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IN THIS ISSUE

CRE READING PROGRAM INSTRUCTIONS

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You can earn **2 CRE credits** for each of the 4 quarterly issues by taking a simple, online test after reading each issue. There will be a total of 9-20 questions depending on the number of articles in the issue. The passing grade is 66%. To take the test, read all of the articles in the issue. Go to the Members section of the SOFE website to locate the online test. This is a password-protected area of the website, and you will need your username and password to access it. If you experience any difficulty logging into the Members section, please contact **sofe@sofe.org**.

NOTE: Each new test will be available online as soon as possible within a week of the publication release. The Reading Program online tests are free. Scoring is immediate upon submission of the online test. Retain a copy of your online test score in the event you are audited or you need the documentation for any other organization's CE requirements. Each test will remain active for one year or until there is a fifth test ready to be made available. In other words, there will only be tests available for credit for four quarters at any given time.

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CRE Reading Program Questions

All quizzes MUST be taken online.

*Questions will be **available online July 15, 2019.***

Data Analytics in the Insurance Industry

True or False Questions — Submit Answers Online

1. Businesses, including insurance companies, are using data analytics to diagnose outcomes to drive business decisions.
   a. True
   b. False

2. The most appropriate place to begin the questioning is at the top of the organizational chart, with the Chief Financial Officer.
   a. True
   b. False

3. Models must be built with clean data in order to produce meaningful conclusions.
   a. True
   b. False

4. Actuaries have just begun using analytics in order to appraise and control risks through segmentation of various populations in order to analyze the costs of risks and develop pricing variables.
   a. True
   b. False

5. Examiners need to realize that it is not imperative to equally understand the processes and procedures involved in all areas using data analytics.
   a. True
   b. False

Adding Customer Value Through InsurTech

Multiple Choice and True or False Questions — Submit Answers Online

6. Smart devices and the ability to connect to information have become essential for which generations to function in today's world?

   a. Millennials (those born between 1981-1996.
   b. Gen Z (those born between 1997-2015.
   c. All generations
   d. None of above

7. The smartphone applications or telematic devices are able to use machine-to-machine (M2M) communication to capture vehicle values such as:

   a. Miles driven
   b. Driving time of day
   c. Sudden acceleration or braking
   d. All of the above

8. Technologies are being introduced across all insurance categories, but funding and innovation during the first quarter of 2019 is currently being led by:

   a. The automotive market
   b. The healthcare market
   c. A & B
   d. None of the above

9. Smartphone platform apps and social media have become an integral component of how insurers interact with consumers over the last several years.
   a. True
   b. False

10. What opened a significant opportunity for companies to provide innovative technology to meet the changing landscape of the insurance industry?
    a. Customer expectations of simplicity
    b. Customer expectations of transparency
    c. None of the above
    d. A & B

Reliance on Third-Party Control Documentation: A Question of Judgement

True or False Questions — Submit Answers Online

11. SOC stands for Service Operating Control.
    a. True
    b. False

12. There are three thresholds that must be assessed prior to placing reliance on Third-Party Controls.
    a. True
    b. False

13. A SOC Type II report assess internal controls over a period of time.
    a. True
    b. False

14. One of the thresholds that must be assessed is if the information is professionally prepared and completed.
    a. True
    b. False

15. Data center controls of a company are not considered ITGC's for the examination.
    a. True
    b. False

NAIC Spring Meeting Notes

True or False Questions — Submit Answers Online

16. At the meeting of the Innovation and Technology Task Force, the chair indicated that states would now be required to adopt the Insurance Data Security Model Law without amendment.
    a. True
    b. False

17. At the meeting of the Statutory Accounting Principles Working Group, the Group exposed for comment at statement that no changes were necessary to SSAP 101 as a result of the recent Federal tax law changes.
    a. True
    b. False

18. The Group Capital Calculation Working Group adopted the final template for the new group capital calculation.
    a. True
    b. False

19. The newly-formed Restructuring mechanisms Working Group formed a Subgroup which has been charged with a number of tasks, including defining "run-off company".
    a. True
    b. False

20. The Casualty Actuarial and Statistical Task Force continued its work on revising the definition of "Qualified Actuary" and revising the instructions related to the Statement of Actuarial Opinion. It is unknown at this time whether or not the revised instructions will apply to 2019 actuarial opinions.
    a. True
    b. False

Data Analytics in the Insurance Industry

By Kevin Rupp
CFE, CGMA, ChFC, CISA, CPA (Inactive)
Ohio Department of Insurance

Introduction and Qualification

I am not a data analyst and this is not intended as a technical article. Rather, I am an insurance examiner who has some hands on experience using data analytics and who has seen data analytics functions at insurance companies grow exponentially over the years, especially in the last five to ten years. My goals with this article are to rationally explain my view on the data analytics explosion in business in general, explain how to deal with data analytics functions of insurance companies on examinations and to give my view on where insurance companies are at and are headed with data analytics.

Overview of the Process

Data analytics is a buzz term used today probably as much as any other buzz term in business. What does the term mean? In its basic form, it is the process of collecting data and using it for some purpose. Roots of data analytics lie in the study and application of statistics, a discipline that has been around for centuries. The invention and proliferation of the computer and subsequent advances in technology have exponentially enhanced the availability of data and the capabilities of data analytics.

So what is new aside from the quantity of data available? For one, more and more businesses, including insurance companies, are using data analytics to predict outcomes and drive business decisions. Thus, efforts of data analytics are being focused more, percentage-wise, towards predictive (what will happen) and prescriptive (what to do) analyses and less towards the traditional descriptive (what happened) and diagnostic (why did it happen) analyses. The next general discussion is focused on the former two types of data analyses in order to explain the processes and procedures currently in place or being developed in order to drive business decisions.

Before raw data can be used for actionable items in business decisions, several intermediate steps must take place. Pared down to the basics, the intermediate steps are: 1.) Identify the objective(s), 2.) Collect the data, 3.) Clean the data, 4.) Model the data, and 5.) Repeat. Let's look at each one of these steps individually.

Identify the Objective(s)

In reality, this is not an intermediate step. This should be the beginning step before any raw data is identified for analyses. The business unit(s) should first identify the objective(s) of the exercise. In addition, key performance indicators, often referred to as KPIs, should be identified as early in the process as possible. These KPIs must be measurable and consistent with the objectives of the analysis in order to maintain direction over the entire process.

Collect the Data

The key to data collection is to get as much data from as many different sources as possible. The variety of sources should include internal and external data equally to the extent possible. Generally, the more data that is gathered provides for more correlations between data sets, which leads to better, more sophisticated modeling.

Clean the Data

Data cleaning may be the most important step in the process. During this step, issues such as missing or garbage data are identified. These issues must be addressed with actions such as elimination or correction of data sets. By having data collected from diverse sources, the analysis team may be able to identify biases in and among the data sets and make appropriate adjustments.

Model the Data

We've all heard the phrase "garbage in, garbage out." Models must be built with clean data in order to produce meaningful conclusions. The conclusions are used to make recommendations for business decisions and results should be measurable using the KPIs identified during earlier steps. It is important that interpretations of the results be developed with a statistical background in conjunction with knowledge of the business. Too much of a slant towards the statistical results may result in business recommendations that do not make sense to the unique properties of the business, while too much of a slant from the standpoint of the business aspect may result in business recommendations and decisions that are not supportable by the data.

Repeat

The process must be repeatable in order to provide scale to the company. Once the process is completed, the company should look to automate data collection, data cleaning and data analysis as much and as soon as possible while data teams work with the business unit(s) to identify further refinements to the process in order to produce results that are even more meaningful. Ideally, after enough times through the process, the decision makers at the company will have continuous dashboards containing results that are measurable and actionable and the data analysis team will move on to a different project.

Where We Are Seeing Data Analytics

So where do we see data analytics being used in the insurance industry? Some of you may have seen data analytics used elsewhere besides the areas that I am about to identify, but most of my exposure to data analytics use has been in four areas of insurers being examined, which are:

- Claims and reserving
- Pricing and underwriting
- Marketing and customer focus
- Fraud, waste and abuse

Claims and Reserving

Actuaries and reserving are cornerstones of the insurance industry. Since the inception of insurance commerce, actuaries have been estimating present values of claims and contingencies. Likewise, claims adjusters, most times armed with actuarial data, have been estimating the amounts to be ultimately paid on existing claims with different amounts of information available during different points in the lifecycles of the claims. Now, rapid advances in the availability of data has resulted in some larger insurers forming teams of varying disciplines whose charges are to predict and drive reserving and claims handling decisions based on interpretations of the analyses of large data sets. Likewise, small and mid-size insurers may not have the teams in place, but they may have differing functions within their operations that are coordinating to produce similar results on a smaller scale. Results include better predictability of the behaviors of claims and better identification of clean or troublesome claims based on data properties and relationships in data. These results are allowing insurance companies and agents to complete assignments to claims and to qualitatively and quantitatively assess claims at an earlier point in the claim lifecycle, thus diverting resources away from traditional exercises of dealing with what has already happened.

Pricing and Underwriting

As is true of actuaries and reserving, the same is true of actuaries and pricing. Whereas claims adjusters have historically been armed with actuarial data in the claims estimation process, the same holds true of underwriters in the underwriting process. Pricing and underwriting are huge components of insurance, maybe its most important components. Like claims and reserving, actuaries have long been using analytics in order to appraise and control risks through segmentation of various populations in order to analyze the costs of risks and develop pricing variables. Now, advances in data are permitting companies to streamline the application process and shorten the placement of business. Where permitted by regulation, data properties and relationships in data are allowing companies to develop additional ratings and rates that appear to be more sophisticated than traditional methods. In addition, the diversion of resources away from the traditional exercises of dealing with what has already happened can now be diverted towards growing the business with existing and prospective customers.

Marketing and Customer Focus

There is no commerce without a customer. That fact is first and foremost in the mind of this regulator. In some cases, a policyholder is obligated to obtain insurance according to regulations. Other times, insurance purchases are optional to a prospective policyholder. So what developments have provided benefits in the areas of marketing and customer focus?

Insurance companies are using data analytics to design products and develop markets. Every day, when humans make decisions, their decisions are being tracked from their smartphones, laptops and other electronic devices in order to build a profile of the individual and to assemble that data amongst data of other individuals. The result in the insurance industry is that companies are better able to predict potential customer behaviors as well as existing customer behaviors. That results in products that are better designed to fit current demands and possibly demands of the future customer.

Fraud, Waste and Abuse

Insurance companies are always looking for ways to curb insurance fraud, waste and abuse. Such behavior has manifested itself into positions and departments at insurance companies that are dedicated to attempts to detect such behavior and to deal with its aftermath. Now, insurance companies are using actionable data as a result of analytics that assists in identifying who, what and where occurrences of deceptive, wasteful and abusive practices likely are occurring or may occur. As such, data analytics have allowed companies to use relational data in order to be better and quicker at identifying insurance fraud, waste and abuse.

What to do on an Examination

The best place to start on an examination is to ask appropriate questions during executive interviews. The proper executive(s) to ask such questions depends on the company and how the data analytics function is aligned. In all likelihood, the function will not be centralized and will be spread amongst different areas of operations. Many times, these areas in the operations are not readily identifiable by their locations or by titles on the personnel organization chart. Also, in many cases, employees involved in the data analytics function perform other functions aside from analytics. For these reasons, the most appropriate place to begin the questioning is at the top of the organizational chart, with the Chief Executive Officer. Relevant basic questions to ask include the following:

- Where are data analytics used in your company?
- From where is your data derived?
- Who identifies the properties of and correlations in the data collected?
- Who is responsible for the output?
- What is the output?
- How is the output used?

Keep in mind that, depending on the response to each question, the remaining questions may be best deferred to a different executive. Also, keep in mind that there will likely be multiple answers to each question depending on the number of different areas in which data analytics are used. Finally, examiners need to realize that it is not imperative to equally understand the processes and procedures involved in all areas using data analytics. For instance, understanding processes and procedures involved in pricing and underwriting analytics may be more important to the examination effort than understanding the processes and procedures involved in fraud, waste and abuse, as understanding the former will allow examiners to identify mitigating controls and design control tests that are more significant to the examination's inherent risks.

Where I Am Not Seeing Data Analytics

Surprisingly or not, I have not seen an abundance of data analytics being used in the investment function at insurance companies. Companies appear to be using tried and true investment methodologies that have been developed internally over the years. Statisticians could provide evidence to insurance company management that investment decisions based on data contain less bias than decisions based on human judgment. However, investment codes of the various states providing regulation to these companies undoubtably stifle the benefit that can be derived by insurance companies that may use innovative investment decision techniques based on analytics.

What to Expect

What I expect is more of the same. Data is plentiful and becoming more so every day. Data storage is relatively inexpensive. Barring any drastic regulatory intervention, insurance companies will continue to amass and assemble data in order to obtain a competitive advantage. Companies not on the leading edge of the movement and companies that do not identify analytics as a means for competitive advantage may become obligated to put at least a basic data analytics function in place so as to pacify the demands of brokers, agents and policyholders that desire the latest innovations. I see data analytics as a major disruptor in the industry, but I also see an industry full of insurance companies, most of which are appropriately identifying their risks and mitigating those risks to the extent that is desired and prudent.

About the Author

Kevin J. Rupp, CFE, CGMA, ChFC, CISA, CPA (Inactive) Kevin has over 27 years of experience as an Insurance Examiner for the State of Ohio. On behalf of his current employer, he has led multiple efforts to gain and maintain accreditation status according to NAIC standards. He began to research and study data analytics approximately 2-3 years ago as an area he found intriguing for possible effects to the insurance industry. His study is ongoing.

