NAIC NATIONAL MEETING SPRING 2023

Draft date: 3/6/23

*2023 Spring National Meeting*
*Louisville, Kentucky*

**FINANCIAL CONDITION (E) COMMITTEE**
Friday, March 24, 2023
1:30 – 2:00 p.m.
Omni Louisville—Commonwealth Ballroom—Level 2

**ROLL CALL**

| | | | |
|---|---|---|---|
| Elizabeth Kelleher Dwyer, Chair | Rhode Island | Mike Chaney | Mississippi |
| Nathan Houdek, Vice Chair | Wisconsin | Chlora Lindley-Myers | Missouri |
| Mark Fowler | Alabama | Marlene Caride | New Jersey |
| Michael Conway | Colorado | Adrienne A. Harris | New York |
| Michael Yaworsky | Florida | Michael Wise | South Carolina |
| Amy L. Beard | Indiana | Cassie Brown | Texas |
| Doug Ommen | Iowa | Scott A. White | Virginia |
| Timothy N. Schott | Maine | | |

NAIC Support Staff: Dan Daveline/Julie Gann/Bruce Jenson

**AGENDA**

1. Consider Adoption of its 2022 Fall National Meeting Minutes — Attachment One
   —*Superintendent Elizabeth Kelleher Dwyer (RI)*

2. Consider Adoption of its Task Force and Working Group Reports
   — *Superintendent Elizabeth Kelleher Dwyer (RI)*
   A. Accounting Practices and Procedures (E) Task Force — Attachment Two
   B. Capital Adequacy (E) Task Force — Attachment Three
   C. Financial Stability (E) Task Force — Attachment Four
   D. Receivership and Insolvency (E) Task Force — Attachment Five
   E. Reinsurance (E) Task Force — Attachment Six
   F. Valuation of Securities (E) Task Force — Attachment Seven
   G. Mortgage Guaranty Insurance (E) Working Group — Attachment Eight
   H. National Treatment and Coordination (E) Working Group — Attachment Nine
   I. Risk-Focused Surveillance (E) Working Group — Attachment Ten

3. Receive a Referral from the Valuation of Securities (E) Task Force — Attachment Eleven
   —*Carrie Mears (IA)*

4. Adopt the Securities Valuation Office (SVO) Modeling of Collateralized Loan Obligations (CLOs) for NAIC Designations —*Superintendent Elizabeth Kelleher Dwyer (RI)* — Attachment Twelve

5. Consider a Request for NAIC Model Law Development Extension from the Mortgage Guaranty Insurance (E) Working Group—*Jackie Obusek (NC)* — Attachment Thirteen

6. Discuss Any Other Matters Brought Before the Committee —*Superintendent Elizabeth Kelleher Dwyer (RI)*

7. Adjournment

# Draft Pending Adoption

Draft: 12/20/22

Financial Condition (E) Committee
Tampa, Florida
December 15, 2022

The Financial Condition (E) Committee met in Tampa, FL, Dec. 15, 2022. The following Committee members participated: Scott A. White, Chair (VA); Elizabeth Kelleher Dwyer, Vice Chair (RI); Michael Conway represented by Rolf Kaumann (CO); David Altmaier represented by Jane Nelson (FL); Doug Ommen and Daniel Mathis (IA); Timothy N. Schott, Vanessa Sullivan, and Robert Wake (ME); Grace Arnold represented by Fred Andersen (MN); Chlora Lindley-Myers represented by Debbie Doggett (MO); Mike Chaney represented by David Browning (MS); Marlene Caride (NJ); Adrienne A. Harris represented by John Finston (NY); Michael Wise (SC); Cassie Brown represented by Jamie Walker (TX); Nathan Houdek and Amy Malm (WI); and Jeff Rude (WY). Also participating were: Dale Bruggeman (OH); and Kevin Baldwin (IL).

1. Adopted its Nov. 15 and Summer National Meeting Minutes

The Committee met Nov. 15 and took the following action: 1) adopted a pre-receivership memorandum of understanding to be used by states as a template in ensuring that the guaranty funds are prepared and have the appropriate information; and 2) adopted its 2023 proposed charges.

Superintendent Dwyer made a motion, seconded by Commissioner Houdek, to adopt the Committee's Nov. 15 (Attachment One) and Aug. 12 (*see NAIC Proceedings – Summer 2022, Financial Condition (E) Committee*) minutes. The motion passed unanimously.

2. Adopted the Reports of its Task Forces and Working Groups

Commissioner White stated that the Committee usually takes one motion to adopt its task force and working group reports that are considered technical, noncontroversial, and not significant by NAIC standards; i.e., they do not include model laws, model regulations, model guidelines, or items considered to be controversial. He reminded Committee members that after the Committee's adoption of its votes, all the technical items included within the reports adopted will be sent to the NAIC members for review shortly after the conclusion of the Summer National Meeting as part of the Financial Condition (E) Committee Technical Changes report. Pursuant to the technical changes report process previously adopted by the Executive (EX) Committee and Plenary, the members will have 10 days to comment. Otherwise, the technical changes will be considered adopted by the NAIC and effective immediately. With respect to the task force and working group reports, Commissioner White asked the Committee: 1) whether there were any items that should be discussed further before being considered for adoption and sent to the members for consideration as part of the technical changes; and 2) whether there were other issues not up for adoption that are currently being considered by task forces or workings groups reporting to this Committee that require further discussion. The response to both questions was no.

In addition to presenting the reports for adoption, Commissioner White also noted that the Financial Analysis (E) Working Group met Oct. 5, Nov. 7, and Dec. 12 in regulator-to-regulator session, pursuant to paragraph 3 (specific companies, entities or individuals) of the NAIC Policy Statement on Open Meetings, to discuss letter responses and financial results. Additionally, the Valuation Analysis (E) Working Group met Sept. 1 and Dec. 12 in regulator-to-regulator session, pursuant to paragraph 3 (specific companies, entities or individuals) of the NAIC Policy Statement on Open Meetings, to discuss valuation items related to specific companies.

Superintendent Dwyer made a motion, seconded by Andersen, to adopt the following task force and working group reports: Accounting Practices and Procedures (E) Task Force; Capital Adequacy (E) Task Force; Examination

 

Oversight (E) Task Force; Financial Stability (E) Task Force; Receivership and Insolvency (E) Task Force; Reinsurance (E) Task Force; Risk Retention Group (E) Group Task Force; Valuation of Securities (E) Task Force; Group Solvency Issues (E) Working Group (Attachment Two); Mortgage Guaranty Insurance (E) Working Group (Attachment Three); NAIC/American Institute of Certified Public Accountants (AICPA) (E) Working Group (Attachment Four); National Treatment and Coordination (E) Working Group (Attachment Five); Restructuring Mechanisms (E) Subgroup (Attachment Six); and Risk-Focused Surveillance (E) Working Group (Attachment Seven). The motion passed unanimously.

3. Heard a Presentation from the NCIGF

Roger H. Schmelzer (National Conference of Insurance Guaranty Funds—NCIGF) and Barbara F. Cox (NCIGF) provided a summary of some of the items they considered in suggesting changes to the *Property and Casualty Insurance Guaranty Association Model Act* (#540). Cox discussed the process used by the NCIGF to develop its proposed changes to Model #540. She described the significant number of Committee meetings held during the year, which included expertise from those with both guaranty fund coverage knowledge, as well as those with cybersecurity knowledge. She discussed how it was determined that guaranty fund coverage should exist for both small and medium size companies purchasing cybersecurity coverage. She discussed that such coverage should allow both immediate relief after a covered event, as well as in the long run for all claims. She emphasized how the immediate included a wide way of expenses, including the need to mitigate further losses, forensics work, and other expenses that if not incurred immediately could lead to further deterioration. She described how claims related to service providers were also important. Finally, she described how ultimately, the focus of the NCIGF on the issue is not dissimilar to the focus of other guaranty fund issues where early planning and action with guaranty funds is extremely important.

4. Adopted a Request for NAIC Model Law Development Regarding Model #540

Baldwin stated that as the NCIGF described, the Request for NAIC Model Law Development is a proposal to amend Model #540 to address and clarify guaranty fund coverage of cybersecurity insurance. This is a unique line of business, and it is important that the guaranty fund coverage of this line is clear. The recommendation from the NCIGF aims to update Model #540 to eliminate any ambiguity about guaranty fund coverage. The changes that the NCIGF proposes address a cybersecurity insurance liquidation, either a company that writes cybersecurity exclusively or writes it as one line of business. The NCIGF Legal Committee, led by Rowe W. Snider (Locke Lord LLP), studied cybersecurity insurance at a technical level over the past year, conferring with different experts in the cybersecurity area. The NCIGF's proposed amendments to sections of Model #540 result from the findings and recommendations from this research. The proposed amendments to Model #540 were drafted with a minimalized approach so that they give state guaranty associations the solvency tools needed to handle a cybersecurity insurance claim. The amendments do not erase all the challenges in handling these types of claims; however, there would need to be a lot of planning to get ready for such an insolvency. Baldwin stated that the Task Force exposed the proposal for a 30-day public comment period and did not receive any comments.

Superintendent Dwyer made a motion, seconded by Kaumann, to adopt the Request for NAIC Model Law Development regarding Model #540 (Attachment Eight). The motion passed unanimously.

