

## NAIC 2019 Spring National Meeting Highlights

April 24, 2019

The National Association of Insurance Commissioners (“NAIC”) held its 2019 Spring National Meeting from April 6 to 9, 2019 in Orlando. 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.

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## Life Insurers

### Suitability in Annuity Transactions

The NAIC's consideration of amendments to the Suitability in Annuity Transactions Model Regulation seems to have slowed in order to better align the NAIC's proposed amendments with the SEC's development of a new standard of conduct regulation.

Last year, the **Annuity Suitability (A) Working Group** held multiple in-person meetings and exposed a number of proposed amendments for public comment. At the 2018 Fall National Meeting, the Working Group approved several "clean-up" amendments to the Model Regulation and a drafting note explaining why the NAIC's current draft of the Model Regulation does not include the term "best interest," which is used in the SEC's April 2018 proposed Regulation Best Interest.

During this meeting, the 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 Model Regulation and to consider the comments that had been received on the current draft of the revisions, as well as comments from Working Group members, interested state insurance regulators and interested parties.

Working Group members expressed a willingness to wait for the SEC to release amendments to Regulation Best Interest, which is expected this fall, in order to achieve a consistent standard of conduct for the sale of annuities under the federal securities laws and state insurance laws. The Working Group expects to hold an additional in-person meeting in May or June.

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## Property/Casualty Insurers

### Big Data

During the 2018 Fall National Meeting, the **Casualty Actuarial and Statistical (C) Task Force** presented a draft of a white paper that addressed the sources and selection of data, predictive models and state rate filings. The draft provided 16 best practices and

identified 92 items of information that may be collected to fulfill those best practices. At this meeting, the **Big Data (EX) Working Group** heard an update from the Task Force, which had exposed a draft of its white paper for public comment. The Working Group discussed the 10 comments that were received and noted that many of the comments were critical of the scope of the data to be collected and the potential overreach by regulators in seeking so much information. 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. The Working Group also recognized that the white paper presents only one model, which may not be a good fit for all lines of insurance.

Furthermore, the Working Group heard concerns related to the apparent lack of transparency in predictive models, especially with respect to the factors or components that go into setting the amount of premium that consumers have to pay. One regulator raised the possibility that the complexity of these models may hinder agents in their ability to understand and explain to a consumer the reasons for a particular underwriting decision and its effect on the cost of coverage. Although the Working Group did not pursue this line of inquiry, as this was beyond the scope of the meeting, it did agree to consider the use of big data in insurer claim practices, such as claim valuation and antifraud efforts. Additionally, the Working Group adopted a motion to request that the **Life Insurance and Annuities (A) Committee**, in collaboration with the ongoing work of the **Life Actuarial (A) Task Force**, study insurers' use of external data and data analytics in accelerated life underwriting and propose appropriate state guidance or best practices.

The Working Group continued its discussion of the NAIC's need for technical staff and resources in order to provide better technical support to state insurance regulators when reviewing complicated predictive models. Among such resources is the development of a training and education program and tools for insurance departments to share information. The NAIC legal division is working on a memorandum to ensure that sharing information about predictive models would not endanger statutory confidentiality protections. The **Innovation and Technology (EX) Task Force** heard a report from South Carolina Insurance Director Raymond Farmer on cybersecurity initiatives and the implementation of the Insurance Data Security Model Law. Director Farmer also briefed the Task Force about a cybersecurity tabletop exercise that the South Carolina Department of Insurance hosted in collaboration with the U.S. Department of the Treasury to aid regional insurers in preparing for, responding to and recovering from a cyberattack. Among the takeaways was a finding that smaller insurance companies were not paying sufficient attention to cybersecurity issues until they were forced to either because of a breach or the enactment of state cybersecurity laws.

The Task Force heard presentations from several speakers on the insurance regulatory challenges facing insurance startups. Among these was Plug and Play Tech Center, a Silicon Valley insurtech accelerator and venture capital provider, which presented its findings from a survey it conducted of 34 insurance startups regarding their experience dealing with insurance regulations. Although half of the respondents viewed insurance regulations as a barrier to their growth, the businesses of these respondents were all market-facing and consumer directed. The other half of respondents, whose businesses were engaged in mid-office or back office businesses (i.e., not customer facing) and in streamlining processes or enabling more effective analytics, did not view regulations as a barrier to their growth. Both sets of respondents expressed a desire for greater engagement with insurance regulators.

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## Restructuring

### Insurance Business Transfers

During the 2018 Fall National Meeting, the **Financial Condition (E) Committee** agreed to form a new working group to study the legal and financial issues relating to insurance business transfer (“IBT”) statutes and insurance division statutes, which, broadly speaking, authorize an insurer to separate a portion of its in-force business and transfer it to a new insurer. At least six states have such laws and others are actively considering them.

The new working group — the **Restructuring Mechanisms (E) Working Group** — held its first meeting by conference call on March 11, during which it discussed its charges, including preparing a White Paper that examines existing state restructuring statutes, the perceived need for such statutes and alternatives that insurers currently employ to achieve similar results; reviewing and proposing changes to the Guaranty Association Model Act to ensure that guaranty fund protection continues after a restructuring; addressing legal issues that may arise in connection with restructuring orders issued by out-of-state courts or insurance regulators; and developing financial solvency and reporting requirements for companies in runoff, for which the Working Group will create a subgroup.