Adding Customer Value Through InsurTech

By Terry Ryals, CISA, CDFE
The INS Companies

What do smartphones and insurance have in common? At first glance, not very much.

The same could have been said for smartphones and payment systems only a few years ago. But today smartphones and social media payment systems like Venmo, Facebook Pay, WhatsApp and several others have become a common way to exchange payment for goods and services. Venmo and countless other companies have recently disrupted the long-established traditional credit card form of payment in a similar way that Bank of America did with the BankAmericard in 1958 (the BankAmericard later became better known as VISA). These newer companies, which are disrupting the financial industry with innovative technology, have been dubbed "FinTech", short for financial technology companies.

The same type of revolution is going on within the insurance industry. Insurance technology companies better known as "InsurTech" companies are revolutionizing the industry. Although the term InsurTech came into existence just over a decade ago, the industry has seen explosive growth in recent years. How much? In 2013, it is estimated that $270 million was provided in funding compared to approximately $4 billion in 2018. Through March of 2019, the industry has already funded almost $2 billion[1].

Let's go back to our original question "What do smartphones and insurance have in common?" For starters, smartphone platform apps and social media have become an integral component of how insurers interact with consumers over the last several years. In 2015, Millennials (those born between 1981-1996) became the largest generation in today's workforce according to Forbes magazine[2]. With Millennials being the first generation to experience life always connected and Gen Z (those born between 1997-2015) starting to enter the workforce, different outlooks and service expectations have emerged across a number of industries. Millennials are well known for being tech savvy and often tethered to a smart device. However, smart devices and the ability to connect to information have become essential for all generations to function in today's world.

A publication by PricewaterhouseCoopers written in 2012 titled "Insurance 2020: Turning Change into Opportunity"[3] offered the following:

"Customer expectations of simplicity and transparency will foster innovations in product/service design and delivery. Leading insurers will get better at targeting customers and customizing product and service attributes to meet their specific needs, amassing greater customer surplus."

"People exchange more personal information and start building networks of trusted friends, family and acquaintances, shifting the balance of trust from insurance agents and advisers to online communities. Online social networks wielding substantial purchasing power become new group insurance channels, benefiting from information-driven online intermediaries. Eventually, online social networks become pooling mechanisms for self-insurance, changing the role of insurers at a primary level from product manufacturers to administration service providers."

Customer expectations of simplicity and transparency have opened a significant opportunity for companies to provide innovative technology to meet the changing landscape of the insurance industry. The changing needs, trends and innovative technologies have even fostered the formation of new insurers in an industry which has historically had significant barriers of entry. In short, the fabric of the insurance industry is being rewoven to include new business models and changes to the core components of insurance, including policy creation, distribution, underwriting and administration.

Technologies are being introduced across all insurance categories, but funding and innovation during the first quarter of 2019 is currently being led by the automotive and healthcare market[4].

Automotive

The auto insurance market was one of the first to capitalize on innovative technology that challenged the current auto insurance pricing model and allowed consumers to have more control over their rates. Progressive Insurance introduced "Snapshot" in 2008, a telematics device that captures driving patterns, and they don't need to look in the rear-view mirror to see their competition. In fact, most insurers have begun using similar telematics devices that plugs into the On-Board Diagnostic System (OBD-II) port on cars manufactured since 1996. The continued reliance on smartphones by consumers has seen this evolve into smartphone applications. The smartphone applications or telematic devices are able to use machine-to-machine (M2M) communication to capture vehicle values such as miles driven and more detailed behaviors like time of day, sudden acceleration or braking which can be used to better determine a user's risk. These devices allow for a more granular pricing of auto insurance based on the perceived risk. This has generated a large market for Usage Based Insurance (UBI) also known as pay as you drive (PAYD) and mile-based auto insurance.

As a result, in 2015, Root Insurance, an innovative technology driven auto insurance company was formed. Root is using technology to simplify the user experience and deliver low cost insurance to safe drivers. There is no agent to contact for quotes; one must simply download the application on their smartphone, and accounts can be setup using Facebook or email. The user enables location, motion and notifications on their phone, snaps a picture of their driver's license and provides applicable contact information. In turn, one starts a two- or three-week test drive period using the application which monitors their driving. Once enough data is collected, the user is notified if they qualify as a safe driver and of their rate.

Understanding the frustrations of the claims process, Root has made the unfortunate event of an accident as painless as possible. The entire process is initiated through the application and includes a convenient way to snap pictures for the claim. In the event one has rental coverage and needs a rental car, Root can even provide Lyft credits versus a traditional rental car option.

Healthcare

One of the largest InsurTech companies to date, Oscar Health, was founded in 2012 and started offering policies in New York City in late 2013. The company came to fruition following the passing of the Affordable Care Act and a frustrating billing experience by one of the co-founders. Oscar Health, co-found by Joshua Kushner, 29, Kevin Nazemi (no longer with the company), 33 and Mario Schlosser, 34, has sought to revolutionize the healthcare industry through the innovative use of technology and data to simplify the overall customer experience. The company has a current valuation of around $3.2 billion and has received funding from a number of investors including PayPal co-founder Peter Theil, Alphabet's Capital G (formerly Google Capital) and Verily Life Sciences, the healthcare subsidiary of Google's parent company, Alphabet[5].

Oscar Health makes it easy for members to obtain access to care through an intuitive and innovative smartphone application[6]. The application allows members to easily book appointments, leveraging geofencing technology similar to Uber. The application connects members to a list of available doctors for their specific need based on their current location. Additionally, through the smartphone application, members can even communicate with a board-certified doctor to treat common conditions or obtain prescriptions without leaving the office or house. Consumer friendly features such as the booking of appointments through a smartphone application and telemedicine are providing a customer focused experience[7]. Such experiences can lead to lower cost of administrative burdens through automation and telemedicine. Telemedicine avoids the need to block the providers time to treat simple aliments.

On the back-end of things, Oscar Health is using technology to revolutionize the claims and billing process. The complexity of healthcare billing is understood by few outside of the industry and does not align with a streamlined process which lowers cost. The current billing complexity tends to create billing delays and additional interactions between the physician and payer to process claims. The final cost of healthcare is significantly influenced by these administrative costs experienced by the hospital, provider or physician as well as the actual insurer. Oscar Health has essentially taken a ground up approach in developing a technology infrastructure that generates a better experience for all parties involved in the claim's adjudication process. A simplified and shortened claims process using automation reduces processing time and simplifies the billing complexity. By aligning technology that keeps the customer the center of attention, Oscar Health recently reported its first underwriting profit and is continuing to expand its market each year[8]. The company is challenging traditional health insurers and even filed suit[9] as one traditional health insurer recently tried to thwart their expansion within a new market.

Innovative technology will continue to disrupt the insurance industry as companies look for competitive advantages by leveraging data and consumer needs. Last year saw a significant increase in acquisitions of InsurTech startups by major carriers, and the trend is expected to continue. Startups and traditional insurance companies will inevitably face hurdles as they introduce revolutionary products that change how the current market functions. However, the door is currently open to these changes as the InsurTech industry and regulators continue to overcome differentiating views and form a beneficial environment that provides value to consumers.

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About the Author

Terry W. Ryals, CISA, CDFE functions as the Cybersecurity and Forensic Manager for the INS Companies, overseeing security risk assessments, forensic reviews and E-discovery engagements. Mr. Ryals has been instrumental in assisting with the integration of cybersecurity and IT forensic procedures within traditional market and financial regulatory examinations. His efforts have identified vulnerabilities exposing policy databases, and other personally identifiable information (PII), permitting insurers to remediate prior to a costly compromise. Other experience includes Information Technology General Controls (ITGC) and financial reviews, penetration testing, data analytics, database administration, interim management, financial fraud investigations and reviews of general regulatory concerns of misconduct. Mr. Ryals has participated on financial fraud investigations with a combined total in excess of $125 million dollars of fraud.

Reliance of Third-Party Control Documentation: A Question of Judgement

By Dave Gordon, CISA, CIA, CFE, CDFE
The INS Companies

Based upon recent best practices, it is recommended that the financial examination team rely upon third-party information technology controls when possible and appropriate. The Financial Condition Examiners Handbook indicates that within Phase Two, the examiners are to identify and document risks of the examined insurer and that examiners may identify risks from the insurer's own risk assessment, internal and external audit risk assessments, the Sarbanes-Oxley Act of 2002, as well as other sources that would provide such meaningful information.

Other directives indicate that based on the review of internal and external audit work, the examiners may determine that sufficient testing has been performed to fully address specific risks or areas of concern. In cases such as in these, examiners may plan reliance on the specific internal and/or external audit work reviewed. Obviously, the reliance on other third-party control evaluations are beneficial to almost everyone involved as the examiners are able to more efficiently evaluate controls of the insurer and the insurers benefit from not having to go through duplicate (or more frequently repeated) audit steps that have already been completed.

Additionally, as information technology control assessments are to be completed by the end of Phase Two of the examination, the efficient evaluation of the information systems control (information technology general controls or ITGCs) environment with support from the review and reliance on third party work also can help expedite the completion of Phase Two of a financial examination.

Basic audit examination principles allow for less substantive (detail and transactional level) testing in activity processes where controls are evaluated as effective as "effective" controls provides comfort to the financial examination team that the company is either preventing processing errors from occurring through the use of effective preventive controls or is correcting processing errors by self-testing process outcomes through the use of detective controls. Therefore, there are multiple advantages to be gained for advantage by relying upon third party control work where applicable. However, relying upon others' work raises multiple question as to what third party control work may be relied upon as well as under what conditions the work may be relied upon. Questions such as "just because information (third party audit work) is available, can it be relied upon?" are universal throughout the examination process. As with all evidence, the examiner must use professional judgment in relying upon the work of others. The fact that work is provided by what are thought to be independent third parties, does not automatically ensure that the work is of adequate coverage, nor does it ensure that the work is of adequate quality.

The answers to those questions are based upon judgment and with this article, we hope to provide some guidance or at least help point out some guidance that would help examiners ask the correct questions to point them in the right direction in relying upon other third-party work.

Some notes and qualifications to consider for this article are as follows:

- Please note that as this article pertains to internal controls and internal control evaluations and there will be limited discussion on detailed substantive testing in this article.
- Additionally, please note that "third-party" may have two different meanings when conducting control assessment. In relation to the insurer/company, a third-party may be in reference to a "third party" processor that performs work for the insurer. For the sake of this article, "third-party" work means audit and/or assessment work performed by examiners/auditors other than the examination team.

Third-Party Assessment Options

On most examinations, unless for very small insurers, third-party assessment work is usually available from either one or multiple sources. Whether it be external audit workpapers, internal audit workpapers, Service Organization Control (SOC) reports or similar other sources of controls, the sources may be relied upon under the correct conditions. Of course, as with all examination evaluations, steps need to be taken to be sure that the third-party are professionally prepared, meet the proper scope and address the risks applicable to the particular examination.

External audit workpapers and accompanying reports usually provide an extensive overview of the company's financial reporting process as well as any existing controls related to the financial reporting control process. The scope of such external audit work is usually focused on how the financial reporting process is performed, key controls over the financial reporting process (whether directly related to the financial reporting process or not) and an evaluation of proper financial reports procedures and results.

Most external audits consider and evaluate the company's internal control structure as part of their work and in some cases, rely upon the company's internal controls when the control structure is assessed to be reliable. This reliability provides the external auditors with an additional level of comfort and support for the conclusions they reach as well as efficiencies in performing their overall work by reducing the overall level of work required to reach an adequate audit opinion. If the external auditors perform an internal control assessment, consideration should be made to whether or not this assessment should be relied upon.

Internal audit workpapers should also to be considered as potential sources for reliance. As internal audit department vary from company to company, reliance may vary as well. A typically guide for reliance may be size of the company's internal audit department, however other factors need to be considered such as the scope of the work performed, the experience level of the internal auditors, the quality of the work performed and maybe most importantly, the true level of independence of the internal audit team. When considering the independence of the internal team, due care must be taken to determine what kind of influence that management may have over the internal audit assessments and whether that influence may affect the accuracy of those assessments. In some cases, the influence over internal audit by be so strong that it is not easily detected as it is not even apparent to management nor the internal audit team itself.

Similar to internal audit workpapers and sometimes overlapping internal audit work is the NAIC's Model Audit Rule (or MAR) or Sarbanes Oxley Act (or SOX) work which is a company's self-assessment process related to financial reporting controls. MAR and/or SOX workpapers also provide another level of comfort to the external auditors as they evaluate an insurers' financial reporting control structure.

Additionally, one of the more reliable sources of third-party work to be relied upon are Service Organization Control (or SOC) reports. SOC reports are as the name clearly identifies reports on the controls of a service organization. SOC reports have multiple variables to which consider whether or not they are relevant to a particular financial examination, however since their primary focus is on control evaluation and assessment, the details provided are extremely useful in most cases.

A SOC report summarizes an assessment of the internal controls at a service organization. Service organizations are usually external vendors which have been hired by the insurer to process and/or protect an insurers' data and the SOC report describes and assesses the service organization's control structure. SOC engagements are performed in accordance with the Statement on Standards for Attestation Engagements (SSAE). As defined, there are three "views" (identical to various scopes) of control evaluation within various SOC reports and each of those "views" or "scopes" are defined independently by name as either SOC1, SOC2 or SOC3 reports. For example, a SOC 1 assessment is comprised of control objectives which are used to accurately represent internal control over financial reporting (ICFR).

