate State of the determination and the extent of the inconsistency;

(ii) establish a reasonable period of time, which shall not be less than 30 days, before the determination shall become effective; and

(iii) notify the Committees on Financial Services and Ways and Means of the House of Representatives and the Committees on Banking, Housing, and Urban Affairs and Finance of the Senate.

(3) Notice of effectiveness.—Upon the conclusion of the period referred to in paragraph (2)(C)(ii), if the basis for such determination still exists, the determination shall become effective and the Director shall—

(A) cause to be published a notice in the Federal Register that the preemption has become effective, as well as the effective date; and

(B) notify the appropriate State.

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10. Reinsurance Ceded

State law should contain the NAIC *Credit for Reinsurance Model Law* (#785), the NAIC's *Credit for Reinsurance Model Regulation* (#786) and the NAIC *Life and Health Reinsurance Agreements Model Regulation* (#791) or substantially similar laws.

REFERENCE

Credit for Reinsurance Model Law (#785)

a. Credit allowed for reinsurance ceded to a licensed insurer? _____

b. Credit allowed for reinsurance ceded to an accredited insurer who meets requirements similar to those in Section 2B and ~~2I~~2J of the model law? _____

c. Credit allowed for reinsurance ceded to an insurer domiciled and licensed in a state which employs substantially similar standards regarding credit for reinsurance and who maintains capital and surplus of at least $20,000,000 and submits to this states authority to examine its books and records? _____

d. Credit allowed for reinsurance ceded to an insurer who maintains a trust fund, established in a form approved by the commissioner, in a qualified U.S. financial institution for the payment of the valid claims of its U.S. policyholders and ceding insurers, their assigns and successors in interest and who reports financial information annually to the commissioner to determine the sufficiency of the trust fund? _____

e. In instances where reinsurance is ceded to insurers maintaining a trust fund, trustees of the trust required to report to the department annually, on or before February 28, the balance of the trust and a listing of the trust's assets as of the end of the year and a certification of the date of termination of the trust, if so planned, or certify that the trust shall not expire prior to the next following December 31? _____

f. Credit for reinsurance allowed under c. or d. above only permitted where assuming insurer agrees in the reinsurance agreements: 1) that in the event of a failure of the assuming insurer to perform its obligations, the assuming insurer shall submit to the jurisdiction of any court of competent jurisdiction in any state of the U.S.; and 2) to designate the commissioner or a designated attorney as its true and lawful attorney upon whom may be served any lawful process instituted by or on behalf of the ceding company? _____

g. Credit allowed for reinsurance ceded to an insurer not meeting the requirements of a., b., c., or d. above, or with respect to a certified reinsurer described below, in an amount not exceeding the liabilities carried by the ceding insurer and only in the amount of funds held by or on behalf of the ceding insurer in the form of cash, securities listed by the Securities Valuation Office of the NAIC, including those deemed exempt from filing as defined by the *Purposes and Procedures Manual of the Securities Valuation Office,* and qualifying as admitted assets, clean, irrevocable, unconditional letters of credit, and other forms of security acceptable to the commissioner? _____

h. Ceding insurers must be subject to notification requirements with respect to reinsurance concentration risk substantially similar to those in Section ~~2J~~2K of Model #785. _____

Life and Health Reinsurance Agreements Model Regulation (#791)

i. Scope similar to Section 3? _____

j. No insurer, for reinsurance ceded establishes any asset or reduces any liability due to the terms of the reinsurance agreement, in substance or effect if any of the conditions in Section 4A exist? _____

k. Agreements entered into after the effective date of this regulation which involve the reinsurance of business issued prior to the effective date of agreements, along with subsequent amendments shall be filed by the ceding company with the commissioner within 30 days from the execution date along with attachments noted in Section 4C(1)? _____

l. Any increase in surplus net of federal income tax resulting from arrangements described in Section 4C(1) to be reported as described in Section 4C(2)? _____

m. Written agreements with provisions similar to Section 5? _____

n. Insurers required to reduce to zero any reserve credits or assets established with respect to existing reinsurance agreements entered into prior to the effective date of this regulation which would not be recognized under the provisions of this regulation? _____

Credit for Reinsurance Model Regulation (#786)

o. Credit for reinsurance allowed for reinsurance ceded by domestic insurers to assuming insurers that were licensed in the state as of the last date of the ceding insurers' statutory financial statement? _____

p. Credit for reinsurance provisions for accredited reinsurer similar to Section 5? _____

q. Credit for reinsurance provisions for reinsurers licensed and domiciled in other states similar to Section 6? _____

r. Credit for reinsurance provisions for reinsurers maintaining trust funds similar to Section 7? _____

s. Credit for reinsurance required by law similar to Section ~~9~~10? _____

t. Reduction from liability for reinsurance ceded to an unauthorized assuming insurer similar to Section ~~10~~11? _____

u. Provisions for trust agreements similar to Section ~~11~~12? _____

v. Provisions for letters of credit similar to Section ~~12~~13? _____

w. Provisions for unencumbered funds similar to Section ~~13~~14? _____

x. Provisions for reinsurance contracts similar to Section ~~14~~15? _____

y. The adoption of Form AR-1—Certificate of Assuming Insurer. _____

Reinsurance Ceded to Certified Reinsurers

z. A state's laws and regulations shall allow credit for reinsurance ceded to a certified reinsurer, including affiliated reinsurance transactions. Its laws and regulations shall contain provisions that are substantially similar to those applicable to certified reinsurers contained in Section 2E of Model #785 and Section 8 of Model #786.

i. The credit allowed is based upon the security held by or on behalf of the ceding insurer in accordance with the rating assigned to the certified reinsurer by the commissioner? The amount of security required in order for full credit to be allowed shall not be less than that required under Section 8A(1) of Model # 786. _____

ii. The security provided by the certified reinsurer is in a form consistent with the provisions of Section 2E(5) of Model #785 and Section 8A of Model #786? _____

iii. The commissioner requires the certified reinsurer to post 100% security upon the entry of an order of rehabilitation, liquidation or conservation against the ceding insurer? _____

iv. A state's laws or regulations shall include provisions for granting a certified reinsurer a deferral period for posting security applicable to catastrophe recoverables, substantially similar to Section 8A(4) of Model #786. The deferral period shall not exceed one year from the date of the first instance of a liability reserve entry by the ceding company as a result of a loss from a catastrophic occurrence as recognized by the commissioner, and shall not apply to lines of business other than those provided in Section 8A(4) of Model #786. _____

v. Credit for reinsurance ceded to a certified reinsurer shall apply only to reinsurance contracts meeting requirements substantially similar to Section 8A(5) of Model #786?

aa. In order to be a certified reinsurer, an assuming insurer must be certified by the commissioner in accordance with the process similar to Section 8B of Model #786?

i. The commissioner is required to post notice upon receipt of any application for certification substantially similar to the requirements of Section 8B(1) of Model #786?

ii. The commissioner is required to publish a list of all certified reinsurers and their ratings substantially similar to the requirements in Section 2E(4) of Model #785 and Section 8B(2) of Model #786?

iii. A certified reinsurer must be domiciled and licensed to transact insurance or reinsurance in a qualified jurisdiction, as determined by the commissioner?

iv. A certified reinsurer must maintain capital and surplus, or its equivalent, of no less than $250,000,000, calculated in accordance with Section 8B(4)(h) of Model #786? This requirement may also be satisfied by an association including incorporated and individual unincorporated underwriters having minimum capital and surplus equivalents (net of liabilities) of at least $250,000,000 and a central fund containing a balance of at least $250,000,000.