At its first in-person meeting during the 2019 Spring National Meeting, the Working Group heard presentations from the ACLI, two insurers with experience in utilizing insurance restructuring mechanisms and representatives from guaranty fund associations. Among the points raised in the presentations were the need to study IBT mechanisms and their potential interaction with the Model Holding Company Act, and to consider the experience of Part VII transfers under English law. The presenters explained the importance of providing policyholders and other stakeholders with access

to the restructuring process, considering the financial condition of the insurer and the quality of assets involved in the restructuring. One insurer noted that it was not aware of an IBT transaction where the assets provided by the acquirer have been insufficient to support the acquired obligations.

In light of the fact that insurers that only assume restructured business in a state will not write any direct coverage, some member of the Working Group asked the insurance company representatives why a state regulator would license a new company in such circumstances. Members also discussed the potential impact that such insurers may have on guaranty fund protection, since insurers licensed in a state must become members of such state's guaranty fund association and are assessed based on their direct written premiums.

The Working Group also exposed for public comment until April 26 proposed charges for its subgroup, which will consider financial surveillance tools for companies in runoff, potential changes to the RBC formula, minimum standards for capital requirements and reporting obligations and actuarial guidance for establishing initial reserve levels.

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## Group-Wide Supervision

### Group Capital

The **Group Capital Calculation (E) Working Group** continued to develop the field testing template for the group capital calculation, with field testing scheduled to begin by mid-May 2019. An NAIC staff memo related to the field testing process suggests that field testing volunteers should use the information contained in or related to their 2018 annual statutory financial filings as the source for the data requested in the template. The memo also states that volunteers would have 60 to 90 days to complete the template followed by a 60-day review period by working group members and NAIC staff.

The Working Group reported that confidentiality of the field testing results remains an issue. The NAIC staff memo suggests that the template will be submitted to the field testing volunteer's lead state regulator, who will then, subject to a confidentiality agreement, share the template with the Working Group and NAIC staff. The Working Group is in the process of developing and executing confidentiality agreements with the applicable lead states. Members of the Working Group noted that sensitive company data has been shared with the NAIC in the past, and there have not been any instances of unauthorized release of such data.

Stakeholders questioned how the field testing results would be shared with volunteers and non-volunteers. The Working Group acknowledged that the way in which data is

shared may not be finalized until after the data is submitted so that it can be determined how to share data without compromising the confidentiality of the field testing volunteers. Stakeholders also questioned the short timeline between the end of the field testing process and the 2019 Fall National Meeting in December, given that the Working Group has set a goal of finalizing the group capital calculation by the end of 2019. The Working Group noted that finalizing the group capital calculation could be an iterative process, if necessary.

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## International Insurance

### IAIS Activities

The **International Insurance Relations (G) Committee** heard from a panel of interested parties representing companies with international business. The interested parties raised a number of concerns about the Insurance Capital Standard (“ICS”) version 2.0, including technical aspects of the calculation, the development process and questions about confidentiality.

With respect to confidentiality, panel members questioned whether third parties, such as rating agencies or investment banks, would require information about a company’s ICS calculation as part of a diligence process. Panel members were concerned that such requests could lead to adverse consequences for companies operating in certain markets or doing certain types of business because of the way in which the ICS is structured. Panel members supported the creation of a group capital calculation that would be deemed equivalent to the ICS as a means of monitoring insurance group capital. Panel members also noted that the group capital calculation should be properly viewed as part of a suite of tools that U.S. regulators have to monitor the financial health of U.S. insurance companies.

### Reinsurance

Last year, the **Reinsurance (E) Task Force** completed its work amending the Credit for Reinsurance Model Law and Model Regulation (the “Models”), so that they conform to the requirements of the Bilateral Agreement between the United States and the European Union on Prudential Measures Regarding Insurance and Reinsurance (the “Covered Agreement”) and a substantially almost identical Covered Agreement with the United Kingdom. The Task Force held a public hearing in February and subsequently exposed drafts for public comment in June and September.

At the 2018 Fall National meeting in November, the Task Force and the **Financial Condition (E) Committee** adopted revisions to the Models, and recommended that the

**Executive (EX) Committee and Plenary** adopt the amended Models with certain technical changes that the NAIC staff would prepare. Because of the election of NAIC officers at the end of the previous meeting, the Executive Committee did not have time to vote on several matters, including the revised Models and announced that it would do so on a conference call in December 2018.

During the December conference call, the Executive Committee and Plenary did not vote on the revised Models because, prior to the call, representatives of the U.S. Department of the Treasury and the Office of the U.S. Trade Representative expressed to NAIC staff concerns as to whether the Models as revised met the requirements under the Covered Agreements. Similar concerns were raised by representatives of the European Commission at last year's Task Force and E Committee meetings. Specifically, the European Commission questioned whether the amendments go beyond the Covered Agreement and give too much discretion to state insurance regulators to add unspecified requirements by regulation. The Task Force expressed its view that the amendments were consistent with the Covered Agreements.