SOC2 reports, as opposed to SOC1 reports, are for service organizations that hosting or process information for insurers that does not directly impact the insurer's financial reporting. SOC2 reports are more concerned whether you are handling their data in a secure way and if the data is available to them in the way the way that the insurer has contracted with the service organization. A SOC 2 report, similar to a SOC 1 report, evaluates internal controls, policies, and procedures. However, the difference is that a SOC 2 reports on controls that directly relate to the security, availability, processing integrity, confidentiality and privacy at a service organization.

A SOC3 report generally has the same information as a SOC2 report. The main difference between the reports is that a SOC3 is intended for a general audience and therefore, the reports are shorter and do not include the same details as a SOC2 report, which is generally distributed to a more informed audience.

SOC reports are also defined by the time period for which they cover their control assessment. The main difference between a SOC Type I report and SOC2 report is that a SOC is an assessment of controls at a service organization at a specific point in time, whereas a SOC Type II report is an attestation of controls at a service organization over a defined (minimum of six months) time period. A comparison between the two types of reports are that a SOC Type I report is a "picture" at a certain time, where a SOC Type 2 report is more of a "video" over a period of time.

Note that if an insurer does not have any SOC reports available from their service organization and the service organization actually produces a SOC report, this is usually an indication that the insurer is not properly assessing their third party/vendor management process properly, which is a problem and most likely a significant issue in itself.

Also keep in mind while assessing SOC reports that in order for the service organization's controls to fully work as designed, there is an automatic assumption that certain controls must be effectively implemented by user entities (i.e. companies using the services provider's services). Within most SOC reports there should be a section that describes additional controls that user entities should have in operation to complement the controls of the service organization.

As an illustration of a practical application or metaphor of an example of the narrative above, in cases where a service organization may have adequate security controls such as enforcing adequate segregation of duty controls over data security, those controls in themselves may not adequately address underlying security controls if the user entity does not have adequate controls in place over segregation of duties to compliment the service organization's controls. To summarize, if a service provider has an adequately effective control structures and the company to which services are provided does not have adequate supporting, then it's unlikely security controls may be relied upon without adequate compensating controls being in place.

Other control assessments may be available for review and assessment, such as agreed-upon procedures, cybersecurity assessments as well as other control assessment documents made available to the examination team.

In order to determine whether third-party controls may be relied upon, there are three thresholds that need to be assessed based upon the examiner's judgment. These three thresholds are whether or not the documentation is in within scope, whether it's part of a key activity and whether or not the work is professionally prepared and completed.

As a default, based upon professional skepticism, we would start in a state of "no reliance", however as we determine that the controls, findings and testing performed can pass certain thresholds of judgment, we can rely upon the third-party control documentation.

To start, we need to determine if the documentation being reviewed is within scope as obviously, if documentation is not relevant for the entities, the key processes nor the key controls within scope, there is no reason to rely upon that work further. Scope issues are usually easy to determine unless there is an overarching process or control that may be representative across various entities or processes. In cases where processes or controls are overarching, such documentation should be further evaluated for reliance and inclusion. Once scope is determined, the inclusion of the third-party control assessment documentation should be further assessed as to whether the controls and related risks are relevant for the key activities within scope of the financial examination. For example, while it may be an important process, payroll controls would most likely be considered outside of scope for most financial examinations and therefore, payroll SOC reports should most likely not be assessed for reliance. On the other hand, if a company outsources its primary data center, the data center's physical and environmental controls would most likely be considered within scope of most financial examinations as data center controls are ITGCs being used across a wide range information technology environment.

The final major threshold as to whether control documentation should be considered or relied upon is whether the information is professionally prepared and completed. This is where the examiner's judgment is most vital to determine reliance. Unfortunately, not all documentation is professionally prepared and therefore, all documentation must be judged upon a high and consistently applicable set of factors.

For external audit workpapers, the examiner should determine the experience and reputation of the firm producing the results. Typically, the documentation of a larger firm with a more established presence should be acceptable, however there are also smaller firms that do a great job in producing quality products. Beyond the size and reputation of an external audit firm, the examiner should consider the quality of the work, specifically control documentation.

According to established auditing standards, external auditors are required to evaluate an auditee's (insurer's) management assessment over the internal controls associated with the financial reporting process. The documentation (usually in the form or a summary memo or equivalent) associated with this assessment should indicate control weaknesses, the extent of any weaknesses as well as an opinion on whether controls can be relied upon. It's with this opinion that the examiner can gain an overview of the work performed to evaluate internal controls.

For internal audit work, the examiner must not only determine independence of the internal audit function, but also the methods for which the work has been completed. The professionalism of internal audit departments varies company-by-company. Each department has their own methods of performance, level of expertise and ability to deliver a quality product.

In regards to SOC reports, there are established professional guidelines and procedures on how these reports should be documented and performed. Therefore, the ability to judge this work for reliance is fairly consistent. As the SOC report is a primarily a summary of controls, associated testing of those controls as well as a summary of exceptions that may have been discovered during testing. Therefore, in most cases the the reports lend themselves to being relied upon as long as the controls, testing and evaluations are within scope.

In order to obtain a clear view of what reliance should be relied upon and what should not be relied upon, the examiner should consider the following questions to evaluate the usability of third-party work. If the documentation does not match the criteria below, the examiner needs to determine how much of the documentation (if any) may be relied upon:

- Is the assessment risk-based?
  - If not, what principals guide the assessment?
- Do the control objectives and associated controls match the risks?
  - If not, why not?
- Are there enough meaningful controls in place to satisfy the control objectives identified?
  - If not, which controls are missing? Why are these controls missing?
- Does the testing performed match the associated controls and risk identified?
  - Sometimes gaps between risks, controls and testing performed. If such gaps exist, the examiner must consider why such information may be missing. Is it due to a lack of professional judgment or competence?
- Do the processes and/or controls identified match the financial examiners' understanding of the company?
  - If not, why not?
- What is the effect of findings/exceptions found in the third-party work?
  - Are they material and/or significant for the insurer being examined?
- Are identified findings an indication of deeper, less mature problems that may be turn more significant over time?

The financial examiner needs to consider various factors to determine which third-party work may be relied upon for a financial examination. As professional judgment is the primary driver in evaluating the level of reliance and that third-party audit work can vary significantly in scope, applicability and quality, the most difficult part of relying upon third party work is to consider what documentation needs to be included and then retro-fitting that information to supplement financial examination requirements.

By considering all the third-party work and using professional judgment, examiners should be able to more efficiently perform examination work, however every opportunity to rely upon such work also is met with new challenges to be more efficient and provide more valuable in delivering financial examinations. The effective use of third-party work allows for this to occur.

About the Author

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PwC NAIC Newsletter

April 2019

The National Association of Insurance Commissioners held its Spring National Meeting in Orlando. This newsletter contains information on activities that occurred in some of the committees, task forces and working groups that met there and includes subsequent conference calls through April 24. For questions or comments concerning any of the items reported, please feel free to contact us at the address given on the last page.

In this issue

Executive Summary

- The NAIC announced that long-term care insurance issues are its number one priority in 2019 and formed the Long-Term Care (EX) Task Force to focus on market stability.
- The Statutory Accounting Principles Working Group adopted new guidance on structured notes and cloud computing assets. The working group also exposed for comment proposed guidance on leases, affiliated transactions, deferred income tax assets, limitations on goodwill, and rejection of ASU 2018-12 related to long-duration life insurance contracts.
- The Blanks Working Group adopted revised AVR factors for year-end 2019 reporting to reflect the Federal tax rate changes implemented in 2018 and exposed for comment extensive revisions to Schedule DB for new guidance related to derivatives used to hedge variable annuity guarantees.
- The Life RBC Working Group finalized its Interpretation of 2018 Life Risk-Based Capital Results in Light of the 2017 Tax Cuts and Jobs Act document. The P/C RBC Working Group adopted revised underwriting risk "line 4" factors for 2019 RBC filings. The Investment RBC Working Group has not met publicly since November, as the regulators are deliberating next steps on the life RBC bond factor project.
- The VOS Task Force adopted guidance for its P&P Manual related to the filing exempt process for credit tenant loans.
- The Group Capital Calculation Working Group worked to finalize its field testing process and Excel template, with the project kick-off in May.
- The Reinsurance Task Force has proposed additional revisions to the credit for reinsurance models to reflect adoption of the covered agreement as a result of comments received in late 2018. The task force anticipates final adoption this summer.
- The Life Actuarial Task Force adopted many Valuation Manual amendments, including requirements for the Deterministic Reserve scenario for Indexed Universal Life.
- The Variable Annuity Capital and Reserve Subgroup met nearly weekly this winter and spring to draft edits to VM-01, VM-21, and AG 43 to adopt the recommendations of the VA Framework ahead of the January 1, 2020 implementation date.
- The newly formed Restructuring Mechanisms Working Group began its work on addressing the perceived need for restructuring statutes; a draft white paper is expected later this year.
- The Casualty Actuarial and Statistical Task Force continued work on the Appointed Actuary project with discussions related to attestation, experience and continued competence. The NAIC hopes to adopt changes to the Statement of Actuarial Opinion instructions in time to implement for 2019 opinions.

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PwC NAIC Newsletter

April 2019

All documents referenced can be found on the NAIC website naic.org.

Executive Committee and Plenary

During a special election held January 24, the NAIC elected Commissioner David Altamier of Florida as Vice-President. Commissioner Altamier replaces Gordon Ito (HI), who returned to his role as deputy commissioner, effective January 1, 2019.

Long-term care prioritized
At the Spring National Meeting, the commissioners voted unanimously to create a task force focused on long-term care insurance market stability, which will report to the Executive Committee. The first meeting of the Long-Term Care Insurance Task Force is tentatively scheduled during the NAIC Insurance Summit the first week in June in Kansas City. Virginia will chair the task force with Colorado as vice chair. The task force is charged with "developing a consistent national approach for reviewing long-term care insurance rates that result in actuarially appropriate increases being granted by the states in a timely manner, and eliminates cross-state rate subsidization."

During the Spring National Meeting, the commissioners gave final adoption to the following:

- Amendments to the Accident and Sickness Insurance Minimum Standards Model Act #170
- Revisions to the Health and Welfare Plans Under the Employee Retirement Income Security Act: Guidelines for State and Federal Regulation (ERISA Handbook), the NAIC Medicare Supplement Insurance Model Regulation Compliance Manual, and the Shopper's Guide to Long-Term Care Insurance
- Guideline on Nonadmitted Accident and Health Coverages

Innovation and technology initiatives

Insurtech – collaborations and regulatory challenges
The Innovation and Technology Task force received presentations in Orlando from guest innovators. Markel Corporation presented how they collaborated with an Insurtech to provide the technology and customer acquisition strategy for episodic general liability coverage (e.g. short-term policies for contractors that are typically 2 days or less) that traditional brokers do not serve. The American Association of Insurance Services presented on its creation of a Blockchain technology that can streamline regulatory reporting and provide insights on data gathered that could be used for tasks such as regulatory data calls.

There was an update provided on innovation and regulatory challenges including a presentation of the survey performed by Plug and Play regarding Insurtechs' perception of regulatory barriers to their growth. Of the 34 Insurtechs surveyed, 50% did perceive barriers, especially those who are market facing, but they did not provide detail as to any specific regulations driving this; 76% of respondents believe a more open dialogue with the NAIC would be of value.

Cybersecurity initiatives
Four states (South Carolina, Michigan, Ohio, and most recently Mississippi) have now adopted the Insurance Data Security Model Law (#668) with four more states (Alabama, Connecticut, Nevada and New Hampshire) considering adoption this session. At the Spring National Meeting, the chair encouraged other states to adopt the model without amendment to ensure consistency. He noted that no Federal legislation on cybersecurity has been adopted that might conflict with the NAIC model.

Ohio's cybersecurity legislation is based on the NAIC model and was effective March 20, 2019 for most provisions. The Data Protection Act applies to most Ohio insurers; only licensees having fewer than 20 employees, less than $5 million in gross annual revenue, or less than $10 million in assets are exempt. Each insurer domiciled in Ohio will be required to submit to the Superintendent of Insurance a written statement certifying that the insurer complies with the bill's cybersecurity requirements by February 15 of each year; the first statement will be due from insurers on February 15, 2020.

Michigan has also adopted cybersecurity requirements based on the NAIC model, effective January 20, 2022 for most provisions; it exempts insurers with licensees having less than 25 employees.

Anti-rebating
The Innovation and Technology Task Force discussed progress by its subgroup on reviewing anti-rebating, cancellation/ renewal, and e-

signatures laws. The discussion focused mostly on anti-rebating, which relates to rebates of premium or other consideration associated with the use of smart home devices and telematics to mitigate risk. The subgroup has noted uncertainty in the application of these laws to new technology, whether they are impediments to innovation and whether additional guidance should to be provided. The task force will be meeting at the NAIC Insurance Summit in June to discuss this issue, including consideration of the current anti-rebating language contained in the NAIC's Unfair Trade Practices Act.

Blockchain educational event
The NAIC's Center for Insurance Policy & Research sponsored an educational event entitled The Future of Blockchain in Insurance including the history and evolution of blockchain and regulatory hurdles blockchain implementation may face. For more information on blockchain in insurance, see these PwC publications: Transformation, Catalyst Part 1, and Catalyst Part 2.