v. A certified reinsurer must maintain financial strength ratings from two or more rating agencies deemed acceptable by the commissioner, and the maximum rating that a certified reinsurer may be assigned will correspond to its financial strength rating as set forth in Section 8B(4)(a) of Model #786? These ratings must be based on interactive communication between the rating agency and the assuming insurer and not based solely on publicly available information.

vi. A certified reinsurer is rated by the commissioner on a legal entity basis, with consideration given to the group rating where appropriate (an association including incorporated and individual unincorporated underwriters that have been approved to do business as a single certified reinsurer may be evaluated on the basis of its group rating)? Factors may be considered in the evaluation process similar to those provided under Section 8B(4) and (5) of Model #786.

vii. A certified reinsurer must submit a properly executed Form CR-1 as evidence of its submission to the jurisdiction of the state, appointment of the commissioner as an agent for service of process in the state, and agreement to provide security for one hundred percent (100%) of its liabilities attributable to reinsurance ceded by ceding insurers if it resists enforcement of a final U.S. judgment? The commissioner must not certify any assuming insurer that is domiciled in a jurisdiction that the commissioner has determined does not adequately and promptly enforce final U.S. judgments or arbitration awards.

viii. A certified reinsurer must agree to meet applicable information filing requirements substantially similar to those provided under Section 8B(7) of Model #786, both with respect to an initial application for certification and on an ongoing basis?

ix. Changes in rating or revocation of certification of a certified reinsurer are applied by the commissioner in a manner substantially similar to the provisions of Section ~~2I~~2J of Model #785 and Section 8B(8) of Model #786?

x. A certified reinsurer must file audited financial statements, regulatory filings and actuarial opinion (as filed with the certified reinsurer's supervisor, with a translation into English) consistent with the requirements set forth in Section 8B(4)(h) and Section 8B(7)(d) of Model #786? Upon the initial application for certification, the commissioner will consider audited financial statements for the last two (2) years filed with its non-U.S. jurisdiction supervisor?

bb. The commissioner is required to create and publish a list of qualified jurisdictions, under which an assuming insurer licensed and domiciled in such jurisdiction is eligible to be considered for certification by the commissioner as a certified reinsurer?

i. In determining whether the domiciliary jurisdiction of a non-U.S. assuming insurer is eligible to be recognized as a qualified jurisdiction, the commissioner evaluates the reinsurance supervisory system of the non-U.S. jurisdiction, both initially and on an ongoing basis, under criteria substantially similar to those provided under Section 8C(2) of the model regulation?

ii. The commissioner shall consider the list of qualified jurisdictions published by the NAIC in determining qualified jurisdictions? If the commissioner approves a jurisdiction as qualified that does not appear on the NAIC list of qualified jurisdictions, the commissioner must provide thoroughly documented justification with respect to criteria substantially similar to that provided under Section 8C(2) of Model #786.

iii. U.S. jurisdictions that meet the requirements for accreditation under the NAIC financial standards and accreditation program are recognized as qualified jurisdictions?

cc. A state's laws and regulations shall allow a commissioner to defer to the certification and rating of a certified reinsurer issued by another NAIC accredited jurisdiction. Recognition of certification is made in accordance with provisions substantially similar to Section 8D of Model #786?

dd. Reinsurance contracts entered into or renewed with a certified reinsurer must include a proper funding clause, which requires the certified reinsurer to provide and maintain security in an amount sufficient to avoid the imposition of any financial statement penalty on the ceding insurer for reinsurance ceded to the certified reinsurer?

Reciprocal Jurisdictions

ee. A state's laws and regulations shall allow credit for reinsurance ceded to an assuming insurer that has its head office or is domiciled in, and is licensed in, a Reciprocal Jurisdiction. Its laws and regulations shall contain provisions that are substantially similar to those contained in Section 2F of Model #785 and Section 9 of Model #786. Its laws and regulations must provide that a Reciprocal Jurisdiction is a jurisdiction that meets one of the following:

i. A non-U.S. jurisdiction that is subject to an in-force covered agreement meeting the requirements of Section 2F(1)(a)(i) of Model #785 and Section 9B(1) of Model #786?

ii. A U.S. jurisdiction that meets the requirements for accreditation under the NAIC Financial Standards and Accreditation Program pursuant to Section 2F(1)(a)(ii) of Model #785 and Section 9B(2) of Model #786?

iii. A Qualified Jurisdiction that meets all of the requirements of Section 2F(1)(a)(iii) of Model #785 and Section 9B(3) of Model #786?

ff. Credit shall be allowed when the reinsurance is ceded to an assuming insurer that is licensed to transact reinsurance by, and has its head office or is domiciled in, a Reciprocal Jurisdiction, and which meets each of the conditions set forth in Section 2F(1)(b) – (g) of Model #785 and Section 9C of Model #786:

i. The assuming insurer must have and maintain on an ongoing basis minimum capital and surplus, or its equivalent, calculated on at least an annual basis as of the preceding December 31 or at the annual date otherwise statutorily reported to the Reciprocal Jurisdiction of no less than $250,000,000 similar to Section 2F(1)(b) of Model #785 and Section 9C(2) of Model #786? This minimum capital and surplus requirement may also be satisfied by an association including incorporated and individual unincorporated underwriters having minimum capital and surplus equivalents (net of liabilities) or own funds of at least $250,000,000 and a central fund containing a balance of at least $250,000,000.

ii. The assuming insurer must have and maintain on an ongoing basis a minimum solvency or capital ratio, as applicable, as set forth in Section 2F(1)(c) of Model #785 and Section 9C(3) of Model #786?

iii. The assuming insurer must submit a properly executed Form RJ-1 consistent with Section 2F(1)(d) of Model #785 and Section 9C(4) of Model #786:

- The assuming insurer must agree to provide prompt written notice and explanation to the commissioner if it falls below the minimum requirements set forth in this subsection, or if any regulatory action is taken against it for serious noncompliance with applicable law pursuant to Section 2F(1)(d)(i) of Model #785 and Section 9C(4)(a) of Model #786?

- The assuming insurer must consent in writing to the jurisdiction of the courts of this state and to the appointment of the commissioner as agent for service of process pursuant to Section 2F(1)(d)(ii) of Model #785 and Section 9C(4)(b) of Model #786? The commissioner may also require that such consent be provided and included in each reinsurance agreement under the commissioner's jurisdiction.

- The assuming insurer must consent in writing to pay all final judgments, wherever enforcement is sought, obtained by a ceding insurer, that have been declared enforceable in the territory where the judgment was obtained pursuant to Section 2F(1)(d)(iii) of Model #785 and Section 9C(4)(c) of Model #786?

- Each reinsurance agreement must include a provision requiring the assuming insurer to provide security in an amount equal to one hundred percent (100%) of the assuming insurer's liabilities attributable to reinsurance ceded pursuant to that agreement if the assuming insurer resists enforcement of a final judgment that is enforceable under the law of the jurisdiction in which it was obtained or a properly enforceable arbitration award, whether obtained by the ceding insurer or by its legal successor on behalf of its estate, if applicable pursuant to Section 2F(1)(d)(iv) of Model #785 and Section 9C(4)(d) of Model #786?

- The assuming insurer must confirm that it is not presently participating in any solvent scheme of arrangement, which involves this state's ceding insurers, and agrees to notify the ceding insurer and the commissioner and to provide one hundred percent (100%) security to the ceding insurer consistent with the terms of the scheme, should the assuming insurer enter into such a solvent scheme of arrangement pursuant to Section 2F(1)(d)(v) of Model #785 and Section 9C(4)(e) of Model #786?