5. Adopted Qualified Jurisdictions and Reciprocal Jurisdictions

Wake stated that since the Summer National Meeting, the Mutual Recognition of Jurisdictions (E) Working Group met once on Nov. 7 in regulator-to-regulator session, pursuant to paragraph 8 (consideration of strategic planning issues) of the NAIC Policy Statement on Open Meeting, to discuss the qualified and reciprocal jurisdictions. He reminded Committee members that when the *Process for Evaluating Qualified and Reciprocal Jurisdictions* was updated in 2019, the Working Group moved from doing a full re-review of the jurisdictions every five years to now

performing a due diligence review every year. On the call, the Working Group re-approved the status of the seven existing qualified jurisdictions—Bermuda, France, Germany, Ireland, Japan, Switzerland, and the United Kingdom (UK)—and the three reciprocal jurisdictions that are not subject to an in-force "Bilateral Agreement Between the United States of America and the United Kingdom on Prudential Measures Regarding Insurance and Reinsurance" (UK Covered Agreement)—Bermuda, Japan, and Switzerland. Wake noted that during that meeting, NAIC staff provided a detail of the due diligence review process that they performed and a recommendation to the Working Group that all these jurisdictions should retain their status, and this recommendation was then approved by the Working Group. The Working Group did not express any reservations and unanimously adopted the reapproval of the statuses for the jurisdictions.

Wake made a motion, seconded by Doggett, to adopt the report of the Mutual Recognition of Jurisdictions (E) Working Group (Attachment Nine). The motion passed unanimously.

6. Heard an Overview and Update on the IMR

Bruggeman, chair of the Statutory Accounting Principles (E) Working Group, provided a technical overview and update on the interest maintenance reserve (IMR), known as the IMR liability. He suggested that in trying to understand the IMR, people should think of fixed-income investments or debt instruments as investments that primarily generate income through interest receipts versus dividends or market price growth, or more simply referred to as bonds for the purposes of this overview and update. Basically, the IMR liability is a statutory-specific accounting mechanism for life and fraternal companies that effectively smooths the impact from the gains and losses of sales of bonds into income over time. For statutory accounting, most bonds are reported at an amortized-cost basis; i.e., the asset is recorded at what the insurer paid for the bond while amortizing the difference in cost and maturity value to income over the life of the bond. This avoids balance sheet fluctuations due to market changes, as most insurers can hold those bonds until maturity. Prior to 1992, when the IMR liability went into effect, state insurance regulators recognized that life companies were selling bonds that had higher contract interest rates than what was in the market—i.e., a declining interest rate market—which generated a gain to income and surplus. Bond market value change is inverse to the change in interest rate; therefore, surplus would grow via the sale gain and increase the availability of dividends, but the new bond would have a lower yield, albeit probably the same dollar of interest. Besides the dividend item, the new investments could create a mismatch with related liabilities.

Bruggeman noted that the intent of the IMR is to ensure that the selling activity of insurers represents the intent to match assets and liabilities and discourage investment churning for short-term purposes when longer-term assets are needed for policyholder claims. The IMR concept was to defer recognition of the gain, or loss, of that sale when it was solely related to interest rates. That deferral would happen through amortization to income over the remaining life of the bond sold. This had the effect of putting surplus in a similar position to where it was before the sale of the bond. Historically, since the early 1990s, interest rates have generally been declining, except for the short-term rate increase during the financial crisis, and until the recent rounds of Federal Reserve rate increases. Thus, the sale of a bond more often resulted in a gain to an insurance company; i.e., the amount received was greater than the reported book value. This net gain is added to the IMR liability, which is a dedicated line on the liabilities page, and amortized into income over the average remaining life of the investments sold. The IMR liability does not reflect an actual amount owed by an insurer, but rather reflects the obligation to meet policyholder claims with potentially mismatched assets, as investments were sold for a short-term gain, and the cash from that sale will need to be reinvested at current market rates. In 1992 when the IMR was established, the concept of a net negative IMR—i.e., when sales resulted in a net loss to the insurer and overcame any prior buildup of gains to the IMR—was considered, and it was concluded that the overall theoretical basis for the IMR supports negatives added to the IMR, as well as the positives. This discussion noted that there is a need to have investment return match the liabilities associated with the investment and a need to remove the incentive for a company to make investment decisions based on the short-term balance sheet effect, and these needs exist also on the

negative side of the IMR. However, the NAIC codification project indicated that a net negative IMR liability would be an asset, and as such be non-admitted, as it represented deferred losses. Further discussion of a negative IMR was anticipated but was not concluded prior to the dissolution of the IMR dedicated to the Working Group. As industry noted in its commentary, at that time in a declining interest rate environment, the IMR was not anticipated to be a net negative, and there were other more important topics to resolve; therefore, the topic eventually fell off the radar. *Annual Statement Instructions* specify that when the IMR reaches a net negative position, the company is to report a zero on the liability page, recognize a "disallowed IMR asset" on the asset page, and non-admit this asset. This non-admittance is a direct reduction to surplus. Non-admittance is consistent with the statutory statement of concepts, which indicates that assets that cannot be used for policyholder obligations shall not be recognized on the balance sheet.

The result of these asset sales represents realized losses to an insurer, and the deferral of losses would also not be supported under the concepts. For non-life companies, the sale of bonds in the current environment would result in the realized losses being reported directly as reductions to investment income. The current economy is now in a rapidly rising interest rate environment. Insurers are electing to sell bonds, likely resulting in a loss, because the cash received is less than the current book value. Although asset sales have always had the potential to reflect losses, the current environment and level of sale activity at a loss are eliminating prior IMR balances so that the overall IMR position for some companies is a net negative; now it is a topic to resolve.

On Oct. 31, the American Council of Life Insurers (ACLI) provided a comment letter to the Statutory Accounting Principles (E) Working Group requesting that urgent attention be given to the reporting of the net negative IMR, with a request that the negative position be permitted as an admitted asset. Two key themes were noted in that letter: 1) in general, rising interest rates are favorable to the financial health of the insurance industry and policyholders; however, with a negative IMR, there is an inappropriate perception of decreased financial strength through lower surplus and risk-based capital (RBC); and 2) a negative IMR could affect the rating agency view of the industry or incentivize companies to avoid prudent investment transactions that are necessary to avoid mismatches between assets and liabilities. In either scenario, a negative IMR encourages short-term non-economic activity that is not in the best long-term interest of a reporting entity's financial health or its policyholders. The letter also noted that the non-admitted negative IMR could result in a double counting of losses within the asset adequacy testing (AAT). These comments were recently addressed by the Life Actuarial (A) Task Force, such that double counting would not happen. The Statutory Accounting Principles (E) Working Group heard original comments on the issue from the ACLI during the Committee's Nov. 16 conference call, and an initial agenda item was presented at the Fall National Meeting. Although industry may be looking for a quicker resolution, the following highlights key concerns, with a rush on this discussion: 1) this is a complex topic that requires detailed discussion and coordination with other groups, such as the Life Actuarial Task Force. A rush to establish statutory precedent could have negative future consequences without proper consideration. That dedicated IMR working group mentioned earlier did not resolve in its several year existences; 2) the statutory approach permits states to issue permitted practices providing departures from the statutory accounting principle (SAP). These provisions permit the domiciliary regulators to review the company's specific situation and determine the appropriate accounting treatment. It also allows the domicile to consider stipulations and additional separate reporting to monitor the situation as it evolves. This provision only requires notification to other states in which a company is licensed and disclosure in Note 1 of the financials; and 3) the potential for a negative IMR only arises for companies that are selling bonds. Although the ACLI is accurate that reinvestment at higher interest rates could be favorable to insurers, and policyholders, it is important to highlight that such benefits only arise if the cash received from the sale is reinvested to match liabilities. If the cash received is not reinvested, the result simply allows the financial statements to reflect an improved balance sheet position and deferred losses as assets, which would not be available for policyholder claims. This may provide further support for individual state review to assess the reason for sales and how the cash is being used. Also, many companies used and are using derivatives as a hedging strategy for interest rate risk. Bond sale losses are offset against related derivative gains before being

included in the IMR calculation, making that another potential complication, especially if one side is sold but the other is not.

Bruggeman noted that a review of the financial statements has shown a noted decline in the IMR liability balance since year-end 2021. Additionally, 60 companies with prior IMR liability balances have been identified as flipping to a net negative with a disallowed, or nonadmitted, asset on the balance sheet representing $1 billion as of Q3 2022. Identification of the net negative within the NAIC's data is a manually intensive process, as it is an aggregate write-in. At the Fall National Meeting, the Statutory Accounting Practices (E) Working Group decided to: 1) continue exposure of the ACLI letter and the staff discussion of the topic, which included summarized financial data; 2) give NAIC staff direction to keep the Life Actuarial (A) Task Force or its staff up to date on any actions; 3) ask industry and any specific companies to show unique examples/situations through regulator-only discussions with Working Group and Task Force representatives; 4) discuss what risks could be posed by allowing admittance; and 5) request that Interested Parties suggest viable guardrails to protect surplus and policyholders, such as requiring bond reinvestment; recording special surplus equivalent to a net negative IMR, which would limit dividends; limiting a net negative IMR to percent of surplus, or percent of bonds, invested assets, or total assets; and limiting a net negative IMR amortization time, AAT adjustments—i.e., level of haircut when in a net negative IMR—and/or other prudent considerations. Bruggeman noted that in the meantime, while considering any admittance or not, companies should have discussions with the domestic regulator for possible consideration of permitted practices or stipulations.