Big data

New York Circular Letter 1 (2019)
The New York Department of Financial Services issued in January a circular letter on Use of External Consumer Data and Information Sources in Underwriting for Life Insurance, which applies to all insurers authorized to write business in New York. (The NYDFS is the first regulator to issue guidance on use of external data.) The guidance requires that insurers should not use an external data source, algorithm, or predictive model in underwriting or rating unless the insurer can establish that the underwriting or rating guidelines are not unfairly discriminatory. An insurer may not "simply rely on a vendor's claim of non-discrimination or the proprietary nature of a third-party process as a justification for a failure to independently determine compliance with anti-discrimination laws." Insurers must also disclose to consumers the content and source of any external data which the insurer used to arrive at an adverse underwriting decision.

Predictive models
Property/casualty underwriting - The Big Data Working Group heard an update on the work of the Casualty Actuarial and Statistical Task Force including a summary of comments received on its draft whitepaper, Regulatory Review of Predictive Models, which includes a discussion of best practices for regulators when reviewing predictive analytics and the information the regulator may need to review the model. Recommended policy issues to consider further include confidentiality, models other than the generalized linear model, correlation, and transparency.

The group also heard a preview of the recommendations from NAIC staff on areas such as the skillset and resources needed to assist with reviews of the models and methods and procedures to maintain confidentiality. The recommendations included hiring at least one technical staff other than an actuary to support regulators, developing a tool or database for states to share information about models and developing a big data training program. (A pilot training program is already underway.) The NAIC legal division is continuing its work on confidentiality considerations, which will be presented separately at another time. The task force is targeting completion of the whitepaper in 2019.

Life underwriting - The review of the use of data in life insurance underwriting has been referred to the Life Insurance and Annuities Committee, which is expected to create a working group or utilize an existing working group to continue the study of the use of data in accelerated life underwriting and then draft guidance or best practices.

New project
As its next project, the Big Data Working Group agreed that it should review insurer claim practices such as claim valuation and antifraud efforts to evaluate if the regulatory structure is sufficient to cover such data use and prevent misuse.

Statutory Accounting Principles Working Group

Significant actions taken by the working group at the Spring National Meeting are summarized below. (Appendix A to this Newsletter summarizes all actions taken by the working group since the Fall National Meeting.) The working group plans to hold an interim conference call May 29 to discuss issues exposed with a May 10 comment deadline and 2019 Blanks Working Group proposals.

SSAPs 2, 26R, 43R & 86 – Structured Notes (#2018-18) – The working group adopted guidance that structured notes for which contractual principal amounts are at risk for reasons other than failure of the borrower to repay should be classified and accounted for as derivatives under SSAP 86 and valued at fair value, effective December 31, 2019. Comments from industry to clarify and narrow the scope of instruments included in this guidance were also adopted by the working group; mortgage-referenced securities are excluded from the scope and are to be accounted for in accordance with SSAP 43R.

The working group also approved a new agenda item proposing revisions to SSAP 86 to specify the valuation of these "other" derivatives, since the structured notes do not meet the definition of hedging, replication or income generation transactions.

SSAP 16R, ASU 2018-05, Customer's Accounting for the Implementation Costs Incurred in a Cloud Computing Arrangement that is a Service Contract (#2018-40) – The working group adopted proposed revisions to SSAP 16R to adopt this new ASU with some modifications, which require companies to capitalize implementation costs (related to both the hosting arrangement and the software license) as non-admitted non-operating systems software. The non-admitted asset is amortized over a period not to exceed five years. The guidance is effective January 1, 2020 with early adoption permitted.

SSAP 101 revisions (#2019-09 & #2019-10) – The SAP Working Group exposed for comment extensive proposed changes drafted by an industry interested parties group, with input from the working group. The proposed changes focus on two areas:
1) necessary "housekeeping" revisions to reflect the tax law changes, particularly in the Q&A's illustrative examples (#2019-09), and more substantively,
2) new clarifying guidance related to the issue of the reversal patterns of deferred tax items (#2019-10).

The second exposure discusses what constitutes "scheduling," "detailed scheduling," "additional detailed scheduling," and how "historical and/or currently available information" should be considered in the context of the DTA admission test under paragraph 11.c of SSAP 101. One significant proposed change is to clarify that absolutely no consideration of reversals patterns is required in paragraph 11.c (the third test of the DTA admittance calculation) if the reporting entity did not rely upon reversing DTLs as a source of future taxable income in determining the need for a statutory valuation allowance. Reporting entities that did rely upon reversing DTLs as a source of future taxable income "should" consider reversal patterns and "significant and relevant historical and/or currently available information;" however, any consideration of scheduling of DTLs would be consistent with that considered in the valuation allowance assessment.

The proposed revisions also clarify that consideration of knowledge regarding a fixed straight-line reversal pattern is "scheduling," and if the reporting entity did not rely upon reversing DTLs for the statutory valuation allowance, this information is not considered for 11.c. purposes. This revision is proposed to apply by tax character.

Another significant issue related to the paragraph 11.c. is the starting pool of DTAs for the test. Q&A 4.2 was revised to make clear that each part of the test may consider all of the adjusted gross DTAs and gross DTLs. Additionally, proposed revisions to Q&A 4.24 (3) address the "double counting issue," where differences of interpretation have arisen. Subparagraph 3 (part of an illustrative DTA calculation), per the proposed modification, now simply states that "the fact that reversing deductible ordinary temporary differences were used in the paragraph 11.a. and 11.b. calculations does not prevent their inclusion in the paragraph 11.c. calculation." However, per the illustration, adjustments must be made to ensure that the summation of the three tests does not result in over/double counting.

SSAP 22 – ASU 2016-02, Leases (#2016-02) – A substantively revised and restructured SSAP 22R was exposed for comment at the Spring National Meeting (along with the proposed issue paper), which rejects ASU 2016-02 and retains the guidance that all leases are operating leases. SSAP 22R clarifies the guidance on sale-leaseback transactions, which may only be executed with property, plant and equipment, including computer software. Therefore, both admitted and non-admitted software can continue to be sold and leased back by an insurance entity. SSAP 22R is proposed to be effective for all new leases entered into, and for existing leases with changes in contractual terms, on or after January 1, 2020, with early adoption permitted.

SSAP 25 and Investment SSAPs – Affiliated Transactions (#2019-03) – This proposed guidance seeks to clarify that transactions with affiliated entities or with investments issued by affiliates that involve an unrelated intermediary are still considered related party transactions and should be accounted for and disclosed in accordance with SSAP 25. The proposed guidance appears to have been issued in response to regulatory scrutiny over the alleged $2 billion of investments made by insurance companies of ELI Global LLC to other affiliated entities through intermediaries.

Life reinsurance risk transfer (#2017-28) – At the Fall National Meeting, the working group received comments from both CT and NJ regulators who raised concerns about recent YRT reinsurance agreements of group life insurers with "excessive" YRT premiums which they believe should not be accounted for as reinsurance. These comments and proposed amendments to SSAP 61R proposed by CT and NJ were referred to the life reinsurance informal drafting group for discussion.

The drafting group met four times in 2019 and continues to make progress on these complex issues. The primary guidance being considered for revision are Appendix A-791 Q&As and the YRT guidance in paragraph 19 of SSAP 61R. The drafting group hopes to have a proposal for the SAP Working Group to consider at the Summer National Meeting in August.

SSAP 37 – Acquired Mortgage Loans (#2018-22) The regulators have been working with industry since last August to refine the scope of which investments are included in the scope of SSAP 37. At the Spring National Meeting, the working group exposed for comment extensive revisions to the guidance exposed in November. This includes revisions to the exclusion of "bundled" mortgage loans, to allow mortgage loan classification of "bulk purchases" in which an insurer's interest in each mortgage loan is "legally separate and divisible and the purchase just facilitates the acquisitions of multiple single mortgage loan agreements." The revisions also clarify the requirements of participating interests.

SSAPs 50, 51R, 52, 56, 71 and 86 – ASU 2018-12, Targeted Improvements to the Accounting for Long-Duration Contracts (#2019-06) – The working group officially exposed for comment its anticipated conclusion to reject the accounting provisions of this new U.S. GAAP standard. The exposure also asks for feedback as to whether any of the new disclosures from the standard should be incorporated into statutory accounting such as the rollforwards of the liability for future policy benefits and for policyholders' account balances and the rollforward of market risk benefits.

Regulatory Transactions referral from the Reinsurance Task Force (#2018-06) – The SAP Working Group proposed in 2018 that items acquired as part of "regulatory transactions" that meet the definition of an asset could only be admitted with approval of the domiciliary regulators as a permitted practice. Interested parties raised significant objections including unintended consequences of an overly broad proposal.

At the Spring National Meeting, the working group agreed to dispose of this agenda item without any proposed changes to the SSAPs and will refer to the VOS Task Force a recommendation that two new codes be used to identify regulatory transactions: RTS and RT. RTS will apply to a regulatory transaction in which a state insurance department requested assistance from the SVO in reviewing the security, and the SVO reviewed the security and provided an SVO analytical value, e.g. 3RTS. RT securities are not eligible for an SVO analytical value and would receive an NAIC 6 designation.

SSAPs 68 and 97 goodwill reconsiderations – The regulators exposed for comment three new issues that would impose additions restrictions on goodwill, as follows:

- ASU 2014-17, Business Combinations-Pushdown Accounting (#2019-12) would be rejected and proposed revisions would explicitly prohibit insurance entities that hold SCAs valued using U.S. GAAP from reflecting pushdown of goodwill to an acquired entity. This conclusion is a change from current interpretations of SSAPs 68 and 97. There was no discussion of whether the guidance, if adopted, would be applied retroactively or only to new acquisitions.

- The SSAP 97 "look-through approach" would be clarified that it only applies to the downstream level directly below the noninsurance holding company. In addition, revisions propose goodwill may be admitted only if its value has been supported by an audit report (#2019-13).

- Proposed revisions to SSAP 68 would require that in connection with the acquisition of a holding company, purchase price and goodwill amounts must be attributed downstream to the entities that the holding company directly owns (#2019-14). The working group believes this is necessary for several reasons such as determining tax basis of individual entities and the need for allocated purchase price and goodwill to calculate any gain or loss on a future sale of an individual entity owned by the holding company. However, this required allocation could be viewed conceptually as being inconsistent with the related proposal to prohibit pushdown (#2019-12).

Blanks Working Group

The working group met in Orlando and adopted eight proposals, which include the following, and are effective for year-end 2019.

- Add questions 34.1 and 34.2 to the general interrogatories part 2 of the life annual statement, applicable to fraternals only. These questions were inadvertently left out of the 2018 annual statement when the fraternal blank was combined with the life blank (2018-23BWG).

- Revise the AVR Factors (basic contribution, reserve objective and maximum reserve) in the life annual statement to be consistent with the RBC after-tax factors, which were amended in 2018 as a result of federal tax reform (2018-24BWG).

- Remove line 5, contract loans, from the separate accounts asset page to reflect the guidance under SSAP 56 that indicates all policy loans shall be reported in the general account (2018-29BWG).

The working group also exposed 17 items for comment through May 21, which include the following significant proposals, and which have a proposed effective date of year-end 2019.

- Revise the instructions to Part 1 of the VM-20 Reserves Supplement to provide clarifying guidance on line reporting for the product group types (2019-02BWG).

- Add a designation column for mutual funds to annual Schedule D, Part 2, Section 2, and modify instructions for NAIC Designation and Administrative Symbol columns for quarterly Schedule D Parts 3 and 4 to facilitate reporting the designations of these funds (2019-03BWG).

- Remove the reference "Life and Fraternal only" from the instructions for Schedule BA as well as add additional lines to the categories "Fixed or Variable Interest Rate Investments that Have the Underlying Characteristics of a Bond, Mortgage Loan or Other Fixed Income Instrument" and "Joint Ventures or Partnership Interests for Which the Primary Underlying Investments are Considered to Be Fixed Income Instruments" to provide consistency in reporting on Schedule BA across statement types for all investments in those categories (2019-04BWG).

- Modify the instructions for question 2 of the supplemental investment risk interrogatories to exclude diversified foreign mutual funds and add a new interrogatory to require disclosure of the top 10 fund managers determined by aggregating by fund manager across all types of funds and on all schedules, allocated between diversified and non-diversified funds (2019-13BWG).

- Revise the instructions and illustrations for Note 8-Derviatives to incorporate disclosures required by SSAP 108 and add a new 19-column Part E to Schedule DB, Derivatives Hedging Variable Annuity Guarantees as of December 31 of Current Year, along with other extensive revisions to Schedule DB and instructions (2019-14BWG).

- Add a new column "YRT Mortality Risk Only" to the Analysis of Operations by Lines of Business and Analysis of Increase in Reserves During the Year to disclose YRT reinsurance where mortality is the only risk covered; it will be reported in its own column (2019-16BWG).

Risk-based capital

The regulators made the following significant progress on RBC projects. (Appendix B summarizes other actions taken by the various RBC Working Groups since the Fall National Meeting.)

Investment RBC
The Investment RBC Working Group has not met since the Fall National Meeting. There appears to be uncertainty as to status of the working group's bond factor proposal (in process since 2011) and whether further independent validation of the AAA-proposed model should be performed. The next meeting of the working group is scheduled for May 16; an agenda is not yet available.

