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NAIC 2019 Summer National Meeting Highlights

August 23, 2019

The National Association of Insurance Commissioners ("NAIC") held its 2019 Summer National Meeting from August 3 to 6, 2019 in New York City. In this update, we highlight meeting developments of particular interest to our insurance industry clients.

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Acronyms and abbreviations used in this report:

- ACLI: American Council of Life Insurers.
- EU: European Union.
- IAIS: International Association of Insurance Supervisors.
- RBC: NAIC risk-based capital.
- SEC: U.S. Securities and Exchange Commission.

Life Insurers

Suitability in Annuity Transactions

During the 2019 Spring National Meeting, the **Annuity Suitability (A) Working Group** held a joint meeting with the **Life Insurance and Annuities (A) Committee** and heard a presentation on the SEC's proposed Regulation Best Interest, including the fact that the proposed regulation does not define "best interest." After the presentation, the Working Group adopted a motion to continue its work on revising the Suitability in Annuity Transactions Model Regulation ("Model Regulation") and expressed a willingness to wait for the SEC to release amendments to Regulation Best Interest.

The SEC released a final version of Regulation Best Interest on June 5, and the Working Group held an in-person meeting in Columbus, Ohio on June 20 to consider amendments to the Model Regulation that could be harmonized with the SEC's rule. Although Regulation Best Interest requires that a broker-dealer making a recommendation act in the best interest of the customer, "without placing the [broker-dealer's] financial or other interest . . . ahead of the interest of the retail customer," it does not define the term "best interest." Instead, the SEC rule identifies four obligations, which, if satisfied by a broker-dealer, would collectively equate to acting in the customer's best interest.

The obligations set forth in Regulation Best Interest are: (1) disclosure obligation; (2) care obligation; (3) conflict of interest obligation; and (4) compliance obligation, which the Working Group described as the insurer's obligation to supervise compliance with the standards in the Model Regulation. The Working Group also discussed adding a separate "documentation obligation" to enhance recordkeeping for recommendations made by a producer and to document a consumer's refusal to provide financial information or decision to engage in a transaction that was not recommended.

Prior to the meeting in Columbus, Iowa Commissioner Doug Ommen (who is Vice Chair of the Working Group and Chair of the **Life Insurance and Annuities (A) Committee**) released a version of the Model Regulation that was re-formatted in a manner similar to Regulation Best Interest, allowing the Working Group to map the provisions of the Model Regulation to the obligations set forth in the SEC regulation. The Working Group used the Iowa draft as a starting point for its consideration.

At the Columbus meeting, the Working Group discussed each of the obligations in the Model Regulation and considered specific language that may be included to carry out the intended result. Although the Working Group touched on all of the obligations, it noted that there was disagreement with respect to many of the key provisions and that additional input would be required. No final decisions were made at the Columbus meeting, and the Working Group requested additional comments on several substantive issues, including what standard of conduct to use, whether it should be called "best interest," what such a standard would mean and how it would be enforced. The Working Group then held two additional conference calls in July, during which it discussed additional comments that had been received, and focused on the remaining open questions.

At this National Meeting, the Working Group explained that a "best interest" standard of conduct is somewhere above a "suitability" standard but below a fiduciary duty, but the exact contours of the standard are yet to be determined. The current draft of the revised Model Regulation defines a producer's care obligation in part as recommending an annuity that would be "best suited to the consumer over the life of the product." The Working Group considered two elements that potentially could be included in the care obligation: a duty to have a reasonable basis to believe (1) that the consumer "would benefit from certain features of the annuity" and (2) that the annuity as a whole "would address the consumer's needs." Although the Working Group members generally agreed that such concepts should be included in the Model Regulation, some members expressed the view that the standard described by Regulation Best Interest and the current draft of the Model Regulation was not much stronger than suitability.