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

Https://naiconline.sharepoint.com/sites/NAICSupportStaffHub/Member Meetings/E CMTE/2022-3-Fall/121522 E Minutes.docx

Attachment Two

*2023 Spring National Meeting*
*Louisville, Kentucky*

**ACCOUNTING PRACTICES AND PROCEDURES (E) TASK FORCE**
Thursday, March 23, 2023
11:00 a.m. – 12:00 p.m.

**Meeting Summary Report**

The Accounting Practices and Procedures (E) Task Force met March 23, 2023. During this meeting, the Task Force:

1. Adopted its 2022 Fall National Meeting minutes.

2. Adopted the report of the Statutory Accounting Principles (E) Working Group, which met March 22 and took the following action:

   A. Adopted its 2022 Fall National Meeting minutes.

   B. Adopted *Issue Paper No. 16X—Derivatives and Hedging*, which historically documents new Statutory Accounting Principles (SAP) concept revisions to the documentation and assessment of hedge effectiveness, measurement method guidance for excluded components, and modified incorporation of the U.S. generally accepted accounting principles (GAAP) portfolio layer method and the partial-term hedging method in *Statement of Statutory Accounting Principles (SSAP) No. 86—Derivatives*. (Ref #2017-33)

   C. Adopted the following clarifications to statutory accounting guidance:

      i. Revisions clarify that any invested asset held by a reporting entity that is issued by an affiliated entity, or which includes the obligations of an affiliated entity, is an affiliated investment. (Ref #2022-15)

      ii. Revisions add and data-capture additional investment income disclosures. Directed NAIC staff to submit a corresponding blanks proposal for year-end 2023. (Ref #2022-17)

      iii. Revisions adopt *Accounting Standards Update (ASU) 2022-03, Fair Value Measurement of Equity Securities Subject to Contractual Sales Restrictions* with a modification to reject the contractual sales restrictions disclosures. (Ref #2022-16)

      iv. Revisions reject guidance from *ASU 2017-12, Derivatives and Hedging* and *ASU 2022-04, Disclosure of Supplier Finance Program Obligations*, as the disclosures are for borrowers, not insurance entity investors. (Ref #2022-18)

D. Exposed the following SAP clarifications to statutory accounting guidance until June 9, except for agenda items 2023-03 and 2023-11EP, which have a comment deadline of May 5:

i. Exposed revisions to *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets* and *Issue Paper No. 16X—Updates to the Definition of a Liability* that defer to topic-specific SSAP guidance that varies from the liability definition. (Ref #2022-01)

ii. Exposed revisions to *SSAP No. 20—Nonadmitted Assets* and *SSAP No. 21R—Other Admitted Assets* to clarify that pledged collateral must qualify as an admitted invested asset for a collateral loan to be admitted. The revisions require audits and the use of net equity value for valuation assessments when the pledged collateral is in the form of partnerships, limited liability companies (LLCs), or joint ventures. (Ref #2022-11)

iii. Exposed revisions to *SSAP No. 24—Discontinued Operations and Unusual or Infrequent Items* to clarify the rejection of *ASU 2021-10, Government Assistance* and the incorporation of disclosures regarding government assistance. (Ref #2023-06)

iv. Exposed revisions to incorporate changes to add collateralized loan obligations (CLOs) to the financial modeling guidance and clarify that CLOs are not legacy securities. (Ref #2023-02)

v. Exposed revisions to adopt with modification *ASU 2019-08, Compensation—Stock Compensation (Topic 718) and Revenue from Contracts with Customers (Topic 606): Codification Improvements—Share-Based Consideration Payable to a Customer*. The revisions add guidance to include share-based consideration payable to customers. (Ref #2023-07)

vi. *Interpretation (INT) 03-02: Modification to an Existing Intercompany Pooling Arrangement*: Exposed the intent to nullify INT 03-02, as it is inconsistent with *SSAP No. 25—Affiliates and Other Related Parties*. (Ref #2022-12)

vii. Exposed revisions to revise the expiration date of *INT 20-01: ASU 2020-04 and 2021-01 – Reference Rate Reform* to Dec. 31, 2024. (Ref #2023-05)

viii. Exposed revisions to refine guidance for the principles-based bond project and Schedule D reporting. Directed NAIC staff to continue interim discussions with interested parties. (Ref #2019-21)

ix. Exposed a proposed new project to review the annual and quarterly statement instructions to ensure that accounting guidance is reflected within the SSAPs. (Ref #2023-01)

x. Exposed revisions providing new disclosures, which provide the net amount at risk detail needed to support updates to the life risk-based capital (RBC) C-2 mortality risk charges. This item was exposed with a shortened comment deadline of May 5. (Ref #2023-03)

xi. Exposed editorial revisions with a shortened comment deadline of May 5. (Ref #2023-11EP)

xii. The following U.S. GAAP standards were exposed with revisions to reject, as they are not applicable to statutory accounting:

a. *ASU 2019-07, Codification Updates to SEC Sections: Amendments to SEC Paragraphs Pursuant to SEC Final Rule Releases No. 33-10532, Disclosure Update and Simplification, and Nos. 33-10231 and 33-10442, Investment Company Reporting Modernization, and Miscellaneous Updates* (Ref #2023-08)

b. *ASU 2020-09, Amendments to SEC Paragraphs Pursuant to SEC Release No. 33-10762—Debt (Topic 470)* (Ref #2023-09)

c. *ASU 2022-05, Transition for Sold Contracts* (Ref #2023-10)

E. Directed NAIC staff on the following items:

i. Directed NAIC staff to proceed with drafting revised accounting guidance and a related issue paper for both *SSAP No. 93—Low-Income Housing Tax Credit Property Investments* and *SSAP No. 94R—Transferable and Non-Transferable State Tax Credits*. (Ref #2022-14)

ii. *SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve*: Directed NAIC staff regarding the consideration of negative interest maintenance reserve (IMR) with an intent to work on both a 2023 solution and a long-term solution as follows:

a. Recommend a referral to the Life Actuarial (A) Task Force on further consideration of the asset adequacy implications of negative IMR. Items to include: 1) developing a template for reporting within asset adequacy testing (AAT); 2) considering the actual amount of negative IMR that is admitted to be used in the AAT; 3) better consideration of cash flows within AAT (and documentation), as well as any liquidity stress test (LST) considerations; 4) ensuring that excessive withdrawal considerations are consistent with actual data (sales of bonds because of excess withdrawals should not use the IMR process); and 5) ensuring that any guardrails for assumptions in the AAT are reasonable and consistent with other aspects.

b. Recommend a referral to the Capital Adequacy (E) Task Force for the consideration of eliminating any admitted net negative IMR from total adjusted capital (TAC) and the consideration of sensitivity testing with and without negative IMR.

c. Develop guidance for future Working Group consideration that would allow the admission of negative IMR up to 5% of surplus using the type of limitation calculation similar to that used for goodwill admittance. The guidance should also provide for a downward adjustment if the RBC ratio is less than 300.

d. Review and provide updates on any annual statement instructions for excess withdrawals, related bond gains/losses, and non-effective hedge gains/losses to clarify that those related gains/losses are through asset valuation reserve (AVR), not IMR.

e. Develop accounting and reporting guidance to require the use of a special surplus (account or line) for net negative IMR.

f. Develop governance related documentation to ensure that sales of bonds are reinvested in other bonds.

g. Develop a footnote disclosure for quarterly and annual reporting. (Ref #2022-19)

iii. Directed NAIC staff to continue work with industry and Working Group members on developing guidance for the reporting of the corporate alternative minimum tax (CAMT) for interim Working Group discussion. (Ref #2023-04)

F. Received an update on the following items:

i. Received a referral from the Valuation of Securities (E) Task Force to inquire about the NAIC Securities Valuation Office (SVO) obtaining the ability to calculate analytical information.

ii. Announced that copyrighted PDF copies of the *Accounting Practices and Procedures Manual* (AP&P Manual) will be made available through an Account Manager upon purchase of the 2023 AP&P Bookshelf subscription.

iii. Received a request from the American Academy of Actuaries (Academy) for clarification on observed diversity across issuers regarding long-term care (LTC) AAT under *Actuarial Guideline LI—The Application of Asset Adequacy Testing to Long-Term Care Insurance* Reserves (AG 51), *SSAP No. 54R—Individual and Group Accident and Health Contracts*, and *Appendix A-010, Minimum Reserve Standards for Individual and Group Accident and Health Insurance Contracts*.

iv. Received an update on international activity as discussed by the International Association of Insurance Supervisors (IAIS) Accounting and Auditing Working Group (AAWG), noting that public consultations *of Insurance Core Principle (ICP) 14: Valuation* and *ICP 17: Capital Adequacy* are expected in July 2023.

v. Received an update on U.S. GAAP exposures, noting that pending items will be addressed during the normal maintenance process.