- The assuming insurer must agree in writing to meet the applicable information filing requirements pursuant to Section 9C(4)(f) of Model #786?

iv. The assuming insurer or its legal successor must provide, if requested by the commissioner, on behalf of itself and any legal predecessors, the documentation to the commissioner as outlined in Section 2F(1)(e) of Model #785 and Section 9C(5) of Model #786:

- For the two years preceding entry into the reinsurance agreement and on an annual basis thereafter, the assuming insurer's annual audited financial statements, in accordance with the applicable law of the jurisdiction of its head office or domiciliary jurisdiction, as applicable, including the external audit report pursuant to Section 9C(5)(a) of Model #786?

- For the two years preceding entry into the reinsurance agreement, the solvency and financial condition report or actuarial opinion, if filed with the assuming insurer's supervisor pursuant to Section 9C(5)(b) of Model #786?

- Prior to entry into the reinsurance agreement and not more than semi-annually thereafter, an updated list of all disputed and overdue reinsurance claims outstanding for 90 days or more, regarding reinsurance assumed from ceding insurers domiciled in the United States pursuant to Section 9C(5)(c) of Model #786?

- Prior to entry into the reinsurance agreement and not more than semi-annually thereafter, information regarding the assuming insurer's assumed reinsurance by ceding insurer, ceded reinsurance by the assuming insurer, and reinsurance recoverable on paid and unpaid losses by the assuming insurer pursuant to Section 9C(5)(d) of Model #786?

v. The assuming insurer must maintain a practice of prompt payment of claims under reinsurance agreements consistent with Section 2F(1)(f) of Model #785 and Section 9C(6) of Model #786?

vi. The assuming insurer's supervisory authority must confirm to the commissioner on an annual basis that the assuming insurer complies with the minimum capital and surplus requirements and the minimum solvency or capital ratio requirements as required under Section 2F(1)(g) of Model #785 and Section 9C(7) of Model #786?

gg. The commissioner is required to timely create and publish a list of Reciprocal Jurisdictions similar to Section 2F(2) of Model #786 and Section 9D of Model #786?

i. If the commissioner approves a jurisdiction that does not appear on the NAIC list of Reciprocal Jurisdictions, the commissioner must provide thoroughly documented justification in accordance with criteria published through the NAIC Committee Process pursuant to Section 2F(2)(a) of Model #785 and Section 9D(1) of Model #786?

ii. The commissioner may remove a jurisdiction from the list of Reciprocal Jurisdictions upon a determination that the jurisdiction no longer meets one or more of the requirements of a Reciprocal Jurisdiction pursuant to Section 2F(2)(b) of Model #785 and Section 9D(2) of Model #786, except that the commissioner shall not remove from the list a Reciprocal Jurisdiction as defined under Section 9B(1) and (2) of Model #786?

hh. The commissioner shall timely create and publish a list of assuming insurers to which cessions shall be granted credit consistent with Section 2F(3) of Model #785 and Section 9E of Model #786? Such assuming insurer must submit a properly executed Form RJ-1 and additional information as the commissioner may require.

i. If an NAIC accredited jurisdiction has determined that the conditions set forth in Section 2F of Model #785 and Section 9 of Model #786 have been met, the commissioner has the discretion to defer to that jurisdiction's determination and add such assuming insurer to the list of assuming insurers to which cessions shall be granted credit in accordance pursuant to Section 2F(3) of Model #785 and Section 9E(1) of Model #786? The commissioner may accept financial documentation filed with another NAIC accredited jurisdiction or with the NAIC with respect to such reinsurer.

ii. When requesting that the commissioner defer to another NAIC accredited jurisdiction's determination, an assuming insurer must submit a properly executed Form RJ-1 and additional information as the commissioner may require pursuant to Section 9E(2) of Model #786?

ii. If the commissioner determines that an assuming insurer no longer meets one or more of the requirements set forth in Section 2F of Model #786 and Section 9 of Model #786, the commissioner may revoke or suspend the eligibility of the assuming insurer consistent with Section 2F(4) of Model #785 and Section 9F of Model #786?

i. While an assuming insurer's eligibility is suspended, no reinsurance agreement issued, amended or renewed after the effective date of the suspension qualifies for credit except to the extent that the assuming insurer's obligations under the contract are otherwise secured pursuant to Section 2F(4)(a) of Model #785 and Section 9F(1) of Model #786?

ii. If an assuming insurer's eligibility is revoked, no credit for reinsurance may be granted after the effective date of the revocation with respect to any reinsurance agreements entered into by the assuming insurer, including reinsurance agreements entered into prior to the date of revocation, except to the extent that the assuming insurer's obligations under the contract are otherwise secured in a form acceptable to the commissioner pursuant to Section 2F(4)(b) of Model #785 and Section 9F(2) of Model #786?

iii. Before denying statement credit or imposing a requirement to post security or adopting any similar requirement that will have substantially the same regulatory impact as security, the commissioner shall follow the process set forth in Section 9G of Model #786?

jj. If subject to a legal process of rehabilitation, liquidation or conservation, as applicable, the ceding insurer, or its representative, may seek and, if determined appropriate by the court in which the proceedings are pending, may obtain an order requiring that the assuming insurer post security for all outstanding liabilities in accordance with Section 2F(5) of Model #785 and Section 9H of Model #786?

kk. Nothing shall limit or in any way alter the capacity of parties to a reinsurance agreement to agree on requirements for security or other terms in that reinsurance agreement, except as expressly prohibited by other applicable law or regulation similar to Section 2F(6) of Model #785?

ll. Credit may be taken only for reinsurance agreements entered into, amended, or renewed on or after the effective date of the statute, and only with respect to losses incurred and reserves reported on or after the later of (i) the date on which the assuming insurer has met all eligibility requirements, and (ii) the effective date of the new reinsurance agreement, amendment, or renewal consistent with the provisions of Section 2F(7) of Model #785?

MEMORANDUM

To: Financial Regulation Standards and Accreditation (F) Committee

From: NAIC Staff

Date: March 3, 2020

Re: 2011 & 2019 Revisions to *Credit for Reinsurance Model Law* (#785) and *Credit for Reinsurance Model Regulation (#786)*—Applicability to Risk Retention Groups (RRGs)

Executive Summary

On June 25, 2019, the NAIC Executive (EX) Committee and Plenary unanimously adopted revisions to the NAIC *Credit for Reinsurance Model Law* (#785) and *Credit for Reinsurance Model Regulation* (#786). These revisions were intended to incorporate the relevant provisions of the "Bilateral Agreement Between the United States of America and the European Union on Prudential Measures Regarding Insurance and Reinsurance" (Covered Agreement), which was signed on Sept. 22, 2017. At the 2019 Fall National Meeting, the Financial Regulation Standards and Accreditation (F) Committee adopted these revisions to the *Reinsurance Ceded* accreditation standard effective Sept. 1, 2022, for consideration by the Executive (EX) Committee and Plenary for final adoption at the Spring National Meeting.

The purpose of this memorandum is to clarify the applicability of these revisions to risk retention groups (RRGs) organized as captives. The recommendation to this Committee is that the 2019 revisions to Model #785 and Model #786, as well as the 2011 revisions establishing certified reinsurers and qualified jurisdictions (which became applicable as an accreditation standard Jan. 1, 2019), also should be made applicable to RRGs.