The Working Group also considered whether to require a customer to sign a statement documenting the customer's refusal to provide suitability or other financial information. Although many members of the Working Group supported the idea, some noted their experience with producers who encourage customers to refuse to provide such information in order to make the process "easier," by reducing the amount of information and paperwork required of the customer. A consumer representative suggested that because annuities have become complex investment vehicles, no sale should occur at all if the customer refuses to provide financial information, despite the customer's insistence. Other interested parties responded that such an approach risks being overly paternalistic.

Several members of the Working Group cautioned against using the term "best interest" in the revised Model Regulation if the substantive language does not actually require a producer to make recommendations based exclusively on the consumer's best interest (i.e., the consumer's interest should not only be placed ahead of the producer's, but should also be the only interest that a producer considers). The concern expressed by these Working Group members was that characterizing the revised Model Regulation as imposing a best interest standard would enable insurers and producers to market themselves as consumer-friendly, which could lead to a false sense of security if the producer does not act exclusively in the consumer's best interest.

The Working Group also noted that its next step would be to form a technical drafting group to develop a draft of proposed revisions to the Model Regulation reflecting the Working Group's deliberations thus far and comments received from interested parties. The technical drafting group is expected to meet in early September to produce a new draft of the Model Regulation, which will then be exposed for public comments. Thereafter, the Working Group plans to set an aggressive call schedule with weekly conference calls to discuss the comments received. The Working Group's goal is to present a complete draft of the revised Model Regulation to the **Life Insurance and Annuities (A) Committee** for its consideration prior to or at the Fall National Meeting in December.

Property/Casualty Insurers

Big Data

During the 2019 Spring National Meeting, the **Big Data (EX) Working Group** heard an update from the **Casualty Actuarial and Statistical (C) Task Force** about comments that were received in response to a draft of the Predictive Analytics White Paper, which addresses the sources and selection of data, predictive models and state rate filings. The Working Group said that the comments have been mapped onto the draft of the white paper and that it would work to address all of them.

At the Summer National Meeting, the Working Group received a report from the **Casualty Actuarial and Statistical (C) Task Force** on the second draft of the Predictive Analytics White Paper, which was exposed in May for a 45-day comment period. The Task Force said that it received eight comment letters and was in the process of reviewing them and drafting a third exposure of the white paper. They noted in particular that there were two issues that may be contentious and may require the Working Group's review: (1) the confidentiality of the information and algorithms used in predictive models and (2) whether a predictive model's use of a particular characteristic in underwriting reflects a causal relationship between the characteristic and the risk being insured or is it merely a statistical correlation that appears related to cost.

The **Innovation and Technology (EX) Task Force** heard an update on data privacy issues and adopted a recommendation to refer a charge to the **Market Regulation and Consumer Affairs (D) Committee** to review state insurance privacy protections regarding the collection, use, and disclosure of information gathered in connection with insurance transactions. The Task Force also adopted a recommendation to appoint a new working group, the **Artificial Intelligence (EX) Working Group**, to study the development of artificial intelligence, its use in the insurance sector and its impact on consumer protection and privacy, marketplace dynamics and the state-based insurance regulatory framework.

Group-Wide Supervision

Group Capital

The **Group Capital Calculation (E) Working Group** continued to make progress in its development of a group capital calculation and received a report about on-going field testing. Field testing began in the second half of May, using a template that had been discussed at, and revised following, the 2019 Spring National Meeting. Thirty insurers volunteered to participate in the field test, as well as 14 lead state regulators. A number of additional insurers have reviewed the field testing template, which has been posted to the Working Group's web page. The Working Group expects to receive all field testing results by the end of August with a goal of adopting the group capital calculation in 2020.

The Working Group heard a presentation from the National Association of Mutual Insurance Companies ("NAMIC"), reporting feedback from a number of NAMIC members who have reviewed the publicly posted field testing template but are not participating in the formal field testing process. The members providing comments fell into three categories: (1) holding companies that do not own a bank or other regulated entity, (2) non-holding companies that own an insurance agency, and (3) non-holding companies that do not own any other entities.

