

PROJECT HISTORY - 2008

MODEL REGULATION TO DEFINE STANDARDS AND COMMISSIONER'S AUTHORITY FOR COMPANIES DEEMED TO BE IN HAZARDOUS FINANCIAL CONDITION (#385)

1. Project Description

In June 2004, the Examination Oversight (E) Task Force received a referral from the Financial Condition (E) Committee to review Model Law #385: Model Regulation to Define Standards and Commissioner's Authority for Companies Deemed to be in Hazardous Financial Condition. The Task Force was asked to work with the Receivership and Insolvency (E) Task Force in reviewing the model as it represented an accreditation standard that had not been revised since its adoption in 1985. Based on the initial review performed in 2005, the Task Force recommended that the model be revised and updated. A charge was adopted for 2006 instructing the Task Force to produce revisions to the model in coordination with the Receivership and Insolvency (E) Task Force. Preliminary work was completed on the charge in 2006 but in 2007, in accordance with the NAIC's adoption of a revised Model Law Development Framework, the project to revise the model was put on hold until the approval of an Appendix A by the Executive Committee. The Appendix A was approved by the Executive Committee at the 2007 Winter National Meeting and the task forces resumed their work to revise the model at this time.

2. Group Responsible for Drafting the Regulation

The project to review and produce revisions to Model #385 was given to the Examination Oversight (E) Task Force and the Receivership and Insolvency (E) Task Force. The two task forces formed a joint subgroup, entitled the Hazardous Financial Condition Model Revisions Subgroup, to draft revisions to the model regulation. The following states participated in the subgroup:

Iowa, Chair	Pennsylvania
Arkansas	Tennessee
Florida	Utah
New York	Virginia
Ohio	

3. Charge Authorizing the Project

The Examination Oversight (E) Task Force and the Receivership and Insolvency (E) Task Force have been working on this project in accordance with related charges since 2004. In 2007, in accordance with the revised Model Law Development Framework, the task forces prepared an Appendix A-Request for Model Law Development, for the approval of the Financial Condition (E) Committee and the Executive (EX) Committee. The Appendix A received final approval of the Executive Committee at the 2007 NAIC Winter National Meeting and the Examination Oversight (E) Task Force was asked to proceed with the following charge:

Produce in coordination with the Receivership and Insolvency Task Force, revisions to Model 385 – Model Regulation to Define Standards and Commissioner's Authority for Companies Deemed to be in Hazardous Financial Condition.

4. General Description of the Drafting Process and Due Process

In November 2004, the Examination Oversight (E) Task Force conducted a survey of state insurance departments to determine state satisfaction with the current version of Model #385. As a result of the survey, a number of suggested revisions were proposed by various state insurance departments. When the approval to proceed with the project was received in December 2007, the Hazardous Financial Condition Subgroup utilized the suggested revisions from the survey results as a starting point to draft revisions to the Model. These suggested revisions were discussed on a call of the Subgroup on February 20, 2008. During this call, draft revisions to the model were finalized and the Subgroup voted to expose the proposed revisions for a 45-day comment period. The exposure period was subsequently extended to 60-days at the request of the Examination Oversight (E) Task Force. After the exposure period concluded, the Subgroup held a conference call on May 22, 2008, to discuss the three comment letters received during the exposure period. During this conference call, the group discussed the comments received and agreed to add explanatory language to amend several of the proposed revisions. The proposed revisions to Model #385 were then adopted as amended. The revisions to the model were then unanimously adopted by both the Examination Oversight and Receivership & Insolvency (E) Task Forces and the Financial Condition (E) Committee at their June 2008 meetings.

5. Discussion of Key Issues

Section 3. Standards

The following additions were made to the standards that may be considered by the commissioner to determine whether the continued operation of any insurer transacting an insurance business in this state might be deemed to be hazardous to the policyholders, creditors or the general public:

- Findings from audit reports and actuarial opinions, reports or summaries;
- Whether the insurer has made adequate provision, according to presently accepted actuarial standards of practice, for the anticipated cash flows required by the contractual obligations and related expenses of the company, when considered in light of the assets held by the company with respect to such reserves and related actuarial items including, but not limited to, the investment earnings on such assets, and the considerations anticipated to be received and retained under such policies and contracts;
- Whether the insurer's operating loss in the last twelve-month period or any shorter period of time, excluding net capital gains, is greater than twenty percent (20%) of the insurer's remaining surplus as regards policyholders in excess of the minimum required;
- Whether the insurer has failed to meet financial and holding company filing requirements in the absence of a reason satisfactory to the commissioner;
- Whether management has established reserves that do not comply with minimum standards established by state insurance laws, regulations, statutory accounting standards, sound actuarial principles and standards of practice;
- Whether management persistently engages in material under reserving that results in adverse development;
- Whether transactions among affiliates, subsidiaries or controlling persons for which the insurer receives assets or capital gains, or both, do not provide sufficient value, liquidity or diversity to assure the insurer's ability to meet its outstanding obligations as they mature;
- Any other finding determined by the commissioner to be hazardous to the policyholders, creditors or general public.