Risk Retention Groups Organized as Captives

Article 3 (Reinsurance) of the Covered Agreement is applicable to ceding insurers, which Article 2(j) defines as "an undertaking which is authorized or licensed to take up or engage in the business of direct or primary insurance." This would arguably include RRGs that are organized or incorporated by states as captive insurers. *Reinsurance Ceded* is part of the Part A accreditation requirements for RRGs, and requires that state law should contain Model #785 and Model #786, or substantially similar laws. The primary difference between the current reinsurance accreditation standard for RRGs is that "a state's laws and regulations may allow RRGs to take credit for reinsurance without posting collateral in circumstances not contemplated by the Credit for Reinsurance Model Law and Regulation. For such cases, the Accreditation Interlineations include 'Reinsurance Guidelines for Risk Retention Groups Licensed as Captive Insurers' and a state's laws and regulations must comply with the guidelines in order to be considered substantially similar with this standard."

NAIC staff has reviewed the laws and regulations with respect to the fifteen (15) NAIC jurisdictions which currently license multi-state RRGs as captive insurers (AL, AZ, CO, DE, DC, HI, KY, ME, MT, NV, NC, OK, SC, TN and VT), and each meets the current *Reinsurance Ceded* accreditation standard in a very similar manner. First, each states' laws require that an RRG must be licensed as a captive insurer (and in some instances, a specific type of captive insurer) subject to its captive insurance laws. Second, the captive insurance laws generally exempt captive

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insurers from the general laws with respect to traditional insurers, except as is otherwise specified in statute. Finally, the statutes make RRGs that are licensed as captive insurers subject to the state's credit for reinsurance laws, either generally (e.g., an RRG licensed as a captive insurer must comply with all of the laws, rules, regulations and requirements applicable to insurers chartered and licensed in the state) or specifically (e.g., an RRG licensed as a captive insurer must comply with the laws specified in this chapter, including specifically the credit for reinsurance laws). We also reviewed the proposed legislation of the five states currently considering adoption of the 2019 revisions to the models (ME, OK, SC, TN & VT), and the proposed legislation would not change this outcome.

Recommendation

NAIC staff recommends that the Committee consider making the 2019 revisions to Model #785 and Model #786 an accreditation standard for RRGs effective Sept. 1, 2022, with enforcement of the standard to commence Jan. 1, 2023. Staff further recommends that the 2011 revisions to the models relating to certified reinsurers and qualified jurisdictions also be made a part of the accreditation standard, because the 2019 revisions are in large part based on these earlier revisions. Finally, we recommend that the changes in the attached redlined accreditation standard be adopted as the new accreditation standard for reinsurance ceded to RRGs.

Note: The Risk Retention Group (E) Task Force met on March 2, and approved these recommendations. The Reinsurance (E) Task Force will meet March 11 to consider approval of the recommendations.

10. Reinsurance Ceded

State law should contain the NAIC *Credit for Reinsurance Model Law* (#785), the NAIC's *Credit for Reinsurance Model Regulation* (#786) or substantially similar laws.

	YES	NO
Complete the following question only if this is an interim annual review:		
Have there been any changes to the department's ceded reinsurance requirements since last year's review?	_____	_____

If the response is **NO**, there is no further information needed regarding this standard, please proceed to the next standard.

If the response is YES, in the reference column please provide the applicable citation for each of the questions in this particular standard. Additionally, please attach a copy of the statutes or regulations that had a change and ensure that they are clearly marked for the changes that have been made (i.e., highlight the changes, redlined version, etc.) Please place an asterisk (*) in the reference column on the right-hand side of the page by each citation that has been changed. Also, please include below a brief description of the nature or reason for the change.

If the department is completing the self-evaluation guide due to an upcoming full review, please provide the applicable citation for each of the questions in this particular standard. Additionally, please attach a copy of the statutes or regulations that are listed in the reference column.

Credit for Reinsurance Model Law (#785)	REFERENCE
a. Credit allowed for reinsurance ceded to a licensed insurer? If the reinsurer is licensed as a RRG, then the ceding RRG or its members must qualify for membership with the reinsurer.	_____
b. Credit allowed for reinsurance ceded to an accredited insurer who meets requirements similar to those in Section 2B of the model law?	_____
c. Credit allowed for reinsurance ceded to an insurer domiciled and licensed in a state which employs substantially similar standards regarding credit for reinsurance and who maintains capital and surplus of at least $20,000,000 and submits to this states authority to examine its books and records?	_____
d. Credit allowed for reinsurance ceded to an insurer who maintains a trust fund, established in a form approved by the Commissioner, in a qualified U.S. financial institution for the payment of the valid claims of its U.S. policyholders and ceding insurers, their assigns and successors in interest and who reports financial information annually to the Commissioner to determine the sufficiency of the trust fund?	_____
e. In instances where reinsurance is ceded to insurers maintaining a trust fund, trustees of the trust required to report to the department annually, on or before February 28, the balance of the trust and a listing of the trust's assets as of the end of the year and a certification of the date of termination of the trust, if so planned, or certify that the trust shall not expire prior to the next following December 31?	_____

f. Credit for reinsurance allowed under c. or d. above only permitted where assuming insurer agrees in the reinsurance agreements: 1) that in the event of a failure of the assuming insurer to perform its obligations, the assuming insurer shall submit to the jurisdiction of any court of competent jurisdiction in any state of the U.S.; and 2) to designate the Commissioner or a designated attorney as its true and lawful attorney upon whom may be served any lawful process instituted by or on behalf of the ceding company?

g. Credit allowed for reinsurance ceded to an insurer meeting requirements similar to those in Section 2E (Certified Reinsurers) of the model law?

h. Credit allowed for reinsurance ceded to an insurer meeting requirements similar to those in Section 2F (Reciprocal Jurisdictions) of the model law?

~~g~~i. Although not required for accreditation, a state's laws and regulations may allow RRGs to take credit for reinsurance without posting collateral in circumstances not contemplated by the Credit for Reinsurance Model Law and Regulation. For such cases, the Accreditation Interlineations include "Reinsurance Guidelines for Risk Retention Groups Licensed as Captive Insurers" and a state's laws and regulations must comply with the guidelines in order to be considered substantially similar with this standard. If your state's laws and regulations do allow credit for reinsurance without collateral as discussed in the Accreditation Interlineations, please include the citation.

Note: An RRG's reinsurers as of Jan. 1, 2011, are grandfathered in as acceptable without meeting the requirements in the Reinsurance Guidelines. The requirements in the Reinsurance Guidelines should be used for new reinsurers with which business is placed after Jan. 1, 2011.

~~h~~j. Credit allowed for reinsurance ceded to an insurer not meeting the requirements of a., b., c., d., g., h. or ~~g~~i. above in an amount not exceeding the liabilities carried by the ceding insurer and only in the amount of funds held by or on behalf of the ceding insurer in the form of cash, securities listed by the Securities Valuation Office of the NAIC and qualifying as admitted assets, clean, irrevocable, unconditional letters of credit, and other forms of security acceptable to the Commissioner?