The comments from these groups primarily addressed three broad issues: (1) the burden that the calculation will place on small insurers, including the trouble associated with delivering a calculation at the same time that annual reporting is ongoing and whether the calculation will necessitate the hiring of additional employees, (2) the effects on insurance companies after the calculation is adopted, including how regulators will benchmark the results, any potential regulatory action that could result from the calculation and whether the calculation may eventually evolve into a standard, and (3) which insurers will be required to submit the calculation, including whether small mutual insurers that are not required to file electronic annual statements will be required to perform the calculation.

The Working Group's focus has also turned to implementation of the group capital calculation. The Working Group released a draft memorandum from the Working Group to the **Group Solvency Issues (E) Working Group** proposing that the Insurance Holding Company System Regulatory Act may need to be modified in order to maintain confidentiality with respect to any group capital calculation submissions. The memorandum notes that certain critical decisions remain to be addressed before such a step is required, including determining who will be required to complete and file the calculation, whether the calculation will be filed with the NAIC and whether there might be limited circumstances in which the calculation can be disclosed (e.g., by insurance groups to non-U.S. regulators in connection with the Bilateral Agreement Between the United States of America and the European Union on Prudential Measures Regarding Insurance and Reinsurance (the "EU Covered Agreement")). The Working Group has scheduled a call for August 29, 2019 to further discuss issues related to confidentiality of the calculation.

International Insurance

IAIS Activities

The **International Insurance Relations (G) Committee** heard an update on the status of key IAIS projects. IAIS Deputy Secretary General Romain Paserot provided an update on the Insurance Capital Standard version 2.0 ("ICS"), which the IAIS expects to adopt at its November 2019 meeting. A number of stakeholders have raised the concern that the ICS is not sufficiently developed to be implemented in 2020. The IAIS has clarified that the five-year ICS monitoring period that begins in 2020 will monitor the performance of the ICS over time rather than monitor the Internationally Active Insurance Groups that calculate the ICS. Mr. Paserot emphasized that third parties, such as credit rating agencies, should not receive ICS results during the monitoring period, nor should the results trigger supervisory action. In addition, the IAIS expects continued stakeholder engagement about the ICS throughout the monitoring period. Prior to adoption of the ICS as a prescribed capital requirement, the IAIS expects to hold another public consultation.

Committee members noted that the NAIC is focused on gaining clarity as to how the IAIS will determine whether other capital measurement tools, including aggregation methods such as the group capital calculation being developed by the NAIC, will be deemed comparable to the ICS. The NAIC and other U.S. officials have encouraged the IAIS to provide a road map and criteria that will be used to assess comparability. Members of the IAIS Secretariat reported that the IAIS will hold a number of internal meetings on this topic prior to November but cautioned that developing the criteria for assessment may not be completed by November.

Reinsurance

Last year, the **Reinsurance (E) Task Force** largely completed its work revising the Credit for Reinsurance Model Law and the Credit for Reinsurance Model Regulation (the "Models") to incorporate the EU Covered Agreement and a similar "Bilateral Agreement Between the United States of America and the United Kingdom Regarding Insurance and Reinsurance" (collectively, the "Covered Agreements"). At the 2019 Spring National Meeting, the Task Force agreed to consider a number of technical changes to the Models that were raised by interested parties and directed a drafting group to update the Models for final adoption.

The drafting group met on April 16 and April 30 by conference call in regulator-only sessions to discuss the remaining issues from the Spring National Meeting. On April 25, NAIC staff discussed with representatives of the U.S. Department of the Treasury, the Federal Insurance Office and the Office of the U.S. Trade Representative whether the draft revisions to the Models were consistent with the Covered Agreements. The drafting group made certain technical edits to the Models based on comments from the federal officials, as well as representatives of the European Commission. Representatives from the Federal Insurance Office were unable to give assurances at this time that states adopting the draft revisions would not be subject to a potential preemption analysis by the federal government, but after those discussions the sense was that state legislatures "can feel comfortable" adopting the draft revisions. The drafting group exposed further revisions to the Models on May 1 and received five comment letters.