3. Adopted the report of the Blanks (E) Working Group, which met March 7 and took the following action:

A. Adopted its Nov. 17, 2022, minutes.

B. Adopted its editorial listing and the following proposals:

   i. 2022-14BWG Modified – Modify Exhibit 1, Part 1 and 2, and Exhibit 8, Part 1 and 2, in the life and accident and health/fraternal blank, to include the line of business detail reported on the Analysis of Operations by Lines of Business pages.

   ii. 2022-15BWG – In the life, accident and health/fraternal, and property/casualty blanks, revise the language of the Schedule H, Part 5 to remove the 5% of premiums filing exemption.

   iii. 2022-16BWG – Remove Supplemental Health Care Exhibit Part 3 and Supplemental Health Care Exhibit's Expense Allocation Report.

   iv. 2022-18BWG – For the life and accident and health/fraternal blank instructional corrections on the handling of Exchange Traded Funds (ETFs) and/or Securities Valuation Office (SVO-Identified Funds within the IMR and the AVR.

   v. 2022-20BWG – Modify the instructions and blanks for various health exhibits to change the order of the Vision and Dental lines of business to be consistent with all other statement types.

C. Re-exposed the following proposal:

   i. 2022-17BWG – Add new disclosure paragraph for Note 8 – Derivative Instruments and illustration to new disclosure to be data-captured. Add electronic-only columns related to derivatives with excluded components to Schedule DB, Part A and Part B for both Section 1 and Section 2. Add new code column instructions for Schedule DB, Part A and B (SAPWG 2021-20). Re-exposed for a public comment period ending April 28.

D. Exposed nine new proposals for a public comment period ending April 28 for eight of the proposals and June 30 for proposal 2023-06BWG addressing Schedule D, Part 1 reporting.

NAIC NATIONAL MEETING SPRING 2023

*2023 Spring National Meeting*
*Louisville, Kentucky*

**CAPITAL ADEQUACY (E) TASK FORCE**
Thursday, March 23, 2023
4:00 – 5:00 p.m.

**Meeting Summary Report**

The Capital Adequacy (E) Task Force met March 23, 2023. During this meeting, the Task Force:

1. Adopted its Feb. 3, 2023; and 2022 Fall National Meeting minutes, which included the following action:
   A. Adopted proposal 2022-12-CR (2022 U.S. and Non-U.S. Catastrophe Risk Event Lists).

2. Adopted the report of the Health Risk-Based Capital (E) Working Group, which met March 21 and took the following action:
   A. Adopted its Feb. 7 minutes, which included the following action:
      i. Adopted its 2022 Fall National Meeting Minutes.
      ii. Adopted proposal 2022-14-H (Trend Test Instructions), which the Working Group exposed for a 30-day public comment period ending Dec. 7, 2022.
      iii. Referred the runoff company response letter to the Capital Adequacy (E) Task Force.
      iv. Exposed proposal 2022-16-CA (Underwriting Risk Factors – Investment Income Adjustment) for a 30-day public comment period ending March 9, 2023.
      v. Received an update from the American Academy of Actuaries (Academy) on the H2 – Underwriting Risk Review project.
   B. Adopted proposal 2022-15-H (Page XR008 Renumbering).
   C. Referred proposal 2022-16-CA (Underwriting Risk Factors Investment Income Adjustment) to the Task Force for a 30-day exposure for all lines of business.
   D. Adopted its 2023 working agenda.
   E. Exposed proposal 2023-01-CA (Stop Loss Instructions) for a 20-day public comment period ending April 10.
   F. Discussed the stop loss data and factors.
   G. Received an update on the Health Test Ad Hoc Group and the draft proposal with revisions to the health test language and general interrogatories.
   H. Discussed the effect of the COVID-19 pandemic and pandemic risk in the health risk-based capital (RBC) formula.
   I. Received an update on the H2 – Underwriting Risk review.

3. Adopted the report of the Life Risk-Based Capital (E) Working Group, which met March 22 and took the following action:
   A. Adopted its Jan. 26 minutes, which included the following action:
      i. Exposed the Academy's C2 Mortality Risk Work Group's proposal for a 30-day public comment period ending March 1.

   ii. Exposed proposed revisions to the CM6 and CM7 mortgage RBC factors and formula for a 45-day public comment period ending March 16.
   iii. Exposed proposed revisions to remove the dual presentation of the trend test for a 15-day public comment period ending Feb. 14.
B. Adopted its 2022 Fall National Meeting Minutes.
C. Discussed C-2 mortality risk.
D. Discussed its 2023 working agenda.
E. Discussed runoff companies.
F. Received an update on the status of the Economic Scenarios (E/A) Subgroup.

4. Adopted the report of the Risk-Based Capital Investment Risk and Evaluation (E) Working Group, which met March 23 and took the following action:
   A. Adopted its Feb. 27 minutes, which included the following action:
      i. Discussed the Academy's follow-up to its presentation on collateralized loan obligations (CLOs).
      ii. Discussed comments received on the referral from the Valuation of Securities (E) Task Force.
      iii. Discussed comments received on the potential structure change to address residual tranches.
   B. Adopted its 2022 Fall National Meeting Minutes.
   C. Received updates from the Valuation of Securities (E) Task Force and the Statutory Accounting Principles (E) Working Group.
   D. Continued discussion of CLOs.
   E. Discussed the residual tranche structure change.
   F. Discussed residual tranche factor and next steps.

5. Adopted the report of the Property and Casualty Risk-Based Capital (E) Working Group, which met March 22 and took the following action:
   A. Adopted its Jan. 30 minutes, which included the following action:
      i. Adopted proposal 2022-12-CR (2022 U.S. and Non-U.S. Catastrophe Risk Event Lists), which the Subgroup exposed for a seven-day public comment period ending Jan. 25.
   B. Adopted its 2022 Fall National Meeting minutes.
   C. Adopted the report of the Catastrophe Risk (E) Subgroup, which met March 21 minutes and took the following action:
      i. Adopted its Jan. 30, 2023, and 2022 Fall National Meeting minutes.
      ii. Discussed its working agenda.
      iii. Received a status update from its Catastrophe Model Technical Review Ad Hoc Group.
      iv. Heard a presentation from Travelers on the climate overview and scenario analysis.
      v. Discussed the wildfire peril impact analysis.
   D. Exposed proposal 2023-02-P (Underwriting Risk Line 1 Factors) for a 30-day public comment period ending April 21.
   E. Discussed annual statement proposal 2023-01BWG, which removes pet insurance from the inland marine line of business and adds new schedule P parts to pet insurance.
   F. Discussed annual statement proposal 2022-15BWG, which removes the 5% of premium filing exemption on Schedule H, Part 5.
   G. Discussed its 2023 working agenda.
   H. Heard an update on current property and casualty (P/C) RBC projects from the Academy.

I. Discussed the possibility of reviewing or analyzing the P/C RBC charges that have not been reviewed since developed.

6. Adopted proposal 2022-09-CA (Revised Affiliated investments Structure and Instructions), which the Task Force forwarded to the Blanks (E) Working Group and the Statutory Accounting Principles (E) Working Group for a 45-day comment period ending Jan. 28.

7. Adopted proposal 2022-13-CA (Health Premiums and Underwriting Risk Premium References), which the Task Force exposed for a 45-day public comment period ending Jan. 28.

8. Adopted proposal 2022-14-H (Trend Test Info Only Instruction), which the Health Risk-Based Capital (E) Working Group exposed for a 30-day comment period ending Dec. 6, 2022.

9. Adopted proposal 2022-15-H (Renumber XR008), which the Health Risk-Based Capital (E) Working Group exposed for a 30-day comment period ending Feb. 28.

10. Adopted its working agenda.

11. Discussed the response from the Health Risk-Based Capital (E) Working Group regarding runoff companies, which the Working Group exposed for a 30-day comment period ending March 9.

12. Discussed the "Proposed Amendment to the Purposes and Procedures Manual of the NAIC Investment Analysis Office (P&P Manual to Define and Add Guidance for Structured Equity and Funds" and the "Additional Market and Analytical Information for Bond Investments" referrals from the Valuation of Securities (E) Task Force. The Task Force and the Risk-Based Capital Investment Risk and Evaluation (E) Working Group exposed "Additional Market and Analytical Information for Bond Investments" for a public comment period ending March 31.

13. Discussed the current turmoil in the banking sector.

14. Discussed other matters brought before the Task Force, which included: 1) the proposed revised proposal form; 2) health test exposure updates; and 3) established ad hoc groups to review or analyze: i) current non-investment charges; ii) missing risks; and iii) modernizing asset concentration instructions.

Attachment Four

*2023 Spring National Meeting*
*Louisville, Kentucky*

**JOINT MEETING OF THE FINANCIAL STABILITY (E) TASK FORCE AND THE MACROPRUDENTIAL (E) WORKING GROUP**
Wednesday, March 22, 2023
2:00 – 3:00 p.m.

**Meeting Summary Report**

The Financial Stability (E) Task Force met March 22, 2023, in joint session with the Macroprudential (E) Working Group. During this meeting, the Task Force:

1. Adopted its Fall National Meeting minutes.

2. Heard an update on Financial Stability Oversight Council (FSOC) developments.

3. Received a Macroprudential (E) Working Group update.

4. Received a Valuation Analysis (E) Working Group update.

5. Heard an international update, which included an update on the International Association of Insurance Supervisors (IAIS) Global Monitoring Exercise (GME). The GME includes the individual insurers monitoring exercise and the sector-wide monitoring exercise with three more additional topics of interest: private equity (PE), climate, and cyber.