Credit for Reinsurance Model Regulation (#786)

k.~~i.~~ Credit for reinsurance allowed for reinsurance ceded by domestic reinsurers to assuming insurers that were licensed in the state as of the last date of the ceding insurers' statutory financial statement? If the reinsurer is licensed as a RRG, then the ceding RRG or its members must qualify for membership with the reinsurer.

l.~~j.~~ Credit for reinsurance provisions for accredited reinsurer similar to Section 5?

m.~~k.~~Credit for reinsurance provisions for reinsurers licensed and domiciled in other states similar to Section 6? _____

n.~~l.~~ Credit for reinsurance provisions for reinsurers maintaining trust funds similar to Section 7? _____

o.~~m.~~Credit for reinsurance required by law similar to Section 9, to the extent permitted by 15 USC 3902(a)? _____

p.~~n.~~ Reduction from liability for reinsurance ceded to an unauthorized assuming insurer similar to Section 10? Note: See significant element g. above regarding allowance of credit for reinsurance in certain situations not contemplated by the Model Law. _____

q.~~o.~~ Provisions for trust agreements similar to Section 11? _____

r.~~p.~~ Provisions for letters of credit similar to Section 12? _____

s.~~q.~~ Provisions for unencumbered funds similar to Section 13? _____

t.~~r.~~ Provisions for reinsurance contracts similar to Section 14? Note: For those reinsurance contracts for which credit is allowed under significant element g. above, the reinsurance contract should contain language similar to Section II of the "Reinsurance Guidelines for Risk Retention Groups Licensed as Captive Insurers." _____

u.~~s.~~ The adoption of Form AR-1—Certificate of Assuming Insurer. Note: For situations in which credit for reinsurance is taken under significant element g. above, the reinsurance contract should contain language similar to Section II of the "Reinsurance Guidelines for Risk Retention Groups Licensed as Captive Insurers." _____

v. Credit for reinsurance provisions for certified reinsurers similar to Section 8? _____

w. Credit for reinsurance provisions for reciprocal jurisdictions similar to Section 9? _____

W:\National Meetings\2020\Summer\Plenary\Att 8 Reciprocal Jurisdiction Referral to F Cmte.pdf

The Aug. 24, 2017 referral was adopted by the Financial Regulation Standards and Accreditation (F) Committee on Dec. 7, 2019. A March 20, 2017 referral is also attached for reference.

Attachment A (proposed accreditation standard and significant elements) includes a tracked change to significant element "b". This change is the result of technical changes to Model #787 adopted by the Reinsurance (E) Task Force and does not change the substance of the proposed standard. The F Committee is scheduled to consider adoption of this technical change on Aug. 12, 2020. It is recommended that the Executive (EX) Committee and Plenary consider adoption of the technical change in conjunction with adoption of the Aug. 24, 2017 referral.

MEMORANDUM

TO: Financial Regulation Standards and Accreditation (F) Committee

FROM: Reinsurance (E) Task Force

DATE: August 24, 2017

RE: *Term and Universal Life Insurance Reserve Financing Model Regulation* (#787)

Executive Summary

The NAIC membership adopted the *Term and Universal Life Insurance Reserve Financing Model Regulation* (#787) at the 2016 Fall National Meeting on Dec. 13, 2016. At that same time, the NAIC membership also adopted revisions 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) to conform with the provisions of Model #787, effective Jan. 1, 2017. Model #787 establishes uniform, national standards governing reserve financing arrangements pertaining to term life and universal life insurance policies with secondary guarantees, and ensures that funds consisting of primary security and other security are held in the forms and amounts required.

At its meeting on Aug. 7, 2017, the Reinsurance (E) Task Force agreed to submit the following recommendations to the Financial Regulation Standards and Accreditation (F) Committee:

1. Model #787 should be adopted as a new accreditation standard by the NAIC, with significant elements as outlined in Attachment A.

2. The Financial Regulation Standards and Accreditation (F) Committee should consider a waiver in its normal timeline for adoption of an accreditation standard, and expeditiously consider adoption of this standard. The Task Force recommends that the accreditation standard become effective Jan. 1, 2020. The

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Task Force further recommends that a state's adoption of AG 48 will serve to satisfy this accreditation standard until such time that the state adopts the significant elements of Model #787.

3. The 2016 revisions to the *Credit for Reinsurance Model Law* (#785) should be considered acceptable but not required by the states.

In addition to the preceding recommendations, the Task Force is offering the following additional information in order to assist the Financial Regulation Standards and Accreditation (F) Committee in reviewing the proposed accreditation standard for Model #787.

Substantially Similar

The Task Force has recommended in the draft accreditation standard that the "substantially similar" standard be utilized to meet the minimum requirements of the standard. However, the Task Force did note that Drafting Notes to Section 2, Section 3 and Section 5 of Model #785 might suggest a stronger standard of review than "substantially similar." The Drafting Notes provide, as follows: "To assist in achieving national uniformity, commissioners are asked to strongly consider adopting regulations that are **substantially similar in all material respects** to NAIC adopted model regulations in the handling and treatment of such reinsurance arrangements." [**Emphasis added**]. In recognition of this, and to assist in review of the actuarial method used to determine the required level of primary security as described in Section 6 of Model #787, the Task Force recommends that the NAIC Legal Division specifically note any material changes in a state's regulation during an accreditation review for consideration by the Financial Regulation Standards and Accreditation (F) Committee.

State Adoption of AG 48

The Task Force recommends that the accreditation standard become effective on an expedited basis beginning Jan. 1, 2020. However, the Task Force further recognizes that meeting the expedited date may not be feasible for some states in instances due, in whole or part, to other legislative priorities of the states. It is the recommendation of the Task Force that, in such cases, a state's compliance with AG 48 should be considered as satisfactory to the Financial Regulation Standards and Accreditation (F) Committee as substantial compliance with Model #787. AG 48 became effective Jan. 1, 2015, and became part of the *Accounting Practices and Procedures Manual* through its inclusion in Appendix C, and has been amended to conform with Model #787 effective Jan. 1, 2017.

2016 Revisions to Model #785

The Task Force does not recommend that the 2016 revisions to Model #785 be included in the proposed accreditation standard. These revisions provide that the commissioner may adopt regulations with respect to: 1) life insurance policies with guaranteed nonlevel gross premiums or guaranteed nonlevel benefits; 2) universal life insurance policies with provisions resulting in the ability of a policyholder to keep a policy in force over a secondary guarantee period; 3) variable annuities with guaranteed death or living benefits; 4) long-term care insurance policies; and 5) other life and health insurance and annuity products as to which the NAIC adopts model regulatory requirements with respect to credit for reinsurance. The revisions to Model #785 also contain a "professional reinsurer exemption" for reinsurers that maintain at least $250 million in capital and surplus when determined in accordance with the *Accounting Practices and Procedures Manual*, including all amendments thereto adopted by the NAIC, excluding the impact of any permitted or prescribed practices, and is: 1) licensed in at least 26 states; or 2) licensed in at least 10 states, and licensed or accredited in a total of at least 35 states.

The reasoning of the Task Force is that Model #787 only applies to term life and universal life with secondary guarantees (XXX/AXXX) captive reinsurance transactions, and that variable annuities, long-term care insurance and other life and health insurance and annuity products are not currently addressed. Therefore, it would be considered to be premature to require the states to adopt these provisions. In addition, the professional reinsurer exemption of Section 5B(4) of Model #785 is specifically referenced in the draft accreditation standard. Therefore, it is the recommendation of the Task Force that the 2016 revisions to Model #785 are optional, and should be considered as acceptable but not required by the states.