The Task Force held a conference call on May 15 to discuss the May 1 revisions and receive additional comments. At the conclusion of the call, the Task Force adopted several revisions to the Models based on the comments received. The **Financial Condition (E) Committee** then adopted the revisions during a May 28 conference call, and the **Executive (EX) Committee and Plenary** unanimously adopted the revisions during a June 25 conference call.

At this meeting, the Task Force discussed the implementation process for the revised Models and stated that state legislatures were sent a formal notice of the adoption of the 2019 revisions to the Models on July 16. Each state legislature has five years from the execution of the EU Covered Agreement (September 22, 2017) to amend its reinsurance laws and/or regulations or be subject to federal preemption by the Federal Insurance

Office, which may begin its preemption analysis on April 1, 2021, with potential federal preemption beginning on October 1, 2022.

Various NAIC groups will have to implement additional changes before the end of 2019 to reflect the revised Models, including amendments to the P&P Manual and revisions to Schedules F and S of the statutory statement blanks to reflect reinsurance ceded to a new type of reinsurer (i.e., one that does not have to post collateral).

The Task Force also discussed the impact of the revised Models on accreditation standards. The Task Force noted that the Reinsurance Ceded portion of the accreditation standard (under the Financial Regulation Standards and Accreditation Program) currently authorizes a reduction of reinsurance collateral, but not its complete elimination. Thus, states that adopt the revised Models (which require elimination of collateral for certain reinsurers) before the accreditation standard changes will be out of compliance with that part of the standard.

The Task Force made a recommendation to the **Financial Regulation Standards and Accreditation (F) Committee**, which the Committee accepted, to recognize that states may begin to adopt provisions that are substantially similar to the 2019 revisions to Models and remain in compliance with the Reinsurance Ceded accreditation standard. The Task Force also recommended that the accreditation standard be modified in accordance with the normal processes and procedures outlined in the Accreditation Program Manual, and that the Task Force and **Financial Condition (E) Committee** prepare a formal recommendation to the **Financial Regulation Standards and Accreditation (F) Committee** for consideration at the 2020 Spring National Meeting. Finally, the Task Force recommended that, in the interim, states should be encouraged to begin adopting the 2019 revisions in order to avoid potential federal preemption.

Long-Term Care Insurance

At the 2019 Spring National Meeting, the **Executive (EX) Committee and Plenary** voted to establish a new **Long-Term Care Insurance (EX) Task Force** under the Executive Committee. The Task Force is chaired by Virginia Commissioner Scott White and has 36 members, all of whom volunteered to join. The Task Force was given two specific goals: (1) to develop 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 (2) to focus on ensuring that consumers are provided with meaningful options to reduce their benefits in situations where the premiums are no longer affordable.

The Task Force had met about six times since the Spring National Meeting in regulator-to-regulator session. These meetings were educational in nature and offered members a shared base of knowledge. The Chair noted that the discussions by members of the Task Force revealed strong views but a lack of consensus on how to move forward. These discussions led the Task Force to identify the following six work streams to accomplish its goals.

- The Multistate Rate Review Practices work stream, led by Colorado Commissioner Michael Conway, is the centerpiece of the Task Force's work and will review the wide variety of practices used by states in their review of rate increase requests. As part of the development of a state-based framework, this workstream will be evaluating different actuarial methodologies that the states use. The Task Force currently is focused on two approaches to develop a consistent, nationwide system of reviewing long-term care insurance rates: (1) expanding the scope of the Interstate Insurance Product Regulation Commission, and (2) developing a multistate examination model.