NAIC NATIONAL MEETING SPRING 2023

*2023 Spring National Meeting*
*Louisville, Kentucky*

**RECEIVERSHIP AND INSOLVENCY (E) TASK FORCE**
Thursday, March 23, 2023
11:00 a.m. – 12:00 p.m.

**Meeting Summary Report**

The Receivership and Insolvency (E) Task Force met March 23, 2023. During this meeting, the Task Force:

1. Adopted its 2022 Fall National Meeting minutes.

2. Adopted the report of the Receiver's Handbook (E) Subgroup, which met Dec. 21, 2022. Chapters 3, 4, and 5 of the *Receiver's Handbook for Insurance Company Insolvencies* (Receiver's Handbook) were adopted by the Subgroup. Chapters 6 and 7 were exposed for a 45-day public comment period ending Feb. 6. The drafting groups continue to make progress on drafting revisions to the remaining chapters.

3. Adopted the report of the Receivership Law (E) Working Group. The drafting group that is reviewing comments received on amendments to the *Property and Casualty Insurance Guaranty Association Model Act* (#540) for restructuring mechanisms is making progress and plans to meet again in April.

4. Adopted the report of the Receivership Financial Analysis (E) Working Group. The Working Group will meet March 23 in regulator-to-regulator session, pursuant to paragraph 3 (specific companies, entities or individuals) of the NAIC Policy Statement on Open Meetings, to discuss companies in receivership and related topics.

5. Heard an update on international resolution activities. The International Association of Insurance Supervisors (IAIS) released an application paper on policyholder protection schemes for public comment. Comments to be considered by the International Insurance Relations (G) Committee should be sent to NAIC staff by March 27.

6. Heard a presentation from the National Organization of Life and Health Insurance Guaranty Associations (NOLHGA) and the National Conference of Insurance Guaranty Funds (NCIGF) on a proposed receivership tabletop session.

NAIC NATIONAL MEETING SPRING 2023

*Virtual Meeting*
*(in lieu of meeting at the 2023 Spring National Meeting)*

**REINSURANCE (E) TASK FORCE**
Monday, March 6, 2023
12:00 – 1:00 p.m. ET / 11:00 a.m. – 12:00 p.m. CT / 10:00 – 11:00 a.m. MT / 9:00 – 10:00 a.m. PT

**Meeting Summary Report**

The Reinsurance (E) Task Force met March 6, 2023. During this meeting, the Task Force:

1. Adopted its 2022 Fall National Meeting minutes.

2. Adopted the report of the Reinsurance Financial Analysis (E) Working Group, which met Jan. 31, 2023; Dec. 19, 2022; and Nov. 22, 2022, in regulator-to-regulator session, pursuant to paragraph 3 (specific companies, entities, or individuals) of the NAIC Policy Statement on Open Meetings. During these meetings, the Working Group completed the reviews of certified reinsurers and reciprocal jurisdiction reinsurers.

3. Received a status report on the reinsurance activities of the Mutual Recognition of Jurisdictions (E) Working Group.

4. Received a status report on the states' implementation of the *Term and Universal Life Insurance Reserve Financing Model Regulation* (#787).

NAIC NATIONAL MEETING SPRING 2023

*2023 Spring National Meeting*
*Louisville, Kentucky*

**VALUATION OF SECURITIES (E) TASK FORCE**
Thursday, March 23, 2023
2:00 – 3:30 p.m.

**Meeting Summary Report**

The Valuation of Securities (E) Task Force met March 23, 2023. During this meeting, the Task Force:

1. Adopted its Feb. 21, 2023, and 2022 Fall National Meeting minutes. During these meetings, the Task Force took the following action:
   A. Adopted a *Purposes and Procedures Manual of the NAIC Investment Analysis Office* (P&P Manual) amendment to update references to 5GI. The amendment had previously been exposed for a 60-day public comment period ending Feb. 13.
   B. Adopted a P&P Manual amendment to add instructions for the financial modeling of collateralized loan obligations (CLOs). The amendment had previously been exposed for a 15-day public comment period ending Jan. 9.
   C. Discussed proposed CLO modeling methodology (excluding scenarios and probabilities).

2. Received a report on the projects of the Risk-Based Capital (RBC) Investment Risk and Evaluation (E) Working Group.

3. Discussed an amendment to the P&P Manual to add instructions for structured equity and funds and deferred a decision on the amendment. The amendment had previously been exposed for a 60-day public comment period ending Feb. 13. The Task Force directed staff to send a referral to the Statutory Accounting Principles (E) Working Group to request that it consider the definition of structured equity and funds in its residual guidance.

4. The Task Force directed staff to draft an amendment outlining recommended procedural steps for reviewing filing exempt (FE) investment securities for which it has concerns about the assigned NAIC Designation and the steps insurers could take to clarify and rebut the Securities Valuation Office's (SVO's) concerns about the proposed NAIC Designation.

5. Discussed next steps for the CLO modeling project.

6. Discussed proposed questions for NAIC credit rating providers (CRPs) and requested that any recommendations be sent to SVO staff.

7. Exposed a proposed P&P Manual amendment to update the Notice of Credit Deterioration for the List of Qualified U.S. Financial Institutions for a 15-day public comment period ending April 10, followed by an e-vote. The Task Force directed staff to also refer the amendment to the Reinsurance (E) Task Force.

8. Received the Annual Report from the SVO on year-end carry-over filings.

9. Received a staff report on projects of the Statutory Accounting Principles (E) Working Group.

Attachment Eight

*2023 Spring National Meeting*
*Louisville, Kentucky*

**MORTGAGE GUARANTY INSURANCE (E) WORKING GROUP**
Wednesday, March 22, 2023
8:00 – 9:00 a.m.

**Meeting Summary Report**

The Mortgage Guaranty Insurance (E) Working Group met March 22, 2023. During this meeting, the Working Group:

1. Adopted its 2022 Fall National Meeting minutes.

2. Discussed comments received on the exposure of the *Mortgage Guaranty Insurance Model Act* (#630).

3. Discussed a proposed U.S. Securities and Exchange Commission (SEC) rule.

Draft: 3/15/23

National Treatment and Coordination (E) Working Group
Virtual Meeting
February 14, 2023

The National Treatment and Coordination (E) Working Group of the Financial Condition (E) Committee met Feb. 14, 2023. The following Working Group members participated: Debbie Doggett and Kelly Hopper, Co-Chair (MO); Cameron Piatt, Co-Chair (OH); Jacline Nguyen (CO); William Mitchell (CT); Sherry Wilson (DE); Alison Sterett (FL); Tangela Byrd (LA); Doug Hartz (OR); Karen Feather (PA); John Carter (TX); Jay Sueoka (UT); Ron Pastuch (WA); Christopher Martin (WI); and Doug Melvin (WY).

1. Adopted Proposal 2022-03

Doggett said the proposal was exposed for a 30-day comment period ending Dec. 12, 2022. There were no comments received. Doggett reminded the Working Group that the proposal adopted today is subject to change once the electronic format is developed to accommodate for electronic modifications.

Hartz made a motion, seconded by Wilson, to adopt proposal 2022-03 (Domestic Corporate Amendment Application and Instructions) (Attachment). The motion passed unanimously.

2. Adopted Proposal 2023-01

Piatt explained the modifications to proposal 2023-01 (Redomestication Form 2R) were to remove information that pertained to the primary (start-up) application now that the previous Form 2P has been split into two separate applications and is determined to not be necessary for a redomestication application. Piatt said that the edits to this form are self-explanatory and suggested adopting the proposal instead of exposing it for comment.

Sueoka made a motion, seconded by Pastuch, to adopt proposal 2023-01 (Redomestication Form 2R) (Attachment). The motion passed unanimously.

3. Discussed Other Matters

Jane Barr (NAIC) said that the electronic primary application is available for testing in production. Any company interested in participating should contact Barr, as the link has not been posted on the website. The developers will begin working on the Redomestication application. It has yet to be determined if that application will be available to pilot test. Barr anticipates that both applications will be ready for public use by July 1.

Barr also mentioned that the Uniform Certificate of Authority Application (UCAA) logo is being rebranded. A sample is provided on the redomestication form. Once the logo is approved, the application forms and website will be updated to coincide with the new application release. Barr will keep the Working Group updated on the timeline for that change. The intent is to update every UCAA form and content on the website. Karen Fallstrom (UnitedHealthcare) asked if that applied to form 11 and the addendum pages. Barr confirmed it did include form 11 and the addendum page.

Barr said the ad hoc groups will resume in March with a slight change to the domestic state applications. Ad hoc groups will meet on Thursday afternoons every two weeks to coincide with the enhancement release schedule. The Form A and Biographical Database Ad Hoc Groups will meet on alternate Monday afternoons beginning in March. Anyone interested in participating should email Barr.

 

Having no further business, the National Treatment and Coordination (E) Working Group adjourned.