Attachment A

Proposed Accreditation Standard
***Term and Universal Life Insurance Reserve Financing Model Regulation* (#787)**

State statute and/or regulation should be substantially similar to uniform, national standards that govern reserve financing arrangements pertaining to life insurance policies containing guaranteed nonlevel gross premiums, guaranteed nonlevel benefits and universal life insurance policies with secondary guarantees, to ensure that both the total security and the primary security are provided in forms and amounts that are in compliance with the requirements set forth in the *Term and Universal Life Insurance Reserve Financing Model Regulation* (#787).

a. Provides that the *Credit for Reinsurance Model Regulation* (#786) and Model #787 shall both apply to reinsurance treaties that cede liabilities pertaining to Covered Policies; provided, that in the event of a direct conflict between the provisions of Model #787 and the provisions of Model #786, the provisions of Model #787 shall apply, but only to the extent of the conflict, substantially similar to Section 3 of Model #787?

b. Provides that Model #787 does not apply to reinsurance exempt by the provisions of Section 4 of Model #787, including reinsurance ceded to an assuming insurer that meets the requirements of ~~either~~ Section 5B(4)~~(a)~~ of the *Credit for Reinsurance Model Law* (#785)~~, which pertains to certain certified reinsurers, or Section 5B(4)(b) of Model #785, which pertains to reinsurers meeting certain threshold size and licensing requirements~~? ***[Note: this change is due to technical changes to Model #787 adopted by the Reinsurance (E) Task Force and does not change the substance of the standard – see March 3 referral attached]***

c. Provides definitions of "Covered Policies," "Grandfathered Policies," "Required Level of Primary Security," "Actuarial Method," "Primary Security," "Other Security" and "Valuation Manual" that are substantially similar to such terms as defined in Section 5 of Model #787?

d. Provides for an Actuarial Method to establish the Required Level of Primary Security for each reinsurance treaty subject to this regulation that is substantially similar to the methodology as set forth in Section 6A of Model #787?

e. Provides for valuations to be used 1) in calculating the Required Level of Primary Security pursuant to the Actuarial Method; and 2) in determining the amount of Primary Security and Other Security, as applicable, held by or on behalf of the ceding insurer, that are substantially similar to the valuations set out in Section 6B of Model #787?

f. Provides for requirements to obtain credit for reinsurance with respect to ceded liabilities pertaining to Covered Policies that are substantially similar to the requirements set out in Section 7A of Model #787?

g. Provides for requirements at inception date and on an ongoing basis substantially similar to Section 7B(1) of Model #787?

h. Provides that if the requirements to hold Primary Security and total security are not both 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, unless any deficiency has been eliminated pursuant to remediation provisions substantially similar to Section 7B(2) of Model #787?

i. Includes a prohibition against avoidance provision similar to Section 9 of Model #787?

MEMORANDUM

TO: Financial Regulation Standards and Accreditation (F) Committee

FROM: John F. Finston (CA)
Chair, Reinsurance (E) Task Force

DATE: March 20, 2017

RE: 2016 Revisions to *Credit for Reinsurance Model Law* (#785)
Term and Universal Life Insurance Reserve Financing Model Regulation (#787)

Executive Summary

On June 30, 2014, the Principle-Based Reserving Implementation (EX) Task Force adopted the recommendations in the report of Rector & Associates, Inc. dated June 4, 2014, regarding a proposal for the XXX/AXXX Reinsurance Framework. The Framework sought to address concerns regarding reserve financing transactions and to do so without encouraging them to move offshore. The changes would be prospective and apply only to life insurance policies containing guaranteed nonlevel gross premiums, guaranteed nonlevel benefits and universal life with secondary guarantees business (XXX/AXXX). The NAIC Executive (EX) Committee adopted the Framework (in concept) on Aug. 17, 2014. As an interim step to implementing the Framework, the NAIC adopted 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) on Dec. 16, 2014. It was expected that AG 48 would eventually be replaced by effective codification through the *Credit for Reinsurance Model Law* (#785) and creation of a new model regulation to establish requirements regarding the reinsurance of XXX/AXXX policies.

The NAIC adopted revisions to Model #785 on Jan. 8, 2016, which give insurance commissioners authority to issue regulations codifying AG 48 and the XXX/AXXX Reinsurance Framework. The Reinsurance (E) Task Force adopted the *Term and Universal Life Insurance Reserve Financing Model Regulation* (#787) at the Summer National Meeting on Aug. 27, 2016, and it was adopted by the Financial Condition (E) Committee with slight revisions via conference call on Sept. 30, 2016. Model #787 was then adopted by the Executive (EX) Committee and Plenary on Dec. 13, 2016. At that same time, the NAIC also revised AG 48 to conform with the provisions of Model #787, effective Jan. 1, 2017.

The Reinsurance (E) Task Force hereby submits the following recommendations to the Financial Regulation Standards and Accreditation (F) Committee:

1. The 2016 revisions to Model #785 and new Model #787 should be adopted as a new accreditation standard by the NAIC.

2. The F-Committee should consider a waiver in its normal timeline for adoption of an accreditation standard, and expeditiously consider adoption of this standard. The Task Force would recommend that the accreditation standard become effective January 1, 2020.

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

The 2016 revisions to Model #785 provide that the commissioner may adopt regulations with respect to (1) life insurance policies with guaranteed nonlevel gross premiums or guaranteed nonlevel benefits; (2) universal life insurance policies with provisions resulting in the ability of a policyholder to keep a policy in force over a secondary guarantee period; (3) variable annuities with guaranteed death or living benefits; (4) long-term care insurance policies; and (5) other life and health insurance and annuity products as to which the NAIC adopts model regulatory requirements with respect to credit for reinsurance. The revisions to Model #785 also contain a "professional reinsurer exemption" for reinsurers that maintain at least $250 million in capital and surplus when determined in accordance with the NAIC *Accounting Practices and Procedures Manual*, including all amendments thereto adopted by the NAIC, excluding the impact of any permitted or prescribed practices; and is (1) licensed in at least 26 states; or (2) licensed in at least 10 states, and licensed or accredited in a total of at least 35 states.

Model #787 does not materially change the ability of insurers to obtain credit for reinsurance ceded to "certified" reinsurers or to obtain credit for reinsurance ceded to "licensed" or "accredited" reinsurers that follow statutory accounting and risk-based capital (RBC) rules. As a practical matter, the Model #787 requirements apply to reinsurance ceded to captive insurers, SPVs, reinsurers that are not eligible to become "certified" reinsurers, or reinsurers that materially deviate from statutory accounting and/or RBC rules. In those situations, subject to certain exemptions and grandfathering provisions, the ceding insurer may receive credit for reinsurance if:

- The ceding insurer continues to establish gross reserves, in full, using applicable reserving guidance;
- 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 contract, on a funds withheld, trust, or modified coinsurance basis;
- The Actuarial Method used to establish the Required Level of Primary Security for each reinsurance treaty subject to Model #787 is based on VM-20, applied on a treaty-by-treaty basis;
- 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 are held by or on behalf of the ceding insurer as security under the reinsurance contract; and
- The reinsurance arrangement is approved by the ceding insurer's domestic regulator.

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

The NAIC Principle-Based Reserving Implementation (EX) Task Force serves as the coordinating body for all NAIC technical groups involved with projects related to the Principle-Based Reserves (PBR) initiative for life and health policies. This Task Force was also charged with further assessing, and making recommendations regarding the solvency implications of life insurance reserve financing mechanisms addressed in the June 6, 2013, NAIC White Paper *Captives and Special Purpose Vehicles*, which provides in relevant part:

> The Captive and Special Purpose Vehicle (SPV) Use (E) Subgroup studied the use of captives and SPVs formed by commercial insurers. The Subgroup concluded that commercial insurers cede business to captives for a variety of business purposes. The Subgroup determined that the main use of captives and SPVs by commercial insurers was related to the financing of XXX and AXXX perceived reserve redundancies. The implementation of principle-based reserving (PBR) could reduce the need for

> commercial insurers to create new captives and SPVs to address perceived reserve redundancies; however, existing captives and SPVs are likely to remain in existence for several years or decades, until the existing blocks of business are run-off. **Regulators need to be able to assess and monitor the risks that captives and SPVs may pose to the holding company system, and the current regulatory process should be enhanced to provide standardized tools and processes to be used by all regulators when reviewing such transactions.** Commercial insurer-owned captives and SPVs should not be used to avoid statutory accounting. **To the extent that insurer-affiliated captives and SPVs may be created in the future for unforeseen purposes, additional guidance should be developed by the NAIC to assist the states in a uniform review of transactions. [Emphasis added].**

In addition, in coordination with the adoption in principle of the XXX/AXXX Reinsurance Framework, the Financial Regulation Standards and Accreditation (F) Committee was given the following charge: "As the various work products are adopted by the Principle-Based Reserving (EX) Task Force, Executive Committee, and Plenary, consider them for inclusion in the Part A and Part B Accreditation Standards."