- The Restructuring Techniques work stream, led by Commissioner Kent Sullivan of Texas, will focus on restructuring techniques and will explore possible alternatives for protecting policyholders from guaranty fund caps and review the impact of potential inequities that may result from states' inconsistent approaches to rate increase decisions. A consumer advocate expressed concern that recent state enactments of insurance business transfer statutes could be used by long-term care insurers to split off legacy long-term care insurance liabilities. The regulator from Oklahoma, which recently enacted such a statute, stated that its insurance business transfer statute will not be used for long-term care insurance business.

- The Reduced Benefit Options and Consumer Notices work stream, led by Pennsylvania Commissioner Jessica Altman, will review the options that insurers have been developing over the last few years to offer consumers who cannot afford to pay higher premiums, and the notices sent by insurers to consumers to explain their options.

- The Valuation of Long-Term Care Insurance Reserves, led by Minnesota Commissioner Steve Kelley, will continue the NAIC's previous efforts to update Actuarial Guideline LI–The Application of Asset Adequacy Testing to Long-Term Care Insurance Reserves ("AG 51") as part of the discussion on how to properly balance rate increase assumptions with reserving assumptions. AG 51 was adopted in 2017 to clarify requirements for the calculation of long-term care insurance reserves and was a regulatory response to concerns about the lack of specificity and uniform practice in testing long-term care insurance reserve adequacy. AG 51 requirements are effective for reserves reported as of December 31, 2017, and are applicable to insurers with more than 10,000 inforce long-term care insurance contracts (whether written directly or assumed through reinsurance) as of the valuation date.

- The Non-Actuarial Variations work stream, led by Washington Commissioner Mike Kreidler, will examine what is referred to as non-actuarial variances among the states in approving rate increases. Recognizing that not all states base their final rate decisions solely on actuarial analysis, the focus of this work stream will be to better understand the rationale behind factors that are not actuarial and, if possible, to develop a model set of non-actuarial practices.

- The Data Call Design and Oversight work stream will be led by Virginia Commissioner White and will explore whether additional data is needed to support the work of the Task Force and/or to refine its understanding of the financial impact of different state practices.

The Chair explained that the Task Force is currently in the planning stages, which will likely continue through the end of August. At some point, some of the work streams may become full working groups, with significant interaction in open sessions, but others will continue to operate confidentially until they develop work products, which will be discussed in open sessions. The Task Force has been charged with delivering a proposal on these and other related matters to the **Executive (EX) Committee** by the 2020 Fall National Meeting.

Financial Condition

Valuation of Securities

The **Valuation of Securities (E) Task Force** exposed proposed revisions to the Purposes and Procedures Manual of the NAIC Investment Analysis Office ("P&P Manual") to update the Definition and Instructions for Principal Protected Notes. The deadline for comments is September 19.

The proposed revisions provide that principal protected notes ("PPNs"), which are sometime referred to as "principal protected securities," "principal protected loans," or "combo notes," would not be eligible for a filing exemption. PPNs are a type of structured security where a portion of the underlying assets are dedicated to ensure the repayment of principal at maturity or where a third party may guarantee the repayment of principal at maturity. The remaining assets in the structure, the performance assets, are intended to generate additional returns and may be of a type that would not be eligible for reporting on Schedule D. These may include derivatives, equities, commodities, non- rated debt, loans, funds, private equity, real estate or other similar assets. Investments in PPNs must be submitted to the NAIC Securities Valuation Office for analysis. Based on the proposed revisions, PPNs would likely need to be reported on Schedule BA, rather than receive the more favorable bond treatment of Schedule D.

Collateralized Fund Obligations

The **Statutory Accounting Principles (E) Working Group** discussed proposed revisions to SSAP No. 43R (Loan-backed and Structured Securities) which have the potential to affect insurer capital charges for holding investments in collateralized fund obligations ("CFOs") and similarly structured products. The proposed revisions are intended to require insurers that invest in structures that are issued in the form of bonds or debt instruments, but have return characteristics that are equity-like, to report such investments on Schedule BA rather than Schedule D.