Life RBC
Effect of tax reform on life RBC – The working group adopted in February its document entitled Interpretation of 2018 Life Risk-Based Capital Results in Light of the 2017 Tax Cuts and Jobs Act. The communication is designed for regulators and other users of RBC to explain the changes to the formula so that users can distinguish between a change that is due to tax reform and a change due to something else. Some sampling was done to confirm that the estimate of the increase to required capital is between 5% and 15%, but some companies will be on either side of the range. The guidance separately

discusses the effect on tax reform on TAC (total adjusted capital) and ACL (authorized control level capital).

Variable Annuities Capital and Reserve Subgroup
The Life RBC Working Group exposed for comment until May 7 changes to the Life RBC instructions proposed by the VACR Subgroup; see the summary of the variable annuities framework on page 11 for additional discussion.

Longevity risk – The Longevity Risk Subgroup exposed the report of the AAA's Longevity Risk Task Force for comment until May 23. The Academy is recommending that a capital structure with longevity C-2 factors be applied to base statutory reserves and that a covariance adjustment within C-2 be implemented to reflect the "offsetting nature of mortality and longevity risk." The proposal also includes a "working version" of a proposed set of factors. The goal of the subgroup is to finalize the proposal for implementation for 2020 RBC filings, effective for all in-force business as of year-end 2020.

Along with the Academy's report, the subgroup also exposed four specific questions for industry input, which include the following:

- Is the Academy's proposed approach appropriate if the covariance factor with mortality is not adopted?
- Would it be feasible to adopt or consider an adjustment to the C-2 factors presented based on the potential that some issue years of past business have reserves that may not meet the 85th percentile risk coverage assumed by the Academy field study?
- Are the break points in the proposed approach appropriate or should they have been based on a proxy for size of individual exposure rather than an assumption of number of deaths through an average size of 50,000?

Mortality Risk – The AAA's C-2 Work Group is reviewing the assumptions and methodology for life insurance (individual, industrial, group and credit life) and provided an update presentation in Orlando. The work group has developed a preliminary model and has "approximately replicated" the original 1993 factors and has created preliminary distributions and assumptions for each mortality risk component.

The next steps are to continue model assumption development considering mix of business, lapse rates, reinsurance and other factors, define the group life approach, finalize model development and testing and recommend factors. The goal is to develop preliminary factors by year-end 2019.

2019 Life RBC projects – The Life RBC Working Group discussed possible new projects and those in process. The chair noted that the combination of the Life and Fraternal formulas into one RBC formula is on schedule for year-end 2019 completion, which is consistent with the combination of the two annual statements into one. The project on the treatment of fixed annuities without living benefit riders has been incorporated into the Academy's work on C-3 Phase I. The working group also discussed the structural changes to Life RBC related to tax reform that the working group could not complete in 2018 due to lack of time and whether they should resume effort on those issues. The chair asked the ACLI to study the issues and provide a recommendation.

<u>Operational risk</u>
The Operational Risk Subgroup disbanded at the Spring National Meeting after referring its projects in progress to the Life, Health and P/C RBC Working Groups. The status of those projects is discussed below.

Life RBC growth risk charge – The Life RBC formula does not include a provision for growth risk. (The informational growth risk calculation on LR029-A was removed from the formula beginning with 2019 RBC filings.) The Operational Risk Subgroup explored various options for a growth risk charge but was unable to reach a consensus with industry representatives on a proposal, many of whom believe a separate growth risk charge is not necessary. The subgroup drafted a detailed "hand-off" memo for the Life RBC Working Group, which provides a history of its work and the pros and cons of adding a growth risk charge. At its meeting in Orlando, the chair of the Life RBC Working Group expressed some concern about the ability to develop an appropriate measure for life growth risk but believes discussion by the working group is necessary.

Health RBC growth risk charge – The Health RBC Working Group adopted a recommendation from the Operational Risk Subgroup to form an ad hoc subgroup of regulators and interested parties to review the existing excessive growth risk methodology. In its referral document, the subgroup suggests reviewing whether the 10% threshold (i.e. if growth Underwriting Risk RBC exceeds growth in underwriting risk revenue by greater than 10%) is reasonable, whether the charge should apply to start-up companies, and whether the health growth risk methodology should be applied to life companies that write a material amount of health business. Work on this project will begin later this year.

P/C RBC

Underwriting risk – The P/C RBC Working Group and the CADTF adopted a new set of underwriting risk "line 4" factors (industry loss and expense RBC percentages), based on a 2017 study done by the AAA (proposal 2018-16-P), which had exposed for comment at the Fall National Meeting. The proposal uses 35% capped factors for Commercial Insurance, Medical Professional Liability, and All Other Lines, and uncapped factors for Personal Lines and Reinsurance Lines. Both the working group and industry support the 2019 effective date for the revisions.

Catastrophe risk: wildfire – At the Fall National Meeting, the Catastrophe Risk Subgroup reached a consensus that they should study whether wildfire risk should be included in catastrophe risk, in addition to hurricane and earthquake risk. At the Spring National Meeting, the subgroup heard a detailed presentation from AIR Worldwide whose representative gave an overview on historical wildfire losses, model assumptions, mitigation features and model losses. The representative noted that their model is now third generation and that many catastrophe bonds have been issued using this model.

The subgroup also heard a presentation from a representative of A.M. Best on catastrophe analysis in their ratings and assessing wildfire risk within that analysis. The representative noted that many companies are not yet comfortable using models for wildfire risk for enterprise risk management but that interest has significantly increased due to the 2017-2018 wildfire seasons. The chair asked the subgroup to consider the information presented for discussion during its next conference call.

Health RBC

Health care receivable factors – The Health RBC Working Group exposed for comment a proposal (2019-04-H) to apply an additional charge for health care receivables accrued in the prior year but not received in the current year. Pharmaceutical rebate receivables would receive a 5% charge, and all other healthcare receivables would be assessed a 19% charge. The charges would be informational only for 2020 and 2021 with full implementation in 2022.

Annual statement health test – An ad hoc group of the Health RBC Working Group has been considering options on how to capture the nearly one-third of short-term health premiums that are reported on the life blank. The group is developing a two-phase plan to 1) revise the current health test language, and 2) consider adding health annual statement schedules to the life and P/C statements as supplemental schedules. The ad hoc group hopes to have a formal proposal by the Summer or Fall National Meeting, with implementation anticipated for 2020 annual statements.

Valuation of Securities Task Force

The task force has made recent progress on the following projects.

P&P Manual amendment adoptions

Regulatory Transactions – The task force adopted an amendment to the P&P Manual to clarify the status of an investment security component of a regulatory transaction, which has been the subject of much debate in the past year. The amendment states that a stand-alone investment security is not precluded from being considered for an NAIC designation through the FE process just because it is part of a regulatory transaction.

Fund investment framework – The task force adopted proposed revisions to the P&P Manual to provide a comprehensive framework for fund investments that hold a portfolio of bonds. The revisions expand the existing framework to SEC investment companies organized as closed-end management companies and unit investment trusts. The task force noted that the Capital Adequacy Task Force will have to revise RBC factors for these investments for there to be any change from their current common stock factor.

Filing exemption disclosure – The task force adopted proposed P&P Manual amendments to improve the disclosure of securities not eligible for filing exemption and will consolidate the guidance in the beginning of the FE instructions. The revisions reflect the consensus reached with industry that credit tenant loans meeting the four criteria specified in the Manual are eligible for Schedule D reporting and should be filed with the SVO to confirm the criteria are met. The task force agreed to draft a separate amendment after working with industry on issues identified related to "non-traditional CTLs" and whether they can be reported on Schedule D or should be moved to Schedule B (which has RBC implications).

Reformatted P&P Manual – The task force adopted its draft reorganized and reformatted P&P Manual for year-end 2019 (subject to other amendments adopted this year). The project was a "huge undertaking" that has the support of industry.

Private letter ratings
At the Spring National Meeting, SVO staff reported that implementation of CRP data feeds for securities subject to private rating letters has been "challenging" and that companies will have to file pdf copies of private ratings for year-end 2019 if all the feeds are not up and running by then.

Report on credit rating consistency
The SVO gave an update on its "FE logic" project to modernize its internal electronic processes to map NAIC CRP credit rating symbols to the filing exemption designation and exclude those ratings that do not have the appropriate characteristics, in an effort to reduce reporting exceptions. The SVO's spreadsheet showing each distinct symbol for each CRP credit rating scale and grade is now available on the task force's webpage. Filers will need to understand how the revised process may require them to make changes to their own systems and procedures.

Group capital calculation

The focus of the working group since the Fall National Meeting has been on the group capital calculation field testing template, which had been exposed for comment in November, with conference calls this winter to discuss technical questions on the template as well as the field testing process more generally.

The technical topics discussed included:

- Consistency with legal entity rules: The field testing template will allow the calculation to be viewed both with and without adjustments such as prescribed and permitted practices that may be specific to a given legal entity.

- Scope of application: The working group is providing some flexibility to determine the scope of application allowing for discussions between states and volunteers.

- Exclusions: There was some hesitation to make decisions on exclusions by type or size of entity prior to field testing.

With regard to the field testing process, the following was discussed:

- Volunteers: Thirty companies have volunteered, comprised of a mix of lines of business and company structures.

- Timeline: the testing will begin in May. Volunteers will be given ninety days to complete the template and an additional sixty days is provided to review the results.

- Data: The expectation is that data from 2018 will be used; however, the use of 2017 data would be considered in hardship situations.

- Confidentiality: The NAIC has started to execute confidentiality agreements with the various lead-state regulators, relying on state specific confidentiality provisions.

At the working group meeting in Orlando, the chair noted his goal is to adopt a final template by the end of 2019. However, if the results of field testing indicate significant changes or additional field testing are necessary, the chair committed to further consideration by the working group.

Reinsurance Task Force

Credit for Reinsurance Model revisions
Since 2017, the Reinsurance Task Force has been deliberating proposed changes to the Credit for Reinsurance Model Law (#785) and the Credit for Reinsurance Model Regulation (#786) to reflect adoption of the new Bilateral Agreement between the U.S. and EU. The final revisions were expected to be adopted by the end of 2018, but a vote was deferred pending resolution of concerns raised by interested parties and comments from the U.S. Treasury and U.S. Trade Representative received in December (and subsequent similar comments from the European Commission).

The models were revised to address the concerns raised and were re-exposed on March 7. Some of the changes since November 9 draft include the following:

- adding the United Kingdom as a reciprocal jurisdiction as a result of the U.S. signing a bilateral agreement with the UK on December 18, 2018,

- adding that U.S. jurisdictions that meet the requirements for accreditation are reciprocal jurisdictions,

- clarifying that a ceding insurer subject to rehabilitation, liquidation, or conservation may seek an order requiring security for all outstanding liabilities from its assuming reinsurer, and not that the court will require it

- clarifying the effective date is on or after the date when an assuming insurer has satisfied the requirements to take credit for reinsurance under the applicable subsections of the model laws and not when the commissioner has determined the insurer is eligible, and,

- adding drafting notes that address: a) nothing is intended to enhance or limit the authority of U.S. state insurance regulation as it respects group-wide supervision, b) states are encouraged to facilitate the passporting process for multi-state recognition of assuming reinsurers, and c) the respective bilateral agreements specify the minimum solvency ratio for assuming insurers in those jurisdictions.

At the Spring National Meeting the task force heard comments from interested parties on the March 7 exposure draft including; continuing to level the playing field for all jurisdictions specifically related to the allowance of commissioner discretion, eliminating redundant filing requirements for U.S. reinsurers, and possible unintended consequences such as the exclusion of adverse development contracts where losses were incurred prior to the effective date of the models.

The task force directed its drafting group to make final technical revisions, which the task force does not expect will need formal exposure. The task force hopes finalize the revised models by mid-May.

Principles-based reserving

Applicability to fraternals
At the Spring National Meeting, the Financial Regulation Standards and Accreditation Committee exposed for comment revisions to the Part A Preamble of the Accreditation Program Manual to explicitly scope in fraternal benefit societies into the principle-based reserving requirements. (When PBR was originally adopted as an accreditation standard, the intent was that fraternals would be in scope.) The proposed effective date is January 1, 2020, consistent with the requirement for life insurers.

Valuation Manual amendments
Following the Fall National Meeting, activity of the Life Actuarial Task Force remained focused on VM Amendment Proposal Forms (APFs). LATF members exposed, re-exposed or adopted almost forty APFs during this time, many of which provide clarifying revisions to VM-20 (methodology) or VM-31 (reporting). At the meeting in Orlando LATF members adopted several previously exposed APFs and also exposed several new APFs. Many of the APFs deliberated upon since the Fall National Meeting address recommendations from the Valuation Analysis Working Group's October 2018 memorandum titled Principle-Based Reserves Recommendations and Referrals to LATF (the "PBR Report memorandum"). NAIC staff and the California Office of Principle-Based Reserving (CA OPBR) developed many of the APFs that were referred to LATF to address the VAWG recommendations.

APF 2018-44 was adopted in March after several exposures following its introduction at the 2018 Summer National Meeting. This amendment provides requirements for the Deterministic Reserve (DR) scenario for Indexed Universal Life. Specifically, the amendment prescribes equity returns for projected cash flows from invested assets used in hedging indexed accounts within life insurance products. The prescribed return is equal to 100% of the hedge budget in projection years 1-20 and 108% in projection years 21+. Debate during the multiple exposure periods focused on percentages of the hedge budget applied and alignment of the requirements with existing guidance; the final percentages are consistent with the DR scenario for a variable universal life product.