Finally, effective Jan. 1, 2016, the NAIC amended the *Preamble for Part A: Laws and Regulations of the NAIC Policy Statement on Financial Regulation Standards* to apply to the regulation of a state's domestic insurers licensed and/or organized under its captive or special purpose vehicle statutes or any other similar statutory construct with respect to XXX/AXXX business, which is deemed to satisfy the Part A accreditation requirements if the applicable reinsurance transaction satisfies the XXX/AXXX Reinsurance Framework requirements adopted by the NAIC. Further, the revised Preamble provided, as follows: "The revisions to the Credit for Reinsurance Model Act (#785) and the new XXX/AXXX Model Regulation will need to be specifically considered for accreditation purposes once adopted by the NAIC."

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

AG 48 became effective Jan. 1, 2015, and became part of the NAIC *Accounting Practices and Procedures Manual* through its inclusion in Appendix C. As such, provisions similar to the proposal have been effective in all states since that date.

As of this date, three states (Louisiana, Oklahoma and Utah) have gone beyond AG 48 and have adopted the 2016 revisions to Model #785 giving commissioners authority to issue regulations codifying AG 48 and the XXX/AXXX Reinsurance Framework, with several other states currently considering such revisions.

The new Part A Preamble became effective Jan. 1, 2016, with regard to XXX/AXXX reinsurance captives. NAIC staff worked with necessary state insurance departments to assess compliance with the new Part A Preamble related to captives that assume XXX/AXXX business, and reported its findings at the 2016 Fall National Meeting to the Financial Regulation Standards and Accreditation (F) Committee. NAIC staff reviewed all of the Dec. 31, 2015, XXX/AXXX Reinsurance Supplements that were filed with the NAIC to first ascertain whether the appropriate level of primary and other securities was being held to back the non-exempt XXX/AXXX reinsurance transactions. NAIC staff reported that all of the transactions held the required amount of securities, and therefore, all of the transactions satisfied the new Part A requirements.

A statement as to the provisions needed to meet the minimum requirements of the standard. That is, whether a state would be required to have "substantially similar" language or rather a regulatory framework. If it is being proposed that "substantially similar" language be required, the referring committee, task force or working group shall recommend those items that should be considered significant elements:

Regulators needed to be able to assess and monitor the risks posed with respect to XXX/AXXX captive reinsurance transactions, and the regulatory process was enhanced through the adoption of the XXX/AXXX Reinsurance Framework, AG 48 and Model #787 to provide standardized tools and processes to be used by all regulators when reviewing such transactions. However, these new tools are complex and technical in nature, requiring the use of a new actuarial methodology to achieve the desired financial solvency results. Therefore, the Reinsurance (E) Task Force recommends that any new accreditation standard developed for Model #787 be adopted by NAIC-accredited jurisdictions in a "substantially similar" manner, as that term is defined in the Accreditation Interlineations of the NAIC Financial Regulation Standards and Accreditation Program.
In addition, all of the elements of the XXX/AXXX Reinsurance Framework have been put into place, with the exception of the new accreditation standard. Therefore, F-Committee should consider a waiver in its normal timeline for adoption of an accreditation standard, and expeditiously consider adoption of this new standard effective as of January 1, 2020.

An estimate of the cost for insurance companies to comply with the proposal and the impact on state insurance departments to enforce it, if reasonably quantifiable:

The NAIC has not performed a cost/benefit analysis with respect to Model #787, nor do we believe that the specific costs for insurance companies to comply with the proposal and the impact on state insurance departments to enforce it are reasonably quantifiable. However, it should be noted that Model #787 does not require dramatic changes from how insurance companies have been financing XXX/AXXX captive reinsurance transactions since the NAIC's adoption of AG 48. As with AG 48, Model #787 provides "standardized tools and processes to be used by all regulators when reviewing such transactions." Prior to the adoption of AG 48, insurers would enter into various captive reinsurance transactions to "finance" different portions of the statutory reserve differently—i.e., to fund different portions of the reserve using different kinds of assets—based on what insurers believed to be a better correlation between the kind of asset used and the probability that it would be needed. Many state regulators were comfortable with these transactions in theory, but there was significant unease regarding how these transactions were being implemented, and especially as to the lack of consistency from insurer to insurer and regulator to regulator regarding key aspects as to how these transactions may have been approved. Such transactions are still permitted under Model #787, but now a clear and consistent process has been implemented to ensure that the proper amount and type of assets have been applied with respect to these transactions in order to ensure that they continue to meet strong financial solvency standards.

TO: Financial Regulation Standards and Accreditation (F) Committee

FROM: NAIC Staff

DATE: March 3, 2020

RE: Technical Revisions to the *Term and Universal Life insurance Reserve Financing Model Regulation* (#787) as an Accreditation Standard

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At the 2019 Fall National Meeting, the Financial Regulation Standards and Accreditation (F) Committee adopted the *Term and Universal Life Insurance Reserve Financing Model Regulation* (#787), commonly known as the XXX/AXXX model, as a new accreditation standard. The decision is pending approval by Plenary.

Following adoption by the Committee, the Reinsurance (E) Task Force adopted technical changes to Model #787, which included Section 4E as follows:

> 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

The technical changes were due to revisions to the *Credit for Reinsurance Model Law* (#785) adopted by the NAIC in June 2019, which impacted sections referenced in Model #787. The referenced Section 5B(4) provides an exemption to Model #787 for what is commonly referred to as "professional reinsurers." As defined in the 2016 version of Model #785 Section 5B(4)(a) and (b), these professional reinsurers are reinsurers that meet certain minimum capital requirements and are certified reinsurers in a certain minimum number of states. The 2019 revisions to Model #785 add a new Section 5B(4)(a) to provide a similar exemption for reinsurers domiciled in reciprocal jurisdictions, as defined in Section 2F of Model #785. This shifted the original (a) and (b) to (b) and (c). A copy of the revised Section 5 is attached. To accurately reflect the exemption intended by the reference in Model #787, the entire Section 5B(4) is now referenced in Model #787.

NAIC staff therefore recommend that an equivalent change also be made to the accreditation standard. The proposed change affects significant element "b" as follows:

> b. Provides that Model #787 does not apply to reinsurance exempt by the provisions of Section 4 of Model #787, including reinsurance ceded to an assuming insurer that meets the requirements of ~~either~~ Section 5B(4)~~(a)~~ of the *Credit for Reinsurance Model Law* (#785)~~, which pertains to certain certified reinsurers, or Section 5B(4)(b) of Model #785, which pertains to reinsurers meeting certain threshold size and licensing requirements~~?

The original referral from the Reinsurance (E) Task Force with the recommendation to the Committee regarding Model #787 as an accreditation standard, including the accreditation significant elements, is attached for reference.