Currently, insurers report investments in CFOs or similar structures that are in the form of rated debt on Schedule D, along with other long-term bonds, which benefit from lower RBC charges. An insurer likely would be required to take a significantly higher RBC charge if these investments were to be excluded from Schedule D and reported on Schedule BA.

The specifics of the changes to SSAP 43R are still in draft form and likely to be revised following further study by the NAIC and comments from interested parties. As currently drafted, though, certain of the proposed revisions are quite broad and could be read to require a wide range of structured investments to be reported on Schedule BA.

What is likely, though, is that investments that do not have traditional bond-like cash flows but instead cash flows that are contingent on the performance of underlying equity investments (e.g., a significant variable coupon that is based on the performance of underlying equity investments) will be excluded from Schedule D reporting if these new rules take effect. It is also possible that revisions to SSAP 43R will pick up debt tranches of CFOs and other structured products with underlying exposure to limited partnership interests or other equity investments, even where the debt tranches have cash flows more in line with traditional debt instruments.

The proposed revisions are currently classified as "non-substantive," meaning they are meant to clarify the scope of SSAP 43R, rather than substantively change the meaning. There has already been industry resistance to this classification, but if the revisions are ultimately treated as non-substantive, then they could be adopted on a faster time frame. If they are ultimately classified as substantive, then the Working Group would need to produce an issue paper and conduct further analysis, which can take a significant period of time to complete.

The Working Group exposed revisions to SSAP No. 43R on August 8, with a comment deadline of October 11. Interested parties are expected to provide comment on the draft revisions, as well as on whether such revisions should be considered substantive or non-substantive.

Linked Surplus Notes

The Statutory Accounting Principles (E) Working Group also received an update on a referral from the Reinsurance Task Force that asked the Working Group to review and potentially amend the guidance in SSAP No. 41R (Surplus Notes) to restrict surplus note treatment for instruments that are designed as surplus notes but that are linked to other structures.

This issue originated when the Reinsurance Task Force was asked to review an investment product that appeared to be a surplus note but included multi-layered or linked transactions that "embed" the risk of the domiciliary state regulator not approving payment of the surplus note's stipulated principal and interest. As part of that review, questions arose as to whether the statutory accounting provisions allowing equity reporting (rather than debt reporting) of surplus notes fully consider the possibility for subsequent, complex transactions that could influence whether the note continues to be in compliance with SSAP 41R.

The proposed revisions to SSAP 41R were exposed twice before – during the 2018 Spring National Meeting and the 2018 Summer National Meeting. After the exposure period from the 2018 Summer National Meeting, it was noted that more information on "linked surplus notes" was needed for consideration, and NAIC staff requested that regulators and interested parties provide information on transactions for assessment by the Statutory Accounting Principles Working Group assessment.

The Working Group announced that a regulator-only conference call occurred on July 2, 2019 to discuss proposals to obtain additional information from reporting companies. The Working Group noted that there is no information currently in the statutory financial statements that would detail whether the cash flows due under an issued surplus note could be offset by the cash flows due to the surplus note issuer from a "linked asset." Although a few specific scenarios were presented to the Working Group, it was determined that there is no way to identify the extent to which the noted scenarios exist and/or if there are other situations that were not identified in the request for information.

The NAIC staff proposed two options for obtaining additional information from reporting companies: (1) incorporate revisions to SSAP No. 41R for year-end 2019 stating that all issued and outstanding "linked" surplus notes must be identified as permitted or prescribed practices in Note 1 of the statutory financial statements or (2) conduct a data call to request that reporting companies submit information to NAIC staff.

The Working Group heard from interested parties who indicated a preference for a data call over reporting linked surplus notes as a permitted or prescribed practice. The Working Group recommended that NAIC staff and the Working Group cooperate with interested parties to establish data points and an acceptable format for requesting information concerning linked surplus notes.