SharePoint/NAIC Support Staff Hub/Meetings/E CMTE/2023-1-Spring/NTCWG/2_14_ccmin-draft.docx

NAIC NATIONAL MEETING SPRING 2023

*2023 Spring National Meeting*
*Louisville, Kentucky*

**RISK-FOCUSED SURVEILLANCE (E) WORKING GROUP**
Thursday, March 23, 2023
9:30 – 10:30 a.m.

**Meeting Summary Report**

The Risk-Focused (E) Surveillance Working Group met March 23, 2023. During this meeting, the Working Group:

1. Discussed and exposed proposed changes to the NAIC's *Financial Analysis Handbook* and *Financial Condition Examiners Handbook* for a 45-day public comment period ending May 8. The proposed changes, developed by a drafting group consisting of state insurance regulators and industry representatives, are intended to provide additional guidance for regulators in reviewing service agreements put in place between insurers and their affiliates, particularly those that incorporate market-based reimbursement for services performed. In addition to requesting comments on the proposed handbook additions, the exposure also requests input on whether and how guidance on "cost-plus" reimbursement rates for affiliated service contracts should be developed and included in handbook guidance.

2. Discussed plans to conduct an all-state survey to collect data on financial analyst and examiner compensation for purposes of adjusting the salary ranges included in NAIC handbooks.

3. Discussed plans for 2023 peer review training sessions, which include two financial analysis sessions, one financial examination session, and one Own Risk and Solvency Assessment (ORSA)-focused session.

TO: Elizabeth Kelleher Dwyer, Chair, Financial Conditions (E) Committee
Marlene Caride, Chair, Financial Stability (E) Task Force
Bob Kasinow, Chair, Macroprudential (E) Working Group
Thomas Botsko, Chair, Capital Adequacy (E) Task Force
Phillip Barlow, Chair, Risk-Based Capital Investment Risk and Evaluation (E) Working Group
Cassie Brown, Chair, Life Actuarial (A) Task Force
Judy Weaver, Chair, Financial Analysis (E) Working Group
Dale Bruggeman, Chair, Statutory Accounting Principles (E) Working Group
Fred Andersen, Chair, Valuation Analysis (E) Working Group

FROM: Carrie Mears, Chair, Valuation of Securities (E) Task Force

CC: Charles A. Therriault, Director, NAIC Securities Valuation Office (SVO)
Eric Kolchinsky, Director, NAIC Structured Securities Group (SSG) and Capital Markets Bureau
Dan Daveline, Director, NAIC Financial Regulatory Services
Todd Sells, Director, NAIC Financial Regulatory Policy & Data
Marc Perlman, Managing Investment Counsel, NAIC Securities Valuation Office (SVO)
Julie Gann, Assistant Director, NAIC Solvency Policy
Bruce Jenson, Assistant Director, NAIC Solvency Monitoring
Pat Allison, Managing Life Actuary, NAIC Financial Regulatory Affairs
Jane Koenigsman, Sr. Manager II, NAIC L/H Financial Analysis
Andy Daleo, Sr. Manager I, NAIC P/C Domestic and International Analysis
Dave Fleming, Sr. Life RBC Analyst, NAIC Financial Regulatory Affairs
Jennifer Frasier, Life Examination Actuary, NAIC Financial Regulatory Affairs
Scott O'Neal, Life Actuary, NAIC Financial Regulatory Affair
Eva Yeung, Sr. P/C RBC Analyst/Technical Lead, NAIC Financial Regulatory Affairs

RE: Referral on Additional Market and Analytical Information for Bond Investments

DATE: February 13, 2023

**Summary** – The Investment Analysis Office (IAO) staff recommended in its Feb. 25, 2022, memorandum to the Valuation of Securities (E) Task Force (VOSTF) (attached hereto, Blanks Market Data Disclosure v2.pdf) that it would like additional market-data fields added to the annual statement instructions for bond investments. This was, in part, based upon the NAIC's adoption in 2010 of the recommendations of

the Rating Agency (E) Working Group (RAWG), which was formed following the Great Financial Crisis of 2007-2008 to study the NAIC's reliance on rating agencies, and the IAO staff's recent findings in its Nov. 2021 memo regarding disparities between rating agencies. RAWG recommended that: 1) regulators explore how reliance on rating agencies can be reduced when evaluating new, structured, or alternative asset classes, particularly by introducing additional or alternative ways to measure risk; and 2) consider alternatives for regulators' assessment of insurers' investment risk, including expanding the role of the NAIC Securities Valuation Office ("SVO"); and 3) VOSTF should continue to develop independent analytical processes to assess investment risks. These mechanisms can be tailored to address unique regulatory concerns and should be developed for use either as supplements or alternatives to ratings, depending on the specific regulatory process under consideration.

The NAIC's need for alternative measures of investment risk has only increased since RAWG made its recommendations, as privately issued and rated complex structured finance transactions have become commonplace without adequate ways of identifying them. The SVO recommended the following market data fields to be added to the annual statement instructions: Market Yield, Market Price, Purchase Yield, Weighted Average Life, Spread to Average Life UST, Option Adjusted Spread, Effective Duration, Convexity and VISION Issue ID. Please refer to the attached memo for more detail on each data field.

In comments received from industry there were question as to how the SVO, VOSTF and/or other regulators who would receive the analytic data included in the proposal would utilize that information and why it is of value to them. The SVO was also asked to consider industry's recommendation that the NAIC be responsible for calculating this analytical information by utilizing commercially available data sources and investment models instead of having each individual insurance company incur the costs to implement system changes. The SVO shared their thoughts on the alternatives in the Jul. 14, 2022, memorandum to the VOSTF (attached, Blanks_Market_Data_Options_v3.pdf).

Capabilities like this within the SVO would permit it to calculate for regulators all the analytic values previously mentioned for any Schedule D investment along with additional measures such as key rate duration (a measure of interest rate sensitivity to maturity points along the yield curve), sensitivity to interest rate volatility, principal and interest cash flow projections for any security or portfolio for any given interest rate projection, loss estimates for any security for any given scenario and many others measures.

**Referral** – VOSTF refers this matter to the above referenced Committees, Task Forces and Working Groups for consideration and requests a response from you by May 15th outlining:

1. Indicate if your group is supportive of creating this capability within the SVO.
2. List the investment analytical measures and projections that would be most helpful to support the work performed by your respective group.
3. Describe how your group would utilize the data and why it would be of value.
4. Are there other investment data or projection capabilities that would be useful to your group that could be provided by commercially available data sources or investment models? And if so, please list them.
5. Any other thoughts you may have on this initiative.

Please contact Charles Therriault or Marc Perlman with any questions.

NAIC NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

TO: Carrie Mears, Chair, Valuation of Securities (E) Task Force
Members of the Valuation of Securities (E) Task Force

FROM: Charles A. Therriault, Director, NAIC Securities Valuation Office (SVO)
Marc Perlman, Managing Investment Counsel, NAIC Securities Valuation Office (SVO)

CC: Eric Kolchinsky, Director, NAIC Structured Securities Group (SSG) and Capital Markets Bureau

RE: Additional Market Data Fields for Bond Investments

DATE: February 25, 2022

The SVO proposes adding additional market-data fields for bond investments to the annual statement instructions based on 2010 adopted recommendations of the Rating Agency (E) Working Group (RAWG) and the IAO staff's findings regarding the discrepancies between ratings, presented in its Nov. 2021 memo.

The RAWG was formed after the Financial Crisis of 2008 and was charged with gathering and assessing information on:

1. *The problems inherent in reliance on ratings, including impact on the filing exempt ("FE") process and Risk-Based Capital ("RBC");*
2. *The reasons for recent rating shortcomings, including but not limited to structured security and municipal ratings;*
3. *The current and potential future impact of ratings on state insurance financial solvency regulation; and*
4. *The effect of the use of NRSRO ratings on public confidence and public perception of regulatory oversight of the quality of insurance.*

The RAWG made the following summary recommendations in their Apr. 28, 2010, report that was adopted by the Financial Condition (E) Committee (emphasis added):

1. *Regulators **explore how reliance** on ARO (Approved Ratings Organization) ratings **can be reduced** when evaluating new, structured, or alternative asset classes, particularly by **introducing additional or alternative ways to measure risk**;*
2. ***Consider alternatives for regulators' assessment of insurers' investment risk**, including **expanding the role of the NAIC Securities Valuation Office** ("SVO"); and*

3. *When considering continuing the use of ratings in insurance regulation, the* ***steps taken by the NRSROs in correcting the causes that led to recent rating shortfalls****, including the NRSROs' efforts in implementing the recommended structural reforms, should be taken into account.*

As the IAO staff demonstrated with the analysis in its Nov. 29, 2021, memo regarding ratings discrepancies, not all credit rating provider (CRP) ratings reflect a reasonable assessment of a security's risk, indicating that rating shortfalls persist today. The NAIC has not made additional progress in reducing reliance on CRPs and the IAO proposed several steps in its memo to accomplish that objective. As noted by the RAWG and reflected in the IAO's memo, there persists a situation where "*… ratings are neither consistent nor uniform for individual securities, nor across different types and classes of securities…*" However, the role of the SVO has not been expanded to include "*… evaluating credit and other risks of securities*."[1]