EXECUTIVE OFFICE • 444 North Capitol Street NW, Suite 700 • Washington, DC 20001-1509 p | 202 471 3990 f | 816 460 7493
CENTRAL OFFICE • 1100 Walnut Street, Suite 1500 • Kansas City, MO 64106-2197 p | 816 842 3600 f | 816 783 8175
CAPITAL MARKETS & INVESTMENT ANALYSIS OFFICE • One New York Plaza, Suite 4210 • New York, NY 10004 p | 212 398 9000 f | 212 382 4207
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CREDIT FOR REINSURANCE MODEL LAW

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Section 5. Rules and Regulations

A. The commissioner may adopt rules and regulations implementing the provisions of this law.

Drafting Note: It is recognized that credit for reinsurance also can be affected by other sections of the enacting state's code, e.g., a statutory insolvency clause or an intermediary clause. It is recommended that states that do not have a statutory insolvency clause or an intermediary clause consider incorporating such clauses in their legislation.

B. The commissioner is further authorized to adopt rules and regulations applicable to reinsurance arrangements described in Paragraph (1) of this Section 5B.

Drafting Note: This new regulatory authority is being added in response to reinsurance arrangements entered into, directly or indirectly, with life/health insurer-affiliated captives, special purpose vehicles or similar entities that may not have the same statutory accounting requirements or solvency requirements as US-based multi-state life/health insurers. To assist in achieving national uniformity, commissioners are asked to strongly consider adopting regulations that are substantially similar in all material respects to NAIC adopted model regulations in the handling and treatment of such policies and reinsurance arrangements.

(1) A regulation adopted pursuant to this Section 5B, may apply only to reinsurance relating to:

(a) Life insurance policies with guaranteed nonlevel gross premiums or guaranteed nonlevel benefits;

(b) 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) Variable annuities with guaranteed death or living benefits;

(d) Long-term care insurance policies; or

(e) Such other life and health insurance and annuity products as to which the NAIC adopts model regulatory requirements with respect to credit for reinsurance.

(2) A regulation adopted pursuant to Paragraph 1(a) or 1(b) of this Section 5B, may apply to any treaty containing (i) policies issued on or after January 1, 2015, and/or (ii) policies issued prior to January 1, 2015, if risk pertaining to such pre-2015 policies is ceded in connection with the treaty, in whole or in part, on or after January 1, 2015.

Drafting Note: The NAIC's Actuarial Guideline XLVIII (AG 48) became effective January 1, 2015, and covers policies ceded on or after this date unless they were ceded as part of a reserve financing arrangement as of December 31, 2014. One regulation contemplated by this revision to the NAIC *Credit for Reinsurance Model Law* (#785) is intended to substantially replicate the requirements for the amounts and forms of security held under the rules provided in AG 48. AG 48 was written to sunset upon a state's adoption (pursuant to the enabling authority of the preceding paragraph) of a regulation with terms substantially similar to AG 48. The preceding paragraph is intended to provide continuity of rules applicable to those policies and reinsurance arrangements, including continuity as to the policies covered by such rules. The preceding paragraph is not intended to change the scope of, or collateral requirements for policies and treaties covered under AG 48.

(3) A regulation adopted pursuant to this Section 5B may require the ceding insurer, in calculating the amounts or forms of security required to be held under regulations promulgated under this authority, to use the Valuation Manual adopted by the NAIC under Section 11B(1) of the NAIC Standard Valuation Law, including all amendments adopted by the NAIC and in effect on the date as of which the calculation is made, to the extent applicable.

(4) A regulation adopted pursuant to this Section 5B shall not apply to cessions to an assuming insurer that:

(a) Meets the conditions set forth in Section 2F of the *Credit for Reinsurance Model Law* (#785) in this state or, if this state has not adopted provisions substantially equivalent to Section 2F of the *Credit for Reinsurance Model Law* (#785), the assuming insurer is operating in accordance with provisions substantially equivalent to Section 2F of the *Credit for Reinsurance Model Law* (#785) in a minimum of five (5) other states; or

(b) Is certified in this state or, if this state has not adopted provisions substantially equivalent to Section 2E of the *Credit for Reinsurance Model Law* (#785), certified in a minimum of five (5) other states; or

(c) Maintains at least $250 million in capital and surplus when determined in accordance with the NAIC *Accounting Practices and Procedures Manual*, including all amendments thereto adopted by the NAIC, excluding the impact of any permitted or prescribed practices; and is

(i) licensed in at least 26 states; or

(ii) licensed in at least 10 states, and licensed or accredited in a total of at least 35 states.

(5) The authority to adopt regulations pursuant to this Section 5B does not limit the commissioner's general authority to adopt regulations pursuant to Section 5A of this law.

Date: 7/16/2020

State Implementation Reporting of NAIC-Adopted Model Laws and Regulations

Executive (EX) Committee

- Adoption of the new ***Insurance Data Security Model Law* (#668)**—This model was adopted by the Executive (EX) Committee and Plenary at the 2017 Fall National Meeting. Eleven states have enacted this model.

Life Insurance and Annuities (A) Committee

- Amendments to the ***Suitability in Annuity Transactions Model Regulation* (#275)**—These revisions were adopted by the Executive (EX) Committee and Plenary during the February 13, 2020 conference call. Two states have enacted these revisions to the model.

- Amendments to the ***Standard Nonforfeiture Law for Individual Deferred Annuities* (#805)**—These revisions were adopted by the Executive (EX) Committee and Plenary at the 2017 Summer National Meeting. One state has enacted these revisions to the model.

Health Insurance and Managed Care (B) Committee

- Amendments to the ***Health Insurance Reserves Model Regulation* (#10) (Cancer Expense Table)**—These revisions were adopted by the Executive (EX) Committee and Plenary at the 2017 Spring National Meeting. Two states have enacted these revisions to the model.

- Amendments to the ***Health Carrier Prescription Drug Benefit Management Model Act* (#22)**—These revisions were adopted by the Executive (EX) Committee and Plenary at the 2018 Spring National Meeting. NAIC staff are not aware of any state activity regarding this model.

- Amendments to the ***Accident and Sickness Insurance Minimum Standards Model Act* (#170)**—These revisions were adopted by the Executive (EX) Committee and Plenary at the 2019 Spring National Meeting. NAIC staff are not aware of any state activity regarding this model.

- Adoption of the ***Limited Long-Term Care Insurance Model Act* (#642)**—This model was adopted by the Executive (EX) Committee and Plenary at the 2018 Fall National Meeting. NAIC staff are not aware of any state activity regarding this model.

- Adoption of the ***Limited Long-Term Care Insurance Model Regulation* (#643)**—This model was adopted by the Executive (EX) Committee and Plenary at the 2018 Fall National Meeting. NAIC staff are not aware of any state activity regarding this model.

Property and Casualty Insurance (C) Committee

- Adoption of the ***Travel Insurance Model Act* (#632)**—This model was adopted by the Executive (EX) Committee and Plenary at the 2018 Fall National Meeting. Six states have enacted this model.

Market Regulation and Consumer Affairs (D) Committee

- Amendments to the ***Privacy of Consumer Financial and Health Information Regulation* (#672)**—These revisions were adopted by the Executive (EX) Committee and Plenary at the 2017 Spring National Meeting. Eleven states have enacted these revisions to the model.

Financial Condition (E) Committee

- Amendments to the ***Life and Health Insurance Guaranty Association Model Act* (#520)**—These revisions were adopted by the Executive (EX) Committee and Plenary at the 2017 Fall National Meeting. 32 states have enacted these revisions to the model.

- Amendments to the ***Credit for Reinsurance Model Law* (#785)**—These revisions were adopted by the Executive (EX) Committee and Plenary during the June 26, 2019 conference call. NAIC staff are not aware of any state activity regarding this model.

- Amendments to the ***Credit for Reinsurance Model Regulation* (#786)**—These revisions were adopted by the Executive (EX) Committee and Plenary during its June 26, 2019 conference call. NAIC staff are not aware of any state activity regarding this model.

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