In addition, the Working Group approved exposing guidance for determining linked surplus notes that would describe a linked surplus note as a situation in which a reporting company has linked the cash flows payable from an issued surplus note with cash flows receivable under any other agreement or held asset, or when the reporting company uses the proceeds from the surplus note to purchase a financial instrument directly or indirectly from the holder of the surplus note.

Commissions

The **Statutory Accounting Principles (E) Working Group** discussed proposed revisions to SSAP No. 71 (Policy Acquisition Costs and Commissions) that have the potential to affect insurer accounting of liability related to levelized commissions. The proposed revisions clarify that a levelized commission arrangement requires the establishment of a liability for the full amount of unpaid principal and accrued interest payable to a third party at the time the policy is issued. Additionally, the proposed revisions provide that a persistency commission is accrued proportionately over the policy period to which the commission relates and is not deferred until fully earned. The Working Group did not specify whether such revisions would be retroactive.

The proposed revisions are currently classified as “non-substantive”, which means that they are meant to clarify the scope of SSAP No. 71, rather than substantively change the meaning. There was industry resistance to the revisions, mainly because of the requirement to accrue commissions without a legal obligation to pay until the end of a policy persistency period, as well as the “non-substantive” classification. If the revisions are ultimately treated as non-substantive, they could be adopted on a faster time frame. If they are ultimately classified as substantive, the Working Group would need to produce an issue paper and conduct further analysis, which can take a significant period of time to complete.

The Working Group exposed revisions to SSAP No. 71 on August 3, with a comment deadline of October 11. Interested parties are expected to provide comments on the draft revisions, including whether they should be considered substantive or non-substantive.

Restructuring

Insurance Business Transfers

The **Restructuring Mechanisms (E) Working Group** held its first in-person meeting at the 2019 Spring National Meeting and heard presentations from the ACLI, two insurers with experience in utilizing insurance restructuring mechanisms and representatives from guaranty fund associations. During this National Meeting, the Working Group heard presentations by Enstar and Aon, both of whom have experience with Part VII transfers in the UK, which serve a similar purpose of separating certain businesses into new companies. Enstar's presentation focused on the industry need for restructuring mechanisms, and Aon's presentation focused on the benefits of restructuring mechanisms.

Both presenters pointed out that Part VII transfers involve a very rigorous process that requires court supervision, as well as an independent expert, to evaluate whether the new company will be sufficiently capitalized and policyholders will not be adversely affected by the division. They noted that Part VII transfers have been very successful in the UK with about 280 transactions completed since 2000, and none of those transactions resulted in troubled companies.

Members of the Working Group had a number of questions about how the Part VII process might be applied to the US system and the outcomes of the transfers. It was noted that although Part VII transfers involve walling off "toxic business," both presenters expressed some skepticism that long-term care insurance business could be treated similarly.

Regulators were also particularly concerned as to whether existing reinsurance of the business would continue after the transfer. The UK experience has been that companies have begun to add express provisions to their reinsurance agreements, providing that the reinsurance will follow the policies that are transferred under Part VII.

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Please do not hesitate to contact us with any questions.

Click here for a recording of the recent NAIC Summer National Meeting client briefing highlighting these topics.

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Alexander R. Cochran
arcochran@debevoise.com

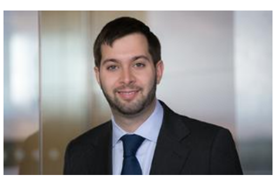
Thomas M. Kelly
tmkelly@debevoise.com

Marilyn A. Lion
malion@debevoise.com

Nicholas F. Potter
nfpotter@debevoise.com

Eugene Benger
ebenger@debevoise.com

Risa B. Gordon
rgordon@debevoise.com



Matthew B. Parelman
mbparelman@debevoise.com

Leron Solomon
lsolomon@debevoise.com