One step towards introducing alternative ways to measure a security's risk would be to require insurers to report various analytical measures about each security including metrics such as its current market yield, interest rate sensitivity, spread relative to risk-free securities such as United States Treasuries and average remaining life. The more a security's market yield and spread differ from similarly rated securities, the more likely it is that the implied market-perceived risk of that security differs from the risk indicated by the credit rating assigned to it. The yield difference or spread in basis points can potentially help identify securities whose risk assessment warrants further review by the SVO, examiners or other regulatory groups, for example, a AAA rated security with a yield of 5%. Other fields that measure a security's price sensitivity to interest rate movements may also help to identify market-perceived risk inconsistent with the assigned credit rating. These additional market data fields would align with the RAWG's referral to the Task Force and SVO Initiatives (EX) Working Group, as noted in their following detailed recommendations (emphasis added):

1. *Referral to the NAIC Valuation of Securities (E) Task Force: VOS should continue to* ***develop independent analytical processes to assess investment risks****. These mechanisms can be tailored to address unique regulatory concerns and should be developed for* ***use either as supplements or alternatives to ratings****, depending on the specific regulatory process under consideration.*
2. *Referral to the NAIC Valuation of Securities (E) Task Force: ARO ratings have a role in regulation; however, since* ***ratings cannot be used to measure all the risks that a single investment or a mix of investments may represent in an insurer's portfolio, NAIC policy on the use of ARO ratings should be highly selective and incorporate both supplemental and alternative risk assessment benchmarks****.*
3. *Referral to the NAIC's SVO Initiatives (EX) Working Group: NAIC should evaluate whether to* ***expand the use of SVO and increase regulator reliance on the SVO for evaluating credit and other risks of securities****.*

**Recommendation:** The SVO recommends the following market data fields and related descriptions be added to all the annual statement instructions, through a referral to the Blanks (E) Working Group, for all bonds reported on Schedule D, Part 1 (those within scope of SSAP No. 26R – Bonds and SSAP No. 43R – Loan-Backed and Structured Securities). To allow sufficient time for insurers to update their systems, the SVO further recommends that the changes be implemented as electronic only fields effective beginning with the reporting year ending December 31, 2023.

- Market Yield – The Market Yield is the internal rate of return discount rate that makes the net present value (NPV) of all expected cash flows equal to zero in a discounted cash flow analysis. Therefore, Fair

[1] Evaluating the Risks Associated with NAIC Reliance on NRSRO Credit Ratings – Final Report of the RAWG to the Financial Conditions (E) Committee, April 28, 2010

Value, which is already reported, is the present value (PV) of all expected cash flows discounted at the Market Yield.

- Market Price – The Market Price per unit of Par Value, which is already reported, is reflected in the Fair Value as of the financial statement date. The Market Price, which excludes accrued interest, when multiplied by Par Value and divided by 100 will be equal to the Fair Value.
- Purchase Yield – The Purchase Yield is the internal rate of return discount rate that makes the net present value (NPV) of all expected cash flows equal to zero in a discounted cash flow analysis as of the Acquired Date. Therefore, Actual Cost is the present value (PV) of all expected cash flows discounted at the Purchase Yield as of the Acquired Date.
- Weighted Average Life – The Weighted Average Life is the average length of time that each dollar of unpaid principal remains outstanding. The time weightings used in weighted average life calculations are based on payments to the principal. The calculation is "weighted" because it considers when the payments to the principal are made—if, for example, nearly all of the principal payments are made in five years, WAL will be close to five years. Weighted average life does not consider payments to interest on the loan. This value is recalculated at each statement date for the remaining principal payments.
- Spread to Average Life UST - The spread is the difference between the interpolated U.S. Treasury bond yield that matches the reported debt security's Weighted Average Life. Spreads between interpolated U.S. Treasuries and other bond issuances are measured in basis points, with a 1% difference in yield equal to a spread of 100 basis points.
- Option Adjusted Spread - The option-adjusted spread (OAS) is the measurement of the spread of a fixed-income security rate and the risk-free rate of return (typically U.S. Treasury yield), which is then adjusted to take into account an embedded option and expressed in basis points. The spread is added to the fixed-income security price to make the risk-free bond price the same as the bond. The option-adjusted spread considers historical data such as the variability of interest rates and prepayment rates. These calculations are complex since they attempt to model future changes in interest rates, prepayment behavior of mortgage borrowers, and the probability of early redemption.
- Effective Duration - This is a duration calculation for bonds that have embedded options. This measure of duration takes into account the fact that expected cash flows will fluctuate as interest rates change and is, therefore, a measure of risk given the security's Fair Value. As a formula, Effective Duration = (P(1) - P(2)) / (2 x P(0) x Y), where P(0) = the bond's Market Price per $100 worth of par value, P(1) = the price of the bond if the yield were to decrease by Y percent, P(2) = the price of the bond if the yield were to increase by Y percent, and Y = the estimated change in yield used to calculate P(1) and P(2).
- Convexity - This is a measure of the curvature, or the degree of the curve, in the relationship between bond prices and bond yields. Convexity demonstrates how the duration of a bond changes as the interest rate changes.
- VISION ISSUE ID: The NAIC VISION system security ID reported in AVS+.

https://naiconline.sharepoint.com/teams/SVOVOSTaskForce/Shared Documents/Meetings/2022/2022-04 - Spring National Meeting/04 - Blanks Referral Analytical Risk Measures/2021-053.01 Blanks Market Data Disclosure v2.docx

NAIC NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

TO: Carrie Mears, Chair, Valuation of Securities (E) Task Force
Members of the Valuation of Securities (E) Task Force

FROM: Charles A. Therriault, Director, NAIC Securities Valuation Office (SVO)
Marc Perlman, Managing Investment Counsel, NAIC Securities Valuation Office (SVO)

CC: Eric Kolchinsky, Director, NAIC Structured Securities Group (SSG) and Capital Markets Bureau

RE: Possible Options for Additional Market Data Fields for Bond Investments

DATE: July 14, 2022

**Summary -** The SVO proposed adding additional market-data fields for bond investments to the annual statement instructions in its memo dated Feb. 25, 2022, titled "Additional Market Data Fields for Bond Investments" that was discussed at the 2022 Spring National Meeting. The recommendation was based, in part, on 2010 adopted recommendations of the Rating Agency (E) Working Group (RAWG) and the NAIC Investment Analysis Office's (IAO) staff's findings regarding the discrepancies between ratings, presented in its Nov. 29, 2021 memo, "Rating Issues and Proposed Changes to the Filing Exemption Process." In this memo the SVO further outlines the regulatory benefits and proposes two possible approaches.

The benefits of collecting additional market-data for each insurer bond investment are several:

- Assist in SVO identification of securities with credit rating provider (CRP) ratings which may be inconsistent with a security's actual overall risk.
- Greater transparency for regulators into the risks and characteristics of insurer investments.
- Incorporation of insurer investment portfolio analysis into the examination process.
- Availability of more Level 1 and 2 Inputs which will be included in the AVS+ pricing data for all securities compared to the mostly Level 3 Inputs for only some securities today.
- Allow state insurance regulators to assess the capabilities of an insurer's investment management or risk management processes by reviewing the quality and accuracy the market data fields.
- Provide NAIC staff with the capability to run cash flow simulations on insurer investments.

Regarding the first bullet, the SVO would use this market-data information to help identify securities with credit rating provider (CRP) ratings that may be inconsistent with the security's actual overall risk. The SVO and SSG have raised concerns over the years about a number of asset classes (e.g. residential

mortgage backed securities (RMBS), commercial mortgage backed securities (CMBS), public and private fund investments, principal protected securities (PPS) including CLO Combo Notes, regulatory transactions, residual interests, and now collateralized loan obligations (CLO), and structure equity and funds) and specific securities in other asset classes where a rating agency rating often does not adequately reflect the investment risk for NAIC purposes. The SVO needs this analytical information so that it can identify and take potential action on investment risk assessment inaccuracies. Without this data and potentially other information in the future, coupled with some level of discretion over NAIC Designations derived from ratings, the SVO and regulators will remain in the dark about these risks. Additionally, the incentive for significant risk-based capital arbitrage utilizing CRP ratings will likely continue to increase and rating agencies will effectively remain a de-facto "super regulator" in that any investment they assign a rating to is automatically accepted by the NAIC without any regulatory discussion, analysis, oversight or consideration as to how the rating agency's decisions align to the NAIC's statutory framework.

Inconsistent and potentially inaccurate assessments of investment risk is a critical issue not only for the Valuation of Securities (E) Task Force but for other state insurance regulatory groups that are interested in identifying and analyzing investment risks, whether it be at the individual security, asset class, legal entity or industry level. The following are just a few groups that have active work streams involving investment risk: Life Actuarial (A) Task Force, Capital Adequacy (E) Task Force and its Working Groups, Statutory Accounting Principles (E) Working Group, Financial Stability (E) Task Force, Macroprudential (E) Working Group and Financial Analysis (E) Working Group. The proposed market data fields will benefit each of these groups in their work assessing insurer investments and portfolio risks.

The requested market data fields other than purchase yield, which should be available from any investment accounting system, are all at the security issue level (i.e. CUSIP). Any insurer system that can receive security issue level data such as a market prices, credit ratings, bond factors, cashflows, or NAIC Designations should be able to accommodate these proposed security issue-level data fields. The SVO acknowledges this change will require time for insurer system providers to accommodate these new data fields into their data structures and Schedule D reporting applications. However, these data fields are very common in the management of a bond portfolio, and it would be a significant enterprise risk deficiency if an insurer's investment managers did not have them.