These standards have been added to give the commissioner additional items to consider in determining whether an insurer is in a hazardous financial condition.

Section 4. Commissioner's Authority

The following additions were made to the commissioner's authority to issue an order requiring the insurer to:

- Correct corporate governance practice deficiencies, and adopt and utilize governance practices acceptable to the commissioner.
- Provide a business plan to the commissioner in order to continue to transact business in the state.
- Notwithstanding any other provision of law limiting the frequency or amount of premium rate adjustments, adjust rates for any non-life insurance product written by the insurer that the commissioner considers necessary to improve the financial condition of the insurer.

These additional requirements have been included in the revised model to allow the commissioner additional authority in preventing the situation at insurers in hazardous financial condition from worsening.

6. Any Other Important Information

No other items identified at this time.

Exhibit A: Illustrative Timeline on Due Process and Drafting Process– Model 385

<i>June 2004</i>	(Summer National Meeting) Examination Oversight Task Force receives the referral of the Financial Condition (E) Committee to review Model #385 in conjunction with the Receivership and Insolvency (E) Task Force.
<i>September 2004</i>	(Fall National Meeting) Subgroup of Examination Oversight Task Force formed to begin review of the model.
<i>October 2004</i>	Subgroup holds a conference call to review the model and develops a survey to be conducted among all states regarding the current effectiveness of the model and whether revisions may be necessary.
<i>November 2004</i>	Survey of states conducted.
<i>December 2004</i>	(Winter National Meeting) Survey responses are briefly discussed. Receivership and Insolvency (E) Task Force indicates that it is actively working on revisions to Model #555 (Insurer Receivership Model Act) and has limited availability to participate in the review of Model #385 at this time.
<i>March 2005</i>	Due to the involvement of the Receivership and Insolvency (E) Task Force in developing revisions to Model #555, the project to review Model #385 is postponed.
<i>December 2005</i>	Financial Condition (E) Committee adopts a charge for the task forces to move forward by drafting revisions to update the model.
<i>2006</i>	Limited work performed on the project due to the Receivership and Insolvency Task Force's work on Model #555.
<i>March 2007</i>	(Spring National Meeting) A joint subgroup of the Examination Oversight (E) Task Force and the Receivership and Insolvency (E) Task Force titled the Hazardous Financial Condition Model Revisions Subgroup is formed to work on the project.
<i>May 2007</i>	The NAIC adopts a new Model Law Development Framework requiring an additional approval process before work to revise the model is begun.
<i>June-August 2007</i>	The Hazardous Financial Condition Model Revisions Subgroup surveys Chief Financial Regulators regarding their support for formally revising Model #385 to comply with the Model Law Development Framework. The results of the survey indicate sufficient support for the project and an Appendix A is created to request approval to proceed with formally revising the model.
<i>September 2007</i>	(Fall National Meeting) The Appendix A to proceed with formally revising Model #385 is approved by both the Examination Oversight and the Receivership and Insolvency (E) Task Forces and the Financial Condition (E) Committee.
<i>December 2007</i>	(Winter National Meeting) The Appendix A is approved by the Executive Committee.
<i>February 20, 2008</i>	In a conference call of the Hazardous Financial Condition Model Revisions Subgroup, proposed revisions to the model are discussed and voted to be exposed for public comment.
<i>May 22, 2008</i>	A conference call of the Hazardous Financial Condition Model Revisions Subgroup is held to discuss comments received during the exposure period. An amended version of the revisions to the model is adopted for presentation to the Examination Oversight and the Receivership and Insolvency (E) Task Forces.
<i>June 1, 2008</i>	The revised model is adopted by both the Examination Oversight and the Receivership & Insolvency (E) Task Forces.
<i>June 2, 2008</i>	The revised model is adopted by the Financial Condition (E) Committee.