APF 2019-38 exposed in Orlando addresses the minimum mortality requirement for nonforfeiture values and reserves for guaranteed issue (GI) policies issued. This amendment was presented by the Nebraska Department of Insurance and replaces implementation of the 2017 Commissioners Standard Guaranteed Issue Mortality Table (2017 CSGI) with the 2001 Commissioners Standard Ordinary ultimate mortality table as the valuation standard for GI business issued after December 31, 2019. The proposed change is to address challenges some companies have found with implementation of the 2017 CSGI table due to the high margins in the table and resulting high reserves. Debate centered around the need to strengthen GI policy reserves which have historically been based on the 2001 CSO table, with the desire to minimize disruption in the marketplace considering pricing already in progress and IRS transition rules pertaining to new mortality tables. The APF is exposed for comment until May 1.

APF 2018-45 received significant air-time at the meeting in Orlando. This APF clarifies procedures for grading to the industry basic table when company mortality experience is worse than the industry table. The proposal presents two options: Option 1 requires testing company experience at the mortality segment level and Option 2 requires testing company experience at the aggregate level. Regulators are concerned that testing at the aggregate level will mask situations where mortality for a segment is worse than the industry and would warrant higher reserves, while the ACLI expressed concern that testing at the mortality segment level is too onerous. The APF was re-exposed for comment to try to reach some middle ground. The comment period ends May 1.

APF 2019-29 was introduced in Orlando by the Academy and was discussed at length. If adopted, this proposal would allow a group of policies to be eligible for exclusion from Stochastic Reserve requirements under VM-20 if a clearly defined hedging strategy (CDHS) is used to support a "non-material product feature" (e.g. an index account option with low utilization). The proposal stems from the addition of indexed account options to Variable Universal Life products, and concern that companies may be incentivized to fail the CDHS in order to allow a group of policies to be eligible for exclusion testing, as well as concern that immaterial features might cause groups of policies to be exempt from exclusion testing. The APF is exposed for comment until May 1.

In Orlando, the Academy presented an APF clarifying PBR treatment for individually underwritten group insurance. Currently the Valuation Manual specifies applicability to life insurance contracts as defined by SSAP 50, which includes group life and franchise life contracts, but sections of the VM are inconsistent relative to scope and requirements for individually solicited group life and franchise life contracts. The proposed changes would be extensive and effect several sections of the VM. After some discussion LATF members concluded a drafting group should be established to work through the issue and identify the necessary changes.

Reinsurance considerations

APFs 2019-17 and 2019-24 were exposed in February and address requirements regarding increases to nonguaranteed yearly renewable term reinsurance premiums that should be reflected in the deterministic and stochastic reserves, as well as related disclosures. This topic was discussed at length at both the Summer and Fall National Meetings, is addressed in the previously exposed APF 2018-58, and was the subject of a recommendation in the VAWG PBR Report memorandum.

APF 2019-24 is a multi-company proposal collectively submitted by Transamerica, Prudential and John Hancock, while APF 2019-17 was submitted by the CA OPBR/NAIC and is based on the multi-company proposal but reflects some changes to the proposed requirements and incorporates disclosures. The proposed changes follow a principle-based approach and incorporate modifications to reflect reinsurer increases in YRT rates to reflect implicit margins in PBR due to the restriction on future mortality improvement, and also incorporate credibility considerations. The comment period for these APFs has ended and discussion will continue on a future LATF call.

Experience reporting

LATF heard an update from the Experience Reporting Subgroup on the proposed changes to VM-51, Experience Reporting Formats (APF 2018-59), to add plan type sub-categories, which will support better analysis by realigning certain aspects of newer and more complex products with their associated mortality risks. The APF was exposed at the Fall National Meeting; the proposal has subsequently been edited to reflect comments and input from contributors. The proposed approach would categorize policies by base plan type rather than specific product features within a plan type, and information regarding specific product features would be captured in distinct categories independent of base plan type. The subgroup expects that the proposed changes would require companies to implement systems changes to capture and report the information at the level of granularity proposed. The effective date of the change is expected to be January 1, 2021.

VM-22 fixed annuity PBR

LATF heard updates from the VM-22 Subgroup and the Academy SVL Modernization Work Group on activities related to fixed annuity PBR; a new section of the Valuation Manual, VM-23 will incorporate assumptions and methodology for deferred annuities in the accumulation phase. The primary focus is fixed annuity products subject to AG 33 and AG 35. Separating VM-22 and VM-23 will facilitate solidifying the VM-22 formula-based minimum reserve requirements for payout annuities more quickly. The VM-22 Subgroup is proposing that the necessary guidance for deferred annuities be incorporated into VM-23 and be effective on January 1, 2022, for valuations on the new basis effective December 31, 2022 at the earliest (transition rules may apply).

The VM-22 Subgroup continues to work on methodology updates to address reinvestment risk and non-level payout annuities, considering current guidance in AG IX-B. The subgroup is targeting the 2020 Valuation Manual (1/1/2020 implementation) for the VM-22 updates related to payout annuities.

PBR Strategy Subgroup

A representative from the Academy PBR Strategy Subgroup spoke to LATF members about concerns over the recent number of non-substantive and prescriptive updates to VM-20 and VM-31, citing support for right-sizing reserves for current products, product innovation, and reporting requirements that will help regulators understand the business being valued and how companies think about that business. The subgroup has drafted a Practice Note Common Practices of Examining Actuaries Involved in Statutory Financial Solvency Examinations of Life and Health Insurers currently exposed for comment until July 1. The Academy encouraged LATF members to review and comment on the exposure draft.

Variable annuities framework

The Variable Annuity Capital and Reserve Subgroup and Variable Annuity Issues Working Group remain active ahead of the implementation of the new reserve and capital framework. The groups met frequently to address outstanding items ahead of the proposed January 1, 2020 required implementation date, with the option for early adoption for year-end 2019. (Note that the Life RBC Working Group has expressed some reservations about allowing early adoption.) The highlights of these meetings are summarized below.

VM-21 and C3 Phase II revisions

The Variable Annuity Capital and Reserve Subgroup convened on a near weekly basis since the Fall National Meeting to address comments received regarding the previous exposure draft and finalize the language to be included in the updated exposure draft. While many edits were made to the exposure drafts, no substantial changes were made to the proposed framework for the determination of reserves under the revised VM-21. However, one significant revision related to how this final reserve will be incorporated under the optional three-year phase-in was adopted. The update modifies the calculation to a simplified approach, which linearly grades between the reserve calculated under the existing and revised VM-21 guidance over the three-year period.

The subgroup exposed the redline and clean versions of the edits made to VM-01, VM-21, and AG 43, and the comment period ended March 28. The revised AG 43 will replace the existing version of the guideline, will be effective concurrently with the effective date of the revised VM-21, and will apply retroactively to all in-force VA contracts issued prior to its effective date.

At the Spring National Meeting, the Life Actuarial Task Force heard comments from the ACLI on the proposed revisions; their comments covered a variety of topics, but the presentation focused on the mortality assumption. The ACLI recommends the prescribed assumption be updated to reflect emerging experience that shows actual mortality greater than the proposed standard, which suggests prescribed reserves for living benefits are overly conservative. The ACLI plans to propose changes to the standard projection mortality this summer or fall, to be effective for the 2021 Valuation Manual; they also presented interim options for 2020 that include consideration of currently available data and anticipated release later in 2019 of a Society of Actuaries study of deferred annuity mortality. Additional discussion of comments on the three exposed documents will occur at future meetings.

Prescribed policyholder behavior assumptions

The subgroup discussed Oliver Wyman's (OW) recommendation for the prescribed assumptions for 403(b) business. OW previously noted that 403(b) business had not been included in the experience studies used to determine the proposed prescribed policyholder behavior assumptions. Since 403(b) business potentially exhibits unique policyholder behavior due to key product design differences such as ongoing automatic premium contributions, OW had agreed to conduct a separate study on this business and assess the need for a unique set of prescribed assumptions.

Based on the experience study performed using data from several key writers, OW concluded that 403(b) business does exhibit materially different policyholder behavior from traditional VA business, and thus recommended that the group adopt a unique set of prescribed policyholder behavior assumptions; regulators support this recommendation. As a result, the prescribed assumption set used in the determination of the Standard Projection Amount will contain unique assumptions for 403(b) business.

Cash surrender value flooring
The Variable Annuity Issues Working Group met in March to address a concern raised by the ACLI regarding the application the Cash Surrender Value (CSV) floor in determining VM-21 reserves. Under the current system, the CSV floor is applied on a scenario-by-scenario basis in the determination of the CTE70 Amount. The ACLI noted that this approach also impacts the Standard Projection Amount (SPA) because the company-specific market path is selected based on the CTE70 Amount.

The current approach will produce a higher CTE70 Amount for some companies, which will result in the selection of a more adverse company-specific market path and, in turn, more adverse policyholder behavior assumptions used to determine the SPA. The ACLI noted they do not believe it is necessary that the margin added by the scenario-by-scenario flooring should also be incorporated into the determination of the SPA. An industry representative agreed that they believed this approach produced unnecessary conservatism in the SPA.

OW's response maintains its support of the current framework, noting that removing the scenario flooring could result in an understated SPA. Regulators agreed and noted that this is expected to affect only a small number of companies in certain circumstances, and would likely produce a small overall impact. It would come into play particularly for companies with more aggressive assumptions, where regulators are more comfortable requiring higher reserves. Moreover, several regulators expressed comfort with the impact of this approach because it is counter-cyclical; the flooring will effect reserves more significantly when guarantees are out-of-the-money, and will not introduce unnecessary conservatism in times of stress when scenario reserves will already exceed the CSV. Based on the limited impact, the regulators did not move to alter the current approach using scenario-by-scenario flooring in the framework.

Looking forward
The need for any further refinements to the proposed regulations will be assessed based on the comments received during the latest exposure period. The new framework appears on-track for the proposed January 1, 2020 implementation date.

Retirement security initiative

As part of its charge to promote retirement security, the Life Insurance and Annuities Committee discussed the components of the project including 1) educating both consumers and producers on the topic, 2) promoting consumer protection and ensuring suitability and 3) encouraging innovation. The committee plans to form a working group to oversee the project, which will consider all forms of education, not just NAIC materials.

Life Actuarial Task Force

IUL Illustration Subgroup
LATF members received an update from the Indexed Universal Life Illustration Subgroup on activity to study the effectiveness of AG 49 and the use of index return multipliers to circumvent index option budget limitations and provide more favorable illustrations of riskier products. Some regulators and industry participants have expressed concerns that IUL products are illustrated with overly optimistic returns and that the downside risks are not sufficiently communicated to consumers.

The subgroup held calls in February and March to discuss the matter and exposed eight questions for public comment. At the meeting in Orlando discussion focused on responses to the question regarding how downside risk should be communicated with applicants. All responses were supportive of additional disclosure, but there is wide variety in recommendations, and in some cases, practices implemented by companies, which the subgroup will evaluate. A representative from the Center for Economic Justice spoke to LATF members about the risk of potential abuse and concern that additional disclosure requirements will only confuse consumers and not address the gravity of the issue. He suggests the issue is broader than AG 49 and recommends that the Life Illustration Model Regulation be opened up to address the issue. No further action was taken at this meeting.

Long-term care issues

Long-Term Care Insurance (B/E) Task Force
The co-chair of the task force began the meeting in Orlando announcing the formation of a new high level Long-Term Care Insurance (EX) Task Force and that long-term care issues are the number one priority of the NAIC for 2019.

The task force heard a presentation from the chair of the Financial Analysis Working Group on LTCI trends and regulatory pressures. The chair discussed the significant challenges faced by the industry; 170 companies previously wrote LTCI polices; the number writing new business is down to 12, with 15 companies holding 80% of reserves.

Per the FAWG comments, there is an increasing trend of companies not being able to or no longer willing to use other lines of business to subsidize LTCI. Two of the biggest challenges are the rate increase environment and inconsistency of rate approvals from state to state. Some insurers request inadequate rate increases, which hides the true cost to consumers. In addition, LTC services have changed enormously with a dramatic shift from nursing home care to in-home care. The Pricing Subgroup has concluded that solvency should not be a factor for a state approving a rate increase, so that two companies would get the same result with the same set of facts. The actuaries have concluded that mortality experience will very likely be the cause of future rate volatility and there is a consensus that the average length of time claims are paid has increased.

LTC actuarial topics
The Long-Term Care Actuarial Working Group heard an update on Academy activities from the chair of the Academy's LTC Valuations and Combo Valuations Working Groups. In early March, the Academy published an issue brief exploring the potential for catastrophic LTC costs facing older Americans. The LTC Practice Note Working Group has published an exposure draft of its Practice Note on long-term care insurance. The LTC Combo Valuation Working Group has created a draft Practice Note, which expects to expose for comment by the end of June. The LTC Valuations Working Group is continuing work on six workstreams, and expects to issue a draft report by the end of September.

The LTC Actuarial Working Group discussed the SOA Report, The Long-Term Care Medical Symposium, which was a one-day conference in February to address the historical and future trends that will influence future LTCI claims experience. The report discusses the use of drugs for the treatment of Alzheimer's, and increasing life expectancy.

The chair of the Pricing Subgroup provided an update on its work focused on LTC rate filing review topics including multi-state rate review, impact of solvency concerns on rate review, cross subsidy among states, and a survey among states on rate increase review practices.