As a result, the Task Force further revised the Models, which were exposed on March 7 for a 25-day comment period that ended April 1. The new revisions address the concerns expressed by reducing a commissioner's discretion to determine which jurisdictions are considered "Reciprocal Jurisdictions."

The proposed amendments, among other things, add a new section to the Models that allows credit for reinsurance with zero collateral for insurance ceded to an insurer that has its head office in, or is domiciled in, a "reciprocal jurisdiction." The concept of "reciprocal jurisdiction" is similar to existing Model provisions relating to "qualified jurisdiction" in the certified reinsurer context (current qualified jurisdictions are also reciprocal jurisdictions). The definition of "reciprocal jurisdiction" is meant to include not only EU jurisdictions and the United Kingdom under the Covered Agreements but existing "qualified jurisdictions" that have not entered into an "international reinsurance agreement." This is meant to provide parity between EU reinsurers and non-EU reinsurers from existing qualified jurisdictions, including Switzerland, Japan and Bermuda.

At this meeting of the Task Force, a number of industry representatives suggested further technical changes, which the Task Force will consider in preparing new drafts for consideration. It expects to have the new drafts by mid-May and will re-expose them for public comment.

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## Long-Term Care Insurance

The **Long-Term Care Insurance (B/E) Task Force**, a joint task force of the **Health Insurance and Managed Care (B) Committee** and the **Financial Condition (E) Committee**, provided an update on the work that it has completed and stated that long-term care insurance is the NAIC's top priority for 2019.

Among the items completed by the Task Force is a report containing ten policy options to encourage innovative long-term care financing strategies, which was shared with members of Congress. Among the recommendations are hybrid life-annuity products with long-term care coverage, allowing retirement savings accounts to be used for long-term care without penalty, establishing long-term care savings accounts similar to existing Health Savings Accounts ("HSAs") and/or allowing HSAs to be used for long-term care, and tax incentives, such as deducting long-term care insurance premiums.

A representative of the **Financial Analysis (E) Working Group** provided an update on long-term care insurance trends and regulatory pressures, including the Working Group's surveillance of potential solvency issues involving long-term care insurers. Additionally, the Working Group noted that inconsistencies across states have made it difficult to put rate increases into effect and available consumer options to withstand sudden rate increases have been insufficient.

The **Long-Term Care Valuation (B) Subgroup** also provided an update on its efforts to update Actuarial Guideline LI—The Application of Asset Adequacy Testing to Long-Term Care Insurance Reserves ("AG 51"). 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 subsequent annual statutory financial statements, and it is 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 Subgroup expects AG 51 filings made by insurers to provide helpful information with which they can take next steps, but noted that morbidity experience is the most likely cause of future volatility.

To highlight the importance of long-term care insurance, the **Executive (EX) Committee and Plenary** voted to establish a new **Long-Term Care Insurance (EX) Task Force** under the Executive Committee and adopted its charter. The Committee stated that the Task Force would consider all options to strengthen the long-term care



insurance industry, and, in order to allow a candid discussion, the initial meetings of the Task Force would be open only to regulators.

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## Financial Stability Task Force

### Macro-Prudential Monitoring

The **Receivership and Insolvency (E) Task Force** received updates from the drafting group formed to consider the referrals that the Task Force had received from the **Financial Stability (EX) Task Force** related to assessing recovery and resolution planning in light of the ongoing NAIC Macro-Prudential Monitoring Initiative, which is focused on enhancing liquidity, recovery and resolution, capital stress testing and identifying exposure concentrations.

The drafting group identified areas where powers given to state regulators in the event of a receivership are implicit rather than explicit, including the ability to establish bridge institutions and to ensure continuity of essential functions performed by non-regulated entities. In addition, the drafting group noted several provisions that are contained in the Insurer Receivership Model Act that are not explicitly addressed in earlier versions of the NAIC model receivership law. The drafting group will consider providing guidance and will have further discussion on these issues.

The drafting group also assessed the NAIC model laws for conflict with federal laws. In particular, the drafting group noted that the federal rule recognizing temporary stays on terminating master netting agreements for qualified financial contracts does not recognize stays in a state receivership proceeding. The drafting group proposed amendments to the Guideline for Stay on Termination of Netting Agreements and Qualified Contracts, which were exposed for a 30-day comment period that will end on May 7.

The **Financial Stability (EX) Task Force** received an update from the **Liquidity Assessment (EX) Subgroup**, which has formed a small study group consisting of regulators, companies and NAIC staff to consider issues related to a proposed liquidity stress test, including the purpose of a stress test, stress test scenarios and the scope of entities that should participate in the stress test. The study group expects to report on its work to the Subgroup in June. The Subgroup aims to present its initial conclusions to the Task Force at the 2019 Summer National Meeting in August, with a more detailed proposal to follow at the 2019 Fall National Meeting in December.

Please do not hesitate to contact us with any questions.

[Click here](#) for a recording of the recent NAIC Spring National Meeting client briefing highlighting these topics.

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