Some alternate measures of risk (e.g. Sharpe Ratio and Sortino Ratio) were mentioned during the Task Force discussion. These metrics, however, would require insurers to calculate the total return and the standard deviation of those returns for each security they own in order to produce and report these metrics which would be significantly more costly and more appropriate for assessing relative value and less applicable for assessing investment risk.

**Alternatives –** The SVO was asked to consider industry's recommendation that the NAIC produce these fields. Below are our thoughts on each alternative.

- **NAIC Produced Analytics** – The SVO can take on the responsibility for producing the analytical data elements requested in this proposal. To do so it would require enhancements to the SVO's existing systems (VISION, AVS+ and STS), and vendor pricing data, investments in new systems to provide the modeling, more staff for the incremental and on-going support of these systems and processes, new data feeds to support the modeling software, and new data bases and reporting capabilities to provide the information to regulators. Enhancements would also

need to include the ability for insurers to provide electronically to the SVO the full security structure of any security that the modeling software does not know about. We strongly believe that the benefits to be gained by state regulators, the SVO and other NAIC groups with interests in investment risk of bringing this modelling capability in-house greatly outweigh, in the long run, the initial costs and effort to make these capabilities operational.

- **Pros:**
  - Market analytical information would be independently and consistently produced.
  - The SVO's pricing data would need to include more Level 1 and 2 Inputs for all securities versus primarily Level 3 Inputs for only some securities today.
  - Regulators would eventually be able to ask NAIC staff to model the risks or cash flows of any bond security or insurer bond portfolio, including, stress testing those securities and portfolios.
  - Regulators would have significantly greater transparency into the risks and characteristics of insurer investments.
  - Analytical analysis of insurer investment portfolios could be incorporated into the examination process.
  - The overall cost to insurers through any increased fee would likely be much less than each insurer building out its own capability to provide the data.
- **Cons:**
  - The NAIC would need to make significant enhancements to VISION, AVS+, and STS, and develop new reporting data bases.
  - The NAIC will need to license a security analytic modelling system and provide it with the data it requires, some of which may require new data licenses. This includes full access to vendor applications like Bloomberg or Aladdin.
  - The NAIC will incur additional fees for higher level of security pricing data. The NAIC will also need additional staff to develop and support the technology enhancements and to support the on-going modeling of securities and portfolios.
  - It may take longer for the NAIC to build this capability.
  - Insurers would still need to report some of this information on their Schedule D filings from data published through AVS+.
  - Insurers would need to provide the SVO with full security structure modeling and supporting data (e.g. collateral, payments, actions) for any security the analytic modelling system does not have within its data base.

- **Insurer Produced Analytics** – Insurer investment managers should already have the market data fields requested in this proposal. Insurers would need to get this information into their systems that produce their Schedule D filings. This option would require more up-front work on the part of the insurers and less by the NAIC. The uses of the data, however, whether by regulators, the SVO or other interested

NAIC groups, could be significantly more limited than in the first option, because of the inconsistency in data between insurers.

- **Pros:**
  - Insurers already have this information as part of their investment management or risk management processes.
  - State insurance regulators could assess the capabilities of an insurer's investment management or risk management processes by reviewing the quality and accuracy the market data fields.
  - The timeframe to implement would likely be shorter than the SVO having to build out this capability.
- **Cons:**
  - Insurer security pricing is very inconsistent today which will lead to a high degree of variability in these analytical values.
  - The modeling software and assumptions used by insurers to produce these analytical value can vary significantly which will also lead to a high degree of variability in the values.
  - Insurers and their system providers will need to develop new interfaces to ingest this data and produce it in their Schedule D filing. That time frame could vary significantly by vendor and insurer.
  - State insurance regulators would not be able to request the modeling of any investment security or portfolio.
  - Insurers would directly bear the expense of these changes which will likely be greater than it would be it the NAIC produced this information.

**Next Steps –** The SVO continues to strongly believe that these market data fields are an important first step in finding alternative ways to measure insurers investment risk and reducing the NAIC reliance rating agency ratings. As noted by the RAWG and reflected in the IAO's memo, there persists a situation where "*… ratings are neither consistent nor uniform for individual securities, nor across different types and classes of securities…*" yet the role of the SVO has not been expanded to include using these alternatives in "*… evaluating credit and other risks of securities*." The objective of this request is to begin addressing these investment risk issues but this may not be the only information needed.

Both alternatives will involve a commitment of resources either by the NAIC or industry. The major question before the Task Force is whether it has a preferred source for these market data fields: the NAIC's SVO or insurer reporting? The SVO believes that the first option would provide the most standardization in data and utility to regulators, the SVO and other interested NAIC groups and would be worth the slightly longer time and cost needed to develop the capabilities.

If, as the SVO recommends, the Task Force prefers the NAIC's SVO as the source of this analysis, then the next step would be a referral to the Financial Condition (E) Committee to request their sponsorship for this initiative and, if provided, begin a fiscal request. If Financial Condition (E) Committee declines to sponsor the initiative or if insurer reporting is the preferred source, we would recommend reverting to insurer reporting and directing the SVO staff to prepare the Blanks referral.

NAIC NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

TO: Carrie Mears, Chair, Valuation of Securities (E) Task Force
Members of the Valuation of Securities (E) Task Force

FROM: Eric Kolchinsky, Director, NAIC Structured Securities Group (SSG) and Capital Markets Bureau
Charles A. Therriault, Director, NAIC Securities Valuation Office (SVO)
Marc Perlman, Managing Investment Counsel, NAIC Securities Valuation Office (SVO)

RE: Amendment to the Purposes and Procedures Manual of the NAIC Investment Analysis Office (the "P&P Manual") to Include Collateralized Loan Obligations (CLO) as a Financially Model Security in Part Four

DATE: September 16, 2022 (**Updated: December 20, 2022**)

**Summary** – A collateralized loan obligation (CLO) is type of structured security backed by a pool of debt, typically corporate loans with low credit ratings. An insurer that purchases every tranche of a CLO holds the exact same investment risk as if it had directly purchased the entire pool of loans backing the CLO. The aggregate risk-based capital (RBC) factor for owning all of the CLO tranches should be the same as that required for owning all of the underlying loan collateral. If it is less, it means there is risk-based capital (RBC) arbitrage. As noted in the Investment Analysis Office's (IAO) memo of May 25, 2022, "Risk Assessment of Structured Securities – CLOs", it is currently possible to materially (and artificially) reduce C1 capital requirements just by securitizing a pool of assets.

**Recommendation** – The Investment Analysis Office recommends the Task Force assign the Structured Securities Group (SSG) the responsibility of financially modeling CLO investments. SSG can model CLO investments and evaluate all tranche level losses across all debt and equity tranches under a series of calibrated and weighted collateral stress scenarios to assign NAIC Designations that create equivalency between securitization and direct holdings, thereby eliminating RBC arbitrage.

The Task Force sent a referral to the Capital Adequacy (E) Task Force (CATF) and its Risk-Based Capital Investment Risk and Evaluation (E) Working Group (RBCIREWG) requesting those groups consider adding two new RBC factors. These recommended new RBC factors would account for the tail risk in any structured finance tranche. Staff also recommends adding NAIC Designation Categories (e.g. 6.A, 6.B and 6.C) with possible interim RBC factors of 30%, 75% and 100%, respectively, until those groups can further study structured securities. Staff request approval to draft a Blanks proposal for the new NAIC Designation Categories.

**Proposed Amendment -** The proposed text changes to P&P Manual are shown below with additions in red underline, deletions in ~~red strikethrough~~ as it would appear in the 2022 P&P Manual format. Changes made on December 20, 2022 are highlighted in yellow.

Attachment
Financial Condition (E) Committee
3/24/23


To: Superintendent Elizabeth Kelleher Dwyer (RI), Chair, Financial Condition (E) Committee

From: Jackie Obusek (NC), Chair, Mortgage Guaranty Insurance (E) Working Group

Date: March 1, 2023

Re: Request for Extension – Mortgage Guaranty Insurance Model Act (#630)

The Mortgage Guaranty Insurance (E) Working Group is in the process of fulfilling its charge to update the *Mortgage Guaranty Insurance Model Act* (Model #630). The Working Group anticipated completion of its Charge by the 2023 Spring National Meeting. As Chair, I would like to update that request to the Financial Condition (E) Committee in accordance with NAIC procedures.

The Working Group exposed for public comment the Draft Mortgage Guaranty Insurance Model Act (#630) during its October 6, 2022 interim meeting. The exposure ended on November 7 and several comments were received and discussed during the 2022 Fall National Meeting. During January and February 2023, the drafting group discussed and addressed each comment. As a result, several revisions were made to draft Model #630. The drafting group exposed the Model for a secondary public comment period just prior to the 2023 Spring National Meeting. It is anticipated that following discussion of additional comments received as a result of the exposure, the Working Group will be in a better position to vote to adopt draft Model #630 following review and discussion on any additional comments.

At this time, we believe we can complete this work by the 2023 Fall National Meeting. The request for additional time is to allow the necessary time to address comments and ensure that a comprehensive regulatory framework is in place to effectively regulate these complex insurance entities. We are aware that we have been unable to complete our work within the one-year time period expected under the NAIC model law process and request an extension until the 2023 Fall National Meeting in order to finalize a product that can be adopted by the domestic states of the mortgage insurers, as well as any other state also wishing to adopt the same.