AG 51 filings
The chair of the Valuation Subgroup discussed its review of 2017 AG 51 filings on LTC asset adequacy testing. Regulators saw a tight range among companies for assumptions used for mortality, lapse and interest, which reflect increasing length of claims. There was no consistency observed among companies for incidence assumptions. The preliminary results for AG 51 filings for 2018 show companies updating morbidity assumptions and increased discipline in assumption setting. The NAIC provided a guidance document for the 2018 submission, which included additional questions addressing morbidity and trend, including information on the use of outside data and morbidity improvement. The guidance requests standardized sensitivity tests including no morbidity improvement, no future rate increases, and a restriction on investment yield. There were also morbidity-focused calculations requested for the 2018 filings. The Valuation Subgroup will have additional observations related to the 2018 AG-51 filings after their review later this year.

International Insurance Standards Act

The NAIC submitted a statement for the record to Senate Banking Committee in February to support the adoption of the International Insurance Standards Act (H.R. 4537), which passed the U.S. House of Representatives in July 2018. The NAIC believes the legislation "clarifies the respective roles of "Team USA," and requires federal negotiators to seek the expertise of insurance regulators which will not only establish a sensible process for international negotiations but, more importantly, better outcomes for U.S. stakeholders."

Those opposed to the bill believe it would make U.S. efforts to adopt international insurance standards too difficult and it would remove the ability of the FIO to negotiate covered agreements.

Financial Stability Task Force

Financial Stability Oversight Council developments
At the Spring National meeting, the task force discussed FSOC's proposed interpretive guidance for nonbank financial company designations issued in March, which would put in place a cost/benefit analysis requirement before any entity is designated as systemically important. (See PwC's views on this

proposed change here.) The guidance would take an "activity-based approach" to assessing potential risks to financial stability and only designate a company 1) if its regulator cannot address the risks, 2) it is likely the company will fail, and 3) the benefits of designation outweigh the costs. There will be increased transparency, and more information will be provided earlier in the process to address perceived risks prior to designation. The task force also heard comments from interested parties to help inform whether the NAIC will submit a comment letter on the proposal. There was overall support for the proposal including the direction of the activity-based approach and recognition of state regulation, but there were several areas noted where interested parties felt more clarity was needed around the specifics of activity-based approach in practice.

Liquidity disclosures

The task force adopted the Excel template for the May 31, 2019 data call related to the new liquidity disclosures (Analysis of Operations and Analysis of Reserves schedules) effective for the 2019 life and fraternal annual statements. No additional data points from the draft will be requested in the final template. The issue raised by reinsurers about not having enough information from ceding insurers to complete the new schedules will be resolved at a later date; the initial data call will be for all life insurers and the data received will be for regulator use only. The final template with all data and filing instructions will be posted to the website no later than early May.

Liquidity stress testing framework

At the Spring National meeting, the task force received an update on liquidity stress testing and discussed the areas they are currently working on including: questions the stress test should answer (e.g. volume of assets sales in a stress event, sources and uses), test scenarios (e.g. 2008 financial crisis, cyber risk, rating downgrade), time horizons, and entities to include (e.g. insurance and non-insurance). The subgroup expects to present the final proposal at the Summer National Meeting and finalize it by the end of the year.

Restructuring Mechanisms Working Group

This newly formed working group was established to draft a white paper that 1) addresses the perceived need for restructuring statutes and the issues those statutes are designed to remedy, 2) consider alternatives that insurers are currently employing to achieve similar results, and 3) address the legal issues posed by a court order or approval by an insurance department in one state affecting the policyholders of other states. Other charges include:

- Review and propose changes to the Guaranty Association Model Act to ensure that policyholders with guaranty fund protection prior to a restructuring continue to have it after the restructuring, and

- Review and propose changes to the Protected Cell Companies Model Act to allow for restructuring mechanisms.

At the Spring National Meeting, the working group discussed that certain states (AZ, CT, IL, MS, OK, PA, RI and VT) have adopted either insurance business transfer laws or corporate divisions laws (i.e. separating active business from runoff business into two companies). The working group plans to review these laws in detail for purposes of drafting the white paper.

The working group also heard presentations from interested parties who believe there is a real need for business transfer laws. The regulators also heard from two guaranty fund trade associations on policyholder protection issues. The working group hopes to have an initial draft of a white paper by the Summer National Meeting.

The working group also formed a Restructuring Mechanisms Subgroup, which will be considering the development of financial surveillance tools specifically designed for companies in run-off, and has asked for comments on defining "run-off company" as a first step. The subgroup will also be considering the need for changes to RBC to better assess the minimum surplus requirements for companies in run-off.

International Insurance Relations Committee

IAIS Holistic Framework on Systematic Risk

The committee approved the submission of NAIC comments on the Holistic Framework on Systematic Risk which is intended to assess and mitigate systemic risk in the insurance sector with a focus on five key elements: 1) an enhanced set of supervisory policy measures, 2) a global monitoring exercise by the IAIS, 3) supervisory powers of intervention, 4) mechanisms that help ensure the global consistent application of the framework, and 5) an assessment by the IAIS of consistent implementation. The NAIC's comments focused on specific points on the five key elements.

Other IAIS papers
The task force also approved the submission of NAIC comments on the following two application papers: 1) the IAIS draft Application Paper on Recovery Planning, and 2) the IAIS draft Application Paper on Proactive Supervision of Corporate Governance. The comments on these application papers are mostly editorial in nature. The comment letters have not yet been posted to the committee's webpage.

Risk-focused surveillance

Operational risk referral
The Operational Risk Subgroup referred to the Risk-focused Surveillance Subgroup a request to continue further study the 3% operational risk charge developed by the subgroup. The Risk-Focused Surveillance Subgroup agreed to consider the referral and intends to proceed with transparency.

Peer review sessions
Following the four NAIC staff hosted peer review sessions held during 2018, best practices from those sessions were incorporated into training content and clarifying guidance for the Financial Analysis Handbook. Five additional sessions are planned for 2019 focusing on implementation of the risk-focused analysis approach, risk-focused exams and ORSA review.

P/C Appointed Actuary project

The Casualty Actuarial and Statistical Task Force continued its work as part of the Appointed Actuary project on its three charges related to attestation, experience and continued competence. Efforts related to the attestation and experience charges are reflected in the proposed revisions to the Statement of Actuarial Opinion (SAO) instructions, which they have partnered with an ad hoc group of the Executive Committee to revise.

The revised instructions were exposed on December 15, with a public hearing in March to discuss the comments received. The discussion included the following topics relating to definitions in the SAO instructions (which are the responsibility of the ad hoc group):

- Whether membership in the AAA should be included in the Qualified Actuary definition; although there was some support on the task force, the definition currently excludes required membership.
- Whether those that were qualified prior to the revised definition of Qualified Actuary would be "grandfathered;" the grandfathering clause was retained with some restrictions.

The comments were incorporated in the revised instructions with the changes to be considered during the Spring National Meeting; the revisions to be considered by the task force were only those related to the attestation and experience charges.

During the meeting in Orlando, task force members and interested parties requested that the complete instructions be circulated in order to consider the task force changes in the context of the entire document. It was resolved that a call would be scheduled at a later date once the task force had a chance to review the complete instructions. The revised language is as follows:

> *The Appointed Actuary shall provide to the Board of Directors qualification documentation on occasion of their appointment, and on an annual basis thereafter, directly or through company management. The documentation should include brief biographical information and a description of how the definition of "Qualified Actuary" is met or expected to be met (in the case of continuing education) for that year, including specific actuarial experiences relevant to the company's structure and lines of business. The Board of Directors shall document the company's review of those materials and any other information they may deem relevant, including information that may be requested directly from the Appointed Actuary. The qualification documentation shall be available for inspection upon regulator request or during a financial examination.*
>
> *The Actuarial Report should be consistent with the documentation and disclosure requirements of ASOP No. 41, Actuarial Communications. The Actuarial Report must contain both narrative and technical components, as well as the Appointed Actuary's qualification documentation. The narrative component should provide sufficient detail to clearly explain to Company management, the Board of Directors, the regulator or other authority the findings, recommendations and conclusions, as well as their significance. The technical component should provide sufficient documentation and disclosure for another actuary practicing in the same field to evaluate the work. This technical*

component must show the analysis from the basic data (e.g., loss triangles) to the conclusions.

The meeting of the task force to consider adoption of its changes to combine with the ad hoc group's proposals was expected shortly after the Spring National Meeting, but has not yet been scheduled. As of the publication date of this Newsletter, it is unclear whether the revised SOA instructions will be finalized in time to implement for 2019 actuarial opinions.

Climate change developments

The newly renamed Climate Risk and Resiliency Working Group held a conference call in April to hear a presentation from a representative of the U.S. Department of Energy on the government's "Fourth National Climate Assessment: Implications for Insurance, Risk Management, and Resilience" to consider how the findings of the assessment can help guide them as regulators on this issue. The assessment, conducted by over 350 scientists, observes, attributes, and then projects the impact on temperature and precipitation, sea levels, air quality, transportation, outdoor labor, and coral reefs from the effects of the emission of greenhouse gases. The projections vary based on level of mitigation technology that is employed and estimates the direct economic impact of climate change. The Department of Energy is already working on its 2022 publication (the assessment is required by Congress every four years) and is asking for input from NAIC and many other constituents.

***

The next National Meeting of the NAIC will be held in New York City August 3-6.

We welcome your comments regarding issues raised in this newsletter. Please provide your comments or email address changes to your PwC LLP engagement team, or directly to the NAIC Meeting Notes editor at jean.connolly@pwc.com.

Appendix A

This table summarizes actions taken by the SAP Working Group since the PwC NAIC 2018 Fall National Meeting Newsletter on all open agenda items. Items exposed for comment are due June 12, 2019, except for three items noted below. For full proposals exposed and other documents, see the SAP Working Group webpage.

Issue/ Reference #	Status	Action Taken/Discussion	Proposed Effective Date
SSAP 22 – ASU 2016-02 - Leases (#2016-02)	Exposed for comment	A third substantively revised SSAP 22R was exposed for comment at Spring National Meeting, along with the proposed issue paper, which retains the guidance that all leases are operating leases. See additional discussion in the SAPWG summary on page 3.	Years ending January 1, 2020, with early adoption permitted
SSAP 108 - Derivatives Hedging Variable Annuity Guarantees (#2016-03)	Status Update	With the adoption of SSAP 108, NAIC staff worked with industry to develop a new Schedule DB reporting schedule and notes to financial statements. See additional discussion in the Blanks Working Group summary.	December 31, 2019
ASU 2016-13 - Credit Losses (#2016-20)	Deferred	The SAP Working Group determined that they will defer further discussions related to ASU 2016-13 until after the FASB completes its work on two new related projects: targeted transition relief related to the fair value option, and vintage disclosures for gross writeoffs and gross recoveries. NAIC staff will also be monitoring issues related to recent concerns raised by banks related to adoption of the ASU.	TBD
SSAP 41 – Surplus Note Amortization and Accretion (#2017-12)	Discussion deferred	NAIC staff continues to work with industry to resolve issues and propose related accounting for surplus notes issued at a discount. There was no discussion of this topic at the Spring National Meeting.	TBD
SSAP 61R – Reinsurance Risk Transfer for Short Duration Contracts (#2017-28)	Status update	The working group continued discussion of proposed revisions to SSAP 61R with a focus on risk transfer issues related to group life YRT contracts. See additional discussion in the SAPWG summary.	TBD
SSAP 86 – ASU 2017-12, Derivatives and Hedging (#2017-33)	Discussion deferred	This project will review the overall accounting and reporting changes required by this ASU as potential substantive revisions to SSAP 86. There was no discussion of this standard at the Spring National Meeting.	TBD
SSAP 43R – Reporting NAIC Designations as Weighted Averages (#2018-03)	Exposed	The working group re-exposed revisions to SSAP 43R Implementation Question 8 to require that for SSAP 43R securities with different NAIC designations by lot, the reporting entity shall either report the entire investment in a single reporting line at the lowest NAIC designation that would apply to a lot, or report the investments individually by purchase lot in the investment schedules.	TBD
SSAPs 21 & 26 – Bank Loan Referral (#2018-04)	Exposed	The working group exposed for comment in 2017 a proposed recommendation that "borrowing base loans" and "DIP financing loans" be classified as collateral loans as opposed to bank loans under SSAP 26R. Based on feedback from industry, the working group revised their conclusion that SSAP 26R classification is appropriate and exposed for comment a proposed revision to SSAP 21 to note that "securities captured in SSAP 26R that are also secured with collateral shall continue to be captured within scope of SSAP 26R."	TBD

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Regulatory Transactions Referral from the Reinsurance Task Force (#2018-06)	Referral to VOSTF and Blanks Working Group	The SAP Working Group concluded its discussion of this issue without recommending any changes to the SSAPs and referred certain narrow issues to other groups. See further discussion in the summaries of the SAP Working Group and the VOS Task Force.	N/A
SSAP 41R – Surplus Notes Linked to Other Structures (#2018-07)	Regulator call in April	At the 2018 Summer National Meeting, the SAP Working Group exposed for comment proposed revisions to SSAP 41R to disallow capital treatment for surplus notes which are linked to other structures that are not subordinate, which interested parties strongly object to. At the Spring National Meeting, the regulators did not discuss comments received. Instead, the working group reiterated its request that insurance reporting entities that have issued "linked" surplus notes, and which file statutory financial statements with the NAIC, contact NAIC staff to discuss the effect of proposed SSAP 41R guidance on those entities. A regulator-only call is expected in April, followed by public discussion later in 2019.	TBD
SSAP 21 – Structured Settlements (#2018-17)	Issue Paper adopted	In 2018, the working group adopted proposed accounting for structured settlements acquired in accordance with applicable state and federal law. At the Spring National Meeting, the working group adopted the related Issue Paper 160, for historical documentation purposes.	December 31, 2018
SSAPs 2, 26R, 43R & 86 – Structured Notes (#2018-18)	Adopted	The working group adopted certain proposed revisions to provide guidance on securities with non-credit related risk as to principal. See additional discussion in the SAPWG section above.	December 31, 2019
SSAP 37 – Acquired Mortgage Loans (#2018-22)	Re-exposed	Significant additional proposed revisions to SSAP 37 were exposed to clarify guidance for mortgage loan participation agreements. See additional SAPWG discussion above.	TBD
SSAP 97 – Negative equity of SCAs (#2018-26)	Re-exposed	The working group had exposed proposed revisions to SSAP 97 to clarify under which circumstances an SCA should be reported at negative equity when the insurance company parent has guaranteed obligations of the SCA or provided commitments. As a result of comments from interested parties, which reiterated their concerns that the guidance would lead to "double counting" the impact of the parental guarantee or commitment, the working group re-exposed proposed revisions to eliminate the possibility of double counting.	TBD
SSAP 26R – Prepayment Penalties (#2018-32)	Re-exposed	The working group re-exposed for comment proposed revisions to SSAP 26R on determining the prepayment penalty for called bonds when the consideration received is less than par as a result of comments received, including a request to reduce operational complexity. (This issue is exposed until May 10.)	TBD
SSAP 30R – Pledges to FHLBs (#2018-33)	Adopted	The working group adopted clarifications to SSAP 30R that pledges of assets to a Federal Home Loan Bank by an insurer on behalf of an affiliate should be non-admitted.	April 6, 2019
SSAP 30R – Foreign Mutual Funds (#2018-34)	Adopted	The working group adopted guidance in SSAP 30R to specify that foreign open-end mutual funds governed and authorized in accordance with regulations established by the applicable foreign jurisdiction are admitted assets.	January 1, 2019

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SSAP 104R and SSAP 95 – ASU 2018-07, Improvements to Nonemployee Shared-Based Payments (#2018-35)	Adopted	The regulators adopted proposed revisions to SSAP 104R to align the statutory guidance with the new GAAP guidance that applies the same requirements to both employee and non-employee share-based payments, which were previously significantly different. The revisions eliminate the current SSAP 104R separate section on non-employee share-based payment guidance and apply the employee guidance to both.	January 1, 2020 with early adoption permitted
SSAP 100R – ASU 2018-13, Changes to the Disclosure Requirements of Fair Value Accounting (#2018-36)	Adopted	The working group adopted proposed revisions to SSAP 100R to incorporate the majority of ASU 2018-13, which removes certain fair value disclosures and modifies others. In addition, two new GAAP disclosures are not adopted related to level 3 assets.	April 6, 2019 for the deleted disclosures and January 1, 2020 for the revised disclosures, with early adopted permitted
SSAPs 92 and 102 – ASU 2018-14, Changes to the Disclosure Requirements of Defined Benefit Plans (#2018-37)	Exposed	The working project is proposing adoption of nearly all of ASU 2018-14, which removes some current disclosures, clarifies others and adds two new disclosures related to interest crediting rates and reasons for significant gains and losses related to changes in the benefit obligation. Changes not adopted related to removal of disclosures for non-public entities since the NAIC requires the same disclosures for public and non-public entities.	TBD
SSAP 55 – Prepaid Providers (#2018-38)	Re-exposed	The regulators re-exposed proposed changes to SSAP 55 related to claim and other prepayments made by insurers as a result of industry comments that they prefer nonadmitting the prepaid asset versus "expense and reclassify as amounts are paid," and to allow flexibility as to classification as either underwriting or claim expenses based on the nature of the payment.	TBD
SSAP 55 – Interest on Claims (#2018-39)	Adopted	The working group adopted proposed changes to SSAP 55 to require that interest paid on A&H claims in accordance with prompt pay or other similar regulations would be classified as other claim adjustment expenses when paid to policyholders and regulatory fines and fees when remitted to regulators.	January 1, 2020, applied prospectively
SSAP 16R/22 ASU 2018-15, Cloud Computing (#2018-40)	Adopted	The working group adopted proposed revisions to SSAP 16R to incorporate this ASU with modifications. See the SAPWG summary above for additional discussion.	January 1, 2020 with early adoption permitted
SSAP 86 – Benchmark Interest Rates (#2018-46)	Adopted	As a result of the issuance of guidance by the FASB, the working group adopted guidance to add the Securities Industry and Financial Markets Municipal Swap Rate and the Secured Overnight Financing Rate Overnight Index Swap Rate as U.S. benchmark interest rates for hedge accounting.	April 6, 2019

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Issue Paper 99 – Proposals to reject recent GAAP guidance	Adopted	The working group adopted the proposed rejection of the following GAAP guidance as not applicable to statutory accounting: ASU 2017-13, Amendments to SEC Paragraphs (#2018-41), ASU 2018-02, Reclassification of Certain Tax Effects from AOCI (#2018-42), ASU 2018-04, Debt Securities and Regulated Operations (#2018-43), ASU 2018-05, Income Taxes, Amendments to SEC paragraphs (#2018-44), and ASU 2018-06, Codification Improvements to Topic 942 (#2018-45).	April 6, 2019
INT 19-01 - Extension of Ninety-Day Rule for the Impact of California Camp Fire, Hill Fire and Woolsey Fire	Exposed and adopted	The working group exposed in January and then adopted at the Spring National Meeting a voluntary 60-day extension of the 90 day rule under SSAP 6 for uncollected premiums from policyholders affected by the California wildfires in November of 2018.	April 6, 2019, expiring April 24, 2019
INT 19-02 - Freddie Mac Single Security Initiative	Exposed and adopted	In February the working group exposed for comment a proposal to allow a limited scope exception to the exchange and conversion guidance in SSAP 26R for instruments converted in accordance with the Freddie Mac Single Security Initiative. The guidance was adopted in Orlando, which allows companies that exchange "45 day securities" for "55 day securities" not to recognize any gain or loss on the exchange.	April 6, 2019
SSAP 25 and Investment SSAPs - Affiliated Transactions (#2019-03)	Exposed	The working group exposed for comment a significant new proposal that provides additional guidance for related party investments and transactions. See the SAPWG summary above for additional discussion.	TBD
Investment Classification Project – Preferred Stock (#2019-04)	NAIC staff to draft issue paper	The regulators directed staff to draft substantive revisions to SSAP 32 to update definitions, accounting and valuation, dividends, impairments, and interactions with SSAPs 48 and 97.	TBD
SSAP 103R – Repurchase Disclosures (#2019-05)	Exposed	The SAP Working Group approved for exposure a proposal to reduce disclosure requirements for repurchase and reverse repurchase agreements, which would remove the counterparty and default disclosures and the minimum and average daily balance disclosure. This issue has a May 10 comment deadline.	December 31, 2019
SSAP 51 – ASU 2018-12, Targeted Improvements (#2019-06)	Exposed	As expected, the working group exposed a conclusion to reject the new GAAP standard for life insurance contracts. See page 4 for further discussion.	TBD
SSAP 72 – Bonds Received as Dividends or Capital Contributions (#2019-07)	Exposed	Clarifications are proposed to SSAP 72 and SSAP 25 for bonds received as dividends or capital contributions. Such assets would be valued at fair value at the transaction date when considered economic transactions under SSAP 25. This issue has a May 10 comment deadline.	December 31, 2019

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SSAP 52 – Reporting Deposit-Type Contracts (#2019-08)	Exposed	As requested by the Financial Stability Working Group, the SAP Working Group asked for information from industry as to why some guaranteed investment contracts, or other deposit-type contracts, are reported in Exhibit 5–Aggregate Reserves for Life Contracts or Exhibit 6–Aggregate Reserves for Accident and Health Contracts, as opposed to Exhibit 7 – Deposit-Type Contracts.	N/A
SSAP 101 – Q&A Updates (#2019-09 & 10)	Exposed	The working group exposed for comment two sets of proposed changes to SSAP 101; the first suggests revisions to the Implementation Q&A to update references for the Federal Tax Cuts and Jobs Act of 2017 and the second is meant to clarify the application of the deferred tax admittance calculation in paragraph 11 of SSAP 101. See the discussion of the SAPWG for additional detail.	TBD
SSAP 62R – Reinsurance Credit Transition Guidance (#2019-11)	Exposed	To provide explicit direction, the working group exposed for comment proposed transition guidance for the revisions to SSAP 62R that were adopted in November. The revised guidance applies to all contracts in effect as of January 1, 2019. Any changes as a result of the clarified guidance is treated as a change in accounting principle.	January 1, 2019
SSAPs 68 & 97 – ASU 2014-17, Pushdown Accounting (#2019-12)	Exposed	The working group is proposing rejection of this ASU, which would prohibit pushdown accounting for SCA entities reported under audited U.S. GAAP. See discussion at the SAPWG summary above for additional detail.	TBD
SSAP 97 – Clarification of the Look-Through Approach (#2019-13)	Exposed	These revisions propose that goodwill can only be admitted if the related SCA value has been supported by an audit report and that the look-through provision only applies to the downstream level directly below the noninsurance holding company. See further discussion on page 4.	TBD
SSAP 68 & 97 – Attribution of Goodwill (#2019-14)	Exposed	The working group is proposing to clarify that the acquisition of a holding company requires the purchase price and goodwill to be attributed to the downstream entities that the holding company directly owns. See the SAPWG summary for additional discussion.	TBD
Editorial Updates (#2019-15EP)	Exposed	The working group exposed minor changes to five SSAPs to update cross references and correct typos.	August 2019
Issue Paper 99 – Proposals to reject recent GAAP guidance	Exposed	The working group exposed for comment proposed rejection of the following GAAP guidance as not applicable to statutory accounting: ASU 2015-08, Business Combinations-Pushdown Accounting, SEC Paragraphs (#2019-16) and ASU 2019-02, Accounting for the Cost of Films and License Agreements (#2019-17).	TBD

Appendix B

This chart summarizes action on other proposals of the RBC Working Groups since the 2018 Fall National Meeting, i.e. those not discussed on pages 5-7 of this Newsletter. The detail of all proposals adopted for 2019 RBC are posted to the Capital Adequacy Task Force's webpage (under Related Documents).

RBC Formula	Action taken/discussion	Effective Date/ Proposed Effective Date
All formulas		
Stop Loss Interrogatories (2018-14-CA)	The Capital Adequacy Task Force **adopted** a proposal to capture additional health stop loss data to allow regulators to distinguish between aggregate and specific stop loss data.	2019 RBC Filings
Rounding Function in Capitation Tables (2018-17-CA)	The Capital Adequacy Task Force **exposed** for comment a proposal that would add a rounding function to the Health formula, making it consistent with the Life and P/C formulas. In addition, the proposal would make the tables captured electronic-only for all three formulas.	2019 RBC Filings
Informational-Only Growth Operational Risk (2019-01-O)	The Operational Risk Subgroup and CADTF **adopted** deletion of the "informational only" Growth Operational Risk pages (LR029-A – Life RBC; FR029-A–Fraternal RBC; XR022–Health RBC) and related instructions.	2019 RBC Filings
Risk-Based Capital Procedures (2019-06-CA)	The Capital Adequacy Task Force **adopted** a proposed change to the RBC procedures document to address referrals sent by other NAIC groups: "if the referral suggests changes to the RBC factors or structural changes for added granularity, an impact analysis may be conducted."	2019 RBC Filings
Risk-Based Capital Preamble	The Capital Adequacy Task Force **exposed** for comment an RBC Preamble, which formally documents the background, purpose, history, objectives and critical concepts of risk-based capital.	2019 RBC Filings
P/C RBC		
Catastrophe List Event (2018-15-CR)	The Capital Adequacy Task Force **adopted** the catastrophe event list for 2018 RBC filings.	2018 RBC Filings
Asset concentration and preferred stock and hybrid labels (2018-20-P)	The P/C RBC Working Group and CADTF **adopted** minor changes to the PR011 line descriptions to be consistent with the instructions.	2019 RBC Filings

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P/C RBC	Action taken/discussion	Effective Date/ Proposed Effective Date
Modify RBC average growth (2019-02-P)	The P/C RBC Working Group and CADTF **adopted** changes to the P/C RBC instructions to conform to the P/C RBC formula for the excessive premium growth calculation (PR016).	2019 RBC Filings
Underwriting risk line 1 factors (2019-05-P)	The P/C RBC Working Group **exposed** for comment the annual update of the industry underwriting factors (premium and reserve).	2019 RBC Filings

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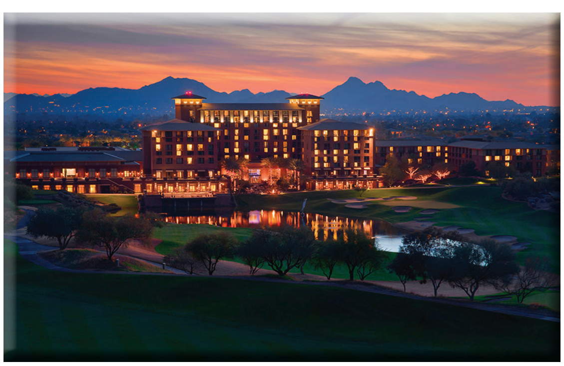

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